

Business Associations II, Simulation 3: Mergers & Acquisitions

From: Wendy I. Zeller [mailto:Ms.WIZ@work.com]
To: Project Titanic mailing list
Sent: Wednesday, March. 12, 2009 8:00 AM
Subject: The Big Deal

Welcome aboard 'Project Titanic'! Most of us just call it 'the big deal'. It's going to be our biggest merger of the year, and you were assigned to help me structure it.

To maintain confidentiality, I will use codenames for the relevant corporations rather than their real names. Our client, to which we gave the codename Norman, is taking over another corporation, code-named Anglo-Saxon. The investment bankers have already hammered out the main details. Norman will pay \$40 billion for Anglo-Saxon: \$10 billion in cash, and the other \$30 billion in shares of the merged company. This is a friendly deal – both Anglo-Saxon's board and Norman's board are inclined to approve it.

There's a catch, though. Anglo-Saxon has a joint venture with a corporation codenamed Viking, to produce nuclear-powered widgets (NPWs). Under the joint venture, Viking has NPW marketing rights in the United States & Canada, and Anglo-Saxon has NPW marketing rights in the rest of the world. Norman's investment bankers estimate that Anglo-Saxon's NPW marketing rights are worth about \$10 billion. That's not exactly petty cash.

The joint venture includes the following clause:

Change in Control. If either party is acquired by a third party or otherwise comes under Control (as defined in Section 1.4 above) of a third party, it will promptly notify the other party not subject to such change of control. The party not subject to such change of control will have the right, however not later than thirty (30) days from such notification, to notify in writing the party subject to the change of Control of the termination of the Agreement taking effect immediately. As used herein "Change of Control" shall mean (i) any merger, reorganization, consolidation or combination in which a party to this Agreement is not the surviving corporation; or (ii) any "person" (within the meaning of Section 13(d) and Section 14(d)(2) of the Securities Exchange Act of 1934), excluding a party's Affiliates, is or becomes the beneficial owner, directly or indirectly, of securities of the party representing more than fifty percent (50%) of either (A) the then-outstanding shares of common stock of the party or (B) the combined voting power of the party's then-outstanding voting securities; or (iii) if individuals who as of the Effective Date constitute the Board of Directors of the party (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board of Directors of the party; provided, however, that any individual becoming a director subsequent to the Effective Date whose election, or nomination for election by the party's shareholders,

was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board [...]

Section 1.4 of the joint venture agreement defines control as:

the ability of any entity (the “Controlling” entity), directly or indirectly, through ownership of securities, by agreement or by any other method, to direct the manner in which more than fifty percent (50%) of the outstanding voting rights of any other entity (the “Controlled” entity), whether or not represented by securities, shall be cast, or the right to receive over fifty percent (50%) of the profits or earnings of, or to otherwise control the management decisions of, such other entity (also a “Controlled” entity).

As you can see, this means that if Norman buys Anglo-Saxon, Viking could terminate the joint venture. Other provisions of the joint venture agreement specify that when the joint venture is terminated, Viking retains all rights regarding NPWs, so such termination would cause a \$10 billion reduction in the value of Anglo-Saxon.

Needless to say, that would be a deal breaker for our merger. So, we need to figure out how to have Norman buy Anglo-Saxon (paying \$10B in cash & \$30B in stock) without triggering the change of control clause. That’s not easy – the clause was tailored precisely to catch deals such as this. But finding creative ways around such problems is why we’re paid big bucks.

Thanks,

Ms. WIZ