

The background features a dynamic, abstract design with numerous thin, parallel lines in shades of red and blue, creating a sense of motion and depth. The lines are most concentrated on the right side and fan out towards the left.

Morgan Lewis

THE INS AND OUTS OF NON- DISCLOSURE AGREEMENTS AND LETTERS OF INTENT

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January 23, 2024

The background features a dynamic, abstract composition of light trails. On the left, numerous thin, parallel lines in shades of red and orange streak across the frame, creating a sense of motion. These lines transition into a more solid, deep blue area on the right, which is also filled with subtle, lighter blue streaks. The overall effect is one of high energy and modern technology.

NON-DISCLOSURE AGREEMENTS

INITIAL CONSIDERATIONS

Non-Disclosure Agreements

Why Have a Written Confidentiality Agreement?

- Confidentiality agreements are standard and an expected part of most negotiated deals
- Protection of trade secrets under state law can be lost (deemed waived) if they are disclosed without a written agreement
- Written contracts are typically easier to enforce
- Written confidentiality agreements are often required under prior agreements with third parties
- They avoid confusion over what the parties consider to be confidential
- The parties have more flexibility in defining what is confidential
- The parties can specify what they expect from each other
- Confidentiality agreements often cover issues unrelated to confidentiality, such as non-solicitation, exclusivity and absence of binding commitments to complete a transaction

Non-Disclosure Agreements

Are You More Likely to Receive or Disclose Information?

- A simple question with big implications
- Whether you are primarily disclosing confidential information or receiving confidential information will drive some of your strategy for the structure of the confidentiality agreement
- A Buyer's interest is different from a Seller's interest
- Buyer's Interest:
 - A Buyer typically wants the exclusions from confidential information to be as broad as possible and permission to disclose all confidential information to Buyer's advisors and representatives and any financing sources
- Seller's Interest:
 - A Seller typically wants the Buyer's exclusions to be as narrow as possible and, to the extent possible, to exert control over the sale process through confidentiality provisions and limitations on disclosures to third parties

Non-Disclosure Agreements

Should the NDA be unilateral or mutual?

Unilateral

vs.

Mutual

Positive:

- Restricts the disclosing party only

Challenges:

- Does not protect confidential information of the other party that may be disclosed later
- Does not protect nonbusiness information (such as deal terms or deal process) that both parties will likely want to keep confidential

Positives:

- Protects confidential information of both parties
- Protects nonbusiness information about the actual deal
- Provides a more balanced form that typically results in a faster review and signing process

Challenge:

- Imposes restrictions on both parties to the transaction, regardless of which party has more leverage in the deal

Non-Disclosure Agreements

When Should We Sign an NDA?

- As soon as possible
- Prior to disclosure of any confidential information

Practice Tip

- If disclosures of confidential information have been made prior to entering into a confidentiality agreement, make sure that the confidentiality agreement specifically covers all prior disclosures (written and oral)

Non-Disclosure Agreements

Should the NDA be separate or part of the Term Sheet?

Having a separate confidentiality agreement:

- Gives the parties the flexibility to conduct due diligence of certain nonpublic information before negotiating a term sheet or letter of intent
- Is typically easier to negotiate
- Provides the parties with written protection in the event of disclosure of confidential information prior to entering into a term sheet or letter of intent

Practice Tips

- Confidentiality provisions included in a term sheet or letter of intent should be made expressly binding on the parties
- A separate confidentiality agreement should be incorporated by reference in the term sheet or letter of intent

Non-Disclosure Agreements

Is the Disclosing Party a Public Company?

If you answer "**YES**" to this question, then consider the following:

- Include a standstill agreement in the confidentiality agreement restricting Buyer's unsolicited bids for the Seller
- Obtain a representation that the recipient and its representatives are in compliance with securities laws (or, at a minimum, are aware of their obligations under securities laws)
- Determine whether the terms of the confidentiality agreement qualify for Regulation FD under the Securities Exchange Act of 1934, as amended – should qualify in most circumstances

Non-Disclosure Agreements

Limitations on Effectiveness

- The disclosing party cannot “undisclose” confidential information that has been wrongfully disclosed and has become part of the public domain
- The disclosing party’s remedy for wrongful disclosure of confidential information is limited and damages for breach of contract may be the only legal remedy
- The disclosing party has the burden of proof with respect to proving that a breach has occurred
- The disclosing party may not be able to effectively prevent the recipient of confidential information from inevitably taking the confidential information into account in its own commercial plans

Practice Tip

- To protect confidential information, the disclosing party should carefully manage the disclosure process, consider additional confidentiality procedures (i.e., “clean teams”) for extremely secretive information, and have a contingency plan for dealing with leaks

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NON-DISCLOSURE AGREEMENTS

PROVISIONS OF NOTE

Non-Disclosure Agreements

- **Parties:**
 - Buyer
 - Seller
 - Others
 - Investment Banks
 - Parent Companies
 - Key Sellers

Non-Disclosure Agreements

- Permitted Disclosures to Affiliates/Representatives:
 - Disclosing party may require Affiliates/Representatives to sign a separate acknowledgment agreement to be bound by the NDA
 - Disclosing party may hold receiving party responsible for any breach of Affiliates/Representatives.

Practice Tips

- Even when not required by agreement to do so, Buyers and Sellers often have their Representatives enter into separate confidentiality agreements or acknowledge the terms of the confidentiality agreements as a matter of practice
- Note that certain Representatives (such as lenders, investment bankers, and law firms) may not wish to be bound by certain sections of the Buyer's or Seller's confidentiality agreement, such as the standstill or nonhire provisions

Non-Disclosure Agreements

Definition of “Confidential Information”

- Defining what is confidential is central to any confidentiality agreement
- Types of Matters:
 - Business information (including trade secrets)
 - Derivatives of business information
 - The contemplated transaction itself, including any terms
- Labeling disclosed information as “Confidential”

Practice Tips

- The confidentiality agreement should make it clear when confidential information is being disclosed.
- If the confidentiality agreement requires certain steps to be taken for information to be protected, such as marking the information as confidential, the disclosing party must be very careful that this process is followed. In general, providers of confidential information should resist this requirement.
- Disclosing parties must also be careful not to disclose information that is restricted by other confidentiality agreements.

Non-Disclosure Agreements

Exceptions to Confidentiality

- Is or becomes public other than through a breach of the confidentiality agreement by the recipient
- Was already in the recipient's possession
- Becomes available through a third party not bound by a confidentiality agreement or obligation
- Is independently developed by the recipient without using the confidential information

- Buyers usually require that all of these exclusions apply to the "Confidential Information" definition generally and not just to the "nondisclosure" provisions

Non-Disclosure Agreements

Other Common Exceptions to Confidentiality

- Disclosing the existence and terms of the deal to a bank or other lending source to secure financing
- Disclosures required by law
 - Confidentiality agreements usually allow the recipient to disclose confidential information if required to do so by court order or other legal process
 - The recipient usually has to notify the disclosing party of any such order and cooperate (at the disclosing party's cost) with the disclosing party to obtain a protective order

Non-Disclosure Agreements

Permitted Use and Restrictions on Disclosures

- Making clear what the information can be used for
- Mutually acceptable or agreed form of transaction
- Financing commitments

Non-Disclosure Agreements

Issues with Direct Competitors

- What level of information should the parties disclose if they are direct competitors?
 - Consider business and legal (antitrust) risks
- Direct competitors should consider the following when contemplating the terms of a confidentiality agreement:
 - Disclosures may be limited to aggregated information, or sensitive information may otherwise be masked
 - For sensitive information, consider signing a separate nondisclosure agreement (NDA) and a “clean team” approach with much more specific provisions and controls regarding the disclosure of such information
 - Avoid reviewing any documents that may lead to a claim of misappropriation of information
 - Be sure to check whether sharing certain information with a competitor violates any antitrust laws; a violation could kill the deal or result in regulatory action

Non-Disclosure Agreements

Term

- Indefinite or termination upon a certain date or event
- Depends on the type of information involved and how fast such information changes
- Disclosing parties typically prefer an indefinite period
- Recipients typically prefer a set term

Practice Tip

- Be sure to set specific expiration dates for those provisions that are not related to confidentiality obligations (for example, standstill agreements or non-solicitation clauses)

Non-Disclosure Agreements

Return of Confidential Information

- Confidentiality agreements typically provide for the return of confidential information in the following circumstances:
 - On the termination of negotiations between the parties
 - At the end of the term of the agreement
 - At any time upon the disclosing party's request
- Recipients often want:
 - The option to destroy the confidential information instead of returning it to the disclosing party
 - To include language that allows them to keep copies of the confidential information for archival or evidentiary purposes or if required to do so under law or professional standards

Practice Tip:

- Disclosing parties should make sure they have rights to the return of their confidential information or an adequate process to confirm destruction or archival under satisfactory procedures

Non-Disclosure Agreements

Remedies

- Injunctive relief in addition to monetary damages
- Indemnification provision holding the recipient responsible for all costs relating to the enforcement of the agreement
 - Recipients will resist including the indemnification provision
 - A typical compromise is to have the losing side to a dispute pay the fees and expenses (including legal fees)

No-Disclosure Agreements

Other Covenants/Provisions

- No Representations or Warranties
 - The disclosing party may clarify that it makes no representations or warranties with respect to any of the disclosed information. If the recipient claims that the information is incomplete or inaccurate in any way, the disclosing party points to this clause to avoid liability.
- Non-solicitation / Nonhire
 - Restricts the recipient from soliciting and/or hiring the disclosing party's employees for a certain period of time (one year is common). Parties will negotiate whether this is non-solicitation or nonhire, and whether it applies to all employees or just more senior people.
 - Sometimes will restrict the recipient from soliciting the disclosing party's customers and suppliers.

No-Disclosure Agreements

Other Covenants/Provisions

- Standstill Agreement
 - May be included in the confidentiality agreement when the Seller is a public company.
 - Prevents the prospective Buyer from making a hostile takeover attempt after the parties fail to complete a friendly deal when the Buyer has had access to the Seller's confidential information.
 - Often limits the Buyer's ability to buy and sell the Seller's stock.
 - Buyers often seek to limit the term of the standstill to a period typically ranging from 6 months to 18 months.
 - Sometimes includes a "don't ask, don't waive" provision limiting a Buyer from requesting a waiver of the standstill. This may raise issues about the adequacy of the sale process and the Seller board's fulfillment of its fiduciary duties and should be reviewed carefully.
 - Buyers may also seek to have the standstill "fall away" in certain circumstances, such as once the Seller signs up a deal with another party, or if the Seller becomes subject to a "hostile" bid, to preserve Buyer's options.

Non-Disclosure Agreements

Other Covenants/Provisions

- Trading in Securities
 - Use when the disclosing party is a public company.
 - Reminds the parties of their obligations under securities laws.
- Keeping quiet about the deal
 - Prohibits the parties from making a public announcement or other disclosure about the deal unless agreed to in advance by both sides. Both sides can have an interest in keeping negotiations quiet.
- Exclusivity
 - Sometimes referred to as a “no-shop” clause, this provision requires the Seller to deal exclusively with the Buyer for a certain period of time.
 - Exclusivity agreements are usually separate agreements or sometimes included in the term sheets/letters of intent for deals.
 - Can be problematic for a public Seller, depending on the length of the exclusivity period and size of the deal.

Non-Disclosure Agreements

Other Covenants/Provisions

- No license granted
- Obligation to inform of unauthorized disclosure
- No further obligations
- Residual rights
 - Residual rights clauses allow the recipient's employees to use any confidential information retained in their memories
 - Sellers often strongly object to residual rights clauses and have concerns over abuse

Practice Tip:

- To limit potential abuse, some residual rights provisions state that employees cannot “intentionally” remember information to sidestep confidentiality obligations

Non-Disclosure Agreements

Miscellaneous Provisions

- Often viewed as “standard” or “boilerplate” but may have unintended consequences, restricting the Buyer’s activities in the industry and the Buyer’s options as the negotiations progress, even if a transaction never materializes
- Terms may prove very consequential in the event of a subsequent dispute between the parties

Non-Disclosure Agreements

Miscellaneous Provisions

- Topics include
 - Entire agreement
 - Assignment
 - Choice of law and jurisdiction
 - Waiver of jury trials
 - Availability of equitable relief
 - Notice provisions
 - Amendments and waivers

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LETTERS OF INTENT

INITIAL CONSIDERATIONS

Letters of Intent

Initial Considerations

- Watch out for unintended binding contracts
- Auction process

Practice Tips

- Prior to negotiating a Letter of Intent (LOI), think through and assess:
 - Why are we negotiating an LOI? Is my side better off just signing an NDA and (maybe) an exclusivity agreement, rather than an LOI?
 - If an LOI will be prepared, is my side better off with a more detailed/less detailed LOI or more binding/less binding LOI?

Letters of Intent

Why Sign a Letter of Intent?

- Get “buy-in” on the deal from the business teams
- Opportunity to confront certain issues up front before incurring substantial deal expenses or devoting significant time dealing with the counterparty
- Develop a “roadmap” for the transaction
- The Seller sees a level of commitment before disclosing confidential information
- The Buyer can obtain exclusivity, break-up fee, expense reimbursement provisions

Letters of Intent

Why Avoid Signing a Letter of Intent?

- Time to negotiate – could spend this time on negotiating definitive documents
- Obligation to negotiate in good faith
- Creates inflexibility on terms of proposed deal – may prematurely lock in parties to terms they later don't like

Letters of Intent

Private vs. Public Company Issues

- Possible disclosure issues if a public company signs a letter of intent for a material transaction
- As a way to address disclosure issues, parties may use an exclusivity letter with a separate unexecuted term sheet

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LETTERS OF INTENT

CONTENTS OF AN LOI

Letters of Intent

Contents of a Letter of Intent

- Parties to letter of intent
 - Buyer (perhaps Parent Company)
 - Seller
- Description of transaction
 - Stock/asset/merger
 - Price
 - Purchase price adjustments, Holdbacks, Earnouts

Letters of Intent

Contents of a Letter of Intent

- Conditions to the transaction
 - Escrow
 - Financings (buyer or seller)
- Detailed versus Skeleton

Letters of Intent

Contents of a Letter of Intent

- Binding LOI provisions
 - Exclusivity
 - Fiduciary Out
 - Break Up Fee, Reverse Break Up Fee, Expense Reimbursement
 - Conduct of business after execution of letter
 - Access
 - Expenses

Practice Tip:

- Parties should be careful not to undo useful “nonbinding” language in the LOI through conduct indicating a binding commitment.

Letters of Intent

Contents of a Letter of Intent Continued

- Termination
- Binding and nonbinding provisions
- Implied duty to negotiate in good faith
- Waiver of jury trial

Practice Tip:

- Consider adding a provision eliminating any implied duty to negotiate in good faith. As an alternative, minimize the impact of any implied duty by adding unilateral termination provisions to the LOI or outside termination dates.
- Even though the LOI may be nonbinding, prepare for disputes – consider adding jury trial waiver, governing law, forum selection clause.

Key Takeaways for NDAs and LOIs

- Focus on definition of “confidential information” and exclusions
- Ensure that the NDA permits sharing of information to those representatives you need to get the deal done
- Have a contingency plan for dealing with leaks and take appropriate measures to protect extremely sensitive information.
- Be careful not to create binding contract when entering into an LOI– clarify which provisions, if any, are binding, and which are not binding.
- Although deal terms set forth in an LOI are typically marked as not binding, deviating from those terms in the definitive can cause negotiation disputes.

A long-exposure photograph of a highway at night, showing vibrant red and blue light trails from cars. The trails curve from the top left towards the bottom right, creating a sense of motion and depth. The background is a dark, deep blue.

QUESTIONS?

Biography



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Greer Longer focuses on mergers and acquisitions with an emphasis on advising middle market private equity firms and financial sponsors on control investments, liquidity events, joint ventures, and equityholder arrangements. She regularly counsels private equity portfolio companies on a variety of issues, including add-on transactions, management team incentives, and general corporate matters. Greer assists private and public companies across a wide range of industries, including specialty manufacturing, consumer brands and products, food products, healthcare, and telecom.

Biography



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Corey S. Mueller advises clients in corporate and securities matters. His practice centers on venture capital financing, private equity transactions, mergers and acquisitions, and securities, with an emphasis on investment in emerging companies. Prior to joining Morgan Lewis, Corey interned at the SEC's Enforcement Division in San Francisco and at a boutique bankruptcy law firm in Walnut Creek, California. In law school, he volunteered with the Investor Justice Clinic, assisting clients who could not otherwise afford legal representation in FINRA arbitration.

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