FROM THE CHAIR

By Richard E. Climan

I’m expecting a sizable turnout at the Business Law Section’s Spring Meeting in Los Angeles on April 3-6, 2003. Our full Committee meeting will be held at 2:30 p.m. on Saturday, April 5th. The meeting will be preceded by separate task force meetings throughout the day Friday and on Saturday morning.

At 3:30 p.m. on Saturday, April 5th, immediately following our full Committee meeting, Leigh Walton and Joel Greenberg will present a Committee Forum program entitled The Impact of Sarbanes-Oxley on M&A. Our Committee is co-sponsoring three other programs at the Spring Meeting: Training Lawyers and Law Students How to Do Deals (featuring one of our Vice Chairs, Byron Egan, as a panelist); Acquisition of a European Company by a United States Buyer (featuring John Leopold as moderator and David Katz as a panelist); and Joint Ventures: In the Antitrust Gunsights Again?

Our Committee cocktail reception and dinner will take place Saturday evening at the Penthouse of The Regency Club on Wilshire Boulevard. Please submit your registration form if you have not already done so. Many thanks to Neal Brockmeyer for organizing this event.
Our summer meeting this year will be held in San Francisco in conjunction with the ABA’s Annual Meeting in early August. We will hold our Fall stand-alone meeting either in Chicago or in Toronto, in October or early November. I will be canvassing Committee members at our April meeting to get a sampling of views on the preferred location for the stand-alone meeting.

We held our 2002 stand-alone meeting in Paris this past October. This was the first meeting of our Committee ever held outside North America, and it was a resounding success. Committee members from a dozen countries participated in the meeting and related festivities. Special thanks to Reid Feldman, Guy Weijer and Nat Doliner for their extraordinary contributions to this memorable event.

In conjunction with our Paris meeting, the Committee presented the first International Institute on Mergers & Acquisitions, featuring speakers from leading European law firms and global investment banks, as well as a number of members of our Committee – John Leopold, Guy Weijer, Nat Doliner, Reid Feldman, Joel Greenberg, David Katz, Henry Lesser, Daniel Rosenberg and Leigh Walton. At the conclusion of our Committee meeting, David Katz moderated a very informative program on M&A developments in France, featuring a French lawyer and a French investment banker.

In November 2002, a number of Committee members spoke at the ABA’s Seventh Annual National Institute on Negotiating Business Acquisitions in Chicago. Participating Committee members included Nat Doliner, Vince Garrity, David Albin, Byron Egan, Diane Frankle, Joel Greenberg, Robert Harper, Jon Hirschoff, David Katz, Donald McKenzie, Robert Shields, Larry Tafe, Leigh Walton and Alison Youngman. The National Institute continues to serve as an excellent showcase for the work of our Committee.

As reported elsewhere in this issue of Deal Points, two of the Committee’s task forces held their own stand-alone meetings over the winter. The Task Force on Acquisitions of Public Companies met in Wilmington in January, and sponsored a lively roundtable discussion with several distinguished Delaware jurists (organized by Diane Frankle and Mark Morton). Also in January, the Model Stock Purchase Agreement Task Force and related working groups met in Dallas.

Our Committee continues to grow, both in its size and in its diversity. We now have over 800 members from 45 different states and 23 different countries. I am pleased to report that Wilson Chu will be taking over as Chair of our Membership Subcommittee, replacing Alison Youngman who has served tirelessly in that role for a number of years. Thank you, Alison, for your superb efforts in that capacity. (Fortunately, Alison will remain a member of the Membership Subcommittee and intends to continue her active involvement in our Committee’s membership activities.) Wilson and I are seeking volunteers to join the Membership Subcommittee and assist in the process of identifying and integrating new Committee members. Please contact Wilson or me if you are interested in serving on this subcommittee.

Our newest task force, chaired by David Katz, will be producing a “Dealmakers’ Dictionary” – a comprehensive glossary of M&A terms – for publication in 2004. The task force’s inaugural report appears elsewhere in this issue of Deal Points.

See you in Los Angeles.
The following article is part of an edited transcript from a panel presentation for the Committee Forum of the Committee on Negotiated Acquisitions held in Washington, D.C. on August 12, 2002 at the Annual Meeting of the American Bar Association. The program, entitled “So what does THAT mean? Interpreting Preferred Stock Terms in the Negotiated Acquisition,” included the following panelists:

- Mark A. Morton (moderator) – Partner in the Corporate Group of Potter Anderson & Corroon LLP, Wilmington, Delaware
- Diane H. Frankle – Partner in the Palo Alto office of Gray Cary Ware & Freidenrich LLP, Co-Chair of the firm’s Mergers & Acquisitions Group and Co-Chair of the Task Force on Acquisitions of Public Companies of the Committee on Negotiated Acquisitions
- John F. Grossbauer – Partner in the Corporate Group of Potter Anderson & Corroon LLP, Wilmington, Delaware
- David A. Bronner – Partner in the Chicago office of Jenner & Block and Chair of the firm’s Mergers & Acquisition Practice
- Patricia O. Vella – Associate, Morris Nichols Arsht & Tunnell, Wilmington, Delaware

* * *

After discussing the principles to be applied to the construction of preferred stock terms and the relevant case law addressing the voting rights of preferred stock, particularly in the merger context, the panel discussed the so-called “deemed liquidation” provisions that are commonly found in preferred stock designations. The hypothetical considered by the panel included a series of preferred stock with the following “deemed liquidation” provision, which stated that certain events shall be included within the definition of liquidation and shall entitle the holders of preferred stock to be paid their liquidation preference of $50 million:

A Deemed Liquidation shall include any consolidation or merger of the Corporation with or into any other corporation or other entity, or any other corporate reorganization, in which the stockholders of the Corporation immediately prior to such consolidation, merger or reorganization, own less than 50% of the surviving entity’s voting power immediately after such consolidation, merger or reorganization, or any transaction or series of related transactions in which in excess of 50% of the Corporation’s voting power is transferred.¹

Morton: A deemed liquidation clause is a provision that sets forth a number of triggers that will result in the payment of the liquidation preference. The hypothetical provides that a merger or consolidation where, after the transaction, the stockholders hold less than 50% of the surviving company, will be deemed to be a liquidation. On their face, such provisions seem pretty straightforward. Diane, why do investors even negotiate for these provisions in the first place?

Frankle: A deemed liquidation clause is, as most of you know, a very typical provision. The investors in a transaction that are putting money in are going to want to be very clear in their minds as to what kind of a return they get, not just in a true liquidation of the

¹ The full text of the hypothetical, as well as copies of the other materials that were distributed at the Committee Forum in connection with the presentation may be obtained by contacting Mark Morton, the editor of this publication, at mmorton@potteranderson.com.
company but on certain exits and, most importantly, on some kind of change of control transaction like a merger. In that event, the investors want to make sure that they are going to take out a defined return before the holders of common stock. They negotiate for that right and it is quite typical to see it in this kind of a provision. In fact, with the terms getting tougher and tougher in equity financing these days, it is not even just a defined return of one to four times the initial investment. Quite often these days it is also either a partial or a full participation beyond that return to allow the investors to sit at the table with the holders of common stock and take their pro rata share. The point is that the investors negotiate this provision in order to be sure that they get their desired return in the event of an “exit” before the holders of common stock.

Morton: John, is a deemed liquidation clause something new? Or is it something that’s been around for a while?

Grossbauer: Well, I have been doing this for about fifteen years and deemed liquidation provisions have been around the whole time. In the late eighties we reviewed a lot of liquidation provisions. Then, in the early nineties, with things dying down in the economy, we didn’t see a lot of them. We started seeing a lot of them again three or four years ago. We are seeing more and more of them now, in part because people have had to start to actually deal with them and figure out how the mechanics work.

Morton: David, is the provision in the hypothetical the kind of provision that you see in your practice, or are they even broader than this one?

Bronner: I do see provisions like this one, but I also see them drafted in an even broader fashion. After a certain point in time, private equity players want to have a clear exit strategy. A deemed liquidation provision enables them to cash out when certain transactions occur or at least gives them leverage to renegotiate their transaction when the organic change to the company occurs. There is an example of a deemed liquidation provision that illustrates this
point in the appendix.\(^2\) This provision triggers in the event of either a “fundamental change,” which is designed to cover transactions not involving stock, or a “change of control,” which by its terms covers transactions involving the company’s stock. At first blush, these definitions appear to cover the full gamut of possible transactions.

\(^2\) The deemed liquidation provision in the appendix provided:

So long as any shares of Series A Convertible Preferred Stock are outstanding, then unless waived in writing by the holders of at least a majority of the shares of Series A Convertible Preferred Stock outstanding, a Fundamental Change or Change of Control shall be deemed a Liquidating Event within the meaning of Section 8(a) above. The term “Fundamental Change” shall mean a reorganization, consolidation or any other transaction of a similar nature in which the Corporation is a party (except any reorganization, consolidation or other transaction where, after giving effect thereto, the holders of the Corporation’s outstanding capital stock (on a fully diluted basis) immediately prior to such reorganization, consolidation or other transaction will own immediately following such reorganization, consolidation or other transaction outstanding capital stock of the surviving entity (on a fully diluted basis) possessing the voting power under ordinary circumstances (without regard to any agreements among holders of capital stock of the Corporation regarding the election of the Corporation’s Board of Directors) to elect a majority of such surviving entity’s Board of Directors). The term “Change of Control” shall mean any sale, transfer, issuance or redemption or series of sales, transfers, issuances or redemptions (or any combination thereof) of shares of the Corporation’s capital stock by the holders thereof or the Corporation which results in any person or entity group of affiliated persons or entities other than the owners of the Corporation’s capital stock (on a fully diluted basis) immediately prior to such transaction or series of transactions or their Permitted Transferees (as defined in the Shareholders Agreement) owning capital stock of the Corporation possessing the voting power under ordinary circumstances (without regard to any agreements among holders of capital stock of the Corporation regarding the election of the Corporation’s Board of Directors) to elect a majority of the Corporation’s Board of Directors. Upon the grant of a waiver, the Fundamental Change or Change of Control shall not be deemed to be a Liquidating Event within the meaning of Section 8(a) above.

However, after reading the cases, I think that even this provision may have its problems. First, it does not specifically state that a sale of assets is, in fact, a fundamental change. And, second, Mark tells me that one of the terms used in the definition of “fundamental change” is not a term of art for Delaware law purposes.

**Morton:** David, there’s a drafting lesson here. When you look at the provision in the appendix that you referenced, it provides that a “reorganization” is a trigger under the definition of “fundamental change.” The drafter made every effort to have the definition cover every conceivable transaction under the sun. However, “reorganization” is not a term that is defined by the General Corporation Law of Delaware. And the few cases that have considered the meaning of the term have thrown up their hands and conceded that there’s no commonly accepted meaning for the term. So, the cautionary note here is that the drafter needs to think about the words being used and consider whether those words actually give the court the tools it will need to resolve an interpretational dispute. Sometimes, even the broadest provisions are subject to interpretational debates.

**John,** let’s turn back to the deemed liquidation provision in the hypothetical. In some respects, this provision seems straightforward. For example, it provides that a merger of equals where the stockholders prior to the merger only own 45% of the stock of the entity following the merger will be a “deemed liquidation.” In that case, John, the holders of the preferred stock would get paid their liquidation preference, right? Where do people go wrong with these provisions? What’s the problem?

**Grossbauer:** Most plain vanilla deemed liquidation provisions start by providing that the company’s assets will get distributed to stockholders when there is a liquidation of the company. In many cases (including our hypothetical), the drafters add a paragraph at the end of the section that says a consolidation or
merger will be deemed to be a liquidation. When considering “deemed” liquidation provisions, my first question always is “what is it exactly that the preferred would get if you were to apply this provision?” Because the company is not actually liquidating, the terms of the preferred are merely deeming the merger to be a liquidation. The liquidation provision generally provides that the company first must pay the creditors. But in a merger a company doesn’t pay its creditors, so it is not clear what the deemed liquidation provision requires the company to do. Even if the company were to pay its creditors, it may be difficult to determine the actual amount that a full participation preferred gets. What would be left over? Do you have to do a valuation of the company?

Let’s say you get over that hurdle. The next question is - how do the preferred holders get their liquidation preference? When a company actually dissolves and liquidates, there’s a statutory mechanic. The fundamental problem with most “deemed liquidation” events is that, in most cases, there is no statutory hook because the company is not actually liquidating. It is doing something else. What’s the statutory mechanic to get this money out? One way would be a redemption. But this deemed liquidation provision (like most that we see) is not drafted as a forced redemption.

Finally, even if you can figure out all of those issues, what happens after the company pays this money? Is the stock cancelled? For that matter, is it always money that should be paid? Assume that the company enters into a stock for stock merger and the deemed liquidation provision says that the holders of preferred get $100 plus an 8% return. Do the preferred holders get $100 in cash plus 8%? And, if so, do the preferred holders get both their deemed liquidation amount and the right to stay in and continue to get their 8% return until there is another deemed liquidation? When you put all of this together, it is easy to conclude that there is a substantial risk that many “deemed liquidation” clauses may not be explicit enough to create the kind of “preference” right that a court can figure out with any sort of confidence.

Frankle: John, I assume it’s even more difficult if the company is actually surviving as opposed to a change of control transaction.

Grossbauer: I think that’s right because then you have the interesting question – although the common might be sticking around, does the preferred stay in?

Bronner: For those of us who practice in the private equity marketplace, trying to put the words “deemed liquidation” into the context of Delaware corporate law is one that we usually don’t undertake. Instead, we focus on all sorts of practical mechanical questions raised by particular transactions that are being provided for computation and on the determination of how much a stockholder is going to be paid when a merger occurs. But you can see from our discussion here, the Delaware lawyers have put this into a literal context. If it’s a deemed liquidation, how does it really work and are the preferred holders going to end up getting what they think they are getting?

Morton: Part of what we struggle with here is what do you do – within the confines of our statute - to fix the problems we’ve identified. So, for example, even if the deemed liquidation concept is written as a forced redemption, if a company doesn’t have enough surplus then it can’t do a redemption. Which leads us to the next question. While it’s easy for us to sit here and complain about deemed liquidation provisions, what do you do when you get the phone call, Tricia, and someone says, “I’ve got this deemed liquidation provision in my preferred terms that doesn’t seem to make sense.” What are they supposed to do?

Vella: It depends on the facts and circumstances of the situation and how the issue
has come up. For example, if a majority of the preferred holders affected by the provision are on board with the transaction, notwithstanding the fact that they may be getting no consideration, as in a financing transaction that triggers the deemed liquidation provision, or are getting less than their liquidation preference, then the best approach may be to amend the charter to eliminate the deemed liquidation provision or to carve out the proposed transaction from the deemed liquidation provision. But that solution only works when the company can get the votes necessary to amend the charter, including the series vote of the preferred with the deemed liquidation right.

What if there are disgruntled investors who don’t like the deal and they want to rely on the deemed liquidation provision to try to get more for themselves or to try to block the transaction? The Delaware case law suggests some creative solutions. For example, if you take a look at the Delaware cases we have discussed today, one option would be to do a “dummy” merger to amend the terms of the deemed liquidation provision. First, though, you have to determine whether the terms of the series of preferred stock provide for a series vote in a merger. That includes looking to the amendment provision to make sure it does not apply to amendments effectuated in a merger. Under Delaware’s merger statute, it’s clear that preferred stockholders won’t get a separate class vote on the merger. You will have to check, however, to be sure that the dummy merger would not trigger the deemed liquidation provision. If you look at the deemed liquidation provision in the hypo, you’ll see that it only picks up mergers where the stockholders before the merger own less than 50% of the surviving company after the merger. In a dummy merger, however, the Company’s stockholders are the same both before and after the merger. So, you may be able to use a “dummy” merger to remove or modify a deemed liquidation provision that’s an obstacle to your transaction. The bottom line is – realize that there may be creative solutions under Delaware law to dealing with deemed liquidation provisions.

Frankle: By the way, keep in mind that when the company and the investors’ counsel are drafting these provisions, they often discuss this very issue - whether the investors should get a vote on a dummy merger. The example that’s always thrown out is, if the company wants to reincorporate to another state or wants to do some very minor structuring change, the company ought to be able to do that without triggering the deemed liquidation clause or a stockholder vote. Many times that argument will carry the day in the drafting. If it does, then both the deemed liquidation provision, which theoretically only delivers value to the preferred when there is a true change of control, and the amendment provision, which theoretically protects the preferred in a true substantive merger, may fail to protect investors from the effects of a “dummy” merger. When the preferred holders check to see whether they have a class vote to prevent their deemed liquidation provision from being stripped out, they may be surprised to find they don’t have one. The irony, of course, is that they may have lost this substantive right simply by accommodating company counsel’s seemingly reasonable request for some flexibility.

Morton: So, to summarize, as Tricia has suggested there may be creative “after the fact” solutions to the problems created by deemed liquidation clauses. And, as John points out, on the front end, your drafting decisions may enable you to avoid some of the problems associated with “deemed liquidation” provisions. For example, you may choose to provide the preferred with an exit strategy in the form of a forced redemption,
rather than a liquidation. Or, you might protect the preferred by giving them an absolute voting right for all mergers. In the latter cases, the question, Diane, is whether that’s really what the preferred holders want and whether that’s a viable solution for them?

**Frankle:** A forced redemption works really well if it is in the terms from the start, you don’t have a surplus problem at the end, and the preferred don’t have a full participation right. But it becomes less workable if the investors want to get a full participation right in addition to their set return. In that case, your drafting challenge is to determine how the company is to be valued in order to get the preferred the full value of the participation right.

Another alternative that’s probably more effective is to give the investor a vote, a class vote, at the time that the preferred is negotiated. But I can tell you that from the company’s standpoint this will be hotly negotiated, especially when new money is coming in and there already are existing investors. The company doesn’t want every corporate transaction they do to trigger a series of class or series votes and it doesn’t want to have a lot of different stakeholders with blocking rights.

**Grossbauer:** From the Delaware standpoint, I think that one of the optimal ways is to give the series a separate vote. The challenge is to define it narrowly enough so that both the company and the preferred holder are comfortable. For example, the voting provision could provide that the preferred holders will get a series vote in a merger unless the merger gives the holders X, Y, and Z. Of course, as Diane said, if the preferred will have a full participation right, defining what X, Y, and Z will cover may prove to be challenging.

**Bronner:** You probably have to assume that you’re having a sale of the company. If it’s publicly traded stock, you probably have to use your normal valuations. If it is not, then you would have to go out and get an independent appraisal in order to afford the preferred stockholder that right. In fact, I have done that in cases of forced redemptions where there have been participation rights. This is complex, but the forced redemption provisions are basically designed to give the private equity players an opportunity to block the transaction when there isn’t a true liquidation of the business, such as a merger of equals where the business is going on and there is no cash available to pay the forced redemption price.

**Morton:** There’s one final point on liquidation provisions. John, depending upon how a liquidation preference is expressed, couldn’t it also cap what the preferred is entitled to in a merger?

**Grossbauer:** Yes. The *Ford Holdings* case in the outline involves this issue. In that case, there were two series of preferred stock at issue. The terms of one series provided that in the event of a merger the holders of that series would get X dollars. The holders of that series sought appraisal arguing that their pro rata share of the company was really worth more than X. The court said no, the terms of the series defined what the holders would get in a merger, so that’s what they get in an appraisal -- no more, no less. By contrast, for another series of preferred in the very same case, the charter provided that, unless the preferred received a specific dollar amount, they would get a class vote on the merger. That provision, the court said, merely created a voting right. That’s not the same as saying “here’s what you will get.” As a result, that series was able to argue for a higher value than the merger consideration in the appraisal action. So, once again, we’re reminded of the importance of drafting language that clearly expresses preferences. The failure to pay attention to what the statutory hooks are when you are drafting may be outcome-determinative.

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5 *In re Appraisal of Ford Holdings,* 698 A.2d 973, 974 (Del. Ch. 1997).
Morton: To bring some closure to this topic, let’s summarize a few points that you’ve heard. First, broad definitions in these deemed liquidations clauses are sometimes hazardous to your health. Be quite careful when drafting to make sure that you’ve covered exactly what you wanted to cover. If it’s too broad, it may actually end up collapsing on itself. Second, when drafting, ask yourself whether the mechanics of the provision work - not just what’s the trigger, but also what do you do once it’s been triggered. Third, if it appears that a transaction may trigger a deemed liquidation clause, consider whether there are ways of structuring the transaction to avoid triggering the provision. As we’ve heard from the panel, there are various solutions to the problems we’ve identified, but the utility of each may be limited by the legal and economic realities.

Frankle: Mark, we’ve focused today on Delaware law, but I think it is important to note that you have to go back to your own jurisdiction to see if the rules of construction that are applied by the Delaware courts also apply in your jurisdiction. It’s an open question in many states. They just don’t have a decision one way or another. So again, Delaware jurisprudence may or may not rule the day in another jurisdiction when the court actually looks at this issue.

Bronner: Also, remember that this is a problem that, quite honestly, can be avoided fairly easily up front. As I told Mark when we started talking about this, I never have this problem because I always ask for a class vote on a merger.

Frankle: When I was talking to this panel yesterday, John made the point that when he tells clients about these potential defects, their reaction often is, well that’s ok -- I’ll have a seat at the table to discuss this. I think one of the things that might be evident from this discussion is - not so fast, not necessarily. You do need to think this through in advance. As I think David will acknowledge, just because everybody would say this is easy to fix at the front end, there are still lots of people out there that have these provisions right now and now the dynamics have changed. For them, it may not be so easy to fix now.

**TASK FORCE REPORTS**

**Task Force on the Acquisitions of Public Companies**

**November 16, 2002 Meeting in Chicago**

We met in Chicago at Baker & McKenzie's offices, on Saturday, November 16 from 9:00 a.m. to 4:00 p.m. Thanks to Phil Stamatakos and Chris Bartoli for hosting us on Saturday and for a wonderful dinner Friday evening at the trendy Nines, attended by 20+ Task Force members and spouses.

We reviewed the current draft of the model acquisition agreement and our schedule and assignments.

The Task Force discussed plans for the specialty representations (tax, environmental, intellectual property, employee benefits, employment). One law firm will provide an expert on each set of specialty representations, with Kaye Scholer and Gray Cary providing additional input in revising the representations and commentary. We then discussed how to address Sarbanes compliance and corporate governance issues in the representations.

We also reviewed an excellent draft of the miscellaneous provisions and commentary provided by Byron Egan and Neal Brockmeyer.

**January 11, 2003 Meeting in Wilmington**

We had a truly memorable meeting of our Task Force in Wilmington, DE. Many thanks to Mark Morton and Potter, Anderson & Corroon for organizing and hosting our meeting and a
wonderful dinner Friday evening at the Hotel Dupont's historic Brandywine Room, with after
dinner remarks by Chancellor Chandler. We were
joined Saturday morning by the following
members of the Delaware bench:

The Honorable Joseph T. Walsh
The Honorable Myron T. Steele
The Honorable William B. Chandler, III
The Honorable Stephen P. Lamb
The Honorable Leo E. Strine, Jr.
The Honorable Jack B. Jacobs

We were also pleased to welcome former
Chancellor William T. Allen, now Director of
NYU's Center for Law and Business. Our
morning session was a lively and candid dialogue
between members of the bench and our Task
Force regarding issues raised by current deal-
making practices and case law, including
standards of review and board duties, standstill
and exclusivity agreements, and deal lockup
provisions. Pending cases were, of course, off
limits and the discussion centered on practitioners'
desire to provide clear advice to directors and
officers in a changing area and the bench's interest
in understanding the typical factual scenarios and
negotiation practices which produce the
agreements they see in M&A cases. Thanks to
Rick Climan for moderating and Mark Morton and
David Katz for facilitating this dialogue, and to all
who participated.

We heard from members of the bench and
Task Force that this was a very valuable program
and we will explore the possibility of another such
program in the future.

After lunch we had another great program
presented by Task Force members Rick
Alexander, Steve Bigler and John Grossbauer on
"Section 203 - Tricks and Traps for the Unwary."
This was a really good review of the key issues
under Section 203.

We confirmed our upcoming meeting in L.A.
on Saturday, April 5, 2003, from 9 a.m. to noon.
Joel Greenberg agreed to host a 3-hour preparation
session at his firm’s Los Angeles office from
2:00 - 5:00 p.m. on Friday, April 4, 2003, and we
will have a Task Force dinner on Friday night -
more soon about that! At our April meeting we
will be discussing Article I and commentary,
Covenants and commentary and updates to the
Termination commentary.

We had a brief discussion of evolving
practices in M&A agreements and diligence
practices arising from Sarbanes-Oxley concerns.
We discussed the impact of the SEC's proposed
Rule 307 on M&A practice. We also discussed
the recent Mobile Toys and Liquid Audio cases.

Jon Perry reviewed the schedule for specialty
representations (tax, IP, benefits, environmental).
Eileen Nugent then reviewed the proposed
ancillary agreements. Finally, we reviewed the
fact pattern and provided comments. We
adjourned at approximately 4:30 p.m. and many
members joined Mark Morton and Rick Alexander
for dinner in Wilmington.

Diane Holt Frankle
Stephen H. Knee
Co-Chairs

Task Force on the Dictionary of
M&A Terms – Inaugural Report

I am pleased to announce that work has begun
on developing a “Dealmakers’ Dictionary” – a
comprehensive glossary of M&A terms – for
publication in 2004. A number of people have
indicated that that they are willing to work on the
Task Force and new members are welcome. We
are in the process of reviewing various sources in
an effort to develop a comprehensive list of M&A
terms. While the focus will be on terms used in
United States M&A transactions, we are hopeful
that we will get contributions from our
international members so that our Dictionary can
be as comprehensive in scope as possible. (Our
Dictionary will be broader in scope than the
lexicon to be included in the Manual on
Acquisition Practice & Process, which will focus
primarily on private company acquisitions.)
Once the list is developed, we will be assigning members of the Task Force responsibility for reviewing existing definitions and updating them as appropriate. In addition, terms that do not currently have a definition also will be assigned. Our goal is to have a comprehensive, updated draft to be submitted for broad review by early next year, so that we can have it published before the end of 2004.

To the extent that people would like to join the Task Force, please e-mail me at dakatz@wlrk.com. Even if you do not have time to join the Task Force, we would welcome lists of terms that you believe should be covered by our Dictionary. These may also be conveyed to me by e-mail at dakatz@wlrk.com and I will circulate suggestions received to Task Force members.

While we will not hold a meeting in April, we will have one this summer, by which time an initial draft of the Dictionary will be well underway. Please contribute your time, your thoughts on terms to be included, or both!

David A. Katz  
Chair

International Transactions  
Task Force

The International Transactions Task Force had a very productive meeting in Paris with approximately 40 attendees. Among our attendees, we had a number of first time participants who were drawn to our Task Force because of the International Institute on Mergers & Acquisitions.

The focal point of our meeting was a presentation made by Pierre Servan-Schreiber, a partner at Skadden Arps in Paris, who spoke on the hot topic of privatizations.

Our meeting also focused on both the current and future product of our task force. Of note to the rest of our committee members, we will be starting a new project - an international overview of the Model Asset Purchase Agreement - at our Spring Meeting in Los Angeles. Our meetings for this new project will be designed to be interactive so that all members of the Task Force can provide their views and comments at the meetings themselves.

John W. Leopold  
Guy-Martial A.X. Weijer  
Co-Chairs

Joint Venture Agreements  
Task Force

The Joint Venture Agreements Task Force is in the process of finalizing the joint venture (partnership) agreement and the commentary. The editorial committee will be meeting on February 28 and March 1 to review the work that has been accomplished to date. Several members of the Task Force have done sterling work getting us to this point and we really can see the light at the end of the tunnel. We are working with the publications committee of the ABA to finalize this product and will report on our progress at the L.A. meeting.

The Task Force is co-sponsoring a program on joint ventures at the Spring Meeting with the Antitrust Committee entitled: In the Antitrust Gunsights Again? This program is a follow-on to the program we did at the Spring Meeting in Boston where Will Tom provided antitrust commentary on joint venture agreements. Finally, the program we did at the Spring Meeting - Joint Ventures - Negotiating the Rapids - (but without the antitrust piece) will be repeated by videoconference on April 28.

Thomas B. Hyman, Jr.  
Alison J. Youngman  
Co-Chairs
Manual on Acquisition Practice and Process Task Force

At the Paris meeting in October, we had a good working group of twelve Task Force members present, including Jackie McGlamery from the ABA Publications Committee. The Task Force continued the process of reviewing and refining topic outlines prepared by Task Force members. The Task Force discussed outlines developed by Ric Brown on "Confidentiality," Ted Lenz on "Regional Differences," John Clifford on "International Aspects," and Howard Barnhorst on "Management Presentations and Site Visits." We also discussed the format and scope of the Manual and eliminating overlaps in the outlines.

The Task Force felt that a bibliography with meaningful resources on M&A topics should be added to the Manual. Nancy Kaiser, who recently joined our Task Force, will lead this project. Nancy will contact authors of outlines for recommendations of resources so that we can begin building the bibliography.

The Co-Chairs asked several authors of completed chapter outlines to begin drafting text under fairly broad style guidelines. Authors include Bob Copeland on "Ethics," Jon Hirschoff on "Valuation," George Taylor on "Closings," and Norm Zilber on "Who is the Client?"

To keep our momentum, the Task Force also held a conference call/meeting on February 1, hosted by Vince Garrity at his offices at Duane Morris in Philadelphia, joined by four folks in person and nineteen by conference call on a frigid Saturday. Rob Ouellette had revised our Master Outline inserting new material, including outlines prepared by Bill Payne on "Context of a Merger Transaction," Dave Gavsie on "Style" Issues, Ralston Steenrod on "Due Diligence," John Clifford, Christian Franz and Mario Jorge Yanez Vega on "International Transactions," and Deborah Telman on "In-House Counsel Perspective." Tom and Vince asked a number of authors of outlines to commence drafting text. Neal Brockmeyer reported that he has been in touch with Rick Climan and David Katz to coordinate the Manual's Lexicon with the new M&A dictionary project.

The Task Force will meet again in April at the Spring Meeting in Los Angeles.

Thomas M. Thompson
Vincent F. Garrity, Jr.
Co-Chairs

Task Force on the Model Stock Purchase Agreement


Members of our Working Groups (agreement revisions, seller’s response documents and ancillary documents) produced significant materials for our review and comment. In order to coordinate efforts, the Working Groups met in Dallas as a single unit to review drafts of the materials prepared for the revised Model Stock Purchase Agreement and Revised Ancillary Documents. Review of the Sellers’ Response Memorandum was deferred to the Spring Meeting in Los Angeles.

The Task Force will meet as a group at the Spring Meeting in Los Angeles on Friday, April 4, 2003. The morning meeting will concentrate on materials prepared in connection with the Model Stock Purchase Agreement and the afternoon meeting will concentrate on the materials related to the Sellers’ Response Memorandum. To allow attention to be devoted to these two topics, there will be no meeting of the Ancillary Documents Working Group at the Spring Meeting.

The Task Force is always seeking new members and we hope you will be able to attend our meetings in Los Angeles. There are still
plenty of assignments available. If you are interested in signing up or have any questions, please email me at rtharper@klettrooney.com.

Robert T. Harper
Chair

Recent Judicial Developments Subcommittee

The Subcommittee on Recent Judicial Developments has been busy since its inauguration at the Summer 2002 ABA Annual Meeting in Washington, D.C. We have completed our first annual survey of significant judicial decisions in the area of mergers and acquisitions, and the survey is scheduled for publication in the August 2003 issue of The Business Lawyer. We thank the following Subcommittee members who contributed to the drafting: Patrick J. Leddy, Robert R. Ouellette, Michael A. Pittenger, Patricia O. Vella, and Arthur Wright. We also thank all members of the Committee on Negotiated Acquisitions who suggested cases for publication.

In addition to the contributors listed above, Howie Wong and Christopher Sandefur also volunteered for the Subcommittee. This brings our membership to nine, which we believe is a workable number.

We need the continued help of all members of the Committee on Negotiated Acquisitions in identifying significant judicial decisions to include in this survey. If you become aware of a decision that was published during 2003 and is a candidate for inclusion, please inform either of us by email: Scott Whittaker at swhittaker@stonepigman.com, or Jon Hirschoff at jhirshoff@fdh.com. Or you can fax the case either to Scott at (504) 596-0836 or to Jon at (203) 348-5777.

The first criterion for inclusion is that the decision must involve a merger, an equity sale of a controlling interest, a sale of all or substantially all assets, a sale of a subsidiary or division, or a recapitalization resulting in a change of control. The second criterion is that the decision must (a) interpret or apply the provisions of an acquisition agreement or an agreement preliminary to an acquisition agreement (e.g. a letter of intent, confidentiality agreement or standstill agreement), (b) interpret or apply a state statute that governs one of the constituent entities (e.g. the General Corporation Law of the State of Delaware, or the

Committee Forum
Subcommittee

Title:
“The Impact of Sarbanes-Oxley on M&A"

Time and Place:
At 3:30 p.m. on Saturday, April 5, 2003 in Los Angeles

Moderator:
Leigh Walton (a partner in the Nashville, Tennessee office of Bass, Berry & Sims PLC)

Panelist:
Joel I. Greenberg (a partner in the New York office of Kaye Scholer LLP)

Description:
This Committee Forum will focus on the impact that Sarbanes-Oxley will have on M&A practices, concentrating on changes in the due diligence process and standard contractual terms mandated by the enactment of this far-reaching statute. The forum will cover difficulties in the certification process that may arise in connection with the transaction and other uncertainties created by the law.

Keith A. Flaum
Chair
Louisiana Limited Liability Company Law), (c) pertain to a successor liability issue, or (d) decide a breach of fiduciary duty claim. We are currently excluding cases dealing with federal law, securities law, tax law, and antitrust law. But if you feel a case dealing with an M&A transaction is significant please send it, even if it does not meet the foregoing criteria. If you submit a case, please provide a brief statement as to why you consider it to be significant. We look forward to receiving your submissions.

Set forth below is a summary of the recent decision of the U.S. District Court for the Southern District of New York in *In re Enron Corp.*, 2002 WL 31374717, which we feel will be of interest to the Committee members.

Jon T. Hirschoff  
Scott T. Whittaker  
Co-Chairs

**Shareholders as Third Party Beneficiaries of Merger Agreement**

In *In re Enron Corp.*, decided October 22, 2002, the Court held that shareholders of a target company could sue the acquiror under a Merger Agreement that the shareholders alleged had been improperly terminated by the acquiror. This case arises out of the failed merger between Enron Corp. and Dynegy. On November 9, 2001, after Enron’s financial crisis had become well publicized, Enron entered into a Merger Agreement with Dynegy providing for the issuance of 0.2685 shares of Dynegy common stock for each share of Enron common stock held by Enron shareholders. On November 28, 2001, Dynegy announced the termination of the merger, based on alleged misrepresentations by Enron and violation of the material adverse effect provision of the Merger Agreement. On December 2, 2001, Enron filed for Chapter 11 bankruptcy in the bankruptcy court for the Southern District of New York, and filed simultaneously an adversary proceeding against Dynegy, alleging breach of the Merger Agreement. On December 20, 2001, a shareholder class action suit was commenced in the U.S. District Court for the Southern District of New York against Dynegy, seeking damages or specific performance on behalf of the shareholders as third party beneficiaries to the Merger Agreement. The bankruptcy court enjoined the further prosecution of the shareholders’ suit, pursuant to the automatic stay provisions of the bankruptcy code, holding that even if the shareholders were third party beneficiaries, their claims were derivative and therefore property of the bankruptcy estate. The issue in this case was thus whether the bankruptcy stay was properly applied to enjoin the shareholders litigation.

In the appeal to the U.S. District Court for the Southern District of New York, which reversed the bankruptcy court, the issue turned on whether the shareholders’ claims against Dynegy under the Merger Agreement were derivative, in which case they would be the proper subject of the automatic stay, or were separate and independent, in which case the proceedings could progress separately from the bankruptcy proceedings. The court applied Texas law, which was the governing law provided in the Merger Agreement. The District Court limited its decision to an interpretation of the language of the Merger Agreement, without consideration of any extrinsic evidence. The critical provision of the Merger Agreement was Section 10.3, which stated in pertinent part as follows:

```plaintext
Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned by any of the parties hereto . . . without prior written consent of the other parties. Subject to the preceding sentence, this Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors and assigns. Notwithstanding anything contained in this Agreement to the contrary, except for the provisions of Article 4, Section 7.13 and Section 9.5(a) and except as provided in any agreements delivered pursuant hereto (collectively, the “Third-Party Provisions”), nothing in this
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Agreement...is intended to confer on any person other than the parties hereto or their respective heirs, successors, executors, administrators and assigns any rights, remedies, obligations or liabilities under or by reason of this Agreement. The Third-Party Provisions may be enforced by the beneficiaries thereof. . . .

Article 4 provided that, upon consummation of the merger, each outstanding share of Enron common stock would be exchanged for the equivalent of 0.2685 shares of Dynegy common stock. Enron argued that any rights granted to the shareholders to enforce Article 4 did not accrue because under Section 1.3 of the Merger Agreement, the conversion of Enron’s shares into Dynegy shares was not to occur until the “Effective Time” provided in the Merger Agreement, which was “the time that Dynegy and Enron shall have agreed upon and designated.” Furthermore, the consummation of the transactions under the Merger Agreement was conditioned on the approval of the respective shareholders of Dynegy and Enron, and on appropriate regulatory authorities’ approval, none of which had been obtained. The District Court dismissed this argument as irrelevant, analyzing the claim as one of contract repudiation. Citing the Restatement (Second) of Contract Law, Section 253 (1981), the court reasoned that repudiation of an agreement before a party has committed a breach by non-performance, and before that party has received all of the consideration due to it, gives rise to a claim for damages for a total breach. Thus, if the shareholders were correct that Dynegy improperly terminated the Merger Agreement, they were entitled to damages for failure to perform Section 4, regardless of whether the Effective Time had been reached. The court did note that if Enron and Dynegy had terminated the Merger Agreement by mutual consent, as opposed to Dynegy’s unilateral termination based on the material adverse change provisions, then the shareholders would not have a claim.

In deciding whether the shareholders had an action distinct from the corporation, as opposed to a derivative claim only, the court examined the “nature of the wrong.” The court acknowledged that no claim against Dynegy would exist on the part of the shareholders if the alleged wrong of Dynegy caused an injury to both the shareholders and Enron; rather a separate action could only be brought if Dynegy’s conduct caused an injury to the shareholders distinct from any injury to the corporation. The court reasoned that the Merger Agreement provided separate benefits to Enron as opposed to the shareholders. The benefit to Enron was having its debts assumed by Dynegy; the benefit to the shareholders was to become shareholders of Dynegy. According to the court, “[t]hese are distinct and separate benefits; therefore the injuries sustained by their loss are distinct and separate.”

The corporation also argued that the Settlement Agreement that had been entered into between Enron and Dynegy cut off any cause of action by the shareholders. The Court disagreed. Although Dynegy and Enron had entered into a Settlement Agreement, whereby Dynegy paid Enron $25,000,000 and allowed Enron to keep a $67,000,000 deposit that was in escrow, the Settlement Agreement only released Dynegy from claims made against it by Enron, and did not purport to release the shareholders’ claims. This, according to the court, further proved that the shareholders’ claims were separate and distinct from the claims of Enron.

This case is troubling to M&A practitioners, who sometimes draft merger agreements containing provisions similar to those at issue in this case, under the belief that any ability of the shareholders to enforce the merger agreement will only arise after the consummation of the merger, and only with respect to the obligation of the acquiror to issue the merger consideration (which obligation at that time will be unconditional). The court’s contrary holding in this case illustrates the need for careful drafting of third party beneficiary provisions in Merger Agreements.