EXAM NO. _____

MERGERS & ACQUISITIONS

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Spring Semester 2007

FINAL EXAMINATION

Instructions:

1. This is an open-book examination. You may bring any materials you wish to the examination with the exception of computers, telephones or other electronic devices. Calculators, however, are permitted – although we do not believe they will be necessary.

2. This is a 3-hour examination and is worth 125 points. There are 9 short- to medium-answer essay questions. The point allocation by question is as follows:

Question 1 = 20 points	
Question 2 = 20 points	
Question 3 = 15 points	
Questions 4 – 9 are based on a single fact pattern:	
►No. 4 = 15 points ►No. 5 = 15 points ►No. 6 = 5 points	►No. 7 = 5 points ►No. 8 = 15 points ►No. 9 = 15 points

It is your responsibility to apportion your time appropriately among the nine questions. If you base your time on the number of possible points per question, the time apportionment should be approximately:

►Question No. 1 = 29 minutes
►Question No. 2 = 29 minutes
►Question No. 3 = 21.5 minutes
►Question No. 4 = 21.5 minutes
►Question No. 5 = 21.5 minutes
►Question No. 6 = 7 minutes
►Question No. 7 = 7 minutes
►Question No. 8 = 21.5 minutes
►Question No. 9 = 21.5 minutes

3. Do not write your name on the examination or your blue books – only your examination number.

4. Please answer the questions in blue books. Remember to write your examination number on each blue book that you use. The only answers that will be graded are the answers written into blue books. While you are free to use scratch paper, answers written on scratch paper, or anything else other than a blue book, will not be read and will not be counted for any credit. <u>Please write only on the front side of the pages in the blue book</u>.

5. Please remember that organization, persuasiveness, neatness and legibility all count in determining your grade on an answer. To improve the organization of an answer, you may wish to quickly outline the answer on a separate sheet of paper prior to writing your full answer in the blue book.

6. Should you find it necessary in answering a question to assume a fact not given in the problem as stated, you may do so. However, you should clearly indicate that you are making an assumption and you should explain why you consider it a reasonable assumption to make.

<u>Good luck on the examination</u>!

DO NOT TURN TO PAGE 2 UNTIL THE PROCTOR TELLS YOU TO BEGIN

<u>QUESTION NO. 1</u> (20 points possible)

Your firm has a client that is referred to you regarding a potential business deal. The client owns a relatively small, privately held manufacturing company without a lot of excess cash. They are interested in acquiring one of their suppliers. The supplier is also a small, privately held family business. The two principal shareholders of the supplier are active in the business and would like to stay on with the company after the transaction.

Please explain what you would discuss during your initial meeting with the client. You are not expected to recommend a deal structure yet, just highlights of important issues for your client to consider and the process you will undertake to advise them.

<u>QUESTION NO. 2</u> (20 points possible):

Lance Inc. ("Lance") is a leading manufacturer of custom bicycles. Lance wishes to acquire substantially all of the assets (but none of the liabilities) of Voodoo Co. ("Voodoo"), another custom bicycle manufacturer. Specifically, Lance will be acquiring all of Voodoo's inventory and intellectual property (e.g., the trademark, the patented technology and the trade secrets). The purchase price that is being discussed between Lance and Voodoo is roughly $10 million for Voodoo's assets. In the deal, however, Lance will not be purchasing Voodoo's manufacturing facility (the "Facility").

During the due diligence on Voodoo, Lance discovered some environmental issues. It turns out that the Facility is likely contaminated. The contamination stems from chemicals that Voodoo used in its manufacturing process roughly 20 years ago. Based on a preliminary examination of the site, the cost for cleaning up the contamination is estimated to be between $20 million and $25 million.

You are an attorney with Milkem and Bilkem, a leading Wall Street law firm, where you specialize in M&A transactions. Lance is one of your most important clients and has called you to advise it on its possible acquisition of Voodoo. Lance does not want to incur any liability on the environmental clean-up for the Facility. Please analyze Lance's potential exposure to the environmental liability surrounding the Facility if Lance continues with the planned asset acquisition with Voodoo.

<u>QUESTION NO. 3</u> (15 points possible):

Monkey Corp. ("Monkey") is attempting to acquire Banana Inc. ("Banana") pursuant to a forward triangular merger. In the merger, each outstanding share of Banana's capital stock will be converted into the right to receive $10 in cash. Both Monkey and Banana are Delaware corporations. Banana has three classes of equity stock: (1) Common Stock; (2) Series A Preferred Stock; and (3) Series B Preferred Stock. More specifically, Banana's capital structure can be summarized as follows:

(a) **<u>Common Stock</u>:**

►Outstanding shares = 8,000,000

(b) **Series A Preferred Stock:**

▶Outstanding shares = 1,000,000; liquidation preference of $20 per share.

(c) **Series B Preferred Stock:**

▶Outstanding shares = 1,000,000; liquidation preference of $25 per share

(d) **Relative Voting Power:**

▶Voting as a single class, the holders of Banana's common stock would have 80% of the voting power of Banana, the Series A Holders would have 10% of the voting power and the holders of Series B would have 10% of the voting power.

Banana's amended certificate of incorporation includes the following provisions related to class voting:

> **Article IV – Part 2.3:** Banana may not, without the affirmative vote of greater than 66 2/3% of the outstanding shares of Series A Preferred Stock, (i) alter or change any rights or preferences of the Series A Preferred Stock pursuant to §242 of the Delaware General Corporation Code, or (ii) engage in a dissolution, liquidation or winding up of the corporation.
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> **Article IV – Part 3.3:** Banana may not, without the affirmative vote of greater than 66 2/3% of the outstanding shares of Series B Preferred Stock, (i) alter or change any rights or preferences of the Series B Preferred Stock pursuant to §242 of the Delaware General Corporation Code, or (ii) engage in a dissolution, liquidation or winding up of the corporation.

Holders of approximately 95% of the outstanding common stock have informed Banana that they are in favor of the merger with Monkey. However, all of the Series A and Series B shareholders have informed Banana that they are opposed to the merger with Monkey and will vote against the transaction.

Will Banana's Series A and Series B shareholders be able to block, or otherwise impede, the merger with Monkey? Are Banana's Series A and Series B shareholders entitled to receive their liquidation preference in lieu of the merger consideration?

QUESTIONS 4 – 9 WILL BE BASED ON THE FOLLOWING FACT SCENARIO:

Pierce Corporation ("Pierce") is a Delaware corporation that is traded on the New York Stock Exchange (the "NYSE"). Pierce does not have a controlling shareholder. Pierce is a diversified worldwide entertainment company with operations in a number of business segments, including (1) network, cable and radio broadcasting and programming, (2) amusement parks and family resorts and (3) studio entertainment.

Pierce had been a dominant corporation for much of its existence. From 1962 through 1997, Pierce's stock was a high-flyer on Wall Street and increased at an average rate of 20% per year. Unfortunately, Pierce's days of exceptional performance came to a screeching halt in 1997. Since 1997, Pierce's stock has performed rather poorly. At January 1, 1997, Pierce's stock price was $36/share, compared to $22/share at January 1, 2007. Rather than increase, the stock price declined 39% over the ten-year period.

The majority of investment analysts have attributed the poor stock performance to Pierce's management team, which has made a number of strategic blunders since 1997. One analyst summarized Pierce as follows: "A wonderful collection of assets that is being managed by a group of fools."

BroadCom, Inc. ("BroadCom") is also a Delaware corporation that is traded on the NYSE and does not have a controlling shareholder. BroadCom is involved in the management and operation of broadband communications networks, and in the management of programming content that is distributed over national cable television networks. In short, BroadCom is a cable company. In fact, BroadCom is the largest cable company in the country. For years, BroadCom has desired to broaden its business by acquiring a major content provider. BroadCom wishes to combine its delivery networks with a company that provides substantial media content capabilities.

Sensing that Pierce would provide the content capabilities that BroadCom is seeking and that Pierce was attractively priced, BroadCom approached Pierce during January 2007 about a possible business combination. BroadCom suggested a merger of the two entities, with Pierce shareholders receiving a combination of BroadCom stock and cash equal to $28/share ("BroadCom's Friendly Offer"), which was a 27% premium to Pierce's then share price of $22/share. Pierce refused BroadCom's Friendly Offer. To be more specific, Pierce refused to speak, or even meet, with BroadCom. Pierce's board informed BroadCom that it would never consider combining with BroadCom.

QUESTION NO. 4 (15 points possible):

> **What standard of review would be applied to the decision by Pierce's board to reject BroadCom's Friendly Offer? Please explain, including an analysis of whether Pierce's board satisfied that standard.**

On February 23, 2007, BroadCom launched an unsolicited cash and stock tender offer for all outstanding shares of Pierce at $31/share ("BroadCom's Hostile Offer"), which was a 29% premium to Pierce's closing share price of $24/share on February 22, 2007. The $31/share consisted of (a) $21/share in cash and (b) $10/share in BroadCom common stock. BroadCom's Hostile Offer included a statement by BroadCom that it would follow up the tender offer with a second-stage merger. BroadCom's Hostile Offer was contingent upon Pierce not maintaining any defensive measures in opposition to the tender offer or a second-stage merger. In connection with its tender offer, BroadCom announced its financing plan for integrating Pierce into BroadCom's business. The financing plan would require BroadCom to take on a substantial amount of debt, which would have a very negative impact on Pierce's note holders.[1] Taking on a substantial amount of debt would cause the credit rating for the existing Pierce notes to decrease. For purposes of this question, please assume that the aggregate current market value of Pierce notes is $10 billion and that the expected reduction in the credit rating would cause the market value of those same notes to decrease to $6 billion.

Following the announcement of BroadCom's Hostile Offer, Pierce's board met and did the following:

- Carefully examined BroadCom's Hostile Offer;

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[1] Notes are debt securities.

- Listened to reports from various managers within Pierce to get their opinion on how a business combination with BroadCom would impact Pierce; and

- Received an opinion from Henniker Securities (Pierce's financial advisor), which stated that in Henniker's opinion, BroadCom's Hostile Offer was not adequate.

At the end of the board meeting, Pierce's board concluded that BroadCom's Hostile Offer was not in the best interests of Pierce's shareholders and rejected the offer. In addition, Pierce's board implemented a poison pill plan. The poison pill plan provided, in short:

- The poison pill is triggered if a shareholder acquires more than 15% of the outstanding shares of Pierce without the prior approval of Pierce's board.

- If triggered, the poison pill plan will result in Pierce shareholders receiving preferred stock in Pierce. The specific rights associated with the preferred stock are not relevant for purposes of this question. You can assume, however, that if triggered, the poison pill plan would render a takeover of Pierce too expensive to pursue.

- There are two principal methods for "turning off" the poison pill:

  (1) Pierce's board can decide to turn off the poison pill by redeeming the preferred stock; or

  (2) A shareholder who has triggered the poison pill plan (a "Triggering Shareholder") can call for a special shareholder meeting to consider the poison pill plan. If more than 50% of Pierce's outstanding voting rights, other than the Triggering Shareholder, vote to turn off the poison pill plan, the pill will be dissolved.

<u>QUESTION NO. 5</u> (15 points possible):

> **BroadCom has sued to have Pierce's poison pill struck down. Please explain how a court would analyze the issue. Please also provide your forecast on whether the court will uphold or strike down the poison pill plan.**

Concord Co. ("Concord") is also a Delaware Corp and traded on the NYSE. Concord also does not have a controlling shareholder. Concord is another major entertainment company that has major operations in the television and movie industries. Following the announcement of BroadCom's Hostile Offer, Concord opened up discussions with Pierce about a possible business combination. Those talks advanced very nicely and on March 23, 2007, Concord and Pierce entered into a merger agreement (the "Concord/Pierce Merger Agreement") and announced a friendly merger. The announced terms of the Concord/Pierce merger were as follows:

- Concord will acquire Pierce through a forward triangular merger under §251 of the Delaware General Corporation Law.

- Concord will pay $5 billion to acquire Pierce through the merger. On a per share basis, Pierce shareholders will receive $30 per share in the merger. The $30 will consist of:

    (a) $21 of cash; and

    (b) $9 of Concord common stock.

On March 24, 2007, BroadCom issued a public statement that it believed BroadCom's Hostile Offer of $31/share was superior to the $30/share deal offered by Concord.

On March 25, 2007, Pierce responded to BroadCom's public statement by stating that one reason it has deemed the Concord proposal as being more favorable than BroadCom's Hostile Offer was the fact that the Concord/Pierce merger would not negatively impact Pierce's existing note holders.

<u>QUESTION NO. 6</u> (5 points possible):

> **In deciding between the BroadCom and Concord offers, was Pierce's board of directors allowed to take into account the impact on Pierce's note holders?**

On April 20, 2007, BroadCom sent a further proposal to Pierce ("BroadCom's New Proposal"). The terms of BroadCom's New Proposal were as follows:

- BroadCom will acquire Pierce through a forward triangular merger under §251 of the Delaware General Corporation Law.

- On a per share basis, Pierce shareholders will receive $35 per share in the merger. The $35 will consist of:

    (a) $25 of cash; and

    (b) $10 of BroadCom common stock.

On April 27, 2007, after substantial deliberation, Pierce's board of directors determined that BroadCom's New Proposal was superior to the terms of the Concord/Pierce merger. The Concord/Pierce Merger Agreement included a number of deal protections. The primary deal protections were:

- A "no shop" clause (which was not violated);

- A clause requiring Pierce to use "best efforts" to close the transaction (which was subject, however, to a "fiduciary out" clause); and

- A $1 billion termination fee.

Pursuant to the fiduciary out clause, Pierce's board of directors was entitled to terminate the Concord/Pierce Merger Agreement in the event that Pierce received a "Superior Offer" (such term was defined in the Concord/Pierce Merger Agreement). Pierce's board of directors determined that BroadCom's New Proposal qualified as a Superior Offer and the board and now wishes to terminate the Concord/Pierce Merger Agreement and agree to a merger with BroadCom. Terminating the Concord/Pierce Merger Agreement as a result of a Superior Offer, however, will trigger the termination fee provision. Specifically, the provision states that if Pierce's board of directors were to terminate the agreement as a result of a Superior Offer, Pierce would be required to pay Concord a $1 billion termination fee (the "Termination Fee") within 30 days of such termination.

QUESTION NO. 7 (5 points possible):

> **Would the Termination Fee from the Concord/Pierce Merger Agreement be enforceable? Please explain.**

On May 2, 2007, Concord announced that it would not attempt to top BroadCom's New Proposal. As a result, BroadCom and Pierce will go forward in consummating their business combination.

QUESTION NO. 8 (15 points possible):

> **Please provide a diagram for the proposed BroadCom/Pierce forward triangular merger and describe the board and shareholder approvals that would be required to consummate that transaction.**

QUESTION NO. 9 (15 points possible):

Will the shareholders for either BroadCom or Pierce be entitled to appraisal rights as a result of the BroadCom/Pierce forward triangular merger?

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