Ghosts of Transactions Past
Strategies for Resolving Post-Closing Disputes

2025 Fall Forensics Institute

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Forvis Mazars

Overview

With a legacy spanning more than 100 years, Forvis Mazars is committed to providing a different perspective and an unmatched client experience that feels right, personal and natural. We respect and reflect the range of perspectives, knowledge and local understanding of our people and clients. We take the time to listen to deliver consistent audit and assurance, tax, advisory and consulting services worldwide.

We nurture a deep understanding of our clients' industries, delivering greater insight, deeper specialization and tailored solutions through people who listen to understand, are responsive and consult with purpose to deliver value.

Global Industry & Services

Forvis Mazars' deep understanding of industry-specific environments, issues and trends helps us anticipate and address evolving needs to prepare you for strategic opportunities ahead.

Every industry is different, and we put a strong focus on specific industry experience and knowledge of your complex and evolving environment. We provide a range of audit and assurance, tax, advisory and consulting services to help your business by bringing together experienced professionals from all over the globe who understand local contexts and cultures.

We serve global industries including:

- Financial Services
- Manufacturing & Distribution
- Technology, Media & Telecommunications
- Life Sciences
- Private Equity

$5B
Combined Revenue (2023)

100+
Combinded Countries, Territories & Markets

400+
Combined Offices & Locations

1,800+
Combined Partners

40,000+
Combined Team Members

Forensics & Valuation Services Overview

Our Commitment to Excellence In Valuation

Forvis Mazars has extensive experience with the increasingly complex issues associated with delivering reliable valuations and the ever-expanding application of these services.

Our forensics & valuation services practice at Forvis Mazars is a multidisciplinary team of professionals including forensic accountants, forensic technologists, and business valuation professionals. We serve clients across the country ranging from owner managed businesses to Fortune 100 corporations as well as nonprofits and federal, state, and local governmental agencies.

What We Do

Our valuators adhere to applicable valuation standards while striving to provide superior client service. We are committed to providing high-quality deliverables for all projects. Our approach tailors services to meet our clients' specific needs and focuses on identifying services to any problems that arise from a valuation.

Our Services

- Financial Reporting
- Tax Planning & Reporting
- Transactions & Planning
- Financial Modeling
- Dispute Consulting & Expert Testimony

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Meet the Presenters

Brian Burns, CPA/ABV/CFF, ASA, MAFF

Partner, Forvis Mazars

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Brian is a partner and member of the Forensics & Valuation service line. He practices in valuation and forensic accounting, including financial investigations, litigation support, and consulting services. He has been designated as an expert witness or retained as a neutral advisor and qualified to testify by report, deposition, and/or trial testimony in federal and state courts or arbitrations across the United States in commercial and divorce matters. The focus areas of his forensic accounting services include litigation support and consulting services in matters such as shareholder disputes, divorces, breach of contract, breach of warranties, misappropriation of trade secrets, post-acquisition disputes, tortious interference, intellectual property disputes, statutory conspiracy, business interruption claims, employee embezzlement, investment scams, and fraud. With respect to his practice in valuation, Brian assists businesses and individuals with valuation services in litigation and shareholder disputes, divorce, transaction consulting, tax planning and compliance, financial reporting, stock-based compensation, and employee stock ownership plans.

He is often retained as an expert in matters involving disputed valuations and diminution of value claims. He assists clients with financial matters that may arise before, during, or following the closing of transactions. Brian has experience consulting in areas relating to working capital adjustments, earn-out calculations, and financial claims related to alleged breaches of purchase agreements or other actions. While his experience spans a broad scope of industries, Brian has strong experience in the construction, real estate, and government contracting industries providing dispute consulting in these industries involving matters such as post-acquisition disputes, business interruption claims, fraud, delays, and other disputes involving economic damages such as lost profits, lost value, and increased cost related claims.

Brian currently co-chairs the National Forensic and Valuation Services Conference Committee of the AICPA. He previously served on the Accredited in Business Valuation Credential Committee and the Business Valuation Committee of the AICPA and as president of the Richmond chapter of the American Society of Appraisers. Brian's certifications include Accredited in Business Valuation (ABV), Certified in Financial Forensics (CFF), Accredited Senior Appraiser (ASA) in business valuation, and Master Analyst in Financial Forensics (MAFF).

He is a *magna cum laude* graduate of Virginia Polytechnic Institute and State University, Blacksburg, with a B.S. degree in finance, and a graduate of Virginia Commonwealth University, Richmond, with a post-baccalaureate certificate in accounting.

Meet the Presenters

Jesse L. Noa, Esquire

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Jesse is a partner in Potter Anderson & Corroon LLP's General Litigation Group. Jesse represents businesses and individuals in a wide variety of complex commercial, bankruptcy, employment, and real estate litigation matters in the state and federal courts of Delaware. These matters include contract and sale transaction disputes, expedited restrictive covenant and trade secret litigation, alternative entity disputes, business torts, and commercial foreclosure actions. Jesse's practice also includes providing counseling to clients regarding business and regulatory compliance matters, as well as cybersecurity and information governance issues.

Jesse is ranked in Chambers USA, Super Lawyers, and Best Lawyers. Jesse has also served on and counseled for-profit and non-profit boards.

Jesse obtained his law degree from Villanova University School of Law, J.D., *cum laude* where he was the Managing Editor of Technology, Jeffrey S. Moorad Sports Law Journal, and was named a Daniel F. O'Dea Fellow. While in law school, Jesse served as a judicial intern for the Honorable Michael M. Baylson of the U.S. District Court for the Eastern District of Pennsylvania. Jesse graduated *summa cum laude* from Rowan University.

Jesse served on active duty in the United States Marine Corps and was honorably discharged in 2005. He received a commendation from the New Jersey Senate and General Assembly for his service in 2009.

Meet the Presenters

Tyler E. Cragg, Esquire

Associate, Potter Anderson & Corroon LLP

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Tyler is an associate in Potter Anderson & Corroon LLP's General Litigation Group. Tyler litigates a broad spectrum of disputes in all of Delaware's federal and state courts, leveraging his background in the sciences to his clients' advantage. His practice focuses on commercial litigation—involving breach of contract, fraud, noncompete, and trade secret claims in the Delaware Superior Court's Complex Commercial Litigation Division and Court of Chancery—as well as intellectual property litigation—involving semiconductor and pharmaceutical patents—in the U.S. District Court for the District of Delaware.

Tyler is a Super Lawyers, Rising Star.

Tyler previously worked at a Washington, D.C., think tank where he contributed to technology policy related to the gig economy and the internet of things, sparking his interest in the legal impact of emerging technologies. Prior to law school, Tyler researched novel thin film sensors for the petrochemical industry involving solid-state vaporchromic platinum compounds.

Tyler obtained his law degree from Washington & Lee University School of Law, where he was awarded the Roy L. Steinheimer Jr. Commercial Law Award. While in law school, Jesse served as a judicial intern for the Honorable John A. Parkins of the Superior Court for the State of Delaware. Tyler graduated from Carleton College with a bachelors of arts in Chemistry.

Post-Close Services

Common Disputed Provisions

- Post-closing purchase price adjustments
  - Working capital
  - Taxes
- Earnouts (if applicable)
  - Contingent future payments increasing purchase price subject to certain conditions
- Representations and warranties of parties
  - Financial statements and tax returns
  - Customers and contracts
  - Workforce
- Indemnification provisions

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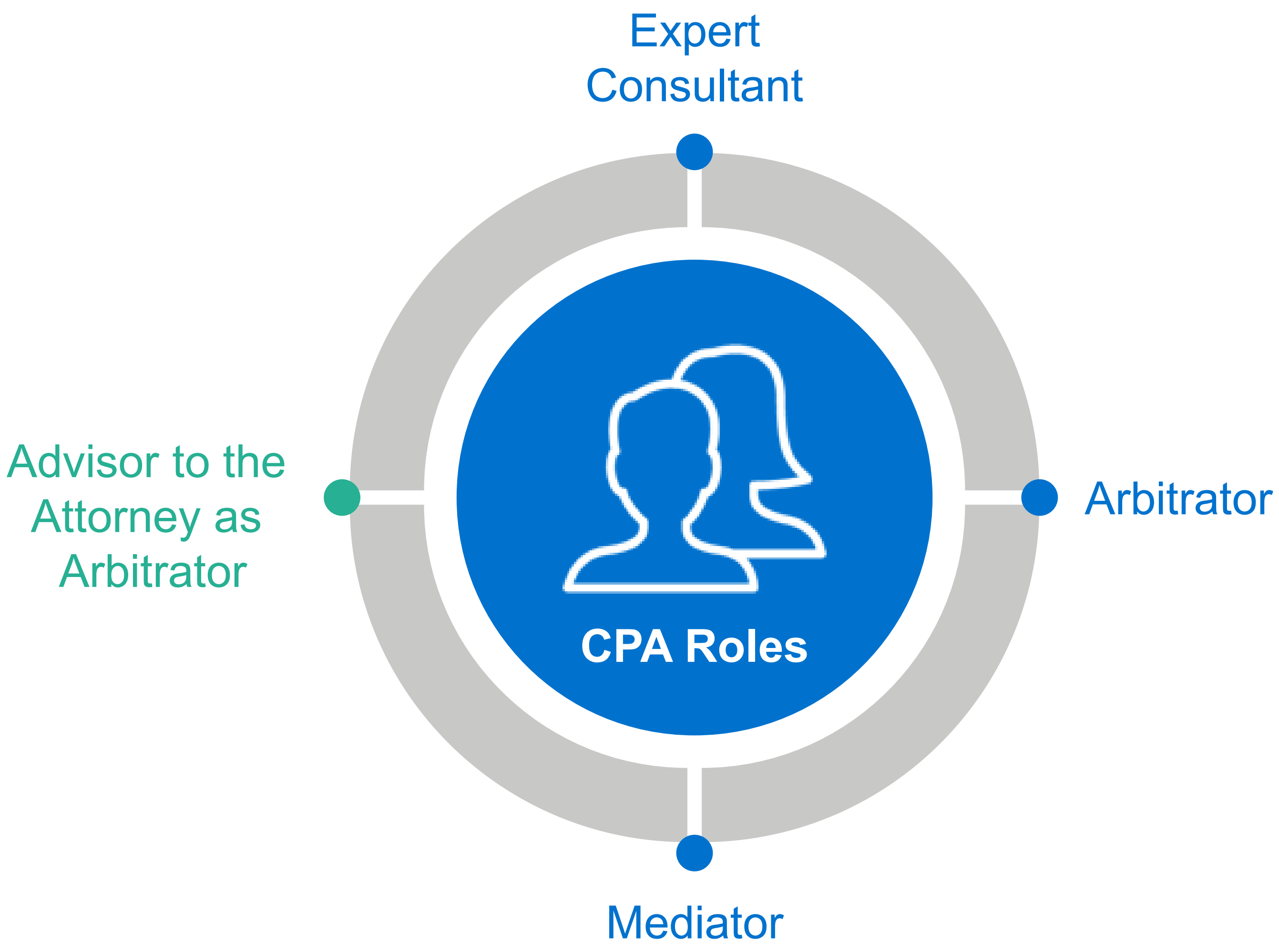
Roles of CPA and Advisors



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Working Capital

Working Capital

- "… in accordance with GAAP as consistently applied …"
  - What if past practice is not GAAP?

- Common accounts with disputes
  - Accounts receivable
  - Work in Progress
  - Inventory
  - Contingent Liabilities (FAS 5)
  - Reserves and other accounts that require judgment and estimates

Case Study – Working Capital

	Large Projects	Small Projects
Commercial Customers	?	Completed Contract
Government Customers	Percentage of Completion	N/A

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02

Earnouts

Earnouts

Contingent element of acquisition's purchase price determined post-closing based on target business's performance against contractually defined criteria

Appeals to Sellers

- Helps to realize more value of business
- Allows for greater consideration
- Advantageous in difficult economic settings
- When Seller management will still be involved post-close, allows Seller to control results

Appeals to Buyers

- Protection from overpayment
- Reduces cash necessary at closing
- Cause Buyer's bid to stand out among other potential Buyers
- Indicates Seller confidence
- Motivates Seller management should they remain involved post-close

Why are earnouts not used?

- Buyer concerns
  - Restrict integration of target
  - Indicates uncertainty
  - Compensating Seller for Buyer advancements
- Seller concerns
  - Lack of control
  - Lack of records
  - Concern value will not be realized
- Shared concerns
  - Manipulation of buyout
  - Ability to "move on" post-closing

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Areas of Dispute Regarding Operation of Target

When business is operated by *Buyer* post-closing:

- Perceived management of business to minimalize performance measures and in turn the earnout
- Alleged deviation from consistent historical operating norms
- Alleged failure to invest in the business/provide for adequate capital
- Alleged failure to pursue opportunities
- Alleged impairment of earnout due to discontinuation of business
- Alleged shifting of sales or customer relationships from target to other Buyer entities

When business is operated by *Seller* management post closing:

- Perceived management of business is to maximize performance measures and turn in the earnout

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Areas of Dispute Regarding Operation of Target

What should/should not be included when measuring target's performance against earnout benchmarks?

- Costs of transaction
- Post-closing capital investments
- Goodwill amortization
- Intercompany overhead allocations
- Depreciation
- Discontinued operations
- Extraordinary items

Litigation Example

Dispute Concerning Achievement of Earnout Targets

- Seller sold their bio-tech research company to a private-equity buyer and agreed to an earnout with payments based upon financial milestones.
  - Milestones were based in part on promise of increased resources from Buyer.
- Buyer assumed management of the Company and agreed to use “commercially reasonable” efforts to meet milestones.
- Company failed to meet earnout milestones and no payments were made to Seller.
- Seller sued, alleging that Buyer failed to use commercially reasonable efforts during earnout period.
  - Seller alleged Buyer delayed promised additional resources.
  - Seller alleged Buyer changed Company’s revenue and expense recognition on financials.
- Buyer counterclaimed alleging Seller engaged in fraud.
- **Issues for experts**:
  - Whether Buyer’s management decisions were commercially reasonable.
  - Whether Seller’s financial disclosures pre-sale were accurate.

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Earnout Examples

Example 1:

- “In accordance with GAAP” and Adjustments
- Liabilities/Expenses triggered by Buyer’s Management
- Measurement Period
- Formula Multipliers
- Contemporaneous Knowledge/Communications

Example 2:

- Out of Pocket Costs – $0 or $9 million

Example 3:

- Milestone Earnout Entitlement
  - Execution of a customer contract vs. inability to execute on customer contract due to misrepresentations concerning software capability

03

Representations and Warranties

Representations and Warranties

Buyers will require assurances from the Seller in order to gain confidence in valuing the target

- Financial statements provided during due diligence are presented fairly and in accordance with GAAP
- Material information has been disclosed
- No undisclosed Material Adverse Changes have occurred
  - Any event, development, circumstance, change, or effect that is or would reasonably be expected to be materially adverse to the business, financial condition, or results of the operations of the Acquired Company.
- Operation of business in ordinary course

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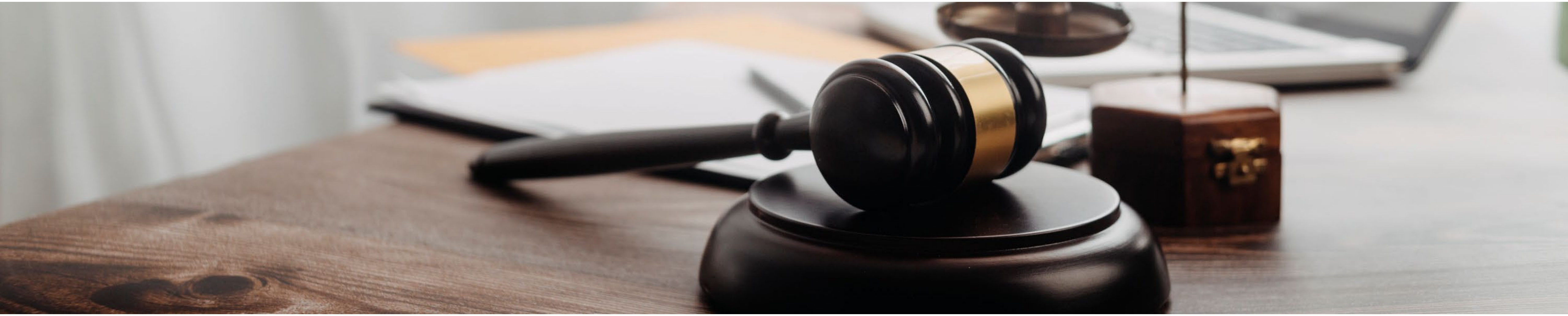
Economic Damages in Post-Acquisition Disputes

Return Plaintiff to Same Economic Position

- Put plaintiff in position it would have been but for the defendant’s breach/wrongful conduct

Post-Acquisition Dispute Damages:

1. Dollar for Dollar Damages = one-time, non-recurring impact on business
2. Benefit of the Bargain Damages = permanent diminution in value, or over payment



Damage Methodology Overview

Type of Damages: Benefit of the Bargain Damages

Difference Between:

- Value of what Buyer expected to receive
  - *In reliance upon Defendant's misrepresentations*
- Value of what Buyer actually received

Benefit of Bargain Damages:

- Adjustments to Earnings Stream
- Adjustments to the Multiple

Earnings Stream (Revenue, EBITDA, etc.) **X Multiple** (Rate of Return - Growth) = **Value**

Value

- Profitability
- Growth Profile
- Risk Profile

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Litigation Example 1

Dispute Concerning Scope of Indemnification

- Seller sold a brokerage and financial advisory firm to a competitor.
- As part of the sale, a portion of purchase price was placed into escrow to cover indemnification claims arising from pre-closing litigation.
- Prior to escrow release date, Buyer made multiple claims for indemnification concerning dozens of lawsuits filed by Company's investor clients against individuals' brokers with indemnification rights.
- Buyer sought indemnification from Seller and refused to release escrow.
- Seller sued for release of escrow claiming that indemnification claims either: 1) did not relate to pre-closing issue; 2) the Company was not required to indemnify individual brokers for certain claims; or 3) Buyer had overvalued its indemnifiable losses.
- **Issues for experts**:
- Proper calculation of the indemnifiable losses.
  - Are there other sources of recoupment for loss, such as insurance, that reduce indemnification?
  - Did indemnification claims result in a tax benefit that would reduce the indemnifiable loss?

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Litigation Example 2

Court Rejects Both Sides Damages Theories Relating to Fraud

- Buyer purchased software company for which Seller represented it had a market-ready product.
- After closing, Buyer discovered the software required significant development to be marketable and sued Seller for breach of representations and warranties and fraud.
- As damages for fraud, Buyer sought benefit of bargain damages and expert opined that the value of the Company was zero.
- Seller countered that there was no fraud and that benefit of bargain damages were zero.
- After bench trial, Court found liability for fraud but concluded that the value of Company was more than zero. The Court further concluded that neither party had presented expert testimony of damages as both theories were rejected.
- Ordered supplemental reports on issue of benefit of bargain damages.
- **Issues for experts**:
- In fraud cases arising from the sale of a business, consider whether the Court is being presented with an all or nothing damages dispute.
- Is there an alternative damages theory that should be presented to the Court?

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Litigation Example 3

Misrepresented Information

1. Related Party, off the books compensation – Related entity paid compensation of Seller contractors and employees
2. Overtime – unpaid and unreported overtime compensation
3. Employees and Contractors – unpaid and unreported payroll taxes on payments to contractors misrepresented as employees
4. Workforce – misrepresented job titles, including un-qualified project manager

Undisclosed Risks

1. Allowing workers to drive company vehicles without driver's license
2. Unlawful characterization of independent contractors serving as employees
3. Contracting/employing workers unauthorized to work in the United States
4. Unqualified workers being assigned industry titles that don't correspond with qualifications
5. Unreported cash payments to employees, unreported payroll tax

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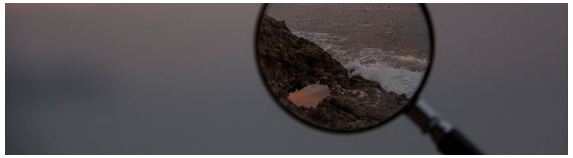
Litigation Example 3

Steps to Quantify Damages



Forensic Investigation of the Misrepresentations

- Analyzed the historical financial performance
- Quantified the financial impact of the Undisclosed Costs on the tax returns and financial statements

Analyze the Transaction and Valuation Modeling

- Gain an understanding of the transaction, negotiations, and documents
- Gain an understanding of valuation methodology, inputs, and assumptions
- Use implied transaction multiple or replicate the valuation financial model and methodology

Quantify the Reduced Value of Seller

- Incorporating the impact of:
- Financial data
- Risks on the multiple/capitalization rate

Plaintiff’s overpayment calculated as difference between:

- Purchase price
- Adjusted value incorporating the information that the Defendants misrepresented and/or omitted

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Litigation Example 4
Misrepresented and Concealed Information

Alleged Material Omissions and/or False Representations

- Government contract
- Updating of waterfall forecasts
- Status of contractual option year negotiations
- Internal email communications with the seller
- Email communications between seller and government

Annual Loss
$5.7 - $6.4 million

Every year in Perpetuity

Increasing at long term growth rate

Damages
$37.58 - $42.74 million

Discount Rate (rate of return)

Present Value

Earnings Stream (Revenue, EBITDA, etc.) **X Multiple** (Rate of Return - Growth) = **Value**

Litigation Example 4

Rebuttal to Perpetual Damage Premise

Alleged Omission – One-Time, Non-Recurring Damage

- Heavily diligenced transaction – Awareness of risks
- Contract characteristics
  - Finite
  - Subject to recompete
  - Small business set aside – would have to be reclassed to full and open
- Flawed corroborating analysis
- Contrary to post-closing audit financial statements – No Goodwill Impairment
- Failure to mitigate

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