"How to Handle Hostile Attacks"

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Audio Archive

The increasing number of hostile attacks warrants preparation in advance. Careful planning is critical, as some attacks are designed to facilitate a takeover or force a sale of the target. Learn the art of responding to an attack from this team of experts:

- **Ian Foster**, Managing Director, Goldman Sachs
- **Jim Langston**, Partner, Cleary Gottlieb Steen & Hamilton LLP
- **Scott Winter**, Managing Director, Innisfree

John Jenkins, *Editor, DealLawyers.com*: This is John Jenkins, Editor of DealLawyers.com. I'd like to welcome you to today's program, "How to Handle Hostile Attacks."

Hostile activity is alive and well in the M&A marketplace, and recent years have seen a tremendous growth in the number of contested deals involving unsolicited bids, deal jumping and various types of deal activism. If you represent a public company when it comes to hostile activity, ask not "for whom the bell tolls" because it tolls for thee. Today's panel of top practitioners is going to explore the latest developments in hostile activity and provide some insights on how to put your client in the best position to deal with them.

With that, I'd like to introduce our panelists now. Joining me today are Ian Foster, a Managing Director at Goldman Sachs; Jim Langston, a partner at Cleary Gottlieb and Scott Winter, a Managing Director at Innisfree.

I'm going to turn things over to Ian who will kick things off by discussing the current environment for hostile activity. Ian?

What's the current environment for hostile activity?

Ian Foster, *Managing Director, Goldman Sachs*: Thanks, John. Let me kick this off by giving some context. As John alluded to hostile activity is alive and well.

There are several different flavors of what we mean when we talk about hostile activity, which we'll get through in this session. To give some context on elevated hostile volumes, if we look at the last five years as a proxy, each of those years there has been significant activity.

It's unprecedented unless you go back many years to the late 90's apart from the boom time period of 2006 and 2007. As you parse through it analytically, certainly the data would suggest that there is more activity now than there has been in the past.

What's interesting to think about as you peel back the layers is to ask yourself why and is that symptomatic of broader things going on in the M&A market - Is it related to the equity valuations? Is it related to what's going on in the boardroom and takeover defenses? We'll probably talk about many of those things today, and you will see the answer probably lies somewhere in between.

A point of comment about the prior M&A cycles and how people thought about hostile activity - We would observe that there was a time period where the view was hostile activity was binary, meaning someone would go out and make a hostile bid and either it worked or didn't. Frankly, most often, it did not work out, and people would move on.

What's changed is that we see more of the confluence of different aspects of the M&A market in hostile transactions. You have unsolicited deals or hostile deals that lead to topping bids. Topping bids that either lead to a deal outcome or not and maybe that brings in an activist component, and that can be either pre or post a definitive deal announcement, so on and so forth.

As I said, the confluence of different things in different parts of the M&A market manifest themselves in many of the deals. For context, I'll talk about some of the recent deals that I think many of you will be familiar with. Many of these are very large and notable transactions.

When we think about topping bids, certainly the Occidental Chevron Anadarko saga was top of mind and received a lot of press. It also has an activist component with Icahn coming out against the buyside rationale and form of financing procured by Occidental.

There was the Barrick-Newmont-Goldcorp saga which ended with, effectively, two different transactions. Newmont and Goldcorp got together, and then a separate joint venture agreement between Barrick and Newmont.

There was the RPC Packaging-Apollo-Berry Plastics deal, which was a deal that was signed up by Apollo on a friendly basis only to be later topped by a strategic buyer in Berry Plastics.

There was a private German company called Knauf and a public US company called USG where we saw the first example of a 13D filing by Berkshire Hathaway coming out against the recommendation of the USG board not to engage in merger talks with Knauf. So certainly there has been some unprecedented activity that has been very sizeable and notable involving key companies and investors across the landscape.

We saw Bristol Meyers-Celgene and the opposition from both Starboard and Wellington. That deal ultimately went through and the lesson there is probably about the importance of ISS and Glass Lewis. If there is support by those firms, it's hard to take down broader support for a merger. You'll probably hear more about that as we go through this.

There's UTC Raytheon that's playing out now and a couple of others not in the public domain - the theme with many of these is the use of equity as merger consideration. A large amount of equity currency creates a fertile backdrop for potential activism. Buyer stock prices have recently skewed negative on M&A announcements which gives opposition an opportunity window to agitate for a different outcome.

If you take a step back, again, that's just a bit of context and you'll hear more about these deals. The question is why is all that happening now?

What you'll hear from us is several different things. There's the basic reality that corporate and board defense profiles are increasingly limited versus where they have been in years past. There's been a shift in the balance of power and some of what was previously governed only within the boardroom has generally transitioned to shareholders and the public domain.

On the buy side there are elements that have contributed to a strong M&A market. There's confidence in the boardroom. There's substantial dry capital in the form of leverage that's available, and equity valuations are certainly strong so people can use equity as currency.

That generally means people are leaning more on their front foot than on their back foot. Not surprisingly, that ultimately leads to more of this hostile and unsolicited activity.

Then the last piece I would highlight is the way that deals are structured. At this point in the cycle we are seeing a gradual shift to equity financed deals. Along with equity deals comes lower premiums or even no premium merger of equal transactions.

The theme and consistency there are that we are at a point in the M&A cycle where, for a variety of reasons, there's simply dry powder to go around. Also, there's plenty of opportunities for people to say with this size of game changing M&A do I or do I not want to enter the fray?

Often it seems like people are willing to take risks that they haven't in the past. Generally, that has led to an increase in activity.

Again, that's a little context. I'll pause there and hand it over to Jim for some context on the legal framework.

What's the legal framework for evaluating hostile attacks?

Jim Langston, *Partner, Cleary Gottlieb*: Thanks, Ian. I agree. It's important for folks to be aware of this emerging threat and to also have a good grasp of the legal framework that's going to shape the target companies in their sore spots.

We're going to look at least this section for most of the podcast through the eyes of the target company. The two questions we get asked most often by U.S. public companies who are on the receiving end of a private takeover proposal or some other hostile attack are:

1. Do they have to publicly disclose it?
2. Do they have to engage or negotiate with the potential acquirer or can they just say no?

Taking those in order on the disclosure question, the analysis is highly fact-intensive; but, in general, a U.S. public company is not going to be legally required to disclose that it has received a takeover proposal, but that can change.

For example, if there's been a leak in the company was the source of the leak it may have to confirm that it has, in fact, received some takeover proposal or other proposal or if there were rumors or speculation, as there often is, regarding a potential deal, that can cause this target stock price to run up.

It's possible, but at least in the U.S. not likely that the stock exchange may compel the company to make a disclosure. That rarely happens, at least in the U.S., that the exchange gets involved.

The other way that the duty to disclose can be triggered is if the company is pursuing some other transaction that triggers line item disclosure under the SEC rules. This is an area where companies must be careful.

Generally, what this means for the target company is they can maintain a no comment posture. If reporters, analysts or someone calls up and makes inquiries about a potential deal, are wondering whether something's afoot, unless the circumstances change or the company feels that the situation calls for a different tactical approach, they can just say "no comment".

That's important because you're going to want to keep the fact that you've received a takeover proposal confidential and private for as long as possible. You don't want that to become public typically.

The reason why you want to keep it confidential is because once the takeover proposal becomes public, the company is essentially put in play. Boards who are likely to push for a deal are going to trade into the stock. The pressure on the company intensifies as it finds itself in the public spotlight, as a result, it loses some control over its own destiny.

On the second question of how the board's fiduciary duties shape its initial response to an approach, in a Delaware corporation, the board doesn't have a duty to engage or negotiate with the bidder, much less accept the proposal. That's only so long as that course of action is supported by the record that's in front of the board. It's important for the management and the advisors to work with the board to help build the right record.

That's true - not having a duty to engage and negotiate - even if the offer is at a premium and the company has received an actual offer letter that has a price in it and other key terms. Typically, the board's duty is to evaluate that offer in good faith, with due care and to respond, and that's it.

In this context it's the business judgment rule that's going to apply. If the board's response is subsequently challenged in court, the courts are generally going to defer to the board's business judgment and not seek to second guess the board's decision. I think that's a good thing.

Also, depending on the nature of the approach, the board's going to want to reassess the adequacy of its takeover defenses. It will need to consider whether there's a threat that warrants fortifying its defenses, such as by adopting a poison pill, for example.

The takeover defenses that you can adopt in response to a takeover bid can't and won't eliminate the threat of a takeover. They are designed to give the board breathing room to respond, leverage to negotiate if the board chooses to do so, and time to consider the other alternatives and make its case to shareholders.

If the board is considering deploying additional takeover defenses in response to a threat, there's two points I think that are important to be mindful of. One, after a threat has emerged, if those takeover defenses are adopted on a cloudy day the board's decision to implement those additional defenses is going to be subject to enhanced judicial scrutiny under *Unocal*.

What *Unocal* is going to require in this context is that the defensive measure must be in response to a legally cognizable threat. One of those threats is a takeover proposal that's made at an inadequate price, and the defensive measures also must be reasonable in relation to the threat. They can't be coercive or preclusive.

The other thing to keep in mind here is that takeover defenses are generally disfavored by institutional investors and proxy advisory firms. That's one of the reasons why they've been disappearing across corporate America, as Ian said.

In fact, ISS will generally recommend against the election of directors at a subsequent meeting if they amend the bylaws of the company without shareholder approval in a manner that ISS believes materially diminishes shareholder rights. From ISS's perspective that's what many takeover defenses do.

The bottom line here is that the takeover defenses are all legally valid, but you're going to have to also consider the reaction of the stockholder and the proxy advisory firms. Finally, it's

also possible that the takeover proposal won't show up on a clear day.

As Ian mentioned, after you sign up a deal with someone else an interloper will emerge and make a topping bid. In the context of a topping bid, the legal framework does shift somewhat.

First, you're going to be signed up to a merger agreement for the existing deal, and that's going to regulate under what circumstances and manner the target can engage with the interloper. You're going to have to carefully follow those procedures.

Second, if the existing deal involves the sale of the target for all cash or a majority of cash, or some breakup of the company, the board's going to be in what's called the "Revlon mode." At that point it's going to be charged with getting the highest value reasonably available. In the Revlon context, the target board just can't say no.

The situation's a little different as a legal matter when the topping bid arises in response to an all stock deal. In that case, typically, the business judgment rule and Revlon will apply to evaluating the board's conduct.

As a practical matter, it's not going to make much of a difference because the target is going to be hard pressed to resist an all cash fully financed offer that's at a higher premium to the existing deal on the table absent a regulatory or other reason that makes it unlikely that all cash topping bids will close. That's simply because your shareholders aren't going to allow you to do that.

You saw this play out recently with Merck's all cash topping bid for Versum that busted up Versum's all stock merger with Entegris. Versum initially resisted Merck's proposals, but after Merck bumped its price several times, the all cash premium became too compelling to resist.

I think that also highlights one of the themes that Ian was talking about that as you have more and more low to no premium in the like transactions, those are the ones that are more susceptible to being jumped by a higher premium cash takeover.

Scott, that's the legal framework. I know every step in the takeover dance involves some tactical decision. Once the situation becomes public, both parties will be battling for the hearts and minds of shareholders and proxy advisors.

What's the latest on how shareholders and proxy advisors are shaping takeover battles? What other threats do you see out there that you think the target should be focused on?

▲ How do you win the battle for hearts and minds of shareholders & proxy advisors?

Scott Winter, *Managing Director, Innisfree*: Thanks, Jim. When an unsolicited offer or topping bid comes in, or even quite frequently during an activist proxy fight situation, there's no phrase that gets thrown around more than the phrase "shareholder value," and that's ultimately what these situations are all about.

The typical hostile M&A situation or topping bid runs through a bunch of different field dynamics. I'm going to take a second to run through them, and then we can talk about shareholders who receive them. Often, they are either started through a private approach or a public bail plug.

Then you will either see a tender offer or a proxy contest for directors as some focal point that gets put in front of shareholders because the company and the bidder has been unable to strike a deal privately with the target. Therefore, they have decided that they want the

shareholders to be aware of the offer and then put pressure on the target board and management team to come to the table.

Ultimately, all hostile deals go friendly if they're going to completion or they fall apart. The goal of the hostile bidder and target company is to win the hearts and minds of the shareholders. Typically, you will break the shareholder base into its various component parts. The biggest parts are the following.

It's those shareholders that are influenced by the voting advisory firms, ISS and Glass Lewis, which can run, depending on the company, anywhere from 15% to 35% of the shareholder base.

The next is going to be the largest of the passive investors, the biggest of which are Vanguard, BlackRock and State Street have been reported in some academic literature that they own about 25% of many companies today. Over the next two decades those three alone could grow to 40% of the outstanding of many public companies.

All three of these, plus some of the other large index funds like BNY Mellon and Northern Trust have dedicated proxy voting or investment stewardship teams. They typically subscribe to ISS or Glass Lewis, but in these situations large index funds do not follow either the voting advisors blindly. It's a data point they use as research, and they make up their own minds when it comes to how they vote or interact with boards.

The other big component of a shareholder base is going to be the merger arbitrageurs who aren't in the stock from the outset. They only come in once there's a deal in play.

The arbs can range from a couple of percentage points to nearly 50%. If we go back to the Airgas - Air Products hostile bid where the arbs owned nearly 50% of the outstanding at various points during the fight. They can be highly influential to the outcome.

ISS is still important when it comes to a proxy contest, if a hostile M&A situation gets to that point. In topping bids where there's a merger vote, very often ISS is going to weigh in as they did in the Bristol Meyers - Celgene situation.

In most straight pure hostile M&A, ISS doesn't often get the opportunity to opine, but when they do, they look at the certainty of the offer. They look at whether the bidder is presenting a compelling value to the shareholders relative to the company's standalone plan or other alternatives.

Then they look at the appropriateness of how the board responded and see whether the board has considered it in good faith and entered in discussions or at least articulated a reason why they have not. The ISS recommendation could often be outcome determinative if it ever gets that far. As Ian previously said, it'll be important in a merger vote, and that's why you're seeing more and more topping bids because there is a vote.

There is a central focus point that shareholders are being asked to act on. When an alternative competing bid comes in, whether it's for the target or bidder, shareholders have a choice. They have a choice to go left or right with the direction of this company.

Sometimes shareholders prefer to receive a premium in the form of a topping bid rather than to pay a premium in the form of the acquisition that's been signed, which is why you see some transactions fall apart like the Merck-Versum transaction. The topping bidder was able to come in with a tender offer, with a fully financed bid, and the Merck deal didn't go to a vote. The deal was cancelled, and the transaction was struck.

One other tool that you see from time to time, although it's not as common as tender offers or even the threat of a proxy fight, is the use of withhold campaigns. It was used very successfully by Knauf in acquiring USG in the last couple of years.

I think they had a couple of interesting facts that most companies don't benefit from. Namely one, as Ian said, is that Berkshire Hathaway had a large position and they filed a 13D saying they wanted the target company to enter discussions with the Knauf family.

Knauf owned over 10% of the stock and had the stock for more than a decade. They indicated publicly that they were willing to see this through whether it took a year, two years or three years to buy the company, they weren't going anywhere.

Most hostile bidders don't show that same level of intestinal fortitude to really stick with a bid. Most hostile bidders, especially ones that we have worked with, often want to shoot a lot of bullets in the beginning. They hope that the target which had previously rejected their bid will come running into their arms.

When they don't, they'll stick around for some period of time. Often, they don't stick around for the one to two years it could take in order to make a hostile transaction go to completion.

Langston: Right. It wasn't just any 30% shareholder telling the board to engage, right? It was Warren Buffett which makes a big difference.

Winter: That's exactly right, and the withhold campaign was a massive success. The company then promptly entered negotiations with Knauf. They signed a deal at a slight increase in price. I think all the shareholders were extraordinarily happy with the outcome there.

Foster: It gets back to my point earlier on the confluence of these different topics, it also goes to takeover defenses and protections. For all those headwinds against USG the one piece of ammunition that the board had was a staggered board.

I think USG did utilize that in a very appropriate way to drive stockholder value by using time and that leverage to force Knauf to put more money on the table. Without the staggered board, you are staring into the abyss against a logical acquirer who is effectively backed by Berkshire-Hathaway. That's a very challenging place to be, but fortunately USG had retained that structural defense over a long period of time.

Winter: That's a great point. One other point worth talking about here because it's been in the governance news lately - and will continue to be as the SEC continues to evaluate it - is whether to implement universal proxy cards.

We did recently see a large universal proxy card contest at EQT, which was waged by the Rice brothers successfully even though a lot of the press got it wrong. The Rice brothers nominated a majority of directors and were successful in obtaining a majority of the seats in the proxy fight. The press talked about how this was a big success for universal proxy, but I think the press got it wrong.

Universal proxy, for those that don't know, allows all the nominees to show up on a single proxy card as opposed to the company slate appearing on one card and the dissident slate appearing on another card. By everyone appearing on a single card it allows shareholders to mix and match and pick the ideal slate of candidates that each shareholder wants to vote for.

That ability to mix and match makes it harder to get a majority of directors elected as a dissident, not easier. The win by Rice therefore was done in spite of the fact there was a universal ballot, not because of the universal ballot.

If the SEC goes to a universal ballot - I'm sure it's a matter of when, not if - then the universal ballot becomes mandatory. It will make hostile bids more difficult, not easier because it will give shareholders the opportunity to elect a minority dissident shareholder slate from a hostile bidder. When you're the hostile bidder that is not what you want to happen.

You want to throw out a majority of the board because you want to put a full new board in place that can explore the bid that was put in by the hostile bidder when the prior board did not. So, turning over a minority is not particularly helpful to the hostile bidder, but we'll see how this practice develops.

What's the latest in deal activism?

Winter: Just moving on a little to deal activism. We've talked a lot about topping bids. Topping bids are simple. If a company strikes a deal to sell itself and someone wants to pay more, shareholders today, for the most part, are going to be very interested in taking more money.

It's hard enough to manage money, it's hard enough to make money for the investors that have given capital to those asset managers. They're really going to want to get the most money they can on a change of control, regardless of whether it's stock or cash. They are sympathetic to deal certainty.

Where you've seen a lot of deal activism is on the bidder side. As Ian said, at this point in the cycle you're seeing more and more equity consideration deals, mergers of equals, which means you're going to have a buyer side vote if they're issuing at least 20% of their outstanding shares.

There's a stock exchange required vote. If they don't have enough authorized shares under their charter, they're going to need to ask for more authorized shares. That's a charter amendment that would require a majority of the outstanding.

In some cases, you're seeing straightforward mergers or "double dummy" mergers, which also require a majority of the outstanding shares. In any of those cases where there's low premium or no premium deals, you have the potential as the stock prices rotate for one or either of the sets of shareholders to get upset.

In cases where there is a premium being paid and the bidders' shareholders would have preferred to see the company get sold rather than to pay a premium to someone else's shareholders you're seeing some pushback. You saw that with T. Rowe Price at Occidental Petroleum.

They came out publicly against Occidental Petroleum. They didn't want to see Occidental Petroleum make a bid for Anadarko. Occidental Petroleum ultimately restructured and got some outside financing, again from Berkshire Hathaway and Mr. Buffett.

They were able to restructure the deal so that they didn't need a vote on their side, which then attracted the wrath of Carl Icahn, but Occidental shareholders don't have the opportunity to vote on the Anadarko deal. The Anadarko shareholders will vote, but it's a nice premium.

The market expects that there will not be any vote issues. It's interesting that they were able to restructure it. Many companies cannot and don't have the flexibility. They have to power through the vote. They need to go and explain to their shareholders why this is the right deal, price, time and opportunity.

That's exactly what Bristol Meyers had to do in connection with the Celgene deal. Starboard and Wellington had both opposed the transaction, but Bristol was able to go to their shareholders. They spoke, went to ISS and Glass Lewis and got enough shareholders to support the transaction even though Starboard preferred the deal not go through and continued to believe it wasn't a great deal, at least that's what they said publicly. Time will tell.

The Bristol Meyers shareholders did show enough level of support there but only because ISS supported it as well as some of the index funds. You've seen, as a result, there's a lot of incentive to try and structure around having buyer side votes. If it can be done at all, it's worth taking a long look at.

Sellers are going to be interested in making sure buyers don't have votes if they can avoid it because one thing that everyone needs to recognize as they're structuring a deal is shareholders have minds of their own. While the boards of both companies may be excited about the transaction they're about to announce, that's not always the case with shareholders.

If they can't anticipate that, they may be in for quite a rough road in trying to solicit those votes to get over the line. That makes communications incredibly important and communications at rollout are important. It's always worth taking the extra couple of days to make sure that the investor presentation that's getting put out on announcement is as good as it could be, that synergies are really detailed, people really understand the rationale and strategic rationale and economic rationale for a transaction because you only get an opportunity to launch a transaction to the public markets once.

You can try to remediate and do it a second time, but you're really trying to dig yourself out of a hole. What a lot of companies don't do if they're looking at transformative transactions, just launching it with a strong launch is a great idea.

It would be even better if they had been forecasting to the marketplace and their shareholders that they might be looking at large transactions, depending on the space. When shareholders are caught off guard and surprised by a transaction that is when they react most severely and there may not be a way to dig out of that.

I think Ian's going to talk a little about why we're seeing an increase in activist related takeovers.

Why are activist-initiated takeovers on the rise?

Foster: Thanks, Scott. This is an interesting topic. As we think about things that are new on the horizon the concept of an activist initiated takeover is certainly top of mind.

Historically when you think about Carl Icahn, for example, as one of the old guard activists, is a name that, from time to time, has ended up taking full control over companies that have been part of an activist campaign.

What has evolved is both strategies of how to put companies in play and simply the number of funds that are pursuing control strategies. Again, the question is why. In this case the reasons are fascinating.

The first reason why is if you think about economic returns over the last cycle. In the last 10 years think about economic returns for tier one private equity funds, they've been nothing short of extraordinary - fully levered equity returns which in some funds exceed well north of 20% per annum. That is a very enviable position if you are a manager of capital and you're trying to get returns, which both traditional activists as well as any active fund managers of

course are. There's simply an element of chasing returns, and so pursuing strategies that resemble private equity is only rational and makes sense that ultimately more managers will try to do that.

The second reason is more nuanced, which is if you think about the traditional activist campaigns, you think about the time horizon for the changes that are being suggested or put forth by the activist - in some cases, the risk tolerance that's required for some of those changes if they are very aggressive or significant in relation to the size of the enterprise - it's not always going to synch up with how the public markets typically value companies.

The result is you will have situations where the public markets won't be able to efficiently value something, for whatever reason, and the activist, of course, is not burdened by those same constraints. The activist ultimately is just managing a pool of capital and has its own risk tolerances and time horizons in mind that are appropriate for whatever its fund is.

So, to the extent that you have an activist fund that is of sufficient size and tenor so that it can hold an asset in private for three, five or seven years or longer to reshape a company, it may actually be the case - I would suggest it's often going to be the case - that the highest potential return is for the activist to simply take full control of the company.

What we've seen recently and the activist which I would say has been very calculated and smart about how they've rolled out the strategy is Elliott. Most people are familiar with Elliott and many of their campaigns. They are prolific and historically can be very aggressive... but in part have rotated their focus and softened their stance. In the tech and software space Elliott has been very active and has consummated a number of control transactions.

Gigamon was a take private transaction for north of $1 billion. Travelport is another company in the healthcare space. Athena health is nearly $5 billion of market cap. So large and sizeable transactions. We would say that's a very interesting phenomenon for the reasons I mentioned and suggest its likely to continue, at least in the current economic climate.

To Jim's comment about we're approaching this from the lens of what do you need to think about if you are the target and you find yourselves in one of these situations, I think there's a lot to think about because it's a very unusual place to find yourself.

The first thing is I would divide this into a category of activists who have done this before, which is basically Elliott and Icahn. There's a couple of others that have had flavors of it like Sycamore and Vintage Capital. Then there are people who haven't, which is basically everyone else. As people who have been around deals and take private transactions know they are very complicated from a governance, process, financing and conditionality standpoint.

What I think you need to understand if you do find yourselves in one of these situations is that the dynamic can be very different from interacting with the regular way private equity community - those are firms that do this day in and day out. Activists are typically arriving to the scene with a different orientation.

The second thing is you want to be very careful of finding yourselves in a situation where, by definition, if the activist is in the stock and considering actually taking control of the company, taking the company private or otherwise, by definition you've found yourself in an unusual situation. That is not the typical backdrop of how boards and companies will launch a volitional sale process.

I think that making sure to avoid the tendency of being, let's say, lax on things that are very important such as keeping confidentiality and on terms that protects the Board and its process, limiting any conditionality in definitive agreements, having an appropriate sell side

process for the company and really making sure you're getting the best bid because ultimately the record will be heavily scrutinized.

Last is on financing - the only funds that can do this in size and by themselves are ones that have either permanent capital or are sufficiently large because, by definition, the natural holding period for a take private is going to be five years or beyond, or is certainly traditionally that way.

In the smaller size range, you need to think about when is the financing really coming through? Who are the other equity partners and what do they need to know and diligence? What is the conditionality associated with that? Again, all the things that would be, I would say, normal and part and parcel of the private equity process but with a different breed of buyer, so to speak, certainly can take some twists and turns.

Again, that's a few things that are new and evolutionary in terms of how we're thinking about some of these stickier situations in the confluence of activist initiated M&A.

Langston: Ian, one question. Do you think boards that are now receiving inbound bids from strategics, are they more receptive to them because of the threat of activism so that if activists ever found out about it, they might be in trouble which it lubricates the bid from strategic bidders?

Foster: I think the answer is certainly yes. I would probably characterize it, though, as activism - as defined by traditional activists as well as just much more active regular shareholders - has become so common place, that management teams and boards have come up the curve quite quickly on the nuances of all this.

What's happened over the last, probably, three years is people have adopted the mantra internally of thinking like an activist. If you're a board member and you're looking at a strategic plan or a letter comes in that's unsolicited from a strategic and you're thinking do I really need to explore this? Do I need to think about benchmarking this against my plan? Do I need to do all the work, or can I brush it off, certainly the specter of potential activism plays into that?

And that result is generally healthy because, as Jim and Scott both talked about, a lot of the appropriate defense comes from understanding from soup to nuts, A to Z how any potential alternative stacks up against the strategic plan that's in place today. Certainly, if the board isn't doing the work itself, it is possible that an activist is going to come over the top and do that work and do it in a very public way. That's not a position that anyone wants to find themselves in.

What can companies do to level the playing field?

Langston: That's right. This is all occurring against the backdrop of activism and that threat. If there is some hostile approach or unsolicited proposal that becomes public often parts of defense will be in the strategic plan, the merits of that plan, how that the current board and management team are the ones who are poised to deliver superior value.

That puts them under the spotlight as well, because you've seen situations where in some of the generic pharmaceutical takeover battles where one of the companies, part of its defense is the strategic plan and ability to execute, and when it fell short and wasn't able to deliver what it said it would, that created an opening for an activist. It's a vicious cycle in certain respects as well.

As you have heard from all of us in the current environment there are quite a few potential threats lurking in the shadows, but I don't think it's all bad news. It is true that the threats

are on the rise and companies are increasingly vulnerable.

Ian talked about the dismantling of the takeover defenses with a staggered board at USG and how that was important. The fact of the matter is it's rare for a company to have a staggered board, particularly if you look at the S&P 500. Today less than 10% of the companies in the S&P 500 have a classified board.

These threats are on the rise at a time that companies are increasingly vulnerable. As Scott said, this is coinciding, and I don't think it's any accident, with an environment in which ownership of most U.S. public companies is increasingly concentrated in the hands of fewer and fewer stockholders.

In a certain sense, if you're a company you almost feel like the deck is stacked against you. Then the question is what you should do to level the playing field? From my perspective, that all starts with preparedness. Takeover proposals, hostile attacks, whether it's the casual pass from the CEO, the proposal letter, the tender offer, the bear hug, those all arise at a moment's notice and without much, if any, advance warning.

If you're a target board and you're thinking about your defense, you want to have a playbook in place. You don't want to be thinking about these issues for the first time when the threat first emerges.

The other thing about preparedness is that you want to do everything you can to be responding, not from a position of weakness, but a position of strength. That's part of what any preparedness strategy is designed to do.

One of the things you should think about doing is assembling the swat team that's charged with helping develop and execute the company's response. That's going to include key members of management.

You're also going to want to have an investment banker, a law firm, proxy solicitor and PR firm all on the team. That's going to be your core team. Certainly, as the situation calls for, you'll bring in other experts to assure you have the resources you need.

I do think it's true that the best takeover activist response teams are sized to be nimble. It obviously can't just be one person, but it can't be so large that it can't be assembled or change directions at a moment's notice.

You can't just put the team in place, right? It has to do something. One of the things that we think it should do is regularly assess not just the company's strengths but also its weaknesses.

We talked about thinking like an activist. Where is the company vulnerable? What can it do today to seek to proactively address those weaknesses? If it can't fix the weakness, how is it going to explain it to the market and shareholders? What's the defense going to be?

From the lawyers' perspective, that's going to include looking at the company's takeover defenses, what gaps are in the armor? What, if anything, you can do to fix it without attracting unwanted attention?

You're also going to want to get the SWAT team together periodically on a clear day and engage in preparedness exercises if you can. You can test out the scripts, the messaging, the communication strategy, and the other plans you've developed before you start shooting with live ammo.

Scott talked a little about this earlier, but as he said, in a takeover battles and battles with activists the shareholders are going to weigh in and have their say one way or another. It's going to be important to put as many of those shareholders on your side as you can.

I think for that and for other reasons a thoughtful shareholder engagement strategy is going to be an important feature of your preparedness plan. The goal here is to get to know your shareholders, develop relationships on clear days that are going to help you weather stormy ones.

That it's also going to give you a realistic sense of where you stand with your shareholders and which ones are likely to support you on the dark days and which ones are not.

The other benefit that we see of shareholder engagement is occasionally when a hostile attack or some other threat is brewing, particularly if there's an activist involved, you can get an advance warning of that when you talk to your shareholders.

They may not tell you that they've been approached by an activist overtly, but if you start to hear the same critique or the same thesis from more and more of your shareholders almost verbatim the chances are that an attack is imminent.

The other thing that I would say about shareholder engagement is you have to be careful when doing that. There can be a fair amount of downside to those engagements if the engagement goes poorly.

That doesn't mean you shouldn't engage with your shareholders. You should. It just means that you need to be prepared and deliberate when doing so. One of the other things that Scott and Ian were talking about earlier is the messaging and how you communicate with your investors and with the street and are telling your story. It's important to reexamine that over time, particularly as the business and the strategic plan evolve.

The best messaging is going to be aligned with the company's strategic plan. This is going to make it more likely that the company is attracting the right kind of investors and analysts, and that the analysts and the investor community have a clear sense of what they should expect from the company and that you're not creating false expectations or being held accountable for executing on a plan that's not your own.

Preparedness is a broad category. There's lots to do. That's just the tip of the iceberg, but that's some things for companies to think about.

Jenkins: That was a very informative and you certainly covered a lot of ground. Thank you very much for participating, and I also want to thank everyone online for listening. That concludes today's webcast.