because the impact of new technology and the importance of data will resonate through a wide variety of industries, the Broadcom intervention may have broader impact than is readily apparent.

Litt: The OPM [Office of Personnel Management] hack a couple of years ago really focused attention on the national security implications of big data. I think we're seeing CFIUS now look at transactions that involve not only traditional tech companies but also transactions that would give foreign acquirers access to large amounts of personal data.

MAL*: Are there any upcoming deals to watch that could potentially suffer a similar fate as Broadcom?*

Townsend: It's a very strong M&A market right now so I fully expect the parameters of CFIUS issues are going to be further developed over the course of this year.

Litt: And clearly any company that's contemplating such a transaction needs to anticipate this.

MERIT MANAGEMENT PROVIDES AN OPPORTUNITY TO REFLECT ON BANKRUPTCY RISKS IN M&A TRANSACTIONS

By Dusty Wolverton, Christian Salaman, and Cecily Dumas

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On February 27, the United States Supreme Court resolved a long-standing circuit split by ruling, in *Merit Management Group, LP v. FTI Consulting, Inc.*[1], that the purchase price paid to a stockholder of an acquired corporation *could* be recovered by the bankruptcy trustee of the buyer, even though the payment had been made through a third-party financial institution (Citizens Bank of Pennsylvania, as escrow agent). Prior to this ruling, the majority of circuit courts had held that such payments could *not* be recovered by a bankruptcy trustee, due to the safe harbor provided by Section 546(e) of the Bankruptcy Code.

While the outcome of *Merit Management* hinged on whether certain payments made through third-party financial institutions could be recovered in bankruptcy, it can also serve as a more general reminder to M&A legal practitioners, or perhaps a "wake-up call" to some, that clients and their stockholders may be at risk of forfeiting consideration previously received in a deal, not because of their own company's liabilities, but because of the liabilities of the buyer. In fact, it may be even more of a wake-up call to those who had previously advised their clients based on the majority view, and now must take a step back to reassess the risks involved.

Much time and effort is spent in most transactions, by both sides, preparing for and conducting due diligence of the target, its business, assets and liabilities, among myriad other concerns. And attorneys regularly spend countless hours drafting and negotiating representations, warranties and related indemnification provisions to address known and unknown liabilities relating to the target's business. Conversely, substantially fewer hours seem to be spent on diligence of the buyer's business and the representations, warranties and related indemnities by the buyer.

Client sensitivities to additional transaction fees, as well as pressures to sign and close a transaction within a given timeframe, certainly require a weighing of the benefits to be gained by further due diligence and additional provisions in a purchase agreement, but legal practitioners should keep in mind the following considerations when advising a target or its stockholders.

At the outset, a general understanding of the bankruptcy principle at issue in *Merit Management* is helpful. In that case, the issue was not whether the debtor intended to defraud its creditors by consummating the acquisition of the target, but instead revolved around whether "constructive fraud" had occurred. Section 548(a)(1)(B) of the Bankruptcy Code provides, in relevant part, that a bankruptcy trustee may avoid a transfer of an interest of a debtor in property if, within two years before the date of the filing of the bankruptcy petition, the debtor voluntarily or involuntarily (a) received less than a reasonably equivalent value in exchange for such transfer and (b) was insolvent on the date that such transfer was made or such obligation was incurred, became insolvent as a result of such transfer or obligation, or intended to incur, or believed it would incur, debts that would be beyond its ability to pay as they matured. In determining whether reasonably equivalent value was received in exchange for a transfer or obligation, a number of courts examine as evidence whether the transfer was made in an arm's length transaction, whether the parties acted in good faith and whether there was a substantial difference between the fair market value of the transfer or obligation and the amount paid.

There are at least two ways that courts have found the existence of constructive fraudulent transfers in M&A transactions. The first is in a leveraged buyout (or "LBO"), where the buyer finances the acquisition using a loan secured by the target's assets. In an LBO, if the target was insolvent at the time of the transaction or becomes insolvent as a result of the transaction, then creditors can make the argument that less than a reasonably equivalent value was received by the target in exchange for granting security interests on its assets, since the loan proceeds are typically paid to the buyer or the selling stockholders and do not inure to the benefit of the target. The second is illustrated by *Merit Management*, where as a result of the purchase of the stock of the target, the buyer was left unable to pay its debts as they became due in part because the business case for the combined business was never fully realized.[2]

The first situation is easy to identify. A target in an LBO will be intimately involved with the financing transaction, since the lender will likely conduct due diligence on the target's business and assets, and moreover, the target may be in the best position to assess whether it is currently insolvent or is likely to be made insolvent as a result of the transaction. The latter, where a buyer becomes unable to meet its debts after completing an acquisition, may be more difficult. For instance, the target and its stockholders are typically not insiders of the buyer and unless the buyer is a publicly traded company, it may not be willing to provide comprehensive financial statements, or if it does, the financial statements may not be audited. The target does not have visibility into the buyer's post-closing business plan and whether the acquisition will be accretive to the value of the buyer. On the other hand, the target is in a good position to establish that the buyer is receiving reasonably equivalent value in the transaction, since it will have been engaged in a marketing process and will have developed some indication of the fair market value of the target as compared to the purchase price being paid in the transaction. The good faith of the buyer in the acquisition is often also shown by its participation in a market process and being an arms-length buyer.

To the extent that a target's management and legal counsel determine that the risk of a transaction being unwound warrants undertaking additional diligence, then given the previous analysis, it would seem appropriate to focus first on solvency—of the target itself in the LBO context, and of the buyer in other contexts—since in the absence of an insolvent debtor—or a debtor who becomes insolvent as a result of the transaction—the second prong of the constructive fraud test is not met and the transaction will not be unwound. In this respect, if the buyer is a private company, it will be important to request financial statements early in order to ask any follow-up questions as the acquisition process moves forward. If, as a consequence of this initial diligence, the target's management and legal counsel have reasonable concern that the buyer may become insolvent in the future, the target should take steps to ensure that the exchange of reasonably equivalent value for the stock of the target is established. This may include recitals pertaining to the target's marketing process, the arms-length relationship between seller and buyer and other evidence that the sale fairly reflects the market value of the target.

Ultimately, in either case, there may always be some risk that a court could find that there has been constructive fraud and avoid the transfer for the benefit of buyer's creditors. Although this risk cannot be eliminated completely, some additional protection can be afforded by the purchase agreement, chiefly through inclusion of buyer solvency representations and warranties (and related indemnification provisions). To explain why these are helpful, assume that the buyer does not represent and warrant that it is, at the time of closing, solvent, and that following the transaction, it will continue to be solvent. Assume further that as a result of the transaction the buyer becomes insolvent, and a court determines that the transaction constituted constructive fraud. In the absence of such solvency representations and warranties, the target's stockholders will be required to return the sale proceeds to the debtor and may have no recourse against the buyer other than the return of the business they sold (potentially in a much worse state that when they sold it). Conversely, if the buyer had represented that it was currently solvent and would remain solvent as a result of the transaction, then these stockholders may have a claim for indemnification against the buyer and would thus be creditors (albeit unsecured) with a claim against the buyer's assets in bankruptcy.

In a typical example of such a provision, the buyer would make representations as to certain standard indicia of its solvency such as ability to its pay debts as they become due and having a surplus of assets over liabilities, and it may also represent that it is not entering the transaction with the intent to defraud its creditors. In negotiating the provision, a buyer may require certain qualifying language to reflect the fact that its solvency may be based, in part, on buyer's reliance on the target's own representations and warranties regarding the assets and business being sold. However, given the typical focus of purchase agreement negotiations on myriad other material factors, such provisions are unlikely to be the subject of intense debate. Nonetheless, we note that a number of recent publicly available transactions do not include them, and, as a result, counsel to a target or its stockholders should be mindful of this when reviewing drafts prepared by buyer's counsel.

Finally, in any given transaction, whether or not additional diligence is undertaken or representations and warranties are included in the definitive transaction agreements, the risks described in this article certainly merit discussion between an M&A legal practitioner and his or her client.

ENDNOTES:

[1]*Merit Management Group, LP v. FTI Consulting, Inc.*, 138 S. Ct. 883, 65 Bankr. Ct. Dec. (CRR) 92 (2018).

[2]Note that the Supreme Court did not reach the question of whether the debtor received less than a reasonably equivalent value in exchange for the consideration paid to acquire the stock of the target and remanded the case for further proceedings.

BIG DATA AND MERGER CONTROL IN THE EU

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The rapid expansion in companies' use of big data and algorithms has attracted considerable attention from European antitrust authorities. In 2016, the French and German authorities published a joint study on big data and antitrust[1] in which they acknowledged the many benefits of big data but also outlined a variety of potential antitrust concerns. In late 2017, the UK CMA announced the formation of a new technology team to keep pace with the use of algorithms, artificial intelligence and big data in 2017.[2]

Meanwhile, the European Commission has addressed big data issues primarily in the merger review context, including several recent merger cases, *Verizon/Yahoo*.[3] *Microsoft/LinkedIn*,[4] and *Facebook/WhatsApp*.[5] The Commission looks at big data issues from two main perspectives; so-called "vertical" issues, whether the transaction would give the merged entity the incentive and ability to foreclose downstream competitors' access to data as an input, and so-called "horizontal" issues, whether a merger raises barriers to entry through the combination of the parties' datasets.

As discussed below, the Commission's treatment of big-data-related vertical issues is relatively clear and in line with the Commission's published Guidelines (the "Non-Horizontal Guidelines")[6] on the assessment of non-horizontal mergers under the EU Merger Regulation (EUMR). Nonetheless, the Commission's decisions highlight the difficulties in applying the traditional framework to situations in which the data in question are not already being offered as a product to third parties.

The Commission's treatment of horizontal issues raises even more questions, as the Commis-