Three key points for maximizing the value of acquihires

While the term "acquihire" has yet to find formal recognition in the *Oxford English Dictionary*, it is well recognized in the corporate and venture capital lexicon. Simply stated, an acquihire is the acquisition of another company with the goal of acquiring specific employees or groups of employees.

The inherent value of an acquihire transaction is not centered around the technology or services provided by the company being acquired; rather, it is the synergy of the team of employees and their collective innovation potential, market share or goodwill. The ability to acquire the integrated talent of an entire team is the lightning-in-a-bottle element of an acquihire.

But an acquihire can fail. Buyers may find that, for an array of reasons, an acquired team may not produce the expected results – most notably, when team members choose to move on to a new venture.

Most of the potential problems that may arise following an acquihire can be avoided or minimized through a properly and strategically structured transaction, including giving appropriate care and attention to the drafting of the various employment agreements and compensation structures for the acquired team.

Here are three key points.

- **Retention payments**. Buyers need to think strategically about the way they structure the employment-based compensation scheme as well as the payment schedule for the purchase of the target company. With the appropriate structure, compensation arrangements can motivate newly acquired teams to stay and achieve intended results. For example, consider retention payments based on the achievement of specific milestones and on how long the acquired team, or its individual members, remains employed with the buyer. Also, the buyer can be creative in structuring the payment schedule for the purchase price of the target company through the use of earnouts and other deferred payments. Including time-based incentive compensation arrangements can help to more fully integrate the acquired team as a fully functioning part of the buyer's business.

- **Restrictive covenants**: A properly structured acquihire arrangement will allow a buyer to obtain restrictive covenants against founders and other key employees of the acquired team who own a material portion of the business. In fact, in states like California, an employer would otherwise be prohibited from obtaining a non-compete against a new hire. This limited exception to the broad ban on non-competes in California does not extend to those acquired employees who own only a small percentage of the business or none at all. Even in states that permit non-competes in the traditional employment context, those types of restrictions are strictly scrutinized by the courts. Non-competes entered into in connection with the sale of a business are routinely subjected to less scrutiny. It is worth noting that, in an acquihire, buyers sometimes wind down the acquired business because the impetus for the acquisition is the value in the acquired team. Before proceeding with a wind down, however, consider the potential impact on the enforceability of the restrictive covenants. For more on non-competes and non-solicits, see our article.

- **Individualization**. Avoid cookie-cutter employment agreements. As the primary driver of the transaction's value, employment agreements and compensation packages should be individually negotiated and sufficiently tailored to ensure that acquired employees do not feel like they are merely the buyer's amalgamated new hires An individualized employment agreement allows the acquired team members to feel that the transaction acknowledges the unique value that the team, and each of its members, brings to the buyer's business. In addition, more often than not, the synergy of the acquired team is due in part to the innovative and dynamic startup culture of the company itself, including many employee policies characteristic of that environment, such as schedule flexibility, working remotely and paid time off. Rather than merely grafting the acquired team wholly into the buyer's existing structure on day one, consider appropriate exceptions to policies or processes; also consider staggering in changes that impact compensation or fringe benefits.

Failing to understand the unique nature of your acquisition's human capital could diminish its value to your business and call the wisdom of the entire transaction into question. Instead, by paying attention to just a few key issues in an acquihire, a buyer can optimize the prospects and results for its business.
