

# DOING DEALS 2010

## *Choosing a Structure*

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## Acquisition Methods

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## Broad Categories of Acquisition Agreements

- |   |   |                  |
|---|---|------------------|
| I. Investment Agreement                 | } | Private          |
| II. Asset Purchase Agreement            |   |                  |
| III. Stock Purchase Agreement           | } | Usually Private  |
| IV. Merger Agreement (one-step)         |   |                  |
| V. Merger Agreement (with tender offer) | } | Generally Public |
|   |   |                  |
|   | } | Public           |
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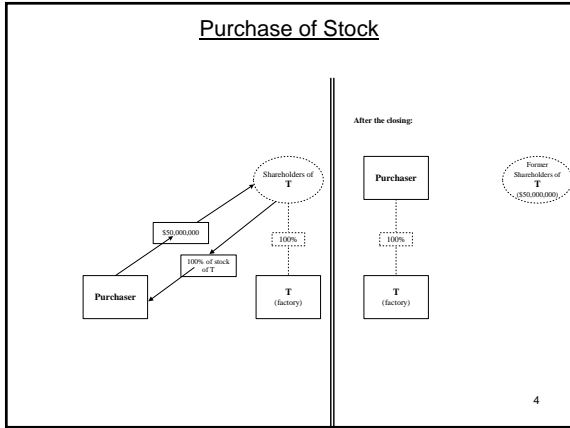
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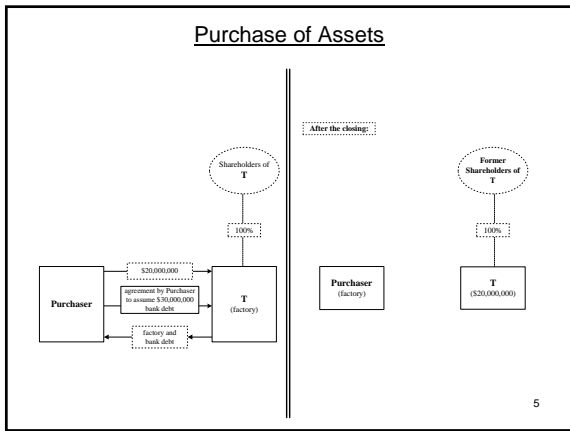
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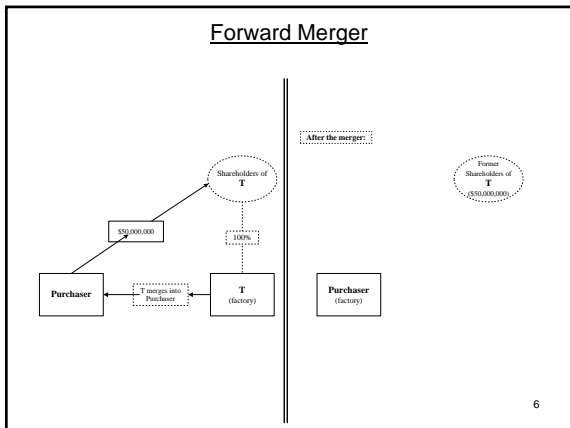
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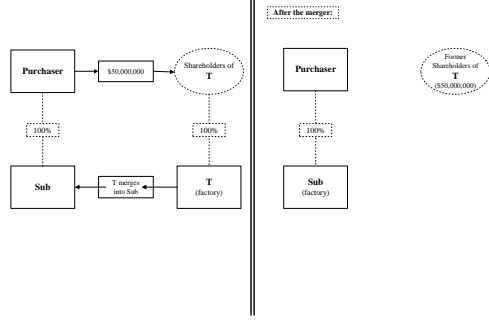
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### “Forward Subsidiary” Merger




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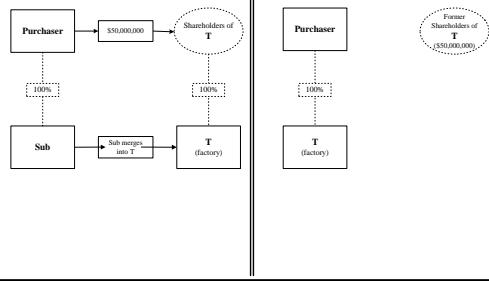
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### “Reverse Subsidiary” Merger




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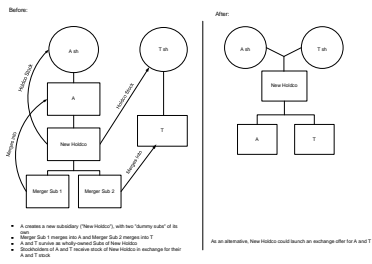
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### Double Dummy/Holding Company Merger




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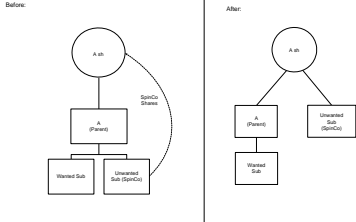
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## Spin-Off

- A separate spin-off subsidiary (SpecialCo)
- A distributes shares of SpecialCo to A's stockholders on a tax-free dividend



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## Deal Structure driven by many factors

- Basic Questions about Target ..... (a) Public Company/Private Company  
 (b) State of Incorporation  
 (c) What is Acquirer buying?
- Corporate Law ..... (a) Target shareholder approval  
 (b) Acquirer shareholder approval  
 (c) Appraisal Rights
- Tax Considerations ..... (a) Cash  
 (b) Stock  
 (c) Hybrid cash & stock/Other  
 (d) Tax benefits  
 (e) Pass-through treatment
- Timing/Other ..... (a) Relative leverage of the parties  
 (b) Liability profile of the target business  
 (c) Financing Structures  
 (d) Buyout fund structures  
 (e) Third Party/Other Consents  
 (f) State Statutes  
 (g) Optical/political considerations

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## Structuring Hypothetical

- Acquirer (A) is a \$10 billion market cap company, seeking to acquire a target (T), a \$5 billion market cap company
- A is willing to do a cash/stock election deal, with 75% cash and 25% stock
- The shares issuable for the 25% stock consideration are about 15% of A's outstanding shares today
- Neither party wants to subject the deal to a shareholder vote of A

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### Benefits of a One-Step Merger vs. a Tender Offer

- **100% Ownership.** A merger accomplishes 100% ownership in a single step, which may be important for financing the transaction. A tender offer will require a second-step merger to acquire 100% of a public company.
- **Possible Timing Advantage.** If regulatory approvals or other conditions delay consummation of a tender offer for more than approximately three to four months, a one-step merger can be completed more quickly than a two-step tender offer/merger that does not obtain tenders sufficient for a short-term merger.
- **Acquisition of Target Shares in the Market.** A bidder is prohibited from acquiring shares outside of a tender offer. An acquiror not making a tender offer may acquire target shares during the pendency of its proposal subject to any applicable legal or contractual restrictions.

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### The Impact of the Tender Offer Rules

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### Disclosure Obligations – Section 13 Filing if Own More than 5 Percent

- Section 13: Any person that acquires "beneficial ownership" of more than 5 percent of any registered class of a public company's equity securities must report the ownership by filing a Schedule 13D or 13G with the SEC:
  - Schedule 13G: if the acquiror is a U.S. bank, registered broker-dealer, insurance company, registered investment adviser, etc., and the securities were acquired in the ordinary course of business and not with the purpose or effect of changing or influencing the control of the issuer.
    - Must be filed within 45 days after year-end (or, if ownership is more than 10 percent, within 10 days after the end of the month when ownership is more than 10 percent).
  - Schedule 13G can also be filed by any acquiror if its beneficial ownership is less than 20 percent and the securities were *not* acquired with the purpose or effect of changing or influencing the control of the issuer.
    - Must be filed within 10 days after acquisition.
  - Schedule 13D (longer form, disclosing more information) if Schedule 13G is not available.
    - Must be filed within 10 days after acquisition.
    - Schedule 13D disclosure includes the purposes for the securities purchase and any plans or proposals that relate to or would result in an acquisition of additional securities, an extraordinary corporate transaction, a change in the board, etc., and any contracts, arrangements, understandings or relationships with any other persons with respect to any securities of the issuer.
- Schedule 13D Filings receive very close scrutiny by the market.

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Disclosure Obligations – Section 13 Filing if Own More than 5 Percent (cont'd)

- Amendments to Section 13 Filings
  - Once a Section 13 filing is made, amendments must be filed to report certain changes:
    - Amendment to Schedule 13G generally must be filed within 45 calendar days after end of the calendar year if any change to previous filing, except:
      - For U.S. banks, registered broker-dealers, etc., amendment must be filed within 10 calendar days after end of first month in which ownership exceeds 10 percent (and thereafter for increases or decreases by more than 5 percent of class).
      - For other Schedule 13G filers, amendment must be filed "promptly" after ownership exceeds 10 percent (and thereafter promptly after increases or decreases by more than 5 percent of class).
    - Amendment to Schedule 13D must be filed "promptly" after any "material change" (1 percent change in ownership is deemed material).
  - A Schedule 13G filer who ceases to qualify for Schedule 13G (e.g., holding the securities with the purpose or effect of changing or influencing control of the issuer) must file Schedule 13D within 10 days.
  - Note that special rules apply to holders of more than 5 percent of a company that does an IPO. (They become subject to a Schedule 13G, without a requirement for passive intent).

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Disclosure Obligations – Section 13 Filing if Own More than 5 Percent (cont'd)

- "Beneficial Ownership" and "Groups"
  - Beneficial ownership includes any person with an agreement, understanding or relationship giving it the power to vote, direct the vote, sell or direct the sale of the security, and any person with a right to acquire beneficial ownership within 60 days.
  - When two or more persons "agree to act together for the purpose of acquiring, holding, voting or disposing of equity securities," each person is deemed to be the beneficial owner of the equity securities held by each other member of the "group." (Rule 13d-5(b)(1))
  - If the group collectively owns more than 5 percent, each member (or the group jointly) must file a 13D or 13G and report changes, even if that member individually does not own more than 5 percent.

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The Impact of the Tender Offer Rules

- Types of Tender Offers
  - Third Party Equity Tender Offer
  - "Going Private" Transaction
  - Exchange Offer
  - Cross-Border Tender Offer
  - Issuer Self-Tender Offer
  - Debt Tender Offer

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### The Impact of the Tender Offer Rules

- What is a Tender Offer?
  - The Williams Act does not define the term "tender offer."
  - The courts have used two tests to determine whether a series of purchases or offers constitutes a "tender offer" within the meaning of the Williams Act:
    - Eight Factor Test - No single factor dispositive and you need not have all eight factors.
      - active and widespread solicitation of public shareholders;
      - solicitation for a substantial percentage of target's stock;
      - offer made at a premium over the prevailing market price;
      - terms are firm rather than negotiable;
      - offer contingent on the tender of a minimum number of shares;
      - offer open for a limited period of time;
      - offeree subjected to pressure to sell stock; and
      - public announcements precede or accompany rapid accumulation of large amounts of target's stock.
    - Totality of Circumstances Test - Some circuits focus on the totality of the circumstances to determine whether there is a likelihood that, unless Section 14(d) is complied with, there will be a substantial risk that shareholders will lack information needed to make a carefully considered evaluation of the bidder's proposal/offer.
  - Why does it matter whether a bidder or issuer is engaging in a Tender offer?
    - once Tender offer is being made, the relevant regime of SEC rules - e.g., 14D, 13e-4, 15e-3 - must be complied with.

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### The Impact of the Tender Offer Rules (cont'd)

- Exchange Offers
  - Rules now permit third-party exchange offers to commence upon filing of the registration statement. To commence offer early (before effectiveness), the bidder must:
    - file a registration statement including a preliminary prospectus containing all information (including price) necessary to allow holders to make an informed investment decision;
    - disseminate the preliminary prospectus to all security holders; and
    - file a tender offer statement (Schedule TO) with the SEC.
  - Any securities tendered in the offer may not be purchased until after the registration statement becomes effective and the minimum 20 business day tender offer period (from commencement) has expired.

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### The Impact of the Tender Offer Rules (cont'd)

- Minimum & Subsequent Offering Period
  - Rule 14e-1(a) requires that a tender offer be held open to receive tenders for not less than 20 business days from the date it is first published or sent or given to security holders. There is no maximum offering period.
  - Rule 14e-1(d) provides that the only way a bidder may extend its offer is by issuing a public notice of extension, including disclosure of the approximate number of securities tendered to date, no later than 9:00 a.m., Eastern time (or if the class of subject securities is listed on any national securities exchange, the opening of trading on such exchange) on the next business day after the scheduled expiration date of the offer.
  - New Rule 14d-11 permits a bidder to provide an optional subsequent offering period after completion of a tender offer during which security holders may tender their shares without withdrawal rights (similar to extended offering period under U.K. law).
  - Among the requirements for a subsequent offering period:
    - Initial tender offer must be for all outstanding shares.
    - Bidder must announce results of initial offering period (shares tendered) and must accept and promptly pay for all securities tendered during the initial offering period at the closing of such period.
    - The subsequent offering period is at the option of the bidder and, if provided, must be open at least 3 business days and not more than 20 business days. Bidder is not required to state in its initial tender offer whether or not it will provide a subsequent offering period.

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### The Impact of the Tender Offer Rules (cont'd)

- Announcement of a Target's Position
  - "Stop, Look and Listen" Communication - requests that shareholders defer making any determination whether to accept or reject the tender offer until they have been advised of the target company's position with respect to the offer.
  - Rule 14e-2(a) requires the target's Board, no later than 10 business days from date of commencement, to disclose its position with respect to the offer on Schedule 14D-9.
  - This applies whether the tender offer is friendly or hostile. However, it is customary in friendly deals for the target's response to be filed and mailed simultaneously with the bidder's materials.
  - The target board has four options:
    - it may affirmatively recommend acceptance of the offer;
    - it may affirmatively recommend rejection of the offer;
    - it may state that it is expressing no opinion and is remaining neutral; or
    - it may state (if such is the case) that it is unable to take a position.
  - The target is prohibited from making a recommendation or solicitation in response to the commencement of the tender offer unless it files its Schedule 14D-9 on the date of such communication.

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### The Impact of the Tender Offer Rules (cont'd)

- "All holders"/"Best price" Rule – Rule 14d-10
  - "All holders" rule: Tender offer must be open to all security holders of the class of securities subject to the offer.
  - "Best price" rule: The "best price" rule (which provides that consideration paid to any security holder must equal the highest consideration paid to any other security holder) was recently revised by the SEC to resolve conflicting interpretations of the rule by courts, several of which determined that certain non-compete and other executive compensation payments were disguised tender offer consideration that must also be paid to all holders of the shares that were subject to the offer. The new rule:
    - Amends the basic standard: Clarifies that the rule applies only with respect to consideration offered and paid for securities tendered in a tender offer. Specifically, no one may make a tender offer unless "[t]he consideration paid to any security holder pursuant to the tender offer for securities tendered in the tender offer is the highest consideration paid to any other security holder during such tender offer for securities tendered in the tender offer." (blacklining added to show changes in SEC rule).

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### The Impact of the Tender Offer Rules (cont'd)

- "All holders"/"Best price" Rule – Rule 14d-10 (contd)
  - Provides an exemption for compensatory arrangements: Includes a specific exemption from Rule 14d-10 for the negotiation, execution or amendment of an employment compensation, severance or other employee benefit arrangement if the amounts payable under the arrangement relate solely to past or future services or future services to be refrained from and are not based on the number of shares the executive owns or tenders.
  - Provides a safe-harbor for arrangements approved by independent directors: The most practically significant aspect of the amendments is the "safe harbor" provided by new Rule 14d-10(d)(2), which provides a safe-harbor from the best price rule for any compensatory arrangement that is approved by the compensation committee of independent directors of the target, regardless of whether the target is a party to the arrangement; or (if the bidder is a party to the arrangement) approved by the compensation committee of the bidder. In other words, approval by the target's board is sufficient to satisfy the requirements of the safe harbor even if the target is not a party to the compensation arrangement.

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### The Impact of the Tender Offer Rules (cont'd)

- Rule 14d-10 Timing Considerations
  - Defining the time frame of the tender offer:
    - "Tender Offer" is not defined in the Federal securities laws.
    - Date of Commencement - Under Rule 14d-2(a), a tender offer commences for purposes of the Best Price Rule "at 12:01 a.m. on the date when the bidder has first published, sent or given the means to tender to security holders."
    - Under Rule 14e-5, the prohibition on purchases outside the tender offer begins upon public announcement, not commencement.
    - There is no rule that specifies when a tender offer will be deemed to have ended. Although tender offers are required to be kept open for 20 business days under Rule 14e-1, courts have declined to hold that the expiration date constitutes the end of the tender offer for purposes of the Best Price Rule.

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### Tender Offers and Private Equity

- Best price rule reform will lead to increased use of tender offers but PE firms have traditionally not used tenders
- Private equity bidders face special challenges in using tender offers
  - PE firms must provide financing for an offer that doesn't produce enough shares to permit immediate short-form merger (90% in most states)
  - This "bridge financing" poses challenges because margin rules provide that only 50% of value of borrower's stock can be used as collateral
  - Solution is to either use an unsecured bridge loan or put up over 50% of the equity to permit a secured loan
    - For example, in bidding war for Elk, Carlyle proposed to fund more than 50% of the tender with its equity; in hot lending market, may be pressure on banks to offer unsecured bridge

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