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Should an Accounting Firm or Auditor Really Decide Our Acquisition Disputes?

Post-acquisition disputes often involve accounting issues to be resolved by an accounting firm or auditor. Clients need to analyze those issues carefully, particularly as legal issues often overlap with the accounting issues. In Delaware—often the choice of law—a strict difference exists when an accounting firm operates as an "expert" versus as an "arbitrator." Understanding this distinction can create opportunities and potential leverage.

In mergers and acquisitions, post-closing disputes routinely address a variety of issues ranging from net working capital and purchase price adjustments to specific valuations (*i.e.*, contracts or inventory) and the release of funds from escrow. Many of the issues focus on accounting or accounting procedures. Indeed, commercial transactions generally often have accounting-specific provisions, such as a mechanism for the verification of certain transactions or accounts. Because of the technical accounting expertise required to address these issues, parties often incorporate a provision in their agreements delegating certain decision-making authority to an accounting firm (also referred to as settlement auditor, independent auditor, or similar references).

But, accounting issues are rarely able to be decided in a vacuum, particularly in the context of commercial transactions. What do the words of the contract mean? What did the parties intend based on the language they used? What was meant by "GAAP, consistently applied"? And, how much leeway did the parties provide to the accounting firm? Questions about contract interpretation and intent are generally issues of law.

Is the accounting firm to be used as an "expert," or an "arbitrator"? Is the accounting firm's decision binding and non-appealable, or is it merely advisory? While many of these issues can be addressed with specificity in the commercial document, a party may still be able to take advantage of the distinction between "expert" and "arbitrator" to find an opportunity.

In Delaware—the law chosen to govern many commercial transactions—the law maintains a strict distinction between an arbitrator and an expert. A somewhat recent 2017 decision from the Delaware Supreme Court (***Chicago***

Bridge & Iron Co. N.V. v. Westinghouse Elec. Co. LLC) emphasizes this point. There, the parties had a working capital dispute, which the seller pursued in court. The buyer asked the trial court to enter judgment for it, finding that the accounting firm was the mandatory and exclusive method to resolve the dispute. The Court of Chancery agreed with the buyer and dismissed the seller's claim.

On appeal, however, the Supreme Court disagreed. The Supreme Court highlighted the importance of understanding the limited role of the accounting firm acting as an "expert." The accounting firm's authority was not a mandate to decide any issue on the post-closing dispute but was confined instead to a discrete set of narrow accounting issues. While noting that the buyer was free to pursue arguments with the accounting firm in the limited scope of its authority, the Supreme Court explained that the trial court should otherwise enjoin the buyer from pursing other claims with the accounting firm.

In a recent 2019 decision (*Ray Beyond Corp. v. Trimaran Fund Mgmt. LLC*), Ray Beyond filed a complaint asking the Court of Chancery to order Trimaran Fund to submit certain purchase agreement disputes to the accounting firm designated in the merger agreement. There, the merger agreement set the role of the accounting firm as "expert, not an arbitrator." The court explained that, when parties call for "expert" determinations, the accounting firm is not expected to, nor authorized, to make final and binding rulings on issues of law. The court rejected Ray Beyond's effort to put the dispute before the accounting firm.

Since disputes about contract interpretation and contractual intent are issues of law, where the parties designate an accounting firm to act as an "expert, not an arbitrator," the accounting firm is not authorized to resolve those issues. Such issues need to be resolved in court, with the opportunity to pursue discovery and present evidence on the meaning of the contract and the parties' intent.

Companies involved in M&A transactions should evaluate the issues carefully when confronted with post-acquisition disputes. Because of the overlap between accounting and legal issues inherent in such disputes, opportunities may exist to gain leverage in such potential post-closing disputes—whether that is to compel the expert process or to delay it while gaining a potential tactical advantage in court to help guide the expert analysis.

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