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Retention Awards at Acquired Companies

By Jacob O'Neill, Senior Analyst of Towers Watson*

The number of mergers and acquisitions announced in 2014 has increased over previous years and includes some of the largest deals in history. Through the third quarter of this year, 73 M&A deals with a total transaction value greater than $1 billion have been announced, including 10 that each had a value greater than $25 billion (three of these deals have since been cancelled). By way of comparison, only nine deals closed in the U.S. with a value of over $25 billion over the four years prior to 2014.

Towers Watson's Executive Compensation Resources unit tracks and analyzes special compensation arrangements for executives involved in acquisitions on an ongoing basis. For our most recent analysis of retention award practices, we looked at U.S.-based public companies involved in 181 acquisitions with a transaction value greater than $1 billion between the beginning of 2010 and the end of March 2014.

Our analysis specifically reviews retention awards and/or programs put in place at acquired companies in the course of the merger and focuses on awards with executive participation. Our review identified 69 companies (39% of all acquired companies during this period) that offered some form of retention award to employees and/or executives prior to the close of the deal. While we focus on the companies with executive-level retention awards, we also note that there are other considerations involved in retaining and protecting employees during acquisitions, including change-in-control severance agreements as well as retention programs for employees below the executive level.

Key Consideration: Leadership Requirements

Our analysis brings to light that retaining leadership through the close of the merger and retaining certain key executives in the integration period thereafter are driving factors for companies making these awards. Companies carefully evaluate their retention needs and tailor awards to reflect their interests. Awards address these issues with customized vesting terms—sometimes on an individual basis—to match the company's retention concerns. Subsequently, the award retention or vesting term impacts the value awarded, with longer terms having substantially larger values than shorter terms.

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Closer inspection of companies' disclosure of these awards reveals myriad reasons that can justify retention bonuses. Some companies call out the uncertainty of future employment post-transaction as a driver for retention awards, while others identify the forgone severance payments for executives who stay with the company in their rationale for such programs. In the latter case, the awards are designed to secure continued employment with the company following the transaction and through the severance window.

Generally, target companies initiate programs that define a vesting period up to or shortly following the deal close. The goal is to ensure the leadership team remains in place in order to successfully close the transaction. In some cases, target companies may make awards at the behest of buyers to ensure continuity of key leaders they deem important to successfully integrating the company post-transaction. These awards have vesting terms typically from one to two years following the close of the deal, during the key integration period.

Retention awards take a number of forms. While primarily made in cash, award designs vary from broad-based programs to single awards made to one or more executives heavily involved in the transaction or key to the success of the business. Many companies used a maximum bonus pool from which to make grants, while other awards were determined on an individual basis.

Bonus Pools

About 45% of the companies providing retention awards established a bonus pool to fund the awards. Awards are granted out of a maximum pool to a group of key employees, which may or may not include executives. These pools had a median aggregate value of $9.3 million, or 0.19% of the total transaction value *(Figure 1)*.

Approximately half of the awards granted using an established bonus pool disclosed executive participation in the pool. For bonus pool programs with executive participation, executives as a group received almost half (43%) of the bonus pool at the median. The CEO was awarded 26% of the total pool at the median for those companies that included the chief executive in the retention program.

Figure 1. Retention bonus pools at acquired companies

	Total bonus pool value (in millions)	Percent of deal size	CEO share*	All executives' share*
25th percentile	$3.6	0.10%	12%	14%
Median	$9.3	0.19%	26%	43%
75th percentile	$16.5	0.39%	38%	60%

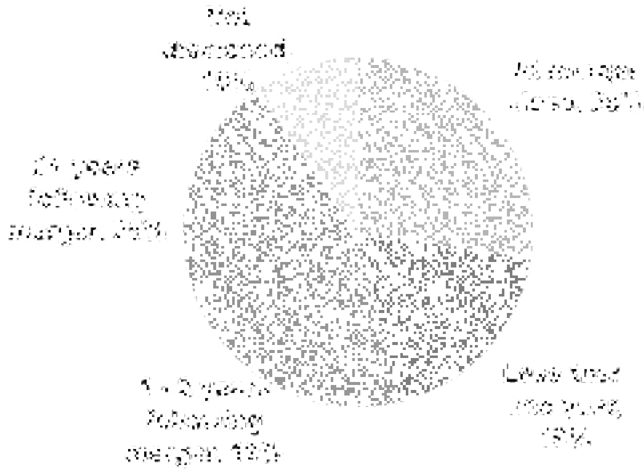
*Half (16) of the awards with bonus pools disclosed executive participation.

Vesting Terms Influenced by Purpose

Awards with a shorter vesting term were provided mainly to encourage the executive to remain with the company and to motivate the successful closing of the merger. In almost every case, these awards are contingent on the merger successfully closing. Longer vesting terms indicate a desire by the surviving company to retain the leadership team in order to maintain leadership continuity and assist in integrating the businesses.

The vesting term of the awards varied widely *(Figure 2)*. Almost half of the awards (47%) had maximum vesting terms of less than 12 months following the close of the merger. Over a quarter (28%) vested fully at the close of the merger, and 19% vested less than one year (typically six months) following the close. Approximately 19% of awards vested at 12 or 18 months following the close, and 25% of awards granted to target company executives had terms at or longer than two years (10% did not disclose the vesting term).

Figure 2. Vesting term of awards



Half of the awards (53%) had a cliff-vesting schedule, meaning the entire award vested at the end of the vesting term, while 37% had a graded or ratable vesting schedule, with portions vesting up to the final vesting date (11% did not disclose the vesting schedule). Forty-three percent of all awards either fully vested or had a portion of the award vest on the merger closing date. For awards that vested following the merger close, approximately [illegible] had some portion that vested at the closing date.

Award Values

Retention award values as a percentage of the executive's base salary vary with the executive's role and involvement in the transaction *(Figure 3)*. Almost half of the companies in our sample included the CEO in their award programs. At the median, the CEO received 250% of base salary as a retention award, and all other executives received awards at 125% of base salary. In dollar terms, CEOs received approximately $1.6 million as their retention award at the median, with all other executives receiving a median of $400,000.

Figure 3. Award multiples and values by position

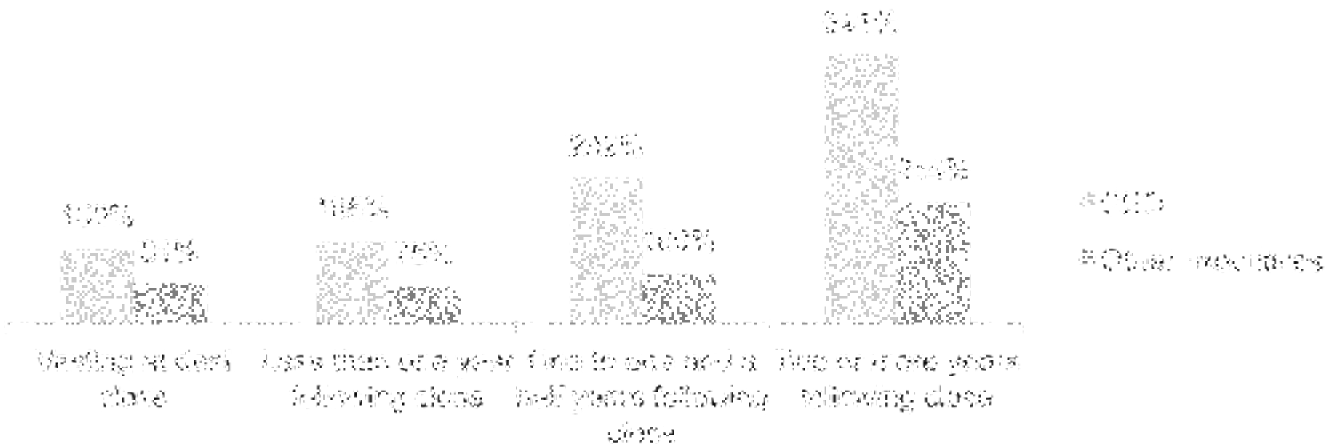
Position	Multiple % of base salary			Dollar value		
	25th percentile	Median	75th percentile	25th percentile	Median	75th percentile
CEO	100%	250%	485%	[illegible]	[illegible]	[illegible]
All executives (excluding the CEO)	75%	125%	240%	$193,000	$400,000	$900,000

Our analysis found that the size of the award is largely dependent on the length of the vesting term. Measured as a percentage of base salary, retention awards are smaller for shorter terms, with the largest awards being granted to executives with vesting terms longer than one year following the deal close (Figure 4).

At the median, CEOs received [illegible] of their base salary as a retention award that would vest and be paid at the close of the deal, while other executives received [illegible] of base salary at the median. The value of these awards did not differ significantly from those vesting less than 12 months following the close of the deal. At the median, those shorter-term awards delivered value of [illegible] of base salary for the CEO and 75% for non-CEO executives.

As the length of the retention term climbed, so did the award value. Awards vesting at 12 or 18 months following the close of the deal grew to 292% of base salary for the CEO and 100% of base salary for other executives at the median. About 25% of our sample had awards with vesting terms at or longer than two years following the close, with most awards being delivered at two years. These awards had the highest grant values, paying the CEO 541% of base salary at the median and other executives 244%. The upper quartile for awards vesting two or more years following deal close revealed even larger grants, with CEOs receiving 822% of base salary and other executives 400% of base salary.

Figure 4. Median award values as a percentage of base salary, based on vesting term



Final Thoughts

Mergers and acquisitions are a transformative time for both organizations involved in the deal. Retaining key executives is often instrumental to successfully closing the deal, and effectively integrating the organizations to grow the business and, ultimately, deliver enhanced value to shareholders.

Our analysis offers insight into the structure of executive-level retention programs put in place at acquired companies in the past three years. Many companies provide retention awards through bonus pools that are distributed to executives and other employees. Award values vary across executive positions and more significantly based on the vesting term. Finally, about half of all awards provide some value to the executive at the merger closing date.

Towers Watson continues to monitor how companies implement M&A retention programs in order to provide in-depth analyses and robust market data to our clients facing the challenges of retaining top talent through the uncertainty that an acquisition brings.

Delaware Chart: Determining the Likely Standard of Review for Board Decisions

By Rob Little, Chris Babcock, Katherine Cournoyer, Tim Fisher and Mike Cannon of Gibson, Dunn & Crutcher LLP

M&A practitioners are well aware of the several standards of review applied by Delaware courts in evaluating whether directors have complied with their fiduciary duties in the context of M&A transactions. Because the standard applied will often have a significant effect on the outcome of such evaluation, establishing processes to secure a more favorable standard of review is a significant part of Delaware M&A practice.

The chart below identifies fact patterns common to Delaware M&A and provides a preliminary assessment of the likely standard of review applicable to transactions fitting such fact patterns. However, because the Delaware courts evaluate each transaction in light of the transaction's particular set of facts and circumstances, and due to the evolving nature of the law in this area, this chart should not be treated as a definitive statement of the standard of review applicable to any particular transaction.

No.	Facts	Likely Standard of Review[1]
1.	Fully independent and disinterested[2] board of directors; no controlling stockholder[3]	Business judgment[4]
2.	Majority of board is independent and disinterested; no controlling stockholder	Business judgment[5]
3.	Board is evenly split between directors who are independent and disinterested and directors who are not independent and disinterested; no controlling stockholder	Entire fairness[6] Business judgment if transaction is approved by a properly functioning special committee[7] or a fully-informed stockholder vote[8]
4.	Majority of board is not independent and disinterested; no controlling stockholder	Entire fairness[9] Business judgment if transaction is approved by a properly functioning special committee[10] or a fully informed stockholder vote[11]
5.	Entire board is not independent and disinterested; no controlling stockholder	Entire fairness[12] Business judgment if transaction is approved by a fully informed stockholder vote[13]
6.	Transaction with a controlling stockholder where majority of the board is independent and disinterested	Entire fairness, but either (a) a properly functioning special committee or (b) approval of a majority of the minority will shift the burden of proof to the plaintiff[14] Business judgment if both (a) a properly functioning special committee and (b) approval of a majority of the minority[15]

7.	Transaction with a controlling stockholder where a majority of the board is *not* independent and disinterested	Entire fairness, but *either* (a) a properly functioning special committee or (b) approval of a majority of the minority will shift the burden of proof to the plaintiff[16] Business judgment if *both* (a) a properly functioning special committee and (b) approval of a majority of the minority[17]
8.	Controlling stockholder; majority of the board is independent and disinterested with respect to the controlling stockholder; controlling stockholder is *not* the counterparty in the transaction; and controlling stockholder is treated the same as other stockholders	Business judgment[18]
9.	Controlling stockholder; majority of the board is *not* independent and disinterested with respect to the controlling stockholder; controlling stockholder is *not* the counterparty in the transaction; and controlling stockholder is treated the same as other stockholders	Business judgment[19]
10.	Controlling stockholder; majority of the board is independent and disinterested with respect to the controlling stockholder; controlling stockholder is *not* the counterparty in the transaction; and controlling stockholder receives different treatment in the transaction than other stockholders	Entire fairness, but *either* (a) a properly functioning special committee[20] or (b) approval of a majority of the minority will shift the burden of proof to the plaintiff[21] Business judgment if *both* (a) a properly functioning special committee and (b) approval of a majority of the minority[22]
11.	Controlling stockholder; majority of the board is *not* independent and disinterested with respect to the controlling stockholder; controlling stockholder is *not* the counterparty in the transaction; and controlling stockholder receives different treatment in the transaction than other stockholders	Entire fairness, but *either* (a) a properly functioning special committee[23] or (b) approval of a majority of the minority will shift the burden of proof to the plaintiff[24] Business judgment if *both* (a) a properly functioning special committee and (b) approval of a majority of the minority[25]

[1] Assumes duty of care is discharged. In addition to the standards of review identified in this chart, a transaction is subject to enhanced judicial scrutiny under *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986), "when a company embarks on a transaction—on its own initiative or in response to an unsolicited offer—that will result in a change of control." *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 242 (Del. 2009).

[2] "Independence means that a director's decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences." *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984), *overruled in part on other grounds by Brehm v. Eisner*, 746 A.2d. 244, 254 (Del. 2000). "Such extraneous considerations or influences may exist when the challenged director is controlled by another." *Orman v. Cullman*, 794 A.2d 5, 24 (Del. Ch. 2002). Thus, a "lack of independence can be shown when a plaintiff pleads facts that establish that the directors are beholden to [the controlling person] or so under [that person's] influence that [the directors'] discretion would be sterilized." *Id.* (first alteration in original) (internal quotation marks omitted). Disinterestedness means that "directors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of

self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally." *Id.* at 23.

[3] A stockholder is a controlling stockholder under Delaware law where the stockholder (1) owns more than 50% of the voting power of a corporation or (2) exercises control over the business affairs of the corporation. *Kahn v. Lynch Commc'n Sys.*, 638 A.2d 1110, 1113-14 (Del. 1994). When evaluating whether a stockholder exercises the requisite control, Delaware courts will evaluate whether the stockholder controlled the board "such that the directors . . . could not freely exercise their judgment with respect to a transaction." *In re KKR Fin. Holdings LLC S'holder Litig.*, No. 9210-CB, 2014 Del. Ch. LEXIS 207, at *29-*30 (Oct. 14, 2014). *See also In re Crimson Exploration Inc. S'holder Litig.*, No. 8541-VCP, 2014 Del. Ch. LEXIS 213, at *31-*39 (Oct. 24, 2014) (analyzing Delaware case law concerning controlling stockholders).

[4] *See In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 36 (Del. Ch. 2013) (clarifying that the "business judgment rule" applies to decisions by board members who are "disinterested and independent").

[5] The business judgment rule is generally the applicable standard of review where a majority of the board is disinterested and independent. *See Cinerama, Inc. v. Technicolor*, 663 A.2d 1156, 1173 (Del. 1995). Nonetheless, a transaction must be "approved by a majority consisting of the disinterested directors" in order for the business judgment rule to apply. *See Aronson v. Lewis*, 473 A.2d at 812, *overruled in part on other grounds by Brehm v. Eisner*, 746 A.2d. at 254; *see also In re Trados Inc. S'holder Litig.*, 73 A.3d at 44 ("To obtain review under the entire fairness test, the stockholder plaintiff must prove that there were not enough independent and disinterested individuals among the directors making the challenged decision to comprise a board majority. . . . To determine whether directors approving the transaction comprised a disinterested and independent board majority, the court conducts a director-by-director analysis."); *Chaffin v. GNI Group, Inc.*, No. 16211-NC, 1999 Del. Ch. LEXIS 182, at *16-*19 (Sept. 3, 1999) (holding that where a board had three independent and disinterested members and two interested members, and the board approved a merger by a vote of 4-1, with one of the independent and disinterested directors voting against the merger, the merger approval "was one vote short of the required disinterested majority"); *Puma v. Marriott*, 283 A.2d 693, 693-94, 696 (Del. Ch. 1971) (rejecting a derivative challenge to a corporate acquisition where the five outside directors on a nine-member board unanimously authorized the acquisition).

[6] "A board that is evenly divided between conflicted and non-conflicted members is not considered independent and disinterested." *Gentile v. Rossette*, No. 20213-VCN, 2010 Del. Ch. LEXIS 123, at *30-*31 n.36 (May 28, 2010). "[T]he business judgment rule has no application" to a merger transaction that is "not approved by a majority consisting of the disinterested directors," *Aronson v. Lewis*, 473 A.2d at 812, *overruled in part on other grounds by Brehm v. Eisner*, 746 A.2d. at 254, and where the "business judgment rule" has been "rebut[ted]" this "lead[s] to the application of the entire fairness standard," *In re Crimson Exploration Inc. S'holder Litig.*, 2014 Del. Ch. LEXIS 213, at *68.

[7] The relevant law is not entirely clear, but the better reasoned view appears to be that a properly functioning special committee brings the business judgment rule to bear. *See In re W. Nat'l S'holder Litig.*, No. 15927, 2000 Del. Ch. LEXIS 82, at *35-*38 (May 22, 2000) (explaining that the use of an "independent special committee, bargaining at arm's length with a controlling shareholder, to shift the burden of proving entire fairness is well noted . . . . The policy rationale requiring some variant of entire fairness review, to my mind, substantially, if not entirely, abates if the transaction in question involves a large, though not controlling, shareholder. In other words, because the absence of a controlling shareholder removes the prospect of retaliation, the business judgment rule should apply to an independent special committee's good faith and fully informed recommendation."); *see also In re PNB Holding Co. S'holders Litig.*, No. 28-N, 2006 Del. Ch. LEXIS 158, at *50 n.69 (Aug. 18, 2006) (then-Vice Chancellor Strine explaining that the business judgment rule would apply if a properly functioning special committee had "negotiated and approved the transaction"). There is, however, some other precedent that could be read to suggest that a properly functioning special committee does no more than shift the burden of the proof to the plaintiff, *see In re Tele-Commc'ns, Inc. S'holders Litig.*, No. 16470, 2005 Del. Ch. LEXIS 206, at *32-*33 (Dec. 21, 2005), although the better reading of this precedent may be that it involved a controlling stockholder, *see In re John Q. Hammons Hotels Inc. S'holder Litig.*, No. 758-CC, 2009 Del. Ch. LEXIS 174, at *34 (Oct. 2, 2009) (interpreting *In re Tele-Commc'ns* as having involved a controlling shareholder). In

any event, the Delaware Supreme Court has not definitively resolved the question of which standard of review applies when a special committee approves a transaction and there is no controlling stockholder.

[8] "[P]laintiffs do not disagree with defendants' position that the legal effect of a fully-informed stockholder vote of a transaction with a non-controlling stockholder is that the business judgment rule applies and insulates the transaction from all attacks other than on the grounds of waste, even if a majority of the board approving the transaction was not disinterested or independent. This position is supported by numerous decisions . . ." *In re KKR*, 2014 Del. Ch. LEXIS 207, at *50-*51; *see also* Vice Chancellor J. Travis Laster, *The Effect of Stockholder Approval on Enhanced Scrutiny*, 40 Wm. Mitchell L. Rev. 1443 (2014) (providing substantial discussion of the interplay between stockholder approval and the standard of review). However, while decisions from the Court of Chancery have consistently held that a fully informed, non-coerced stockholder vote will reduce the standard of review to business judgment, the Delaware Supreme Court has not decided whether a stockholder vote that is required by law is sufficient to reduce the standard of review. *Compare In re KKR*, 2014 Del. Ch. LEXIS 207, at *50-*51, *with Gantler v. Stevens*, 965 A.2d 695, 713 (Del. 2009). Further, the failure to disclose all material information to stockholders can prevent a stockholder vote from being fully informed, and would thus prevent the vote from "ratifying" the transaction. *See Chen v. Howard-Anderson*, 87 A.3d 648, 669 (Del. Ch. 2014) (noting that, even if defendants had argued that the stockholder vote ratified the challenged transaction, "disclosure deficiencies" would undermine the vote and render the ratification ineffective).

[9] *See In re Trados Inc. S'holder Litig.*, 73 A.3d at 45 (holding that entire fairness was the applicable standard of review in scrutinizing a board's approval of a merger where the plaintiff proved at trial that six of the seven . . . directors were not disinterested and independent); *In re Tele-Communications, Inc.*, 2005 Del. Ch. LEXIS 206, at *25-*32 (explaining that an "entire fairness analysis" is required whenever "evidence in the record suggests that a majority of the board of directors were interested in the transaction" and providing several examples).

[10] *See* note 7, *supra*.

[11] *See In re KKR*, 2014 Del. Ch. LEXIS 207, at *50-*51.

[12] *See In re PNB Holding Co.*, 2006 Del. Ch. LEXIS 158, at *40-*41, *50 (concluding that all of the members of the board were interested and that entire fairness was the standard of review, recognizing that stockholder approval for the merger was accordingly "the only basis for the defendants to escape entire fairness review," but ultimately concluding that "[b]ecause a majority of the minority did not vote for the Merger, the directors cannot look to our law's cleansing mechanism of ratification to avoid entire fairness review").

[13] *See* note 11, *supra*.

[14] *See Kahn*, 638 A.2d at 1117 (the "standard of judicial review in examining the propriety of an interested cash-out merger transaction by a controlling or dominating shareholder is entire fairness. . . . However, an approval of the transaction by an independent committee of directors or an informed majority of minority shareholders shifts the burden of proof . . . to the challenging shareholder-plaintiff.").

[15] The detailed requirements for the business judgment review to apply to a controlling-stockholder transaction are set forth in *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014) as follows: "(i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority." *Id.* at 645.

[16] *Kahn*, 638 A.2d at 1117.

[17] *See* note 15, *supra*.

[18] *See In re Synthes, Inc. S'holder Litigation*, 50 A.3d 1022, 1046 (Del. Ch. 2012) (applying business judgment review despite pled facts that a majority of the board was not independent with respect to the controlling stockholder because the controlling stockholder "received equal treatment in the Merger").

[19] "Entire fairness is not triggered solely because a company has a controlling stockholder. The controller also must engage in a conflicted transaction." *In re Crimson Exploration Inc. S'holder Litig.*, 2014 Del. Ch. LEXIS 213, at *35; *see also id.* at *41–*47 (continuing on to note that a conflicted transaction could arise when (i) a controlling stockholder stands on both sides of a transaction, (ii) a controlling stockholder receives consideration that differs from that received by the other stockholders, or (iii) a controlling stockholder receives a special benefit from the transaction, such as meeting a unique need for liquidity or effectively extinguishing a claim against it); *see also In re Synthes*, 50 A.3d at 10[illegible].

[20] *See In re John Q. Hammons Hotels Inc. S'holder Litig.*, No. 758-CC, 2011 Del. Ch. LEXIS 1, at *7 (Jan. 14, 2011) ("[P]laintiffs bear the ultimate burden to show the transaction was unfair given the undisputed evidence that the transaction was approved by an independent and disinterested special committee of directors.").

[21] Although we have not identified any Delaware cases explicitly addressing the effect on the standard of review of approval by a majority of the minority stockholders in this factual scenario, it would be reasonable to conclude that the reasoning of *Kahn v. Lynch*, 638 A.2d 1110, would apply.

[22] *See In re John Q. Hammons Hotels Inc. S'holder Litig.*, 2009 Del. Ch. LEXIS 174, at *39 (in transaction where controlling stockholder receives different consideration than minority stockholders, "business judgment would be the applicable standard of review if the transaction were (1) recommended by a disinterested and independent special committee, and (2) approved by stockholders in a non-waivable vote of the majority of all the minority stockholders").

[23] *In re Tele-Commc'ns, Inc.*, 2005 Del. Ch. LEXIS 206, at *32–*33 (explaining that because of the directors' interested status "[t]he initial burden of proof rests upon the director defendants to demonstrate . . . fairness," but further explaining that "[r]atification by a majority of disinterested directors, generally serving on a special committee, can have the effect of shifting the burden onto the plaintiff shareholders to demonstrate that the transaction in question was unfair. In order to shift the burden, defendants must establish that the special committee was truly independent, fully informed, and had the freedom to negotiate at arm's length.").

[24] *See* note 21, *supra*.

[25] *See* note 22, *supra*.

Respecting Boilerplate: Liability, Party & Enforcement Provisions

By Rob James of Pillsbury Winthrop Shaw Pittman LLP[1]

The charts in this series of *Respecting Boilerplate* articles are intended to facilitate the process of drafting, reviewing, negotiating, and *respecting* boilerplate provisions. The common topics are illustrated in the first column by a "reference" clause—which is assuredly *not* a universally recommended text, and which is neither the most simple nor the most complex possible provision, but one that illustrates the basic purposes. For each reference clause, the second column identifies questions or other comments to consider. These reference clauses are neither necessary nor sufficient for any particular deal, and the comments are far from exclusive (this sentence sounds like boilerplate itself). Nonetheless, the charts may help you select an appropriate subset of general clauses for a specific transaction.

REFERENCE CLAUSE	COMMENTS
LIABILITY PROVISIONS	
Force Majeure. Except for obligations to pay money, neither Party is liable for any failure to perform or observe any of its obligations under this Agreement for, as long as and to the extent that, such performance is prevented or hindered by any circumstances beyond such Party's reasonable control (and for a reasonable period thereafter necessary for resumption of such performance) including, without limitation, declared or undeclared war, revolution, civil commotion, labor disputes, acts of public enemies, or due to any law, proclamation, regulations, ordinance, demand or requirement of any Governmental Authority. The Party whose performance is so prevented or hindered shall notify the other Party in writing of the details thereof, with reasonable specificity, within [__] days of the occurrence of such circumstances and shall take all reasonable steps to resume performance as soon as possible.	Force majeure really should not be treated as boilerplate at all. Parties should actively consider what grounds should constitute excuses for performance of their respective obligations in this particular agreement. There is background law in each state or other jurisdiction on such topics as the allocation of supplies during a shortage, whether excused or not excused. Consider whether the agreement should expressly state obligations to treat all similarly situated customers the same, the right of a manufacturer to [illegible] supply to its affiliates or itself in such allocations, or the right to treat long-term customers or customers under contract differently from short-term or spot customers. Should the other Party have an express termination right after some extended duration of suspension of performance?
Cumulative Remedies. All rights and remedies under this Agreement or by Law are cumulative and not alternative.	Watch for use of this rule with liquidated damages or exclusive remedy provisions, which may [illegible] intended to be exclusive of other possible claims.
Expenses. Except as otherwise expressly provided in this Agreement, whether or not the transactions contemplated hereby are consummated, each Party shall pay its own costs, fees and other expenses incurred in anticipation of, relating to and in connection with the negotiation and execution of this Agreement and the transactions contemplated hereby.	Do you want exceptions for certain fees, stamp taxes, other transfer taxes or other expenses? Do you want a different rule if the transaction is not consummated? "Costs," "fees" and "expenses" may have different meanings in litigation and other contexts, even if drafters tend to use them as synonyms.

[1] For the complete charts, see http://www.pillsburylaw.com/siteFiles/Publications/RespectingBoilerplate131022.pdf.

Waiver of Consequential Damages. Neither Party is liable to the other Party, whether in contract or tort, for any [consequential, incidental, indirect, special or punitive] damages incurred by such other Party relating to the breach or alleged breach of this Agreement. This exclusion applies whether or not the possibility of such damages has been disclosed or could have reasonably been foreseen, but does not apply to any such damages claimed by a third party for which a Party has an indemnification obligation under this Agreement.		Consider what kinds of damages are possible in your type of transaction. "Consequential damages" and "incidental damages" are defined in the Uniform Commercial Code, which definitions may not fit contracts in corporate and commercial or other settings. "Special damages" and "indirect damages" are defined by pleading rules and court decisions. See Glenn D. West and Sara G. Duran, *Reassessing the "Consequences" of Consequential Damage Waivers in Acquisition Agreements*, 63 The Business Lawyer 777 (May 2008). Consider whether lost profits or lost earnings are "consequential damages" in the context of this transaction. Some contracts expressly exclude cases of fraud or willful misconduct. Consequential damages for personal injury in the case of consumer goods may not be subject to waiver. Waivers might cause the remaining remedy to fail of its essential purpose or be unconscionable and thus be unenforceable. (See UCC § 2-719)
PARTY PROVISIONS		
Successors and Assigns. This Agreement is binding on and inures to the benefit of each Party and its successors and permitted assigns.		If one of the Parties is a natural person, by background law his or her successors may include estates, executors, heirs and legatees.
No Third-Party Beneficiaries. Except for the [indemnity and defense] provisions of Section [__] (which are intended to be for the benefit of the Persons identified therein), the terms of this Agreement are intended solely for the benefit of the Parties, and it is not the intention of the Parties to confer third-party beneficiary rights upon any other Person.		Consider expressly excluding fund trustees and benefit plan participants. Employee benefit provisions sometimes have a robust no-third-party beneficiaries clause.
Assignment. [Buyer may assign its rights and delegate performance of its obligations hereunder to an Affiliate and Seller may assign its rights for security purposes to a [lender]. Except as provided in the preceding sentence,] neither Party may assign its rights [or delegate performance of its obligations] under this Agreement without the prior written consent of the other party, [such consent not to be unreasonably withheld]. [Any attempt to make any assignment or delegation not in compliance with this Agreement is void.] [Unless expressly agreed otherwise, no assignment shall release the assigning Party from its obligations hereunder.]		Do you want to permit assignments to Affiliates? What about changes in control of a Party? What about mergers or reorganizations? What about the initial assignment of rights in the Agreement for security for financing purposes? What about subsequent foreclosures of such security interests? Should assignment be prohibited outright, or subject expressly to consent? If the latter, should a reasonableness standard be imposed, or should it be expressly disclaimed ("sole discretion")? Do you want any attempted assignment to be "void," or to just be voidable or a breach? Is the assignor released upon an effective assignment? If not, the assignor may be treated as a surety for its assignee's performance, with some but not all of the traditional suretyship defenses. Do you want to prohibit delegation or subcontracting of obligations? Do you want the Parties to split net profits from any assignment? Do you want the Party proposing assignment to pay the other Party's costs, including attorneys' fees, for reviewing the assignment? Do you want to provide for a preemptive right (a right of first refusal or right of first offer) in lieu of, or in addition to, an assignment restriction?

ENFORCEMENT PROVISIONS		
Governing Law. This Agreement and all rights and obligations of the Parties arising out of or relating to this Agreement or the negotiation, execution or performance hereof, including any tort obligations, are governed by and construed in accordance with the Law of the State of X, without giving effect to any conflict or choice of law provision that would result in the imposition of another state's Law.		Consider expressly addressing not only the agreement but also the negotiation process, and tort as well as contract obligations. In contracts for sale of goods, consider disclaiming applicability of United Nations Vienna Convention on the International Sale of Goods ("CISG"). In contracts that involve a mixture of goods and services, or sale and leases or licenses, consider specifying whether the UCC or another particular body of law governs.
Attorneys' Fees. If either Party brings an action arising out of or relating to this Agreement, the prevailing party shall be entitled to recover its reasonable attorneys' fees and expenses incurred in such action from the unsuccessful party.		Do you want a fee-shifting clause? For all clauses or just some? Consider scenarios, depending on whether this is in your client's interest. Some forms define what kind of victory is needed (total, or at least better than the other party's last settlement offer) for one to be a "prevailing" Party. In some states, a one-way fee shifting clause is automatically read as a two-way fee shifting clause (e.g., California Civil Code § 1717).

APPENDIX

One lawyer's boilerplate is another's deal term

The preceding concise chart necessarily excludes many provisions that may appear in a large number of contracts of a particular type. Some drafters may consider them boilerplate, while others would bring some of them up explicitly with their clients or with subject-matter specialists in the main negotiation. Just listing the following clauses here in this appendix may provoke some thoughts and serve some purpose.

DEFINITIONS AND RULES

- Priority as between agreements, between main text and exhibits, between words and numerals
- Disclaimer of purchase order or invoice terms--salvoes in the "battle of the forms"
- "Charter Documents," "Hazardous Materials," "Liabilities" (and "Environmental Liabilities"), "Liens" (and "Permitted Liens"), "Permits," "Release," "Remediation," "Taxes"

LIABILITY

- "Default," "Event of Default"
- Remedies and process for default
- Termination for default or convenience
- Consequences of termination
- Waiver or confirmation of setoff rights
- Joint and several, or several, liability
- Waiver or limitation of debtor exemptions, or guarantor and surety defenses
- Late charges, interest, usury savings clauses
- Disclaimers of warranties
- Limitations of liability
- Liquidated damages
- Passage of title and risk of loss
- Indemnification, "Claims," "Proceedings"
- Release--in California, quoting Civil Code § 1542

DISPUTE RESOLUTION

- Consent to exclusive or non-exclusive jurisdiction and forum
- Executive resolution of disputes
- Mediation
- Arbitration
- Waiver of jury trial
- Waiver of sovereign or tribal immunity
- Consent to specific performance
- Consent to temporary or permanent injunctive relief
- Change of statute of limitations

OTHER

- Disclaimers of fiduciary duties or partnership status
- Legally required disclosures, especially in consumer contexts
- Currency, conversion and non-convertibility
- Ownership, protection and infringement of intellectual property
- Handling of FOIA requests
- Compliance with laws generally, or with those on equal employment opportunity, or other specific bodies of law
- Export of encryption technology
- Unauthorized payments, prohibited counterparties
- Independent contractor
- No brokers or finders

More on "Anatomy of a Proxy Contest: Process, Tactics & Strategies"

In response to inquiries received from some of the several hundred attendees who tuned into the DealLawyers.com webcast—"Anatomy of a Proxy Fight: Process, Tactics & Strategies" (or the hundreds more who listened to the audio archive or read the webcast transcript posted on that site)—we spoke with ***Cliff Neimeth****, senior M&A partner of Greenberg Traurig LLP, who offered the following addendum to the webcast:*

1. Solicitations, Non-Solicitations & Exempt Solicitations

One area we were asked to address following our webcast is: what is a solicitation and which solicitation activities are exempt from the federal proxy rules? The starting point is Rule 14a-1(l)(1) under Regulation 14A. Rule 14a-1(l)(1) defines "solicitation" to include (i) any request for a proxy, irrespective of whether the request is accompanied by or included in a formal proxy card; (ii) any request to sign or abstain from signing or to revoke a proxy; and (iii) the furnishing of a form of proxy or other communication to securityholders under circumstances reasonably calculated to result in obtaining, withholding or revoking a proxy.

Clause (iii) captures a broad range of communications prior to the start of a formal solicitation that are designed to influence voting decisions. That said, Rule 14a-1(l)(2)(iv) provides that a communication by a securityholder who does not otherwise engage in a solicitation that is limited to a statement of how the securityholder intends to vote and the reasons for its voting decision, is not a solicitation provided that the statement is communicated by certain prescribed means. Disclosure by a significant institutional holder regarding its voting intentions and the reasons therefor can be very useful for an activist stockholder or for the registrant depending on the circumstances. However, knowing the boundary between the third clause of Rule 14a-1(l)(1) and the exemption in Rule 14a-1(l)(2)(iv) requires careful analysis.

Rule 14a-2 also exempts certain solicitation activities from the full breadth of the federal proxy rules. For example, Rule 14a-2(b)(1) exempts solicitations by any person who does not, directly or indirectly, seek authority to act on its own behalf or on behalf of another person as a proxy or furnish or request a proxy. This exemption is often used in "vote no" campaigns—where a securityholder is opposing a merger or similar transaction—and in "withhold authority" campaigns for the election of directors.

Importantly, the foregoing exemption does not apply to solicitations by the registrant or any of its officers, directors, affiliates or associates; any director-nominee on whose behalf proxies are being solicited; Schedule 13D filers, unless such persons have disclaimed in Item 4 any intention or reservation of the right to engage in a control transaction; and certain other enumerated persons. Pursuant to Rule 14a-6(g), persons who utilize the exemption for solicitations conducted in reliance on Rule 14a-2(b)(1), and who own securities with a market value in excess of $5 million, must file with the SEC (i.e., under cover of a "Notice of Exempt Solicitation") all written materials used in the solicitation not later than three days after the date of first use.

"The Rule of 10": The Rule of 10 is a private solicitation exemption sometimes used by activist investors. Under Rule 14a-2(b)(2), any solicitation by a person, other than on behalf of the registrant, where the aggregate number of persons solicited is not more than 10, is exempt from the proxy statement filing and informational requirements (but not the anti-fraud requirements) of the federal proxy rules. This can be meaningful exemption where the institutional ownership of a Registrant is extremely concentrated. Accordingly, many advance notice bylaw provisions these days require disclosure of whether an opposition stockholder intends to engage in a full (public) proxy solicitation or, instead, rely on any one or more exemptions from solicitation.

If a dissident uses The Rule of 10, it elects to forgo public solicitation activities and it cannot conduct a public (widespread) messaging campaign. Even in the case of an institutionally concentrated registrant, this can have some practical adverse consequences. For example, a number of large index funds, asset managers and other (non-hedge fund) institutions may not, as a matter of policy, meet with a contestant who has declined to file with the SEC and mail to stockholders a definitive opposition proxy statement and proxy card. Moreover, ISS similarly may not meet (in person or by telephone conference) with a dissident who has not filed definitive materials and will only reference in its report information that's in the public domain. Lastly, if the dissident is a 13D filer, The Rule of 10 may not be available to it depending on the dissident's Item 4 disclosures and, to the extent the dissident does communicate with ISS, under certain circumstances such communication could be deemed to exceed the Rule's 10-person limitation.

2. Rule 14a-12 Solicitations Before Filing Proxy Statements

Under Rule 14a-12, a contestant—be it the registrant or a dissident stockholder—is permitted to engage in a solicitation (and, therefore, furnish written solicitation materials) before furnishing a definitive proxy statement to stockholders. There are, however, certain requirements to utilize the rule; namely that each communication has to identify the persons who are participants in the solicitation and describe their stock ownership and other interests in the solicitation. Alternatively, the communication can advise securityholders where to obtain that information so long as the disclosure is clear and prominent.

The 14a-12 communication also has to advise securityholders, again in a clear and prominent legend, that they should read the actual filed and mailed proxy statement once it becomes available because it contains important information and the legend also has to advise where to obtain the proxy statement (e.g., on the SEC's EDGAR website) and other documents free of charge.

The 14a-12 communication cannot contain or furnish a form of proxy card, voting authorization or written consent. These are furnished to securityholders together with or prior to furnishing the definitive proxy statement.

All 14a-12 communications must be filed with the SEC on the date they are first published or disseminated to securityholders, meaning, before 5:30 p.m. Eastern time, on the day the communication is first furnished. The filing is made on Schedule 14A and there is a "14a-12 box" to check on the cover page.

Registrants typically use 14a-12 for "stop-look & listen" communications that caution stockholders not to make up their minds or take any action until they receive from the registrant all relevant information. 14a-12 can be used for a variety of messaging purposes and there are certain additional technical requirements where 14a-12 is used in opposition solicitations.

The SEC Staff has made it clear that Rule 14a-12 cannot be used unless, at the time of use, the user has a good faith intention to file with the Staff and furnish in definitive form to securityholders a proxy statement and proxy card. This is sometimes a point of attack by registrants where an activist or dissident stockholder in its advance notice bylaw letter or other communication — includes an equivocal intention to file a proxy or merely reserves a right to do so.

3. SEC Filing & Staff Comment-Review Process

In a contest, the registrant's preliminary proxy materials and the insurgent's opposition proxy materials are filed publicly with the SEC. These are live filings with special EDGAR tags that denote "proxy contest" so that the filings are routed to the SEC's Office of Mergers & Acquisitions ("OMA") for assignment to the appropriate Staff attorneys.

The trigger event requiring registrant's to file preliminarily, i.e., file not just mailing definitive proxy materials to stockholders, is the disclosure in the proxy statement that refers to—or comments on—a contest or an impending opposition solicitation. If the registrant has received a formal nomination letter under its advance notice bylaws or otherwise indicating a dissident's intention to run an opposition solicitation, or if a public announcement has been made by the dissident of such an intention (such as in a 13D filing), the registrant is on notice. Sometimes there are 'proxy threat' threat letters and other more equivocal communications from a dissident that may not rise to the level of an absolute statement of intention to nominate and run an opposition slate or to launch a vote no campaign against a pending M&A deal.

The disclosure in the registrant's proxy statement about an impending contest usually is contained in a "background section" that describes the material past contacts, meetings and communications between the registrant and its opponent and the events that led to submission of the nomination letter or other opposition notice.

Typically, the proxy statement also will state, briefly, why the board believes that the reelection of its nominees or, if applicable, a vote in favor of its other business or transaction proposal is in the best interests of the registrant and its stockholders. The registrant's proxy statement also will notify stockholders that they may be receiving opposition proxy materials and that such materials should be disregarded, as well as other information about returning the registrant's (white) proxy card and not the dissident's (other color) proxy card, how to change a previously submitted vote by submitting a later dated and signed proxy card, the inability to "split votes" on cards, and other technical disclosures of that nature.

Under the federal proxy rules, definitive proxy materials cannot be filed and mailed until at least 10 calendar days after the preliminary filing. That, of course, presumes that either there was no review or no SEC Staff comments received on the preliminary filing, or that the comments that were received were cleared to the OMA Staff's satisfaction within 10 calendar days. I'll never say never, but I can't remember a time where I've seen either a "no review" or no comments received from the Staff in a proxy contest. Also, it's hard to get proxy materials in and out of the SEC in exactly 10 days.

However, the OMA attorneys are extremely diligent about issuing comments and trying to get filings cleared for mailing quickly—usually two weeks, depending on how careful the filing parties are with their disclosure—because the Staff understands how time sensitive a contested election (or other type of proxy contest) is and the importance of providing stockholders with as much time as possible to digest full disclosure from both sides about the nature, reasons for and consequences of the proxy contest and to allow unrestricted public solicitation activity by both sides.

Very often the OMA attorneys will work outside of ordinary business hours. They will review proposed disclosures in advance of formal EDGAR amendments to preliminary filings, depending on the sensitivities and time pressures involved. The OMA attorneys really deserve commendation for this. That said, it behooves both sides to expedite the SEC Staff review and comment process and to get out onto the street with their proxy materials as soon as possible.

4. Fight Letters

The best way to reduce SEC staff comments and to expedite the review process is to file preliminary materials that are "light" in terms of advocacy and platform statements. The real campaign talking points and theme statements are saved for the "fight letters." Unlike the proxy statement—which is reviewed by the SEC Staff in advance of definitive mailing—under the proxy rules, fight letters are additional solicitation materials and are not pre-cleared. These materials can be mailed right away to stockholders so long as they are filed with the SEC no later than 5:30 p.m. Eastern time, on the date the materials were first used or disseminated.

So what typically happens is that both sides will file their preliminary proxy statements with minimal campaign statements, and on the day the definitive proxy statement is first mailed, it will be accompanied by a fight letter that was not pre-cleared by the SEC Staff—although it will be filed with the SEC on the date it is first mailed. Stockholders typically receive the proxy statement and fight letter in the same mailing package.

The fight letters, which are aimed more at the retail stockholder audience, are usually two-page documents that advocate—in a pithy/attention grabbing format—the contestant's most persuasive campaign talking points and themes. They usually contain both qualitative and quantitative historical performance information and, in the case of the registrant, its plans and proposals being implemented to improve financial results and the stock price. These communications highlight what the contestant believes are the most important "selling points" to obtain stockholder votes.

In the typical proxy fight, each side will mail three (sometimes four) fight letters commencing on the definitive proxy statement mailing date up to a week or so prior to the stockholder meeting date. One or two of the letters are usually in the form of an "attack ad" emphasizing the key negatives about the opposition's experience, platform and qualifications.

Even though fight letters are not pre-cleared by the SEC Staff, the parties must make certain that the content doesn't contain false, exaggerated or misleading statements, characterizations or other statements that are expressed as fact, but instead are unsubstantiated or merely matters of opinion or belief. Otherwise, you could run afoul of Rule 14a-9—which could result in embarrassing corrective mailings or retractions.

5. Bed Bug Letters

Because getting in and out of the SEC as quickly as possible is key, the more time a contestant has to seek votes and engage in full solicitation activities, the better. Each contestant will try to delay the other side as much as possible.

There are lots of tactical maneuvers that are used. One of the tactics to accomplish this is the poison pen (or "bed bug") letter. From the perspective of counsel to the registrant, as soon as the dissident's opposition proxy materials are filed with the SEC in preliminary form, counsel and the appropriate personnel at the company will comb through every statement of fact, reference, statistic, past performance disclosure, everything couched as a conclusion, statement of belief, [illegible] proxy statement, if any, —literally everything cover-to-cover—in the proxy statement to see if there is anything that is mischaracterized, taken out of context, omits material information (or tells a half truth), anything that is unsubstantiated and the like.

You also look for any line-item disclosure defects and technical proxy rule compliance failures in the opposition's disclosures. In the case of a dissident who is a 13D filer, you would also look to see if there were any failures to timely file amendments and make requisite disclosures and any failures to file exhibits.

Then, in a very pointed manner, in correspondence addressed to the SEC's examining attorney in OMA, you bring all of these issues to his or her attention. With respect to everything being challenged as factually inaccurate or unsubstantiated, it's important to provide the OMA attorney with copies of all supporting data, primary sources of information, published reports and the like to support your allegations and to make his or her review easier. Of course, the dissident will go through the same process to try to challenge the registrant's preliminary filings.

Although it's important not to inundate the SEC Staff—you should pick and choose your battles judiciously—bed bug letters and all of the supporting materials can sometimes be lengthy, so it's important to get them submitted as quickly as possible after the opponent's preliminary materials are first filed.

The purpose of bed bug letters—which, by the way, are not on EDGAR correspondence (although they eventually become publicly available)—is not to convince the Staff to halt the proxy contest or commence an enforcement proceeding against your opponent (although in the most egregious and rare case, that could be a possibility). Instead, it is to bring to the SEC Staff's attention any disclosures that, in good faith, you know are inaccurate so that the disclosures are either corrected or deleted.

So, in effect, you're assisting the SEC Staff in ensuring that stockholders have fair, complete and accurate disclosure to base their voting decision. Of course, from a tactical perspective, the more successful you are in diluting your opponent's arguments, the better—and the bed bug letter also is used to delay the OMA attorney's issuance of comments (or to increase the number of comments they issue) so that clearing the opposition's proxy statement for definitive mailing takes additional days. You're putting yourself in the shoes of the OMA attorney assigned to review the opposition's materials and you're trying to write comments for the examiner in the hopes that they will agree with many of them (at least in part) and issue them in a Staff comment letter. At a minimum, you're trying to give the examiner a head start and to influence the way they read the opposition's materials.

It's always gratifying when you materially delay the other side. In a recent contest to replace the entire board where I defended the registrant, I filed a 25-page poison pen letter a couple of days after the insurgent's preliminary proxy filing and it took the activist fund almost one month to mail its definitive materials. You could plainly see in the definitive proxy statement all of the deletions and changes and new qualifying disclosures that were made since the date of the preliminary filing. That gave us a great jump start on the street and the entire incumbent board was reelected.

A sister publication of the popular newsletter, *The Corporate Counsel*, *Deal Lawyers* is a bi-monthly newsletter for M&A practitioners to keep them abreast of the latest developments and analyze deal practices.

Publisher: **Jesse M. Brill.** Formerly an attorney with the Securities and Exchange Commission and a leading authority on executive compensation practices, Mr. Brill is the Publisher/Editor of *The Corporate Counsel*, Chair of the National Association of Stock Plan Professionals, CompensationStandards.com and DealLawyers.com.

Editor: **Broc Romanek**, former SEC attorney and Editor of DealLawyers.com and TheCorporateCounsel.net. Broc can be reached at broc@naspp.com.