Liability Management

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Supplemental Materials

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Top 10 Practice Tips: Debt Tender Offers

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The following 10 practice points are intended to help you in assisting an issuer with a proposed debt tender offer for cash. Often, issuers of debt securities seek to manage their liabilities through liability management transactions, including debt tender offers for cash. A cash tender offer consists of a public offer by the issuer to purchase all or a portion of the outstanding principal amount of the relevant debt securities from the holders at a price, and subject to conditions, set forth in the issuer's offer to purchase.

1. Consider whether the issuer has enough cash and whether there are more effective liability management alternatives.

Prior to undertaking a debt tender offer for cash, an issuer will need to determine whether it has sufficient cash on hand to effect the repurchases. If an issuer does not have enough cash on hand or views the use of cash to effect a tender offer as an inefficient alternative under the circumstances, the issuer may consider a liability management transaction that does not require deploying cash, such as an exchange offer. In an exchange offer, the issuer offers to exchange new debt securities for certain of its outstanding debt securities. This approach would allow the issuer to achieve a similar result as a debt tender offer by purchasing its outstanding debt securities for non-cash consideration in the form of new securities, thereby obviating the need to deploy cash.

2. Determine whether the class of debt securities is widely held.

In connection with choosing the appropriate liability management approach, the issuer should consider whether the debt securities are widely held as well as the status (retail versus institutional) and location of the holders. If the debt securities are widely held, privately negotiated or open market purchases may not be efficient for an issuer. In such a situation, a tender offer may be the best way to restructure the issuer's indebtedness. A tender offer allows an issuer to approach or make an offer to all of the holders of a series of its debt securities. Because tender offers do not have to close until specified (and disclosed) conditions are satisfied (including, in some cases, receipt of consents from debt holders to modify the terms of the debt securities that remain outstanding, completion of any necessary financing for the tender offer and receipt of other necessary consents from third parties), it may be possible to conduct a tender offer and achieve the issuer's objectives.

3. Consider whether the tender offer rules would apply.

A key consideration in formulating a liability management strategy is the extent to which the Securities and Exchange Commission's (SEC) tender offer rules apply to the contemplated transaction, given that these rules affect the manner in which the transaction must be conducted. The tender offer rules can apply when a company is offering securities and/or cash for its outstanding securities, and the level of regulation of the offer (in terms of timing and mandated procedural protections) varies depending on the type of security that is the subject of the offer and whether certain conditions necessary for an abbreviated process are satisfied.

An issuer repurchasing its debt securities, either in privately negotiated transactions or in open market purchases runs the risk that it may inadvertently trigger the SEC's tender offer rules. The term "tender offer" is not specifically defined in statute or in the SEC's regulations. The lack of a specific definition has permitted the SEC and the courts to apply the tender offer rules to a broad range of transactions. Any analysis of whether an offer constitutes a tender offer begins with the often-cited eight-factor test in the Wellman v Dickinson case:

- An active and widespread solicitation of public shareholders for the shares of an issuer.
- A solicitation made for a substantial percentage of the issuer's securities.
- The offer to purchase is made at a premium over the prevailing market price.
- The terms of the offer are firm rather than negotiable.
- The offer is contingent on the tender of a fixed number of shares, often subject to a fixed maximum number to be purchased.
- The offer is open only for a limited period of time.
- The offeree is subjected to pressure to sell his or her security.
- Public announcements of a purchasing program concerning the target issuer precede or accompany a rapid accumulation of large amounts of the target issuer's securities.

These eight factors need not all be present for a transaction to be deemed a tender offer, and the weight given to each element varies based on the facts and circumstances.

Courts have also applied a totality-of-the-circumstances test in determining whether a transaction involves a tender offer that should be subject to the statutory requirements and the SEC's rules. In this context, the courts have examined whether, in the absence of disclosure and procedures required under the tender offer rules, there will be a substantial risk that the offeree lacks the information needed to make an investment decision with respect to the offer. The SEC staff has historically focused on whether a tender offer involves an investment decision on the part of the offeree, particularly where the protections afforded by the tender offer requirements would appear to be necessary based on the nature of the transaction.

For debt repurchases, it is generally possible to structure repurchases in order to avoid the application of these rules. To the extent that an issuer would prefer to avoid the application of the tender offer rules, any repurchase should:

- Be undertaken for a limited amount of securities
- Made to a limited number of holders who are sophisticated
- Not specify a time period or expiration time for the offer
- Be made at prices that are privately and individually negotiated (i.e., the same terms should not be imposed on all offerees) -and-
- Not be conditioned on the issuer having attained a specific principal amount

4. Determine whether the target class of debt securities is nonconvertible.

The issuer's structuring options also will depend, in part, on the characteristics of the outstanding security. A repurchase or tender for straight debt securities typically will be less complex than a repurchase or tender relating to convertible debt securities. This is because convertible debt securities are treated like equity securities for purposes of the tender offer rules. Specifically, in connection with tenders for convertible debt securities, issuers must comply with the requirements of Rule 13e-4. The obligation to comply with these provisions makes tender offers for convertible or exchangeable debt securities more complicated and time consuming, and subject the offer to SEC review, which could result in time delays.

In addition, the requirements of Rule 13e-4 result in less flexibility for tenders for convertible or exchangeable debt securities compared to tenders for straight debt securities. A good illustration of this reduced flexibility is that it is not possible for issuers to sweeten the tender offer for convertible or exchangeable debt securities with an early tender premium as would be possible for straight debt securities.

There also may be some accounting issues in connection with repurchasing or tendering for convertible or exchangeable debt securities. While some effects (such as the elimination of the retired debt from the issuer's balance sheet) may be more intuitive, others may not be. Issuers may wish to consult their accountants early in the process. Issuers that intend to restructure their outstanding convertible debt also should consider the effects of such tender on any of their related call spread transactions or share lending agreements.

Finally, under certain circumstances, repurchases of convertible debt securities could be deemed a forced conversion and, therefore a distribution of the underlying equity security for purposes of Regulation M. Therefore, it is important to identify early on whether the subject debt securities are convertible debt securities and to structure the tender offer accordingly.

5. Determine whether the conditions for the abbreviated tender process apply.

In January 2015, the Staff of the SEC issued a no-action letter indicating that it would not recommend enforcement action in connection with a tender offer or exchange offer for nonconvertible debt securities that is held open for as few as five business days, to the extent that the offer is conducted in accordance with the following significant conditions (among others):

- The offer must be structured as an any and all offer, but, may include a minimum tender condition.
- The offer must be made by the issuer of the debt securities or a parent or a wholly owned subsidiary of the issuer (i.e., third parties tendering for debt securities of an issuer will not be permitted to avail themselves of the shortened tender period).
- The offer must be open to all record and beneficial holders of the targeted debt securities.
- The offer must be made solely for cash or other qualified debt securities, which term is defined as securities that are materially identical to the securities that are the subject of the tender offer.
- The consideration offered in the tender offer must be fixed or based on a benchmark spread (e.g., U.S. Treasury rates, LIBOR or swap rates).
- The offer cannot be combined with an exit consent to amend or eliminate covenants or with any other consent solicitation to amend the provisions of the indenture or the debt securities.
- Holders must be entitled to withdrawal rights until the earlier of the expiration date and, if the offer is extended, the tenth business day following the launch. Holders also must be allowed to withdraw tenders after the 60th business day following the launch if the offer has not been consummated by such time.
- The offer must permit tenders prior to the expiration time through guaranteed delivery procedures.

The no-action relief is not available for partial tenders or for tenders or exchanges with exit consents. In addition, the relief is not available:

- If there exists a default or event of default under the relevant indenture, or under any other indenture or material credit agreement to which the issuer is a party
- At a time when the issuer is the subject of bankruptcy or insolvency proceedings, or otherwise has commenced activity geared toward accomplishing an out-of-court restructuring or pre-packaged bankruptcy
- In anticipation of, or in response to, or concurrently with, a change of control or other extraordinary transaction involving the issuer, such as a merger, business combination, or sale of all or substantially all of the issuer's assets
- In anticipation of, or in response to, a competing tender offer; concurrently with a tender offer for any other series of the issuer's securities made by the issuer or certain affiliates of the issuer if the effect of such offer would result in a change to the capital structure of the issuer (e.g., addition of obligors or collateral, increased priority of liens or shortened weighted average life to maturity of such other series) -or-
- In connection with a material acquisition or disposition that would require the furnishing of pro forma financial information with respect to the transaction pursuant to Article 11 of Regulation S-X (whether or not the issuer is an SEC-reporting company)

Finally, counsel should be aware that any investment grade tender offer that does not qualify for the abbreviated tender offer no-action relief will be subject to the 10 and 20-day period requirements under the tender offer rules.

6. Familiarize yourself with the various pricing methodologies that are used for tender offers.

There are several pricing mechanisms that an issuer can use to determine the consideration that it will pay holders to tender their securities. For instance, in order to limit exposure to interest rate fluctuations, issuers may choose fixed spread pricing. Fixed spread pricing permits an issuer/offeror to choose a specific yield spread between the debt being tendered for and a benchmark U.S. Treasury security, which matures at or near the earliest redemption date for such debt security. The purchase price is calculated as the present value of the security subject to the tender offer, discounted at an interest rate equal to the applicable spread. While the actual price to be paid in the tender offer is not fixed at the commencement of the offer, the formula for determining the price is fixed. The greater the spread, the higher the discount rate, resulting in a lower present value and purchase price.

In addition, in a tender offer for nonconvertible debt, an issuer has the flexibility to choose to accept tenders of securities on a first-come, first-served basis, or offer limited or no withdrawal rights, or conduct a Dutch auction or modified Dutch auction for pricing purposes. In a Dutch auction, a holder submits a bid at a specified price which the issuer can accept or reject.

7. Consult with the issuer about retaining a dealer-manager.

Generally, the more complex and significant a restructuring, the more helpful it may be to engage an investment bank as financial adviser. The investment bank will help formulate a plan, locate and identify security holders, structure the transaction, solicit participation, assist with presenting the structure to the various stakeholders, assist with rating agency discussions and manage the marketing efforts in order to achieve a successful restructuring. Issuers should consider a number of factors, such as the number of debt holders, their sophistication, and whether the issuer has information about, and any contact with, the debt holders.

The investment bank's role varies in liability management transactions. In a cash tender offer for nonconvertible debt, an issuer may engage an investment bank in an advisory role. In a tender offer for convertible debt securities, which is subject to additional tender offer rules, an issuer may choose to engage an investment bank in an advisory role in order to contact and negotiate the terms with debt holders or to act as an active dealer-manager. In a tender offer coupled with a consent solicitation or a public tender offer for all outstanding debt securities, an issuer usually engages a dealer-manager to manage the entire process. In these transactions, issuers also often use a professional services firm to act as information agent during the process. There are no specific rules regarding compensation preventing issuers from using—and paying—an investment bank to solicit tenders.

8. Understand the principal negotiating issues arising in connection with the dealer-manager agreement.

The issuer will engage the dealer-manager pursuant to the terms of a dealer-manager agreement. The dealer-manager agreement may be the only agreement between the issuer and the investment bank, or it may supersede an engagement letter relating to the mandate. Usually, the dealer-manager's counsel will prepare the draft agreement, which will detail the dealer-manager's obligations in respect of the transaction and set out the agreement relating to the fees payable to the dealer-manager. The issuer will make representations and warranties to the dealer-manager related to the offer to purchase and other offer materials used in connection with the tender, as well as make representations regarding receipt of all necessary authorizations (if any), corporate approvals, and make other representations comparable to those found in an underwriting agreement. Generally, the dealer-manager agreement will be executed just prior to commencement of the offer. Usually the agreement will require that certain documents, including officers' certificates and legal opinions, be delivered to the dealer-manager at various junctures during the tender offer period.

9. Familiarize yourself with other securities disclosure requirements applicable to debt tender offers.

Section 14(e) of the Securities Exchange Act is an antifraud provision that establishes the baseline for tender offer regulation. It prohibits an offeror from making any untrue statement of a material fact, or omitting to state a material fact necessary in order to make the statements made, in light of the circumstances in which they were made, not misleading. Section 14(e) also prohibits any fraudulent, deceptive or manipulative acts in connection with a tender offer, and applies to cash tender offers, as well as to exchange offers subject to the tender offer requirements.

Under Regulation 14E, an issuer is not required to file any tender offer documents with the SEC, and Regulation 14E does not prescribe any form requirements with respect to offering materials. Any offer to purchase, or other tender offer documentation, is subject, however, to the general antifraud provisions of the Exchange Act, notably section 10(b), Rule 10b-5 and section 14(e), and, therefore, may not contain any material misstatement or omission. Some courts have found that section 14(e) does not impose a scienter requirement (like Rule 10b-5), because, among other things, section 14(e) prohibits 'any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender

offer' in addition to a Rule 10b-5 scienter-based approach that forms part of the first clause in section 14(e). For example, the Ninth Circuit recently held that section 14(e) requires only a showing of negligence, without a showing of scienter, to bring a case in connection with alleged misstatements or omissions in connection with a tender offer.

10. Determine whether there are any tax consequences for holders.

Tax issues can be an important consideration in any liability management transaction. Even with sound tax advice certain tax consequences are inescapable and must be carefully considered. For instance, corporations with outstanding debt may be subject to tax on cancellation-of-indebtedness (COD) income when all or a portion of such debt has been economically cancelled. COD income can arise in a number of circumstances, including forgiveness of debt by the debt holder, the repurchase of debt by the issuer at a discount, the exchange of one debt instrument of the issuer for another, the modification of debt and the exchange of debt for equity of the issuer. Additionally, repurchases or exchanges by persons related to the issuer can create COD income. Section 108(a) of the Internal Revenue Code provides a number of exceptions to the inclusion of COD income, including exceptions related to insolvency and bankruptcy.

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Managing Your Balance Sheet

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Choosing the right liability management alternative to restructure or retire outstanding debt securities or to manage risk and reduce funding costs may depend on a number of factors. Below we summarize the principal considerations for issuers.

	Benefits	Consideration
Redemptions	• Efficiency (no registration required, no documentation needed) • Flexible (may redeem all or part of an outstanding class of debt securities)	• Requires deploying cash on hand • Expensive (redemption price usually preserves yield to maturity) • Notice generally must be outstanding between 30 and 60 days (rates may fluctuate during the time period)
Repurchases	• Efficiency (no registration required and no documentation needed) • Privately negotiated • Pricing takes advantage of market fluctuations • Less transparency • For financial institutions, may help improve Tier 1 regulatory capital position • May be part of an ongoing repurchase program	• Requires deploying cash on hand • May result in retiring only a small percentage of securities from a limited number of holders • May require public disclosure • May trigger the application of the tender offer rules
Debt Tenders	• Efficiency (no registration required and not subject to SEC review, unless the securities are convertible debt) • Flexible (able to retire an entire series or class of debt securities) • Able to approach all holders (subject to compliance with applicable tender offer rules) • May engage investment bank to undertake the tender • Can be paired with a consent solicitation	• Requires deploying cash on hand • If subject to the tender offer rules, debt tenders must be held open for a specified time period and be in compliance with other conditions • Holdout issue • Convertible debt tenders generally are subject to the tender rules for equity securities • Must pay all investors of the same class the same price (if subject to the tender offer rules)
Private exchange offer	• Efficiency (no registration required and not subject to SEC review, unless convertible debt) • Does not require deploying cash on hand • Flexible (able to retire an entire series or class of debt securities) • May engage investment bank to solicit • Able to pre-certify investor status • No section 11 liability in respect of offering memorandum • Can be paired with a consent solicitation • Often can be accomplished on a tax- free basis for debt holders	• Generally limited to QIBs • Holdout issue • The new securities issued in the exchange may be restricted securities (but holder may be able to tack its holding period from the original issue date of the tendered security) • Holders may request registration of the resale of the new securities

	Benefits	Consideration
Debt Tenders	• Efficiency (no registration required and not subject to SEC review, unless the securities are convertible debt) • Flexible (able to retire an entire series or class of debt securities) • Able to approach all holders (subject to compliance with applicable tender offer rules) • May engage investment bank to undertake the tender • Can be paired with a consent solicitation	• Requires deploying cash on hand • If subject to the tender offer rules, debt tenders must be held open for a specified time period and be in compliance with other conditions. • Holdout issue • Convertible debt tenders generally are subject to the tender rules for equity securities • Must pay all investors of the same class the same price (if subject to the tender offer rules)
Private exchange offer	• Efficiency (no registration required and not subject to SEC review, unless convertible debt) • Does not require deploying cash on hand • Flexible (able to retire an entire series or class of debt securities) • May engage investment bank to solicit • Able to pre-certify investor status • No section 11 liability in respect of offering memorandum • Can be paired with a consent solicitation • Often can be accomplished on a tax- free basis for debt holders	• Generally limited to QIBs • Holdout issue • The new securities issued in the exchange may be restricted securities (but holder may be able to tack its holding period from the original issue date of the tendered security) • Holders may request registration of the resale of the new securities
3(a)(9) exchange offer	• Efficiency (no registration required and not subject to SEC review) • Flexible (able to retire an entire series or class of debt securities) • Does not require deploying cash on hand (only minimal costs) • Able to approach all holders (subject to compliance with applicable tender offer rules) • No section 11 liability with regard to offering memorandum • Can be paired with a consent solicitation • Often can be accomplished on a tax-free basis for debt holders	• New securities may be restricted securities (but holder may be able to tack its holding period) • Limited ability to engage and compensate an investment bank for solicitation • Holdout issue • May be integrated with other offers made in close proximity to the exchange offer • Must pay all investors of the same class the same price (if subject to the tender offer rules)
Registered exchange offer	• Efficiency (able to retire an entire series or class of debt securities) • Does not require deploying cash on hand • New securities are freely transferable • May engage an investment bank to solicit exchanges; no restrictions on compensation to the investment bank • Able to approach all holders (subject to compliance with the tender offer rules) • Can be paired with a consent solicitation • Often can be accomplished on a tax-free basis for debt holders	• Time consuming (subject to SEC review and filing requirements) • Generally must remain open for 20 business days (if subject to the tender offer rules) • Section 11 liability • Holdout issue • Must pay all investors of the same class the same price (if subject to the tender offer rules)

Managing Your Balance Sheet

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	Benefits	Consideration
Debt for equity exchanges	• Often used by issuers under distressed conditions or even as an alternative to bankruptcy because of upside potential for investors • Improves the issuer's debt-to-equity ratio, also potentially improving the issuer's credit ratings • Does not require deploying cash on hand (only minimal costs) • Can be paired with a consent solicitation • Often can be accomplished on a tax-free basis for debt holders	• If registered, can be time consuming (subject to SEC review and filing requirements) • Must remain open for a specified time period if subject to the tender offer rules • Equity issuance may trigger securities exchange issuance limitations or shareholder vote requirement • Terms of equity securities may be onerous • Must pay all holders of the same class the same price (if subject to the tender offer rules)
Equity for equity exchanges	• Does not require deploying cash on hand • Terms of new securities may be less onerous • Generally a tax-free transaction • Able to approach all holders subject to compliance with the tender offer rules	• Must be permitted under state law • If registered, can be time consuming (subject to SEC review and filing requirements) • Must remain open for a specified time period if subject to the tender offer rules • No balance sheet impact • •Must pay all holders of the same class the same price (if subject to the tender offer rules)
Consent solicitation	• May be undertaken alone or paired with a tender offer or exchange offer; however, SEC guidance does not permit exit consents to be solicited in connection with expedited tenders • Allows the issuer to modify onerous or restrictive covenants • Not subject to SEC review or to the tender offer rules • No section 11 liability • Does not require deploying cash on hand (only minimal costs) • Generally tax-free unless considered a significant modification of the outstanding debt securities	• May require a supermajority to enact modifications • The Trust Indenture Act does not permit modification of interest, principal, maturity and other provisions without 100% approval; TIA provisions may serve to limit certain amendments that deprive holders of a right to a source of payment • Modifications may result in the remaining securities being considered "new" for Securities Act purposes • Holdout issue

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Stock Repurchase Alternatives for Issuers

The following chart compares and contrasts in summary form the characteristics associated with alternative issuer stock repurchase approaches.

	OPEN MARKET REPURCHASES	PREPAID/ACCELERATED SHARE REPURCHASE	TENDER OFFER
ADVANTAGES	• Continued stock support • "At-market" repurchase • Maximum flexibility • Lowest cost • Can be executed through a Rule 10b5-1 program	• Optional upfront share count reduction • "At-market" repurchase • Potential tax efficiencies • Strong signal • Economic protection/discount available	• Speed of repurchase completion near current valuation • Strongest signal • Liquidity event for investors • Rapid share count reduction
DISADVANTAGES	• Limited by daily volume • Exposed to market price over time • Share count reduction over time • Weaker signal • No guarantee of completion	• Exposed to market price over time • Fully funded upfront • Commits issuer to complete repurchases	• Requires premium to current price • Investors determine success of tender offer • Higher transaction costs • No ongoing stock support
MECHANICS	• Issuer purchases shares in the open market over time • Can buy back stock during blackout period through a Rule 10b5-1 plan	• Broker sells the block to issuer upfront • Broker repurchases stock in the open market over time • True up payment and/or additional shares delivered at completion of cover period	• Issuer specifies a number of shares to be repurchased within a defined price range or at specific fixed price • Shareholders decide whether they would like to participated in the offer • Tender offer open for a minimum of 20 days
DOCUMENTATION	• Short form appointment letter for a repurchase broker • No public documentation	• Master confirmation • No public documentation	• Schedule Tender Offer filed with SEC
APPLICATIONS	• Desire to maintain flexibility including ability to stop	• Minimum value of shares issuer desires to purchase	• Repurchase large block of stock in a short period of time

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