Security Detail Protects NYSE Deal

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A type of poison pill or just prudent protection?

That is the question some are asking about a side agreement in the deal for a rival to buy the parent of the New York Stock Exchange NYX +2.29% .

When IntercontinentalExchange Inc. ICE +3.17% announced an $8.2 billion deal for NYSE Euronext, observers speculated other suitors could follow due to the exchange industry's recent history—and indeed Warren Buffett's Berkshire Hathaway Inc. BRKB +0.01% already had made a competing preliminary bid.

Softbank Corp. President Masayoshi Son, left, with Dan Hesse, CEO of Sprint Nextel., at the merger announcement last year.

But NYSE and ICE reached a separate, less-talked-about deal for NYSE's European derivatives unit, known as Liffe, to clear its trades through ICE for at least two years, according to people familiar with the contract. The contract stands regardless of whether the merger closes.

That agreement serves the short-term business interests of both companies, analysts say, but it also could ward off other companies thinking of making competing bids for NYSE.

The setup, and others recently like it, could be the latest iteration of what was once known as a "crown-jewel lockup," a frowned-upon mergers-and-acquisitions technique that can thwart competitors from making rival bids that could offer a better deal for shareholders.

"Anybody looking to take over a company that has a longer-term clearing relationship with a competitive clearinghouse will probably think twice," said Alex Kramm, an analyst who covers exchanges for UBS AG, speaking of the side agreement.

People close to NYSE and ICE say the pact wasn't intended to thwart other bidders. But lawyers said it could have that effect, and perhaps prompt imitators. "Even if it wasn't intended to start out, it will end up that way," says Randall Katz, an M&A partner at law firm Baker & Hostetler LLP.

In the most extreme type of crown-jewel lockup, a potential buyer is allowed to purchase a certain desirable asset from the seller if a third-party comes in with a bid. Courts have criticized the technique, which saw its heyday in the 1980s, as bad for shareholders.

The 1985 buyout fight for makeup giant Revlon Inc. REV -6.77% led to a landmark ruling on the subject. Investor Ronald Perelman had made a hostile offer for the company, which instead embraced an offer by Forstmann Little & Co. In the course of a bidding war, Revlon granted

Forstmann Little an option to purchase two divisions for $525 million if Mr. Perelman got a 40% stake.

"The result of the lock-up was not to foster bidding, but to destroy it," Delaware's Supreme Court wrote, blocking the lockup. Mr. Perelman eventually prevailed and took control of Revlon.

Since that period, such lockups have been largely nonexistent. In the past 10 years, data provider FactSet found only one deal with a true crown-jewel lockup and 24 with so-called stock-lockups, in which a buyer gets a chunk of stock in the seller if a third-party makes a bid. Instead, companies largely rely on breakup fees for protection from a failed deal, which courts permit within reason.

Yet, along with NYSE, two other recent deals suggest the concept could be making a comeback in an evolved form.

In Apple Inc.'s AAPL -0.88% $355 million purchase last year of AuthenTec Inc., a maker of fingerprint-authentication sensors, Apple had an option to license AuthenTec's patents—forever, but not exclusively—for $115 million even if it didn't buy the company. That provision provided defense for Apple in case it lost out on the deal, a Wells Fargo WFC -1.52% analyst said at the time. AuthenTec filings show Apple had concerns about other bidders, at one point threatening to pull its offer if AuthenTec shopped itself. The filing also says AuthenTec's board was focused on ensuring the deal terms wouldn't preclude a third-party bidder. The deal closed last year.

In Sprint Nextel Corp.'s S +0.57% announced $20 billion sale to Softbank Corp. 9984.TO -1.66% last year, Softbank paid $3.1 billion for a note that can convert into nearly 20% of Sprint's outstanding shares. The bond was sold as the first stage of Softbank's purchase, but wasn't contingent on the deal going through, giving Softbank a potential edge against any other bidders.

Softbank's note also provided Sprint with funding it has since pledged to purchase the half of wireless-broadband provider Clearwire Corp. CLWR -0.74% it doesn't already own, a person familiar with the deal said.

Court rulings generally say an agreement that makes business sense for the seller, and its shareholders, is allowable, says Harvard Law School professor John C. Coates, a former M&A lawyer. "Delaware law is always a mixture of effects and motives," he said.

Lawyers not involved in the NYSE deal said the side agreement appears to benefit both companies. Clearing Liffe's trades is potentially lucrative for ICE if it loses out on NYSE. The deal also fills a need for NYSE, which was facing the expiration of its contract with another clearinghouse this summer.