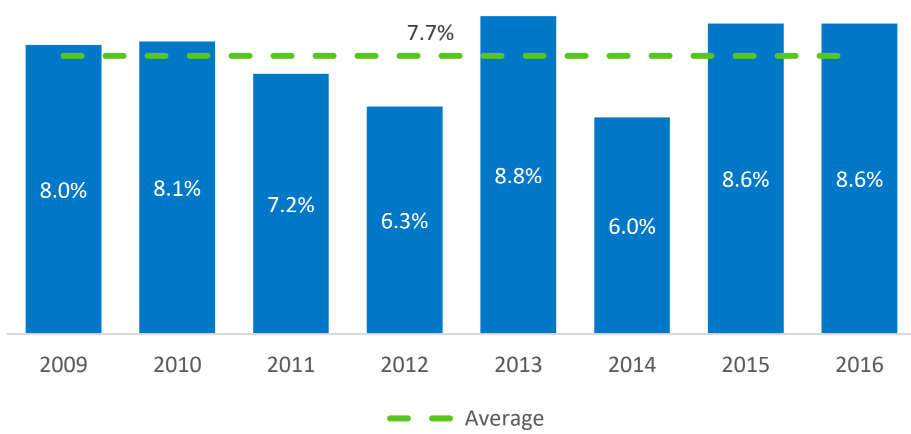
Valitas Insights: Confidentiality is King… Transaction Leaks and Private Sellers

Intralinks Annual M&A Leaks Report 2017 dives into the investigative analysis of deal leakage, drawing on a sample of 5,997 publicly traded targets. The study determined that an average of 7.7% of deals were leaked over the 2009 – 2016 period. The most compelling finding was that, over this period, leaked transactions exhibited a median premium 20% higher than deals that were not leaked.

Percentage of Worldwide M&A Leaks



Median Premium

	2015	2016	2009 - 2016
Leak	38%	54%	47%
No Leak	26%	24%	27%

Source: Intralinks Annual M&A Leaks Report 2017

What explains this leak premium? There are a couple of plausible explanations:

1. Historically, leaked deals have a higher rate of rival bidders. More rival bidders increase competitive tension in the process, resulting in higher bid prices relative to unleaked deals; and
2. Leaking a deal may draw out the "optimal" acquirer, the one that has the greatest potential to realize synergies, and can therefore pay the highest price.[1]

As our focus is on private mid-market companies, we considered whether this leak premium effect might apply to privately owned businesses. In our experience, in contrast to large publicly traded entities, private sellers tend to have a stronger personal connection to their business, employees, and other stakeholders. Because of this, the negative effects of an informational leak are amplified, and are

[1] Intralinks Report, p. 7

likely to outweigh any benefits that may accrue. In a private mid-market transaction, negative effects are likely to materialize in three areas:

1. **Undermining stakeholder confidence:** A leaked sale can be perceived negatively by employees, customers and other stakeholders. Employee confidence in future employment diminishes, customers fear a disruption to their product or service, and overall uncertainty creates potential risks for other stakeholders. This is often detrimental to business operations and disruptive to the sale process.
2. **Benefitting strategic competitors:** Without the correct protocols in place, competitors may benefit by leveraging confidential internal information without legal repercussion.
3. **Damaging employee and stakeholder relationships:** A significant consequence of information leakage is the risk of damage to personal relationships. Private business owners often have longstanding, strong personal relationships with their employees and stakeholders. For these individuals, learning about a sales process through leaked information is likely to generate a sense of betrayal, which could have negative repercussions for the sale completion.

Frank Guarascio, a senior partner at leading law firm Blake, Cassels & Graydon, has seen the negative effect of transaction leaks in his own active M&A practice. “Private companies typically have a narrower band of relationships than larger public companies, and are more dependent on those relationships,” he told us. “As a result, leaks that damage customer, supplier, or employee relationships can negatively impact a company’s ability to complete a transaction at its highest value, and in some cases, even interfere with the company’s ability to close the deal.”

Regardless of how watertight the process is, the possibility of a leak remains, and a contingency plan addressing this possibility is essential. We subscribe to a practical rule here at Valitas: *expect the best and prepare for the worst.*

Confidentiality and leak mitigation is a priority for Valitas. You can read about our approach in our Confidentiality and Communications Protocols.