2016

Fleecing the Family Jewels

Christina M. Sautter
Louisiana State University Law Center, christina.sautter@law.lsu.edu

TULANE LAW REVIEW

VOL. 90 | FEBRUARY 2016 | NO. 3

Fleecing the Family Jewels

Christina M. Sautter*

Crown jewel lock-up options, a common deal protection device employed during the 1980s' mergers and acquisitions boom, are back. During their popularity in the 1980s, these options took the form of agreements between a target company and a buyer, pursuant to which the target granted the buyer the right to purchase certain valuable assets, or crown jewels, of the target corporate family in the event the merger did not close. After both state and federal courts questioned the validity of these lock-ups in the 1980s, lock-ups lost their luster and dealmakers stopped using them. But as the saying goes, "everything old becomes new again," and crown jewel lock-ups have made a return in recent transactions. This time around, dealmakers have been quick to distinguish the modernized crown jewel lock-ups from their predecessors. Although there has been limited case law addressing the validity of these lock-ups, courts appear more likely to uphold the lock-up if the lock-up can be attributed to a business purpose other than the merger and if the lock-up could be a stand-alone agreement, separate and apart from the merger. This Article argues, however, that today's lock-ups are not significantly different from their predecessors. Practitioners and courts should not lose sight of the 1980s jurisprudence that closely scrutinized the sale process preceding a lock-up as well as the deterrent effects of the lock-up on potential bidders. Failing to consider these factors and not giving these factors proper weight potentially results in companies and their shareholders being fleeced of their corporate family jewels and their value. At the same time, however, dealmakers should not be as quick to shy away from lock-ups as they have been in the past. As the 1980s jurisprudence made clear, lock-ups can be used to enhance shareholder value. In particular, this Article argues that dealmakers may use lock-ups after an extensive sale process to incentivize bidders and extract additional value for shareholders.

* © 2016 Christina M. Sautter. Cynthia Felder Fayard Professor of Law & Byron R. Kantrow Professor of Law, Louisiana State University Paul M. Hebert Law Center.

Thank you to Lee Ann Lockridge, Therese Maynard, and Eric Wilder for their comments. Many thanks to participants at the 2013 National Business Law Scholars Conference, at which an early draft of this Article was presented, and to my research assistants, Mallory McKnight and Anne Kathryn Hunter, for their substantial assistance.

I. INTRODUCTION 546
II. FORCING CROWN JEWELS OUT OF FASHION 551
A. *The "Fashion Police": The Courts' Treatment of Crown Jewel Lock-Ups* 551
1. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.* 551
2. *Mills Acquisition Co. v. Macmillan, Inc.* 553
3. *Hanson Trust PLC v. ML SCM Acquisition Inc.* 554
4. *Cottle v. Storer Communication, Inc.* 556
5. *In re Holly Farms Corp. Shareholders Litigation* 557
B. *Dealmakers' Responses to the Changing Trends* 560
III. BACK IN STYLE: REFURBISHING CROWN JEWEL LOCK-UPS 561
A. *Modern Crown Jewel Lock-Ups* 563
1. Apple-AuthenTec: Demonstrable Business Purpose 564
2. NYSE-ICE: Crown Jewel Lock-ups as Stand-Alone Agreements 569
3. Pacific Rubiales-Petrominerales: A Modern Crown Jewel Lock-Up with Traditional Roots 573
B. *Crown Jewel Lock-Ups and the Financially Distressed Company* 576
IV. MODERN CROWN JEWEL LOCK-UPS: A PASSING FAD, AN ENDURING CLASSIC, OR A FLEECING OF SHAREHOLDER VALUE? 579
A. *The Family Jewels* 581
B. *The Bidding Process: A Fleecing of Shareholder Value?* 584
C. *Can Lock-ups Become an Enduring Classic?* 586
V. CONCLUSION 588

I. INTRODUCTION

In 1981, Prince Charles proposed to Lady Diana Spencer with an oval sapphire and diamond ring.[1] The announcement of the royal engagement made global headlines, and the nontraditional ring choice

1. *Untold Stories Behind Kate's 18-Carat Sapphire*, TODAY, http://www.today.com/id/40217151/ns/today-today_news/t/untold-stories-behind-kates--carat-sapphire/ (last updated Nov. 16, 2010, 12:05 PM).

spawned a vast demand for replicas.[2] Demand for replicas of the ring, however, eventually withered like the royal marriage.[3] Almost three decades later, Prince Charles and Princess Diana's son, Prince William, proposed to Kate Middleton with the same sapphire ring.[4] As was the case in 1981, within minutes of the ring's unveiling, "jewelry stores around the world started getting calls . . . requesting replicas of the ring."[5] The now-iconic sapphire ring is not the only crown jewel from the 1980s that has awoken from its slumber this decade.[6] The crown jewel lock-up, a once-popular 1980s mergers and acquisitions (M&A) device, has reemerged in recent years and is gaining a modern-day following.[7]

A crown jewel lock-up[8] is an agreement between a target company and a buyer that provides the buyer with an option to purchase certain vital and profitable assets, or "crown jewels," of the

---

2. *Id.*

3. *See Kate Middleton's Engagement Ring: 'Everyone Wants To Copy Her,'* HELLO! (Jan. 9, 2014), http://www.hellomagazine.com/brides/2014010916431/kate-middleton-engagement-ring-cost/ (stating that "[w]ith Diana, everyone loved her but there was always a lot of controversy surrounding her marriage and death" and further describing how jewelers did not carry replicas of the ring until Kate Middleton started wearing it); Peter Victor & Colin Brown, *Diana Accepts Charles's Divorce Terms*, INDEPENDENT (Feb. 28, 1996), http://www.independent.co.uk/news/diana-accepts-charless-divorce-terms-1321560.html (detailing Prince Charles and Princess Diana's divorce).

4. *Untold Stories Behind Kate's 18-Carat Sapphire*, *supra* note 1.

5. *Id.*; *see also* Lauren Milligan, *The Kate Effect*, BRITISH VOGUE (July 22, 2011), http://www.vogue.co.uk/news/2011/07/22/kate-middleton-fashion-style--shopping-influence (describing the increase in demand for diamond and sapphire rings following the royal engagement).

6. The term "crown jewel" is used broadly here, because the sapphire ring is not technically a Crown Jewel of the United Kingdom; the Crown Jewels are those "ceremonial and symbolic objects associated with the coronations of English Kings and Queens." *The Crown Jewels*, OFFICIAL WEBSITE BRITISH MONARCHY, http://www.royal.gov.uk/the%20royal%20collection%20and%20other%20collections/thecrownjewels/overview.aspx (last visited Jan. 2, 2016). The Crown Jewels of the United Kingdom are kept at the Tower of London and "include the crowns of Sovereigns, Consorts and Princes of Wales, both past and present, scepters, orbs, rings, swords, spurs, bracelets and robes, all of which have a specific part to play in the ritual of the English coronation service." *Id.*

7. *See* Daniel E. Wolf, David B. Feirstein & Joshua M. Zachariah, *Crown Jewels—Restoring the Luster to Creative Deal Lock-Ups?*, KIRKLAND M&A UPDATE 1 (Feb. 14, 2013), http://www.kirkland.com/Files/MA_Update/021413.pdf; Ronald Barusch, *Dealpolitik: Three Trends for 2013 in the Corporate and Deal World*, WALL STREET J. DEAL J. (Dec. 27, 2012, 3:47 PM), http://blogs.wsj.com/deals/2012/12/27/dealpolitik-three-trends-for-2013-in-the-corporate-and-deal-world/.

8. The term "crown jewel lock-up" will be referred to as a "lock-up option," a "lock-up," or as an "asset lock-up" throughout this Article. Although the term "lock-up" can be used in the M&A context to refer to other deal protection devices, the term "lock-up" refers only to crown jewel lock-ups in this Article.

target.[9] The option to purchase is at a preset price that is generally less than the assets' market value.[10] Although the target and buyer enter into the lock-up in anticipation of, or at the same time as, a merger agreement, the lock-up is typically a separate, stand-alone agreement.[11]

The option typically becomes exercisable if a third party acquires the target or if the target otherwise withdraws from the proposed transaction.[12] Accordingly, if the frustrated buyer exercises the option, the target no longer owns those highly valuable assets, or crown jewels.[13] Thus, a third party may value the target for less, and more than likely, the target will no longer be a desirable acquisition opportunity for a third party.[14] Consequently, the crown jewel lock-up acts as a deterrent; it is a deal protection device protecting the transaction between the target and the buyer.[15]

Crown jewel lock-ups became popular in the 1980s and were mainly used as a defensive mechanism in hostile takeovers, as a way of favoring one bidder over another in those transactions.[16] When

---

9. Wolf, Feirstein & Zachariah, *supra* note 7, at 1; *see also* Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1286 n.37 (Del. 1989) ("[Crown jewels] are valuable assets or lines of business owned by a target company.").

10. Alan R. Palmiter, *Reshaping the Corporate Fiduciary Model: A Director's Duty of Independence*, 67 TEX. L. REV. 1351, 1424 n.349 (1989); *see also Macmillan*, 559 A.2d at 1286 n.37 (explaining that crown jewels are sold or optioned "at bargain prices"). Although the option is generally priced at less than market value, the option must be fair to shareholders. *See* Hanson Trust PLC v. ML SCM Acquisition Inc., 781 F.2d 264, 278 (2d Cir. 1986) (explaining that, in reviewing a lock-up challenge, a court does not need to determine the "'precise value' of the optioned assets," nor must a court determine "whether the asset option prices represented fair value," but instead courts will examine the overall fairness of the option).

11. *See* Barusch, *supra* note 7.

12. Palmiter, *supra* note 10, at 1424 n.349.

13. *Id.*

14. *See* Stephen Fraidin & Jon D. Hanson, *Toward Unlocking Lockups*, 103 YALE L.J. 1739, 1747-48 (1994) ("Because lockups of all types guarantee the recipient bidder some of the target's assets if a nonrecipient bidder wins the auction, lockups are thought to lower the value of the target to nonrecipient bidders, and, thus to give the recipient bidder an advantage in the auction."); Wolf, Feirstein & Zachariah, *supra* note 7, at 1 ("[T]he traditional crown jewel lock-up can serve as a significant deterrent to competing bidders and, in some circumstances, a poison pill of sorts."). Commentators also have stated that lock-ups aid in protecting an executed transaction because a third party may lower its valuation if that valuation "was based on a value for the optioned assets that is higher than the exercise price." 1 LOU R. KLING & EILEEN T. NUGENT, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 4.04[6] n.102 (2005).

15. Palmiter, *supra* note 10, at 1424 n.349; *see also* Sean T. Wheeler, SEC Hot Topics Institute: Mergers & Acquisitions Update (Sept. 26, 2013) (unpublished presentation) (on file with author) (describing how a crown jewel lock-up deters third-party bidders).

16. *See* Barusch, *supra* note 7 (describing the invention of lock-ups in the 1980s); James A. Wachta, Note, *Down but Not Out—The Lock-Up Option Still Has Legal Punch When Properly Used*, 43 WASH. & LEE L. REV. 1125, 1125-26 (1986) (stating that target

challenged, courts across the country responded with skepticism.[17] Although the courts stressed that crown jewel lock-ups were not per se illegal, the courts emphasized that target boards must not use lock-ups in a manner that hinders stockholder value.[18] The courts repeatedly stated that if target boards used a lock-up to draw bidders into the bidding process and to maximize value, the courts would likely uphold the lock-up.[19] In most of those cases in the 1980s, however, the courts determined that the lock-ups at issue were invalid because they had hindered the bidding processes.[20] Because they hindered the bidding processes, the lock-ups had the effect of leaving money on the table and thus fleecing the shareholders. Confronted with this negative case law, practitioners shied away from lock-ups, and, like a passing fad, lock-ups went out of style.[21] But as the saying goes, "everything old becomes new again," and just like the royal sapphire and diamond engagement ring, crown jewel lock-ups have reappeared in recent years.[22]

These "modern" crown jewel lock-ups are different, however, from their 1980s counterparts. First, these modern lock-ups have thus

---

companies used asset lock-ups as a way of "induc[ing] a friendly suitor or 'white knight' to acquire . . . a principal asset of the target company for the purpose of inhibiting hostile bidders").

17. *See* Barusch, *supra* note 7 ("[T]he Delaware courts began to look skeptically at [crown jewel lockups]."); *see also infra* Part II (providing examples of courts' reviews of crown jewel lock-ups).

18. For a detailed description of the courts' analyses, see *infra* Part II.A.

19. *See, e.g.*, Hanson Trust PLC v. ML SCM Acquisition Inc., 781 F.2d 264, 274 (2d Cir. 1986) (stating that lock-ups that encourage bidders to compete in the bidding process may be beneficial); *In re* Holly Farms Corp. S'holders Litig., No. 10350, 1988 WL 143010, at *6 (Del. Ch. Dec. 30, 1988) (stating that lock-ups that "encourage a prospective bidder to submit an offer" may be upheld).

20. *See, e.g.*, *Hanson*, 781 F.2d at 283 (holding that the lock-up precluded a bidder from competing with the option holder); Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1286 (Del. 1989) (finding that the lock-up hindered the maximization of stockholder value); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 183 (Del. 1986) (finding that the lock-up "had a . . . destructive effect on the auction process"); *Holly Farms*, 1988 WL 143010, at *6 (finding that the lock-up precluded bidding). *But see* Cottle v. Storer Commc'n, Inc., 849 F.2d 570, 576 (11th Cir. 1988) (upholding the lock-up after considering a five-month-long search process and the board's decision process).

21. *See* Wolf, Feirstein & Zachariah, *supra* note 7, at 1 (stating that lock-ups "fell out of favor" after the Delaware Supreme Court's rulings in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, and *Mills Acquisition Co. v. Macmillan, Inc.*); Abigail P. Bomba et al., *Vintage Deal Tools Reemerge*, FRIED FRANK M&A Q. 1 (2012), http://www.friedfrank.com/siteFiles/Publications/Fried_Frank_M_A_quarterly_October1.pdf ("Asset lock-ups generally fell out of use after the late 1980s, when Delaware courts expressed disfavor.").

22. *See* Wolf, Feirstein & Zachariah, *supra* note 7, at 1 ("[M]odern and modified versions of the traditional crown jewel lock-up[s] have been finding their way back into the dealmakers' toolkit.").

far arisen in the context of negotiated, rather than hostile, transactions.[23] Moreover, practitioners have been careful to attribute the "modern" crown jewel lock-ups to reasons other than a potential acquisition.[24] For example, if the lock-up can stand alone, separate and independent from the acquisition agreement, or satisfies an independent business purpose, today's courts are more likely to uphold those agreements as not precluding third-party offers.[25] Despite these differences, this Article contends that the fundamental idea of the lock-up remains the same. Namely, the acquirer has an option to acquire some of the most valuable jewels of the target's corporate family. In addition, like the lock-ups of the 1980s, the question remains as to whether the target's family jewels, or crown jewels, are being fleeced.

Part II briefly summarizes the most significant jurisprudence from the 1980s on crown jewel lock-ups as well as practitioners' and commentators' responses. This Part also briefly addresses the standards applicable to a board's actions in M&A transactions as well as to deal protection devices. Part III illustrates examples of "modern" crown jewel lock-ups. This Part also argues that recent Delaware jurisprudence lays the foundation for the use of crown jewel lock-ups in transactions involving the purchase of financially distressed companies. Part IV argues that despite initial appearances and attempts to differentiate them, today's crown jewel lock-ups are the same as their 1980s predecessors. Accordingly, today's courts, like the courts in the 1980s, should focus on the sale process preceding the crown jewel lock-up. When confronted with a challenge to a crown jewel lock-up, the courts should not be swayed by whether the lock-up satisfies an independent business purpose or could stand alone as a separate agreement independent of the merger. By validating lock-ups for these reasons, courts would allow acquirers to fleece the crown jewels of targets. At the same time, however, dealmakers should not be as quick to shy away from lock-ups as they have been in the past. As the 1980s jurisprudence made clear, lock-ups can be used to enhance shareholder value. In particular, this Article argues that dealmakers may use lock-ups after an extensive sale process to incentivize bidders and extract additional value for shareholders.

---

23. *Compare infra* Part III (describing transactions and "modern" crown jewel lock-ups), *with infra* Part II.A. (describing cases involving lock-ups in the 1980s).

24. For a description of these reasons, see *infra* text accompanying notes 136-142.

25. Wolf, Feirstein & Zachariah, *supra* note 7, at 2.

II. FORCING CROWN JEWELS OUT OF FASHION

A. *The "Fashion Police": The Courts' Treatment of Crown Jewel Lock-Ups*

During the heyday of crown jewel lock-ups, courts across the country examined their use. The resulting jurisprudence provided a framework for the use of lock-ups in future transactions.

1. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*

One of the earliest and best-known cases examining crown jewel lock-ups was the Delaware Supreme Court's landmark decision in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*[26] In that case, the court struck down a lock-up option after finding that the option "had a . . . destructive effect on the auction process" between a white knight and a hostile bidder.[27] The court found that the lock-up and other deal protection devices had been entered into precisely when the board's "role [had] changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company."[28] This obligation to maximize stockholder value has become known as a board's "*Revlon* duties."[29]

In addressing the lock-up, the court noted that the Revlon board had not used the lock-up as a way of enhancing the bidding process, either by incentivizing the existing bidders to bid more or by attracting new bidders.[30] Instead, the board used the lock-up as a way of favoring one bidder willing to issue new debt to Revlon noteholders "to support the par value" of the notes, which were trading well below par value.[31] This, in turn, protected the Revlon board from personal liability in noteholder suits against the board.[32] Accordingly, the Delaware Supreme Court found that the Revlon board had breached its fiduciary duties in agreeing to the lock-up because the lock-up protected the "noteholders[' interests] over the shareholders' interests," when the board owed fiduciary duties solely to the shareholders.[33] In its opinion, the court was careful to point out that lock-ups are "permitted under Delaware law where their adoption is untainted by director interest or

26. 506 A.2d 173 (Del. 1986).
27. *Id.* at 183.
28. *Id.* at 182.
29. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1288 (Del. 1989).
30. *See Revlon*, 506 A.2d at 183.
31. *Id.* at 178-79.
32. *Id.* at 184.
33. *Id.*

other breaches of fiduciary duty," but that the Revlon board had not satisfied that standard.[34] In other words, the court determined that the lock-up had fleeced Revlon's shareholders because it shut down an active bidding process and accordingly left money on the table.

To truly understand the courts' subsequent application of *Revlon* and cases involving crown jewel lock-ups, we must consider the intersection of *Revlon* and the Delaware Supreme Court's decision in the landmark case *Unocal Corp. v. Mesa Petroleum Co.*,[35] which announced an enhanced standard of review for a target board's actions in response to a hostile takeover.[36] In *Unocal*, the court stated that in the context of hostile takeovers, there is an "omnipresent specter that a [target] board may be acting primarily in its own interests," and thus a board must show it "had reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership."[37] Moreover, any defensive measures adopted by the board had to be proportional or "reasonable in relation to the threat posed."[38] In a subsequent case applying *Unocal*, the Delaware Supreme Court clarified that the proportionality analysis required a two-part inquiry: first, the board's defensive response must not be "coercive or preclusive"; second, the response must fall within a "range of reasonableness."[39]

As previously noted, *Revlon* involved a hostile takeover, and the court was applying the *Unocal* enhanced scrutiny. Despite this, the Delaware courts quickly extended *Revlon* duties to negotiated transactions involving a change of control, such that a board's actions in these transactions are subject to enhanced scrutiny.[40] Conversely, if the transaction does not result in a change of control, the board's actions are subject to the business judgment rule.[41] Although not free from controversy, in 2003, the Delaware Supreme Court extended the *Unocal* enhanced scrutiny standard to deal protection devices in negotiated, non-change-of-control transactions.[42] Accordingly, "a

34. *Id.* at 176.
35. 493 A.2d 946 (Del. 1985).
36. *See id.* at 954-55.
37. *Id.*
38. *Id.* at 955.
39. Unitrin, Inc. v. Am. Gen. Corp. (*In re* Unitrin, Inc. S'holders Litig.), 651 A.2d 1361, 1387-88 (Del. 1995) (quoting Paramount Commc'ns, Inc. v. QVC Network Inc. (*In re* Paramount Commc'ns Inc. S'holders' Litig.), 637 A.2d 34, 45 (Del. 1994)).
40. Clark W. Furlow, *Reflections on the Revlon Doctrine*, 11 U. PA. J. BUS. L. 519, 549-50 (2009).
41. *Id.* at 551.
42. *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 932-33 (Del. 2003).

target board's decision to engage in an M&A transaction with an unaffiliated third party, the negotiation process, and the board's actions during the preclosing period will be reviewed using either the deferential business judgment rule or the enhanced *Revlon* standard depending on the transaction structure."[43] The deal protection devices, no matter if they appear in a *Revlon* transaction or a non-*Revlon* transaction, are subject to the enhanced scrutiny standard under *Unocal*.[44] Thus, crown jewel lock-ups should be subject to the enhanced scrutiny standard, even if they appear in a non-*Revlon* transaction.

2. *Mills Acquisition Co. v. Macmillan, Inc.*

The Delaware Supreme Court later reiterated, in *Mills Acquisition Co. v. Macmillan, Inc.*,[45] that lock-ups are not per se illegal and that there may be instances where lock-ups may be validly used.[46] Specifically, if the lock-up attracts bidders to the bidding process, the lock-up may be upheld.[47] Still, the court was careful to point out that when the lock-up "involves 'crown jewel' assets[,] careful board scrutiny attends the decision."[48] The court will scrutinize the board's efforts to "negotiate alternative bids" before granting the lock-up and will consider "improvement[s] in the final bid."[49] Like in *Revlon*, the court in *Macmillan* held that the lock-up did not help to maximize stockholder value and, in fact, had a "directly opposite effect."[50]

---

43. Christina M. Sautter, *Rethinking Contractual Limits on Fiduciary Duties*, 38 FLA. ST. U. L. REV. 55, 71-72 (2010).

44. *See Omnicare*, 818 A.2d at 932-33 (applying *Unocal* review to deal protection devices in non-change-of-control transactions). Deal protection devices in change-of-control transactions are subject to enhanced scrutiny because they appear in a transaction governed by enhanced scrutiny under *Revlon*, but the courts usually apply the *Unocal* enhanced scrutiny standard to such deal protection devices. Steven M. Davidoff & Christina M. Sautter, *Lock-Up Creep*, 38 J. CORP. L. 681, 702-03 (2013) (stating that in "examining [deal protection devices in change of control transactions], the Chancery Court has tended to apply, or at least mention, the preclusion or coercion elements of *Unocal* review").

45. 559 A.2d 1261 (Del. 1989).

46. *See id.* at 1284-86.

47. *Id.* at 1286.

48. *Id.*

49. *Id.*

50. *Id.*

3. *Hanson Trust PLC v. ML SCM Acquisition Inc.*

A little over two months after the Delaware Supreme Court issued its oral decision in *Revlon*,[51] the United States Court of Appeals for the Second Circuit barred the exercise of a lock-up under New York law in *Hanson Trust PLC v. ML SCM Acquisition Inc.*[52] The lock-up had resulted from "an intense struggle for control" of SCM Corporation (SCM) between Merrill Lynch, Pierce, Fenner & Smith Incorporated (Merrill Lynch) and Hanson Trust PLC (Hanson).[53] In an attempt to prevent Hanson from taking over SCM, SCM's management entered into an agreement with Merrill Lynch to engage in a management-led buyout of SCM.[54] Merrill Lynch predicated its participation on a lock-up option for SCM's Pigments and Consumer Foods businesses.[55] Under the lock-up, Merrill Lynch "would have the irrevocable right to purchase SCM's Pigments business for $350,000,000, and SCM's [Consumer Foods business] for $80,000,000, in the event that a third party acquired more than one third of SCM's common stock."[56] After SCM's independent directors unanimously approved the lock-up, Hanson made an all-cash tender offer "for any and all shares of SCM common stock, conditioned on the withdrawal or judicial invalidation of the lock-up option."[57]

The Second Circuit reversed the lower court's finding that the SCM board's approval of the lock-up option was protected by the business judgment rule.[58] The Second Circuit first recognized that "under New York law, the initial burden of proving directors' breach of fiduciary duty rests with the plaintiff," unlike under Delaware law, where, in a takeover context, the initial burden is on the target board to show that it had a reasonable ground for believing that the takeover threat was a danger to corporate policy.[59] But, like the Delaware Supreme Court in *Revlon*, the Second Circuit noted that lock-ups are not per se illegal and "that some lock-up options may be beneficial to the shareholders, such as those that induce a bidder to compete for

---

51. The Delaware Supreme Court issued its oral decision on November 1, 1985, while its written decision was issued on March 13, 1986. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 173 (Del. 1986).
52. 781 F.2d 264 (2d Cir. 1986).
53. *Id.* at 267.
54. *Id.* at 268-69.
55. *Id.* at 270.
56. *Id.*
57. *Id.* at 271-72.
58. *Id.* at 267, 283.
59. *Id.* at 273.

control of a corporation."[60] At the same time, the Second Circuit also noted that some lock-ups "may be harmful, such as those that effectively preclude bidders from competing with the optionee bidder."[61] The court found that the lock-up in *Hanson* was one that precluded bidders.[62]

In determining that the lock-up precluded bidders, the Second Circuit took particular issue with the pricing of the lock-up.[63] Specifically, the court criticized the board for failing to question the valuation methods used to price the optioned businesses.[64] Although the court recognized that the courts need not determine "'the precise value' of the optioned assets" nor "whether the asset option prices represented fair value," it stated that SCM had to "justify[] the fairness of the lock-up."[65] The court found that in agreeing to the lock-up, the SCM directors "failed to meet their duty of inquiry and had an inadequate basis for concluding one way or the other that the prices were 'within the range of fair value.'"[66]

In addition to valuation, the Second Circuit considered SCM's claim that the objective of the option was maximizing shareholder value.[67] The court found that the option foreclosed, rather than facilitated, bidding and that "a competing bidder [was] deterred from making a tender offer, unless conditioned on the withdrawal or invalidation of the subject lock-up."[68] Moreover, the court found that the existence of the option forced shareholders into a dilemma.[69] If shareholders did not tender, they would either end up in the 20% minority who would be forced out in the second step of the merger or,

---

60. *Id.* at 274.

61. *Id.*

62. *See id.* at 283.

63. *See id.* at 278-83.

64. *See id.* at 278-79. In his dissent, Judge Kearse disagreed with the majority's holding that the directors failed to ask questions. *See id.* at 290 (Kearse, J., dissenting) (listing questions that the directors asked during the September 10th board meeting).

65. *Id.* at 278 (majority opinion). The court stated that in "engaging in defensive maneuvers, such as a lock-up option, a director's primary obligation is to ensure the overall fairness, including a fair option price, to the shareholders." *Id.*

66. *Id.* at 279. In considering whether the optioned price fell within a range of fair value, the court considered various financial institutions' valuations of the Pigments division *alone*, including SCM's own investment bank's valuation. *See id.* The lowest valuation of these indicated "a $70 million undervaluation in the optioned price." *Id.* This 20% differential was greater than the percent differential of the option struck down in *Revlon*. *Id.* at 280 n.10. Accordingly, the Second Circuit found that there was a "very serious question" as to whether the assets were "significantly undervalued." *Id.* at 281.

67. *Id.* at 281.

68. *Id.* at 282.

69. *Id.*

if the merger was not consummated, the shareholders would be "left facing the prospect of the transfer of effectively half the company for inadequate consideration."[70] Thus, like the Delaware Supreme Court in *Revlon* and *Macmillan*, the Second Circuit upheld the lower court's enjoinment of the lock-up in *Hanson*.[71]

4. *Cottle v. Storer Communication, Inc.*

The United States Court of Appeals for the Eleventh Circuit took a slightly different approach to lock-ups than the Delaware Supreme Court in *Revlon* and *Macmillan* and the Second Circuit in *Hanson*.[72] In its 1988 decision, *Cottle v. Storer Communication, Inc.*,[73] the Eleventh Circuit acknowledged the Delaware Supreme Court's and Second Circuit's treatment of lock-ups, but also noted that "[a]ll auctions must end sometime, and [the] lock-ups by definition must discourage other bidders."[74] Hence the Eleventh Circuit stated that the relevant inquiry was whether the target "conducted a fair auction, and whether [the party granted the option] made the best offer," *not* whether the lock-up "effectively ended the bidding process."[75]

In applying this inquiry to the lock-up in *Cottle*, the court first noted that, unlike *Revlon* and *Hanson*, *Cottle* was "not a classic hostile takeover case."[76] The takeover in *Cottle* involved Storer Communications, Incorporated (Storer). In early 1985, an insurgent shareholder group announced it would solicit proxies for nominees to the company's board who would implement a liquidation and distribution of Storer's assets.[77] The Storer board determined that this liquidation was not in the best interests of the company's shareholders.[78] Thus, in March and April 1985, Storer's financial advisor "contacted twenty-two potential purchasers" and provided confidential information to twelve of the twenty-two.[79] Two of those potential white knights were Kohlberg Kravis Roberts & Company

70. *Id.*
71. *See id.* at 283.
72. *See* Cottle v. Storer Commc'n, Inc., 849 F.2d 570 (11th Cir. 1988).
73. *Cottle*, 849 F.2d 570.
74. *Id.* at 575-76.
75. *Id.* at 576.
76. *Id.*
77. *Id.*
78. *Id.*
79. *Id.* at 572.

(KKR) and Comcast Corporation (Comcast), who ultimately ended up in a bidding war for Storer.[80]

After receiving several revised bids from both KKR and Comcast, the board determined that KKR's bid was superior to Comcast's bid.[81] KKR's bid, however, included a lock-up, pursuant to which KKR would have the option to purchase either Storer's cable stations or its television stations.[82] A Storer shareholder brought suit arguing, inter alia, that by granting the lock-up option, the Storer board "hindered Comcast's ability to evaluate Storer's remaining assets, and thus effectively ended the bidding."[83] The Eleventh Circuit stated that the issue was not whether the lock-up "effectively ended the bidding process," but "whether Storer conducted a fair auction, and whether KKR made the best offer."[84] Along these lines, the court examined the lock-up "in the context of the entire negotiated transaction."[85] The court considered the five-month-long search the board conducted, the fact that only two bidders—KKR and Comcast—had expressed an interest in Storer, and the board's negotiations with both parties.[86] The court distinguished the lock-up from those in both *Hanson* and *Revlon* in that the Storer lock-up resulted in a significant improvement in the share price.[87] Moreover, unlike in *Hanson* and *Revlon*, the fairness of the option price was not at issue in the case.[88] Accordingly, the Eleventh Circuit determined that the Storer board had not abused its discretion in granting the lock-up.[89]

5. *In re Holly Farms Corp. Shareholders Litigation*

A few months after the Eleventh Circuit issued its decision in *Cottle*, the Delaware Court of Chancery followed up on the Eleventh Circuit's idea of a "fair auction" in *In re Holly Farms Corp. Shareholders Litigation*.[90] The events leading up to the *Holly Farms* litigation began in Spring 1988, when the CEO of Holly Farms Corporation (Holly Farms) met with the CEO of ConAgra,

80. *Id.*
81. *Id.* at 573.
82. *Id.*
83. *Id.* at 575.
84. *Id.* at 576.
85. *Id.*
86. *See id.*
87. *See id.* ("Storer ultimately received a cash price of $91 per share, $16 more per share than KKR's previous offer, and $7.50 more per share than Comcast's.").
88. *See id.* at 577.
89. *See id.*
90. No. 10350, 1988 WL 143010 (Del. Ch. Dec. 30, 1988).

Incorporated (ConAgra), to discuss the advantages of a possible combination of the two companies.[91] At the end of June, however, the Holly Farms board terminated those discussions after determining that a combination of the two companies was not in the Holly Farms shareholders' best interests.[92] A couple of months later, in October 1988, Tyson Foods submitted a cash and stock offer worth approximately $49 per share.[93] Holly Farms rejected the offer, finding that it was "financially inadequate," but instructed its financial advisor, Morgan Stanley, to "actively explore available alternatives to the offer."[94] As a result, Morgan Stanley entered into negotiations with ConAgra and contacted other potential buyers.[95]

On October 21, 1988, Tyson Foods "commenced a cash tender offer for all of Holly Farms' outstanding common stock at an improved $52 per share price."[96] The Holly Farms board rejected the tender offer as "financially inadequate," and Morgan Stanley continued its discussions with ConAgra while also continuing to explore other alternatives to the Tyson Foods offer.[97] On November 11, Holly Farms sent a letter to Tyson Foods stating that it would be holding a board meeting on November 16 to consider its alternatives.[98] The letter stated that the board had not yet reached a decision as to whether Holly Farms was for sale.[99] On November 16 and 17, the Holly Farms board met to discuss its "viable alternatives."[100] The board decided that a sale of Holly Farms was in the best interests of its shareholders and that the ConAgra swap proposal was the best financial alternative.[101] ConAgra's proposal included three key deal protection devices: a $15 million termination fee, an expense reimbursement provision, and "a lock up option on Holly Farms' prime poultry operations."[102]

Tyson Foods brought suit seeking a preliminary injunction of the deal protection devices, arguing that Holly Farms did not conduct a

91. *Id.* at *1.
92. *Id.*
93. *Id.* at *2.
94. *Id.*
95. *Id.*
96. *Id.*
97. *Id.*
98. *Id.*
99. *Id.*
100. *Id.* Those alternatives were a leveraged recapitalization valued at $56-57 per share; Tyson Foods' cash tender offer, which had been increased to $54 per share; a "ratio stock swap proposal from ConAgra which had a non-discounted nominal value of $57.75 per share"; or Holly Farms could do nothing. *Id.*
101. *Id.*
102. *Id.*

fair auction and that Tyson Foods never had the opportunity to actively bid for Holly Farms.[103] In reviewing the facts, the Court of Chancery observed that "at some point" during the board meeting on November 16 and 17, the board decided to sell Holly Farms.[104] The court noted that at that point, the board's *Revlon* duty to maximize stockholder value became applicable.[105] The court critiqued Holly Farms' sale process, finding that no attempt was made to auction the company in a manner that would satisfy *Revlon*.[106] Instead, Holly Farms "favored ConAgra as a business partner" and negotiated with ConAgra throughout November 16 and 17, while it did not negotiate with Tyson Foods during that same period.[107] In fact, the court found that despite Tyson Food's "numerous inquiries" regarding the adequacy of its proposal, Holly Farms did not encourage Tyson Foods to submit a revised proposal.[108]

In reviewing the lock-up, the court first noted that lock-ups may be upheld where the lock-up is being used "to encourage a prospective bidder to submit an offer," but the court also recognized that lock-ups cannot "end an active auction [or] foreclose further bidding."[109] The court then found that the Holly Farms board did not use the lock-up as a way of drawing ConAgra into the bidding process or as a way of otherwise encouraging ConAgra to submit an offer.[110] Instead, the court stated, "the lock up was nothing but a 'show stopper' that effectively precluded the opening act."[111] The court recognized further that the lock-up precluded Tyson Foods from bidding for Holly Farms.[112] Accordingly, like the courts before it, the Court of Chancery enjoined the lock-up option in *Holly Farms*.[113]

---

103. *Id.* at *3.
104. *Id.* at *4.
105. *See id.*
106. *See id.* at *4-5.
107. *Id.* at *5.
108. *Id.*
109. *Id.* at *6 (quoting Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 183 (Del. 1986)) (internal quotation marks omitted).
110. *See id.*
111. *Id.*
112. *See id.*
113. *See id.* The court also enjoined the termination fee and the expense reimbursement provision. *See id.*

B. Dealmakers' Responses to the Changing Trends

With the overwhelming majority of cases criticizing crown jewel lock-ups, the M&A bar was left in a conundrum.[114] Dealmakers could continue to use lock-ups in their deals but risked a court's enjoining a lock-up for any number of reasons, including that it foreclosed other bidders, did not reflect the fair value of the assets, abruptly ended the sale process, did not enhance shareholder value, or coerced the shareholders into voting for the transaction. With so much uncertainty, practitioners chose to avoid crown jewel lock-ups altogether. Professors John C. Coates IV and Guhan Subramanian probably best summed up practitioners' response to the negative case law by observing and opining:

> What is noteworthy about practitioner response to these cases, however, is not the direction but the magnitude. . . . Presumably an asset lockup combined with otherwise immaculate manager behavior could withstand scrutiny, particularly if the deal were scrutinized under *Unocal* rather than *Revlon*. Nevertheless, the evidence suggests that practitioners have chosen to avoid these more nuanced readings in favor of a bright-line avoidance of asset lockups.[115]

In addition to the courts' hostility toward lock-ups, some commentators have surmised that boards may not want to risk losing a company's crown jewels "if the entire company is not being acquired."[116] Moreover, target boards may not want to "completely lockup deals for an initial bidder, thereby precluding the possibility of a higher bidder emerging (particularly, but not only, where there has been no pre-signing market check)."[117] Similarly, target boards may avoid lock-up options simply due to the "prevailing wisdom" that such options harm shareholders because "(i) the bid premium is not allowed to reach its full potential, and (ii) an enhanced ability to hand-select acquirers insulates managers from the disciplining aspects of the takeover market."[118] Whether due to the negative jurisprudence or the

---

114. *See, e.g.*, Hanson Trust PLC v. ML SCM Acquisition Inc., 781 F.2d 264 (2d Cir. 1986); Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261 (Del. 1989); *Revlon*, 506 A.2d 173; *Holly Farms*, 1988 WL 143010.

115. John C. Coates IV & Guhan Subramanian, *A Buy-Side Model of M&A Lockups: Theory and Evidence*, 53 STAN. L. REV. 307, 327-28 (2000).

116. KLING & NUGENT, *supra* note 14, § 4.04[6] n.102.

117. *Id.*

118. Timothy R. Burch, *Locking Out Rival Bidders: The Use of Lockup Options in Corporate Mergers*, 60 J. FIN. ECON. 103, 105 (2001).

practical implications of lock-ups, asset lock-ups went out of style by the mid-to-late 1990s.[119]

Some commentators and practitioners have even gone so far as to suggest that crown jewel lock-ups may be invalid altogether. For example, in determining the validity of deal protection devices in a *Revlon* transaction, commentators have stated that a relevant inquiry is whether the deal involved a crown jewel lock-up.[120] Moreover, while referring to the use of lock-ups in the 1980s, one prominent practitioner stated, "I just don't think the law now lets you do that."[121] Until recently, practitioners have shied away from crown jewel lock-ups, and lock-ups have been virtually nonexistent in deals.[122]

III. BACK IN STYLE: REFURBISHING CROWN JEWEL LOCK-UPS

The once-popular deal protection device has awoken from its slumber in recent years.[123] The resurgence of crown jewel lock-ups appears to be a direct result of JPMorgan Chase's (JPMorgan) acquisition of financially distressed Bear Stearns during the Great Recession.[124] As part of the acquisition, Bear Stearns, which "was on the verge of filing for bankruptcy," granted JPMorgan an option to purchase Bear Stearns' Madison Avenue, Manhattan headquarters for

---

119. Coates & Subramanian, *supra* note 115, at 315, 327 ("[A]sset lockups were rare by the late 1980s and extinct by the late 1990s."); Wheeler, *supra* note 15, at 23 ("Fiduciary risks associated with these lockups caused them to fall out of favor by the 1990s."); Eleonora Gerasimchuk, *Stretching the Limits of Deal Protection Devices: From* Omnicare *to* Wachovia, 15 FORDHAM J. CORP. & FIN. L. 685, 690 (2010) ("Asset options have been virtually non-existent since *Revlon* and *Mills Acquisition v. Macmillan*."). What is perhaps even more interesting is that Professors Coates and Subramanian's research suggested that practitioners did not use crown jewel lock-ups as much as the literature suggested. *See* Coates & Subramanian, *supra* note 115, at 327 n.51. *But see* Wolf, Feirstein & Zachariah, *supra* note 7, at 1 (referring to lock-ups as a "staple of high-stakes dealmaking technology in the 1980s M&A boom").

120. *See* 1 ARTHUR FLEISCHER, JR. & ALEXANDER R. SUSSMAN, TAKEOVER DEFENSE § 14.05 (6th ed. 2000) ("Are 'crown jewel' assets involved so that other bidders would be dissuaded from continuing the auction if the lockup were granted?").

121. Coates & Subramanian, *supra* note 115, at 327 n.54 (quoting an interview with Robert E. Spatt) (internal quotation marks omitted). Professors Coates and Subramanian also stated that practitioners responded to the negative case law as if the courts had stated that lock-ups were per se illegal. *See id.* at 327.

122. *See id.* at 327-28.

123. Wolf, Feirstein & Zachariah, *supra* note 7, at 2 ("After a long period of dormancy, lock-ups—'crown jewel' or otherwise—have seen a recent creative rebirth with some structural twists.").

124. *Reynolds Holding Sticky Fingers*, BUS. STANDARD, http://www.business-standard.com/article/opinion/sticky-fingers-113022300064_1.html (last updated Feb. 22, 2013, 9:21 PM) ("The financial crisis inspired a revival.").

$1.1 billion.[125] Under the terms of the merger agreement, the option was only exercisable if the merger agreement was terminated, and prior to the termination, an alternative acquisition proposal for Bear Stearns had been made.[126] Bear Stearns shareholders challenged the JPMorgan-Bear Stearns merger, arguing, among other things, that the lock-up option for the headquarters, combined with the other deal protection devices, "disenfranchised the shareholders and depressed the ultimate purchase price" and that the lock-up option was the equivalent of a 36% termination fee.[127]

Applying Delaware law at trial, the Supreme Court of New York held that the board's decision to merge with JPMorgan should be governed by the business judgment rule and that the board "acted expeditiously to consider the company's limited options" and avoided bankruptcy.[128] Accordingly, the court found that it should not question the board's decision.[129] The court, however, did not stop there. It stated that even if an enhanced scrutiny standard were applicable, the court would not disturb the transaction.[130] Notably, the court stated that Bear Stearns "contacted over a dozen other potential corporate parties without obtaining a viable alternative bid"[131] and observed that the "board was apparently concerned with preserving Bear Stearns' existence by ensuring a merger with the only bidder possessing the credibility and financial strength to help facilitate a government-assisted rescue."[132] With respect to the deal protection devices, the court stated that a heightened standard of review was inapplicable and that the "financial catastrophe confronting Bear Stearns, and the economy generally, justified the inclusion of the" deal protection devices.[133] Regarding the lock-up option specifically, the court considered the head of Bear Stearns' real estate group's conclusion that the "$1.1 billion [lock-up value] represented the building's fair

---

125. JPMorgan Chase & Co., Current Report (Form 8-K), exhibit 2.1, art. 6.11 (Mar. 20, 2008) [hereinafter JPMorgan Chase Current Report]; *In re* Bear Stearns Litig., 870 N.Y.S.2d 709, 728 (Sup. Ct. 2008).

126. JPMorgan Chase Current Report, *supra* note 125, § 6.11. Applicable termination events triggering the option included JPMorgan's terminating the agreement because the Bear Stearns board of directors changed its recommendation in favor of the merger or because the requisite Bear Stearns stockholder approval had not been obtained. *See id.* §§ 6.10, 8.1(e), 8.1(f).

127. *Bear Stearns*, 870 N.Y.S.2d at 730, 734.

128. *Id.* at 730-31.

129. *See id.* at 731.

130. *See id.* at 732.

131. *Id.* at 731.

132. *Id.* at 734.

133. *Id.* at 735.

value."[134] Thus, the court dismissed the stockholders' complaint.[135] Some would say that this has paved the way for lock-ups in modern transactions.

A. *Modern Crown Jewel Lock-Ups*

Despite the extraordinary circumstances leading up to the JPMorgan-Bear Stearns merger, the Bear Stearns lock-up has brought lock-ups back into fashion. Practitioners, however, are conscious of the lessons learned from the 1980s case law. They note that courts may view lock-ups "more favorably" if they involve targets, like Bear Stearns, who are "facing 'merge-or-die' financial distress."[136] At the same time, practitioners are quick to stress that "[w]hat might pass muster for targets in 'life-or-death' situations or in financial distress may not be advisable forms of deal protection in the ordinary course."[137] Practitioners point out, however, that if the target board "has a demonstrable business purpose for, or benefit from," the lock-up, it may be easier to defend.[138] Also, if the lock-up can "stand[] on its own," separate and apart from the business combination, the arrangement may be more likely to withstand judicial scrutiny.[139] Likewise, if the parties can articulate a "particular need of the *buyer*" that is satisfied by the lock-up, commentators suggest that the courts may be more likely to uphold the lock-up.[140] Possible examples of a buyer's need or other justification for demanding a lock-up include "foregoing another acquisition opportunity or business development efforts" to pursue an acquisition of the target.[141] Practitioners have incorporated these "lessons" into recent transactions.[142] The following is a detailed description of those recent transactions including "modern" crown jewel lock-ups.

---

134. *Id.* at 734.

135. *See id.* at 741.

136. Wheeler, *supra* note 15, at 25.

137. Wolf, Feirstein & Zachariah, *supra* note 7, at 2.

138. *Id.*; *see also* David Benoit, *Security Detail Protects NYSE Deal*, WALL STREET J. (Jan. 30, 2013, 6:36 PM), http://www.wsj.com/news/articles/SB1000142412788732392 6104578274112350462452 (summarizing Professor Coates' opinion that "[c]ourt rulings generally say an agreement that makes business sense for the seller, and its shareholders, is allowable"); Wheeler, *supra* note 15, at 25 ("Seller should have a discernible benefit from executing an independent agreement other than circumventing fiduciary concerns.").

139. Wolf, Feirstein & Zachariah, *supra* note 7, at 2; *see also* Wheeler, *supra* note 15, at 25 (noting that a crown jewel lock-up written as an "[i]ndependent agreement [is] more likely to be upheld if [it is] not contingent on the consummation of the merger").

140. Wolf, Feirstein & Zachariah, *supra* note 7, at 2.

141. Wheeler, *supra* note 15, at 25.

142. *See supra* Part II.A.

1. Apple-AuthenTec: Demonstrable Business Purpose

Apple Inc.'s (Apple) 2012 acquisition of AuthenTec, Inc. (AuthenTec), a provider of "mobile security software licenses and fingerprint sensor technology," is an example of crown jewel lock-up's being attributed to a demonstrable business purpose.[143] But that is only part of the story. The crux of this tale involves a powerful company (Apple) using its unique bargaining power and limited competition to corner a much smaller company (AuthenTec) into a deal with terms beneficial to Apple. Apple's acquisition of AuthenTec began in late 2011 and early 2012 when AuthenTec contacted "several leading consumer electronics companies to gauge potential market interest" in its new fingerprint technology.[144] Of the several parties contacted, Apple was the only potential customer that expressed an interest in the development of the technology.[145] In February 2012, the officers of both companies met to negotiate the terms for a commercial contract regarding "the further development of this new technology."[146] During the meetings, Apple's representatives told the AuthenTec representatives that they were not satisfied with the financial terms within the commercial agreement, but did make a suggestion for an acquisition of AuthenTec.[147] By May 2012, Apple had decided to propose an acquisition of AuthenTec for $7 per share, instead of pursing a stand-alone commercial agreement.[148] In fact, Apple made it clear that it would no longer negotiate a commercial agreement for the technology outside of an acquisition context.[149] In addition, Apple stated that it would not participate in an auction and that it would rescind its offer if

---

143. Christopher Versace, *Securing the Future of Apple's iPhones and iPads*, FORBES (Jan. 22, 2013, 10:03 AM), http://www.forbes.com/sites/greatspeculations/2013/01/22/securing-the-future-of-apples-iphones-and-ipads/.

144. AuthenTec, Inc., Proxy Statement (Schedule 14A), at 18 (Aug. 31, 2012) [hereinafter AuthenTec Proxy Statement]. Although AuthenTec's filings do not include the names of the parties contacted, AuthenTec "counts Alcatel-Lucent, Cisco, Fujitsu, HBO, HP, Lenovo, LG, Motorola, Nokia, Orange, Samsung, Sky, and Texas Instruments among its customers." Matt Brian, *Why Apple Really Bought AuthenTec: It Wanted "New Technology" for Upcoming Products, and Quickly*, NEXT WEB (Aug. 16, 2012, 12:52 PM), http://thenextweb.com/apple/2012/08/16/the-real-reason-apple-acquired-authentec-because-needed-new-technology-quickly-products/. In the preceding two years, "multiple parties" had contacted AuthenTec regarding "possible strategic transactions," but those conversations never progressed beyond the preliminary stages. AuthenTec Proxy Statement, *supra*, at 18.

145. AuthenTec Proxy Statement, *supra* note 144, at 18.

146. *Id.*

147. *Id.*

148. *Id.* at 19.

149. *Id.*

AuthenTec were to solicit alternative proposals.[150] After meeting with outside financial and legal counsel, AuthenTec's board allowed its representatives to pursue a transaction with Apple for $8 a share, but directed the representatives to seek the ability to solicit other offers either presigning or postsigning via a go-shop provision.[151] Apple responded that it would not allow AuthenTec to pursue other alternatives presigning nor would it agree to a go-shop provision; however, it indicated it would allow for the customary no-shop and fiduciary-out provisions, which would allow AuthenTec to respond to any unsolicited offers.[152] On May 9, 2012, the AuthenTec board authorized its representatives to continue negotiations on the terms Apple outlined, and both merger negotiations and due diligence proceeded from May through the end of July 2012.[153]

On July 26, 2012, when the two parties entered into an all-cash merger agreement, the parties simultaneously entered into an Intellectual Property and Technology Agreement (IP Agreement).[154] The IP Agreement functioned as a type of crown jewel lock-up, according to which Apple paid $20 million in exchange for AuthenTec's granting Apple the right to acquire "non-exclusive, perpetual, irrevocable, worldwide license[s]" in AuthenTec hardware and software technology and sensor patents.[155] This right would continue to exist whether or not the merger was consummated.[156] To exercise these acquisition rights, Apple was obligated to provide AuthenTec with written notice of its intent to exercise within the 270 days following the IP Agreement's effective date of July 26, 2012.[157] If Apple chose to exercise the hardware and patent license acquisition

150. *Id.*

151. *Id.* at 19-20.

152. *Id.* at 20.

153. *See id.* at 20-24. During May 2012, Apple conducted due diligence, and on May 30, Apple communicated its unwillingness to proceed with the acquisition due to concerns raised through its due diligence. *Id.* at 20-21. These issues were resolved by July 3, 2012, and Apple announced they would continue with the transaction in lieu of a traditional commercial transaction. *Id.* at 22. AuthenTec's board agreed to the merger transaction on July 26, 2012, after discussion with outside financial and legal counsel. *Id.* at 24.

154. AuthenTec, Inc., Current Report (Form 8-K), at 3 (July 27, 2012) [hereinafter AuthenTec Current Report].

155. *Id.* exhibit 10.1, at 1, 2. An attorney representing Apple in Delaware litigation relating to the transaction stated that "the only technology that is being licensed under the IP agreement is technology relating to the 2-D project, the two-dimensional fingerprint verification product that Apple and AuthenTec were in the process of developing." Telephonic Oral Argument Motion To Expedite Proceedings at 18-19, *In re* AuthenTec, Inc. S'holder Litig., No. 7735-VCP (Del. Ch. Nov. 25, 2013).

156. Wolf, Feirstein & Zachariah, *supra* note 7, at 1.

157. AuthenTec Current Report, *supra* note 154, exhibit 10.1, at 1, 12.

right, Apple was obligated to pay a total of $90 million to AuthenTec.[158] If Apple chose to exercise the software and patent license acquisition right, it was obligated to pay a total of $25 million to AuthenTec.[159] Once AuthenTec received these payments, Apple did not owe any other payments. Thus, the license rights did not provide any ongoing income to AuthenTec. Due to the one-time nature of the payments, the IP Agreement acted as a type of crown jewel lock-up because AuthenTec was in essence selling the technology to Apple.

With the IP Agreement appearing to be a type of "crown jewel lock-up," the AuthenTec Board made sure to document, in its proxy statement, the independent business reasons for recommending that the stockholders vote to approve the IP Agreement.[160] Specifically, the proxy statement stated that the AuthenTec board believed that the IP Agreement "would provide significant value to any third party seeking to make an acquisition proposal," stating further that "the successful integration into Apple's products . . . would increase demand for [AuthenTec's] technologies and products from third parties."[161] Not everyone agreed with the AuthenTec board's opinion that the IP Agreement would entice third parties to make an acquisition proposal for AuthenTec. For example, in his *N.Y. Times DealBook* "Deal Professor" column, Professor Steven Davidoff Solomon explained that the likely impact of the IP Agreement would be to "severely discourage" third-party jumping bids.[162] He explained that because "Apple is such a dominant force in the electronics world and would no longer need to license or buy AuthenTec's products, it would make any acquisition less worthwhile."[163] As described previously, this was the case because Apple's license acquisition rights were one-time payments and did not provide ongoing income to AuthenTec. Hence even though the licenses were nonexclusive, it was as if the technology had been sold to Apple.

---

158. *Id.* exhibit 10.1, at 5. The $90 million payment was split up such that $72 million was due thirty days after the date on which Apple sent AuthenTec written notice and the other $18 million was due in four $4.5 million installments. *Id.*

159. *Id.* exhibit 10.1, at 8. The $25 million payment was split up such that $20 million was due thirty days after Apple provided written notice to AuthenTec and $5 million was due in four $1.25 million installments. *Id.*

160. AuthenTec Proxy Statement, *supra* note 144, at 25-28.

161. *Id.* at 26-27.

162. Steven Davidoff Solomon, *Apple's Quiet Deal for AuthenTec*, N.Y. TIMES DEALBOOK (Aug. 1, 2012, 9:36 AM), http://dealbook.nytimes.com/2012/08/01/apples-quiet-deal-for-authentec/.

163. *Id.*

Professor Davidoff Solomon was not the only person to hold this view of the acquisition. By August 30, 2012, stockholders filed thirteen putative class-action suits against AuthenTec, members of AuthenTec's Board, and Apple, nine of which were filed in the Delaware Court of Chancery.[164] The suits sought to enjoin consummation of the merger and performance of certain obligations under the IP Agreement and, among other things, alleged that the AuthenTec board had breached its fiduciary duties "by failing to maximize stockholder value and by failing to disclose material information."[165] During a hearing on a motion to expedite in Delaware, the defendants argued that calling the IP Agreement a crown jewel lock-up was a "misnomer" because it did not involve crown jewel assets and further that "it didn't lock anything up and it didn't lock anybody out."[166] In response, Vice Chancellor Parsons stated that the determination of whether the case involved a crown jewel lock-up turned on two issues.[167] First, the importance of the patents must be weighed against AuthenTec's other intellectual property, a balancing determination that the court was unable to make based on the existing record.[168] Parsons noted that the patents had to be somewhat important simply "given the nature of the alternative agreement . . . Apple has entered into regarding them."[169] Second, he noted that although the licenses were nonexclusive, the court must determine the "impact" the licenses may have on third parties who may be considering a jumping bid.[170] This was also an issue that the court could not determine based on the existing record.[171] Parsons compared the option to a reverse

---

164. AuthenTec Proxy Statement, *supra* note 144, at 10. The remaining suits were filed in the state of Florida. Final resolution of those cases is unclear, but the following is clear: on March 19, 2013, one of the suits filed in the Florida Eighteenth Judicial Circuit Court for Brevard County was dismissed, and this dismissal was affirmed by the Florida Fifth District Court of Appeal. *See* Brown v. AuthenTec, Inc., 109 So. 3d 219 (Fla. Dist. Ct. App. 2013) (unpublished table decision). The plaintiffs in the remaining Florida cases filed a motion to expedite on August 2, 2012, which the defendants opposed; the defendants also moved to dismiss or stay the Florida cases. *See* AuthenTec Defendants' Brief in Opposition to Plaintiffs' Motion for Expedited Proceedings, *In re* AuthenTec, Inc. S'holder Litig., No. 7735-VCP (Del. Ch. Nov. 25, 2015). The Florida court declined to stay the cases, and the plaintiffs then filed a motion for preliminary injunction on September 5, 2012. *Id.* As of September 17, 2012, a preliminary injunction hearing had not been set. *Id.*

165. AuthenTec Proxy Statement, *supra* note 144, at 46.

166. Telephonic Oral Argument Motion To Expedite Proceedings, *supra* note 155, at 17.

167. *Id.*

168. *See id.* at 18.

169. *Id.* at 17-18.

170. *Id.* at 18.

171. *See id.*

termination fee, in that Apple would be paying a fee if the deal between Apple and AuthenTec did not close.[172] Once Apple paid the fee, it would have the rights to the technology.[173] Although Parsons did not pass judgment on whether the agreements amounted to a crown jewel lock-up, he did say that he believed the agreement would "have some impact on the value, the marketability, of AuthenTec, or at least there is a colorable claim to that effect."[174] He ultimately denied the motion to expedite, and by November 25, 2013, the nine Delaware Court of Chancery suits had been dismissed with prejudice, without the court's addressing the merits or validity of the crown jewel lock-up.[175]

Vice Chancellor Parsons' treatment of the Apple-AuthenTec transaction likely has limited precedential value because he was ruling on a motion to expedite, and thus he did not have a complete record before him. At the same time, however, Parsons' ruling sends a mixed message. As an all-cash transaction, the Apple-AuthenTec deal should be subject to a heightened level of scrutiny under *Revlon*, and any deal protection devices, including a crown jewel lock-up, would also be subject to enhanced scrutiny (no matter if that scrutiny is under *Revlon* or *Unocal*). But it is unclear from Parsons' ruling if he was applying enhanced scrutiny or would apply enhanced scrutiny to a full record. Parsons seems to have sidestepped the issue by stating that he could not determine on the limited record whether the agreement was in fact a crown jewel lock-up. This sends a message that although the transaction may be an all-cash, *Revlon* transaction, enhanced scrutiny may only apply if a particular deal provision were deemed to be a deal protection device. By recognizing that the patents had to be at least somewhat important given the fact that the parties had entered into a specific agreement and by stating that the agreement had to have at least "some impact on value," Parsons came close to ruling that the IP Agreement was a crown jewel lock-up, but then punted the issue. Accordingly, it is unclear whether enhanced scrutiny applies or whether the more deferential business judgment rule applies. In any event, the Apple-AuthenTec transaction provides an example of parties attributing what is likely a crown jewel lock-up to a demonstrable

---

172. *See id.* at 20.

173. *Id.*

174. *Id.* at 21.

175. *See id.* at 37 (denying the motion to expedite); AuthenTec Proxy Statement, *supra* note 144 (stating that three of the lawsuits filed in Delaware were voluntarily dismissed with prejudice); *In re* AuthenTec, Inc. S'holder Litig., No. 7735-VCP, 2013 WL 6180252 (Del. Ch. Nov. 25, 2013).

business purpose in an attempt to avoid the agreement being classified as a crown jewel lock-up and presumably hoping to obtain deferential treatment.

2. NYSE-ICE: Crown Jewel Lock-ups as Stand-Alone Agreements

Another popular argument that attempts to justify lock-ups is that the lock-up agreement could be a stand-alone agreement, separate and independent from the merger. The merger of NYSE Euronext (NYSE) and IntercontinentalExchange, Inc. (ICE), is an example of a transaction in which this argument has been used to justify a lock-up. Before entering into a merger agreement with ICE, NYSE had attempted to engage in another potential transaction that fell through, paving the way for a merger with ICE. That first transaction was announced on February 15, 2011, and was a "merger of equals" between NYSE and Deutsche Börse AG.[176] Following that announcement, on April 1, 2011, NYSE received an offer from ICE and NASDAQ OMX Group, Inc. (NASDAQ), offering to buy all the outstanding shares of NYSE common stock for a mixture of cash and NASDAQ and ICE common stock.[177] NASDAQ and ICE hoped to merge the "two biggest stock exchange operators in the United States" and create synergies in a competitive marketplace.[178] On April 11, the NYSE board of directors rejected the offer from NASDAQ and ICE and reaffirmed the potential transaction with Deutsche Börse AG.[179]

On April 19, 2011, NASDAQ and ICE sent NYSE a letter with more details regarding their offer; however, NYSE's board rejected the offer again, with concern that the NASDAQ and ICE proposal would not receive regulatory approval.[180] On May 16, 2011, ICE and NASDAQ issued a press release, stating that they would not pursue an acquisition of NYSE due to regulatory concerns.[181] On February 1, 2012, the European Commission prohibited the transaction between NYSE and Deutsche Börse AG due to anticompetitive concerns, and the parties subsequently terminated their agreement.[182] During

176. IntercontinentalExchange, Inc., Proxy Statement (Schedule 14A), at 77 (Apr. 30, 2013) [hereinafter IntercontinentalExchange Proxy Statement].

177. *Id.*

178. Michael J. de la Merced, *Nasdaq and ICE Make Hostile Bid for NYSE Euronext*, N.Y. TIMES DEALBOOK, http://dealbook.nytimes.com/2011/04/01/nasdaq-ice-make-hostile-bid-for-nyse-euronext/ (last updated Apr. 1, 2011, 8:02 PM).

179. IntercontinentalExchange Proxy Statement, *supra* note 176, at 77.

180. *Id.*

181. *Id.*

182. *Id.*

September 2012, the CEOs of NYSE and ICE met sporadically and discussed the possibility of a transaction between ICE and NYSE.[183] On September 13, ICE's board of directors gave ICE's CEO permission to explore a potential transaction with NYSE.[184] That same day, the NYSE board met to discuss possible strategic alternatives.[185] The NYSE board evaluated a stand-alone strategy and reviewed potential partners for other potential transactions.[186] Furthermore, the board considered the separation or sale of its businesses, including its European derivatives business or its continental European cash-trading and listings business.[187] The board ultimately decided to pursue potential opportunities regarding these options.[188] A mutual confidentiality agreement was signed on October 5, 2012, which ultimately led to the final merger agreement between the parties on December 20, 2012.[189] Pursuant to the merger agreement, NYSE shareholders would receive approximately 67% stock and 33% cash.[190]

The same day that ICE and NYSE entered into a merger agreement, their subsidiaries simultaneously entered into a Clearing and Financial Intermediary Services Agreement (Clearing Services Agreement).[191] Under the terms of the Clearing Services Agreement, ICE Clear Europe Limited (ICE Clear), a wholly owned subsidiary of ICE, agreed to provide London International Financial Futures and Options Exchange (LIFFE) Administration and Management, a wholly owned subsidiary of NYSE, clearing services for LIFFE's London derivatives trading market.[192] In exchange, LIFFE agreed to pay ICE Clear certain fixed clearing service costs "plus an applicable margin."[193] LIFFE also agreed to provide financial intermediary services to ICE Clear.[194] The Clearing Services Agreement was a stand-alone agreement, which would go into effect whether or not the merger was consummated.[195] On July 2, 2013, NYSE and ICE

183. *Id.*
184. *Id.* at 78.
185. *Id.*
186. *Id.*
187. *Id.*
188. *Id.*
189. *Id.* at 78, 85.
190. IntercontinentalExchange, Inc., Current Report (Form 8-K), at 2 (Dec. 20 2012) [hereinafter IntercontinentalExchange Current Report].
191. IntercontinentalExchange Proxy Statement, *supra* note 176, at 85.
192. *Id.* at 85, 128.
193. *Id.* at 128.
194. *Id.*
195. *Id.* at 129.

announced completion of the clearing transition of NYSE LIFFE's London derivatives market to ICE Clear Europe.[196]

In a joint ICE-NYSE definitive proxy statement dated April 30, 2012, the two boards of directors acknowledged the concern that certain provisions of the merger agreement and the Clearing Services Agreement might discourage third parties from submitting superior bids to acquire NYSE, either during the preclosing period or if the deal was terminated prior to closing.[197] Despite this concern, both the ICE and NYSE boards recommended that the shareholders of each company approve the transactions because of the substantial cost-saving synergies for both entities.[198] For ICE, the Clearing Services Agreement would "see ICE make [its] mark in the European clearing space and lay down the gauntlet for competition."[199] For NYSE, the agreement would eliminate nearly $80 million in costs associated with NYSE's development of its own clearing house, as well as the risk that NYSE would have a difficult time creating its own internal clearing house after the announcement of the ICE transaction.[200] Even if the merger between ICE and NYSE was not consummated, NYSE was guaranteed clearing of its European futures trades.[201]

Once ICE and NYSE announced the execution of the merger agreement, a total of thirteen putative stockholder class action complaints were filed.[202] All complaints included similar allegations concerning the NYSE board of directors' breach of the fiduciary duties of both care and loyalty.[203] They specifically alleged that both the merger agreement and the Clearing Services Agreement included preclusive deal protection provisions that had deterred third-party bidders from submitting competitive offers for NYSE.[204] In the Delaware Court of Chancery, then-Chancellor Strine found that the deal protection provisions were not preclusive because there was "no

196. *See* Press Release, IntercontinentalExchange, Inc., ICE Clear Europe Completes Clearing Transition of NYSE Liffe Derivatives Contracts (July 2, 2013), http://ir.theice.com/tools/viewpdf.aspx?page={5E4147A8-B609-4035-AF46-25D656E52C38}.

197. IntercontinentalExchange Proxy Statement, *supra* note 176, at 40.

198. *Id.* at 87, 101.

199. *ICE Deal Ends Liffe's Clearing Countdown*, FUTURES & OPTIONS WORLD (Dec. 21, 2012, 10:26 AM), http://www.fow.com/3134319/ICE-deal-ends-Liffes-clearing-countdown.html.

200. IntercontinentalExchange Proxy Statement, *supra* note 176, at 87.

201. Nina Mehta & Nandini Sukumar, *IntercontinentalExchange To Acquire NYSE for $8.2 Billion*, BLOOMBERG BUS. (Dec. 20, 2012, 8:07 PM), http://www.bloomberg.com/news/2012-12-20/intercontinentalexchange-said-in-merger-talks-with-nyse-euronext.html.

202. IntercontinentalExchange Proxy Statement, *supra* note 176, at 160.

203. *Id.*

204. *Id.*

evidence in the record that presents a barrier to any serious acquirer."[205] Strine found it undisputed that the Clearing Services Agreement was crucial to NYSE, which would have a difficult time implementing its own clearing services. He specifically stated, "So that issue of the so-called crown jewel isn't there."[206] In reaching this conclusion, Strine placed a particular emphasis on the lack of other deal partners in existence. Specifically, he noted that NYSE was unable to get a deal done with Deutsche Börse AG, and he further stated that the plaintiffs' suggestion that NYSE could get a deal done with the NASDAQ was "sort of . . . funny to" him.[207] Then-Chancellor Strine further noted that if another person wanted to do a deal with NYSE, it could "play Let's Make a Deal with ICE and you buy them out of that contract or, frankly, you just make clear to them [that] they better be a great clearinghouse."[208] Accordingly, Strine was of the opinion that the Clearing Services Agreement did not amount to a crown jewel lock-up.[209]

Like Vice Chancellor Parsons' opinion in the Apple-AuthenTec case, Strine's treatment of the agreement in this case sends a mixed message as to the proper standard of review regarding lock-ups. The 67% stock/33% cash consideration in this case likely would not trigger *Revlon*, but deal protection devices are presumably still subject to an enhanced level of scrutiny.[210] At first glance, Strine appears to have been applying an enhanced-scrutiny standard by finding that the deal protection devices, including the crown jewel lock-up, were not preclusive. But then he went on to state that the Clearing Services Agreement was not a crown jewel lock-up because it did not preclude any bidders. There is a "chicken and the egg" problem with this analysis. If the agreement was not a crown jewel lock-up, then it was not a deal protection device and thus not subject to enhanced scrutiny (i.e., the preclusiveness and coerciveness inquiry under *Unocal*).[211] Maybe Strine was saying that the agreement *is* a crown jewel lock-up, but that it is not a *preclusive* crown jewel lock-up. In any event, the

205. *In re* NYSE Euronext S'holders Litig., No. 8136-CS, slip op. at 1, 12 (Del. Ch. May 10, 2013).

206. *Id.* at 13.

207. *Id.* at 11.

208. *Id.* at 12.

209. *Id.*

210. *See, e.g.*, *In re* Santa Fe Pac. Corp. S'holder Litig., 669 A.2d 59, 65, 70-71 (Del. 1995) (finding that a transaction consisting of 33% cash consideration did not trigger *Revlon*).

211. See *supra* text accompanying notes 38-42 for a description of the application of the *Unocal* enhanced scrutiny test and its application to deal protection devices.

opinion is unclear and likely leaves practitioners in a conundrum as to how to negotiate crown jewel lock-ups.

3. Pacific Rubiales-Petrominerales: A Modern Crown Jewel Lock-Up with Traditional Roots

Of the modern crown jewel lock-ups, Pacific Rubiales Energy Corporation's (Pacific Rubiales) acquisition of Petrominerales Limited (Pretrominerales) is the most similar to the traditional crown jewel lock-ups of the 1980s. In January 2012, Petrominerales "concluded that prevailing market conditions" could lead to unsolicited acquisition offers for its operations and subsequently hired TD Securities to help it identify potential acquisition partners and provide advice for any potential transactions.[212] From January to August 2012, Petrominerales received several unsolicited offers, including an offer from Pacific Rubiales, which led Petrominerales to have its financial advisor prepare a data room and invite a select number of parties to enter into confidentiality and standstill agreements.[213] From September 2012 to February 2013, seven parties, not including Pacific Rubiales, entered into confidentiality agreements with Petrominerales and proceeded to conduct due diligence.[214] One of those parties submitted an offer, but Petrominerales and that party were unable to come to an agreement on the terms of the transaction.[215]

In June 2013, Petrominerales determined that access to the data room and interactions with potential parties would not likely result in a strategic transaction, and thus Petrominerales closed its data room and ceased all active discussions with potential parties.[216] In August 2013, Pacific Rubiales reached out to Petrominerales to discuss the potential for a transaction and submitted an offer for an all-cash transaction.[217] From August to September 2013, Petrominerales renewed discussions with the other parties who had previously signed confidentiality agreements.[218] On September 16, 2013, Pacific Rubiales submitted a second, revised nonbinding expression of interest to Petrominerales,

212. Petrominerales, *Notice of Special Meeting of Shareholders*, ALVOPETRO 19 (Oct. 29, 2013), http://www.alvopetro.com/files/galleries/Print_Circular_Petrominerales_OCT291939.pdf [hereinafter Petrominerales Information Circular].

213. *Id.*

214. *Id.*

215. *Id.*

216. *Id.*

217. *Id.*

218. *Id.* at 19-20.

and subsequent negotiations were held.[219] The next day, Petrominerales' board of directors met to review potential transactions with various parties, including Pacific Rubiales.[220] At that meeting, the board directed the management to negotiate with an eye towards completing a transaction with Pacific Rubiales.[221] On September 18, 2013, both parties signed a letter of intent and commenced negotiations on the terms of the transaction.[222]

On September 29, 2013, Pacific Rubiales announced that it had entered into an "Arrangement Agreement" with Petrominerales for a cash-only acquisition of all of its current and outstanding stock.[223] The agreement proposed a cash-for-stock acquisition, with Pacific Rubiales paying for each Petrominerales common share CAD$11 cash and one common share of a newly formed exploration and production company.[224] The Arrangement Agreement was detailed in Petrominerales' Information Circular and stated that Pacific Rubiales made an irrevocable offer to purchase "Midstream Assets."[225] Specific details of the offer are limited regarding its exact terms, which were set forth in a disclosure letter that is not available for public disclosure.[226]

The Midstream Assets offer had been in the works since May 2013, when Petrominerales "commenced a formal process to pursue opportunities to monetize certain of its Midstream Assets."[227] The Midstream Assets included "Petrominerales' transport rights in the OCENSA Pipeline; . . . Petrominerales' 9.65% equity interest and transport rights in the OBC Pipeline"; and "Petrominerales' 5% equity interest in the OCENSA Pipeline," which is located in Colombia.[228] Due to Colombia's "rugged terrain and lack of infrastructure," the pipeline assets were particularly valuable because they are "the only cost effective method of transporting crude in a country that is now Latin America's fourth largest oil producer."[229]

---

219. *Id.* at 20.
220. *Id.*
221. *Id.*
222. *Id.*
223. Press Release, Pac. Rubiales Energy Corp., Pacific Rubiales Announces Strategic Acquisition of Petrominerales (Sept. 29, 2013), http://sedar.com/DisplayCompanyDocuments.do?long=EN&issuerNO=00007953 (select "Sept. 29, 2013" entry).
224. *Id.*
225. Petrominerales Information Circular, *supra* note 212, at 27.
226. *Id.* app. C, art. 9.5.
227. *Id.* at 27.
228. *Id.* at 15, 17.
229. Matt Smith, *What Does the Pacific Rubiales Acquisition of Petrominerales Mean for Investors?*, MOTLEY FOOL (Oct. 30, 2013), http://www.fool.ca/2013/10/30/what-does-the-pacific-rubiales-acquisition-of-petrominerales-mean-for-investors-2/.

This crown jewel lock-up was different from the traditional lock-up in that the *target company*, Petrominerales, could accept the offer (but did not have to) if the acquisition with Pacific Rubiales was "not completed by December 10, 2013 for any reason."[230] Moreover, unlike the traditional lock-up, which typically binds the target to sell the assets to the optionholder if the target enters into an agreement with another buyer, Petrominerales was not bound to the agreement were another offer to emerge for its stake in the OCENSA pipeline.[231] However, Petrominerales could not enter into another agreement without the consent of Pacific Rubiales.[232] If no other offer presented itself, however, Pacific Rubiales was obligated to purchase the Midstream Assets *if* Petrominerales accepted the irrevocable offer.[233] This modified crown jewel lock-up provided cash to Petrominerales, which had seen its cash flow drop 45% in the preceding year due to lower oil prices, but it also dissuaded other buyers from bidding for Petrominerales' oil assets.[234]

Unlike the preceding transactions, the Pacific Rubiales-Petrominerales transaction was not litigated, and thus it is not clear how a court would address a similarly structured transaction in the future. The next Subpart, however, does provide some guidance to

---

230. Petrominerales Information Circular, *supra* note 212, at 27.

231. *Id.*

232. *Id.* app. C, art. 6.1(5)(a). Such consent was "not to be unreasonably withheld." *Id.*

233. *Id.* app. C, art. 9.5.

234. Liz Hoffman, *Norton Rose Reps Pacific Rubiales in $1.5B Energy Co. Buy*, LAW360 (Sept. 30, 2013, 11:26 AM), http://www.law360.com/articles/476615/norton-rose-reps-pacific-rubiales-in-1-5b-energy-co-buy (subscription required). As of the date of the Information Circular, no shareholder suits had been instituted against Petrominerales or Pacific Rubiales at the time of the acquisition. Petrominerales Information Circular, *supra* note 212, app. C, sched. D, § (r). The acquisition closed on November 28, 2013, and a month later, Pacific Rubiales sold the 5% equity interest in the OCENSA pipeline it had obtained in the Petrominerales acquisition to Darby Private Equity, an arm of Franklin Templeton Investments, for US$385 million and retained a long-term agreement for transportation of its oil production in the same pipeline. Press Release, Pac. Rubiales Energy Corp., Pacific Rubiales Announces Closing of U.S.$385 Million Sale of its OCENSA Pipeline Interest (Apr. 1, 2014), http://sedar.com/DisplayCompanyDocuments.do?long-EN&issuerNo=00007953 (select "April 1, 2014" entry). Pacific Rubiales sold the OCENSA pipeline to pay down the debt from the Petrominerales acquisition, a US$400 million balance outstanding on Petrominerales' U.S. dollar revolving credit facility; it gained additional transportation capacity through a secure pipeline in Colombia. Pac. Rubiales Energy Corp., Management Discussion and Analysis, PAC. ENERGY 4 (May 8, 2014), http://www.pacific.energy/sites/default/files/documents/reports/2014/financial%20reports/q1/PRE%20MD&A%20Q1%202014.pdf; Press Release, Pac. Rubiales Energy Corp., Pacific Rubiales Announces $385 Million Sale of OCENSA Pipeline Interest (Dec. 23, 2013) http://sedar.com/DisplayCompanyDocuments.do?long-EN&issuerNo=00007953 (select "Dec. 23, 2013" entry).

practitioners on the possible use of crown jewel lock-ups in a sale of a financially distressed company.

B. Crown Jewel Lock-Ups and the Financially Distressed Company

A number of commentators have cited to the 2012 BGI-Shenzen (BGI)-Complete Genomics merger as yet another example of a modern crown jewel lock-up providing benefits to the target company separate and apart from the merger.[235] As this Subpart details, however, the option in that transaction was not a crown jewel lock-up option, but rather a stock option. This Article nevertheless contends that the BGI-Complete Genomics transaction and the resulting Delaware jurisprudence stemming from this transaction set the foundation for using crown jewel lock-ups in transactions when the target is financially distressed. Although BGI-Complete Genomics involved a stock option, the arguments advanced in support of the deal structure are transferable to crown jewel lock-ups.

The merger of Complete Genomics and BGI began on June 5, 2012, when Complete Genomics retained Jefferies as its financial advisor to help it review strategic alternatives, including the possibility of a merger.[236] Jefferies contacted forty-two parties, of which nine parties executed confidentiality agreements.[237] The board then requested interested parties to submit nonbinding proposals.[238] Of the nine parties who had executed confidentiality agreements, two submitted nonbinding proposals regarding a transaction and four indicated their interest in an equity investment.[239] Negotiations "quickly focused on the two transactional proposals," a period of negotiations with both parties ensued, and then one of the two parties requested exclusivity.[240] On June 15, 2012, Jefferies instructed BGI that written, nonbinding, preliminary proposals for a transaction involving the sale of the company should be submitted by June 29, 2012.[241] BGI signed a confidentiality agreement on June 19, 2012, and

---

235. *See, e.g.*, Wolf, Feirstein & Zachariah, *supra* note 7, at 2.

236. Complete Genomics, Inc., Tender Offer Statement (Schedule TO-T), exhibit 99.(A)(1)(A)), at 14 (Sept. 25, 2012) [hereinafter Complete Genomics Tender Offer Statement].

237. *In re* Complete Genomics, Inc. S'holder Litig., No. 7888-VCL, slip op. at 7-8 (Del. Ch. Nov. 9, 2012).

238. *Id.* at 8.

239. *Id.*

240. *Id.*

241. Complete Genomics Tender Offer Statement, *supra* note 236, exhibit 99.(A)(1)(A), at 14.

received a management presentation on Complete Genomics.[242] On July 3, 2012, BGI submitted a written, nonbinding preliminary proposal to acquire Complete Genomics, and BGI was later informed that a final written proposal was due by July 31, 2012.[243]

During July 2012, BGI conducted research and due diligence on Complete Genomics, and it ultimately asked for additional time to submit its final written proposal, which was granted.[244] On August 6, 2012, BGI submitted a nonbinding proposal to acquire Complete Genomics.[245] Complete Genomics' management and financial and legal advisors reviewed the proposed agreement and provided BGI with a term sheet for bridge financing.[246] On August 29, 2012, BGI provided a letter from a financial entity in China stating that the entity would finance the transaction for $3.15 a share; however, on August 31, BGI provided another letter from the Export-Import Bank of China, stating that it would also finance the acquisition for $3.15 a share.[247] BGI's financial advisors decided that the Export-Import Bank of China would be a better lender for the proposed transaction.[248] On September 15, 2012, the parties executed and delivered the all-cash merger agreement, representing a transaction value of nearly $117.6 million, and issued a press release regarding the acquisition on September 17, 2012.[249]

On the same date the parties executed the merger agreement, Complete Genomics, BGI, and BGI-HONGKONG Co. (BGI-HONGKONG), a wholly owned subsidiary of BGI, entered into a Convertible Subordinated Promissory Note (Note).[250] Under the terms of the Note, BGI-HONGKONG, the lender, agreed to loan Complete Genomics, the borrower, up to an aggregate amount of $30 million to be used "solely for working capital and capital expenditure requirements in the ordinary course of business."[251]

The Note was structured so that the "first draw" of $6 million would occur on October 1, 2012.[252] Thereafter, beginning in November

242. *Id.*
243. *Id.* at 14-15.
244. *Id.*
245. *Id.*
246. *Id.*
247. *Id.* at 16.
248. *Id.*
249. *Id.* at 17; Complete Genomics, Inc., Current Report (Form 8-K), exhibit 99.1 (Sept. 17, 2012) [hereinafter Complete Genomics Current Report].
250. Complete Genomics Current Report, *supra* note 249, exhibit 99.1.
251. *Id.* exhibit 10.2, § 3(e).
252. *Id.* exhibit 10.2, § 3(a).

2012, Complete Genomics could request funding of $6 million per month by giving written request to BGI-HONGKONG no fewer than three days prior to the "requested funding date."[253] The Note included certain conditions, including that "the Merger Agreement has not been terminated and remains a valid and binding obligation of the parties thereto."[254] The Note also gave Complete Genomics certain conversion and registration rights, pursuant to which BGI-HONGKONG had the right to convert the principal and interest due into common stock of Complete Genomics at the offer price.[255] BGI-HONGKONG had the right to exercise this conversion right either upon termination of the Merger Agreement or upon a change of control of Complete Genomics.[256] If BGI-HONGKONG were to exercise its conversion rights, it could own up to 22% of Complete Genomics' stock.[257]

Shareholders brought suit in the Delaware Court of Chancery, seeking to enjoin the merger between Complete Genomics and BGI.[258] The shareholders argued that the Complete Genomics board had breached its fiduciary duties by implementing certain deal protection provisions into the merger agreement.[259] Although Vice Chancellor Laster enjoined the "don't ask, don't waive" standstill provision in a potential bidder's confidentiality agreement with Complete Genomics, he did not enjoin the merger between Complete Genomics and BGI.[260] Laster stated that the combination of the deal protection provisions and the bridge loan made the question of whether the merger agreement was preclusive a closer case.[261] Ultimately, however, Laster was able to distinguish the bridge loan from the stock option in *Paramount Communications Inc. v. QVC Network Inc.* on the ground that the bridge loan provided a "substantial benefit" to Complete Genomics because of the company's need for immediate cash.[262] Laster recognized that the stock option in *QVC* "didn't provide any benefit to

253. *Id.*
254. *Id.*
255. *Id.* exhibit 10.2, § 4(a).
256. *Id.*
257. Wolf, Feirstein & Zachariah, *supra* note 7, at 2.
258. Complete Genomics Tender Offer Statement, *supra* note 236, amend. no. 1, at 2.
259. In re Complete Genomics, Inc. Shareholder Litigation, SULLIVAN & CROMWELL LLP 1 (Nov. 30, 2012), http://www.sullcrom.com/siteFiles/Publications/SC_Publication_In_re_Complete_Genomics_Inc_Shareholder_Litigation.pdf.
260. *See id.* at 4. For a detailed description of "don't ask, don't waive" standstills, see Christina M. Sautter, *Auction Theory and Standstills: Dealing with Friends and Foes in a Sale of Corporate Control*, 64 CASE W. RES. L. REV. 521 (2013).
261. *See In re* Complete Genomics, Inc. S'holder Litig., No. 7888-VCL, slip op. at 16 (Del. Ch. Nov. 9, 2012).
262. *Id.*

the target and only came into play in the event of a topping bid."[263] Thus, Laster found that although the bridge loan (a crown jewel lock-up) could be preclusive in other contexts, the fact that it provided a benefit to the target company in this particular transaction made it a nonpreclusive deal protection device.[264] Accordingly, he refused to grant a preliminary injunction.[265]

Although, as earlier stated, the Complete Genomics option was a stock lock-up, not an asset lock-up, Laster's reasoning potentially sets the groundwork for upholding asset lock-ups under similar circumstances. Like the Supreme Court of New York in *Bear Stearns*, which emphasized the "financial catastrophe confronting Bear Stearns,"[266] Laster focused on the "highly fragile state" of Complete Genomics in refusing to grant a preliminary injunction in *In re Complete Genomics, Inc. Shareholder Litigation*.[267] Moreover, he emphasized that granting a preliminary injunction without a topping bid present would be imprudent because it could risk the current deal.[268] Although it is clear that Complete Genomics' economic state was far from healthy and it is completely possible a topping bid had not emerged due to Complete Genomics' "fragile state," it is equally possible that a topping bid had not emerged due to the deterrent effects of the lock-up. Nonetheless, courts appear inclined to uphold lock-ups when an argument can be made that the target company is financially unwell.[269] The parameters of how unwell a company must be for a court to uphold a lock-up have yet to be determined.

IV. MODERN CROWN JEWEL LOCK-UPS: A PASSING FAD, AN ENDURING CLASSIC, OR A FLEECING OF SHAREHOLDER VALUE?

The revival of crown jewel lock-ups in recent transactions renews the debate from the 1980s regarding the validity of lock-ups. Unlike the courts in the 1980s, today's courts have not yet enjoined the modern crown jewel lock-ups.[270] Consequently, it remains to be seen whether the modern crown jewel lock-up is a passing fad or an enduring classic.

---

263. *Id.*
264. *See id.*
265. *See id.* at 17.
266. *In re* Bear Stearns Litig., 870 N.Y.S.2d 709, 735 (Sup. Ct. 2008).
267. *Complete Genomics*, slip op. at 17.
268. *See id.*
269. *See, e.g.*, *id.*
270. *See, e.g.*, *Bear Stearns*, 870 N.Y.S.2d 709.

Modern lock-ups appear to differ in some material respects from their predecessors. The most significant difference is that, thus far, today's lock-ups have only appeared in negotiated transactions, rather than in hostile transactions where they were typically combined with other defensive mechanisms such as poison pills and white knights.[271] The Delaware Supreme Court in *Revlon* even noted that economic conditions in the 1980s were such that enticing a white knight to enter a bidding war required "some form of compensation to cover the risks and costs involved."[272] Although hostile transactions are on the rise, amicable transactions remain the hallmark of today's economic environment.[273] As a result, modern lock-ups have morphed in the more harmonious environment in which they are being used.

Another significant difference is that the 1980s case law has influenced dealmakers and their practices.[274] Dealmakers have been careful to document the decision process leading up to the lock-up.[275] In doing so, dealmakers have taken almost painstaking steps to differentiate today's lock-ups from the lock-ups of the 1980s and have attempted to make clear that the lock-ups could be stand-alone transactions or have business purposes separate and apart from the merger transactions themselves.[276]

Dealmakers' preoccupation with issues such as whether the lock-up can be attributed to another business purpose or can be a stand-alone transaction from the merger is misplaced. Although at first glance these modern lock-ups can appear benign and different from their 1980s predecessors, today's lock-ups do not differ greatly from their predecessors. The saying "everything old becomes new again" holds true for today's lock-ups. Although today's lock-ups have

---

271. The Eleventh Circuit's opinion in *Cottle* is an excellent example of the hostile transactions of the 1980s in which lock-ups arose and were analyzed. The court noted, "This is a shareholder derivative action involving white knights, poison pills, shark repellants, stalking horses, crown jewels, hello fees, goodbye fees and asset lock-up options." Cottle v. Storer Commc'n, Inc., 849 F.2d 570, 572 (11th Cir. 1988); *see also In re* Holly Farms Corp. S'holders Litig., No. 10350, 1988 WL 143010, at *1 (Del. Ch. Dec. 30, 1988) (noting that the plaintiffs were not only seeking to enjoin a lock-up, but also were seeking "to compel Holly Farms to redeem its stock rights plan").

272. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 183 (Del. 1986).

273. *See* David Gelles, *Hostile Takeover Bids for Big Firms Across Industries Make a Comeback*, N.Y. TIMES DEALBOOK (June 12, 2014, 8:25 PM), http://dealbook.nytimes.com/2014/06/12/hostile-takeover-bids-for-big-firms-across-industries-make-a-comeback (describing an increase in hostile transactions in 2014).

274. Wolf, Feirstein & Zachariah, *supra* note 7, at 7.

275. For an example of this documentation, see *supra* Part III.A.1.

276. Wolf, Feirstein & Zachariah, *supra* note 7, at 2.

evolved into more sophisticated transactions as a result of historical precedents, economic development, and outside socio-political influences, at the heart of the matter, modern lock-ups are the same as their 1980s predecessors.

A. The Family Jewels

The lock-ups of the 1980s concerned some of the most significant and valuable assets of the target company, typically divisions of the target. For example, the *Revlon* lock-up was for the company's Vision Care and National Health Laboratories divisions.[277] Similarly, the *Macmillan* lock-up involved eight Macmillan subsidiaries,[278] while the *Hanson* lock-up pertained to SCM's Pigments and Consumer Foods businesses.[279] Likewise, the *Cottle* lock-up gave KKR the right to purchase either Storer's cable stations or its television stations,[280] and the *Holly Farms* lock-up provided ConAgra the right to purchase Holly Farms' "prime poultry operations."[281]

Like their predecessors, modern lock-ups still concern some of the most significant and valuable assets of the target company. Unlike their predecessors, however, today's lock-ups generally do not involve subsidiaries or divisions, but rather technology or other rights. For example, AuthenTec granted Apple the right to acquire "non-exclusive, perpetual, irrevocable, worldwide license[s]" in AuthenTec hardware and software technology and sensor patents.[282] The technology and patents went to the heart of AuthenTec's business, which developed and provided "mobile security software licenses and fingerprint sensor technology."[283] Although these licenses were nonexclusive, the effect of the licenses was exclusivity because Apple no longer had to buy or license AuthenTec technology. Once Apple made the payments as required under the IP Agreement, Apple no longer owed any consideration; the agreement did not provide ongoing income to AuthenTec. In addition, although the licenses were nonexclusive, there were likely no other companies interested in licensing the technology. This much was evident from AuthenTec's initial search for a company

277. *Revlon*, 506 A.2d at 178.

278. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1275 (Del. 1989).

279. Hanson Trust PLC v. ML SCM Acquisition Inc., 781 F.2d 264, 270 (2d Cir. 1986).

280. Cottle v. Storer Commc'n, Inc., 849 F.2d 570, 573 (11th Cir. 1988).

281. *In re* Holly Farms Corp. S'holders Litig., No. 10350, 1988 WL 143010, at *2 (Del. Ch. Dec. 30, 1988).

282. AuthenTec Current Report, *supra* note 154, exhibit 10.1, at 1, 2.

283. Versace, *supra* note 143.

with which to partner to develop the technology. Thus, the money AuthenTec could make from the technology was likely to come from Apple. But AuthenTec essentially sold the technology to Apple, which meant that in the long run, AuthenTec would not enjoy that stream of income. Accordingly, when evaluating AuthenTec as a takeover target, AuthenTec's value would be greatly diminished.[284]

I must note, however, that this is not to say that every merger-agreement-related intellectual property agreement should be classified as a crown jewel lock-up. Instead, the business effects of the agreement must be evaluated, as well as the relationship between the agreement and any merger agreements. The unique aspects of each business and transaction must be considered, as well as the preceding sale process (if the company is in *Revlon*-mode) and the deterrent effects of the intellectual property agreement on other potential bidders.

Similarly to the Apple-AuthenTec deal, Petrominerales granted Pacific Rubiales an option to purchase Petrominerales' equity and transportation rights in certain pipelines located in Colombia.[285] This option was particularly valuable because the pipeline was the most efficient manner in which to transport oil in Colombia, a country whose transportation infrastructure is lacking.[286] Pacific Rubiales announced that these equity and transportation rights would help it to cut costs on transportation of some of its crude oil.[287] Like the options of old, this option worked to deter "competing buyer[s] from cherry-picking Petrominerales' oilfield assets."[288] But unlike the options of old, if a competing bid emerged for these assets, Petrominerales was not bound to sell the assets to Pacific Rubiales.[289] Despite this unique out, the option still had the potential to deter bidders because bidders who were only willing to buy all of the Petrominerales assets subject to

---

284. Although the courts never ultimately ruled on whether the agreement amounted to a crown jewel lock-up, Vice Chancellor Parsons was of the belief that the agreement would have "some impact on the value" of AuthenTec. Telephonic Oral Argument Motion To Expedite Proceedings, *supra* note 155, at 21.

285. Petrominerales Information Circular, *supra* note 212, app. C, art. 9.5.

286. *See* Press Release, Pac. Rubiales Energy Corp., *supra* note 223.

287. Peter Murphy & Nelson Bocanegra, *Petrominerales Colombia Shares Surge on Takeover by Pacific Rubiales*, REUTERS (Sept. 30, 2013, 4:54 PM), http://www.reuters.com/article/2013/09/30/us-pacificrubiales-petrominerales-idUSBRE98T12Z20130930 ("Greater access to pipelines would also reduce its spending on more expensive road haulage to transport some of its crude, the company said, as well significantly increase its exploration and production acreage.").

288. Hoffman, *supra* note 234.

289. Petrominerales Information Circular, *supra* note 212, app. C, art. 9.5.

the lock-up would likely not be as attractive as Pacific Rubiales, who was bound to buy all the assets. Moreover, in order to be competitive, bidders would have to offer at least a little bit more than the Petrominerales offer for all of the Midstream Assets.

The NYSE-ICE transaction is the most unlike the traditional crown jewel lock-up. Instead of acquiring an asset of the *target* company (here, NYSE), the acquirer (here, ICE) *provided* services *to* the target in exchange for a fixed fee plus a margin of the services.[290] This agreement remained in place even if the proposed merger were to fall through.[291] When considering the ramifications of this agreement, it becomes clear that although the form may be different, the substantive result is that the Clearing Services Agreement was a crown jewel lock-up. A third party considering whether to jump the NYSE-ICE transaction would be forced to consider that, unless it had its own clearing services, it most likely would be doing business with (indeed, obtaining an essential service from) the party whose very deal it just disrupted. Then-Chancellor Strine was of the opinion that this was not a crown jewel lock-up because a third party could buy ICE out of its contract or "frankly, you just make clear to them [that] they better be a great clearinghouse."[292] From a practical perspective, this seems easier said than done. If ICE were not a "great clearinghouse," what would the third party do then? The third party would be forced to take on additional costs in creating its own clearing services or possibly find another party to provide those clearing services. Then-Chancellor Strine himself recognized that the Clearing Services Agreement was crucial to NYSE because of the various approvals that would be needed.[293] Accordingly, to find that the Clearing Services Agreement was not a crown jewel lock-up is a misstatement.

Instead, this Article contends that what then-Chancellor Strine intended to hold was that the NYSE-ICE lock-up—while a lock-up—was not preclusive because, as a practical matter, there were not any viable merger partners to preclude from making a bid. NYSE had already executed a deal with Deutsche Börse AG that fell through after the European Commission had prohibited the transaction over anticompetitive concerns.[294] Other than ICE, it seems the one other

---

290. *See* IntercontinentalExchange Current Report, *supra* note 190.
291. IntercontinentalExchange Proxy Statement, *supra* note 176, at 129.
292. *In re* NYSE Euronext S'holders Litig., No. 8136-CS, slip op. 1, 12 (Del. Ch. May 10, 2013).
293. *See id.* at 11-12.
294. IntercontinentalExchange Proxy Statement, *supra* note 176, at 77.

viable strategic potential merger partner would have been NASDAQ. NYSE had already rejected a joint offer from ICE and NASDAQ, citing regulatory concerns.[295] Apart from the fact that NYSE and NASDAQ are direct competitors, the idea that NYSE and NASDAQ could successfully engage in a transaction without raising any regulatory concerns was, as then-Chancellor Strine summed up, "funny."[296]

As these cases show, dealmakers and the courts alike seem to shy away from declaring that certain assets are crown jewels.[297] This avoidance likely stems from the 1980s jurisprudence questioning the validity of lock-ups involving crown jewels. It is easier to say that something is not a crown jewel asset than to wrestle with the close scrutiny applicable to crown jewel lock-ups. In concentrating on whether an asset is a crown jewel, dealmakers seemed to have lost sight of the fact that the 1980s jurisprudence focused on the auction process preceding entry into the lock-up and the role the lock-up played within that process.

B. The Bidding Process: A Fleecing of Shareholder Value?

Under the 1980s jurisprudence, the preceding sale process and the target board's actions are outcome determinative in evaluating whether a crown jewel lock-up will be upheld. In *Revlon*, the Delaware Supreme Court made clear that lock-ups would be valid where "their adoption is untainted by director interest or other breaches of fiduciary duty."[298] Similarly, the Second Circuit in *Cottle* explained that the relevant inquiry should be whether there was a fair auction and whether the bidder being afforded the lock-up made the best offer, *not* whether the lock-up effectively ended the bidding process.[299] The courts in the 1980s were concerned with whether a target was using a lock-up to favor one bidder over another in a manner that minimized, not maximized, shareholder value.[300] If a target used a lock-up to favor one bidder over another, there was a potential that the target was leaving money on the table that should instead be in the shareholders' pockets. Accordingly, the courts in the 1980s focused on whether the

---

295. *Id.*

296. *NYSE Euronext*, slip op. at 11.

297. *See, e.g.*, *id.* at 13.

298. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 176 (Del. 1986).

299. *See* Cottle v. Storer Commc'n, Inc., 849 F.2d 570, 576 (11th Cir. 1988).

300. For a description of the courts' treatment of crown jewel lock-ups, see *supra* Part II.A.

target was using a lock-up in a manner that shut down the bidding process.[301] Along these lines, the courts repeatedly stated in dicta that if the target was using the lock-up to draw bidders into the bidding process and to enhance shareholder value, the courts would be more inclined to uphold those lock-ups.[302] Commentators have recognized the importance of the sale process, stating that crown jewel lock-ups "should normally be preceded by an auction or market canvass and would need to withstand close scrutiny."[303]

Upon first glance, it would appear that target boards and their attorneys have taken these lessons to heart and have conducted sale processes intended to maximize stockholder value. But things are not always as they seem, and upon a closer examination, the transactions leading up to today's lock-ups fall short of the sale processes envisioned by the courts in the 1980s. The Apple-AuthenTec transaction provides the best example of things not always being what they seem to be. At the outset, AuthenTec contacted "several leading consumer electronics companies" to gauge their interest in AuthenTec's new technology.[304] Of the companies contacted, only Apple expressed an interest in the technology and moved forward with negotiating a commercial contract.[305] The tides soon changed, however, and Apple used the commercial contract negotiations and its bargaining power to essentially force AuthenTec into merger negotiations without allowing AuthenTec to otherwise test the market.[306] AuthenTec was forced into a corner—either proceed in a lucrative deal with Apple on Apple's terms or contact other potential buyers and risk losing out on any and all potential transactions with Apple.

Counsel for AuthenTec argued that the fact the lock-up arose out of commercial agreement negotiations that "morphed into a merger agreement cuts directly against the notion" that the lock-up was "designed to preclude bidding, designed to preclude somebody jumping the merger."[307] Counsel argued that the manner in which the

---

301. *See* cases cited *supra* note 20 (describing cases in which the courts held that a lock-up hindered the sale process).
302. *See, e.g.*, *Revlon*, 506 A.2d at 183.
303. 1 KLING & NUGENT, *supra* note 14, § 4.04[6] n.102.
304. AuthenTec Proxy Statement, *supra* note 144, at 18.
305. *See id.*
306. *See id.* at 19-20.
307. Telephonic Oral Argument Motion To Expedite Proceedings, *supra* note 155, at 23.

lock-up arose was "exactly the reverse of how lock-ups occur."[308] In making that argument, however, AuthenTec's counsel failed to recognize that AuthenTec never engaged in an auction or a market canvass for the *entire company*, or at least not to the standard envisioned by the courts in the 1980s. Approaching customers to sell software or to otherwise coordinate to develop software is simply not the same as approaching those customers to sell an entire company. As such, AuthenTec did not engage in any market check and then found itself cornered by Apple.

Of the modern crown jewel lock-up transactions discussed in this Article, the Pacific Rubiales-Petrominerales transaction is the only one that was preceded by a market check approaching the type envisioned by the courts in the 1980s. In the months leading up to its transaction with Pacific Rubiales, Petrominerales hired a financial advisor to advise it on potential acquisition partners.[309] Moreover, seven parties executed confidentiality agreements and proceeded with due diligence, which resulted in one party's making an offer.[310] Petrominerales continued discussions with the parties who entered into confidentiality agreements up to September 2013, the same month that it entered into an agreement with Pacific Rubiales.[311] Although Pacific Rubiales was not one of the seven parties who initially entered into confidentiality agreements and was not the one party who made an offer early in the process, through this market canvass, the Petrominerales board should have been able to effectively assess Petrominerales' value and to evaluate potential merger partners' interests in the company. If the courts in the 1980s had been reviewing this transaction, they most likely would have upheld the lock-up and would have urged future dealmakers to engage in a similar type of sale process before agreeing to a lock-up.[312]

C. Can Lock-ups Become an Enduring Classic?

Despite some alterations, modern crown jewel lock-ups are not materially different from their 1980s predecessors. A limited number of recent deals have included lock-ups, and it remains to be seen whether more dealmakers will follow this trend and incorporate these

---

308. *Id.*
309. Petrominerales Information Circular, *supra* note 212, at 19.
310. *Id.*
311. *Id.* at 19-20.
312. *See, e.g.*, Cottle v. Storer Commc'n, Inc., 849 F.2d 570, 576-77 (11th Cir. 1988) (holding that the lock-up was valid because it aided the auction process).

devices into their future transactions or whether they will continue to be deterred by the 1980s jurisprudence.

Although limited modern case law addresses crown jewel lock-ups and is mainly in the form of dicta, today's courts appear willing to uphold lock-ups, particularly if the assets of a financially distressed company are at stake or if the court is of the opinion that limited serious merger partners exist.[313] In potentially upholding a lock-up based on one of these reasons, however, courts should be cautious that dealmakers are not using these "reasons" as a means of concealing a fleecing of the target's assets and, consequently, shareholder value. As Vice Chancellor Parsons alluded to in the Apple-AuthenTec litigation, courts should scrutinize the underlying business transaction and the sale process preceding entry into the lock-up.[314]

This is not to say that dealmakers should eschew crown jewel lock-ups. To the contrary, dealmakers should not be as quick to shy away from lock-ups as they have been in the past. In agreeing to lock-ups, however, targets must be sure that an active auction process or an extensive market canvass has taken place (at least a process similar to that which occurred in the Pacific Rubiales-Petrominerales transaction). Moreover, targets may even inform bidders that the target would be willing to agree to a crown jewel lock-up following an extensive sale process. As a result, and consistent with arguments I have made in previous articles addressing deal protection devices, bidders may be enticed to submit even higher bids for the target company.[315] To avoid the possibility that the target may be left at the altar without its most valuable family jewels, target boards also must ensure that the option to purchase is only triggered when the target has terminated the agreement to enter into a definitive agreement with another bidder. Admittedly, this will deter potential third-party overbids, but because the target will have already engaged in an extensive sale process, pursuant to which any potential bidders will have already had the opportunity to pursue a transaction, the likelihood that the target or its shareholders will be harmed is minimal. Undeniably, this entails a weighing of the extensiveness of the sales process and the likelihood that no additional value has been left on the table against the deterrent nature of the lock-up itself. Engaging in an

313. *See supra* text accompanying notes 206-207.

314. *See supra* text accompanying notes 206-207.

315. *See, e.g.*, Sautter, *supra* note 260, at 567-69 (setting forth a framework allowing for "don't ask, don't waive" standstills to be used that is based on the target engaging in an extensive presigning sales process).

extensive sale process in which all bidders are told that the target is willing to, and is likely to, agree to a lock-up at the end of the process should result in achieving the highest possible value for stockholders.[316] Engaging in an extensive sale process and permitting lock-ups only under these limited circumstances will ensure that the target's family jewels are not being fleeced and that crown jewel lock-ups could become an enduring classic.

V. CONCLUSION

As the saying goes, "everything old becomes new again." Crown jewel lock-ups are no different. Once a popular deal protection device in the 1980s, crown jewel lock-ups have reemerged in some recent deals. This time around, dealmakers have attempted to distinguish these lock-ups from their predecessors. Dealmakers have taken almost painstaking steps to differentiate today's lock-ups from earlier lock-ups and have attempted to make clear that the lock-up could be a stand-alone transaction or has a business purpose separate and apart from the merger transaction itself. This Article argues, however, that today's lock-ups are not significantly different from their predecessors. Practitioners and courts should not lose sight of the 1980s jurisprudence that closely scrutinized the sale process preceding the lock-up as well as the deterrent effects of the lock-up on potential bidders. Failing to consider these factors and not giving these factors proper weight potentially results in companies and their shareholders being fleeced of their corporate family jewels and their value.

---

316. Professor Franklin A. Gevurtz has argued that "if the lock-up is large enough to chase away any higher bidders and pressure shareholders into voting for the transaction simply to avoid triggering the lock-up, then the lock-up gains nothing of value by buying time for the shareholders." Franklin A. Gevurtz, *Removing* Revlon, 70 WASH. & LEE L. REV. 1485, 1508 (2013). Although this argument may be true, if the target has engaged in the type of sale process this Article envisions *and* makes it clear to all potential bidders that there may be certainty in the form of a crown jewel lock-up at the end of the process, there should not be a situation where a higher bidder is deterred; that higher bidder will have already submitted its bid on the front end. Of course, this argument presupposes that the sale process was quite extensive in nature (i.e., that virtually every possible buyer was contacted) and that all bidders were operating with the same information and rules. Hence, the courts would be scrutinizing the sale process and whether the target board and its advisors ran the sale process in good faith.