

**King Pharmaceutical's Acquisition of Alharma:
A Tough Deal in Tough Times**

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On December 29, 2008, King Pharmaceuticals Inc. (King) completed its \$1.6 billion all-cash acquisition of Alharma Inc. (Alharma). The transaction was structured as a two-step transaction consisting of a first step all-cash tender offer of \$37 per share for the outstanding shares of Alharma's common stock, followed by a second step short-form merger pursuant to which a wholly-owned merger subsidiary of King was merged with and into Alharma, with Alharma surviving the merger as a wholly-owned subsidiary of King. According to King, the combination of Alharma and King will create a leading specialty pharmaceuticals company with greater scale and capabilities, and a stronger platform to deliver innovation, including (1) the addition of Alharma's animal health division to increase the diversification of King's business and to provide steady cash flow to fuel future strategic initiatives, and (2) increased commercialization capabilities to enhance the anticipated launches of Remoxy® (King's long-acting oral oxycodone product) and Embeda™ (Alharma's morphine sulfate extended-release product with sequestered naltrexone hydrochloride), both of which are designed to resist or deter common methods of opioid misuse and abuse.¹

This acquisition offers an opportunity to take a closer look at the many challenges a buyer can face in an M&A transaction in the current environment, including antitrust

¹ See joint press release of King and Alharma issued on November 24, 2008, *available at* www.kingpharm.com/Investors/News_Details.cfm?news_item_id=490

regulatory issues, defensive tactics from an initially unwilling seller, and rapidly changing market conditions. We begin with a detailed chronology of the transaction from start to finish, followed by an analysis of the antitrust process and a comment on how financing risks were allocated in the transaction given the deteriorating credit markets.

Background²

- On July 11, 2008, at the request of Brian A. Markison, Chairman, President, and Chief Executive Officer (CEO) of King, Mr. Markison met with Dean J. Mitchell, President and CEO of Alparma, to discuss a negotiated business combination in which King would acquire Alparma. At that meeting, Mr. Mitchell indicated that King would need to offer a large premium and informally indicated a price range of \$41 to \$45 per share. Mr. Markison responded that although King was prepared to offer a significant premium, he did not believe the premium referred to by Mr. Mitchell was within the range that King was prepared to offer. Nonetheless, Mr. Markison noted his desire to engage in acquisition discussions as soon as possible.
- On July 15, Mr. Markison again contacted Mr. Mitchell to reiterate King's interest in acquiring Alparma at a significant premium, and King's desire to engage in discussions and begin a due diligence review of non-public information related to Alparma as soon as possible. Mr. Mitchell told Mr. Markison that Alparma's Board of Directors was meeting the following week and that he would discuss the matter at that meeting.
- On July 28, Mr. Mitchell called Mr. Markison and said that he had discussed King's interest in Alparma with Alparma's Board of Directors, and noted again that in order for any offer to be considered seriously, it would need to reflect the substantial premium that Mr. Mitchell had referred to in the July 11 meeting. Mr. Markison responded by calling Mr. Mitchell on July 31 and indicated King's interest in acquiring

² The information provided in this Background section is taken from public filings with the Securities and Exchange Commission (SEC) by King and Alparma, including the Offer to Purchase, filed as Exhibit 99.A.1.A to the Tender Offer Statement (Form SC TO-T) filed by King on September 12, 2008, as subsequently amended, and the Solicitation/Recommendation Statement on Schedule 14D-9 filed by Alparma on September 26, 2008, as subsequently amended.

all of the outstanding shares of Alpharma's stock for \$33 per share in cash, which represented a 45% premium to the closing price per share of Alpharma's stock on that day. On August 1, Mr. Mitchell called Mr. Markison and stated that he had discussed the offer with Alpharma's Board of Directors, and that they had declined the offer.

- On August 4, after further discussions regarding the proposed transaction, Mr. Markison sent a letter to Mr. Mitchell: (1) reiterating King's \$33-per-share cash offer; (2) noting that King had retained legal and financial advisors, including Credit Suisse as its financial advisor; (3) making clear that the offer was not subject to any financing contingencies;³ (4) expressing confidence that within four weeks, King could complete confirmatory due diligence, and the parties could negotiate and sign a merger agreement; (5) indicating that King expected the letter and its contents to remain private; and (6) asking for a response no later than August 12.
- On August 7, Mr. Mitchell called Mr. Markison and indicated that Alpharma had retained Bank of America as its financial advisor, and that he and the Alpharma Board of Directors were taking King's offer seriously but needed more time to consider it.
- On August 21, Mr. Mitchell contacted Mr. Markison and indicated that Alpharma's Board of Directors had declined King's proposal. Mr. Mitchell stated that although Alpharma was not actively exploring a sale of the company, it would consider seriously any bona fide proposal that reflected the fair value of the company—which Alpharma's Board believed was in excess of \$40 per share. Mr. Markison noted to Mr. Mitchell that King might soon send another proposal letter and this time make it public. Also on August 21, representatives of Bank of America contacted representatives at Credit Suisse and indicated that Alpharma would not engage in discussions or permit King to

³ This means that with the combination of cash-on-hand and King's access to credit, King was proposing "deal certainty" in that King did not need the right to walk away from the acquisition for failure to obtain financing. King likely knew that this was an important point for Alpharma's Board and its shareholders given the deteriorating credit markets and lack of liquidity for acquisition financing. The merger agreement ultimately signed by King and Alpharma did not include a financing closing condition for King, and required that King pay to Alpharma a reverse break-up fee of \$60 million if King was not able to close the transaction because of an inability to obtain financing.

perform any due diligence unless King entered into a confidentiality agreement containing a standstill provision with Alpharma.⁴

- On August 22, Mr. Markison sent a letter to Mr. Mitchell and to Alpharma's Board of Directors and made its contents public in a press release. In this letter, King again reiterated its \$33-per-share cash offer and the other points in the August 4 letter, and concluded by indicating that if the parties were unable to negotiate a transaction, then King was prepared to take its offer directly to Alpharma's stockholders.
- Later the same day, Mr. Mitchell sent a letter to Mr. Markison reiterating Alpharma's rejection of King's \$33-per-share offer. In this letter, Alpharma invited King to enter into a confidentiality agreement (presumably with a standstill provision) so that Alpharma could share with King non-public information that Alpharma believed would demonstrate that \$33 per share significantly undervalued Alpharma. In particular, the letter indicated that a number of near-term events surrounding one of its products (Embeda™) were not reflected in King's offer⁵ and would drive increased value for Alpharma's shareholders.
- On August 27, Alpharma received notification from King that King made a filing with the Federal Trade Commission (FTC) stating that King intended to acquire a majority of Alpharma's outstanding common stock and, correspondingly, seeking clearance under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act).⁶ On

⁴ A "standstill" in this context is basically a commitment by the buyer not to engage in a "hostile" takeover attempt while the parties are negotiating a transaction and for some period of time thereafter if negotiations terminate. The purpose of a standstill is to require a potential buyer to deal solely with the target's Board of Directors (rather than directly with the target's stockholders) concerning a potential transaction so that the Board may conduct an orderly process with a level playing field among all potential buyers.

⁵ On September 2, Alpharma announced positive news that Alpharma's New Drug Application for Embeda Capsules had been accepted and designated for priority review by the Food and Drug Administration (FDA).

⁶ If a transaction meets certain minimum thresholds, the HSR Act requires notice filings by the parties followed by a waiting period to allow the government to review and investigate the proposed deal's competitive implications before a proposed transaction is consummated. See The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (2006).

August 28, in connection with King's HSR filing, the FTC contacted Alparma and made an informal request for information.⁷

- On September 1, Alparma's Board of Directors adopted a limited duration shareholders' rights plan (so-called poison pill) in response to King's \$33-per-share offer (Rights Plan). Under the Rights Plan, the rights would have become exercisable if a person had acquired 15% or more of the stock of Alparma or commenced a tender offer that could have resulted in that person owning 15% or more of the stock of Alparma. The Rights Plan had a limited term of one year and would have expired on September 1, 2009, unless the rights were redeemed earlier or the Rights Plan was terminated earlier by Alparma.⁸
- On September 2, Mr. Mitchell had a meeting with the CEO of an undisclosed company (Company X) at which that CEO indicated an interest in pursuing a negotiated business combination between Alparma and Company X.
- On September 3, Alparma's Board of Directors held a meeting with management and Alparma's legal and financial advisors to discuss updates on the King offer and third-party interest in a potential business combination with Alparma, including Company X. After these discussions, Alparma's Board unanimously determined, among other things, that (1) the company should initiate a process to explore all strategic alternatives, including a potential sale of the company, (2) Bank of America should more formally contact third parties that could have an interest in a potential business combination with Alparma,⁹ and (3) Mr. Mitchell should communicate back to

⁷ Complying with an informal request for information, also known as an informal request for "clarification," is not a Second Request and is voluntary. Responding to the FTC's requests and beginning a dialogue with the agency during the initial waiting period can help the parties avoid a Second Request or narrow its scope.

⁸ The primary reason for a target to adopt a limited duration rights plan in the face of an unsolicited tender offer is for the Board of the target to buy additional time to consider and pursue alternatives.

⁹ When the Board of Directors of a Delaware corporation affirmatively decides to approve a transaction involving a sale of control, the Board is charged with the obligation to achieve the best value reasonably available for stockholders. See *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.* 506 A.2d 173 (Del. 1986) (hereinafter, *Revlon*). While the unsolicited offer from King did not compel Alparma's Board to commence an auction process to look for the highest bidder, Alparma's Board likely wanted to assure itself and its shareholders that if Alparma were to later accept King's (or another bidder's) offer, then the Board could demonstrate, having run an auction for the highest bidder, that the Board had discharged its *Revlon* duties.

Company X's CEO the Board's interest in better understanding the structure and per-share value to be offered in connection with a potential transaction.

- On September 4, Credit Suisse contacted Bank of America and communicated that King would consider increasing its offer price to \$37 per share. Later that day, Bank of America communicated to Credit Suisse that Alharma was planning to initiate an auction process as part of its review of strategic alternatives and, with a proposal of \$37 per share, King would be invited to participate in that process if they signed a confidentiality agreement that would not include a "standstill" provision; however, a price in excess of \$40 per share would be required for Alharma to forego the auction process.
- In response, Credit Suisse communicated that King would be willing to enter into a merger agreement with Alharma at \$37 per share containing a "go-shop" provision, which would permit Alharma to actively solicit third-party offers during an agreed-upon period after the signing of the merger agreement. King's offer was once again rejected by Alharma.
- At a meeting of the Alharma Board of Directors on September 8, representatives of Bank of America and Mr. Mitchell informed the Board that Company X was preparing to submit a written preliminary indication of interest relating to a potential business transaction with Alharma in a day or two, and that it was expected that the indication of interest would be at a price in excess of \$37 per share. The Board and its advisors then discussed the potential chilling effect that a "go-shop" and break-up fee merger structure with King could have on the willingness of potential bidders for Alharma (including Company X and other parties) to pursue a transaction with Alharma at a per-share value in excess of \$37. The Board unanimously determined that it would not be in the best interests of the company and its shareholders to enter into a merger agreement at \$37 per share with a "go-shop" provision in lieu of conducting an auction process, but resolved that it would be willing to consider moving to an accelerated process with King if King were willing to raise its offer to \$39 per share.

- On September 9, Bank of America informed Credit Suisse of the Board's decision and counteroffer. Later that day Credit Suisse informed Banc of America that King was not prepared to raise its offer and encouraged Alharma to reconsider its position.
- At a meeting of the Alharma Board of Directors on September 10, Mr. Mitchell informed the Board that Alharma had received a written preliminary indication of interest from Company X for a business combination with a proposed merger consideration to be a mixture of cash and equity in Company X, valued in total in the range of \$38 to \$42 per share. The Board unanimously agreed (1) to continue to invite King to participate in the sale process at \$37 per share, but was not prepared to move forward with King on an accelerated basis at such price level, (2) that outbound efforts to encourage other potential bidders to participate in an auction process should move forward expeditiously, and (3) that Alharma should enter into a confidentiality agreement with Company X and allow Company X to promptly initiate due diligence.
- On September 10, Bank of America informed Credit Suisse that Alharma's position remained unchanged from the day before. Later that evening, Credit Suisse informed Bank of America that King was planning to launch a tender offer to acquire all of Alharma's stock at \$37 per share in cash, unless Alharma reconsidered its position.
- On September 12, King filed with the SEC a tender offer to purchase Alharma's outstanding common stock at \$37 per share in cash, conditioned on (1) the tender of a number of shares that, together with the number of shares held by King, would represent a majority interest in Alharma; (2) Alharma's Board of Directors redeeming the rights under the Rights Plan, or King being satisfied that the rights had been invalidated or determined to be inapplicable to the proposed transaction; and (3) the expiration of all waiting periods imposed under the HSR Act. Thereafter, King filed a new Notification and Report under the HSR Act specifically for its tender offer that initiated a new review period by the FTC expiring on September 26.¹⁰

¹⁰ Sometimes it is in the interest of the parties to "pull-and-refile" the HSR filing with the agencies. A pull-and-refile has the effect of restarting the initial waiting period and can be done once without an additional fee if the HSR filing is refiled within two days of being withdrawn. Employing this tactic gives the parties more time for discussion with agency staff before a decision on a Second Request is necessary. A pull-and-refile can be done more than once, but after the first time an additional filing fee is required.

- On September 12, King filed a complaint for declaratory and injunctive relief in the Delaware Court of Chancery against Alpharma and the members of Alpharma's Board of Directors, seeking to compel Alpharma to amend the Rights Plan to render it inapplicable to King's pending tender offer. The complaint alleged, among other things, that Alpharma's directors had breached their fiduciary duties to Alpharma's stockholders by adopting the Rights Plan in response to King's offer of \$33 per share, characterizing the Rights Plan as a "disproportionate and unreasonable" defensive measure to thwart King's offer.
- At the expiration of the FTC initial review period on September 26, Alpharma and King each received a Request for Additional Information and Documentary Material (collectively, the Second Request) from the FTC in connection with the FTC's review of King's tender offer. The effect of the Second Request was to extend the waiting period imposed by the HSR Act until ten days after King (as opposed to Alpharma) substantially complied with such request, unless that period was extended voluntarily by King or terminated sooner by the FTC.¹¹
- On September 30, Credit Suisse contacted Bank of America to discuss King's offer and the possibility of King conducting due diligence on certain non-public information regarding Alpharma. During October 2 and 3, King and Alpharma negotiated and entered into a confidentiality agreement that gave King access to such non-public information, and King commenced its review of the information on October 4.
- On November 23, Alpharma and King entered into a merger agreement (Merger Agreement) under which King agreed to revise its outstanding tender offer to reflect the terms and conditions set forth in the Merger Agreement. The per-share price to be paid to Alpharma's stockholders remained at \$37 per share in cash, subject to certain closing conditions, including the expiration of the waiting period under the HSR Act.
- During the period from September 3 through the date that King and Alpharma entered into the Merger Agreement, Bank of America contacted numerous parties to determine their interest in a potential business combination with Alpharma. During this period,

¹¹ See The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a.(e)(2) (2006).

Alpharma (1) entered into confidentiality agreements with eight other potential bidders, (2) provided access to company documents and information through an online data room, and (3) held multiple due diligence sessions with potential bidders. Of the eight parties that executed confidentiality agreements, two parties—Company X and another undisclosed company (Company Y)—submitted preliminary indications of interest.

- After conducting further due diligence and meetings with Alpharma’s management, Company X informed Alpharma that because of market conditions and certain other factors, it was no longer willing to pursue a negotiated transaction with Alpharma.
- After conducting further due diligence, Company Y indicated that it was not interested in pursuing an acquisition of the entire company, that it would be interested in purchasing Alpharma’s pharmaceuticals business, and that it did not have any interest in Alpharma’s animal health business. Although the Alpharma Board discussed and considered a possible sale of the pharmaceuticals business to Company Y or attempting to find a third party to partner with Company Y to acquire the entire company, ultimately the Board determined that such a transaction would take significantly longer, would be significantly more challenging to implement, and would be unlikely to result in a transaction that would be more favorable to Alpharma’s shareholders than King’s offer.
- Following the announcement of the Merger Agreement, Alpharma released a statement disclosing its reasons for ultimately recommending King’s \$37-per-share offer, which included (1) the “drastic decline in the financial markets,” (2) “the lack of a compelling alternative transaction,” (3) a fairness opinion provided to the company by Bank of America, and (4) the inclusion of a \$60 million buyer termination fee in the Merger Agreement payable by King to Alpharma in the event that King failed to obtain antitrust clearance or financing.
- Immediately prior to the execution of the Merger Agreement, Alpharma amended the Rights Plan to provide that neither the execution of the Merger Agreement nor the consummation of the tender offer or the merger thereunder would trigger the exercise of the rights under the Rights Plan.

- On November 29, the FTC accepted an agreement (Consent Agreement) from King and Alpharma containing a preliminary consent order to settle the FTC's charges that King's acquisition of Alpharma would be anticompetitive, and would violate Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act. Specifically, the FTC's complaint alleged that King's product, Avinza, and Alpharma's product, Kadian, were the only two significant branded morphine sulfate products on the U.S. market for oral long-acting opioids. The complaint further alleged that the U.S. market for oral long-acting opioids is highly concentrated, and that the effect of the proposed transaction, if consummated, might be to substantially lessen competition and to create a monopoly in that market.
- The Consent Agreement required that Alpharma's Kadian product be divested to the then manufacturer of that product, Actavis Elizabeth LLC (Actavis), no later than ten days following the consummation of King's acquisition of Alpharma.
- In accordance with the Consent Agreement, King entered into an Asset Purchase Agreement (Asset Purchase Agreement) with Actavis, pursuant to which, effective upon King's acquisition of Alpharma on December 29, 2008, King divested to Actavis King's assets exclusively related to Kadian.
- Under the terms of the Asset Purchase Agreement, King will receive from Actavis a purchase price of up to an aggregate of \$127.5 million in cash if Kadian achieves certain quarterly gross-profit-related milestones for the period beginning January 1, 2009, and ending June 30, 2010.
- On December 29, King completed the acquisition of Alpharma and Alpharma became a wholly owned subsidiary of King.

The Antitrust Process

Timing, Filing, and Second Requests

If a transaction meets certain minimum thresholds, the HSR Act requires notice filings by the parties, followed by a waiting period to allow the government to review and investigate the proposed deal's competitive implications before the transaction is

consummated.¹² The HSR filing is made with both the Department of Justice Antitrust Division (DOJ) and the FTC (collectively, the agency or agencies). Technical review of the filings for completeness and compliance is carried out by the FTC Premerger Notification Office. Assuming there are no problems with the filings, the time period begins to run immediately; however, the preliminary investigation cannot begin until the case is assigned to either the FTC or DOJ.

In many situations, there is no dispute over which agency should review a deal because the FTC and DOJ have different product market expertise. However, the agencies do have overlapping expertise and occasionally engage in a “clearance battle” regarding which agency will review a deal. The internal clearance procedure can take time and limit the period that the regulators have to review a deal—whether or not there is a battle—because no investigation can begin until one agency has “cleared” the matter to the other. Because the FTC has expertise in pharmaceuticals, it was clear that the FTC would handle the investigation of King/Alpharma.

Typically, the FTC and DOJ have thirty days to review the initial filings before deciding to close the initial investigation into the transaction or to issue a Request for Additional Information and Documentary Material (the Second Request, noted earlier).¹³ However, if a transaction involves a cash tender offer or an acquisition in bankruptcy, then the initial review period is limited to fifteen days.¹⁴

The King/Alpharma transaction involved a cash tender offer; therefore, the FTC had only fifteen days for the initial review. Because it was readily apparent that the transaction involved a significant competitive overlap involving just a few additional players and the FTC had less than fifteen days to review the overlap during the initial waiting period, this deal was highly likely to receive a Second Request.

Typically, to expedite review of a transaction during the initial waiting period, the agency requests that the parties voluntarily provide lists of key customers, strategic business

¹² See The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a(a) (2006).

¹³ 15 U.S.C. § 18a(b)(1)(B) (2006).

¹⁴ *Id.*

and marketing plans, and access to interview company executives. The FTC will also interview industry competitors and customers.

During the initial waiting period, parties will typically be advised by antitrust counsel to work with the agency and provide responses to the voluntary requests. By working with the FTC at an early juncture, parties can begin substantive dialogue with regulators promptly, potentially avoid a Second Request, narrow the scope of a Second Request, and/or frame the issues presented by the transaction.

As mentioned above, on September 26, 2008, the FTC concluded its initial fifteen-day investigation of the King/Alpharma transaction and issued a Second Request to King. By issuing a Second Request, the FTC prevented the consummation of the tender offer until ten days after King substantially complied with the Second Request, or the FTC agreed terminate to the waiting period upon a settlement.¹⁵

A Second Request provides regulators the opportunity to obtain information that they need to evaluate the proposed transaction while maintaining the status quo. Second Requests are very thorough and represent the agency's opportunity to perform "discovery" to prepare its case should the agency pursue litigation. The scope of a Second Request can often be narrowed through negotiation before and/or after it is issued. Model Second Requests are freely available and antitrust counsel know what detailed information will be sought.¹⁶ Therefore, if the parties anticipate a Second Request and would like to push the timing of their response, document collection and other preparations can begin well before the Request is issued.

Once a Second Request is issued, parties tend to follow one of two paths. In the first path, parties can gather all information requested by the agency in the Second Request and produce that information as soon as possible. By gathering and producing quickly, this path endeavors to compress the period in which the agency will have to muster its case against the parties should litigation result. However, responding to a Second

¹⁵ Had the deal not been a cash tender offer (or an acquisition in bankruptcy), the transaction could not go forward until thirty days after substantial compliance with the Second Request.

¹⁶ The FTC provides a model Second Request and explanatory guide *available at* www.ftc.gov/bc/hsr/introguides/guide3.pdf or by searching www.ftc.gov for "model second request."

Request can be very costly because of the significant e-discovery involved and is fraught with litigation risk that could significantly extend the resolution process.

In the alternative path, some deals involve competitive overlaps that might require non-material divestitures that can be resolved cleanly and quickly while appeasing regulators. In these cases, parties negotiate with the agency over settlement terms, limit the scope of documents provided to the agency, and agree to give the agency more time to prepare its case beyond the statutory requirements should negotiations fail and the parties substantially comply with the Second Request. This path forgoes the need to respond to the Second Request in full and can speed resolution of the agency review significantly.

In the King/Alpharma transaction, the Consent Agreement negotiated by the parties dispatched with the only anticompetitive issue alleged by the FTC in its complaint—an overlap in the U.S. oral long-acting opioids (oral LAOs) market.¹⁷ Specifically, the FTC found that King and Alpharma had the only two competitively significant branded morphine sulfate oral LAOs and were particularly close competitors in the larger oral LAO market alleged by the FTC.¹⁸ The FTC expected that a loss of competition between Avinza (King's product) and Kadian (Alpharma's product) would result in higher prices for both drugs.¹⁹ The consent order that settled the charges against King and Alpharma was agreed to on December 29, 2008.

Remedy for the Substantive Issues

The FTC's analysis of the King/Alpharma transaction led to a focus on the overlap between Avinza and Kadian. That focus was not surprising and could have been predicted when the transaction was announced based upon a review of publicly available information.

¹⁷ *In the Matter of King Pharmaceuticals, Inc. and Alpharma Inc.* FTC File No. 0810240 (decision and order) (Dec. 29, 2008) available at: www.ftc.gov/os/caselist/0810240/081229do0810240.pdf; *In the Matter of King Pharmaceuticals, Inc. and Alpharma Inc.* FTC File No. 0810240 (complaint) (Dec. 29, 2008) available at: www.ftc.gov/os/caselist/0810240/081229cmp0810240.pdf.

¹⁸ King Pharmaceuticals Inc. and Alpharma Inc., 74 Fed. Reg. 295 (FTC Jan. 5, 2009) (aid to public comment), available at: www.ftc.gov/os/caselist/0810240/081229anal0810240.pdf.

¹⁹ *Id.*

The FTC reasoned that because all branded oral LAOs are used to manage moderate-to-severe pain and have similar indications, mechanisms of action, dosage forms, and dosage frequency, a difference in chemical compound did not segment the alleged market.²⁰ More importantly, the FTC determined that short-acting opioids and non-oral opioids did not compete with the oral LAOs.²¹ The FTC's finding of a lack of direct competition between these opioid products was not surprising given the qualitative facts of each because of significant differences in indication, pricing, mechanism of action, and dosage.

Because the branded oral LAO market alleged by the FTC is highly concentrated among only four total competitors (King, Alpharma, Purdue Pharma, and Endo Pharmaceutical), and because Avinza and Kadian were each other's closest substitute, the FTC required a divestiture to maintain competition after the King/Alpharma combination.²² As is often the case in negotiated settlements, the FTC required that King find a purchaser upfront for the divested assets before the FTC would approve the consent decree.²³

In situations where the FTC had previously required a divestiture of a branded pharmaceutical, the FTC typically had required that the buyer of the divested product have experience with brand marketing.²⁴ In this case, the FTC reasoned that the buyer required no such experience because the buyer was both the manufacturer of the divested asset (Kadian) and a strong generics company.²⁵ The FTC approved this buyer anticipating that the buyer would be incentivized to bring a generic to market quickly and perhaps prior to Kadian's patent expiration in 2010—a solution that would benefit consumers.²⁶

In light of the antitrust clearance risks associated with the transaction, Alpharma bargained for a provision in the Merger Agreement that King would have been obligated

²⁰ *Id.*

²¹ *Id.*

²² *Id.*

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.*

²⁶ *Id.*

to pay Alharma a \$60 million reverse break-up fee if ultimately the deal had been terminated because of a failure to obtain antitrust clearance.

Alharma's Defensive Measures

Another obstacle that King faced with the acquisition of Alharma was the initial opposition by Alharma's Board of Directors and Alharma's adoption of the Rights Plan. A rights plan or "poison pill," as it is commonly known, is a takeover defense mechanism that provides a target company's existing stockholders with the right to purchase new shares of the company's stock at a discount to the market price upon certain triggering events associated with an unsolicited takeover attempt. A poison pill is an effective deterrent against an unsolicited takeover attempt because if a potential hostile acquirer were to trigger the pill by acquiring more than the pill's triggering percentage of the target company's stock (usually around 15%), then the target company's shareholders (other than the hostile buyer) become entitled to purchase a large number of the target company shares at a deep discount.²⁷ By threatening massive dilution, a rights plan makes it uneconomical for a prospective acquirer to acquire more than a limited percentage of the target company's stock (typically less than 15%) without approval of the target company's board of directors.

One of the basic features of the poison pill is that it can be adopted or redeemed by the target company's board of directors relatively quickly, without stockholder approval. Thus, Alharma's Board of Directors was not required to obtain stockholder approval before implementing the Rights Plan, which the Board was able to implement within only a few weeks after rejecting King's offer of \$33 per share.

In adopting the Rights Plan, Alharma's Board of Directors was required to exercise its fiduciary duties to shareholders. In assessing a board's decision to implement an anti-takeover measure in response to an alleged threat to corporate control, Delaware courts will apply the *Unocal* standard of review. Under that standard, the directors must show

²⁷ Many rights plans also have a feature that enables the target company's shareholders (other than the hostile buyer) to exchange their rights for additional shares and thereby avoid the need to make a cash payment. Similar to a cashless exercise provision in a stock option, this feature permits the shareholder to exchange a right granted under the rights plan, once triggered, for a net number of shares equal to the total shares subject to the right, less the exercise price.

that (1) “they had reasonable grounds for believing that a danger to corporate policy and effectiveness exist[s],”²⁸ and (2) the defensive measure adopted by the board of directors was “reasonable in relation to the threat posed.”²⁹ For example, a target’s Board might determine that it is in the best interests of the corporation and its stockholders to remain independent and pursue a well-defined, long-term plan to enhance shareholder value; that a bidder’s unsolicited offer to acquire control of the target threatens that plan; and therefore that the adoption of a rights plan to deter the bidder is reasonable in relation to the threat posed (“just say no” response).³⁰ Or, in the face of an unsolicited bid to acquire the company, the Board might decide to adopt a rights plan to enable the Board to have additional time to pursue and consider other alternatives.³¹

Alpharma’s Board of Directors adopted a limited duration rights plan to give the Board up to a year to continue to conduct an auction process and to pursue and consider other alternatives without King acquiring control of the stock of the company. Prior to making its decision to adopt the Rights Plan, Alpharma’s Board met with the company’s management, representatives of Bank of America, and its outside counsel to discuss the decision and the Rights Plan.³² Alpharma’s Board of Directors concluded that the Rights Plan would not preclude a change of control transaction, but rather would provide the Board with additional time and flexibility (in the face of King’s offer) to explore alternative transactions to enhance shareholder value.

Deteriorating Credit Markets

Between the time that King first approached Alpharma in early July 2008 and the time that King’s final financing arrangements for the deal were announced in late December 2008, the deterioration of the global credit markets escalated dramatically. Some of the events that took place during this timeframe included the following:

²⁸ *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

²⁹ *Id.*

³⁰ See *Paramount Communications Inc. v. Time Inc.*, 571 A.2d 1140 (Del. 1990).

³¹ See *MAI Basic Four, Inc. v. Prime Computer, Inc.*, 1988 Del. Ch. LEXIS 161 (Dec. 20, 1988); *In re Holly Farms Corp. S’holders Litig.*, 1988 Del. Ch. LEXIS 164 (Dec. 30, 1988).

³² King, Amendment No. 5 to Solicitation/Recommendation Statement (Schedule 14D-9) at 9 (Dec. 8, 2008).

- July 30, 2008—President Bush signs into law the Housing and Economic Recovery Act of 2008.
- September 7, 2008—Federal government takes over Fannie Mae and Freddie Mac.
- September 14, 2008—Lehman Brothers files for Chapter 11 bankruptcy protection.
- September 17, 2008—The Federal Reserve lends \$85 billion to American International Group (AIG) to avoid AIG filing for bankruptcy protection.
- September 25, 2008—Washington Mutual is seized by the Federal Deposit Insurance Corporation (FDIC), and its banking assets are sold to JP Morgan Chase.
- October 3, 2008—President Bush signs the Emergency Economic Stabilization Act, creating the Troubled Asset Relief Program to purchase failing bank assets.

Based on King's SEC filings relating to the Alharma acquisition, it appears that as of the end of December 2008, the aggregate amount of the debt financing utilized by King was approximately \$625 million³³—an amount that was far smaller than the \$1 billion provided for in the debt commitment letter King entered into with its lenders on September 11, 2008.³⁴ Based on these numbers, it appears that King was required to use more of its available cash for the acquisition than it had initially expected to use.

In light of the potential financing risks in the transaction associated with the deteriorating credit markets, Alharma bargained for a provision in the Merger Agreement that King would have been obligated to pay Alharma a \$60 million reverse break-up fee if ultimately the deal had been terminated because of a failure by King to obtain financing for the acquisition.

³³ According to the Current Report (Form 8-K) filed by King on December 29, 2008, \$37.9 million remained committed but undrawn under King's revolving credit facility after giving effect to the \$425 million utilized by King for its acquisition of Alharma, and after giving effect to letters of credit totaling \$12.1 million; King also entered into a \$200 million term facility for the purpose of completing the transaction.

³⁴ Filed as Exhibit 99.B.1 to Tender Offer Statement by Third Party (Form SC TO-T) filed by King on September 12, 2008.

Conclusion

King's acquisition of Alpharma provides a good example of some of the challenges that buyers can face in the public M&A market and demonstrates the need for careful and thorough upfront planning to anticipate and be prepared for these challenges. It is reasonable to speculate whether this transaction could have been completed as promptly as it was, even given King's strong cash position, had King not undertaken careful antitrust analysis and planning upfront, and provided for reasonably anticipated contingencies in its merger offer and regulatory filings.

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