$1.50 VOL. 36 NO. 10 www.ocbj.com MARCH 11-17, 2013

ORANGE COUNTY BUSINESS JOURNAL

New Drill on Due Diligence

Pace Quickens for M&A in OC Despite Heightened Caution Among Buyers and Sellers

By JANE YU

Due diligence on mergers and acquisitions has gotten increasingly rigorous in the past couple of years, with prospective buyers and sellers more sensitive to potential risks in the wake of the recent financial crisis and recession, and lenders maintaining tougher standards.

The heightened caution on deals hasn't slowed business down for Orange County law offices, investment banks and accountants.

Data from Los Angeles-based investment bank **B. Riley & Co.** indicate that OC remained busy on M&A for the second year in a row (see related story, page 28).

The new rigor on due diligence meant the local gains were hard-earned, according to **Stephen Perry**, a managing director at Irvine-based investment bank **Janes Capital Partners**.

"Due diligence is taking longer, it's more thorough—it's resulting in higher risk and incidence of deal 'fallout,' " Perry said. "Deals are getting done; they just take longer. They take more man hours to complete."

Janes Capital specializes in the aerospace and defense industry. It wrapped up 2012 with six deals for a combined value of about $475 million.

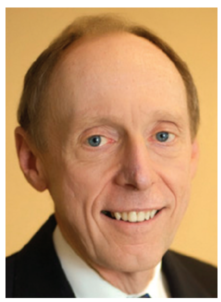
That was "about twice our typical activity," Perry said, in part buoyed by "a spike in activity in the fourth quarter" due to uncertainty about tax-rate increases in 2013 (see related story, page 30).

Another OC firm that saw a banner year in terms of M&A transactions was Costa Mesa-based law firm **Rutan & Tucker LLP**.

George Wall, a partner in the firm's corporate section, said he worked on 25 deals last year, compared with the "usual 15." The combined value topped $2 billion, with disclosed prices ranging from $1 million to $500 million.

"Generally, the bigger the transaction or the target, there are more things that need to be addressed," Wall said. "However, [regardless of size], the complexities that can rise on a particular transaction [can vary]. There are the legal components on structuring the transaction. There are problems that may be unique to that particular company. Those can include not just accounting issues or environmental issues; they can also be personality issues, as well as passive and active owners of a company."

Wall said his team faced an "extremely complex" situation when representing **maxIT Healthcare Holdings Inc.** in a $500 million sale



Rutan's Wall: 25 deals last year, up from the "usual 15"

Janes Capital's Perry: six deals combined for about $475 million

by Los Angeles-based private equity firm **Riordan Lewis & Haden** to **Science Applications International Corp.** in McLean, Va. **Kenneth Hubbs**, a managing director in Riordan's Irvine office, oversaw maxIT for five years before the exit.

"There were a couple of thousand employees all across the country," Wall said. "So then there were complicated stock option plans, and there were a number of consulting contracts regarding the assignability of those contracts because of the change of control. I believe the letter of intent was signed in the latter part of June, and we closed in the middle of August. Two months. That was on a fast track. We had to put a lot of people on it, divide it all up."

Smaller deals generally tend to be simpler, thanks to "fewer moving parts," according to **Wayne Pinnell**, managing partner of Irvine-based accounting firm **Haskell & White LLP**.

Pinnell recalled a "relatively simple" deal last year that included only inventory and intangible assets for "a few hundred thousand" dollars.

"The process involved very short documents," he said. "It was straightforward. And … they were able to figure out [the purchase price] pretty easily. Asset purchases are easier, because you can cherry-pick ... and know what you're getting. But when you buy the company's stock, you get all the assets and all the liabilities—including the liabilities that are not disclosed."

Pinnell heads the firm's overall operations, while also serving as an audit partner.

"From the buy side in the due diligence process, we go into the seller's records, and we have to understand the client base [and] technology … ultimately helping the buyer understand what they're buying," Pinnell said. "Sometimes you don't know what you're getting."

It can work the other way, too.

"Sometimes sellers don't know what they're selling," added **Gary Curtis**, corporate tax partner who heads Haskell & White's M&A practice. "Sellers want to sell stock, and buyers typically want to buy assets. So reconciling that can be a lot of complexity in itself."

Haskell & White had about half a dozen transactions last year, a "strong year," according to Pinnell, considering "the fairly lengthy process of getting through the due diligence process and reaching agreements … which could take around six months."

Activity in OC has generally slowed down in the first few months of this year, compared with how 2012 ended, but "that's been typical for the past three years," he said.

That's been the norm globally, too.

An analysis of data from Janes Capital indicates that the total number of deals around the world in the fourth quarters of recent years is 10% higher than the sum for the first quarters of those years.

"As this year progresses there will be much more momentum on the transactions and more traction," Rutan's Wall said.

Macroeconomics and politics remain concerns for all parties involved in the M&A market, "given the fiscal cliff, sequestration and debt-ceiling issues dominating headlines and airwaves," according to **Richard Anderson**, a managing director at the Irvine office of investment banking firm **Moss Adams Capital LLC**. "However, M&A activity tracks the trajectory of the global stock markets, [which] have materially advanced in the first two months of the year. This, coupled with vast sums of cash held by corporations and committed equity capital held by private equity groups—and the stage is set for an incredible amount of transactions." ■