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Setting the Record Straight: Regulation G Doesn't Apply to M&A Forecasts

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Last year, Cleary Gottlieb published an alert memo highlighting the SEC Staff's renewed focus on whether the use of non-GAAP financial measures (NGFMs) by domestic registrants complies with the requirements of Regulation G.[1]

Recently, a number of plaintiff-stockholders of target companies in M&A transactions have brought purported class actions in federal court alleging that the "Forecasts" section in M&A disclosure documents violates Regulation G. In support of these M&A disclosure related claims, plaintiffs have been citing our memo and a related blog post about these SEC Staff initiatives, which relate to earnings releases and periodic reports, even though our prior publications did not address the application of Regulation G to M&A disclosure documents.

It is true that the projections in the "Forecasts" section of M&A disclosure documents include projections that are not GAAP. Indeed, projected unlevered free cash flows are a central input into any discounted cash flow analysis. But in our view, the contention that these projections are subject to Regulation G is incorrect.

M&A Forecasts Don't Prompt Reg G Concerns

The provision of a GAAP reconciliation for these forecasts would not serve the purpose for which Regulation G was adopted—namely, to prevent a company from misleading investors by providing NGFMs that obscure its GAAP results and guidance. No such concern applies to the "Forecasts" section of M&A disclosure documents, where the data are being provided solely to enable shareholders to understand the specific, projected financial metrics that the company's financial advisor used in its financial analyses to support a fairness opinion.

The standard introduction to these projections in every M&A disclosure document states that these forward-looking data are not intended to provide reliable guidance about historical or future financial performance of the company, but are disclosed because they were used by the financial advisors in their fairness opinion analyses. Indeed, for this reason, Regulation G contains a special exemption (Rule 100(d)) for

[1] Cleary Alert Memorandum: Non-GAAP Financial Measures: The SEC's Evolving Views, June 13, 2016, available at https://www.clearygottlieb.com/~/media/cgsh/files/publication-pdfs/alert-memos/2016/201660.pdf

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all communications made pursuant to Item 1015(b)(6) of Regulation M-A, which provides for disclosure of a summary of "the bases for and methods of arriving at" a fairness opinion.[2]

Genealogy of the "Forecasts" Section in M&A Disclosure Documents

To understand the relationship between the "Forecasts" section and the Item 1015(b)(6) exemption from Regulation G, it is important to understand the genealogy of the "Forecasts" section in M&A disclosure documents.

The SEC rules applicable to disclosure about fairness opinions differ depending on whether the transaction is structured as a merger (where the fairness opinion disclosure is typically in a proxy statement and governed by Regulation 14A) or as a tender offer or exchange offer (where the fairness opinion disclosure is typically in a recommendation statement governed by Regulation 14D).

In a merger proxy statement, if it references the receipt by the target board of an opinion that the transaction is fair to the target shareholders, Item 14(b)(6) of Schedule 14A requires that the disclosure include a long-form summary of the financial analyses underlying the fairness opinion.

Prior to 2002, however, proxy statements rarely, if ever, included a "Forecasts" section to accompany the summary of the financial analyses. Moreover, in a tender offer recommendation statement, there has never been a line-item requirement to include a summary of the financial analyses underlying a fairness opinion.

Then, with its 2002 decision in *In re Pure Resources*,[3] the Delaware Chancery Court kicked off several years of opinions focused on disclosure requirements in connection with M&A transactions. Then Vice Chancellor (now Chief Justice) Leo Strine observed that disclosure of a banker's fairness opinion, without more, was insufficient, and that a "fair summary" of the analyses was required.[4] This reasoning was based on a straightforward interpretation of the case law about what is "material" to investors and echoed the rationale for the SEC rule that requires disclosure of a summary of the financial analyses in merger proxy statements:

> [I]nvestment bankers' analyses … usually address the most important issue to stockholders—the sufficiency of the consideration being offered to them for their shares in a merger or tender offer. … [C]ourts must be candid in acknowledging that the disclosure of the banker's "fairness opinion" alone and without more, provides stockholders with nothing other than a conclusion…[5]

Prior to *Pure Resources*, the Delaware courts had, in their own words, been reluctant to mandate disclosure requirements in proxy statements and tender offer documents due to "[f]ear [of] stepping on the SEC's toes."[6] But, beginning with *Pure Resources*, the Delaware judiciary has regularly opined on what disclosure is (and is not) required for a "fair summary" of the analyses underlying the fairness opinion in M&A disclosure documents (whether they are proxy statements or tender offer recommendation statements).

Eventually the Court of Chancery, prompted by a plaintiffs' bar energized by disclosure claims, began to focus on the extent to which, when a fairness opinion is disclosed to the target shareholders, the key projections used in the financial analyses underlying the opinion should also be disclosed. Citing *Pure Resources*, the Court held that a fair summary should include, in some instances and subject to a

[2] The projections included in the "Forecasts" section of M&A disclosure documents are similarly exempt from Item 10(e) of Regulation S-K, which also includes an exemption for disclosure contained in communications made pursuant to Item 1015 of Regulation M-A. In addition, Item 10(e) includes an exemption for financial measures "required to be disclosed by … [SEC] rules, or a system of regulation of a government or governmental authority … that is applicable to the registrant," which would apply to the projections to the extent they are included in an M&A disclosure document in order to satisfy Rule 12b-20 or state law requirements such as the requirements stemming from Delaware case law described below.

[3] *In re Pure Res., Inc., S'holders Litig.,* 808 A.2d 421 (Del. Ch. 2002).

[4] *Id.* at 448-450.

[5] *Id.* at 449.

[6] *Id.*

number of facts and circumstances, not just a summary of the underlying financial analyses but also the key financial projections underlying those analyses:

> Once a board broaches a topic in its disclosures, a duty attaches to provide information that is "materially complete and unbiased by the omission of material facts." For this reason, when a banker's endorsement [in a fairness opinion] of the fairness of a transaction is touted to shareholders, the valuation methods used to arrive at that opinion as well as the key inputs … must also be fairly disclosed.[7]

Forecasts in M&A Disclosure Documents are Exempt from Regulation G

Meanwhile, just as this Delaware-driven evolution of disclosure requirements in M&A disclosure documents was getting going—in fact a mere three months after the *Pure Resources* decision—in January 2003 the SEC adopted Regulation G. In response to strong arguments in comment letters on the proposed rule from the M&A community, the SEC included the special exemption for all communications made pursuant to Item 1015 of Regulation M-A.[8]

However, there are two potential misunderstandings that might cast doubt on whether the projections really are part of the summary of what underlies the fairness opinion and therefore exempt from Regulation G due to their being disclosed pursuant to Item 1015.

First, these financial projections typically appear in a separate section titled "Forecasts," rather than the section titled "Opinion of the Financial Advisor", which is more obviously a summary of what underlies the fairness opinion and therefore more clearly made pursuant to Item 1015(b)(6).

The reason for the appearance of the projections in a separate "Forecasts" section is to emphasize that the management of the target company, rather than the financial advisor, prepared the projections; but the rationale for including the "Forecasts" section, and therefore the availability of the exemption from Regulation G, is unaffected and falls squarely within Item 1015(b)(6)—to summarize what underlies the fairness opinion.

The second misunderstanding is that, while Item 1015(b)(6) is cross-referenced in the form for a proxy statement on Schedule 14A, there is no express reference to Item 1015(b)(6) in the form for a tender offer statement on Schedule TO or a tender offer recommendation statement on Schedule 14D-9. As a result, it could be argued that the Rule 100(d) exemption from Regulation G does not extend to the "Forecasts" section in a tender offer disclosure document.

However, the SEC Staff has explicitly recognized the applicability of the Rule 100(d) exemption to tender offer documents in the SEC's Compliance and Disclosure Interpretations (C&DIs) on NGFMs.[9] In addition, *Pure Resources* and its progeny filled this gap in Schedule 14D-9, so for tender offer recommendation statements we have a regime where target boards, by mandate of the Delaware courts, effectively comply with Item 1015(b)(6) when preparing Schedule 14D-9.

In commenting on M&A disclosure documents, the SEC Staff has from time to time raised the GAAP reconciliation requirement of Regulation G in the context of the disclosure of management projections used by financial advisors in their fairness analyses. In response to these comments, several companies and their outside counsel have argued that the reconciliation exemption in Rule 100(d) of Regulation G applies to these forecasts consistent with our analysis above. The SEC Staff has sometimes challenged such arguments, leading some companies to ultimately include a GAAP reconciliation of the financial

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[7] *In re Netsmart Techs., Inc. S'holders Litig.,* 924 A.2d 171, 203-204 (Del. Ch. 2007) (emphasis added). See also *Maric Capital Master Fund, Ltd. V. Plato Learning, Inc.,* 11 A.3d 1175 (Del. Ch. 2010); Transcript Ruling on Motion for Expedited Proceedings, *In re S1 Corp. S'holders Litig.,* Consolidated C.A. No. 6771-VCP (Del. Ch. 2011). The Court has never adopted a bright line rule that forecasts are always required to be disclosed and has always deferred to the general standard of materiality, which takes account of the specific facts and circumstances.

[8] See SEC, Final Rule: Conditions for Use of Non-GAAP Financial Measures (Release No. 33-8176; 34-47226), Section II.A.1.c., available at https://www.sec.gov/rules/final/33-8176.htm.

[9] Non-GAAP Financial Measures, Compliance and Disclosure Interpretations, Question 101.01 (Jan. 11, 2010). In connection with the issuance of the new C&DI described below, the prior C&DI has been updated effective as of October 17, 2017 and renumbered as Question 101.02. The prior reference to the applicability of the Rule 100(d) exemption to tender offers has been removed as part of that update.

forecasts in order to end the comment process, but a number of companies have mailed the disclosure documents to the target's shareholders without such a reconciliation and without further comment from the SEC Staff.[10]

In sum, in our view Regulation G does not require that the management projections used by financial advisors to opine on the financial fairness of merger consideration be reconciled to GAAP. This information is not the type of information that Regulation G was adopted to police and should be considered exempt from the reconciliation requirements of Regulation G pursuant to the exemption for disclosures of data underlying the fairness opinion as described in Item 1015(b)(6) of Regulation M-A.

New SEC Interpretation Helps Limit Reg G as an Enabler of Merger Litigation

We urged the SEC Staff to provide guidance confirming the applicability of the exemption from Regulation G to disclosure of projections underlying a fairness opinion in M&A disclosure documents, and we are pleased to report that the SEC Staff provided such guidance in a new C&DI on NGFMs dated October 17, 2017.

The new C&DI confirms that financial measures included in forecasts provided to financial advisors and used in connection with business combination transactions are not NGFMs if:

– The financial measures are included in forecasts provided to the financial advisor for the purpose of rendering an opinion that is materially related to the business combination transaction; and

– The forecasts are being disclosed in order to comply with Item 1015 of Regulation M-A or requirements under state or foreign law, including case law, regarding disclosure of the financial advisor's analyses or substantive work.

This confirmatory guidance is especially important in view of the spate of federal court complaints challenging M&A disclosure documents since the Delaware Chancery Court's 2016 *Trulia* decision.[11] In *Trulia*, the Court made it clear that Delaware state courts would no longer approve previously commonplace disclosure-only settlements containing only immaterial disclosures, and courts of other states have increasingly cited *Trulia* with approval and followed it.[12] Plaintiffs then turned to the federal courts, and in order to eliminate the risk of a delay in transactions stemming from the allegation that the inclusion of the forecasts without a GAAP reconciliation violates Regulation G, the target companies would often provide the GAAP reconciliation and pay the plaintiffs' lawyers a mootness fee. The SEC Staff's new guidance should put an end to the need to prepare unnecessary reconciliations and pay undeserved attorney's fees to dispose of these meritless claims.

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[10] See, *e.g.*, Oracle Corp., Response to SEC Comment Letter, Oct. 4, 2016 (in respect of projections included in a combined Tender Offer Statement/Rule 13e-3 Transaction Statement on Schedule TO); Brocade Communications Systems, Inc., Response to SEC Comment Letter, May 19, 2016 (in respect of projections included in a registration statement on Form S-4 pertaining to an exchange offer); Symmetry Surgical, Inc., Response to SEC Comment Letter, Oct. 8, 2014 (in respect of projections included in a registration statement on Form S-4). But see Apollo Commercial Real Estate Finance, Inc., SEC Comment Letter, June 3, 2016 (suggesting the disclosure of projections is not required by Item 1015 as it relates to Form S-4 or Schedule 13E-3); HomeAway, Inc., SEC Comment Letter, December 2, 2015 (suggesting the disclosure of projections is not required by Item 1015 as it relates to Schedule 14D-9).

[11] *In re Trulia, Inc. S'holder Litig.,* 129 A.3d 884 (Del. Ch. 2016).

[12] *Id.* at 898. For further information on the impact of *Trulia* on M&A-related stockholder litigation, please read our blog post at https://www.clearymawatch.com/2016/08/update-about-disclosure-only-settlements-in-ma-litigation/.

Structuring Asset Deals: "Traditional" vs. "Our Watch, Your Watch" Constructs

By Jonathan Corsico, Partner, and Benjamin Bodurian, Associate, of Gibson, Dunn & Crutcher LLP

In M&A transactions that are structured as asset purchases, the buyer and seller must define how the various assets and liabilities of the target business are to be divided between them. This exercise is unique to asset deals—in deals structured as mergers or stock purchases, all assets and liabilities of the target business effectively transfer to the buyer.

But, in an asset deal, the parties have significantly more flexibility. This flexibility can be both a blessing and a curse. From the buyer's perspective, it allows the buyer to cherry pick which liabilities should transfer to the buyer and which liabilities should remain with the seller (leaving liabilities with the seller is obviously good for the buyer).

From the seller's perspective, it allows the seller to cherry pick which assets should transfer to the buyer and which assets should remain with the seller (leaving assets with the seller is obviously good for the seller).

As can be imagined, this level of flexibility often engenders significant negotiation and even confusion among the deal teams. When defining assets and liabilities should transfer, the parties must consider two core questions: (1) what types of assets and liabilities should transfer (*e.g.*, cash, accounts receivable, accounts payable, facilities, product warranty liabilities, raw materials, etc.) and (2) how should those various types of assets and liabilities be divided temporally (*e.g.*, if the buyer is going to acquire accounts receivable, is it all accounts receivable that exist at the closing? Or just accounts receivable generated in the period between signing and closing? Or some other construct?).

Because of the significant level of flexibility afforded in an asset deal, parties often attempt to simplify negotiations by agreeing to generalized rules for dividing assets and liabilities. Two such rules relate to the temporal division—the "traditional" approach and the "our watch, your watch" approach.

The "Traditional" Approach

The traditional approach mirrors the results obtained in a stock purchase or merger structure. Specifically, in the traditional approach, the buyer purchases assets and assumes liabilities of the target business regardless of whether such assets and liabilities relate to the pre-closing or post-closing period.

For example, the buyer might purchase "all rights in respect of any offensive litigation relating to the target business, regardless of when the facts giving rise to such offensive litigation arise." Conversely, the buyer would assume "all liabilities in respect of any defensive litigation relating to the target business, regardless of when the facts giving rise to such defensive litigation arise."

As can be seen, the traditional approach has no temporal limitation. Instead, the buyer simply acquires everything, as would occur in a stock purchase or merger deal.

The "Our Watch, Your Watch" Approach

In the our watch, your watch approach, the buyer purchases assets and assumes liabilities of the target business only to the extent such assets and liabilities relate to the post-closing period.

The concept behind this approach is that the target business was owned by the seller for the pre-closing period, and thus the seller should keep the full benefit and bear the full burden of the business for that period. In essence, the buyer is purchasing only the future, while the past remains with the seller.

In an our watch, your watch deal, the previous example regarding offensive and defensive litigation would be reformulated as follows:

- The buyer purchases "all rights in respect of any offensive litigation to the extent (a) relating to the target business and (b) based upon underlying facts and circumstances occurring after the closing."

- The buyer assumes "all liabilities in respect of any defensive litigation to the extent (a) relating to the target business and (b) based upon underlying facts and circumstances occurring after the closing."
- The seller retains "all rights in respect of any offensive litigation to the extent based upon underlying facts and circumstances occurring prior to the closing."
- The seller retains "all liabilities in respect of any defensive litigation to the extent based upon underlying facts and circumstances occurring prior to the closing."

Which Approach is Better?

At a high level, neither approach is better than the other. The two approaches are simply different ways of dividing the target business between the buyer and the seller. That said, on balance, most sellers prefer the traditional approach because it results in the buyer assuming all legacy liabilities of the target business.

This can be particularly important for businesses that have long-lived liabilities (*e.g.*, asbestos liabilities), where the seller wants to wash its hands of the target business.

Conversely, on balance, most buyers prefer the our watch, your watch approach because it results in the seller retaining those same long-lived liabilities. Most buyers envision themselves as purchasing the future, and they would be happy to leave the past behind with the seller.

Depending upon the nature and magnitude of the historical liabilities of the target business, the our watch, your watch construct may warrant a higher deal price than the traditional approach. For example, if the seller is going to retain millions of dollars in projected pre-closing liabilities, it seems appropriate for the buyer to compensate the seller accordingly.

In practice, many deals are structured with a "hybrid" approach, in which some assets and liabilities are divided using the traditional approach and others are divided using the our watch, your watch approach. This hybrid structure can result in a very confusing deal, where it is hard to concisely explain how the deal is structured. It can also result in significant negotiation, where the parties fight item-by-item rather than agreeing to a more generalized construct.

Depending upon the negotiating leverage of the parties (and the drafting skills of their attorneys), this hybrid structure can also result in counterintuitive outcomes, where one party may acquire/retain assets for a given period, but not also assume/retain associated liabilities for such period.

For example, it is entirely possible that a buyer could acquire all pre-closing accounts receivable, but not assume any pre-closing accounts payable. This seemingly unfair result would be achieved by changing only a handful of words in the purchase agreement.

Unexpected Consequences of the "Our Watch, Your Watch" Construct

Even in its pure form, the our watch, your watch construct can create unexpected consequences. None of these consequences are necessarily bad—but they can be surprising.

For example, the our watch, your watch construct obviates the need for a working capital adjustment (and the associated negotiation and accounting diligence that go into such a provision). Since the seller is retaining all pre-closing assets and all pre-closing liabilities, there is nothing to adjust following the closing (as described below, the parties will still need to consider difficult questions about how to temporally divide "work- in-progress" assets and liabilities).

Similarly, the our watch, your watch construct significantly minimizes the utility of many, if not most, of the seller's representations and warranties and the indemnity backing those reps. This fact can come as a surprise to deal teams that spent significant time and political capital negotiating the reps and the indemnity package.

For example, suppose that the seller represents to the buyer that, as of the signing of the purchase agreement, the seller is not aware of any basis for any defensive litigation involving the target business. However, after the closing, a third party sues the buyer over a pre-closing event that the seller knew about at signing, thus rendering the seller's rep untrue.

Assuming the deal has a customary indemnity package, under both the traditional and our watch, your watch constructs, the seller must indemnify the buyer for losses arising from the breached rep. This indemnity obligation will be limited, however, by the caps, baskets and other similar provisions that the parties carefully negotiated.

But, under the typical our watch, your watch construct, the seller must also indemnify the buyer for all of the buyer's losses arising from the litigation, because the events underlying the litigation arose pre-closing (*i.e.*, on the "seller's watch"). This indemnity obligation arises regardless of whether or not the rep was breached, and will not be subject to the caps, baskets and the like that apply to rep breaches.

Thus, this indemnity obligation effectively moots all of the time and energy that the parties devoted to negotiating both the rep related to pre-closing litigation and the provisions of the indemnity related to that rep.

Finally, the our watch, your watch approach can raise difficult questions about how to temporally divide "work-in-progress" assets and liabilities. For example, assume that the seller is party to a contract under which the target business provides prepaid repair and maintenance of construction equipment, and that right before the closing, one of the pieces of equipment breaks down.

The buyer will want the seller to honor the contract, since the breakdown occurred in the pre-closing period and the seller received prepayment for the services. However, the buyer has just acquired the business, including all of the employees, tools and spare parts that would be put to use in repairing the equipment. Thus, the seller is effectively unable to repair the equipment.

To further complicate matters, assume the seller believes that the equipment was damaged through negligent use, and therefore does not want to honor the contract for this particular repair.

This results in the seller being in a dispute with a customer of the target business. The buyer will not be pleased with that situation, since the seller has every incentive to minimize its liability, even if doing so poisons the buyer's future relationship with the customer.

Controlling Stockholders: Forging Ahead With "Entire Fairness" (Or Playing It Safer)

By Paul Scrivano and Jane Goldstein, Partners, and Sarah Young, Associate, of Ropes & Gray LLP

Controlling stockholder buyouts of Delaware corporations are generally scrutinized under the lens of "entire fairness" to determine whether the transaction was the product of fair dealing and fair price. Notably, however, under *M&F Worldwide*,[1] the Delaware Supreme Court confirmed that a target corporation's use at the outset of a transaction of a special committee of disinterested directors and an informed vote of a majority of the minority of the target's stockholders, among other factors, will result in a transaction that would be reviewed under the deferential business judgment rule instead of the stringent entire fairness test.

The burden of proving entire fairness and the perception of a significant risk of a negative outcome under an entire fairness review frequently results in deal participants allowing the fate of the transaction to be determined not only by a special committee, but, even more critically, by the majority of the minority stockholder vote.

ACP Master: Entire Fairness Standard May Not be Fatal

However, the recent Delaware Chancery Court decision in *ACP Master, Ltd. v. Sprint Corp. / ACP Master, Ltd. v. Clearwire Corp*. highlights that entire fairness may not be fatal, and that a finding of entire fairness may overcome earlier instances of conduct or process that may fall short or that otherwise had "flaws" and "blemishes."

In *ACP Master*, the Delaware Chancery Court acknowledged instances of alleged unfair conduct of Sprint Nextel Corporation (the controlling stockholder) and Softbank Corp. (the proposed acquirer of Sprint) in connection with an attempted buyout of Clearwire Corporation, including, among others: obstructing several material business opportunities of Clearwire (including the potential sale of spectrum); vote buying; making retributive threats to Clearwire's minority stockholders; and insisting on dilutive conversion pricing in bridge financing.

The Chancery Court noted that "[i]f Clearwire's stockholders had approved the original merger at $2.97 per share . . . this array of misconduct would have resulted in a finding of unfair dealing and a damages award in the form of a fairer price." Notwithstanding, the Chancery Court found that such instances of alleged unfair conduct "made little difference" after Clearwire's stockholders refused to support Sprint's initial $2.97 per share offer and an interloper, DISH, drove the deal price up in an arm's-length process and at a price of $5.00 per share that the Chancery Court found to be fair.

The Chancery Court noted that "[t]he stockholders' refusal to take [the $2.97 per share] price, and DISH's intervention in the sale process, freshened the atmosphere and created a competitive dynamic . . . [that] led to the $5.00 per share merger consideration, independent of the earlier acts of unfair dealing by Sprint and Softbank." The transaction presumably did not qualify for business judgment rule review under *M&F Worldwide* because Sprint and Softbank did not propose the transaction with the procedural protections of a special committee and informed majority of the minority vote at the outset.

In *ACP Master*, Vice Chancellor Laster accepted, without deciding, that Sprint was Clearwire's controlling stockholder. Under Delaware law, a controlling stockholder exists when a stockholder: (1) owns more than 50% of the voting power of a corporation; or (2) exercises control over the business and affairs of the corporation. Vice Chancellor Laster noted that Sprint owned a majority of Clearwire's equity, which "traditionally sufficed to confer controlling stockholder status and concomitant fiduciary duties."

Sprint, however, argued that it was not a controlling stockholder because certain governance provisions in an equityholders agreement had prevented it from exercising effective control over Clearwire, and, as a result, it did not owe fiduciary duties to Clearwire and its minority stockholders. In other words, Sprint attempted to argue that, while it was a majority stockholder of Clearwire, it did not exercise actual control over Clearwire because of contractual provisions that neutered its controller status.

While there may be some appeal to Sprint's position, Vice Chancellor Laster did not ultimately rule on Sprint's argument because he found that, in any event, the Clearwire-Sprint merger was entirely fair and Sprint did not breach its fiduciary duties.

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[1] *Kahn v. M&F Worldwide Corp.,* 88 A.3d 635 (Del. 2014).

Lessons for Controlling Stockholders

Although the Chancery Court found that Sprint's and Softbank's alleged misconduct was later "cleansed" by DISH's intervention in the sale process, ACP Master provides important lessons for a controlling stockholder on actions that it could take, or should avoid taking, when negotiating a transformative transaction with its controlled affiliate to reduce the risk of a Delaware court finding that the controlling stockholder cannot satisfy procedural fairness.

Interfering Actively with Potential Alternatives. A controlling stockholder may be permitted to veto any sale to a third party; however, where the controlling stockholder holds more than 50% of the voting equity, the controlling stockholder runs substantial risks, if it uses its control position to foreclose or deter alternatives that may be available to the target company (*e.g.*, the potential sale of Clearwire spectrum to either Qualcomm or Google).

With regard to the spectrum sale to Qualcomm, Vice Chancellor Laster concluded that the effect of Sprint's and Softbank's alleged interference on Clearwire's ultimate bargaining position with Sprint was unclear. However, Vice Chancellor Laster noted that the Qualcomm incident would have provided some evidence of unfairness if the final deal price had remained at $2.97 per share. Sprint and Softbank also allegedly interfered with a potential sale of spectrum to Google.

After DISH intervened and the merger consideration increased to $5.00 per share, the Google incident diminished in importance because, even if Clearwire's Special Committee had known about Google's interest, it might have enabled them to bargain for a transaction above $2.97 per share, but it could not have led to the realization of value exceeding the final deal price of $5.00 per share.

Fiduciary Duty of Candor. The plaintiffs criticized the negotiations between Clearwire's Special Committee and Sprint by arguing that Sprint deprived the Special Committee of material information by failing to disclose its projections for its use of Clearwire's spectrum. Vice Chancellor Laster rejected the plaintiffs' claim, observing that "the controller's duty of disclosure stops at the point when forcing disclosure would undermine the potential for arm's-length negotiations to take place." Thus, he concluded that a controller is not required to disclose private information that reveals how a controller values the company and hence what the controller is willing to pay.[2]

Vote-Buying and Coercion. Vice Chancellor Laster noted that, if the transaction had been approved at $2.97 per share, Sprint could have been liable for fiduciary duty breaches for an array of alleged conduct, which included securing support from a block of minority stockholder votes by promising a broader commercial arrangement and the lack of fulsome disclosure of that side deal and the threat to exercise a conversion right under a note purchase agreement that would have resulted in substantial dilution of the minority stockholders of Clearwire if the Clearwire-Sprint merger was not approved.

Pre-emption Ultimatum. While plaintiffs complained that Sprint's demand, as a condition for its offer of $5.00 per share, that Clearwire terminate all discussions with DISH had cut short a potential bidding war between DISH and Sprint that might have yielded a higher price for Clearwire, Vice Chancellor Laster found that Sprint's alleged demand was not unduly coercive or otherwise out of bounds.

He noted that the Special Committee's acceptance of Sprint's offer and its decision to not go back to DISH was not evidence of unfair dealing. Controlling stockholders thus remain unfettered by their fiduciary duties from demanding exclusivity or other pre-emptive concessions.

Role of Projections & Synergies in Appraisal Side of *ACP Master*

Having found the transaction to be entirely fair, the Chancery Court then determined that, in the related appraisal action, the fair value for Clearwire's shares on the date of the merger was $2.13 per share—an amount significantly lower than the initial negotiated deal price of $2.97 per share. The Chancery Court adopted Sprint's expert's discounted cash flow (DCF) analysis in full, which relied on projections prepared by Clearwire's management team in the ordinary course of business.

[2] Note, however, that Schedule 13E-3 may require the controller to disclose, after the deal has been signed, any projections that were prepared in connection with the transaction, and would seem to potentially create an interesting dynamic in post-signing appraisal arbitrage claims.

In contrast, the petitioners' expert's DCF analysis relied on unrealistic projections that were prepared by Sprint's management team and were created for a specific purpose (namely, to help convince Softbank to increase its offer). Because those projections were not prepared in the ordinary course, and included assumptions that were not fully supported by the evidence, they did not reflect the operative reality of Clearwire on the date of the merger. Thus, ACP Master demonstrates the importance of ordinary-course management projections to support a meaningful DCF analysis to determine fair value.

Notably, Vice Chancellor Laster observed that there was no evidence that anyone at Sprint or SoftBank "believed that Clearwire was worth $5.00 per share [on a standalone basis]. Rather, they agreed to pay that price because of the massive synergies from the transaction and the threat that DISH posed as a hostile minority investor." Indeed, Sprint estimated potential synergies of the merger ranging from $1.5 to $2 billion, Softbank's financial adviser estimated synergies between $3 to $5 billion, and Clearwire's own estimate was over $3 billion in synergies.

Although Vice Chancellor Laster did not ultimately determine the value of these synergies, the Chancery Court's decision remains an additional reminder—following on the Delaware Supreme Court's decision in *DFC Global*[3] and Vice Chancellor Laster's prior decision in *Lender Processing Services*[4]—that Delaware courts are keenly aware of the central role that synergies play in competitive strategic transactions. However, such synergies are appropriately excluded from the calculation of fair value in an appraisal proceeding.

ACP Master suggests that respondents in appraisal actions arising out of competitive strategic transactions are well positioned to litigate synergies in appraisal actions, provided they have adequately documented the role synergies played in the transaction and that the seller successfully extracted the lion's share of the synergies that the buyer hoped to achieve.

Post-Signing Events Can Influence Entire Fairness Assessment

In addition, *ACP Master* demonstrates how events occurring after questionable negotiations, such as an interloper proposing a topping bid, have the potential to cleanse prior unfair conduct. While no controlling stockholder ever hopes for a topping bid on its transaction, it is instructive that subsequent conduct and changes in deal landscape can shift in a way that ultimately changes the result of the entire fairness assessment.

Similarly, it would seem plausible, by the Chancery Court's reasoning, that the occurrence of other events—such as a broader market sell-off, or a substantial decline in the target corporation's business—could serve as the basis for a transaction that initially appeared unfair to become entirely fair at a later point in time.

The Potential Effect of a "Majority of the Minority" Condition

ACP Master also illuminates the potential effect of including a majority of the minority stockholder vote as a condition to a controlling stockholder buyout or in an entity's governing documents. By repeatedly threatening to vote down the deal at $2.97 per share, Clearwire's minority stockholders leveraged the required majority of the minority vote to extract a meaningfully higher final offer from Sprint and Softbank.

In light of the Chancery Court's decision that the transaction was ultimately entirely fair, and the resurgence of "bumpitrage," with activist investors threatening to engineer "no" votes on deals unless the acquirer increases the deal price, deal participants would be well-advised to carefully consider the desired benefits of a majority of the minority vote provision against the potential and very real downside of being "held hostage" by activist investors.

Of course, nothing in M&A should ever be done in a vacuum, and there is certainly no "one size fits all" strategy. Deal participants should carefully weigh whether the transaction would benefit more from proceeding without a majority of the minority vote (and therefore having greater deal certainty) and facing entire fairness review if, for example, there are (or are expected to be) stockholders in the target's stockholder base who may use the majority of the minority vote to extract a higher price, or instead, requiring both a special committee and a majority of the minority vote at the outset to benefit from the more deferential business judgment rule review of the transaction.

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[3] *DFC Global Corp. v. Muirfield Value Partners, L.P.,* No. 518, 2016 (Del. Aug. 1, 2017).

[4] *Merion Capital L.P. v. Lender Processing Services, Inc.,* C.A. No. 9320-VCL (Del. Ch. Dec. 16, 2016).

PRC Acquirors: How M&A Agreements Handle Risks & Challenges

By Ethan Klingsberg, Ling Huang and Denise Shiu, Partners, and Rob Gruszecki, Practice Development Lawyer, of Cleary Gottlieb Steen & Hamilton LLP

U.S. and European companies continue to receive bids to sell themselves and their significant assets to companies based in the People's Republic of China. Evaluation of these proposals requires due diligence of the acquiror's ownership structure, assets, cash position, and financing sources.

Moreover, even if this due diligence exercise gives rise to satisfactory results, the continued unpredictability of the PRC government (including its recently enhanced foreign exchange control measures), coupled with the ties of some of these buyers and financing sources to governmental entities in the PRC, as well as the challenges that a non-PRC counterparty faces when seeking to enforce contractual obligations and non-PRC judgments in PRC courts, merit the implementation of an array of innovative provisions in M&A Agreements to protect the seller/target.

Several months ago, we reviewed these provisions in a popular blog post.[1] This article updates that post to reflect recent regulatory developments and the evolution of market practice.

The Traditional LBO Structure: Reverse Break-Up & Sponsor Guarantee

Borrowing from the private equity playbook. In the typical leveraged buyout by private equity fund sponsors since the mid-2000s, the acquiror vehicle that signs the M&A agreement is an unfunded shell company.

In these scenarios, if there is a failure to close due to a risk allocated to the acquiror vehicle (such as failures to obtain regulatory clearances or the disbursement of acquisition financing) or a material breach by the acquiror vehicle (such as a failure to use the requisite efforts to cause disbursement of the financing or the failure to close when the closing conditions have been satisfied), then the target is able to be made whole through a combination of (a) contractually-specified liquidated damages amounts payable as reverse break-up fees and (b) a guaranty of the shell vehicle's payment of these fees by the actual private equity fund which in turn has binding contribution commitments from its limited partners.

PRC Acquiror Structure: Reverse Break-Up & Credit Support

In the case of PRC acquirors, even though these entities may be well-funded holding or operating companies rather than shell vehicles, it has become a common approach to include reverse break-up fee provisions similar to those in the financial sponsor LBOs and, in place of the sponsor guaranty seen in LBOs, to employ a form of credit support for the reverse break-up fee obligation.

These credit support mechanics include payment by the acquiror of a deposit to the seller/target or into an escrow account or the delivery by the acquiror of a letter of credit or bank guaranty. Here are some observations about the workings of these reverse break-up fee structures, and the related security arrangements, in acquisitions by PRC entities.

Magnitude of the Reverse Break-up Fee. Recent reverse break-up fees accepted by PRC buyers have ranged in magnitude from approximately 3% to as high as 15% of the enterprise value of the transaction.

Timing of Security for the Reverse Break-up Fee. The required timing for having the credit support mechanic in place to secure the payment of the reverse break-up fee ranges from having the full amount of the deposit or other form of credit support in place concurrently with the signing of the M&A agreement, which can present challenges given the internal and Chinese regulatory processes required for PRC entities to obtain hard currency, to phasing in the security arrangements over periods that extend, in some cases, up to several months after the initial signing and announcement of the execution of the M&A agreement.

In some cases, the phasing in of the security arrangements is tied to the occurrence of a specific transaction-related event (*e.g.*, shortly in advance of the target's shareholder vote, upon an election to extend the drop-dead date to continue to pursue a particular regulatory approval or upon receipt of target shareholder approval).

[1] Ethan Klingsberg and Rob Gruszecki, "How M&A Agreements Handle the Risks and Challenges of PRC Acquirors," (March 24, 2016) available at http://www.clearymawatch.com/2016/03/how-ma-agreements-handle-the-risks-and-challenges-of-prc-acquirors/

In view of the risks associated with the rapidly changing foreign exchange control regime, it has become increasingly standard to require that at least a meaningful portion of the deposit or other credit support arrangement be in place at the time the definitive acquisition agreement is signed.

Magnitude of the Security Arrangements Relative to the Reverse Break-up Fee. The security arrangement will typically cover 100% of the amount of the highest possible reverse break-up fee specified in the agreement, although there are exceptions in deals involving tiered reverse break-up fees.

Currency and Jurisdiction of Security Arrangements. Escrow deposits securing reverse break-up fees are almost always in a Western currency and usually with a Western banking institution or the branch of a PRC bank located in the jurisdiction of the target, although sellers and targets are increasingly permitting portions of the deposits to be in renminbi (based on fixed foreign exchange ratios) and/or in banks in the mainland PRC.

We expect, however, that the acceptance of credit support from PRC branches of PRC banks will become more rare in view of the risks arising from recently enhanced foreign exchange controls.

Triggers for Payment of the Reverse Break-up Fee. The triggers for payment of these fees often include not only terminations as a result of failures of the PRC acquiror to perform the obligation to close when the closing conditions are satisfied and instances of similar material breaches by the PRC acquiror (including breaches of the escrow deposit covenants), but also a number of other instances, some of which are arguably specific to, or at least of heightened concern in the case of, PRC acquirors:

- Failure of CFIUS to Clear the Transaction. Targets often favor reverse break-up fees as the contractual hammer to incentivize non-US acquirors to obtain CFIUS clearance in contrast to the provisions governing the allocation of antitrust clearance risk where targets are frequently satisfied with undertakings by the acquiror to make the concessions that the antitrust authorities require as a condition to clearance.

- The reason for the different treatment is that CFIUS authorities often are not forthcoming about what, if anything, could be done by the acquiror to make the transaction palatable. Thus, even if there were a way to specifically enforce a "hell or high water" covenant by buyer to do whatever is necessary to obtain CFIUS clearance, the risk remains that the target would never be able to prove what is or was necessary to obtain CFIUS clearance due to the opaqueness of the process.

- Failure of PRC Authorities to Clear the Transaction. The theory here is that these authorities are indirectly "affiliated", or otherwise have good relationships, with the PRC acquiror and therefore any failure on their parts to clear the transaction may be more attributable to old fashioned buyer's remorse than a bona fide regulatory problem.

  In addition, the lack of transparency of these PRC regulatory authorities arguably makes it impractical for a non-PRC target, especially a publicly traded entity, to assume these execution risks. In many instances, the required PRC-related regulatory approvals that trigger the reverse break-up fee are specifically identified (*e.g.*, MOFCOM, NDRC, SAFE); however, in some agreements there is also a catch-all for any other regulatory approval related to the PRC.

- Prohibition of the Consummation of the Transaction by a PRC Governmental Entity. The rationale for this trigger is the same as for the trigger relating to the failure to obtain requisite PRC regulatory clearances, but practitioners sometimes include the latter trigger but neglect to include the former trigger. In addition, it is especially important for targets and sellers to be expansive in the scope of PRC governmental impediments that trigger the reverse break-up fee and, in particular, to cover currency conversion and cash transmission impediments.

  It is not uncommon for all PRC regulatory approvals for the combination of the businesses in question to be in hand, but for the sign off of SAFE to remain outstanding – not for the consummation of the acquisition per se but solely for the conversion of the PRC buyer's renminbi into foreign currency funds and the transmission of foreign currency funds out of the PRC.

Assuring Payment of the Purchase Price at Closing

In view of the difficulties and risks relating to securing PRC buyers' reverse break-up fee obligations, sellers and targets have been shifting their focus from reliance on the threat of a reverse break-up fee payment as a lever to assure payment of the entire purchase price at closing, to other mechanisms to assure payment of the entire purchase price at closing.

One recent U.S. public company target required the acquiror to deposit the aggregate merger consideration three business days before the target's shareholders meeting to approve the transaction. And a small-cap U.S. public company target required the acquiror to deposit into escrow at signing the full amount that would be payable to the unaffiliated stockholders at closing.

In other transactions, the parties have included specific covenants to assure that necessary steps were taken, such as incurring U.S. dollar debt outside the PRC, in the event that cash resources located within the PRC were unavailable for payment of the purchase price at closing due to currency conversion delays. However, reliance on the availability of U.S. dollar loans from PRC banks has become more challenging in recent months due to enhanced scrutiny by the PRC regulatory regime of the use of PRC assets to secure such loans.

Ability to Enforce Obligations

Although it is generally advisable for targets and sellers to include at least a reverse break-up fee structure backed by a form of reliable credit support, targets and sellers will typically include more traditional enforcement mechanics in tandem with a secured reverse break-up fee structure.

Although the enforcement by PRC courts of judgments by U.S. state and federal courts can be challenging and uncertain given the absence of a judicial treaty between the two countries, there are relatively reliable precedents for the enforcement by PRC courts of international arbitration awards obtained in accordance with the New York Convention. Arbitration provisions, however, will not be helpful when a quick order of specific performance or other equitable relief against the PRC acquiror is needed to save the transaction.

Some agreements try to combine dispute resolution provisions that specify the speedy and innovative Delaware Court of Chancery as the forum for specific performance and other equitable relief with provisions that specify arbitration as the forum for claims for damages (including, more recently, Delaware's newly adopted rapid arbitration proceedings).

However, this approach may give rise to complications, since many disputes involve claims for both equitable relief and damages, and, in any event, the access to Delaware courts may well turn out to be of value only to the PRC acquiror when seeking equitable relief against the non-PRC target.

For now, as manifested by the chart following this article, practice on all these points still varies.

Data Points from Selected Recent Transactions Involving PRC Acquirors

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Silver Biotech Investment Limited (Caymans) Affiliates of GL Capital Management, Bank of China Group Investment Limited and various other PRC based sponsors	SciClone Pharmaceuticals (Delaware)	6/7/17	▪ $7.2m (1.2%) ▪ $21m (3.5%) ▪ $31.5m (5.2%)	▪ $7.2m: Acquiror fails to deposit into escrow additional $24m in cash to secure payment of maximum potential RTF within 21 days after signing ▪ $21m: Governmental/regulatory-related termination scenarios (the agreement does not specify which approvals will be necessary) ▪ $31.5m: Failure to close due to financing	▪ At signing, Acquiror deposited into escrow shares of Target's common stock owned by Acquiror and its affiliates with an aggregate value of $7.2m ▪ Within 21 days of signing, Acquiror is required to deposit approximately $24m in cash into escrow to secure payment of the maximum potential RTF (Escrow with Computershare)	Delaware
Unic Capital Management (PRC), an affiliate of Sino IC Capital China Integrated Circuit Industry Investment Fund (PRC sponsor)	Xcerra Corporation (Massachusetts)	4/7/17	▪ RMB 98,315,025 ($14.3m; 3.0%) ▪ $22.8m (4.9%) (Agreement includes fixed exchange rate of US$1: RMB6.8993)	▪ $14.25m: PRC-related regulatory and investment authority termination scenarios ▪ $22.8m: Failure to close due to financing or termination for certain Acquiror breaches	Within three business days of signing, Acquiror must deliver to Target a letter of guarantee from the Bank of Beijing in favor of a PRC wholly owned subsidiary of Target guaranteeing payment of the RMB 98,315,025 RTF	▪ Massachusetts law ▪ Federal Arbitration Act and Rules of Arbitration of the International Chamber of Commerce (in NY)
Ta Chen Stainless Pipe Co (Taiwan)	Empire Resources Inc (Delaware)	3/30/17	None	No RTF Note: Transaction structured as a tender offer under DE law	At signing, buyer deposited $15m into escrow with JPMorgan Chase for payment to unaffiliated tendering shareholders upon closing of the tender offer	▪ Delaware law ▪ Delaware courts
Zhonghong Zhuoye Group Co (PRC) Sun Wise (UK) Co (an affiliate of ZZG)	Funds affiliated with Blackstone (Sale of 21% stake in SeaWorld by Blackstone)	3/24/17	▪ $50m (6.9%) ▪ $25m (3.5%)	<u>$50m</u> ▪ Termination or inability to close solely as a result of PRC regulatory order ▪ CFIUS-related termination scenarios ▪ Failure to close due to financing or termination for certain Acquiror breaches <u>$25m</u> ▪ Termination or inability to close and at time an order is in effect from a PRC governmental authority preventing the transaction (lesser fee appears to be payable in circumstances where PRC is not necessarily the only regulatory-related issue)	$50m deposited into escrow at signing (Citibank in New York) Agreement also includes representation that Acquiror has sufficient funds (free of any liens, etc.) at Wing Lung Bank in Hong Kong to pay the purchase price and has provided seller with an accurate bank statement showing proof thereof	▪ Delaware law ▪ Delaware courts

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Alipay Holding Limited (Hong Kong) as Guarantor Alipay (UK) Limited (Affiliates of Alibaba)	MoneyGram International (Delaware)	1/26/17	▪ $82m (4.1%) ▪ $30m (1.5%)	$82m ▪ CFIUS-related termination scenarios resulting from a willful and material breach ▪ Failure to close due to financing or termination for certain Acquiror breaches $30m ▪ CFIUS-related termination scenarios not involving breach by Acquiror	$45m irrevocable payment guarantee issued by Citibank, Hong Kong branch at signing to secure payment of RTF	▪ Delaware law ▪ Delaware courts
HNA Tourism Group Co (PRC)	Funds affiliated with Blackstone (Sale of 25% stake in Hilton by Blackstone)	10/24/16	▪ $500m (5.6%)	▪ PRC regulatory-related termination scenarios ▪ Failure to close due to financing or termination for certain Acquiror breaches	$500m deposited into escrow at signing (JP Morgan Chase)	▪ Delaware law ▪ Delaware courts
Asia Pacific Global Capital, a subsidiary of China Oceanwide Holdings Group (PRC)	Genworth Financial (Delaware)	10/21/16	▪ $210m (7.8%)	▪ PRC and Taiwan regulatory-related termination scenarios ▪ Failure to close due to certain Acquiror breaches	Acquiror pays full amount of RBF to Target at signing pursuant to an escrow agreement and the funds are subsequently deposited into an escrow account with Citibank	▪ Delaware law ▪ Delaware courts (with disputes resolved under Delaware Rapid Arbitration Act)
Avolon Holdings (Caymans) Bohai Financial Investment Holding (PRC) HNA Group (PRC) as guarantor	CIT Group's aircraft leasing unit	10/6/16	▪ $500m (3.8%) ▪ $600m (4.5%) (RTF increases upon completion of internal restructuring allowing for acquisition of additional assets)	▪ PRC regulatory-related termination scenarios ▪ CFIUS-related termination scenarios ▪ Additional antitrust-related termination scenarios ▪ Failure by Acquiror to obtain stockholder approval ▪ Failure to close due to financing or termination for certain Acquiror breaches	$500m deposited into escrow prior to signing (JPMorgan Chase Bank) with additional $100 million deposited upon completion of internal restructuring	▪ Delaware law ▪ Delaware courts (with disputes resolved under Delaware Rapid Arbitration Act)
GlobalWafers Co (PRC)	SunEdison Semiconductor (Singapore)	8/17/16	▪ $40m (6.0%)	▪ PRC regulatory-related termination scenarios ▪ CFIUS-related termination scenarios ▪ Failure to close due to financing or termination for certain Acquiror breaches	At signing buyer deposited $40m into an escrow account at Mega International Commercial Bank	▪ Delaware law (with exception for laws relevant to scheme of arrangement and internal corporate matters) ▪ Delaware courts

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Alpha Frontier Limited (Caymans) China Oceanwide Holdings Group and various PRC-based sponsors	Caesars Interactive Entertainment sale of Playtika (Israel)	7/30/16	▪ $300m deposit (6.8%)	▪ Regulatory-related termination scenarios in connection with required approvals ▪ Termination for certain breaches by Acquiror In addition, if buyer does not make the second $150m deposit on time it forfeits the initial $150m	Buyer deposited $150m into escrow with U.S. Bank NA at signing and was required to deposit an additional $150 million within 10 days	▪ Delaware law ▪ Delaware courts
Fujian Grand Chip Investment Fund (PRC)	AIXTRON SE (Germany)	5/23/16	▪ EUR 25m (3.7%)	▪ PRC regulatory-related termination scenarios ▪ German regulatory-related termination scenarios ▪ Additional scenarios involving a failure by buyer to launch or consummate the takeover offer (including inability to finance the transaction) Agreement includes a CFIUS condition which does not trigger the RTF	Buyer deposited EUR 25m or its RMB equivalent "into a bank account with a reputable PRC bank" to be held in escrow	▪ German law ▪ Arbitration in Germany
Apex Technology (PRC) Various Caymans entities	Lexmark International (Delaware)	4/19/16	▪ $150 million (4.1%) ▪ $95 million (2.6%)	<u>$150m</u> ▪ PRC regulatory-related termination scenarios ▪ Buyer fails to deliver the letter of credit ▪ Failure to close due to financing or termination for certain Acquiror breaches <u>$95m</u> ▪ CFIUS-related termination scenarios ▪ Regulatory-related termination scenarios in Austria, Germany, Poland or Russia	Acquiror required to deliver to Target a letter of credit issued by Bank of China Limited, New York Branch in the face amount of $150m within 10 days of signing	▪ Delaware law ▪ Delaware courts (with disputes resolved under Delaware Rapid Arbitration Act)
ShangHai Pudong Science and Technology Investment Co (PRC)	Montage Technology Group (Caymans)	6/11/14	$67.9m (12.8%)	▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE and Anti-Monopoly Bureau) ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to on date when closing should occur per the terms of the agreement) ▪ Acquiror fails to deposit RTF into escrow on either of the specified dates (provided that Target has made its escrow deposits)	Deposited in two parts: ▪ 50% at signing (or on first business day escrow account is set up to receive deposits) ▪ 50% within five business days after target shareholder approval (Escrow with Citibank, N.A. in New York) Target was similarly required to deposit its termination fee.	▪ New York law ▪ New York courts

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Tianjin Tianhai Investment Company (PRC) HNA Group Co as Guarantor (PRC)	Ingram Micro Inc (Delaware)	2/17/16	▪ $200m (3.2%) if terminated before 3/18 ▪ $300m (4.8%) if terminated between 3/18 and 4/16 ▪ $400m (6.4%) if terminated after 4/16	▪ CFIUS-related termination scenarios ▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE, Anti-Monopoly Bureau) ▪ HSR and other non-PRC-related antitrust termination scenarios ▪ Failure to obtain clearance from Shanghai Stock Exchange ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within seven business days) ▪ Failure to obtain Acquiror shareholder approval ▪ Acquiror fails to deposit RTF into escrow on any of the specified dates	Deposited in three parts: ▪ $200m within week of signing ▪ $100m more within one month ▪ $100m more within two months (Escrow with Deutsche Bank Trust Company Americas)	▪ Delaware law ▪ Delaware courts
Suzhou Dongshan Precision Manufacturing Co (PRC)	Multi-Fineline Electronix, Inc (Delaware)	2/4/16	▪ $27.45m (6.7%) ▪ $37.45m (9.2%) if termination occurs at some point after Acquiror elects to extend drop dead date	▪ CFIUS-related termination scenarios ▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE, Anti-Monopoly Bureau and any other PRC Governmental Authorities) ▪ Certain HSR-related termination scenarios where Parent elects not to close due to the imposition of a burdensome condition ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to by drop dead date) ▪ Failure to obtain Acquiror shareholder approval	Deposited in three parts: ▪ $20m on signing date ▪ $7.45m within 21 days of signing ▪ $10m upon Acquiror election to extend drop dead date (Escrow with Citibank N.A., New York)	▪ Delaware law ▪ Delaware courts
China National Chemical Corporation (PRC) China National Agrochemical Corporation (PRC)	Syngenta AG (Swiss)	2/2/16	$3 billion (6.5%)	▪ PRC regulatory-related termination scenarios (NDRC, SAFE, Ministry of Commerce) ▪ PRC Anti-Monopoly, HSR and other antitrust-related termination scenarios (Agreement includes a CFIUS condition)	No escrow	▪ Swiss law ▪ Arbitration under the rules of the International Chamber of Commerce (in Zurich)

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Beijing E-town Dragon Semiconductor (PRC limited partnership) Beijing E-Town International Investment & Development Co as Guarantor (PRC)	Mattson Technology, Inc (Delaware)	12/1/15	$17.16m (6.7%)	▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within five business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants (Agreement includes CFIUS and PRC regulatory conditions, but there is no RTF in connection with those other than as it would relate to a breach or failure to close by Acquiror described above)	No escrow	▪ Delaware law ▪ Hong Kong International Arbitration Centre (Acquiror parties also waive right to claim sovereign immunity or immunity of any other kind)
Anbang Insurance Group Co (PRC)	Fidelity & Guaranty Life (Delaware)	11/8/15	None	None (Agreement includes a CFIUS condition, as well as insurance-related regulatory approvals in the U.S. and PRC)	No escrow	▪ Delaware law ▪ Delaware courts
Bohai Leasing Co (PRC) HNA Group Co as Guarantor (PRC)	Avolon Holdings Limited (Caymans)	9/3/15	$350m (4.6%)	▪ CFIUS-related termination scenarios ▪ PRC regulatory-related termination scenarios (approvals not specified) ▪ Failure to obtain clearance from Shenzhen Stock Exchange ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within three business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants ▪ Failure to obtain Acquiror shareholder approval ▪ Acquiror fails to deposit RTF into escrow within seven business days	Deposited in two parts: ▪ $200m within one business day of signing ▪ $75m within seven business days of signing ▪ $75m had previously been placed in escrow in connection with potential equity investment (Escrow with Citibank N.A.)	▪ Delaware law ▪ International Court of Arbitration of the International Chamber of Commerce, but Delaware courts for certain disputes, including specific performance, closing conditions and termination
Shuanghui International Holdings (Caymans) Rotary Vortex as depositor of escrow (Hong Kong)	Smithfield Foods, Inc. (Virginia)	Smithfield Foods, Inc. (Virginia)	$275m (3.9%)	▪ Antitrust or other regulatory-related termination scenarios in any country (other than CFIUS approval) ▪ Willful failure to close by Acquiror when conditions satisfied ▪ Financing failure	At signing of merger agreement (Bank of China, New York Branch)	▪ Delaware law ▪ Delaware courts

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Leyard American Corporation (Delaware) Leyard Opto-electronic Co as Guarantor (PRC)	Planar Systems, Inc (Oregon)	8/12/15	$8m (5.7%)	▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within three business days) ▪ Failure to obtain Acquiror shareholder approval (Agreement includes CFIUS and other unspecified regulatory conditions but they do not trigger the RTF)	At signing of merger agreement (Escrow with Wilmington Trust, NA)	▪ New York law ▪ New York courts except Singapore International Arbitration Centre for claims by Target against Guarantor
Xiamen Insight Investment Co (PRC)	Xueda Education Group (Caymans but operations located in PRC)	7/26/15	▪ $4.4m (4.0%) for failure to obtain Acquiror shareholder approval ▪ $14m (13.0%) for Acquiror breach or failure to close ▪ $17m (15.8%) for all other RTF scenarios	▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE, CSRC, Ministry of Education, Ministry of Finance and Anti-Monopoly Bureau) ▪ Failure to obtain clearance from Shenzhen Stock Exchange ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within five business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants ▪ Failure to obtain Acquiror shareholder approval	Within five business days after Target's shareholder approval is obtained (RMB-denominated escrow account in PRC with escrow agent to be agreed by parties)	▪ New York law, except Cayman law for certain corporate matters ▪ Hong Kong International Arbitration Centre
Total Merchant Limited (Samao) Company is controlled by the Chairman of the Board of the Ye Chiu Group, which includes Ye Chiu Metal Recycling (China) Ltd.	Metalico, Inc (Delaware)	6/15/15	$3.12m (3.0%)	▪ Acquiror fails to deposit the amount of the RTF into escrow within 21 business days ▪ Acquiror fails to deposit the aggregate consideration (sufficient to pay all shareholders and make certain other payments at closing) three business days prior to Target's shareholder meeting	▪ $3.12m within 21 days after signing (with a nationally recognized U.S. bank) ▪ Aggregate consideration (sufficient to pay all shareholders and make certain other closing payments) three business days prior to Target's shareholder meeting (with the U.S. branch of Maybank Banking Berhad)	▪ Delaware law ▪ Delaware courts

Acquiror	Target/Seller	Signing Date	Reverse Termination Fee (in USD and as a % of Enterprise Value)	Reverse Termination Fee (RTF) Triggers	Approach to Securing RTF and/or Other Payment Obligations	Governing Law and Dispute Resolution
Pegasus Investment Holdings (Cayman) Beijing HT Capital Investment and various PRC-based sponsors	China Mobile Games and Entertainment Group (Caymans but operations located in PRC)	6/9/15	RMB 300m (7.5%)	▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE and any other PRC Governmental Authorities), as well as orders by non-PRC entities prohibiting the transaction ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within five business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants	Within five business days after signing (Escrow with Shenzhen branch of China Merchants Bank)	▪ New York law except Cayman law for certain corporate matters ▪ Hong Kong International Arbitration Centre
Seagull International Limited (Caymans) Hua Capital Management and various PRC-based sponsors	OmniVision Technologies, Inc (Delaware)	4/30/15	$56m (4.1%)	▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within three business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants (Agreement includes CFIUS and PRC regulatory conditions, but there is no RTF in connection with those other than as it would relate to a breach or failure to close by Acquiror described above)	No escrow	▪ Delaware law ▪ Hong Kong International Arbitration Centre
Beijing Uphill Investment Co (PRC) Summitview Capital (Pujiang) and various PRC-based sponsors	Integrated Silicon Solution, Inc (Delaware)	3/12/15	$19.17m (2.8%)	▪ PRC regulatory-related termination scenarios (NDRC, MOFCOM, SAFE and any other PRC Governmental Authorities) ▪ Taiwan regulatory-related termination scenarios (approvals not specified) ▪ Acquiror failure to close (all conditions satisfied, Target is prepared to close and Acquiror fails to within three business days) ▪ Termination for uncured breach by Acquiror of its reps/covenants	At signing in two accounts: ▪ $11.4m in RMB equivalent (Deutsche Bank (China) Co., Ltd. Shanghai Branch) ▪ $7.8m (China Merchants Bank) Target also required to deposit its termination fee into a U.S. escrow account within 20 business days of signing (with 7.0% per annum penalty for failure to do so).	▪ Delaware law ▪ Hong Kong International Arbitration Centre

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