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The Law and Finance of M&A Contracts

Christel Karsten



Universiteit van Amsterdam

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The Law and Finance of M&A Contracts

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1

Introduction and Summary

What role do contracts play in mergers and acquisitions (M&A)? M&A transactions can be complicated because of economic concerns related to information asymmetry, agency problems, and risk allocation. Contract design can provide mechanisms to mitigate these concerns (Gilson (1984)). The empirical question is, however, to what extent contracts are indeed used as instruments to alleviate such concerns? And to what extent do the involved law firms or lawyers also influence acquisition contracts and negotiations?

This thesis will shed light on these questions by analyzing contracts between buyers and sellers from 151 acquisitions of privately held targets. The contracts were obtained from one of the largest law firms in The Netherlands and span the period from 2005 to 2010. These contracts contain detailed provisions used to transfer companies. In addition, they allow us to identify the individual law firms and lawyers advising both buyers and sellers.

The focus is on M&A contracts, as corporate acquisitions are among the most important strategic decisions in the lifetime of a company, requiring large amounts of resources and management time. While most prior literature has focused on *public*

acquisitions, our sample concerns acquisitions of privately held targets.[1] These are important deals to analyze, as they constitute the vast majority of M&A deals.[2]

Existing literature has provided various insights to our understanding of mergers and acquisitions. For example, there is substantial evidence on how buyer and seller characteristics, or investment banks, affect acquisition outcomes such as deal completion rates, premiums, or announcement returns.[3] However, contracts signed between buyers and sellers have received relatively little attention, even though they form a key element in corporate acquisitions, especially those involving private targets.[4] Moreover, considerable fees are paid for drafting and negotiating these contracts.[5]

This thesis consists of three chapters that address different, but related, aspects of the law and finance of M&A contracts. Chapter 2 describes the drivers of variation in contract provisions across deals. Chapter 3 then relates these provisions to premiums paid. Finally, Chapter 4 considers the role of lawyer expertise on negotiation outcomes, such as contract design and premiums, but also the negotiation process itself.

Chapter 2 studies the extent to which variation in acquisition contracts reflects the economic deal environment, and whether part of this variation can be explained by the styles of the involved legal advisors. Two views can be contrasted on the role of contracts and legal advisors in acquisitions. The first view, as proposed by Coase (1937), holds that contracts are instruments to mitigate economic problems between parties. As a result, the negotiation process should yield contracts which are a pure reflection of the economic

[1] Papers based on M&A contracts concerning mostly public deals have focused on payment mechanisms (Cain, Denis, and Denis (2011) and Coates (2012)), MAC clauses (Gilson and Schwartz (2005), Choi and Triantis (2010), and Denis and Macias (2012)) and on termination fees (Bates and Lemmon (2003) and Officer (2003)).

[2] For example, 96% of the cross-border transactions in Erel, Liao, and Weisbach (2012) involve privately held targets. Betton, Eckbo, and Thorburn (2007) document for US takeovers that about 63% of the targets are privately held.

[3] Examples include Shleifer and Vishny (1989), Lang, Stulz, and Walkling (1991), Harford (1999), Bargeron et al. (2008), Masulis, Wang, and Xie (2007), Moeller (2005), and Stulz, Walkling, and Song (1990). For investment bank influence, see See Kale, Kini, and Ryan (2003), Rau (2000), Servaes and Zenner (2000), Bao and Edmans (2012), Golubov, Petmezas, and Travlos (2012), and Ertugul and Krishnan (2011).

[4] An exception is Coates (2012), who studies 60 takeover contracts to assess how relative law firm expertise affects the use of earn outs, price adjustment clauses, and indemnification clauses.

[5] Based on UK public deals in 2012, the fees charged by law firms for their services average a substantial 1.3% of deal value, ranging between 0.1% and 4.5% depending on deal size (Freedman (2013)).

conditions of that transaction. This hypothesis forms the foundation to most contract theory, where economic concerns (such as adverse selection, moral hazard, and risk allocation) are optimally addressed contractually, subject only to limitations of complete contracts. In this view, referred to as the *economic-contracting hypothesis*, legal advisors map an objective contract design to each combination of deal characteristics (Gilson (1984)).

In contrast, the second view argues that contract design is partly driven by the biases or styles of the legal advisors involved in advising on these acquisitions (as suggested by e.g., Coates (2001, 2012), Krishnan and Masulis (2013), and Kaplan, Martel and Strömberg (2007)). This is considered the *lawyer-contracting hypothesis.* Whereas such influence from legal advisors need not necessarily lead to inefficient contracting, the implications of the drivers of contracting can be important when those contract provisions affect values.

The empirical analysis focuses on two sets of crucial contract provisions – warranties and covenants.[6] Warranties are guarantees that sellers make about the quality of the targets, while covenants restrict seller behavior in the period between the signing of the contract and the transfer of the target.[7] To test whether styles of legal advisors map into contract design beyond objectively applying provisions to an economic environment, we start by analyzing the economic characteristics that drive variation in warranties and covenants. Consistent with the view that contract design can mitigate economic concerns, the results indicate that deals with more information asymmetries between buyers and sellers use more warranties. Similarly, deals that are more prone to agency conflicts rely on more covenants to protect buyers. Moreover, higher buyer bargaining power is associated with better protection, reflected in both more warranties and covenants. Together, these

[6] Warranties and covenants are considered two of the key provisions in takeover contracts. Gilson and Schwartz (2005, p.333), for example, state that "three sets of provisions reflect the three basic engineering elements of a corporate acquisition agreement: representations and warranties, covenants and conditions." Similarly, Martinius (2005, p.36), claims that "representations and warranties […] are the primary means to protect the buyer."

[7] Covenants in acquisition contracts are comparable to those in debt or venture capital contracts (see Gompers and Lerner (1996), Kaplan and Strömberg (2003), Murfin (2012), and Bradley and Roberts (2004)).

economic determinants explain 39% of the variation in warranties and 34% of the variation in covenants.[8]

Whereas this suggests that deal economics are relevant in explaining contract design, it also indicates that about two thirds of the variation in warranties and covenants is driven by other factors. To analyze whether the styles of law firms can explain part of the remaining variation, we exploit information on the identity of the law firms that drafted the first versions of the contracts. Law firms generally use firm-specific standardized internal specimens as a basis for new contracts (see Miller (2008) and Coates (2001)). If, during the negotiations, contracts are not fully adjusted to deal circumstances, final contracts will partly reflect these specimens.[9] As such, the identity of the drafting law firms allows us to empirically identify their styles. To test for their impact on contracts, we use law firm fixed effects of these drafting law firms. Supporting the *lawyer-contracting hypothesis*, we find that these law firm fixed effects are jointly significant and that they modestly increase the explained variation in both covenants and warranties.

Further, if styles of law firms affect contract design, then personal styles of lawyers could also be influential. To empirically identify the lawyer styles, we again focus on the first draft contracts, and consider the lead lawyers who drafted this first version (partner fixed effects).[10] Providing further support for the *lawyer-contracting hypothesis,* we find that the styles of the individual lawyers also mirror into contract design. Interestingly, it seems that the explanatory power of the lawyer styles is stronger than that of the law firm styles.

To obtain a better understanding of the effect of styles of legal advisors on contracting, two additional analyses are conducted. As a first additional analysis, we assess the impact of these styles on categories of warranties and covenants, where the categories are based on the economic and legal concerns addressed by the provisions. We find that the

[8] Variation explained is represented by the Adjusted R-squared.

[9] The literature on standardization of contracts suggests that contracting parties might not deviate strongly from such specimen contracts due to transaction costs or to avoid enforcement uncertainty (Kahan and Klausner (1997), Gennaioli and Perotti (2010)).

[10] To ensure that law firm styles are held constant, the sample is restricted to contracts drafted by lawyers at the law firm that provided our data.

impact of law firms and lawyers depends highly on the concern addressed by the provision. Some categories are driven mostly by economic conditions, whereas others are related more to styles of legal advisors.[11] As a second additional analysis, we examine whether observable lawyer characteristics can capture some of these lawyer styles. The results suggest that the style of lawyers in drafting warranties can, to a large extent, be explained by their risk aversion. Conversely, their style in drafting covenants can rather be explained by the business education and corporate experience of drafting lawyers.

Together, the above results highlight the relevance of legal advisors for contract design. An important related question is whether such contract design is reflected in pricing. To analyze this, Chapter 3 investigates whether variation in contract design affects premiums paid. Two opposing views can be distinguished with respect to the relation between contract design and acquisition pricing. The *independence hypothesis* holds that the negotiation process does not allow for interactions between price and non-price terms (i.e. contract provisions), implying that both are determined independently from each other. Conversely, the *feedback hypothesis* argues that the distinct timing of negotiations does not prevent pricing and contract design from being jointly determined, for example, because prices are set in expectation of certain contract provisions that will be included later (Schwartz and Scott (2003), Choi and Triantis (2012)).[12]

To analyze whether contract design affects pricing, we distinguish between two types of provisions: value increasing versus value distributing provisions. This distinction is interesting, as the impact on premiums could be different for both types of provisions. Value increasing provisions should positively impact the premium, because - for a given division of surplus - an increase in the joint surplus should be split accordingly. In contrast, value distributing provisions could be traded off against each other within a contract, such that they would not affect the price. To reflect the difference in impact, we consider both a

[11] To illustrate, law firm styles seem to be most influential for warranties and covenants that address concerns which are generally similar across deals, whereas lawyer styles seem to matter more for categories where the interests of the two parties are often misaligned and where value can be distributed.

[12] This is supported empirically for walk-away rights in public acquisitions by Denis and Macias (2010), Officer (2003), and Bates and Lemon (2003)).

strong and a weak form of the *feedback hypothesis*. The strong form of the *feedback hypothesis* holds that both value increasing and distributing provisions should reflect onto pricing, whereas the weak form suggests that this only holds for value increasing provisions. According to the *independence hypothesis*, neither type should affect premiums.

As value increasing provisions, we consider warranties and covenants, because they reduce adverse selection or moral hazard concerns. As a consequence, they increase the probability of deal completion and prevent costly measures, such as monitoring and screening. As value distributing, we consider provisions that determine the allocation of risk between buyers and sellers. Bearing additional risk imposes costs on one party while benefitting the other, such that these provisions cannot benefit both parties simultaneously. To reflect contractual risk allocation, we consider clauses that limit the scope or enforceability of the warranties, thereby limiting the extent to which warranties provide insurance next to signaling quality. Moreover, as another measure of risk allocation, we consider the extent to which sellers bear the risk of adverse events occurring between signing and closing.

To identify a causal relation between contract design and acquisition pricing, we use an instrumental variables approach. To this end, we build on the findings in Chapter 2 and exploit exogenous variation in contract design that arises as different law firms use different internal specimen contracts as a starting point when advising their clients. If these contracts are not fully customized to deal specifics, then variation in contract design partly reflects variation in the specimen contracts. Therefore, law firm fixed effects, of the law firms who provided the first drafts, are employed as instruments.

The findings in Chapter 3 support the weak form of the *feedback hypothesis.* Both warranties and covenants significantly increase premiums paid in acquisitions, which we measure using the market-to-book value of the target (e.g., López-de-Silanes (1997) and Masulis and Nahata (2011)). This suggests that buyers pay for protection granted against adverse selection and agency concerns with higher prices. In contrast, value distributing provisions do not seem to affect prices. This could indicate that parties do not anticipate

contractual value allocation when they set prices. On the other hand, some value distributing provisions do positively affect premiums in samples where sellers have high bargaining power, for example when they are large relative to buyers. This could suggest that the value of risk-allocating provisions is known, but that sellers need to have high bargaining power to demand compensation for bearing such additional risk.

To obtain a better understanding of the price impact from warranties and covenants, we next analyze whether mitigating some concerns is more valuable than others. To this end, we categorize these provisions according to the concerns they address, as in Chapter 2, and test whether there is heterogeneity in the price impact across categories. We find that the positive effect of warranties on premiums is mainly driven by warranties that relate to target financials and intellectual property rights. Conversely, independent of the covenant category, we find that more covenants relate to higher premiums. However, the strongest impact is driven by covenants on divestments.

Taken together, Chapter 2 and 3 show that styles of legal advisors are important drivers of contract design, and that this contract design has real value consequences. An important next question is, therefore, *how* the lawyers influence acquisitions? To shed light on this, Chapter 4 investigates whether lawyer expertise is one of the drivers behind lawyer styles, as documented in Chapter 2. As such, lawyer expertise will be related to negotiations dynamics and outcomes in acquisitions.

Analyzing the impact from lawyer expertise on acquisition outcomes is interesting, because -if expert lawyers are indeed better at negotiating contracts- two approaches can be distinguished on how lawyers use their expertise. According to the *cooperative-advice hypothesis*, the main objective of lawyers is to execute legal elements of a transaction and mitigate any economic issues that arise between buyers and sellers. This view asserts that lawyer expertise is only used to maximize the joint value of both parties (e.g., Gilson (1984) or Mnookin, Peppet, and Tulumello (2000)). In contrast, according to *competitive-advice hypothesis*, lawyers compete to negotiate outcomes in favor of their own clients' interests. As a result, lawyers with more legal expertise relative to the counterparty distribute value

away from the opposing parties and towards the own clients. As lawyers, we consider only the lead lawyers representing the buyer and seller. They oversee all legal aspects of the negotiations for their clients and are usually partners at their firms.

To test whether these lawyers compete to yield benefits for their own client, Chapter 4 focuses on the impact from a divergence in expertise between the lawyers. To this end, we create measures of the expertise of the buyer lawyer *relative* to that of the seller lawyer (relative lawyer expertise). As proxies for lawyer expertise, we consider measures of both their experience and education. These expertise measures are then related to negotiation outcomes where the interests of buyers and sellers are conflicting, such that there is scope for lawyers to compete in obtaining value for their own client. As negotiation outcomes, we use proxies for (i) contract design, (ii) the bargaining process, and (iii) acquisition pricing.

The findings in Chapter 4 support the *competitive-advice hypothesis*, as more relative lawyer expertise relates favorably to all three types of negotiation outcomes. First, as proxies for contract design, we consider provisions that allocate risk between buyers and sellers, because incentives are most conflicting there. We find that more expertise on the buyer's side (relative to the seller side) is associated with more risk being allocated to sellers in the contract design, and vice versa.

Second, expert lawyers are encouraged to influence the bargaining process in their clients' favor, as this has implications for both contract design and pricing. Supporting the *competitive-advice hypothesis*, we find that more relative legal expertise on the buyer side is associated with a process that favors buyers. In such deals, the probability is higher that the buyer can come up with the first draft, leading to a first mover advantage. Moreover, more buyer expertise is associated with shorter negotiation and shorter closing times (i.e., the time between signing and closing). Buyers benefit from short negotiations as they reduce agency problems, save transaction costs, and avoid that the period of exclusive negotiations expires. Sellers could benefit from longer negotiations as it increases the opportunities to look for alternative bidders. Similarly, buyers prefer shorter closing times, as sellers keep control over the target until the closing date, which allows them to extract private benefits.

Third, we find that more legal expertise is associated with more favorable pricing (i.e., lower prices for buyers), also after controlling for the effects of financial advisors and contract design. Whereas lawyers are generally not the primary parties bargaining over acquisition prices, contract negotiations can result in adjustments to initial prices. Buyer lawyer expertise can, for example, result in adjustments if lawyers spot problems in the due diligence that justify a price reduction, or by demanding higher discounts for including seller-friendly clauses. Together, the results in Chapter 4 are consistent with the hypothesis that higher relative lawyer expertise is associated with more favorable negotiation outcomes.

Overall, this thesis underscores the relevance of contracts in financial transactions, specifically in private acquisitions. First, this thesis shows that acquisition contracts show substantial variation across deals and that this variation is partly driven by deal economics. As such, we contribute to an M&A literature on public takeovers, which has focused on drivers of contracts terms such as payment mechanisms and MAC clauses.[13] Moreover, this thesis documents that these contracts have value implications that reflect into premiums paid. This highlights that contract design is an important additional, and often unobserved, factor in explaining acquisition premiums. This contributes to an extensive literature that aims at identifying these drivers.[14] Third, this thesis emphasizes the influence of legal advisors when advising their clients in M&A. The styles of these advisors affect contract design, bargaining strategies, and acquisition premiums. This contributes to an increasing literature that measures to what extent styles of advisors affect corporate decisions and contracts.[15] To conclude, this thesis shows that it is important to integrate a law and finance perspective when studying mergers and acquisitions, as this sheds light on important determinants of M&A outcomes.

[13] See e.g., Faccio and Masulis (2005), and Cain, Denis, and Denis (2011)) on payment mechanisms, and Gilson and Schwartz (2005), Choi and Triantis (2010), and Denis and Macias (2012) on MAC clauses.
[14] See e.g., Erel, Jang, and Weisbach (2012) for the impact of expected syngeries, Aktas, De Bodt, and Roll (2010), and Betton and Eckbo (2000) emphasize bargaining power. And Harford (1999), Masulis, Wang, and Xie (2007) , Stulz, Walkling, and Song (1990), and Moeller (2005), document an impact from governance.
[15] See Servaes and Zenner (1996), Kale, Kini, and Ryan (2003), Rau (2000), Calomiris and Hitscherich (2007), or Bao and Edmans (2011)) on financial advisors, and Coates (2001, 2012), Krishnan and Laux (2007), and Krishnan and Masulis (2013) on legal advisors.

2

What Drives the Variation in Acquisition Contracts: Economics or Lawyers?

2.1 Introduction

What is the role of contracts in financial transactions? Are contracts instruments to primarily mitigate economic problems between contracting parties, as suggested by Coase (1937)? Or do contracts also reflect non-economic conditions, such as the styles of the legal advisors involved in these transactions (as suggested by e.g., Coates (2001, 2012), Krishnan and Masulis (2013), and Kaplan, Martel and Strömberg (2007))? According to the first view, which we refer to as the *economic-contracting hypothesis,* the negotiation process should yield contracts which are a pure reflection of the economic determinants of a transaction. This hypothesis forms the foundation to most of contract theory, where economic concerns (such as adverse selection, moral hazard, and risk allocation) are optimally addressed contractually, subject only to limitations of incomplete contracting.[1] According to this hypothesis, legal advisors function as "transaction cost engineers", by projecting an optimal contracting structure to any combination of economic issues (Gilson (1984)).

[1] See Bolton and Dewatripont (2005) or Hart (2001) for extensive overviews of contract theory.

Conversely, according to the second view, styles of legal advisors, i.e., their preferences or biases, also partially influence contracting outcomes, leading to deviations from contracts that purely reflect economic deal conditions. We consider this the *lawyer-contracting hypothesis.* Whereas influence from legal advisors need not necessarily imply inefficient contracting, the implications of the drivers of contracting can be important if contract provisions affect transaction prices.

To address these two views, we analyze contracts used to acquire private targets. Private acquisition contracts provide an interesting set-up to analyze contracting, because they are the result of extensive negotiations between buyers and sellers, and often constitute one of the most important decisions in the lifetime of a company. Moreover, private acquisitions make up for the vast majority of mergers and acquisitions.[2] We have access to 151 proprietary purchase agreements, which have been made available by one of the largest law firms in The Netherlands. These contracts span the period from 2005 to 2010, with deal values averaging about EUR 220 million.

Our empirical analysis focuses on two sets of key contract provisions that are used to protect buyers—warranties and covenants.[3] Warranties are guarantees that sellers make about the quality of targets that are sold. Covenants restrict seller behavior in the period between the signing of the contract and the transfer of the target, comparable to covenants in debt or venture capital contracts (e.g., Gompers and Lerner (1996), Kaplan and Strömberg (2003), Murfin (2012), and Bradley and Roberts (2004)). We study variation in the *intensity* of warranties and covenants, which is measured by the number of such provisions in a contract.[4]

Our empirical findings support the *lawyer-contracting hypothesis*: next to economic deal characteristics, styles of legal advisors explain parts of the variation in

[2] Erel, Liao, and Weisbach (2011) document that 96% of cross-border transactions involve privately held targets. Betton, Eckbo, and Thorburn (2007) show that, for US takeovers, about 63% of the targets are privately held.

[3] Gilson and Schwartz (2005, p.333), state that "three sets of provisions reflect the three basic engineering elements of a corporate acquisition agreement: representations and warranties, covenants and conditions." Similarly, Martinius (2005, p.36), claims that "representations and warranties […] are the primary means to protect the buyer."

[4] This approach of counting the number of contract provisions to measure the intensity of contract strictness is similar to Murfin (2012), Gompers and Lerner (1996), and Lerner and Malmendier (2010). We benchmark the number of provisions to a model takeover contract to assess whether a given contract grants relatively high or low protection on a certain issue.

contract design. To arrive at this conclusion, we first examine the economic environment in which a contract is signed and the extent to which it explains contract provisions. We find that economic conditions, such as information asymmetry, agency conflicts, and bargaining power significantly affect contracts. To illustrate, deals where information (agency) concerns are more pronounced use contracts containing more warranties (covenants). Moreover, higher buyer bargaining power is associated with stronger protection, reflected by more warranties and covenants. Taken together, a regression which controls for proxies of economic variables explains 39% of the variation in warranties and 34% of the variation in covenants. This raises the question whether styles of legal advisors (i.e., law firms and lawyers) might explain some of the remaining unexplained variation.

We first assess whether law firm styles affect contracting. To this end, we focus on the law firms that are drafting the first versions of the acquisition contracts. Law firms typically use standardized internal specimens when drafting new contracts and, due to path dependence, parts of these first versions tend to be reflected in the final purchase agreements.[5] By exploiting information on the identity of the 28 drafting law firms, we empirically identify the effects of their preferences or biases on the final contract design using law firm fixed effects. In support of the *lawyer-contracting hypothesis*, we find that the law firm fixed effects are jointly statistically significant for both warranties and covenants. Relative to baseline specifications that account for economic deal determinants only, adding law firm fixed effects increases the explanatory power with a modest 3% for warranties, and 6% for covenants.

To further examine the effect of legal advisors, we then ask whether the personal styles of individual lawyers also mirror into contract design. To empirically identify their effect, we again focus on the first versions of the contracts and consider the identities of the individual lead lawyers who provided these drafts (partner fixed effects). To identify these effects, we hold the law firm style constant and only consider contracts first drafted by the law firm that provided our data; this restricts the sample to 94 contracts drafted by 20 different lead lawyers. We find that partner fixed effects also significantly

[5] Contracting parties might not deviate strongly from such specimen contracts due to transaction costs or to avoid enforcement uncertainty (Kahan and Klausner (1997), Gennaioli and Perotti (2012)).

impact contract design. After controlling for economic deal characteristics, adding partner fixed effects increases the explanatory power with 7% for warranties, and 19% for covenants.

Together, these results suggest that styles of legal advisors impact contract design, above and beyond their role as simply projecting contract provisions to economic issues faced by contracting parties. We next analyze whether this impact is homogeneous across different categories of warranty and covenant provisions. By considering categories, we can test whether some provisions are driven more by economic conditions, whereas others are more related to styles of legal advisors. We create categories based on the concerns that different warranties and covenants address and find substantial variation in the effect of law firm and partner fixed effects across these categories. Law firm styles are most influential for provisions that address concerns which are generally similar across deals, implying that adjustments to the specimen contracts are not needed. Examples are warranties on employees and legal compliance, and covenants on employees and divestments. Conversely, lawyer styles seem to matter most for provisions where the interests of the two parties are usually not very aligned and where value can be distributed. Examples are warranties on legal compliance, intellectual property, and insurance matters, and covenants on litigation, employees, and acquisitions.[6] Misalignments of interests between buyers and sellers in these categories implies that the negotiation styles of lawyers matter for the distribution of value. Lastly, neither law firm nor partner fixed effects seem to contribute to the explanatory power of warranties on financial accounts or corporate documents, and covenants on corporate records and dividends. This could be because concerns covered with these categories have a very direct economic impact, implying that contract provisions tend to be highly customized to the economics of the deal environment; they are almost fully driven by economic variables.[7]

[6] These categories contain a relatively high portion of warranties or covenants that affect risk allocation between buyers and sellers, such that objectives of contracting parties are conflicting (both prefer, ceteris paribus, to allocate more risk to the counterparty), and each warranty could affect value distribution by shifting the risk.

[7] Supporting this view, we find that these categories derive the most explanatory power from our proxies for economic variables.

Finally, we examine whether *observable* law firm and lawyer characteristics capture parts of the variation explained by styles of law firms and lawyers. For law firms, we consider measures of deal experience, law firm ranking, and whether the headquarters are located in the US. We find that law firms with US-based headquarters draft contracts with more warranties, while law firm ranking or deal experience are not related to warranties and covenants. We then look at lawyer characteristics, which we measure using experience, education, and risk aversion. The latter variable is proxied by (i) whether the lawyer is female, and (ii) a self-assessed risk aversion level elicited in the interviews with lawyers of our law firm.

We find that variation in covenants can partially be explained by whether a lawyer has a business degree, her deal experience, and whether she has corporate sector experience. However, partner fixed effects capture a larger chunk of variation in covenants than any of these observable characteristics, suggesting that unobservable characteristics remain influential for those provisions. We further find that higher risk aversion is associated with fewer warranties. This impact is strongest for the categories for which partner fixed effects have the highest explanatory power, suggesting that risk aversion reflects a large fraction of the impact of lawyer styles on warranties. In contrast, risk aversion does not seem to affect covenants.

Our results emphasize the influence of legal advisors on contracting. However, if legal advisors are endogenously matched to deals or clients, the results could still be consistent with the *economic-contracting hypothesis*—styles of law firms or lawyers could merely reflect unobservable deal or client characteristics. We perform several robustness tests to show that this is unlikely. To start, our data suggest that the vast majority of deals are assigned to law firms and lawyers based on historically determined, long-term relations, with clients engaging with the same law firm over many consecutive deals, independent of deal characteristics.[8] Further, our results are robust to controlling for target industry and client fixed effects, which absorb unobserved deal and client heterogeneity.

[8] Our results are robust to limiting the sample to contracts where the law firm and client already have an established business relation prior to a transaction. Moreover, they are robust to controlling for client-lawyer switches and client fixed effects.

Our paper makes several contributions to the literature. First, we provide one of the first analyses of warranties and covenants in private acquisition contracts. We thereby contribute to the M&A literature on public deals, which has focused on economic drivers of other contract provisions such as payment mechanisms or MAC clauses.[9] Second, we contribute to an increasing literature that measures to what extent styles of advisors affect corporate decisions and contracts.[10] Third, by considering the impact of personal lawyer styles in addition to law firm styles, we contribute to the literature that stresses the impact of personal characteristics for corporate decision making.[11]

The paper proceeds as follows. Section 2.2 describes the data and provides summary statistics. Section 2.3 provides the empirical analysis of the impact of economic variables on warranties and covenants. Section 2.4 analyzes the role of law firm and partner styles. Section 2.5 discusses endogeneity and robustness issues, and Section 2.6 concludes.

2.2 Data and Summary Statistics

2.2.1 Data Description

We analyze a proprietary dataset of purchase contracts underlying acquisitions of privately held targets. The contracts have been made available by one of the largest law firms in The Netherlands. The law firm is specialized in corporate law and mergers and acquisitions and acted in all deals as legal advisor to either a buyer or seller. Our initial sample comprises all acquisitions of privately held targets that the law firm has advised on between 2005 and 2010, yielding an initial sample size of around 300 transactions. We exclude deals where key contract information was missing. For these deals, it is

[9] See Eckbo, Giammarino, and Heinkel (1990), Faccio and Masulis (2005), Martin (1996), and Cain, Denis, and Denis (2011)) on payment mechanisms, and Gilson and Schwartz (2005), Choi and Triantis (2010), and Denis and Macias (2012) on MAC clauses.

[10] See Servaes and Zenner (1996), Kale, Kini, and Ryan (2003), Rau (2000), Calomiris and Hitscherich (2007), or Bao and Edmans (2011)) on financial advisors, and Coates (2001, 2012), Krishnan and Laux (2007), and Krishnan and Masulis (2013) on legal advisors.

[11] For example on the effect of manager styles on financial decisions (e.g., Bertrand and Schoar (2003), Ben-David, Graham, and Harvey (2012), and Malmendier and Tate (2005, 2008)) or on the effects of judges for court rulings (e.g., Chang and Schoar (2006), Eisenberg, Fisher, and Rosen-Zvi (2012)).

unclear whether the negotiations were abandoned or whether the contract has not been filed properly. This leaves us with a final sample of 151 transactions.

We match these contract data with financial data on the targets, buyers, and sellers.[12] Financial data on buyers and sellers are obtained from Amadeus or their financial statements. We use the annual accounts of the year preceding the closing of a transaction to ensure that the effects of the transaction are not incorporated in the accounts yet. Financial data on targets has been obtained from: (i) the financial statements of buyers or sellers; (ii) Amadeus or national trade registers; and (iii) financial accounts in the appendices to the contracts.[13] Information on the identity of the involved law firms and lawyers is derived from the contracts and Merger Market, which contains data on financial and legal advisors in corporate acquisitions. For each of these involved law firm and lawyers, we collect profile data from Merger Market, the law firms' corporate websites, and internet searches.

Table 2.1 Panel A provides summary statistics for our sample. The average transaction has a deal value of EUR 222 million. In terms of target characteristics, 9% of the deals are transfers of assets, while the rest involve share deals. Targets are spread across different industries and countries, though there is, by construction, a concentration of targets in The Netherlands (see Appendix A-2.3). The median book value of the buyers is EUR 1.4 billion, while that of the sellers is EUR 2.1 billion. Appendix A-2.3 also shows that 38% of the transactions arise as one corporation sells a subsidiary to another one. Our sample contains private-equity buyers (22%), private-equity sellers (15%), and families selling their businesses (18%).[14]

To identify the impact of law firm and lawyer styles, we focus on the law firms and lead lawyers who provide the first contract drafts for a transaction. We can identify who has provided the first draft by the business label that is printed on the layouts of the final contracts. A total of 28 different law firms provide first drafts in our sample, with

[12] Note that, as opposed to public acquisitions, targets are different legal entities than sellers, where sellers can be a corporation, institution, or family selling the shares/ assets of a target company.
[13] For target financials derived from financial statements of buyers or sellers, we consider the accounts of the year in which the acquisition occurred, such that the accounts list the value of assets and liabilities acquired, or divested.
[14] Correlations between these variables are given in Appendix A-2.9.

our law firm providing them for 94 deals.[15] The remaining law firms provide first drafts for, on average, two deals. From these 28 law firms, a total of 66 individual lawyers provided a first contract draft in the sample. These lawyers are the lead lawyers on a transaction and mostly at partner rank within their firms.[16] For most of the analysis on lawyers styles, we will restrict our attention to contracts drafted by our law firm, as this allows us to keep the law firm style constant. There are 20 lead lawyers from our law firm in the sample.

Table 2.1 Panel B reports summary statistics of the characteristics of these drafting law firms and lawyers. It reports that 15% of the contracts were drafted by a law firm in the top 10 ranking, based on deal volume between 1995 and 2010. In terms of location, 3% of the contracts are drafted by a law firm with headquarters in the US. The partners have, on average, advised on 37 M&A deals, and 27% of the contracts is drafted by lawyers who have corporate work experience. Moreover, almost one third of the contracts is from lawyers who have studied in the US, and 9% of the sample has been drafted by a female lawyer.

We have two measures of risk aversion. The first measure simply indicates whether a lawyer is a female or male, assuming that women are generally more risk averse (e.g., Eckel and Grossman (2008) and Sapienza, Zingales, and Maestripieri (2009)).[17] The second measure is based on interviews with 14 of the 20 lead lawyers of our law firm; they drafted a total of 66 contracts together. Using the methodology from Dohmen et al. (2011), we asked the lawyers:

"How do you see yourself: are you generally a person who is fully prepared to take risks or do you try to avoid taking risks? Please place yourself on the scale of 0 to 10, where the value 0 means: 'not at all willing to take risks' and the value 10 means: 'very willing to take risks'."

[15] Our results are robust to excluding all deals where our law firm provided the first draft.
[16] We can identify the lead lawyer from Merger Market, which indicates the lead lawyer if more than one lawyer is listed. We complement this with information from internet searches of deal announcements.
[17] This correlation between gender and risk aversion should be assumed with caution, as this has been found to be less persistent in certain specific contexts, for example with female board members (Adams and Funk (2012)).

On average, the interviewed lawyers scaled themselves at position 6.4, with a median of 7.0. We use the interview responses to create a measure of risk aversion by calculating 10 minus this scale position, thereby ensuring that higher values indicate a higher level of risk aversion. Table 2.1 Panel B reports that the average contract was drafted by a lawyer with a risk aversion of 3.1.

2.2.2 Summary Statistics on Contract Provisions

We study the determinants of two key provisions that are used to protect buyers: warranties and covenants. While warranties are a list of statements that a seller makes about target quality, covenants limit the behavior of the seller or target management in the period between the signing and closing of the contract.[18]

To measure contract design, we consider two types of dependent variables for both warranties and covenants. First, we count the number of all warranties and covenants in a contract. Table 2.2 Panel A shows that contracts contain, on average, 98 warranties and 20 covenants.[19] Figure 2.1 plots the distribution of warranties (Panel A) and covenants (Panel B), documenting considerable cross-sectional variation for both types of provisions. To allow for comparability, we benchmark the number of warranties and covenants relative to a model contract provided by Miller (2008). This model contract lists the warranties and covenants required to offer full buyer protection and it contains a total of 271 warranties and 35 covenants.

Second, we categorize warranties and covenants according to the underlying concerns that they address. To identify these concerns, we rely on a classification in Miller (2008).[20] Table 2.2 Panel B lists these categories and the number of warranties and covenants per category. It shows that the numbers of warranties in the model contract varies considerably across categories, suggesting that certain topics require more warranties to grant a given of protection. We divide the number of provisions in each category by its respective number in the model contract to allow for a comparison across

[18] Appendix A-2.2 lists the most frequently used warranties and covenants.

[19] Summary statistics on covenants are based on transactions where signing and closing (transfer) dates are not the same as covenants are only relevant if there is time between signing and closing.

[20] In terms of the warranties, Miller (2008, p. 51) lists seven issues that the "the buyer's lawyers should look for to avoid bombs", which serve as the categories along which warranties are divided. For covenants, the concern categories are also derived from the model contract in Miller (2008), which specifies the clauses that govern the actions of the seller (or the target) in the period between signing and closing.

categories. As such, we measure whether a relatively high or low level of protection is granted with respect to a certain concern category.[21]

2.3. Economic Determinants of Acquisition Contracts

2.3.1 Predictions on Economic Determinants

According to the *economic-contracting hypothesis*, variation in contract provisions are purely driven by economic determinants of contract design. To assess how much variation can be explained by these factors, we create proxies for the main economic drivers of warranties and covenants.

Economic Determinants of Warranties

Three economic determinants have been identified as drivers of the variation in warranties: (i) information asymmetry; (ii) risk-bearing capacity; and (iii) bargaining power.

First, if sellers are better informed about target quality than buyers, an adverse selection problem can occur (Akerlof (1970)). Whereas sellers commonly mitigate this problem by allowing buyers to perform due diligence, some asymmetry may remain about data completeness or unverifiable information. Warranties can be used by sellers to complement disclosed information and to signal target quality to the buyer (Emons (1989), Grossman (1981), Spence (1970)). Grossman (1981) shows that, if there are no costs to granting warranties, it is optimal for sellers to provide a full set of warranties as any deviation thereof reduces the buyers' willingness to pay. However, there can be costs to warranties too, which include transaction costs or a loss of competitiveness from disclosing sensitive information. Admati and Pfleiderer (2000) show that the optimal amount of warranties varies with information asymmetry if it is costly to provide warranties.

[21] This standardization does not affect the statistical significance of our results but makes the regression coefficients more comparable across categories.

We proxy for information asymmetry by including five dummy variables, which equal one if: (i) a deal is cross-border (e.g., Datar, Frankel and Wolfson (2001), Kohers and Ang (2000), Faccio and Masulis (2005)); (ii) a deal is cross-industry; (iii) the buyer owns target shares (a toehold) prior to the takeover (Servaes and Zenner (1996)); (iv) the target operates in a high R&D industry; and (v) a deal is an asset deal. In asset deals, contracts contain a list of all assets acquired and liabilities transferred, which reduces uncertainty about the balance sheet of the target. Finally, we include the natural logarithm of the transaction value and assume more information asymmetry for larger deals (e.g., Martin (1996), Cain, Denis, and Denis (2011) and Kohers and Ang (2000)).

Second, warranties can also serve as risk-allocation (or insurance) devices if sellers grant warranties on quality issues about which they are uncertain (e.g., Emons (1989)). For example, sellers may guarantee that no third party is violating the intellectual property of the target. Whereas sellers might have more information about this than buyers, they still may not be fully certain. Nevertheless, sellers can agree to pay for damages in case of a violation of such a warranty, thereby essentially providing insurance to the buyers. Sellers should grant these warranties if they have a higher risk-bearing capacity than buyers (Heal (1977)).[22]

We consider several buyer and seller characteristics as proxies for risk-bearing capacity. Assuming that risk-bearing capacity increases with buyer or seller portfolio diversification, we include three dummy variables, which equal one if: (i) the buyer is a private-equity fund; (ii) the seller is a private-equity fund; and (iii) the seller is a family. Private-equity funds may have a higher risk-bearing capacity as they tend to have diversified investments in multiple industries. On the other extreme, family sellers typically only have investments in one company and are therefore relatively undiversified. To proxy for risk-sharing possibilities among multiple sellers, we measure the percentage of shares (or assets) sold by the largest seller. The smaller this figure, the more (similar sized) sellers there are in a deal, and we assume that this increases risk-bearing capacity of those sellers. We also include a measure of the relative size of the buyers to the sellers, assuming that bigger companies have a higher risk-bearing capacity.

[22] Sellers could also grant such warranties if they are better informed about the probability of a risk occurring, suggesting again that more warranties are associated with more information asymmetry.

Third, we measure relative bargaining power. Warranties can allocate risk from buyers to sellers in a way that each additional warranty distributes value away from sellers to buyers. The extent of such distributional effects is likely to depend on the relative bargaining power of the two parties (e.g., Choi and Triantis (2012)). We proxy for buyer bargaining power by including three dummy variables, which are one if: (i) the first contract draft was provided by the advisors of the buyer[23]; (ii) a deal was signed during or after the financial crisis (Aktas, De Bodt, and Roll (2010)); and (iii) the transaction was organized through a controlled auction. The latter could either reflect a better bargaining position for sellers as there are more bidders (Boone and Mulherin (2007)) or a better bargaining position for the buyer as the deal is initiated by the seller (Aktas, De Bodt, and Roll (2010)). In addition, we use the relative size of buyers to sellers as a measure of relative bargaining power.

Economic Determinants of Covenants

Covenants restrict the behavior of sellers in the period between the signing of the contract and the closing (i.e., the actual transfer of control). Signing and closing dates can differ as the parties may need to obtain approvals from competition authorities or financial regulators. On average, this period is around two months in our sample. Three economic determinants may drive variation in covenants: (i) agency conflicts; (ii) value of flexibility of management; and (iii) bargaining power.

First, agency conflicts can arise as sellers remain in control of the target after signing and before closing, i.e., in a period during which the purchase price has already been fixed. As a result, sellers have incentives to extract private benefits by granting discounts to customers or shirking in managing the target. Covenants can serve as an instrument to commit sellers not to extract such benefits (see Gompers and Lerner (1996)).[24] We capture agency conflicts using different variables. We proxy for monitoring costs, which should be related to agency conflicts, by including our proxies for information asymmetry. To reflect the expected *ex-ante* length of the time period that

[23] The party whose law firm has provided the first draft has a first mover advantage (e.g., Molod (1994)). It is therefore likely that the party with the most bargaining power will demand the right of providing the first draft.

[24] Gompers and Lerner (1996) find for venture capital contracts that the number of covenants increases if agency problems increase and monitoring costs decrease.

allows sellers to engage in opportunistic behavior, we include a dummy which equals one if competition approval is required after signing. In addition, we control for the *ex-post* number of days between the signing and closing dates. Finally, based on Jensen (1986), we use a measure of the availability of cash by including the ratio of target cash to assets (see Lang, Stulz, and Walkling (1991)).

Second, covenant intensity may also be related to the value of retaining flexibility in managing the target in the interim period. As pointed out by Kahan and Yermack (1998), covenants may be costly if they constrain sellers in responding to changing market circumstances or pursuing profitable opportunities. This is important to a seller as the deal could still fail, such that the seller will remain the owner of the target. Flexibility in control is most valuable in industries with high investment opportunities, such that contracts concerning targets in those industries should contain fewer covenants (e.g., Kahan and Yermack (1998), Nash, Netter, and Poulson (2003)). We proxy for investment opportunities with a dummy variable which takes the value one if the target is active in an industry with high capital expenditure needs.[25]

Finally, bargaining power can also be a determinant for covenants (Choi and Triantis (2012), Gompers and Lerner (1996)) and we control for it by using the proxies outlined above.

2.3.2 Empirical Evidence on the Role of Economic Determinants

We start our empirical analysis by assessing the effect of our proxies for economic determinants on warranties and covenants. Table 2.3 reports regressions of our measures of warranty intensity (i.e., the number of warranties relative to the model contract) and covenant intensity (i.e., the number of covenants relative to the model contract) on the proxies for economic determinants of contract design. When covenant

[25] The industries classified as high capital expenditures are the following: Petroleum and Natural Gas, Consumer Goods, Non-Metallic and Industries, Real Estate, Communication, Retail, Transportation, Utilities, Food Products, Personal Services, and Other. These industries are in the top 25% of our sample in terms of the industry mean of capital expenditures to assets, where industries are classified according to the Fama French 48 Industries-classification.

intensity is the dependent variable, we restrict the sample to deals where signing and closing dates are not the same, as covenants serve no purpose if those dates coincide.[26]

Our regressions suggest the following two findings. First, economic characteristics matter for contract design. For example, we find that cross-country deals are associated with more warranties, whereas asset deals and toehold deals have fewer warranties; this suggests that more warranties are used in deals with more information asymmetries. Further, deals where buyers have more bargaining power, reflected in the first contract draft being provided by the buyer and deals after 2008, contain significantly more warranties. There is some evidence in support of the risk-bearing motive of warranties, since the percentage sold by the main seller is significantly negatively related to warranty intensity. However, contracts from private-equity sellers appear to contain fewer warranties, inconsistent with predictions based on risk-bearing considerations. Overall, these results suggest that information asymmetry and bargaining power are important determinants of warranty intensity, with risk-bearing issues being somewhat less relevant. Similarly, covenant intensity seems to be positively related to agency conflicts, consistent with Gompers and Lerner (1996). For example, an increase in the number of days between signing and closing is associated with more covenants. Moreover, deals where competition approval is required and larger deals contain more covenants, whereas asset and toehold deals are associated with fewer covenants. Second, our proxies for these economic deal characteristics explain a substantial part of the variation in contract design. Together, proxies for economic determinants explain 39% of the variation in the number of warranties, and 34% of the variation in the number of covenants.[27]

We next study whether the impact of deal characteristics on contract provisions is heterogeneous across categories in a way that supports the importance of deal economics on contract design. To this end, Appendix A-2.4 Panel A reports regressions that explain the number of warranties per category using our previous set of proxies. We find that proxies for information asymmetry seem are only statistically significant for

[26] The total number of contracts with time between signing and closing is 99, but three observations are lost in the regression as not all explanatory variables are available for all contracts.

[27] To bias against finding additional explanatory power from law firm or partner fixed effects, the proxies for economic determinants have been selected such that we maximize their joint explanatory power on the warranties and covenants.

categories where such asymmetries are most relevant. For example, asset deals contain fewer warranties only for financial accounts, corporate records, contracts, and insurance. This is intuitive as the list of transferrable assets in such deals reduces the asymmetry only on those topics. Similarly, only contracts involving targets in research-intense industries contain significantly more warranties on intellectual property rights. Across all warranty categories, 25% of the variation in warranties can be explained, on average, with our proxies for economic determinants of contract design. However, there is substantial variation across categories, as economic drivers explain 49% of the variation of warranties on financial accounts, whereas they only account for 11% of the variation in warranties on assets.

Appendix A-2.4 Panel B reports similar regressions for the covenants categories. Supporting the relevance of agency concerns, contracts on targets with high cash holdings contain significantly more covenants on only dividend payments. Moreover, in terms of the value of flexibility of target management, we find that deals involving targets from industries with high investment requirements are associated with significantly fewer covenants on dividends, debt, and business conduct; these are the categories with the strongest impact on a target's cash position. In line with the findings of the warranty categories, these results suggest that such provisions are mainly included in situations where they seem most relevant. On average, 19% of the variation across covenant categories can be explained by economic determinants, and they have the highest explanatory power for covenants on dividends (33%) and divestments (26%).

Together, the impact of economic determinants on contract design provides initial support of the *economic-contracting hypothesis*. However, about two thirds of the variation in contract design cannot be explained by the economic deal environment, suggesting that other factors such as the styles of legal advisors might also be important.

2.4 Effect of Legal Advisors on Acquisition Contracts

2.4.1 Predictions on Legal Advisors Styles

Law Firm Styles

According to the *lawyer-contracting hypothesis*, law firms and lawyers affect contracting beyond merely objectively applying contract provisions to address economic concerns. Law firm styles can impact contract design if three conditions are satisfied. First, law firms must use standardized specimen contracts when advising clients on transactions. When two parties negotiate over an acquisition, both generally consult with (at least one) law firm. One of the law firms will then provide a first draft version of the acquisition contract, which is typically a combination of a standard internal specimen contract used by the law firm, and some adaptation to deal-specifics (e.g., Miller (2008), Coates (2001)). This draft will form the basis for future negotiations.

Second, during the negotiations, contracts should not be fully adjusted to the deal-specific circumstances (economic determinants), such that the design of these first drafts still affects the final contractual outcomes. Partly maintaining the first draft of a contract can be optimal *ex-ante* from a transaction cost perspective, as this prevents negotiations over all possible clauses (Armour (2004)). Moreover, there are externalities in terms of enforcement certainty when these specimen contracts contain highly standardized provisions (Kahan and Klausner (1997), Gennaioli and Perotti (2012)). However, fully applying a standardized specimen would yield a contract that is not customized to specific deal circumstances. As such, it is likely that first draft contracts are most influential for provisions that require little customization to deal specifics, for example, because they relate to concerns which are comparable across deals.

The third condition is that these standard specimen contracts vary across law firms, which could be due to heterogeneity in preferences, biases or expertise (Coates (2001, 2012), Krishnan and Masulis (2013), Kaplan, Martel and Strömberg (2007)). If all three conditions hold, then the styles of the drafting law firms can reflect onto the final contracts. Consequently, our empirical analysis will exploit information on the identity of the drafting law firms to measure the effects of law firm styles.

Lawyer Styles

Next to law firm styles, variation across contracts may also reflect the personal styles of lawyers employed by the law firms. Prior literature suggests that individual

characteristics can have a substantial impact on financial and legal decision making (e.g., Bertrand and Schoar (2003), Kaplan, Klebanov, and Sorensen (2008), Chang and Schoar (2006), and Eisenberg, Fisher and Rosen-Zvi (2012)). Personal preferences of lawyers should be most apparent for provisions where the interests of the negotiating parties are not aligned, such that the personal negotiation styles of lawyers become important.

2.4.2 Empirical Analysis of the Role of Law Firm Styles

To test whether our data provide evidence for the *lawyer-contracting hypothesis,* we analyze to what extent the styles of legal advisors—that is law firms and lawyers—provide additional explanatory power in explaining the variation in contract provisions, above and beyond the economic variables assessed in Section 2.3.

Measuring Law Firm Styles

We test for the effects of law firm styles by running regressions of contract design on a set of dummy variables which indicate the law firms that have provided the first draft of a contract (law firm fixed effects). We then test, similar to the methodology in Bertrand and Schoar (2003) and Bao and Edmans (2011), whether these fixed effects are jointly different from zero after controlling for the economic determinants of contract design. Using adjusted R-squares, we compare the explanatory power of this estimation with a model which only controls for economic determinants. This follows the approach in Dougal et al. (2011) and Gennaioli et al. (2013).

As the inclusion of 28 law firm dummies in our relatively small sample restricts the power of the estimation, a concern could arise whether these fixed effects merely reflect spurious correlations rather than a systematic difference across law firms. To mitigate this, we create a second measure of law firm styles. We construct a variable which reflects the law-firm-specific tendency to include relatively many or few provisions. This variable is obtained by ranking all law firms based on the magnitude of their coefficients in the law firm fixed effects regression. We then create a dummy variable which equals one if a law firm is ranked in the top half in terms of its propensity to

include many warranties or covenants.[28] If the fixed effects were indeed driven by small sample mechanics without reflecting an underlying pattern, then this law firm style dummy should not reflect anything either, and would be insignificantly different from zero.

Impact from Law Firm Styles on Warranties and Covenants

Table 2.4 Panel A shows regressions that explain the number of warranties and covenants with law firm fixed effects (Columns 1 and 3) and the law firm style variable (Column 2 and 4). All regressions control for the proxies of economic determinants described in Section 2.3.

Supporting the *lawyer-contracting hypothesis*, we find that law firm fixed effects are jointly significant at the 1% level for both warranties and covenants. Moreover, adding law firm fixed effects modestly increases the explanatory power of the model from 39% to 41% for the warranties, and 34% to 39% for the covenants. In terms of economic significance, contracts written by a law firm with an above median tendency to include many warranties contain 15% more warranties (relative to the model contract; this translates into 41 additional warranties). Similarly, contracts drafted by law firms with an above median tendency to include many covenants contain 28% more covenants (i.e., 10 additional covenants).

Taken together, these results suggest that law firms have specific styles, and that these styles significantly affect contracting outcomes. In terms of variation explained, these styles, however, only modestly affect the design of warranties and covenants.[29]

[28] Note that, as the number of deals is not uniformly distributed across law firms, these style-dummies are not equal to one for half of the sample. In fact, for warranties 16 contracts are drafted by law firms with a high tendency to include warranties, and 135 by law firms with a low tendency to include warranties. Similarly, for the covenants, 22 contracts are drafted by law firms with a high tendency to include covenants, and 80 by law firms with a low tendency to include covenants.

[29] Note, that the increase in variation explained is stronger upon considering the law firm style variable, where the variation explained increases to 45% for the warranties and to 44% for the covenants.

2.4.3 Empirical Analysis of the Role of Lawyer Styles

Measuring Lawyer Styles

Next, we ask whether individual styles of lawyers also reflect in contract design. To test for the impact of personal styles while keeping the law firm style constant, we restrict the sample to deals where lawyers from our law firm provided the first contract drafts. This provides us with a sample of 94 contracts drafted by 20 different lead lawyers. Similar to the analysis of law firm fixed effects, we include both dummies for the individual lawyers (partner fixed effects) and a dummy variable based on their tendency to include many or few provisions.

Impact from Lawyer Styles on Warranties and Covenants

Table 2.4 Panel B shows regressions that explain the number of warranties and covenants, benchmarked to the model contract, after including partner fixed effects (Columns 1 and 3) and the partner style dummy (Columns 2 and 4). For the covenant regressions, the sample is restricted to deals where signing and closing dates do not coincide. Providing further support for the *lawyer-contracting hypothesis*, we find that partner fixed effects are jointly statistically different from zero for both warranties and covenants. The explanatory power of the warranties model increases by 7% relative to a specification with economic determinants only. Similarly, including partner fixed in a model explaining covenants increases the explanatory power with 19%. Contracts drafted by a lawyer with an above median tendency to include warranties contain 10% more warranties relative to the model contract, which corresponds to 27 more warranties. Moving from a low to a high covenant style lawyer increases the number of covenants by 30% relative to the model.

2.4.4 Empirical Analysis of the Role of Law Firm and Lawyer Styles per Category

Our results indicate that both law firms and lawyers significantly affect contract design. To develop a further understanding of the precise effect of legal advisors, we study whether the impact of law firms or lawyers is contract-provision specific. As explained in Section 2.3, one would expect that law firm styles are most influential for provisions addressing issues that are comparable across deals. On the other hand, lawyer

styles might be more relevant for provisions where the interests of buyers and sellers are misaligned, such that they require negotiations, which could be driven by the personal negotiation styles of lawyers. Lastly, contract provisions should be relatively unaffected by legal advisors if they address concerns which are very deal-specific and have a direct economic impact. To test whether such patterns can be observed, we repeat our previous analysis per warranty and covenant category.

Impact of Law Firm and Lawyer Styles on Warranties per Category

Table 2.5 Panel A reports regression per warranty category, using both law firm fixed effects (left half) and partner fixed effects (right half); we control for the same economic determinants as in Table 2.3. Whereas both law firm fixed effects and partner fixed effects are jointly significant at the 1% level across all categories, there is substantial heterogeneity in terms of their contribution to explanatory power. The pattern that arises is consistent with the expectations described above, suggesting that provisions over similar concerns are mostly driven by styles of law firms, while deal-specific concerns are driven by lawyers or the economic environment of a deal.

To illustrate, neither law firm nor lawyer styles substantially increase the explanatory power for warranties on financial accounts, corporate records, and assets. In fact, these categories are also among those that derive most of their explanatory power from economic determinants. As financial accounts and assets form the core basis on which valuations are based, and are highly deal-specific, it seems intuitive that these provisions are mostly driven by signaling needs and therefore highly customized to deal specifics.[30]

On the other hand, warranties on intellectual property, contracts, and insurance issues are driven by lawyer styles, and to a lesser extent by law firm styles.[31] These categories typically contain provisions that allocate risk in addition to signaling target quality (e.g., a warranty stating that no third party is infringing on the intellectual

[30] Supporting this view, Kling et al. (1997, p.786) state that "because the company's financial statements provide significant and complete information about the business being acquired, the [warranties on, ed.] financial statements and undisclosed liabilities are key to the acquisition agreement." Similarly, for warranties on corporate records, including approvals for executing the contract, Kling et al. (1997, p.786) claim that "this representation is critical to the buyer."

[31] Here, we use a cut-off of an increase in explanatory power of 5% to be considered a substantial impact.

property rights of the target). Therefore, they distribute value between buyers and sellers and negotiation skills of individual lawyers (i.e., their styles) become very relevant. Finally, warranties on employees and legal compliance derive explanatory power from both law firm and lawyer styles. These provisions partly address concerns that are comparable across deals, implying that standard specimen contracts of law firms can be used. They further address concerns where value is allocated through warranties, implying that lawyer style become relevant.[32]

Impact of Law Firm and Lawyer Styles on Covenants per Category

Regressions explaining covenants per category are reported in Table 2.5 Panel B. As with warranties, both law firm and partner fixed effects are jointly significant across all categories, but the categories vary substantially in terms of explanatory power derived from these fixed effects. The covenant categories can be grouped in a way that is similar to the warranty categories. The first group, for which neither law firms nor lawyers substantially increase explanatory power, includes covenants on dividends and corporate records, which could reflect the direct economic impact of changes to dividend payments or corporate documents. The second group of provisions, which are affected by lawyer styles but not by law firm styles, include covenants on debt (10% contribution in explanatory power from adding partner fixed effects to the model), acquisitions (14% contribution), and litigation (26% contribution). This indicates that these are areas in which sellers demand some target control (e.g., to grant pay rises to employees or to engage in capital expenditures), but for which buyers would like to maintain a tight hold. The resulting misalignment of interests implies a higher impact of the negotiation styles of the lawyers. The third group consists covenants on employees, business conduct, and divestments and they derive explanatory power from both law firms and lawyers. This suggests that these covenant categories contain provisions which are similar across deals, as well as provisions which are adjusted, but require negotiation. The overview of frequently used covenants in Appendix A-2.2 Panel B provides examples of this. The

[32] This argumentation is supported, for example, by legal literature on legal compliance warranties. On the one hand, legal compliance warranties address full compliance with laws and permits obtained by the target (Kling et al. (1997)). The concerns regarding such general laws tend to be comparable across deals. On the other hand, they also address issues of environmental compliance and Kling et al. (1997, p.788) argue that "the portion of this representation which is the most debated concerns environmental matters," making negation styles of lawyers important.

category of business conduct, for example, contains “Target shall maintain good contact with suppliers and customers”, which will be applicable to most deals. However, this category also contains covenants restricting the seller (or target) to enter into contracts outside the ordinary course, which is typically accompanied with a value restriction. This latter provision would require more negotiations, rendering individual lawyer styles influential.

2.4.5 Empirical Analysis of Observable Law Firm and Lawyer Characteristics

Upon finding that styles of law firms and lawyers map into contract design, an important remaining question is what these styles actually reflect, since fixed effects capture both observable and unobservable characteristics. To shed some light on this, we test whether observable characteristics can explain variation in contract design.

Table 2.6 Panel A reports regressions of the number of warranties and covenants on three observable law firm characteristics: (i) deal experience between 1995 and 2010; (ii) whether the law firm is in the Top 10 ranking based on deal volume; and (iii) whether the headquarters of the law firm are located in the US. Each row represents the coefficient (*t*-statistic) of a separate regression that uses a different law firm characteristic.

Consistent with Coates (2001), we find that geographic differences between law firms affect contract design, as contracts drafted by law firms with a US base contain significantly more warranties. Deal experience and ranking do not seem to affect either warranties or covenants, whereas these have been found to impact other M&A outcomes, such as takeover premiums and deal completion rates (Krishnan and Masulis (2013)).

The rest of Table 2.6 reports regressions of the number of warranties and covenants on lawyer characteristics proxied using measures of experience, education and risk aversion. To hold law firm styles constant, we report two specifications for each regression: regressions on (i) a full sample of all 28 law firms which control for law firm fixed effects (Columns 1 and 3); and (ii) a restricted sample of contracts drafted by our law firm (Columns 2 and 4).

Table 2.6 Panel B shows that variation in warranties can mostly be attributed to variation in risk aversion. Female lawyers draft contracts with 11% less warranties. Similarly, higher self-assessed risk aversion is associated with fewer warranties. Moving from 0 to 10 in terms of the risk aversion scale is associated with 30% fewer warranties. Table 2.6 Panel C shows that risk averse lawyers draft significantly fewer warranties across all categories which could be explained using partner fixed effects.[33] Moreover, the risk aversion measure captures almost all of the contribution of the explanatory power of the partner fixed effects, suggesting that this is a relevant lawyer trait. This relation between warranties and the risk aversion of the lawyer is depicted graphically in a partial scatterplot in Figure 2.2, Panel A.

Conversely, risk aversion does not seem to affect the number of covenants in acquisition contracts (Table 2.6 Panel D). Instead, covenants are mostly driven by experience and education, where more deal experience and corporate experience are associated with more covenants. Similarly, lawyers who have obtained a business degree draft contracts with more covenants. This suggests that exposure to business through work experience or education might point lawyers toward risks from agency problems; such lawyers are more inclined to limit these risks. Business education is the most relevant characteristic for explaining variation in covenants per category. Figure 2.2, Panel B depicts the impact of business education on covenants in a partial scatterplot.

Combined, these results suggest that observable *law firm* characteristics can explain only a very minor part of law firm styles, while observable *lawyer* characteristics capture a substantial component of lawyer styles.

2.5 Endogeneity Concerns and Robustness Checks

Our results provide evidence that support the *lawyer-contracting hypothesis*. Three concerns can be raised to whether our evidence truly rejects the *economic-contracting hypothesis*.

[33] We use here a 5% threshold to indicate whether the difference in explanatory power is substantial.

2.5.1 Endogenous Allocations of Law Firms and Lawyers

The first concern is that deals are allocated endogenously to law firms and lawyers based on unobservable deal or client characteristics. This would imply that observed law firm or lawyer styles actually reflect unobserved deal or client characteristics. Even though this is still consistent with the view that styles of legal advisors matter, it would suggest a different force behind this finding—namely unobserved deal or client characteristics. Several tests suggest that it is unlikely that our results are driven by such endogenous allocations.

First, if lawyer allocation were endogenous to deal characteristics, buyers and sellers would newly select law firms or lawyers for each upcoming transaction. However, anecdotal evidence from structured interviews with the lawyers of our law firm indicate this is unlikely; deals are rather allocated based on historically determined client relations. Specifically, clients usually have established relationships with law firms and ask them repeatedly for advice on transactions. This is independent of whether they are on the buyer or seller side of a transaction, and also independent of deal characteristics. This interview argumentation is supported by our data. When looking at deals with clients that performed prior transactions, we find that—in 80% of the deals—the advising law firms have been involved in at least one prior deal with these clients over the past five years.[34] Moreover, these law firms have advised these clients, on average, on seven prior deals. This suggests that historical relations are driving the choice for lawyers and that it is unlikely that clients choose new law firms for new deals based on specific deal characteristics.

Second, if law firm and lawyer styles reflect deal characteristics, we should observe systematic differences in observable deal and client characteristics across law firms and lawyers with different styles. To test this, Table 2.7 reports sample means of various deal and client characteristics for samples of contracts drafted by law firms and lawyers with high versus low warranty styles, and similarly with high versus low covenant styles. Difference-in-means tests show that deal and client characteristics are largely

[34] This is calculated using data on deal activity from Merger Market. Note that client refers in this context to the party represented by the law firm that drafted the first version of the contract. Whereas each deal always involves (at least) two clients, i.e. the buyer and seller, these statistics will only concern the 151 clients whose law firm was drafting the contract.

similar across law firms and lawyers with different styles. Table 2.7 further indicates that some differences exist across styles with respect to industry characteristics. To show that such industry differences do not drive our results, we re-estimate our previous regressions after adding industry fixed effects. The corresponding results, reported in Table 2.8 Panel A, show that our results do not change. Consequently, for deal allocation to be endogenous, they would have to be based on unobservable deal or client characteristics which are uncorrelated to any of these observable variables.

Third, to further show that unobservable deal characteristics do not drive our findings, we restrict our analysis to a sample of transactions where long-term relations between law firms and clients are very likely. As a consequence, we eliminate the deals where allocation of law firms may have been driven by unobserved deal characteristics. Table 2.8 Panel B restricts the sample to deals where the law firm that advises a client has provided advice to this client on at least one other deal during the previous five years. Similarly, Table 2.8 Panel C restricts the sample to deals where the law firms and their clients are located in the same country, making it likely that both interacted already in the past. We find that law firm and lawyer styles remain statistically significant for both of these subsamples, Similarly, Table 2.8 Panel D reports regressions where we follow Calomiris and Hitscherich (2007) and include a dummy variable, which equals one if a client switched to a new lawyer. We find that this client-switch variable is not statistically significantly different from zero, implying that client switches—even if they indicates an endogenously chosen lawyer—do not systematically affect the number of warranties or covenants.

Taken together, these robustness checks suggest that *deal* characteristics do not drive the choice for the drafting law firm or lawyer. We next address the possibility that unobserved *client* characteristics drive such a choice. To address this concern, we show that our results are robust to controlling for various client characteristics (Table 2.8 Panel E) and, more importantly, for client fixed effects (Table 2.8 Panel F). To estimate regressions with client fixed effects, we restrict the sample to deals where one of the involved parties appears at least three times in our sample, which limits the sample to 85 contracts. These contracts were drafted by 17 different law firms for 19 clients, who have been involved, on average, in five deals in our sample. Table 2.8 Panel F shows that the

law firm fixed effects remain jointly statistically significant at the 1% level, even after controlling for client fixed effects.[35]

Consequently, whereas law firms and lawyers are not randomly assigned to deals, the above results suggest that it is unlikely that our findings are driven by allocations based on unobservable deal or client characteristics.

2.5.2 Sample Selection Issues

The second concern relates to the fact that our data has been provided by one law firm only, which has been involved in all deals as advisor of either buyers or sellers. If our law firm drafts non-typical contracts or only advises on non-typical deals, then our results could be unrepresentative for a larger sample of acquisition contracts. We provide three types of analyses to show that the sample construction does not bias our results.

First, the contract design in our sample is comparable to other samples that use data on private acquisitions. Appendix A-2.5 compares the presence of various provisions in our sample with that in other samples. One can see that, for most types of provisions, our sample is similar and it, especially, resembles other studies using European data. This suggests that our law firm does not use any unconventional methods when drafting acquisition contracts.

Second, to mitigate the concern that transactions in our sample are unrepresentative for acquisitions in general, Appendix A-2.6 compares various sample characteristics with those of two comparison groups. The first group consists of other private acquisitions in which our law firm was involved in during the sample period, but which are not included in our sample. The second group consists of all private acquisitions during the sample period that have at least one of the involved parties located in The Netherlands. This latter group captures deals that our law firm could have potentially advised on and we obtain data on this from Merger Market (the Merger

[35] Due to the strong restrictions imposed on the sample size, the partner fixed effects for the covenants lose statistical significance.

Market deals).[36] The comparisons suggest that transactions in our sample are smaller than other deals advised on by our law firm, but larger than the Merger Market deals. Compared to the Merger Market deals, our sample contains, by construction, more targets, buyers, and sellers from The Netherlands. The samples are similar in terms of industry distribution. However, it appears that both buyers and sellers in our sample have been advised by more and better law firms and banks, suggesting that our sample probably contains a relatively high level of advisor sophistication.

Third, to show that our results are not driven by the style of only our law firm, we re-estimate the analysis on a sample excluding all contracts that have been drafted by our law firm, restricting the sample to 57 observations. The results in Appendix A-2.7 shows that both law firm fixed effects and the law firm style variable remain statistically significant.

2.5.3 Controlling for Acquisition Premiums and the Role of Banks

The last concern that can be raised relates to other, potentially omitted, variables. In Section 2.5.1, we show that omitted deal or client characteristics do not drive our results. However, contract terms are usually determined simultaneously, such that some provisions could act as substitutes for other provisions. For example, earn out or equity payments (i.e., conditional payments) could serve as substitutes for warranties. If some law firms draft contracts with more warranties, whereas other law firms focus rather on including conditional payments, then contract design would be affected by law firm styles, but the actual protection granted to buyers would not. Similarly, purchase price adjustments could serve as substitutes for covenants. If these provisions were fully traded-off against each other, and legal advisors merely affect the relative division between both types of provisions, then their styles would no longer be significant when controlling for those provisions. Appendix A-2.8 Panel A reports regressions which control for various other contract provisions as well as the acquisition premium, and shows that our results are robust to including these variables.

[36] All statistics in Appendix A-2.6 use Merger Market data, which typically contain less information about deals than our data. Consequently, some of the reported sample means may deviate from the means provided in Table 2.1.

Finally, one could be concerned about the involvement of investment banks. A growing body of literature stresses the importance of investment banks in the takeover process (among others: Servaes and Zenner (1996), Kale, Kini and Ryan (2003), Rau (2000), and Bao and Edmans (2011)). If there is a relation between law firms and the choice to engage an investment bank, then law firm fixed effects might pick up bank influence rather than law firm styles. This does not seem to hold in our sample, as Appendix A-2.8 Panel B shows that our results are robust to controlling for the presence of investment banks advising buyers or sellers.

2.6 Conclusions

We study the variation in contract provisions of 151 takeover contracts, focusing on the intensity of warranties and covenants to test whether contracts are purely driven by economic deal conditions (*economic-contracting hypothesis*), or whether styles or biases of legal advisors also influence contract design (*lawyer-contracting hypothesis*).

We find that the economic determinants significantly affect contract design and explain 39% of the variation in the number of warranties, and 34% of the variation in the number of covenants. Supporting *the lawyer-contracting hypothesis*, we document that the styles of law firms and lawyers impact these contractual outcomes as well, though the increase in explanatory power is relatively modest. However, the increase in explanatory power is substantially stronger when we add partner fixed effects.

Upon considering the concerns addressed by different warranty and covenant provisions, we find that the impact of legal advisors depends on the type of contract provisions. Neither law firms nor lawyers seem to influence provisions which are highly deal-specific and have a direct economic impact, such that deal customization is very valuable. On the other extreme, law firms appear most influential for provisions that address concerns which are similar across deals; the use of standardized provisions seems sufficient for such concerns. The impact of lawyers is strongest for provisions that distribute value, implying that negotiation styles of lawyers are particularly valuable.

Finally, we assess whether observable law firm and lawyer characteristics can explain these law firm and lawyer styles. We find that US based law firms draft contracts with significantly more warranties. Further, we show that more risk averse lawyers include more warranties, and that variation in covenants can be explained by lawyers' business exposure and deal experience.

Table 2.1
Acquisition Contracts: Sample Description

This table provides summary statistics of the main variables used in the analysis. The sample covers 151 M&A transactions conducted in the period between 2005 and 2010. As some information is not available for all transactions, some statistics are based on less than 151 observations. Panel A reports summary statistics of target, buyer, seller, and deal characteristics. Panel B reports information on law firm and lawyer characteristics, based on the law firm and lead lawyers who provided the first contract drafts in the deal. Detailed variable definitions are provided in Appendix A-2.1.

Panel A: Deal, Target, Buyer, and Seller Characteristics

Target	**Mean**	**Median**	**10th**	**90th**	**Std. Dev.**	**Obs.**
Transaction Value (mEUR)	222	34	2	371	795	151
Target Book Value (mEUR)	318	45	2	538	990	146
Target Market Value (mEUR)	434	80	6	864	1,290	146
Target Cash/Assets	12%	3%	0%	45%	21%	146
Asset Deal	9%					151
High R&D Industry	28%					151
High Capex Industry	25%					151
Buyer						
Buyer Book Value (mEUR)	40,000	1,410	12	45,900	139,000	150
Toehold Deal	3%					151
Buyer Private Equity	22%					151
Buyer Publicly-Listed	44%					151
Seller						
Seller Book Value (mEUR)	90,800	2,080	2	124,000	316,000	147
Main Seller	88%	100%	49%	100%	21%	151
Seller Private Equity	15%					151
Seller Family	18%					151
Seller Publicly-Listed	35%					151
Deal Characteristics						
Deal After 2008	37%					151
Cross-Country Deal	44%					151
Cross-Industry Deal	50%					151
Controlled Auction	23%					151
Negotiation Time (days)	170	141	47	334	134	147
Closing Time (days)	46	24	0	123	66	151
First Draft by Buyer	44%					151
Competition Approval	45%					151

Panel B: Drafting Law Firm and Drafting Lawyer Characteristics

	Mean	**Median**	**10th**	**90th**	**Std. Dev.**	**Obs.**
Law Firm Characteristics						
Deal Experience	744	458	458	1836	711	151
Top 10 Ranking	15%				36%	151
US Location	3%				18%	151
Lawyer Characteristics						
Deal Experience	37	33	5	79	26	150
Corporate Experience	27%				45%	144
Business Education	23%				43%	145
US Education	29%				45%	147
Female	9%				28%	151
Risk Aversion	3.1	2.5	2.0	6.5	1.8	68

Table 2.2
Acquisition Contract Provisions: Descriptive Statistics

This tables reports summary statics of the warranty and covenant provisions in the contracts. We count the number of warranties and covenants to reflect the intensity of these provisions. Summary statistics for covenants are reported for contracts where signing and closing dates were not the same. Panel A provides statistics on the number of warranties or covenants. We report both the absolute number and the absolute number divided by a benchmark contract ("Model Contract"). This model contract is a standardized contract provided in Miller (2008). We further report the number of pages devoted to warranties and covenants. Panel B provides summary statistics on the number of warranties and covenants by category. The categories reflect the underlying concerns addressed with the provisions (as categorized in Miller (2008)). We report again both the absolute number and the absolute number divided by the number in the benchmark contract in Miller (2008). Examples of warranties and covenants are given in Appendix A-2.2.

Panel A: Warranties and Covenants

	Mean	Median	Min	Max	Std. Dev.	Obs.	Model Contract
Warranties	97.5	99.5	4.0	247.0	49.2	150	271
Warranties Relative to Model	0.4	0.4	0.0	0.9	0.2	150	1
Pages Warranties	8.9	8.3	0.5	35.0	5.0	150	28
Covenants	19.9	21.0	0.0	50.0	11.1	102	35
Covenants Relative to Model	0.6	0.6	0.0	1.4	0.3	102	1
Pages Covenants	2.2	2.0	0.0	8.0	1.4	102	8

Panel B: Warranties and Covenant by Categories

	Warranties			Model	Warranties/Model Contract		
Warranty Category	Mean	Median	Max	Contract	Mean	Median	Max
Corporate Records	17.4	18.0	37.0	41	0.4	0.4	0.9
Employees	12.3	12.0	49.0	40	0.3	0.3	1.2
Financial Accounts	24.1	22.0	62.0	64	0.4	0.3	1.0
Assets	8.5	7.0	49.0	34	0.3	0.2	1.4
Contracts	12.6	12.0	38.0	25	0.5	0.5	1.5
Insurance	3.0	3.0	11.0	7	0.4	0.4	1.6
Intellectual Property	8.2	5.0	40.0	36	0.2	0.1	1.1
Legal	9.8	10.0	32.0	24	0.4	0.4	1.3
	Covenants			**Model**	**Covenants/Model Contract**		
Covenant Category	**Mean**	**Median**	**Max**	**Contract**	**Mean**	**Median**	**Max**
Corporate Documents	1.3	1.0	7.0	2	0.7	0.5	3.5
Employees	2.2	2.0	7.0	4	0.5	0.5	1.8
Dividend Payments	3.6	3.0	13.0	7	0.5	0.4	1.9
Debt	2.0	2.0	6.0	3	0.7	0.7	2.0
Business Conduct	7.4	7.0	24.0	15	0.5	0.5	1.6
Acquisitions	1.5	1.0	5.0	1	1.5	1.0	5.0
Divestments	1.5	2.0	4.0	2	0.7	1.0	2.0
Litigation	0.5	0.0	3.0	1	0.5	0.0	3.0

Table 2.3
Economic Determinants of Warranties and Covenants

This table shows OLS regressions to look at the determinants of the number of warranties (Column 1) and covenants (Column 2). The dependent variable is the number of these provisions relative to those of the model contract. The sample covers 151 M&A transactions conducted in the period between 2005 and 2010, but the regressions are on fewer observations because of missing data for some variables. All regressions report the effect of economic variables. Column 2 restricts the sample to deals where signing and closing dates were not the same. We report *t*-statistics in parentheses, calculated using robust standard errors. Detailed variable definitions are provided in Appendix A-2.1. *** indicates significance at 1%, ** at 5% and * at 10%.

	Dependent Variable:	
	Warranties/Model Contract	**Covenants/Model Contract**
	(1)	(2)
Cross-Country Deal	0.08***	-0.00
	(2.86)	(-0.01)
Cross-Industry Deal	-0.02	-0.02
	(-0.60)	(-0.32)
Toehold Deal	-0.40***	-0.44***
	(-8.34)	(-3.62)
Transaction Value (log)	0.01*	0.02***
	(1.71)	(2.72)
Asset Deal	-0.08**	-0.32***
	(-2.42)	(-4.81)
High R&D Industry	-0.00	
	(-0.07)	
Buyer Private Equity	-0.00	
	(-0.05)	
Seller Private Equity	-0.08*	
	(-1.94)	
Seller Family	0.00	
	(0.01)	
Main Seller Percent	-0.26***	
	(-3.49)	
Target Cash/Assets		0.18
		(1.40)
High Capex Industry		-0.11
		(-1.50)
Interim Period (log)		0.07***
		(3.52)
Competition Approval		0.03**
		(2.25)
Relative Size	0.01	0.02
	(0.84)	(1.16)
First Draft by Buyer	0.09**	0.04
	(2.37)	(0.54)
Deal After 2008	0.08***	0.05
	(3.35)	(0.93)
Controlled Auction	0.04	0.15**
	(1.51)	(2.15)
Obs.	145	96
R^2	45%	43%
Adj. R^2	39%	34%

Table 2.4
Impact of Legal Advisors on Warranties and Covenants

This table shows OLS regressions with the number of warranties and covenants relative to the model contract as dependent variables. The sample covers 151 deals conducted in the period between 2005 and 2010, but regressions are on fewer observations because of missing data or sample restrictions. In addition to the controls from Table 2.3, the regressions in Panel A control for: Law Firm Fixed Effects (Columns 1 and 3), Law Firm High Warranty Style (Column 2), and Law Firm High Covenant Style (Column 4). Similarly, in Panel B, in addition to the controls from Table 2.3, controls are added for: Partner Fixed Effects (Columns 1 and 3), Partner High Warranty Style (Column 2), and Partner High Covenant Style (Column 4). For the law firm and partner fixed effects, we report the *F*-statistic and *p*-value of their joint significance. In all regressions with covenants relative to the model contract as dependent variable, the sample is restricted to deals where signing and closing dates were not the same. The sample in Panel B is additionally restricted to deals where the first contract is drafted by the law firm that provided the data. Both Panels report the difference in adjusted R^2 relative to regressions on the same sample, which controls for economic determinants only. In parentheses are *t*-statistics, calculated using robust standard errors. . *** indicates significance at 1%, ** at 5% and * at 10%.

Table 2.4 (continued)

Panel A: Impact of Law Firm Styles on Warranties and Covenants

	Dependent Variable:			
	Warranties/Model Contract		Covenants/Model Contract	
	(1)	(2)	(3)	(4)
Law Firm FE: *F*-test (*p*-value)	53.40		332.93	
	(0.000)		(0.000)	
Law Firm High Warranty Style		0.15***		
		(4.19)		
Law Firm High Covenant Style				0.28***
				(3.96)
Cross-Country Deal	0.08*	0.08***	0.05	0.01
	(1.85)	(2.81)	(0.57)	(0.22)
Cross-Industry Deal	-0.03	-0.02	-0.01	-0.00
	(-1.07)	(-0.85)	(-0.16)	(-0.04)
Toehold Deal	-0.41***	-0.41***	-0.74***	-0.67***
	(-9.47)	(-13.22)	(-4.90)	(-6.07)
Transaction Value (log)	0.01	0.00	0.02*	0.02**
	(1.13)	(1.06)	(1.73)	(2.02)
Asset Deal	-0.08**	-0.08**	-0.24**	-0.24***
	(-2.00)	(-2.56)	(-2.50)	(-3.64)
High R&D Industry	-0.01	-0.01		
	(-0.37)	(-0.40)		
Buyer Private Equity	0.02	0.00		
	(0.43)	(0.12)		
Seller Private Equity	-0.08	-0.08**		
	(-1.46)	(-2.13)		
Seller Family	0.02	0.01		
	(0.37)	(0.15)		
Main Seller Percent	-0.21***	-0.26***		
	(-2.92)	(-3.85)		
Target Cash/Assets			0.04	0.18
			(0.30)	(1.63)
High Capex Industry			-0.14*	-0.12**
			(-1.78)	(-2.04)
Interim Period (log)			0.07**	0.08***
			(2.31)	(3.46)
Competition Approval			0.04**	0.04***
			(2.31)	(2.78)
Relative Size	0.01	0.01	0.01	0.01
	(0.76)	(1.16)	(0.51)	(1.11)
First Draft by Buyer	0.10**	0.09**	0.20	0.11
	(2.20)	(2.44)	(1.66)	(1.58)
Deal After 2008	0.09***	0.07***	-0.01	-0.05
	(2.82)	(3.25)	(-0.13)	(-0.78)
Controlled Auction	0.07*	0.05**	0.17*	0.15**
	(1.81)	(2.04)	(1.89)	(2.46)
Obs.	145	145	96	96
Adj. R^2	41%	45%	39%	44%
Diff. in Adj. R^2	3%	7%	6%	11%

Table 2.4 (continued)

Panel B: Impact of Lawyer Styles on Warranties and Covenants

	Dependent Variable:			
	Warranties/Model Contract		Covenants/Model Contract	
	(1)	(2)	(3)	(4)
Partner FE: *F*-test (*p*-value)	6.31		17.11	
	(0.000)		(0.000)	
Partner High Warranty Style		0.10***		
		(4.06)		
Partner High Covenant Style				0.30***
				(4.60)
Cross-Country Deal	0.06	0.07	0.08	0.04
	(1.19)	(1.47)	(0.56)	(0.44)
Cross-Industry Deal	-0.01	-0.01	-0.13	-0.11*
	(-0.33)	(-0.34)	(-1.69)	(-1.72)
Toehold Deal	-0.48***	-0.48***		
	(-9.13)	(-9.57)		
Transaction Value (log)	0.00	0.00	0.00	0.00
	(0.93)	(0.77)	(0.05)	(0.54)
Asset Deal	-0.11**	-0.08*	-0.34	-0.29***
	(-2.12)	(-1.98)	(-1.61)	(-3.56)
High R&D Industry	0.01	-0.00		
	(0.22)	(-0.06)		
Buyer Private Equity	0.05	0.08**		
	(0.93)	(2.11)		
Seller Private Equity	-0.06	-0.06		
	(-0.98)	(-1.17)		
Seller Family	0.03	0.05		
	(0.72)	(1.17)		
Main Seller Percent	-0.11	-0.11*		
	(-1.35)	(-1.90)		
Target Cash/Assets			0.18	-0.05
			(0.74)	(-0.24)
High Capex Industry			0.00	-0.05
			(0.01)	(-0.63)
Interim Period (log)			0.09**	0.08***
			(2.56)	(3.33)
Competition Approval			0.03	0.03***
			(1.42)	(3.46)
Relative Size	0.00	0.01	-0.01	0.00
	(0.52)	(1.23)	(-0.50)	(0.20)
First Draft by Buyer	0.12*	0.09**	0.18	0.15
	(1.85)	(2.10)	(1.02)	(1.21)
Deal After 2008	0.05	0.07**	-0.00	0.01
	(1.26)	(2.32)	(-0.03)	(0.12)
Controlled Auction	0.05	0.06	0.10	0.16*
	(1.05)	(1.63)	(0.63)	(2.01)
Obs.	89	89	51	51
Adj. R^2	48%	51%	56%	59%
Diff. in Adj. R^2	7%	9%	19%	22%

Table 2.5
Warranties and Covenants by Category: Impact of Law Firm and Partner Fixed Effects

This table shows OLS regressions to explain warranties (Panel A) and covenants (Panel B) per category. The dependent variable is the number of warranties (covenants) per category relative to that in the same category of the model contract. Each row represents a separate regression with a different warranty or covenant category as dependent variable (listed vertically). The sample covers 151 observations, but regressions are on fewer observations because of missing data. All regressions control for the variables as in Table 2.3. In addition, both panels include Law Firm Fixed Effects (left half) and for Partner Fixed Effects (right half), respectively. The regressions on Partner Fixed Effects are restricted to deals for which the first contract is drafted by the law firm that provided the data. The sample in Panel C is further restricted to deals where signing and closing dates were not the same. For law firm and partner fixed effects, we report the *F*-statistic and *p*-value of their joint significance. We also report the difference in adjusted R^2 of the regressions relative to regressions on the same sample that only control for economic determinants. All regressions use robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Warranties per Category: Impact of Law Firm and Partner Fixed Effects

	Law Firm Fixed Effects					**Partner Fixed Effects**				
Dependent Variable: Warranties on…	Law Firm FE: *F*-test	(*p*-value)	Obs.	Adj. R^2	Diff. in Adj. R^2	Partner FE: *F*-test	(*p*-value)	Obs.	Adj. R^2	Diff.in Adj. R^2
Corporate Records	26.75	(0.000)	145	39%	3%	3.89	(0.000)	89	41%	0%
Employees	51.07	(0.000)	145	24%	6%	6.30	(0.000)	89	29%	11%
Financial Accounts	208.82	(0.000)	145	50%	2%	5.97	(0.000)	89	61%	1%
Assets	2,458.08	(0.000)	145	5%	-6%	2.40	(0.007)	89	8%	3%
Contracts	114.90	(0.000)	145	33%	3%	6.02	(0.000)	89	30%	10%
Insurance	34.97	(0.000)	145	13%	-3%	11.17	(0.000)	89	29%	13%
Intellectual Property	171.75	(0.000)	145	19%	-3%	16.64	(0.000)	89	29%	12%
Legal	386.80	(0.000)	145	27%	10%	5.05	(0.000)	89	41%	22%
Average				**26%**	**2%**				**34%**	**9%**

Panel B: Covenants per Category: Impact of Law Firm and Partner Fixed Effects

	Law Firm Fixed Effects					**Partner Fixed Effects**				
Dependent Variable: Covenants on…	Law Firm FE: *F*-test		Obs.	Adj. R^2	Diff. in Adj. R^2	Partner FE: *F*-test		Obs.	Adj. R^2	Diff. in Adj. R^2
Corporate Records	25.74	(0.000)	96	23%	3%	4.52	(0.001)	51	16%	-14%
Employees	105.60	(0.000)	96	26%	17%	19.26	(0.000)	51	29%	20%
Dividends	26.84	(0.000)	96	28%	-5%	4.09	(0.001)	51	40%	0%
Debt	27.13	(0.000)	96	1%	-13%	8.28	(0.000)	51	15%	10%
Business Conduct	341.58	(0.000)	96	34%	12%	9.99	(0.000)	51	37%	6%
Acquisitions	2,297.05	(0.000)	96	10%	-3%	7.52	(0.000)	51	18%	14%
Divestments	33.18	(0.000)	96	37%	11%	9.74	(0.000)	51	50%	9%
Litigation	7.55	(0.000)	96	6%	-9%	7.95	(0.000)	51	36%	26%
Average				**21%**	**2%**				**30%**	**9%**

Table 2.6
Warranties and Covenants: Impact of Law Firm and Lawyer Characteristics

This table shows OLS regressions to explain warranties and covenants with observable law firm and lawyer characteristics. The sample covers 151 observations, but regressions are on fewer observations because of missing data for some variables and sample restrictions. Each row represents a separate regression on a different measure of law firm or lawyer characteristics. All regressions control for the variables as in Table 2.3. In Panel A, we additionally control for the law firm characteristics: the natural logarithm of Deal Experience, Top 10 Ranking, and US Location. In Panel B, we rather control for the following partner characteristics: the natural logarithm of Deal Experience, Corporate Experience, Business Education, US Education, Female, and Risk Aversion. For each of these partner characteristics, we report two types of regressions: (i) on a sample of all law firms controlling for law firm fixed effects (Columns 1 and 3), and (ii) on a sample restricted to contracts drafted by our law firm (Columns 2 and 4). As the risk aversion measure is only available for lawyers at our law firm, regressions are only on a sample restricted to our law firm. In Panel C, we regress the warranties per category on the following variables: Law Firm US Location, Partner Female and Partner Risk Aversion, in three sets of separate regressions. The regressions which control for Partner Female control for Law Firm Fixed Effects. The regressions which include the Partner Risk Aversion are on a sample limited to contracts drafted by our law firm. In Panel D, we regress the covenants per category on the following partner characteristics: the natural logarithm of Deal Experience, Corporate Experience, and Business Education in three separate sets of regressions. In all regressions in Panel D, we also control for Law Firm Fixed Effects. We also report the difference in adjusted R^2 of the reported regressions relative to ones on the same sample which only exclude that law firm or lawyer characteristic. All regressions use robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Warranties and Covenant: Impact of Law Firm Characteristics

Dependent Variable:	**Warranties/Model Contract**	**Covenants/Model Contract**
Law Firm Characteristic	(1)	(2)
Deal Experience (log)	-0.00	-0.00
	(-0.38)	(-0.03)
Obs.	145	96
Adj. R^2	38%	33%
Difference in Adj. R^2	0%	-1%
Top 10 Ranking	0.02	-0.05
	(0.48)	(-0.70)
Obs.	145	96
Adj. R^2	38%	33%
Difference in Adj. R^2	0%	0%
US Location	0.24***	0.28
	(2.77)	(0.94)
Obs.	145	96
Adj. R^2	44%	35%
Difference in Adj. R^2	5%	1%

Table 2.6 (continued)

Panel B: Impact of Partner Characteristics on Warranties and Covenants

	Dependent Variable:			
	Warranties/Model Contract		Covenants/Model Contract	
Partner Characteristics	(1)	(2)	(3)	(4)
Experience				
Deal Experience (log)	0.00	0.01	0.08**	0.12***
	(0.22)	(0.69)	(2.27)	(3.16)
Obs.	144	90	96	51
Adj. R^2	41%	41%	43%	45%
Difference in Adj. R^2	0%	-1%	4%	9%
Corporate Experience	-0.01	-0.01	0.17**	0.21**
	(-0.30)	(-0.22)	(2.21)	(2.58)
Obs.	139	86	90	47
Adj. R^2	43%	41%	43%	47%
Difference in Adj. R^2	-1%	-1%	4%	10%
Education				
Business Education	-0.01	0.02	0.26***	0.29***
	(-0.42)	(0.63)	(3.17)	(3.64)
Obs.	140	90	92	51
Adj. R^2	41%	41%	48%	50%
Difference in Adj. R^2	-1%	-1%	9%	13%
US Education	0.03	0.04	-0.10	-0.18*
	(0.84)	(1.08)	(-1.22)	(-1.91)
Obs.	141	86	92	47
Adj. R^2	43%	42%	39%	46%
Difference in Adj. R^2	0%	0%	1%	9%
Risk Aversion				
Female	-0.11**	-0.14*	-0.15	-0.03
	(-2.23)	(-1.97)	(-1.02)	(-0.20)
Obs.	145	90	96	51
Adj. R^2	42%	43%	39%	35%
Difference in Adj. R^2	1%	2%	0%	-2%
Risk Aversion	n.a.	-0.03***	n.a.	-0.04
		(-3.40)		(-0.93)
Obs.		66		36
Adj. R^2		48%		32%
Difference in Adj. R^2		9%		-5%

Table 2.6 (continued)

Panel C: Impact of Law Firm and Partner Characteristics on Warranties per Category

	Dependent Variable: Warranties/Model Contract							
	Corporate Records	Employee	Financial Accounts	Assets	Contracts	Insurance	Intellect. Property	Legal
Law Firm:	(1)	(2)	(3)	(4)	(5)	(5)	(6)	(7)
US Location	0.33***	0.42***	0.15	0.11	0.28**	0.47***	0.17	0.23**
	(9.91)	(2.97)	(1.41)	(1.26)	(2.08)	(2.66)	(1.45)	(2.20)
Obs.	145	145	145	145	145	145	145	145
Adj. R^2	48%	29%	49%	11%	33%	21%	23%	19%
Diff. in Adj. R^2	12%	12%	1%	0%	2%	5%	1%	2%
Partner:								
Female	-0.00	-0.21***	-0.13***	0.03	-0.10	-0.08	-0.23**	-0.12
	(-0.11)	(-3.29)	(-3.21)	(0.24)	(-1.05)	(-0.43)	(-2.53)	(-1.54)
Law Firm FE	YES	YES	YES	YES	YES	YES	YES	YES
Obs.	145	145	145	145	145	145	145	145
Adj. R^2	38%	28%	51%	4%	33%	12%	22%	27%
Diff. in Adj. R^2	-1%	4%	1%	-1%	0%	-1%	3%	1%
Risk Aversion	-0.01	-0.04***	-0.02	-0.03	-0.06***	-0.06**	-0.04**	-0.06***
	(-1.11)	(-3.68)	(-1.50)	(-1.55)	(-3.16)	(-2.32)	(-2.62)	(-3.79)
Obs.	66	66	66	66	66	66	66	66
Adj. R^2	39%	38%	58%	6%	22%	17%	27%	31%
Diff. in Adj. R^2	0%	16%	1%	2%	10%	7%	5%	18%

Panel D: Impact of Partner Characteristics on Covenants per Category

	Dependent Variable: Covenants/Model Contract							
	Corporate Records	Employee	Dividends	Debt	Business Conduct	Acquis.	Divest.	Litigation
Partner:	(1)	(2)	(3)	(4)	(5)	(5)	(6)	(7)
Deal Experience	0.13	0.09*	0.13***	0.12	0.03	0.23*	0.09	0.05
(log)	(1.58)	(1.68)	(3.00)	(1.39)	(0.71)	(1.92)	(1.62)	(0.44)
Law Firm FE	YES	YES	YES	YES	YES	YES	YES	YES
Obs.	96	96	96	96	96	96	96	96
Adj. R^2	20%	24%	33%	3%	33%	14%	35%	7%
Diff. in Adj. R^2	-2%	-2%	5%	2%	-1%	4%	-2%	1%
Corporate	0.40	0.15	0.25*	0.18	0.11	0.39	0.09	0.00
Experience	(1.47)	(1.09)	(2.00)	(0.86)	(1.49)	(1.00)	(0.60)	(0.01)
Law Firm FE	YES	YES	YES	YES	YES	YES	YES	YES
Obs.	90	90	90	90	90	90	90	90
Adj. R^2	26%	26%	30%	1%	35%	10%	36%	5%
Diff. in Adj. R^2	5%	1%	4%	0%	1%	1%	-1%	-2%
Business	0.40	0.14	0.29**	0.51**	0.16*	0.94***	0.17	0.39*
Education	(1.24)	(0.98)	(2.22)	(2.62)	(1.82)	(2.74)	(0.97)	(1.75)
Law Firm FE	YES	YES	YES	YES	YES	YES	YES	YES
Obs.	92	92	92	92	92	92	92	92
Adj. R^2	27%	24%	33%	12%	38%	17%	41%	10%
Diff. in Adj. R^2	4%	0%	5%	10%	3%	9%	0%	3%

Table 2.7
Comparison of Deal Characteristics across Law Firm and Lawyer Styles

This table provides means of various client, target and deal characteristics across different cuts of the sample. The left half splits the sample according to whether the law firm warranty style is high or low and whether the law firm covenant style is high or low. In the right half of the table, the sample is restricted to deals for which the first contract is drafted by the law firm that provided the data. We then split the sample according to whether the partner warranty style is high or low and whether the partner covenant style is high or low. We report difference-in-means tests that compare the high and low style groups. *** indicates significance at 1%, ** at 5% and * at 10%.

		Law Firm Style						Partner Style					
		Warranty Style			Covenant Style			Warranty Style			Covenant Style		
	Sample	High	Low	Diff.	High	Low	Diff.	High	Low	Diff.	High	Low	Diff.
Client Characteristics	Mean	Mean	Mean		Mean	Mean		Mean	Mean		Mean	Mean	
Client Asset Size (bnEUR)	80.0	77.5	80.3	-2.8	140.0	103.0	37.0	106.0	41.0	64.8*	121.0	97.0	24
Client Deal Experience	14.2	7.8	15	-7.3**	21.3	14.3	7.0**	11.8	13.8	-2	15.4	12.1	3.3
Client Deals with Lawyer	4.9	2.9	5.1	-2.2**	4.9	4.8	0.1	4.3	5.8	-1.5*	5.2	4.3	0.9
Client Lawyer Switch	17%	25%	16%	9%	18%	18%	0%	23%	9%	13%**	12%	23%	-11%
Target Characteristics													
Target Book Value	318	538	293	245	376	470	-94	427	107	320*	202	532	-330
Target Cash / Assets	12%	20%	12%	8%*	11%	9%	2%	11%	10%	1%	6%	7%	-1%
Asset Deal	9%	6%	9%	-3%	0%	13%	-13%**	13%	11%	1%	12%	17%	-5%
Deal Characteristics													
Deal After 2008	37%	44%	36%	7%	68%	25%	43%***	35%	30%	5%	28%	20%	8%
Cross-Country Deal	44%	56%	43%	13%	50%	50%	0%	38%	43%	-6%	52%	43%	9%
Cross-Industry Deal	50%	56%	49%	7%	59%	54%	5%	50%	49%	1%	64%	50%	14%
Controlled Auction	23%	19%	24%	-5%	36%	29%	8%	10%	25%	-15%**	32%	23%	9%
Competition Approval	45%	50%	44%	6%	82%	61%	21%**	40%	28%	12%	68%	43%	25%**
Target Industry													
Wholesale & Retail	15%	13%	15%	-2%	23%	18%	5%	8%	17%	-9%*	20%	13%	7%
Business Equipment	13%	6%	13%	-7%	9%	8%	2%	15%	15%	0%	8%	10%	-2%
Manufacturing	9%	25%	7%	18%**	9%	10%	-1%	5%	8%	-3%	12%	7%	5%
Money & Finance	11%	0%	12%	-12%*	5%	16%	-12%*	20%	8%	12%**	24%	13%	11%
Chemicals	6%	0%	7%	-7%	0%	6%	-6%	13%	2%	11%**	0%	10%	-10%*
Consumer Non-Durables	6%	0%	7%	-7%	5%	8%	-3%	10%	4%	6%	8%	10%	-2%
Other	42%	56%	40%	16%	50%	35%	15%	30%	47%	-17%**	28%	37%	-9%

Table 2.8
Robustness Checks: Allocation of Deals to Law Firms and Partners

This table shows OLS regressions of the number of warranties and covenants. The regressions control for the same variables as in Table 2.3. Panel A controls for industry fixed effects. Panel B restricts the sample to deals where the law firm that drafted the contract had advised this client on at least one other deal in the last five years. This limits the sample to 103 observations. Panel C restricts the sample to deals where the law firm and the client are from the same country (119 observations). Panel D controls for a dummy which indicates whether a client switches to a new law firm with which she did not have a prior M&A deal relationship over the past five years. Panel E controls for Client Book Value, Client Deal Experience, and Client English Legal Origin (LO). "Client" refers to the party which is represented by the law firm that provided the first draft. Panel F controls for client fixed effects. We restricted the sample to 86 deals for which one of the parties (i.e., a buyer or a seller) has appeared at least three times in the sample. There are 18 different parties that occur at least three times as a client. In this panel, "Client" refers to the contracting party which appears more than three times in the sample. This does not necessarily reflect the party represented by the drafting law firm. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: Controlling for Industry Fixed Effects

	Warranties/Model Contract				**Covenants/Model Contract**			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	53.99				670.05			
	(0.000)				(0.000)			
Partner FE: F-test			5.78				3.759	
			(0.000)				(0.004)	
High Warranty Style		0.16***		0.10***				
		(4.14)		(3.63)				
High Covenant Style						0.27***		0.28***
						(3.50)		(3.86)
Industry FE: *F*-test	1.20	1.95	6.05	3.05	1.30	0.54	2.34	1.30
	(0.306)	(0.058)	(0.000)	(0.008)	(0.265)	(0.825)	(0.084)	(0.287)
Obs.	145	145	89	89	96	96	51	51
Adj. R^2	40%	44%	52%	50%	35%	40%	55%	61%
Diff. in Adj. R^2	3%	7%	11%	9%	5%	10%	16%	22%

Panel B: Sample Restricted to Established Relations

	Warranties/Model Contract				**Covenants/Model Contract**			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	11.89				11.20			
	(0.000)				(0.000)			
Partner FE: F-test			2.63				5.80	
			(0.011)				(0.001)	
High Warranty Style		0.10***		0.11***				
		(2.83)		(3.21)				
High Covenant Style						0.24***		0.33***
						(3.21)		(5.01)
Obs.	100	100	65	65	70	70	39	39
Adj. R^2	34%	42%	46%	50%	42%	42%	47%	68%
Diff. in Adj. R^2	-6%	2%	6%	10%	7%	7%	7%	28%

Table 2.8 (continued)

Panel C: Sample Restricted to Deals where Law Firm and Client are from Same Country

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	102.50				2.85			
	(0.000)				(0.006)			
Partner FE: F-test			6.38				10.58	
			(0.000)				(0.000)	
High Warranty Style		0.09**		0.11***				
		(2.12)		(3.55)				
High Covenant Style						0.20***		0.35***
						(2.79)		(5.20)
Obs.	114	114	77	77	75	75	46	46
Adj. R^2	30%	37%	47%	48%	34%	42%	58%	64%
Diff. in Adj. R^2	-5%	1%	10%	11%	-4%	4%	24%	30%

Panel D: Controlling for Client-Lawyer Switches

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	1,514.76				707.87			
	(0.000)				(0.000)			
Partner FE: F-test			5.98				10.81	
			(0.000)				(0.000)	
High Warranty Style		0.15***		0.11***				
		(4.33)		(4.22)				
High Covenant Style						0.28***		0.29***
						(4.06)		(4.51)
Client-Lawyer	0.03	0.05	-0.03	-0.05	-0.04	0.04	-0.03	-0.05
Switch	(0.81)	(1.39)	(-0.54)	(-1.18)	(-0.54)	(0.70)	(-0.30)	(-0.56)
Obs.	145	145	89	89	96	96	51	51
Adj. R^2	41%	46%	47%	51%	38%	44%	54%	58%
Diff. in Adj. R^2	1%	6%	7%	11%	5%	10%	17%	21%

Table 2.8 (continued)

Panel E: Controlling for Client Characteristics

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	469.06				272.81			
	(0.000)				(0.000)			
Partner FE: F-test			6.85				12.07	
			(0.000)				(0.000)	
High Warranty Style		0.16***		0.11***				
		(4.39)		(3.74)				
High Covenant Style						0.26***		0.31***
						(3.52)		(4.57)
Client Book Value	0.01*	0.01	0.00	0.00	-0.01	-0.00	-0.03	-0.02
	(1.71)	(1.61)	(0.31)	(0.06)	(-0.57)	(-0.17)	(-0.91)	(-0.98)
Client Deal Experience	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00*
	(1.08)	(1.30)	(0.35)	(1.60)	(0.99)	(1.11)	(0.53)	(1.91)
Client English LO	0.11***	0.10***	0.07	0.05	0.11	0.05	0.13	0.23**
	(2.73)	(3.03)	(0.82)	(0.87)	(1.08)	(0.58)	(0.76)	(2.61)
Obs.	145	145	89	89	96	96	51	51
Adj. R^2	46%	50%	46%	51%	38%	43%	57%	62%
Diff. in Adj. R^2	3%	7%	5%	9%	4%	8%	21%	26%

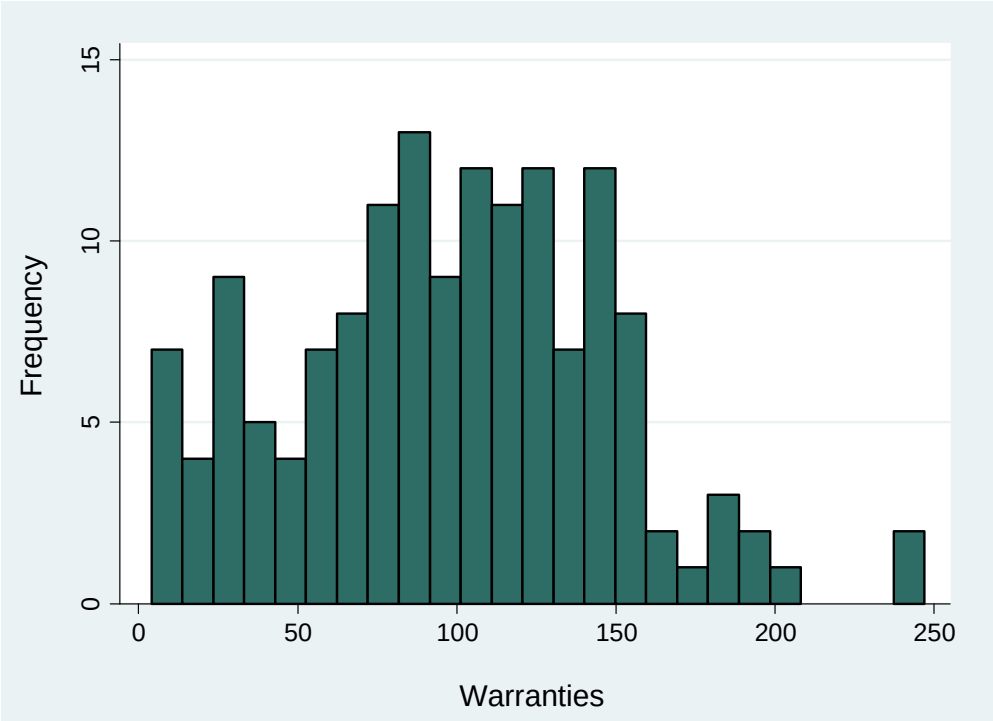
Panel F: Controlling for Client Fixed Effects

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	4.17				5.29			
	(0.000)				(0.002)			
Partner FE: F-test			2.51				8.14	
			(0.038)				(0.114)	
High Warranty Style		0.05		0.02				
		(0.85)		(0.37)				
High Covenant Style						0.14		0.33
						(0.94)		(1.20)
Client FE: *F*-test	1.35	0.79	4.14	3.23	2.85	2.40	2.29	7.12
	(0.216)	(0.695)	(0.003)	(0.005)	(0.028)	(0.030)	(0.332)	(0.008)
Obs.	84	84	56	56	52	52	31	31
Adj. R^2	26%	32%	45%	41%	38%	45%	34%	72%
Diff. in Adj. R^2	-7%	-1%	2%	-2%	-8%	-1%	-29%	10%

Figure 2.1
Distribution of Warranty and Covenant Provisions

Panel A shows a histogram of the distribution of the number of warranties in the sample. The sample covers 151 M&A transactions conducted in the period between 2005 and 2010. Panel B shows a histogram of the distribution of the Covenants in the sample. The sample in Panel B is restricted to deals where signing and closing dates were not the same.

Panel A: Histogram of the Distribution of Warranties



Panel B: Histogram of the Distribution of Covenants

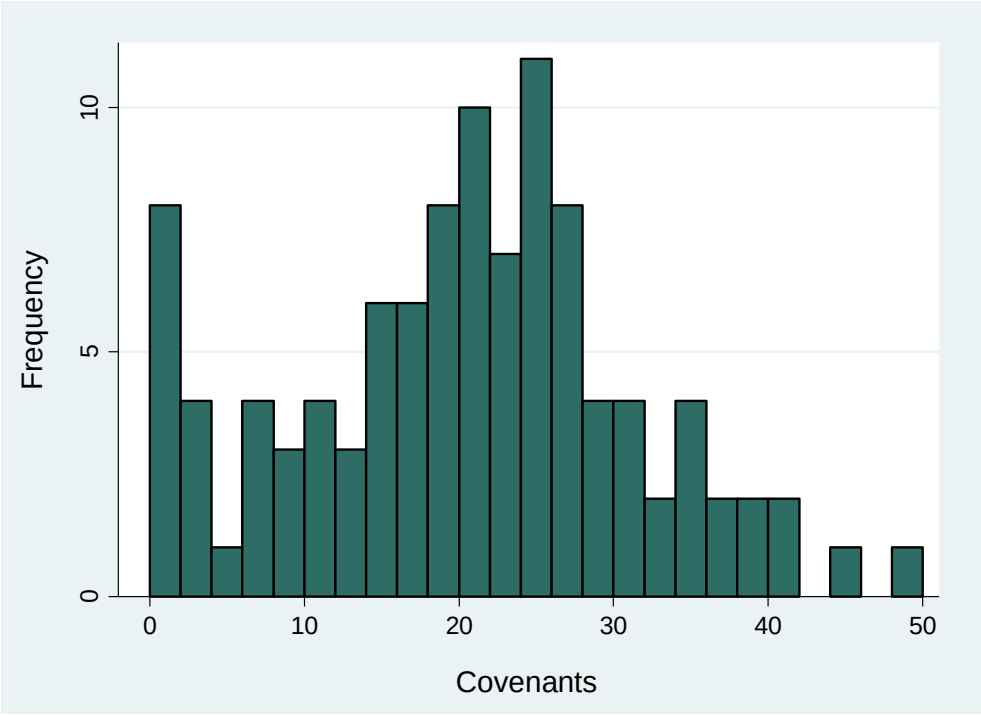
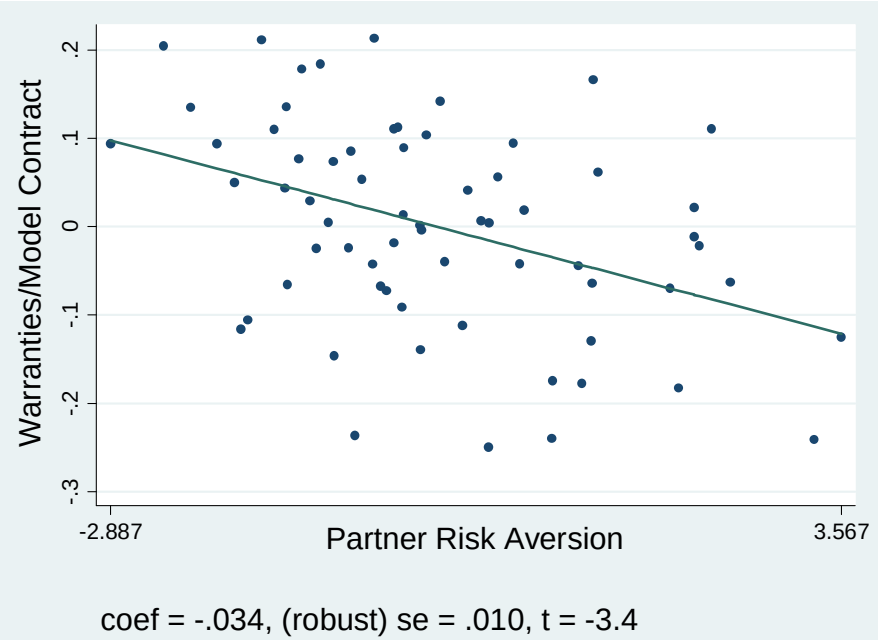


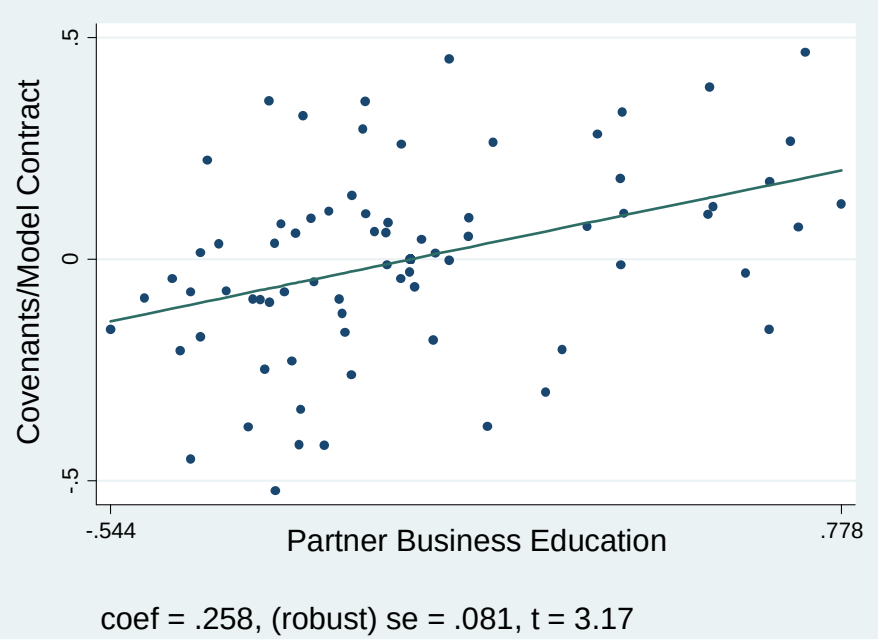
Figure 2.2
Partial Scatterplots: Impact of Partner Characteristics on Warranties and Covenants

Panel A shows a partial scatterplot derived from a regression that explains Warranties/Model Contract with partner risk aversion, controlling for the economic determinants, reported in Table 2.4, Panel B, Colum 2. The sample is restricted to contracts drafted by our law firm. Panel B shows a partial scatterplot derived from a regression that explains Covenants/Model Contract with partner business education, controlling for economic determinants as well as Law Firm Fixed Effects The sample in Panel B is restricted to deals where signing and closing dates were not the same.

Panel A: Partial Scatterplot Explaining Warranties/Model Contract with Partner Risk Aversion



Panel B: Partial Scatterplot Explaining Covenants/Model Contract with Partner Business Education



Appendix A-2.1
Definition of Variables

Variable	Description
Target Characteristics	
Transaction Value (mEUR)	Total amount of payments by the buyer to the seller. This is equal to the market value of equity of the target unless the buyer purchases less than 100% of the equity. (Source: Acquisition contracts).
Target Book Value (mEUR)	Book value of the assets of the targets. (Source: Acquisition contracts, buyer or seller financial accounts, Amadeus, trade register).
Target Market Value (mEUR)	Market value of the equity of the target (indicated by price paid for the equivalent of 100% of equity) plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Acquisition contracts, buyer or seller financial accounts, Amadeus, trade register).
Target Cash/Assets	Value of cash holdings of the target divided by the book value of the target. (Source: Amadeus, Buyer or seller financial accounts, contract, or trade registers).
Asset Deal	Dummy variable which takes the value 1 if the transaction is an asset deal (i.e., the target is a list of assets and liabilities which will transfer to the buyer), and 0 if it is a share deal or a combination of a share and an asset deal. (Source: Acquisition contracts).
High R&D Industry	Dummy variable which takes the value 1 if the target is active in a high R&D industry. High R&D industries are: Business Services, Electronic Equipment, and Pharmaceutical Products. An industry is considered a high R&D industry if the industry median level of R&D expenditures to assets is in the top 5 across Fama-French 48 industries. (Source: Compustat, Amadeus).
High Capex Industry	Dummy variable which takes the value 1 if the target is active in a high capex industry. High capex industries are: Petroleum and Natural Gas, Consumer Goods, Non-Metallic and Industries, Real Estate, Communication, Retail, Transportation, Utilities, Food Products, Personal Services, and Other. An industry is considered a high capex industry if the target's industry median level of capital expenditures to assets is in the top 25% of our distribution. (Source: Compustat, Amadeus).
Buyer Characteristics	
Buyer Book Value (mEUR)	Book value of the assets of the buyer. If there is more than one buyer in a transaction, we use the weighted average of the assets of the buyers. We use the percentage of the shares bought by the different buyers as weights. (Source: Buyer financial accounts, Amadeus).
Toehold Deal	Dummy which takes the value 1 if the buyer owns some shares in the target prior to the signing of the contract and 0 otherwise. (Source: Acquisition contracts).
Buyer Private Equity	Dummy variable which takes the value 1 if the buyer is a private equity firm, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that buys the highest portion of the shares is a private equity firm, and 0 otherwise. (Source: Merger Market, Amadeus).
Buyer Publicly-Listed	Dummy variable which takes the value 1 if the buyer is listed on a stock exchange, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that buys the highest portion of the shares is a listed on a stock exchange, and 0 otherwise. (Source: Merger Market, Amadeus).
Seller Characteristics	
Seller Book Value (mEUR)	Book value of the assets of the seller. If there is more than one seller in a transaction, we use the weighted average of the assets of the sellers. We use the percentage of the shares sold by the different sellers as weights. (Source: Seller financial accounts, Amadeus).
Main Seller Percent	This variable indicates what percentage of the total amount of shares (or total value of assets) is sold by the main seller. If there are more sellers, we define the main seller as the one that sells the largest stake. (Source: Acquisition contracts).

Appendix A-2.1 (Continued)

Seller Private Equity	Dummy variable which takes the value 1 if the seller is a private equity firm, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that sells the highest portion of the shares is a private equity firm, and 0 otherwise. (Source: Merger Market, Amadeus).
Seller Family	Dummy variable which takes the value 1 if the seller is a private person or family, and 0 otherwise. If there are more sellers, the variable takes the value 1 if the party that sells the highest portion of the shares is a private person or family, and 0 otherwise. (Source: Merger Market, Amadeus).
Seller Publicly-Listed	Dummy variable which takes the value 1 if the seller is publicly-listed 0 otherwise. If there are more sellers, the variable takes the value 1 if the company that sells the highest portion of shares is publicly-listed, and 0 otherwise. (Source: Merger Market, Amadeus).
Relative Size	Variable indicating the size of the buyer relative to the seller. To create this variable, we first calculate the ratio of the assets of the buyer to the assets of the seller. We then divide this ratio into ten deciles. The resulting variable therefore ranges between 1 and 10, with 10 (1) indicating that the buyer is very large (small) relative to the seller. Transactions in which the seller is a private person or family, and transactions in which the buyer is a government organization are coded such that the relative size variable takes the value 10. (Source: Buyer or seller financial accounts, Amadeus).
Client Characteristics	
Client Book Value	Book value of the assets of the client who is represented by the law firm which provided the first draft contract. If the first draft was provided by the buyer's law firm, this variable equals Buyer Book Value. If the first draft was provided by the seller's law firm, this variable equals Seller Book Value. (Source: Buyer or seller financial accounts, Amadeus).
Client Deal Experience	Number of transactions that the client who is represented by the law firm which provided the first draft contract has been engaged in over the five years preceding the signing date of a contract. (Source: Merger Market).
Client English LO	Dummy variable which takes the value 1 if the client who is represented by the law firm which provided the first draft contract is located in a country with English legal origin, and 0 otherwise (Source: Buyer or seller financial accounts, Amadeus, La-Porta, Lopez-de-Silanes, and Shleifer (2008)).
Client-Lawyer Switch	Dummy variable which takes the value 1 if the client who is represented by the law firm which provided the first draft contract switches to a new law firm with which she did not have a prior M&A deal relationship over the past five years, and 0 otherwise. (Source: Merger Market).
Client Deals with Lawyer	Number of transactions on which the client who is represented by the law firm which provided the first draft contract has requested advice from that law firm during the 5 years preceding this deal (Source: Merger Market).
Deal Characteristics	
Deal After 2008	Dummy variable which takes the value 1 if the contract is signed on or after January 1, 2008 (i.e., during the financial crisis), and 0 otherwise. (Source: Acquisition contracts).
Cross-Country Deal	Dummy variable which takes the value 1 if the target is not located in the same country as the buyer, and 0 otherwise. (Source: Amadeus).
Cross-Industry Deal	Dummy variable which takes the value 1 if the buyer is not active in the industry of the target, and 0 otherwise. We compare the first two digit of the buyer and target industry classifications (Fama-French 48 industries). (Source: Amadeus)
Controlled Auction	Dummy variable which takes the value 1 if the transaction is organized through a controlled auction, and 0 otherwise. (Source: Merger Market).

Appendix A-2.1 (Continued)

Negotiation Time	Number of days between the start of negotiations over a transaction and the signing of a contract. The start of the transaction negotiations is defined as the date at which the law firm which has provided the data has opened a file on a transaction (Source: Acquisition contracts, Acquisition files).
Interim Period	Number of days between the signing of a contract and the closing (transfer) date. The closing (transfer) date is the date at which there is a transfer of control of the target through the transfer of shares or assets. (Source: Acquisition contracts, Merger Market).
First Draft By Buyer	Dummy variable which takes the value 1 if the first draft of a contract was provided by the lawyer who represents the buyer, and 0 if the first draft of a contract was provided by the lawyer who represents the seller. (Source: Acquisition contracts)
Competition Approval	Dummy which takes the value 1 if a contract states that competition approval is still required, and 0 otherwise. (Source: Acquisition contracts)
Warranty Variables	(Source for all warranty variables: Acquisition contracts, Miller (2008))
Warranty Pages	Number of pages that are dedicated to warranties in the contract. This only refers to warranties of sellers and target, not to warranties granted by buyers.
Warranties	Number of warranties in the contract which provide statements about the seller or target quality. Each separate quality statement is considered a separate warranty. Warranties that form a specialization of another warranty are counted as a separate warranty. The warranties have been coded along a complete list of possible warranties, such that differences in phrasing are not reflected in the number of warranties.
Warranties/Model Contract	Number of warranties in a contract divided by the number of warranties included in the model contract. The model contract is derived from Miller (2008).
Corporate Records	Number of warranties within the category “Corporate Records” divided by the number of warranties within this category in the model contract.
Employee	Number of the warranties within the category “Employees” divided by the number of warranties within this category in the model contract.
Financial Accounts	Number of warranties within the category “Financial Accounts” divided by the number of warranties within this category in the model contract.
Assets	Number of the warranties within the category “Assets” divided by the number of warranties within this category in the model.
Contracts	Number of the warranties within the category “Contracts” divided by the number of warranties within this category in the model contract.
Insurance	Number of the warranties within the category “Insurance” divided by the number of warranties within this category in the model contract.
Intellectual Property	Number of the warranties within the category “Intellectual Property” divided by the number of warranties within this category in the model contract.
Legal	Number of the warranties within the category “Legal” divided by the number of warranties within this category in the model contract.
Covenant Variables	(Source for all covenant variables: Acquisition contracts, Miller (2008))
Covenant Pages	Number of pages that are dedicated to covenants in the contract. This only refers to pre-closing covenants restricting behavior of seller or target management in the period between signing and closing. This excludes pre-closing covenants relating to: consents to obtain, exclusivity of negotiations, access to premises and documents, and notifications regarding changes, and post-closing covenants.
Covenants	Number of the covenants in the contract that prescribe the behavior of the target and the seller in the period between the signing date and the transaction date. Each separate statement of behavior is considered a separate covenant. Covenants that form a specialization of another covenant are counted as a separate covenant. The covenants have been coded along a complete list of possible covenants, such that differences in phrasing are not reflected in the number of covenants.
Covenants/Model Contract	Number of covenants in a contract divided by the total number of covenants included in the model contract. The model contract is derived from Miller (2008).

Appendix A-2.1 (Continued)

Corporate Records	Number of covenants within the category "Corporate Documents" divided by the number of covenants within this category in the model contract.
Employees	Number of covenants within the category "Employees" divided by the number of covenants within this category in the model contract.
Dividends	Number of covenants within the category "Dividends" divided by the number of covenants within this category in the model contract .
Debt	Number of covenants within the category "Debt" divided by the number of covenants within this category in the model contract.
Business Conduct	Number of covenants within the category "Business Conduct" divided by the number of covenants within this category in the model contract.
Acquisitions	Number of covenants within the category "Acquisitions" divided by the number of covenants within this category in the model contract.
Divestments	Number of covenants within the category "Divestments" divided by the number of covenants within this category in the model contract.
Litigation	Number of covenants within the category "Litigation" divided by the number of covenants within this category in the model contract.
Law Firm Styles	
Law Firm High Warranty Style	Dummy variable which reflects the propensity of a law firm to include many warranties. To create this variable, we first calculate the coefficients on law firm fixed effects in a regression on Warranties/Model Contract that controls for the economic determinants. Second, we create a dummy which takes the value 1 for contracts drafted by law firms whose estimated coefficients on the law firm fixed effects are above median across all law firms, and 0 otherwise. (Source: Acquisition contracts)
Law Firm High Covenant Style	Dummy variable which reflects the propensity of a law firm to include many covenants. To create this variable, we first calculate the coefficients on law firm fixed effects in a regression on Covenants/Model Contract that controls for the economic determinants. Second, we create a dummy which takes the value 1 for contracts drafted by law firms whose estimated coefficients on the law firm fixed effects are above median across all law firms, and 0 otherwise. (Source: Acquisition contracts)
Deal Experience	Variable which reflects the deal experience of the drafting law firm, calculated as the number of deals that a law firm has advised on between 1995 and 2010. (Source: Merger Market).
Top 10 Ranking	Dummy variable which takes the value 1 if the drafting law firm is ranked in the top 10 based on a ranking of law firms using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Merger Market).
US Location	Dummy variable which takes the value 1 if the headquarters of the drafting law firm are located in the US, and 0 otherwise. (Source: Merger Market).
Lawyer Styles	
Partner High Warranty Style	Dummy variable which reflects the propensity of a lawyer to include many warranties. To create this variable, we first calculate the coefficients on partner fixed effects in a regression on Warranties/Model Contract that controls for the economic determinants, on a sample restricted to contracts drafted by our law firm. Second, we create a dummy which takes the value 1 for contracts drafted by lawyers whose estimated coefficients on the partner fixed effects are above median across all lawyers, and 0 otherwise. (Source: Acquisition contracts)
Partner High Covenant Style	Dummy variable which reflects the propensity of a lawyer to include many covenants. To create this variable, we first calculate the coefficients on partner fixed effects in a regression on Covenants/Model Contract that controls for the economic determinants, on a sample restricted to contracts drafted by our law firm. Second, we create a dummy which takes the value 1 for contracts drafted by lawyers whose estimated coefficients on the partner fixed effects are above median across all lawyers, and 0 otherwise. (Source: Acquisition contracts)

Appendix A-2.1 (Continued)

Deal Experience	Variable which reflects the deal experience of the drafting lawyer, calculated as the number of deals that a lawyer has advised on between 1995 and 2010. (Source: Merger Market).
Corporate Experience	Dummy variable which takes the value 1 if the drafting lawyer has worked in the corporate sector, and 0 otherwise. We classify as the corporate sector any company with commercial operation other than a law firm, excluding courts and universities. (Source: LinkedIn, corporate websites of law firms).
Business Education	Dummy variable which takes the value 1 if the drafting lawyer has had business education, and 0 otherwise. We consider as business education an MBA, a PhD in business or economics, or an undergraduate degree in any business or economics related topic. (Source: LinkedIn, corporate websites of law firms).
US Education	Dummy variable which takes the value 1 the drafting lawyer has studied at a US law school, and 0 otherwise. (Source: LinkedIn, corporate websites of law firms).
Female	Dummy variable which takes the value 1 the drafting lawyer is a female, and 0 otherwise. (Source: LinkedIn, corporate websites of law firms).
Risk Aversion	Variable which reflects the self-assessed risk aversion of the lead lawyers. In interviews with 14 lead lawyers, we asked the following question: "How do you see yourself: are you generally a person who is fully prepared to take risks or do you try to avoid taking risks? Please place yourself on the scale of 0 to 10, where the value 0 means: 'not at all willing to take risks' and the value 10 means: 'very willing to take risks'." The risk aversion measure is estimated as 10 – scale-position, such that higher values imply higher risk aversion. (Source: Interviews with lead lawyers).
Other Contract Provisions	
Acquisition Premium	Target Market Value (as defined above) divided by the book value of the target, winsorized at 2% (Source: Acquisition contracts, Amadeus, trade register).
Conditional Payment	Dummy variable which takes the value 1 if (part of) the payment contains a conditional element, and 0 otherwise. Earn out payments and equity payments are considered conditional payments. (Source: Acquisition contracts)
Maximum Claim	Ratio of the maximum amount that a buyer can claim in case of a breach of warranties relative to the transaction value. For deals where the transaction value is negative (the seller pays the buyer to accept the liabilities), this variable is set equal to 0. (Source: Acquisition contracts)
Price Adjustments	Number of purchase price adjustments contained in a contract. A purchase price adjustment is an agreed upon adjustment of the transaction value if the book values of the target are different on the transaction date than on the signing date, for specified items in the target accounts (e.g., Debt, Equity, Cash, Net Operating Capital). This variable indicates for how many of these items such an adjustment is included in a contract. (Source: Acquisition contracts)
Financial Advisors	
Seller Bank Advice	Dummy variable which takes the value 1 if the seller has obtained advice from an investment bank for this deal, and 0 otherwise. (Source: Merger Market).
Buyer Bank Advice	Dummy variable which takes the value 1 if the buyer has obtained advice from an investment bank for this deal, and 0 otherwise. (Source: Merger Market).

Appendix A-2.2
Overview of Warranty and Covenant Provisions

Panel A of this table provides an overview of the most frequently occurring warranties and how often they occur across contracts. Panel B provides an overview of typical covenants and how frequently they occur across contracts. The overview is limited to the top 5 warranties within each category, excluding warranties (covenants) which appear in less than 40% (30%) of the contacts. We further indicate whether the provision is included in the model contract of Miller (2008).

Panel A: Examples of Warranty Provisions

Warranty Example	Sample	Model Contract
Corporate Records		
The target and all its subsidiaries are validly existing entities.	79%	1
The shares of the target are 100% of the share capital, validly issued and fully paid up.	90%	1
There are no encumbrances on the shares of the target and the subsidiaries.	87%	1
The seller has the authority to sign this agreement.	76%	1
This agreement will constitute a valid, binding and enforceable agreement.	70%	1
Employees		
All (specified) employee contracts have been disclosed.	71%	1
Target is complying with all applicable laws and regulation relating to employment.	45%	1
Target is not involved in any strike or industrial related dispute.	46%	1
Target has complied with all benefit (pension, disability, and unemployment) plans.	52%	1
The current employee benefit plans are in compliance with laws and regulations.	49%	1
Financial Accounts		
The accounts give a true and fair view of financial affairs of the target.	79%	1
Target has accurately filed all tax returns, within the time limit.	71%	1
Target has paid all taxes which are due and payable.	59%	1
Since accounts date, target's operations have been carried on in the ordinary course.	69%	0
Since accounts date, target has not paid any dividends or made another distribution.	65%	1
Assets		
All assets listed in the financial accounts are legally owned by the target.	65%	1
The assets are not subject to encumbrances.	64%	1
The assets owned by the target are in a good state, subject to normal wear and tear.	45%	1
All lease agreements of assets leased by the target have been disclosed.	41%	1
Contracts		
All material contracts of the target are disclosed.	53%	1
Other than listed in the accounts, there is no liability or indebtedness of the target.	47%	1
Target has not received a notice of termination or intent to terminate a contract	43%	1
All contracts have been complied with by the target.	75%	1
Insurance		
The insurance policies of the target have been disclosed, and are accurate.	49%	1
Target carries insurance for risks and amounts which are customary in the industry.	40%	0
Intellectual Property		
The intellectual property is owned by the target, or target has valid licences to use it.	53%	1
Target does not infringe on the intellectual property of any third party.	47%	1
There are no third parties infringing on the intellectual property of the target.	48%	1
Legal		
The target is running the business in compliance with all applicable laws.	63%	1
All licences, permits, and dispensations have been obtained and are complied with.	62%	1
Target is not involved in any legal dispute (claim, proceeding, litigation, et.).	87%	1
There is no threat of a legal dispute.	67%	1
No investigations have been initiated against the target for violation of any law.	55%	0

Appendix A-2.2 (Continued)

Panel B: Examples of Covenant Provisions

Covenant Examples	Sample	Model Contract
Corporate Documents		
Target shall not amend the charter documents.	53%	1
Employees		
Target shall not amend any employee benefit plans.	55%	0
Target shall not increase any salaries or wages.	41%	1
Target shall not enter into any new employment contracts.	36%	0
Target shall not terminate any employment contract.	31%	0
Dividend Payments		
Target shall not pay dividends or make any other distributions to its shareholders.	75%	1
Target shall not issue, deliver or sell any shares in its capital stock.	62%	1
Target shall not repurchase or otherwise acquire any shares in its capital stock.	48%	1
Debt		
Target shall not incur any new debt.	61%	1
Target shall comply with all debt payment obligations.	30%	0
Target shall not Issue a guarantee or security for an obligation of any third party.	34%	1
Business Conduct		
Target will carry on the business in the ordinary course as conducted so far.	90%	1
Target will preserve the relationship with its customers, suppliers, and distributors.	51%	1
Target shall not enter into any contract outside the ordinary course of business.	74%	1
Target shall not terminate any contract outside the ordinary course of business.	51%	1
Target will maintain the insurance policies in force.	47%	1
Acquisitions		
Target shall not make any material capital expenditures.	64%	0
Target shall not acquire any corporation, partnership or business combination.	42%	1
Divestments		
Target shall not sell, lease, licence or dispose of any of the assets of the business.	58%	1
Target shall not pledge, encumber or mortgage any of the assets of the business.	54%	1
Litigation		
Target shall not settle any legal claim, action or proceeding.	41%	1

Appendix A-2.3
Distribution of Sample Characteristics

Panel A of this table provides the distribution of targets across different industries, locations, and deal years. Industries are categorized according to the Fama-French 12 industry classification. Panel B reports information on the different types of buyers and sellers in the sample and cross-tabulates their frequency. Panel C reports information on the location of buyers and sellers in the sample and cross-tabulates their frequency.

Panel A: Distribution of Targets across Industries, Locations, and Deal Years

Industry	Percentage	Location	Percentage	Year	Percentage
Wholesale & Retail	15%	Netherlands	85%	2005	6%
Business Equipment	13%	Europe	11%	2006	26%
Manufacturing	9%	USA	2%	2007	31%
Money & Finance	11%	Other	2%	2008	17%
Chemicals	6%			2009	15%
Consumer Non-Durables	6%			2010	5%
Other	42%				

Panel B: Buyer and Seller Types

		Seller Type					
		Strategic	Family	Private Equity	Financial	Government	Total
Buyer Type	Strategic	38%	13%	8%	3%	1%	64%
	Family	1%	0%	0%	1%	0%	1%
	Private Equity	11%	4%	6%	1%	0%	22%
	Financial	3%	0%	1%	2%	0%	7%
	Government	5%	1%	0%	0%	1%	7%
	Total	58%	18%	15%	7%	2%	100%

Panel C: Buyer and Seller Locations

		Seller Location				
		Netherlands	Europe	North America	Other	Total
Buyer Location	Netherlands	48%	10%	0%	1%	59%
	Europe	20%	3%	1%	2%	26%
	North America	7%	1%	1%	0%	9%
	Other	4%	1%	1%	0%	6%
	Total	79%	15%	3%	3%	100%

Appendix A-2.4
Economic Determinants of Contract Provisions by Category

This table shows OLS regressions to look at the determinants of the warranties (Panel A) and covenants (Panel B) by category. The sample covers 151 M&A transactions, but the regressions are on fewer observations because of missing data for some variables. The regressions report the effect of economic determinants. In Panel B the sample is restricted to deals where signing and closing dates were not the same. We report in parentheses *t*-statistics, calculated using robust standard errors. Detailed variable definitions are provided in Appendix A-2.1. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: Economic Determinants per Warranty Category

	Dependent Variable: Warranties/Model Contract per Category							
Categories:	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellect. Property	Legal
Cross-Country	0.09***	0.09**	0.05	0.05	0.20***	0.07	0.08*	0.09**
	(3.24)	(2.31)	(1.49)	(1.45)	(3.62)	(1.09)	(1.82)	(2.18)
Cross-Industry	-0.03	-0.05	0.02	-0.01	-0.03	-0.04	-0.02	-0.02
	(-1.29)	(-1.53)	(0.71)	(-0.14)	(-0.60)	(-0.63)	(-0.49)	(-0.48)
Toehold Deal	-0.32***	-0.31***	-0.50***	-0.33***	-0.53***	-0.51***	-0.27***	-0.47***
	(-7.35)	(-7.05)	(-5.92)	(-6.44)	(-8.14)	(-7.62)	(-3.52)	(-8.03)
Transaction Value	0.00	0.01	0.01*	0.01**	0.01*	0.01	0.01	0.00
	(0.38)	(1.02)	(1.76)	(2.04)	(1.75)	(1.21)	(1.33)	(0.71)
Asset Deal	-0.22***	0.05	-0.16***	-0.01	-0.11**	-0.30***	0.03	-0.02
	(-5.47)	(1.09)	(-3.73)	(-0.32)	(-2.04)	(-4.17)	(0.40)	(-0.27)
High R&D Industry	-0.01	-0.02	-0.01	-0.01	-0.06	-0.02	0.13***	-0.08*
	(-0.19)	(-0.39)	(-0.14)	(-0.16)	(-1.13)	(-0.35)	(2.74)	(-1.91)
Buyer Private Eq.	0.06*	-0.02	0.05	-0.07	-0.11*	-0.06	-0.00	0.01
	(1.80)	(-0.55)	(1.06)	(-1.49)	(-1.89)	(-0.86)	(-0.08)	(0.29)
Seller Private Eq.	-0.04	-0.07	-0.05	-0.07	-0.12*	-0.08	-0.05	-0.20***
	(-1.21)	(-1.25)	(-1.01)	(-1.61)	(-1.88)	(-0.97)	(-1.16)	(-3.63)
Seller Family	-0.01	0.10	0.01	-0.03	0.10	0.09	-0.13*	-0.05
	(-0.33)	(1.64)	(0.15)	(-0.59)	(1.55)	(1.01)	(-1.90)	(-0.76)
Main Seller Pct.	-0.15**	-0.29**	-0.35***	-0.13	-0.40***	-0.26	-0.33***	-0.11
	(-2.10)	(-2.53)	(-3.62)	(-1.52)	(-3.10)	(-1.59)	(-3.03)	(-1.15)
Relative Size	-0.00	-0.01	0.02**	-0.00	-0.00	-0.00	0.02**	0.01
	(-0.48)	(-0.79)	(2.14)	(-0.43)	(-0.30)	(-0.17)	(2.16)	(1.27)
First Draft by	0.04	0.08	0.13***	0.10*	0.17***	0.11	0.07	0.04
Buyer	(1.00)	(1.25)	(2.74)	(1.84)	(2.66)	(1.29)	(1.47)	(0.72)
Deal After 2008	0.06**	0.01	0.16***	0.09**	0.04	0.08	0.06	0.08**
	(2.44)	(0.39)	(4.94)	(2.28)	(0.82)	(1.34)	(1.57)	(2.02)
Controlled	0.03	0.09**	0.06	-0.01	0.11*	0.10	-0.02	0.05
Auction	(0.82)	(1.99)	(1.63)	(-0.27)	(1.85)	(1.51)	(-0.43)	(1.06)
Obs.	145	145	145	145	145	145	145	145
Adj. R^2	36%	17%	49%	11%	31%	15%	22%	17%

Appendix A-2.4 (continued)

Panel B: Economic Determinants per Covenants Category

	Dependent Variable: Covenants/Model Contract per Category							
Categories:	Corporate Records	Employee	Dividends	Debt	Business Conduct	Acquis.	Divest.	Litigation
Cross-Country	-0.04	0.04	0.04	0.04	-0.04	0.03	0.03	0.07
	(-0.28)	(0.38)	(0.48)	(0.28)	(-0.74)	(0.13)	(0.32)	(0.47)
Cross-Industry	0.12	0.04	0.09	-0.02	-0.08	-0.06	-0.15	0.00
	(0.97)	(0.45)	(1.26)	(-0.15)	(-1.56)	(-0.30)	(-1.45)	(0.00)
Toehold Deal	-0.34*	-0.49*	-0.22*	-0.59***	-0.48***	-1.23***	-0.43*	-0.20
	(-1.94)	(-1.93)	(-1.78)	(-3.02)	(-3.57)	(-3.85)	(-1.92)	(-0.83)
Transaction Value	0.01	0.02	0.02***	0.02*	0.02***	-0.00	0.04***	0.06*
	(0.68)	(1.61)	(2.68)	(1.81)	(2.68)	(-0.05)	(2.94)	(1.87)
Asset Deal	-0.57***	-0.10	-0.42***	-0.63***	-0.19***	-1.12***	-0.48***	0.16
	(-4.36)	(-0.58)	(-4.36)	(-5.11)	(-2.74)	(-3.67)	(-3.78)	(0.65)
Target	-0.02	0.23	0.30**	-0.00	0.17	0.63	-0.02	0.23
Cash/Assets	(-0.07)	(0.86)	(2.07)	(-0.01)	(0.96)	(0.70)	(-0.06)	(0.76)
High Capex	-0.03	0.03	-0.19*	-0.24*	-0.11*	-0.28	-0.04	0.13
Industry	(-0.27)	(0.19)	(-1.95)	(-1.75)	(-1.71)	(-0.97)	(-0.29)	(0.68)
Interim Period	0.11**	0.13***	0.07**	0.07*	0.04**	0.06	0.07*	0.04
	(2.08)	(3.98)	(2.31)	(1.79)	(2.17)	(0.75)	(1.89)	(0.85)
Competition App.	0.05	0.02	0.04	-0.00	0.03**	0.03	0.05**	0.02
	(1.51)	(0.89)	(1.64)	(-0.15)	(2.44)	(0.80)	(2.08)	(0.30)
Relative Size	0.04	0.01	0.02	0.02	0.01	-0.01	0.03	0.03
	(1.30)	(0.27)	(0.98)	(0.99)	(0.78)	(-0.22)	(1.05)	(0.94)
First Draft by	0.41**	0.21	-0.10	0.02	0.09	-0.58*	-0.08	-0.15
Buyer	(2.42)	(1.43)	(-0.88)	(0.14)	(0.98)	(-1.87)	(-0.55)	(-0.71)
Deal After 2008	0.20	-0.08	0.25***	-0.13	0.05	-0.08	-0.18*	-0.05
	(1.50)	(-0.72)	(3.41)	(-1.29)	(0.93)	(-0.38)	(-1.67)	(-0.40)
Controlled Auction	0.11	0.20*	0.04	0.26**	0.12*	0.20	0.24*	0.52***
	(0.87)	(1.80)	(0.41)	(2.01)	(1.71)	(0.78)	(1.91)	(2.93)
Obs.	96	96	96	96	96	96	96	96
Adj. R^2	20%	9%	33%	14%	22%	13%	26%	15%

Appendix A-2.5
Comparison of Sample Provisions with Other Samples

This table compares the contract provision on our sample to those in four studies carried out by law firms or the American Bar Association. We report across all five samples the fraction of contracts that contain certain provisions. ABA 2010 Europe is the 2010 European Private Target Mergers and Acquisitions Deal Points Study as printed by the American Bar Association. ABA 2009 US is the 2009 Private Target Mergers & Acquisitions Deal Points Study as printed by the American Bar Association. CMS 2010 Europe is the CMS European M&A Study 2010 as published by CMS Legal Services EEIG. SRS 2010 is the 2010 SRS M&A Deal terms study as published by the Shareholder Representative Services LLC.

Sample	**This Study**	**ABA 2010 Europe**	**ABA 2009 US**	**CMS 2010 Europe**	**SRS 2010**
Sample Size	151	97	106	250	88
Sample Period	'05 –'10	2008	2008	2009	'07 – '10
Contract Location	World	Europe	USA	Europe	USA
Payment Mechanisms					
All Cash at Closing	66%	73%			
Earn Out/Equity	18%	11%	29%	18%	25%
Vendor Loan	19%	15%			
Other	0%	1%			
Warranties					
Financial statements fairly represent target financials	79%	86%	100%		
Target has no liabilities other than disclosed	47%	40%	97%		97%
Seller has disclosed all material target information	53%	46%	68%		53%
Target is complying with all applicable laws	63%		100%		
Maximum Time to Claim					
No time limitation given	3%	9%	4%		0%
Limit 0 to 6 months	2%	1%	0%		1%
Limit 7 to 12 months	20%	22%	20%	16%	35%
Limit 13 to 18 months	47%	28%	50%	20%	51%
Limit 19 to 24 months	16%	31%	18%	24%	11%
Limit is more than 24	11%	9%	6%	27%	2%
Maximum that Buyer can Claim					
<10% of transaction value	16%	19%	48%	7%	46%
10% - 15% of transaction value	12%	18%	16%	18%	37%
15% - 25% of transaction value	23%	22%	14%		17%
25% - 50% of transaction value	23%	20%	13%	16%	4%
50% - 99% of transaction value	14%	4%	4%	9%	0%
≥100% full transaction value	11%	10%	5%	22%	0%

Appendix A-2.6
Comparison of Sample Characteristics with Other Samples

This table compares mean values of deal, target, seller, and buyer characteristics of our sample to those in two other samples: (i) all other private takeovers that our law firm has been advised on between April 2005 and May 2010, and (ii) all takeovers in the Merger market database. To construct the first comparison sample, we include transactions where at least one of the parties involved (buyer, seller, or target) is located in the Netherlands. To compare the different sample, we focus on variables that are available in Merger Market. As not all the deals in our sample are reported in Merger Market, our sample in this comparison is restricted to 119 deals. We report difference-in-means tests that compare our sample and the two comparison samples. *** indicates significance at 1%, ** indicates significance at 5% and * indicates significance at 10%.

	This Study	Our Law Firm		Merger Market Deals	
	Mean	Mean	Difference	Mean	Difference
Observations	**119**	**101**		**2,601**	
Deal Characteristics					
Transaction Value (mEUR)	555	1,149	-594*	242	314**
Value Announced	52%	46%	7%	39%	13%**
Equity Payment	2%	2%	0%	2%	0%
Percentage Equity Payment	2%	2%	0%	2%	0%
Revenue Multiple	2.3	1.7	0.6	2.3	1%
EBIT Multiple	15.8	21.9	-6.1	36	-20.2
EBITDA Multiple	10	10.9	-0.9	44.9	-34.9
PE Multiple	20.3	578	-557.7	235.5	-215.2
Cross Border	51%	56%	-5%	66%	-15%***
Controlled Auction	3%	7%	-4%	2%	1%
Management Buyout	15%	13%	2%	11%	4%*
Transatlantic	14%	18%	-4%	16%	-2%
Private Equity	11%	17%	-6%	11%	0%
Secondary Buyout	9%	8%	1%	5%	5%**
Target Location					
Asia	0%	0%	0%	3%	-3%**
Eastern Europe	2%	3%	-1%	5%	-4%**
Middle East	1%	0%	1%	1%	0%
Netherlands	86%	79%	7%	57%	29%***
North America	2%	6%	-4%**	6%	-4%**
Oceania	0%	0%	0%	1%	-1%
Western Europe	10%	12%	-2%	24%	-14%***
Target Industry					
Agriculture	1%	1%	0%	1%	0%
Mining	4%	4%	0%	5%	-1%
Construction	17%	8%	9%**	18%	-1%
Manufacturing	18%	18%	1%	17%	2%
Transport and Communication	13%	27%	-14%**	15%	-3%
Wholesale Trade	11%	7%	4%	13%	-2%
Retail Trade	12%	14%	-2%	9%	2%
Finance and Real Estate	3%	4%	-1%	4%	-2%
Services	22%	18%	4%	16%	5%*
Public Administration	0%	0%	0%	0%	0%

Appendix A-2.6 (continued)

	This Study	Our Law Firm		Merger Market Deals	
Seller Location	**Mean**	**Mean**	**Difference**	**Mean**	**Difference**
Asia	0%	2%	-2%	3%	-3%**
Eastern Europe	0%	0%	0%	3%	-3%**
Middle East	1%	0%	1%	2%	-1%
Netherlands	83%	72%	10%*	43%	39%***
North America	3%	9%	-6%**	14%	-11%**
Oceania	1%	2%	-1%	1%	0%
Western Europe	12%	15%	-3%	32%	-20%***
Seller Industry					
Agriculture	3%	2%	1%	2%	0%
Mining	9%	6%	3%	8%	1%
Construction	22%	6%	16%***	20%	1%*
Manufacturing	23%	9%	14%**	17%	6%**
Transportation and Communication	15%	15%	0%	20%	-5%
Wholesale Trade	12%	4%	8%**	15%	-4%
Retail Trade	32%	27%	5%	34%	-2%
Finance and Real Estate	1%	3%	-2%	5%	-4%**
Services	24%	7%	17%***	20%	4%**
Public Administration	9%	10%	-1%	4%	6%***
Seller Advisors					
Advised by Our Law Firm	36%	49%	-12%**	2%	-2%***
Nr. of Law Firms Involved	1.2	1.2	0	0.5	-0.5***
Top 10 Law Firm Involved	18%	12%	6%	11%	-11%**
Bank Involved	63%	51%	12%**	38%	-38%***
Number of Banks Involved	86%	73%	12%	45%	-45%***
Top 10 Bank Involved	17%	25%	-8%*	11%	-11%**
Buyer Location					
Asia	5%	1%	4%**	2%	3%**
Eastern Europe	0%	0%	0%	2%	-2%*
Middle East	0%	2%	-2%*	1%	-1%
Netherlands	57%	57%	0%	66%	-9%**
North America	11%	18%	-7%*	9%	2%
Oceania	0%	1%	-1%	1%	-1%
Western Europe	26%	21%	5%	19%	7%**
Buyer Industry					
Agriculture	2%	2%	0%	3%	-1%
Mining	9%	10%	-1%	10%	-1%
Construction	17%	5%	12%**	19%	-2%
Manufacturing	26%	14%	12%**	21%	5%*
Transport & Communication	14%	27%	-12%**	19%	-5%
Wholesale Trade	13%	8%	5%	16%	-4%
Retail Trade	40%	38%	3%	32%	9%**
Finance & Real Estate	3%	5%	-2%	6%	-3%*
Services	28%	24%	4%	26%	2%
Public Administration	3%	5%	-2%	3%	0%
Buyer Advisors					
Advised by Our Law Firm	50%	52%	-2%	2%	-2%***
Nr of Law Firms Involved	1.8	1.5	0.2	0.8	-0.8***
Top 10 Law Firm Involved	10%	10%	0%	15%	-15%
Investment Bank Involved	43%	37%	6%	30%	-30%***
Number of Banks Involved	55%	52%	2%	35%	-35%***
Top 10 Bank Involved	18%	21%	-2%	9%	-9%***

Appendix A-2.7
Robustness Checks: Sample Selection

This table shows OLS regressions as in Tables 2.3, 2.4, 2.5, based on a sample excluding contracts where our law firm provided the first draft (limits the sample to 57 observations). *t*-statistics are in parentheses, calculated using robust standard errors. Detailed variable definitions are provided in Appendix A-2.1. *** indicates significance at 1%, ** indicates significance at 5% and * indicates significance at 10%.

Panel A: Warranties and Covenants: Excluding Our Law Firm

	Dependent Variable:					
	Warranties/Model Contract			Covenants/Model Contract		
Law Firm FE: *F*-test (*p*-value)		58.47 (0.000)			134.82 (0.000)	
Law Firm High Warranty Style			0.15***			
			(3.82)			
Law Firm High Covenant Style						0.38***
						(4.14)
Cross-Country Deal	0.13***	0.12	0.13***	0.05	0.23	0.09
	(2.78)	(1.17)	(3.39)	(0.51)	(0.67)	(1.19)
Cross-Industry Deal	-0.00	-0.15	-0.05	0.05	0.18	0.06
	(-0.02)	(-1.13)	(-1.09)	(0.54)	(0.95)	(0.70)
Toehold Deal	-0.39***	-0.38	-0.39***	-0.45***	-0.30	-0.62***
	(-4.75)	(-1.24)	(-6.49)	(-3.37)	(-0.31)	(-6.98)
Transaction Value	0.04**	0.04	0.03**	0.04	0.06	0.06**
	(2.45)	(1.24)	(2.24)	(1.37)	(0.70)	(2.63)
Asset Deal Dummy	-0.14**	-0.16	-0.18***	-0.30***	-0.23	-0.13
	(-2.18)	(-0.73)	(-4.06)	(-3.20)	(-0.47)	(-1.61)
High R&D Industry	-0.04	-0.08	-0.08*			
	(-0.66)	(-0.84)	(-1.71)			
Target Cash/Assets				0.39	0.42	0.54***
				(1.57)	(0.65)	(2.97)
High Capex Industry				-0.06	-0.09	-0.08
				(-0.45)	(-0.20)	(-0.96)
Interim Period (log)				0.07**	0.16	0.10***
				(2.09)	(1.46)	(3.00)
Competition Approval				-0.03	-0.06	-0.02
				(-0.41)	(-0.60)	(-0.44)
Buyer Private Equity	-0.14***	-0.02	-0.09**			
	(-2.75)	(-0.19)	(-2.17)			
Seller Private Equity	-0.14***	-0.13	-0.12**			
	(-2.82)	(-1.55)	(-2.61)			
Seller Family	-0.05	-0.01	-0.04			
	(-0.59)	(-0.06)	(-0.55)			
Main Seller	-0.57***	-0.54***	-0.57***			
	(-3.55)	(-3.29)	(-4.28)			
Relative Size	-0.00	-0.01	0.00	0.01	0.02	0.02
	(-0.05)	(-0.57)	(0.14)	(0.61)	(0.33)	(1.26)
First Draft by Buyer	0.14**	0.21	0.14**	-0.03	0.02	0.00
	(2.11)	(1.55)	(2.28)	(-0.25)	(0.03)	(0.03)
Deal After 2008	0.06	0.06	0.04	-0.03	-0.30	-0.20*
	(1.19)	(0.48)	(1.01)	(-0.24)	(-0.63)	(-1.93)
Controlled Auction	0.10*	0.21*	0.14***	0.17	0.26	0.18**
	(1.88)	(2.02)	(3.56)	(1.32)	(1.03)	(2.33)
Obs.	55	55	55	44	44	44
Adj. R^2	51%	50%	62%	20%	27%	57%
Diff. in Adj. R^2		-1%	12%		7%	38%

Appendix A-2.7 (continued)

Panel B: Warranties per Category: Excluding Our Law Firm

	Law Firm Fixed Effects					Law Firm High Warranty Style				
Dependent Variable:	Law Firm FE:			Adj.	Diff. in				Adj.	Diff.in
Warranties on…	*F*-test (*p*-value)		Obs.	R^2	Adj. R^2	High Warranty Style		Obs.	R^2	Adj. R^2
Corporate Records	12.57	(0.000)	55	20%	-5%	0.09*	(1.74)	55	28%	4%
Employees	137.54	(0.000)	55	48%	4%	0.12	(1.55)	55	47%	3%
Financial Accounts	9.90	(0.000)	55	33%	-8%	0.16***	(2.76)	55	49%	8%
Assets	8.08	(0.000)	55	13%	-12%	0.11**	(2.18)	55	30%	5%
Contracts	32.92	(0.000)	55	69%	10%	0.28***	(6.08)	55	72%	13%
Insurance	95.25	(0.000)	55	35%	-2%	0.07	(0.74)	55	37%	-1%
Intellectual Property	38.36	(0.000)	55	66%	36%	0.16**	(2.14)	55	39%	9%
Legal	2.59	(0.034)	55	26%	0%	0.25***	(3.27)	55	43%	17%
Average				**39%**	**3%**				**43%**	**7%**

Panel C: Covenants per Category: Excluding Our Law Firm

	Law Firm Fixed Effects					Law Firm High Covenant Style				
Dependent Variable:	Law Firm FE:			Adj.	Diff. in				Adj.	Diff.in
Covenants on…	*F*-test (*p*-value)		Obs.	R^2	Adj. R^2	High Covenant Style		Obs.	R^2	Adj. R^2
Corporate Records	30.02	(0.000)	44	32%	43%	0.57***	-3.41	44	13%	24%
Employees	41.43	(0.000)	44	37%	43%	0.58***	-4.5	44	27%	33%
Dividends	23.79	(0.000)	44	1%	-29%	0.33***	-3.14	44	41%	11%
Debt	23.10	(0.000)	44	-58%	-70%	0.54***	-3.08	44	36%	24%
Business Conduct	1.321	(0.356)	44	-16%	-16%	0.30**	-2.07	44	20%	20%
Acquisitions	34.91	(0.000)	44	63%	36%	0.21	-0.7	44	26%	-2%
Divestments	26.76	(0.000)	44	60%	27%	0.51***	-3.48	44	57%	24%
Litigation	4.86	(0.015)	44	-122%	-131%	0.14	-0.56	44	6%	-2%
Average				**0%**	**-12%**				**28%**	**17%**

Appendix A-2.8
Robustness Checks: Other Contract Provisions or Advisors

This table shows OLS regressions to look at the determinants of warranties and covenants. All regressions control for the variables in Table 2.3. The sample covers 151 M&A transactions, but the regressions are on fewer observations because of missing data for some variables. Panel A includes additional controls on the premium and contract design. Panel B controls for the presence of financial advisors. We report in parentheses *t*-statistics, calculated using robust standard errors. Detailed variable definitions are provided in Appendix A-2.1. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: Warranties and Covenants: Controlling for Other Contract Provisions

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	51.39				3,910.95			
	(0.000)				(0.000)			
Partner FE: F-test			9.06				9.52	
			(0.000)				(0.000)	
High Warranty Style		0.16***		0.12***				
		(4.25)		(4.63)				
High Covenant Style						0.30***		0.29***
						(3.96)		(4.79)
Acquisition Premium	-0.00	-0.00	-0.00	-0.00	-0.04**	-0.02	0.02	0.00
	(-0.33)	(-0.03)	(-0.49)	(-0.51)	(-2.05)	(-1.31)	(0.57)	(0.41)
Conditional Payment	0.01	-0.01	0.03	0.06*	0.14	0.06	-0.07	0.02
	(0.20)	(-0.34)	(0.64)	(1.76)	(1.12)	(0.63)	(-0.45)	(0.28)
Maximum Claim	-0.03	-0.02	-0.04	-0.00	-0.03	0.03	-0.06	-0.04
	(-0.69)	(-0.67)	(-0.89)	(-0.08)	(-0.27)	(0.35)	(-0.25)	(-0.38)
Price Adjustments	0.03***	0.03***	0.03**	0.02**	-0.01	0.02	0.01	0.05**
(Nr.)	(2.88)	(2.87)	(2.60)	(2.28)	(-0.21)	(0.80)	(0.17)	(2.17)
Obs.	131	131	78	78	91	91	48	48
Adj. R^2	46%	47%	52%	51%	42%	44%	54%	62%
Diff. in Adj. R^2	7%	8%	15%	14%	11%	13%	13%	21%

Panel B: Warranties and Covenants: Controlling for Investment Banks

	Warranties/Model Contract				Covenants/Model Contract			
	Law Firm Styles		Partner Styles		Law Firm Styles		Partner Styles	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm: *F*-test	80.38				207.02			
	(0.000)				(0.000)			
Partner FE: F-test			3.51				19.58	
			(0.000)				(0.000)	
High Warranty Style		0.15***		0.10***				
		(4.21)		(4.16)				
High Covenant Style						0.29***		0.32***
						(3.93)		(4.62)
Seller Bank Advice	0.04	0.03	0.05	0.05*	0.09	0.11**	-0.08	-0.10
	(1.21)	(1.00)	(1.41)	(1.67)	(1.25)	(2.04)	(-0.76)	(-1.48)
Buyer Bank Advice	-0.06*	-0.05*	-0.02	-0.05	0.03	0.00	0.19*	0.02
	(-1.68)	(-1.86)	(-0.67)	(-1.60)	(0.44)	(0.09)	(1.82)	(0.27)
Obs.	145	145	89	89	96	96	51	51
Adj. R^2	42%	46%	48%	52%	40%	45%	59%	59%
Diff. in Adj. R^2	3%	7%	5%	10%	5%	11%	26%	26%

Appendix A-2.9
Explanatory Variables: Correlations

This table reports correlation coefficients between explanatory variables. * indicates significance at the 5% level.

		Cross-Country Deal	Cross-Industry Deal	Toehold Deal	Trans-action Value	Asset Deal	High R&D Industry	Buyer Private Equity	Seller Private Equity	Seller Family	Main Seller Percent	Target Cash/ Assets	High Capex Industry	Interim Period	Com-petition Approv.	Relative Size	First Draft by Buyer	Deal After 2008	Contr. Auction
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(19)
Cross-Country	(1)	1.00																	
Cross-Industry	(2)	0.02	1.00																
Toehold Deal	(3)	-0.06	0.08	1.00															
Transaction Value	(4)	0.08	0.15	0.01	1.00														
Asset Deal	(5)	-0.23*	-0.02	-0.05	-0.25*	1.00													
High R&D Indus.	(6)	0.29*	-0.03	-0.01	0.00	-0.09	1.00												
Buyer Private Eq.	(7)	-0.18*	0.37*	0.01	0.21*	-0.16*	-0.04	1.00											
Seller Private Eq.	(8)	0.03	0.10	-0.07	0.15	0.00	-0.06	0.18*	1.00										
Seller Family	(9)	-0.07	-0.01	0.03	-0.19*	-0.14	0.02	0.00	-0.20*	1.00									
Main Seller Pct	(10)	-0.05	-0.01	0.01	0.06	0.17*	-0.14	-0.12	-0.18*	-0.40*	1.00								
Trgt Cash/Assets	(11)	0.09	-0.02	0.01	-0.04	-0.15	0.36*	-0.02	0.02	-0.14	-0.07	1.00							
High Capex Indus.	(12)	-0.27*	-0.21*	-0.10	-0.11	0.09	-0.36*	-0.12	-0.03	-0.03	0.17*	-0.20*	1.00						
Interim Period	(13)	0.18*	0.08	-0.12	0.33*	0.06	-0.24*	0.14	0.15	-0.27*	0.17*	-0.24*	-0.05	1.00					
Competition Appr	(14)	0.24*	0.05	-0.04	0.27*	-0.13	-0.07	0.07	-0.01	-0.16*	0.07	-0.17*	-0.11	0.43*	1.00				
Relative Size	(15)	-0.02	-0.03	0.02	-0.10	-0.26*	0.02	0.20*	-0.06	0.55*	-0.29*	0.06	0.03	-0.11	-0.15	1.00			
First Draft Buyer	(16)	-0.20*	-0.09	0.19*	-0.29*	-0.08	0.01	0.04	-0.23*	0.42*	-0.13	0.11	0.04	-0.40*	-0.31*	0.47*	1.00		
Deal After 2008	(17)	0.03	-0.02	0.13	-0.06	-0.09	-0.08	-0.04	0.02	0.04	0.02	-0.02	0.16	0.01	-0.03	0.11	0.11	1.00	
Contr. Auction	(19)	0.08	0.18*	-0.09	0.14	0.06	0.18*	0.09	0.12	-0.17*	0.07	-0.04	-0.07	0.18*	0.15	-0.11	-0.43*	-0.03	1.00

3

Contract Design and Premiums:

Evidence from Acquisitions of Private Targets[1]

3.1 Introduction

Does contract design in corporate acquisitions affect the prices that are being paid for targets? In most acquisitions, large amounts of time and money are dedicated to negotiating over contract provisions.[2] But do these provisions have value implications that translate into premiums paid? Whereas prior literature has identified several important drivers of acquisition premiums, such as synergies, bargaining power, and governance, relatively little is known about the impact of contracts.[3]

Two opposing views can be distinguished with respect to the relation between contract design and acquisition pricing. The first view holds that the negotiation process does not allow for interactions between price and non-price terms (i.e. contract

[1] The research in this chapter is joint work with F. López-de-Silanes.

[2] Based on UK public deals in 2012, fees charged by law firms for their services average a substantial 1.3% of deal value, ranging between 0.1% and 4.5% depending on deal size (Freedman (2013)).

[3] Evidence on the effects of expected synergies is provided in Slusky and Caves (1991), Maquiera, Megginson, and Nail (1997) or Erel, Jang, and Weisbach (2012). Evidence on bargaining power is documented in Bradley, Desai, and Kim (1988), Aktas, De Bodt, and Roll (2010), Betton and Eckbo (2000). There is further evidence on the effects of bidder governance in Shleifer and Vishny (1989), Lang, Stulz, and Walkling (1991), Harford (1999), Masulis, Wang, and Xie (2007), and on seller governance in Stulz, Walkling, and Song (1990) and Moeller (2005).

provisions), such that both are determined independently from each other. We will call this the *independence hypothesis*. This view is based on legal literature that generally describes the negotiation process in corporate acquisitions as a negotiation game with two distinct stages (e.g., Choi and Triantis (2012) Freund (1975), and Frankel (2005)). While the price is negotiated and fixed in the first stage, contract design is negotiated in the second stage. As Choi and Triantis (2012, p.1690) argue: "[Contract] terms are usually settled without adjustments to the price." This lack of price adjustment from contract provisions indicates, according to this view, that contract provisions either have no value implications, or are only traded off against each other.

Conversely, the second view argues that the distinct timing of negotiations does not prevent that pricing and contract design are being determined jointly. This view rather holds that contract design affects pricing as the price is determined in expectation of a set of contract provisions that will later be included (Schwartz and Scott (2003), Choi and Triantis (2012)). If these expectations are not met, the initial price will be adjusted. We will consider this the *feedback hypothesis*.[4]

We will shed light on these two conflicting views using a proprietary dataset of contracts that are underlying acquisitions of 146 privately held targets. Private acquisitions form an interesting empirical set-up for our analysis as contracts in such deals tend to be highly negotiated. In contrast to most public acquisition contracts, private transactions typically also contain legal obligations that extend beyond the target transfer date. To illustrate, buyers can, on average, claim damages from sellers up to 1.5 years after the transfer.

To analyze whether contract design affects pricing, we first isolate the provisions that are most price relevant. Broadly speaking, acquisition contracts contain provisions that (i) facilitate legal elements of a deal; (ii) mitigate adverse selection or moral hazard concerns; and (iii) allocate risk between buyers and sellers.

The first set of provisions typically only addresses legal formalities and definitions and have a limited value impact. In contrast, the second set reduces economic problems

[4] Supporting evidence for this view comes from public acquisitions, where it has been show that a relation between premiums and walk-away rights in acquisition contracts exists (Denis and Macias (2010), Officer (2003), and Bates and Lemon (2003)).

and, consequently, can increase the joint surplus of both parties. The *feedback hypothesis* holds that such provisions should be associated with higher premiums. Consider, for example, that contracting parties have agreed to split the gains from trade equally. Any increase in those gains due to contract design should then, according to the *feedback hypothesis*, accrue proportionately to sellers, implying an increase in premium. Conversely, the *independence hypothesis* predicts no relation.

The third set of provisions distributes value between contracting parties, because the allocation of risk generally imposes costs on the risk-bearer, while benefiting the insured. Whether such value distribution is reflected in prices depends on the ex-ante expectations of both contracting parties. On the one hand, the *independence hypothesis* suggests that value allocation exclusively occurs through pricing, whereas contract design is only aimed at maximizing joint surplus (Coase (1937), Posner (1969) and Schwartz and Scott (2003)).[5] According to this view, provisions that allocate risk should be traded off against each other within the contract, without any interaction to pricing. On the other hand, according to the *feedback hypothesis*, contracts do affect the distribution of value, and this should be reflected in premiums. This view is supported by legal literature that finds that the bargaining position of buyers and sellers is a key factor in determining contract design, suggesting that contracts are employed for value distribution.[6]

To differentiate between value increasing and value distributing provisions, we consider both a strong-form of the *feedback hypothesis,* which holds that both types of provisions should reflect onto pricing, and a weak-form which suggests that this only holds for value increasing provisions. In contrast, the *independence hypothesis* states that none of the provisions are related to pricing.

Empirically testing the relation between contract design and pricing is challenging due to unobservable deal characteristics which could affect both factors simultaneously. For example, information asymmetry poses downward pressure on prices, but is associated with more warranties in contracts, such that this affects both variables in

[5] Schwartz and Scot (2003, p. 554) argue: "Bargaining power instead is exercised in de division of the surplus, which is determined by price terms. Parties jointly choose the contract terms that maximize the surplus, which the price may then divide unequally."

[6] ABA Mergers & Acquisitions Committee (2010) confirms this in the notes to the Model Stock Purchase Agreement, as they consider the "relative negotiation positions of the parties" one of the main determinants of contract design.

opposite directions ((Akerlof (1970) and Grossman (1981)). If such characteristics are not fully controlled for econometrically, simple OLS estimations of acquisition pricing on contract design could lead to biased coefficients.

We identify the causal effect of contract design on pricing by employing instrumental variables (IV) models which exploit partially exogenous variation in contract design. The exogenous variation is obtained from law firms that provide the same first draft version of an acquisition contract across clients. These drafts are generally based on law-firm specific internal specimen contracts (Miller (2008), Coates (2001)). Importantly, final contracts are typically not fully customized to deal characteristics, implying that final contracts still contain some provisions from the initial specimen contracts (Armour (2004) and Kahan and Klausner (1997)). As specimen drafts vary across law firms, variation in contract design is partly driven by the law firms that provided the first drafts.[7] Our analysis will thus exploit this variation through the use of law firm fixed effects as instruments for contract design.

As measures for contract provisions that *increase value*, we consider clauses that mitigate adverse selection (warranties) and agency concerns (covenants). Adverse selection concerns arise when sellers are better informed about target quality than buyers, and buyers fear overpaying. Warranties are quality statements that sellers make, which can serve as signals about target values ((Akerlof (1970) and Grossman (1981)). Agency concerns arise if there is time between the signing of the contract and the transfer of the target (closing). Whereas the price is fixed contractually, sellers remain in control of the target during this period, and can extract assets from targets. Covenants can mitigate this concern by restricting the actions sellers may engage in until closing.

As provisions that *distribute value*, we consider clauses that affect risk allocation. The first three provisions define the extent to which warranties grant insurance in addition to signaling quality. Warranties provide insurance to buyers when they relate to items of which sellers are unaware, such that sellers accept the risk of paying damages in case that warranty is violated. Sellers can prevent bearing this risk in various ways, for example, by reducing the scope of warranties through defining that they are only

[7] Supporting this, Karsten (2013) shows that fixed effects of the law firms that provide the first contract drafts significantly affect both warranties and covenants.

violated if the seller was aware of that violation, or if a warranty is untrue "in a material respect." Such qualifiers reduce the enforceability of warranties, and thereby shift risk to buyers. Moreover, sellers can limit their exposure to risk by disposing of their available capital prior to any damage claim. To ensure that sellers maintain sufficient funds to cover damages, buyers can demand that part of the purchase price is secured, for example, by placing it in an escrow account. To reflect the risk allocated to sellers through warranties, we consider (i) the fraction of warranties without a knowledge qualifier, (ii) whether warranties need to be fully true (rather than only materially true), and (iii) the fraction of the payment that is secured for potential future claims.

Whereas these provisions refer to risks of existing situations at the time of signing, another relevant risk refers to adverse events occurring between signing and closing. In principle, buyers bear this risk, as they are contractually obliged to complete the transaction and pay the agreed price. To prevent this, contracts may include a material adverse change (MAC) clause, entitling buyers to cancel the deal in case such an adverse event happens.. Including a MAC shifts this risk to sellers. As with warranties, the scope of the MAC is determined by the number of exceptions to this rule. As such, to reflect the allocation of risk relating to events between signing and closing, we create an index which increases as more of the interim-period risk is borne by sellers.

Our findings support the weak-form of the *feedback hypothesis*. Both warranties and covenants significantly increase premiums paid in acquisitions, which we measure using the market-to-book value of the target (as in e.g., López-de-Silanes (1997) and Masulis and Nahata (2011)). Our IV estimates suggest that each additional warranty causes a 1% increase in the premium, and each additional covenant even causes an increase of 11%. This suggests that buyers pay for protection granted against adverse selection and agency concerns with higher prices. In contrast, value distributing provisions do not affect prices, suggesting that parties do not anticipate value allocation through contract design when setting prices.

To obtain a better understanding of the price impact from warranties and covenants, we next analyze whether the mitigation of some concerns is more valuable than that of others. To this end, we categorize these provisions according to the economic and legal concerns that they address. We then test whether there is

heterogeneity in the impact across the categories. We find that the positive impact from warranties on premiums is almost exclusively driven by warranties that relate to target financials and intellectual property rights. Conversely, covenants in nearly all categories significantly relate to premiums; the strongest impact comes from covenants on divestments. Interestingly, categories with the strongest price impact also derive a relatively high explanatory power from the economic deal environment (Karsten (2013)). This indicates that provisions with high value implications are mostly driven by economic deal characteristics.

Our analysis has so far not looked at the effect of bargaining power, which is crucial if contract design is reflected into pricing. Specifically, bargaining power determines the division of the joint surplus and, as a result, the impact that an increase in this surplus should have on pricing. Contract-price feedback should not occur if sellers have no bargaining power, as any value increase would then be captured by buyers. As such, the relation between warranties (or covenants) and pricing should be larger in deals with stronger sellers. Similarly, strong sellers should be able to demand a higher compensation for bearing additional risk through value distributing provisions. To investigate these predictions, we split the sample based on different proxies for seller bargaining power and re-estimate our IV models on these subsamples.[8] We find that the impact of *value increasing* provisions on pricing is higher for most subsamples with high seller bargaining power. Moreover, we find that even some *value distributing* provisions positively affect premiums when sellers have high bargaining power.

Our findings contribute to the literature that analyzes variation in acquisition contracts, such as Coates (2001, 2012), Karsten (2013), and Choi and Triantis (2010), by showing that such variation reflects into pricing. Moreover, we also contribute to Denis and Macias (2012), Officer (2003), and Bates and Lemmon (2003), who show pricing effects of walk-away rights in contracts. Finally, our paper contributes to the literature on acquisition premiums by documenting an additional, and usually unobserved, determinant of these premiums.

[8] In this analysis, we restrict the warranties to the financial account warranties, as this category has the strongest impact on premiums.

The paper will proceed as follows. Section 3.2 discusses the negotiation process surrounding private acquisitions. Section 3.3 describes the data, Section 3.4 discusses the instrument and empirical methodology, Section 3.5 provides the main empirical analysis, and Section 3.6 concludes.

3.2 Negotiations on Premiums and Contract Design

The intensity of feedback from contract design to pricing is to a large extent affected by the negotiation process in corporate acquisitions. In principle, negotiations on acquisitions can take any form. However, two patterns are frequently observed.[9]

The first pattern arises typically in controlled auction deals, where sellers (or their advisors) invite various potential buyers to bid for the target. Sellers provide those bidders, who have indicated their interest, with a proposed acquisition contract, which includes an initial set of contract provisions. Following this, bidders submit offers that contain bid prices as well as adjustments to the proposed contract. As a result, in auctions, bidders set prices in combination with amendments to contract provisions. After these first bids, sellers may enter into further negotiations with one or more selected bidders, covering both contract provisions and price. Consequently, contract design and prices are simultaneously discussed, allowing for interaction between them.

However, more commonly, acquisitions are based on one-on-one negotiations, where sellers negotiate with only one potential buyer. Typically, these negotiations take the form of a game with two distinct stages. The first stage begins when a seller and buyer communicate their mutual interest in a transaction. To specify this mutual interest, an indication of the price is typically determined in this first stage, combined with procedural matters, such as confidentiality of information and exclusivity of negotiations.[10] Parties then move to the second stage in which contract design is discussed, whereas the price is generally considered fixed. However, negotiations over contract design may still affect prices, for example, because prices could be set in

[9] See Frankel (2005), Karsten and Sautner (2013), and Choi and Triantis (2012) for discussions of standard negotiation processes in corporate acquisitions.

[10] Parties may formalize these agreements in a non-binding Letter of Intent. Even though this Letter of Intent is not binding for the agreed price, the exclusivity and confidentiality arrangements are binding.

expectation of contracts containing a given set of provisions (Schwartz and Scott (2003), Choi and Triantis (2012)).[11] Alternatively, if negotiations fail to include the expected provisions in the contract, adjustments to prices may occur (Choi and Triantis (2012)).

In sum, contract design is generally not negotiated simultaneously with prices, as stressed by the *independence hypothesis*. Nonetheless, through ex-ante expectations or ex-post adjustments, contract provisions could still affect pricing, as suggested by the *feedback hypothesis*.

3.3 Data and Descriptive Statistics

3.3.1 Sample Construction

Our analysis is based on a proprietary dataset of 146 acquisition contracts that are underlying acquisitions of private targets. These contracts have been made available by one of the largest law firms in The Netherlands, specialized in corporate law and mergers and acquisitions. The starting point is all acquisitions of privately held targets that this law firm has advised on between 2005 and 2010, yielding an initial sample size of 300 transactions. From this initial sample, deals are excluded where important contract information was missing, reducing the sample to 151 contracts.[12] As financial data is missing for 5 targets, the final sample consists of 146 transactions. The contracts contain detailed information on provisions used, as well as identities of targets, buyers and sellers.[13] Moreover, the business logo on the layout of each final contract allows us to identify the law firm on whose specimen that contract is based.

We complement these contract data with financial data of buyers, sellers and targets. For buyers and sellers, financial data have been obtained from Amadeus or their

[11] To illustrate, Choi and Triantis (2012, p.1690) state: "The parties would probably have an expectation of these terms when they struck a price in the first stage."

[12] This sample is essentially the same as used in Karsten (2013). Please refer to that paper for more information on sample construction, characteristics, and sample selection concerns.

[13] Note that, as these are private acquisitions, sellers and targets are separate identities, where sellers can, for example, be corporations selling a division, private equity funds selling a company, or families selling their family business.

financial statements, and are based on the year preceding the transaction.[14] Such annual reports are not readily available for targets, as they are privately held. Financial data on targets have been obtained from three sources: (i) financial accounts of buyers or sellers; (ii) Amadeus or national trade registers; and (iii) appendices to the contracts.[15]

Table 3.1 Panel A provides summary statistics of our sample, with variable definitions provided in Appendix A-3.1. The average transaction value is €229 million. However, this is highly skewed with a median of €36 million. Targets have, on average, a 14% return on assets (EBIT/Assets) and a leverage ratio of 60%. Moreover, even though targets are privately held, 44% of the bidders and 35% of the sellers are publicly listed. Finally, about 22% of the deals in our sample were organized through a controlled auction.

3.3.2 Measuring Acquisition Premiums

The ideal benchmark for an acquisition premium is the "pre-offer secondary market price of the target" Eckbo (2009). As this is essentially unobservable, most research relies on the share value at some date prior to a bid (Betton, Eckbo, and Thorburn (2009)). However, as our sample only concerns private targets, also this reference is unattainable. Following López-de-Silanes (1997) and Masulis and Nahata (2011), we measure the acquisition premium as the implied market-to-book value of the target, defined as follows:[16]

$$\text{Acquisition premium} = \frac{(\text{price paid for shares}/\%\ \text{shares in deal}) + \text{book value of liabilities}}{\text{book value of assets}}$$

Table 3.1 Panel A shows that the average (median) premium is 244% (155%), which is comparable in magnitude to other studies using similar measures. To illustrate, based on public acquisitions, Betton, Eckbo and Thorburn (2009) find an average premium of 146.1%. Similarly, Moeller (2005) finds mean (median) premiums of 131%

[14] For private equity buyers or sellers, we use the total assets under management of the whole private equity firm as a measure of asset size.

[15] We obtained the financial data from the buyer's or seller's accounts in 32% of the deals, from Amadeus (trade registers) in 30% , and from the contract appendices in 37%.

[16] In the analysis, this variable is winsorized at 2% to avoid that the results are driven by outliers. As robustness checks, we will consider other premium measures.

(128%).[17] Figure 3.1 Panel A plots the distribution of the premiums.[18] Appendix A-3.2 Panel A documents the distribution of the premium across years and target industries. In spite of the financial crisis, the median acquisition premium was highest for targets acquired in 2008.

3.3.3 Measuring Contract Provisions

Value Increasing Provisions

Contract provisions can affect pricing when they increase the total joint surplus, for example by mitigating economic concerns between buyers and sellers. To reflect value increasing contract design, we consider provisions that address adverse selection and agency concerns.

First, when sellers have private information about target quality, an adverse selection problem can occur, resulting in a downward adjustment of buyer valuation (Akerlof (1970)). Sellers can mitigate this by granting guarantees about target quality (warranties), with a commitment to repay part of the purchase price in case any of these is violated. Thereby, warranties can serve as signals for target value, reducing the information asymmetry (Grossman (1981) and Spence (1977)). For example, a frequently used warranty is that the target's financial accounts give a fair representation of its financial condition.[19]

Second, agency concerns can arise when there is time between the date of contract signing and the transfer date. This time might be necessary, for example, to apply for competition or regulatory approvals. Whereas the price is fixed contractually, sellers remain in control of targets until closing, allowing them to extract private benefits or shirk in managing the targets' operations. Sellers can commit to refrain from these actions by including covenants, similar to those in debt or venture capital contracts. [20] For example, covenants can state that targets may not make capital expenditures exceeding a given amount, or that no dividends may be paid.

[17] Based on acquisitions of private targets, Masulis and Nahata (2011) report mean (median) premiums of 1703% (469%), but targets in their sample are substantially smaller than in our sample.
[18] In robustness check with the log of the premium, we show that this skewness does not drive our results.
[19] Karsten (2013) gives an overview of frequently used warranties and covenants in acquisition contracts.
[20] See Kaplan and Strömberg (2003), Murfin (2012), and Bradley and Roberts (2004).

To measure the protection granted through these provisions, we consider the number of warranties and covenants included in the contract (similar to Murfin (2012), Gompers and Lerner (1996), and Lerner and Malmendier (2010)). Table 3.1 Panel B reports summary statistics of this. The average contract contains 98 warranties and 14 covenants.[21] Figure 3.1 plots the distribution of the warranties (Panel B) and covenants (Panel C), documenting that there is plenty cross-sectional variation across contracts.[22]

In addition to considering warranties and covenants in the aggregate, we analyze the impact of specific categories of these provisions, with categories defined by the economic and legal concerns that the provisions address (Miller (2008)).[23] This is potentially interesting when mitigating some concerns is more valuable than others. Panel C of Table 3.1 lists these categories and reports summary statistics of the number of provisions per category. There is considerable variation in the average number of warranties (or covenants) across categories. For example, the average contract contains 24 warranties on target financials, whereas it only contains 3 warranties related to the target's insurance contracts.

Value Distributing Provisions

Next to mitigating economic issues, contract provisions can have distributional consequences, for example, by allocating risk surrounding acquisitions. Two types of risk are relevant in corporate acquisitions.

The first risk refers to situations that exist at the time of signing, but of which neither buyers nor sellers are aware. For example, the target's main customer might be planning to terminate the business relation with the target. Whereas sellers are typically better informed about the likelihood of such a situation existing, because of their communications with that customer, sellers might still not be 100% certain. Granting warranties on such uncertain target aspects effectively implies providing insurance to buyers (Emons (1989) and Heal (1977)). Sellers can prevent this by refusing certain

[21] This is based on the full sample, including contracts with zero covenants. Therefore, the number is smaller than the average number of covenants reported in Karsten (2013).
[22] Panel C of Figure 3.1 only shows the distribution of contracts with at least one covenants. In total, there are 51 contracts with zero covenants. These are mostly deals where signing and closing were simultaneous.
[23] For the warranties, Miller (2008 p. 51) considers these the categories that the "the buyer's lawyers should look for to avoid bombs". For the covenants, these categories are based on the clauses in a standard form contract provided in Miller (2008).

warranties. However, as warranties also serve as valuable signals. Therefore, contracting parties generally use affiliated provisions, which determine the scope and enforceability of warranties, to restrict the insurance provided.

First, sellers can restrict the scope of each individual warranty, by adding the qualifier: "so far as the seller is aware". As a result, buyers cannot claim damages for events of which sellers were unaware, thereby excluding the insurance part of the warranty. Consequently, to reflect the risk borne by sellers, we measure the fraction of total warranties which is granted without this qualifier (%Warranties w/o qualifier). Second, sellers can limit the enforceability of warranties by including an overarching qualifier stating that warranties are only violated if they are untrue "in a material respect." This implies that only material violations of warranties can be enforced (see Kling, Simon, and Goldman (1996)). As such, we use a dummy variable which equals one if this qualifier is not included, and zero if it is included (Warranties Fully True). Third, enforcing warranties is only valuable if sellers have sufficient funds available at the time of a claim to compensate any damages. To prevent that sellers no longer have access to capital, buyers can secure part of their payment by placing it in an escrow account, by demanding a bank guarantee, or by setting a reserve requirement. We capture this secured payment with the fraction of transaction value that is secured contractually (%Payment Secured). Table 3.2 Panel B reports summary statistics of these provisions. The average contract contains 87% unqualified warranties, implying that an average of 13% of warranties is qualified with: "so far as the seller is aware". In addition, in 83% of the contracts, warranties are required to be fully true, and, on average, 5% of transaction value is secured for potential claims. Figure 3.1 reports histograms of the %Warranties w/o Qualifier (Panel D) and %Payment Secured (Panel E).[24]

The second type of risk that is relevant in acquisitions relates to events occurring between signing and closing (interim period). If any event reduces target value in this period, buyers are in principle obliged to proceed with the transfer and pay the agreed price. They can prevent this by including a MAC clause, which states that buyers are entitled to cancel the deal in case of a material adverse change to targets. However, the

[24] The histogram of %Payment Secured is based on the 49 contracts where a nonzero amount is secured. In 102 contracts, no money was secured at all. As "Warranties Fully True" is a dummy variable, we do not show the histogram of this variable.

scope of the MAC clause is restricted by the exceptions. Contracts may contain a list of situations, for example natural disasters or acts of terrorism, that should be considered exceptions to the MAC. Panel C of Appendix A-3.2 provides examples of frequently used MAC exceptions. As a result, if target value falls due to such an event, the buyer is still obliged to proceed with the transaction. Whereas including a MAC clause allocates the interim-period risk to sellers, each exception shifts this partly back to buyers. To reflect this, we use an index (MAC Strength Index). This index equals 100% for contracts that include a MAC clause without any exceptions, and 0% if contracts include no MAC at all. The range in between reflects the breadth of the MAC included, where a higher number of exceptions moves the index towards 0%.[25] The average MAC Strength Index is 28%.

3.4 Identification Strategy

3.4.1 Instrumental Variables: Law Firm Fixed Effects

Ordinary least squares (OLS) regressions of acquisition premiums on contract design shed light on correlations between these terms, but we need to address endogeneity concerns to make a causal inference. As both contracts and premiums could be affected by unobservable deal characteristics (e.g., information and agency concerns), simple OLS regressions would show biased results.

To address this, we perform an instrumental variables analysis. As instrumental variables, we exploit variation in contract terms driven by law firms providing the first draft of the contract. In corporate acquisitions, both parties typically consult with law firms when negotiating on contract terms. One of the law firms involved provides a first draft of the contract, which will then form the basis for negotiations. This first draft is usually a combination of the internal standard specimen contract used by the law firm and some deal specific terms (Miller (2008), Coates (2001)). Whereas these first drafts only form the starting point for negotiations, there is a strong path dependence and they are rarely fully customized to deal characteristics (Armour (2004), Kahan and Klausner

[25] Each exception is assigned a weight of 1/13, as the contract with the maximum number of exceptions contains 13 exceptions. For deals which include a MAC clause, the index is estimated as: [1-(1/13 * Number of Exceptions)].

(1997)). Consequently, if these internal specimens vary across law firms, and final contracts partly reflect their first drafts, then part of the variation in contract terms is driven by the styles of the law firms providing those first drafts.

Moreover, variation driven by these specimens could affect premiums in two ways. First, when the specimens are inconsistent with expectations, prices could be adjusted as a result. Second, expectations of clients are typically based on these specimen contracts. Clients tend to have historically determined long-term relations with law firms. For example, when looking at clients in our sample with prior deal experience, we find that -in 80% of the deals- the advising law firms had already advised these clients at least once before.[26] As a result, contracting parties have typically been previously confronted with these specimens, such that they set their expectations accordingly.

We exploit this variation by using dummy variables for all law firms providing first drafts (Law Firm Fixed Effects) as instrumental variables. In total, our sample contains 27 law firms. The law firm which has provided the data has drafted the first version in 90 deals.[27] The remaining law firms have, on average, provided two first drafts each.

3.4.2 Validity of the Instruments

Relevance of the Instruments

Instrumental variables analysis provides consistent estimators if two conditions are met. First, the instrumental variables must be sufficiently correlated with the endogenous variables. Table 3.2 reports regressions that test whether drafting law firms significantly influence variation in warranties and covenants, after controlling for economic determinants of premiums. Supporting the findings by Karsten (2013), Law Firm Fixed Effects are jointly significant for both models. Appendix A-3.3 reports the first stage regressions for the warranties and covenants per category.[28] Across all categories, Law Firm Fixed Effects are jointly significant at the 1% level.

[26] This is based on Merger Market data and refers to the five years preceding the deal.
[27] These numbers differ slightly from Karsten (2013) as five deals are excluded from our sample due to missing information on target financials. In Karsten (2013), there are 28 drafting law firms, and our law firm had drafted 94 contracts.
[28] These regressions also control for the economic determinants of premiums (not reported).

However, as the model contains more instruments than endogenous variables, a "weak instrument" problem could arise if not all instrumental variables are sufficiently correlated with the endogenous variable (Bound, Jaeger, and Baker (1995)). If this occurs, IV-coefficients may be biased towards OLS estimates. According to Staiger and Stock (1997), instruments are considered weak when their *F*-statistic in the first stage regression is less than 10. Table 3.2 reports first stage *F*-statistics in our model well above this critical level. However, the criterion set by Staiger and Stock (1997) is based on distributions with 10 to 20 observations per instrument. As our analysis contains 27 instruments on 146 observations, this benchmark may not be applicable.

To test whether the number of instruments might pose a weak instrument problem, we perform a reduced rank test suggested by Kleibergen and Paap (2006). Table 3.2 reports the resulting Kleibergen-Paap LM rank test-statistics (Kleibergen-Paap χ^2 -test) and the associated *p*-values. The null-hypothesis in this test is that the model is weakly identified, such that rejecting the null indicates sufficiently strong instruments. However, as we cannot reject the null hypothesis, weak instruments are a valid concern in our methodology. We mitigate this concern by considering two alternative sets of instrumental variables, that reflect the styles of law firms using fewer variables. Section 3.5.4 will discuss these alternative instrumental variables in detail and show that our main results are robust to alleviating the weak instruments problem.

Exogeneity of the Instruments

The second condition for consistent IV-estimates is that instruments are exogenous, implying that drafting law firms only affect premiums through variation in warranties and covenants. This condition would be violated if deals are allocated to law firms on the basis of unobservable deal characteristics. Several tests suggest that this is unlikely to hold in our sample.

First, as discussed above, deals appear to be allocated to law firms based on historically established relations between clients and law firms, rather than on deal characteristics. Legal literature suggests that clients engage in such long term relations for reasons related to information, agency, or trust (e.g., Coates et.al. (2011) and Gilson, Mnookin, and Pashigian (1985)). This is supported by our data, as 80% of the clients in

our sample who have been engaged in acquisitions before, had requested advice from the same law firm in prior transactions. On average across those established relations, clients had already been advised by this law firm on seven deals. This suggests that specific *deal characteristics* do not drive the law firm choice, as clients choose the same law firm for a variety of deals.

Second, deals do not seem to be allocated based *client characteristics* either. Karsten (2013) documents that observable client characteristics are similar across law firms with a high versus low tendency to include warranties or covenants. Moreover, law firms significantly affect warranties and covenants in that study after controlling for observable client characteristics, and even for client fixed effects.[29]

Last, we perform a Sargan-Hansen test whether the error terms of the IV-model are uncorrelated with the Law Firm Fixed Effects (Sargan (1958) and Hansen (1982)). Table 3.2 reports the Hansen J-statistics (Hansen χ^2-test). The null hypothesis is that the exclusion restriction is valid, such that failure to reject this supports the validity of the instruments. Table 3.2 shows that this holds for all types of provisions, and Appendix A-3.3 confirms this for the categories of warranties and covenants.

3.5 Empirical Results

3.5.1 Acquisition Premiums: Baseline Regression

We start our empirical analysis with a baseline regression of the acquisition premium on its potentially important economic determinants. We control for: (i) target characteristics, (ii) bargaining power, (iii) governance, and (iv) information and agency concerns.

As target characteristics, size (book value of assets), return on assets (EBIT/Assets), leverage, and growth potential are included. As a proxy for growth potential, we use a dummy variable which equals one when the target industry is in a

[29] Please refer to Karsten (2013) for a discussion of these measures and robustness checks.

high R&D industry (Masulis and Nahata (2011) and Denis and Macias (2012)).[30] Second, to control for the relative bargaining power, four dummy variables are included which equal one if: (i) the deal took place during or after the financial crisis (Aktas, De Bodt, and Roll (2010)); (ii) the deal was organized as an auction (Boone and Mulherin (2007) and Aktas, De Bodt, and Roll (2010)); (iii) the first draft of the contract was provided by buyer's advisors (Molod (1994)); and (iv) the buyer owned part of the shares prior to the acquisition, i.e., a toehold deal (Betton, Eckbo and Thorbun (2009)). We also include the relative size of the buyer to the seller (in book value of assets) to reflect the bargaining. Third, to reflect the governance of buyers and sellers, two dummy variables are included that, respectively, equal one when the seller is publicly traded, and when the buyer is publicly traded.[31]

Finally, we proxy for information asymmetries and agency issues with two dummy variables, which equal one if: (i) the buyer is located in a different country than the target (cross-country deal); (ii) the deal was an asset deal. Contracts in asset deals contain a list of the assets and liabilities to be transferred, reducing information asymmetry on the target's balance sheet. Moreover, to capture the expected time between signing and closing, the number of required approvals is included.

The regression results are reported in Table 3.3 and indicate that premiums increase with target's profitability and growth potential, but fall in target size. Moreover, contrary to predictions from bargaining power, premiums seem higher when buyers are large relatively to sellers. Together, these factors explain 42% of variation in premiums.

3.5.2 Acquisition Premiums and Contract Design

Next, we analyze whether contract design also affects premiums. To this end, Table 3.4 reports OLS regressions (Panel A) and 2SLS regressions (Panel B) of acquisition premiums on the contract design measures, controlling for the economic determinants

[30] Industries are considered high R&D industries if they are in the top 5 of the Fama French 48 industry classification based on median R&D expenses to assets. The industry median levels are estimated based on Compustat data. Appendix A-3.1 describes this variable in more detail. Appendix A-3.6 also controls for industry fixed effects.

[31] Morck, Shleifer, and Vishny (1990) show that poor governance might result in bidder management engaging in bad deals or overpaying. Conversely, Moeller (2005) shows that poor governance of the seller could lead to acceptance by seller management of low offer prices.

described above.[32] Combined, the results provide support for the *feedback hypothesis*. In the full sample, we find only evidence in support of the weak form of this hypothesis. However, in samples with strong seller bargaining power, there is some support for the strong form of the *feedback hypothesis,* suggesting that both value increasing and value distributing provisions affect premiums.

Value Increasing Provisions

The regressions that test the impact from warranties and covenants on acquisition premiums support *feedback hypothesis.* Based on the OLS model, Panel A in Table 3.4 shows that warranties and covenants are positively related to premiums, significant at the 10% level. However, as unobservable characteristics might push premiums in opposite directions to contract provisions, these estimates could underestimate the underlying relation. Confirming this, the 2SLS estimates, reported in Panel B of Table 3.4, indicate a stronger impact from warranties and covenants on premiums. Each additional warranty is associated with a 1% increase in premium, and each additional covenant with an 11% increase. This suggests that contracting parties anticipate a given contract design when they determine price levels, or that prices adjust as value is generated during contract negotiations. Figure 3.2 depicts the relation between premiums and warranties in partial scatterplots, and Figure 3.3 shows partial scatterplots of the relation between premiums and covenants. The Panels B of both figures show partial scatterplots of the IV-estimation model, implying that the first-stage predicted value of the contract provisions is used as explanatory variable.[33]

Value Distributing Provisions

These results support the view that higher joint surplus is associated with higher premiums. However, this interaction is less pronounced for provisions that affect the distribution of the surplus, implying that we only find support for the weak form of the *feedback hypothesis.* The results in Table 3.4 indicate that, in spite of substantial cross-

[32] As data is missing for some observations, the regressions are on fewer observations.

[33] These partial scatterplots seem to suggest that outliers might be affecting the relation. To show that these distributions do not contain outliers, Panel C of both figures documents the distributions of the predicted warranties (Figure 3.2) and covenants (Figure 3.3). These histograms indicate that there are not outliers in the predicted value, similar to the true distributions depicted in Figure 3.1.

sectional variation in risk allocation, this does not seem to reflect onto premiums. Both OLS and IV estimates of the coefficients are not significantly different from zero.

There are several potential explanations for this. First, as suggested by the independence hypothesis, different risk allocating provisions could be traded off against each other within the contract, such that the final contract is "risk neutral". However, this seems not to be supported by the data, as Panel B of Appendix A-3.2 shows that the risk allocating provisions are all positively correlated with each other, indicating that contracts that allocate more risk to sellers seem to do so on all fronts. Alternatively, contracting parties could base their expectations purely on the joint surplus, as suggested by Schwartz and Scott (2003), and underestimate or be unaware of the potential value implications from shifts in risk allocation.[34]

As a third explanation, shifts in risk allocation driven by law firms (or lawyers) could be within a specified range of expectations, such that adjustments are not deemed necessary. Choi and Triantis (2012, p. 1691) argue: "Although the first stage agreement [i.e., price, ed.] is not legally binding, there would be non-legal costs to allowing the deal to collapse after this point. This leaves lawyers with meaningful space within which to bargain on behalf of their clients." Supporting this, Karsten and Sautner (2013) document that lawyers with more expertise can negotiate a risk allocation that is more favorable for their own client.

Finally, as both price terms and risk allocating contract provisions are driven by the relative bargaining power of buyers and sellers, the lack of feedback could reflect that sellers have insufficient bargaining power. With low bargaining power, sellers might have to grant both high protection and accept a low premium, offsetting the positive effect of these provisions in other contracts. Section 3.5.3 will examine this relation with bargaining power further.

[34] However, Denis and Macias (2010) show that MAC conditions in public acquisitions do relate to premiums, suggesting that, if these terms are jointly negotiated, risk allocation is recognized in premiums.

Warranties and Covenants per Category

The impact from warranties and covenants on premiums suggests that value increasing contract provisions are reflected in pricing. However, these provisions address a wide array of concerns, of which some might be more price-relevant than others. To test this, we next analyze whether the impact on premiums varies across different types of provisions. We categorize warranties and covenants based on the concerns they address, based on Miller (2008). Table 3.5 reports the IV-regressions of the acquisition premiums on these categories separately, controlling for the economic determinants. [35]

The results indicate that there is indeed heterogeneity in pricing of contract provisions. For the warranties, Panel A shows that the impact on the premium is driven by the warranties on financial accounts and intellectual property rights. Including an additional warranty on financial accounts increases the premium with 6% and each additional IP-related warranty increases the premium with 8%. In contrast, the impact of covenants on premiums is quite consistent across categories. One additional covenant significantly increases the premium across all categories except for those on litigation. The highest impact is derived from covenants on divestments.

Together, this supports the view that the value impact of provisions varies across warranties, and to some extent, covenants. Interestingly, categories with the strongest price impact also derive a relatively high explanatory power from the economic deal environment (Karsten (2013)). This suggests that provisions with high value implications are mostly driven by economic deal characteristics.

3.5.3 Impact of Bargaining Power

The results so far have not yet accounted for the impact of bargaining power on the relation between contract design and pricing. However, as premiums determine the division of value between buyers and sellers, any feedback from contract design is conditional on the relative bargaining positions. For example, warranties and covenants may increase the joint surplus, but only strong sellers are able to capture part of this

[35] Appendix A-3.4 reports OLS regression results from acquisition premiums on warranties and covenants per category.

added value, resulting in higher premiums. Similarly, strong sellers should be able to demand a higher compensation for bearing additional risk.

To investigate these predictions, we split the sample based on five different proxies for seller bargaining power and re-estimate our IV models on these subsamples.[36] As a first proxy, we consider whether the right to provide the first contract draft was obtained by the seller or buyer. Supplying the first draft provides a first mover advantage (Molod (1994)), such that it is likely that the stronger party claims this right. In our sample, 79 contracts were supplied by sellers and 62 by buyers, indicating that there is no default allocation of this right. Second, we consider deals prior to 2008 relative to deals occurring during or after the financial crisis (Aktas, De Bodt, and Roll (2010)). This is based on the assertion that potential buyers were scarcer during the crisis, increasing their bargaining power. Third, we split the sample according to the asset size of buyers relative to sellers, with the cutoff being at equal size. In 65 deals, sellers were larger, and in 72 deals buyers were larger. Fourth, we consider deal experience over the prior five years, based on Merger Market data. We split the sample according to whether buyers or sellers have engaged in more deals. Finally, we assess whether sellers have obtained advice from investment banks. Banks can improve bargaining positions by advising sellers on negotiating strategies (Kale, Kini, and Ryan (2003)).

The regressions are reported in Table 3.6. Our results suggest the following findings. First, the impact of value increasing provisions is stronger for subsamples with high seller bargaining power. Whereas financial accounts warranties significantly affect premiums in all samples with high seller bargaining power, this impact is mostly insignificant for samples with low seller bargaining power. Similarly, the significance of the impact from covenants on premiums is stronger for all subsamples with high seller bargaining power. This provides further support for the *feedback hypothesis*, as it implies that, when sellers can capture a sufficiently large fraction of the surplus, changes in the surplus are reflected in premiums.

Moreover, there is initial support for the strong form of the *feedback hypothesis*, as some of the value distributing provisions significantly affect pricing in subsamples with

[36] In this analysis, we restrict the warranties to the financial account warranties, as this category has the strongest impact on premiums.

high seller bargaining power; relatively large sellers seem to receive higher compensation for bearing additional risk than relatively smaller sellers. In a sample where seller size exceeds buyer size, the price-impact is significant across all risk allocation provisions. Conversely, in samples with low seller bargaining power, this feedback is insignificant. Interestingly, in spite of the buyer-friendly market conditions during the crisis, the MAC Strength Index and Warranties Fully True condition have a stronger impact on premiums in contracts signed after 2008. This could indicate that the financial crisis confronted buyers and sellers with the risks involved in acquisitions and the value of these provisions, such that the "price" of these provision increased.

3.5.4 Alternative Instrumental Variables

Combined, the above results suggest that contract provisions that increases the joint surplus (i.e., warranties and covenants) affect premiums paid in corporate acquisitions, in favor of the *feedback hypothesis*. A first concern that could be raised is that these results are driven by the amount of instruments, which could create a weak instrument problem. As discussed in Section 3.3, weak instruments is a valid concern for our methodology.

To show that the relation between contract provisions and pricing is not driven by weak instruments, we re-estimate the analysis on two sets of alternative instrumental variables. For these alternative variables, we again exploit the variation in contracts driven by the styles of law firms that have provided the first contract drafts. However, rather than using individual law firm dummies, we capture their styles in fewer variables.

Law Firm Style Dummy

As a starting point, we consider the analysis in Karsten (2013), where variation in warranties and covenants is related to economic determinants and Law Firm Fixed Effects.[37] Based on the coefficients of the fixed effects in those regressions, law firms are ranked according to their tendency to include warranties or covenants. This ranking is split into two groups. We then create a dummy variable which equals one if the contract

[37] As these regressions include the relevant economic determinants of warranties and covenants, the coefficients of the law firm fixed effects are a better reflection of the law firm style, after controlling for the economic factors that drive the variation in those provisions. This in contrast to the controls in this paper, which are selected as they drive the variation in acquisition premiums.

was drafted by a law firm with above median tendency to include warranties (Law Firm High Warranty Style Dummy) or covenants (Law Firm High Covenant Style Dummy).[38]

First, we show that this alternative instrument fulfills the relevance requirements of instrumental variables, Panels A and B of Table 3.7 report first stage regressions of warranties and covenants on these style dummies. The warranty style dummy significantly affects the total warranties and all categories of warranties, except for those on assets and insurance. Similarly, the covenant style dummy is significant for total covenants as well as most covenant categories, excluding covenants on litigation. As the instrumental variable is a single variable, the weak instrument concern no longer applies, which is supported by the Kleibergen-Paap tests.

Second, we Table 3.7 Panels C and D show that the impact of warranties and covenants on acquisition premiums is robust to using this alternative instrument, as both types of provisions still significantly affect premiums. Moreover, warranties in nearly all categories significantly increase premiums in this specification, even though the financial accounts warranties still report the highest statistical significance.[39] Similarly, for the covenants, the impact on premiums is significant for all categories which were also significantly driven by the instrument.

Law Firm Style Quartiles

However, one drawback of a single variable instrument is that the Sargan-Hansen test of exogeneity cannot be applied (Sargan (1958) and Hansen (1982)). As such, the Law Firm Style Dummy could be relevant, but potentially endogenous. To mitigate this concern, we repeat the analysis with a second set of alternative instruments. As with the style dummies, we start with a ranking of law firms, based on their tendency to include warranties or covenants. In this model specification, we split this ranking into four groups rather than two, and create four dummy variables (Law Firm Warranty Style Quartiles and Law Firm Covenant Style Quartiles).

[38] As the contracts are not uniformly distributed across law firms, the Law Firm High Warranty Style or Law Firm High Covenant Style variables do not reflect half the sample.
[39] The warranties that do not affect premiums are also insufficiently explained by the instrument.

Appendix A-3.5 reports regressions using these law firm quartile dummies as instrumental variables and shows that these instruments meet the relevance and exogeneity criteria for several of the categories.[40] Panel A shows that the style quartiles are sufficiently relevant and exogenous instruments for total warranties, and for warranties on corporate records, employees, contracts, and legal concerns. Similarly, Panel B documents that the covenant style quartiles are valid instruments for covenants on dividend payments, business conduct, acquisitions, divestments, and litigation. Furthermore, Panels C and D report that the categories -for which these instruments are valid- significantly impact acquisition premiums. This supports the assertion that our results are not driven by concerns regarding strength of the instruments.

3.5.5 Robustness Checks

Alternative Premium Measures

The analysis above uses the implied market-to-book value of the target as a proxy for the acquisition premium. A second concern that could be raised is whether this is a good reflection of premiums paid. Table 3.8 reports robustness checks to show that our results also hold with alternative proxies for premiums.

As a first alternative proxy, we consider the EBIT multiple, defined as the target market value divided by the EBIT of the year preceding the acquisition.[41] Table 3.8 reports IV-regressions of the EBIT multiple on warranties (Panel A) and covenants (Panel B) using all three types of instrumental variables. Both total warranties and covenants significantly affect the EBIT multiple, though the impact of warranties is only significant in models using the alternative instruments.

Further, Panel C of Table 3.8 shows that the results are robust to four further variations of the market-to-book premium.[42] The premium measure in Column 1 is equal to the one used in the main analysis. As a second measure, we divide the target market

[40] Recall that, to meet the relevance criteria, the Kleibergen-Paap test should be rejected, and to meet the exogeneity criteria, the Hansen-Sargan test should not be rejected.
[41] Appendix A-3.1 describes these measures in more detail.
[42] We restrict these robustness checks to total covenants and financial accounts warranties, as these show the strongest impact on premiums.

value by the value of tangible assets, rather than total assets.[43] The third measure is the unwinsorized acquisition premium, and the fourth is the log of the acquisition premium. Our results are robust to these different measures, indicating that the choice for premium measure does not bias the findings.[44]

Target Industry and Investment Banks

A third concern could be raised about the drivers of law firm styles, which form the basis of the instruments. For example, if law firms specialize in certain industries, then their styles could be a reflection of variation across industries. Similarly, if some law firms always pair up with certain investment banks, then law firm styles could be a reflection of bank involvement or bank quality (as in Bao and Edmans (2011)). Appendix A-3.6 Panel A shows that these concerns are not affecting our results, as the impact of contract provisions is robust to controlling for target industry fixed effects, and buyer and seller bank advice. Moreover, our results are robust to controlling for whether the buyer or seller had obtained advice from a top 10 investment bank, based on a ranking of deal volume between 1995 and 2010.

Other Contract Provisions

The positive impact of warranties and covenants on premiums suggests that these value increasing contract provisions are not traded off against each other. However, a fourth concern to our results could suggest that provisions function as complements. As Panel B in Appendix A-3.2 indicates, warranties and covenants are significantly positively correlated. If buyers demand both more warranties and covenants, then a positive relation between warranties and premiums could merely reflect the impact of the covenants in that contract. To test whether this is reflected in our results, Panel B of Appendix A-3.6 shows regressions of the premium on financial account warranties and covenants, while controlling for other contract provisions which could reflect buyer protection.[45] Our results are robust to these alternative contract controls.[46]

[43] This measure is also winsorized at 2%.

[44] Only the financial accounts warranties lose significance in the unwinsorized sample, possibly due to outliers.

[45] The contract provisions that are being controlled for are considered exogenous in these regression. Therefore, the financial accounts warranties and covenants are not significant when used as a control.

Distribution of Covenants

A final potential concern to the findings on covenants could be that these are biased due to their asymmetric distribution of covenants, with clustering at zero. As a robustness check, Panel C of Appendix A-3.6 reports regressions of the premium on covenants controlling for a dummy variable which equals one if a contract contains at least one covenant. If there would be a jump in the impact from covenants on premiums when moving from zero to one covenant, this should be reflected in this coefficient. Along the same lines, Panel D of Appendix A-3.6 controls for a dummy variable which equals one if there is any time between signing and closing, as it is likely that zero covenants are included when there is no time between signing and closing. The results indicate that covenants significantly affect premiums after controlling for both these variables. Moreover, the "jump-variables" do not significantly affect premiums, suggesting that there is no non-linearity in the impact on pricing at zero.

3.6 Conclusions

We analyze whether contract provisions affect premiums paid in corporate acquisitions. Using detailed contract data on 146 private acquisitions, we relate two types of contract provisions to acquisition premiums. First, we consider provisions that affect total surplus, by reducing information or agency concerns. Second, we consider provisions that distribute value between buyers and sellers by affecting the relative risk allocation. The *independence hypothesis* suggests that, because price and non-price terms are negotiated at separate points in time, they are determined independently. Conversely, according to the *feedback hypothesis*, contract design should be reflected in premiums. We address the endogeneity of contract terms by using an instrumental variables analysis, which exploits variation in internal specimen contracts of law firms as a source of exogenous variation in contract design.

[46] The other contract provisions do not significantly affect the premium. This could be because they are considered as exogenous, whereas there might be unobserved variables affecting these provisions and the premiums in opposite directions, as with warranties and covenants.

Supporting the weak form of the *feedback hypothesis*, we find that provisions that increase value (i.e., warranties and covenants) significantly positively affect the premiums paid by buyers. An additional warranty increases the premium with 1% and an additional covenant increases the premium with 11%. We find that this impact on premiums varies across different types of provisions, based on the underlying concerns they address. In contrast, provisions which allocate risk do not seem to impact premiums. However, there is some evidence supporting the strong-form of the *feedback hypothesis*, which suggests that value distributing provisions also affect premiums, as relatively large sellers seem to be compensated for bearing higher risk.

Table 3.1
Summary Statistics of the Sample

This table provides summary statistics of the variables used in the analysis. The sample covers 146 M&A transactions conducted in the period between 2005 and 2010. Panel A reports summary statistics of target, buyer, seller, and deal characteristics. Panel B reports summary statistics for our proxies of contract design. Panel C reports summary statistics of the warranties and covenants per category. As warranty data is missing for one transaction, these statistics are based on 145 observations. Detailed variable definitions are provided in Appendix A-3.1.

Panel A: Transaction Characteristics

Premium	**Mean**	**Median**	**10th**	**90th**	**Std. Dev.**	**Obs.**
Acquisition Premium	244%	155%	100%	506%	230%	146
Acquisition Premium Tangible Assets	278%	173%	101%	631%	253%	145
Target						
Transaction Value (mEUR)	229	36	2	391	807	146
Target Book Value (mEUR)	318	45	2	538	990	146
Target Tangible Assets (mEUR)	290	38	2	408	963	145
Target Market Value (mEUR)	434	80	6	864	1290	146
Target EBIT/Assets	14%	14%	1%	33%	16%	146
Target Leverage	59%	60%	21%	97%	30%	146
High R&D Industry	28%				45%	146
Asset Deal	8%				26%	146
Buyer and Seller						
Buyer Publicly-Listed	44%				50%	146
Seller Publicly-Listed	35%				48%	146
Toehold Deal	3%				16%	146
Cross-Country Deal	45%				50%	146
Deal						
Approvals Required (number)	1	0	0	2	2	146
Deal After 2008	38%				49%	146
Controlled Auction	22%				42%	146
First Draft by Buyer	45%				50%	146

Panel B: Contract Design

	Mean	**Median**	**Min**	**Max**	**Std. Dev.**	**Obs.**
Value Increasing						
Warranties	98.0	101.0	4.0	247.0	48.7	145
Covenants	14.0	14.5	0.0	50.0	13.0	146
Value Distributing						
%Warranties w/o Qualifier	87%	89%	17%	100%	12%	145
Warranties Fully True	83%				38%	145
%Payment Secured	5%	0%	0%	29%	9%	144
MAC Strength Index	28%	0%	0%	100%	42%	146

Table 3.1 (continued)

Panel C: Warranties and Covenants per Category

	Mean	Median	Min	Max	Std. Dev.	Obs.
Warranties per Category						
Corporate Records	17.5	18.0	1.0	37.0	6.6	145
Employees	12.4	12.0	0.0	49.0	8.7	145
Financial Accounts	24.2	22.0	0.0	62.0	16.1	145
Assets	8.6	7.0	0.0	49.0	7.1	145
Contracts	12.6	12.0	0.0	38.0	7.8	145
Insurance	3.0	3.0	0.0	11.0	2.4	145
Intellectual Property	8.2	6.0	0.0	40.0	9.2	145
Legal	9.9	10.0	0.0	32.0	5.8	145
Covenants per Category						
Corporate Documents	0.9	0.0	0.0	7.0	1.2	146
Employees	1.5	1.0	0.0	7.0	1.8	146
Dividend Payments	2.5	1.0	0.0	13.0	3.1	146
Debt	1.4	1.0	0.0	6.0	1.6	146
Business Conduct	5.2	5.0	0.0	24.0	5.0	146
Acquisitions	1.1	1.0	0.0	5.0	1.1	146
Divestments	1.0	1.0	0.0	4.0	1.1	146
Litigation	0.4	0.0	0.0	3.0	0.6	146

Table 3.2
First Stage Results: Warranties and Covenants

This table reports OLS regressions of contract design on Law Firm Fixed effects, after controlling for economic determinants of premiums. Each column represents a separate dependent variable (listed horizontally). Variable definitions are provided in Appendix A-3.1. The sample covers 146 M&A transactions, but regressions are on fewer observations because of missing data. We report the *F*-statistic and *p*-value of the joint significance of Law Firm Fixed Effects, and their Partial R-squared. We also report the Kleibergen-Paap LM-statistic, and the Hansen J-Statistic from 2SLS regressions as in Table 3.4. In parentheses are *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: First Stage Regressions of Contract Design

	Dependent Variable: Contract Design					
Contract Design:	**Value Increasing**		**Value Distributing**			
	Warranties	Covenants	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Strength Index
	(1)	(2)	(3)	(4)	(5)	(7)
Law Firm FE: *F*-test (*p*-value)	103.97 (0.000)	797.16 (0.000)	51.13 (0.000)	25.56 (0.000)	1,052.98 (0.000)	28.44 (0.000)
Target Book Value (log)	0.89	1.30**	0.00	-0.07***	-0.01*	-0.00
	(0.30)	(2.00)	(0.31)	(-2.96)	(-1.73)	(-0.04)
Target EBIT/Assets	23.61	-8.19	0.07	-0.19	0.03	0.01
	(0.90)	(-1.33)	(0.87)	(-0.83)	(0.55)	(0.04)
Target Leverage	17.26	3.65	0.03	0.16	0.01	0.15
	(1.26)	(1.19)	(0.77)	(1.50)	(0.23)	(0.97)
High R&D Industry	-4.47	-2.24	0.01	-0.09	-0.03	-0.09
	(-0.44)	(-0.78)	(0.42)	(-1.05)	(-1.13)	(-0.80)
Relative Size	2.66	0.96**	0.00	0.04**	0.00	0.03
	(1.28)	(2.08)	(0.33)	(2.18)	(0.98)	(1.31)
Deal After 2008	24.72**	-2.59	-0.03	0.03	-0.03	0.00
	(2.57)	(-1.08)	(-0.84)	(0.42)	(-1.28)	(0.02)
Controlled Auction	17.38	7.22**	-0.05	-0.19	0.02	0.01
	(1.61)	(2.37)	(-1.11)	(-1.65)	(0.79)	(0.12)
Toehold Deal	-104.40***	-9.89**	0.24**	-0.14	0.03	-0.17
	(-8.64)	(-1.99)	(2.37)	(-0.63)	(0.57)	(-0.66)
First Draft by Buyer	25.51**	1.26	0.07**	0.06	0.03	0.29**
	(2.11)	(0.39)	(2.15)	(0.52)	(1.17)	(2.48)
Seller Publicly-Listed	3.43	2.05	-0.01	0.08	-0.03*	0.14
	(0.31)	(0.79)	(-0.33)	(0.71)	(-1.72)	(1.02)
Buyer Publicly-Listed	-4.02	-1.43	-0.01	0.02	0.01	-0.09
	(-0.42)	(-0.59)	(-0.36)	(0.30)	(0.55)	(-0.79)
Cross-Country Deal	16.47	2.97	0.02	0.00	-0.01	0.11
	(1.50)	(1.16)	(0.49)	(0.05)	(-0.38)	(0.96)
Asset Deal	-28.06**	-1.87	0.07	-0.14	-0.04	0.17
	(-2.05)	(-0.62)	(1.65)	(-0.73)	(-1.37)	(0.70)
Approvals Required	0.77	2.17**	0.01	0.07***	0.00	0.02
	(0.28)	(2.60)	(1.13)	(4.22)	(0.63)	(0.86)
Obs.	140	141	140	140	140	141
Adj. R^2	0.363	0.403	0.039	0.221	0.068	-0.025
Partial R^2 Instruments	0.315	0.267	0.233	0.336	0.115	0.191
Kleibergen-Paap LM: χ^2-test (*p* -value)	24.38 (0.609)	26.48 (0.492)	25.93 (0.523)	31.20 (0.263)	20.85 (0.750)	29.88 (0.320)
Hansen J: χ^2-test (*p* -value)	27.46 (0.339)	1.85 (0.174)	23.87 (0.583)	23.81 (0.587)	22.97 (0.579)	23.38 (0.612)

Table 3.3
Acquisition Premium: Base Regression

This table report an OLS regressions to explain the effects of economic determinants on the acquisition premium in M&A transactions. The sample covers 146 M&A transactions conducted between 2005 and 2010, but the regression is on 141 observations because of missing data for some variables. Detailed variable definitions are provided in Appendix A-3.1. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

	Dependent Variable: Acquisition Premium
Target Book Value (log)	-0.35***
	(-3.97)
Target EBIT/Assets	3.45***
	(3.08)
Target Leverage	-0.68
	(-1.17)
High R&D Industry	1.82***
	(4.02)
Relative Size	0.17*
	(1.91)
Deal After 2008	0.31
	(0.86)
Controlled Auction	-0.55
	(-1.52)
Toehold Deal	-0.17
	(-0.21)
First Draft by Buyer	-0.39
	(-1.16)
Seller Publicly-Listed	0.00
	(0.01)
Buyer Publicly-Listed	0.33
	(0.93)
Cross-Country Deal	-0.29
	(-0.79)
Asset Deal	0.16
	(0.22)
Approvals Required	0.12
	(1.35)
Obs.	141
Adj. R^2	0.422

Table 3.4
Acquisition Premium: Effect of Contract Design

This table reports OLS (Panel A) and 2SLS (Panel B) regressions to explain the effects of contract design on acquisition premiums in M&A transactions. The sample covers 146 M&A transactions, but the regressions are on fewer observations because of missing data. All regressions control for economic determinants of acquisition premiums. In addition, each columns controls for a proxy of contract design (listed horizontally). Variable definitions are provided in Appendix A-3.1. Panel B report 2SLS regressions where Law Firm Fixed Effects are used as instruments. That panel also reports the *F*-statistic and *p*-value of their joint significance in the first stage regressions. In parentheses are *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: OLS Regressions: Effect of Contract Design on Acquisition Premium

	Dependent Variable: Acquisition Premium					
Contract Design:	**Value Increasing**		**Value Distributing**			
	Warranties	Covenants	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Strength Index
	(1)	(2)	(3)	(4)	(5)	(7)
Contract Design	0.01*	0.03*	0.34	-0.20	-1.14	0.03
	(1.82)	(1.97)	(0.43)	(-0.75)	(-0.72)	(0.06)
Target Book Value (log)	-0.35***	-0.40***	-0.35***	-0.36***	-0.36***	-0.35***
	(-3.90)	(-3.93)	(-3.96)	(-4.10)	(-3.88)	(-3.92)
Target EBIT/Assets	3.37***	3.62***	3.45***	3.45***	3.46***	3.44***
	(3.11)	(3.12)	(3.07)	(3.06)	(3.03)	(3.11)
Target Leverage	-0.78	-0.87	-0.68	-0.66	-0.69	-0.69
	(-1.32)	(-1.52)	(-1.17)	(-1.11)	(-1.15)	(-1.19)
High R&D Industry	1.82***	1.88***	1.82***	1.82***	1.80***	1.83***
	(3.95)	(4.15)	(4.01)	(3.99)	(3.91)	(3.90)
Relative Size	0.15*	0.13	0.17*	0.17*	0.17**	0.17*
	(1.74)	(1.46)	(1.90)	(1.95)	(2.04)	(1.84)
Deal After 2008	0.20	0.29	0.31	0.31	0.28	0.31
	(0.55)	(0.85)	(0.86)	(0.87)	(0.78)	(0.87)
Controlled Auction	-0.60*	-0.72**	-0.53	-0.55	-0.52	-0.55
	(-1.69)	(-2.05)	(-1.48)	(-1.52)	(-1.44)	(-1.51)
Toehold Deal	0.41	0.15	-0.20	-0.25	-0.19	-0.17
	(0.46)	(0.17)	(-0.24)	(-0.31)	(-0.23)	(-0.21)
First Draft by Buyer	-0.52	-0.27	-0.40	-0.37	-0.36	-0.39
	(-1.54)	(-0.79)	(-1.18)	(-1.11)	(-1.01)	(-1.20)
Seller Publicly-Listed	-0.01	-0.02	-0.00	0.01	-0.01	0.00
	(-0.03)	(-0.07)	(-0.00)	(0.03)	(-0.04)	(0.00)
Buyer Publicly-Listed	0.33	0.36	0.32	0.31	0.34	0.33
	(0.94)	(1.03)	(0.90)	(0.88)	(0.97)	(0.93)
Cross-Country Deal	-0.42	-0.37	-0.29	-0.30	-0.30	-0.30
	(-1.11)	(-1.01)	(-0.77)	(-0.81)	(-0.81)	(-0.78)
Asset Deal	0.32	0.33	0.16	0.15	0.12	0.16
	(0.44)	(0.47)	(0.22)	(0.21)	(0.16)	(0.22)
Approvals Required	0.11	0.05	0.11	0.13	0.12	0.12
	(1.28)	(0.69)	(1.32)	(1.42)	(1.37)	(1.34)
Obs.	140	141	140	140	140	141
Adj. R^2	0.426	0.440	0.416	0.417	0.419	0.418

Table 3.4 (Continued)

Panel B: 2SLS Regressions: Effect of Contract Design on Acquisition Premium

	Dependent Variable: Acquisition Premium					
Contract Design:	**Value Increasing**		**Value Distributing**			
	Warranties	Covenants	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Strength Index
	(1)	(2)	(3)	(4)	(5)	(7)
Contract Design	0.01*	0.11***	2.18	1.13*	-6.68	1.34
	(1.71)	(3.09)	(0.84)	(1.84)	(-0.90)	(1.13)
Target Book Value (log)	-0.35***	-0.51***	-0.35***	-0.31***	-0.40***	-0.36***
	(-4.04)	(-4.41)	(-4.16)	(-3.66)	(-3.37)	(-4.04)
Target EBIT/Assets	3.30***	4.02***	3.42***	3.45***	3.64***	3.29***
	(3.33)	(3.28)	(3.21)	(3.20)	(3.04)	(2.93)
Target Leverage	-0.86	-1.29**	-0.70	-0.81	-0.69	-0.90
	(-1.51)	(-2.16)	(-1.25)	(-1.36)	(-1.13)	(-1.52)
High R&D Industry	1.80***	2.00***	1.78***	1.89***	1.69***	1.95***
	(4.14)	(4.35)	(4.05)	(4.15)	(3.71)	(4.17)
Relative Size	0.14*	0.05	0.16*	0.13	0.21***	0.14
	(1.70)	(0.57)	(1.92)	(1.49)	(3.09)	(1.46)
Deal After 2008	0.11	0.26	0.31	0.29	0.13	0.26
	(0.30)	(0.75)	(0.92)	(0.84)	(0.38)	(0.77)
Controlled Auction	-0.65*	-1.12***	-0.46	-0.49	-0.38	-0.48
	(-1.92)	(-2.97)	(-1.24)	(-1.38)	(-0.98)	(-1.29)
Toehold Deal	0.91	0.89	-0.37	0.27	-0.22	0.02
	(0.96)	(0.92)	(-0.45)	(0.27)	(-0.34)	(0.02)
First Draft by Buyer	-0.64**	0.01	-0.46	-0.46	-0.18	-0.63*
	(-2.01)	(0.02)	(-1.41)	(-1.39)	(-0.42)	(-1.89)
Seller Publicly-Listed	-0.02	-0.08	0.01	-0.07	-0.14	-0.08
	(-0.05)	(-0.23)	(0.04)	(-0.20)	(-0.33)	(-0.22)
Buyer Publicly-Listed	0.34	0.43	0.30	0.37	0.40	0.41
	(1.02)	(1.19)	(0.89)	(1.07)	(1.07)	(1.11)
Cross-Country Deal	-0.52	-0.56	-0.24	-0.27	-0.37	-0.43
	(-1.51)	(-1.50)	(-0.65)	(-0.71)	(-0.95)	(-1.13)
Asset Deal	0.45	0.72	0.12	0.27	-0.07	0.06
	(0.64)	(1.07)	(0.17)	(0.38)	(-0.09)	(0.09)
Approvals Required	0.11	-0.09	0.11	0.06	0.13	0.08
	(1.29)	(-0.90)	(1.30)	(0.76)	(1.52)	(1.04)
Obs.	140	141	140	140	140	141
Adj. R^2	0.418	0.324	0.407	0.372	0.378	0.360
Law Firm FE:	103.97	797.16	51.13	25.56	1,052.98	28.44
F-test (*p*-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 3.5
Acquisition Premium: Effects of Warranties and Covenants per Category

This table reports 2SLS regressions to explain the effects of warranties and covenants per category on acquisition. The dependent variable is the Acquisition Premium, and regressions control for the control variables in Table 3.3. In addition, Panel A includes the warranties per category and Panel B the covenants per category. Detailed variable definitions are in Appendix A-3.1. Law Firm Fixed Effects are used an instrumental variables. The *F*-statistic and *p*-value for the joint significance of these fixed effects in the first stage regression is reported. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: 2SLS Regressions: Warranties per Category

	Dependent Variable: Acquisition Premium							
Warranty Categories:	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellect. Property	Legal
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Warranties per Category	0.04	0.05	0.06***	-0.02	0.04	-0.07	0.08**	0.02
	(0.85)	(1.42)	(2.72)	(-0.42)	(1.37)	(-0.51)	(2.00)	(0.44)
Obs.	140	140	140	140	140	140	140	140
Adj. R^2	0.425	0.407	0.391	0.413	0.419	0.413	0.408	0.415
Law Firm FE:								
F-test	98.78	135.86	123.61	58.07	73.57	32.05	163.82	11,537.18
(*p*-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Panel B: 2SLS Regressions: Covenants per Category

	Dependent Variable: Acquisition Premium							
Covenant Categories:	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquis.	Divest.	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Covenants per Category	0.44*	0.57***	0.41***	0.59*	0.20**	0.72*	0.89***	0.67
	(1.80)	(2.85)	(3.11)	(1.85)	(2.39)	(1.92)	(2.76)	(1.25)
Obs.	141	141	141	141	141	141	141	141
Adj. R^2	0.400	0.360	0.326	0.348	0.371	0.363	0.375	0.431
Law Firm FE:								
F-test	191.03	435.86	84.08	124.22	2449.69	97.72	385.03	36.95
(*p*-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 3.6
Acquisition Premium: Accounting for Bargaining Power

This table reports 2SLS regressions of the Acquisition Premium on proxies for contract design (listed horizontally) for different subsamples, based on various proxies for seller bargaining power. All regressions control for the controls as in Table 3.3. Variable definitions are in Appendix A-3.1. Law Firm Fixed effects are used as instruments. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

	Dependent Variable: Acquisition Premium											
Contract Design:	**Financial Accounts Warranties**		**Covenants**		**%Warranties w/o Qualifier**		**Warranties Fully True**		**%Payment Secured**		**MAC Strength Index**	
Seller Bargaining power	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**
First Draft by Seller	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO
Contract Design	0.05***	-0.01	0.07***	0.10*	2.01	3.13	1.08*	-0.44	-0.88	-2.38	-0.14	1.82
	(2.59)	(-0.49)	(2.95)	(1.73)	(1.57)	(0.58)	(1.86)	(-0.45)	(-0.17)	(-0.45)	(-0.23)	(1.33)
Obs.	78	62	79	62	78	62	78	62	78	62	79	62
Adj. R^2	0.316	0.512	0.238	0.448	0.253	0.522	0.119	0.526	0.298	0.513	0.296	0.480
Deal Before 2008	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO
Contract Design	0.02*	0.06	0.06***	0.10**	0.25	12.51**	1.16	0.42	-6.48	-4.23	-0.80	2.11*
	(1.78)	(1.61)	(3.01)	(2.05)	(0.15)	(2.15)	(1.36)	(0.52)	(-1.20)	(-0.70)	(-0.95)	(1.91)
Obs.	87	53	88	53	87	53	87	53	88	52	88	53
Adj. R^2	0.433	0.440	0.417	0.417	0.426	0.221	0.368	0.421	0.376	0.405	0.445	0.392
Seller Size ≥ Buyer Size	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO
Contract Design	0.07*	0.00	0.17***	0.03	13.22*	-0.42	1.20*	0.22	-7.60	-5.85*	2.29*	1.32
	(1.91)	(0.20)	(4.00)	(1.47)	(1.81)	(-0.18)	(1.79)	(0.37)	(-1.05)	(-1.77)	(1.74)	(1.35)
Obs.	64	72	65	72	64	72	64	72	65	71	65	72
Adj. R^2	0.254	0.487	0.029	0.487	.	0.485	0.098	0.485	0.208	0.462	0.156	0.449
Seller Deal Exper. ≥ Buyer	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO
Contract Design	0.05**	0.04**	0.14***	0.08***	7.34	3.40	1.47*	0.29	-8.30	3.43	2.53**	0.53
	(1.98)	(2.00)	(3.36)	(2.94)	(1.17)	(0.95)	(1.76)	(0.46)	(-0.73)	(0.46)	(2.12)	(0.56)
Obs.	59	80	60	80	59	80	59	80	60	79	60	80
Adj. R^2	0.340	0.474	0.213	0.407	0.247	0.443	0.161	0.462	0.314	0.437	0.203	0.445
Seller Bank Advice	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO	YES	NO
Contract Design	0.09***	0.01	0.13***	0.03	0.58	0.82	1.19*	0.26	-8.30	3.43	1.10	1.20
	(3.10)	(0.64)	(3.39)	(0.67)	(0.39)	(0.15)	(1.71)	(0.36)	(-0.73)	(0.46)	(0.63)	(1.09)
Obs.	67	73	68	73	67	73	67	73	60	79	68	73
Adj. R^2	0.475	0.344	0.436	0.339	0.420	0.349	0.384	0.341	0.314	0.437	0.389	0.288

Table 3.7
Alternative Instrumental Variable

This table reports first and second stage regressions from a 2SLS model explaining the effect of warranties (per category) and covenants (per category) on acquisition premiums, using a single variable as instrument. Panel A reports first stage OLS regressions of warranties (Column 1) and warranties per category (Columns 2 to 9) on Law Firm High Warranty Style Dummy are in. Panel B reports first stage OLS regressions of covenants (Column 1) and covenants per category (Columns 2 to 9) on Law Firm High Covenant Style Dummy. The Law Firm High Warranty (Covenant) Style Dummy which equals one if the first draft contract was provided by a law firm with an above median tendency to include warranties (covenants), and zero otherwise. In both panels, we report the *F*-statistic and *p*-value of the significance of the Law Firm Style Dummy, and the Partial R-squared of this variable. Moreover, Panels A and B report the Kleibergen-Paap LM-statistic based on the 2SLS regressions in Panels C and D. Panels C and D report second stage regressions of the acquisition premium on warranties (Panel C) and covenants (Panel D). The Adjusted R-squared is not reported if the R-squared is negative. All regressions control for the same variables as in Table 3.3 column 1. Detailed definitions of all variables are in Appendix A-3.1. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: First Stage Regressions: Warranties and Law Firm High Warranty Style Dummy

	Dependent Variable: Warranties								
	Warranties	**Warranties per Category**							
	Total	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellectual Property	Legal
Law Firm High Warranty Style Dummy	45.00***	4.30***	8.60***	10.21***	1.72	8.33***	0.85	5.30**	6.07***
	(3.73)	(2.62)	(3.44)	(2.87)	(0.81)	(4.43)	(1.58)	(1.99)	(3.66)
Obs.	140	140	140	140	140	140	140	140	140
Adj. R^2	0.350	0.308	0.143	0.463	0.094	0.302	0.095	0.164	0.234
Partial R^2 Instruments	0.116	0.056	0.101	0.072	0.006	0.138	0.014	0.04	0.126
Instruments F-test (*p* -value)	13.88	6.88	11.82	8.23	0.65	19.66	2.48	3.96	13.42
	(0.000)	(0.010)	(0.001)	(0.005)	(0.442)	(0.000)	(0.118)	(0.049)	(0.000)
Kleibergen-Paap LM: χ^2-test (*p* -value)	8.51	5.46	7.77	6.10	0.70	10.13	2.42	3.59	9.15
	(0.004)	(0.019)	(0.005)	(0.014)	(0.404)	(0.002)	(0.120)	(0.058)	(0.003)

Table 3.7 (Continued)

Panel B: First Stage Regressions: Covenants and Law Firm High Covenant Style Dummy

	Dependent Variable: Covenants								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
Law Firm High Covenant Style Dummy	8.95***	0.67***	1.39***	1.91***	1.00***	2.55**	0.33*	0.88***	0.21
	(3.60)	(2.77)	(3.29)	(3.14)	(3.00)	(1.99)	(1.66)	(3.79)	(1.45)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.413	0.239	0.209	0.393	0.250	0.284	0.294	0.406	0.254
Partial R^2 Instruments	0.090	0.045	0.085	0.073	0.057	0.042	0.015	0.114	0.020
Instruments *F*-test (*p* -value)	12.93	7.68	10.81	9.87	9.00	3.97	2.76	14.36	2.11
	(0.001)	(0.006)	(0.001)	(0.002)	(0.003)	(0.048)	(0.099)	(0.000)	(0.149)
Kleibergen-Paap LM: χ^2-test (*p* -value)	10.80	7.51	9.53	10.01	7.80	3.94	2.83	10.57	2.26
	(0.0001)	(0.006)	(0.002)	(0.002)	(0.005)	(0.047)	(0.093)	(0.001)	(0.133)

Panel C: 2SLS Regressions: Warranties and Warranties per Category

	Dependent Variable: Acquisition Premium								
	Warranties	**Warranties per Category**							
	Total	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellectual Property	Legal
Warranties	0.02*	0.24*	0.12*	0.10**	0.60	0.12*	1.20	0.19*	0.17*
	(1.90)	(1.65)	(1.84)	(2.01)	(0.78)	(1.75)	(1.16)	(1.88)	(1.65)
Obs.	140	140	140	140	140	140	140	140	140
Adj. R^2	0.327	0.180	0.273	0.272	.	0.327	.	0.111	0.257

Table 3.7 (Continued)

Panel D: 2SLS Regressions: Covenants and Covenants per Category

	Dependent Variable: Acquisition Premium								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
Covenants	0.09**	1.26**	0.61**	0.44**	0.84*	0.33*	2.54	0.96**	3.98
	(2.29)	(2.03)	(2.20)	(2.37)	(1.87)	(1.73)	(1.57)	(2.22)	(1.30)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.361	0.131	0.346	0.305	0.229	0.193	.	0.362	.

Table 3.8
Alternative Premium Measures

This table reports 2SLS regression results explaining the effect of warranties (per category) and covenants (per category) on acquisition premiums, using various proxies for premiums paid. The sample covers 146 M&A transactions, but the regressions are on fewer observations because of missing data for some variables. The dependent variable in Panels A and B is the EBIT-multiple (Target Market Value/EBIT). Panels A and B reports 2SLS regressions of the EBIT multiple on warranties (Panel A) and covenants (Panel B), using three types of instruments (listed vertically): (1) Law Firm Fixed Effects; (2) Law Firm High Warranty (Covenant) Style Dummy; (3) Law Firm Warranty (Covenant) Style Quartiles. Panel C reports regressions with as dependent variables (listed horizontally): (1) Acquisition Premium winsorized at 2% (the standard used so far); (2) Target Market Value / Tangible Assets; (3) acquisition premium unwinsorized; and (4) natural logarithm of the (unwisorized) acquisition premium. Panel C reports 2SLS regressions of these dependent variables on Financial Accounts Warranties and on Covenants, using Law Firm Fixed Effects as instruments. All regressions in this table control for the same variables as Table 3.3 Column 1. Appendix A-3.1 describes these measures in more detail. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5% and, * at 10%.

Panel A: IV Regressions of EBIT Multiple on Warranties

	Dependent Variable: EBIT Multiple								
	Warranties	**Warranties per Category**							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	Total	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellectual Property	Legal
Warranties	0.34	2.72*	2.76**	1.02	-1.75	0.93	0.69	2.82*	-0.02
Instrument: Law Firm FE	(1.19)	(1.67)	(2.33)	(0.91)	(-0.86)	(0.66)	(0.12)	(1.85)	(-0.01)
Instrument: High Warranty Style Dummy	0.82*	10.63	4.37*	3.87*	14.92	4.25	30.01	5.49*	7.59
	(1.86)	(1.64)	(1.95)	(1.94)	(0.79)	(1.58)	(1.29)	(1.91)	(1.64)
Instrument: High Warranty Style Quartiles	0.55*	6.58	2.87*	1.56	6.05	3.58	8.13	3.92**	6.66
	(1.84)	(1.46)	(1.93)	(1.31)	(0.96)	(1.60)	(0.88)	(1.97)	(1.62)
Obs.	106	106	106	106	106	106	106	106	106

Table 3.8 (Continued)

Panel B: IV Regressions of EBIT Multiple on Covenants

	Dependent Variable: EBIT Multiple								
	Covenants	**Covenants per Category**							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
Covenants	3.05***	22.48*	13.36**	7.83*	12.00	6.48***	22.30	23.87**	25.96
Instrument: Law Firm FE	(3.50)	(1.68)	(2.28)	(1.79)	(1.28)	(4.67)	(1.63)	(2.49)	(1.01)
Instrument High Covenant Style	3.27*	55.90	21.63*	16.58	26.50*	11.20	54.56*	31.98*	199.73
Dummy	(1.79)	(1.41)	(1.82)	(1.49)	(1.67)	(1.54)	(1.71)	(1.93)	(1.00)
Instrument: High Covenant Style	4.36***	33.60	21.81**	24.24**	30.16**	11.82***	68.46***	43.49***	110.81**
Quartiles	(3.03)	(1.03)	(1.99)	(2.37)	(2.13)	(2.81)	(2.97)	(3.19)	(2.10)
Obs.	107	107	107	107	107	107	107	107	107

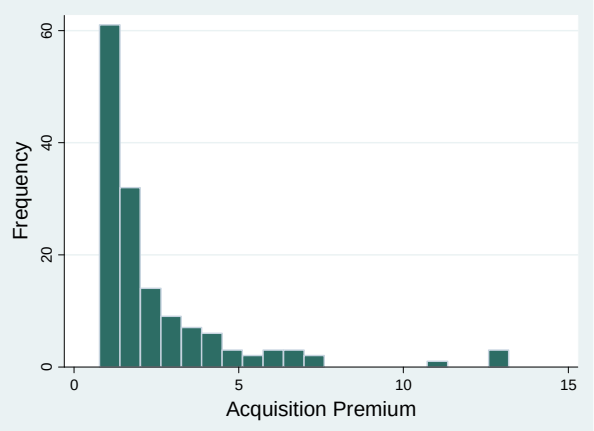
Panel C: IV Regressions of Other Premium Measures

	Dependent Variable: Acquisition Premium			
	Winsorized (2%)	Tangible Assets	Unwinsorized	Log
	(1)	(2)	(3)	(4)
Financial Accounts Warranties	0.06***	0.07**	0.13	0.02***
	(2.72)	(2.33)	(1.56)	(2.71)
Obs.	140	139	140	140
Total Covenants	0.11***	0.12***	0.31*	0.03***
	(3.09)	(3.30)	(1.69)	(3.27)
Obs.	141	140	141	141

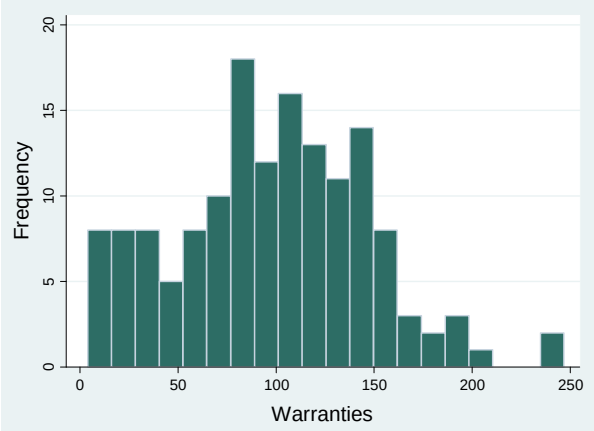
Figure 3.1
Histograms for Acquisition Premium, Warranties, and Covenants

This table shows histograms of the distributions of Acquisition Premium (Panel A), Warranties (Panel B), Financial Accounts Warranties (Panel C), and Covenants (Panel D).

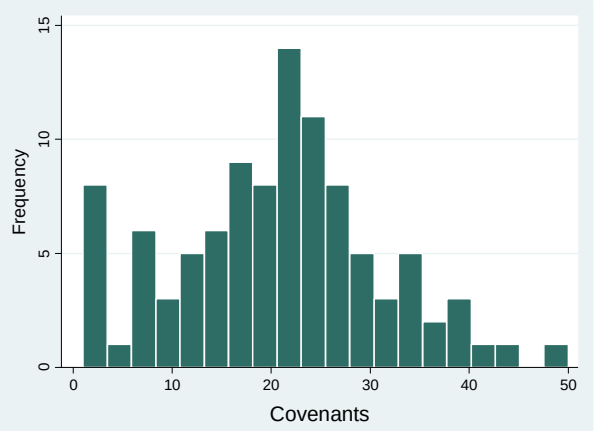
Panel A: Histogram of Acquisition Premium



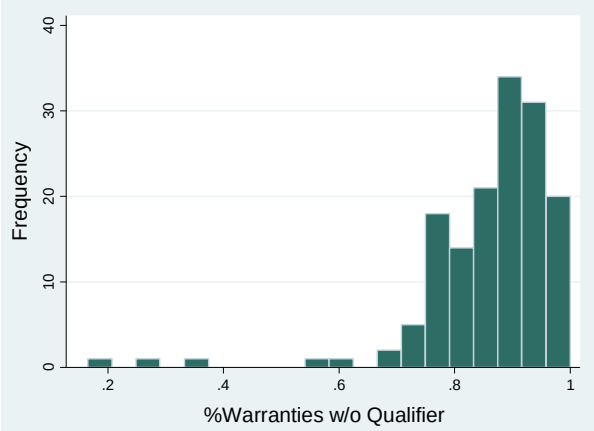
Panel B: Histogram of Warranties



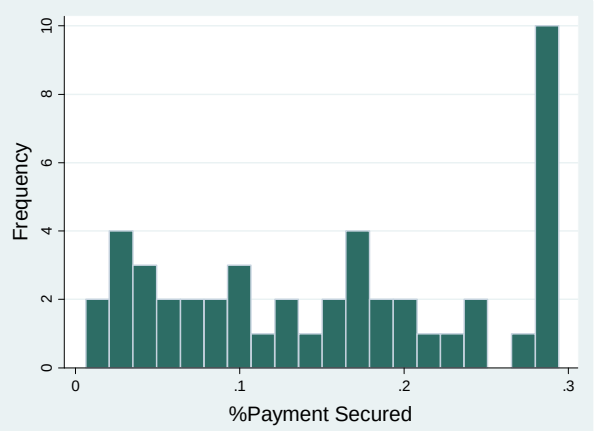
Panel C: Histogram of Covenants
(Subsample of Contracts with At Least One Covenant)



Panel D: Histogram of %Warranties w/o Qualifier



Panel E: Histogram of %Payment Secured
(Subsample of Contracts with More than 0% Secured)



Panel F: Histogram of MAC Strength Index
(Subsample of Contracts with a MAC Clause)

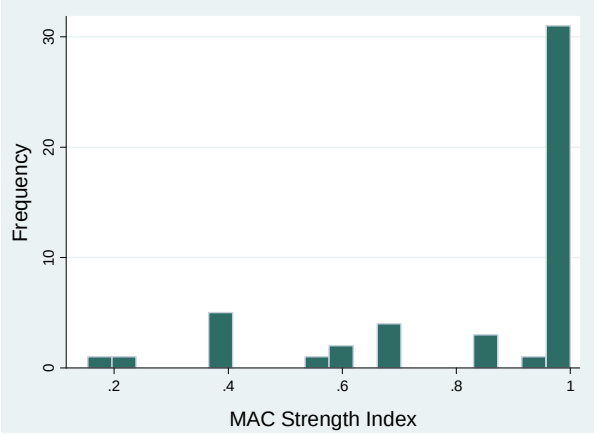
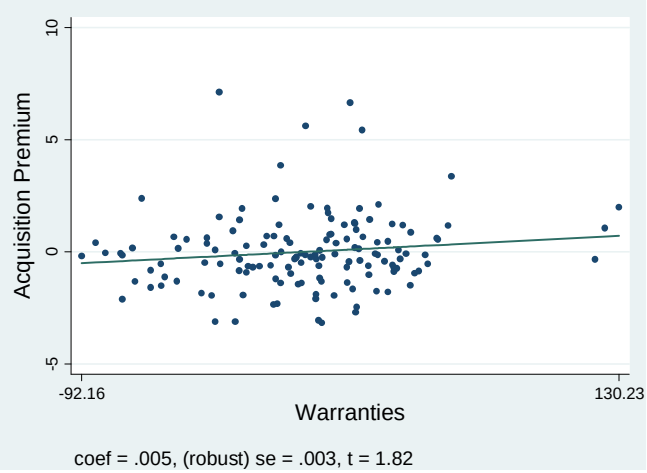


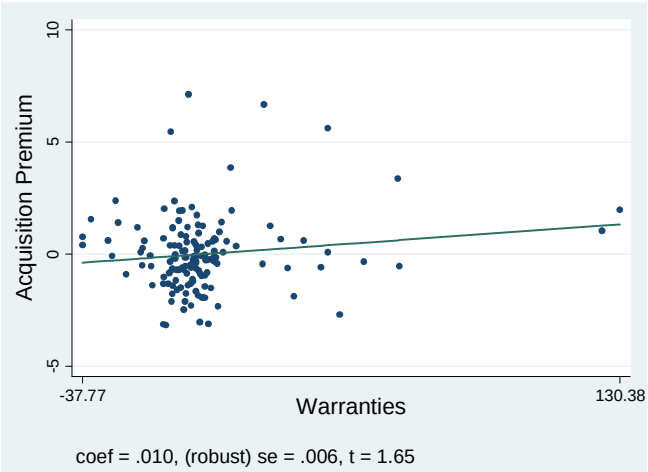
Figure 3.2
Partial Scatterplots of Acquisition Premium on Warranties

This table shows partial scatterplots derived from OLS (Panel A) and 2SLS (panel B) regressions that explain the Acquisition Premium using Warranties. The effects are estimated after controlling for deal characteristics as in the regressions of Table 3.3. Panel C shows a histogram of the predicted Warranties based on first stage regressions reported in Table 3.2.

Panel A: Partial Scatterplot of OLS regressions of Acquisition Premium on Warranties



Panel B: Partial Scatterplot of 2SLS regressions of Acquisition Premium on Financial Accounts Warranties



Panel C: Histogram of Predicted Values of Financial Accounts Warranties

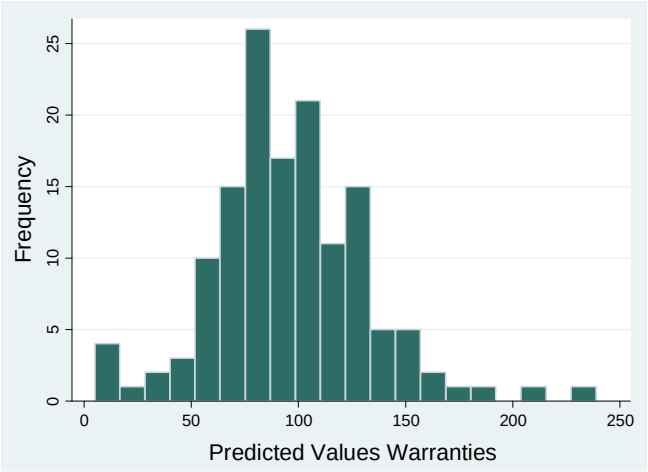
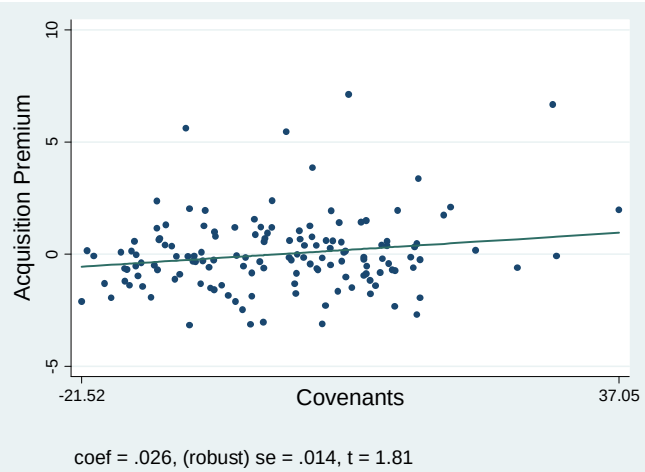


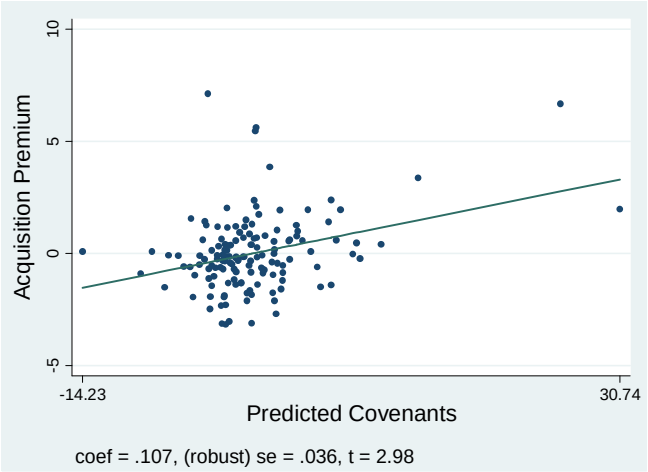
Figure 3.3
Partial Scatterplots of Acquisition Premium on Covenants

This table shows partial scatterplots derived from OLS (Panel A) and 2SLS (panel B) regressions that explain the Acquisition Premium using Covenants. The effects are estimated after controlling for deal characteristics as in the regressions of Table 3.3. Panel C shows a histogram of the predicted Covenants based on first stage regressions reported in Table 3.2.

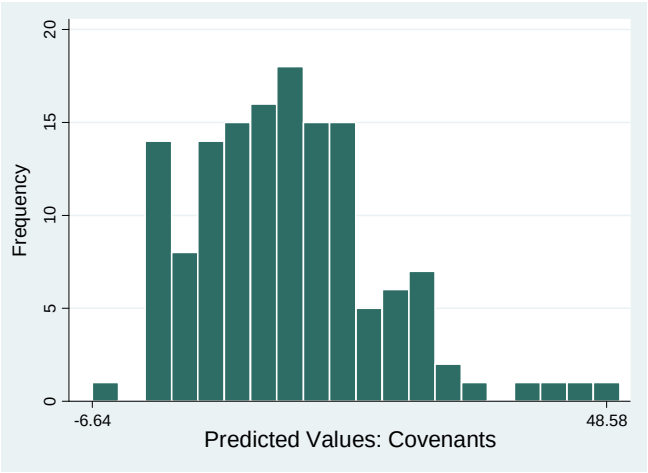
Panel A: Partial Scatterplot of OLS regressions of Acquisition Premium on Covenants



Panel B: Partial Scatterplot of 2SLS regressions of Acquisition Premium on Covenants



Panel C: Histogram of Predicted Values of Covenants



Appendix A-3.1
Definition of Variables

This table provides the definitions of the variables used in this paper. If the source for the data is not mentioned, the information has been obtained from the contracts.

Variable	Description
Premium	
Acquisition Premium	Target Market Value divided by the book value of the target, winsorized at 2%. Target market Value is defined as the price paid for (the equivalent of 100% of) target equity of plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Acquisition contracts, Amadeus, trade register).
Acquisition Premium Tangible Assets	Target Market Value divided by the book value of the tangible assets of the target. (Source: Acquisition contracts, Amadeus, trade register).
Target	
Transaction Value (mEUR)	Total amount of payments by the buyer to the seller. This is equal to the market value of equity of the target unless the buyer purchases less than 100% of the equity. (Source: Acquisition contracts).
Target Book Value (mEUR)	Book value of the assets of the target. (Source: Acquisition contracts, Amadeus, trade register).
Target Tangible Assets (mEUR)	Target book value of assets minus the intangible assets (Source: Acquisition contracts, Amadeus, trade register).
Target Market Value (mEUR)	Price paid for (the equivalent of 100% of) the equity of the target plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Acquisition contracts, Amadeus, trade register).
Target Leverage	Book value of liabilities of the target divided by book value of assets of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Amadeus, trade register).
Target EBIT/Assets	EBIT of the target divided by the book value of the assets of the target. If EBIT data is not available (48 observations), we use the mean value of EBIT/Assets (13.6%) of the sample. (Source: Amadeus, trade register).
High R&D Industry	Dummy variable which takes the value 1 if the target is active in a high R&D industry. High R&D industries are: Business Services, Electronic Equipment, and Pharmaceutical Products. An industry is considered a high R&D industry if the industry median level of R&D expenditures to assets is in the top 5 across Fama-French 48 industries. (Source: Compustat, Amadeus).
Asset Deal	Dummy variable which takes the value 1 if the transaction is an asset deal (i.e., the target is a list of assets and liabilities which will transfer to the buyer), and 0 if it is a share deal or a combination of a share and an asset deal. (Source: Acquisition contracts).
Seller	
Relative Size	Variable indicating the size of the buyer relative to the seller. To create this variable, we first calculate the ratio of the assets of the buyer to the assets of the seller. We then divide this ratio into ten deciles. The resulting variable therefore ranges between 1 and 10, with 10 (1) indicating that the buyer is very large (small) relative to the seller. Transactions in which the seller is a private person or family, and transactions in which the buyer is a government organization are coded such that the relative size variable takes the value 10. (Source: Financial accounts buyer and seller, Amadeus).
Seller Publicly-Listed	Dummy variable which takes the value 1 if the seller is publicly-listed 0 otherwise. If there are more sellers, the variable takes the value 1 if the company that sells the highest portion of shares is publicly-listed, and 0 otherwise. (Source: Merger Market, Amadeus).

Appendix A-3.1 (Continued)

Seller Deal Experience	Number of transactions that a seller has been engaged in over the 5 years preceding the signing date of a contract. (Source: Merger Market).
Seller Bank Advice	Dummy variable which takes the value 1 if the seller has obtained advice form an investment bank for this deal, and 0 otherwise. (Source: Merger Market).
Seller Bank Top 10	Dummy variable which takes the value 1 if the bank representing the seller is ranked in the top 10 based on a ranking of banks using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).
First Draft By Seller	Dummy variable which takes the value 1 if the first draft of a contract was provided by the lawyer who represents the seller, and 0 if the first draft of a contract was provided by the lawyer who represents the buyer. (Source: Acquisition files).
Buyer	
Buyer Publicly-Listed	Dummy variable which takes the value 1 if the buyer is listed on a stock exchange, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that buys the highest portion of the shares is a listed on a stock exchange, and 0 otherwise. (Source: Merger Market, Amadeus).
Buyer Deal Experience	Number of transactions that a buyer has been engaged in over the 5 years preceding the signing date of a contract. (Source: Merger Market).
Buyer Bank Advice	Dummy variable which takes the value 1 if the buyer has obtained advice form an investment bank for this deal, and 0 otherwise. (Source: Merger Market).
Buyer Bank Top 10	Dummy variable which takes the value 1 if the bank representing the buyer is ranked in the top 10 based on a ranking of banks using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).
First Draft By Buyer	Dummy variable which takes the value 1 if the first draft of a contract was provided by the lawyer who represents the buyer, and 0 if the first draft of a contract was provided by the lawyer who represents the seller. (Source: Acquisition files).
Toehold Deal	Dummy which takes the value 1 if the buyer owns some shares in the target prior to the signing of the contract, and 0 otherwise. (Source: Acquisition contracts).
Deal	
Cross-Country Deal	Dummy variable which takes the value 1 if the target is not located in the same country as the buyer, and 0 otherwise. (Source: Amadeus).
Approvals Required	Number of approvals which are to be obtained from competition or financial authorities between the signing date and the transfer date of a contract. The transfer date is the date at which there is a transfer of control of the target through the transfer of shares or assets. (Source: Acquisition contracts).
Deal After 2008	Dummy variable which takes the value 1 if the contract is signed on or after January 1, 2008 (i.e., during the financial crisis), and 0 otherwise. (Source: Acquisition contracts).
Controlled Auction	Dummy variable which takes the value 1 if the transaction is organized through a controlled auction, and 0 otherwise. (Source: Merger Market).
Contract Design	(Source for all contract design variables: Acquisition contracts)
Warranties	Number of warranties in a contract. Warranties provide statements about target (or seller) quality. Each separate quality statement is considered as a separate warranty.
Covenants	Number of covenants in a contract. Covenants prescribe the behavior of the target and the seller in the period between the signing date and the closing (transfer) date. Each separate prescription of behavior is considered a separate covenant.
%Warranties w/o Qualifier	Percentage of warranties in a contract which are not qualified with the statement: "so far as the seller is aware" (or any equivalent thereof)

Appendix A-3.1 (Continued)

Warranties Fully True	Dummy variable which takes the value 1 if a contract stipulates a clause that states that the warranties are true without any materiality qualifier, and 0 if the contract stipulates that the warranties are only materially true.
%Payment Secured	Percentage of the total transaction value which is secured to be available for claims the buyer might have at a later point in time towards the seller. This money is secured by placing it in an Escrow account, an obligation to maintain cash reserves, or a bank guarantee. This variable is winsorized at 5%.
MAC Strength Index	Index ranging between 0% and 100% which reflects the extent to which the risk of a material adverse event is allocated to the seller (100%) or the buyer (0%). We construct the variable in the following way: Contracts which stipulate a MAC clause have a value of 100% minus a reduction for each exception to the MAC clause which is included the contract. Each exception has a weight 1/13 (the maximum number of exceptions is 13), such that the variable equals (1 – (1/13 * number of exceptions) for contracts containing a MAC and zero for those without a MAC clause.
Warranties per Category (Source for all warranties per category variables: Acquisition contracts)	
Corporate Records	Number of warranties within the category: "Corporate Records", which describe the target's corporate documents, capital structure, and the authority of the seller to sign the contract.
Financial Accounts	Number of warranties within the category: "Financial Accounts", which describe the quality of the financial accounts of the target, the tax administration, as well any events that might have occurred since those accounts.
Contracts	Number of warranties within the category: "Contracts", which describe the validity and enforceability of the target's contractual relations, the compliance with these contracts, the continuation of these contracts, and excludes the possibility of abnormal contracts.
Employees	Number of warranties within the category: "Employees", which describes the employee agreements of the target, as well as the retirement plans, and any collective agreements.
Intellectual Property	Number of warranties within the category: "Intellectual Property", which describes the intellectual property rights and information technology of the target.
Assets	Number of warranties within the category: "Assets", which describes the ownership rights, the user rights, and quality of the assets of the target, including the equipment and the real estate.
Insurance	Number of warranties within the category: "Insurance", which describe the insurance coverage of the target, as well as outstanding insurance claims.
Legal	Number of warranties within the category: "Legal", which describes the compliance of the target with laws in general, and competition and environmental laws specifically. Plus, it includes the involvement of target company in legal disputes.
Covenants per Category (Source for all covenants per category variables: Acquisition contracts)	
Corporate Records	Number of covenants in the category: "Corporate Records", which limit the behavior of the seller/target to change the charter documents or the corporate structure of the target.
Employees	Number of covenants in the category: "Employees", which limit the behavior of the seller/target to enter into, amend or terminate any contracts with employees.
Dividend Payments	Number of covenants in in the category: "Dividend Payments", which limit the behavior of the seller/target to make distributions to itself from target funds.
Debt	Number of covenants in the category: "Debt", which limit the behavior of the seller/target to issue new debt or extend loans.
Business Conduct	Number of covenants in the category: "Business Conduct", which limit the behavior of the seller/target to change the general business operations of the target.

Appendix A-3.1 (Continued)

Acquisitions	Number of covenants in the category: "Acquisitions", which limit the behavior of the seller/target to acquire material assets.
Divestments	Number of covenants in a contract in the category: "Divestments", which limit the behavior of the seller/target to dispose of material assets.
Litigation	Number of covenants in a contract in the category: "Litigation", which limit the behavior of the seller/target to settle legal claims
Other Contract Provisions	
Conditional Payment	Dummy variable which takes the value 1 if (part of) the payment contains a conditional element, and 0 otherwise. Earn out payments and equity payments are considered conditional payments. (Source: Acquisition contracts).
Price Adjustments	Number of purchase price adjustments contained in a contract. A purchase price adjustment is an agreed upon adjustment of the transaction value if the book values of the target are different on the transaction date than on the signing date, for specified items in the target accounts (e.g., Debt, Equity, Cash, Net Operating Capital). This variable indicates for how many of these items such an adjustment is included in a contract. (Source: Acquisition contracts).
MAC Clause	Dummy variable which takes the value 1 if the contract stipulates that the transaction does not have to be completed if a material adverse event occurs in the period between the signing date and the closing (transfer) date, and 0 otherwise. (Source: Acquisition contracts).
Law Firm	
Law Firm High Warranty Style	Dummy variable from Karsten (2013) that reflects the propensity of a law firm to include many warranties. To create this variable, we first calculate the coefficients on law firm fixed effects in a regression on Warranties/Model Contract that controls for the economic determinants. Second, we create a dummy which takes the value 1 for contracts drafted by law firms whose estimated coefficients on the law firm fixed effects are above median across all law firms, and 0 otherwise. (Source: Acquisition contracts)
Law Firm Warranty Style Quartiles	Four dummy variables derived from Karsten (2013) that reflect the propensity of a law firm to include many warranties. To create these variables, we first calculate the coefficients on law firm fixed effects in a regression on Warranties/Model Contract that controls for the economic determinants. Second, we rank the law firms on their law firm fixed effect coefficients, and divide them into four groups. We create four dummy variables for contracts drafted by a law firm in each of these groups, where Law Firm Warranty Style Quart 1 represents the law firms with the lowest tendency to include warranties and Law Firm Warranty Style Quart 4 the law firms with the highest tendency.
Law Firm High Covenant Style	Dummy variable derived from Karsten (2013) which reflects the propensity of a law firm to include many covenants. To create this variable, we first calculate the coefficients on law firm dummies in a regression with Covenants/Model Contract as dependent variable and various controls and the law firm dummies as independent variables. Second, we create a dummy which takes the value 1 for all law firms whose estimated coefficients on the law firm dummies are in the upper half across all coefficients, and 0 otherwise.
Law Firm Covenant Style Quartiles	Four dummy variables derived from Karsten (2013) that reflect the propensity of a law firm to include many covenants. To create these variables, we first calculate the coefficients on law firm fixed effects in a regression on Covenants/Model Contract that controls for the economic determinants. Second, we rank the law firms on their law firm fixed effect coefficients, and divide them into four groups. We create four dummy variables for contracts drafted by a law firm in each of these groups, where Law Firm Covenant Style Quart 1 represents the law firms with the lowest tendency to include covenants and Law Firm Covenant Style Quart 4 the law firms with the highest tendency.

Appendix A-3.2
Additional Descriptive Statistics

Panel A of this table shows the distribution of the Acquisition Premium across deal years and target industries. Panel B reports correlation coefficients between contract design measures. Panel C given examples of frequently used exceptions to the MAC. The second column of this panel indicates the percentage of the contracts that contain a MAC which include this specific exception. Panel D reports correlation coefficients between explanatory variables. * indicates significance at the 5% level.

Panel A: Distribution of Acquisition Premium

	Acquisition Premium		
Year	**Mean**	**Median**	**Obs.**
2005	178%	135%	8
2006	236%	150%	38
2007	260%	169%	45
2008	304%	200%	25
2009	252%	119%	22
2010	168%	129%	8
Target Industry	**Mean**	**Median**	**Obs.**
Wholesale & Retail	228%	144%	22
Business Equipment	394%	271%	19
Manufacturing	182%	153%	13
Money & Finance	145%	109%	16
Chemicals	153%	143%	8
Consumer Non-Durables	147%	117%	7
Other	267%	176%	61

Panel B: Correlations of Contract Design Measures

		Warranties	Covenants	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Strength Index
		(1)	(2)	(3)	(4)	(5)	(6)
Warranties	(1)	1.000					
Covenants	(2)	0.227*	1.000				
%Warranties w/o Qualifier	(3)	0.022	0.007	1.000			
Warranties Fully True	(4)	0.264*	0.220*	0.207*	1.000		
%Payment Secured	(5)	0.263*	-0.046	0.147	0.183*	1.000	
MAC Strength Index	(6)	0.178*	0.264*	0.025	0.148	0.103	1.000

Panel C: Examples of MAC Exceptions

MAC Exceptions:	**Sample**
Any change is not considered a material adverse change if it is the result of:	
An event arising from (the announcement of) this transaction.	29%
A change in economic conditions or financial markets in general	47%
Changes in economic or market conditions in the industry of the target.	53%
A change in laws or regulations.	45%
A change in generally accepted accounting principles.	31%
Acts of war, armed hostilities, sabotage or terrorism.	27%

Appendix A-3.2 (Continued)

Panel D: Correlations of Explanatory Variables

		Target Value (log)	Target EBIT/ Assets	Target Leverage	High R&D Industry	Rel. Size	Deal After 2008	Controlled Auction	Toe-hold Deal	First Draft by Buyer	Seller Publicly Listed	Buyer Publicly Listed	Cross-Country Deal	Asset Deal
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Target Book Value (log)	(1)	1.00												
Target EBIT/Assets	(2)	-0.34*	1.00											
Target Leverage	(3)	-0.03	-0.17*	1.00										
High R&D Industry	(4)	-0.35*	0.10	-0.04	1.00									
Relative Size	(5)	-0.28*	0.13	0.07	0.03	1.00								
Deal After 2009	(6)	0.06	-0.01	0.02	-0.08	0.11	1.00							
Controlled Auction	(7)	0.13	-0.01	0.01	0.19*	-0.12	-0.03	1.00						
Toehold Deal	(8)	0.02	-0.06	-0.01	-0.01	0.02	0.13	-0.09	1.00					
First Draft by Buyer	(9)	-0.38*	0.06	0.01	0.01	0.47*	0.12	-0.43*	0.19*	1.00				
Seller Publicly-Listed	(10)	0.22*	-0.08	-0.04	0.04	-0.52*	-0.19*	0.06	0.05	-0.35*	1.00			
Buyer Publicly-Listed	(11)	0.00	-0.11	-0.02	0.05	0.20*	-0.01	0.02	-0.06	-0.01	0.11	1.00		
Cross-Country Deal	(12)	0.01	-0.13	-0.02	0.29*	-0.02	0.03	0.08	-0.06	-0.20*	0.07	0.37*	1.00	
Asset Deal	(13)	-0.10	-0.08	0.03	-0.09	-0.26*	-0.09	0.06	-0.05	-0.08	0.12	0.02	-0.23*	1.00
Approvals Required	(14)	0.52*	-0.15	0.05	-0.07	-0.15	-0.03	0.15	-0.04	-0.31*	0.11	0.11	0.24*	-0.13

Appendix A-3.3
First Stage Regressions of Warranties and Covenants per Category

This table reports OLS regressions of the warranties per category (Panel A) and covenants per category (Panel B) on the Law Firm Fixed effects. All regressions control for economic determinants of acquisition premiums. Detailed variable definitions are provided in Appendix A-3.1. The sample covers 146 M&A transactions conducted in the period between 2005 and 2010, but the regressions are on fewer observations because of missing data for some variables. For the Law Firm Fixed Effects, we report the *F*-statistic and *p*-value of their joint significance. The table also reports the Partial R-squared of the Law Firm Fixed Effects, the Kleibergen-Paap LM-statistic, and the Hansen J-Statistic from 2SLS regressions of the Acquisition Premium on contract provisions (reported in Table 3.3). In parentheses are *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: First Stage Regressions on Warranties per Category

	Dependent Variable: Warranties per Category							
Warranty Categories:	Corporate Records	Employee	Financial Accounts	Assets	Contracts	Insurance	Intellect. Property	Legal
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm FE:	98.78	135.86	123.61	58.07	73.57	32.05	163.82	11,537.18
F-test (*p*-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Obs.	140	140	140	140	140	140	140	140
Adj. R^2	0.469	0.204	0.446	0.068	0.286	0.147	0.132	0.285
Partial R^2 Instruments	0.428	0.340	0.243	0.193	0.304	0.265	0.213	0.355
Kleibergen-Paap LM:	36.48	29.98	24.11	23.48	26.97	27.98	22.59	26.12
χ^2-test (*p* -value)	(0.105)	(0.315)	(0.624)	(0.658)	(0.466)	(0.412)	(0.707)	(0.512)
Hansen J:	25.09	24.52	26.78	24.12	26.36	24.99	29.11	25.40
χ^2-test (*p* -value)	(0.514)	(0.547)	(0.421)	(0.569)	(0.444)	(0.519)	(0.306)	(0.496)

Panel B: First Stage Regressions on Warranties per Category

	Dependent Variable: Covenants per Category							
Covenant Categories:	Corporate Records	Employee	Dividend Payments	Debt	Business Conduct	Acquis.	Divest.	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Law Firm FE:	191.03	435.86	84.08	124.22	2,449.69	97.72	385.03	36.95
F-test (*p*-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Obs.	141	141	141	141	141	141	141	141
Adj. R^2	0.168	0.294	0.339	0.166	0.357	0.339	0.489	0.241
Partial R^2 Instruments	0.173	0.353	0.200	0.170	0.319	0.269	0.394	0.209
Kleibergen-Paap LM:	25.77	31.46	32.13	29.56	25.27	29.48	36.50	26.63
χ^2-test (*p* -value)	(0.531)	(0.253)	(0.227)	(0.334)	(0.560)	(0.338)	(0.105)	(0.484)
Hansen J: χ^2-test (*p* -value)	25.92 (0.468)	26.17 (0.304)	16.85 (0.914)	23.96 (0.578)	24.30 (0.559)	21.56 (0.712)	22.79 (0.645)	26.36 (0.555)

Appendix A-3.4
Acquisition Premium: Effects of Warranties and Covenants per Category

This table reports OLS regressions to explain the effects of warranties and covenants per category on acquisition premiums in M&A transactions. The dependent variable in all regressions is the Acquisition Premium, and all regressions control for the control variables in Column 1 of Table 3.3. In addition, Panel A includes the warranties per category and Panel B includes the covenants per category. Detailed definitions of all variables are in Appendix A-3.1. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** indicates significance at 5% and * indicates significance at 10%.

Panel A: OLS Regressions: Warranties per Category

	Dependent Variable: Acquisition Premium							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Warranty Categories:	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellect. Property	Legal
Warranties per Category	0.04	0.02	0.02**	-0.00	0.02	-0.01	0.04	-0.00
	(1.42)	(0.94)	(2.20)	(-0.01)	(1.49)	(-0.22)	(1.59)	(-0.05)
Obs.	140	140	140	140	140	140	140	140
Adj. R^2	0.426	0.420	0.432	0.416	0.421	0.416	0.434	0.416

Panel B: OLS Regressions: Covenants per Category

	Dependent Variable: Acquisition Premium							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Covenant Categories:	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquis.	Divest.	Litigation
Covenants per Category	0.14	0.19	0.11**	0.15	0.07	0.15	0.30	0.53*
	(1.35)	(1.64)	(2.19)	(1.13)	(1.64)	(0.88)	(1.59)	(1.75)
Obs.	141	141	141	141	141	141	141	141
Adj. R^2	0.422	0.437	0.432	0.426	0.435	0.421	0.432	0.433

Appendix A-3.5
Acquisition Premium: Law Firm Style Quartiles as Instrumental Variables

This table reports first and second stage regression results of acquisition premiums on warranties (per category) and covenants (per category), using Law Firm Warranty (Covenant) Style Quartile dummies as instruments. Panel A reports first stage regressions of warranties on Law Firm Warranty Quartile dummies, reflecting the distribution of law firms to include warranties in their drafts. Panel B reports first stage regressions of the covenants on Law Firm Covenant Style Quartile dummies. In both panels, we report the Partial R-squares of these quartiles dummies, as well as the *F*-statistic and *p*-value of their joint significance. Panels A and B also report the Kleibergen-Paap LM-statistic and the Hansen J-statistic from the second stage regressions. Panels C and D report regressions of acquisition premiums on warranties (Panel C) and covenants (Panel D), using Law Firm Warranty (Covenant) Style Quartiles as instruments. All regressions control for the variables as in Table 3.3 column 1. Detailed definitions are in Appendix A-3.1. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: First Stage Regressions: Warranties and Law Firm Quartiles of Warranty Style

	Dependent Variable: Warranties								
	Warranties	**Warranties per Category**							
	Total	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellectual Property	Legal
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Law Firm Warranty Style Quart 2	1.98	-1.76	-2.39	1.27	2.00	-0.03	-0.31	1.28	1.34
	(0.16)	(-0.83)	(-0.87)	(0.40)	(1.10)	(-0.02)	(-0.41)	(0.79)	(0.92)
Law Firm Warranty Style Quart 3	24.80*	0.83	2.28	4.49	0.77	6.27**	-0.27	2.87	7.62**
	(1.81)	(0.29)	(0.67)	(1.14)	(0.30)	(2.24)	(-0.30)	(0.92)	(2.41)
Law Firm Warranty Style Quart 4	65.85***	4.61	10.45**	17.21***	5.66*	10.09***	1.36	9.44**	6.78***
	(3.18)	(1.60)	(2.44)	(3.00)	(1.84)	(3.32)	(1.37)	(2.38)	(3.66)
Obs.	140	140	140	140	140	140	140	140	140
Adj. R^2	0.360	0.313	0.161	0.473	0.101	0.297	0.095	0.168	0.228
Partial R^2 Instruments	0.143	0.078	0.133	0.104	0.031	0.146	0.230	0.060	0.133
Instruments *F*-test (*p*-value)	6.57	3.52	5.95	3.68	1.22	7.04	1.77	2.09	6.67
	(0.000)	(0.017)	(0.001)	(0.014)	(0.305)	(0.000)	(0.156)	(0.105)	(0.003)
Kleibergen-Paap LM: χ^2-test (*p* -value)	10.75	6.66	10.62	6.74	3.46	10.28	3.80	4.93	11.22
	(0.013)	(0.083)	(0.014)	(0.081)	(0.326)	(0.016)	(0.284)	(0.177)	(0.011)
Hansen J: χ^2-test (*p* -value)	3.69	1.33	2.34	4.69	6.53	3.06	2.17	5.62	3.59
	(0.158)	(0.514)	(0.311)	(0.096)	(0.038)	(0.217)	(0.339)	(0.060)	(0.166)

Appendix A-3.5 (Continued)

Panel B: First Stage Regressions: Covenants and Law Firm Quartiles of Covenant Style

	Dependent Variable: Covenants								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Law Firm Covenant Style Quart 2	5.43*	0.02	0.29	1.08	0.15	2.39*	0.55*	0.60**	0.35**
	(1.80)	(0.06)	(0.53)	(1.18)	(0.37)	(1.89)	(1.86)	(2.16)	(2.15)
Law Firm Covenant Style Quart 3	6.49***	0.96***	0.76	1.69***	0.76**	1.25	0.23	0.72**	0.11
	(2.94)	(3.24)	(1.58)	(3.02)	(2.36)	(1.18)	(0.88)	(2.49)	(0.67)
Law Firm Covenant Style Quart 4	14.38***	0.34	2.24***	2.69***	1.35**	5.18**	0.72***	1.35***	0.50**
	(3.54)	(1.02)	(3.35)	(2.86)	(2.48)	(2.48)	(2.81)	(4.13)	(2.09)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.437	0.238	0.229	0.400	0.244	0.322	0.314	0.437	0.293
Partial R^2 Instruments	0.140	0.060	0.122	0.098	0.065	0.106	0.058	0.170	0.086
Instruments F-test (*p*-value)	5.56	3.56	4.25	5.29	3.16	2.72	3.17	6.75	2.87
	(0.001)	(0.016)	(0.007)	(0.002)	(0.027)	(0.040)	(0.027)	(0.000)	(0.039)
Kleibergen-Paap LM: χ^2-test (*p* -value)	13.04	9.01	9.86	15.26	8.13	6.87	8.40	14.07	8.88
	(0.005)	(0.029)	(0.020)	(0.002)	(0.043)	(0.076)	(0.038)	(0.003)	(0.031)
Hansen J: χ^2-test (*p* -value)	4.84	9.00	9.66	1.97	5.80	3.79	0.64	4.39	0.81
	(0.089)	(0.011)	(0.008)	(0.374)	(0.055)	(0.150)	(0.726)	(0.112)	(0.667)

Appendix A-3.5 (Continued)

Panel C: 2SLS Regressions: Warranties and Warranties per Category

	Dependent Variable: Acquisition Premium								
	Warranties	**Warranties per Category**							
	Total	Corporate Records	Employees	Financial Accounts	Assets	Contracts	Insurance	Intellectual Property	Legal
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Warranties	0.02**	0.23**	0.11***	0.05*	-0.05	0.11*	0.66	0.08	0.13
	(2.00)	(2.48)	(2.61)	(1.70)	(-0.34)	(1.86)	(1.32)	(1.39)	(1.27)
Obs.	140	140	140	140	140	140	140	140	140
Adj. R^2	0.388	0.214	0.309	0.408	0.396	0.347	-0.026	0.404	0.325

Panel D: 2SLS Regressions: Covenants and Covenants per Category

	Dependent Variable: Acquisition Premium								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Covenants	0.13***	0.78*	0.67***	0.67***	1.02**	0.38***	2.61***	1.41***	3.78**
	(3.23)	(1.89)	(2.86)	(3.10)	(2.00)	(2.74)	(2.64)	(3.40)	(2.39)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.232	0.325	0.314	0.068	0.112	0.092	.	0.231	.

Appendix A-3.6
Additional Robustness Checks

Panel A reports regressions of acquisition premiums on financial accounts warranties (left half) and covenants (right half). In addition, Columns 1 and 4 control for Industry Fixed Effects (based on the 12 Fama French industries), Columns 2 and 5 control for Buyer Bank Advice and Seller Bank Advice, and Columns 3 and 6 control for Buyer Bank Top 10 and Seller Bank Top 10. Panel B reports regressions of acquisition premiums on financial accounts warranties (left half) and covenants (right half). The regressions in Panel B control for: Price Adjustments (nr.); Conditional Payment; and MAC Clause. Panels C and D report regressions of acquisition premiums on covenants (Column 1) and covenants per category (Columns 2 to 9). Panel C controls for contracts with at least one covenant (Total Covenants Non-Zero). Panel D controls for deals with at least one day between signing and closing. All regressions in this table are 2SLS regressions, using Law Firm Fixed Effects as instruments, and control for the variable in Column 1 of Table 3.3. Detailed variable definitions are in Appendix A-3.1. We report in parentheses *t*-statistics, calculated using robust standard errors. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Controlling for Target Industry and Investment Banks

	Dependent Variable: Acquisition Premium					
	(1)	(2)	(3)	(4)	(5)	(6)
Financial Accounts Warranties	0.07***	0.06***	0.06***			
	(3.25)	(2.85)	(2.66)			
Covenants				0.10***	0.10***	0.10***
				(3.02)	(3.06)	(2.83)
Industry Fixed Effects	YES	NO	NO	YES	NO	NO
Buyer Bank Advice		0.56			0.62*	
		(1.57)			(1.68)	
Seller Bank Advice		0.28			-0.41	
		(0.72)			(-1.04)	
Buyer Bank: Top 10			0.14			0.15
			(0.47)			(0.46)
Seller Bank: Top 10			-0.42			-0.80*
			(-1.12)			(-1.78)
Obs.	140	140	140	141	141	141
Adj. R^2	0.363	0.406	0.390	0.302	0.341	0.356

Panel B: Controlling for Other Contract Provisions

	Dependent Variable: Acquisition Premium							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Financial Accounts	0.04**	0.06***	0.07***	0.06***	-0.00			
Warranties	(2.21)	(2.77)	(2.95)	(2.75)	(-0.15)			
Covenants	0.02				0.11***	0.11***	0.11***	0.11***
	(1.24)				(2.84)	(2.98)	(3.52)	(2.92)
Price Adjustments		0.15				0.18		
(Nr.)		(1.40)				(1.58)		
Conditional			0.59				0.60	
Payment			(1.12)				(1.19)	
MAC Clause				-0.05				-0.76*
				(-0.15)				(-1.74)
Obs.	140	140	140	140	140	141	141	141
Adj. R^2	0.429	0.392	0.386	0.389	0.322	0.331	0.313	0.329

Appendix A-3.6 (Continued)

Panel C: Covenants: Controlling for Deals with at least One Covenant

	Dependent Variable: Acquisition Premium								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Covenants	0.09**	-0.20	0.45**	0.31**	0.07	0.15	0.30	0.79**	0.21
	(2.34)	(-0.51)	(2.18)	(2.47)	(0.27)	(1.64)	(0.84)	(2.31)	(0.42)
Covenants Non-Zero	-1.20	0.69	-0.46	-0.36	0.29	-0.57	0.03	-0.45	0.37
	(-1.53)	(0.88)	(-0.79)	(-0.57)	(0.41)	(-0.89)	(0.04)	(-0.80)	(0.75)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.402	0.406	0.404	0.384	0.422	0.421	0.412	0.395	0.427

Panel D: Covenants: Controlling for Deals with Non-zero Time Between Signing and Closing

	Dependent Variable: Acquisition Premium								
	Covenants	**Covenants per Category**							
	Total	Corporate Records	Employees	Dividend Payments	Debt	Business Conduct	Acquisitions	Divestments	Litigation
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Covenants	0.11**	-0.13	0.49**	0.31**	0.21	0.17*	0.44	0.81**	0.24
	(2.39)	(-0.34)	(2.33)	(2.53)	(0.73)	(1.81)	(1.04)	(2.32)	(0.48)
Time Signing - Closing Non-Zero	-1.08	0.95	-0.13	-0.05	0.41	-0.34	0.25	-0.09	0.72
	(-1.20)	(1.25)	(-0.21)	(-0.08)	(0.63)	(-0.49)	(0.33)	(-0.15)	(1.47)
Obs.	141	141	141	141	141	141	141	141	141
Adj. R^2	0.342	0.430	0.385	0.381	0.426	0.397	0.403	0.385	0.440

4

M&A Negotiations and Lawyer Expertise[1]

4.1 Introduction

How do corporate lawyers negotiate over contracts in M&A deals? Do lawyers that advise buyers and sellers mainly cooperate to write contracts that best resolve economic and legal issues surrounding an acquisition? Or do they negotiate competitively to achieve contract outcomes that are primarily favorable to their own client, at the expense of the counterparty? To investigate these questions, we use the market for acquisitions of private targets as a laboratory. Specifically, we investigate whether lawyers with more legal expertise yield better negotiation outcomes for their own clients.

Negotiations in corporate acquisitions involve buyers and sellers, but also investment banks that advise on financial issues, and lawyers that provide legal counsel. Financial literature has produced substantial evidence on how the characteristics of buyers, sellers, and investment banks affect M&A outcomes.[2] To the contrary, though very important for M&A transactions, we know little about how lawyers affect

[1] The research in this chapter is joint work with Z. Sautner.

[2] Examples of buyer and seller characteristics include Shleifer and Vishny (1989), Lang, Stulz, and Walkling (1991), Harford (1999), Bargeron et al. (2008), Masulis, Wang, and Xie (2007), Moeller (2005), and Stulz, Walkling, and Song (1990). For investment bank characteristics, see Kale, Kini, and Ryan (2003), Rau (2000), Servaes and Zenner (2000), Bao and Edmans (2012), Golubov, Petmezas, and Travlos (2012), and Ertugul and Krishnan (2011).

acquisitions.[3] This lack of empirical evidence is due to the difficulty of observing "outcomes" of lawyer negotiations, as the contracts that lawyers advise on –for example- are usually not publicly available.

Our paper tries to close this gap by shedding light on the role of lawyer expertise in the negotiation process, which has usually been treated as a "black box". We contrast two views of how lawyer expertise may affect negotiations. According to the *cooperative-advice hypothesis,* the main objective of lawyers is to jointly execute legal elements of a transaction and to mitigate any economic issues that arise between buyers and sellers. Under this view, lawyer expertise is used to maximize the joint value of both parties, for example by reducing transaction costs and facilitating deal completion (e.g., Gilson (1984) or Mnookin, Peppet, and Tulumello (2000)). Conversely, the *competitive-advice hypothesis* holds that lawyers primarily compete with each other to achieve negotiation outcomes that are in favor of their own clients' interests. According to this view, lawyers who possess more legal expertise relative to the counterparty distribute value towards their own clients at the expense of the counterparty. Whereas both hypotheses are not mutually exclusive, support of the *competitive-advice hypothesis* would suggest that the involvement of lawyers in M&A deals can have distributive welfare implications.

We investigate these questions using data from detailed law firm files of 151 acquisitions of privately held targets that were executed between 2005 and 2010.[4] These files have been made available by one of the largest law firms in The Netherlands, and include the original contracts signed between buyers and sellers. Our data further allow us to identify the individual lawyers advising both buyers and sellers. To analyze the effects of expertise, we create for each transaction several proxies for the expertise of the buyer lawyer *relative* to that of the seller lawyer ("relative lawyer expertise"). We construct these measures for the two parties' lead lawyers, who are usually partners at their firms and oversee all legal aspects of M&A negotiations for their clients. Our

[3] Karsten (2013) provides evidence that styles, for example expertise, of law firms and lawyers can explain (part of) the variation in contract provisions, but does not document *how* these styles affect contracts.

[4] Acquisitions of privately held targets constitute a large proportion of mergers and acquisitions. For example, 96% of the cross-border transactions in Erel, Liao, and Weisbach (2012) involve privately held targets. Betton, Eckbo, and Thorburn (2007) document for US takeovers that about 63% of targets are privately held.

expertise proxies span different dimensions of legal expertise, covering both aspects of experience and education. Our sample contains 112 different lead lawyers—20 of them work for our law firm.

To test whether a divergence in legal expertise results in outcomes that are in favor of one party at the expense of the other, we focus on negotiation outcomes where the incentives of buyers and sellers are relatively contradictory. Measuring outcomes of M&A negotiations is challenging as they are often simultaneously determined or unobservable. Our acquisition files allow us to quantity negotiation outcomes across three important dimensions, namely contract design, the bargaining process, and acquisition pricing.

We first look at the effects of relative lawyer expertise on contract design as the drafting of acquisition contracts is typically the main duty of lawyers. We focus our analysis on contract provisions that affect how risks are allocated between buyers and sellers, as incentives are most conflicting there. For any given price, buyers prefer to allocate a maximum level of risk to sellers, while sellers prefer the opposite.[5]

Our first three measures of contract design relate to the allocation of risk through warranties. Warranties are guarantee statements by sellers about the quality of a target. Though warranties can perform a signaling function if sellers are better informed about target quality (e.g., Grossman (1981)), they also provide insurance when they concern issues that both buyers and sellers are unaware of.[6] Due to the signaling value of warranties, buyers and sellers typically do not use warranties themselves to allocate risk. Instead, risk allocation is usually negotiated through related provisions that affect the scope and enforceability of warranties. We consider three types of such provisions. First, warranties may come with the statement "so far as the seller is aware," which means that they are not enforceable if a seller was unaware of a warranty violation at the time of signing (Freund (1975)). As a result, circumstances unknown to both parties are not covered through warranties with such qualifications, and risks are reallocated back to the

[5] Our tests on contract design control for the acquisition price. We show they are robust to adding proxies for relative bargaining power and risk-bearing capacity of buyers and sellers.

[6] For example, sellers may warrant that there is no legal dispute pending or threatened at the time of signing. If sellers are not fully certain about this issues, any remaining risk of legal disputes lies with the sellers, who would have to cover the damages if such litigation occurs.

buyers. Sellers, therefore, prefer the inclusion of many knowledge qualifiers, whereas buyers prefer as few as possible. To capture the risk allocated to sellers, our first measure is the percentage of warranties that come without knowledge qualifiers.

Second, sellers can reduce their risk exposure by adding an overarching qualifier, which states that any warranty is only violated if it is untrue "in a material respect." As with the knowledge qualifiers, this statement reduces the enforceability of warranties, because the requirement that a potential breach needs to be material provides sellers with counter-arguments in case of warranty enforcement (see Kling, Simon, and Goldman (1996)). Buyers therefore prefer warranties that are required to be fully true, whereas sellers prefer the opposite.

Third, buyers' risk exposure from warranties is larger if sellers have insufficient funds to cover damages at the time of a claim. Buyers can protect themselves against this by requiring sellers to put aside part of the acquisition payment as collateral. Naturally, buyers prefer this collateral to be high, whereas sellers prefer the opposite.

Our empirical analysis of these contract provisions provides support for the *competitive-advice hypothesis;* we find that more expertise of the buyer lawyer relative to the seller lawyer is associated with more risks being are allocated to sellers. Specifically, we show that higher buyer lawyer expertise is related to more warranties without knowledge qualifiers, a higher probability that warranties need to be fully true, and a higher percentage of the payment being secured against future claims.

Warranty-related provisions refer to risks of situations existing at the time of signing that neither buyers nor sellers are aware of. Another important risk in acquisitions arises because of potentially adverse events that can occur between the signing and closing (or target transfer) dates. This risk typically lies with buyers as they committed themselves to purchase the target at a price that was fixed at the signing date. However, contracts can shift this risk to sellers through inclusion of a MAC clause, which allows buyers to cancel the deal if the target suffers a material adverse change (MAC) before closing. While buyers prefer the inclusion of such a clause, sellers prefer not to carry this risk (see Denis and Macias (2012)). Therefore, our fourth measure of risk allocation is the presence of a MAC clause. Similar to warranties, MAC clauses can come

with exceptions, where each exception states a scenario in which the MAC clause does not apply. To capture the extent of these exceptions, we create an index that measures the strength of a MAC clause by calculating the number of exceptions added.

Consistent with the *competitive-advice hypothesis*, we find that more relative buyer lawyer expertise increases both the probability that a MAC clause is added and the strength of a MAC clause.

In addition to contract design, we assess the impact of lawyer expertise on two other negotiation outcomes: the bargaining process and acquisition pricing. Negotiation strategies during the bargaining process have implications for both contract design and pricing, and expert lawyers can influence this process by pushing negotiations in their clients' favor.

As a first element of the bargaining process, we look at the party who provides the first draft of the acquisition contract as this allows for a first-mover advantage for the upcoming negotiations by setting a reference point (e.g., Molod (1994)). We find that more relative legal expertise on the buyer side is associated with a higher probability that the buyer can provide the first draft. Next, we consider the duration of deal negotiations and closing times. Buyers benefit from shorter negotiations as they reduce agency problems at target management, save transaction costs, and avoid that the period of exclusive negotiations expires.[7] Sellers also benefit from shorter negotiations because of lower transaction costs, but this comes at a cost as it reduces their opportunities to look for alternative bidders. Similarly, buyers prefer shorter times between signing and closing, as sellers keep control over the target until the closing date, which allows them to extract private benefits. We show that more buyer legal expertise is associated with both shorter negotiation and shorter closing times.

Finally, we study the impact of lawyer expertise on acquisition pricing. Whereas lawyers are generally not the primary parties bargaining over acquisition prices, negotiations during the due diligence and contract drafting process often result in adjustments of the initial prices. Lawyer expertise on the buyer side can, for example,

[7] Transactions usually start with a letter of intent, which specifies an exclusivity period in which sellers are not allowed to negotiate with other bidders. This limits the outside opportunities of sellers.

cause adjustments if lawyers spot target quality issues during the due diligence process that justify a price reduction, or by demanding higher discounts for the inclusion of seller-friendly clauses. We find that more buyer expertise is associated with more favorable acquisition pricing (i.e., lower prices). Importantly, these results are obtained after controlling for the role of financial advisors and contract design.

Together, our results suggest that lawyers with more expertise direct negotiations outcomes in the favor of their own client, supporting the *competitive-advice hypothesis*. One concern with our analysis could be that our measures of relative lawyer expertise proxy in some way for combined lawyer expertise. This could imply that our findings reflect a relation between joint expertise and "better" contracts, supporting the *cooperative-advice hypothesis.*[8] If our expertise measures would indeed reflect combined expertise, they should also affect contract outcomes where incentives of buyers and sellers are aligned. To test this notion, we perform a set of placebo tests that relate our measures of relative lawyer expertise to provisions that increase the joint surplus of buyers and sellers. Specifically, we show that relative expertise is unrelated to the *number* of warranties and covenants, which serve important signaling and commitment functions and facilitate deal completion. Similarly, relative expertise is unrelated to the presence of earnout mechanisms, which reduce information asymmetry about future target profitability (e.g., Datar, Frankel, and Wolfson (2001), Cain, Denis, and Denis (2011)).[9] These falsification tests indicate that relative expertise only comes into play for outcomes where the objectives of buyers and sellers are conflicting.

Another concern could be that relative lawyer expertise proxies for unobserved deal or client characteristics, which could occur if lawyers are endogenously allocated to deals or clients. We address lawyer allocations based on unobservable *deal* characteristics in several ways. First, we interview the lead lawyers of our law firm to understand how lawyers get allocated to deals. The interviewees uniformly state that new deals are allocated mainly based on existing, usually long-lasting and historically

[8] Our measures could reflect joint expertise if, for example, seller lawyer expertise shows little variation across deals, implying that that higher relative expertise simply reflects more buyer expertise.

[9] These findings supports theories by Sen (2000) and Inderst and Müller (2004), which show that bargaining is less likely to occur for clauses where incentives are less adversarial.

determined, client relations.[10] Second, we follow Calomiris and Hitscherich (2007) and show that results are robust to controlling for newly initiated law firm-client relations that arise as clients switch law firms, possibly in response to deal or target characteristics. Further, our results hold for deals where law firms and clients are located in the same country, making a pre-existing lawyer-client relation very likely.

We then address lawyer allocation based on *client* characteristics. We first mitigate the concern that variation in client bargaining power and risk-bearing capacity drive our results. We show that relative expertise is not systematically related to various bargaining power and risk-bearing capacity proxies. Further, our previous results are robust to adding these proxies as controls. Lastly, we show that our findings are largely robust to adding client fixed effects, which absorb any remaining time-invariant unobserved client heterogeneity.

Our analysis is related to three papers that look at the effects of law firm characteristics on M&A outcomes. Coates (2012) studies 60 acquisition contracts to assess how relative law-firm expertise affects the use of earnouts, price adjustment clauses, and indemnification clauses. Krishnan and Masulis (2013) study how law firm rank affects completion rates and takeover premiums, and Krishnan and Laux (2007) relate law firm size to deal completion rates and acquirer returns. We further relate to Krishnan et al. (2012) who show that shareholder litigation affects M&A outcomes, and Beatty and Welch (1996) who link law firm characteristics and IPO under-pricing.

This paper is structured as follows. Section 4.2 presents the data and summary statistics. Section 4.3 describes the negotiation process during M&A transactions and describes our measures of negotiation outcomes and lawyer expertise. Section 4.4 provides the results and Section 4.5 concludes.

[10] Coates et al. (2011) provide evidence of such long lasting lawyer-client relations. In the rare case that partners leave their law firms, they frequently take their clients with them.

4.2 Data

Our sample is built around the files of 151 acquisitions of privately held targets between 2005 and 2010.[11] The files have been made available by one of the largest law firms in The Netherlands, which specializes in corporate law and mergers and acquisitions. The law firm acted as advisor of either buyers (86 deals) or sellers (65 deals). The files contain the original acquisition contracts, information on the involved lawyers, and details on the bargaining and pricing. If missing, we complete information on the involved lawyers with data from Merger Market, which contains information on financial and legal advisors in M&A transactions. To measure lawyer expertise, we collect profile data of the lawyers from the corporate webpages of their law firms, internet searches, and Merger Market. Our analysis focuses on the lead lawyers that are advising the sellers and buyers, respectively. These are usually partners at their law firms and identified in our files and in Merger Market as the lead lawyers on a transaction.

Across our sample, lead lawyers of 49 different law firms are involved in the negotiations.[12] Out of those law firms, 25 are headquartered in The Netherlands, which implies that in 74% (75%) of the deals, the buyers (sellers) are advised by a Dutch law firm.[13] Across all deals, 112 individual lead lawyers negotiate on behalf of one of the two deal sides, with the average lead lawyer advising on 2.3 deals in our sample.[14]

We complement these data with financial information on the buyers and sellers from Amadeus or their financial statements. We obtain target data from three sources: (i) financial accounts added as appendices to the acquisition contracts; (ii) financial statements of the buyers or sellers; and (iii) Amadeus or national trade registers. All financial variables are based on the year preceding the closing of a transaction.

[11] Details about sample construction and sample selection issues are provided in Karsten (2013).
[12] A total of 30 (36) law firms advised the buyers (sellers), and 17 law firms occurred as advisors of both sellers and buyers.
[13] Our sample contains many leading international law firms, including eight out of the top 10 law firms according to a Merger Market ranking based on deal volume (e.g., Clifford Chance, Linklaters, Freshfields Bruckhaus Deringer or Kirkland & Ellis).
[14] The buyers (sellers) were advised by 66 (70) different lawyers, with 24 lawyers advising both sellers and buyers. In total, 20 (18%) of the lead lawyers come from the law firm that provided the data, with 16 (17) different lawyers advising buyers (sellers). On average, each lead lawyers of our law firm advised on seven deals in the sample. Naturally, this high number is an artifact of the data and does not reflect a bias in overall deal activity outside the sample.

Table 4.1 Panel A contains summary statistics on the deals. Variable definitions are provided in Appendix A-4.1. The average transaction value in our sample is EUR 222m. Buyers and sellers are relatively equal in terms of size, with a median book value of EUR 1.4bn and EUR 2.0bn, respectively. Sellers and buyers also have similar levels of deal experience, having both performed about twelve M&A transactions over the past five years. Almost half of all transactions are international; a quarter is executed as controlled auctions.

Appendix A-4.2 Panel A contains additional information, including statistics on the sample's industry and country distribution. We also report information on the rank of the involved law firms and investment banks. As in Krishnan and Masulis (2013) and Beatty and Welch (1996), we categorize law firms and banks based on whether they are ranked in the top 10 based on deal volume between 1995 and 2010.

4.3 M&A Negotiations and Lawyer Expertise: Process and Measurement

4.3.1 M&A Negotiation Process

The negotiation process preceding a private acquisition is in principle free of form and can be different for every deal. However, there are some conventions of the steps typically taken in such negotiations. This section provides a short overview of these steps for one-on-one negotiations.[15] Appendix A-4.3 describes these patterns also for controlled auctions.

Negotiations usually begin with one party communicating interest in a deal. If a buyer initiates a deal, this can be a simple statement of interest, whereas a seller typically approaches potential buyers with a few pages of target information (a "teaser"). From then until the signing, the seller faces a trade-off between providing information to attract or improve an offer, versus withholding sensitive details in case the deal is cancelled. Consequently, if there is mutual deal-interest, both parties first enter into a non-disclosure agreement (NDA), whereby they commit to keep information confidential.

[15] This overview is based on the acquisition files and the interviews with 14 lead lawyers of our law firm. It is complemented with information from Freund (1975), Frankel (2005), and Clifford Chance (2011).

The preparation of an NDA is generally the moment where lawyers are called into the negotiations.

In spite of the NDA, the seller often does not yet provide unrestricted access to the target's books and premises. The parties first want to assess whether they are thinking along a similar target price range. To facilitate an offer from the buyer, the seller will ask her lawyer to provide high-level data about the target in an information memorandum (IM). Based on the IM, the buyer makes an initial non-binding offer, which is a high-end estimate, i.e. a price that the buyer offers if "no skeletons appear in the closet." If this offer does not discourage the seller, the lawyers write down initial agreements in a letter of intent (LOI). Most of the LOI is non-binding and its main purpose is to provide a structure to the deal to avoid miscommunication and to set a timeline for contract negotiations. In addition, the LOI contains a binding exclusivity clause, which prohibits the seller from entering into negotiations with other bidders for a specific period of time. After the signing of the LOI, the buyer is granted access to the most relevant target data in a due diligence process (DD). As a due diligence can be time-consuming, lawyers usually proceed simultaneously with contract negotiations.

Contract negotiations start with a draft contract provided by the lawyer of one of the two parties. This first draft is a combination of a standard specimen contract used by the law firm and deal specific details. Law firms generally have different specimen contracts, depending on whether they represent a buyer or seller, and the first draft contract is usually biased towards their own party. The counter-party lawyer then prepares a mark-up on this document and indicates preferred changes. The lawyers extensively discuss these changes and send various mark-ups of the contract back and forth by email. This exchange of mark-ups, and discussions about them, can continue over months. If the due diligence is on-going during the contract negotiations, any arising concerns about the target value will affect the negotiations (e.g., by demanding warranties). The target price is often not part of these contract negotiations and mostly not even mentioned in the draft contract until late in the negotiation phase. As such, there is no explicit interaction between the pricing and the contract design. However, the price can be adjusted downward if issues appear that are not fully mitigated in the contract (e.g., through warranties or covenants).

If the transfer of control (closing) does not occur directly with the signing, the contract stipulates what conditions need to be met before the closing. If these conditions are satisfied, there is no renegotiation after the signing. However, if some conditions are violated, for example the MAC conditions, then the contract can be annulled and parties renegotiate.

4.3.2 Measuring Negotiation Outcomes

We test whether lawyers with more expertise negotiate outcomes that are more favorable to their clients. Our key assumption is that lawyer expertise improves the bargaining position of their own party, such that more favorable outcomes can be negotiated. We revert to bargaining theory to guide our analysis and to predict for which negotiation outcomes we expect the strongest effects. Generally, one can separate negotiation outcomes into those that *create* value for both parties, and those that *distribute* value among them (e.g., Gilson (1984)).

Rubinstein (1982) shows that relative bargaining power is crucial for the distribution of surplus if two trading parties negotiate over outcomes where incentives are adversarial (i.e., opposite). To the contrary, for provisions that can create value for both parties, Sen (2000) and Inderst and Müller (2004) show that relative bargaining power should not matter, as incentives are aligned. In light of these theories, we expect that relative expertise is most likely to direct negotiation outcomes when buyers and sellers bargain over adversarial issues. We measure adversarial negotiation outcomes along three dimensions: contract design, the bargaining process and acquisition pricing.[16]

Contract Design

Acquisition contracts contain provisions that facilitate legal actions, mitigate information asymmetry or agency concerns, and allocate risk between buyers and sellers. Provisions facilitating legal actions address legal formalities and definitions and rarely require negotiations. Clauses that address information or agency concerns are usually instruments that *create* rather than *distribute* value. As a result, incentives are relatively aligned over clauses addressing these issues. To measure the impact of relative lawyer

[16] Appendix A-4.3 provides an overview of these outcomes and the associated buyer and seller objectives.

expertise, we therefore focus on contract provisions that allocate risks between buyers and sellers, and which have been identified by legal literature as both important and subject to extensive negotiations (see Gilson and Schwartz (2005), Martinius (2005), and Freund (1975)). We define these contract-design measures such that higher (lower) values reflect more risk being allocated to sellers (buyers).

The first set of provisions relate to warranties, which are statements about target quality that sellers give with the commitment to repay part of the purchase price if any of them are violated (see Appendix A-4.5 for examples).[17] Warranties can serve as a signaling device for target quality if sellers are better informed than buyers (Grossman (1981) and Spence (1977)). As such, to the extent that warranties relate to issues of which sellers are aware, the incentives of buyers and sellers are aligned as more warranties reduce the information gap better (Grossman (1981)). However, warranties can (partially) refer to circumstances of which sellers are not completely certain; warranties then provide insurance over these issues to buyers.[18] Sellers can circumvent this insurance provision by adding a knowledge qualifier to warranties, which states that a certain warranty is only true "so far as the seller is aware." If a warranty is qualified with such a statement, buyers cannot enforce a breach thereof if sellers were unaware of the breach at the time of signing (e.g., Freund (1975)). As a result, warranties without knowledge qualifiers provide insurance to buyers by allocating risk to sellers, while warranties with them allocate risk to buyers (see Kling, Simon, and Goldman (1996)). Therefore, our first measure of risk allocation is the fraction of warranties that come *without* knowledge qualifiers (%Warranties w/o Qualifier). For any given price, buyers want to include few qualifiers, while sellers have the opposite incentives. Table 4.1 Panel B shows that 86% of warranties come without a knowledge qualifier.

As an alternative to knowledge qualifiers, sellers can reduce the enforceability of warranties by adding a materiality qualifier. This is an overarching clause stating that the warranties need to be only *materially*, as opposed to *fully*, true. As a result, warranty

[17] Martinius (2005, p.36), claims that "representations and warranties given by the seller often cover more than 50% of the purchase agreement and are the primary means to protect the buyer." Freund (1975, p.229) argues that "I'm willing to bet my briefcase that lawyers spend more time negotiating 'Representations and Warranties of the Seller' than any other single article in the typical acquisition agreement."

[18] An example of a warranty of which the seller may not be certain is that there is no third party infringing on the intellectual property rights of the target.

violations without material damages cannot be claimed by buyers. This provides sellers with a strong defense as buyers then need to prove both that the warranty is violated and that the damage is material (see Kling, Simon, and Goldman (1996)). As such, sellers can limit their exposure to risks from warranties by adding a materiality qualifier. Our second measure of risk allocation is therefore a dummy variable, which takes the value one if warranties are required to be fully true, and zero if a materiality qualifier is included (Warranties Fully True). About 80% of contracts state that warranties must be fully true, whereas the rest state that warranties only need to be materially true (see Table 4.1 Panel B).

A third warranty-related provision is the availability of money that sellers might have to repay in case of a warranty beach. On average across our contracts, buyers can file a claim for damages up to 1.5 years after closing the deal. If, at the time of filing a claim, sellers do not have funds available to pay for these damages, enforcing such warranties is worthless. To prevent this scenario, parts of the purchase price can be collateralized by placing it in an escrow account, by a cash reserve requirement, or by a bank guarantee. Such secured funds are valuable for buyers as they increase the value of warranties, while they are costly for sellers. Our third measure of contract design is therefore the percentage of transaction value which is collateralized (%Payment Secured). We find that funds are secured in 47 deals, with the average collateral being equal to 16% of the transaction value. This corresponds to an unconditional average of 5% secured funds across the total sample (see Table 4.1 Panel B).

Risk allocation through warranties relates to risk that exists at the time of signing, but that neither sellers nor buyers are aware of. Risk can also occur between the signing and closing date of a transaction.[19] If a material event substantially reduces target value, buyers may want to cancel the deal. However, they have signed a contract and fixed a price. As a result, in the default case, buyers have to complete the deal and bear this risk. Contracts allow for this risk to be shifted back to sellers through inclusion of a MAC clause, which stipulates that buyers can refuse to complete a transaction if the target has suffered a material adverse change. As such, buyers *ceteris paribus* prefer the inclusion of

[19] Some contracts state that warranties need to be true both at signing and at closing. If that is statement is included, the risk of events between signing and closing is, to some extent, also covered through warranties. However, there is no significant correlation between this provision and the MAC clause.

an MAC clause, while sellers have opposite incentives. Our fourth measure of risk allocation is thus a dummy variable, which takes the value one if the contract contains a MAC clause. This occurs in 34% of our sample (Table 4.1 Panel B), compared with 99% of transactions in the case of public takeovers (see Denis and Macias (2012)).

As with warranties, the strength of a MAC clause can be reduced through exceptions. These exceptions stipulate that buyers' rights to refuse deal completion are not applicable when the adverse event is due to specific situations described in the exceptions. These situations can be acts of war or terrorism, natural disasters, or even an economic downturn.[20] As a result, parts of the risk are allocated back to buyers. To reflect this risk reallocation, we create an index measure (MAC Strength Index), which equals 0% if no MAC clause is included and 100% if a MAC is included without any exceptions. Contracts with MAC clause exceptions are placed in between in range such that more (few) exceptions put the index closer to 0% (100%).[21]

Bargaining Process

While the bargaining process itself is not directly a negotiation outcome, it has important implications for contract design and pricing. As such, lawyers have incentives to direct the process in a way that is favorable to their own clients. We look at three aspects of the bargaining process.

First, we identify which law firm provided the first draft of the acquisition contract. Both parties prefer to deliver the first draft because it provides a first-mover advantage as a reference point for upcoming negotiations (e.g., Freund (1975) and Molod (1994)).[22] We are able to identify this information based on the layouts of contracts, which contain the business labels of the law firms that drafted the first version. Table 4.1 Panel B shows that the first draft contract comes in 44% of the deals from the buyer law firm.

[20] See Appendix A-3.2 panel C for further examples of situations which can be considered exceptions.

[21] Each exception is assigned a weight of 1/13, as the contract with the maximum number of exceptions contains 13 exceptions. For deals which include a MAC clause, the index is estimated as: [1-(1/13 * Number of Exceptions)].

[22] Freund (1975, p.26) states that "in negotiating acquisitions, the axiom is: If you have an opportunity to draft the documents, do so; you will jump into the lead, and your opponent will never catch up completely."

Second, we measure the time spent on negotiations, defined as the days between the start of negotiations and the signing of the contract. We define the start of negotiations as the date at which our law firm opened a file on a transaction. Buyers generally prefer shorter negotiation times to minimize transactions costs (e.g., lawyer fees), reduce moral hazard at the target, and avoid that the period of exclusive negotiations expires. Sellers, however, have mixed incentives—they prefer short negotiations to also save on transaction costs, but they can benefit from long negotiations as the expiration of the exclusivity period enables them to obtain competing offers and negotiate a higher premium. Negotiations take, on average, 170 days in our sample (Table 4.1 Panel B).

Third, we measure the closing time, which is the time between the signing of a contract and the transfer of the target. Closing times are sometimes necessary, for example, to apply for competition or other regulatory approvals. Whereas the length of this period is largely affected by the number of required approvals, lawyers may influence it by filing the documents more quickly, lobbying for fast responses, or complying with certain requirements on short notice. Buyers usually prefer shorter closing times as, with the transaction price already determined, sellers remain in control of the target before the closing and can exploit this situation by acting opportunistically. Incentives of sellers are again mixed as shorter closings mean fewer opportunities for private benefits, but also earlier closing payments, which are important if they are financially constrained. Our data suggest that there is usually a considerable time period -about 46 days- between the signing and closing, making opportunistic seller actions a potential concern for buyers.

Acquisition Pricing

Finally, we look at acquisition pricing. Whereas pricing is obviously an important negotiation outcome, it is less clear how lawyer expertise might influence it. As described above, acquisition prices in one-on-one transactions are usually set prior to contract negotiations. Lawyers can affect the final transaction price in the following ways. First, the initial price is normally only an upper bound, which is subject to issues that may arise during the due diligence or negotiation process. Buyer lawyers with more expertise may be better able to identify any “skeletons” during the due diligence process, demanding

price reductions as a result. Second, if lawyer expertise affects negotiation times and this again affects prices, then buyer lawyers can indirectly reduce (or prevent increases to) the price by keeping negotiations short.

We consider two measures of acquisition pricing. First, we measure the acquisition premium, which is defined as the target's market-to-book ratio. Second, we measure the ratio of the target market value divided by its EBIT in the last financial year. Buyers, *ceteris paribus*, prefer to pay a low price for the target, while sellers want a high price. Table 4.1 Panel B shows that the average acquisition premium in our sample equals 250%, which compares with a range of 131% to 146% as documented for public takeovers (e.g., Betton, Eckbo, and Thorburn (2009) and Moeller (2005)).[23] The average EBIT multiple in our sample is 28.

4.3.3 Measuring Relative Lawyer Expertise: Experience and Education

We create several variables to proxy for the expertise of the buyer lead lawyer relative to that of the seller lead lawyer ("relative lawyer expertise"). The first set of proxies relates to the relative *experience* level of the lawyers, which we measure using (i) a lawyer's number of years as partner; (ii) her deal experience; (iii) her corporate sector experience; (iv) whether she is an M&A specialist; and (v) whether she is listed as an M&A expert in the Chambers Expert Lawyer ranking. The second set of proxies measures the *education* of lawyers, using (i) the ranking of her university; (ii) whether she has a business degree; and (iii) whether she graduated from a US law school.

The exact construction of each *relative* lawyer expertise variable depends on the distribution of the underlying profile data, which can be continuous or binary. If the underlying lawyer data is continuous (e.g., years as partner), we divide the expertise value of the buyer lawyer by that of the seller lawyer, such that a higher ratio indicates higher relative buyer lawyer expertise.[24] A similar methodology is used in Coates (2012) and Kale, Kini, and Ryan (2003). We standardize these variables such that they range between zero and one. If the underlying profile data is binary (e.g., US law school

[23] For comparison, Masulis and Nahata (2011) report for their sample of private takeovers mean (median) premiums of 1073% (469%), but the targets in their analysis are much smaller in size.

[24] For the university rankings, we use the inverse of the rank as the underlying variable, such that higher values always indicate higher quality or expertise.

education), we create relative expertise variables such that they can take three values: 0 if the seller lawyer has more expertise; 0.5 if both have the same expertise; and 1 if the buyer lawyer has more expertise. Details are provided in Appendix A-4.1

Finally, we create two aggregate indexes. *Experience Index* is the average of our five proxies for experience, and Education Index is the average of the three proxies for education. Table 4.2 Panel A contains summary statistics for the relative expertise variables and shows that expertise is not clustered on one side of the negotiation table.[25] Table 4.2 Panel B further indicates that the expertise variables are positively, but far from perfectly correlated; they seem to capture different aspects of expertise.

4.4 Empirical Results

4.4.1 Negotiation Outcomes: Baseline Regressions

Before relating negation outcomes to relative lawyer expertise, we estimate a set of baseline regressions to look at other potentially important variables explaining negotiations outcomes. We include proxies for law firm—as opposed to lawyer—quality, deal and target characteristics, and proxies for client bargaining power.[26] When explaining contract design and the bargaining process, we further control for the acquisition premium, as contract provisions and prices may be interrelated. Further, for all measures that are related to warranties, we control for the number of warranties.

The corresponding regressions, reported in Table 4.3 Panel A, show that contracts with relatively large buyers contain more warranties without qualifiers, are more likely to require that warranties are fully true, and contain a higher percentage of the payment secured against future claims. These relations may arise as relative size reflects bargaining power. Moreover, the results in Table 4.3 Panel B indicate that

[25] Sellers did not hire an external law firm and relied on internal in-house lawyers in 11% of the transactions. We assume that this reflects low legal expertise and give the relative expertise variables the value 1 for these observations (i.e., low relative seller expertise). Similarly, if the buyer has not requested any legal advice (5% of deals), observations are given the value 0 (i.e., low relative buyer expertise). This approach is similar to Yermack (1992) and Matsunaga, Shevling, and Shores (1992).

[26] In Appendix A-4.7, we will include additional proxies for bargaining power, control for the role of investment banks, and include proxies for contract design when explaining the acquisition premium.

relatively large buyers are more likely to come up with a first draft. Further, negotiations take more time for cross-border deals, and less time if the target is highly levered. As expected, closing times are longer if more approvals from authorities are required before a deal can be completed. Moreover, closing times are longer if the seller is represented by a top 10 law firm, supporting the notion that it is in the seller's interest to delay the closing. The regressions further show that acquisition premiums are higher if the target is more profitable, as reflected in a higher EBIT to assets ratio, and if the target is smaller.

4.4.2 Negotiation Outcomes and Lawyer Expertise

We next turn to the question whether more relative lawyer expertise is associated with more favorable negotiation outcomes (*competitive-advice hypothesis*), or whether relative expertise does not drive negotiations in one direction or another (*cooperative-advice hypothesis*). To this end, we regress in Table 4.4 our proxies for negotiation outcomes on the measures of relative lawyer expertise. Note that higher (lower) values indicate more legal expertise on the buyer (seller) side across all relative expertise measures. Each row in Table 4.4 represents the coefficient (*t*-statistic) of a separate regression that uses an alternative proxy of relative expertise.

Table 4.4 Panel A reports regressions with contract design measures as dependent variables. The regressions control for the variables used in Table 4.3 (not reported)—most importantly they control for the acquisition pricing. Recall that higher values of any contract design measure imply that more risk is allocated to sellers, such that the *competitive-advice hypothesis* would imply a positive relation between relative lawyer expertise and contract design across all proxies. Supporting this view, the table shows that more buyer lawyer experience, measured using by years as partner, deal experience, or M&A specialization, is associated with both more warranties without a qualifier and a higher probability that warranties need to be fully true. In economic terms, a one-standard deviation increase in deal experience of the buyer lawyer relative to the seller lawyer is associated with 3% more warranties without qualifiers. Similarly, if only the buyer lawyer has corporate experience (as opposed to both or neither), contracts contain 7% more warranties without qualifiers. Moreover, if only the buyer lawyer is recognized by Chambers as an M&A expert, then a higher percentage of the payment is collateralized, there is a higher propensity to include a MAC clause, and the

MAC clause tends to be stronger. The overall level of relative experience, as indicated by the experience index, is significantly associated with all contract design measures (except for the percentage of secured payments). Figure 4.1 depicts these relations through partial scatter plots.

In addition to experience, education is also an important factor related to contract design, as buyer lawyers from better universities or those who have studied at US law schools negotiate contracts that have a higher propensity to require that warranties need to be fully true. US law school education is also positively associated with both the fraction of unqualified warranties and the strength of the MAC clause. Partial scatterplots of the relation between the education index and negotiation outcomes are provided in Figure 4.2.

Table 4.4 Panel B reports regressions that relate the bargaining process and pricing to relative lawyer expertise; we again control for the variables reported in Table 4.3.[27] With respect to the bargaining process, we find that more legal experience on the buyer side, proxied using years of partner experience, M&A specialization, M&A expert listing, or the experience index, is associated with a higher probability that the buyer can provide the first draft. Similarly, lawyer education also seems strongly related to the probability of providing the first contract draft, which increases when buyer lawyers have studied at higher ranked universities or at US law schools. This is also reflected in a significant relation between the right to come up with the first contract draft and the education index. In terms of the duration of the deal process, more experience is associated with both shorter negotiation and closing times, at least when measured as years of experience, deal experience or the experience index.[28]

The results in Table 4.4 Panel B further suggest that more legal experience is associated with more favorable acquisition pricing, especially when pricing is measured using the market-to-book premium. Specifically, if the buyer lawyer has more deal experience, an M&A specialization, or is listed as an M&A expert, this is associated with a lower premium paid by the buyer. In terms of economic significance, deals where buyer

[27] Note that the bargaining process proxies control for the acquisition premium, whereas the pricing measures instead control for the target asset value.

[28] In terms of economic magnitudes, a one-standard deviation increase in the buyer lead lawyer's years of experience is associated with 30 days shorter negotiation and 17 days shorter closing times.

lead lawyers have high (top quartile) and seller lead lawyers low (bottom quartile) deal experience are associated with acquisition premiums that are 34% lower compared to situations where both have equal experience. Moreover, higher relative experience is associated with significantly lower EBIT multiples—at least for corporate experience and M&A expert listing. These results suggest that experienced lawyers affect pricing in M&A deals, in spite of price indications generally being set prior to contract negotiations. Appendix A-4.6 shows that these results are robust to controlling for the rank of the investment banks involved in a transaction. The results are further robust to controlling for our proxies of contract design.

Overall, our results are consistent with the *competitive-advice hypothesis* as higher relative lawyer expertise is reflected in more favorable negotiation outcomes across various dimensions of acquisition negotiations. In terms of expertise drivers, it seems that both experience and education are relevant, but experience is generally more influential for the bargaining process and acquisition pricing.

4.4.3 Relative versus Joint Legal Expertise: Placebo Tests

In the analysis above, we find support for the *competitive-advice hypothesis* as a divergence in expertise between buyer and seller lawyers is significantly related to negotiation outcomes. However, if our relative expertise measures in some way also reflect the combined (joint) expertise of the lawyers and the observed negotiation outcomes are considered to be "better" for both parties, these results do not reject the *cooperative-advice hypothesis*. Our measures could reflect joint expertise if, for example, seller lawyer expertise shows little variation across deals, implying that that higher relative expertise is only driven by more buyer expertise. Several tests indicate that this concern does not apply to our results.

First, Appendix A-4.2, which reports summary statistics of expertise variables separately for buyer and seller lawyers, shows that there is considerable variation across deals in terms of expertise levels for both buyer and seller lawyers. It is thus unlikely that our relative expertise measures reflect "total expertise."

Second, bargaining theory shows that bargaining power should not affect contract terms that create value for both parties. Contract terms can be value-increasing

when they, for example, mitigate information asymmetry or agency problems (e.g., Sen (2000) and Inderst and Müller (2004)). Joint expertise should affect such provisions, as lawyer teams with more expertise are better at identifying the set of provisions that maximizes the joint surplus of both parties. On the other hand, *relative* expertise should be unrelated to such contract provisions, as incentives of the parties are aligned.

To test whether relative expertise is indeed unrelated to value-increasing contract outcomes, we perform a set of placebo tests. To this end, we look at three types of contract provisions that increase the joint surplus of both parties by mitigating problems of information asymmetry and agency (e.g., Gilson (1984)). These provisions are (i) the number of warranties; (ii) the number of covenants; and (iii) whether an earnout-payment mechanism is included. We look at warranties as they can play an important function in reducing information asymmetry by signaling target quality to buyers (e.g., Grossman (1981), Spence (1977)). They not only protect buyers against missing information, but also increase the probability that the target is sold to begin with. Warranties thereby increase the joint surplus of both parties, making them an area of negotiations where incentives of buyers and sellers are relatively aligned. Similar arguments can be applied to covenants. Covenants are in the interest of both parties as they are commitment devices that mitigate opportunistic behavior by sellers between the signing and closing dates. The inclusion of covenants facilitates deal completion and is thus also beneficial for both parties. Finally, it is argued that earnout mechanisms can facilitate deal completion by reducing information asymmetry (e.g., Datar, Frankel, and Wolfson (2001), Cain, Denis, and Denis (2011)). Earnouts stipulate that part of the purchase price will be contingent on target performance after the closing date, thereby reducing uncertainty about future target profitability.

Table 4.5 reports regressions similar to those in Table 4.4, but uses the number of warranties and covenants, as well as earnout mechanisms as dependent variables. The regressions show that our proxies for relative lawyer experience and education are unrelated to these contract outcomes across most expertise proxies. This confirms that divergence in expertise is used to bargain for outcomes that are favorable to the respective own clients, rather than to affect provisions that maximize joint surplus.

4.4.4 Endogenous Allocations of Lawyers

Our evidence suggests that negotiation outcomes are more favorable for buyers if the expertise of buyer lawyers exceeds that of seller lawyers. This raises the question whether this reflects a causal link or rather a spurious correlation. For example, it could be that our relations arise because of an endogenous allocation (matching) of lawyers to certain deals or clients. Lawyer expertise could then reflect unobserved deal characteristics such as deal complexity. Similarly, expertise could reflect the bargaining power or other unobserved characteristics of clients, implying that these variables -rather than lawyer expertise- are the drivers of the observed relations. While we try to control as much as possible for potential drivers behind such relations, we cannot exploit fully exogenous expertise variation. However, we are able to mitigate concerns of endogenous lawyer-allocations in several different ways.

The concern that lawyers are endogenously allocated based on *deal* characteristics is mitigated in two ways. First, in structured interviews with 14 (70%) of the 20 lead lawyers of our law firm, all interviewees state that deals are allocated to lead lawyers mainly based on existing lawyer-client relations.[29] Lawyers, when at partner rank, usually own a client portfolio and advise these clients on all M&A transactions that are being executed, with clients being both on the seller and buyer side. This seems supported by our data, as firms in our sample are frequent buyers and sellers of targets, implying repeat business by most partners. Moreover, deal information from Merger Market shows that 82% (60%) of the sellers (buyers) with prior deal experience have requested advice from the same law firm over the past five years. The interviewees further state that, in case a client is newly acquired, the allocation of deals to lawyers is generally driven by lawyer availability and internal firm politics. Overall, this indicates that lawyers are selected to advice on deals based on historically determined relations, rather than on the specifics of a deal or counterparty.

Second, our results are robust to controlling for newly initiated law firm-client relations that arise as clients switch law firms, potentially in response to deal or target

[29] These long-term relations between client and lawyers are also recognized in the legal literature (e.g., Coates et al. (2011) and Gilson, Mnookin, and Pashigian (1985)). It is argued that these relations arise because of uncertainty about lawyer quality.

characteristics. To show this, we follow Calomiris and Hitscherich (2007) and create dummy variables that take the value one if a buyer (seller) switches to a new law firm from which she did not obtain prior M&A advice over the past five years. The regressions in Table 4.6 Panel A, reported for the expertise and education indexes only, show that the previously documented relation are robust to controlling for such potentially endogenous client-lawyer relations. Further, the client-lawyer switch dummies are statistically not different from zero, indicating that contract design is unlikely to be related to potentially endogenous client switches.

Exploiting a similar idea, we next re-estimate our regressions for deals where law firms and their clients are located in the same country, making a fixed lawyer-client relation very likely. Specifically, we exploit the interview information that clients are generally reluctant to hire new lawyers, but might be forced to do so when deals require legal expertise about a country where neither the lawyer nor the client are located. Therefore, the regressions in Table 4.6 Panel B restrict the sample to deals where (i) the buyer and the buyer law firm; and (ii) the seller and the seller law firm are located in the same country. We find that many of the relations between relative lawyer expertise and negotiation outcomes survive in this smaller, but better identified subsample. Moreover, Table 4.6 Panel C shows that our results are robust to controlling for dummy variables which equal one if the buyer (seller) and the buyer (seller) law firm are located in different countries. As with the client-lawyer switch dummies, we expect these two variables to be statistically different from zero if lawyers are endogenously allocated to deals. The regressions in Table 4.6 Panel C show that this is generally not the case; the exception is that the propensity to include a MAC clause is higher for deals with cross-country relations.

While this evidence suggests that the allocation of lawyers to deals is unlikely to be driven by *deal* characteristics, it does not address allocations based on *client* characteristics. We perform several tests to mitigate this concern. The first tests show that the bargaining power and risk-bearing capacity of clients, possibly two of the most important client characteristics in M&A deals, are not driving our results. In the second tests, we mitigate the concern that unobservable client characteristics are driving our results by showing that they are robust to adding client fixed effects.

To address concerns that relative expertise reflects the bargaining power of clients, we first look directly at determinants of (relative) lawyer expertise. Though this analysis does not allow us to test for the extent to which unobserved client characteristics affect expertise, it is useful to understand the drivers behind the matching of lawyers to clients. It further allows for some empirical verification of whether the views expressed by the lawyers in our interviews are consistent with our data. Across three different panels, the analyses in Appendix A-4.7 regress lawyer expertise on variables related to the bargaining power of buyers and sellers. We look at the expertise of buyer (Panel A) and seller (Panel B) lawyers individually, and at our proxies of relative expertise (Panel C). We employ six bargaining power proxies: Buyer and Seller Book Value, Buyer and Seller Deal Experience, Deal After 2008, and Controlled Auction. Thereby, we assume that bargaining power is positively associated with firm size and deal experience. We further assume that the financial crisis reduced the bargaining power of sellers (e.g., Aktas, De Bodt, and Roll (2010)), and that sellers generally have more power in controlled auctions (e.g., Boone and Mulherin (2007), Aktas, De Bodt, and Roll (2010)). The regressions further include proxies for deal characteristics (deal size and complexity, similar to Krishnan and Masulis (2013)), and two variables that indicate that a past client-law firm relation is unlikely. The regressions provide little evidence that lawyer expertise is systematically related to bargaining power, though we find that larger clients are more likely to hire M&A specialists. Consistent with the responses in our interviews, variation in lawyer expertise is partly driven by whether a client is located in a different country than her law firm.[30]

Nevertheless, to ensure that any correlation between lawyer expertise and client bargaining power does not drive our results, we also directly control for these proxies in regressions explaining negotiation outcomes. Appendix A-4.8 Panel A and B show that our relations between relative lawyer expertise and negotiation outcomes remain largely unaffected after including various bargaining power proxies. As our proxies for bargaining power may not capture the financial position of the seller, which may also affect the

[30]However, we do not find any systematic patterns across our regressions, with foreign clients matching both with more and less experienced lawyers, depending on the expertise measure we use. Confirming the previous view that lawyers are unlikely to be allocated to deals based on deal characteristics, we find that lawyer expertise is largely unrelated to deal characteristics, as proxied by target size and complexity (number of countries a target operates in).

bargaining position, Appendix A-4.8 Panel C and D document that our results are also largely robust to controlling for proxies for seller financial distress. We proxy for seller financial distress by using a seller leverage and a dummy variable which takes the value one if the target has negative book equity. Overall, these results suggests that, whereas bargaining power might be relevant for negotiation outcomes, our measures of relative lawyer expertise are not simply reflecting such differences in bargaining power.

Next to bargaining positions, risk-bearing capacity of clients could affect the risk allocation through contracts as well, with more risks being allocated to parties that have a higher capacity to bear them. To this end, Appendix A-4.8 Panel E reports regressions of the negotiation outcomes on various proxies for risk-bearing capacity. Assuming that risk-bearing capacity increases with buyer or seller portfolio diversification, we include three dummy variables, which equal one if: (i) the buyer is a private-equity fund; (ii) the seller is a private-equity fund; and (iii) the seller is a family. Private-equity funds may have a higher risk-bearing capacity as they tend to have diversified investments in multiple industries. On the other extreme, family sellers typically only have investments in one company and are therefore relatively undiversified. To proxy for risk-sharing possibilities among multiple sellers, we measure the percentage of shares (or assets) sold by the largest seller. The smaller this figure, the more (similar sized) sellers there are in a deal, and we assume that this increases risk-bearing capacity of those sellers. The estimates in Appendix A-4.8 Panel F show that our previous results on the relation between relative lawyer expertise and negotiation outcomes are robust to controlling for variation in risk-bearing capacity.

Our previous measures of bargaining power and risk-bearing capacity cannot exclude the possibility that unobservable client characteristics drive relative lawyer expertise. To mitigate this concern, we next re-estimate the regressions reported in Table 4.4 and add client fixed effects. Client fixed effects allow us to account for any time-invariant unobserved client characteristics that may drive negotiation outcomes. To be able to estimate these regressions, we restrict the analysis to 86 contracts for which one of the clients has appeared at least three times in the sample. There are 18 such clients that occur at least three times as buyer and/or sellers. The regressions in Table 4.7 show

that our results are again largely robust to adding these fixed effects, though they are statistically weaker due to the reduced econometric power of the tests.

4.5 Conclusions

We study whether lawyers with more legal expertise yield better negotiation outcomes for their own clients in M&A transactions. Our analysis is built around the files of acquisitions of privately held targets. Our data allow us to shed light on the effects of lawyer expertise on three important negotiation outcomes: contract design, the bargaining process, and acquisition pricing.

Across several measures, we find that more lawyer expertise is associated with more beneficial negotiation outcomes. We find that buyers with high expertise lawyers generally sign contracts that have fewer warranty qualifiers and a higher propensity to require that warranties are fully true. We further show that more buyer legal expertise is associated a higher propensity to include a MAC clause. With respect to the bargaining process, we find that more legal expertise on the buyer side is associated with shorter negotiation and closing times, and a higher probability that the buyer can provide the first contract draft. Finally, we show that legal expertise is related to more favorable acquisition pricing even after controlling for contract design and investment bank expertise. We perform a set of placebo tests that show that lawyer expertise is less important for provisions that increase the joint surplus of both parties by facilitating deal completion and reducing transaction costs. This provides support that our measures of relative lawyer expertise proxy for the divergence in expertise rather than combined levels of expertise. These findings do not seem to be driven by an endogenous allocation of lawyers to deal or clients. Together, our findings are consistent with the *competitive-advice hypothesis*, which holds that lawyers with more legal expertise are better able to negotiate in favor of the interest of their clients.

Table 4.1
Transaction Characteristics: Summary Statistics

This table provides summary statistics of the main variables used in the analysis. The sample covers 151 M&A transactions conducted in the period between 2005 and 2010. As some information is not available for all transactions, some statistics are based on less than 151 observations. Panel A reports summary statistics of target, buyer, seller, and deal characteristics. Panel B reports summary statistics of proxies for negotiation outcomes: contract design, bargaining process, and acquisition pricing. Appendix A-4.1 provides detailed variable definitions.

Panel A: Target, Buyer, Seller, and Deal Characteristics

Target	**Mean**	**Median**	**10th**	**90th**	**Std. Dev.**	**Obs.**
Transaction Value (mEUR)	222	34	2	371	795	151
Target Book Value (mEUR)	318	45	2	538	990	146
Target Market Value (mEUR)	434	80	6	864	1,290	146
Target Leverage	59%	60%	21%	97%	30%	146
Target EBIT/Assets	14%	14%	1%	32%	15%	151
Target Shares Transferred	92%	100%	60%	100%	18%	151
Asset Deal	9%				28%	151
Countries Target	4	1	1	7	6	151
Target Negative Equity	6%				24%	146
Buyer						
Buyer Book Value (mEUR)	40,000	1,410	12	45,900	139,000	150
Buyer Deal Experience	12	5	1	33	16	147
Buyer Private Equity	22%				41%	151
Seller						
Seller Book Value (mEUR)	90,800	2,080	2	124,000	316,000	147
Seller Deal Experience	13	5	1	36	16	151
Multiple Sellers	32%				47%	151
Seller Leverage	55%	60%	0%	97%	35%	147
Seller Private Equity	15%				36%	151
Seller Family	18%				38%	151
Main Seller Percent	88%	100%	49%	100%	21%	151
Deal						
Cross-Country Deal	44%				50%	151
Approvals Required (number)	1	0	0	2	2	151
Deal After 2008	37%				48%	151
Controlled Auction	23%				42%	151

Panel B: Negotiation Outcomes

	Mean	**Median**	**10th**	**90th**	**Std. Dev.**	**Obs.**
Contract Design						
Warranties	98	100	27	152	49	150
%Warranties w/o Qualifier	86%	89%	76%	99%	12%	150
Warranties Fully True	81%				39%	150
%Payment Secured	5%	0%	0%	21%	9%	149
Covenants	14	14	0	31	13	151
MAC Clause	34%				47%	151
MAC Strength Index	27%	0%	0%	100%	42%	151
Bargaining Process						
First Draft By Buyer	44%				50%	151
Negotiation Time	170	141	47	334	134	147
Closing Time	46	24	0	123	66	151
Pricing						
Acquisition Premium	244%	155%	100%	506%	230%	146
EBIT Multiple	28	16	-9	93	56	109
Earnout	18%				38%	151

Table 4.2
Relative Lawyer Expertise: Summary Statistics

This tables reports summary statics of ten relative lawyer expertise variables, reflecting the legal expertise of the buyer's lead lawyer relative to the seller's lead lawyer. These variables have been standardized to range between 0 and 1, where higher values indicate higher relative buyer lawyer expertise. Panel A shows summary statistics (means and medians). We further report for what percentage of the sample: (i) seller lawyer has more expertise than buyer lawyer; (ii) both have the same expertise; and (iii) buyer lawyer has more expertise than seller lawyer. The first five variables proxy for relative lawyer experience. We further report Experience Index, which is an average of the five experience variables. The next three variables proxy for relative lawyer education. We further report Education Index, which is an average of the three education variables. The variables Years as Partner, Deal Experience, and University Ranking are based on continuous variables and defined as the expertise value of the buyer lawyer divided by the expertise value of the seller lawyer. (For University Ranking, the inverse is used, such that higher values reflect higher university quality). These ratios are winsorized at 5%. The variables Corporate Experience M&A Specialist, M&A Expert Listing, Business Education, and US Education are based on dummy variables and can take three values: 0 if the seller lawyer has more expertise; 0.5 if both have the same expertise; and 1 if the buyer lawyer has more expertise. If a seller has not requested legal advice from a law firm, observations are given the maximum value from the respective variable distribution (i.e., high relative buyer expertise). Similarly, if a buyer has not requested any legal advice from a law firm, observations are given the minimum value from the respective variable distribution (i.e., high relative seller expertise). Panel B reports rank correlations of the relative expertise variables. * indicates significance at least at the 5% level.

Panel A: Measures of Relative Lawyer Expertise

	Relative Lawyer Expertise		**Buyer Layer Expertise Relative to Seller Lawyer Expertise**			
	Mean	**Median**	**Buyer < Seller**	**Buyer = Seller**	**Buyer > Seller**	**Obs.**
Experience						
Years as Partner	0.35	0.22	45%	2%	53%	117
Deal Experience	0.25	0.08	43%	0%	57%	127
Corporate Experience	0.54	0.50	15%	60%	24%	123
M&A Specialist	0.55	0.50	9%	71%	20%	132
M&A Expert Listing	0.59	0.50	17%	48%	35%	151
Experience Index	0.45	0.41	70%	0%	30%	105
Education						
University Ranking	0.28	0.09	38%	10%	52%	127
Business Education	0.53	0.50	19%	56%	25%	125
US Education	0.50	0.50	20%	67%	21%	119
Education Index	0.44	0.38	57%	2%	42%	120

Panel B: Spearman Rank Correlations

	Years as Partner	Deal Exper.	Corp Exper.	M&A Specialist	M&A Listing	Exper. Index	Univ. Ranking	Business Educ.	US Educ.
Years as Partner	1.000								
Deal Experience	0.509*	1.000							
Corporate Exper.	-0.149	0.269*	1.000						
M&A Specialist	0.633*	0.663*	0.135	1.000					
M&A Listing	0.293*	0.610*	0.190	0.513*	1.000				
Experience Index	0.583*	0.824*	0.477*	0.745*	0.767*	1.000			
Univ. Ranking	0.588*	0.442*	0.021	0.569*	0.274*	0.498*	1.000		
Business Educ.	-0.045	0.324*	0.572*	0.134	0.303*	0.398*	-0.091	1.000	
US Education	0.339*	0.045	-0.072	0.265*	0.159	0.232*	0.681*	-0.187	1.000
Education Index	0.453*	0.434*	0.279*	0.519*	0.364*	0.585*	0.820*	0.353*	0.741*

Table 4.3
Negotiation Outcomes: Baseline Regressions

This table reports OLS and logit regressions to explain negotiation outcomes in M&A transactions. The sample consists of 151 acquisitions of private targets between 2005 and 2010. Each column contains a regression with a different dependent variable (listed horizontally). In Panel A, the dependent variables are measures of contract design: %Warranties without Qualifier; Warranties Fully True; %Payment Secured; MAC Clause; and MAC Strength Index. In Panel B, the dependent variables are measures of the bargaining process and pricing: First Draft By Buyer; Negotiation Time; Closing Time; Acquisition Premium; and EBIT Multiple. Detailed variable definitions are provided in Appendix A-4.1. We report in parentheses *t*-statistics, calculated using robust standard errors. The regressions have less than 151 observations because of missing data for some variables. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: Base Regressions of Contract Design

	Contract Design				
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index
	(1)	(2)	(3)	(4)	(5)
Buyer Law Firm Top 10	-0.03	-0.85	0.00	-1.40*	-0.17
	(-0.70)	(-1.29)	(0.14)	(-1.95)	(-1.28)
Seller Law Firm Top 10	-0.02	-0.50	-0.01	-0.85	-0.11
	(-0.54)	(-0.80)	(-0.71)	(-1.46)	(-0.85)
Acquisition Premium	0.01*	-0.00	-0.00	0.01	-0.00
	(1.68)	(-0.03)	(-0.44)	(0.09)	(-0.16)
Warranties	-0.00	0.01*	0.00**		
	(-0.83)	(1.80)	(2.10)		
Cross-Country Deal	-0.02	-0.45	-0.02	0.23	-0.03
	(-0.85)	(-0.87)	(-1.33)	(0.47)	(-0.35)
Asset Deal	0.01	-0.21	-0.02	-0.66	-0.02
	(0.21)	(-0.25)	(-1.38)	(-0.70)	(-0.12)
Target Leverage	0.00	0.91	-0.01	0.61	0.15
	(0.05)	(1.11)	(-0.33)	(0.75)	(0.91)
Target EBIT/Assets	-0.02	1.22	0.05	0.36	0.31
	(-0.41)	(0.61)	(1.12)	(0.20)	(0.81)
Approvals Required	0.00	0.35*	-0.00	0.16	0.00
	(0.56)	(1.81)	(-1.08)	(1.24)	(0.25)
Multiple Sellers	0.02	-0.22	0.01	0.44	0.09
	(0.75)	(-0.41)	(0.46)	(0.87)	(0.86)
Relative Size	0.01*	0.30***	0.01***	0.10	0.04**
	(1.79)	(3.00)	(3.30)	(1.18)	(2.32)
Obs.	140	140	139	96	96
Adj. (Pseudo) R^2	-0.016	(0.165)	0.134	(0.087)	0.037

Table 4.3 (continued)

Panel B: Base Regressions of the Bargaining Process and Pricing

	Bargaining Process			Pricing	
Dependent Variable:	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)
Buyer Law Firm Top 10	0.00	29.15	4.08	0.75	-10.92
	(0.00)	(0.70)	(0.22)	(1.51)	(-0.58)
Seller Law Firm Top 10	-0.75	36.29	52.20**	0.92	8.04
	(-1.33)	(1.00)	(2.56)	(1.49)	(0.48)
Acquisition Premium	0.05	-9.51**	1.10		
	(0.45)	(-2.38)	(0.67)		
Target Book Value (log)				-0.56***	-0.58
				(-4.06)	(-0.18)
Cross-Country Deal	-1.21***	50.25**	1.91	0.15	13.53
	(-2.71)	(2.07)	(0.15)	(0.44)	(1.15)
Asset Deal	-1.61*	4.05	33.49	0.38	65.75
	(-1.68)	(0.12)	(1.18)	(0.55)	(1.12)
Target Leverage	-0.21	-81.41**	16.12	-0.71	-2.83
	(-0.32)	(-2.08)	(1.01)	(-1.08)	(-0.10)
Target EBIT/Assets	-2.46	-21.82	-49.57*	3.46***	-20.61
	(-1.63)	(-0.31)	(-1.94)	(3.17)	(-0.79)
Approvals Required	-0.97***	-1.84	11.39***	0.13*	1.52
	(-2.91)	(-0.32)	(2.66)	(1.88)	(0.61)
Multiple Sellers	-0.46	-42.71*	-0.94	-0.12	8.83
	(-0.86)	(-1.83)	(-0.08)	(-0.31)	(0.81)
Relative Size	0.39***	-6.01	-0.47	0.13*	0.79
	(4.38)	(-1.59)	(-0.23)	(1.88)	(0.44)
Obs.	141	137	141	141	107
Adj. (Pseudo) R^2	(0.320)	0.206	0.223	0.406	0.068

Table 4.4
Negotiation Outcomes and Lawyer Expertise: Main Results

This table reports OLS and logit regressions of negotiation outcomes. The sample consists of 151 M&A acquisitions. Each column reports a regression with a different dependent variable and each row a regression with a separate measure of relative lawyer expertise. All expertise variables range between 0 and 1, where higher values indicate more legal expertise on the buyer's side. Variable definitions are provided in Appendix A-4.1. In parentheses are *t*-statistics, calculated with robust standard errors. All regressions control for the variables in Table 4.3. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Contract Design and Lawyer Expertise

	Contract Design				
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index
Experience	(1)	(2)	(3)	(4)	(5)
Years as Partner	0.08**	2.07*	0.04	-0.14	0.05
	(2.08)	(1.90)	(1.26)	(-0.15)	(0.30)
Obs.	109	109	108	76	76
Adj. (Pseudo) R^2	-0.005	(0.188)	0.133	(0.154)	0.073
Deal Experience	0.08**	3.93**	0.01	0.44	0.10
	(2.37)	(2.40)	(0.34)	(0.46)	(0.55)
Obs.	119	119	118	89	89
Adj. (Pseudo) R^2	-0.007	(0.213)	0.120	(0.145)	0.119
Corporate Experience	0.06*	0.32	-0.02	0.18	0.14
	(1.95)	(0.27)	(-0.74)	(0.21)	(0.92)
Obs.	116	116	115	82	82
Adj. (Pseudo) R^2	0.037	(0.197	0.163	(0.147	0.120
M&A Specialist	0.14*	1.98*	0.03	1.53	0.31
	(1.95)	(1.81)	(0.76)	(1.25)	(1.27)
Obs.	124	124	123	89	89
Adj. (Pseudo) R^2	0.033	(0.173)	0.131	(0.113)	0.048
M&A Expert Listing	0.03	1.16*	0.04**	1.83**	0.27*
	(1.02)	(1.79)	(2.07)	(2.42)	(1.92)
Obs.	140	140	139	96	96
Adj. (Pseudo) R^2	-0.018	(0.184)	0.144	(0.138)	0.067
Experience Index	0.17***	2.96*	0.06	5.80**	0.80**
	(2.98)	(1.76)	(1.25)	(2.17)	(2.52)
Obs.	99	99	98	70	70
Adj. (Pseudo) R^2	0.068	(0.189)	0.127	(0.284)	0.314
Education					
University Ranking	0.05	2.40**	-0.02	0.76	0.21
	(1.58)	(2.08)	(-0.83)	(0.96)	(1.50)
Obs.	119	119	118	84	84
Adj. (Pseudo) R^2	-0.014	(0.237	0.163	(0.139	0.090
Business Education	0.02	0.46	0.06**	0.29	0.09
	(0.75)	(0.50)	(2.04)	(0.30)	(0.55)
Obs.	118	118	117	84	84
Adj. (Pseudo) R^2	-0.029	(0.174)	0.172	(0.144)	0.128
US Education	0.11***	2.73**	-0.02	0.83	0.33*
	(3.44)	(2.42)	(-0.71)	(1.01)	(1.88)
Obs.	121	121	120	86	86
Adj. (Pseudo) R^2	0.097	(0.255)	0.168	(0.124)	0.080
Education Index	0.12**	4.28**	0.00	1.72	0.54**
	(2.41)	(2.39)	(0.06)	(0.97)	(2.14)
Obs.	113	113	112	79	79
Adj. (Pseudo) R^2	0.060	(0.274)	0.160	(0.177)	0.186

Table 4.4 (continued)

Panel B: Bargaining Process, Pricing and Lawyer Expertise

	Bargaining Process			Pricing	
Dependent Variable:	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
Experience	(1)	(2)	(3)	(4)	(5)
Years as Partner	2.02**	-84.09***	-47.21***	-0.55	1.57
	(2.11)	(-2.79)	(-3.15)	(-1.49)	(0.10)
Obs.	109	105	109	109	83
Adj. (Pseudo) R^2	(0.344)	0.181	0.216	0.328	-0.012
Deal Experience	1.38	-61.63*	-38.17***	-0.93**	-30.99
	(1.59)	(-1.79)	(-2.78)	(-2.05)	(-1.59)
Obs.	120	116	120	120	93
Adj. (Pseudo) R^2	(0.336)	0.156	0.144	0.306	-0.026
Corporate Experience	0.65	52.32	8.41	-0.88	-39.07**
	(0.67)	(1.04)	(0.52)	(-1.64)	(-2.32)
Obs.	116	112	116	116	91
Adj. (Pseudo) R^2	(0.297)	0.140	0.116	0.326	-0.019
M&A Specialist	2.87**	-57.82	-69.56**	-1.25**	-10.09
	(2.11)	(-1.51)	(-2.28)	(-2.33)	(-0.35)
Obs.	124	120	124	124	96
Adj. (Pseudo) R^2	(0.327	0.156	0.173	0.313	-0.055
M&A Expert Listing	1.14*	-44.95	-16.45	-0.75*	-38.87**
	(1.65)	(-1.27)	(-0.78)	(-1.83)	(-2.11)
Obs.	141	137	141	141	107
Adj. (Pseudo) R^2	(0.333)	0.148	0.164	0.365	0.011
Experience Index	7.22***	-132.97*	-62.71*	-1.91**	-60.49
	(3.60)	(-1.92)	(-1.96)	(-2.15)	(-1.61)
Obs.	99	95	99	99	77
Adj. (Pseudo) R^2	(0.451)	0.133	0.181	0.349	0.019
Education					
University Ranking	1.84**	-67.91**	-7.06	-0.69*	-3.10
	(2.49)	(-2.09)	(-0.51)	(-1.67)	(-0.20)
Obs.	119	115	119	119	93
Adj. (Pseudo) R^2	(0.312	0.180	0.120	0.324	-0.060
Business Education	-0.77	7.81	37.03*	0.01	-20.61
	(-0.91)	(0.15)	(1.83)	(0.02)	(-0.90)
Obs.	118	114	118	118	91
Adj. (Pseudo) R^2	(0.288)	0.135	0.150	0.284	-0.044
US Education	2.01**	-5.47	16.17	0.06	2.12
	(2.11)	(-0.13)	(0.60)	(0.10)	(0.09)
Obs.	121	117	121	121	95
Adj. (Pseudo) R^2	(0.332)	0.149	0.131	0.303	-0.057
Education Index	2.81**	-48.70	26.94	-0.50	-18.58
	(2.11)	(-0.77)	(0.70)	(-0.64)	(-0.47)
Obs.	113	109	113	113	90
Adj. (Pseudo) R^2	(0.316)	0.142	0.129	0.306	-0.054

Table 4.5
Lawyer Expertise: Placebo Regressions

This table reports OLS and logit regressions to explain Warranties, Covenants, and Earnouts in M&A contracts. The sample consists of 151 acquisitions. Each column contains a regression with a different dependent variable and each row a separate measure of relative lawyer expertise. All expertise variables range between 0 and 1, where higher values indicate more legal expertise on the buyer's side. Variable definitions are provided in Appendix A-4.1. In parentheses are *t*-statistics, calculated using robust standard errors. All regressions control for the variables used in Table 4.3. *** indicates significance at 1%, ** at 5%, and * at 10%.

	Contract Design		**Pricing**
Dependent Variable:	Warranties	Covenants	Earnout
Experience	(1)	(2)	(3)
Years as Partner	-18.95	-2.98	0.65
	(-1.35)	(-0.71)	(0.57)
Obs.	109	76	109
Adj. (Pseudo) R^2	0.162	0.228	(0.285)
Deal Experience	-21.60	-4.63	-0.84
	(-1.59)	(-1.17)	(-0.75)
Obs.	119	89	120
Adj. (Pseudo) R^2	0.130	0.242	(0.260)
Corporate Experience	8.38	1.80	-2.38**
	(0.58)	(0.45)	(-2.27)
Obs.	116	82	116
Adj. (Pseudo) R^2	0.139	0.267	(0.329)
M&A Specialist	-10.63	5.76	-1.73
	(-0.62)	(1.07)	(-1.18)
Obs.	124	89	124
Adj. (Pseudo) R^2	0.134	0.238	(0.282)
M&A Expert Listing	19.43*	0.92	-0.50
	(1.72)	(0.29)	(-0.57)
Obs.	140	96	141
Adj. (Pseudo) R^2	0.167	0.203	(0.196)
Experience Index	-8.19	-6.36	-1.00
	(-0.30)	(-0.69)	(-0.58)
Obs.	99	70	99
Adj. (Pseudo) R^2	0.126	0.268	(0.294)
Education			
University Ranking	-19.00	-0.17	-0.42
	(-1.61)	(-0.05)	(-0.45)
Obs.	119	84	119
Adj. (Pseudo) R^2	0.159	0.215	(0.293)
Business Education	-19.10	1.83	-1.24
	(-1.25)	(0.51)	(-1.21)
Obs.	118	84	118
Adj. (Pseudo) R^2	0.154	0.238	(0.269)
US Education	4.73	1.50	0.68
	(0.32)	(0.36)	(0.61)
Obs.	121	86	121
Adj. (Pseudo) R^2	0.146	0.232	(0.280)
Education Index	-26.34	0.56	-0.50
	(-1.26)	(0.09)	(-0.32)
Obs.	113	79	113
Adj. (Pseudo) R^2	0.168	0.217	(0.293)

Table 4.6
Negotiation Outcomes and Lawyer Expertise: Fixed Client-Lawyer Relations

This table reports OLS and logit regressions of Experience Index and Education Index on negotiation outcomes. Experience Index is the average of five proxies for relative lawyer experience, and Education Index is the average of three proxies for relative lawyer education. Both variables range between 0 and 1, where higher values indicate more legal expertise on the buyer side. Each column reports a regression with a different dependent variable. The full sample consists of 151 acquisitions of private targets between 2005 and 2010, but regressions are on fewer observations due to missing data or sample restrictions. Panel A reports regressions of the relative expertise indices on negotiation outcomes as in Table 4.4 but adds two control variables to the analysis: (i) Buyer Lawyer Switch, and (ii) Seller Lawyer Switch. These dummy variables take the value one if a buyer (seller) switches to a new law firm with which she did not have an M&A deal relationship over the past five years, and zero otherwise. Panel B restricts the sample to 75 acquisitions that fulfill two conditions: (i) the buyer and the buyer's law firm are located in the same country; and (ii) the seller and the seller's law firm are located in the same country. Panel C controls for the following variables: (i) Buyer/Law Firm Diff Countries, and (ii) Seller/Law Firm Diff Countries. Variable definitions are provided in Appendix A-4.1. In parentheses are *t*-statistics, calculated with robust standard errors. All regressions control for the variables used in Table 4.3. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Controlling for Client-Lawyer Switches

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	0.18***	3.26*	0.06	6.20**	0.85***	7.31***	-140.40*	-50.09	-1.73*	-59.16
	(2.94)	(1.96)	(1.12)	(2.40)	(2.68)	(3.49)	(-1.95)	(-1.61)	(-1.94)	(-1.57)
Buyer Lawyer Switch	0.02	-0.06	-0.01	-0.57	-0.02	-0.43	28.69	-13.54	-0.45	6.61
	(0.72)	(-0.06)	(-0.38)	(-0.87)	(-0.20)	(-0.63)	(0.84)	(-0.84)	(-1.09)	(0.41)
Seller Lawyer Switch	0.04		-0.03	0.75	0.22	-1.06	-21.53	47.16	0.43	5.91
	(1.13)		(-1.23)	(0.62)	(1.22)	(-1.07)	(-0.62)	(1.35)	(0.79)	(0.19)
Obs.	99	91	98	70	70	99	95	99	99	77
Adj. (Pseudo) R^2	0.064	(0.193)	0.114	(0.294)	0.312	(0.461)	0.120	0.204	0.349	-0.009
Education Index	0.12**	4.39**	-0.00	1.71	0.55**	3.10**	-49.49	36.46	-0.24	-13.53
	(2.51)	(2.31)	(-0.03)	(0.99)	(2.10)	(2.13)	(-0.77)	(0.98)	(-0.32)	(-0.34)
Buyer Lawyer Switch	0.02	-0.37	0.00	-0.21	-0.03	-0.71	-3.79	-12.42	-0.57	-2.97
	(0.70)	(-0.42)	(0.06)	(-0.33)	(-0.25)	(-1.20)	(-0.11)	(-0.83)	(-1.32)	(-0.19)
Seller Lawyer Switch	0.02	1.19	-0.04**	-0.26	0.03	-0.99	-18.70	59.29*	1.01	25.82
	(0.59)	(1.20)	(-2.35)	(-0.30)	(0.17)	(-1.24)	(-0.57)	(1.90)	(1.61)	(0.96)
Obs.	113	113	112	79	79	113	109	113	113	90
Adj. (Pseudo) R^2	0.049	(0.286)	0.163	(0.179)	0.162	(0.333)	0.126	0.188	0.338	-0.055

Table 4.6 (continued)

Panel B: Subsample with Clients and Law Firms from Same Country

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	0.18**	-4.64	0.06	9.16**	0.80	7.69**	-162.26**	-101.83**	-1.40	-83.61
	(2.66)	(-1.37)	(0.87)	(2.20)	(1.46)	(2.43)	(-2.33)	(-2.11)	(-1.60)	(-1.37)
Obs.	59	59	59	39	39	59	58	59	59	43
Adj. (Pseudo) R^2	0.278	(0.509)	0.118	(0.386)	0.242	(0.469)	0.304	0.151	0.322	0.096
Education Index	0.16***	2.32	-0.04	1.36	0.41	3.34	-64.49	53.83	-0.12	29.80
	(3.40)	(0.95)	(-0.72)	(0.59)	(1.13)	(1.47)	(-0.87)	(0.69)	(-0.15)	(0.49)
Obs.	69	69	69	46	46	69	68	69	69	51
Adj. (Pseudo) R^2	0.225	(0.508)	0.194	(0.310)	0.249	(0.396)	0.277	0.042	0.197	-0.104

Panel C: Controlling for Clients and Law Firms from Different Countries

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	0.17***	3.04*	0.06	8.49***	0.82**	7.59***	-130.18*	-60.75*	-1.98**	-56.23
	(3.17)	(1.81)	(1.21)	(2.89)	(2.57)	(3.35)	(-1.98)	(-1.97)	(-2.28)	(-1.45)
Buyer/Law Firm Diff	-0.05	-0.45	-0.01	-3.00***	-0.09	-0.14	-83.24	-27.51	0.70	-17.25
Countries	(-1.46)	(-0.56)	(-0.44)	(-3.09)	(-0.85)	(-0.14)	(-1.62)	(-1.34)	(1.52)	(-0.63)
Seller/Law Firm Diff	-0.02	0.65	-0.02	-2.35***	-0.14		-36.79	-6.54	0.54	0.75
Countries	(-0.49)	(0.61)	(-1.07)	(-2.84)	(-1.27)		(-0.78)	(-0.43)	(1.07)	(0.03)
Obs.	99	99	98	70	70	85	95	99	99	77
Adj. (Pseudo) R^2	0.081	(0.197)	0.113	(0.396)	0.309	(0.465)	0.152	0.183	0.362	-0.001
Education Index	0.13***	4.19**	0.00	2.13	0.57**	2.69**	-35.82	31.40	-0.60	-17.42
	(2.81)	(2.32)	(0.08)	(1.19)	(2.28)	(1.97)	(-0.52)	(0.81)	(-0.77)	(-0.45)
Buyer/Law Firm Diff	-0.06*	0.22	-0.01	-1.91***	-0.13	-0.23	-91.40*	-25.11	0.94*	-2.58
Countries	(-1.79)	(0.27)	(-0.62)	(-2.71)	(-1.17)	(-0.31)	(-1.79)	(-1.39)	(1.92)	(-0.12)
Seller/Law Firm Diff	-0.02	0.93	-0.02	-1.61**	-0.14	-1.75**	-34.09	-6.61	0.83	1.71
Countries	(-0.60)	(0.98)	(-1.19)	(-2.03)	(-1.18)	(-2.06)	(-0.77)	(-0.51)	(1.34)	(0.09)
Obs.	113	113	112	79	79	113	109	113	113	90
Adj. (Pseudo) R^2	0.082	(0.285	0.152	(0.259)	0.189	(0.349)	0.174	0.128	0.343	-0.081

Table 4.7
Negotiation Outcomes and Lawyer Expertise: Client Fixed Effects

This table reports OLS regressions with client fixed effects to explain negotiation outcomes in M&A transactions. We restrict the analysis to 86 acquisitions for which one of the clients (i.e., a buyer or a seller) has appeared at least three times in the sample. There are 18 different clients that occur at least three times as a client. Each column contains a regression with a different dependent variable and each row a separate regression with a different expertise index. These indices vary between 0 and 1, with higher values indicating more legal expertise on the buyer side. Variable definitions are provided in Appendix A-4.1. We report *t*-statistics in parentheses, calculated using robust standard errors. All regressions control for Buyer Law Firm Top 10 and Seller Law Firm Top 10. *** indicates significance at 1%, ** at 5% and * at 10%.

	Contract Design					**Bargaining Process**			**Pricing**	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	0.19**	15.65***	0.09	7.43**	1.04***	10.05***	-132.19**	-45.35	-0.70	-53.91
	(2.54)	(3.29)	(1.59)	(2.20)	(4.52)	(3.10)	(-2.08)	(-1.58)	(-0.82)	(-1.04)
Client FE: *p*-value	(0.00)	(0.06)	(0.16)	(0.47)	(0.00)	(0.21)	(0.00)	(0.00)	(0.00)	(0.00)
Obs.	59	41	59	30	40	49	58	59	57	43
Adj. (Pseudo) R^2	0.112	(0.441	0.067	(0.242)	0.389	(0.339)	0.321	0.423	0.172	0.056
Education Index	0.13	5.10	0.05	2.03	0.91**	4.21**	-113.45	-79.73*	-0.13	-36.41
	(1.53)	(1.63)	(0.94)	(0.87)	(2.53)	(2.24)	(-1.54)	(-2.01)	(-0.16)	(-0.81)
Client FE: *p*-value	(0.31)	(0.98)	(0.28)	(0.48)	(0.00)	(0.35)	(0.00)	(0.01)	(0.00)	(0.00)
Obs.	62	45	62	33	41	50	61	62	60	45
Adj. (Pseudo) R^2	-0.022	(0.161	0.057	(0.248)	0.471	(0.185)	0.277	0.177	0.284	-0.028

Figure 4.1
Negotiation Outcomes and Experience Index: Partial Scatterplots

These figures show partial scatterplots derived from OLS regressions that explain negotiation outcomes with the Experience Index. This index is an average of five proxies for relative lawyer experience. It ranges between 0 and 1, where higher values indicate more legal expertise on the buyer's side. Each figure reports regressions using a different dependent variable, namely: %Warranties without Qualifier; Warranties Fully True; %Payment Secured; MAC Clause; MAC Strength Index; First Draft By Buyer; Negotiation Time; Closing Time; Acquisition Premium; and EBIT Multiple. All regressions control for the economic determinants included in Table 4.3. Note that, even though some dependent variables are binary variables, all regressions for these figures are estimated using OLS.

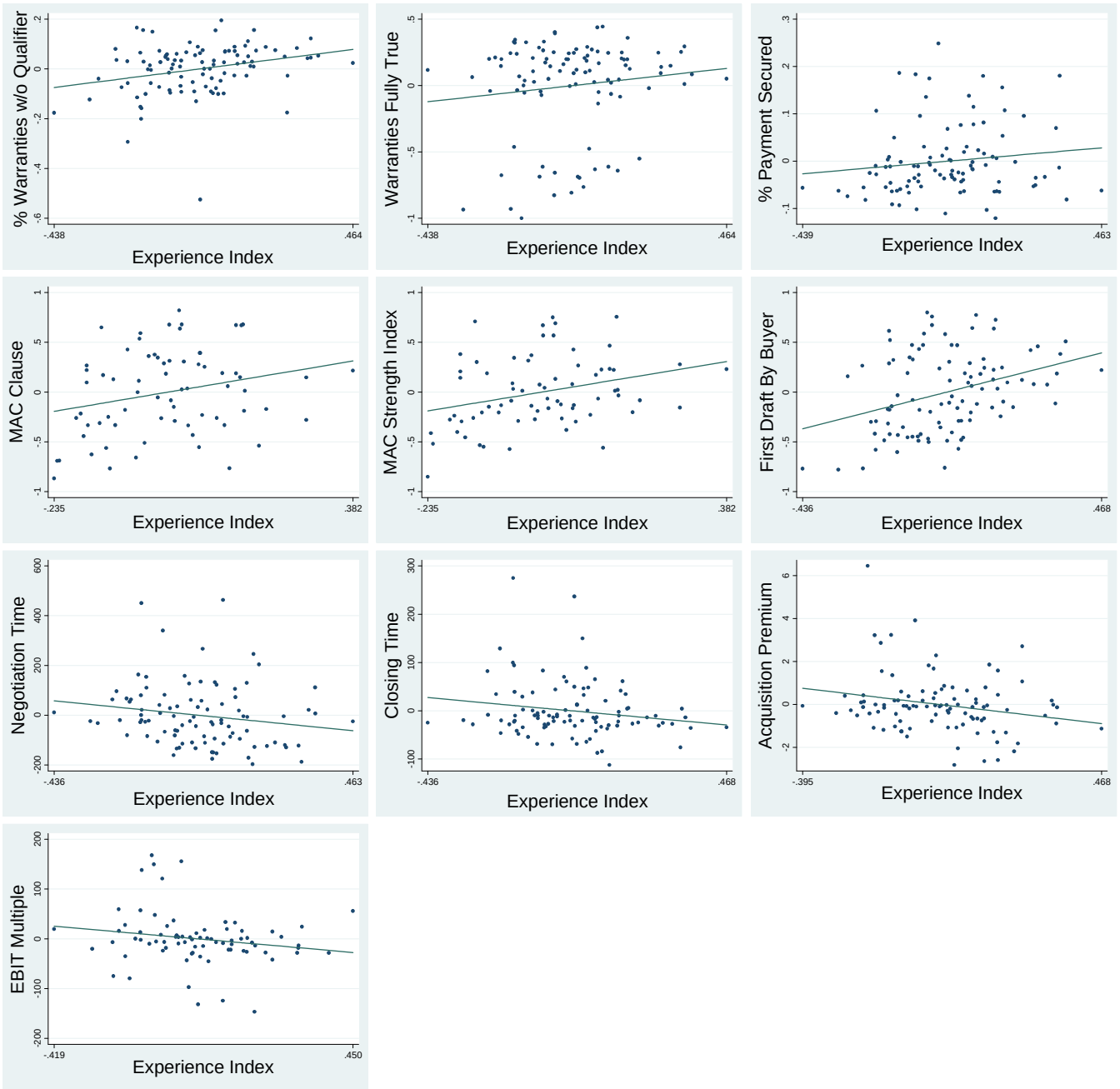
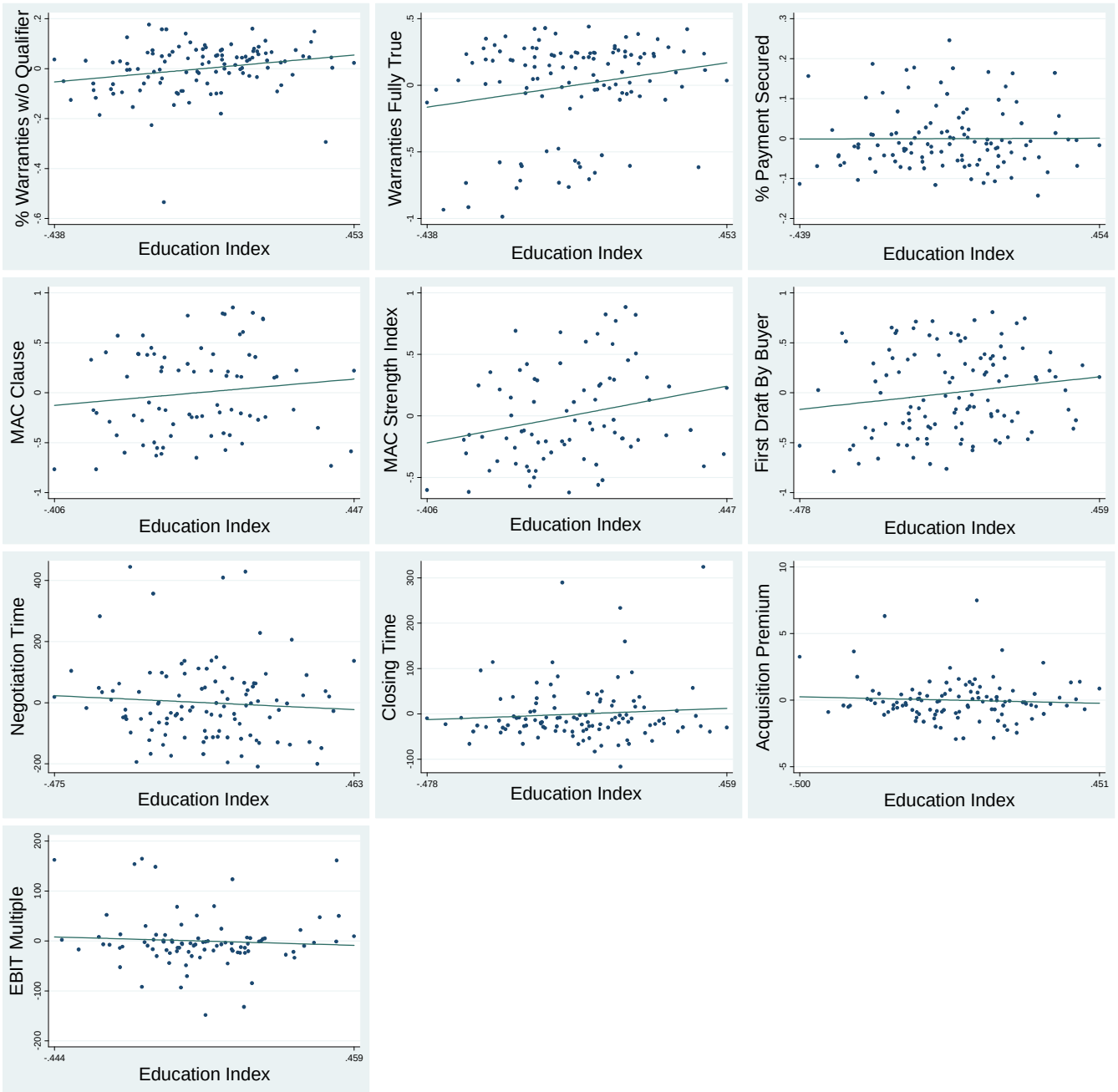


Figure 4.2
Negotiation Outcomes and Education Index: Partial Scatterplots

These figures show partial scatterplots derived from OLS regressions that explain negotiation outcomes with the Education Index. This index an average of five proxies for relative lawyer education. It ranges between 0 and 1, where higher values indicate more legal expertise on the buyer's side. Each figure reports regressions using a different dependent variable, namely: %Warranties without Qualifier; Warranties Fully True; %Payment Secured; MAC Clause; MAC Strength Index; First Draft By Buyer; Negotiation Time; Closing Time; Acquisition Premium; and EBIT Multiple. All regressions control for the economic determinants included in Table 4.3. Note that, even though some dependent variables are binary variables, all regressions for these figures are estimated using OLS.



Appendix A-4.1
Definition of Variables

This table provides the definitions of the variables used in this paper.

Variable	Description
Target Characteristics	
Transaction Value (mEUR)	Total amount of payments by the buyer to the seller. This is equal to the market value of equity of the target unless the buyer purchases less than 100% of the equity. (Source: Acquisition contracts).
Target Book Value (mEUR)	Book value of the assets of the target of the last financial accounts preceding the acquisition. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Target Market Value (mEUR)	Market value of the equity of the target (estimated as the amount paid for the equivalent for 100% of target shares) plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Target Leverage	Book value of liabilities of the target divided by book value of assets of the target. Liabilities include short term debt, long term debt, and provisions. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Target EBIT/Assets	EBIT of the target divided by the book value of the assets of the target. If EBIT data is not available (48 observations), we use the mean value of EBIT/Assets (13.6%) of the sample. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Target Shares Transferred	Percentage of target shares which is transferred from the seller to the buyer. (Source: Acquisition contracts).
Asset Deal	Dummy variable which takes the value 1 if the transaction is an asset deal (i.e., the target is a list of assets and liabilities which will transfer to the buyer), and 0 if it is a share deal or a combination of a share and an asset deal. (Source: Acquisition contracts).
Countries Target	Number of countries in which the target is operating. (Source: Acquisition contracts).
Target Negative Equity	Dummy variable which takes the value 1 if the book value of equity of the target is negative, and 0 otherwise. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Buyer Characteristics	
Buyer Book Value (mEUR)	Book value of the assets of the buyer. If there is more than one buyer in a transaction, we use the weighted average of the assets of the buyers. We use the percentage of the shares bought by the different buyers as weights. (Source: Financial accounts buyer, Amadeus).
Buyer Deal Experience	Number of transactions that a buyer has been engaged in over the 5 years preceding the signing date of a contract. (Source: Merger Market).
Buyer Private Equity	Dummy variable which takes the value 1 if the buyer is a private equity firm, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that buys the highest portion of the shares is a private equity firm, and 0 otherwise. (Source: Merger Market, Amadeus).
Seller Characteristics	
Seller Book Value (mEUR)	Book value of the assets of the seller. If there is more than one seller in a transaction, we use the weighted average of the assets of the sellers. We use the percentage of the shares sold by the different sellers as weights. (Source: Financial accounts seller, Amadeus).
Seller Deal Experience	Number of transactions that a seller has been engaged in over the 5 years preceding the signing date of a contract. (Source: Merger Market).

Appendix A-4.1 (continued)

Multiple Sellers	Dummy variable which takes the value 1 if there is more than one seller involved in a transaction, and 0 if there is only one seller. (Source: Acquisition files).
Seller Leverage	Ratio of total debt to total assets of the seller. This variable is winsorized at 1% to account for outliers. (Source: Financial accounts seller, Amadeus).
Seller Private Equity	Dummy variable which takes the value 1 if the seller is a private equity firm, and 0 otherwise. If there are more buyers, the variable takes the value 1 if the company that sells the highest portion of the shares is a private equity firm, and 0 otherwise. (Source: Merger Market, Amadeus).
Seller Family	Dummy variable which takes the value 1 if the seller is a private person or family, and 0 otherwise. If there are more sellers, the variable takes the value 1 if the party that sells the highest portion of the shares is a private person or family, and 0 otherwise. (Source: Merger Market, Amadeus).
Main Seller Percent	This variable indicates what percentage of the total amount of shares (or total value of assets) is sold by the main seller. If there are more sellers, we define the main seller as the one that sells the largest stake. (Source: Acquisition contracts).
Deal Characteristics	
Cross-Country Deal	Dummy variable which takes the value 1 if the target is not located in the same country as the buyer, and 0 otherwise. (Source: Acquisition contracts, Amadeus).
Approvals Required	Number of approvals which are to be obtained from competition or financial authorities between the signing date and the transfer date of a contract. The transfer date is the date at which there is a transfer of control of the target through the transfer of shares or assets. (Source: Acquisition contracts).
Deal After 2008	Dummy variable which takes the value 1 if the contract is signed on or after January 1, 2008 (i.e., during the financial crisis), and 0 otherwise. (Source: Acquisition contracts).
Controlled Auction	Dummy variable which takes the value 1 if the transaction is organized through a controlled auction, and 0 otherwise. (Source: Acquisition contracts, Merger Market).
Relative Size	Variable indicating the size of the buyer relative to the seller. To create this variable, we first calculate the ratio of the assets of the buyer to the assets of the seller. We then divide this ratio into ten deciles. The resulting variable therefore ranges between 1 and 10, with 10 (1) indicating that the buyer is very large (small) relative to the seller. Transactions in which the seller is a private person or family, and transactions in which the buyer is a government organization are coded such that the relative size variable takes the value 10. (Source: Financial accounts buyer and seller, Amadeus).
Contract Design	
%Warranties w/o Qualifier	Percentage of warranties in a contract which are not qualified with the statement: “so far as the seller is aware” (or any equivalent thereof) (Source: Acquisition contracts).
Warranties Fully True	Dummy variable which takes the value 1 if a contract stipulates a clause that states that the warranties are true without any materiality qualifier, and 0 if the contract stipulates that the warranties are only materially true. (Source: Acquisition contracts).
%Payment Secured	Percentage of the total transaction value which is secured to be available for claims the buyer might have at a later point in time towards the seller. This money is secured by placing it in an Escrow account, an obligation to maintain cash reserves, or a bank guarantee. This variable is winsorized at 5%. (Source: Acquisition contracts).
MAC Clause	Dummy variable which takes the value 1 if the contract stipulates that the transaction does not have to be completed if a material adverse event occurs in the period between the signing date and the closing (transfer) date, and 0 otherwise. (Source: Acquisition contracts).
MAC Clause	Dummy variable which takes the value 1 if the contract stipulates that the transaction does not have to be completed if a material adverse event occurs in the period between the signing date and the closing (transfer) date, and 0 otherwise. (Source: Acquisition contracts).

Appendix A-4.1 (continued)

MAC Strength Index	Index ranging between 0% and 100% which reflects the extent to which the risk of a material adverse event is allocated to the seller (100%) or the buyer (0%). We construct the variable in the following way: Contracts which stipulate a MAC clause have a value of 100% minus a reduction for each exception to the MAC clause which is included the contract. Each exception has a weight 1/13 (the maximum number of exceptions is 13), such that the variable equals (1 – (1/13 * number of exceptions) for contracts containing a MAC and zero for those without a MAC clause. (Source: Acquisition contracts).
Warranties	Number of warranties in a contract. Warranties provide statements about target (or seller) quality. Each separate quality statement is considered as a separate warranty. (Source: Acquisition contracts).
Covenants	Number of covenants in a contract. Covenants prescribe the behavior of the target and the seller in the period between the signing date and the closing (transfer) date. Each separate prescription of behavior is considered a separate covenant. (Source: Acquisition contracts).
Bargaining Process	
First Draft By Buyer	Dummy variable which takes the value 1 if the first draft of the contract was provided by the buyer's lawyer, and 0 if it was provided by the seller's lawyer. (Source: Acquisition contracts).
Negotiation Time	Number of days between the start of negotiations over a transaction and the signing of a contract. The start of the transaction negotiations is defined as the date at which the law firm which has provided the data has opened a file on a transaction (Source: Acquisition files).
Closing Time	Number of days between the signing date and the closing (transfer) date. The closing (transfer) date is the date at which there is a transfer of control of the target through the transfer of shares or assets. (Source: Acquisition contracts, Merger Market).
Pricing	
Acquisition Premium	Market value of the target divided by the book value of the target. The market value of the target is estimated as the amount paid for the equivalent for 100% of target shares plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. This variable is winsorized at 2% to account to outliers. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
EBIT Multiple	Market value of the target divided by the (annualized) EBIT of the last accounts of the target. The market value of the target is estimated as the price paid for the equivalent for 100% of target shares plus the book value of liabilities of the target. Liabilities include short term debt, long term debt, and provisions. This variable is winsorized at 2% to account to outliers. (Source: Acquisition contracts, Financial accounts buyer and/or seller, Amadeus, trade register).
Earnout	Dummy variable which takes the value 1 if the contract stipulates that part of the purchase price will be conditional on target performance after the closing date, and 0 otherwise. (Source: Acquisition contracts).
Relative Lawyer Experience	
Years as Partner	Variable which reflects the years of experience as partner of the buyer's lead lawyer relative to that of the seller's lead lawyer. Years of experience is calculated as the number of years between the year in which the lead lawyer has been promoted to partner status and the year in which a contract is signed. This ratio is standardized such that it ranges between 0 (more seller lawyer years of experience) and 1 (more buyer lawyer years of experience). Transactions where the seller (buyer) has not requested legal advice are coded such that the variable takes the value 1 (0). (Source: LinkedIn, corporate websites of law firms, Acquisition files).

Appendix A-4.1 (continued)

Deal Experience	Variable which reflects the deal experience of the buyer's lead lawyer relative to that of the seller's lead lawyer. Deal experience is calculated as the number of deals that a lawyer has advised on between 01/1995 and 05/2010. This ratio is standardized such that it ranges between 0 (more seller lawyer deal experience) and 1 (more buyer lawyer deal experience). Transactions where the seller (buyer) has not requested legal advice are coded such that the variable takes the value 1 (0). (Source: Merger Market).
Corporate Experience	Variable which takes three values: 0 if only the seller's lead lawyer has worked in the corporate sector; 0.5 if both or neither lead lawyers have worked in the corporate sector; and 1 if only the buyer's lead lawyer has worked in the corporate sector. We classify as the corporate sector any company with commercial operation other than a law firm, excluding courts and universities.
M&A Specialist	Variable which takes three values: 0 if only the seller's lead lawyer is an M&A specialist; 0.5 if both or neither lead lawyers are M&A specialists; and 1 if only the buyer's lead lawyer is an M&A specialist. A lead lawyer is considered an M&A specialist if the corporate web-profile of the lawyer explicitly specifies M&A law as the specialization of the lawyer (rather than other specializations such as tax law or competition law). (Source: websites of law firms).
M&A Expert Listing	Variable which takes three values: 0 if only the seller's lead lawyer is recommended in the Chambers Expert Lawyer ranking; 0.5 if both or neither lead lawyers are recommended in this ranking; and 1 if only the buyer's lead lawyer is recommended in this ranking. The Chambers Expert Lawyer ranking provides information on "the world's leading lawyers" (Source: www.chambersandpartners.com).
Experience Index	Variable which averages the above five relative lawyer experience measures. The variables ranges between 0 (more seller lawyer expertise) and 1 (more buyer lawyer expertise).
Relative Lawyer Education	
University Ranking	Variable which reflects the quality of the university at which the buyer's lead lawyer has studied relative to that of the seller's lead lawyer. The quality of the university is the inverse of the rank of each lawyer's best law school using the following ranking: www.topuniversities.com/university-rankings/world-universityrankings/2012/subject-rankings/social-science/law. We use the inverse of the rank to ensure that higher values indicate higher quality. This ratio is standardized such that it ranges between 0 (seller lawyer from better university) and 1 (buyer lawyer from better university). (Source: LinkedIn, corporate websites of law firms, Acquisition files).
Business Education	Variable which takes three values: 0 if only the seller's lead lawyer has a business degree; 0.5 if both or neither lead lawyers has a business degree; and 1 if only the buyer's lead lawyer has a business degree. We consider as business degree an MBA, a PhD in business or economics, or an undergraduate degree in any business or economics related area. (Source: LinkedIn, corporate websites of law firms, Acquisition files).
US Education	Variable which takes three values: 0 if only the seller's lead lawyer has studied at a US law school; 0.5 if both or neither lead lawyers have studied at a US law school; and 1 if only the buyer's lead lawyer has studied at a US law school. (Source: LinkedIn, corporate websites of law firms).
Education Index	Variable which averages the above three relative lawyer education measures. The variables ranges between 0 (seller lawyer better educated) and 1 (buyer lawyer better educated).
Other Advisor Variables	
Buyer Lawyer Switch	Dummy variable which takes the value 1 if the buyer switches to a new law firm with which she did not have a prior M&A deal relationship over the past five years, and 0 otherwise. (Source: Merger Market).

Appendix A-4.1 (continued)

Seller Lawyer Switch	Dummy variable which takes the value 1 if the seller switches to a new law firm with which she did not have a prior M&A deal relationship over the past five years, and 0 otherwise. (Source: Merger Market).
Buyer/ Law Firm Different Countries	Dummy variable which takes the value 1 if the buyer's headquarters is not located in the country of the law firm that is advising the buyer, and 0 otherwise. If a law firm has several locations, we use the country in which the lead lawyer on the transaction was located (Source: Financial accounts buyer, Amadeus, Merger Market).
Seller/Law Firm Different Countries	Dummy variable which takes the value 1 if the seller's headquarters is not located in the country of the law firm that is advising the seller, and 0 otherwise. If a law firm has several locations, we use the country in which the lead lawyer on the deal was located (Source: Financial accounts seller, Amadeus, Merger Market).
Buyer Law Firm Top 10	Dummy variable which takes the value 1 if the buyer's law firm is ranked in the top 10 based on a ranking of law firms using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).
Seller Law Firm Top 10	Dummy variable which takes the value 1 if the seller's law firm is ranked in the top 10 based on a ranking of law firms using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).
Buyer Bank Top 10	Dummy variable which takes the value 1 if the buyer's bank is ranked in the top 10 based on a ranking of banks using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).
Seller Bank Top 10	Dummy variable which takes the value 1 if the seller's bank is ranked in the top 10 based on a ranking of banks using the number of transactions advised on between 1995 and 2010, and 0 otherwise. (Source: Acquisition files, Merger Market).

Appendix A-4.2
Additional Summary Statistics

Panel A provides summary statistics of the industry, location and advisor distribution of the targets, sellers, and buyers in the sample. The sample consists of 151 acquisitions of private targets between 2005 and 2010. Panel B provides an overview of the legal expertise of the lead lawyers representing the buyer and seller, respectively. This data is used to create the ten relative legal expertise variables use in the paper. Panel C cross-tabulates the presence of top 10 law firms and top 10 banks that are advising buyers and sellers. Across all three panels, statistics are reported at the acquisition level.

Panel A: Industry, Location, Type, and Advisor Distribution of Sample

Industry	**Target**	**Buyer**	**Seller**
Insurance & Real Estate	11%	37%	45%
Manufacturing	28%	17%	23%
Public Administration	0%	0%	1%
Services	32%	16%	5%
Transportation & Communication	9%	10%	7%
Wholesale Trade	12%	13%	11%
Other Industry	8%	7%	8%
Location	**Target**	**Buyer**	**Seller**
The Netherlands	85%	59%	79%
Western Europe (excl. NL)	9%	26%	15%
Eastern Europe	1%	0%	0%
North America	2%	9%	3%
Rest of the World	2%	2%	2%
Advisors	**Target**	**Buyer**	**Seller**
In-House Lawyer	n/a	5%	11%
Lawyer Switch	n/a	31%	11%
Law Firm Top 10	n/a	15%	15%
Client/Law Firm Different Countries	n/a	31%	14%
Bank Top 10	n/a	19%	12%

Panel B: Lawyer Expertise: Summary Statistics

	Advising the Buyer				**Advising the Seller**			
	Mean	**Median**	**Std. Dev.**	**Obs.**	**Mean**	**Median**	**Std. Dev.**	**Obs.**
Experience								
Years as Partner	7.9	7.0	6.2	139	6.7	6.0	5.7	132
Deal Experience	34.5	32.0	25.4	144	32.7	30.5	28.3	134
Corporate Experience	29%	0%	45%	140	21%	0%	41%	133
M&A Specialist	89%	100%	32%	143	79%	100%	41%	140
M&A Expert Listing	64%	100%	48%	151	46%	0%	50%	151
Education								
University Ranking	7%	2%	17%	140	7%	2%	18%	135
Business Education	27%	0%	45%	139	22%	0%	42%	137
US Education	25%	0%	44%	143	21%	0%	41%	136

Panel C: Cross-Table: Buyer and Seller Law Firms and Banks

		Buyer Law Firm Top 10		**Seller Law Firm Top 10**	
		No	Yes	No	Yes
Buyer/Seller Bank Top 10	No	108	15	118	15
	Yes	21	7	11	7
Pearson Chi^2 - Statistic			3.00		9.71
Pearson *p*-value			0.083		0.002

Appendix A-4.3
Overview of Negotiation Process

This table provides an overview of the negotiation process for the acquisitions of privately targets, based on the acquisition files and interviews with 14 lead lawyers (partners) of our law firm. It is completed with information from Freund (1975), Frankel (2005), and Clifford Chance (2011). We report the negotiation process separately for acquisitions organized with and without auctions.

Step	Issue	One-on-One Negotiations	Auction
Step 1	Signaling Interest	• Buyer or seller initiates the contact, either directly or via advisors. • If seller initiates the sale, often a "teaser" is provided: a two page document with initial information on the target.	• Seller initiates negotiations and searches (via banks) for potentially interested buyers. • Bidders are contacted with a "teaser": a two page document with initial information on the target.
Step 2	Non-Disclosure Agreement	• Parties sign a non-disclosure agreement (NDA), where they commit to keep information confidential.	• Interested bidders sign a non-disclosure agreement.
Step 3	Information Memo-randum	• Seller provides more detailed information about the target, often in a formal information memorandum (IM).	• Seller provides more detailed information about target financials and performance.
Step 4	Letter of Intent	• Buyer indicates initial (non-binding) offer price. • Parties may sign a Letter of Intent (LOI), which outlines the initial price, the structure of the deal, and exclusivity during negotiations. Usually prepared by a law firm.	• Bidders indicate their initial offers through 1) an offer LOI, or 2) an offer mark-up of a seller provided contract draft (which includes the price). • Seller selects a few bidders and continues negotiations with them.
Step 5	Due Diligence	• Buyer engages in an in-depth due diligence investigation of the target, usually with the help of an investment bank.	• Seller provides a due diligence report containing detailed target information.
Step 6	Contract Negotiation	• One party provides a first draft of an initial acquisition contract, based on a specimen provided by the advising law firms. • Negotiations take place and are reflected in the contract through mark-ups of the draft. • This can continue for many rounds of mark-ups. • Adjustments to the initial offer price are typically only downwards as new information arises and warranties or covenants are not granted to the buyer.	• Unless done in Step 4, the seller provides a draft acquisition contract. • Bidders provide a binding offer, which contains a combination of a price and a mark-up of the draft acquisition contract. • Price and contract provisions are determined jointly in the offers that bidders make. • Seller selects the final bidder(s) to finalize negotiations.
Step 7	Signing	• Parties sign the acquisition contract, specifying the conditions that need to be fulfilled before the closing. • Closing conditions may also allow for renegotiations if information arises and/or adverse events occur.	• After final negotiations, the seller chooses the winning bidder and both parties sign the contract. • A set of closing conditions may apply as in the one-on-one negotiations.
Step 8	Closing	• Transfer of control of the target from the seller to the buyer.	• Transfer of control of the target from the seller to the buyer.

Appendix A-4.4
Negotiating Outcomes: Buyer and Seller Interests

This table provides an overview of the negotiation outcomes considered in our analysis and the economic interests of the buyer and seller, respectively.

	Buyers		Sellers	
Contract Design	**Prefer**	**Reason**	**Prefer**	**Reason**
%Warranties w/o Qualifier	High	Warranties can come with the statement: "so far as the seller is aware". Without such a qualifier, warranties also cover issues that sellers are unaware of (i.e., sellers provides insurance). So buyers prefer more warranties without knowledge qualifiers.	Low	Warranties can come with the statement: "so far as the seller is aware". This implies that the sellers do not provide insurance for issues they are unaware of. Sellers prefer more warranties with a knowledge qualifier.
Warranties Fully True	Yes	If warranties are only required to be "materially true" (rather than fully true), they are more difficult to enforce. Buyers prefer that this provision is not included, so that warranties are fully true.	No	Seller prefers warranties to only be materially (rather than fully) true, as they become less enforceable. As such, sellers want to include this provision, such that warranties do not need to be fully true.
%Payment Secured	High	Buyer wants to secure as much money as possible to ensure that seller can pay any damage claims that may come up.	Low	Sellers want to place as little money as possible in a secured account, as this implies that sellers cannot yet have access to this money.
MAC Clause	Yes	A MAC clause allows buyers to cancel a deal if an adverse event occurs between signing and closing. Buyers prefer including a MAC clause, as this places the risk of such events on sellers.	No	Sellers prefer not including a MAC clause, as this places the risk of adverse events on buyers, and increases deal certainty.
MAC Strength Index	High	Each exception to the MAC clause reduces the right of buyers to cancel a deal if an adverse event occurs between signing and closing. As such, buyers prefer few exceptions, implying a high MAC index.	Low	Each exception to the MAC clause allocates risk of adverse events occurring between signing and closing back to buyers. This reduces buyers' right to cancel a deal. As such, sellers prefer many exceptions, i.e., a low MAC index.
Bargaining Process				
First Draft By Buyer	Yes	Buyers prefer to deliver the first draft contract, as this provides a first-mover advantage due to path dependence in negotiations.	No	Sellers prefer to deliver the first draft contract, as this provides a first-mover advantage due to path dependence in negotiations.

Appendix A-4.4 (continued)

	Buyers		Sellers	
	Prefer	**Reason**	**Prefer**	**Reason**
Negotiation Time	Short	Buyers prefer short negotiation times to minimize transactions costs and to reduce moral hazard on the side of the target's management once it hears that a deal is pending. Buyers also prefer short negotiation times to avoid that the period of exclusive negotiations expires. These periods (specifying that sellers may not contact other bidders) are usually set at the start of negotiations in an LOI.	Mixed	On the one hand, sellers prefer short negotiation times to minimize transactions costs. On the other hand, sellers prefer long negotiation times so that the period of exclusive negotiations expires. Upon expiration of this period, sellers can shop around for higher offers by alternative bidders.
Closing Time	Short	Buyers prefer short closing times (time between signing and closing of a transaction) as sellers still control the targets until closing even though the price has been fixed. Until the closing, sellers can act opportunistically and extract private benefits from targets.	Long	Sellers prefer long closing times (time between signing and closing of a transaction) as sellers still have control over the target until closing whereas the prices have been fixed. Until closing, sellers can act opportunistically and extract private benefits from targets.
Pricing				
Acquisition Premium	Low	Buyers prefer to pay a low price.	High	Sellers prefer to receive a high price.
EBIT Multiple	Low	Buyers prefer to pay a low multiple.	High	Sellers prefer to receive a high price.

Appendix A-4.5
Examples for Warranties and Covenants

This table provides examples of warranties and covenants that are typically observed in our acquisition contracts.

Warranty Area	**Examples**
Corporate Records	Target and all subsidiaries validly exist.
	Constitution documents/articles of association are true, complete and accurate.
Financial Accounts	The accounts give a true and fair view of the state of financial affairs of the company.
	The accounts have been prepared and filed in compliance with legal requirements.
	Target has properly and accurately filed all tax returns.
	All tax returns filed by the target are in compliance with applicable laws.
	No material adverse effect has occurred since the last balance sheet date.
	Target has not paid any dividends or made any other distribution to shareholders.
	Target has not incurred any new loans, debt or issued debt securities.
Assets	All assets listed in the accounts are legally and beneficially owned by the target.
	The target's assets are in good operating state, subject to normal wear and tear.
	The assets owned or leased by the company are sufficient to continue the operations.
Contracts	All contracts have been complied with by the target.
	Target has not defaulted on its debt obligations or failed to pay for any obligation.
	Target has not received a notice of termination or intent to terminate a contract.
Insurance	The insurance policies of the target have been disclosed and are accurate.
	Target carries insurance for amounts and risks that are customary in the industry.
	Target has paid all insurance premiums.
Intellectual Property	Target has valid ownership or licenses to the intellectual property.
	Target does not infringe on any intellectual property rights of a third party.
Legal	Target is conducting the business in compliance with all applicable laws.
	Target is not involved in any legal dispute (claim, proceeding, litigation, etc.).
	All environmental permits have been obtained, are in full force and are complied with.
Covenant Area	**Example**
Employees	Target/Seller shall not adopt or amend any pension or retirement plan.
	Target/Seller shall not increase any salaries or wages.
	Target/Seller shall not pay any bonuses other than those under existing contracts.
	Target/Seller shall not enter into new/terminate employment contracts.
Dividend Payments	Target/Seller shall not declare or pay any dividends.
	Target/Seller shall not make any payments to any of the sellers.
	Target/Seller shall not issue or sell any shares in its capital stock.
	Target/Seller shall not issue or sell any options, or warrants on the target shares.
Debt	Target/Seller shall not issue any debt securities.
	Target/Seller shall not amend the debt contracts, or agree to a higher interest rate.
	Target/Seller shall comply with all payment obligations of the debt contracts.
	Target/Seller shall not make or extend a loan to any other person.
Business Conduct	Target/Seller will carry on the business in the ordinary course as conducted so far.
	Target/Seller shall maintain the equipment in good condition, subject to wear and tear.
	Target/Seller will preserve the relationship with customers and suppliers.
Acquisitions	Target/Seller shall not enter into any contract or commitment to acquire any assets.
Divestments	Target/Seller shall not sell, lease, or dispose of any of the assets of the business.
	Target/Seller shall not pledge, encumber or mortgage any of the assets of the business.

Appendix A-4.6
Robustness Checks on Acquisition Premium

This table reports OLS regressions with two robustness checks on pricing in M&A transactions. The table provides regressions that control for (i) Buyer/Seller Bank Top 10 (Bank Controls); and (ii) proxies of contract design (Contract Controls). As Contract Controls we include: %Warranties w/o Qualifier, Warranties Materially True, %Payment Secured, and MAC Strength Index. The regressions in Columns 1 and 2 use the Acquisition Premium as dependent variable, while those in Columns 3 and 4 use the EBIT Multiple as dependent variable. The sample consists of 151 acquisitions. Each row represents a separate regression with a different measure of relative lawyer expertise. All regressions control for the variables used in Table 4.3. Variable definitions are provided in Appendix A-4.1. We report *t*-statistics in parentheses, calculated using robust standard errors. *** indicates significance at 1%, ** at 5% and * at 10%.

	Pricing			
Dependent Variable:	**Acquisition Premium**		**EBIT Multiple**	
Experience	(1)	(2)	(3)	(4)
Years as Partner	-0.44	-0.50	6.50	7.42
	(-1.18)	(-1.20)	(0.36)	(0.42)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	109	108	83	82
Adj. (Pseudo) R^2	0.338	0.310	-0.017	-0.038
Deal Experience	-0.94**	-0.92**	-28.49	-29.46
	(-2.05)	(-2.00)	(-1.46)	(-1.49)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	120	118	93	91
Adj. (Pseudo) R^2	0.305	0.328	-0.018	-0.059
Corporate Experience	-0.78	-0.98	-45.38**	-33.75**
	(-1.59)	(-1.65)	(-2.54)	(-2.06)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	116	115	91	90
Adj. (Pseudo) R^2	0.323	0.319	0.012	-0.057
M&A Specialist	-1.22**	-1.26**	-6.81	-2.32
	(-2.31)	(-2.14)	(-0.25)	(-0.07)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	124	123	96	95
Adj. (Pseudo) R^2	0.311	0.310	-0.040	-0.083
M&A Expert Listing	-0.76*	-0.67	-37.37**	-44.71**
	(-1.83)	(-1.44)	(-2.09)	(-2.41)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	141	139	107	105
Adj. (Pseudo) R^2	0.365	0.351	0.017	0.009
Experience Index	-1.92**	-1.79*	-59.04	-58.44
	(-2.11)	(-1.84)	(-1.55)	(-1.40)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	99	98	77	76
Adj. (Pseudo) R^2	0.352	0.348	0.007	-0.021

Appendix A-4.6 (continued)

	Pricing			
Dependent Variable:	**Acquisition Premium**		**EBIT Multiple**	
Education	(1)	(2)	(3)	(4)
University Ranking	-0.60	-0.81*	-2.14	0.03
	(-1.52)	(-1.67)	(-0.14)	(0.00)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	119	118	93	92
Adj. (Pseudo) R^2	0.332	0.318	-0.047	-0.090
Business Education	0.05	0.18	-22.20	-19.40
	(0.10)	(0.36)	(-1.01)	(-0.84)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	118	117	91	90
Adj. (Pseudo) R^2	0.284	0.281	-0.040	-0.059
US Education	0.15	0.08	-2.99	5.34
	(0.25)	(0.12)	(-0.12)	(0.17)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	121	120	95	94
Adj. (Pseudo) R^2	0.310	0.293	-0.043	-0.084
Education Index	-0.27	-0.66	-22.92	-15.32
	(-0.36)	(-0.78)	(-0.62)	(-0.34)
Bank Controls	YES	NO	YES	NO
Contract Controls	NO	YES	NO	YES
Obs.	113	112	90	89
Adj. (Pseudo) R^2	0.318	0.297	-0.050	-0.071

Appendix A-4.7
Determinants of Lawyer Expertise

This table reports OLS and (ordered) logit regressions to explain the legal expertise. The sample consists of 151 acquisitions of private targets. Each column contains a regression with a different dependent variable (listed horizontally). In Panel A the expertise measures refer to the lead lawyer advising the buyer. In Panel B the expertise measure relate to the lead lawyer advising the seller. Finally, in Panel C they relate to relative lawyer expertise. Summary statistics of these variables are reported in Appendix A-4.2 Panel B. Detailed variable definitions are provided in Appendix A-4.1. We report *t*-statistics in parentheses, calculated using robust standard errors. The regressions have less than 151 observations because of missing data for some variables. *** indicates significance at 1%, ** at 5%, and * at 10%.

Panel A: Determinants of Expertise of Buyer Lead Lawyer

	Dependent Variable: Buyer Lawyer Expertise							
Dependent Variable	Years as Partner	Deal Exper.	Corporate Exper.	M&A Specialist	M&A Listing	Univ. Ranking	Business Educ.	US Educ.
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Target Book Value (log)	-0.07	-1.32	-0.11	0.05	-0.11	-0.01*	-0.19	-0.06
	(-0.21)	(-1.08)	(-0.94)	(0.20)	(-0.77)	(-1.70)	(-1.28)	(-0.39)
Countries Target	0.08	0.05	0.01	-0.18***	0.01	0.01	0.04	0.05
	(0.65)	(0.12)	(0.37)	(-2.94)	(0.24)	(1.20)	(0.94)	(1.34)
Buyer/Law Firm Diff	3.09**	-4.03	-1.49***	0.67	0.25	0.10**	-1.39**	0.56
Countries	(2.45)	(-0.79)	(-2.62)	(0.49)	(0.50)	(2.10)	(-2.51)	(1.25)
Buyer Book Value (log)	-0.07	0.62	0.12	0.49***	0.13	0.01	-0.15	0.04
	(-0.32)	(0.66)	(1.46)	(3.64)	(1.60)	(1.28)	(-1.54)	(0.46)
Seller Book Value (log)	0.00	-0.30	0.01	-0.15	-0.09	0.01*	0.07	0.01
	(0.01)	(-0.57)	(0.20)	(-1.00)	(-1.04)	(1.80)	(1.07)	(0.17)
Buyer Deal Experience	0.23	5.21***	-0.06	1.51***	0.12	-0.02*	0.47**	-0.34*
(log)	(0.50)	(2.73)	(-0.36)	(2.80)	(0.68)	(-1.70)	(2.10)	(-1.69)
Seller Deal Experience	-0.21	-1.45	-0.01	0.58	-0.06	0.01	-0.19	-0.15
(log)	(-0.42)	(-0.71)	(-0.05)	(1.10)	(-0.32)	(0.66)	(-0.91)	(-0.75)
Deal After 2008	2.91***	1.03	0.30	-0.76	0.55	-0.01	1.06**	0.44
	(2.88)	(0.21)	(0.69)	(-0.66)	(1.18)	(-0.23)	(2.17)	(1.00)
Controlled Auction	0.94	4.25	-0.27		0.85	-0.01	0.06	0.02
	(0.83)	(0.77)	(-0.51)		(1.53)	(-0.32)	(0.11)	(0.03)
Obs.	124	128	125	99	135	125	124	127
Adj. (Pseudo) R^2	0.073	0.065	(0.076)	(0.489)	(0.115)	0.139	(0.131)	(0.059)

Appendix A-4.7 (continued)

Panel B: Determinants of Expertise of Seller Lead Lawyer

	Dependent Variable: Seller Lawyer Expertise							
Dependent Variable	Years as Partner	Deal Exper.	Corporate Exper.	M&A Specialist	M&A Listing	Univ. Ranking	Business Educ.	US Educ.
Target Book Value (log)	0.50	3.48**	-0.06	0.23	0.26*	0.02	0.16	-0.05
	(1.27)	(2.17)	(-0.36)	(0.76)	(1.93)	(1.04)	(1.03)	(-0.33)
Countries Target	-0.14*	-0.09	0.01	0.12	0.04	0.00	0.03	-0.01
	(-1.66)	(-0.16)	(0.26)	(1.03)	(0.85)	(0.20)	(0.88)	(-0.16)
Seller/Law Firm Diff	3.02**	-15.46**	-0.70	-1.67**	-1.10	-0.03	-0.97	-0.01
Countries	(2.21)	(-2.43)	(-0.80)	(-2.03)	(-1.54)	(-0.81)	(-1.05)	(-0.02)
Buyer Book Value (log)	0.03	0.87	0.02	-0.05	0.04	0.01	-0.09	-0.04
	(0.11)	(0.84)	(0.21)	(-0.36)	(0.41)	(1.31)	(-0.78)	(-0.33)
Seller Book Value (log)	0.32***	-0.66	-0.06	0.01	0.06	0.00	-0.15***	0.16*
	(2.88)	(-0.66)	(-1.21)	(0.18)	(0.53)	(0.98)	(-2.76)	(1.91)
Buyer Deal Experience	-0.27	-0.90	-0.16	0.16	0.03	-0.01	-0.12	0.44*
(log)	(-0.59)	(-0.41)	(-0.77)	(0.47)	(0.15)	(-0.86)	(-0.52)	(1.92)
Seller Deal Experience	-0.60	3.92	0.11	0.65*	0.27	-0.01	0.37	-0.42**
(log)	(-1.48)	(1.63)	(0.51)	(1.93)	(1.29)	(-0.53)	(1.62)	(-2.05)
Deal After 2008	0.09	-3.04	0.16	-0.39	0.10	0.02	-0.08	-0.88
	(0.08)	(-0.55)	(0.31)	(-0.51)	(0.23)	(0.59)	(-0.15)	(-1.53)
Controlled Auction	-0.99	11.28*	1.01*	-1.77**	-0.00	0.03	0.68	-0.40
	(-0.86)	(1.82)	(1.83)	(-2.34)	(-0.00)	(0.78)	(1.28)	(-0.68)
Obs.	109	111	110	116	125	112	113	113
Adj. (Pseudo) R^2	0.097	0.100	(0.063)	(0.239)	(0.163)	0.006	(0.105)	(0.088)

Panel C: Determinants of Relative Lawyer Expertise

	Dependent Variable: Relative Lawyer Expertise							
Dependent Variable	Years as Partner	Deal Exper.	Corporate Exper.	M&A Specialist	M&A Listing	Univ. Ranking	Business Educ.	US Educ.
Target Book Value (log)	0.01	-0.01	-0.18	0.03	-0.22*	0.00	-0.35**	0.17
	(0.79)	(-0.98)	(-1.39)	(0.13)	(-1.75)	(0.24)	(-1.98)	(0.98)
Countries Target	0.00	0.01	0.06*	-0.07	0.01	0.01*	0.04	0.01
	(0.65)	(1.09)	(1.71)	(-1.24)	(0.54)	(1.71)	(1.08)	(0.36)
Buyer/Law Firm Diff	0.05	-0.12**	-2.00***	-0.49	-0.24	0.15**	-1.30***	1.19***
Countries	(0.82)	(-2.34)	(-3.33)	(-0.82)	(-0.56)	(2.31)	(-2.67)	(2.93)
Seller/Law Firm Diff	-0.09	0.08	-0.54	0.06	-0.04	-0.09	0.33	-0.47
Countries	(-1.32)	(1.28)	(-1.08)	(0.05)	(-0.08)	(-1.39)	(0.64)	(-0.81)
Buyer Book Value (log)	-0.01	-0.00	0.09	0.28**	0.08	0.02*	-0.00	0.07
	(-0.50)	(-0.46)	(1.04)	(2.14)	(1.13)	(1.98)	(-0.03)	(0.63)
Seller Book Value (log)	-0.01	-0.01	0.03	-0.15**	-0.07	0.01	0.12**	-0.02
	(-1.15)	(-1.19)	(0.46)	(-2.25)	(-0.95)	(1.39)	(2.44)	(-0.45)
Buyer Deal Experience	0.05*	0.02	-0.01	0.31	0.03	-0.05**	0.39*	-0.41**
(log)	(1.69)	(0.94)	(-0.08)	(1.04)	(0.22)	(-2.55)	(1.83)	(-2.56)
Seller Deal Experience	-0.00	-0.03*	-0.11	-0.16	-0.25	0.01	-0.34*	0.07
(log)	(-0.13)	(-1.72)	(-0.48)	(-0.58)	(-1.32)	(0.34)	(-1.78)	(0.39)
Deal After 2008	0.02	0.00	0.78	0.37	0.38	-0.04	0.92*	0.51
	(0.31)	(0.04)	(1.57)	(0.54)	(0.89)	(-0.68)	(1.91)	(1.05)
Controlled Auction	0.01	0.03	-0.96*	1.27	0.24	-0.05	-0.57	0.12
	(0.21)	(0.42)	(-1.70)	(1.64)	(0.50)	(-0.73)	(-1.24)	(0.27)
Obs.	90	100	98	104	121	100	98	103
Adj. (Pseudo) R^2	0.005	0.079	(0.119)	(0.199)	(0.099)	0.125	(0.126)	(0.090)

Appendix A-4.8
Negotiation Outcomes and Lawyer Expertise: Controlling for Bargaining Power and Risk-Bearing Capacity

This table reports OLS and logit regressions to explain negotiation outcomes in M&A transactions. The sample consists of 151 acquisitions of private targets between 2005 and 2010. Each column contains a regression with a different dependent variable (listed horizontally). All regressions control for the variables used in Table 4.3 (not reported). In addition, the regressions in Panel A and Panel B control for proxies of bargaining power using the following variables: Buyer Deal Experience, Seller Deal Experience, Deal After 2008, and Controlled Auction. In Panel B we add Experience Index and Education Index to these variables (listed vertically). We only report Experience Index and Education Index and not the bargaining power proxies. The regressions in Panel C and D control for proxies of financial distress of the seller: Seller Leverage, and Target Negative Equity. In Panel D we add the Experience Index and Education Index to these are variables (listed vertically). We only report Experience Index and Education Index and not the financial distress proxies. The regressions in Panel E and F control for proxies of risk-bearing capacity of buyers and sellers using the following variables: Buyer Private Equity, Seller Private Equity, Seller Family, and Main Seller Percent. In Panel F we add the Experience Index and Education Index to these variables (listed vertically). We only report Experience Index and Education Index and not the risk bearing capacity proxies. Detailed variable definitions are provided in Appendix A-4.1. We report *t*-statistics in parentheses, calculated using robust standard errors. The regressions have less than 151 observations because of missing data. *** indicates significance at 1%, ** at 5% and * at 10%.

Panel A: Negotiating Outcomes– Effects of Bargaining Power

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Relative Size	-0.01	-0.42***	0.01	0.04	0.04*	0.36***	-5.02	0.82	0.06	-0.94
	(-1.15)	(-2.95)	(1.61)	(0.32)	(1.94)	(2.90)	(-0.88)	(0.23)	(0.76)	(-0.37)
Buyer Deal Experience (log)	0.00	0.14	0.00	-0.05	-0.03	0.08	-8.27	-1.85	0.27*	12.75**
	(0.41)	(0.59)	(0.49)	(-0.22)	(-0.69)	(0.26)	(-0.83)	(-0.45)	(1.83)	(2.56)
Seller Deal Experience (log)	0.00	-0.26	-0.01**	-0.24	-0.00	-0.17	1.61	3.94	-0.03	2.52
	(0.22)	(-1.01)	(-2.24)	(-1.10)	(-0.11)	(-0.78)	(0.16)	(0.59)	(-0.30)	(0.42)
Deal After 2008	-0.01	0.36	-0.03*	0.51	0.07	0.63	39.68	6.10	0.16	-14.60
	(-0.41)	(0.67)	(-1.77)	(1.00)	(0.70)	(1.05)	(1.57)	(0.64)	(0.47)	(-1.43)
Controlled Auction	0.05*	0.98	-0.00	-0.71	-0.24**	-3.24***	8.42	-5.26	0.05	-17.30*
	(1.79)	(1.53)	(-0.04)	(-1.33)	(-2.38)	(-3.40)	(0.33)	(-0.50)	(0.16)	(-1.82)
Obs.	139	139	138	95	95	140	136	140	140	107
Adj. (Pseudo) R^2	-0.007	(0.201)	0.185	(0.134)	0.076	(0.453)	0.142	0.146	0.364	0.039

Appendix A-4.8 (continued)

Panel B: Effects of Relative Lawyer Expertise – Controlling for Bargaining Power

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	-0.16***	-2.38	0.06	5.31*	0.59	8.25***	-149.61**	-62.05*	-1.76*	-48.11
	(-2.78)	(-1.15)	(1.11)	(1.83)	(1.52)	(3.65)	(-2.27)	(-1.70)	(-1.84)	(-1.31)
Obs.	99	99	98	70	70	99	95	99	99	77
Adj. (Pseudo) R^2	0.046	(0.260)	0.116	(0.315)	0.312	(0.525)	0.165	0.167	0.326	0.138
Education Index	-0.11**	-4.66**	0.02	1.22	0.35	3.13**	-85.61	20.51	-0.50	-3.51
	(-2.20)	(-2.31)	(0.36)	(0.62)	(1.23)	(2.28)	(-1.34)	(0.48)	(-0.60)	(-0.08)
Obs.	113	113	112	79	79	113	109	113	113	90
Adj. (Pseudo) R^2	0.058	(0.332)	0.163	(0.209)	0.230	(0.442)	0.171	0.102	0.303	-0.016

Panel C: Negotiating Outcomes– Effects of Financial Distress

	Contract Design					Negotiation Dynamics			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Seller Leverage	-0.00	-0.93	-0.00	1.41*	0.26*	0.69	-35.94	22.05*	-0.76	-19.39
	(-0.15)	(-1.01)	(-0.14)	(1.67)	(1.82)	(1.01)	(-0.91)	(1.69)	(-1.40)	(-1.08)
Target Negative Equity	-0.05	0.40	-0.11***	-2.35	-0.41	-0.18	-5.37	-49.90***	-0.07	13.56
	(-1.59)	(0.20)	(-4.09)	(-1.47)	(-1.23)	(-0.19)	(-0.16)	(-2.64)	(-0.09)	(0.36)
Obs.	140	140	139	96	96	141	137	141	141	107
Adj. (Pseudo) R^2	-0.025	(0.174)	0.185	(0.124)	0.061	(0.324)	0.137	0.184	0.361	-0.038

Appendix A-4.8 (continued)

Panel D: Effects of Relative Lawyer Expertise – Controlling for Financial Distress

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	-0.17***	-2.84	0.07	5.72**	0.78**	7.28***	-118.53*	-62.85*	-1.71*	-55.21
	(-2.90)	(-1.63)	(1.56)	(2.01)	(2.45)	(3.55)	(-1.70)	(-1.97)	(-1.97)	(-1.55)
Obs.	99	99	98	70	70	99	95	99	99	77
Adj. (Pseudo) R^2	0.053	(0.199)	0.180	(0.308)	0.308	(0.454)	0.151	0.187	0.358	0.006
Education Index	-0.12**	-4.37**	-0.00	1.24	0.47*	2.80**	-48.97	23.65	-0.47	-18.79
	(-2.41)	(-2.28)	(-0.01)	(0.63)	(1.75)	(2.14)	(-0.80)	(0.63)	(-0.61)	(-0.49)
Obs.	113	113	112	79	79	113	109	113	113	90
Adj. (Pseudo) R^2	0.051	(0.275)	0.240	(0.232)	0.199	(0.325)	0.168	0.152	0.302	-0.057

Panel E: Negotiating Outcomes– Effects of Risk-Bearing Capacity

	Contract Design					Negotiation Dynamics			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Buyer Private Equity	-0.04	-0.97	0.04*	-0.41	-0.13	-0.68	-6.25	4.17	1.07***	4.64
	(-1.00)	(-1.38)	(1.80)	(-0.54)	(-1.05)	(-1.00)	(-0.24)	(0.27)	(2.64)	(0.31)
Seller Private Equity	-0.03	0.40	-0.01	-3.04***	-0.36***	-1.18	-48.57	1.85	0.09	21.80
	(-1.01)	(0.43)	(-0.49)	(-2.83)	(-2.92)	(-1.59)	(-1.45)	(0.13)	(0.22)	(1.05)
Seller Family	0.01	0.45	0.10***	0.44	0.09	1.74	-16.73	-9.31	-0.04	-17.04
	(0.40)	(0.39)	(3.55)	(0.40)	(0.52)	(1.62)	(-0.63)	(-0.63)	(-0.05)	(-1.39)
Main Seller Percent	-0.04	3.14	-0.20***	7.08**	0.80*	2.69	1.06	30.12	-2.15*	-5.87
	(-0.45)	(0.96)	(-3.04)	(2.08)	(1.91)	(1.05)	(0.01)	(0.97)	(-1.85)	(-0.10)
Obs.	140	140	139	96	96	141	137	141	141	107
Adj. (Pseudo) R^2	-0.016	(0.187)	0.311	(0.235)	0.139	(0.376)	0.130	0.145	0.377	-0.028

Appendix A-4.8 (continued)

Panel F: Effects of Relative Lawyer Expertise – Controlling for Risk-Bearing Capacity

	Contract Design					Bargaining Process			Pricing	
Dependent Variable:	%Warranties w/o Qualifier	Warranties Fully True	%Payment Secured	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Acquisition Premium	EBIT Multiple
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Experience Index	0.17***	3.34*	0.03	6.34*	0.71**	7.53***	-150.67**	-59.63*	-1.82*	-43.92
	(2.90)	(1.70)	(0.73)	(1.89)	(2.26)	(3.34)	(-2.17)	(-1.91)	(-1.84)	(-1.17)
Obs.	99	99	98	70	70	99	95	99	99	77
Adj. (Pseudo) R^2	0.031	(0.216)	0.259	(0.419)	0.358	(0.495)	0.105	0.161	0.343	0.004
Education Index	0.12**	4.74**	0.01	0.57	0.41	2.71*	-55.65	23.98	-0.21	-8.39
	(2.46)	(2.22)	(0.33)	(0.32)	(1.46)	(1.88)	(-0.82)	(0.62)	(-0.26)	(-0.21)
Obs.	113	113	112	79	79	113	109	113	113	90
Adj. (Pseudo) R^2	0.036	(0.310)	0.303	(0.289)	0.205	(0.359)	0.114	0.106	0.306	-0.018

Appendix A-4.9
Negotiation Outcomes: Correlations

This table reports the correlation coefficients between negation outcomes variables. * indicates significance at least at the 5% level.

		Warranties	%Warrant w/o Qualifier	Warrant Fully True	%Pay-ment Secured	Covenants	MAC Clause	MAC Strength Index	First Draft By Buyer	Negotiation Time	Closing Time	Earnout	Acquis. Premium
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Warranties	(1)	1.00											
%Warranties w/o Qual.	(2)	0.01	1.00										
Warranty Materially True	(3)	0.26*	0.21*	1.00									
%Payment Secured	(4)	0.26*	0.15	0.18*	1.00								
Covenants	(5)	0.20*	0.00	0.22*	-0.05	1.00							
MAC Clause	(6)	0.22*	-0.02	0.08	0.05	0.34*	1.00						
MAC Strength Index	(7)	0.20*	0.03	0.15	0.10	0.28*	0.91*	1.00					
First Draft By Buyer	(8)	0.23*	0.28*	0.22*	0.31*	-0.29*	0.10	0.18*	1.00				
Negotiation Time	(9)	-0.03	-0.09	-0.18*	-0.15	0.04	0.15	0.08	-0.13	1.00			
Closing Time	(10)	-0.01	-0.12	0.13	-0.12	0.48*	0.21*	0.17*	-0.29*	0.06	1.00		
Earnout	(11)	0.05	0.12	0.05	0.12	-0.17*	0.03	-0.05	0.11	-0.05	-0.10	1.00	
Acquisition Premium	(12)	0.19*	0.12	0.07	0.16	-0.10	-0.05	-0.02	0.16	-0.20*	-0.09	0.31*	1.00
EBIT Multiple	(13)	-0.01	0.00	-0.02	-0.12	0.17	0.09	0.12	-0.14	0.01	0.16	-0.12	0.10

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6

Samenvatting (Summary in Dutch)

6.1 Introductie

Bedrijfsovernames zijn in zowel juridisch als in economisch opzicht een intrigerende aangelegenheid. Doordat koper en verkoper doorgaans niet beschikken over dezelfde informatie, kunnen overnames risico's en economische kwesties met zich meebrengen. Zo kan er onzekerheid zijn over de waarde van de targetonderneming of over het gedrag van het management. In theorie kunnen deze kwesties worden beperkt door de inzet van overnamecontracten, bijvoorbeeld doordat dergelijke contracten kopers bescherming kunnen bieden tegen onaangename verassingen achteraf. De vraag is of overname-contracten hier ook daadwerkelijk voor worden gebruikt. Indien contracten worden ingezet om dit soort problemen bij een overname te ondervangen, dan zouden deze contracten een zuivere reflectie moeten zijn van de (economische) eigenschappen van een deal. Het is echter ook mogelijk dat, naast alle economische facetten, de betrokken juridische adviseurs van invloed zijn op overnamecontracten. Advocaten zouden dan een eigen aanpak of stijl kunnen hebben in de manier waarop zij contracten onderhandelen. Dat werpt de vraag op wat de rol is van contracten en juridische adviseurs bij overnames.

In dit onderzoek benader ik overnamecontracten vanuit een financieel-economisch perspectief om licht te werpen op de volgende drie vragen: Waarom variëren contracten bij verschillende deals van elkaar? Wat is het effect van deze variatie op de prijs die is betaald? En wat is de invloed van de betrokken advocaten en advocatenkantoren bij een overname? Ik heb 151 koopcontracten geanalyseerd van onderhandse bedrijfsovernames, dat wil zeggen overnames van niet-beursgenoteerde ondernemingen. Deze contracten zijn ter beschikking gesteld door een groot Nederlands advocatenkantoor. Onderhandse overnames vormen een interessante basis om contracten te analyseren, omdat kopers hierin direct onderhandelen met één of een paar verkopers.[1] Als gevolg kunnen er veel verschillende contractuele instrumenten worden ingezet.

6.2 Wat verklaart de variatie tussen overnamecontracten?

In hoofdstuk 2 neem ik twee contractuele bepalingen als uitgangspunt om enerzijds de invloed van economische omstandigheden, anderzijds de invloed van juridische adviseurs (advocaten) op de inhoud van een overnamecontract te analyseren. De eerste bepaling die ik als uitgangspunt neem, de zogeheten *garanties*, moet de koper beschermen tegen onaangename verrassingen achteraf over de eigenlijke waarde van de target. De verkoper beschikt doorgaans over meer informatie over de target dan de koper, zodat de koper bezorgd kan zijn dat hem een te optimistische weergave van de feiten is gegeven. Met garanties kan de verkoper haar waardering kracht bijzetten, door bijvoorbeeld te stellen dat de apparatuur in goede staat verkeert, of dat alle patenten en licenties rechtsgeldig zijn. Indien gegarandeerde stellingen onjuist blijken, heeft de verkoper de verplichting om eventuele schade te vergoeden.

De tweede bepaling die ik analyseer zijn de *convenanten*. Met convenanten wordt in het contract een zekere gedragscode afgesproken waar de verkoper zich aan dient te houden. Gedurende een overname bestaat er namelijk een, voor de verkoper gunstige,

[1] Dit in tegenstelling tot publieke overnames, waar verkopers doorgaans verspreide anonieme aandeelhouders zijn, en onderhandelingen plaatsvinden met het bestuur over de voorwaarden waarop zij de deal ondersteunt.

periode waarbinnen de verkoper nog wel het bestuur voert over het target, terwijl er al een overnameprijs is overeengekomen. Tijdens deze periode zou de verkoper allerlei ongewenste acties kunnen ondernemen, zoals dividend uitkeren aan zichzelf. Convenanten beschermen de koper hiertegen, door het toegestane gedrag van de verkoper te definiëren en daardoor te beperken.

De resultaten in hoofdstuk 2 onderschrijven de hypothese dat contracten worden ingezet om economische kwesties bij een overname te beperken, want we vinden dat de economische factoren van invloed zijn op contracten. Zo bevatten contracten bij deals met grote verschillen in informatie tussen de koper en verkoper ook meer garanties. Tegelijk staan er meer convenanten in contracten bij deals waar de kans op misdragingen door verkopers groter is. Samen kunnen deze economische omstandigheden ongeveer een derde verklaren van de variatie in de hoeveelheid garanties of convenanten. Dat betekent dat tweederde van die variatie door andere factoren te verklaren moet zijn, zoals bijvoorbeeld de betrokken advocaten of advocatenkantoren.

Uit mijn onderzoek blijkt dat, naast economische factoren, ook advocatenkantoren en zelfs individuele advocaten van invloed zijn op overnamecontracten. Voor de invloed van het betrokken advocatenkantoor, kijk ik naar de hoeveelheid garanties of convenanten die een kantoor in een vroeg stadium van de contractontwikkeling hanteert. In de praktijk werken advocatenkantoren vaak met modelcontracten als eerste opzet voor een contract. Tijdens de onderhandelingen wordt hier zelden radicaal van afgeweken. Als gevolg zijn veel clausules in overnamecontracten direct te herleiden tot het modelcontract van het kantoor wat de eerste opzet heeft aangeleverd. De resultaten laten zien dat er een correlatie is tussen het kantoor op wiens model het contract is gebaseerd, en de garanties en convenanten die in het uiteindelijke contract zijn opgenomen. Contracten afkomstig van sommige kantoren bevatten stelselmatig meer bepalingen ter bescherming van de koper dan van andere kantoren, onafhankelijk van of ze de koper of verkoper vertegenwoordigen. Dit geeft aan dat kantoren variërende benaderingen hebben van de formulering van hun interne modelcontracten, en dat deze doorwerken in de uiteindelijke overnamecontracten.

Eenzelfde soort correlatie tref ik aan op het niveau van individuele advocaten. De contracten opgesteld door advocaten met een bepaalde voorkeur, bijvoorbeeld voor veel garanties, wijken sterk af van contracten opgesteld door advocaten met een voorkeur voor minder garanties. Dit geldt ook voor convenanten. De aanpak of stijl van individuele advocaten kan een aanzienlijk deel van de variatie tussen contracten verklaren.

De mate waarin kantoren en advocaten invloed hebben op contractsbepalingen blijkt sterk afhankelijk te zijn van het onderwerp van die bepaling. Advocaten hebben bijvoorbeeld relatief veel invloed op garanties over intellectueel eigendom. Een mogelijke verklaring hiervoor is dat daar veel risico mee gepaard gaat, waardoor de belangen van de partijen uiteenlopen en de stijl van onderhandelen een rol gaat spelen.[2] Aan de andere kant hebben advocatenkantoren juist veel invloed op garanties die stellen dat alle regelgeving goed is nageleefd. Het is intuïtief dat contracten hierover niet sterk van modelcontracten hoeven af te wijken, want de toepasselijke regelgeving is vaak vergelijkbaar tussen deals. Ten slotte hebben noch kantoren, noch advocaten invloed op garanties over de financiële balans van het target.[3] Dit kan een indicatie zijn dat deze garanties dermate directe economische gevolgen hebben dat ze puur door economische factoren worden bepaald.

6.3 Het effect van het overnamecontract op de prijs

In hoofdstuk 3 stel ik de vraag of contractbepalingen ook effect hebben op de prijs die voor een overname is betaald. Is er een correlatie tussen de hoeveelheid bepalingen die in een contract zijn opgenomen, en de met de overname gemoeide prijs? Het onderhandelingsproces bij overnames vindt doorgaans in twee stadia plaats. Eerst wordt de prijs bepaald, en vervolgens wordt het contract onderhandeld. Dit suggereert dat de prijs en het contract volledig onafhankelijk van elkaar worden vastgesteld. Niettemin zou er een

[2] Bijvoorbeeld, bij de garanties over intellectueel eigendom kan staan dat er geen derde partij is die de patenten van de targetonderneming schendt. Aangezien de verkoper hier niet 100% zeker van kan zijn, zal zij deze garantie liever niet bieden, terwijl de koper het juist wel graag gegarandeerd zou zien.

[3] Een voorbeeld van een balansgarantie is dat de jaarrekening van de target een goede weergave biedt van de financiële staat van het bedrijf.

relatie kunnen bestaan; in het geval dat de prijs is vastgesteld in verwachting van bepaalde contractclausules bijvoorbeeld, of omgekeerd, wanneer de prijs wordt aangepast als gevolg van contractwijzigingen.

In dit deel van het onderzoek maak ik onderscheid tussen waardeverhogende en waardeverdelende bepalingen. Dit onderscheid is interessant, omdat de twee type bepalingen elk een ander effect kunnen hebben op de overnameprijs. Voor waardeverhogende bepalingen geldt namelijk dat een hogere totale waarde gepaard zou moeten gaan met een hogere prijs. Aan de andere kant kunnen waardeverdelende bepalingen binnen het contract tegen elkaar weggestreept worden, zodat de betreffende bepaling geen effect hoeft te hebben op de overnameprijs. Garanties en convenanten classificeer ik als waardeverhogend, omdat ze de economische problemen reduceren, bijvoorbeeld door de kans verhogen dat de overname doorgaat, of door te voorkomen dat er inefficiënte maatregelen worden genomen ter bescherming van de koper.[4] Als gevolg kunnen ze de totale waarde van de transactie verhogen. Als waardeverdelend kijk ik naar bepalingen die betrekking hebben op de plaatsing van risico omtrent een deal: ieder risico dat voor rekening van de koper komt, legt aan de koper kosten op, terwijl het voordeel biedt aan de verkoper. En omgekeerd geldt hetzelfde. Een bepaling over risicoallocatie verschuift dus uiteindelijk waarde van één partij naar de ander, en werkt waardeverdelend.

De resultaten in hoofdstuk 3 tonen aan dat waardeverhogende bepalingen wel degelijk effect hebben op de prijs: voor deals met meer garanties en convenanten in het contract wordt doorgaans een hogere premie betaald. Dit geeft aan dat garanties en convenanten waardevolle bepalingen zijn, en dat de koper bereid is te betalen voor een hogere mate van bescherming. De grootte van het effect op de prijs van deze bepalingen varieert met het onderwerp ervan. Zo is de prijsimpact van garanties het hoogst voor garanties over de jaarrekening van de target. Binnen de convenanten hebben de bepalingen over dividenduitkeringen de grootste impact op de prijs. Dit zijn tevens de categorieën waarvan een relatief groot deel van de variatie verklaard kan worden door economische

[4] Ter illustratie: bij gebrek aan de garantie dat de machines en apparaten goed functioneren zou de koper dit moeten verifiëren. Dat brengt kosten met zich mee, terwijl het voor de verkoper (bijna) kosteloos zou zijn om dit te garanderen. De garantie voegt dus waarde toe door inefficiënte uitgaven te terug te brengen.

factoren. Dat onderbouwt de suggestie dat contractsbepalingen die directe financiële gevolgen kunnen hebben, minder sterk worden beïnvloed door juridische adviseurs.

Anders dan waardeverhogende bepalingen, hebben waardeverdelende bepalingen geen significant effect op de betaalde premie, zo blijkt uit mijn onderzoek. Dit zou kunnen betekenen dat deze bepalingen binnen het contract tegen elkaar weggestreept worden. Een ander mogelijk scenario is dat kopers en verkopers de contractuele verdeling van waarde onderschatten; in dat geval ontstaat er ruimte voor advocaten om deze verdeling in het voordeel van hun cliënt te onderhandelen, zonder daar in de hoogte van de premie voor te hoeven compenseren.

6.4 De invloed van de expertise van advocaten bij onderhandelingen

Daarmee kom ik aan bij het laatste hoofdstuk van dit proefschrift, waar ik de invloed van de specifieke expertise analyseerde van advocaten die bij overnames betrokken zijn. Waar ik in hoofdstuk 2 aantoonde *dat* advocaten invloed hebben op contracten, bekijk ik hier *hoe* zij die invloed uitoefenen. Ik neem daarbij zowel contracten, als het onderhandelingsproces, als de hoogte van de premie in ogenschouw.

De centrale vraag van dit hoofdstuk is of een hogere mate van expertise van een advocaat ook resulteert in een groter voordeel voor de betrokken partij. Met andere woorden: als ik een advocaat in de arm neem met meer expertise dan mijn wederpartij, zijn de uitkomsten van de overname dan ook meer in mijn voordeel? Als dit het geval is, zou dat kunnen betekenen dat advocaten van beide partijen tijdens onderhandelingen met elkaar concurreren om zoveel mogelijk waarde naar hun eigen cliënt te dirigeren. Anderzijds zouden advocaten ook juist kunnen samenwerken om een contract te ontwikkelen met de grootst mogelijke toegevoegde waarde voor beide partijen - een scenario dat vanuit het gezamenlijke perspectief van koper en verkoper eigenlijk wenselijk zou zijn. De meetpunten die ik hanteer voor de mate van expertise zijn, onder andere, het aantal jaren werkervaring, de hoeveelheid deals waarbij de advocaten hebben geadviseerd, en het opleidingsniveau.

In hoofdstuk 4 toon ik aan dat de uitkomsten bij een overname meer in het voordeel zijn van de partij wiens advocaat relatief meer expertise heeft. Dit bevestigt de hypothese dat advocaten tijdens het onderhandelingsproces met elkaar concurreren. Ten eerste zien we dat meer expertise bij de advocaat van de koper resulteert in een hogere mate van risico voor rekening van de verkoper, en omgekeerd. Ten tweede is de relatieve expertise van een advocaat mede bepalend voor welke partij de eerste contractversie mag aanleveren; dit recht komt meestal de advocaat met de meeste expertise toe. Dit is voor advocaten gunstig, want dan kunnen zij al bij aanvang van het onderhandelingsproces de positie van hun cliënt versterken door contractbepalingen in de opzet op te nemen die voor hun cliënt voordelig zijn. Ten derde zien we dat de duur van de onderhandelingen significant korter is, wanneer de advocaat van de koper meer expertise heeft - en dat is in het voordeel van de koper. Verkopers kunnen namelijk baat hebben bij langere onderhandelingen: als de exclusiviteitsperiode (waarin ze niet in onderhandeling mogen treden met derden) verloopt, kunnen alternatieve kopers worden aangeschreven, waarmee de overnameprijs stijgt. Zo kan een hoger niveau van expertise van de koper dus worden geassocieerd met lagere premies.

6.5 Conclusie

Samenvattend laat dit proefschrift op drie manieren zien hoe economische omstandigheden en de inbreng van juridisch adviseurs een rol kunnen spelen in de totstandkoming van contracten die bij bedrijfsovernames worden opgesteld. Hierbij zijn twee contractuele bepalingen als uitgangspunt genomen om die rol in kaart te kunnen brengen: garanties en convenanten. Als bevindingen zien we ten eerste dat er inderdaad een relatie bestaat tussen de economische dealomstandigheden en de bepalingen die in een contract zijn opgenomen. Ten tweede hebben deze clausules ook effect op de hoogte van de betaalde premie, wat het belang van contracten bij overnames onderstreept. En ten derde hebben de juridische adviseurs die betrokken zijn bij overnames, zowel op het niveau van het vertegenwoordigde kantoor als op individueel niveau, een significante invloed op het

proces. Deze invloed is terug te zien in de inhoud van het contract, in het verloop van het onderhandelingsproces en in de hoogte van de betaalde premie. Met name deze laatste resultaten benadrukken dat de impact van de particuliere handelingswijze van advocaten of kantoren bij overnames niet moet worden onderschat. Daarom is het voor partijen die met bedrijfsovernames te maken hebben van belang met zorg juridisch advies te kiezen. Het verdient sterke aanbeveling om een advocaat te vinden die qua expertise, maar ook qua risicoperceptie en stijl aansluit bij de voorkeuren van de cliënt en bij de specifieke eigenschappen van een bedrijfsovername.

The Tinbergen Institute is the Institute for Economic Research, which was founded in 1987 by the Faculties of Economics and Econometrics of the Erasmus University Rotterdam, University of Amsterdam and VU University Amsterdam. The Institute is named after the late Professor Jan Tinbergen, Dutch Nobel Prize laureate in economics in 1969. The Tinbergen Institute is located in Amsterdam and Rotterdam. The following books recently appeared in the Tinbergen Institute Research Series:

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