

ARB ANALYSIS TOM BURNETT, GUEST COLUMNIST

Strategic Acquisitions Financed With Cash Begin to Resemble Private-Equity Deals



Strategic acquisitions financed with cash are increasingly resembling private-equity transactions in delaying deal closings to arrange financing.

This delay is similar to the “marketing periods” that have generally been

provided for in deals with private-equity buyers whose all-cash consideration is dependent upon the receipt of financing. Traditionally, these marketing periods were the exclusive domain of private equity or leveraged buyout firms whose merger consideration was almost exclusively cash.

When **Southern Union Co.** agreed to be acquired by **Energy Transfer Equity LP** on June 15, it set off a bidding war with **Williams Cos.** Eventually, Southern Union and Energy Transfer agreed to improved terms for the merger, including an option for Southern Union shareholders to elect cash merger consideration, subject to proration. That additional option led to the signing of an amended agreement to increase the value of the merger consideration. On Dec. 9, Southern Union shareholders approved the merger, which awaits final regulatory approval with closing expected in the first quarter of 2012.

Delay of 15 Days

Somewhat overlooked among the competing bids for control of Southern Union was a clause that was inserted into the Southern Union-Energy Transfer merger agreement when it was amended to add cash consideration. That provision gave Energy Transfer the option to delay the closing of the merger by 15 business days, if necessary, to “facilitate the financing of the merger.”

Marketing Periods of M&A Transactions

TARGET	BUYER	ANNOUNCEMENT DATE	CLOSING DATE	MARKETING PERIOD TERMS
Paetec Holdings	Windstream	Aug. 1, 2011	Dec. 1, 2011	15 business days
Graham Packaging	Reynolds Group	June 15, 2011	Sept. 9, 2011	10 business days
Nicor Gas	AGL Resources	Dec. 7, 2010	Dec. 12, 2011	20 business days
Southern Union*	Energy Transfer	Jun. 16, 2011	Pending	15 business days
Medco Health*	Express Scripts	July 21, 2011	Pending	20 calendar days
RSC Holdings*	United Rentals	Dec. 16, 2011	Pending	20 calendar days
Complete Production*	Superior Energy	Oct. 11, 2011	Pending	15 business days

Source: Bloomberg, company reports

1. Marketing period provided for in financing agreement, not merger agreement

*Deals followed by Wall Street Access Merger Research

Up to 60 percent of the total Southern Union deal price is to be paid in cash by Energy Transfer, which will require it to raise financing of up to \$3.7 billion. The company has arranged for this financing with **Credit Suisse**, according to a proxy statement. Energy Transfer also has reserved the 15-business-day delay of the closing if it needs more time to finalize the financing.

Financing Flexibility

This example of financing flexibility reflects an increasing trend in larger strategic mergers where cash represents a material portion of the merger consideration. The pending **Express Scripts Inc.** acquisition of **Medco Health Solutions Inc.** is governed by a July 20 merger agreement that contains specific references defining a marketing period prior to which Express Scripts isn't required to close the merger.

In this example, the period is the first consecutive 20-calendar-day period when all Express Scripts conditions to closing have been satisfied. Various holiday periods are defined as being excluded from the 20-day period. In the Express Scripts-Medco proposal, the \$28 cash consideration per Medco share represents about 40 percent of the total consideration, and Express Scripts' pro forma long-term debt will rise from \$3 billion as of Sept. 30 to \$18.7 billion after the closing, assuming Medco is acquired on the currently announced terms. On Aug. 5, Express Scripts entered into a \$14 billion unsecured bridge facility led by **Citibank** to finance the Medco deal, but the merger agreement still gives Express Scripts the marketing period flexibility in the event more time is needed to complete the financing.

A buyer in some cases may use a market-

ing period that loan agreements provide even when the merger agreement doesn't specifically authorize such a delay. For example, in the merger between **Complete Production Services Inc.** and **Superior Energy Services Inc.**, there is no reference to a formal marketing period in the Oct. 9 merger agreement.

In Superior's negotiations with its lenders, however, the financing agreements refer to a “15 business day marketing period,” subject to blackout dates, according to the definitive proxy statement of Jan. 6. That delay may come into play even though Superior closed the \$800 million debt financing on Dec. 6. While this particular marketing period applies only to the \$700 million bridge facility, which is obviated by the completion of the \$800 million financing, Superior did negotiate for this delay with the lenders in case it had required more time to arrange for the bridge facility.

Strategic Transactions

In the accompanying table, we have listed six corporate, strategic transactions where financing-related delays or marketing periods were included in the respective merger agreements. To our knowledge, none of these strategic proposals has been delayed by this marketing period flexibility. Investors should be aware of these clauses in future merger agreements between corporate parties in a strategic transaction.

In the current, Federal Reserve-driven low interest rate environment, deal financing appears to be readily available but, eventually, this low-rate environment will change and interest rates generally will increase. As this “easy money” period disappears, deal financing risks will take a major role in the pricing of merger target company stocks. It is likely that future strategic merger proposals will continue this trend of adding marketing period flexibility to formal merger agreements, and investors should not be surprised if these marketing periods become standard procedures even among strategic, corporate merger proposals.

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Note: Wall Street Access M&A Research is covering the Southern Union-Energy Transfer, Medco-Express Scripts, Complete Production Service-Superior Energy and RSC Holdings-United Rentals mergers.