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Deal Points

The Newsletter of the Mergers and Acquisitions Committee

FROM THE CHAIR Mark Morton

Before you depart this week for our Spring meeting in the city by the bay, please take a moment to read this issue of Deal Points. In addition to great content, you will find helpful reports from each subcommittee and task force and a complete schedule for our meetings this week. If you are unable to join us in San Francisco, consider participating by phone. Dial in information is set forth at the end of Deal Points. Finally, if you have not purchased tickets yet for our Committee dinner, please plan to do so when you arrive and register at the ABA desk as we still have seats available.

Once again, we are fortunate to have Practical Law/Thompson Reuters as our sponsor - this time for our dinner Saturday at One Market. If you meet a member of the Practical Law/Thompson Reuters team during your stay in San Francisco, please thank them for their generous support.

Full Committee Meeting

Our full Committee will meet on Saturday from 3:00 to 5:00 pm. During the meeting, we will have a number of presenters, including Alex Tsarnas of SRS Acquiom, who will discuss how M&A escrows are being affected by changing banking regulations. In addition, as chair of our newest task force, Leigh Walton will report on the next steps for the Private Company Target Model Merger Agreement Task Force. The PCTMMA Task Force will have its first meeting at the fall meeting in Chicago, but Leigh is already looking to enlist volunteers so please reach out to her if you are interested.

Task Force and Subcommittee Meetings

In San Francisco, our Task Forces and Subcommittees will host a number of substantive programs and discussions. On Friday afternoon, our Women in M&A Task Force is co-sponsoring a program (with a reception to follow). I hope to see many of you at the program and reception. Please see all the subcommittee and task force reports in this issue of Deal Points for a full list of meeting times and locations.

Planning for Chicago

As a reminder, we will be heading to Chicago this fall for our fall meeting. Details to follow, but mark your calendars now. Our meetings will be held from Friday, September 18th to Saturday, September 19th.

Incoming Chair

As I sat down this week to write my report, I was reminded how quickly three years can fly by. Our meeting in Chicago, for which planning is already well underway, will be my last one to Chair. In order to allow our next Chair an opportunity to participate in the planning effort, I recently asked Scott Whittaker to agree to serve as the Committee's next Chair. I am pleased to report that Scott has agreed, effective at the conclusion of the Chicago meeting, to become the Committee's Chair. For many years Scott has been an active member and leader of our Committee, including serving as Chair of the M&A Jurisprudence Subcommittee and, most recently, as Vice Chair of the M&A Committee. Scott will do a great job as Chair and I look forward to working with him. If you see Scott, please congratulate him.

If you have any questions concerning our upcoming meetings, please email or call me. I look forward to seeing all of you. - Mark Morton, Chair

FROM THE CO-EDITORS Eric S. Klinger-Wilensky and Ryan D. Thomas

> The loveliness of Wilmington seems somehow sadly gay
> The glory that was Nashville is of another day
> I've been terribly alone and forgotten in Manhattan
> I'm going home to my city by the bay.

Actually, Wilmington and Nashville are terrific, but we couldn't resist a Tony Bennett reference as we get ready to head to San Francisco. Don't hate us if we've given you an earworm as you read this edition of ***Deal Points***.

As we continue to update ***Deal Points***, we are happy to introduce a new feature (or, better said, an expanded feature). John Clifford, the author of Deal People, had the terrific idea of profiling both a long-term and a new member in each issue of ***Deal Points***. Thank you, John! New member Jim Black is profiled in this edition, along with long-standing member Tracy Bradley. Although Jim will not be in San Francisco, we welcome him to the Committee.

There are not many perks that come with the job of editing ***Deal Points***. But we will now take advantage of one of them. With this big stage, we leave you with two thoughts as winter gives way to spring. Let's go Mets and Let's go Red Sox! See you and them in the fall.

Contents

Feature Articles

New Regulations Will Shake Up the M&A Escrow Landscape 3

Proposed Amendments to Delaware Appraisal Statute Attempt to Curb, Not End, Appraisal Arbitrage 5

Task Force Reports

Joint Task Force on Governance Issues in Business Combinations 7

Task Force on Financial Advisors 7

Task Force on Legal Project Management 8

Task Force on Two-Step Auctions 8

Task Force on Women In Mergers And Acquisitions 8

Task Force on The Revised Model Asset Purchase Agreement 9

Task Force on The Revised Model Stock Purchase Agreement 9

Joint Task Force on M&A Litigation 9

Task Force on A Private Company Target Merger Agreement 10

Subcommittee Reports

Acquisitions of Public Companies Subcommittee 10

International M&A Subcommittee 11

Membership Subcommittee 11

M&A Jurisprudence Subcommittee 12

M&A Market Trends Subcommittee 13

Private Equity M&A Subcommittee 13

Deal People 14

Committee Meeting Materials 16

maintaining higher levels of liquidity, and compliance costs are likely to increase. This combination of factors is likely to result in additional downward pressure on the already very low yields available. Escrow banks will likely charge higher escrow administration fees and limit or eliminate fee waivers since their earnings from placing escrows into money market funds will be constrained or non-existent.

The result is that institutional money market funds, which in the past fit the typical investment criteria for most M&A escrows, are unlikely to satisfy the needs of many future transactions.

Flight to U.S. Treasury Funds?

If bank deposits and money market funds no longer meet the investment criteria required for M&A escrows, parties might look to Treasury funds as an alternative. The primary issue with investing in Treasury funds is that demand may greatly exceed supply as large sums of money (not just those related to M&A escrows) are expected to move into Treasury products. Indeed, some government-backed money funds were closed to new clients during the 2008 financial crisis due to the imbalance resulting from too much demand for too few eligible investments. Gross portfolio yields (not counting fees) neared zero.

Treasury funds are exempt from the floating NAV rules discussed above but are subject to the new rules regarding redemption limits and liquidity fees that the funds' boards may enforce during market duress. As a result, Treasury funds also might not be a suitable solution for many M&A escrows.

New Solutions Needed

In light of the regulatory changes outlined here, historical alternatives for M&A escrow accounts are unlikely to remain viable in many instances going forward. The fundamental reasons for choosing these alternatives for M&A escrows – principal protection and liquidity when needed – can no longer be assured, especially for escrows with maturities beyond 2015.

Attorneys and their clients should fully understand the changes underway and carefully consider their investment options. They will need to reevaluate which investment options will meet their objectives over the entire escrow period rather than simply considering whether it seems to work at the time of closing. They will need to carefully consider alternatives, including solutions not previously utilized.

Proposed Amendments to Delaware Appraisal Statute Attempt to Curb, Not End, Appraisal Arbitrage

Nicholas D. Mozal[1]

When a corporation is acquired for cash in a merger, Delaware, the corporate home of many public companies, generally provides stockholders with appraisal rights. Appraisal allows dissenting stockholders who comply with the requirements set forth in Section 262 of the Delaware General Corporation Law to seek a judicial determination of the "fair value" of their shares. Since 2004, the number of appraisal petitions has increased markedly. Although some petitions are filed by smaller stockholders who seek to extract the nuisance value of their holdings, a more notable trend has been the rapid spike in petitions filed by so-called "appraisal arbitragers." Appraisal arbitrage typically involves investment funds purchasing shares after a merger is announced with the goal of pursuing an appraisal action and a ruling that the "fair value" is above the merger price.

Opponents of appraisal arbitrage have argued for changes that would dramatically curtail this practice. The proposed amendments currently before the Delaware legislature, however, touch upon but do not directly address the practice. Specifically, the amendments contain two changes: one that would reduce the pre-judgment interest corporations pay to petitioners, and another that would require the dismissal of smaller petitions.

Since 2007, interest on appraisal petitions accrues at 5% over the Federal Reserve discount rate from the effective date of the merger through the entry of judgment. Designed to compensate stockholders for having their capital stuck in the post-merger entity, many believe this change contributed to the growth of appraisal arbitrage by guaranteeing a significant rate of return. The proposed amendments would allow corporations to pay cash to petitioners, "[a]t any time before the entry of judgment in the proceedings." After the payment, interest will continue to accrue at the statutory rate only on the difference between the amount paid and the fair value determined by the Court of Chancery. This change would reduce the settlement leverage of appraisal petitioners previously armed with the knowledge that their claim would be more valuable in the future.

Importantly for corporations responding to appraisal petitions, the bill's synopsis provides that such a payment would not result in an inference that the amount paid "is equal to, greater than, or less than the fair value of the shares to be appraised." Corporations thus need not worry that a payment would be used as evidence of fair value in the appraisal proceeding.

The second proposal would impose a *de minimis* requirement on appraisal petitions for stock listed on a national securities exchange. If enacted, the Court of Chancery would be required to dismiss appraisal petitions where less than 1% of the outstanding shares of the class or series entitled to appraisal actually perfect their appraisal rights, and, "the value of the consideration provided in the merger or consolidation"

1 Mr. Mozal is an associate at Ross Aronstam & Moritz LLP. The views expressed in this article are not necessarily those of Ross Aronstam & Moritz LLP or its clients.

for the shares with perfected appraisal rights was less than $1 million. These provisions would not apply to certain short-form mergers under Sections 253 and 267 of the DGCL. The bill's synopsis states that this proposal would minimize the risk that an appraisal petition "will be used to achieve a settlement because of the nuisance value of discovery and other burdens of litigation."

Whereas the proposed amendment relating to the accrual of interest would affect the incentives of every stockholder in evaluating whether to bring an appraisal petition, the *de minimis* requirement is unlikely to significantly affect appraisal arbitrage. Data collected by Professor Charles R. Korsmo of the Case Western Reserve University School of Law and Professor Minor Myers of the Brooklyn Law School indicates that the mean value of appraisal disputes between 2004 and 2013 was approximately $30 million. The professors also identify numerous appraisal arbitrage funds that file petitions valued in the millions of dollars, so these funds should meet the requirement. Consequently, the *de minimis* requirement will not deter the most frequent arbitragers from continuing their practice.

Notably, the proposed amendments come in the wake of two recent decisions by the Court of Chancery that refused to heighten standing requirements on appraisal petitioners.[2] Although opponents of appraisal arbitrage urged the Delaware legislature to impose the stricter standing requirements rejected in those decisions, the proposed amendments do not address the issue.

Overall, the proposed amendments are unlikely to radically change the existing practice of appraisal arbitrage. At most, they would curb incentives for arbitrage to a limited extent. And if adopted, the amendments would not affect existing petitions or pending transactions, as they would apply only to transactions consummated on or after August 1, 2015.

2 *See In re Appraisal of Ancestry.com, Inc.*, 2015 WL 66825 (Del. Ch. Jan. 5, 2015); *Merion Capital LP v. BMC Software, Inc.*, 2015 WL 67586 (Del. Ch. Jan. 5, 2015).