WILMER CUTLER PICKERING HALE AND DORR LLP

2004 M&A REPORT

Table of Contents

2–4 M&A Market Review and Outlook

5 The Complicated Timetable for Reporting Acquisitions on Form 8-K

6–7 Selected Wilmer Cutler Pickering Hale and Dorr M&A Transactions

8 The Impact of Sarbanes-Oxley Section 404 on M&A Transactions

9 Merger Agreement Lock-Ups in the Post-*Omnicare* World

10–11 M&A Deal Terms in Sales of VC-Backed Companies

12 Law Firm Rankings

2004 Review

Worldwide merger and acquisition activity grew to $2.14 trillion in 2004, up 40% from the total of $1.52 trillion in 2003. Both the average M&A deal size and the number of deals increased on a year-over-year basis, with deal size up 33%, from $49 million in 2003 to $65 million in 2004, and the number of deals up 6%, from 30,818 deals in 2003 to 32,765 in 2004.

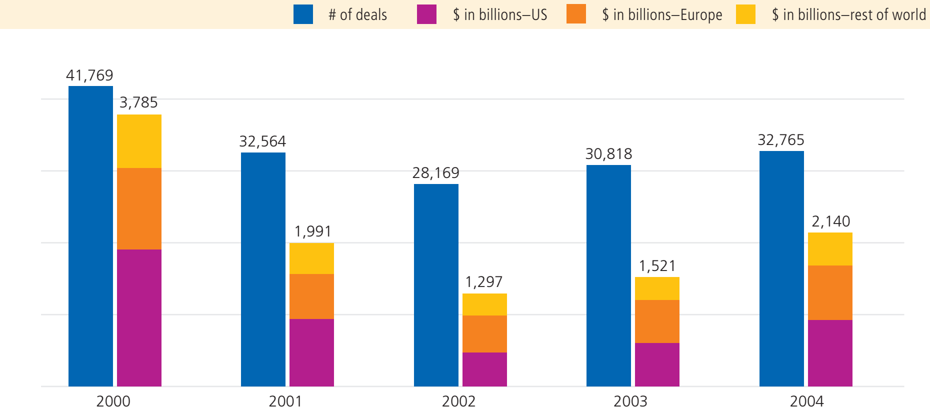
The 2004 M&A dollar volume of $2.14 trillion represents the highest level of M&A activity since 2000, but still falls more than $1.65 trillion short of the record total of $3.79 trillion in 2000. The $309 billion M&A dollar volume announced in December 2004—a dramatic increase over the $115 billion in December 2003—set a new record, solidifying 2004's M&A performance and setting the market on a firm foundation for continued strong activity in 2005, an expectation borne out by early results.

US M&A volume for 2004 largely reflected worldwide results, with a 52% increase in activity, from $605 billion in 2003 to $922 billion in 2004. This total represents the best year-over-year percentage growth since the 1997–1998 period but, in line with worldwide results, is still almost $1 trillion below the record total of $1.90 trillion in 2000. In 2003, there were approximately 8,000 US deals announced, with an average deal value of $76 million. In 2004, the number of deals announced in the United States increased 9% to 8,700, and average deal value grew 40% to $106 million.

Also consistent with worldwide activity, European M&A dollar volume grew to $760 billion in 2004, topping the 2003 total of $595 billion by 29%. Average deal size jumped 35%, from $55 million in 2003 to $74 million in 2004, but the total number of European deals declined 4.6%, from roughly 10,800 in 2003 to 10,300 in 2004.

While overall M&A activity grew throughout the year, much of the increase was attributable to deals greater than $1 billion. In 2004, there were 316 worldwide deals in excess of $1 billion with a combined deal value of $1.30 trillion, compared to 234 such deals in 2003 with a combined value of $788 billion. In the US, there were 137 deals of more than $1 billion in 2004 with an aggregate value of $627 billion, while 2003 saw only 92 such deals with an aggregate value of $347 billion. The number of European deals in excess of $1 billion grew from 99 in 2003 to 106 in 2004, with aggregate values increasing from $338 billion to $462 billion.

M&A Activity – Worldwide



The growth in 2004 M&A activity may largely be attributed to increased confidence in the economy, strengthening corporate profits, solidifying stock prices and stable debt and equity markets.

The generally improved performance of the economy has had several positive effects on M&A activity. First, the solidified balance sheets of many companies have made them more attractive targets than they have been in recent years. More important, as companies have gained more confidence in their own financial positions, they have become more willing to consider M&A transactions. With their competitors returning to the M&A market, companies have been under greater pressure to grow market share and profits, thus contributing to the improved M&A climate.

Increased confidence in M&A performance is evidenced by the growth in public company M&A activity. There were 15,898 public company M&A transactions in 2004, reflecting a 10% increase from the total of 14,522 in 2003. Public company transactions also accounted for a slightly larger percentage of all M&A deals—49% of all M&A transactions in 2004 compared to 47% in 2003.

Historic low interest rates and the willingness of lenders to accept increased leverage ratios have also facilitated M&A growth by providing an inexpensive and willing source of capital. These factors have had a strong positive impact on private equity M&A activity in particular, contributing to a 60% increase in the dollar value of private equity transactions in 2004—a year in which private equity represented 15% of all M&A transactions.

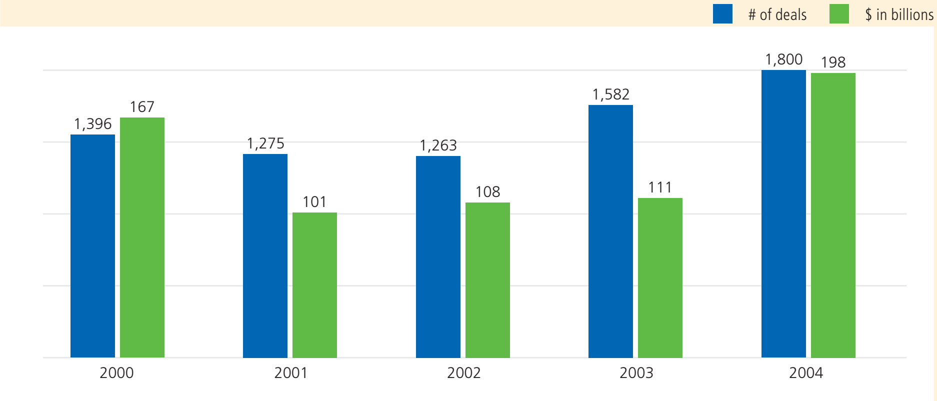
Cash and combined cash and stock transactions still predominated in 2004, but stock-only transactions increased by 15% from 2003. Most of the increase in stock-only transactions can be attributed to deals in excess of $1 billion. For deals below $1 billion, the percentage of cash-based transactions decreased slightly, from 76% of all transactions in 2003 to 74% in 2004.

Worldwide and United States deal volumes for each quarter of 2004 increased over the deal volume for the corresponding quarter in 2003. However, the number of deals in each quarter fluctuated in both 2003 and 2004 and, as a result, there was no consistent quarter-over-quarter improvement in deal volume or deal size in either year.

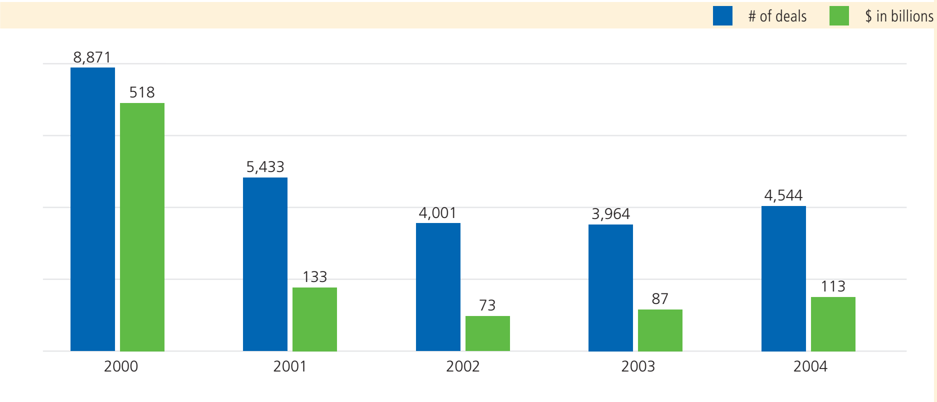
The worldwide increase in M&A dollar volume was led by dramatic growth in the energy and power, telecommunications, healthcare and real estate sectors. The energy and power sector grew to $314 billion in 2004, increasing 61% in aggregate value over 2003, while the telecommunications sector increased 88% to $223 billion, healthcare increased 79% to $198 billion and real estate increased 50% to $195 billion.

Dollar volume in cross-border M&A activity increased almost 60%, from $394 billion in 2003 to $625 billion in 2004. The number of cross-border deals increased 8%, from approximately 7,800 in 2003 to approximately 8,500 in 2004, while the average value of those deals increased 46%, from $50.3 million to $73.6 million.

M&A Activity – Life Sciences



M&A Activity – Information Technology



Sector Analysis

M&A activity in the life sciences sector grew from $111 billion in 2003 to $198 billion in 2004. On a worldwide basis, this increase was led by the $65.7 billion bid by French pharmaceutical company Sanofi-Synthelabo for Aventis SA. The total number of life sciences deals increased from 1,582 in 2003 to 1,800 in 2004, and average deal value grew from $70 million in 2003 to $110 million in 2004.

M&A dollar volume in the information technology sector grew from $87 billion in 2003 to $113 billion in 2004, an increase in activity led by Symantec's $13.5 billion acquisition of Veritas and Oracle's $10.3 billion acquisition of PeopleSoft. Deal volume in this sector increased from 3,964 deals in 2003 to 4,544 deals in 2004, while the average deal value was up modestly from $22 million in 2003 to $25 million in 2004.

Telecommunications M&A activity increased from $119 billion in 2003 to $223 billion in 2004, led by Cingular Wireless's acquisition of AT&T Wireless for $47.1 billion and Sprint's acquisition of Nextel for $46.5 billion. While the number of deals held steady—at 1,087 deals in 2003 and 1,075 deals in 2004—the average deal value almost doubled from $109 million in 2003 to $207 million in 2004.

In the financial services sector, M&A dollar volume increased from $301 billion in 2003 to $347 billion in 2004. The number of deals was also largely unchanged—with 4,331 deals in 2003 versus 4,381 deals in 2004—while average deal value showed a slight increase from $70 million in 2003 to $79 million in 2004.

The M&A market for venture-backed companies also improved, with the number of acquisitions of venture-backed companies growing from 335 in 2003 to 376 in 2004. More important, the median acquisition price paid for venture-backed companies increased dramatically, from $23 million in 2003 to $40 million in 2004. While this figure is well below the median acquisition prices in 1999–2000 (including the staggering $100 million median in 2000), it is higher than the median acquisition prices in the 1997–1998 timeframe. In 2004, the median time from initial funding to an acquisition was 4.7 years, the highest figure since 1996.

2005 Outlook

All of the factors that led to an increase in M&A activity in 2004 are still in place, and the momentum in early 2005 remains positive. The volume of large transactions has held steady or increased in the first quarter, the overall outlook for the economy is positive, and the financial markets have favorably received most of the large M&A transactions that have been announced recently. A significant number of private equity funds are still awaiting investment, a factor that should continue to bolster M&A activity.

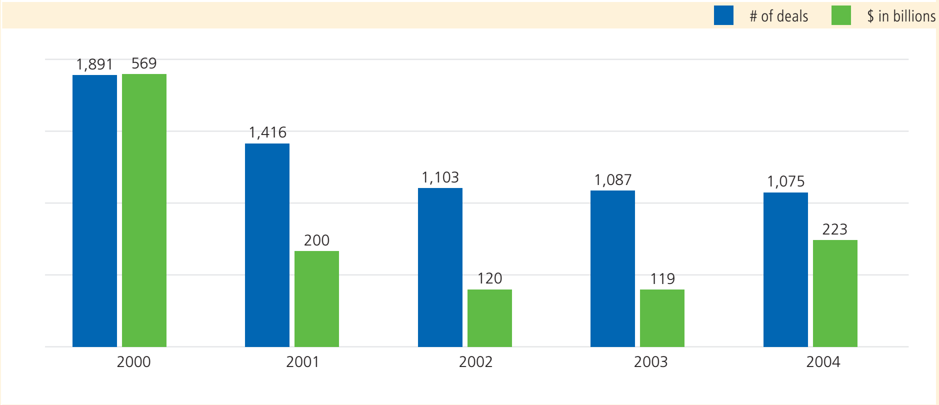
Notwithstanding the favorable outlook, there is still some caution in the marketplace and no one is yet predicting a return to the record levels of M&A activity that occurred in 2000. The recent scandals in the financial markets and the changes implemented by the Sarbanes-Oxley legislation have resulted in greater wariness and increased scrutiny of M&A transactions.

Also reflecting the conservative mood in the marketplace is the apparent trend toward consolidation rather than diversification, with investors keen to consolidate market positions or pursue private equity transactions where they believe they can realize a high return by improving a target over the near term. As a result, while we anticipate ongoing strength in M&A activity in 2005, we do not expect the number of transactions to be significantly higher than the total from 2004.

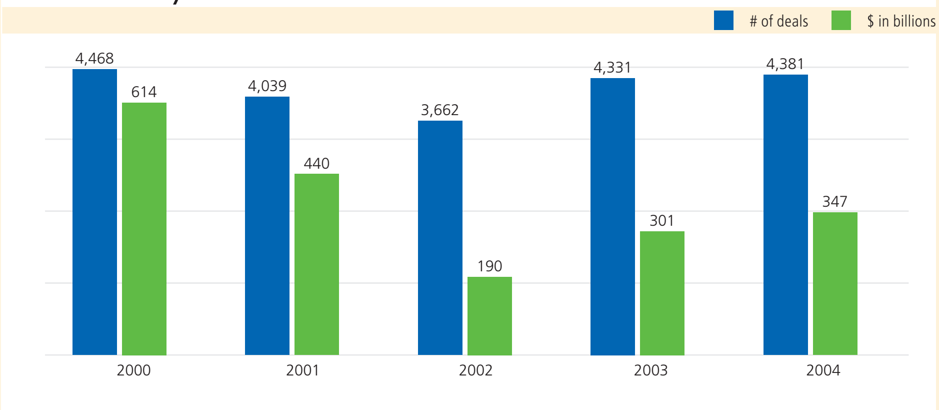
The outlook for technology and life sciences companies appears more favorable than the overall outlook. Many technology companies are maturing, and consolidation appears to offer opportunities to achieve desired growth levels and to cut costs. Similarly, consolidation may be the best way for life sciences companies, particularly those in healthcare—which remain under pressure to reduce costs while achieving growth—to reach their goals.

The M&A slowdown of recent years appears to be over and 2005 promises a favorable climate for M&A activity. ■

M&A Activity – Telecommunications



M&A Activity – Financial Services



Public companies have long been required to file Form 8-Ks with the SEC, reporting the consummation of significant M&A transactions. Recently, however, Form 8-K reporting for acquisitions has become significantly more complicated as a result of changes to Form 8-K that have expanded the number and type of reportable events and reduced the general filing deadline to four business days.

Prior to the Form 8-K rule changes, M&A transactions could be reported in as few as a single 8-K and rarely required more than two. Properly reporting an acquisition transaction under the new Form 8-K rules can now lead to several independent Form 8-K filing obligations, depending on the timing of the transaction and the sequence of actions.

Take, for example, a public company's acquisition of a private company where the acquisition agreement is signed on the evening of business day zero, announced before the markets open on business day one and closed on business day five. In this case—which, for the sake of illustration, poses more Form 8-K complications than most public-private deals—as many as five separate Form 8-Ks may be needed:

- *Business Day One:* A Form 8-K containing a copy of the press release, either furnished under Item 7.01 or filed under Item 8.01, as a means of complying with Rule 425 and/or Rule 14a-12. The odds are high that a same-day filing will be required, although the precise reasons will depend on whether stock or cash is the acquisition currency (Rule 425) and whose stockholders are voting on the deal (Rule 14a-12). This Form 8-K may also be needed to satisfy obligations under Regulation FD.
- *No Later Than Business Day Four:* A Form 8-K filing required disclosures about the acquisition agreement under Item 1.0 within four business days after signing. The same deadline applies to any other material definitive agreements that are signed concurrently with the acquisition agreement, such as executive compensation arrangements with the target's officers. This 8-K will be more detailed than the press release in some respects (for example, in regard to contractual provisions) and less detailed in others (for example, in regard to the business rationale for the deal). If the 8-K can be quickly prepared to reflect the final negotiated terms of the acquisition agreement and other agreements to be reported under Item 1.01, this 8-K can also be filed on business day one. If the acquirer would like to limit immediate public access to the summary of contractual details, this filing can be delayed until business day four.
- *Business Day Five:* A Form 8-K containing the same-day press release that announces the closing (in order to satisfy Rule 425 and/or Regulation FD).
- *No Later Than Business Day Nine:* A Form 8-K filing disclosures about (1) the closing as required by Item 2.01, (2) material definitive agreements entered into concurrently with the closing as required by Item 1.01 (note that this does not include target company contracts assumed in connection with the acquisition, which need only be filed, without description, as exhibits to the Form 10-K or 10-Q covering the period during which the agreement was entered into) and (3) any other closing-related matters, such as debt financing for the transaction (under Item 2.03), issuance of unregistered securities (under Item 3.02), election of additional directors (under Item 5.02) or charter amendments (under Item 5.03).
- *No Later Than Calendar Day Eighty:* A Form 8-K filing the financial statements required by Item 9.01. The relevant deadline is 75 calendar days after the closing (in this example, 80 calendar days after the signing).

New 8-K Items Potentially Triggered by M&A Transactions

- Item 1.01 (Entry into a Material Definitive Agreement)
- Item 2.01 (Completion of Acquisition or Disposition of Assets)
- Item 2.03 (Creation of a Direct Financial Obligation or an Obligation under an Off–Balance Sheet Arrangement of a Registrant)
- Item 3.02 (Unregistered Sales of Equity Securities)
- Item 5.01 (Changes in Control of Registrant)
- Item 5.02 (Departure of Directors or Principal Officers; Election of Directors; Appointment of Principal Officers)
- Item 5.03 (Amendments to Articles of Incorporation or Bylaws; Change in Fiscal Year)
- Item 7.01 (Regulation FD Disclosure)
- Item 8.01 (Other Events)
- Item 9.01 (Financial Statements and Exhibits)

For a public-public acquisition, the number of required Form 8-Ks will be at least double that of a public-private deal, and will typically include an 8-K under Item 5.01 to report a change in control of the target and an 8-K under Item 5.02 to report the departure of the target's directors and principal officers. Additional 8-Ks may be required to report significant intermediate steps in the transaction, such as the receipt of antitrust clearance or stockholder approval or other major developments in the transaction.

In all types of M&A transactions, Form 8-K filings may also be required if a binding letter of intent or other binding preliminary agreement is entered into.

We offer the following suggestions to make sure all Form 8-K filing requirements are met in connection with M&A transactions:

- Well in advance of signing the definitive acquisition agreement, review the list of required Form 8-K disclosures carefully and identify all 8-K items that must be responded to in each stage of the acquisition.
- Before the flurry of last-minute negotiations of the acquisition agreement begins, prepare drafts of all Form 8-Ks that will be required within the first four business days after signing.
- Be nimble in updating and filing the various Items of Form 8-K in a manner that reflects the timetable of your particular deal and relevant filing deadlines. ■

Avid
has acquired
M-Audio
$175,000,000
(plus potential earnout)
August 2004

Netegrity
has been acquired by
Computer Associates
$430,000,000
November 2004

Danaher
has acquired
Trojan Technologies
$185,000,000
November 2004

SallieMae
has acquired
Arrow Financial Services
$165,000,000
September 2004

Switchboard
has been acquired by
InfoSpace
$160,000,000
June 2004
(counsel to principal stockholder)

Mellon
has acquired
EACM
Undisclosed
July 2004

Blockbuster
split-off from Viacom and payment of $905,000,000 special distribution
October 2004
(counsel to special committee)

WebMD
has acquired
ViPS
$160,000,000
August 2004

Kodak
has sold its Remote Sensing Systems operations to
ITT Industries
$725,000,000
August 2004

Bookham
has acquired
New Focus
$330,500,000
March 2004

Quantum Bridge
has been acquired by
Motorola
$200,000,000
(including potential earnout)
May 2004

Verizon Wireless
has acquired spectrum assets from
NextWave Telecom
$930,000,000
October 2004

Legg Mason
has acquired selected offices of the Scudder asset management business of
Deutsche Bank
$81,300,000
(including potential earnout)
December 2004

QAS
has been acquired by
Experian
£106,000,000
October 2004

Bell
has acquired the Canadian operations and selected US assets of
360networks
$275,000,000 CDN
November 2004
(US counsel)

Micro Line
has been acquired by
Pentax
$48,000,000
December 2004

Telica
has been acquired by
Lucent
$295,000,000
August 2004

MSL
has been acquired by
Celestica
$293,000,000
March 2004

Baltimore Ravens
have been acquired by
Stephen J. Bisciotti
$600,000,000
April 2004

Keane
has acquired
Nims Associates
$35,000,000
(including potential earnout)
February 2004

Bose
has acquired
EnduraTEC Systems
Undisclosed
May 2004

FSP Franklin Street Properties
has agreed to acquire
four REITs
$193,000,000
Pending*

CCBN
has been acquired by
Thomson
Undisclosed
March 2004

Bank One
has acquired the private label and co-branded credit card operations of
Circuit City
$1,800,000,000
May 2004

Kronos
has acquired
Ad Opt
$69,000,000 CDN
November 2004

Modus Media International
has been acquired by
CMGI
$230,500,000
August 2004

ETS
has sold its Capstar subsidiary to
Thomson Learning
Undisclosed
October 2004

DoubleClick
has acquired
Performics
$65,000,000
(including potential earnout)
June 2004

Eclipsys
has acquired
CPMRC
Undisclosed
March 2004

Victory Super Markets
has been acquired by
Hannaford Bros.
$175,000,000
November 2004

The Berkshire Group
has sold its mortgage servicing business to
Deutsche Bank
Undisclosed
October 2004

Pure Encapsulations
has been acquired by
Aeterna Laboratories
$50,000,000
March 2004

angioLINK
has been acquired by
Medtronic
$45,000,000
(plus potential earnout)
November 2004

Oracle
has acquired
PeopleSoft
$10,300,000,000
December 2004
(EU antitrust co-counsel)

THE LEADER IN TECHNOLOGY AND LIFE SCIENCES COMPANY MERGERS AND ACQUISITIONS.

* as of December 31, 2004

Wilmer Cutler Pickering Hale and Dorr LLP

The Sarbanes-Oxley Act was enacted two and one-half years ago, and the law continues to vex the corporate world. While public companies by now have largely adapted to Sarbanes-Oxley's stringent governance and disclosure regimes, they continue to grapple with the highly publicized "internal control" requirements contained in Section 404 of the Act. That section requires a public company to have its management annually evaluate the effectiveness of its system of internal controls over financial reporting and to obtain an independent internal control audit.

Section 404 compliance has been complex and expensive for most public companies, and poses special challenges in the M&A context:

- *Integration:* Except in a purely private-private deal, internal controls are now a key integration issue. The parties to the deal are likely to have systems of controls that differ from each other in many respects, most notably in the IT area. After the transaction is completed, the surviving company, if still public, will have to evaluate its internal controls, report on the results and have them audited. If the combined company's system of controls is not fully integrated, it may be prone to a material weakness of internal controls that has to be disclosed.

  The specific integration issues likely to arise will depend on the characteristics of the parties and the nature of the transaction. For example, where two public companies are involved, and both have already had Section 404 evaluations, the integration process may principally consist of converting systems and confirming that the resulting controls are effective. By contrast, if a public company acquires a private company that does not possess a fully developed internal control system—much less one that would pass Sarbanes-Oxley muster—the buyer may have to not only convert systems, but also design or upgrade new systems.

- *Due Diligence:* Internal controls add an entirely new dimension to financial due diligence. Undertaking a full assessment of a target company's internal controls in due diligence would likely be time-consuming and may not be cost-effective, particularly at a stage in the deal where it is uncertain whether an agreement will ultimately be signed. Absent such an assessment, however, the buyer cannot be certain that the target company's controls, whether standing alone or integrated with the buyer's, will be effective. While some degree of sampling can and should be undertaken, and other inquiries made, there is likely to be some uncertainty regardless of the amount of diligence that is performed. The degree of uncertainty—like the scope of integration issues—will be affected by the nature of the parties and the transaction.

- *Deal Terms and Documentation:* Deal terms and agreements need to take account of Section 404 issues by including, for example, representations and warranties about internal controls. These types of provisions will be matters of negotiation, and practice is still evolving in this area. However, dealmakers and their advisers need to recognize that internal control issues are unlikely to be solved through contract language alone. The crucial issue is whether the target company's controls, when integrated with the buyer's, will meet the requirements of Section 404. Target companies are unlikely to agree to representations, closing conditions or indemnification that will protect buyers against the risk that their controls—either standing alone or combined with the buyer's—may subsequently be found ineffective in a Section 404 evaluation.

- *Reporting and Timing:* An acquisition will have an impact on the buyer's Section 404 reporting processes. Section 404 requires that public companies report on the effectiveness of their internal controls as of the end of the fiscal year. Depending on when an acquisition closes, however, it may not be feasible for the buyer to complete an assessment of the target company's controls, much less complete the integration with the buyer's controls, evaluate the effectiveness of the combined system and have that system audited. In recognition of this, the SEC has indicated that buyers may take up to one year after closing an acquisition to complete the Section 404 process as to the acquisition, and the auditor's report in the interim need not cover the acquired business. However, during the one-year period the buyer must still disclose changes to its internal controls resulting from the acquisition.

- *Controls for M&A Activity:* Given the complex accounting questions and substantial financial reporting issues raised by M&A transactions, a company that engages in such transactions must consider whether it has adequate controls for the M&A activity itself. The company must assess whether it has controls that are effective enough to ensure that the transaction is properly accounted for and documented. The nature of the required controls may vary depending on whether the company has an ongoing acquisition program (and therefore relies on internal capabilities) or whether the transaction is a one-time strategic deal (in which case the question may be whether the company has obtained adequate outside resources to ensure accurate reporting).

In sum, Section 404 has introduced substantial new complexities—and potential pitfalls—into the M&A process. While the new requirements are burdensome, maintaining a system of effective internal controls can have benefits besides SEC compliance. A sound internal control system is a fundamental means by which managers can reassure themselves and investors about the integrity of their businesses and their financial reporting. Similarly, knowing the adequacy or effectiveness of an acquired company's controls can help the acquiror assess the degree of risk in the deal. Because the absence of an effective system of controls can raise the risk of misstatement of financials or even fraud, internal control issues need to be front-and-center from the outset of any deal. ■

Substantial effort and expense is usually required to evaluate, negotiate and complete an M&A transaction, and the potential benefits are often very significant. Given the stakes involved, buyers are understandably keen to minimize the risk of a deal not closing, especially when that risk is due to a competing bid, and target companies are likewise eager to avoid the adverse impact a failed deal or protracted battle for control may have on their market valuation, employees, customers and suppliers. Techniques to enhance "deal certainty"—the likelihood that a deal will be completed—have therefore become a staple in acquisitions, but considerable care must be taken in order to guard these techniques against legal challenge.

Countering the desire for deal certainty is the overlay of state corporate law, most importantly the obligation of the target company's directors to act as fiduciaries and obtain the best value for shareholders. How best to balance these competing forces in acquisitions is an issue that has been hotly negotiated by practitioners for years.

In *Omnicare, Inc. v. NCS Healthcare, Inc.*, the Delaware Supreme Court evaluated whether the directors of a target company, NCS Healthcare, breached their fiduciary obligations by approving a merger agreement with competitor Genesis Health Ventures that required NCS to submit the agreement to a shareholder vote—even if the directors changed their recommendation as to the advisability of the merger. In connection with this same merger agreement, the holders of a majority of NCS's outstanding voting power had entered into irrevocable voting agreements obligating them to vote in favor of the transaction with Genesis. NCS had shopped itself extensively and Genesis insisted on the voting agreements in return for significantly increasing the purchase price to match a higher, but conditional, proposal by another bidder, Omnicare. After the merger agreement was signed and the transaction announced, Omnicare made an unconditional and more favorable offer, prompting NCS's directors to change their recommendation on the merger with Genesis. However, the pre-existing obligation to put the Genesis agreement to a shareholder vote, coupled with the voting agreements in favor of Genesis, made the changed recommendation meaningless as to the outcome. On these facts, the court said that the shareholder vote provision and the voting agreements, in combination, were preclusive and that NCS's directors had breached their fiduciary duties.

On their face, fiduciary obligations of directors (as viewed through the *Omnicare* prism) apply to both public and private target companies. Significant consensus on the outer bounds of the balance between deal certainty and fiduciary obligations has emerged with respect to public targets, although the balance in each transaction is still hotly contested. In the private arena, there is much less consensus, as many believe a seller can and should agree to a fully locked-up deal. Nevertheless, the following techniques to increase deal certainty, consistent with *Omnicare*, are being used in acquisitions of public and, in some cases, private companies:

- Bind less than a majority of the voting power to vote in favor of a deal, and require the target company to hold a meeting to consider the transaction, as permitted by Delaware law. Most M&A counsel are comfortable if voting agreements cover up to 40% of the voting power, but some acquirers push for just under 50%.
- Give the directors of the target company the right to terminate the merger agreement under strictly defined procedures (usually including payment of a termination fee) if a "superior proposal" emerges. With a termination right, voting agreements covering all outstanding shares could theoretically be obtained, since the target's directors still have the ability to stop the transaction if a better offer arises. From a buyer's perspective, this provides less protection against a competing bid than requiring a shareholder meeting with fewer shares subject to voting agreements, but may be preferable where insufficient shareholder support—rather than a competing bid—is viewed as a greater risk to the transaction.
- Give the buyer an option to purchase the shares subject to the voting agreements, or require that—if the shares subject to the voting agreements are sold in a competing transaction—some or all of the gain must be paid to the buyer. Dealing directly with the shareholders may help balance the fiduciary obligations of the target's directors, but shareholders are often unwilling to include such provisions.
- If feasible, obtain shareholder approval immediately after signing the merger agreement, since the fiduciary obligations of the directors arguably apply only until the shareholders vote. This technique will not work if the target company is public and must comply with notice and meeting requirements under federal securities laws, but has been utilized by private targets where concentrated ownership makes shareholder approval by written consent or at an immediate shareholder meeting feasible. However, even private targets must make sure to comply with the notice and merger approval formalities of corporate law and disclosure obligations under federal and state laws.

More recently, the Delaware Chancery Court indicated in *Orman v. Cullman* that shareholder "lockout" agreements may be another acceptable technique to enhance deal certainty. These lockouts, usually included in voting agreements in support of a transaction, prohibit shareholders from voting in favor of any competing deal even after the termination of the transaction at hand, and may constitute a powerful disincentive to any competing bid. In *Orman*, an 18-month lockout was found acceptable, although the facts of this case were unusual and caution against stretching this technique too far.

Using some combination of these techniques, buyers of private companies have generally been able to achieve a high degree of deal certainty. While a "fully locked-up" deal is no longer achievable for a public target, significant deal certainty can still be achieved with thought and care. In all of these transactions, establishing the appropriate record to support a target's agreement to any of these techniques is an important step toward successfully overcoming any challenge brought by unhappy shareholders or competing bidders. ■

We reviewed all 54 merger transactions involving venture-backed targets signed up or consummated in 2004 (as reported in VentureSource) where the merger documentation was publicly available and the deal value was $25 million or more. Of these merger transactions, 23 (or 43%) were for cash, 22 (or 41%) were for stock and nine (or 17%) were for a mixture of cash and stock.

Based on this review, we have compiled the following deal data:

Deals with Earn-Out		
Deals that provided contingent consideration based upon post-closing performance of the target (other than balance sheet adjustments)	**With Earn-Out:** 24%	**Without Earn-Out:** 76%
Deals with Indemnification		
Deals where the target's shareholders or the buyer indemnified the other post-closing for breaches of representations, warranties and covenants	**With Indemnification** By Target's Shareholders: 89% By Buyer[1]: 37%	**Without Indemnification** By Target's Shareholders: 11% By Buyer: 63%
Survival of Representations and Warranties		
Length of time that representations and warranties survived the closing for indemnification purposes	**Shortest:** 6 Months **Longest:** 36 Months	**Most Frequent:** 12 Months
Caps on Indemnification Obligations		
Upper limits on indemnification obligations where representations and warranties survived the closing for indemnification purposes	**With Cap:** 85% Limited to Escrow: 72% Limited to Purchase Price: 7% Exceptions to Limits[2]: 74%	**Without Cap:** 15%

[1]The buyer provided indemnification in 48% of the identified transactions where buyer stock was used as consideration; in 65% of the transactions where the buyer provided indemnification, buyer stock was used as consideration.
[2]Generally, exceptions were for fraud and willful misrepresentations.

Escrows	
Deals having escrows securing indemnification obligations of the target's shareholders	**With Escrow:** 83% % of Deal Value: Lowest: 4% Highest: 23% Most Common: 10%–20% Length of Time: Shortest: 6 Months Longest: 36 Months Most Frequent: 12 Months Exclusive Remedy: 64% Exceptions to Escrow Limit Where Escrow Was Exclusive Remedy[3]: 72%

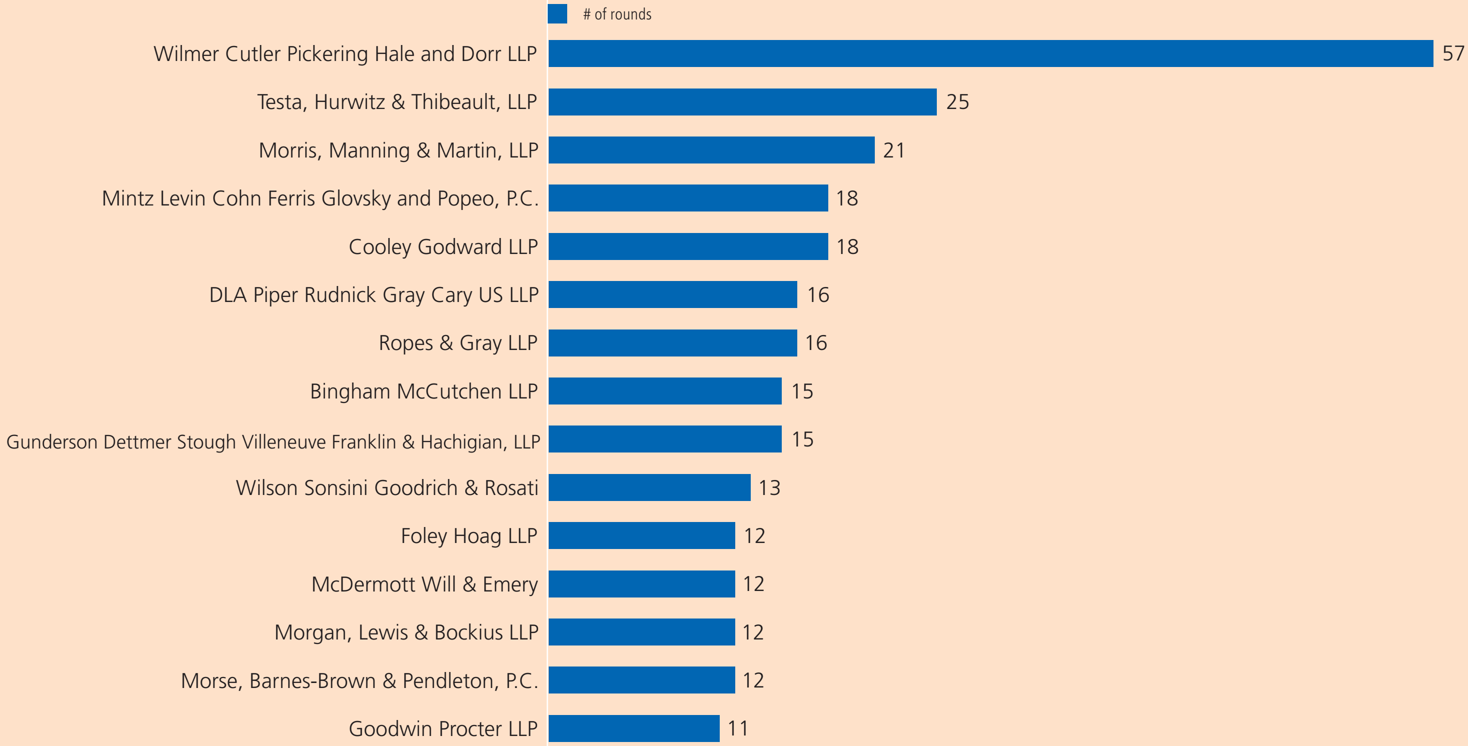
Baskets for Indemnification		
Deals with indemnification where a specified "first dollar" amount did not count towards indemnification, expressed either as a "deductible" (where such amount can never be recovered) or as a "threshold" (where such dollar amount can not be recovered below the threshold but once the threshold is met all such amounts may be recovered)	**Deductible:** 39%	**Threshold:** 51%

MAE Closing Condition		
Deals where the buyer or the target had as a condition to its obligation to close the absence of a "material adverse effect" with respect to the other party or its business	**Condition in Favor of Buyer:** 81%	**Condition in Favor of Target**[4]: 30%

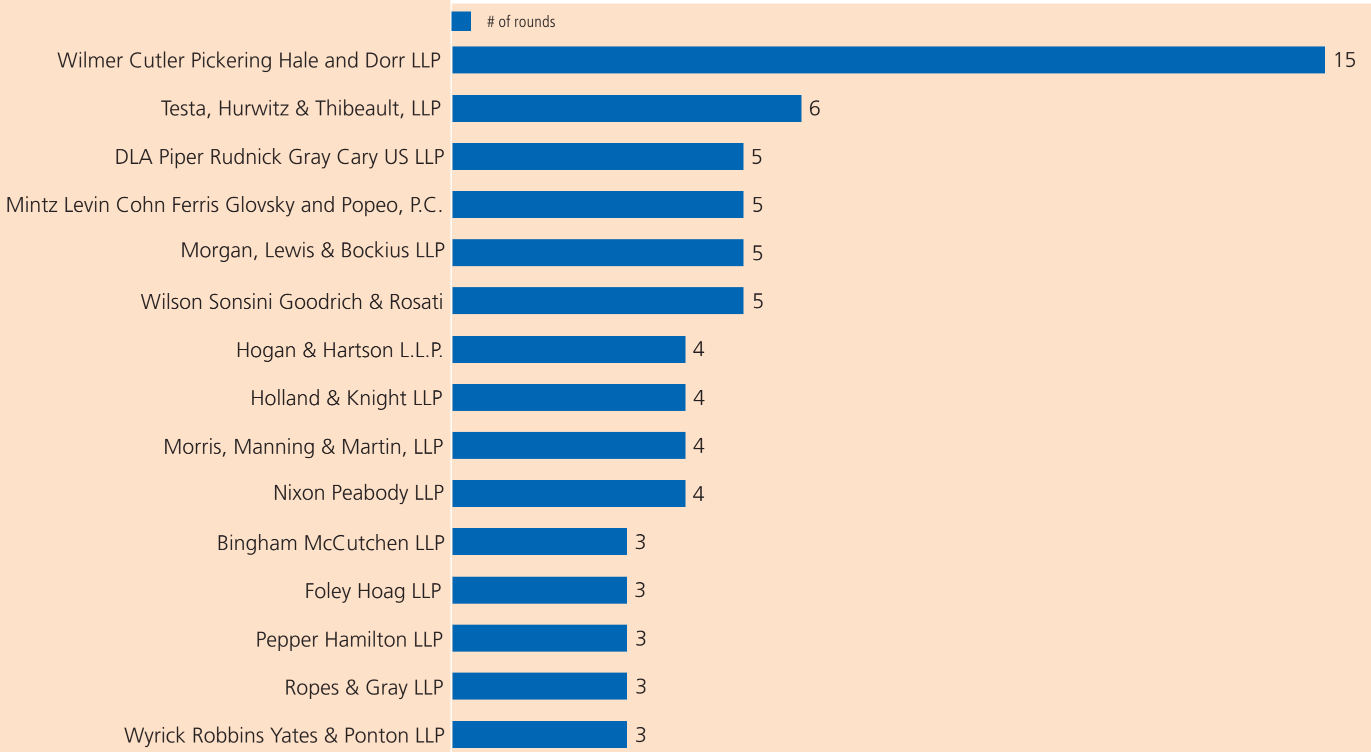
Exceptions to MAE	
Deals where definition of "material adverse effect" for the target contained specified exceptions	**With Exception:** 78%[5]

[3]Generally, exceptions were for fraud and criminal activity.
[4]In 50% of these transactions, buyer stock was used as consideration.
[5]Generally, exceptions were for general economic and industry conditions.

Counsel to Eastern US Companies Receiving VC Financing in 2004



Counsel in Sales of Eastern US VC-Backed Companies in 2004



Note: The above charts are based on companies located east of the Mississippi River that completed a seed, first, second, later stage, corporate or restart round of venture capital financing.

Source: VentureOne

Want to know more about the latest in the IPO and venture capital markets?

See our *2004 IPO Report* for a detailed analysis of the 2004 IPO market and 2005 outlook. The report features regional IPO market breakdowns, a review of the PIPEs and Rule 144A markets, a discussion of proposed changes to IPO "quiet period" rules and tips on 8-K readiness for new public companies.

Our *2004 Venture Capital Report* offers an in-depth review of the US and European venture capital markets and discusses the outlook for 2005. Other highlights include industry and regional breakdowns; practical advice for VC directors; an overview of trends in VC deal terms; and a look ahead to VC fund formation, governance and liquidity in 2005.

To request a copy of either report, please contact marketing@wilmerhale.com or call 617 526 5600.

Data Sources

Except as otherwise described, all M&A data in this report is based on Wilmer Cutler Pickering Hale and Dorr's analysis of Thomson Financial data, and all venture capital data in this report was compiled from the VentureSource database.

Internet Availability

An electronic version of this report can be found at www.mergerleader.com.

Additional Copies

For additional copies of this report, please contact the Wilmer Cutler Pickering Hale and Dorr Marketing Department at marketing@wilmerhale.com or call 617 526 5600.

04_380 VER 04/05 18500

Baltimore

Beijing

Berlin

Boston

Brussels

London

Munich

New York

Northern Virginia

Oxford

Waltham

Washington

wilmerhale.com