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SEC DEVELOPMENTS IN M&A

In a panel last fall, Michele M. Anderson, Chief of the SEC's Office of Mergers & Acquisitions, discussed with practitioners a number of M & A topics from the SEC staff perspective. The topics included disclosures in Delaware General Corporation Law Section 251(h) transactions, satisfaction or waiver of financing conditions in tender offers, "proxy plumbing," and the recent enforcement action against Revlon.

By Richard Hall *

On September 27, 2013, the New York City Bar Association, in conjunction with The Center for the Study of Mergers & Acquisitions, Penn State Law School, hosted the 10th Annual Institute on Mergers & Acquisitions & Corporate Governance. One of the panels at the Institute, entitled "SEC Developments in M&A Governance," included Michele M. Anderson, Esq., Chief, Office of Mergers & Acquisitions, Division of Corporation Finance, U.S. Securities & Exchange Commission, as well as representatives from private practice. In this panel, Ms. Anderson discussed a number of current issues for M&A practitioners from the perspective of the SEC staff.

Section 251(h)

Ms. Anderson noted that, at the time of the Institute, only seven tender offer transactions had been announced using recently enacted Section 251(h) of the Delaware General Corporation Law, which was intended to eliminate the need for approval by the target stockholders for consummation of a second-step merger following successful completion of a tender offer.[1] Although Section 251(h) is a matter of state law, Ms. Anderson took the opportunity to make some observations about disclosure in Section 251(h) transactions in Schedules TO and Schedule 14-9 Solicitation/Recommendation Statements, both of which are subject to SEC oversight. The SEC staff recognized that Section 251(h) was new and that it would take practitioners some time to adapt their forms, precedents, and understandings of proper disclosure to reflect the new transaction structure. Ms. Anderson indicated, however, that some of the disclosure documents that had already been presented to the staff could have been improved. She noted two points in particular.

First, the SEC requirements applicable to Schedule TO mandate disclosure regarding the offeror's plans with respect to the target company following successful completion of the tender offer. In transactions in which

[1] Specifically, for transactions which Section 251(h) is available, Section 251(h) reduced the percentage of the target's outstanding voting stock required to be acquired for a second-step short-form merger, without the need for approval of target stockholders, from 90% to a simple majority.

∗ *RICHARD HALL is a partner in Cravath, Swaine & Moore LLP's New York office. His e-mail address is rhall@cravath.com.*

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the offeror intends to consummate a second-step merger to acquire all the target shares not tendered into the tender offer, these requirements historically have resulted in disclosure of (a) the contemplated second-step merger, (b) possible implications for non-tendering target stockholders during the period between consummation of the tender offer and completion of the second-step merger, and (c) possible implications for non-tendering target stockholders if the second-step merger is never consummated. Ms. Anderson noted that, under Section 251(h), the likelihood of a significant time period between the consummation of the tender offer and the completion of the second-step merger, as well as the likelihood of non-completion of the second-step merger, were significantly reduced. In her view, some offerors (and their legal counsel) were not properly balancing the level of disclosure concerning these events against the low likelihood that these events would actually come to pass. Ms. Anderson suggested that offerors, when drafting Schedules TO for Section 251(h) transactions, take advantage of the simplicity of Section 251(h) to simplify the disclosure describing the period following consummation of the tender offer.

Second, another area of focus for the SEC staff with respect to Section 251(h) is the disclosure concerning mechanisms such as top-up options and obligations to hold stockholder meetings in the event that the approval of the stockholders of the target company was required. The practitioners on the panel noted that a number of Section 251(h) transactions included "fall-back" features (such as top-up options and meeting covenants) to protect against the risk that Section 251(h) was not available for some reason. Ms. Anderson noted that the inclusion of these features was a matter for negotiation between the parties and their advisors, and not a matter for the SEC. She also observed, however, that some offerors, targets, and their legal counsel were not properly disclosing to target company stockholders the reasons for inclusion of these fall-back mechanisms, the circumstances under which they may be invoked, and whether there was (in the context of any particular transaction) any material risk of Section 251(h) not being applicable. The practitioners on the panel, along with Ms. Anderson, discussed the role of these fall-back mechanisms. The consensus of the practitioners was that in most cases these mechanisms were being included out of conservatism and that SEC staff comments requiring offerors to explain the circumstances under which they might be invoked would likely lead over time to more offerors not to insist on their inclusion in Section 251(h) transactions in which there was no real concern as to the availability of Section 251(h).

Financing Conditions

The practitioners on the panel explained that Section 251(h) was motivated, in part, by a desire to increase the ability of highly leveraged acquirors, including private equity sponsors, to use tender offer structures to complete their transactions. The practitioners noted that highly leveraged acquirors and their financing sources were concerned about the ability of acquirors to complete the second-step merger following successful completion of the tender offer, and also were concerned about possible delay in consummation of the second-step merger. Section 251(h) provides to highly leveraged acquirors and their financing sources greater assurance that the second-step merger will be completed very quickly. At the time of the Institute, none of the offerors that had used Section 251(h) was a highly leveraged acquiror.

The discussion of concerns on the part of highly leveraged acquirors about using tender offer structures led to a discussion among the panelists, including Ms. Anderson, of the position of the SEC staff with respect to financing conditions in tender offers. It has historically been the position of the SEC staff that the satisfaction or waiver of a material condition to a tender offer constitutes a "material change" and, accordingly, that a tender offer must remain open for at least five business days following the first public announcement of the satisfaction or waiver. Ms. Anderson noted that this had been a source of tension between the SEC staff and practitioners. She also noted, however, that many highly leveraged acquirors were now comfortable in relying on other conditions to the tender offer (such as continuing correctness of representations and warranties, and absence of material adverse change) or funding into escrow to permit their offers to be conducted in a manner consistent with the position of the SEC staff by waiving or declaring satisfied the financing condition while keeping the offer open. Ms. Anderson explained that the position of the staff was evolving and, although the staff continued to regard the satisfaction or waiver of a financing condition as a material development requiring dissemination prior to expiration of the offer, the staff would now accept that disclosure need only be made one to two business days prior to expiration of the tender offer.

Rule 13e-3

Ms. Anderson also discussed the SEC's recent enforcement action against Revlon, Inc. relating to non-compliance by Revlon with its disclosure obligations under SEC Rule 13e-3 in connection with a "going private" transaction between Revlon and its then-controlling stockholder. This enforcement action came in the form of "cease-and-desist proceedings" under Section 21C of the Securities Exchange Act of 1934 (Release Number 34-69750). The facts underlying the Revlon enforcement action were somewhat special and unlikely to be repeated precisely in any other Rule 13e-3 transaction. Ms. Anderson emphasized to the Institute, however, that the SEC enforcement action was based on broad principles relating to Revlon's failure to comply with its obligation under Rule 13e-3 to disclose all material information and was not limited to a narrow and technical finding, and that this action should be seen as a warning to registrants and practitioners not to rely on highly technical readings of Rule 13e-3 to avoid disclosing material information to minority stockholders. The practitioners on the panel noted the importance to the SEC of the obligation under Rule 13e-3 to disclose information relating to the fairness of the transaction to minority stockholders. Ms. Anderson did not comment on hypotheticals, but the practitioners did observe that the fact that the information not disclosed by Revlon related to a third-party's determination that the transaction was not fair to the minority stockholders may have influenced the decision on the part of the SEC to bring the enforcement action. Ms. Anderson commented that the staff of her Office worked very closely with the staff of the SEC's Enforcement Division with respect to the Revlon enforcement action.

Proxy Plumbing

Ms. Anderson discussed the status of the review by the SEC staff into mechanical aspects of the operation of the U.S. system for the granting and withholding of proxies for the voting of shares (referred to by the SEC and practitioners as "proxy plumbing"), as well as the related questions of the role of proxy advisory services, such as Institutional Shareholder Services and Glass-Lewis, and the role of Broadridge Corporation in the U.S. proxy system. Ms. Anderson explained that proxy plumbing remained an important subject for her Office, although the staff's ability to move forward as a practical matter was limited by the demands being placed on the SEC for required rule-makings under the Dodd-Frank Act.

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Ms. Anderson noted there was a wide range of views among registrants and practitioners with respect to a number of aspects of proxy plumbing, including the desirability of the universal ballot. A "universal ballot" is a single proxy card that is used by both the company and the activist/insurgent that lists all candidates for election. A universal ballot is frequently considered as a possible solution to some of the complexities of the U.S. proxy system with respect to proxy contests involving "short slates" of directors (that is, contests in which the activist or insurgent is seeking the election of fewer directors than are being elected). Short slate contests are particularly complex under the U.S. proxy rules because they normally involve competing proxy cards and many stockholders completing multiple proxy cards.
Ms. Anderson noted that the feedback received by the SEC staff with respect to universal ballots was that registrants preferred not to be required to use universal ballots when facing a short slate contest. The practitioners on the panel indicated that this might be a result of the desire on the part of registrants not to make it easier for activist shareholders to engage in proxy contests for short slates of directors.

Section 13(d)

Ms. Anderson also commented on the long-standing petition to the SEC to reform a number of its rules under Section 13(d) of the Securities Exchange Act of 1934, which require disclosure by substantial stockholders of their ownership positions, as well as related other information. Ms. Anderson indicated that she continued to regard reform of the SEC's rules under Section 13(d) as an important task. She reminded the practitioners on the panel that petition had elicited substantial negative reaction from a number of commentators when filed — in particular, the requested reforms to shorten time periods for initial Schedule 13D filings and expansion of the concept of "beneficial ownership" to include all derivative securities. She observed that the principles underlying Section 13(d) and the related rules are viewed from different perspectives by different participants in the U.S. capital markets and that even the simplest reform may be difficult to achieve. ■