DRAFTING AND NEGOTIATING SHARE PURCHASE AGREEMENTS

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INTRODUCTION

A Share Purchase Agreement is one fundamental document used in business transfers. It is a useful tool in privatization of public enterprises, mergers and acquisitions, joint ventures and other forms of business and company arrangements.

The basic commercial and legal issues in drafting and negotiating commercial contracts apply to share purchase agreements. However, certain terms and provisions are peculiar to the share purchase agreement. There are two types of share purchase: partial purchase and whole purchase. The former involves transfer of only part of the owner's shares such as in privatization[1], partnership, and some joint ventures while the latter involves whole transfer of owner's shares as in business transfers, mergers & acquisitions, etc. The provisions of a share purchase agreement for the two types of share purchase would differ slightly. This Paper will discuss the basic principles as well the specific principles for drafting and negotiating general commercial contracts and share purchase agreements.

THE ART OF DRAFTING AN AGREEMENT

In drafting a commercial contract, the first basic idea to bear in mind is that the contract may be the subject of legal interpretation sooner or later. The objective is therefore to ensure that the court will interpret the contract in the way the draftsman intended. In other words, the contract must be readily understood by the court and any person reading it. The language must be clear, concise and devoid of ambiguity or multiple interpretations.

The courts have developed rules and general techniques for interpretation of contracts and the draftsman should be aware of some of these rules and principles. This is why it is advisable to engage a lawyer or draftsman skilled or knowledgeable in the subject matter of the contract, rather than the practice of general or in-house counsel drafting commercial agreements by mere reliance on precedents or standard templates.

Every precedent is dangerous.[2] This is because every commercial contract involves different facts and circumstances even if it is the same subject matter. A skilled and experienced draftsman is careful to reflect the peculiar circumstances of the contract in whatever precedent is being used and the clauses he includes would depend on the party he is acting for.

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[1] Note that privatization may also be whole sale.

[2] See Simon Beswick, Buying and Selling Private Companies and Businesses, Butterworths, London, Edinburgh and Dublin, 6th Edition 2001 p.315.

In drafting and negotiating share purchase agreements for instance, the clauses you include depends on who you are acting for, that is whether the buyer or the seller. There are clauses favourable to buyer and others to seller on the same issue and then there is the third option which is a balanced clause fair to both parties. You must always start with the draft favourable to the party you are acting for particularly where there is no standard procurement process in place. You should not negotiate against yourself. Usually the process of due diligence and other procurement processes towards the contract determine the agreed draft. At times the procurement process is rigid and a draft Share Purchase Agreement is provided as part of the bid process e.g. in the RFP (Request for Proposal). Even this can be negotiated.

Apart from understanding and employing interpretation principles, the skilled lawyer is better able to identify and manage the various risks and dynamics of the transaction. Thus the role of lawyers in drafting and negotiating commercial contracts cannot be over emphasized.

In drafting a Share Purchase Agreement and other commercial contracts:

Use plain and intelligible English: Avoid legal jargons and archaic English like "wherein before", "whereto fore" etc. Use simple short sentences instead of lengthy paragraphs and phrases as they make the contract difficult to understand and somewhat boring. For instance instead of saying:

> *"Upon the date of execution of this Agreement by the parties hereto, the buyer shall make ready and available, and handover the sum of N5 million naira to the seller being the full and final purchase price for the shares subject matter of this contract. In the event that at any time hereinafter the time set forth for the execution of this agreement, the buyer fails, refuses and/or neglects to make the purchase price ready and available to the seller on the date afore mentioned, or the buyer does any act purporting to show that the buyer is unwilling unable and not ready to make the purchase price available to the seller, this agreement and the provisions and obligations herein before mentioned shall cease and terminate forthwith at the instance of the seller"*

say:

> *"The buyer shall pay to the seller the purchase price of N5 million on the date of execution of this Agreement failing which the seller will be entitled to terminate this contract."*

State obligations in the positive instead of in the negative unless absolutely necessary. For instance, instead of saying: *"The buyer shall not fail to pay the*

purchase price on the date of delivery of the share certificate", say: *"The buyer shall pay the purchase price on the date of delivery of the share certificate".*

Use punctuations correctly. Punctuations, as insignificant as they may seem, play a very important role in the meaning of words and phrases in a contract. For instance the words in the phrase *"Kill him not, spare him." are exactly the same as "Kill him, not spare him."* except for the difference in position of the coma. The difference in position of the coma is significant, in fact, so serious as to cost a life rather than save one in the contrasting phrase!

State obligations clearly –

Contracts confer rights and obligations on the parties. A good contract should state each party's rights and obligations clearly i.e. the specific obligation, the performer of the obligation, to whom the obligation is owed, when the obligation is to be performed, the consideration for the obligation or corresponding obligation of the other party. Example:

> *"Upon payment of the purchase price, the share certificate shall be delivered to the buyer."*

This example is vague because it is not clear when the payment will be made, who pays the price, who prepares and delivers the certificate to the buyer and when the share certificate will be delivered to the buyer. It is more definite to say:

> *"The buyer shall pay the share price of N5 million on the date of execution of this agreement and the seller (or company) shall ensure that the share certificate is delivered to the buyer within 30 days thereafter."*

Also, depending on the nature of the contract, it may be necessary to specify where the obligation is to be performed (e.g. in a sale of goods transaction: where the goods will be supplied, in a charter party: where the vessel will be delivered and redelivered) and how the obligation is to be performed (e.g. whether payment is to be made by cheque, cash, letter of credit or consideration other than cash).

Use Headings for convenience as they make it easy to find particular clauses in the contract and enhance general understanding of the contract.

Use Schedules where necessary: Schedules contain details of specific portions of the agreement which cannot neatly be included in the main body of the agreement. They are used to ensure that certain details of an agreement are incorporated in the agreement and binding on the parties. For instance in a share purchase agreement, issues like share valuation, payment schedule, milestones etc. may be included as

schedules. It is advisable to insert schedules before the execution and attestation page of the agreement so as to eliminate alteration or substitution of schedule pages after parties have signed. However, this situation can also be avoided by parties initialing all the pages of the contract. Below are some provisions that can be found in Schedules to a Share Purchase Agreement (depending on the type of share purchase):

- Schedule of Audited Financial Statements
- Schedule of Company Assets
- Schedule of Material Contracts
- Schedule of Permitted Encumbrances
- Schedule of Leases, Licenses and permits
- Schedule of Employees
- Schedule of Pension and Benefit Plans, Incentive Arrangements
- Post Transaction Plan (Post Privatization Plan for privatization transactions)
- Disclosure Letter

BASIC COMMERCIAL & LEGAL ISSUES IN SHARE PURCHASE AGREEMENTS AND GENERAL COMMERCIAL AGREEMENTS

Parties

Parties are those who have rights or obligations under the contract. A contract should not generally include parties on whom no right or obligation is conferred. This is on the simple principle of privity of contract which presupposes that only parties to a contract can enforce or benefit from it. But sometimes it is necessary to include parties on whom the agreement is intended to be binding. For instance, in a share purchase agreement, the primary parties are the seller (the share owner) and the buyer. In public enterprises, the owner of the shares is usually the government or public authority but in many share purchase agreements of public enterprises, the enterprise or company itself is included as a party in order to bind the company and its other shareholders, although they may not have direct obligations to the buyer. It is noteworthy that the concept that only parties can enforce benefit under a contract is now weaker with the passage of laws such as Contracts (Rights of Third Parties) Act of England by virtue of which a third party beneficiary is entitled to claim under a contract.[3] It follows that in conferring benefits to third parties, it should be borne in mind that in many jurisdictions such third parties can now sue on such contracts.

[3] See Simon Beswick, *Buying and Selling Private Companies and Businesses,* Butterworths, London, Edinburgh and Dublin 2001 p. 243.

It is also important to state the name of the parties correctly and accurately i.e. the exact name by which the company was incorporated or registered so as to avoid the technical (but valid) argument in future that the contracting parties are not legal persons and therefore lacked capacity to contract. In a case we are handling for Federal Airports Authority of Nigeria (FAAN), the Defendant filed a preliminary objection on the ground that the 's' in 'Airports' was omitted from the Plaintiff's name and therefore the Plaintiff is not a juristic person with locus standi to sue!

Where a company is part of a group of companies, it is important to ascertain which member of the group should be party to the contract. One way of determining this is to ascertain the member of the group on whom the rights or obligations are conferred and if the other members of the group would in any way benefit or be affected by such rights or obligations. For the purpose of bindingness and effectiveness of contract, it is advisable to include all members of the group that will be significantly affected by the contract. For example in a share purchase agreement, where the whole or part of the shares of a subsidiary are being sold or transferred, the parent company should be made a party to ensure that it has consented to the transaction. Usually, a share purchase contract (and indeed most other contracts) would contain a representation or warranty that the parties have obtained the necessary consents or approvals to enter into the transaction, but the surest way of achieving this is to make the parent company bound by the agreement and even undertake to guarantee the subsidiary's performance of the contract.

Commencement, Term/Duration

A contract must have a commencement date i.e. the date on which the contract takes effect. This is very important as many rights or obligations are tied to the commencement date. For instance in a share purchase contract, the date of payment, delivery of share certificate, milestone payments, membership rights, and so on are made to take effect within specified periods from the commencement date. It is common to find contracts commencing on the date of execution but this practice is not the best since contracts are sometimes signed after performance has begun and also, parties do not usually all sign on the same date. It is advisable to insert a definite commencement date thus: *"This contract shall commence on the 20th day of October 2010."*

A contract is usually for a fixed term subject to the right of termination by a party upon notice to the other. Some contracts may be short term say for 3 – 5 years (e.g. leases) while others may be long term, say for 15 – 50 years (e.g. power purchase contracts, concessions). A share purchase agreement may enure for the life of the company or enterprise. It may however be terminated upon the occurrence of an

event of default on the part of either party particularly the buyer[4], breach of terms and conditions of the share purchase agreement, buyer's insolvency, etc. Also there could be an option to renew the contract after expiration of its initial term but an intention to exercise this option should be expressed before the actual end of the initial term.

Upon termination of a contract, parties may be required to perform certain obligations. For instance, the buyer in a share purchase agreement may be required to sign the necessary share transfer forms to hand back the shares to the company.

Note that a contract without a term as to termination is terminable on reasonable notice but what is reasonable notice depends on the circumstances of each case. It is better to determine precise mode of termination at the time the contract is negotiated than to leave things to the standard of a reasonable man.

Liability and indemnities

Commercial contracts involve various legal and commercial risks and these risks should be properly allocated and apportioned to the contracting parties. Liability and indemnity clauses are a means of apportioning these risks. In allocating the risks, the party best suited to handle such risks should be made to bear them. For instance in a concession, while political and regulatory risks are better handled by the government or public authority, construction, implementation and design risks are better handled by the concessionaire. In a share purchase agreement, valuation risks are better handled by the owner or seller while investment and tax risks are better handled by the buyer. The draftsman should be careful to ensure that the risks being allocated to his client are commercially acceptable to his client, whether his client can be insured against those risks and whether the price or consideration to be paid under the contract have taken proper account of the risks being borne by each party. These are commercial issues which the parties' lawyers and transaction advisers would consider for effective and fruitful contractual negotiations.[5]

Execution

It is important to ensure that the persons who sign the contract are authorized to do so. In other words they should have authority to bind the company. One of the commonest means of ensuring authority to bind the company is to have the contract signed by 2 directors or a director and secretary. If the person who signs a contract

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[4] For instance in a privatization transaction where the buyer (private investor) is given the obligation to manage and turn around the company, failure to achieve specified results within the time stipulated may amount to breach sufficient to enable termination of the contract.

[5] See Mark Anderson, *Drafting and Negotiating Commercial Contracts,* Butterworths, London, Edinburgh and Dublin, 1997 p. 68.

has no authority to bind the company, the company cannot be held liable on any of the obligations in the contract. In share purchase agreements, one useful way of ensuring authority is to insist on the seller providing a certified copy of the board resolution of the company to show that the company has approved the sale. However with many small contracts this may not be feasible; for instance if a contractor is entering into an agreement with a multinational company, the latter may not be expected to call a board meeting to approve every contract. As a fall back, warranty and representation as to authority should be inserted. Further, it is important that the name of the person who signed is written out in full as CAC now requires full names for any instrument executed on behalf of a company and intended to be filed at CAC.

Closely connected to the issue of authority to execute contract and to bind the contracting party is the doctrine of state immunity which presupposes that a sovereign state cannot be compelled to submit to the jurisdiction of another state. State immunity exists at two levels: at the level of jurisdiction and at the level of execution. In other words, a sovereign cannot be sued in a foreign court without its consent (immunity of jurisdiction) or a judgment or award cannot be enforced or executed against the assets of a sovereign in a foreign jurisdiction (immunity from execution). In privatization or concessioning of public enterprises it is common to find a government agency such as Bureau of Public Enterprises, Federal Ministry of Finance Incorporated, Ministry of Water Resources, Federal Airports Authority of Nigeria, etc. signing the contract on behalf of the government. In drafting such contracts, it is important to ensure that the person or official signing the agreement has the consent of the relevant public authority and authority to bind the government. This can be achieved by joining the government as a party to the agreement, indicating clearly that the government agency is signing for and on behalf of government and inserting a waiver of immunity clause on the part of the government agency and the government on whose behalf the agency is contracting. This will eliminate the risk of the defence of state immunity by the government. Below is an example of a waiver of immunity clause:

> *"The Government shall not claim sovereign immunity or any other immunity from any legal action or proceedings brought in connection with this Agreement and hereby irrevocably waives any such immunity or defence it may have or hereafter acquire under any relevant or applicable legislation."*

Another suggestion if you are working for private party against government party is to request for either legal opinion or letter from the Attorney General representing compliance with local laws and warranting authority to execute on behalf of the government.

Law and jurisdiction

This is a very fundamental clause in commercial contracts since contracts will invariably be subject to legal interpretation by courts or other dispute resolution process. It is particularly important in cross border commercial contracts where parties are from different jurisdictions (or where the contract is to be performed in different jurisdictions) and subject to different laws. This raises conflict of law issues and a good draftsman should ensure that the choice of law clause is clear and unambiguous. In this regard, it is important to state which country's law is applicable as well as the court that will have jurisdiction. For instance, in a share purchase between a foreign (English) investor and a Nigerian public enterprise, it will not be enough to simply say the contract will be governed by Nigerian law; for English courts may well have jurisdiction to adjudicate upon it and apply Nigerian law being the governing law. Whilst this is not impossible or legally wrong, it poses some difficulty and confusion as the English courts may not be skilled in Nigerian law and may in such cases require engaging a Nigerian expert on the subject. Sometimes the facts of the transaction itself may trigger application of a particular national law such as where the contract was performed, the law relating to the subject matter, etc. unless parties have otherwise agreed. We are currently handling a case involving CBN revocation of banking licence, appointment of NDIC as liquidator and its effect on existing contracts of the affected bank. The case is before an English court but because Nigerian law is the applicable law to this issue, we were engaged to give opinion as Nigerian insolvency experts. The situation is similar even where the contract provides for arbitration as the dispute resolution mechanism. Apart from stating that the governing law of the contract is Nigerian law, it should also be stated that the seat of arbitration shall be Nigeria and that the arbitration shall be governed by Nigerian law.

Below is an example of a good law and jurisdiction clause:

Litigation: *"This Agreement shall be governed by Nigerian law excluding its conflict of law rules. Any dispute arising under or in connection with this Agreement shall be subject to the exclusive jurisdiction of the Nigerian courts to which the parties to this Agreement hereby submit."*

Arbitration: *"This Agreement shall be governed by Nigerian law excluding its conflict of law rules. Any dispute arising under or in connection with this Agreement shall be referred to arbitration. The place of arbitration shall be Nigeria and the arbitration shall be governed by Nigerian law in accordance with the Arbitration and Conciliation Act Cap. A18 LFN 2004 and any Rules or amendments made pursuant to it."*

Note that an arbitration clause may be more extensive than the above, as there may be need to state the language of the arbitration, number of arbitrators, time limits for conclusion of arbitration, etc. Where an institution is chosen to administer the arbitration it is better to use the model clause of that institution and there is no need to have elaborate provisions because the rules of that institution would have made provisions for those. Also generally in drafting law and jurisdiction clauses, it is important to exclude the conflict rules in the choice of law because such conflict rules if not excluded may point to the law of another country. This is popularly known as renvor principle.

Boiler Plate Clauses

Boiler plate clauses are standard clauses found in most commercial contracts which have been developed to deal with effects of well established case law. They include clauses on:

- Confidentiality/Non disclosure;
- Notices;
- Force Majeure;
- Entire Agreement;
- Assignment; etc.

It is expected that these would be have been discussed by other resource persons in the course of this training and so we will not go into boiler plate clauses here.

On Boiler Plate Clauses, see generally, Mark Anderson, *A-Z Guide to Boilerplate and Commercial Clauses*, Butterworths, London, Edinburgh and Dublin, 1998 p.42.

ISSUES/CLAUSES PECULIAR TO SHARE PURCHASE AGREEMENTS

In addition to the above general principles and issues, below are the key points to keep in mind when drafting or negotiating a Share Purchase Agreement.

Number of Shares and Purchase Price:

This clause sets out the number of shares being sold and the purchase price of the shares. Details of these may be included as schedules to the agreement. The number of shares sold is one distinguishing factor between a partial sale and a whole sale or acquisition and this will affect the provisions of the share purchase agreement. Indeed in drafting a share purchase agreement, the first task of the draftsman is to determine the type of sale. The price clause will be easy to draft if the price is a fixed amount. If the price is calculated by reference to a rate or as a percentage of revenue or (in a share purchase agreement) percentage value of the

company, it will require more careful drafting. The following are necessary considerations to be determined and negotiated:

- What are the tax obligations and who bears them e.g. does share purchase price include tax? Are deductions or set-offs allowed?

- Mode of payment: lump sum or mile stone payments? Is deposit required? How much deposit? Is deposit refundable or to be treated as advance payment?

- Time of payment and whether time is of the essence.

- Effect of buyer's failure to pay deposit or to meet up with milestone payments: Interest, penalty, forfeiture of deposit, termination of contract? (If you're acting for buyer, you should negotiate for waiver of default).

- Medium of payment: (cheque, letter of credit, cash, promissory notes, technical expertise/technology, intellectual property, labour, convertible notes and so on.

- Currency in which payment is to be made (for cross border contracts), currency conversion medium, who bears rate of exchange risk?

- Who bears ancillary costs such as cost of share valuation, cost of share transfer and regulatory filings?

Seller's Representations and Warranties:

The seller of the shares has an obligation of full disclosure to the buyer, but the buyer has a duty to carry out its own independent investigation/due diligence on the assets and liabilities attached to the shares. The seller is required to warrant that he has made full disclosure. One risk management tool often employed by the seller or disclosing party is the **Disclosure Letter** by which the seller states the facts known by the seller so that the purchaser cannot come round and say there is breach of warranty because it was already aware of those facts by virtue of the disclosure letter. In addition to this, the seller would normally also give the buyer warranties such as that:

(i) the seller is a company in good standing, or a private individual;

(ii) the seller is the owner or beneficial owner of the shares and it has the right to transfer the shares to the buyer;

(iii) the seller has the authority to enter into the share purchase agreement and perform his obligations under it;

(iv) the shares being sold were validly issued, fully paid, and that they have been issued in full compliance with all federal and state laws and that the buyer will receive the shares free of any liens or encumbrances;

(v) all documents and statements of the seller's business or shares provided to the buyer are correct;

(vi) all financial documents and statements in respect of the shares and seller's business were prepared in accordance with generally accepted accounting principles and fairly present the financial condition of the business;

(vii) the seller has provided a complete and accurate list of its assets, rights and liabilities attached to the shares and there are no undisclosed liabilities;;

(viii) the seller has good and marketable title to the shares;

(ix) the seller has not entered into any other contracts that will affect the seller's performance of its obligations under the share purchase agreement or render the contract unenforceable, except those that have been disclosed under the agreement;

(x) the share sale transaction is not in violation of any federal, state, or local laws or any company policy.

Buyer's Representations and Warranties:

The buyer will generally warrant that:

(i) the buyer is a company in good standing, or a private individual;

(ii) the buyer has the authority to enter into the agreement and perform its obligations under the agreement.

(iii) If the purchase is not being made in cash, the buyer should make representations concerning its financial standing or ability to pay the purchase price in future.

(iv) the buyer is capable and willing to carry out the post transaction plan (for instance in privatization share purchase agreements there is usually at negotiation stage a post privatization plan which BPE obtains from the purchaser and is usually inserted as part of the schedules.

Note: If you are acting for the seller, you should seek to minimize the seller's liability under the seller's warranties. This can be done by disclosing certain facts against the warranties so that liability is limited to the extent of facts disclosed. This is the role played by the Disclosure Letter. You can also negotiate to limit the amount that the buyer can claim for breach of warranty as well as the period of time in which the buyer can claim for breach. But if you are acting for the buyer and the disclosure is material, you should seek to negotiate a reduction in the purchase consideration or have the seller rectify the problem prior to signing the contract.

It is also important to ensure that parties have carried out their independent due diligence on each other and in respect of the transaction. In this regard, financial, technical, commercial and legal due diligence, are key. Usually a data room would have been set up during the due diligence stage and the purchaser would have had the opportunity to make its own judgment by examining the books. This process helps limit the liability of the seller. Nowadays data room is held virtually in cyberspace. We were recently involved in due diligence where the data room was a virtual data room ran by BNP Pariba in Paris and we conducted our due diligence by logging in using pass code supplied by the bank to us.

There is a significant legal difference between warranties and representations. The two terms are increasingly being used conjunctively in commercial contracts but it is important to note that they have different legal consequences and remedies for breach. A representation is a statement of a present or past state of facts. When there is breach of representation, the injured party who has relied on the false representation to his detriment is entitled to a claim in tort for deceit or fraudulent misrepresentation. For such claims the injured party can either rescind the contract or affirm the contract and sue for damages. A warranty on the other hand is a promise that a fact is or will be true in the future, and an indemnity if the statement of fact turns out to be false. In other words, a warranty is an undertaking by the maker to protect the recipient if the circumstances turn out to be different from that which was stated. Simply put, a representation is a statement of an existing fact while a warranty is a statement of a future state of facts or circumstances. The purpose of a warranty is to relieve the recipient from liability of having to determine the correctness or accuracy of the fact in question.

Unlike with representations, contract rescission is not usually available for a breach of warranty. The remedy for breach of warranty is usually indemnity i.e. to give the injured party the benefit of its bargain. Again, unlike with representations, reliance on the statement is not an element of breach of warranty; the injured party may

sue for breach of warranty even if it knew the statement was false (with some exceptions).

A court or tribunal's interpretation of representations and warranties may vary depending on the nature of the contract and the circumstances of each case. However, it is advisable to assume that the two terms have different meanings and consequences, even when used together. In a share purchase agreement the owner or seller will prefer to obtain both warranties and representations, whereas the buyer or investor will prefer to give only one or the other, depending on the circumstances. The solicitor's job is to negotiate to achieve the option that is more favourable to his client.

Corporate Liabilities:

The purchase of the entire shares of a business exposes the buyer to the effect of corporate liabilities. This is unlike the mere purchase of assets of a business which exposes the buyer to liabilities in relation to the purchased assets. Thus the Share Purchase Agreement should carefully describe the liabilities of the company being acquired. The buyer should require seller's warranty that there are no other liabilities not specifically listed. The effect of this is that even though the buyer might still inherit unknown liabilities, it may have recourse back to the seller for not disclosing such liabilities. At times it is possible to exclude specific liabilities. In the end though, you buy a company with its history. There are many instances of undisclosed liability coming up after sales. This raises serious questions. We had privilege of involvement in negotiating with Vodacom of South Africa to acquire Econet Nigeria. They refused on basis of fear of risk of its bad history. Were they right having regard to the litigation and bad publicity that subsequent purchaser such as Celtel, Zain and now Airtel have gone through? Also there is the popular 25 billion undisclosed commercial papers in AP Plc acquisition by Sadiq Petroleum. Now the case law seem to have further complicated the matter. In Caparo case[6] it was held that where investors relied on financial statement prepared by the auditors to make an investment which statement turned out untrue the auditor was not liable to the investor because the financial statement was made for the use of the shareholders and not the investor. It is for this reason that it may not be enough to rely on the data room or financial statements supplied. It may be necessary to engage fresh financial consultants to look at the books and verify from providers to the company. Such case law affect drafting of SPA as the parties continually shift risks.

Litigation:

A provision stating the nature and extent of any litigation affecting the company is generally used to protect the buyer if unknown and unanticipated litigation or antitrust or other governmental regulatory problems arise in the future.

[6] See Caparo Industries Plc. V. Dickman (1990) 2 AC 605

Tax Issues:

Financial experts or tax consultants should be engaged to evaluate and advise on the tax consequences of a share purchase since the implications are quite different from the purchase of assets. In a share purchase agreement, the seller will typically be concerned with obtaining capital gains treatment for the sale.

Shareholders' Consent:

If the sale is structured as a merger, the consent of the shareholders and directors of the business being acquired will be required. This is usually done at the EGM or court ordered meeting called for that purpose. The provisions of ISA 2007 may be applicable. This can trigger other compliance issues such as s.131 of ISA. If the sale is a direct share sale by the shareholders, then all of the shareholders selling will need to sign the agreement otherwise a scheme of arrangement or compromise under section 539 of CAMA may be contemplated so as to bind possibly dissenting shareholders. There may be other shareholders, that is, those not selling but have pre-emptory rights such as a right of first refusal. This can be tricky. Due diligence should disclose all foundation and pre-emptory rights and necessary consents should be obtained long before stage of drafting SPA. Even then warranties that all approvals were in place and obtained should be inserted. On the other hand the Disclosure Letter should state the consents obtained. Again the Disclosure Letter can be attached as a schedule as should the warranties and representations.

Employment/Labour Issues:

The share purchase agreement will also contain several employment-related provisions, especially where the share purchase amounts to a business transfer. Such issues will include retaining employees, continuation or alteration of employee benefits, collective bargaining agreements (if any), termination of employees, etc. The buyer would always not want to be burdened with cost of disengaging employees who may not be required post acquisition. This is usually a sticky point for negotiation. Pre or post acquisition, mass disengagement has legal and financial implication for both seller and buyer and how it is structured affects pricing and viability of the transaction.

Environmental & Host Community Issues

Environmental and host community issues have become major issues in large commercial acquisitions as well as privatization based on SPAs. Typically, the seller company (especially in whole share sale transactions) would have environmental issues especially for construction companies, oil and gas or agricultural undertakings. The share purchase agreement has to address the environmental issues, for instance which party bears which part of the risk in respect of responsibilities for actions taken prior to the sale.

Usually, an environmental audit should be undertaken but this could be expensive and time consuming. There is no hard and fast rule as to who bears the risk. The buyer would ultimately seek protection from environmental risks in relation to matters which are outside its control such as those that have arisen prior to the date of the transaction. The seller on the other hand would seek a fair allocation of environmental risks in the transaction.

Generally, the basis of liability is responsibility or ownership as at the date the liability arose. This may vary depending on the type of transaction. For instance in a share purchase transaction, any environmental liability incurred by the seller (company) before completion will remain with the company and should be inherited by the buyer after completion. This is unlike an asset sale whereby the buyer buys only the assets of the company and does not necessarily inherit all of the environmental liabilities associated with the business and undertakings of the company. The share purchase agreement will usually contain a number of detailed warranties and mechanisms designed to limit the claims. Subject to negotiation, these limitations may be varied or added to take account of environmental matters in terms of cap on liability, time limits and percentage sharing liability. It is common for an environmental indemnity to be given by the seller, and even more difficult for the seller to justify refusing to give environmental warranties or indemnities as buyers and lenders continue to develop stringent policies regarding the assumption of environmental risk.

As a risk management tool the parties may consider obtaining environmental insurance cover, which protects against different environmental risks (i.e. land contamination or warranty and indemnity cover). However, commercial reality is such that the need for insurance may not become apparent until the parties reach a deadlock in late stage negotiations. Reconciling the position of the seller and the buyer in relation to risk allocation on environmental matters on a corporate transaction is likely to continue to result in some heated boardroom negotiations. The debate is only set to continue.[7] The negotiating power of the seller may affect the shift of risk, for instance a margin player negotiating with one major.

Host community issues are another risk which buyers will be wary of as the buyer will usually inherit the seller's obligations or liabilities to the community in which the target company is located. Parties may agree to share the liabilities but usually the seller should settle those that have arisen prior to the share purchase or acquisitions while the buyer should be responsible for obligations or liabilities occurring from the date of completion.

[7] Joanne Gallagher, Environmental Risks in Corporate Transactions, 15 May 2009 available on http://www.thefinancedirector.com accessed on 11th October 2010 4.45 p.m.

Exit Strategy

It is important to negotiate and agree on the exit strategies up front. For instance will the buyer be allowed to sell the whole or part of his shares and will he be allowed to sell to third parties? For a private company this would be relatively easy to determine since there is a right of first refusal for the other shareholders. But that too would pose a challenge where there was a whole share sale.

Usually there should be a lock-in period before which the buyer cannot sell or transfer the whole or part of the shares purchased. This could be a period of 5 – 6 years depending on the nature and term of the contract. In privatization of public enterprises, this is key because government would not want to see an unreliable operator take over an important government asset or undertaking and then gasump on it, that is make quick profit through resale. This will attract speculators rather than solid investors for the sale process. In the same vein, where the shares are purchased or acquired through an SPV, there should be a corresponding lock-in period for the holding company of the buyer in the SPV. Otherwise the lock in period for the shares may be of no use as the buyer may exit from the SPV leaving the government with an undesirable partner.

In a share purchase agreement for public enterprises, it is advisable to insert a clause to the effect that government shall have a first right of refusal in case of sale by the buyer. Note however that right of first refusal is usually reciprocal. Also, some share purchase agreements provide tag along rights to the parties in case they do not exercise their right of first refusal. This means that if the buyer is selling his shares to a third party, the initial seller (in case of partial share sale) can require that his shares be also acquired by the third party at the same price.

For the government there could also be a lock-in period after which it can exit from the balance holding at any time. This may be desirable in some cases where the buyer wishes to have government as a partner for some time at least, in order to quickly resolve and deal with regulatory issues like (licences, land issues, etc). Government will then have a 'put' option exercisable after a certain period of time, say 1 year. The buyer may also negotiate a call option to buy out the seller (especially for privatization of public enterprises) but this should typically get triggered after some time. The general idea is that the buyer is there to stay, and depending on the situation, Government would exit after some time.[8]

[8] See Check List on Shareholders & Share Purchase Agreements, Department of Disinvestment, India available on http://www.divest.nic.in/stsale.htm accessed on 11th October 2010 5.15 p.m.

Note that exit strategy and tag along provisions are often contained in the shareholders agreement but where there is no accompanying shareholders agreement (e.g. in a whole share purchase), then they could be provided in the share purchase agreement. Whatever the case, exit provisions require careful thought and would usually involve more than simple termination of contract. However, termination of a contractual alliance will generally be straightforward compared with an equity joint venture where exit provisions will also need to deal with the interests of the parties in the joint venture vehicle itself (e.g. shares in a joint venture company.

Possible protective exit provisions include :

- Right to transfer shares to a third party, subject to pre-emption rights
- Put option whereby majority shareholder is obliged to buy out the minority's investment
- Redeemable shares issued to minority shareholder; the shares are redeemable at the option of the shareholder usually at a stated price.
- Share buy-back: this is subject to corporate law restrictions and procedures
- Tag along which obliges the majority shareholder to include the minority party's stake at the same price per share, in any sale to a third party of majority shareholder's controlling interest.
- Drag along which gives the selling party a right to oblige every other party to also sell its shareholding to a third party or to the selling party at the same price per share as negotiated by the selling party in any sale to a third party.[9]

Closing:

Conditions for the deal closing should also be addressed. There conditions can be conditions precedent or conditions subsequent. As in Asset Purchase Agreements, closing conditions may include: that all representations and warranties are true and correct; that all internal consents and approvals have been obtained; that all covenants have been complied with; that all government consents or permits necessary have been obtained; that various certificates, transfer documents and legal opinions have been prepared and delivered. Below are some important closing provisions:

- Date, time and place or as parties otherwise agree in writing
- Exchange of documents:

[9] Ian Hewitt, *Joint Ventures,* Thompson Sweet & Maxwell, Fourth Edition, 221 - 223

(i) Existing share certificates endorsed for transfer (with appropriate instrument of transfer e.g. share transfer form) or new share certificate issued in purchaser's name.

(ii) Resignation of officers and directors of seller (and releases, if required by seller or purchaser or both). Appointments of new directors and officers and consents to act.

(iii) Transfer of books, records and company seal to buyer (for sale of whole shares) or rectification of books and records (for part sale)

(iv) Minutes of directors' meetings or unanimous directors' resolution authorizing transfer of shares and the transaction

(v) Constitutional documents evidencing the existence and good standing of the acquiring company.

(vi) Waiver of pre-emption rights/share holders resolution consenting to share transfer (in case of private company)

(vii) Title documents of sellers assets (for whole share purchase)

(viii) Assignment of seller's loans and other liabilities? (for whole share purchase)

(ix) Compliance with Investment and Securities Act (ISA), Companies and Allied Matters Act (CAMA) and other regulations as may be applicable: Who bears responsibility?

(x) Any additional contracts contemplated

In order to limit the buyer's exposure during the closing period, the following provisions may be included in the SPA to offer adequate protection:

- Pre-completion covenants to ensure that the target (seller/vendor company) continues business in its ordinary course and does not carry out certain acts without the consent of the buyer in accordance with a pre-approved consent mechanism;
- Repetition of warranties at completion;
- Option to rescind or terminate the SPA upon a breach of warranty prior to completion;
- A "material adverse change" clause which allows the buyer to refuse to complete the deal if the target has suffered a material adverse change between signing the SPA and the completion of the share sale transaction;
- A long stop date so that the buyer can terminate the SPA if any conditions are not satisfied or waived by a certain date; and
- An escrow account mechanism for release of purchase monies on completion of the process

Note that the above protective provisions are useful where the share purchase is structured as an acquisition or there is part payment structure.

Security for Payments

Effort to privatise the country's premier telecommunication company – NITEL/MTEL – has become a classical case in the study of the failure of privatization in Nigeria. The efforts have severally failed after IIL of London, Pentascope of Netherlands, Orascom of Egypt and Transcorp of Nigeria respectively bid, won and failed at different points in time to make the necessary payments. Currently, the New Generation Consortium of Dubai, which emerged preferred bidder, is yet to pay a 30 per cent advance fee amounting to $750 million of the $2.5billion bid price.

Most transactions involving the partial or complete privatization of government business involve very high value transactions and an objective to ensure the continued existence of the enterprise. Based on the value it is not unusual to have the payments spread over a period. In the circumstance, a number of such transactions have failed because of the inability of the preferred bidder to raise the required funds to complete the transaction. Security for payment is thus a crucial issue for all parties.

In the cause of negotiations parties may spell out the clear terms of the offer including payments and the Supreme Court has held that no issues of revocation of an offer can be raised against a party who has started paying under terms agreed upon by the parties. See the case of F.G.N. V. Zebra Ltd. (2002) 18 NWLR (Part 798) 162.

Revocation has always been the major remedy relied upon in cases of failure to make payments under such agreements but this has left several such transactions crippled. There is therefore the need to provide for some form of security to ensure that payment obligations are met by the purchaser. Some possible options include bank guarantees, sovereign guarantees and indemnities. On the other hand, the seller usually incurs enormous cost in preparing a company for sale and conducting the sale procedure. Where a successful bidder is not responsive, the seller may likely lose the expenses incurred unless the SPA anticipates this and makes adequate provision either in the process or in its provisions. There are a couple of disputes that have arisen even where bonds have been provided or deposit made. See transactions like Global Bank and BPE in the initial sale of NICON Hilton Hotel, and IIL/NITEL First Bank. The question usually arises whether forfeiture clause amounts to damages or penalty. If penalty, it is usually unenforceable.

CONCLUSION

There is nothing more likely to start disagreement among people or countries than an agreement.[10] Therefore in drafting a share purchase agreement or any commercial agreement, attention should be paid to the possible interpretation of words and clauses and ensure that the intention of parties is clear, proper allocation of risks, certainty of rights and obligations, interest and protection of each party, proper execution, amongst other factors. Experienced and skilled transaction advisers should be engaged in the process from start to finish. The modern practice encouraged by the World Bank is to make the SPA short and simple model with most of the hard details contained in the schedule.

THANK YOU.

CHIEF ANTHONY IDIGBE, SAN

[10] Elwyn Brooks White