

M&A NOTES



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Standstill Agreements and Tortious Interference

A Kentucky Federal court recently held that a participant in a competitive auction which failed to comply with the standstill terms of a confidentiality agreement with the target could be held liable to a competing bidder, in tort, for the increase in the purchase price that took place after a “deal jump” on the basis that the deal jumper had failed to abide by the “rules of the game.”

Background

Sunrise Senior Living Real Estate Investment Trust (“Sunrise”) was a Canadian REIT listed on the Toronto Stock Exchange. Sunrise owned and invested in senior living communities in metropolitan markets. In late 2006, the Board of Trustees of Sunrise determined that selling the REIT was in the best interest of the unitholders. A process was established whereby interested parties signed confidentiality and standstill agreements (each a “CSA”) and were then given access to a detailed data room containing confidential information about the REIT.

Ventas Inc. (“Ventas”) and Health Care Property Investors, Inc. (“HCP”) were the final two bidders. Ventas submitted a bid of \$15 per unit; HCP did not submit a bid. The Board of Trustees voted to approve the bid by Ventas and to recommend that the unitholders vote in favor of it. Ventas entered into a purchase agreement (the “Agreement”) with Sunrise, which was publicly announced.

The Agreement included a provision that prohibited Sunrise from amending, modifying or waiving standstill terms in CSAs. Under the Agreement, Sunrise was entitled to consider bona fide unsolicited third party superior proposals.

A month after the announcement of the Agreement and while the Agreement was pending unitholder approval, HCP submitted, and made public, a proposal to acquire Sunrise for \$18 per unit. This violated HCP’s CSA, which prohibited HCP from making acquisition proposals without Sunrise’s written consent. HCP was also restricted from making public disclosure about its intention to make proposals. Additionally, HCP was prohibited from requesting that Sunrise amend or waive its CSA.

The next day, Ventas contacted Sunrise and reminded it that the CSA prohibited Sunrise from talking with HCP. Sunrise told Ventas that it had waived the CSA with HCP, and asked Ventas to confirm that it agreed that Sunrise would not be in breach of the Agreement if discussions occurred with HCP. Ventas did not provide the confirmation and wrote Sunrise demanding that Sunrise comply with the terms of the Agreement that required enforcement of the terms of the HCP CSA.

Ontario Suit

The Ontario court held that covenants requiring Sunrise to enforce confidentiality or standstill obligations and prohibiting amendment or waiver of standstill terms with third parties prevented HCP’s offer from being bona fide. The Agreement contained a fiduciary out that allowed Sunrise to consider bona fide third party proposals, but since HCP’s offer was not bona fide, Sunrise was barred from considering it.

Unitholder Vote

The Agreement was rejected when it was submitted to a vote of the Sunrise unitholders, leading Ventas to increase the purchase price from \$15 per unit to \$16.50 per unit. Following this increase in the offer price the purchase was completed by Ventas.

Kentucky Suit

Ventas sued HCP in Kentucky Federal court, bringing claims of tortious interference with contract and tortious interference with prospective business advantage due to the increase in the purchase price that it paid for Sunrise. HCP filed a motion to dismiss for failure to state a cause of action, which was denied.

The Kentucky court, in a very short opinion, rejected HCP's argument that it was merely acting as a competitor, holding that by failing to abide by the "rules of the game" its actions could be found tortious.

Observations

1. Boards of companies being sold in a multi-bidder process should determine whether they want to retain the right to waive standstill provisions in their confidentiality and standstill agreements with bidders.

If they want that right, it should be made explicit by reserving that right in the purchase agreement, perhaps qualified by a fiduciary duty standard.

2. Retaining the right to waive standstill provisions risks not receiving a bidder's "best and final" offer. After all, bidders may wish to wait to see what the initial "winning" bid is before submitting a subsequent topping bid.
3. A crucial element of the decision in the Ventas case (which involved a motion to dismiss) is the definition of a "bona fide" offer. Bidders should consider requesting that confidentiality and standstill agreements acknowledge that a bona fide offer has been made if it contains certain characteristics (e.g., price, terms, purchase agreement, financing) so as to avoid the problem faced by HCP, where a court determined what constituted a bona fide offer.
4. A bidder may be able to negotiate into the standstill agreement a provision that relieves the bidder of its standstill obligations upon (i) the announcement of a tender offer by a third party for the target's shares or (ii) the entry into a purchase agreement between the target and a third party.
5. If a bidder wishes to make an offer after a sale process has been substantially completed, it should do so before the purchase agreement has been signed. Under those circumstances the seller will not - yet - be obligated to the other bidder to comply with standstill agreements. In this case, it is important that the confidentiality and standstill agreements expressly provide that there are no third party beneficiaries.

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