

Key takeaways

Compensation Challenges in M&A Transactions

At our Comp Talks session on September 13, 2023 – **Compensation Challenges in M&A Transactions** – Cooley partners Ali Murata, Rama Padmanabhan and Nyron Persaud discussed various compensation-related challenges in M&A transactions and shared their views on navigating those challenges. Below are some key takeaways summarized by Cooley associate Tony Guan.

Current macroeconomic factors have led to an uptick in the use of equity-based deal consideration and cash-preserving deal structures. We've seen an increase in stock-for-stock (as opposed to cash-for-stock) transactions, and deal volume and transaction valuation to date has been lower than in previous years. Many 2023 transactions have been driven by strategic acquisition of sought-after technology and talent.

Share reserve utilization rates have been a key consideration in the 2023 deal market. If not appropriately addressed during deal design and negotiation, rollovers and go-forward equity retention arrangements can strain an acquirer's equity incentive plan share reserve. Some possible strategic approaches to extend the life of the acquiring company's share reserve under shareholder-approved equity incentive plans include utilizing the Nasdaq and New York Stock Exchange exceptions for substitute awards, assuming unused share reserves under target plan(s), inducement grants and – where the acquiring company is otherwise seeking shareholder approval in connection with a transaction – presenting a new equity plan to the acquiring company's shareholders for approval.

Companies should be mindful of the overlapping and varied priorities of various stakeholders (investors, board, management and employees) when structuring a deal. Parties should carefully consider equity treatment, retention needs and how to tailor executive compensation arrangements to align with deal objectives, keeping in mind the impact to the overall deal value. Additionally, many recent M&A deals have taken longer to close due to increased regulatory scrutiny. Special consideration should be given to interim operating covenants and their restrictions on compensation adjustments, including any increases, bonuses and equity awards, particularly if employee retention is crucial.

Evaluating Section 280G “golden parachute” tax implications early on – particularly for public companies – can help with mitigation strategies. When companies engage advisors early in the transaction process, a fuller range of mitigation strategies can be considered (e.g., designing compensation programs to minimize parachute payments and potentially timing bonus payouts and equity vesting to increase the Section 280G safe harbor threshold). For privately held companies, outside counsel can help navigate the complex processes and disclosures required to seek a shareholder vote, which can “cleanse” the adverse tax consequences of excess parachute payments.

Compensation-related disclosures are often required in connection with a transaction. Given the sensitivity of personal compensation information, companies should be mindful of events and communications

Comp Talks

that could trigger third-party disclosure requirements relating to management and other interested party compensation and employment arrangements. For public companies, compensation disclosures will include details of the deal-related consideration paid or awarded to executives and the overall equity treatment in shareholder solicitation and Form 8-K filings, as well as potential post-transaction employment arrangements. For private companies, the deal team should be mindful of the implications of Section 280G and the disclosure required for a shareholder cleansing vote, which will result in detailed disclosure of executive and management compensation arrangements constituting potential parachute payments to all shareholders eligible to vote.

Alessandra Murata

Partner
Palo Alto

Rama Padmanabhan

Partner
San Diego

Nyron Persaud

Partner
New York

Tony Guan

Associate
Santa Monica

Janice Chan

Resource Attorney
New York