ABOVE THE LAW

Reprinted with permission
from Breaking Media, Inc.

Finding A Way Through A Tight Deal Space

Leaders of WilmerHale's life sciences practice share trends they see regarding acquisitions and initial public offerings.

By JON SHAZAR

May 12, 2017

Stuart Falber

Belinda Juran

Last year's contentious U.S. presidential election is often blamed for the slowdown in dealmaking activity in the life sciences space. While the uncertainty surrounding that contest certainly had an impact, Stuart Falber and Belinda Juran see other secular trends that have made acquisitions and initial public offerings less attractive — and often impossible — forcing companies to seek new partnerships and sources of funding.

Falber and Juran are co-heads of WilmerHale's life sciences practice, which was named one of the top deal firms in the space in the most recent update to the Life Sciences Law Firm Index from Lake Whillans, Above the Law, and MedCity News. The two discussed the current drags on the market, innovative approaches to financing and how to avoid a costly post-deal dispute.

Last year was a down one for M&A and IPOs. What was behind the slowdown, and what is the outlook going forward?

The election and the resulting uncertainty had an impact on both M&A and IPO activity in 2016, but the slower activity in 2016 really was a continuation of what we saw in the second half of 2015.

Last year, M&A activity continued to be impacted by mega-mergers involving pharma companies, leaving those companies focused on consummating those transactions and integrating post-transaction rather than moving forward with acquisitions of smaller biotech companies. Meanwhile, the hot IPO market of 2013, 2014 and the first half of 2015 resulted in private companies that might otherwise have been prime M&A targets becoming public companies and not looking for the M&A exit they might otherwise have been looking for as private companies. On the IPO front, we saw money that had been previously targeted by generalist investors to life sciences IPOs being shifted to other industries. This occurred as the risk of these investments became more apparent with the negative clinical results suffered by several companies that had recently gone public. In addition, we also saw a preference for investments in existing public companies in the life sciences sector due to the lower valuations of these companies.

As we entered 2017, there had been optimism that both M&A and IPO activity would pick up, but that has yet to become a reality. M&A discussions and IPO preparation have picked up in anticipation of better markets, but many of those deals have not yet been consummated. We are hopeful that as we move into the second half of 2017 some of the issues that have tamped down on the activity will be resolved and the optimism for 2017 will come to fruition.

How are companies in need of financing responding to the current environment?

More of our clients have been exploring reverse merger transactions that are designed to result in a private company becoming a publicly traded company without going the IPO route. Because of the lack of IPOs and M&A opportunities for some private companies, at least at the valuations that would be acceptable to these companies and their investors, the need of these companies for additional financing, and the greater availability of financing for public companies, reverse mergers are an attractive option for many.

Option transactions are also a reaction to the limited IPO and M&A markets. For instance, we have had clients looking to fund a clinical trial that, if successful, would be expected to increase the value of the company. However, funding was not available, a sale of the company was not possible at an acceptable valuation and the IPO avenue was closed. Faced with these circumstances, an option transaction that provided the funding to conduct the trial and a future acquisition price that reflected a fair value assuming a positive outcome in the trial was a good outcome for these clients.

There has been an increase in disputes stemming from pharmaceutical deals. Why? And how can players in the space protect themselves?

Many of the deals we work on provide for various contingent payments relating to clinical, regulatory and commercial milestones. In these cases, like a license transaction, the merger agreement contains a diligence standard guiding the level of effort the buyer must take to try to achieve these milestones. However, as these contingent payments have taken on more importance and involved more dollars, we have seen an increase in disputes over the buyer's compliance with its diligence requirements.

This has not resulted in fewer deals with contingent payments, but it has intensified the negotiation of the diligence standard in the merger agreement and resulted in added importance for the audit and reporting features related to the buyer's activities. The increased risk of dispute and litigation has resulted in buyers pushing back on the definition of commercially reasonable efforts and any hooks that could trip them up later. Instead, they are pushing for more discretion in trying to meet the contingent payment triggers. On the other side, sellers have been pushing for requirements to have buyers perform specific activities in the near term, if those activities can be defined, and a commercially reasonable efforts standard that limits the buyer's discretion.

Structured M&A transactions with options, contingent payments and diligence standards resemble the terms of license transactions. As such, clients need attorneys who can advise on the broad range of issues raised by these types of transactions and who can pivot with the client as the structure and terms of a transaction change.

WilmerHale fosters an interdisciplinary, collaborative approach among our attorneys, who have broad experience representing life sciences companies and valuable subject matter expertise. This allows us to provide clients with seamless service and advice throughout the structuring and negotiating of an M&A transaction —from focused attention of attorneys with M&A experience and licensing attorneys who are expert on the negotiation of diligence standards and contingent payments, to attorneys with expertise in the tax, antitrust and regulatory issues that these transactions typically involve.