

The background features a dynamic, abstract design with numerous thin, parallel lines in shades of red and blue, creating a sense of motion and depth. The lines are most concentrated on the right side and fan out towards the left.

**Morgan Lewis**

# **M&A ACADEMY**

## **Current Legal Trends in the Public M&A Market**

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# Topics to Be Covered

- Comparison of Public vs. Private M&A
- Due Diligence Considerations
- General Overview of Transaction Structures
- Typical Merger Agreement Provisions
- The Evolving Litigation and Appraisal Landscape

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**SECTION 1**

# **COMPARISON OF PUBLIC VS. PRIVATE M&A**

# Comparison of Public vs. Private M&A

- Buyer's acquisition of publicly traded securities
  - Enhanced pre and post-signing considerations
- Publicly available information
- Privity of contract
  - In general, Buyer does not gain contractual privity with parties that will receive consideration
- Indemnity/post-closing obligations
- Nature of representations and warranties
- Nature of closing conditions
- Public shareholder approval / tender process, filed with SEC
- Application of "fiduciary out"
- Enhanced consideration of potential transaction failure



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**SECTION 2**

# **DUE DILIGENCE CONSIDERATIONS**

# Due Diligence Considerations

- Utilize SEC filings/public information
  - 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/large interest holders
  - Share price trading history
  - In transactions involving stock consideration, reverse diligence on Buyer will typically focus on, and often be limited to, Buyer’s SEC filings and other public information
- Analyze state law requirements or potential deal impediments

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**SECTION 3**

# **GENERAL OVERVIEW OF TRANSACTION STRUCTURES**

# Transaction Structures

Two Primary Acquisition Structures:

- Merger (One Step)
- Tender Offer (Two Step)
  - 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
- Asset Sales



# One-Step Merger vs. Tender Offer

- One-Step Merger Pros and Cons
  - When closed, Buyer owns 100% of Target
  - Target required to convene a stockholder meeting; receive requisite vote
  - Can take longer than tender offer
- Tender Offer Pros and Cons
  - May close more quickly than a one-step merger
  - Second-step merger can be facilitated without a vote
    - “Top up” option
    - 251(h) merger in Delaware (other states following suit)
- Hostile Tender Offer Considerations
  - Does not require Target board approval (absent a poison pill)
  - May be expensive, time consuming, and less certain of success

# One-Step Merger vs. Tender Offer (cont.)

Transaction Structure (Assumes All Cash)	Two-Step Tender Offer	One-Step Merger
<b>Approximate Overall Timing</b>	<ul style="list-style-type: none"> <li>Two to three month process</li> </ul>	<ul style="list-style-type: none"> <li>Two to five month process (dependent on SEC review of proxy)</li> </ul>
<b>Advantages</b>	<ul style="list-style-type: none"> <li>Quicker path to control of Target than one-step (reduces risk of competing offer)</li> <li>SEC is committed to expedited review</li> <li>Able to avoid a stockholders meeting and proxy solicitation</li> </ul>	<ul style="list-style-type: none"> <li>Able to complete transaction in one step with only 51% of Target stockholders voting in favor of transaction</li> <li>Does not require registration of Buyer shares</li> <li>Extended period between signing and closing to obtain any required consents (e.g., regulatory approval) or buyer financing</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>Shorter time period between signing and closing to obtain any required consents (e.g., regulatory approval) or buyer financing</li> <li>Tender can't close until all conditions are satisfied</li> </ul>	<ul style="list-style-type: none"> <li>Slower path to control of Target (extends risk of competing offer)</li> <li>SEC is not committed to expedited review</li> </ul>
<b>Procedure</b>		
Weeks 1-3	<ul style="list-style-type: none"> <li>Due Diligence and Execution of Merger Agreement</li> </ul>	<ul style="list-style-type: none"> <li>Due Diligence and Execution of Merger Agreement</li> </ul>
Weeks 4-5	<ul style="list-style-type: none"> <li>Prepare SEC filings (1-2 weeks)                             <ul style="list-style-type: none"> <li>Schedule TO</li> </ul> </li> <li>Parties file HSR materials with DOJ or FCC</li> </ul>	<ul style="list-style-type: none"> <li>Prepare SEC filings (1-2 weeks)                             <ul style="list-style-type: none"> <li>Proxy Statement</li> </ul> </li> <li>Parties file HSR materials with DOJ or FCC</li> </ul>
Weeks 5-9	<ul style="list-style-type: none"> <li>Commence Tender Offer (must remain open for longer of 20 business days or SEC approval of filing)</li> <li>HSR waiting period expires (15 days if no second request)</li> <li>SEC review process (3-4 weeks)</li> <li>Close Tender Offer</li> <li>Close Short-form Merger</li> </ul>	<ul style="list-style-type: none"> <li>SEC to confirm no review of proxy (2-4 weeks)</li> <li>If SEC review (add 4-8 weeks )</li> <li>HSR waiting period expires (30 days if no second request)</li> <li>If no SEC review, mail proxy statement and solicit proxies (4 weeks)</li> <li>If no SEC review, conduct Special Meeting and close transaction</li> </ul>
Weeks 9-21		<ul style="list-style-type: none"> <li>If SEC review, parties reconcile comments and amend proxy (add 4-8 weeks)</li> <li>Mail proxy statement and solicit proxies (4 weeks)</li> <li>Conduct Special Meeting and close transaction</li> </ul>

# One-Step Merger Approval Procedures

- Similar to a public company's annual shareholder meeting process
  - Convene a meeting (record date, etc.)
  - File Proxy Statement with SEC
  - SEC may review Proxy Statement
- Company recommendation
  - Target board must make recommendation to stockholders
- Approval standard (state law + Target's charter)
- If stockholder approval necessary, generally may require proxy solicitation
- If sufficient share ownership concentration and state law requirements, can approve by written consent

# Tender Offer Basics

- Commencing the tender offer
  - Commenced with a “Tombstone Ad” containing material terms
- Buyer Filing: Schedule TO – Tender Offer Statement
  - Includes terms of offer and SEC required disclosures about Buyer, Target, and the offer
  - Incorporates by reference Buyer's “Offer to Purchase”
- Company Filing: 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
  - Typically filed at the same time as Schedule TO in a friendly transaction
- SEC may review tender offer filings



## Tender Offer Basics (cont.)

- Tender offer must remain open at least 20 business days
- May offer variety of consideration alternatives: All Cash, All Stock or Fixed Combination or Election
  - If there is a 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
- Buyer 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
- Buyer 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

## Tender Offer — Back End Merger

- Short-Form Merger – if Buyer acquires 90%+ of shares in tender offer (or through a “Top-Up” Option), can complete merger without vote of other shareholders, although still requires Information Statement
- A “Top-Up” Option no longer needed in Delaware if requirements under DGCL 251(h) are satisfied. These include:
  - Target’s stock must be listed on national stock exchange or held of record by more than 2,000 holders
  - Merger agreement 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
  - Tender offer is for “any and all” shares
  - Buyer holds enough stock after the tender offer to adopt the merger

## Other SEC Filing Considerations

- 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 required 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
- **Plan ahead** if filing a Proxy Statement or Solicitation/Recommendation Statement
  - Organize and maintain record of key communications and developments during the course of negotiations
  - Consider optics of actions

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**SECTION 4**

**TYPICAL PUBLIC COMPANY  
MERGER AGREEMENT  
PROVISIONS**



# Consideration; Representations and Warranties

- 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
  - Typically 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

# 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 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

# Deal Protection; Termination Fees

- Deal protection provisions
  - Target non-solicitation structure
    - “No shop” vs. “go shop” vs. “window shop”
      - Buyer matching rights
    - Intervening event
- Termination fees/expense reimbursement
  - Compensates initial Buyer if another Buyer tops the deal with a higher price offer
  - Reverse termination fee for failures to obtain antitrust or other regulatory approvals or for lack of financing

# Deal Conditionality

- Closing conditions (merger closing and tender closing)
  - Stockholder approval (if necessary)
  - Regulatory and third party approvals
    - Typically no required third party contract consents condition
  - 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
- Tender offer back-end merger usually has minimal conditions



# Termination Rights

## Termination of Agreement:

- By mutual consent
- By either party if:
  - Merger doesn't close by specific outside closing date (or "drop dead date")
  - Injunction or other legal prohibition on closing
  - Stockholders don't approve merger

## Termination Rights (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 non-solicitation covenants
  - Breach of Target reps, warranties or covenants resulting in failure of closing condition (often subject to a cure right)
- Target Termination:
  - “Fiduciary Out” – Ends at stockholder approval / closing of tender offer
  - Breach of Buyer reps, warranties or covenants resulting in failure of closing condition (may be subject to a cure right)

## Effects of Termination

- No termination/break fee paid if:
  - Mutual termination
  - No closing by outside closing date (subject to tail)
- 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 non-solicitation covenants
  - Target terminates to accept another deal (typically a reduced fee if termination happens during “go shop” period)
- “Naked No Vote” (more often limited to expense reimbursement)
- Reverse termination/break fee paid for failure of Buyer to close due to absence of financing or if Buyer exercises unilateral termination right

# Termination Fees

- Typically based on a percentage of equity value
- Target termination/break fees
  - Size limited by case law (can't coerce the vote)
  - In 2017, 111 of 173 (64%) surveyed public M&A transactions involved termination/break fees of 3.00-3.99% (per PLC deal points study)
- Reverse termination/break fees
  - More flexibility on size (typically larger than target termination/break fees)
    - In 2017, of 31 surveyed public M&A transactions involving reverse termination/break fee as a cap on damages, average fee was 6.76% of equity value (per PLC deal points study)
  - Financing failures
  - General breaches of reps & covenants
    - Treatment of willful breaches
  - Antitrust failures

## Other Transaction Considerations

- Stockholder support/voting agreements
- Post-merger governance considerations
  - Especially meaningful in “merger of equals”
- Regulatory approvals
  - Hart-Scott-Rodino
  - Exon-Florio/CFIUS – If Buyer 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

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**SECTION 5**

**THE EVOLVING LITIGATION  
AND APPRAISAL LANDSCAPE**

## Things Have Changed

- If we were giving this presentation six years ago, it would be a very different presentation.
  - We would, as dealmakers, be lamenting the fact that over 90% of public company acquisitions were subject to expensive and time consuming litigation.
  - We would not be overly focused on appraisal rights, which were less attractive to the plaintiff's bar than traditional stockholder claims against the target company's directors and others.
  - When discussing controlling stockholder transactions (i.e., transactions in which a majority stockholder acquired 100% of a company from the public via either a tender offer or a one-step merger), we would be trying to untangle a difficult series of cases (*Pure Resources*, *Siliconix* and others) that applied different standards of judicial review depending on whether the transaction was structured as a tender offer or a one-step merger).



# Disclosure Only Settlements

- Disclosure Settlements:
  - For many years, the Delaware court would routinely approve so-called “disclosure only” settlements in stockholder class actions, in which the company and director-defendants obtain a broad release of known and unknown claims in exchange for their agreement to include in the proxy statement additional disclosures in advance of the stockholder vote on the transaction.
  - The Delaware Court of Chancery in early 2016 in the case *In Re Trulia*, announced that it will no longer approve “disclosure only” settlements absent certain conditions — the supplemental disclosures supporting a proposed settlement must address material misrepresentations or omissions, and the release defendants obtain in return must be narrowly tailored to the claims relating to the disclosures. Following *Trulia*, disclosure-based settlements before the Court of Chancery have been all but extinct.
  - Litigation has not subsided in Delaware post-*Trulia* but has taken a different form. Instead of pre-closing requests for injunctive relief, stockholder plaintiffs have focused instead on post-closing monetary damages and have increased their use of statutory relief, such as books and records and appraisal actions pursuant to 8 Del. C. §§ 220 and 262, to challenge transactions.
  - Litigants also appear to be avoiding filing their disclosure claims as state law breach of fiduciary duty claims, instead filing claims relating to a proposed transaction in federal courts pursuant to federal securities laws in order to avoid forum selection bylaws requiring internal corporate state law claims (such as breach of fiduciary duty claims) to be filed in Delaware.

# Appraisal Rights

- Dissenters'/Appraisal rights statutes:
  - Most states have dissenter's/appraisal rights statutes which provide 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 acquisition, but historically the deal price is a reliable indicator of fair value in most cases involving an unhindered, informed and competitive sales process.
  - In *Dell*, court reiterates that it is statutorily required to consider "all relevant factors" without applying any presumption that favors any one indicator of fair value. Post-*Dell*, the Court of Chancery has issued appraisal decisions that departed from the deal price and returned fair values below the deal price.
    - In *Aruba*, the court looked at the unaffected market price to determine the fair value (which was 30% less than the deal price).
    - In *AOL*, looked exclusively at DCF analyses due to concerns in the sales process (which was only slightly less than the deal price).
  - Recent Delaware opinions finding fair value below deal price may deter some stockholders from seeking appraisal in transactions. In 2018, a total of 26 appraisal petitions were filed in Delaware, a 56% decline from the 60 such petitions filed in 2017 and barely one-third of the 76 appraisal actions filed in 2016.
  - The *Dell* decision solidifies the benefit in an appraisal proceeding of a robust and competitive sales process, because if the market for the company and its stock was efficient, the merger price is often found to be the most reliable indicator of fair value.

# Controlling Stockholder Transactions

- In 2014, the Delaware Supreme Court decided *Kahn v. M&F Worldwide*, holding that business judgment is the appropriate standard of review for a merger between a controlling stockholder and its subsidiary, so long as:
  - The controlling stockholder conditions the transaction *ab initio* on the approval of both a special committee and the vote of a majority of the minority stockholders;
  - The special committee is independent;
  - The special committee is empowered to select its own advisors and to reject a proposed transaction;
  - The special committee meets its duty of care in negotiating a fair price;
  - The minority stockholder vote is informed; and
  - The minority vote is uncoerced.

## Controlling Stockholder Transactions (cont.)

- Although the *MFW* requirements are often compressed into two prongs, recent cases demonstrate that each element is important.
- Two cases addressed the *ab initio* requirement:
  - In *Flood v. Synutra*, the controller's initial indication of interest was not conditioned on approval by a special committee and the majority of the minority stockholders. However, two weeks later the controller amended the offer to include the conditions before any economic negotiations took place, and the court held that *MFW* applied.
  - By contrast, in *Olenik v. Lodzinski*, ten months between the time of the controller's initial offer and the time the *MFW* protections were put into place. During that period of time, substantive economic negotiations occurred. The court declined to apply *MFW*.

## Biographies



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Robert W. Dickey advises US and non-US based companies with respect to their most important mergers, acquisitions, divestitures, and other strategic transactions. He also counsels executives, in house counsel, and boards of directors on a wide range of critical corporate matters, including fiduciary duties, corporate governance, and securities law compliance.



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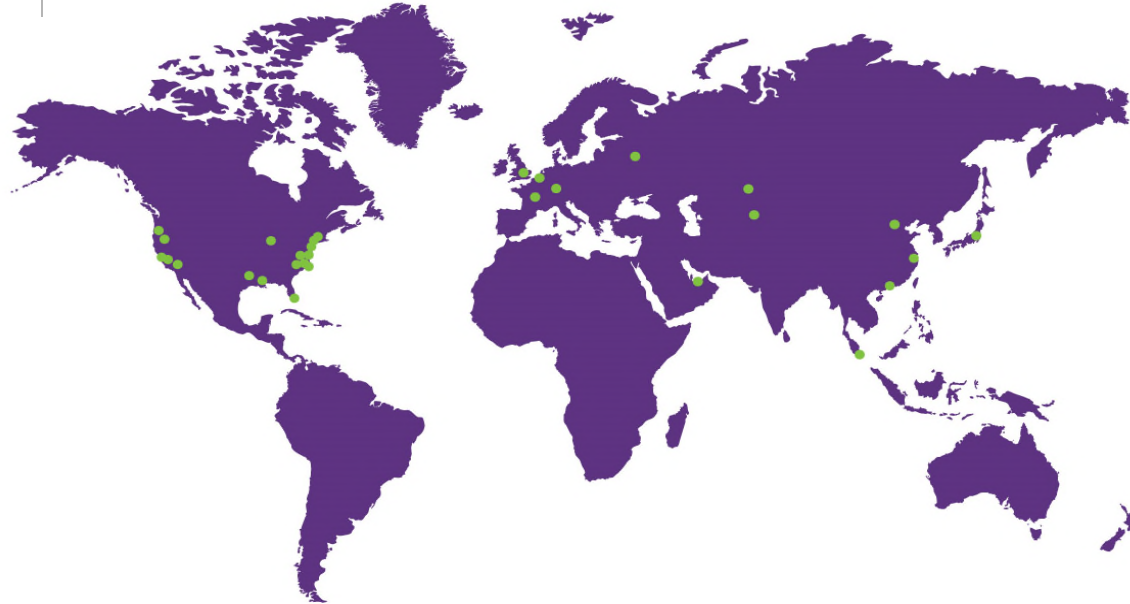
Michael N. Baxter advises clients on mergers and acquisitions (including joint ventures, spin-offs, and strategic alliances), finance and restructuring, securities (including public and private equity and debt offerings), and tax, and also advises clients in financial services regulatory matters. His clients range from Fortune 500 companies to investment banks to businesses in emerging markets. Prior to joining Morgan Lewis, Michael was an associate in the New York office of another major international law firm.

## Our Global Reach

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