Whether to Use a Fairness Opinion

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A fairness opinion is a formal review, typically prepared by a third-party entity (an investment banker or business appraiser) of a M&A deal's price, terms and other financial characteristics. It assesses whether a transaction is fair to shareholders and others involved by comparing the deal with similar ones and evaluating any meaningful differences.

Fairness opinions generally analyze the underlying assumptions of the deal, as well as industry and economic trends. They also determine a range of prices that might be considered fair, impartial and just for all parties.

Impartial View

Fairness opinions are often used when an M&A transaction isn't conducted at arm's length - by two independent parties - or at market price, such as an insider-led financing or a management buyout. Other transactions for which a fairness opinion may be useful include:

- Corporate divestitures.
- Leveraged buyouts.
- Recapitalizations and restructurings.
- Employee Stock Ownership Plans (ESOPs).
- Exchange offers or minority buyouts.
- Stock purchase and repurchased agreements.
- Court-appointed valuations in the event of a hostile takeover.
- Liquidations.
- Bankruptcy reorganizations.
- Dissenting shareholder disputes.

Sellers typically request a fairness opinion when an acquirer first expresses interest. This allows time for other prospective buyers to make competing offers if the original bid is at or below the low end of the fairness opinion's price range.

Not a Foolproof Tool

Both buyers and sellers use fairness opinions to shield themselves from potential lawsuits by shareholders who might claim they were shortchanged by the transaction. But these opinions don't guarantee litigation protection, nor do they necessarily reflect the full value of a proposed deal.

Fairness opinions, for example, don't address a deal's viability from strategic, operational, management, timing or legal standpoints. They also don't offer judgments on the financial projections the buyer relies on for its bid price. Additionally, fairness opinions help sellers evaluate whether an offer is adequate but don't tell buyers whether they should make the acquisition.

Potential Conflicts

To get the most out of a fairness opinion, watch for conflicts of interest. Ensure that the professional who prepares the opinion is impartial and objective.

Conflicts of interest are typically signaled by financial incentives. For example, buyers shouldn't seek a fairness opinion from an investment banker who will receive a percentage of the transaction if it's approved. It's inadvisable for sellers to engage a financial advisor who runs a private equity fund that could potentially bid on the company.

Ultimately, to allow the expert to assess the deal and ensure that there are no conflicts of interest at play, both parties should agree to an impartial professional early in the process.

Some Assurance

A fairness opinion isn't a substitute for thorough due diligence, and it won't guarantee that a deal is a smart business move or will survive legal challenges by shareholders. But an impartial opinion can provide you with some assurance that stakeholders are being treated openly and fairly.

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