FOLEY

FOLEY & LARDNER LLP

Board Considerations in Going Private or Going Dark

2007 NATIONAL DIRECTORS INSTITUTE

©2007 Foley & Lardner LLP • Attorney Advertising • Prior results do not guarantee a similar outcome • 321 N. Clark Street, Suite 2800, Chicago, IL 60610 • 312.832.4500 • 07.3193

BOARD CONSIDERATIONS IN GOING PRIVATE OR GOING DARK

Given the heightened disclosure requirements and costs associated with being a public company in today's environment, public companies are increasingly "going private," often with private equity firms or other financial buyers as the acquiror, to better position themselves to create shareholder value. While these transactions are typically heavily scrutinized by the SEC and shareholders, and often result in minority shareholder litigation, going private is increasingly seen as a viable alternative to selling to a strategic partner or recapitalizing.

At Foley's sixth annual National Directors Institute on March 8, 2007 in Chicago, Pete Underwood, partner, Foley & Lardner, moderated a featured session entitled "Board Considerations in Going Private or Going Dark" to address these issues. Other panelists included Cary Kochman, managing director, UBS Investment Bank; Edward Pendergast, president, Pendergast & Company; James Reddinger, executive director, UBS Securities LLC; and Mark Tresnowski, managing director and general counsel, Madison Dearborn Partners, LLC.

Going Private

"Going private" is a term often used to refer to the acquisition of a public company by a significant shareholder, management or the board of directors that is subject to the "13e-3" regulations of the SEC. However, with the recent increased acquisition activity of private equity firms and other financial buyers in the public company world, the term is increasingly being used to describe any acquisition of a public company by a private buyer, whether or not the 13e-3 rules are implicated. While several of the topics discussed during the breakout session are applicable in both the 13e-3 context and the broader acquisition context, the panelists focused their attention largely on the broader view of the term.

The State of the Going Private Market

Approximately 20% of all recent merger and acquisition activity was attributable to leveraged/management buyout transactions. Hedge funds and private equity firms continue to raise billions of dollars in new capital and there is intense competition among these firms and strategic investors for investments generally, which is helping to fuel the interest of those firms in pursuing public company transactions. Given the relatively low cost of capital for these financial buyers, they are uniquely positioned to outbid strategic investors for public companies. According to Mr. Tresnowski, private equity firms are generally reviewing a far greater number of public company acquisition candidates than in the recent past, in part because the market is increasingly viewing going private as a viable strategic alternative for public companies.

The future of the going private market, however, remains unclear. While there is no apparent imminent downturn in the market, in the face of increasing interest rates, hedge funds and private equity firms may be unable to obtain low cost financing to effectively compete with strategic investors.

Why Companies Go Private

The panelists noted the following factors that drive a public company to go private:

- Impact of increasing costs related to the Sarbanes-Oxley Act (SOX), although the panelists agreed that this was not the sole impetus for going private as many hedge funds and private equity firms still require the companies that they purchase to comply with SOX
- The belief by the chief executive officer and/or the board of the public company that the company's stock is undervalued in the public market
- Decreased coverage of middle market public companies by analysts and a public company's inability to convey its message to the public
- Reluctance by named executive officers and board of directors to comply with new and extremely personal compensation disclosure requirements of the SEC
- Increasing market acceptance of going private transactions as commonplace — fueling the perception in the boardroom that going private is a viable strategic alternative

Process of Going Private

Increasingly, going private transactions are conducted through an auction process, in part, so boards of directors can ensure that they fulfill their fiduciary duties. While there is no systematic approach to beginning a going private transaction, the panelists agreed that cynicism surrounded the process when a chief executive officer brought either a LBO transaction or a specific third party buyer to the board of directors for consideration. A chief executive officer should distance himself or herself from any particular third party buyer, especially in an auction context, or else risk being excluded from important boardroom discussions at a crucial period of the company's development. It is critical that directors who may be involved in the transaction "on both sides" not be involved in the negotiations or approval of the going private transaction. In this context, the board should form a special committee, if appropriate, that is properly empowered to negotiate the transaction and ensure the terms are in the best interests of the minority shareholders.

Mr. Kochman noted the recent increase in transactions containing "go shop" provisions which allow a target company's board of directors a limited period of time following execution of definitive acquisition documents to seek alternative bidders. This trend is expected to continue with respect to going private transactions in the current market.

Fiduciary Duties of the Board

A going private transaction is typically subject to a stricter "entire fairness" standard of judicial review, rather than the more lenient business judgment rule. In this circumstance, the board usually has the burden of proving that the transaction was entirely fair to the unaffiliated shareholders. Courts have scrutinized both the process and the price surrounding these types transaction to make this determination. However, the target company board can, in many circumstances, utilize procedural protections, such as a properly empowered and functioning special committee of independent directors, or a

©2007 Foley & Lardner LLP

"majority of the minority" voting approval condition, in order to shift the burden of proof of fairness onto the plaintiff.

The panelists discussed these procedural protections and generally agreed that boards should be encouraged to establish an independent special committee to negotiate and approve any going private transaction or obtain the vote of a majority of the disinterested stockholders. In addition, the panelists stressed the importance of obtaining experienced legal, accounting and financial guidance for the company, the board and/or any special committee. Legal counsel, the board, the special committee and any other interested parties should ensure that each meeting where the going private transaction is discussed is thoroughly documented so that the information is available to substantiate the procedural fairness of the transaction.

In order to assist in supporting the board's conclusion that the price in a going private transaction is "fair," the panelists suggested that boards of directors consider obtaining a fairness opinion from a reputable investment bank. While the fairness opinion would not alleviate a board's potential liability under a fraudulent conveyance scenario or insolvency situation, a fairness opinion could provide the board with comfort that the company is obtaining a fair price for the minority stockholders.

For More Information

For more information on this session or the sixth annual National Directors Institute, visit Foley.com/ndi2007 or contact the panelists directly.

Cary A. Kochman
UBS Investment Bank
cary.kochman@ubs.com

Edward Pendergast
Pendergast & Company
ed@pendergastco.com

James Reddinger
UBS Securities LLC
james.reddinger@ubs.com

Mark Tresnowski
Madison Dearborn Partners, LLC
mtresnowski@mdcp.com

Peter Underwood
Foley & Lardner LLP
punderwood@foley.com

2007 National Directors Institute Sponsors

Foley proudly recognizes the 2007 National Directors Institute sponsors: UBS, Aon, Korn/Ferry International, Deloitte, RR Donnelley, D. F. King, Ashton Partners, Boardroom Bound, Chicagoland Chamber of Commerce, NASDAQ, NYSE and Springboard Enterprises. The support we receive from our sponsors is crucial to the development of the program and we thank them for their efforts in once again making NDI a huge success.

Save the date! The 7th Annual National Directors Institute will be held on March 6, 2008 in Chicago. Learn more at Foley.com/ndi.