Questions that board members should ask about potential transactions in light of the COVID-19 crisis

Given the uncertainties surrounding COVID-19 and the anticipated scarcity of capital, the scrutiny of board decisions related to mergers, acquisitions and divestitures will increase. What questions do directors need to ask before approving the next transaction?

1. **Transaction thesis:** As many transactions are being delayed, boards need to revisit the proposed transaction rationale.
   - Does the fundamental thesis of the contemplated transaction still hold true?
   - Will there be structural changes in the target’s industry going forward?
   - How can the board reassess the economics of the transaction to be confident it will create long-term value for stakeholders?
   - Are existing deal models robust enough to accurately quantify the impact of key assumptions on shareholder value?

2. **Transaction structure:** Effective transaction structures can mitigate risk and improve outcomes, especially at times of high uncertainty.
   - Given the current economic uncertainty, can a variable purchase consideration (e.g., earnouts and other types of contingent consideration) provide a better risk-adjusted return when compared to a fixed purchase consideration?
   - What are the implications of using noncash consideration in the transaction structure?
   - Do you have tools that would provide an accurate comparison of various deal structures?

Board directors regularly obtain a fairness opinion before approving a material transaction. A robust fairness opinion can help make sure that a board’s decision does not destroy shareholder value. The need for an independent fairness opinion is most apparent in today’s environment. If you are evaluating a potential transaction, here are the key questions you need to ask:
### Short-term outlook and long-term forecasts:
Forecasts are one of the most important inputs in assessing the attractiveness of a transaction.

- Are the projections that were developed before the COVID-19 outbreak still valid?
- Are the key assumptions underlying the financial models consistent with current epidemiological forecasts?
- Do you have visibility into various components of the forecast and potential exposure to COVID-19 driven by geographic, product and channel mix?
- Does the current downturn impact only the short-term outlook or the long-term forecast as well?
- Have scenario analyses and simulations been performed to quantify potential outcomes on shareholder value?

### Risk and discount rate:
Various measures of risk have reached their highest levels since 2008, while the government is planning unprecedented monetary easing and fiscal stimulus.

- With the liquidity crunch and debt markets dislocation, are the discount rates used in the transaction analysis still accurate?
- How should risk premium inputs for the cost of capital be adjusted to reflect increased uncertainty?
- How do the current developments impact both the buyer's and the target's credit capacity? What are the implications for long-term capital structure and the overall cost of capital?

### Market multiples:
Valuation multiples of publicly traded peers are often used as a benchmarking tool to assess the transaction economics.

- How does current volatility in the equities market impact valuation multiples of the deal?
- In the absence of public information on forward-looking metrics of publicly traded peers, how should we think about market multiples?

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As many industries are being disrupted by COVID-19, board members need to ask a new set of questions before approving the next merger, acquisition or divestiture.