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Formula Pricing: “Day 20” Pricing Has Finally Arrived for Debt Tender Offers!

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Late last year, at a time when few were paying attention, the SEC’s Office of Mergers & Acquisitions granted no-action relief to Thermo Fisher Scientific permitting the company to make a tender offer for its outstanding convertible debt securities without having to fix the exact consideration offered until the very *last* day of the offer.¹ In granting relief to Thermo Fisher, one of the primary factors the Staff relied upon, among others, was the company’s representation that there was a very strong correlation between the value of the convertible debt securities sought in the offer and the trading price of the common stock underlying the convertible securities.

To appreciate how far the Staff has come in this recent letter, one need only look back to 1995 when the Staff granted Lazard Freres relief in one of the first no-action letters permitting bidders to use a formula pricing mechanism to determine the offer consideration.² In the *Lazard* no-action letter, the Staff permitted acquirors in business combination transactions to make exchange offers using an exchange ratio based on the average trading prices of the stock offered over a specified period of time, so long as the issuer adequately disclosed the pricing mechanism in its offering documents, provided a “toll-free” number for security holders to call to obtain daily updates regarding the exchange ratio and issued a press release at least *two* full trading days prior to expiration announcing the final exchange ratio. In submitting the request, counsel noted that the formula for determining the consideration was “fixed” from the outset of the offer and a “collar” would be imposed such that the final exchange ratio would not be less than a specified minimum amount or greater than a specified maximum amount.

The Staff accepted counsel’s arguments in *Lazard* that the use of such a formula pricing mechanism would allow the parties to achieve a result that more accurately reflected the objectives of both sides in the transaction. But the Staff has historically held firm in its view that there should be at least two trading days between the date the final exchange ratio is announced and the expiration of the tender offer. The purpose of this two-day period is to give investors adequate time to consider the final terms of the offer and make an informed investment decision. This approach is often referred to as “Day 18” pricing.³

Now, almost 15 years after later, we live in a very different world, where advanced computer technology, the internet and e-mail have become commonplace and the speed with which information is made available to investors and exchanged between market participants is virtually instantaneous. Recognizing these changes, the Staff saw fit to grant the requested relief to Thermo Fisher permitting disclosure of the final offer price by press release no later than 4:30 p.m. on the *last* business day of the tender offer.⁴ This approach of setting the offer price on the last day of the offer is now referred to as “Day 20” pricing.

For those of us who have done more tender offers than we care to count, this development should come as no surprise. It was only a matter of time before the Staff would come to recognize the effect that these changes have had on our markets. For example, in recent years the Staff has become more flexible in other tender offer contexts and granted relief from Rule 14e-1(b), and the corresponding provision in Rule 13e-4(f)(1)(ii), the rules requiring an offer to remain open for at least 10 business days following the announcement of a change in price or consideration offered. To date, however, such relief was generally limited to transactions such as spin-offs, exchange offers and merger transactions, situations more akin to the facts presented in the *Lazard* no-action letter.⁵

In several of these prior no-action letters (outside the issuer debt tender offer context), the offeror capped or limited the maximum number of shares issuable in the transaction. If the pricing mechanism was scheduled to run through Day 20 and the consideration resulting from the formula pricing mechanism exceeded the self-imposed cap, the SEC required the offerors to extend the offer period for up to two business days so that investors could receive and analyze the new information before having to make an investment decision.

In *Thermo Fisher*, the issuer was offering to buy back its own securities (convertible debt) and the consideration offered was all cash. Under the terms of Thermo Fisher's offer a VWAP (volume-weighted average pricing) mechanism was applied through the expiration of the offer (the 20th business day), and a floor price was disclosed at the outset in the offering documents. The self-imposed, fixed minimum price payable (regardless of the application of the VWAP pricing mechanism) gave the Staff some comfort that investors would at least know the minimum price they would receive in the offer.⁶ As such, the SEC Staff did not believe it would be necessary to require the offeror to extend the offer period by up to two business days in the event the formula price fluctuated during the last few days of the offer.

Significant weight was placed on the fact that there: (i) was a high correlation between the price of the underlying common stock (traded on the NYSE) and the trading price of the issuer's convertible debt; (ii) has been an increased use of the internet and other electronic means enabling investors to obtain current pricing information and (iii) was a "floor price" imposed on the consideration offered. Counsel to Thermo Fisher also pointed out that imposing 18-day pricing in such circumstances could very well result in investors missing out on any potential increase in the consideration that might result if the pricing mechanism was not permitted to continue running through to the very last day of the offer.

Thus, *Thermo Fisher* brings us yet another step closer to a more modern application of the SEC's tender offer rules—allowing issuers to apply "real-time" formula pricing in their debt tender offers.

¹ SEC No-Action Letter, *Thermo Scientific Inc.* (available November 13, 2009).

² SEC No-Action Letter, *Lazard Freres & Co.* (available August 11, 1995).

³ Absent relief, Rules 14e-1(b) and 13e-4(f)(1)(ii) of the Exchange Act of 1934 would require the tender offer to remain open for a minimum period of ten business days following the announcement of a change in the consideration offered.

⁴ Thermo Fisher's offer was scheduled to remain open until midnight on the 20th business day, leaving security holders several hours to obtain the pricing information and make an investment decision of whether to tender or not.

⁵ See e.g., SEC No-Action Letters issued to: *Kraft Foods Inc.* (available July 1, 2008), *Halliburton Company* (available March 23, 2007), *Weyerhaeuser Company* (available February 23, 2007), *McDonald's Corporation* (available September 27, 2006) and *TXU Corp.* (available September 13, 2004).

⁶ This floor price in the offer is analogous to the minimum offer price found in modified Dutch auction tender offers.