



Morgan Lewis

**M&A ACADEMY
PUBLIC COMPANY M&A
- PART I
AN OVERVIEW**

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Introductory Notes

- This presentation is an overview of common acquisition structures and issues relevant to the acquisition of a United States public company. Public company acquisitions are complex and may involve a broad range of tax, legal, regulatory, political, accounting, antitrust, non-U.S. law and other issues, based on the specific facts and circumstances of the transaction.
- While these materials are intended to identify major issues and considerations that arise in many transactions, they are not exhaustive and should not be relied upon as a comprehensive guide to U.S. public company mergers and acquisitions. In particular, state law or regulatory requirements, and the terms of the Charter, Bylaws, and contracts of the Target and Acquirer, will impact many aspects of the transaction and may vary widely.

Introductory Notes (cont.)

- For purposes of these materials, we have assumed that the Target and Acquirer are both Delaware corporations and that no unusual Charter or Bylaw provisions vary the default terms provided in the Delaware General Corporation Law (DGCL). We have assumed Acquirer is a strategic corporation (i.e. not private equity sponsored).
- This presentation also does not address specific tax issues or considerations in mergers and acquisitions or other contexts, or alternative transaction structures or commercial arrangements, including Joint Ventures, Spin-Offs, Carve-Outs, Tracking Stocks, and Licensing Arrangements.

Today's Presentation

- General Overview of Transaction Structures
- Scenario 1 – Strategic Acquisition
- Engaging the Target
- Scenario 2 – Activist Approach
- Material Merger Agreement Terms
- Fiduciary Duties/Standard of Review
- Litigation Risk
- Appraisal Rights
- Questions

Transaction Structures

Two Acquisition Structures:

- Merger (One Step)
- Tender Offer (Two Steps)
 - Negotiated
 - Hostile
 - Followed by Second-Step “Freeze Out” Merger
- Consideration
 - All Cash or All Stock
 - Fixed Combination of Cash and Stock
 - Cash and Stock Election
 - Contingent Value or Contingent Payment Rights

One-Step Merger vs. Tender Offer

- One-Step Merger Pros and Cons
 - When Closed, Buyer Owns 100% of the Target
 - Stockholders Entitled Only to Merger Consideration or Appraisal Rights
 - Can Take Longer Than Tender Offer with “Back-End” Merger
- Tender Offer Pros and Cons
 - Does Not Require Target Board Approval (Absent a Poison Pill)
 - May Close More Quickly Than a One-Step Merger
 - Back-End Merger Can Be Facilitated
 - “Top Up” Option
 - 251(h) “Medium Form” Merger in Delaware

Merger vs. Tender Offer (cont.)

- Higher Tender Levels May Be Effective in Pushing Board to Negotiated Transaction
- If Hostile Tender Offer, May Be Expensive, Time Consuming, and Less Certain of Success
 - Target may mount effective defense and persuade stockholders to reject the Tender Offer; or
 - Target may find a White Knight

Scenario 1 – Strategic Acquisition

Buyerco has conducted a strategic review and determined that its best strategy for growth and profitability is to acquire a complementary business. Buyerco's goal is to realize cost savings, gain access to desirable customers, and to grow EBITDA quickly by acquiring a profitable business.

Buyerco has identified a likely target, Synergicorp, which operates in the same or complementary lines of business as Buyerco. However, Synergicorp operates one line of business that Buyerco had exited because it was not profitable, so this is not a perfect fit.

Nonetheless, Buyerco believes that the potential acquisition is compelling and is willing to buy the entire Synergicorp business, even if it may require divesting the undesired line of business after the transaction is completed.

How should Buyerco proceed?

Buyer's Background Research

- Due Diligence (Using SEC Filings/Public Information)
 - Assess Potential Benefits of Transaction and Determine Acquisition Price or Range
 - Identify Business Risks and Valuation Drivers
 - Identify Regulatory Risks and Requirements
 - Review Target Charter and Bylaws
 - Poison Pill; Classified Board; Supermajority Votes; Preferred or Super Voting Stock
 - Change of Control Provisions in Material Contracts
 - Analyze Stockholder Base – Controlling Interest/Large Holders
 - Assess Stockholder Attitudes (Low “Say-On-Pay” Support, Withhold Campaigns, Proxy Contests, etc.)
 - Share Price Trading History
 - Assess Deal Value with Premium

Buyer's Background Research (cont.)

- Analyze State Law Requirements or Potential Deal Impediments
- Analyze Tax Issues/Structure
- Antitrust Analysis
- Foreign Operations (FCPA and Local Political or Regulatory Considerations)
- CFIUS (Committee on Foreign Investment in the United States)/ITAR (International Traffic in Arms Regulation) Analysis
- Industry Regulatory Items (Import/Export Controls, IP Security)
- Should Bidder Buy Shares for a "Leg Up" Position?

Engaging the Target

- Initial Approach
 - Board Member, CEO, Investment Banker?
 - Generally Private
 - Regulation FD Issues
 - Goal — Gauge Interest
- If Receptive
 - Execute Nondisclosure Agreement (NDA) and Commence Due Diligence
 - Bidder wants exclusivity
 - Target wants protections (e.g., standstill on share accumulation or activist activities)
 - Standstill provisions cannot prevent board exercise of fiduciary duty (e.g., “don’t ask, don’t waive”)
- If Target Is Not Receptive
 - Is Buyer Prepared to Proceed on a Hostile Basis?
 - Consider Waiting for a Strategic Opportunity (e.g., Financial Stumble or Activist Approach)

Scenario 1 — Target Response

Buyerco's CEO contacts the Chairman of the Board of Synergicorp to discuss whether Synergicorp might be interested in discussing a transaction. The Chairman indicates that Synergicorp is focused on running its business and likely is not interested in a transaction, but he will discuss it with the Board.

The Chairman contacts Buyerco's CEO and advises him that the Board has discussed Buyerco's interest but determined that Synergicorp is not for sale.

What can Buyerco do?

Friendly vs. Hostile Transaction

- One-Step Merger Is Out if Target Won't Engage
 - Board has to approve Merger Agreement (DGCL § 251(b))
 - State Antitakeover Laws
 - Business Combination Statutes (DGCL § 203)
 - Control Share Statutes (Not in Delaware)
 - Fair Price Statutes (Not in Delaware)
 - Director Discretion Statutes Allowing Consideration of Non-Stockholder Constituencies (Not in Delaware)
 - Board Ability to “Just Say No”
 - Target May Have or Implement Takeover Defenses (e.g., Poison Pill)
- Bear Hug, Hostile Tender Offer, or Proxy Contest?

Hostile Approach

- Bear Hug Letter
 - Letter Sent to Board Formally Proposing Transaction
 - May be private or publicly disclosed
 - Goal is to pressure for engagement
 - If public:
 - May cause analysts or other stockholders to make supportive statements or privately pressure Target Board
 - May encourage stockholders who support a transaction to accumulate shares
- Proxy Contest
 - Proxy Contest: Put Supportive Directors on Board or Send Stockholder Message
 - Can Be Time Consuming and Expensive
 - Even if Successful, Nominees May Not Support Transaction (see, e.g., Air Products/Airgas)

Hostile Approach (cont.)

- Buy Target Stock?
 - Gives Bidder Rights as a Stockholder to Review Target Books and Records
 - Can Lower Cost by Buying Shares Before Target Is “In Play” (i.e., Getting a “Leg Up”)
 - Generally Stay Below 5% (Schedule 13D Filing Threshold) (Subject to HSR Limitations)
 - Implications on Formation of Groups for Beneficial Ownership Purposes
 - Can’t Buy Target Stock if You Have Target Material Nonpublic Information (Other Than Your Own Plans)
 - Voting Impact (% to Approve Transaction; Majority of Minority; Control Share Statutes)
 - If Strategic Buyer, What if Transaction Doesn’t Happen?

Hostile Tender Offer

- Takes the Offer Directly to Stockholders
- High Initial Tender Results Can Persuade Board to Negotiate
- Target Defenses Still Relevant (Poison Pill, etc.) but Shareholders May Exert Pressure Publicly or Privately
- Some State Law Issues May Be Addressed with Tender Conditions
 - DGCL § 203 (Business Contribution with Interested Stockholders) Doesn't Apply if Acquire at Least 85% of Stock
- Retaining Proxy Solicitor May Be Helpful
 - Identify Significant Stockholders and Monitor Trading
 - Make Introductions or Communicate with Stockholders Regarding the Offer
 - Review Institutional Stockholder Voting Policies if Proxy Contest
- Retaining PR Firm May Be Helpful
 - Monitor Media and Arrange Interviews
 - Craft and Communicate Compelling Message

Tender Offer Communications

- Commencing the Tender Offer
 - Can Commence Offer with a “Tombstone Ad” Containing Material Terms and Where to Get More Information
- Schedule TO – Tender Offer Statement
 - Includes Terms of Offer and SEC Required Disclosures About Offeror, Target, and the Offer
 - Incorporates by Reference the Bidder's “Offer to Purchase”
- Bidder and Target Will Also Communicate with Large or Influential Stockholders
- Schedule 14d-9 – Solicitation/Recommendation Statement
 - Target Board Must Make Recommendation to Stockholders Within 10 Business Days — Accept, Reject or Unable to Take a Position
 - Target Board Can Issue “Stop, Look, and Listen” Letter While Considering Stockholder Recommendation

Tender Offer Terms

- Offer Must Remain Open at Least 20 Business Days
- May Offer All Cash, All Stock or Fixed Combination or Choice
 - If Limit on Amount of Cash or Stock, Must Prorate
- Must Offer to All Holders of the Same Class of Security at the Same Price
- If Offeror Changes Percentage of Securities Sought or Consideration Offered, Offer Must Be Open at Least 10 Business Days After Changes
- Other Changes (Including Waiving Tender Offer Conditions) Require Five-Business-Day Extension
- Offeror May Extend Offer Period
 - Public Announcement on First Business Day Following Expiration by Earlier of 9:00 a.m. EST or Opening of Stock Exchange
- Must Promptly Accept and Pay for, or Return, All Securities Tendered Following Termination or Expiration of Offer
- Subsequent Offering Period OK if Original Offer Was for All Shares and Consideration Is Same Type and Amount as Original Offer

Second Step — Back End Merger

- Assumes Majority of Shares Acquired in Tender Offer
- Long-Form Merger – Requires Proxy/Information Statement and at Least 20 Days' Notice of Meeting to Stockholders; May Take 30-60 Days After Offer Depending on Notice Timing and Voting Logistics
- Short-Form Merger – if Acquire 90%+ of Shares in Tender Offer or through Top-Up Option, Can Complete Merger Without Vote of Other Shareholders, Although Still Requires Information Statement
- Medium Form Merger – DGCL 251(h) Allows Acquirer to Close Second Step Merger Without Stockholder Vote – Unavailable for True Hostile Tender Offer

Scenario 1 — Outcome

After evaluating Synergicorp's response and the challenges and ramifications of a Hostile Tender Offer, Buyerco concluded it is better off focusing on its business and either identifying another compelling acquisition or approaching Synergicorp later when it may be more receptive.

Buyerco still believes that Synergicorp is a highly desirable company, however, and continues to monitor its public filings, stockholder base, and performance so that it is prepared to quickly react should the opportunity arise to transact.

Scenario 2 – Activist Approach

A year after Synergicorp rejected Buyerco's transaction overtures, Synergicorp has experienced a decline in its business, and its stock price is down 20% over the prior 12 months. The Chairman of the Board receives a letter from Merle Icon stating that Mr. Icon has acquired a significant stake in Synergicorp and criticizing Synergicorp's recent performance and strategy. Mr. Icon says Synergicorp is trying to do too many things at once and none of them well, and that Synergicorp should explore value maximizing strategic alternatives, including a sale of the company or its noncore businesses.

Mr. Icon requests a meeting with the Chairman and says that he is prepared to go public with his concerns if they don't meet soon.

How should the Chairman proceed?

Activist Playbook

Activist Investors Accumulate Shares as Leverage to Cause Changes at a Company, Including:

- Corporate Governance Changes
- Strategic Changes
- Spin-Off or Sale of Assets/Divisions
- Sale of the Company

Typical Activist Investor Techniques

- Share Accumulation – 13D Filing (Depending on Market Cap and Size of Investment)
- Outreach to Significant Stockholders to Test the Waters
- Contact Members of the Board or Executives for Dialogue
- Private or Public Letters with Analysis, Recommendations, or Proposals (see, e.g., Starboard Value LP/Olive Garden)
- M&A Proposals May Involve the Activist Bidding (or Co-Bidding), or a More General Recommendation to Explore Strategic Alternatives, Including a Sale

Activist Playbook (cont.)

Historically, size was viewed as providing protection from a “Sell the Company” or other Activist Investor M&A approach. However, as the size and number of Activist Funds have grown (and as Activists and Strategic buyers have been willing to make joint bids), no company is too big to be a potential target.

- Icahn/Paulson – AIG
- Icahn/Jana Partners – Time Warner
- Hayman Capital/Appaloosa – GM
- Pershing Square — Target Corp. – (Sell Real Estate/Establish REIT)
- Pershing Square/Valeant – Joint Bid for Allergan
- Starboard Value – Yahoo! (Led to Sale to Verizon)
- Icahn – Xerox (Split the Company)

Activist Investing has become a regular part of hedge fund strategies, and the size of positions taken and companies targeted have steadily increased in the last several years.

Target Response to Activist Approach

- Notify Board and Convene Advisors
 - Attorneys
 - IR/PR Firm
 - Proxy Solicitor
- Prepare PR Response
- Monitor Stock Trading – Is a “Wolf Pack” Forming?
- Potential Business Issues (e.g. Customers, Suppliers, Employees)
- Communicate With Larger Stockholders – Are They Happy? Do They Understand Challenges and Strategy?
- Prepare/Adopt Defensive Measures – Poison Pill?
- Meet with Activists and Hear Them Out – What Do They Want?

Poison Pills

Delaware's Courts Are Clear That Poison Pills Are a Legitimate Defense Consistent with a Board's Right to "Just Say No" to an Acquisition Proposal and Will Be Upheld Absent an Improper Purpose (Like Board Entrenchment)

- Can Set the Threshold as Low as 5% to Protect Net Operating Losses. Selectica, Inc. v. Versata Enter., Inc., C.A. No. 4241-VCN, 2010 WL 703062 (Del. Ch. Feb. 26, 2010), aff'd, 5 A.3d 586 (Del. 2010).
- Board Permitted to Set Different Triggers in Poison Pills Based on Whether the Stockholder Is a Passive Investor (13G Filer) or Potential Activist Investor (13D Filer). Third Point LLC v. Ruprecht, C.A. No. 9469-VCP, 2014 WL 1922029 (Del. Ch. May 2, 2014).
- Board Permitted to Maintain a 20% Poison Pill Trigger Despite Insider's Ownership of More Than 30% of Shares Because There Continued to Be a Mathematical Chance to Succeed in a Proxy Contest. Yucaipa Am. Alliance Fund II, L.P. v. Riggio, 1 A.3d 310 (Del. Ch. 2010).
- Board Permitted to Maintain a Poison Pill That Blocked a Noncoercive, All Cash Tender Offer That Remained Pending for More Than a Year. Air Products & Chems., Inc. v. Airgas, Inc., 16 A.3d 48 (Del. Ch. 2011).

Scenario 2 – Activist Approach (cont.)

The meeting between Merle Icon and the Chairman of Synergicorp is cordial, but clearly Mr. Icon and the Board of Synergicorp do not share the same views on Synergicorp's future.

Following the meeting, Mr. Icon issues a public letter and files an amendment to his Schedule 13D indicating that he believes Buyerco should be sold, that he is prepared to make a bid himself, and that he is prepared to nominate candidates for election to the Board if the current Board is not willing to "do the right thing." Shortly thereafter, other large stockholders issue statements in support of Mr. Icon's views.

The Buyerco Board meets and decides that these developments may change Synergicorp's attitudes towards a transaction, and the CEO again approaches Synergicorp's Chairman. After consulting Synergicorp's Board and advisors, Synergicorp agrees to allow Buyerco to conduct due diligence and indicates a willingness to explore a negotiated transaction.

Negotiated Acquisition

- If Target Board Supports Transaction Can Forgo Tender Offer
- In All Cash Transaction, May Still Be Significant Timing Benefits for Front-End Tender Offer, Especially in Light of DGCL 251(h)
- If Securities Are to Be Issued as Consideration, Must Be Registered
 - Form S-4 Registration Statement for Registration of Securities to Be Issued in Connection with Business Combination Transaction
 - Can Combine S-4/Proxy Statement or Structure as an Exchange Offer
 - Contingent Value or Contingent Payment Rights May Require Registration
 - No Registration if (i) Integral Part of Consideration, (ii) No Rights of a Stockholder Like Voting or Dividend Rights, (iii) No Minimum Payment or Interest Rate, (iv) Not Transferable or Assignable, or (v) Not Certificated
- Generally Will Require Proxy Statement and Proxy Solicitation for Stockholder Approval
 - If Sufficient Share Ownership Concentration, Can Approve by Written Consent

Negotiated Acquisition (cont.)

- Before the Adoption of DGCL 251(h), Some Two-Step Merger Agreements Included a “Top Up” Option
 - Target Agrees to Issue Additional Shares to Buyer to Complete a Short-Form Merger
- A “Top-Up” Option No Longer Needed in Delaware if Satisfy Requirements for a “Medium Form Merger” Under DGCL 251(h), Including:
 - Target’s Stock Must Be Listed on National Stock Exchange or Held of Record by More Than 2,000 Holders
 - Agreement of Merger Expressly Permits or Requires the Merger To Be Effected Under 251(h) and Provides that the Merger Will Happen as Soon as Practicable Following Tender Offer Completion
 - The Tender Offer Is for “Any and All” Shares
 - The Buyer Holds Enough Stock After the Tender Offer to Adopt the Merger

Target Board Considerations

Depending upon the Facts, the Target's Board of Directors May Deem it Prudent to Establish a Special Committee of Independent Directors.

- Independent Directors — Standard for Independence Not Limited to NYSE or NASDAQ Requirements. Must Consider Totality of Relationship.
 - In Del. Cnty. Emps. Retirement Fund v. Sanchez, C.A. No. 9132-VCG, 2015 WL 5766264 (Del. Oct. 2, 2015) Delaware Supreme Court Held That a Close 50-Year Friendship and Significant Business Relationship Were Enough to Support Pleading Stage Inference of Nonindependence
 - Thin Circle of Friends Not Enough to Negate Independence. Beam v. Stewart, 845 A.2d 1040 Del. 2004)
 - Co-Ownership of Plane Compromises Impartiality. Sandys v. Pincus (Del. Supreme Ct. 2016).
- Need Nonconflicted Advisors – Self Interest of, or Conflicts Involving, Investment Bankers Can Taint the Entire Sale Process
- See Public Company M&A Part II

Typical Public Company Merger Agreement Terms

- Consideration
 - Stock Consideration Generally Valued Based on a Volume Weighted Average Price, and May Include Collars
 - Payment Terms for Options, SARs, Warrants, and Different Classes of Stock
 - Consideration May Include Contingent Value or Contingent Payment Rights
 - Bridge Transaction Value Gaps – Particularly if Future Events May Impact Value (e.g., FDA Approvals, Outcome of Pending Litigation, etc.)
- Reps and Warranties
 - May Incorporate Information from Public Filings
 - Don't Survive the Closing – Useful for Disclosure, and Confirming Due Diligence, and May Allow Buyer Not to Close if Extreme Unanticipated Problems (i.e., MAC/MAE)
 - Generally “Brought Down” at Closing Against an Overall Material Adverse Change/Material Adverse Effect Standard
 - Representation and Warranty Insurance – Post-Closing Buyer Protection

Typical Public Company Merger Agreement Terms (cont.)

- Covenants
 - General “Conduct of the Business” Covenants to Operate in the Ordinary Course and to Do or Refrain from Doing Certain Specified Activities
 - Antitrust “Gun Jumping” Considerations
 - Obtain Necessary Third-Party Consents and Approvals
 - May Require Notice of Representation, Warranty or Covenant Breach
 - May Require Cooperation With Buyer’s Financing Efforts
 - Mutual Cooperation With Proxy and Registration Statement Filings and Solicitation of Stockholder Votes
 - May Include a “Force The Vote” Provision
 - Target has to put transaction to a stockholder vote, even if another transaction has been proposed or Board recommendation has changed
 - May Require Specific Actions to Obtain Antitrust or Other Approvals
 - Commercially Reasonable Efforts
 - “Hell or High Water”
 - Other Covenants Specific to the Companies/Circumstances

Typical Public Company Merger Agreement Terms (cont.)

- Deal Protection Provisions
 - Gives Buyer comfort deal will close or Buyer will be compensated if it doesn't
- Exclusivity/No Solicitation
 - Target may not directly or indirectly encourage or engage in activities relating to a competing acquisition
 - Target board always has “fiduciary out” to respond to unsolicited offers and other “intervening events”
 - Typically requires notice of other bids and may include a “matching” right for initial buyer
 - If no pre-signing sale process, may include “go shop” rights with break-up fees if another buyer takes the deal
- Termination or Break Fees/Expense Reimbursement
 - Compensates initial bidder if another buyer tops the deal
 - Reverse Break Fee for Antitrust or Other Regulatory Risk (CFIUS) or Lack of Financing

Typical Public Company Merger Agreement Terms (cont.)

Deal Protections: Locking Up the Deal

- Irrevocable Voting Agreement With Holders of a Majority of Shares Combined With a “Force The Vote” Provision Held Unenforceable By Delaware Supreme Court. Omnicare Inc., v. NCS Healthcare, 818 A.2d 914 (Del. 2003).
- Agreement By a Majority of Holders Not to Accept or Approve Any Competing Proposal For 18 Months Upheld By Chancellor Chandler in Orman v. Cullman, C.A. No. 18039, 2004 WL 2348395 (Del. Ch. Oct. 20, 2004).
- No Injunction Granted Where Acquirer Had Right to Terminate the Acquisition if Shareholder Consent Not Obtained Within 24 hours. Optima Int’l of Miami, Inc. v. WCI Steel, Inc., C.A. No. 3833-VCL (Del. Ch. June 27, 2008).

Typical Public Company Merger Agreement Terms (cont.)

- Closing Conditions
 - Stockholder Approval
 - Majority of the Minority?
 - Regulatory and Third Party Approvals
 - No Injunction or Other Legal Impediment to Closing
 - Buyer and Target Representations and Warranties True and Correct (Usually Against an Aggregate MAC/MAE Standard For Target Reps)
 - Buyer and Target Covenants Performed in All Material Respects
 - Absence of MAC/MAE
 - May Include Limits on Appraisal Demands

Typical Public Company Merger Agreement Terms (cont.)

Termination of Agreement:

- By Mutual Consent
- By Either Party if:
 - Merger Doesn't Close By Specific Outside Closing Date (Other Than as a Result of Rep, Warranty or Covenant Breach By Party Seeking Termination), Which Sometimes is Extended For Necessary Antitrust Approvals or Other Specific Events
 - Injunction or Other Legal Prohibition On Closing
 - Stockholders Don't Approve Merger

Typical Public Company Merger Agreement Terms (cont.)

- Buyer Termination:
 - Target Board Changes or Fails to Reaffirm Recommendation of Initial Buyer Transaction, Commencement of a Third Party Tender Offer Not Opposed By Target Board, Breach of No-Solicit Covenants
 - Breach of Target Reps, Warranties or Covenants Resulting in Failure of Closing Condition (Often Subject to a Cure Right)
 - Buyer May Have Unilateral Termination Right if Pay Reverse Break Fee
- Target Termination:
 - Fiduciary Out – Ends at Stockholder Approval
 - Breach of Buyer Reps, Warranties or Covenants Resulting in Failure of Closing Condition (May Be Subject to a Cure Right)

Typical Public Company Merger Agreement Terms (cont.)

Effects of Termination

- No Termination/Break Fee Paid if:
 - Mutual Termination
 - Stockholders Don't Approve Merger (But Can Get Reasonable Expense Reimbursement)
 - Buyer Breach of Representation, Warranty or Covenant (Damages)
 - No Closing By Outside Closing Date (Depending on Reason)
- Termination/Break Fee (Which May Include Expense Reimbursement) Paid if:
 - Change or Failure to Reaffirm Target Board Recommendation
 - Commencement of Tender Offer Not Opposed By Target Board
 - Breach of No-Solicit Covenants
 - Target Terminates to Accept Another Deal (Typically a Reduced Fee if Termination Happens During Go Shop Period)
- Reverse Termination/Break Fee Paid for Failure of Buyer to Close due to Absence of Financing or if Buyer Exercises Unilateral Termination Right

Other Transaction Considerations

- Regulatory Approvals
 - Hart-Scott-Rodino
 - If HSR filing triggers are met, must make filing and wait for approval or expiration of 30 day waiting period (15 day early termination for tender offer)
 - Can request early termination but requires public disclosure
 - HSR filings can be triggered by accumulating stock, so the timing and amount of shares accumulated should take antitrust issues into account
 - Exon-Florio/CFIUS – If Acquirer is a Foreign Person and the Acquisition Could Implicate National Security – Broadly Construed
 - SEC
 - Securities Registration
 - Tender Offer and/or Proxy Solicitation Filings
 - Industry-Specific Regulatory Approvals
 - Foreign Regulatory Approvals - Cross-Border Transaction

Fiduciary Duties and Standards of Review

- Buyer Directors:
 - Duty of Care (Reasonable Person Standard)
 - Duty of Loyalty (Put Interest of Company and Stockholders Before Yours)
 - Actions Likely Evaluated Under Business Judgment Rule
- Seller Directors:
 - Duty of Care
 - Duty of Loyalty
 - Duty of Candor (Tell Stockholders Anything That Might Reasonably Affect Their Decisions)
- M&A Standards of Review
 - Business Judgment Rule
 - Unocal/Unitrin Standard
 - Revlon Standard
 - Entire Fairness Standard

Duty of Care

- The Delaware Supreme Court Held that Directors Can Be Personally Liable for Breaches of the Duty of Care. Smith v. Van Gorkum, 488 A.2d 858 (Del. 1985).
 - The Board Did Not Act in an Informed and Deliberative Manner Before Approving a Merger and Submitting it to the Stockholders for Approval
- The Delaware Legislature Responded by Enacting DGCL §102(b)(7), Which Permits Delaware Companies to Eliminate or Limit Directors' Personal Liability for Breach of Fiduciary Duty
 - May Not Eliminate or Limit Liability for:
 - Breach of the Duty of Loyalty
 - Acts or Omissions not in Good Faith or Which Involve Intentional Misconduct or Knowing Violation of Law
 - Liability for Unlawful Dividends or Stock Purchases or Redemptions under DGCL § 174
 - Transactions From Which the Director Derived an Improper Personal Benefit
 - Officers Cannot be Exculpated
 - Does not Protect Advisors

Business Judgment Rule

- Not a Duty, but a Standard of Review
 - Default Standard Against Which Board Actions Are Measured
 - Presumption That Protects Directors:
 - Absent self-interest or self-dealing, it is presumed that a Director acts on an informed basis, in good faith, and in the honest belief that the actions taken are in the best interests of the Company and its shareholders
 - Persons seeking to challenge a Director's conduct bear the burden of showing a breach of fiduciary duty
 - No presumption that Directors are infallible and don't occasionally make mistakes or bad decisions, but they are protected from liability in the absence of clear proof of a breach of fiduciary duty
 - A decision made by a loyal and informed Board will not be overturned by the courts unless it cannot be "attributed to any rational business purpose"
 - Should Be The Standard That Applies to Buyer's Board in The M&A Context
 - May Be The Standard That Applies to Target Board in The M&A Context As Noted Below

Business Judgment Rule (cont.)

- Delaware Supreme Court Rules That A Fully Informed, Noncoerced Vote of Disinterested Stockholders Invokes Business Judgment Standard of Review. Corwin v. KKR Fin. Holdings LLC, C.A. No. 629, 2014, 2015 WL 5772262 (Del. Oct. 2, 2015). Corwin has been extended to tender offers as well. Revlon and Unocal Primarily Standards for Determining Availability of Injunctive Relief.
- Transaction Between a Company and Its Controller Is Subject To Business Judgment Standard of Review If (1) Approved By Fully Functioning Special Committee of Independent Directors; and (2) Subject to Fully Informed, Uncoerced, Non-waivable Vote of Majority of the Minority of Stockholders. Kahn v. M&F Worldwide, 88 A.3d 635 (Del. 2014).

Other M&A Standards of Review

- **Unocal Standard: Applies to Board Decisions to Unilaterally Adopt Defensive Measures**
 - Defensive Measures in Response to a Take-Over Attempt Must Be Proportionate and Reasonable in Relation to a Threat to Corporate Policy
 - The Measures Taken Cannot Be Preclusive or Coercive
 - preclusive defenses – e.g. adopting bylaws requiring 100% shareholder approval for a change of control; “No talk” provision in a merger agreement prohibiting discussion of competing and perhaps more favorable transaction proposal
 - coercive defense – e.g. signing merger agreement with a “white knight” with an excessive termination fee if merger is not approved by the stockholders
 - Enhanced Scrutiny is Given to The Perception of a Threat and The Proportionality and Reasonableness of The Defensive Actions Taken
 - If The Board’s Conduct Meets The Unocal Enhanced Scrutiny Standards, They Are Entitled to The Protections of The Business Judgment Rule

Other M&A Standards of Review

- Revlon Standard: Once a Board Decides to Sell a Company, Then The Primary Duty is to Obtain The Highest Price Reasonably Obtainable:
 - Another Form of “Enhanced Scrutiny” Applied to Actions of Directors in the Sale of the Company Context
 - Role Shifts From “Defenders of The Corporate Bastion to Auctioneers Charged With Getting the Best Price”
 - Not The Highest Price Theoretically Possible, Just Reasonably Obtainable
 - Justification in Part For “Fiduciary Out” Provisions in Merger Agreements
 - Applies in a Sale For Cash But Not a Sale For Stock Which Will Be Held Broadly in The Public Markets, Unless The Consolidated Entity Would Have a Controlling Stockholder
 - In a Mixed Consideration Transaction, if Majority of Consideration is Publically Traded Stock, Revlon Review May Not Apply

Other M&A Standards of Review: Gloss on Revlon Duties

No Mandated Sale Process Required If Revlon Standard Met

- Market Check Before Executing a Definitive Agreement Not Required Under Revlon Standard of Review. C & J Energy Services, Inc. v. City of Miami General Emps.' & Sanitation Emps.' Retirement Trust, 107 A.3d 1049 (Del. 2014).
- Vice Chancellor Noble Held That Impeccable Knowledge of Board Obviated Need For Market Check or Investment Banker Fairness Opinion. In Re OpenLane Inc. Shareholders Litig., C.A. No. 6849 – VCN (Del. Ch. Sept. 30, 2011).

Other M&A Standards of Review

- Entire Fairness: Most Demanding Standard of Review, Requires Both a Fair Process as Well as a Fair Outcome (i.e., fair price).
 - Applies When Board is Not Independent or Not Disinterested
 - Applies to a 13e-3 “Going Private” Transaction
 - When an affiliate of the Company or the Company itself is involved in a tender offer, merger, asset sale, or reverse stock split as a result of which the shares of stock of a public company will become eligible for deregistration or delisting
 - Burden of proving “entire fairness” generally is on the party defending the transaction but:
 - properly functioning special committee or
 - Informed approval by a majority of the minority stockholders (i.e. the disinterested stockholders) shifts the burden of proof to the party challenging the transaction
 - If Both a Properly Functioning Special Committee and an Informed Approval by The Majority of The Minority Then Business Judgment Rule Applies
- Plaintiffs can still seek to defeat the burden shift or the Business Judgment Rule standard by proving the Special Committee was not properly functioning or that the minority stockholders were not provided necessary information to make an informed decision.

M&A Litigation Risk

- Buyers Typically Are Not Sued, But Can Be Named on an “Aiding And Abetting” Theory (Which Should Not Survive a Motion to Dismiss in Delaware)
- Buyer Will Inherit Whatever Litigation Results From The Acquisition
- Target Boards in Recent Years Have Been Sued in 95%+ Of Public Company Deals, Generally on Breach of Fiduciary Duty Claims:
 - May Face Lawsuits in Jurisdiction of Organization and in Jurisdiction Where Headquarters or Significant Operations Are Located
 - Exclusive Forum Bylaws – Requires Litigation Regarding Internal Affairs/Stockholder Claims Only in One Jurisdiction (e.g. Delaware Courts). Delaware Prohibits Litigation Fee Shifting Bylaws
 - Have Been Held to Be Legal In Delaware, But Requires Some Level of Judicial Deference in Other Jurisdictions
 - Target Board May Adopt Exclusive Forum Bylaw Provisions Even in The Face of a Takeover, as Long as Action Satisfies Unocal Standard and Other Fiduciary Duties
 - Can Be Adopted Concurrently With Transaction Announcement
- Most Litigation Settled – Sometimes With Additional Disclosures (But Delaware Courts Are Becoming Less Willing To Go Along With “Disclosure Only” Settlements. See In re Trulia, Inc.) 129 A.3d 884
- Fee Shifting Bylaws (Shifting Litigation Cost to Stockholders Who Lose) Prohibited Through Amendment to Delaware Section 109 With Respect to Internal Corporate Claims

Appraisal Rights

- Most States Include Dissenters' Rights or Appraisal Rights Statutes
 - Stockholders Who Did Not Vote For a Merger But Held Shares At The Time of The Merger Can Ask a Court to Determine The "Fair Value" of Their Shares
 - Value Can Be Higher, Lower or The Same As Was Paid in The Transaction
 - No Value is Generally Attributed to The Completion or Expectation of The Merger (i.e. The Value of The Stock Ignores Any Effect of The Transaction Itself)
 - Many Hedge Funds Now Arbitrage Dissenters Rights By Buying Shares After The Merger Announcement, Holding Them Through The Merger, and Then Asserting Appraisal Rights
 - Function of Low Interest Rate Environment, Because Stockholder Gets Fair Value Plus Interest From The Date of The Merger to The Date of Payment at a Rate of 5% Over The Federal Reserve Discount Rate and Compounded Quarterly, Even if The Value Determined is The Same As or Less Than The Merger Price

The Coming Nadir for Appraisal Arbitrage?

- Despite Positive Variance Between Statutory Interest Rate on Appraisal Awards And Market Interest Rates, Appraisal Arbitrage Faces Headwinds. Recent Delaware Decisions Peg The Fair Market of Shares in an Appraisal Preceding at the Merger Price.
- The Most Reliable Indication of Fair Market Value in an Appraisal Action is the Merger Price, if the Price Was negotiated at Arm's Length, i.e. "Where The Sales Process is Thorough, Effective and Free From Any Specter of Self-Interest or Disloyalty"

Merion Capital LP v. BMC Software, Inc., C.A. No. 8900-VCG, 2015 WL 6164771 (Del. Ch. Oct. 21, 2015); see also Huff Fund Inv. P'ship v. CKx, Inc., C.A. No. 6844-VCG, 2014 WL 545958 (Del. Ch. February 12, 2014), in Which The Delaware Supreme Court Confirmed The Chancery Court's Decision That, in an Appraisal Action, The Merger Price Was The Best Indication of Fair Value Where There Was a Full Market Check and Where Traditional Valuation Analysis Was Unavailable. However, in Dunmire v. Farmers & Merchants Bancorp, Chancery Court Granted Valued Shares Higher than Deal Price, Expressing Concerns that Controlling Stockholder Was On Both Sides of Transaction.

The Coming Nadir for Appraisal Arbitrage? (cont.)

- In response to Appraisal Arbitrage, Delaware legislature amended Section 262 of the DGCL to provide:
 - Court to dismiss appraisal proceeding if stock is listed on a national securities exchange unless: (i) total number of appraisal shares exceeds 1% of the outstanding shares of the class or series of stock eligible for appraisal, (ii) the value of the appraisal shares exceeds \$1 million based on the merger price, or (iii) the merger was approved pursuant to Section 253 (merger of corporate parent and subsidiary) or Section 267 (merger of non-corporate parent and subsidiary) of the DGCL.
 - Surviving Corporation can pay cash to each stockholder entitled to appraisal and eliminate interest accrual, except on: (i) the difference, if any, between the amount paid to the stockholder and the fair market value determined by the court and (ii) any accrued and unpaid interest, unless paid when the cash amount is paid to the stockholder.

QUESTIONS?

Biographies



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