

Recent Developments in M&A Law

The following contributions have been prepared and updated by some of the speakers in the 'Recent developments in M&A law' session that was held during the IBA 2004 Annual Conference in Auckland.

United States

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Until the end of 2004, M&A activity in the United States was relatively measured, and well below levels seen in 1999 and 2000. However, activity in December 2004, which totalled US\$284 billion worldwide, established a record for the month of December. This upward trend is continuing in 2005. According to a June article in *New York Times*, if the trend continues this will be the fourth largest year, by deal size, in merger history.

There are several reasons for the recent increase in merger activity. Last year's activity was suppressed for several reasons: caution over recent legislation, such as the Sarbanes-Oxley Act of 2002; uncertainty about the war in Iraq and the 2004 election; the weakened financial position of companies; and concern over powerful investment groups, such as The California Public Employees' Retirement System (CAIPERS), seeking to take a proactive role in the governance of companies. Events and perceptions unfolding towards the end of 2004 have worked to dispel many concerns about these issues.

Companies are finally getting accustomed to recent corporate governance legislation. According to the 2005 Global CEO Survey by PriceWaterhouseCoopers, 68 per cent of CEOs are confident that their organisations can respond to US laws and regulations relating to corporate governance, risk management and compliance. This increased comfort with compliance has also translated into increased trust in the accuracy of companies' financial statements.

The common perception is that much of the US political uncertainty has dissipated as a result of developments in Iraq and the conclusion of the US elections. The situation in Iraq, while far from concluded, has somewhat stabilised with the successful election of an Iraqi Government. Additionally, the Republican victory in the 2004 US election put to rest some fears of the repeal of the Bush tax cuts, and concerns about congressional refusal to bail out the airlines.

Another reason for the recent increased activity is that companies are in better financial positions than they were in 2004. Many companies have accumulated

substantial cash reserves, which can be used for acquisitions. Also, debt financing is available at interest rates which are still low compared to recent historical averages.

According to lawyers, institutional shareholders, executives, directors and other experts, 'the white-hot movement' to overhaul corporate governance has cooled in recent months in Washington and beyond. Although there is little argument on the existence of the cooling, the interpretations of this sudden, little discussed shift vary widely. 'The pendulum has begun to swing back,' said John C Coffee Jr, a securities law professor at Columbia University Law School. 'We are now seeing the counter reaction to the reform movement of the last few years', states Kurt Eichenwald in 'Reform Effort at Businesses Feels Pressure' *New York Times*, 14 January 2005.

With the perception that the concerns that suppressed activity in much of 2004 are dissipating, companies were free to do deals in December, 2004 and 2005. The following are some of the largest recent deals:

- Procter & Gamble's announced acquisition of Gillette (US\$54 million).
- Sprint's announced acquisition of Nextel (US\$35 billion).
- Johnson & Johnson's announced acquisition of Guidant (US\$25 billion).
- SBC's completed merger with AT&T (US\$16 billion).
- Federated Department Stores' announced acquisition of May Department Stores (US\$11 billion).
- Kmart's completed merger with Sears (US\$11 billion).
- Oracle's completed acquisition of PeopleSoft (US\$10 billion).
- MCI's announced merger with Verizon (US\$8.5 billion).
- Washington Mutual's announced merger with Provident Financial (US\$6.5 billion).
- ProLogis' announced merger with Catellus Development (US\$3.6 billion).
- Weatherford International's announced acquisition of the energy services and international drilling division of Precision Drilling (US\$2.28 billion).

The ProLogis/Catellus merger is particularly noteworthy, because Real Estate Investment Trust (REIT) mergers are one area where activity had grown in 2004 and has continued to show activity in 2005. In 2004, REIT mergers totalled more than US\$34 billion,

a 500 per cent increase over the previous year, according to Stan Luxenberg of National Real Estate Investor. According to a major player in the area, they had been receiving money faster than they could identify assets to purchase. In addition to the REIT area, there has been an abundant amount of activity in private transactions involving corporations and

alternative entities: restructurings; sales of assets; joint ventures; private REITs; acquisitions of equity interests; and hedge funds.

Further, recent history has also provided a profuse amount of legal activity in Delaware. Below are some noteworthy Delaware cases relating to mergers:

- *Alessi v Beracha*, (Del Ch 11 May 2004) (upheld claim of failure to disclose merger negotiations at time of buy-back programme);
- *Aspen Advisors LLC v United Artists Theatre Co*, (Del 23 November 2004) (affirming Court of Chancery dismissal of warrant holders' claim of breach of warrant contract in connection with merger);
- *CalPERS v Lone Star Steakhouse and Saloon, Inc* (Del Ch 14 April 2005) (court held that change in control payments, which were triggered if the board became composed of a majority of directors who were not approved by the then existing directors or other directors approved by them, were not a violation of Delaware's dead hand poison pill doctrine, because the approval vote was not a board action).
- *Gilliand v Motorola, Inc* (Del Ch 8 October 2004) (summary judgment granted to plaintiffs on duty of disclosure claim seeking quasi-appraisal remedy – short-form merger notice did not include any financial information about merged-out company).
- *Hollinger v Hollinger International, Inc*, (Del Ch 29 July 2004) (preliminary injunction denied – challenged transaction was not sale of substantially all of the assets requiring shareholder vote).
- *In Re Emerging Communications, Inc*, (Del Ch 3 May 2004) (directors found to have breached fiduciary duty of entire fairness in connection with going private transaction);
- *In Re Cox Communications, Inc Shareholders Litigation*, (Del Ch 6 June 2005) (court voiced its opinion that the decision in *Kahn v Lynch Communications* was encouraging frivolous class-action litigation by lawyers looking solely to settle the action for the concomitant attorney's fees, and suggested a reform to the Supreme Court's rule regarding the application of the business judgment rule to going private mergers).
- *In Re The Mony Group, Inc Shareholder Litigation*, (Del Ch 18 February 2004) (injunction granted based on misleading disclosures).
- *In Re Oracle Corp Derivative Litigation* (Del Ch 2 December 2004) (summary judgment granted to defendants as to claim that officers breached their duty of loyalty by selling company stock).
- *McGowan v Ferro*, (Del Ch 8 October 2004) (summary judgment granted to defendants on merger consideration and corporate opportunity claims; summary judgment denied as to one corporate opportunity claim).
- *Orman v Cullman*, (Del Ch 20 October 2004) (court upheld voting agreement and fiduciary out clause in connection with merger).
- *Prime Hospitality, Inc Shareholders Litigation*, (Del Ch 4 May 2005) (rejected a class-action settlement of claims relating to acquisition of a hotel company, where plaintiffs sought to surrender a Revlon claim even though the buyer immediately sold part of the company's assets for more than it paid for the entire company).
- *Production Resources Group, LLC v NCT Group, Inc*, (Del Ch 17 November 2004) (director personal liability protection extended to derivative claims by creditors).
- *Tooley v AXA Financial, Inc*, (Del Ch 13 May 2005) (court refused to dismiss a claim for breach of duty of loyalty where corporation extended a tender offer to allegedly benefit its majority stockholder).

Note

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