Strafford

Presenting a live 90-minute webinar with interactive Q&A

Going-Private Transactions: Strategic Considerations

Deal Structures, Fiduciary Duties, Procedural Safeguards, Disclosure Obligations

WEDNESDAY, OCTOBER 28, 2020

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

Daniel Grabos, Managing Director, Co-Head of Industrials M&A, **Barclays**, New York

Phillip R. Mills, Partner, **Davis Polk & Wardwell**, New York

The audio portion of the conference may be accessed via the telephone or by using your computer's speakers. Please refer to the instructions emailed to registrants for additional information. If you have any questions, please contact **Customer Service at 1-800-926-7926 ext. 1**.

Tips for Optimal Quality

FOR LIVE EVENT ONLY

Sound Quality

If you are listening via your computer speakers, please note that the quality of your sound will vary depending on the speed and quality of your internet connection.

If the sound quality is not satisfactory, you may listen via the phone: dial **1-877-447-0294** and enter your **Conference ID and PIN** when prompted. Otherwise, please **send us a chat** or e-mail **sound@straffordpub.com** immediately so we can address the problem.

If you dialed in and have any difficulties during the call, press *0 for assistance.

Viewing Quality

To maximize your screen, press the 'Full Screen' symbol located on the bottom right of the slides. To exit full screen, press the Esc button.

Continuing Education Credits

FOR LIVE EVENT ONLY

In order for us to process your continuing education credit, you must confirm your participation in this webinar by completing and submitting the Attendance Affirmation/Evaluation after the webinar.

A link to the Attendance Affirmation/Evaluation will be in the thank you email that you will receive immediately following the program.

For additional information about continuing education, call us at 1-800-926-7926 ext. 2.

Program Materials

FOR LIVE EVENT ONLY

If you have not printed the conference materials for this program, please complete the following steps:

- Click on the link to the PDF of the slides for today's program, which is located to the right of the slides, just above the Q&A box.
- The PDF will open a separate tab/window. Print the slides by clicking on the printer icon.

Going Private Transactions – Strategic Considerations

Presented by Dan Grabos (Barclays) and Phillip Mills (Davis Polk)

October 28, 2020

BARCLAYS Davis Polk

Overview

What is a "going private" transaction?

- "Going private" generally refers to a minority buyout by a **controlling or significant stockholder**, or a leveraged buyout by one or more financial sponsors working with a **significant stockholder / management**.

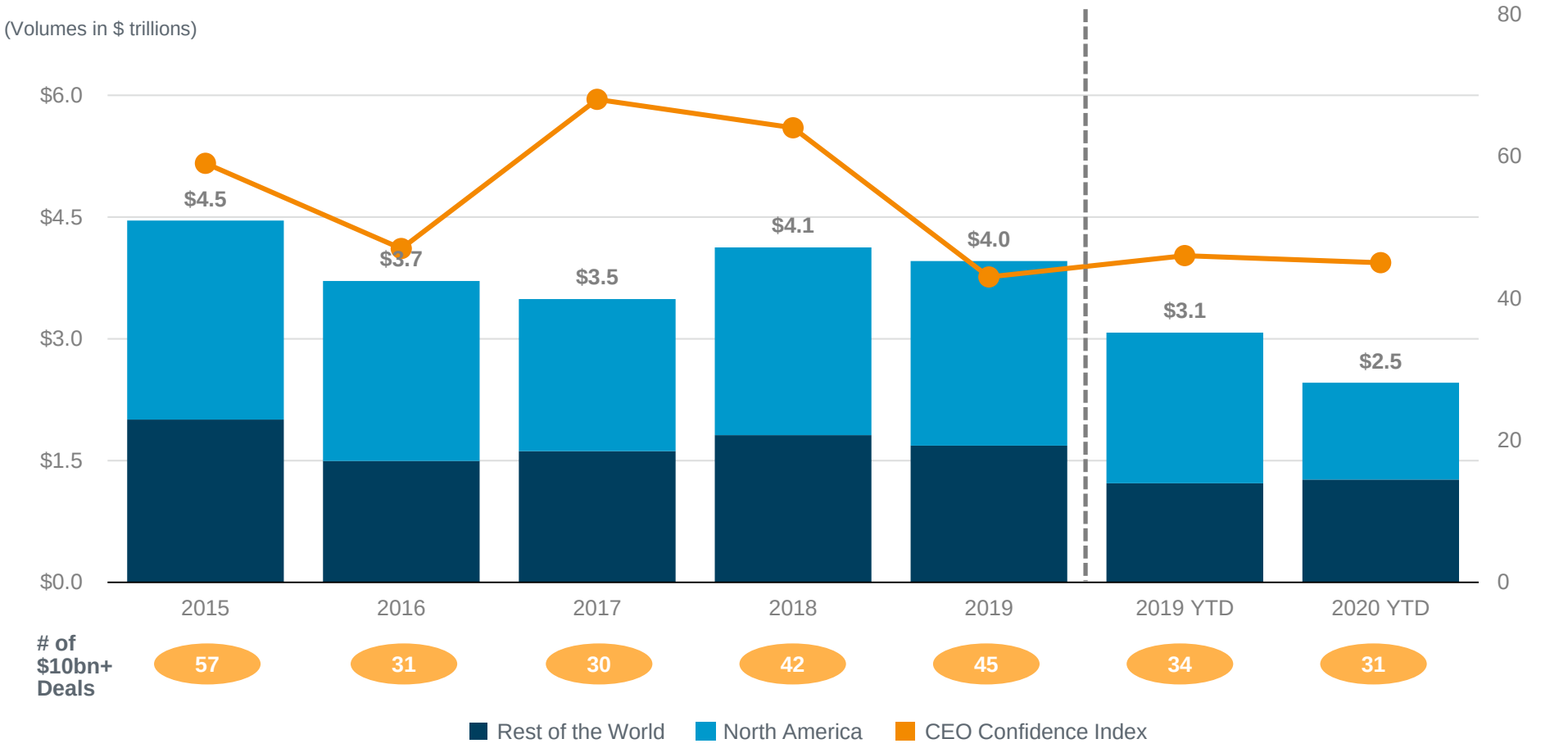
Key distinctions from private deals / other public deals*

- Controlling stockholder fiduciary duties / standards for judicial review affect processes and deal structures.
  - Conflicts of interest are material and obvious.
  - Fiduciary duty implications where a "controlling shareholder" is involved.
  - Working with special committees vs. full board.
  - Majority-of-minority considerations.
- Public disclosure requirements.
  - Enhanced disclosure obligations (Schedule 13E-3) whenever an affiliate is involved on the buy-side.
  - Potential to trigger premature Schedule 13D filing requirements.
    - **New Schedule 13D filing**. Forming a "group" that owns more than 5% of target's outstanding stock.
    - **Amending Schedule 13D filing**. Engaging with an existing Schedule 13D filer in a manner that requires an amendment to their filing to indicate "plans or proposals" for a going private transaction.
- Section 203 of the Delaware General Corporation Law – potential 3-year moratorium imposed if bidder has an "agreement, arrangement or understanding" with a person holding at least 15% of target's voting securities before the target board has approved the transaction.
- Use of books & records demands to search for potential conflicts / litigation hooks.
- MLPs / LPs / LLCs – typically, contractual standards apply in lieu of fiduciary duties but subject to the implied covenant of good faith and fair dealing.

* Discussion assumes Delaware law applies. Other states may apply different standards.

Recent M&A Volume is Down vs. 2019 but Large Deals are Still Being Announced

Global M&A Announced Transaction Volume



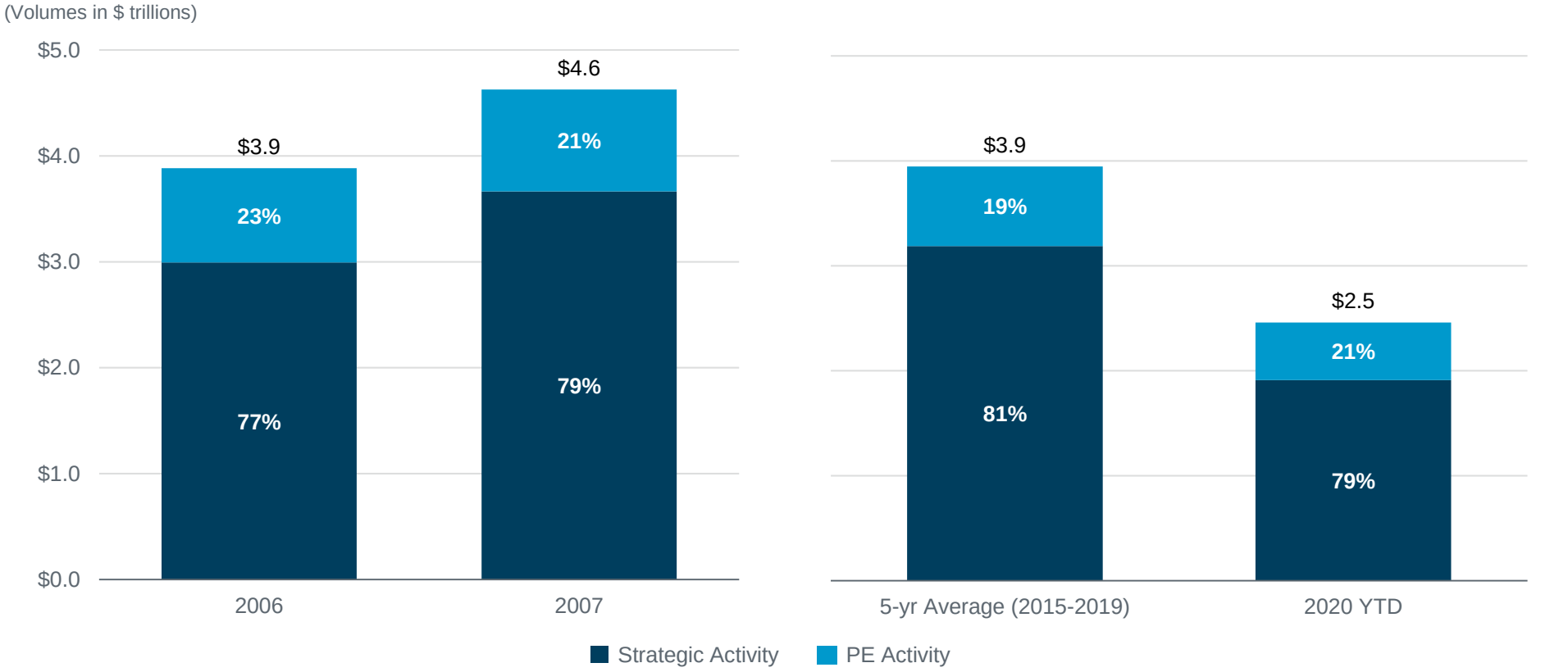
Source: Dealogic, Conference Board and FactSet. 2020 through 08/31/2020.

Private Equity Activity Remains In-Line With Historical Averages

Private Equity Activity as % of Total M&A Activity

Pre-Financial Crisis PE Peak

Historical PE Average vs. YTD



Source: Dealogic as of October 16, 2020.

Fiduciary Issues and Standard for Judicial Review

GOING PRIVATE TRANSACTIONS RAISE SPECIAL ISSUES BECAUSE CONFLICT TRANSACTIONS ARE PRESUMPTIVELY SUBJECT TO ENTIRE FAIRNESS LEVEL OF JUDICIAL REVIEW

When does entire fairness standard of review apply?

1. Controlling stockholder **stands on both sides of the transaction** or receives **different consideration** than other stockholders.
2. Majority of the board is conflicted / interested.

Who is a "controlling stockholder"?

- A controlling stockholder (i) owns more than **50%** of the voting power of the corporation **or** (ii) exercises **control** over the business and affairs of the corporation.
- A minority stockholder can (in very limited circumstances) be a controlling stockholder if it has such **"formidable voting and managerial power"** that, as a practical matter, it is no differently situated than if it had majority voting control.

"Disinterestedness" of directors focuses on material pecuniary interests (but relationships and not meeting "independence" tests matter too).

Fiduciary Issues and Standard for Judicial Review

ENTIRE FAIRNESS REVIEW AND THE BURDEN OF PROOF

- If entire fairness standard of review applies, absent a mitigant, **the controller / conflicted party carries the burden of proof** (i.e., must establish fairness).
- Courts must determine whether transaction included a "**fair price**" and "**fair process**" – was it objectively fair to the stockholders?
- Assessment is made **after trial**.
  - Fact intensive inquiry.
    - "Fair price" inquiry – valuation; exploration of viable alternatives.
    - "Fair process" inquiry – timing of transaction; arms-length bona fide bargaining; coercion and threats; structure of transaction; material information withheld from voting / tendering stockholders.
  - Hindsight assessment.
  - Allows for comprehensive discovery process – information may be discovered that the parties were not aware of at the time of negotiating the transaction.
  - **Undisclosed conflicts of advisors** to special committees can taint the fairness assessment.
- Very expensive / burdensome / intrusive process = **high settlement value**.

Fiduciary Issues and Standard for Judicial Review

WHAT PARTIES CAN DO TO MITIGATE RISK OF ENTIRE FAIRNESS REVIEW

1. *MFW* alternative.

- Parties may be able to escape entire fairness altogether (and return to business judgment rule) by using a **special committee** and including a **majority-of-the-minority** vote, so long as this "**non-waivable" requirement** was imposed by the bidder **prior to the start of substantive economic negotiations**.

2. Burden Shifting.

- Burden can be shifted to stockholder plaintiffs to prove that the transaction was not fair if certain procedural safeguards are used.
  - Negotiated approval of a **fully-functioning** special committee of disinterested directors; or
  - Obtaining approval of the transaction by a **fully-informed** majority-of-the-minority shareholders.

3. Non-Coervice Tender Offer.

- Historically, Delaware courts have not generally applied entire fairness review to **non-coervice** tender or exchange offers with a second-step squeeze-out above 90% without corporate action.
  - Offer conditioned on majority-of-the-minority tendering into the offer.
  - Controlling stockholder has committed to complete a short-form merger at the same price promptly after tender offer is completed.
  - No retributive threats by the controlling stockholder to minority stockholders if they do not tender into the offer.
  - Distinterested directors are given complete discretion and sufficient time to react to tender offer via Schedule 14D-9 filing.
- Structure depends on not needing any board approval (e.g., due diligence, waivers, consents).

Fiduciary Issues and Standard for Judicial Review

"FULLY-FUNCTIONING" SPECIAL COMMITTEE APPROVAL REQUIRES REPLICATING ARMS-LENGTH BARGAINING ON BEHALF OF THE PUBLIC STOCKHOLDERS

- Special committees are needed when **managing conflicts** – either resulting from controlling stockholder or interested-director transactions.
- When confronting a transaction that may be subject to entire fairness review, a board of directors should create a special committee early in the process.
- A proper special committee must be independent and should have full authority to:
  - **Reject any deal**.
  - Hire **independent advisors**.
  - **Explore other viable alternatives**, including a new business plan / capital structure that might offer superior value.
- A controlling / significant stockholder can (and typically will) use its stockholding to block a sale of the company.
- Typically, delay and the power to say "no" are the most powerful negotiating tools the special committee has and those tools can be used effectively by a well-advised and disciplined committee that recognizes the risk to the bidder from coercive responses.
- A board can approve a deal recommended by a special committee. Proceeding with a deal that is not recommended by the special committee is subject to entire fairness judicial review.
- A deal recommendation from a properly functioning special committee process provides strong evidence that a transaction was the result of a fair process.

Private Equity Has Expanded in Scope and Maintains Significant Firepower

Types of Private Equity Capital

Private Equity

The Carlyle Group

KKR

Blackstone

Pension Funds – Direct Investing

CPP Investment Board

AIMCo

Sovereign Wealth Funds

ADIA

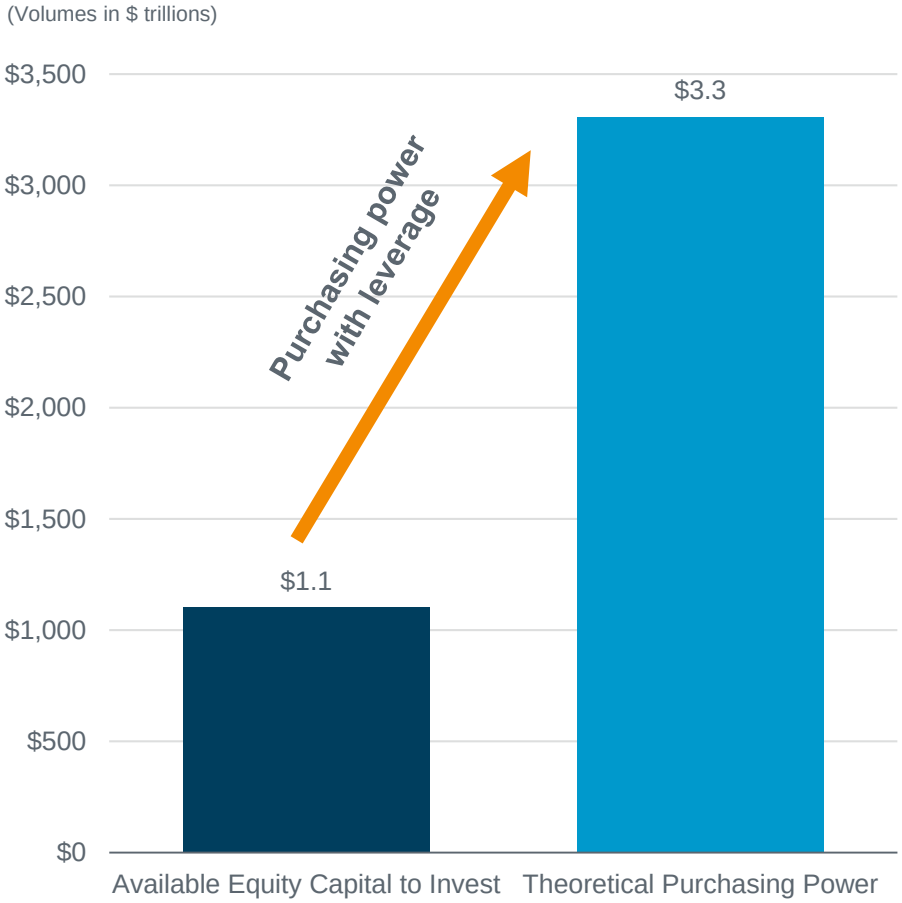
TEMASEK

Family Offices

Koch Industries Inc

Pritzker Group Private Capital

Private Capital Available & Purchasing Power[(1)]

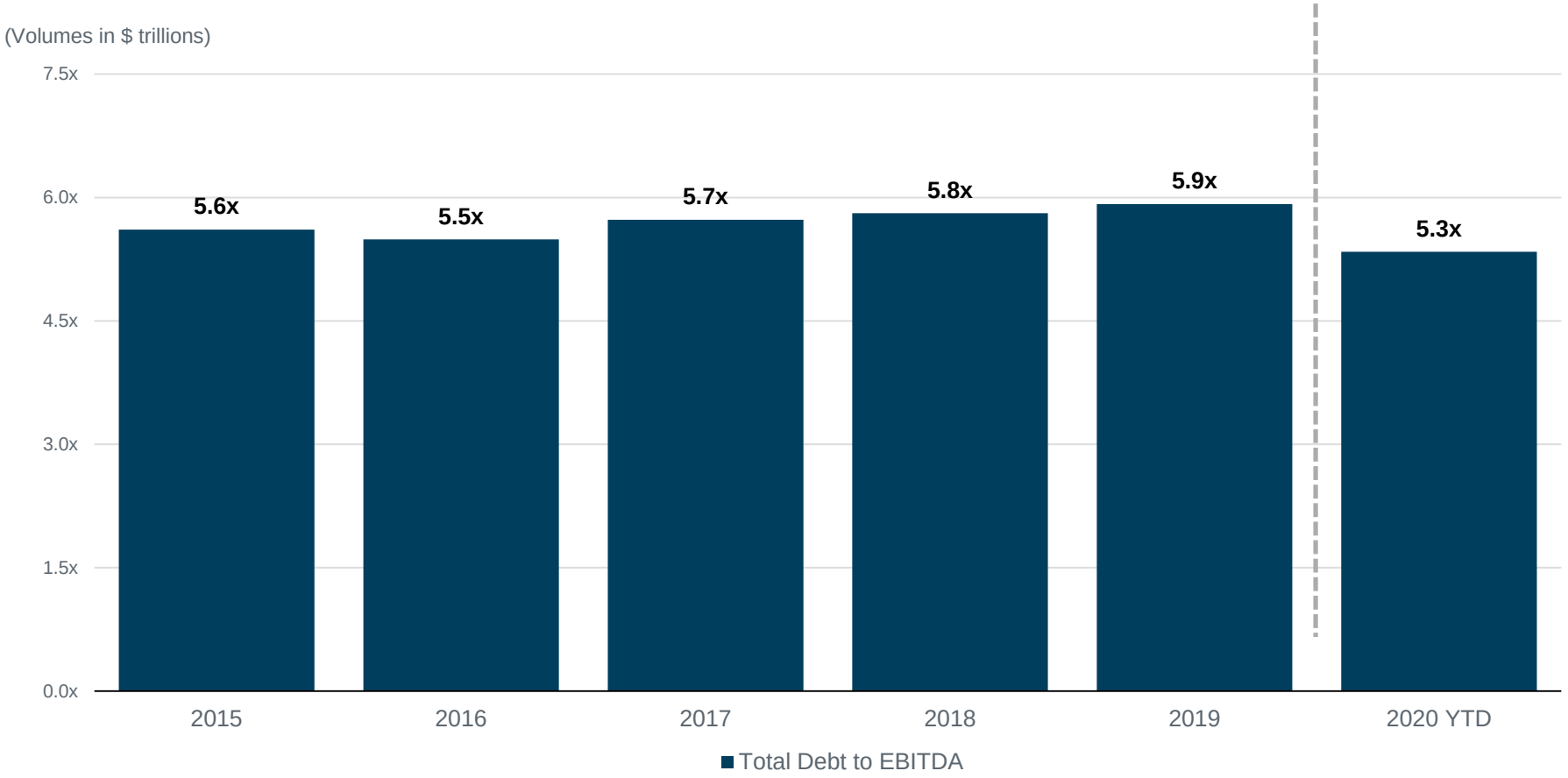


Source: Dealogic. 2019 through 12/31/2019.

(1) Based on 2019 total cumulative dry powder.

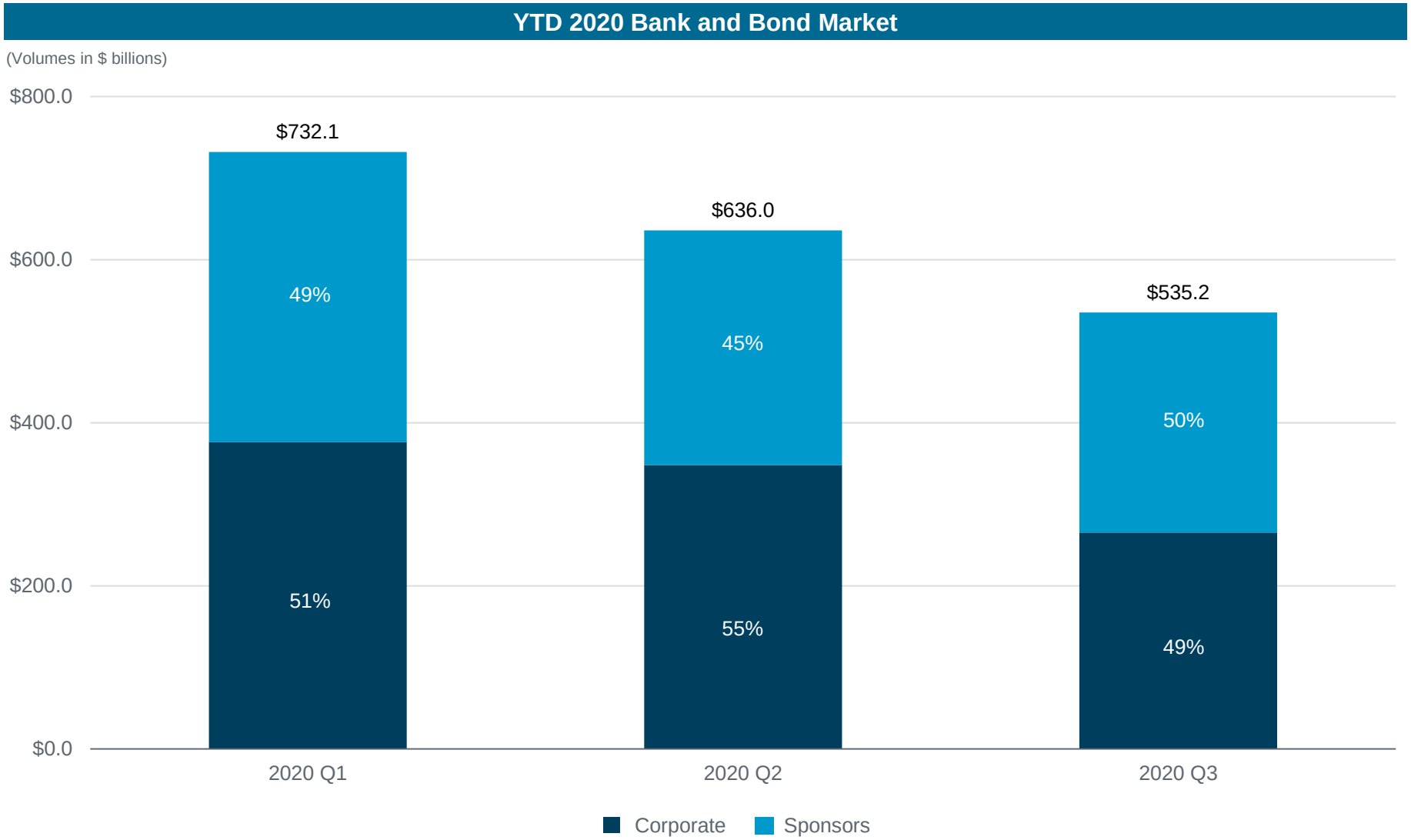
Leverage Buyout Debt Multiples Continue to be Robust

Total Debt to EBITDA Multiples



Source: S&P Global. 2020 through 08/31/2020.
Note: Multiples represent Debt/EBITDA for all LBO transactions.

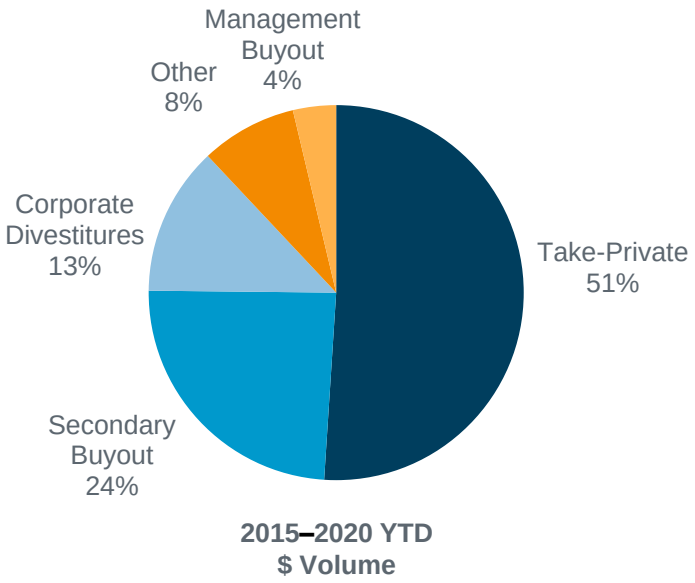
Leverage Finance Market Has Experienced Lower Volumes During COVID but LBO Financing Remains Available



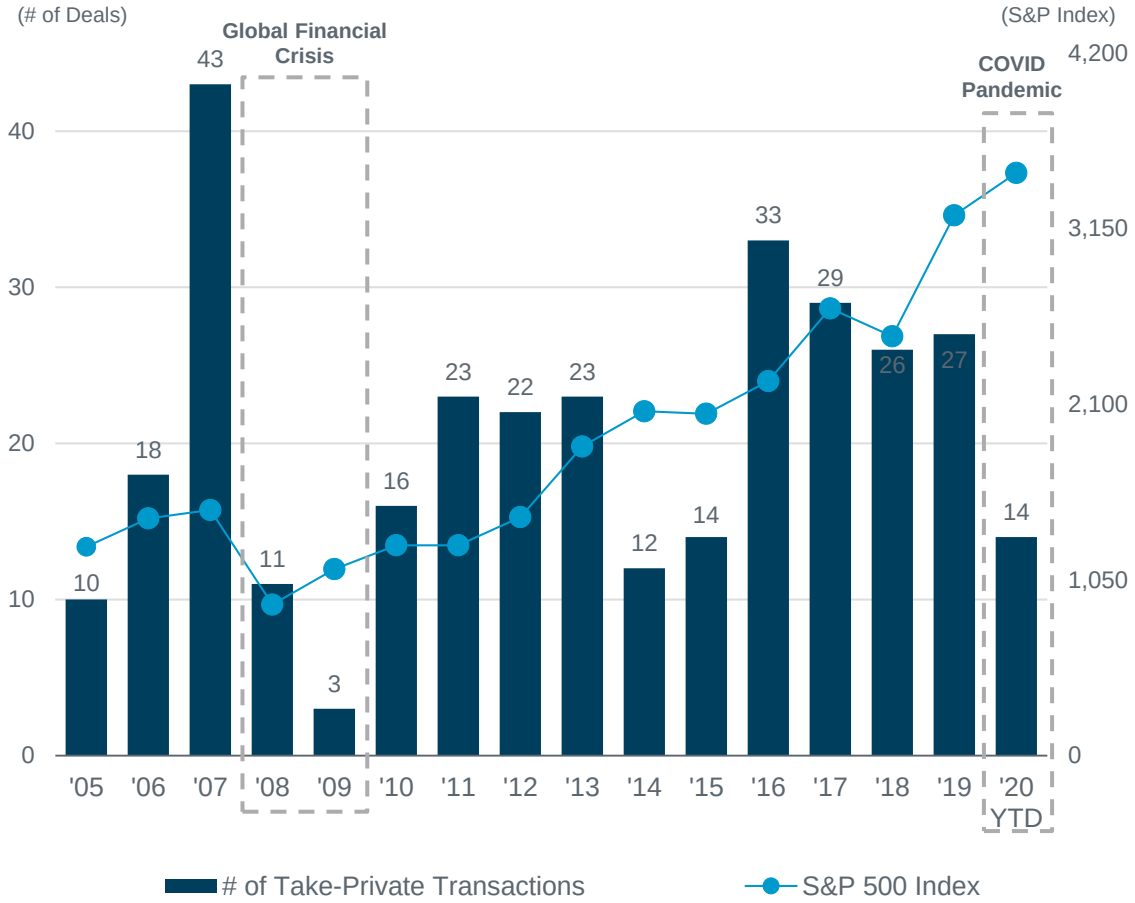
Source: S&P Capital IQ as of October 23, 2020.

Take-Private Transactions Constitute a Significant Proportion of PE Activity

PE Deal Types



PE Take-Private Transactions Tend to Lag Equity Markets



Source: Pitchbook. 2020 through 8/31/2020
Note: Only US take-private transactions over $250mm of enterprise value.

Disclosure Requirements

EXPANDED DISCLOSURE REQUIREMENTS APPLY TO TRANSACTIONS SUBJECT TO THE RULE 13E-3 "GOING PRIVATE" RULES

Is this a "Rule 13e-3 transaction"?

- Generally applicable to transactions where an affiliate is **engaged** in the transaction.
  - Controlling stockholders and members of senior management (e.g., CEO and CFO) are considered to be affiliates.
  - Factors in determining whether senior management is "engaged" in a transaction:
    - Senior management's role with the target company, the buyer and its affiliates following the transaction;
    - **Equity rollovers** and/or **material equity participation**;
    - Representation of senior management on the buyer's or target company's board after the transaction; and
    - Involvement of senior management in the negotiation and process of the transaction.
  - The **timing of management becoming involved** on the buy side is an important determinant.

Implications of triggering Rule 13e-3

- The **target company** and **each affiliate engaged** in the going private transaction must file a Schedule 13E-3 with the SEC.

Disclosure Requirements

ENHANCED DISCLOSURE OBLIGATIONS IN A RULE 13E-3 TRANSACTION

1. Purposes of the transaction. Target company and each affiliate engaged in the transaction must disclose its purposes for the transaction.

2. Fairness of the transaction. Each filing person must **state its belief and reasons** as to whether the transaction is fair to the minority shareholders.

3. Reports, opinions, appraisals. All reports, opinions and appraisals prepared by either party's advisors.

- Financial advisors should prepare **any presentations (not just the final books)** with input and advice of counsel before being rendered. These materials will need to be described in an SEC filing and filed.

- Rule 13e-3 transactions are **more closely reviewed by the SEC** and typically draw more **interest from plaintiffs' lawyers**.
- Fertile opportunity to establish that a majority-of-the-minority approval was **not "fully-informed"**.

Other Considerations

CAREFUL PROCESS IS NEEDED TO AVOID PREMATURE 13D DISCLOSURE OBLIGATIONS AND STATUTORY BUSINESS COMBINATION MORATORIUM PERIODS

- **Section 13(d) of the Exchange Act.**
  - Generally requires 5% shareholders to publicly disclose their current shareholdings and intentions on a prompt basis (subject to exceptions for passive investors, among others).
    - If a buyer teams up with management or other significant stockholders (e.g., bidco), they may **prematurely form a "group"** for purposes of this 5% threshold and trigger a separate Schedule 13D filing obligation (and premature public disclosure of discussions).
    - If a buyer engages with an existing Schedule 13D filer, that Schedule 13D filer may be required to amend its Schedule 13D filing to indicate **new "plans or proposals"**.
- **Section 203 of the Delaware General Corporation Law.**
  - Generally prohibits an "interested stockholder" from engaging in certain business combination transactions for a three-year period if it "owns" (very broadly defined) 15% or more of target's voting securities, unless it first obtains the target board's approval or the business combination is approved by the target board and more than two-thirds of the voting power not held by the buyer.
    - If a buyer / bidco teams up with a significant stockholder without board approval, it could become subject to moratorium period.
    - If a buyer / bidco has any "**agreement, arrangement or understanding for the purpose of acquiring, holding, voting…or disposing of such stock** with another person who owns, or whose affiliates or associates beneficially own [target stock]," the buyer will be deemed to own that stock as well.
    - Even if the target has waived the application of Section 203 to that other person, buyer / bidco will nonetheless be frozen out unless buyer obtains its own waiver.

Other Considerations

BOOKS & RECORDS

- Section 220 of the Delaware General Corporation Law permits a company's stockholder to demand inspection of the company's books and records for any "proper purpose."
- Delaware courts have broadly interpreted **"proper purpose"** to include many different things.
  - Investigate mismanagement or wrongdoing;
  - Evaluate whether to bring claims for breach of fiduciary duty; and
  - Evaluate director independence or interestedness.
- A stockholder is entitled to inspect books and records upon showing a **"credible basis"** for its purpose in seeking the information, which is the lowest burden of proof in Delaware law.
- Several recent Delaware books-and-records decisions have noted the **absence of one or both of the *MFW* conditions is sufficient to "pique suspicion"** about a transaction.
- Stockholders are often successful in obtaining a company's formal books and records such as board minutes and packages.
- Recent Delaware decisions have required companies to **turn over emails and texts** between / among directors, financial advisors, management, and bidders.
- The absence of books and records can be used as an inference that a proper process was not followed.

Transaction Structuring

MOST LBOS ARE STRUCTURED AS ONE-STEP MERGERS

- In the last three years, only approximately **11%** of leveraged buy-outs of Delaware public targets were structured as two-step transactions.
- This could be attributable to a number of factors, including:
  - The presence of additional regulatory approvals, undercutting the timing benefit of a two-step transaction.
  - Existence of a "go shop" period, which may reduce or eliminate the relevant timing benefit of a tender offer.
  - Certain requirements can limit the buyer's flexibility in connection with its financing (e.g., potential margin loan constraints and uncertainty regarding marketing periods).
    - Despite the introduction in Delaware of mechanics to permit the merger to be effected immediately after the tender offer (Section 251(h)), debt financing sources will still closely scrutinize risks to getting the acquisition debt moved into the target company to avoid structural subordination.
  - There is arguably some ambiguity as to whether offering senior executives or other insiders the right to "roll over" into the buyer vehicle violates the "all holders / best price" rule, though most practitioners believe it does not.
    - In 2006, the SEC amended the tender offer rules to exempt certain employment-related arrangements from the "all holders / best price" rule. However, these amendments did not specifically address non-employment-related arrangements like a rollover of shares held by management. In addition, in order to benefit from the safe harbor provided by that amendment, the target compensation committee (or board) must generally approve the arrangements.

Management Incentives in Take-Private Transactions

Entry and Exit Capital Structure

Equity Incentives for PE and Management

($ in millions)	Entry	Exit
PE Investor	$290	$562
Management Co-Investment	10	23
Management Based Options	—	15
	$300	**$600**

Transaction Structuring

KEY ISSUES WHEN ADVISING A MANAGEMENT TEAM / BOARD

- To avoid unintended consequences, a target company's board or management team should carefully consider several key issues **before** initiating a going private transaction.
  - When should management **bring its board into the loop**?
  - **Issues in sharing information** with sponsors and financing sources.
    - Management may become "engaged" in the transaction and trigger Rule 13e-3.
  - Implications of board's **responsibility to maximize value**.
  - Board's responsibility to ensure management's alignment with a sponsor **must not foreclose other bidders**.
  - **How to develop projections and handle due diligence** when management has an interest in a particular bidder.
  - How **few transactions ultimately proceed to announcement** and the scrutiny they attract – e.g., Dell.
  - **Management's incentives to "sandbag" every step of the way** – e.g., taking steps to move pre-closing cash flow to post-closing.

MLPs / LPs / LLCs

CONFLICTS ARE TYPICALLY GOVERNED BY CONTRACTUALLY-DEFINED STANDARDS WITHOUT FIDUCIARY DUTIES BUT SUBJECT TO THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

- Limited partnerships and LLCs have **contractual governance models**.
- PTPs / MLPs typically eliminate entirely (or greatly limit) the fiduciary duties of the general partner and board of the general partner.
- In lieu of fiduciary duties, PTPs / MLPs often adopt contractual standards such as "**good faith**" which may be narrowly defined (e.g., believed to be in the interests of the partnership; or not opposed to the interests of the partnership).
- The **implied covenant of good faith and fair dealing** cannot be contractually eliminated.
- PTPs / MLPs typically provide for one or more of the following options for conflict transactions:
  - **Approval by a conflicts committee** of the board (typically a committee consisting of directors who meet the listing standards for "independence", sometimes audit committee "independence" standards) which itself is not subject to fiduciary duties.
  - Approval by a majority of the unaffiliated unitholders.
  - Board approval.
  - Arms-length terms.
  - "Fair and reasonable" terms.

Disclaimer

This document has been prepared by Barclays Capital Inc. ("Barclays") for information purposes only. This document is confidential and is for the intended recipient and cannot be redistributed, published, reproduced or disclosed, in whole or in part, without the prior written permission from Barclays. This document is an indicative summary of the terms and conditions of the securities/transaction described herein and may be amended, superseded or replaced by subsequent summaries. The final terms and conditions and any applicable risk factors of the securities/transaction will be set out in full in the applicable offering document(s) or binding transaction document(s).

This material has not been produced by the Barclays Group's research department and does not constitute investment research or a research recommendation for the purposes of Financial Conduct Authority rules or a research report under U.S. law. The Barclays Group's research analysts and research departments are independent from Barclays' banking business and are subject to certain regulations and internal policies. The Barclays Group's research analysts may hold and make statements or investment recommendations and/or publish research reports with respect to any company referred to herein, the transactions contemplated herein or any person involved therein or related thereto that differ from or are inconsistent with the views or advice communicated by Barclays' banking business.

Prices shown in this document are indicative only and Barclays is not offering to buy or sell, or soliciting offers to buy or sell any financial instrument. Unless otherwise specified, the source for all graphs, charts, and other information is Barclays. Barclays' databases are derived from various internal and external sources. Barclays makes no warranty or representation, express or implied, as to the accuracy or completeness of information which is contained in this document and which is stated to have been obtained from or is based upon trade and statistical services or other third party sources. Any data on past performance, modelling, scenario analysis or back-testing contained herein is no indication as to future performance. No representation is made as to the reasonableness of the assumptions made within or the accuracy or completeness of any modelling, scenario analysis or back-testing or any other information contained herein. All levels, prices and spreads are historical and do not represent current market levels, prices or spreads, some or all of which may have changed since the issuance of this document. All opinions and estimates are given as of the date hereof and are subject to change, and Barclays assumes no obligation to update this document to reflect any such changes. The value of any investment may also fluctuate as a result of market changes. The information herein is not intended to predict actual results and no assurances are given with respect thereto.

The recipient is responsible for making its own independent investigation and appraisal of the risks, benefits, appropriateness and suitability of any transaction or matter contemplated by this document. Barclays is not making any recommendation (personal or otherwise) or giving any investment advice. The decision to proceed with any transaction or action contemplated by this document must be made by the recipient in light of its own commercial assessments, and Barclays will not be responsible for such assessments. Barclays is not responsible for providing or arranging for the provision of any general financial, strategic or specialist advice, including legal, regulatory, accounting, model auditing or taxation advice or services or any other services in relation to the transaction and/or any related securities described herein.

Neither Barclays nor any of its subsidiaries or affiliates, nor any of their respective officers, directors, employees, agents, advisors or other representatives (Barclays together with such persons being the "Barclays Group") accepts any liability whatsoever for any direct, indirect or consequential losses (in contract, tort or otherwise) arising from the use of this document or its contents or any reliance on the information contained herein. Barclays Group is not responsible for any specialist advice, including legal, regulatory, accounting, model accounting, tax, actuarial or other advice.

This document does not constitute nor does it form part of an offer to sell or purchase, or the solicitation of an offer to sell or purchase, any securities or any of the businesses or assets described herein or an offer or recommendation to enter into any transaction described herein nor does this document constitute an offer or commitment to provide, arrange or underwrite any financing.

Members of Barclays Group are involved in a wide range of commercial banking, investment banking and other activities out of which conflicting interests or duties may arise. Barclays Group may make a market or deal as principal in the securities mentioned in this document or in options or other derivatives based thereon. Barclays Group may be on the opposite side of any orders executed for securities or financial instruments that are related to or the subject of this document. In addition, Barclays Group may also, from time to time, effect transactions for its own account or the account of its clients and hold long or short positions in debt, equity or other securities of the companies referred to herein or in other financial products and instruments. Unless otherwise expressly agreed or provided for in other applicable Barclays disclosures governing such transactions or required by law or regulation, Barclays conducts these activities as principal and executes its principal transactions as an arm's length counterparty. Barclays does not act as a fiduciary in relation to these transactions. Barclays Group operates in accordance with a conflicts of interest policy that identifies conflicts of interest Barclays Group faces in the ordinary course of its business, and establishes organizational and procedural measures to manage those conflicts where it is reasonably able to do so. Neither Barclays nor any other part of Barclays Group shall have any duty to disclose or utilize for the recipient's benefit any non-public information acquired in the course of providing services to any other person, engaging in any transaction (on its own account or otherwise) or otherwise carrying on its business. Members of Barclays Group, may from time to time act as manager, co-manager, arranger or underwriter of an offering or otherwise, in the capacity of principal or agent, transact in, hold or act as market-maker or advisor, broker or commercial and/or investment banker in relation to the securities, instruments or related derivatives which are the subject of this document.

NO ACTION HAS BEEN MADE OR WILL BE TAKEN THAT WOULD PERMIT A PUBLIC OFFERING OF THE SECURITIES DESCRIBED HEREIN IN ANY JURISDICTION IN WHICH ACTION FOR THAT PURPOSE IS REQUIRED. NO OFFERS, SALES, RESALES OR DELIVERY OF THE SECURITIES DESCRIBED HEREIN OR DISTRIBUTION OF ANY OFFERING MATERIAL RELATING TO SUCH SECURITIES MAY BE MADE IN OR FROM ANY JURISDICTION EXCEPT IN CIRCUMSTANCES WHICH WILL RESULT IN COMPLIANCE WITH ANY APPLICABLE LAWS AND REGULATIONS AND WHICH WILL NOT IMPOSE ANY OBLIGATION ON BARCLAYS OR ANY OF ITS AFFILIATES.

THIS DOCUMENT DOES NOT DISCLOSE ALL THE RISKS AND OTHER SIGNIFICANT ISSUES RELATED TO AN INVESTMENT IN THE SECURITIES DESCRIBED HEREIN. PRIOR TO TRANSACTING, POTENTIAL INVESTORS SHOULD ENSURE THAT THEY FULLY UNDERSTAND THE TERMS OF THE RELEVANT SECURITIES AND ANY APPLICABLE RISKS.

THE INFORMATION CONTAINED HEREIN IS NOT INTENDED TO BE DISTRIBUTED TO ANY PROSPECTIVE OR ACTUAL INVESTORS AND, ACCORDINGLY, MAY NOT BE SHOWN OR GIVEN TO ANY PERSON OTHER THAN THE RECIPIENT, AND IS NOT TO BE FORWARDED TO ANY OTHER PERSON (INCLUDING ANY RETAIL INVESTOR OR CUSTOMER), COPIED OR OTHERWISE REPRODUCED OR DISTRIBUTED TO ANY SUCH PERSON IN ANY MANNER WHATSOEVER. FAILURE TO COMPLY WITH THIS DIRECTIVE CAN RESULT IN A VIOLATION OF THE SECURITIES ACT OF 1933, AS AMENDED.