



Tips for Taking on the Role of Shareholder Representative

Individuals considering serving as a shareholder representative following the closing of an M&A transaction often ask the following: How much risk is involved? How hard will it be? How much time will it take? The following guide outlines issues to consider and provides tips for anyone considering taking on the role. It is based on our experience from having served as a shareholder representative on over 250 merger transactions—more than anyone else.

Tips to Help Mitigate Risk

Personal liability.

- Review your insurance policies and determine whether actions you would take as a representative are covered. Since you would not be acting as an officer or director of the company, the D&O policy likely does not apply.
- Consider having your own legal counsel review the merger and escrow agreements. You generally are not a client of the law firm that is managing the transaction; the company is their client. Therefore, you may want to make sure your interests are being properly protected in connection with assuming the role of the representative.

Lawsuit risk.

- Understand that you can be made a party to a lawsuit even if you do nothing wrong. If a dispute related to the transaction goes to litigation, the representative is usually named as either the plaintiff or defendant. In our experience, approximately 4% of transactions end up in litigation following closing, so this scenario can and does occur.
- Determine the consequences of being named in litigation to you and, if applicable, your fund. When fundraising, most funds have to disclose to potential investors all lawsuits to which either the fund or its partners are a party. In addition, if you are or might be applying for a personal loan, mortgage, or

even health insurance in the years following closing of the transaction, being in litigation could jeopardize your approval.

- Consider how you will fund litigation if it arises. Will you have to front the money to pay expenses and hope to be reimbursed later? Will an expense fund be available? Address these issues prior to closing.

Indemnification and Exculpation.

- Review the indemnification terms of the merger agreement applicable to the representative and ensure that you understand them and are comfortable with them. If not, this may be one of the reasons to consider engaging separate counsel.

Conflicts.

- Review potential conflicts you could have between your relationship to the buyer and your duties to the former stockholders you represent as shareholder representative. If there is a conflict, you may find yourself in a position that is impossible to navigate. This is especially true if you will be employed by the buyer after closing or may want to sell another portfolio company to them.
- Consider potential conflicts with the other stockholders. For instance, if you hold a different class or series of stock than other stockholders, might they assert that you were not adequately looking after their interests?

Tips to Prepare for the Time Commitment

Claims.

- The big unknown variable anytime someone agrees to be the representative is whether disputes will arise after closing. According to our data, a claim of some sort is made by the buyer in 56% of transactions (which does not include potential disputes over contingent consideration or earnouts).
- When a claims are made, they take 8 months on average to resolve. If you happen to get embroiled in a dispute, it is unlikely that you will be able to get out of it once the process has started.
- Consider when claims might occur. In our experience, 45% of indemnification claims are made during the last week of the escrow period. Be sure to plan ahead and understand the time commitment for claims made at the 11th hour.

Administrative tasks.

- If you're the representative, the stockholders, escrow bank, buyer, paying agent and any other related parties will all look to you with any open questions. Disbursements of proceeds can involve a lot of work if you will be required to confirm payments amounts or effect payments.
- You can also find yourself responsible for issues you never anticipated, such as being subject to tax reporting related to foreign accounts or escheat laws if any former stockholders cannot be located. Be prepared to allocate substantial time to administrative tasks even when no claims are made.

Date and term tracking.

- If you agree to be the representative, at the time of closing we suggest that you go through the merger agreement in detail and record the important dates and terms that will be relevant in the future. You will need a system to accurately track these terms years into the future. Missing a date could subject you to personal liability.

Always remember, as shareholder representative you are a fiduciary.

Tips to Anticipate Required Resources

You're on your own.

- Serving as a representative is usually something you do alone. You are no longer part of a Board or management team. Anything that needs to be done will need to be done by you. If an issue comes up and you do not have the expertise to address it, you will be on your own to figure out a solution.

Determine who and what will be available to you.

- Your former management team might not be able to speak with you after closing if they continue to work for the combined company. Others may simply lose interest or attention.
- You may no longer have access to the company's files and documents.
- The law firm that represented your side in connection with the transaction might not be available after closing due to conflicts issues. Make sure you plan ahead in thinking about what you might need and how you will get it.

Determine how you will pay for any outside assistance that might be needed.

- If you need help from accountants, attorneys or other advisors, determine how the related expenses will be paid. Some former employees will not want to spend significant time on post-closing matters unless they are compensated.

Quick Tips

- Understand your insurance coverage
- Know your rights and obligations
- Determine who will be available to you after closing
- Consider the implications of being named a party to a lawsuit
- Prepare for the potential time commitment
- Deliver periodic reports to shareholders to mitigate risks and questions.