May 31, 2011 Draft

STANDSTILLS: FRIENDS OR FOES IN A SALE OF CORPORATE CONTROL?

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Abstract

Standstill agreements have been used in the mergers and acquisitions (M&A) context since at least the 1980s and are a standard business practice in today's negotiated M&A transactions. Despite their prevalence, however, academics and courts have paid little attention to standstills over the past three decades. Because of this lack of attention, a number of questions regarding the role of standstills in the sales process remain unanswered. Among these questions is whether standstills truly enhance the bidding process. Due to the intricacies of the bargaining process, it is virtually impossible to isolate standstills to decisively determine whether standstills maximize value. Instead, in this Article I seek to determine whether standstills impede the sales process or serve as a floor to keep the value received in auctions or other pre-signing sale processes relatively high. Former Delaware Court of Chancery Chancellor William T. Allen recently raised a related question of whether a target is obligated to enforce previously executed standstills if an acquirer makes a higher offer for the target after the target has executed a definitive acquisition agreement. This Article seeks to address and answer these questions through two lenses – bargaining norms and auction theory. Through the lens of bargaining norms, I argue that entry into, and abidance to the terms of, standstill agreements is a direct result of bargaining customs that have developed in M&A negotiations. More specifically, I argue that the possibility of incurring reputation costs, not possible contract liability, accounts for parties

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abiding to the terms of the standstill. In addition, this Article examines standstills through the lens of auction theory literature to argue that standstills do indeed help to enhance the sales process. More specifically, I argue that because standstills are inextricably tied to the provision of information to potential bidders, standstills enhance the sales process by at least providing a floor for the value received as a result of the sales process.

I. INTRODUCTION

In the multi-million and –billion dollar playground of mergers, proxy fights, and hostile takeovers, standstill agreements have been called "the [mergers and acquisitions] equivalent of a schoolyard 'time-out.'"[1] When a company puts itself up for sale in an auction or other sale process, it will generally request that auction participants agree to such a "time-out," which can exist as a separate standstill agreement or as a standstill provision in a confidentiality agreement.[2] Although the terms of standstills are anything but boilerplate, standstills typically set forth restrictions on a potential acquirer's ability to acquire or vote securities of a target company or otherwise take steps to exert control over a target company.

Traditionally, these restrictions take the form of a combination of some or all of the following: limitations on 1) purchases of securities or assets in the target without the target's prior consent; 2) the solicitation of proxies to prevent the replacement of the target's management or from otherwise exercising control over management; and 3) making tender offers for the target's securities or making other unsolicited proposals for business combination transactions.[3] In the context of negotiated transactions, the intended purpose of these restrictions is to prevent a potential acquirer from participating in a pre-signing sales process and either "jumping the gun" and bidding before other bidders or, more likely, later overbidding after the target has executed a definitive acquisition agreement with another acquirer.[4]

While standstill agreements have been used in the mergers and acquisitions context since at least the early 1980s,

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[1] *Proxy Battle Time-Out: Standstills Give Boards a Breather*, http://currents.westlawbusiness.com/Articles/2009/07/20090731_0005.aspx?cid=&src= (April 9, 2009); *see also* William G. Lawlor, *Taming the Tiger: Difficult Standstill Agreement Issues for Targets*, 7, 7 (July-Aug. 2007), published in *Deal Lawyers*, available at http://www.dechert.com/library/C&SLawlor-TamingtheTiger.pdf (stating that standstills "provide[] a stable environment in which the sale process can be managed and controlled by the target").

[2] The terms standstill, standstill agreement, and standstill provision will be used interchangeably in this Article.

[3] Marla A. Hoehn, *Letters of Intent, Confidentiality and Standstill Agreements*, in DRAFTING CORPORATE AGREEMENTS 2002-2003 78 (PLI Corp. Law & Practice Handbook Series No. B0-01K0).

[4] *See* Robert E. Spatt, *The Four Ring Circus-Round Fifteen; A Further Updated View of the Mating Dance Among Announced Merger Partners and an Unsolicited Second or Third Bidder* 35 (March 17, 2011), *available* at http://www.stblaw.com/FourRingCircus2011.pdf (discussing intended goal of standstills is to prevent deal jumping).

case law on standstills is "relatively sparse."[5] Courts in the United States and elsewhere have upheld standstills as valid but because of the sparse case law and academic literature on standstills, a number of issues remain unanswered. Among these issues is whether the execution of a standstill during the negotiation of a friendly acquisition results in a sale process that maximizes stockholder value. Vice Chancellor Leo Strine, Jr. of the Delaware Court of Chancery has indicated, in dicta, that a standstill may be required in a pre-signing sale process to "provide the [target] leverage to extract concessions from the parties who seek to make a bid."[6] However, neither courts nor academics have examined the actual impact of standstills on the pre-signing sale process. In fact, "modern academic commentators" have largely ignored standstills altogether.[7]

A related overlooked issue involving standstills is whether a target is obligated to enforce a previously executed standstill if a potential acquirer makes a higher offer for the target after it has executed a definitive acquisition agreement with another party.[8] This issue directly invokes the question of whether the standstill agreements enhance the bidding process pre-signing. Specifically, the question is why a third party who has executed a standstill during a pre-signing auction process would later overbid when the target has entered into an acqui-

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[5] *See* Guhan Subramanian, *Bargaining in the Shadow of Takeover Defenses*, 113 YALE L. J. 621, n.164 (2003) (noting that standstills "first appeared in the early 1980s"); William G. Lawlor, *Taming the Tiger: Difficult Standstill Agreement Issues for Targets*, 7, 7 (July-Aug. 2007), published in *Deal Lawyers*, available at http://www.dechert.com/library/C&SLawlor-TamingtheTiger.pdf (noting standstills have been used in M&A "for decades" and stating, "[r]emarkably, while standstills have been prevalent for a long time, the case law in the area is relatively sparse."); LOU R. KLING & EILEEN T. NUGENT, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 9.04 (2010) (stating "surprisingly little case law" exists on issue of whether target company must enforce standstill when third party makes higher bid in violation of standstill).

[6] *In re* Topps Shareholders Litigation, 926 A.2d 58, 91 (Del. Ch. 2007).

[7] *See* Subramanian, *supra* note [4], at 659 **(insert paren).**

[8] *See* KLING & NUGENT, *supra* note [4], at § 9.04 (articulating this issue and recognizing lack of case law addressing problem); *see also* William T. Allen, *Overview of Process Issues in Going Private Transaction*, *in* GOING PRIVATE 2010: DOING THE DEAL RIGHT 2010, at 69-70 (PLI Corp. L. & Practice Grp., Course Handbook Series No. 22692, 2010) ("If a Special Committee in an auction or quasi-auction process contractually obligates bidders not to overbid, is such a contract term enforceable, and if so, by whom?").

sition agreement containing deal protection devices that generally make a third party's overbid more expensive.[9] If standstills adequately satisfy the purported goals of having an orderly sales process and causing bidders to submit their optimum bids during the sales process, then overbids post-signing by parties who have previously executed a standstill should not occur. However, a few recent cases have demonstrated that this is not necessarily the case.[10] Thus, the question becomes whether these recent examples are simply outliers and are attributable to other factors or whether standstills achieve their "purported" goals in negotiated acquisitions.

This Article scrutinizes the impact of standstills on the sale process to determine whether the execution of a standstill pre-signing results in a sale process that maximizes stockholder value. Moreover, this Article endeavors to determine whether the prevalence of standstills in modern M&A transactions stems from their enhancement of the bidding process or from simple M&A bargaining norms. Part II of this Article traces the history and development of standstills. Part III explores the use of confidentiality agreements and standstills in modern-day "friendly" M&A deals. Part IV examines standstill case law, including the few cases where a court has addressed a bidder's violation of a standstill. Part V looks at standstills through the lens of bargaining norms. In this section, I argue that the entry into standstill agreements stems, in part, from bargaining norms that have developed in M&A. In addition,

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[9] Professors Paul Povel and Rajdeep Singh have alluded to this exact situation saying that, "The loser's valuation of the target may be higher than the price that the winner is supposed to pay, so she may try to break the deal by offering a higher price." Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1402 (2006). Povel and Singh go on to state that:

> In this situation, commitment to the rules is needed from the target's board, but also from the shareholders, to whom a 'hostile' bid may be addressed. . . . targets and bidders agree to use a variety of deal protection devices like lock-ups, termination fees, no-shopping clauses, or the selective lifting of poison pills. These devices make the target less attractive to rejected bidders, thereby reducing their incentive to top up the winning bid.

Id.

[10] For a discussion of topping bids made in violation of a standstill provision, see *infra* Part IV.B.

these bargaining norms include a hesitance by parties to violate the terms of a standstill that a target refuses to waive. In essence, I argue that this hesitance stems, not from a fear of incurring contractual liability, but rather from a desire to be seen as a "team player" in a market in which the party may want to be a repeat player. Part VI examines standstills through the lens of auction theory literature to argue that standstills do indeed help to enhance the sales process. More specifically, because standstills are inextricably tied to the provision of information to potential bidders, standstills enhance the sales process by at least providing a floor for the value received as a result of the sales process.

II. HISTORY AND DEVELOPMENT OF STANDSTILLS IN M&A

Standstill agreements first surfaced "in the early 1980s" and appear to have been a direct answer to the hostile takeover activity prevalent during that period.[11] They developed as a basic contract between a corporation and a substantial stockholder, which limited the ability of the shareholder to acquire and gain ownership of shares to a certain amount.[12] Standstills during this period generally contained provisions in which the shareholder agreed that it would not buy any more of that specific corporation's stock or sell or transfer the stock it already owned without the prior written approval of the corporation, and that it would vote as management directed in any board of directors' election.[13]

The *quid pro quo* of this situation was that the target company's management agreed to not oppose the stock purchase up to the given amount, would give the shareholder representation on the board of directors, and would allow the acquiring shareholder to have some registration rights for its se-

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[11] *See* Subramanian, *supra* note [4], at n.164 (noting that standstills "first appeared in the early 1980s").

[12] Larry Y. Dann & Harry DeAngelo, *Standstill Agreements, Privately Negotiated Stock Repurchases, and the Market for Corporate Control*, 11 J. FIN. ECON. 275, 276 (1983). As an example, the authors cite to an agreement between NVF company and affiliates and City Investing around 1980 in which they agreed that NVF company and affiliates ownership position in City Investing "be limited to a maximum of 21% for the next five years." *Id.*

[13] Steven A. Baronoff, Note, *The Standstill Agreement: A Case of Illegal Vote Selling and a Breach of Fiduciary Duty*, 93 YALE L.J. 1093, 1094-95 (1984).

curities.[14] During the 1980s, the most frequent use of this type of agreement occurred when one corporation bought a large amount of a target corporation's stock and the target became nervous about losing control of the company.[15] Standstill agreements grew out of this anxiety of losing control, the purpose of them being to "maintain the status quo" and to define the terms of what the investor could do during this tedious negotiation period.[16] These agreements helped to further a cooperative relationship between the target's management and the acquiring shareholder, as well as create stability between the target and the acquirer.[17]

After the emergence of standstills in the early 1980s as mainly a defensive measure in the hostile takeover environment, standstills eventually transitioned into negotiated merger agreements or friendly transactions.[18] This progression did not mean that standstills had ceased being used in hostile situations, and they in fact continue to be used as a defensive mechanism in possible hostile takeovers.[19] However, toward the latter half of the 1980s, standstill agreements began to be used in friendly acquisitions, usually in connection with a confidentiality agreement.[20]

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[14] *Id.*

[15] *Id.* at 1096.

[16] Kenneth J. Bialkin, *The Use of Standstill Agreements in Corporate Transactions*, *in* THIRTEENTH ANNUAL INSTITUTE ON SECURITIES REGULATION 1983, at 33 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B2-1281, 1983).

[17] Baronoff, *supra* note [9], at 1096-97; Meryl S. Rosenblatt, *Letters of Intent and Exclusivity, Confidentiality and Standstill Agreements*, *in* DRAFTING CORPORATE AGREEMENTS 2002-2003, at 117 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B0-01K0, 2002-2003).

[18] Edward D. Herlihy, *Various Considerations in Bank Acquisitions*, *in* BANK ACQUISITIONS AND TAKEOVERS 1986, at 540 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B4-6766, 1986); Marc P. Cherno and Lisa Klein, *Practicalities of Handling Litigation in the Context of a Leveraged Buyout*, *in* LEVERAGED ACQUISITIONS AND BUYOUTS 1987, at 273 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B4-6782, 1987).

[19] *See* E. Norman Veasey, Joseph J. Bodnar, and Bonnie Rowe Bennett, *The Growing Complexity of the Business Judgment Rule*, *in* 19th ANNUAL INSTITUTE ON SECURITIES REGULATION [year], at 168 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B4-6803, [year]) (discussing standstills in the context of hostile takeovers).

[20] *See* Alan C. Stephenson, *Auctions: Companies in Play and at Work*, *in* 20th ANNUAL INSTITUTE ON SECURITIES REGULATION [year], at 445 (PLI Corp.

More specifically, selling corporations in auctions and other pre-signing sale processes began to ask bidders to execute a standstill in exchange for access to the seller's due diligence materials. The aim of this use of standstills was less of a defensive measure and more of a deal protection device.[21] Confidentiality agreements, alone, provide for a defense against hostile transactions because the "permitted uses" of confidential information in a confidentiality agreement generally do not include using such information to formulate a hostile offer.[22] However, confidentiality agreements do not fulfill the evidentiary function that standstill agreements do in this context.[23] Namely, showing a violation of a standstill agreement is easier than showing the misuse of confidential information in violation of a confidentiality agreement.[24] Moreover, some commentators have stated that courts "may view the mere existence of standstill as eviden[ce] of the parties' intentions not to proceed on an unfriendly basis.[25] This accounts for one of the reasons that these types of agreements have become so pervasive in the M&A realm. The execution of a standstill agreement or a standstill provision became a common element of the bidding process. In today's M&A environment, standstills have become

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L. & Practice Grp., Course Handbook Series No. B4-6846, [year]) (noting companies conducting auctions might insist that bidders execute confidentiality and standstill agreements); *see also* E. Norman Veasey, et. al, *The Delaware Business Judgment Rule: The Duty to Auction a Corporation and Lock-Ups in Contested Takeovers*, *in* HOSTILE BATTLES FOR CORPORATE CONTROL 1989, at 336 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B4-6869, 1989) (discussing *Yanow v. Scientific Leasing, Inc.*, C.A. No. 9536-V.C. (Del. Ch. Feb. 5, 1988) where defendant, in its search for a bidder, allowed potential bidders access to confidential information upon their signing of confidentiality and standstill agreements).

[21] *See* Dennis J. Block, *Public Company M&A: Recent Developments in Corporate Control, Protective Mechanisms and Other Deal Protection Techniques*, *in* CONTESTS FOR CORPORATE CONTROL 2008: RECENT DEVELOPMENTS IN CORPORATE CONTROL, PROTECTIVE MECHANISMS AND OTHER DEAL PROTECTION DEVICES 2008, at 91-93 (PLI Corp. L. & Practice Grp., Course Handbook Series No. 13964, 2008) (listing standstill provisions under deal protection mechanisms heading and stating they can restrict bidders from attempting hostile takeovers).

[22] Rosenblatt, *supra* note 8, at 117.

[23] Rosenblatt, *supra* note 8, at 117.

[24] *Id.*

[25] KLING & NUGENT, *supra* note [4], at § 9.04.

so common that some have suggested that only the biggest M&A players can avoid executing a standstill.[26]

In the M&A arena presently, two basic different types of standstills are generally used.[27] The first is a standstill imposed on the seller, and it restricts the seller from negotiating with other parties during negotiations between the seller and the acquirer (this is known as a "no shop" agreement).[28] The second is a standstill imposed on the buyer, and it restricts the buyer from attempting a merger or takeover with the target without negotiating with management.[29] This second type is the focus of this Article. Typically, standstill agreements are used with the goal of "avoiding disruption" in negotiations.[30] To this end, although there are other situations in which a standstill may be used, this Article focuses on the standstill executed "in connection with the exchange of confidential information as a prelude to a possible corporate combination."[31]

Such standstills entered into pursuant to a possible corporate combination usually last from one to five years.[32] Typically, a target wants the standstill to last until the sale process is completed or a long as the bidder has material non-public information.[33] However, the oftentimes the bidder will demand

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[26] Subramanian, *supra* note [4], at 660.

[27] Marla A. Hoehn, *Letters of Intent, Confidentiality and Standstill Agreements*, *in* DRAFTING CORPORATE AGREEMENTS 2002-2003, at 78 (PLI Corp. L. & Practice Grp., Course Handbook Series No. B0-01K0, 2002-2003).

[28] *Id.*

[29] *Id.*

[30] *Id.* at 80.

[31] Bialkin, *supra* note [13], at 34. In addition, there are three other situations in which a buyer may be required to execute a standstill agreement:

> [(1)] to govern the terms of a friendly minority investment in the target company; [(2)] incident to a first-step tender offer or exchange offer pursuant to a merger agreement; or [(3)] as part of a resolution of litigation between a target company and an investor with a significant minority interest in the target company, which resolution may provide for the target company to repurchase its shares or permit the investor to retain its holdings in the target company subject to the provisions of the standstill agreement.

Id.

[32] *See* Rosenblatt, *supra* note [8], at 120.

[33] *Id.*

that the standstill expire when a third party attempts to acquire the target.[34]

III. ROLE OF CONFIDENTIALITY AGREEMENTS AND STANDSTILLS IN THE SALE PROCESS

A. The Pre-Signing Sale Process

The seminal Delaware Supreme Court case of *Revlon v. MacAndrews & Forbes Holdings, Inc.* provides that once a sale of corporate control becomes inevitable, "a board's primary duty becomes that of an auctioneer responsible for selling the company to the highest bidder."[35] However, since this holding the Delaware Supreme Court has also recognized that "no single blueprint exists" for a board to satisfy its *Revlon* duties.[36] In addition, the Delaware courts have recognized that not every sale requires a full-blown auction process but rather the board of directors of a selling corporation must meet "a reasonableness standard."[37] As prominent M&A investment banker, Bruce Wasserstein, wrote, "it can be helpful to think of the range of possibilities in terms of two types – the classic two-step auction and the negotiated sale."[38] This latter type, the negotiated sale, can follow a more limited market canvass pre-

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[34] *Id.* A bidder may require that the standstill expire

> upon the filing of a Schedule 13D by a third party disclosing an acquisition of a specified threshold percentage of the target's voting securities, upon commencement of a tender offer or a proxy contest for the election of directors, or the execution of an agreement to acquire the target or its assets.

Id.

[35] Revlon v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986).

[36] Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989).

[37] Steinhardt v. Howard-Anderson, C.A. No. 5878-VCL at 6 (Del. Ch. Jan. 24, 2011); *see also Barkan*, 567 A.2d at 1286 ("Revlon does not demand that every change in the control of a Delaware corporation be preceded by a heated bidding contest."). In Steinhardt v. Howard-Anderson, Chancellor Laster recognized that "[Revlon] was a Cunian paradigm shift if there ever was one. We had language in there like 'auction duty, radically altered state,' really seemingly heavy duty stuff. We now know it's a reasonableness standard." C.A. No. 5878-VCL at 6 (Del. Ch. Jan. 24, 2011).

[38] BRUCE WASSERSTEIN, BIG DEAL: MERGERS AND ACQUISITIONS IN THE DIGITAL AGE 746 (2000).

signing, or, in some cases, post-signing the board of directors of the target can rely on post-signing sales activities to ensure the negotiated sale reflects an adequate sale price.

1. Classic Full-Blown Auction

The classic full-blown auction is generally thought to be the best way for a board of directors to ensure satisfaction of its fiduciary duties pre-signing.[39] Not only is a classic auction thought to be the best way to prove compliance with fiduciary duties but as Professors Jeremy Bulow and Paul Klemperer found in a recent study, "the straightforward, level-playing-field competition that an auction creates is *usually* more profitable for a seller than a sequential process."[40] However, in another study of 400 takeovers of U.S. corporations during the 1990s, Professors Audra Boone and Harold Mulherin found that there were not substantial differences between the wealth effects resulting from auctions versus those resulting from negotiations.[41] Despite finding that auctions were not necessarily better at maximizing stockholder value as negotiations, Boone and Mulherin found that half of the 400 takeovers studied result from an auction process.[42] Thus, the auction process is certainly a popular form of sale even if business scholars debate whether it is more beneficial to stockholders than negotiations.

Generally, the auction begins with the preparation of an offering memorandum describing in detail the target's busi-

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[39] *See* Christina M. Sautter, *Shopping During Extended Store Hours: From No Shops to Go-Shops – The Development, Effectiveness, and Implications of Go-Shop Provisions in Change of Control Transactions*, 73 BROOK. L. REV. 525 at 576 (2008) (hereinafter, "*Go-Shops*") (noting that Delaware courts consider public auctions or pre-signing targeted market canvasses to be value maximization procedures). **GET BETTER CITE HERE**

[40] Jeremy Bulow & Paul Klemperer, *Why Do Sellers (Usually) Prefer Auctions?*, 99 AMER. ECON. REV. **[pinpt-ILL]** (2009). *See also* WASSERSTEIN, *supra* note [32], at 746 ("A wide-ranging auction generally maximizes value, particularly since the 'best buyer' on paper is not always the party who eventually pays the highest price.").

[41] Audra L. Boone & Harold Mulherin, *How are Firms Sold?*, LXII J. of Finan. 847, 871 (2007).

[42] *Id.* at 869.

ness.[43] At the same time the offering memorandum is being prepared, the target's financial advisor devises a list of potential purchasers.[44] The financial advisor then contacts the potential purchasers and those potential buyers who express a potential interest in the target are required to execute a confidentiality agreement before being given the offering memorandum and, in some cases, other information.[45] Thus, auction participants enter the auction process without first determining the value of the company and without knowing what other bidders will bid.[46] It is this this lack of knowledge that Professors Bulow and Klemperer contend enhance value maximization in an auction.[47]

At a predetermined date pursuant to the target's bidding procedures, the interested bidders are required to submit a preliminary, nonbinding indication of interest.[48] These indications of interest "will either be a number or range of numbers that are supposed to represent 'bidders' first approximations of their estimates of value of the target.'"[49] The target and its financial advisor usually then narrow the field of bidders based on the prices contained in the indications of interests and other factors.[50] At this point, the narrowed field of bidders is asked to participate in a second round of bidding.[51] This is usually the point at which the target's management will hold presenta-

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43 WASSERSTEIN, *supra* note [32], at 746.

44 *Id.* at 746; *see also* Robert G. Hansen, *Auctions of Companies*, 39 Econ. Inquiry 30, 30 (2001) (stating that potential bidder list likely includes "competitors, suppliers, customers, and acquisition oriented conglomerates or leveraged buyout houses").

45 WASSERSTEIN, *supra* note [32], at 746.

46 Bulow & Klemperer, *supra* note [34], at [2]. As prominent investment banker, Bruce Wasserstein, explained, "[t]he auction format naturally creates tension-especially the blind auction in which bidders are not told how many other parties they are competing against. . . . If the auctioneer is able and the integrity of the process is maintained, *even a single bidder* can be induced to enter a 'full' bid." WASSERSTEIN, *supra* note [32], at 748 (emphasis added).

47 Bulow & Klemperer, *supra* note [34], at [4] ("[C]ontrary to our usual instinct that auctions are profitable because they are efficient, *it is precisely the inefficiency of the auction – that entry into it is relatively ill-informed and therefore leads to a more random outcome – that makes it more profitable for the seller.*") (emphasis in original).

48 WASSERSTEIN, *supra* note [32], at 746.

49 Hansen, *supra* note [39], at 31.

50 WASSERSTEIN, *supra* note [32], at 747.

51 WASSERSTEIN, *supra* note [32], at 747.

tions for the bidders, the bidders will receive access to either an online or physical data room to perform due diligence, and plant or site visits will occur.[52] In some cases bidders will be expected to complete due diligence review before final bids are submitted.[53] Thus, the final bids will not be subject to satisfactory completion of due diligence.[54] In addition, the target will send the final bidders a sample purchase agreement that the final bidders will mark-up and return with their offers on the final bid date.[55]

The auction winner is chosen based in large part on the offer price but other factors, including the purchase agreement mark-up, can play a significant role.[56] For example, financing, antitrust issues, closing certainty, and reverse termination fees are just some of the factors that targets may consider in choosing an auction winner.[57] Generally, these auctions are "sealed-bid" auctions, meaning that the bidders do not know the terms of the other bidders' bids and the final bids remain final.[58] However, some auctions are "dripping wax" auctions in which the purportedly final bids are not actually final.[59] In such an auction, the "seller goes back to the few highest bidders, with the high bid used as leverage over the others in an attempt to force a raise. If successful, the new prices can be used against the former high bidder."[60]

As Wasserstein has noted the success of an auction depends in large part on how the auction is run with an emphasis on the selective release of information during the auction pro-

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[52] WASSERSTEIN, *supra* note [32], at 747; Hansen, *supra* note [39], at 31.
[53] WASSERSTEIN, *supra* note [32], at 747.
[54] *See* WASSERSTEIN, *supra* note [32], at 747 (noting that in certain instances bid winner is announced on final bid date). **[check]**
[55] WASSERSTEIN, *supra* note [32], at 747. [need support for mark-up]
[56] *See* WASSERSTEIN, *supra* note [32], at 747 (stating "[p]rice often is the determining factor in an auction" and differentiating between bidders who have submitted "unfavorable contract" versus bidders who have submitted "'clean'" contract).
[57] *See In re* Topps*, supra* note [6] at 72 (listing such elements as reasons to deny Upper Deck continued friendly negotiations); *see also* WASSERSTEIN, *supra* note [32], at 747 ("[O]ne bidder may offer a high price, an unfavorable contract, and no concrete details regarding financing. Another bidder might be willing to pay less, but offer a 'clean' contract and quick closure.").
[58] WASSERSTEIN, *supra* note [32], at 747. [other support]
[59] WASSERSTEIN, *supra* note [32], at 747.
[60] WASSERSTEIN, *supra* note [32], at 747.

cess.[61] Although the information provided to bidders in the offering memorandum and through due diligence "is extensive, it is not complete."[62] Information asymmetries will be explored more fully in Part VI.

Although public auctions are thought to be the best way to maximize stockholder value, there are situations in which a public auction is not desirable as boards may view public auctions as placing the company at a competitive disadvantage.[63] For example, if a company conducts a public auction, the company risks losing employees, customers and suppliers.[64] In addition, the company also runs the risk of being viewed by the market for corporate control as "damaged goods" if the company does not receive any indications of interest or if the board determines that the offers it receives are inadequate.[65] Thus, in the event of a failed auction, it may take some time for a company to successfully sell itself.[66] Furthermore, although potential bidders are required to execute confidentiality agreements before being provided with a confidential offering memorandum or commencing due diligence, companies also risk proprietary or sensitive information being disseminated to the public generally, and, in particular, to competitors.[67] In addition, in some cases, the target may have already been approached by a potential purchaser whose bid may be lost if the

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[61] *See* WASSERSTEIN, *supra* note [32], at 748 ("If the process is managed correctly, bidders will be pulled along by the desire for more data.").

[62] Hansen, *supra* note [39], at 32. As Professor Hansen states, "Throughout the auction process, potential buyers may ask for information that the selling company will view as too confidential to reveal." *Id.*

[63] The Delaware Court of Chancery also recognizes the potential risks involved with a public auction. *See In re* MONY Group, Inc. S'holders Litig., 852 A.2d 9, 21 (Del. Ch. 2004) (recognizing benefits to single bidder approaches).

[64] *See* Peters et al., *supra* note [--] (listing reasons boards choose not to conduct public bidding processes).

[65] *See* Heath Price Tarbet, *Merger Breakup Fees: A Critical Challenge to Anglo-American Corporate Law*, 34 LAW & POL'Y INT'L BUS. 627, 633-34 (2003) (describing possibility that customers, suppliers and potential acquirers may view target as damaged goods upon failure of transaction).

[66] *See* Thomas W. Van Dyke, Chapter 6: *Embarking on the Sale Process*, excerpted from A Practical Guide for the Business Lawyer, 2005, at 804 (detailing disadvantages of auctions, including length of time to sell company after failed auction).

[67] *See also Topps*, Nos. 2998-VCS, 2786-VCS, 2007 WL 1732586, at *2 (noting target's "legitimate proprietary concerns" about turning over information to competitor).

target board were to choose to engage in a full-blown auction.[68] Hence a selling corporation may choose instead to engage in an informal auction process or to negotiate exclusively with one bidder.

2. Pre-signing Market Canvass

Another alternative available to target companies is the pre-signing market canvass, or the informal auction. This is really a variation on the full-blown auction process. In this type of sale process, the target or its financial advisor contacts a number of potential bidders to gauge their interest in the target.[69] However, the bidding process (if one does exist) is in "a less structured setting than that of a formal auction."[70]

The pre-signing market canvass may help target companies to avoid the previously discussed costs involved in a "busted" auction as well as the costs involved in running a full auction. Moreover, a pre-signing market canvass may take place after a previously not-for-sale target company has been approached by bidder or in situations, as discussed in the next section, where the target has negotiated initially with only one bidder.

3. Negotiated Acquisitions and Post-Signing Sales Activities

The third, and final form, of sale type is the negotiated acquisition or sequential procedure. In this type of sale process the target negotiates exclusively with one bidder initially.[71] If the initial bidder is willing to pay a high price, then the deal will sign without the target contacting other bidders.[72] Moreover, in some scenarios, a bidder may condition its bid on the

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68 *See, e.g.*, *id.* at *4 (stating buyer's bid contingent on target not conducting public auction); *Lear*, C.A. No. 2728-VCS, 2007 WL 1732588, at *9 (same).
69 Audra L. Boone & J. Harold Mulherin, *How Are Firms Sold?*, 62 J. OF FINANCE [847-75], 8 (2007).
70 *Id.* at [8].
71 Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1400 (2006).
72 *Id.* at 1400.

target not contacting any other bidders or otherwise performing a market canvass pre-signing.

No matter if the target performs an auction or negotiates with only one bidder, the resulting definitive agreement will be publicly announced within a day or two of execution.[73] In addition, the resulting merger agreement will likely contain a no shop provision paired with a fiduciary out.[74] However, in the case of negotiations with only one bidder, a great emphasis may be placed on the no shop and its related fiduciary out.[75] The no shop provision prevents the target company from soliciting offers between signing and closing.[76] However, the fiduciary out allows a target company's board of directors to negotiate with a third party who makes an unsolicited offer if the third party's offer is a superior one or if it is reasonably likely to become a Superior Offer, as that term is defined in the merger agreement.[77] In addition, the fiduciary out allows the target company to terminate the existing agreement in favor a third party offer if the board determines it would be a violation of its fiduciary duties not to do so.[78] Recently, parties have also begun to use go-shop provisions in some cases.[79] Unlike a no shop provision, go-shop provisions allow a target company to actively solicit third party offers post-signing for a limited period of time.[80] The Delaware courts have upheld more exclusive reliance on no shops paired with fiduciary outs as well as go-shop provisions as a way of satisfying a board's fiduciary duties.[81]

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73 Audra Boone & L. Harold Mulherin, *Do Termination Provisions Truncate the Takeover Bidding Process?*, 20 REV. FIN. STUD. 461, 475 (2007).

74 **[insert support]**

75 *See* Christina M. Sautter, *Shopping During Extended Store Hours: From No Shops to Go-Shops – The Development, Effectiveness, and Implications of Go-Shop Provisions in Change of Control Transactions*, 73 BROOK. L. REV. 525, 541 (2008) (hereinafter, "*Go-Shops*") (discussing use of no shop paired with fiduciary out, or post-signing market check, in lieu of auction or market canvass).

76 Christina M. Sautter, *Rethinking Contractual Limits on Fiduciary Duties*, 38 FLA. ST. U. L. REV. 55, 72-73 (2010).

77 *Id.* at 73.

78 *Id.*

79 *See* Sautter, *Go-Shops*, *supra* note [75], at 554-55 (discussing use of go-shops).

80 *Id.* at 557.

81 **[insert support]**

As is evident from the foregoing discussion, target companies that choose either a full-blown auction process or a more limited pre-signing sales process are invariably presented with the question as to what procedures should be followed to ensure a fair sale process and one that results in the maximization of stockholder value. Along these lines target companies must also contend with the possibility of overbidding by losing bidders after the sale process has been completed and an agreement has been entered into with the winning bidder. When they are presented with such a question, the overwhelming majority of target companies choose to execute a confidentiality agreement that includes a standstill provision.[82]

B. Importance of Confidentiality Agreements

Prior to gaining access to nonpublic information during the due diligence period, most bidders must execute a confidentiality agreement. The confidentiality agreement embodies two conflicting interests. Namely, the seller wants to facilitate the bidder's ability to make a "full bid," but the seller also wants to protect itself from the possible repercussions of disclosure of key business information.[83] Certain disclosures, such as a company's customers, suppliers, or future market plans, can be detrimental to a business if they are not protected by such an agreement.[84] Further, it is important to find the balance between the requirement of "due diligence" in corporate law and the prohibition against violating antitrust law where one cannot use unfair methods of competition and agreements in restraint.[85] The need for this type of agreement often arises before the letter of intent is finalized and clearly before any sort

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[82] In fact, Vice Chancellor Strine has suggested that a corporation running a bidding process may even be "mandated" to adopt procedures that ensure the confidentiality of information as well as procedures that result in an "orderly auction" and allow for the target to extract concessions from bidders. *In re* Topps Company Shareholders Litigation, 926 A.2d 58, [pinpt] (Del. Ch. 2007). However, former Chancellor, now Professor William T. Allen recently asked whether participation in a market canvass or full auction, should be "conditioned on willingness to sign a [confidentiality agreement], standstill or bid procedures letter?" Allen, *supra* note [7], at 69.

[83] KLING & NUGENT, *supra* note [4], at § 9.01.

[84] *Id.* at § 9.03.

[85] *Id.*

of explicit acquisition agreement comes into existence.[86] Thus, confidentiality agreements are "standard" business practice in M&A transactions.[87]

Although the exact terms of confidentiality agreements vary from deal to deal, these agreements require that the bidder maintain the confidence of information they are provided during diligence.[88] In other words, these agreements dictate the bidder's use of confidential and proprietary information concerning the target, and they allow the target to be protected while allowing the target to access information that is not publicly available in order to satisfy this "due diligence" requirement.[89]

Confidentiality agreements, and also standstill agreements, are often included in letters of intent or are created as ancillary agreements to the letter of intent.[90] Letters of intent explicitly state the intent of the parties as well as the parties understanding of the terms of the transaction with the purpose of providing "a framework for further negotiation toward a definitive agreement."[91] Further, though letters of intent are often negotiated in this context, confidentiality agreements are still often executed to ensure this specific protection.[92] This type of agreement is primarily of interest to the seller, or disclosing party, since they want to protect themselves from misuse of information that details key aspects of their business; therefore, the seller should, and often does, insist on this type of agreement in addition to the letter of intent.[93] Though the terms in confidentiality agreements vary, each agreement contains some basic elements:

> (i) a broad definition of information constituting "confidential information," (ii) the permitted use and users of confidential information, (iii) certain permitted disclosures and exceptions, and (iv) an

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86 KLING & NUGENT, *supra* note [4].
87 David Marcus, *The case of Travis Laster*, DAILY DEAL, March 25, 2011.
88 Although the exact terms of the confidentiality agreement may vary from deal to deal, confidentiality agreements have been described as "standardized." *Id.*
89 Rosenblatt, *supra* note [8], at 111.
90 Hoehn, *supra* note 21, at 76.
91 Rosenblatt, *supra* note [8], at 97.
92 *Id* at 111.
93 Hoehn, *supra* note [21], at 76-77.

> acknowledgment of the insufficiency of money damages and the disclosing parties right to injunctive relief.[94]

Further, many confidentiality agreements will also not allow the bidder to make public the fact that the parties are in discussions or that they have been given access to the confidential information.[95] Further, the buyer in this situation may provide that it will keep a copy of this information for its records.[96] Due to this, a continuing confidentiality agreement may occur. Sellers generally prefer that that the duty to keep information confidential last indefinitely because it is hard to predict when the seller could be harmed by such disclosure.[97] Buyers, obviously, generally resist this and prefer a specific time period be enunciated in the agreement for when this obligation expires.[98] For all these reasons, confidentiality agreements are often binding and last past the life of the letter of intent.[99]

Confidentiality agreements, as noted by the United States Court of Appeals for the Second Circuit, are key to the investment banking industry and business community; if they could not be used and relied upon, "it could substantially disrupt the present process of negotiating and consummating business acquisitions and mergers."[100] Upon the termination of negotiations, some agreements require that the confidential information either be returned or destroyed.[101] Moreover, many confidentiality agreements contain standstills. For many target companies, a bidder's willingness to agree to a standstill in exchange for the provision of confidential, nonpublic information shows the target company that the bidder is a serious one.[102] In fact, standstills have been described by a former head

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94 Rosenblatt, *supra* note [8], at 111.
95 KLING & NUGENT, *supra* note [4], at § 9.02.
96 Hoehn, *supra* note 21, at 77.
97 KLING & NUGENT, *supra* note [4] at § 9.04.
98 *Id.*
99 Hoehn, *supra* note [21], at 80.
100 Gen. Portland, Inc. v. LaFarge Coppee S.A., CA-3-81-1060-D, 1981 WL 1408 [pinpt] (N.D. Tex. Aug. 28, 1981).
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of Global M&A at Lehman Brothers as "the cost of entry" into negotiations.[103]

However, it is possible for a standstill provision to be removed from the confidentiality agreement and the confidentiality agreement still stand and provide protection. This is because the allowed use of the information given subsequent to the confidentiality agreement will not allow for the information to be used to make a hostile acquisition of the target company.[104] Therefore, by executing a confidentiality agreement alone a bidder is basically agreeing to only acquire the target through friendly terms.[105] As stated above, this does not limit the use of the standstill agreement because it serves an evidentiary function that the confidentiality agreement does not; namely, showing a violation of a standstill agreement is easier than showing a violation of a confidentiality agreement.[106]

IV. STANDSTILLS IN ACTION

A limited number of cases have examined the validity of standstills in the sale process.[107] Courts that take up the issue tend to address standstills as a part of the larger sale process so that the validity or the alleged improper use of a standstill is usually but one challenge the court is addressing. Thus, few cases have addressed standstills at length. However, courts have upheld a target's decision to have potential bidders execute a standstill condition as a precondition to obtaining access to confidential information (even when the deal results in a change of control and heightened scrutiny is applicable).[108]

A. Target Board's Use of Standstills

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[103] Subramanian, *supra* note [4], at 660.
[104] Rosenblatt, *supra* note [8], at 117.
[105] *See* KLING & NUGENT, *supra* note [4], at § 9.05 ("The message is clear that by signing a confidentiality agreement, even without a standstill provision, a Buyer may be foregoing its opportunity to proceed to acquire the Seller on any basis other than a friendly negotiated one in which the Seller will agree to the Buyer's disclosure of pertinent material information concerning the Seller in the Buyer's possession.").
[106] Rosenblatt, *supra* note [8], at 117. *See also infra* Part II.
[107] City Capital Assocs. L.P. v. Interco Inc., 551 A.2d 787, n.21 (Del. Ch. 1988) (recognizing that despite important role that standstills play in M&A process, standstills "rarely get litigated").
[108] Rosenblatt, *supra* note [8], at 121.

The Delaware Court of Chancery has most often examined standstills to determine whether the seller was using the provision for an inequitable purpose such as favoring one bidder over another or favoring one bidder over shareholders' interests.[109] The court recently made clear, in *In re Topps Shareholders Litigation*[110] that a target company may not refuse to waive a standstill to "favor one bidder over another."[111]

In *Topps*, the target company, Topps Company, Inc., entered into a merger agreement with a Michael Eisner-affiliated private equity firm.[112] The merger agreement contained a go-shop provision that allowed Topps to actively shop the company for 40 days following the execution of the merger agreement.[113] During the go-shop period, the Upper Deck Company, a Topps' prime competitor, expressed interest in Topps and "sought access to confidential information."[114] Before providing Upper Deck with access to its confidential information, Topps required Upper Deck to execute a confidentiality agreement containing a standstill provision.[115] In particular, the standstill provision prevented Upper Deck from making "any public disclosure[s] with respect to a proposed transaction between Upper Deck and Topps," from disclosing that it was obtaining confidential information, and from disclosing that it had executed a standstill.[116] Moreover, under the standstill, "Upper Deck agreed for a period of two years not to acquire or offer to acquire any of Topps's common stock by way of purchase in the open market, tender offer, or otherwise without Topps's consent, or to solicit proxies or seek to control Topps in any manner."[117]

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109 *See, e.g.*, J.P. Stevens & Co., Inc. Shareholders Litigation, 542 A.2d 770, 784 (Del. Ch. 1988) (considering whether target company favored existing bidder to stockholders' detriment).
110 926 A.2d 58 (Del. Ch. 2007).
111 *Id.* at 91.
112 *Id.* at 62, 66.
113 *Id.* at 61. For an analysis of the effectiveness of go-shop provisions in the sales process, see Sautter, *Go-Shops*, *supra* note [70]; Guhan Subramanian, *Go-Shops v. No-Shops in Private Equity Deals: Evidence and Implications*, 63 BUS. LAW. 729 (2008).
114 In re *Topps*, 926 A.2d at 62.
115 *Id.* at 66.
116 *Id.* at 66.
117 *Id.* at 66.

Upper Deck submitted formal offers for Topps both during and after the go-shop period.[118] Although each of Upper Deck's bids were higher than Eisner's bids, Topps never negotiated with Upper Deck regarding antitrust issues, price, or the reverse break-up fee offered by Upper Deck.[119] In fact, Topps released proxy statements containing material misstatements and omissions regarding Upper Deck's offers which "intentionally cast[ed] a negative light on Upper Deck's sincerity as a bidder."[120] Upper Deck requested that Topps waive the standstill so that Upper Deck could "make a tender offer on the terms it offered to Topps and . . . communicate with Topps's stockholders" but the Topps board of directors refused Upper Deck's request.[121]

Upper Deck, along with a group of Topps's stockholders, sought a preliminary injunction seeking to enjoin the stockholder vote on the merger, to mandate that Topps correct material misstatements in the proxy statement, and to order Topps to waive the standstill provision so that Upper Deck could communicate with stockholders or make a tender offer.[122] Vice Chancellor Strine granted the preliminary injunction, finding that Topps was most likely "misusing the [s]tandstill" and that the "Topps board [was not] using the [s]tandstill to extract reasonable concessions from Upper Deck in order to unlock higher value."[123] Instead, Strine found that Topps' refusal to waive the standstill prevented Topps stockholders from hearing Upper Deck's version of events and from considering and accepting a higher offer.[124] In addition, Upper Deck was unable to seek antitrust clearance because it could not commence a tender offer nor have an executed merger agreement.[125] Thus, Vice Chancellor Strine found that the Topps

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118 *Id.* at 88, 90.
119 *Id.* at 90.
120 *Id.* at 77-79 (describing Topps's proxy statements).
121 *Id.* at 91-92.
122 *Id.* at 84.
123 *Id.* at 91.
124 *Id.* at 92.
125 *Id.* Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, before a company may file for antitrust clearance a definitive acquisition agreement or a letter of intent must have been executed. *See* KLING & NUGENT, § 5.04[1] (noting that completion of definitive agreement or letter of intent is required for Hart-Scott-Rodino filing). This is required if either the acquirer or target are engaged in U.S. commerce, or in activities effecting

board was "not using the [s]tandstill [a]greement for any apparent legitimate purpose."[126]

In the wake of *Topps*, then practitioner, now Vice Chancellor, Travis Laster, wrote the following:

> The questions created by aggressive standstill agreements and subsequent waivers have been part of the Delaware counseling mix for some time. Without any meaningful decisions on the issue, however, concerns regarding potential fiduciary duty issues were often given short-shrift. *Topps* confirms that the use of standstill agreements and reliance on them to foreclose subsequent bids are areas that must be approached with particular care.[127]

As Vice Chancellor Laster's statement implies, a board of directors' decision to waive or to refuse to waive an executed standstill so that a party can make a topping bid is a delicate

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U.S. commerce, and if the proposed acquisition or parties meet certain size tests. Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (2006). This premerger notification filing may be required under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (Hart-Scott-Rodino) with the Federal Trade Commission (FTC) or the Antitrust Division of the Department of Justice (DOJ). *See id. See also* MARTIN LIPTON & ERICA H. STEINBERGER, TAKEOVERS AND FREEZEOUTS §§ 7.02[1][c], [d] (2009) (detailing Hart-Scott-Rodino size and commerce tests); Robert T. Miller, *The Economics of Deal Risk: Allocating Risk Though MAC Clauses in Business Combination Agreements*, 50 WM. & MARY L. REV. 2007, 2020-21 (2009) (summarizing specifications of Hart-Scott-Rodino filings). The thresholds for the size tests change each fiscal year depending on the gross national product for that fiscal year. *See* Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (2006). For 2011, the size of person threshold is $131.9 million (in assets or annual sales) for one party and $13.2 million for another party to the transaction. [cite] However, if the transaction is worth at least $263.8 million, then the size of person threshold need not be met. [cite] In order for the size of transaction threshold to be met, the transaction must result in the buyer accumulating at least $66.0 million worth of stock, non-corporate interests, and/or assets of the seller. Jacqueline R. Java and Marvin R. Lange, *HSR Thresholds Increase for 2011* (January 25, 2011) http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/9e994535-8d3f-4e1a-9338-8eb306bad70b/HSR_Thresholds_Increase_for_2011.cfm. *See also* Revised Jurisdictional Thresholds for Section 7a of The Clayton Act, 76 Fed. Reg. 4349-03 (Jan. 25, 2011).

126 In re *Topps*, 926 A.2d at 92.

127 Travis Laster, *Must Read Decision: VC Strine Enjoins Merger Vote Topps Case* (June 18, 2007) http://www.deallawyers.com/blog/archives/000779.html

subject. A particularly sensitive question with respect to standstills is when a board of directors may legitimately agree *not* to waive the standstill provision. In *Topps*, Vice Chancellor Strine alluded to such a situation by imagining a hypothetical final round auction with three bidders.[128] In such a scenario, Strine suggested that the highest bidder may legitimately be promised certain deal protection provisions including a promise not to waive the standstill agreement.[129] However, because this was only dicta, it remains unclear how extensive such an auction process must be before such a promise may be made.

B. Topping Bids in Violation of a Standstill

The Delaware courts have never addressed a target board's actions in the wake of a topping bid that violates an existing standstill. But recently Canadian courts have been presented with just such an issue.[130] Healthcare Property Investors, Inc. (HCP) and Ventas Inc.'s 2007 fight for Sunrise Senior Living REIT, a Canadian real estate investment trust, highlights the impact of standstill violations on a company's sale price. Both HCP and Ventas competed in an auction for the assets of Sunrise.[131] As a part of that auction, seven parties, including HCP and Ventas, executed a confidentiality agreement containing a standstill.[132] HCP's standstill prevented it from making an offer to purchase the stock or assets of Sunrise for eighteen months without Sunrise's prior written consent.[133] HCP did not make a formal bid for Sunrise and Ventas won the auction, agreeing to pay 15 Canadian dollars per share, pursuant to a January 2007 agreement.[134] The $15 figure represented a 40% premium over Sunrise's current trading price at the time.[135]

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[128] *Id.* at n.28.
[129] *Id.*
[130] *See* Ventas Inc. v. Sunrise Senior Living Real Estate Inv. Trust, 2007 CarswellOnt 1704, 29 B.L.R. (4th) 292 (Ont. S.C.J. 2007), *aff'd* 2007 CarswellOnt 1705, B.L.R. 29 (4th) 312 (Ont. C.A. 2007) (addressing overbid made in violation of previously executed standstill).
[131] *Ventas*, B.L.R. 29 (4th) at 2.
[132] *Id.* at 2, 11.
[133] *Id.* at 5.
[134] *Id.* at 9, 10, 11.
[135] *Id.* at 11.

After the Ventas-Sunrise agreement had been executed, HCP offered 18 Canadian dollars per share for Sunrise in violation of the standstill agreement.[136] HCP's overbid caused Sunrise's stock price to increase above 18 Canadian dollars per share.[137] As a result, on April 11, 2007, Ventas and Sunrise amended their merger agreement to reflect a price of 16.50 Canadian dollars which was approximately $100 million more than their original agreement.[138] The Ontario Superior Court declared that Sunrise must enforce the standstill agreement with HCP.[139] Moreover, the court found that HCP's bid was not a *bona fide* one because it had been made in violation of the standstill.[140]

The United States District Court for the Western District of Kentucky ultimately found that HCP had tortiously interfered with the Ventas-Sunrise agreement and a $101 million jury verdict was entered against HCP.[141] Although HCP's violation of the standstill agreement was not outcome determinative for purposes of the tortious inference case, the case demonstrates why winners of auctions favor standstills.[142] At the same, it reveals that there may be deals in which a target's shareholders could obtain additional value in a sale of control.[143] Thus, the case displays the tension that standstills attempt to alleviate – more specifically, the desire of an auction

[136] *Id.* at 17.
[137] Ventas, Inc. v. Health Care Prop. Investors, Inc., 635 F. Supp. 2d 612, 632 (W.D. Ky. 2009).
[138] *Id.* at 618.
[139] *Ventas*, 29 B.L.R. (4th) at 41.
[140] *Id.* at 39.
[141] [cite to article re: trial]
[142] Davis Polk & Wardwell LLP partner, Paul Kingsley has been quoted as saying,

> I have on occasion heard bankers -- not lawyers -- say that standstills need not necessarily be respected because there are no damages to the target company or its shareholders from receiving a higher bid. That may be true, but that ignores, of course, circumstances like these in which the competing bidder -- and auction winner -- ended up having to shell out an extra $100 million plus to get its deal done.

When standstills matter, The Deal Magazine, http://www.thedeal.com/newsweekly/insights/safe-harbor/when-standstills-matter.php (Jan. 8, 2010).
[143] **[find support]**

winner to protect its executed transaction from being "jumped" and the desire of stockholders to obtain the highest price possible in a sale of control.

C. Spring Clauses within Standstill Agreements

Though the *Ventas* case determined that a company cannot violate a standstill in order to make a higher offer,[144] a company may contract for a provision allowing higher offers to be made. *Quebecor Media Inc. v. Osprey Media Income Fund*[145] demonstrates that if a Standstill Provision contains a "spring clause," a bidder may be able to legally present a higher offer even after a first round auction winner has been announced.[146]

Osprey Media Income Fund ("Osprey") began an auction process for the sale of its various assets (newspapers and other publications) in Ontario in March 2007.[147] In response, Torstar, Black Press Ltd. ("Black Press"), Quebecor Media, Inc. ("QMI"), and 32 other potential acquirers signed Confidentiality Agreements containing standstill provisions.[148] These standstill provisions, identical in each Confidentiality Agreement, were preventive measures to ensure that the potential acquirers did not endeavor to secure Osprey assets or securities sans Osprey's written permission.[149] The standstill provisions also contained "spring clauses" that allowed previously bound parties to present an offer to Osprey upon completion of the first round of the auction.[150] Specifically, the standstills expired once a bidder made a public announcement of an offer to acquire 20% or more of Osprey's outstanding securities or almost all of Osprey's assets.[151]

Around May 31, 2007, QMI and Torstar presented offers to Osprey, of which, Osprey found the offer of QMI (7.25 Canadian dollars per unit) more favorable and therefore accepted

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144 *Ventas*, 29 B.L.R. (4th) at 39.
145 2007 CarswellOnt 6538 (Ont. S.C.J. 2007).
146 *See* Quebecor Media Inc. v. Osprey Media Income Fund, 2007 CarswellOnt 6538 (Ont. S.C.J. 2007) (demonstrating the use of spring clauses).
147 *Id.* at 1.
148 *Id.* at 8.
149 *Id.* at 8, 9.
150 *Id.* at 15.
151 *Id.* at 9.

it.[152] At this point, Black Press's Standstill clause within its Confidentiality Agreement expired.[153] Subsequently, on June 22, 2007, Black Press made an offer to Osprey at 8.25 Canadian dollars per unit.[154]

QMI contended that the Black Press offer was not a good faith *bona fide* unsolicited acquisition proposal under the terms of the prevailing Support Agreement between Osprey and QMI.[155] This Support Agreement was signed May 31, 2007 and required Osprey to obtain a Standstill Agreement from any third party making an unsolicited offer conditional on acquiring inside information.[156] The standstill would prohibit the maker of any unsolicited superior proposal "from having any communications or understandings with any other party about Osprey's assets or securities."[157] QMI claimed that Osprey's acceptance of Black Press's offer constituted a breach of the Support Agreement due to the failure of the Osprey Board "to duly inquire into the purpose of the Black Press offer and the committed relationship between Black Press and Torstar."[158]

The relationship between Black Press and Torstar is as follows: Black Press, a Victoria-based newspaper publisher, is owned 80.6% by the David Black family and 19.4% by the Torstar subsidiary Metroland Media Group Ltd. ("Metroland").[159] Additionally, the Black Press Board of Directors has 10 seats, 4 of which are held by Torstar and Metroland.[160] Furthermore, Black Press and Torstar have a shareholders' agreement prohibiting each from competing with the other in certain areas of Canada.[161] In order for Black Press to acquire Osprey, it had to obtain the consent of Torstar to waive said prohibition for that sole purpose.[162] Torstar agreed to this on June 22, 2007.[163] However, there was an unofficial agreement

152 *Id.* at 11, 12.
153 *Id.* at 14.
154 *Id.* at 2, 22.
155 *Id.* at 18.
156 *Id.* at 12, 16.
157 *Id.* at 16.
158 *Id.* at 19.
159 *Id.* at 6.
160 *Id.* at 6.
161 *Id.* at 7.
162 *Id.* at 7.
163 *Id.* at 7.

between Torstar and Black Press that, should Black Press succeed in its attempted acquisition of Osprey, it would sell some of the assets to Torstar.[164] The entities never specified the specifics of this agreement.[165]

Due to its June 15 proposal to Osprey, Black Press signed another Standstill Agreement on or about June 20, 2007 (though effective June 17, 2007, the date Black Press received confidential information).[166] This was the Standstill Agreement that QMI declared Black Press violated by having a "deal" with Torstar.[167] QMI posited that the Black Press/Torstar "agreement" precluded the Black Press offer from being *bona fide*, and, therefore, it could not be considered to be superior under the terms of the Support Agreement.[168] However, all discussion of a possible sale by Black Press to Torstar of Osprey assets took place before Black Press's June 15 proposal to Osprey.[169]

The Court found that Black Press had not breached its Standstill Agreement because it found the "deal" between Black Press and Torstar to be simply "discussions…not…amount[ing] to any legally binding agreement on the part of either party."[170] Furthermore, the Court held that the discussions occurred during a time in which neither party was bound by a Standstill Agreement.[171]

The Court further found that Osprey did not breach "its obligation to establish the bona fides of the Black proposal."[172] The Osprey Board recognized that Black Press presented a superior offer and, even if there had been a violation of the standstill, "the Board could operate in a bona fide determination."[173]

In short, QMI claimed that the supposed "deal" between Black Press and Torstar violated the provision of the Osprey/QMI Support Agreement stating that third parties submitting an unsolicited good faith offer, such as Black Press, must sign a Standstill Agreement containing a clause prohibit-

164 *Id.* at 26.
165 *Id.* at 27, 28.
166 *Id.* at 22, 34.
167 *Id.* at 22.
168 *Id.* at 23.
169 *Id.* at 26, 36.
170 *Id.* at 43, 45.
171 *Id.* at 47.
172 *Id.* at 43.
173 *Id.* at 56.

ing the third party "from having any communications or understandings with any other party about Osprey's assets or securities."[174] However, the Black Press/Torstar discussions took place prior to Black Press's signing of the June 17 Standstill Agreement and after Black Press had been "sprung" from the original Standstill Agreement.[175] Thus, by contracting for a spring clause, Black Press was able to present a higher offer to Osprey after QMI announced its offer, and furthermore, its communications with Torstar, which would be prohibited while under a standstill, were permitted since Torstar and Black Press had each been "sprung" from the original Standstill Agreements.

D. Standstills as Stand Alone Provisions

Canadian courts have also examined the interplay between Standstill Agreements and release of confidential information.

Aurizon Mines Ltd. ("Aurizon") and Northgate Minerals Corp. ("Northgate") are both Canadian mining exploration companies.[176] The two companies contemplated a possible business combination, and in October 2005, they signed reciprocal Confidentiality and Standstill Agreements.[177] The two agreements contemplated that each entity would provide confidential information to the other.[178] However, it is debatable as to whether or not Aurizon actually provided confidential information to Northgate.[179] Additionally, Northgate's Standstill Provision prohibited it from procuring Aurizon voting securities and from engaging in communication with Aurizon shareholders for one year.[180]

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[174] *Id.* at 16.
[175] *See Id.* at 47 (noting that "[t]he discussions and "understandings" such as they are, took place during a time period in which neither Torstar nor Black were subject to any standstill obligation").
[176] *Aurizon Mines Ltd. V. Northgate Minerals Corp.*, 2006 CarswellBC 1651, 19 B.L.R. (4th) 318 at 2 (B.C. S.C. 2006), *aff'd* 2006 CarswellBC 1734, 19 B.L.R. (4th) 171 (B.C. C.A. 2006).
[177] *Id.* at 7, 10.
[178] *Id.* at 10.
[179] *Id.* at 31.
[180] *Id.* at 13.

In an effort to determine the best course of action for Aurizon, it employed its financial advisor, National Bank Financial Inc., to perform a "top down review" of Northgate based only on public information in November of 2005.[181] Upon completion of this evaluation, Aurizon decided to cease discussions of a possible business combination with Northgate as the evaluation revealed such action would not be in Aurizon's best interest.[182] In turn, Northgate informed Aurizon that, because Aurizon had ceased discussions and because no confidential information had been exchanged between the two, Northgate considered the Confidentiality and Standstill Agreements to be expired along with all obligations under them.[183] However, Northgate never sought confirmation from Aurizon to such effect.[184] Thereafter, Northgate acquired Aurizon voting securities and began communications with Aurizon shareholders, and on June 1, 2006, Northgate made an offer for all of Aurizon's outstanding voting securities.[185] Aurizon subsequently filed suit for enforcement of the Standstill Provision.[186]

Though Aurizon posited that the Standstill Agreement was still in effect at the time of Northgate's offer, Northgate declared that both parties understood the Agreements to be at an end in December 2005 when Aurizon ceased discussions of a possible business combination.[187] Northgate further asserted that since no confidential information was ever exchanged between the parties, no reason for the Agreements existed anyway.[188]

However, the Court felt differently. It held that no provision in the Northgate Agreement indicated that an exchange of confidential information must take place before the Standstill Provision came into effect.[189] The Court further found that the Standstill Provision stood alone.[190] As such, the Court is-

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181 *Id.* at 22.
182 *Id.* at 22, 23.
183 *Id.* at 24, 25.
184 *Id.* at 26.
185 *Id.* at 27, 28.
186 *Id.* at 6, 7.
187 *Id.* at 29, 30.
188 *Id.* at 34.
189 *Id.* at 63, 64.
190 *Id.* at 66.

sued an injunction against Northgate from proceeding with its offer until expiration of the Northgate Agreement.[191]

The *Aurizon* case demonstrates that confidential information does not need to be released in order for a Standstill Provision to be effective. The two are not contingent upon one another (though it is possible that a contract could be drawn up in such a way to make them interdependent).

E. Backdoor Standstill Provisions

Perhaps one of the more fascinating cases involving standstills is *Certicom Corp. v. Research In Motion Ltd.*[192] Research in Motion Limited ("RIM"), a globally-recognized designer, manufacturer, and marketer of mobile communications wireless devices was a customer of Certicom Corp., a renowned security company specializing in the cryptography market.[193] In February of 2007, discussions ensued regarding the possibility of RIM acquiring Certicom, and on July 11, 2007, they signed a non-disclosure agreement ("2007 NDA") in order to perform due diligence.[194] Under section 4 of the 2007 NDA, RIM could only use the confidential information received to fulfill the Purpose, which was previously defined as, among other things, "some form of business combination between the Parties."[195] By including a Standstill Agreement within the 2007 NDA, Certicom also precluded RIM from engaging in hostile take-over action for 12 months.[196] Subsequently, in September of 2007, RIM received confidential information from Certicom.[197]

RIM, through a subsidiary, launched a hostile take-over for Certicom Corp. on December 10, 2008.[198] Though the Standstill Provision in the 2007 NDA had expired at this

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191 *Id.* at 83.
192 *Certicom Corp. v. Research In Motion Ltd.*, 2009 CarswellOnt 331, 53 B.L.R. (4th) 286 (Ont. S.C.J. 2009).
193 *Id.* at 8, 9, 10.
194 *Id.* at 11.
195 *Id.* at 13.
196 *Id.* at 15.
197 *Id.* at 18.
198 *Id.* at 2, 7.

point,[199] RIM had used confidential information received under the 2007 NDA when determining to launch its hostile take-over bid.[200] The Court determined that using confidential information obtained pursuant to a Non-disclosure Agreement breached said agreement.[201] According to Robert E. Spatt, the Court's decision essentially said that Confidentiality Agreements can create "backdoor standstill provisions."[202]

Therefore, the Court held that RIM was enjoined from furthering its hostile bid of December 10, 2008 due to its breach of the 2007 NDA.[203] However, RIM could negotiate on friendly terms with Certicom or could even launch another hostile takeover bid provided that they first erected a firewell.[204]

Thus, a Confidentiality Agreement acted as a Standstill Agreement in *Certicom*. This creates additional pressure on contracting parties to state their exact intentions and everything allowed and prohibited pursuant to those intentions.

V. BARGAINING NORMS & STANDSTILLS

[NOTE: Section to be reviewed/expanded]

HCP's overbidding for Sunrise demonstrates that there are certainly bidders who are willing to violate a standstill. But in spite of HCP's and other bidders' recent actions, these violations are few and far between. Wasserstein summarized the view of many sellers in the M&A field when he said, "[t]he willingness to sign a standstill . . . serves as a kind of litmus test, an indication of a bidder's true intentions."[205] Essentially, a potential buyer has a choice between preserving the right to bring a hostile transaction or foregoing that right by signing a standstill.[206] However, this does not answer the ultimate ques-

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199 *Id.* at 15.

200 *Id.* at 2, 7.

201 *Id.* at 7.

202 Spatt, *supra* note 4 at 36.

203 *Certicom*, 53 B.L.R. (4th) at 7.

204 *Id.* at 3, 97.

205 WASSERSTEIN, *supra* note [32], at 689.

206 Subramanian, *supra* note [4], at 662 (describing "tactical decision" buyers must make when asked to execute standstill agreement). The decision confronted by buyers is best summarized by Louis Friedman, the former Global Head of Mergers and Acquisitions at Bear Sterns, as:

> [Y]ou could preserve your flexibility to pursue a hostile deal, in which case you do not move forward with the bilateral discussions because the target is not willing to share confi-

tion of whether the execution of a standstill actually incentivizes bidders to submit their best and final offers during the presigning sale process? Asked another way, does the possibility of contract liability incentivize bidders to submit bids during the sale process rather than after the target company has entered into a definitive acquisition agreement with the winning bidder? Or do other factors contribute to the lack of overbidding?

If auction theory literature is considered, it is possible that standstills do not incentivize auction participants to submit their highest bids. As Professors Povel and Singh indicate, at least in a sequential process, because the bidders have asymmetric information, a "loser's valuation of the target may be higher" than the price the winner is paying.[207] Thus, in a sequential procedure, once the winning bidder's price becomes public the losing bidder may want to overbid the winner's deal or even take their offer directly to stockholders.[208] Obviously, if the losing bidder has executed a standstill that continues to be in force, under the standstill the losing bidder technically will be prevented from overbidding. However, as was the case with HCP, the bidder may still violate the standstill or seek a waiver of the standstill from the target company. Because of the possibility of overbids, other deal protection mechanisms are used that may further discourage a losing bidder from overbidding.[209]

Among the deal protection devices that may play a role in a bidder's decision whether to violate a standstill and "jump"

> dential information with you unless you agree to the standstill. Alternatively, you try to modify the standstill as much as you can, but fundamentally give up the basic ability to launch an unsolicited offer.

Id.

[207] Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1402 (2006).

[208] *See* Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1402, 1414 (2006) (recognizing possibility that loser's valuation may be higher than winner's valuation and that loser could make offer directly to target's stockholders).

[209] *See* Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1402 (2006) (discussing deal protection devices and stating, "[t]hese devices make the target less attractive to rejected bidders, thereby reducing their incentive to top up the winning bid.").

a signed transaction is the existence of a termination fee in the definitive agreement. Although a target incurs the termination fee if the target terminates the agreement in favor of an overbidder, the fee is a transaction cost for the overbidder.[210] Therefore, the possible existence of a termination fee in the future may incentivize a bidder to submit their highest bids during the pre-signing sale process and may disincentivize them from overbidding because the termination fee will make a topping bid more expensive. However, Professor Subramanian concluded,

> if the standstill agreement is the standard quid pro quo for access to confidential information and records, and most acquirers in negotiated acquisitions agree to a standstill as standard business practice, *then takeover defenses are irrelevant in determining the final price* received by target shareholders in most negotiated acquisitions.[211]

Along the same lines, Professors Audra Boone and J. Harold Mulherin have found that termination fees do not hinder takeover competition.[212] Instead, Boone and Mulherin found that the "use of termination provisions is directly related to takeover competition."[213] Still, this conclusion does not resolve the question as to whether standstills incentivize bidders in an auction process to submit their highest bids.

A major motivation in abiding by the terms of a standstill may be bargaining norms that have developed in the M&A arena. As Professor Guhan Subramanian notes in the context of hostile tender offers, a bidder who launches a hostile takeover, suffers certain "reputational costs."[214] This is particularly true for repeat market players such as private equity funds who are in the business of buying and selling companies as well as for financial and legal advisors.[215] Along these lines, bank-

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[210] *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 938 (Del. 2003) ("To the extent that defensive measures are economic and reasonable, they becomes an increased cost to the proponent of any subsequent transaction.").

[211] Subramanian, *supra* note [4], at 662 (emphasis added).

[212] *See generally* Audra L. Boone & J. Harold Mulherin, *Do Termination Provisions Truncate the Takeover Bidding Process?*, 20 REV. FIN. STUD. 461 (2007).

[213] *Id.* at 485.

[214] Subramanian, *supra* note [4].

[215] In the context of a seller's commitment to the auction procedures it has established, Professors Povel and Singh have observed that:

ers and lawyers, alike, recognize that, in the future, parties may be unwilling, or at least hesitant, to engage in negotiations with a bidder who has previously engaged in a hostile takeover.[216] Hence, the continuing use of standstills is a result of the standard bargaining process of M&A transactions and the need for target companies to be assured an orderly bidding process. Even in situations where a losing bidder may have a higher valuation of the target company, in making the decision whether to overbid, the losing bidder must balance possible reputational costs against its desire to purchase the company.

To quote Professors Matthew Cain, Steven Davidoff, and Antonio Macias, the authors of *Broken Promises: Private Equity Bidding Behavior and the Value of Reputation:* "The concept of 'reputation' is abstract, but economists generally refer to reputation as a brand, image, or identity that an individual or firm may develop through repeat interactions with customers or counterparties."[217] Businesses develop reputations because businesses are made up of individuals, and individuals naturally form opinions of others due to their interactions. These opinions of individuals then translate into opinions of each individual's company. As Todd D. Rakoff notes,

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> In practice, reputational considerations may be one reason why sellers seem to be able to commit to their rules. Some sellers are in the market repeatedly, for example, private equity funds that regularly buy or sell firms, and it is well understood how reputation allows agents to commit to actions that hurt them in the short run. Other sellers are not in the market regularly, but they typically rely on the services of financial and legal advisors who provide their services to a large number of firms throughout the year. . . . [O]ne-time sellers may "borrow" an investment bank's reputation and credibility, say, and the fees paid to financial and legal advisors (and the importance of league tables for advisor choice) give investment banks an incentive to build up a strong reputation.

Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1414 (2006).

[216] Subramanian, *supra* note [4].

[217] Matthew D. Cain, Steven M. Davidoff, and Antonio J. Macias, *Broken Promises: Private Equity Bidding Behavior and the Value of Reputation* 3 (May 2011) (hereinafter, "*Broken Promises*") http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1540000.

"[p]eople…contract in a cultural setting,"[218] and as Jeffrey N. Gordon concludes, "the success of a market-oriented system ultimately depends on the flourishing of such values as loyalty and fairness."[219] In essence, these men postulate that the traditional idea of reputation is a significant factor in the modern-day business world. Professor Stewart Macaulay performed a study of extra-contractual relationships within business communities and found that seemingly insignificant communications, such as a short letter or a handshake, carry much weight among businessmen.[220] Thus, reputation has an actual value.

Value of reputation especially comes into play within a specific market/industry – any instance where the same people/entities are dealing with each other regularly.[221] In such groups, the more sophisticated and senior participants often gradually form extralegal rules and norms by which all participants are expected to abide.[222] The newest participants perhaps have the most significant incentive for abiding by the traditional norms in that they desire to be accepted into the market and become a prosperous, repeat player.[223]

Fear of harm to one's reputation can drastically effect how a business chooses to operate. For instance, some merchants may choose to allow actions they are not contractually required to allow, such as "accept[ing] late payment, vary[ing] quantity terms, assum[ing] new obligations, waiv[ing] covenants, and adjust[ing] prices" in order to protect their reputation and already formed relationships with other participants

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218 Todd D. Rakoff, *Social Structure, Legal Structure, and Default Rules: A Comment,* 3 S. CAL. INTERDISC. L.J. 19, 24 (1993).
219 Jeffrey N. Gordon, *Corporations, Markets, and Courts*, 91 COLUM. L. REV. 1931, 1986 (1991).
220 Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOCIOLOGICAL REV. 55, 58 (1963).
221 *See* Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry,* 21 J. OF LEGAL STUDIES 115,140 (1992) (noting that "reputation bonds are generally assumed to be effective only within geographically concentrated, homogeneous groups who deal with each other in repeated transactions over the long run").
222 *See id.* at 115. [Here I analogize to Bernstein's observation that, within the diamond industry, high-level parties "have developed an elaborate, internal set of rules."]
223 *See id.* at 152. [This is a comparison of new participants in any compact market to Bernstein's assessment of non-member diamond dealers who seek admittance to a bourse.]

in their relevant market.[224] Furthermore, they may specifically leave out contract provisions dealing with possible contingencies in an effort to *not* seem particularly litigious or inflexible.[225]

Additionally, reputational concerns prove to be a significant consideration among companies debating the pros and cons of contractual non-performance.[226] In the realm of private equity, it is rational to believe that a firm placing no value on the idea of reputation would have no problem with backing out of a contract that is no longer financially beneficial.[227] Yet, due to concerns of losing trust and having to acquiesce to unfavorable contract terms in the future, private equity firms must weigh the possible gain from defaulting as compared to the loss of their good reputation.[228]

Such is the concern with violating a standstill. A potential hostile bidder must compare the cost benefit of acquiring the desired target by overbidding with the grim possibility of losing a respectable reputation. This cost-benefit analysis is forward-looking. The potential violator must consider whether he wants to be a repeat player in the M&A arena, and, if so, how untrustworthy other participants might consider him after his violation. Will they want to do business with him knowing he may violate any agreement the two of them may make? Thus, reputational costs prove to be a significant influential factor for potential hostile bidders.

VI. AUCTION THEORY & STANDSTILLS

[NOTE: This section is to be further developed and synthesized with the foregoing sections as well as footnoted]

There is a substantial body of literature on auction theory and particularly auction theory in the M&A context. However, little of this literature specifically focuses on deal protection devices and none of the literature specifically addresses

224 Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms,* 144 U. Pa. L. Rev. 1765 at 1787-1788 (1996).
225 *Id.* at 1789.
226 *Broken Promises, supra* note 155 at 3.
227 *Id.* at 5.
228 *Id.* at 7.

the use of standstills in the auction process. Nor does the literature address the issue of whether standstills help to enhance the auction process. This Article attempts to fill this gap.

A. Common Value versus Private Value Sales Processes

A number of academics have found that the type of bidders involved in a sale process impacts the sale process and the ultimate results of the process.[229] For example, when financial buyers are the bidders in an auction, academics tend to define those auctions as common value auctions.[230] A common value auction is an auction in which all of the participants have the same or very similar value for the target.[231] This is the case with financial buyers because they "can exploit the same sources of gains (e.g., cost cutting, financial restructuring)."[232] Strategic, or trade, buyers are often interested in a target company to optimize possible unique synergies between the buyer and the target.[233] Thus, strategic buyers tend to have differing values for a target based on the value that the bidders place on those particular synergies.[234] Therefore, auction processes involving strategic bidders tend to be private value auctions.[235]
In addition, if the target's management has teamed up with a financial buyer to engage in a management-led buyout ("MBO") then the MBO team likely has better information regarding the target's value than the typical financial buyer.[236] In such case, the bidding process would be more similar to the private value auction.

Strategic bidders and buyers engaged in an MBO have asymmetric information. That is, these types of bidders have superior information on the target either due to their status as

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[229] *See, e.g.,* Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, [1] (2006).
[230] Jeremy Bulow, Ming Huang, & Paul Klemperer, *Toeholds and Takeovers*, 107 J. OF POLITICAL ECON. 427, [427] (1999).
[231] J. Russel Denton, Note, *Sacked Deck: Go-Shops and Auction Theory*, 60 STAN. L. REV. 1529, 1535 (2008).
[232] Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1400 (2006).
[233] Povel & Singh, *supra* note [129], at 1400.
[234] Denton, *supra* note [148], at 1535.
[235] Povel & Singh, *supra* note [129], at 1400.
[236] Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1399 (2006).

insiders or due to how they value the company based on particular synergies. In these situations involving asymmetric bidders, Professors Povel and Singh argue that "more biased procedures" should be used in the sale process, including deal protection devices.[237]

Despite this, in the real world of dealmaking, the classification of one type of auction as a pure common value one or a pure private value one is not necessarily accurate. As Professor Subramanian recognized in his book, *Negotiauctions*, "[e]ven with a seemingly pure private-value asset, there is a significant common-value element."[238] Thus, information will not be perfectly symmetric between all buyers because, even if they are all using the same information about the target company, each bidder evaluates that information differently. In addition, each bidder adds its own unique private information to reach a final valuation. In reality, there are no two exactly the same companies who use the same exact valuation techniques.

B. Information in the Sale Process

The unique interpretation of information that each bidder brings to the sales table impacts the question of whether standstills enhance the bidding process. This uniqueness is especially relevant because, as discussed above, standstills are inextricably tied to the provision of information. Numerous auction theorists have explored the role of information in the sales process. Professors Boone and Mulherin have found that information costs between buyers and sellers can "severely limit the apparent benefits of an auction."[239] As a result, a seller's management of the sales process to limit the number and kind of bidders and otherwise manage the process to reduce information costs can "actually create value."[240]

Some have argued, using the Revenue Equivalence Theorem, that even by taking into account asymmetric information

[237] Povel & Singh, *supra* note [129], at 1417.
[238] GUHAN SUBRAMANIAN, NEGOTIAUCTIONS 93 (2010).
[239] Boone & Mulherin, p 28.
[240] Boone & Mulherin, p 28.
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an optimal auction, in theory can be created.[241] This particular theorem states that the auction type does not influence the revenue produced by an auction regardless of the information each bidder has.[242] Under this theorem, "all the "standard" auctions… yield the same expected revenue under the stated conditions, as do many non-standard auctions."[243] However, this theory rests on a number of assumptions, including that buyers are risk neutral; that bidders' private information is independent of competitors private information; and that buyers private values are drawn from a common distribution.[244]

Even if these assumptions were tailored to create an optimal auction[245], many other factors can influence the outcome of an auction.[246] These factors include the entry costs and number of bidders; ability of bidders to collude; and the divisibility of the unit for sale in the auction (or multi-unit auctions). The idea of a multi-unit auction or the divisibility of a business into separate units is generally not examined in auction theory literature. [247] However, this singular focus may be misplaced when using auction literature to interpret M&A transactions because of the large indivisible number of assets that make up a business. Of the literature that does focus on multi-unit auctions, the "main message . . . is that it is very hard to achieve efficient outcomes."[248] Hence, the question becomes how to promote efficient outcomes or in other words how to promote increased bidding during the auction process.

Thus far, the answer has been with the distribution of information to auction participants. Because standstills are entered into in consideration for the receipt of information, standstills likely enhance the bidding process by at least

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243 *Id.* at 10.

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245 *See* Paul Klemperer, *Auction Theory: A Guide to Literature*, [__] J. ECON. SURVEY [__] (1999) (finding generally that optimal auction can be created in some cases regardless of assumptions).

246 *See* Paul Klemperer, *Auction Theory: A Guide to Literature*, [__] J. ECON. SURVEY [__] (1999) (discussing implications of various factors on results of Revenue Equivalence Theorem making creation of efficient optimal auctions difficult).

247 *Id.* at 23 ("Most auction theory . . . restricts attention to the sale of a single indivisible unit.")

248 *Id.* at 27.

providing a floor for the valuation received. As Professors Povel and Singh have found, "While target shareholders may benefit by opportunistically accepting late bids that are submitted after a winner has been declared, this possibility undermines the effectiveness of the sequential selling procedure, thereby harming the shareholders of future takeover targets."[249] In other words, harking back to the discussion in Part VI.A, entering into and abiding by the terms of a standstill help to enhance a bidder's reputation in the M&A community. Moreover, although one company's shareholders may benefit from a topping bid made in violation of a standstill like on the one put forth in HCP, if the HCP court had found that the bid was a *bona fide* one then a signal would have been sent that standstills are provisions without a "bite."

VII. CONCLUSION

For the past three decades, standstills have played a significant role in the multi-million and –billion-dollar playground of friendly M&A transactions. These equivalents of a "school-yard time-out" have become standard features of the sales process of most companies – no matter if the target conducts a full auction involving multiple bidders or conducts a sequential process during which the target negotiates exclusively with one bidder at a time. However, despite their prevalence, a number of questions remain open. Chief among them are whether standstills enhance the bidding process for target companies. Recent cases suggest that despite executing a standstill bidders may not be bidding their highest valuations of the target company. In those cases, losing bidders overbid in violation of the standstill. Thus, the question becomes why more losing bidders do not violate the standstill and bid for the target. This is likely a result of bargaining norms that have developed in the M&A market as well as fear of having a poor reputation in the M&A market. Moreover, because standstills are inextricably tied to the provision of information to potential bidders, standstills enhance the sales process by at least providing a floor for the value received as a result of the sales process. Thus, the cases of in which a bidder has violated the

249 Paul Povel & Rajdeep Singh, Takeover Contests with Asymmetric Bidders, 19 REV. FIN. STUD. 1399, 1425-26 (2006).

terms of a standstill to submit a topping bid are simply outliers and not a signal that standstills do not enhance the bidding process.