Fertilizer Wars and Other Recent Events

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There were some interesting developments this week in the three-way tussle that is CF Industries Holdings’ hostile bid for Terra Industries, and Agrium’s hostile bid for CF Industries.

CF Industries, a big manufacturer of fertilizer products, rejected Agrium’s unsolicited offer on Monday. The letter was short and sweet, calling the offer “grossly inadequate” and “a transparent attempt to interfere with CF Industries’ proposed business combination with Terra.”

CF also responded to Terra’s claims that the CF offer was “illusory” since it required a CF shareholder vote — a vote that Terra claimed would not be affirmative because of the pending Agrium offer. More particularly, in a recent letter to Terra’s shareholders, Terra asserted that:

The [CF offer] is highly conditional, and in light of the Agrium Offer, the stockholders of CF are unlikely to approve CF’s bid for Terra, rendering the [CF offer] illusory and creating significant uncertainty for Terra. The [CF offer] is subject to more than 20 conditions, including limits on market index declines, due diligence and CF stockholder approval. In addition, the existence of the Agrium offer creates substantial doubt that CF will obtain the necessary approval from its stockholders to permit it to consummate any transaction with Terra.

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CF’s response to Terra’s defense is quite interesting.

If CF issues more than 20 percent of its voting stock, N.Y.S.E. Listing Rule 312 requires that it have a shareholder vote to approve the issuance. Previously, CF planned to have such a vote, since it was indeed intending to issue more than 20 percent of its common stock to acquire Terra.

This week, though, CF decided to attack the “illusory” charge head-on and revamp its offer to remove the CF shareholder vote. CF is now offering to issue common shares in an amount up to 19.9 percent of its voting stock. CF would then pay the remaining stock consideration in the form of a participating preferred stock that would trade at parity with CF Industries common stock. The shares would then convert once CF shareholder approval is obtained. In addition, the preferred shares would pay a dividend equivalent to the common that would accumulate whether or not a dividend was paid on the common stock.

So, here’s the question: does this side-step N.Y.S.E. Rule 312? That rule requires that:

(c) Shareholder approval is required prior to the issuance of common stock, or of securities convertible into or exercisable for common stock, in any transaction or series of related transactions if:
(1) the common stock has, or will have upon issuance, voting power equal to or in excess of 20 percent of the voting power outstanding before the issuance of such stock or of securities convertible into or exercisable for common stock [...] 

I believe that CF’s steps are appropriate and do not trigger the rule. The rule is pretty straightforward, and CF is simply taking the position that the stock is not convertible until the vote, and so can be issued now. It is a nice maneuver around the vote issue, but of course, CF’s own shareholders may not be so happy.

Here, just a bit of history. In footnote 18 of Chancellor William T. Allen’s famous opinion in Paramount Communication v. Time Warner, the chancellor clearly states that if the vote requirement is only a N.Y.S.E. requirement, it can be avoided by the company without implicating Delaware law. So, CF is on solid ground to take this tack.

CF has thus attempted to cut off Terra’s “illusory” argument, leaving price once again as the main issue. And of course, there are the other conditions to CF’s offer, particularly the due diligence one. But these are rather standard conditions in a hostile situation, which presumably CF would drop if Terra came to the table. At some point, if Terra decides to deal, it will then have a legitimate basis to question these conditions, but for now they are just formalities.

Meanwhile, Terra again rejected the CF offer again on Wednesday. Terra has also set the record date — the date for determining which of its shareholders can vote at its upcoming annual meeting — as March 9. However, Terra has yet to set the date for nominating directors, or for the meeting itself.

CF, however, could not wait, and filed its proxy statement Thursday for the three directors it intends to nominate. This starts the real battle, as CF attempts to elect a short slate of directors to Terra’s board. Hedge fund shareholder activists have found such a task relatively easy, but the question remains whether the same holds for a pure merger or acquisition. I suspect it will not be so easy, unless the price is appropriate.

CF also has to fight off Agrium. Unless shareholder pressure comes to bear, though, this will be a relatively easy task. Agrium has threatened to launch an exchange offer, but since it missed the nominating deadline for a contest to elect CF directors, the exchange offer is hollow. This is because CF has a poison pill, and Agrium cannot close the offer until the board agrees.

In this light, Agrium’s announcement of its hostile bid, only weeks after the nomination deadline, seems increasingly inexplicable. It lost its only real bargaining chip, except, as with CF itself, for price.

Life Sciences Research Inc.

Earlier this month, Life Sciences Research disclosed that its chairman and chief executive officer, Andrew Baker, made a proposal to acquire Life Sciences for $7.50 per share, or roughly
$100 million. Mr. Baker owns 17.5 percent of Life Sciences. Life Sciences also announced that it had formed an independent committee to consider the proposal.

The independent committee would do well to review the debacle at Landry’s Restaurants before acting or negotiating with Mr. Baker. (For more on Landry’s, see this post). Small-cap companies are particularly vulnerable to management buyouts, both in pricing and deal terms, which can leave them alone at the altar. This is because a failure to deal with management without a competing bid means that you are effectively firing them.

The fact that Mr. Baker — who is C.E.O. of his company — included a due diligence condition in his letter (and didn’t link it merely to financing) isn’t a heartening start. Remember, he is the chief executive: Why does he need due diligence? He also put in a financing condition. Expect to see more of these management buyouts pop up as pricing remains distressed. And to give Mr. Baker the benefit of the doubt, maybe he is simply trying to start an auction. Though after the debacles in Landry’s, CKX and Zones — three management buyouts from last year that failed miserably as management attempted to give themselves an advantage at their shareholders expense — I am skeptical.

Bebchuk v. Electronic Arts

Together with a number of other law professors, I am party to a recently filed amicus brief organized by Professor Jeff Gordon at Columbia Law School in the case of Lucian Bebchuk v. Electronic Arts. The case is now pending before the United States Appeals Court for the Second Circuit. In the words of Prof. Gordon:

The case focuses on a shareholder proposal that was submitted by Lucian Bebchuk to Electronic Arts (EA). The proposal is precatory and recommends that the board submit to a shareholder vote a charter or bylaw amendment that, if adopted, would require the company (to the extent permitted by law) to include in the company’s proxy materials qualified proposals for a bylaw amendment. For a proposal to be qualified, the proposal would have to meet certain significant requirements, including being submitted by a shareholder(s) with more than 5% of the company’s stock. The proposal is available here.

The issue is whether this is a valid proposal under Exchange Act Rule 14a-8 and E.A., is thus not allowed to be excluded from the proxy statement. For more information, including the brief, see Prof. Gordon’s posting on the Harvard Law School Corporate Governance Forum.