Third Quarter 2013

# The Ropes Recap

## Mergers & Acquisition Law News

A quarterly recap of mergers and acquisition law news from the M&A team at Ropes & Gray LLP.

**Contents**

News from the Courts ........ 3
"Liquidity Conflict" Rejected; 28% Stockholder Deemed Not a Controlling Stockholder ....... 3
A Fair Price Can Trump an Unfair Process ........ 4
New York State Judge Rules Kenneth Cole's Go-Private Sound........ 5
Delaware Supreme Court Refuses to Expand Exceptions to Ownership Requirement for Derivative Claims ........ 5
Charter Provision Trips Up Vivendi-Activision Deal ........ 6
WARN Class Action Against PE Firm Survives Motion to Dismiss........ 7
Under Massachusetts Law, Shortening the Limitations Period by Contract Must Allow for the Discovery Rule........ 8
Sirius Wins Motion to Dismiss on Statute of Limitations Grounds in Case Involving an Investment Agreement Prohibiting Adoption of a Poison Pill........ 9
Delaware Legislative Update........ 10
Delaware LLC Act Amended to Provide that Fiduciary Duties Apply Unless LLC Agreement States Otherwise ........ 10
Notable Deals........ 11
New Delaware Tender Offer Rules Put Into Practice........ 11
"Material Favorable Change" Clause in AT&T/Leap Wireless Merger ........ 12
Suitor Appears for BlackBerry ........ 13
Shareholders Approve Dell Deal as Icahn Backs Down ........ 13
"Safe Harbor" of MFW Paves the Way for Others........ 14
Smithfield Transaction Approved by CFIUS and Shareholders........ 14
News from the SEC ........ 15

Impact of Federal Government Shutdown ..... 15
Regulation D Update ..... 15
London Update ..... 16
Shareholder Employees: A New Employment Status ..... 16
Piercing the Corporate Veil: A Clarification of the Law ..... 17
European Cross-Border Mergers: Reorganizations or Transactions With a Cross-Border Element ..... 17
Asia Update ..... 18
Applied Materials and Tokyo Electron Join in a "Merger of Equals" ..... 18
Deal Stat Snapshot ..... 20
Contributors ..... 21

## News from the Courts

**“Liquidity Conflict” Rejected; 28% Stockholder Deemed Not a Controlling Stockholder**

A decision concerning the sale of Morton’s Restaurant Group, Inc. (“Morton’s”) is the most recent case in a line of cases issued by the Delaware Court of Chancery (the “Chancery Court”) that has rejected claims based on allegations that large, non-controlling shareholders wrongfully rushed sales at allegedly inadequately prices in order to gain liquidity. Chancellor Strine, who authored the decision dismissing the action, held that, absent certain “narrow circumstances” not present in the Morton’s case, the economic interests of a large stockholder in a sale transaction are presumptively aligned with the interests of the other holders. Chancellor Strine also found that, absent additional indicia of control, a 28-percent stockholder was not a controlling stockholder for purposes of determining whether the Morton’s board complied with its fiduciary duties in a change-in-control transaction.

Plaintiffs in the Morton’s case alleged that Castle Harlan, Inc. (“Castle Harlan”), a 28-percent stockholder and Morton’s former private equity sponsor, forced the Morton’s board to accept an inadequate price in order to satisfy Castle Harlan’s purported liquidity needs, which were allegedly driven by Castle Harlan’s supposed need to raise capital for a new investment fund. Chancellor Strine found that the plaintiffs had not demonstrated that Castle Harlan either specifically controlled Morton’s extensive nine-month sales process or generally controlled Morton’s.

Rejecting the plaintiffs’ allegation that Castle Harlan was conflicted because of its supposed need for immediate liquidity, Chancellor Strine stated that the extensive nine-month sale process rebutted any allegation that Castle Harlan had forced a “fire sale.” He also rejected the plaintiffs’ theory that starting a new investment fund is a sufficient catalyst to cause a private equity fund stockholder to sell its shares at a sub-optimal price. Accordingly, there was no basis to rebut the presumption that Castle Harlan’s interests were aligned with Morton’s other stockholders.

The Chancery Court also dismissed the plaintiffs’ aiding and abetting claims against Castle Harlan and Morton’s financial advisors, holding that such claims could not be stated absent a viable claim alleging an underlying breach of fiduciary duty.

Chancellor Strine’s holistic analysis of Castle Harlan’s potential control over Morton’s indicates a continued willingness by the Chancery Court to focus on factors outside of a larger stockholder’s ownership stake and analyze other relevant indicia of control. The decision also reinforces the Chancery Court’s willingness to dismiss plaintiffs’ claims when their allegations are contradicted by the public record or assert economically irrational theories. (*In re Morton’s Rest. Grp., Inc. S’holders Litig.*, C.A. No. 7122-CS (Del. Ch. July 23, 2013))

**A Fair Price Can Trump an Unfair Process**

In *In re Trados Incorporated Shareholder Litigation*, Vice Chancellor Laster ruled that a $60 million deal to sell translation software firm Trados Inc. ("Trados") to SDL PLC was fair to common shareholders who challenged the transaction, since their shares retained the same value of zero before and after the sale under the Delaware entire fairness test. The case is of particular interest to venture capital and other investors considering transactions involving distressed companies with preferred shares.

Prior to the transaction that eventually led to the shareholder suit, Trados obtained venture capital funding to support a growth strategy intended to lead to an initial public offering. The venture capital investors received preferred stock and placed representatives on the Trados board. In July 2005, Trados was acquired by SDL PLC for $60 million in cash and stock. Under the terms of the merger, the preferred stockholders received $52.2 million of that amount to satisfy their liquidation preference and management received $7.8 million as part of an existing management incentive plan. The other common stockholders received no consideration in the merger. Plaintiff, a holder of common stock, sued Trados's directors for breach of fiduciary duties, alleging that the directors had structured the merger in a way that benefited the preferred shareholders at the expense of the common shareholders.

The Chancery Court reviewed the transaction under the entire fairness standard (rather than under the deferential business judgment rule) because the plaintiff proved that a majority of the board was either directly or indirectly interested in the merger. The Chancery Court found that the board failed the "fair process prong" of the entire fairness test because the directors did not evaluate the transaction from the perspective of the common shareholders, including failing to consider forming a special committee or obtaining a fairness opinion. Instead, the Chancery Court concluded, the Board was focused on finding exit opportunities for the VC investors.

Nevertheless, the directors were found not liable for breach of fiduciary duty because, although the process was not fair, the zero consideration was the economically fair price, making the merger fair in the Vice Chancellor's estimation. Aided by experts, the defendants proved that the common stock "had no economic value before the [m]erger[.]" As such, the transaction satisfied the "fair price" prong of the entire fairness test because the "common stockholders received in the [m]erger the substantial equivalent in value of what they had before."

The *Trados* opinion highlights a circumstance where an economically fair price can arise despite a questionable process. But it also highlights the high litigation risk created by deals that can be construed as structured solely as "VC exits." In such circumstances, a conflicted board dominated by preferred shareholders would still optimize its defense posture by actively considering the interests of common shareholders and ways in which a robust process may mitigate the conflict, including considering a special committee process, hiring independent legal and financial advisors, and obtaining fairness opinions as appropriate to the circumstances. (*In re Trados Inc. S'Holder Litig.*, C.A. No. 1512-VCL (Del. Ch. Aug. 16, 2013)).

**New York State Judge Rules Kenneth Cole's Go-Private Sound**

In a recent decision concerning the take-private of Kenneth Cole Productions, Inc. ("KCP") by its founder, Kenneth Cole ("Cole"), Justice Marks of the Commercial Division of New York State Supreme Court, New York County, dismissed stockholder plaintiffs' claims regarding the propriety of that transaction and held that the business judgment rule governed such claims, absent a showing of "specific unfair conduct" by the KCP special committee. Justice Marks also held that Cole had not acted improperly because controlling stockholders are allowed to act in their own economic interest so long as their conduct does not constitute unfair self-dealing.

Prior to the transaction, Cole owned 46 percent of KCP's common stock and 89 percent of KCP's voting power due to his ownership of the company's super-voting Class B shares. On February 23, 2012, Cole proposed to take KCP private at $15 per share, which represented a 17-percent premium at that time. The KCP Board immediately formed a special committee to consider that proposal and negotiate with Cole. The parties negotiated until June 6, 2012, when they announced a transaction at $15.25 per share (with a condition requiring approval of the transaction by a majority of the non-Cole public stockholders). Stockholders filed suit, were unable to obtain a preliminary injunction, and commenced a post-closing damages action. Because KCP is a New York corporation, Justice Marks applied New York corporate law to the plaintiffs' claims. He first concluded that an action for breach of fiduciary duty must be pled with particularity and went on to hold that the stockholder plaintiffs had not demonstrated any "particular facts" to show that the KCP directors violated their fiduciary duties. To that end, the opinion states that "absent a showing of specific unfair conduct by the special committee, the Court will not second guess the committee's business decisions in negotiating the terms of a transaction." This result under New York law generally aligns with recent Delaware decisions applying the Business Judgment Rule to challenges of majority stockholder take-private transactions when the minority stockholders are appropriately protected from coercion.

With respect to the stockholders plaintiffs' claims against Cole, Justice Marks ruled that New York law permits controlling stockholders to act in their own economic interest, provided that their conduct does not constitute unfair self-dealing. The Court took no issue with Cole's public statement that he would not support any alternative transaction, and in fact stated that "the ability to resist such a transaction would appear to be one of the benefits of having a controlling position in the company." The opinion also states that Cole was not required to subvert his own economic interests to the minority stockholders' interests in obtaining a higher price. (*In re Kenneth Cole Prods., Inc. S'holder Litig.*, Index No. 650571/2012 (N.Y. Sup. Ct. Sept. 3, 2013)).

**Delaware Supreme Court Refuses to Expand Exceptions to Ownership Requirement for Derivative Claims**

The Delaware Supreme Court assuaged fears of a shift in power favoring the plaintiffs' bar in its recent response to a certified question from the Ninth Circuit relating to Bank of America's

rescue merger of Countrywide Financial in 2008. The Ninth Circuit asked the Delaware Supreme Court to opine the following question of law:

> Whether, under the 'fraud exemption' to Delaware's continuous ownership rule, shareholder plaintiffs may maintain a derivative suit after a merger that divests them of their ownership interest in the corporation on whose behalf they sue by alleging that the merger at issue was necessitated by, and is inseparable from, the alleged fraud that is the subject of their derivative claims.

The answer was that such claims do not survive.

The sole exception to the rule that shareholders' rights to assert derivative breach-of-duty claims terminates with their stock ownership remains, as established in *Lewis v. Anderson*, 477 A.2d 1040 (Del. Apr. 18, 1984), when sham mergers are used specifically for the purpose of terminating liability.

Prior to this ruling, it was feared that a contrary result could have generated a costly shift in the balance of power in which shareholders would have had more leverage in, and incentive to pursue, derivative strike suits against corporate boards. Direct claims, of course, continue to survive a merger. (*Ark. Teacher Ret. Sys. v. Countrywide Fin. Corp.*, No. 14, 2013, 2013 WL 4805725 (Del. Sept. 10, 2013)).

**Charter Provision Trips Up Vivendi-Activision Deal**

Vice Chancellor J. Travis Laster has called a halt to Activision Blizzard, Inc.'s plan to buy back the bulk Vivendi's stake in the company for $5.83 billion, coincident with a purchase of Vivendi's remaining shares by Activision's CEO and its co-chairman for an additional $2.34 billion. When Vivendi initially acquired its stake in 2008, the Activision charter was amended to include a provision requiring that any "merger, business combination or similar transaction" involving Vivendi be approved by "the affirmative vote of a majority in interest of the stockholders" other than Vivendi and its affiliates.

The buy-back deal did not include provision for a shareholder vote. Vivendi argued that the deal did not trigger the charter provision, which in its view was designed to prevent an unfair squeeze-out, not an exit. A group of shareholder sued to enjoin the deal until it received a vote that achieved a majority-of-the-minority. In a result that surprised many commentators (and which Activision and Vivendi lawyers described as a "wreck" for their clients), Vice Chancellor Laster agreed that the deal triggered the provision, which he concluded reasonably encompassed "potentially value-transferring business transactions." (*Hayes v. Activision Blizzard, Inc.*, No. 8885-VCL (Del. Ch. Sept. 18, 2013)(transcript ruling)).

**WARN Class Action Against PE Firm Survives Motion to Dismiss**

The U.S. District Court in the Northern District of Indiana has denied a motion to dismiss a class action suit by an employee against his former employer for an alleged WARN Act violation. The plaintiff's claim arose from the closing of a plastics component manufacturing facility located in Forth Smith, Arkansas, where 91 people were employed. Before the facility shut down its operations, employees received notice of the closing approximately ten days in advance, which did not comply with the WARN Act's requirement for 60 days' notice prior to a mass layoff or plant closing. The plaintiff alleged that not only Fortis Plastics, LLC ("Fortis"), which maintained and operated a number of plastic manufacturing facilities, but also Monomoy Capital Partners L.P. ("Monomoy"), a private equity firm based in New York and the sole owner of Fortis, should be liable for the back wages and benefits to which he was entitled under the WARN Act. Monomoy argued that the plaintiff's complaint failed to allege sufficient facts to state a plausible claim that Monomoy was the plaintiff's employer.

In a case of first impression in the Northern District of Indiana, the key question before the court was whether both Fortis and Monomoy constituted a "single employer" of the employees affected by the Fort Smith facility shutdown. The WARN Act applies to an "employer," defined as "any business enterprise" that employs the requisite number of employees. The parties and the court argued that the court should apply a multi-factor test based on U.S. Department of Labor regulations to determine whether liability should extend to Monomoy.

The court weighed the following five factors applicable under the Department of Labor's regulations: (i) common ownership, (ii) de facto control, (iii) common officers and directors, (iv) unity of personnel policies emanating from a common source, and (v) dependence of operations. The court found support for the first two factors in the plaintiff's allegations, which it determined was sufficient for the case to survive a motion to dismiss. The plaintiff alleged that Fortis was a "wholly owned subsidiary of Monomoy" and that Fortis and Monomoy "directly or indirectly owned the Fort Smith Facility," which the court determined was sufficient to allege common ownership. For the affiliated company to exercise de facto control, a court must determine whether the affiliated company was the decision-maker responsible for the employment practice giving rise to the litigation. The plaintiff alleged that the closing was ordered by Monomoy and Fortis, and that "Fortis and Monomoy jointly made the labor decisions concerning [p]laintiff's employment, including the decision to terminate his employment." Together with similar facts alleged by the plaintiff, the court determined such statements were sufficient to allege Monomoy exercised de facto control over Fortis.

The court determined that the plaintiff's other allegations regarding common officers and directors, unity of personnel policies emanating from a common source and dependency of operations, were only conclusory allegations. Yet, based primarily on the plaintiff's clear factual allegations regarding Monomoy's involvement and exercise of control over Fortis, the court determined that the motion to dismiss by the defendants had to be denied. (*Young v. Fortis Plastics, LLC*, No. 3:12-CV-364 JD CAN (N.D. Ind. Sept. 24, 2013), Docket No. 61.

**Under Massachusetts Law, Shortening the Limitations Period by Contract Must Allow for the Discovery Rule**

The Massachusetts Appeals Court (the "Appeals Court") has overturned a determination by the Massachusetts Superior Court that a plaintiff's complaint was barred by a contractually shortened limitations period.

The plaintiff, trustee of the Hersey Street Properties Realty Trust, retained the defendant, I.E.S. Incorporated, to conduct environmental testing and other services. The contract between the parties included a provision which explicitly provided that the trust would not bring any claim after one year following the date of the contract. The initial complaint, however, was filed more than four years after the parties signed the contract. The plaintiff argued that the defendant's violations did not come to its attention until the Massachusetts Department of Environmental Protection issued a notice of non-compliance more than three years after the contract was executed.

The Appeals Court applied the Massachusetts Supreme Judicial Court's recent decision *Creative Playthings Franchising, Corp. v. Reiser*, 978 N.E.2d 765 (Mass. 2012), which held that as a matter of Massachusetts law, a statutory limitations period can be shortened by contract so long as the period is reasonable. To be reasonable, the Appeals Court found, a contractual limitations provision must permit operation of the discovery rule or it will otherwise be considered invalid and unenforceable. As a result, the Appeals Court vacated summary judgment and remanded the case for further proceedings to determine when the plaintiff should have discovered it was harmed by the defendant's actions.

Although on its face this was a commercial contractual dispute case, the opinion may have ramifications for mergers and acquisitions practitioners. For example, in an acquisition agreement governed by Massachusetts law, a provision that allows for an 18 or 24-month indemnity period to bring claims may not be respected because it does not contemplate the parties' ability to bring claims discovered after the contractually agreed upon period. (*Shahin v. I.E.S. Inc.*, 988 N.E.2d 873 (Mass. App. Ct. 2013)).

**Sirius Wins Motion to Dismiss on Statute of Limitations Grounds in Case Involving an Investment Agreement Prohibiting Adoption of a Poison Pill**

Sirius XM Radio Inc. ("Sirius") was struggling with insufficient cash flow during 2009, when it agreed to issue Liberty Media Corporation ("Liberty Media") preferred stock that was convertible into a 40% equity interest in exchange for $530 million. The investment agreement negotiated in connection with the transaction prohibited Sirius from adopting a poison pill or any charter or bylaw provision to prevent Liberty Media from purchasing additional Sirius stock upon the expiration of the standstill period. When the standstill expired in March 2012, Liberty Media announced that it intended to acquire majority control and began purchasing Sirius stock on the open market. The plaintiffs alleged the Sirius board breached its fiduciary duties by complying with the investment agreement and that Liberty Media breached its fiduciary duties as a controlling stockholder by purchasing shares on the open market without paying a premium to the stockholders.

Chancellor Strine granted the defendants' motion to dismiss because the plaintiffs' complaint was time-barred, as the statute of limitations for breach of fiduciary duty in Delaware is three years. He reasoned that stockholders were on notice since 2009 that Liberty Media would have the opportunity to acquire majority control of Sirius on the open market and unhindered by any defensive mechanisms once the standstill period expired. The Chancellor also rejected plaintiffs' attempts to cast their claim as based on a breach in 2012, saying that the Board's not adopting defensive mechanisms was merely a fulfillment of a contractual duty which became effective in 2009. In focusing on the limitations period, Chancellor Strine notably did not raise any concerns with the board of directors contractually agreeing to waive use of the poison pill in advance. (*In re Sirius XM S'Holder Litig.*, C.A. No. 7800-CS (Del. Ch. Sep. 27, 2013)).

# Delaware Legislative Update

**Delaware LLC Act Amended to Provide that Fiduciary Duties Apply Unless LLC Agreement States Otherwise**

Effective August 1, 2013, the Delaware General Assembly amended Section 18-1104 of the Delaware Limited Liability Company Act. Under the amended provision, unless a company's limited liability company agreement provides otherwise, the managers and controlling members of a Delaware limited liability company owe the same fiduciary duties to the limited liability company and its members that directors and controlling stockholders of a Delaware corporation owe to the corporation and its stockholders. The amendment was prompted by the Delaware Supreme Court's decision last November in *Gatz Properties, LLC v. Auriga Capital Corp.* That case created uncertainty as to whether default fiduciary duties exist in the limited liability company context, as the court declined to express a view on the subject and refused to adopt the Chancery Court's earlier holding in the case that "the Delaware Limited Liability Company Act imposes 'default' fiduciary duties upon LLC managers and controllers unless the parties to the LLC Agreement contract that such duties shall not apply." Despite the amendment, members of a limited liability company remain free in their limited liability company agreements to expand, restrict or eliminate fiduciary duties (other than the implied covenant of good faith and fair dealing, which cannot be eliminated).

## Notable Deals

**New Delaware Tender Offer Rules Put Into Practice**

Paulson & Co. Inc. ("Paulson"), chipmaker Maxim Integrated Products Inc. ("Maxim") and biopharmaceutical company Amgen Inc. ("Amgen") are the first buyers to take advantage of new Section 251(h) ("Section 251(h)") of the Delaware General Corporation Law ("DGCL"). The new statutory provision was used by Paulson to acquire piano maker Steinway Musical Instruments Inc. in a $499 million deal completed on September 19, 2013, making it the first deal to avail itself of Section 251(h). Section 251(h) is also being used by Maxim to acquire Volterra Seminconductor Corp. in a $605 million deal announced on August 15, 2013, and by Amgen to acquire Onyx Pharmaceuticals Inc. in a $10 billion deal announced on August 25, 2013.

As discussed in the *Ropes Recap* from the first quarter of 2013, Section 251(h), which went into effect on August 1, 2013, is intended to facilitate the use of tender-offer structures in the acquisition of public companies by eliminating the need for stockholder approval to complete the second-step, "short-form" merger following the first-step tender or exchange offer. Section 251(h) effectively permits parties to close a transaction immediately after the buyer has acquired a simple majority of the target company's outstanding voting stock.

The prerequisites to taking advantage of Section 251(h) are generally straightforward; but some uncertainty remains regarding the requirement that no party to the merger agreement be an "interested stockholder" as that term is defined in Section 203(c) of the DGCL (a stockholder owning 15 percent or more of the target company). Owners of 15 percent or more of the target company cannot take advantage of Section 251(h), but there is some ambiguity as to whether lock-up agreements with substantial investors signed contemporaneously with the merger agreement would disqualify the merger from Section 251(h).

Paulson and Maxim addressed the "interested stockholder" ambiguity by providing for top-up options as a contingency plan in case Section 251(h) was deemed to not apply, and Maxim also provided for the possibility of a stockholder vote as a further backstop. In contrast to the Paulson and Maxim deals, the Amgen merger agreement does not include contingency plans in the event that Section 251(h) does not apply.

While it remains to be seen how Section 251(h) will be interpreted by the courts (and whether the Delaware legislature will revise Section 251(h) to address the "interested stockholder" ambiguity), Section 251(h) is a positive development for dealmakers and should generally make the use of tender offers a more efficient and cost-effective means of buying a public company.

**"Material Favorable Change" Clause in AT&T/Leap Wireless Merger**

The merger agreement for the acquisition of Leap Wireless International, Inc. ("Leap") by AT&T Inc. ("AT&T"), entered into on July 12, 2013, features an unusual twist on a fiduciary out provision. The term includes a standard "fiduciary out" carve-out permitting the target board to change its recommendation in case it receives a superior acquisition proposal. In addition to the standard term, the Leap deal's "Fiduciary Exception to Change in Recommendation" provision also permits the board to change its recommendation in case of certain material developments in Leap's favor (called "Intervening Events") that would make the transaction no longer an attractive prospect for Leap shareholders, provided that outside counsel has advised the board that it must change its recommendation to comply with its fiduciary duties. However, the provision puts limits on which developments are acceptable grounds for the board to change its recommendation. For example, changes in circumstances that were reasonably foreseeable at the time the agreement was signed, general changes in the industry, or the fact in and of itself, that the company exceeded its financial projections, do not count as Intervening Events. The board cannot change its recommendation on these grounds without breaching the agreement.

As a further limitation on the "Intervening Event" fiduciary out, the Leap merger agreement also provides for an enhanced termination fee if the target board recommends against the transaction on the grounds of an Intervening Event and this leads to termination of the transaction: in the case of an Intervening Event termination, Leap would owe a fee of roughly $71 million to AT&T, while the termination fee is just $46.3 million if the Leap board breaks up the deal in favor of a superior acquisition proposal.

The Leap deal's Intervening Event provision mirrors the "material adverse effect" provisions found in many transaction agreements, which allow the buyer to walk away from a deal in the case of material negative developments but carve out certain categories of developments as unacceptable grounds for the buyer to terminate. However, the Intervening Event provision raises some questions as to whether it impermissibly restricts the board's ability to carry out its fiduciary duties. On its face, the provision would prevent the board from changing its recommendation for the carved out reasons (foreseeable developments, general changes in the industry, etc.) even if the board believes its fiduciary duties would require it to recommend against the deal. In certain other contexts, Delaware courts have permitted boards to contractually limit their future options if the board can gain an advantage for shareholders by agreeing to the restriction. For example, Chancellor Strine indicated in *In re Ancestry.com Inc. S'holder Litig.*, C.A. No. 7988-CS (Del. Ch. Dec. 17, 2013) that a company exploring a sale could, in order to maximize its ultimate sale price, agree to restrictions on the ability of potential bidders to communicate their interest to the company, thus contracting around what would otherwise be the board's duty to make a fully informed recommendation to the company's shareholders on the approval of the ultimate transaction. If courts are willing to uphold the Intervening Event provision, it could prove to be a useful tool for allocating the risk that a deal will become unattractive to the sellers in light of favorable developments.

**Suitor Appears for BlackBerry**

On September 23, 2013, embattled Canadian smartphone maker BlackBerry Limited ("BlackBerry") entered into a letter of intent with Fairfax Financial Holdings Limited ("Fairfax") to sell BlackBerry to Fairfax for $4.7 billion, or $9 per share. The announcement comes after BlackBerry posted a $1 billion loss in the second quarter of 2013 and days after BlackBerry announced its plans to layoff 40 percent of its global workforce.

The letter of intent does not create a binding obligation to enter into a definitive agreement and there are a number of conditions. While a potential deal is not surprising, given BlackBerry's woes, the announcement of a letter of intent with a significant degree of conditionality is unusual, especially given the absence of commitment letters from financing sources.

Canadian law gives the Canadian government the right to review takeovers, and the Investment Canada Act stipulates that foreign takeovers of Canadian companies must provide a net benefit for Canada, a concept that gives the government significant latitude. This may have a cooling effect on other potential bidders and provide an advantage to Fairfax, a Canadian company, which would not be subject to such scrutiny. BlackBerry has lobbied the Canadian government to challenge the applicability of the Investment Canada Act to a potential takeover, but the Canadian government may well have an interest in ensuring that BlackBerry stays under domestic control.

While the letter of intent contains a go-shop provision which allows BlackBerry to seek other buyers, the letter of intent contains an unusual feature: a break-up fee payable by BlackBerry to Fairfax upon certain events. If, during the period ending on November 4, 2013, or at any time six months thereafter, BlackBerry (i) enters into a letter of intent or definitive agreement with a third party, (ii) ceases to negotiate in good faith with Fairfax or (iii) enters into a letter of intent or definitive agreement with a third party that first had discussions with BlackBerry during the period between when the letter of intent was signed and November 4, 2013, BlackBerry is obligated to pay Fairfax a fee equal to $0.30 per share, representing approximately $150 million. Upon execution of a definitive agreement with Fairfax, the break-up fee is increased to $0.50 per share.

**Shareholders Approve Dell Deal as Icahn Backs Down**

In an open letter to shareholders of Dell Inc. ("Dell") released on September 9, 2013, Carl Icahn ("Icahn") abandoned his bid to block the proposed $25 billion acquisition of Dell by founder Michael Dell and Silver Lake Partners ("Silver Lake"). Three days later, Dell's shareholders approved the deal. In connection with the transaction, Dell shareholders will receive $13.75 in cash for each share they hold. In addition, Dell will pay a special cash dividend of 13 cents a share, for total consideration of $13.88 per share in cash. The deal is expected to close in 2014.

Faced with strong opposition from Icahn and from Southeastern Asset Management, Inc., the transaction nearly foundered earlier this summer. Dell initially required that the deal be affirmatively approved by a majority of shareholders unaffiliated with the buyout group. This would have meant that shareholders holding a majority of about 86 percent of Dell's shares would have had to vote yes to approve the acquisition. It was only after Dell and Silver Lake raised their bid from $13.65 to $13.75 per share and promised a special dividend of 13 cents per share that Dell announced that the voting standard would be modified to require approval of the transaction by only a majority of disinterested shares actually voting on the matter. After initially pursuing an appraisal action, Icahn has announced that he will take the deal cash.

The Chancery Court has been a sympathetic forum for Dell's buyout process. In June, Chancellor Strine brushed aside allegations that the Dell board had acted improperly, noting that the process looked "as exotic as pistachio gelato would be in Italy, which is … not an unusual flavor in Italy."

**"Safe Harbor" of MFW Paves the Way for Others**

In last quarter's edition of the *Ropes Recap*, we reported on the Delaware Chancery Court's decision in the case *In re MFW S'holders Litig.*, No. CA 6566-CS (Del. Ch. May 29, 2013), in which Chancellor Strine established a framework for review of controlling shareholder takeovers under the business judgment rule: a fully empowered special committee and an up-front promise of a non-waiveable majority-of-the-minority vote. This structure has caught on quickly, and was used in the latest Dole buyout by Chairman David Murdock. The transaction has already triggered litigation, and is likely to produce an opinion that will lay out more detail about what is entailed in having a "fully empowered" special committee.

**Smithfield Transaction Approved by CFIUS and Shareholders**

On September 6, 2013, the Committee on Foreign Investment in the United States (CFIUS) cleared the sale of Smithfield Foods Inc. ("Smithfield") to Shuanghui International Holdings Limited. On September 24, 2013, Smithfield's shareholders approved the deal.

# News from the SEC

## Impact of Federal Government Shutdown

As of the time of the release of this edition of the *Ropes Recap*, the Securities and Exchange Commission ("SEC") was open and in operation, notwithstanding the federal government shutdown. Any changes to the SEC's operation status will be announced on its website.

The SEC has acknowledged that the ongoing uncertainty surrounding the federal governmental shutdown has raised concern for registrants that are planning to request acceleration of their registration statements in the near future, and has indicated that, if a change in its operating status becomes imminent, it will provide as much advance notice as possible and consider granting requests for acceleration of the effective date of pending registration statements.

## Regulation D Update

Section 201(a)(1) of the Jumpstart Our Business Startups Act ("JOBS Act") directed the SEC to permit general solicitation for Rule 506 offerings, provided that sales are limited to accredited investors. On July 10, 2013, the SEC adopted a final rule permitting general solicitation and general advertising, provided the issuer takes "reasonable steps to verify" that their eventual purchasers qualify as accredited investors under Rule 501 of Regulation D. The "reasonable steps" will be evaluated on an objective standard that takes into account the facts and circumstances of the particular investment.

In response to public comments on the draft rule, the SEC provided a non-exclusive list of methods by which issuers may satisfy the "reasonable steps" requirement. These include income verification, such as reviewing copies of an IRS form representing the purchaser's income in conjunction with a representation that sufficient income is also likely to be earned in the current year; net worth verification; and third-party verification, which consists of obtaining written confirmation from such party as a registered broker-dealer, SEC-registered investment adviser, licensed attorney, or certified public accountant that the issuer has taken reasonable steps to verify the purchaser's status.

Additionally, the SEC has modified Rule 144A to permit general solicitation, provided that sales are made only to those whom the seller reasonably believes to be Qualified Institutional Buyers ("QIBs").

Those considering private placements in non-U.S. jurisdictions should be mindful of other countries' regulations, as many still prohibit general solicitations, including those on non-restricted websites accessible to non-U.S. investors.

## London Update

**Shareholder Employees: A New Employment Status**

The introduction of the new employment status of "employee shareholder" is one of a number of measures introduced by the UK Government as part of its broader proposals to promote and facilitate employee ownership of companies. This new regime came into force on September 1, 2013. The initiative is designed to encourage employees to become direct shareholders in their employer company. In order to reflect the shift in emphasis from pure employee to employee-owner, employees will agree to waive certain key statutory employment rights in exchange for an issue of shares in their employer (or in a parent company of their employer).

To achieve "employee shareholder" status:

(a) An employee (or prospective employee) and employer must reach agreement that an employee is to have employee shareholder status (which will require compliance with certain key procedural steps);

(b) The employee will agree to waive his entitlement to certain of his statutory employment rights (including his rights as regards unfair dismissal and entitlement to redundancy pay);

(c) In exchange for the waiver, the employee must receive shares that have a value of at least £2,000 in either the employer company or in a parent company of the employer company; and

(d) The employee must give no further consideration for the issue of the shares.

The new regime confers certain tax advantages upon employee shareholders: most notably, individuals may receive favorable capital gains tax treatment upon a disposal of shares that had a value of up to £50,000 upon issue.

The new regime has received some negative attention in the press. The perceived risk for employees is that they forego significant employment protections in exchange for a shareholding that may not gain in value. In addition, the practicalities and potential costs associated with implementing these measures for a large number of employees may discourage employers from offering this new status as a general practice. This said, the scope for sheltering significant capital gains is not to be ignored. Some companies have already implemented employee shareholder arrangements since the new regime came into force and it is anticipated that further companies may want to explore the possibility of using this new regime as part of their employee incentive arrangements.

**Piercing the Corporate Veil: A Clarification of the Law**

As a matter of English law, a company has a separate legal personality to that of its members. A company is able to own property, it can enter into contractual arrangements with other parties, and it may have its own legal rights and obligations that are separate to those of its members. There are a number of circumstances in which those dealing with a company or with its members may wish to disregard this separate personality and to deal with the company's property, obligations and responsibilities, as if they could be attributed to the controlling member of the company. This process is referred to as "piercing the corporate veil." It runs directly counter to the basic company law principle of corporate separate personality and, until recently, the precise circumstances in which the English Courts were prepared to recognise a power to pierce the corporate veil was unclear.

In the recent case of *Prest v Petrodel Resources Ltd* [2013] UKSC, the English Supreme Court has clarified the law. It held that a power to "pierce the corporate veil" does exist, but that it will only be recognised in one limited circumstance. Where an individual seeks to evade obligations to which he is subject by interposing a company which he controls between himself and the party that is seeking to rely on and/or otherwise assert or enforce these obligations, the English Courts may be prepared to pierce the corporate veil and allow the other party to disregard the corporate separate personality of the company.

**European Cross-Border Mergers:**
**Reorganizations or Transactions With a Cross-Border Element**

The European cross-border merger regime permits a company established in one EEA state to merge with a company established in another EEA state. The regime can be of assistance in the context of both group reorganizations that have a cross-border element as well as for cross-border transactions. In broad terms, three different types of merger may be implemented under this regime:

(a) ***merger by absorption***: where a company formed and registered in one EEA state is absorbed by a company formed and registered in another EEA state;

(b) ***merger by absorption of a wholly owned subsidiary***: where a parent company formed and registered in one EEA state absorbs a subsidiary that is located in another EEA state; and

(c) ***merger by formation of a new company***: where two (or more) companies from at least two different EEA states are absorbed into a third company formed and registered in an EEA state.

This regime has now been in place for a few years, and is becoming more common as parties become more comfortable with using it as a useful tool for implementing internal group reorganisations as well as for genuine third party mergers that have a cross-border element.

# Asia Update

## Applied Materials and Tokyo Electron Join in a "Merger of Equals"

### Transaction Overview

On September 24, 2013, Applied Materials Inc. ("Applied Materials"), the number one chipmaking-equipment company in the world in terms of sales, announced that it will acquire Tokyo Electron Limited ("Tokyo Electron"), the number three company, for over $9 billion. The deal, if and when it closes, will be the second-largest foreign purchase of a Japanese company in history. The merger will create a new company with a combined stock market value of $29 billion. Post-close, Tokyo Electron shareholders will own about 32% of the new company and Applied Materials stockholders will own about 68%. The two companies will merge into a new company which will be incorporated in the Netherlands and listed on Nasdaq and the Tokyo Stock Exchange.

In the chip manufacturing space, the deal has been described as a bold move that will (i) increase Applied Materials and Tokyo Electron's leverage with their customers, (ii) provide cost savings of $500 million in three years, and (iii) create tax savings for both companies due to the reincorporation in the Netherlands. The markets have reflected this positive news, with the stock value of both companies increasing after the announcement.

The deal is scheduled to close in the second half of 2014, after receiving antitrust clearance.

### Promising Japanese Environment

In addition to the deal's size and impact on the industry, analysts have noted the merger due to the rarity of a foreign takeover of a Japanese company. This sense of rarity may not last, as the deal value of Japanese inbound M&A deals has steadily increased, from $9.5 billion in 2011 to $10.0 billion in 2012 to $11.7 billion in the first three quarters of 2013 alone. In addition to the Applied Materials/Tokyo Electron deal, KKR & Co. announced on September 27, 2013 that it would acquire Panasonic Corporation's healthcare unit for $1.7 billion. Investors and Japanese companies seem to be successfully overcoming historic obstacles to foreign takeover deals, including the presumption of incompatible corporate cultures, a perception that selling to a foreign entity would result in employee layoffs, and a perception that foreign entities value shareholder rights too much and stable employment and company health too little.

To pull off what is described by some as a "landmark free-trade deal," Applied Materials and Tokyo Electron appear to have put those traditional reasons for resistance to rest by being extremely sensitive in the public characterization of the transaction. Although Applied Materials is valued at more than double Tokyo Electron, the transaction is described by the companies' executives as a "business combination transaction" and not an acquisition, with Tokyo Electron

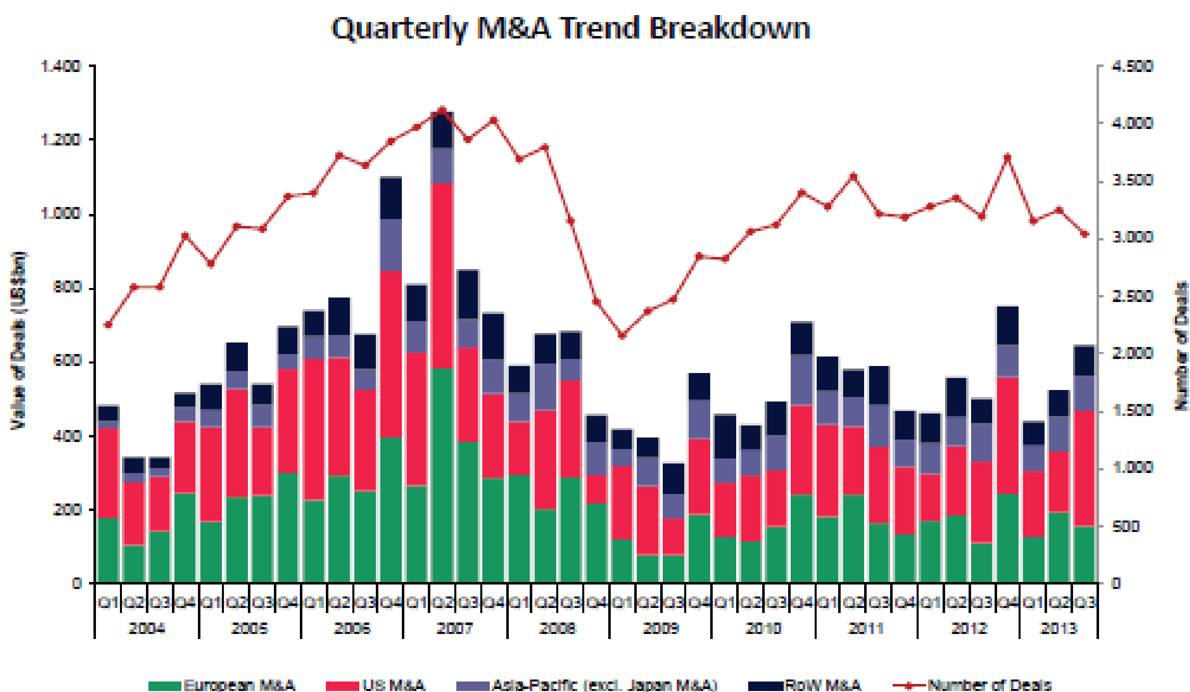
CEO Tetsuro Higashi and Applied Materials CEO Gary Dickerson jointly calling it "a merger of equals" in press releases.

And the parties have taken other steps to show themselves to be on equal footing. The new company will have two headquarters—one in Santa Clara, California, and one in Tokyo. The new company's board will be made up of equal numbers of Applied Materials and Tokyo Electron appointees, plus one mutual appointee. Mr. Dickerson will move to Tokyo to serve as the CEO, with Mr. Higashi serving as the new company's chairman. Finally, the reincorporation will be in the Netherlands, rather than either the United States or Japan.

Japanese outbound deals in Q3 of 2013 also show promise, rising to $21.2 billion, up from $7.3 billion in Q2 of 2013. Though outbound deals in the first half of 2013 suffered due to the weakened yen, the numbers in the third quarter makes it clear it remains to be seen how long the market will be dampened.

Analysts have noted the fact that Tokyo Electron was in good economic shape before the announcement, with a solid balance sheet and profit margins. This indicates that the deal was struck in a spirit not of distress, but of growth. The size and promise of the Applied Materials/Tokyo Electron deal, followed by the KKR & Co./Panasonic Corporation announcement, creates a great deal of excitement and optimism in the Japanese M&A market.

# Deal Stat Snapshot




- Global M&A in Q1 – Q3 was valued at US$ 1,606.7bn which represented a 5.5% increase compared to Q1 – Q3 2012 (US$ 1,522.8bn). Global M&A has increased gradually for the last three years and 2013 is on target to continue the trend and potentially see the highest total since 2008 (US$ 2,407.6bn)

- Growing boardroom confidence has been reflected in consistent quarterly increases in M&A value during 2013. Q3 (US$ 643.8bn) was up 22.7% on Q2 (US$ 524.6bn) and 46.9% higher than Q1 (US$ 438.3bn)

- Q3 2013 also rebounded 28.1% from Q3 2012 (US$ 502.5bn) thanks to post-summer deal announcements in September (US$ 285.4bn), the highest valued month so far this year (previous highest month was December valued at US$ 286.3bn)

- Both the US and Europe registered deal values in Q1 – Q3 2013 that were above Q1 – Q3 2012 – the US (US$ 654.5bn) accounted for a 40.7% market share of global M&A followed by Europe (US$ 478.7bn) with 29.8%

Source: Mergermarket, Q1-Q3 2013 Report (available at www.mergermarket.com).

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