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Buyers should be wary of 'copyleft' software

Certain licenses impact target company's valuation

By TERRENCE H. LINK and LINDSIE EVERETT

Companies are increasingly using open source software in their businesses, and for some companies, this type of software is critical to their business models. Buyers should be mindful of the unique challenges this software poses in M&A transactions, particularly in terms of a target company's valuation. A buyer acquiring a technology company with valuable, revenue-driving proprietary software may spend millions only to purchase software tainted by open source software, rendering it worthless.

Open source software is software with public source code developed through a collaborative process, which is licensed with different sets of requirements. Software developers rely on open source software because it is easy to use, yields better quality code, and is cost-efficient and rapid. Nevertheless, using open source software poses significant risks depending on the licensing scheme.

Link

Everett

Open source software generally falls under two groups of licenses.

Under a "permissive" license, companies with proprietary software incorporating open source software retain proprietary rights in the software by restricting access to the proprietary code. This preserves the software's economic value.

Conversely, when companies develop proprietary software using open source software obtained under a strong "copyleft" license, the open source software is deemed to have "tainted" the proprietary software. This requires disclosure of the software's source code to the public.

Consequently, the ability of the company's competitors, potential clients, and other third parties to have unlimited, free access to the proprietary software destroys the software's economic value.

Buyers can avoid over-valuing a target company by conducting thorough due diligence of the target company's software and use of open source software. Periodically, an audit scan of the software source code may be appropriate. Buyers should also negotiate protective representations, warranties, and indemnification provisions in the purchase agreement to address open source software risks.

While using open source software is beneficial, buyers should identify risks throughout the due diligence process and consider those risks when negotiating purchase agreements. These steps help buyers appropriately value target companies' software and minimize risks of "copyleft" surprises following the closing.

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Northeast Ohio's leading deal makers to be honored

ACG Cleveland, Northeast Ohio's leading organization for merger and acquisition and corporate growth professionals, will recognize the winners of its 21st Annual Deal Maker Awards at 5:30 p.m. Thursday, Jan. 19, at the Huntington Convention Center of Cleveland.

The Deal Maker Awards are a tribute to Northeast Ohio's preeminent corporate deal makers for their accomplishments in using acquisitions, divestitures, financings and other transactions to fuel sustainable growth. The 2017 winners are:

DIEBOLD-NIXDORF

During the past year, Diebold divested a non-core business and made an acquisition that effectively doubled the size of the company. In February, it divested its electronic security business to Securitas AB for approximately $350 million. Then, in August, Diebold completed a $1.8 billion acquisition of Wincor-Nixdorf, a $2.5 billion, publicly traded German business, to create the world's largest financial self-services and ATM company. This transaction transformed the company into a global entity heavily focused on services and software, with annual sales in excess of $5 billion. In addition, Diebold formed two joint ventures in China.

HUNTINGTON BANCSHARES

In August, Huntington Bancshares merged with FirstMerit in a transaction valued at $3.4 billion. The merger established the largest bank in Ohio by deposit market share, with combined assets of nearly $100 billion. It was overwhelmingly approved by shareholders of each bank. FirstMerit shareholders received 1.72 shares of Huntington common stock, plus a fixed $5 per share for each share of FirstMerit stock outstanding. This represented a 32% premium over FirstMerit's share price at the time of the announcement. The combined company will operate approximately 1,000 branches in eight Midwest states, including Ohio, Michigan, Pennsylvania, Indiana, West Virginia, Kentucky, Wisconsin and Illinois.

TRADEMARK GLOBAL LLC

Based in Lorain, Trademark Global is a multimillion-dollar e-commerce and drop-shipping business. Among its clients are household names such as Amazon, Walmart and Overstock. In order to accelerate growth, Trademark Global partnered with Blue Point Capital Partners in 2013. It proceeded to establish a sourcing center in China that increased its speed to market and improved quality control. It also upgraded its IT platform and recreated its inventory management and product development processes, which provided Trademark with increased operational leverage. The company was sold to Bertram Capital in November. During its partnership with Blue Point, Trademark Global demonstrated exceptional top line and margin growth, and nearly doubled its EBITDA.

CAPITALWORKS LLC

CapitalWorks is a Midwestern, family focused private equity firm that acquires lower middle-market companies and gives them the capital, support and freedom to grow. Over the past two years, the firm has been extremely active despite middle-market M&A being very competitive. Since December 2013, CapitalWorks has completed five platform acquisitions, four portfolio add-ons, three portfolio dividend recapitalizations and exited two portfolios.

Sponsors supporting the 2017 Deal Maker Awards include Benesch, Huntington, Grant Thornton, KeyBanc Capital Markets and Oswald Cos.

2017 ACG Events Calendar

For more information and to register, visit www.ACGclevland.org

DATE	EVENT	TIME	LOCATION
Jan. 19	21st Annual Deal Maker Awards	5:30 p.m.	Cleveland Convention Center
Jan. 26	Young ACG Lunch & Learn	Noon	Vorys
Feb. 2	Regional Networking — East — Minority Business Owners	5:30 p.m.	Shaker Country Club
Feb. 9	Regional Networking — Central — Dale Wollschleger, ExactCare	5:30 p.m.	Lockkeepers
Feb. 16	Regional Networking — West — Mike Ripich, AT&F	5:30 p.m.	Lakewood Country Club
Feb. 21	George Veras, CFO, Football Hall of Fame (joint event with FEI)	5:30 p.m.	Union Club
Mar. 9	Anil Makhija, Board Member, National Center for the Middle Market	11:30 a.m.	Union Club
Mar. 23	Young ACG Networking and BVU Presentation	4:00 p.m.	Tucker Ellis
Apr. 27	Dick Pace, President, Cumberland Development, Waterfront Project	4:30 p.m.	Nuevo Modern Mexican
May 10	Women in Transactions, Strategic Charisma, Part 1	7:30 a.m.	Jones Day
May 11	David Given, Frank Linsalata, Stewart Kohl — Wizards & Legends of Private Equity	4:00 p.m.	Ritz-Carlton
May 24	Women in Transactions, Strategic Charisma, Part 2	7:30 a.m.	Plante Moran
Jun. 13	Spring Social	5:30 p.m.	Shoreby Club
Sept. TBD	13th Annual Golf Outing	TBD	Firestone Country Club

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