Wachtell, Lipton, Rosen & Katz

# Takeover Response Checklist

2023

# Takeover Response Checklist

Takeover preparedness has never been more important. Failure to prepare for a takeover exposes potential targets to pressure tactics, reduces the target's ability to control its own destiny and exposes companies to opportunistic short-termism, whether in the form of an undervalued but notional-premium takeover bid or other business decisions that are contrary to the long-term interests of their stakeholders. This outline provides an illustrative checklist of matters to be considered in putting a company in the best possible position to respond to an unsolicited takeover bid. This is a comprehensive illustrative checklist; not all the matters in this outline are appropriate for any one company.

When considering these measures, boards and management should keep in mind that takeover defense is an art, not a science. It is essential to be flexible in responding to changing takeover tactics and circumstances. Whatever the state of the law may be and however it may change, a company must have effective defenses and keep them up to date in order to achieve the best results in a takeover situation. Of equal importance, a company must maintain excellent investor relations, with the CEO and CFO in regular contact with the key investors and analysts, and director(s) prepared to participate directly in engagement with key shareholders in appropriate cases.

## I. Advance Preparation

a) Create Team to Deal with Unsolicited Takeovers

- Small group (2–5) of key officers, plus legal counsel, investment banker, public relations firm and proxy solicitation firm
- Ensure practical ability to convene special meeting of board within 24 to 48 hours
- Hold periodic meetings and maintain real-time communication among key team members
- Give periodic updates to the board
- Update key contacts list regularly

b) Prepare Instructions for Dealing with Communications to:

- Directors
- Press
- Social media, message boards, blogs and other real-time sources
- Stock Exchange
- Employees and unions
- Customers/suppliers/banks
- Institutional investors and analysts
- Public officials and government contacts
- Other key stakeholders

c) Review Structural Defenses; Consider Implementing Additional Defenses If Necessary

1. Bear in mind:

    - In many cases a structural defense is possible only if there has been careful advance preparation by the company and its investment banker and legal counsel.

- Staggered election of the board of directors and/or supermajority merger votes may be effective in deterring (or improving the company's negotiating position when faced with) takeover attempts (including proxy fights) and are worth retaining, if the company has them currently, for as long as possible.
- A staggered board is a particularly potent defensive measure, which, once removed, will be extremely challenging to reinstate.
- Structural defenses need to be reviewed in light of negative reactions from institutional investors and impact on corporate governance ratings and institutional proxy voting services' recommendations. Be wary, however, of reflexive "one size fits all" wholesale removal of defenses, especially at non-mega cap companies, that do not take into account company-specific circumstances and the risk that such removal of defenses may substantially increase vulnerability.

2. Review charter and bylaw provisions for best-in-class provisions pertaining to:

- Staggered board
- Advance notice provisions for nominations and business at stockholder meetings
- Ability of stockholders to act by written consent
- Ability of stockholders to call a special meeting
- Ability of stockholders to remove directors without cause
- Ability of stockholders to expand size of board and fill vacancies
- Supermajority voting provisions
- Authorization of sufficient common and blank-check preferred stock (in order to implement a shareholder rights plan)
- Director qualification requirements
- Cumulative voting
- Treatment of non-shareholder constituencies
- Exclusive forum provisions
- Majority voting (resignation with acceptance in business judgment of the board)

3. Put shareholder rights plans ("poison pill") on the shelf.

- Permits board to "just say no" (Airgas case)
- Purported antidotes ineffective
- Consider treatment of derivatives
- Institutional pressure to submit pills to a shareholder vote
- Dealing with shareholder proposals and director withhold vote recommendations for pill renewals
- Avoid poison pill policies, restrictive governance principles and by-laws, as they limit flexibility
- "Dead Hand" provision not valid in Delaware (and possibly elsewhere)

4. Review structure of loan agreements and indentures (including change of control definitions) for implications in a takeover context

5. Review change of control triggers in joint venture agreements and other material contracts

6. Consider plans to increase employee ownership/ ESOP arrangements

7. Consider applicability of state takeover laws

    - Control share
    - Business combination
    - Fair price
    - Pill validation
    - Constituency statutes
    - Long-term prospects vs. short-term price
    - Disclosure obligations

d) Additional Advance Preparation

- Review of the business portfolio and strategy: dividend policy, leverage, share repurchase, divestitures and spinoffs
- Review of "value unlock" / monetization options, including as to intellectual property and other assets
- Review of company positioning and potential disclosure of go forward "value enhancement plan," including in connection with specially called investor day
- Advance preparation of earnings projections and liquidation values for evaluation of takeover bid and alternative transactions
- Consider advisability of amendments to stock options, employment agreements, executive incentive plans and severance arrangements ("golden parachutes")
- Consider advisability of amendments to employee stock plans with respect to voting and accepting a tender offer
- Consider existence of white knight/white squire arrangements
- Review availability of regulatory defenses, including CFIUS

e) Shareholder Relations

- Monitor changes in institutional holdings on a regular basis
- Maintain excellent investor relations across actively managed funds and index funds
- Review capital allocation, dividend and repurchase policy, analyst presentations and other financial public relations
- Prepare fiduciary holders with respect to takeover tactics designed to panic them
- Plan for contacts with institutional investors (including maintenance of an up-to-date list of holdings and contacts) and analysts and with media, regulatory agencies and political bodies
- Remain informed about activist hedge funds and activist institutional investors and about corporate governance and proxy issues (see our memo, "Dealing with Activist Hedge Funds and Other Activist Investors")
- Role of arbitrageurs and hedge funds

f) Prepare Board of Directors to Deal with Takeovers

- Maintain a unified board consensus on key strategic issues
- Schedule periodic presentations by legal counsel and investment bankers to familiarize directors with common takeover tactics and the law
- Directors must guard against subversion by raiders and should refer all approaches to the CEO
- Avoid being put in play; psychological and perception factors may be more important than legal and financial factors in avoiding being singled out as a takeover target
- Review corporate governance guidelines and constitution of key committees
- Discuss the importance of independent directors meeting with ISS and major shareholders during a proxy solicitation or a takeover

g) Preparation by Investment Banker

- Maintain up-to-date due diligence file and financial analyses
- Consider potential friendly M&A partners, defensive acquisitions, recapitalization, spin-off and tracking stock alternatives
- Perform semiannual review of preparedness and strategic positioning
- Know your raiders — advance preparation for dealing with a specific potential raider may be the key to a successful defense
- Communicate material developments regarding the company and maintain regular contact

h) Preparation by Legal Counsel

- Review structural defenses, such as rights plans
- Review charter and bylaws; make sure they reflect "state of the art" provisions
- Review business to determine products and markets for antitrust analysis of a raider
- Understand regulatory agency approvals for material transactions
- Consider impact of change of control on key business relationships and contracts
- Consider defensive acquisitions, recapitalization, spin-off and tracking stock alternatives
- Consider amendments to stock options, executive compensation and incentive arrangements and severance arrangements, and protection of pension plans
- Consider ESOPs and other programs to increase employee ownership
- Conduct regular communication and annual board presentations about takeover preparedness
- Review company D&O policies to ensure adequate coverage and sufficient scope (including "Side A" coverage)

i) Prepare CEO to Deal with Takeover Approaches

- The CEO should be the sole spokesperson for the company on corporate strategy, mergers and potential takeovers
- Handling casual passes (bear hugs)
- Handling investor pressure for commencement of strategic review (publicly announced)
- Handling unsolicited offers
- Communications with officers and board of directors
- Company may have policy of not commenting upon takeover discussions and rumors

## II. Responding to Bidder Activity

a) Types of Activity

- Accumulation of shares in the market
- Casual pass/nonpublic bear hug
- Public offer/public bear hug
- Tender offer
- Proxy contest/consent solicitation for board representation

b) Responses to Accumulation of Shares in the Market

- Monitor trading, hedge fund accumulation and 13(f) filings
- Maintain contact with stock watch specialists
- Monitor analyst reports and react appropriately
- Look for bidder Schedule 13D and Hart-Scott-Rodino filings
- Monitor/combat disruption of executives, personnel, customers, suppliers, etc.
- Monitor uncertainty in the market; change in shareholder profile
- Consider responses to share accumulation
    - Rights plan can be structured appropriately to a particular threat
    - Litigation
    - Standstill agreement

c) Effect of Hart-Scott-Rodino Antitrust Act and Antitrust Enforcement Policies

- Hart-Scott should prevent dawn raids on big companies, but under Hart-Scott a raider can buy up to the applicable threshold (this figure is updated annually by the FTC, and is as of August 2023, $111.4 million) without triggering filing requirement

- Activists may also seek to use the 10% passive investment exception or split investments across multiple funds which could each acquire up to the HSR threshold without triggering a filing requirement

- A raider cannot complete acquire an interest in excess of $111.4 million without notifying the company, filing HSR and observing the requisite waiting period:
    - Cash tender offer/bankruptcy: 15 calendar days
    - All other situations: 30 calendar days
    - If second request issued: 30 calendar days (10 calendar days in cash tender offer/bankruptcy) after substantial compliance

- Antitrust enforcement policies should be reviewed regularly, particularly when there is a change in administration or personnel.

- Foreign filings are increasingly important, and in some cases involve extensive pre-closing waiting periods.

d) Responses to Casual Passes/Non-Public Bear Hugs

- No duty to discuss or negotiate
- No initial response other than "will discuss with board"
- Call advisors and assemble team; inform directors
- Call special board meeting to consider bidder proposal
- Response to any particular approach must be specifically structured; team should confer to decide proper response; meeting with potential bidder or activist may be best strategy
- Keep the board advised; participation by independent directors may be critical

e) Response to Public Offers/Public Bear Hugs

- No press release or statement other than "stop-look-and-listen"
- Consider stock trading halt (NYSE limits halt to short period)
- Determine whether to meet with raider (refusal to meet may be a negative factor in litigation and public relations campaign)
- In a tender offer, Schedule 14D-9 must be filed within 10 business days and must disclose, among other things, the board's position (favor; oppose; neutral) and reasoning

f) Special Meeting of Board to Consider Offer

1. Board should be informed of the following:

    - Board has no duty to accept or negotiate a takeover offer
    - A premium over market is not necessarily a fair price; a fair price is not necessarily an adequate price
    - The "just say no" response was approved in the Time Warner case and reaffirmed in the Paramount, Unitrin and Airgas cases and—when appropriately deployed and documented— continues to be good strategy and good law
    - Unless a transaction involves a direct conflict with management or certain board members, there is no need for a special committee to consider takeovers, nor do the independent directors need separate legal counsel
    - Board must act in good faith and on a reasonable basis; business judgment rule applies to decision to say no to a takeover offer
    - Defensive actions by Delaware corporations in response to a takeover bid must satisfy the Delaware "proportional response" standard — action must be proportional to threat
    - Partial offers present fairness issues, which itself may warrant rejection and strong defensive action (risk of coercive conduct)

2. Presentation to Board (illustrative content):

   - Management — budgets, financial position, real values (off-balance sheet values), new products, general outlook, timing
   - Investment banker — opinion as to fairness or adequacy, assessment of bidder, quality of bidder's financing, state of the market and the economy, comparable acquisition premiums, timing
   - Legal counsel — terms and conditions of proposal, legality of takeover (antitrust, compliance with SEC disclosure requirements, regulatory approval of change of control, etc.), bidder's history, reasonable basis for board action

3. Board should consider:

   - Company's standalone prospects and plans
   - adequacy of the bid; valuation
   - nature and timing of the offer
   - likelihood of completion, and timing to complete (including risks to the business in the interlocutory period)
   - impact on constituencies other than shareholders
   - nature and quality of the securities being offered (if bid is not all cash)
   - strategic alternatives
   - capitalization and other structural alternatives (spin-offs, divestitures, extraordinary dividends)
   - whether to approach other potential bidders (on a one off basis, or as part of a process)

## III. Strategic Alternatives

a) Remaining Independent

1. "Just say no" defense is available as a legal matter, but may not be available in practice.

   - Refuse to redeem poison pill
   - Wage proxy fight to keep control of board (if board is staggered, bidder cannot get control and redeem pill without two annual meetings)

2. Consider expanded disclosures about company's standalone business plans and forecasts.

3. Consider actions which may increase shareholder value while also decreasing the company's attractiveness as a takeover target.

   - New acquisitions, which increase the scope and scale of the company
   - Asset sales or spin-offs
   - Share repurchases/self-tender
   - Issue tracking stock
   - Recapitalization

b) Merger of Equals

- MOEs offer an alternative to an outright sale; the two organizations of roughly similar size combine in a market-to-market deal, in an effort to create a more valuable combined company
- Early, proactive efforts to pursue mergers of equals are necessary, as they are generally impossible to implement as a takeover defense.
- Management and other "social" issues are key to an MOE's success or failure; these issues can be particularly challenging to address when combining companies with different corporate cultures.
- A variety of contractual and legal structures are available to implement agreements on social issues, although basic trust and common objectives are key.
- MOE parties must consider whether one or both will be "put in play" by announcement of the deal; consider shareholder vote requirements and alternative structures.
- Lock-up protections are appropriate to protect the transaction.
- MOEs can be "fair" even though higher short-term value could be obtained in an outright sale of the company.

c) Joint Ventures and Strategic Alliances

- Strategic alliances and joint ventures have significant control ramifications.
- These transactions raise complex tax, accounting and sale of control considerations, which must be carefully analyzed against the backdrop of alternate strategic options.
- These transactions often present all the complexities of a full acquisition with the added complexity of shared governance and the need to construct an inherently imperfect exit mechanism.
- Short-term objectives need to be carefully balanced against potential longer-term ramifications.

d) Sale of the Company

1. Options:

    - Locate white knight
    - LBO/MBO
    - Auction
    - Sell significant subsidiary or division ("crown jewel" or other)
    - Negotiate with bidder
    - Combined spin-off/sale (Morris Trust transactions)

2. Exploration by CEO of possible sale or merger (including strategic merger of equals) should only be undertaken after consultation with advisors and general discussion with the board.

3. Confidentiality/standstill agreements are not boilerplate forms and must be customized to specific circumstances.