

Vinson&Elkins

MARCH 2019

PUBLIC COMPANY CONSOLIDATIONS: WHAT YOU NEED TO KNOW

Energy Series

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SAVE THE DATE

ENERGY SERIES

Upcoming V&E Programs

High-Yield Bonds in the Energy Industry

Wednesday, April 10, 2019

Speakers: **Noel Hughes; David Stone; David Wicklund**

TODAY'S PANELISTS



JEFFERY BURTON FLOYD
MERGERS & ACQUISITIONS AND PRIVATE
EQUITY

+1.713.758.2194

jfloyd@velaw.com

Partner, Houston



STEPHEN M. GILL
MERGERS & ACQUISITIONS AND CAPITAL
MARKETS

+1.713.758.4458

sgill@velaw.com

Partner, Houston



LANDE ALEXANDRA SPOTTSWOOD
MERGERS & ACQUISITIONS AND CAPITAL
MARKETS

+1.713.758.2326

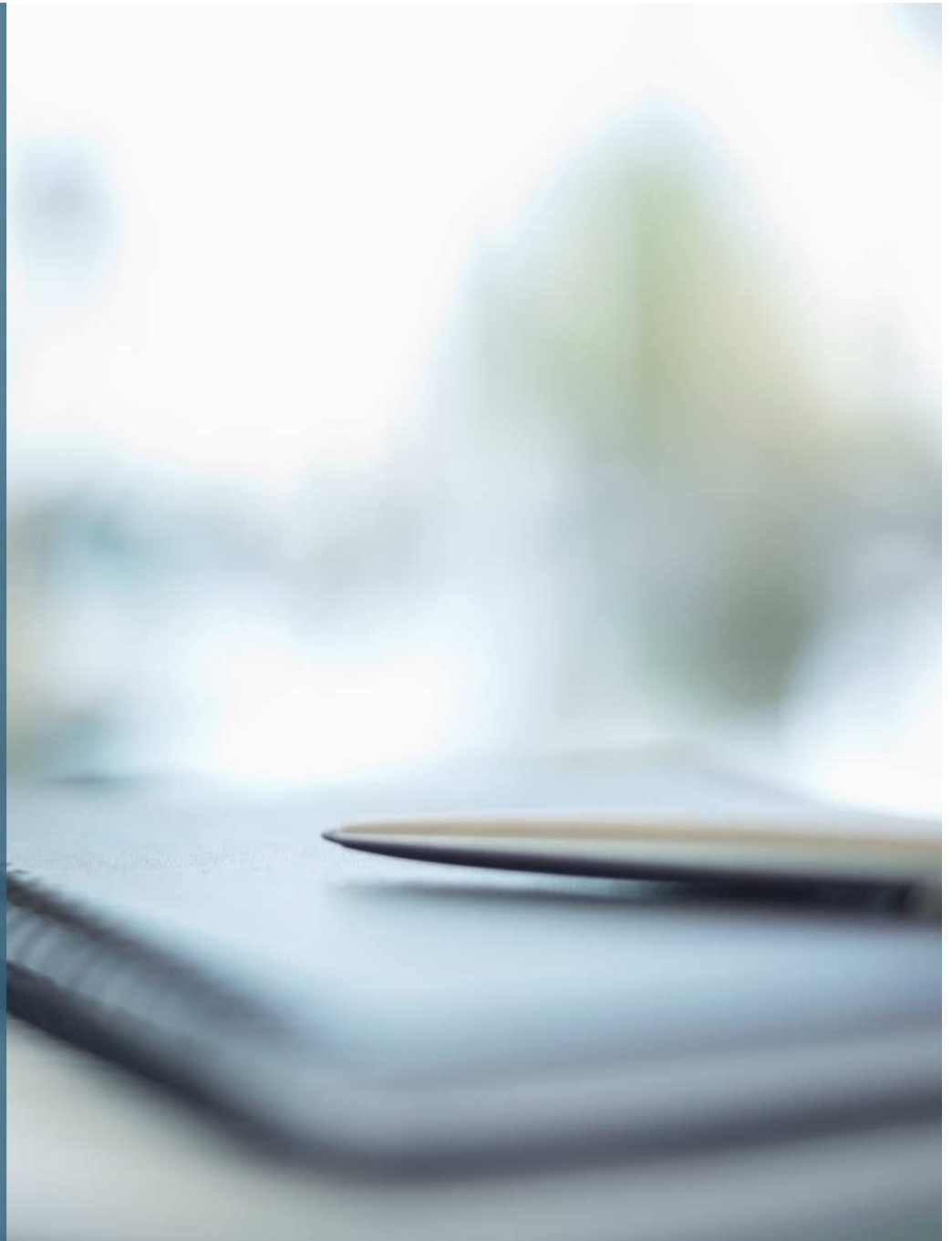
lspottswood@velaw.com

Partner, Houston

DISCUSSION TOPICS

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TRENDS DRIVING CONSOLIDATION



CONSOLIDATION IS COMING! (HAVEN'T WE HEARD THIS BEFORE?)

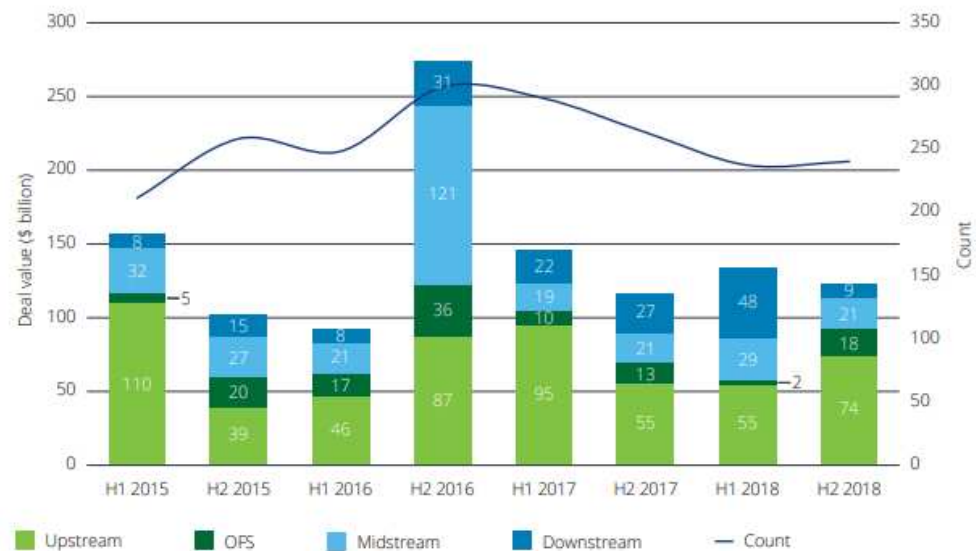
- Accepted wisdom is that long periods of steady commodity prices drive M&A activity in energy sector
- Through Q3 2018, market conditions were ripe for M&A, and activity peaked in October
 - \$32B of M&A in Q3; \$85B in FY2018, most since 2014
 - Single week in October with Denbury/Penn Virginia, Chesapeake/Wildhorse, Encana/Newfield
- But then came....

Figure 1. Crude oil prices precipitously fell and volatilized at the end of 2018



Sources: EIA, Petroleum & Other Liquids spot prices database

Figure 2. Global oil & gas M&A deal value remained flat and the count declined from 2017

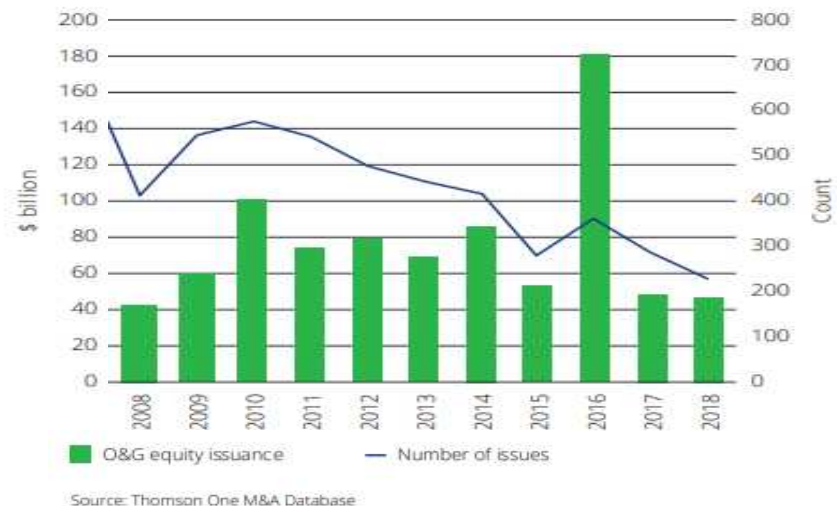


Source: 1Derrick's M&A Database

WHAT TRENDS ARE DRIVING CONSOLIDATION?

INVESTMENT CAPITAL IS SCARCE

- As the shale boom has faded and mature industries and technology have returned to favor, energy has become less relevant to index funds/generalist investors compared to other sectors
 - During the shale boom, energy market capitalization as a percentage of the S&P 500 rose steadily
 - 2001: 7%
 - 2005: 9%
 - 2008: 15%
 - Post-boom, energy market capitalization as a percentage of the S&P 500 has declined steadily
 - 2014: 11%
 - 2016: 7%
 - 2019: 5%
- E&P equity issuances have slowed to a halt
 - 2016: \$34 billion in E&P equity offerings
 - 2019 to Date: \$0
- IPO is not currently a viable exit alternative for private E&P companies



WHAT TRENDS ARE DRIVING CONSOLIDATION?

INVESTOR SENTIMENT

- Current investor sentiment favors the following:
 - Clear path to becoming free cash flow positive
 - Commitment to return capital
 - Solve infrastructure issues
 - Portfolio rationalization
 - No more “growth for growth’s sake”
 - Lower leverage
- Meanwhile, activism has returned to the energy space and become disruptive, including pushing for consolidation
- Difficult for small cap and, to an extent, midcap companies to adjust to this environment

WHAT TRENDS ARE DRIVING CONSOLIDATION?

SCALE MATTERS

- Scale matters within basin to reduce field level costs and generating cash flow to delever
- Scale matters for solving infrastructure issues
- More efficient capital allocation
- Preferred portfolios:
 - Oil-weighted
 - Minimal infrastructure constraints
 - Contiguous acreage
 - Delineated
- Currently, the larger energy companies are attracting the most capital and the highest multiples as investors are now focused on scale and stability
 - For example, in the Permian, the average price / 2019 CFPS is 3.3x for companies between \$1-5B, 4.1x for companies between \$5-20B and 6.3x for companies > \$20B
 - A similar array is true for Appalachia, for E&P generally and for E&P excluding Permian.

WHAT ARE THEY SAYING?

BIGGER IS BETTER

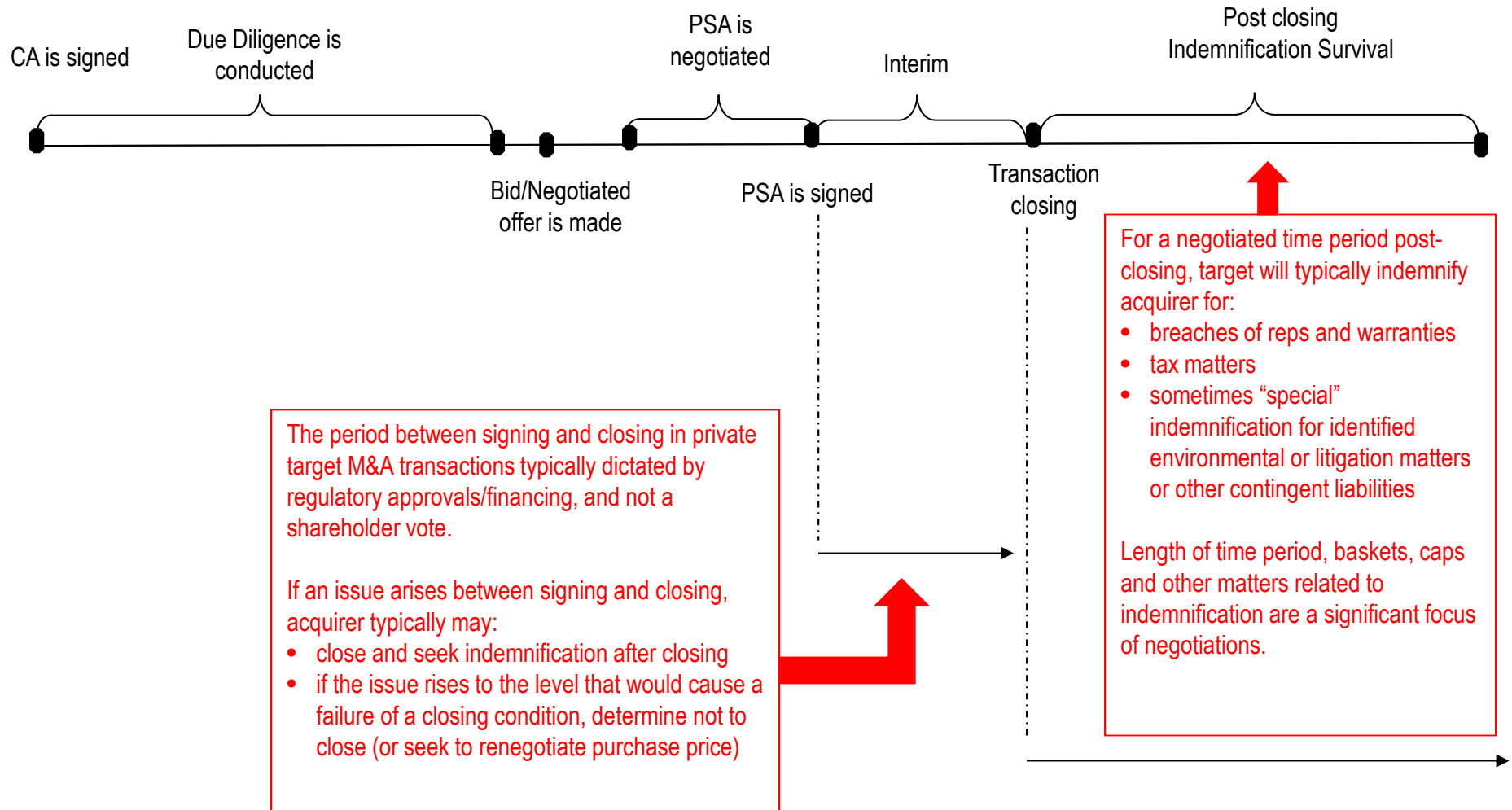
- There are 112 operators in the Permian Basin and that means an excessive number of management teams operating similar assets.....Economies of scale are needed and about 20 companies, or any valued under \$3 billion, should be combined in a “merger of equals.” - **Ben Dell, Kimmeridge Energy, March 11, 2019**
- “There’s just too many shale companies. The only way to add value now is to buy companies and cut heads, cut jobs.” – **Mike Bradley, Tudor Pickering Holt & Co, January 14, 2019**
- The ability of the larger companies to do an accretive acquisition is probably at its highest level since the beginning of the shale revolution. M&A interest is at its highest in nearly a decade.” - **Michael Roomberg, Miller/Howard Investments, March 11, 2019**
- “Large and liquid oil and gas players will be in the best position to ride the cycle and perhaps take advantage of a probable shift to a buyer’s market. For the rest, consolidation may be the key to weathering a deepening uncertainty.” - **Deloitte Oil & Gas Mergers and Acquisitions Report, Yearend 2018**

KEY DIFFERENCES BETWEEN PUBLIC AND PRIVATE M&A



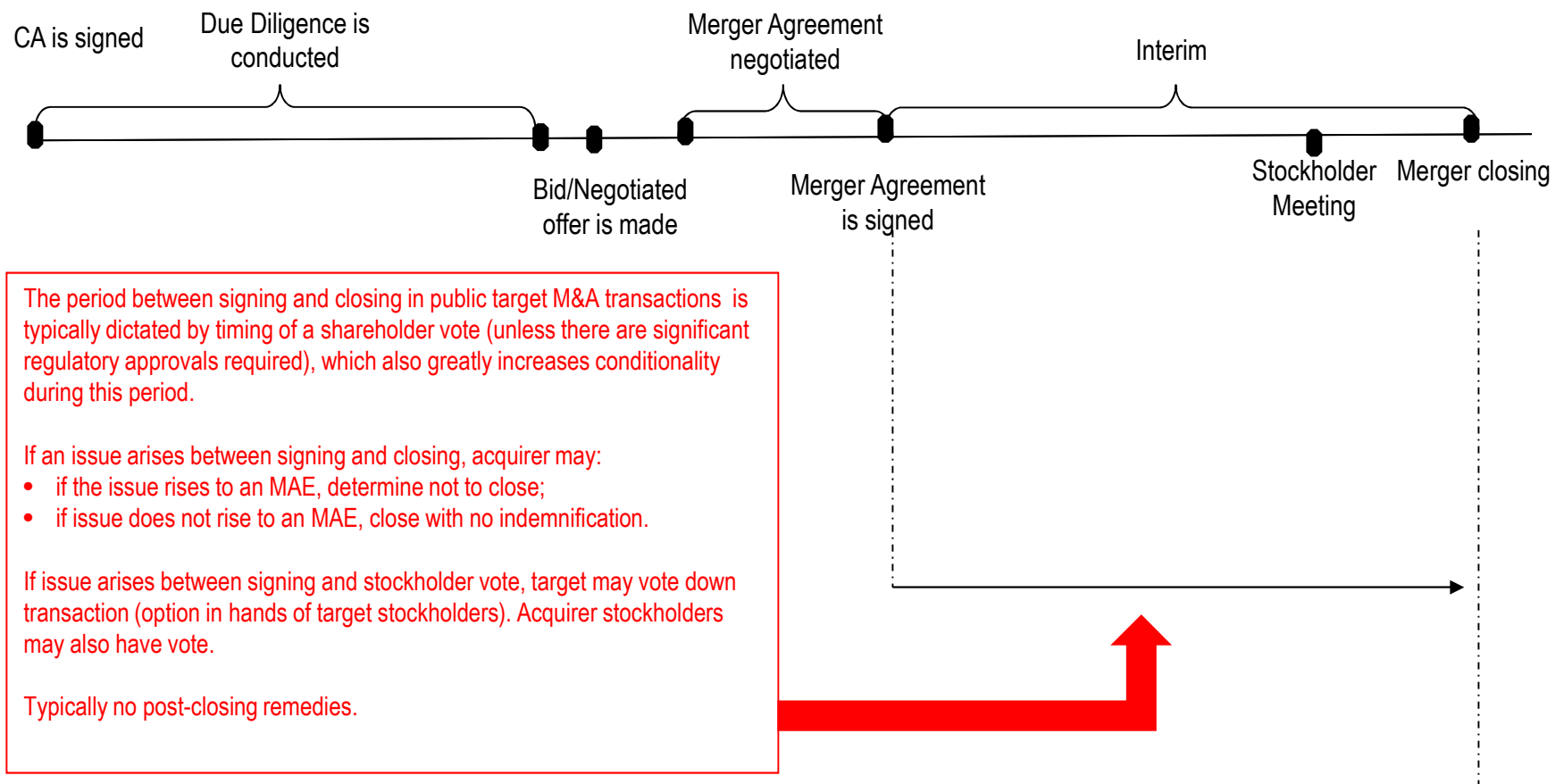
BASICS OF PUBLIC TARGET M&A

WHAT IT IS NOT



BASICS OF PUBLIC TARGET M&A

WHAT IT IS



FIDUCIARY DUTIES OF TARGET BOARD OF DIRECTORS

ASSUMING DELAWARE LAW

- Traditional duties of care and loyalty apply
- Target board members are obligated to act in a manner that they believe will maximize long-term shareholder value
 - May “just say no” and refuse to engage on any offer they believe undervalues the company compared to its long-term prospects
 - But once a target board decides to sell control of the company, it must undertake a process that would be reasonably expected to maximize the value received by stockholders
 - Includes engaging with legitimate bidders that are offering a higher value
- If challenged, the board’s decisions with respect to approving a potential sale will be reviewed by Delaware courts under a heightened, “enhanced” level of scrutiny
 - Terms of merger agreement will also be reviewed to ensure they:
 - do not coerce the stockholder vote
 - do not preclude a better transaction from emerging prior to the vote
 - These constraints have resulted in market practice of fiduciary outs and limited deal protection provisions



THE ROLE OF SHAREHOLDER ACTIVISM

SHAREHOLDER ACTIVISM AND M&A

INTRODUCTION

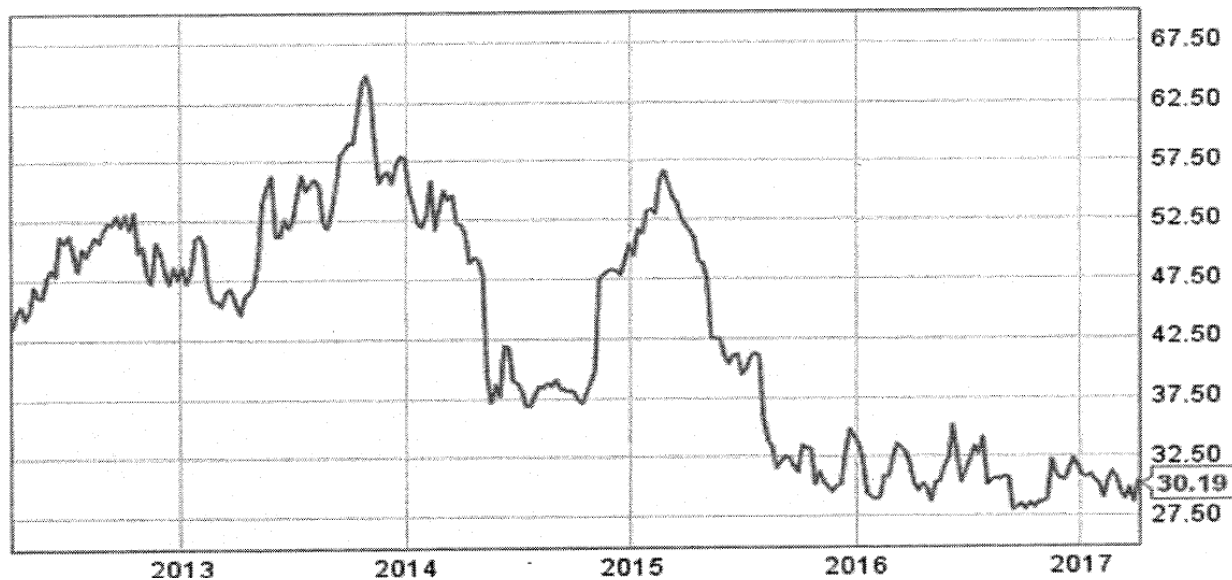
- How activist investors become involved in an M&A transaction:
 - As an existing shareholder that urges the review of strategic alternatives or a sales process
 - As a new shareholder that acquires a position post-announcement of the deal
 - Occasionally, an M&A transaction is announced during the same time period in which the activist is quietly accumulating a stake or staying passive in the stock

SHAREHOLDER ACTIVISM AND M&A

CASE STUDY: WHOLE FOODS / JANA

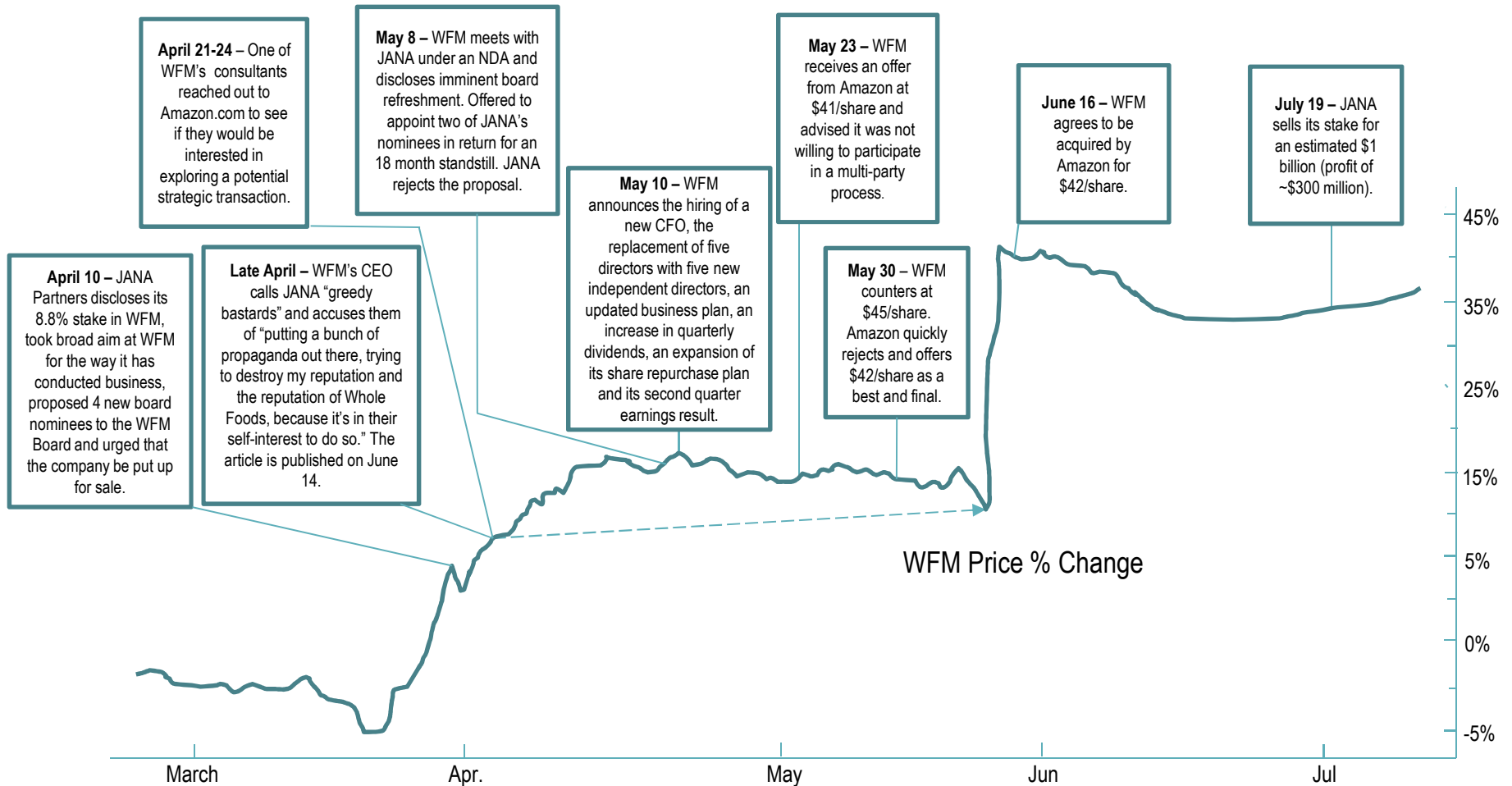
- After being a stock market darling for several years, Whole Foods' (WFM) business had been deteriorating with same-store sales being negative for two years, with the stock price declining over 40% over that period.

Whole Foods Market Price



SHAREHOLDER ACTIVISM AND M&A

ACTIVISM AS A CATALYST



SHAREHOLDER ACTIVISM AND M&A

ACTIVISM AS A CATALYST

ENERGEN



DIAMONDBACK
Energy

SHAREHOLDER ACTIVISM AND M&A ANNOUNCED DEALS

- Activists are looking at **each and every** announced deal:
 - Looking to either get a “**bump**” or **derail** the deal
 - Assessing vulnerabilities
- Opposition to M&A deals in the form of **proxy fights** or “**vote no**” **campaigns** used to be rare and rarely successful, but **has become increasingly common in the past five years**
- Most common is on the sell side, where an activist shareholder of the target believes that the transaction undervalues the target and attempts to cause other shareholders to join with it in rejecting the deal
 - See, e.g., Mangrove Partners’ opposition to the sale of Penn Virginia to Denbury
- Recent trend: **buyside activists** where the buyer requires a vote, opposing transactions because they disagree with the industrial logic of the transaction or they believe the buyer is over-paying.
 - See, e.g., JANA opposition to EQT’s acquisition of Rice Energy

SHAREHOLDER ACTIVISM AND M&A

ACTIVIST STRATEGIES

Against the Transaction

- **Proxy contest** to solicit proxies from the Company's shareholders to **vote against the transaction on the activist's proxy card**
 - Activist would file its own proxy statement and related proxy materials/solicit proxy power
- **"Vote no" campaign** to encourage shareholders to **vote against the transaction on the company's proxy card**
 - Activist would run an exempt solicitation and would not file its own proxy statement/solicit proxy power

Against the Board

- **Proxy contest** to solicit proxies from shareholders to **replace the directors of the acquirer or target company**

SHAREHOLDER ACTIVISM AND M&A

OPPOSITION TO ANNOUNCED DEALS – PROXY CONTEST



SHAREHOLDER ACTIVISM AND M&A
OPPOSITION TO ANNOUNCED DEALS – VOTE NO



SHAREHOLDER ACTIVISM AND M&A

TAKE-AWAYS

- Know Your Shareholder Base
 - Understand who your shareholders are and why they are invested in your company
 - Study known activists or vocal shareholders in your stock
 - Be proactive in identifying and monitoring any rumors about the company
- Have Established Credibility with Your Shareholders
 - Actively engage with your shareholder base to make sure they understand the company's strategy
 - Obtain shareholder feedback and, where appropriate be responsive
- Monitor Changes in the Shareholder Base and Activity in the Stock
 - Early warning regimes under U.S. law are weak
 - Engage a stock watch service

SHAREHOLDER ACTIVISM AND M&A

TAKE-AWAYS

- Evaluate Transaction for Vulnerabilities
 - Is the transaction consistent with existing strategy or will it come as a surprise?
 - Are the promised synergies defensible?
 - Does the transaction exacerbate lingering issues?
- Consider Structuring Alternatives
 - Can a buy-side vote be avoided?
 - Can the deal be structured to avoid super-majority provisions?
 - Take care in agreeing to “majority of the minority” approvals
- Have a Robust PR Rollout of the Transaction
 - Develop a detailed explanation of the deal and why it creates shareholder value and is consistent with the strategy prior to announcement
 - Post-announcement road show

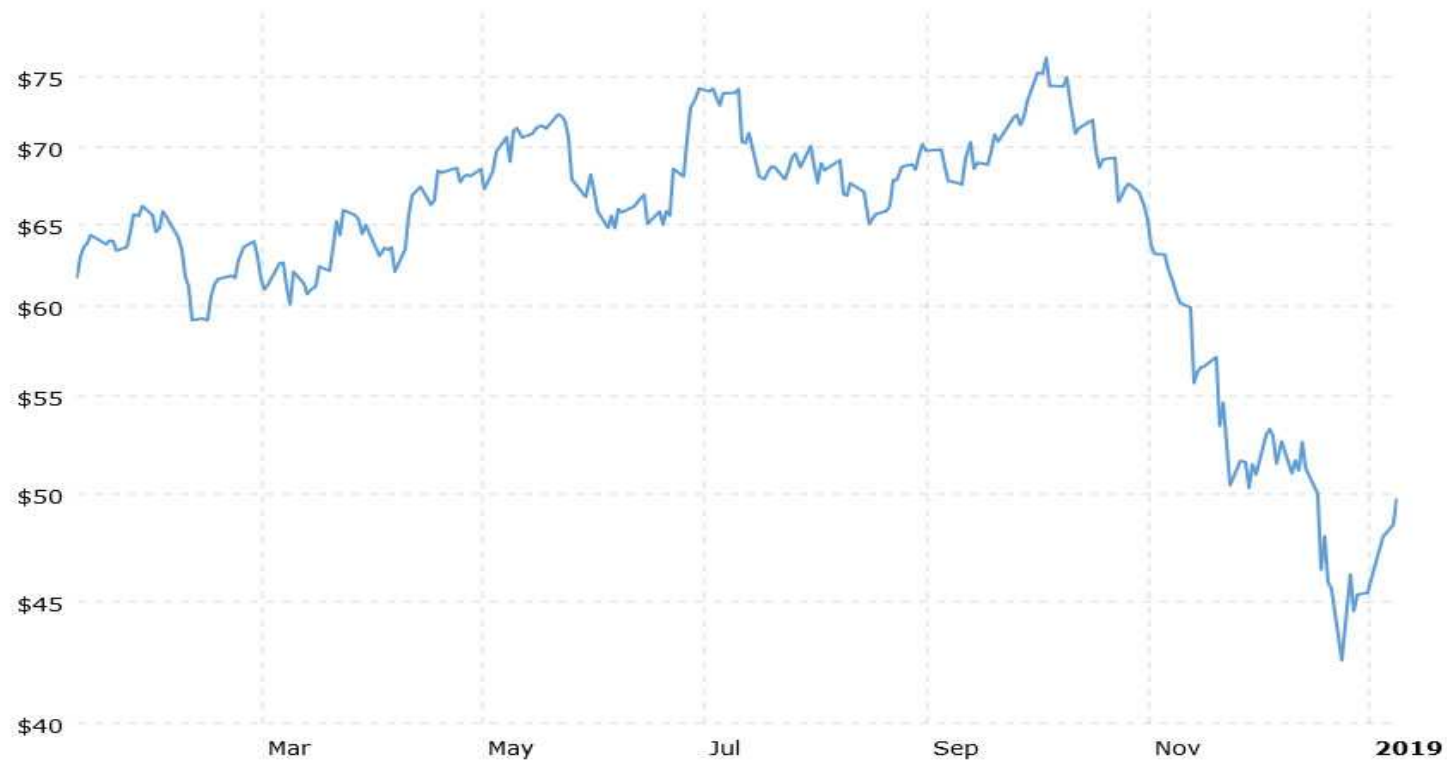
THE IMPACT OF COMMODITY PRICE VOLATILITY



COMMODITY PRICE VOLATILITY

LATE-2018 SWOON

2018 WTI Crude Oil Price Chart



COMMODITY PRICE VOLATILITY

HOW PRE-SWOON DEALS HAVE FARED

- October 8, 2018 – Ensco agrees to acquire Rowan
 - Closed on February 21, 2019 after recutting the deal and obtaining support of key Rowan shareholders
- October 17, 2018 – Earthstone Energy agrees to acquire private company Sabalo
 - Terminated on December 21, 2018 citing and decline in commodity prices and market conditions
- October 28, 2018 – Denbury agrees to acquire Penn Virginia
 - Pending
 - Mangrove Partners, a shareholder of Penn Virginia, is engaged in an opposition proxy contest
- October 30, 2018 – Chesapeake Energy agrees to acquire WildHorse Resource Development
 - Consummated on February 1, 2019
- November 1, 2018 – Encana agrees to acquire Newfield Exploration
 - Consummated February 13, 2019

COMMODITY PRICE VOLATILITY

KEY TAKEAWAYS

- Given that cash is not really an option, except for majors, energy consolidation transactions will be exposed to commodity price risk
- Participants will need to be thoughtful about how their asset mix and geographic overlap can impact valuation in the months post-signing when setting exchange ratios
- “Stronger” buyers will be preferred

IMPACT OF RECENT DELAWARE DECISIONS ON THE PRACTICE

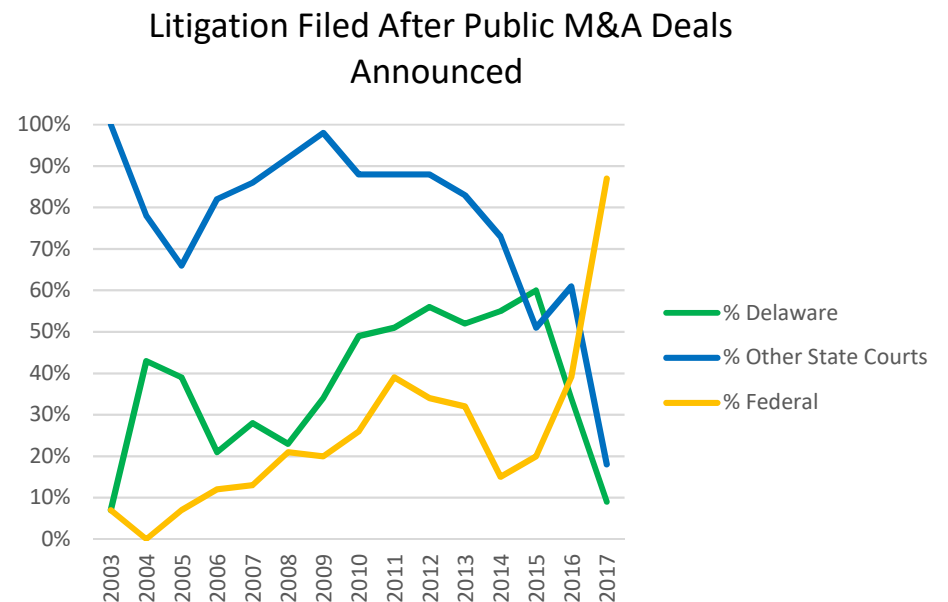


CHANGES IN DELAWARE LAW...

- ***C&J Energy Services, Inc. v. City of Miami General Employees' and Sanitation Employees' Retirement Trust (2014)***
 - Boards have significant flexibility in crafting the sales process under *Revlon*
 - Delaware Supreme Court held that there is no “single blueprint that a board must follow to fulfill its duties” when conducting a sales process
- ***Corwin v. KKR Financial Holdings LLC (2015)***
 - Business judgment deference applies in post-closing damages suits challenging a Board's approval of a merger when the merger has been approved by a fully informed and uncoerced vote of the majority of disinterested stockholders
- ***In re Trulia, Inc. Stockholder Litigation (2016)***
 - Announced Delaware courts will apply greater judicial scrutiny of disclosure-only settlements
 - Disclosure-only settlements “provide no benefit to stockholders and amount to little more than deal ‘rents’ or ‘taxes’,” yet grant broad releases to defendants

...HAVE CHANGED THE BEHAVIOR OF PLAINTIFFS

- Immediate impact of *Corwin & Trulia*
 - Filings in Delaware fell by almost 50% in 2016 and were around ~10% in 2017
 - Most significant shift in filings from Delaware is to federal court (increase from 20% of filings in 2015 to 87% of filings in 2017)
 - Forum selection bylaws do not prevent plaintiffs from bringing federal suits alleging disclosure violations under Rule 14a-9
 - Filings in other state courts rose in 2016 but significantly dropped in 2017
 - General decline in multi-jurisdictional filings

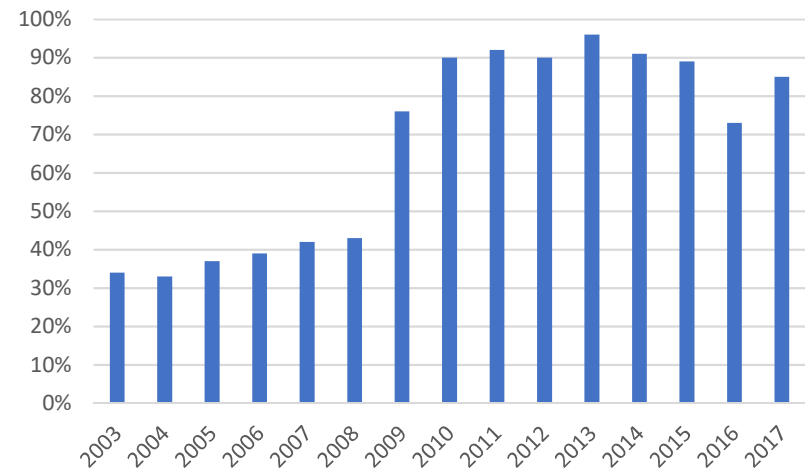


Source: The Shifting Tides of Merger Litigation, University of Pennsylvania Law School, 2018

THE TRADITIONAL PLAYBOOK IS OUT OF DATE

- “Litigation on Every Deal”
 - Number of lawsuits filed per deal has declined:
 - 2014: 4.6 suits / deal
 - 2017: 2.8 suits / deal
- Generic Claims
- “Deal Tax” paid for “Deal Insurance”

Percent of Public Mergers Which Attracted Litigation



Source: The Shifting Tides of Merger Litigation, University of Pennsylvania Law School, 2018

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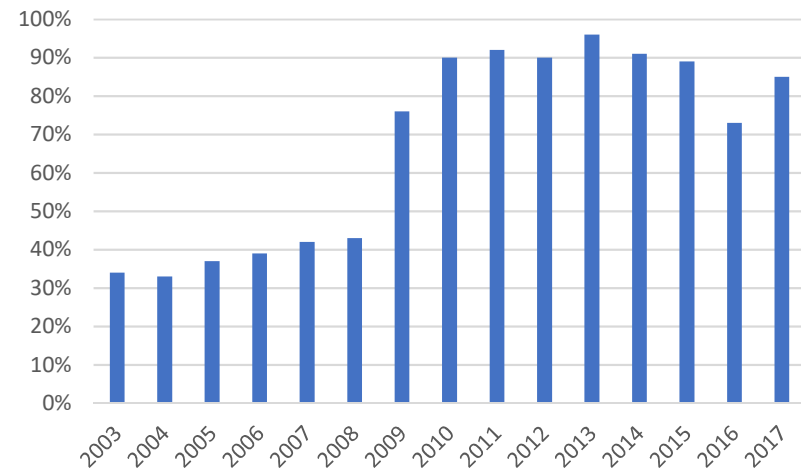
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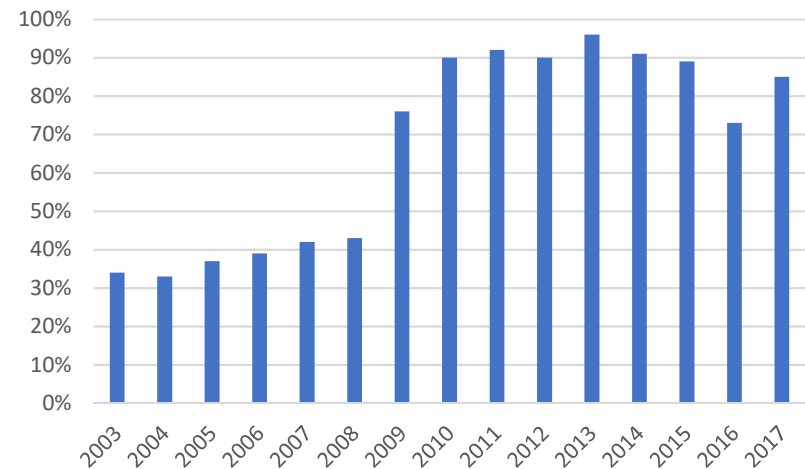
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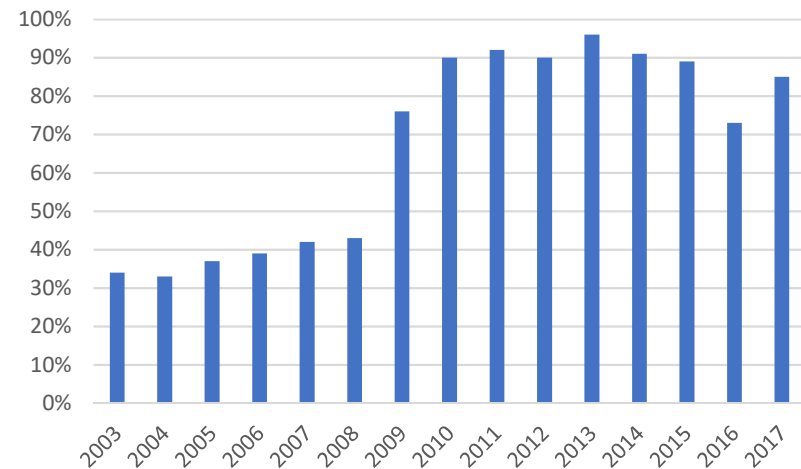


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Percent of Public Mergers Which Attracted Litigation



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LITIGATION LANDSCAPE HAS IMPACTED DEAL TERMS

- Acquirers are demanding and targets are (sometimes) granting stronger deal protection
 - Voting agreements that do not fall away on a change in recommendation
 - Force the vote provisions
 - Tighter post-signing market checks
- Absent conflicts of interest or topping bidders, transactions seem unlikely to be enjoined

THE NEW LITIGATION LANDSCAPE

- Tighter deal protection?
- Rise of shareholder activism
- Rise of mootness fee settlements/dismissals of pre-closing suits
 - Litigation outcomes resulting in mootness fees were near 0% of cases prior to 2014
 - In 2017, mootness fees were paid in 75% of suits
- Rise of appraisal actions
 - Barriers in Delaware to deal litigation have led to an increase in filings seeking relief under Delaware's appraisal statute
 - We are seeing record years for appraisal petitions filed
- Buyer Beware: Changes in the legal landscape doesn't mean the sharks aren't still in the water! Plaintiffs have and will continue adapt to the new regime



Sources: The Shifting Tides of Merger Litigation, University of Pennsylvania Law School, 2018; Shareholder Litigation Involving Acquisitions of Public Companies, Cornerstone Research, 2016

V&E'S LEADING ENERGY
PUBLIC M&A PRACTICE

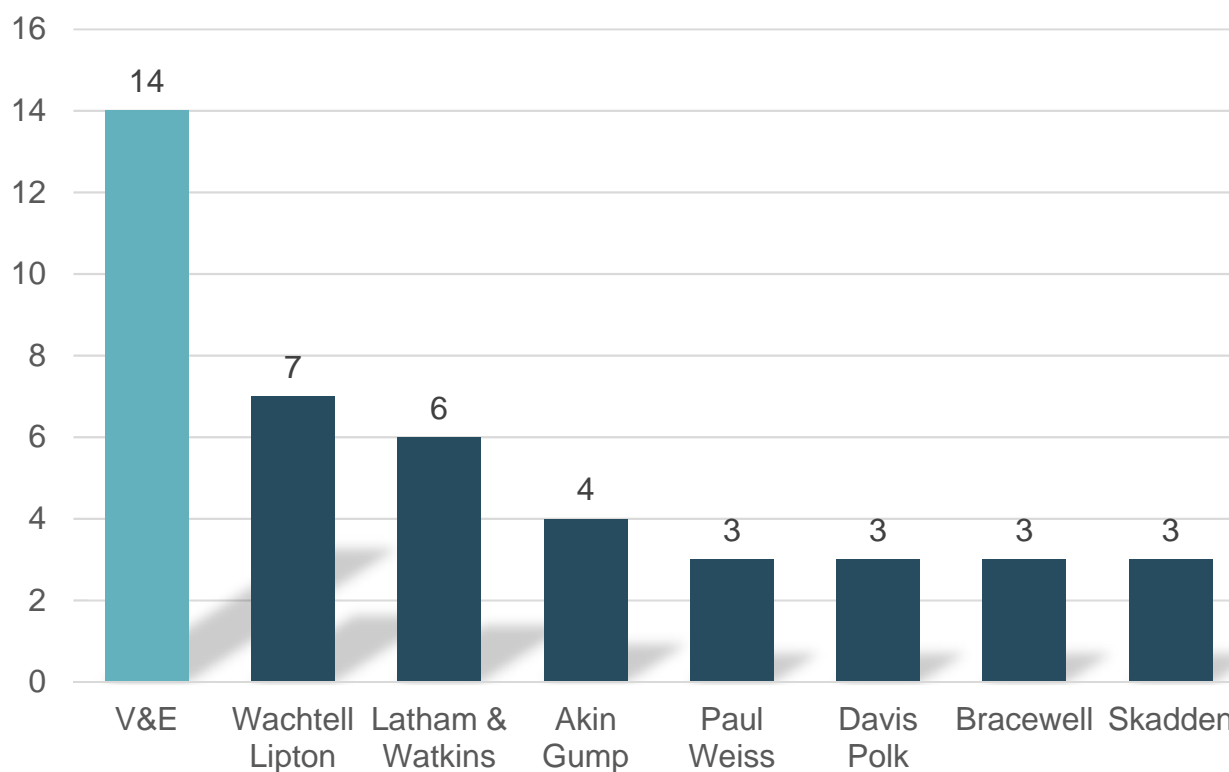


MORE PUBLICLY TRADED UPSTREAM COMPANIES AND THEIR BOARDS TURNED TO V&E TO HANDLE THEIR PUBLIC M&A THAN ANY OTHER LAW FIRM

“The team has a deep bench of talent and best-in-class client service. They’re great value, transparent and particularly strong for energy and deal execution expertise.”

– Chambers USA, 2018

TOP LEGAL ADVISORS IN UPSTREAM PUBLIC COMPANY M&A (23 Total Transactions) LAST 5 YEARS (2014- 2018)



The above summarizes results from a survey of the legal advisors for all transactions in the upstream energy industry since 2014 involving the acquisition of a public company listed on a U.S. stock exchange with a market capitalization of over \$100 million (Source: Capital IQ).

UPSTREAM PUBLIC COMPANY M&A*

LAST 5 YEARS (2014- 2018)

UPSTREAM				
Announced Date	Transaction Value (\$USDmm)	Target	Buyer	Legal Advisors
11/19/2018	\$1,656	Resolute Energy Corporation (NYSE: REN)	Cimarex Energy Co. (NYSE: XEC)	Target: Wachtell Buyer: Akin Gump
11/1/2018	\$8,059	Newfield Exploration Company (NYSE:NFX)	Encana Oil & Gas (USA) Inc.	Target: Kirkland & Ellis; Wachtell Buyer: Paul Weiss; Blake, Cassels & Graydon
10/30/2018	\$4,103	WildHorse Resource Development Corporation (NYSE:WRD)	Chesapeake Energy Corporation (NYSE:CHK)	Target: V&E Buyer: Wachtell; Baker Botts
10/28/2018	\$1,706	Penn Virginia Corporation (NasdaqGS:PVAC)	Denbury Resources Inc. (NYSE:DNR)	Target: Skadden Buyer: V&E
8/27/2018	\$411	Blue Ridge Mountain Resources, Inc. (OTCPK:BRMR)	Eclipse Resources Corporation (NYSE:ECR)	Target: Bracewell Buyer: V&E ; Norton Rose
8/14/2018	\$9,239	Energen Corporation (NYSE: EGN)	Diamondback Energy, Inc. (NasdaqGS:FANG)	Target: Wachtell Buyer: Akin Gump

 = V&E involvement

*Includes all transactions in the upstream energy industry since 2014 involving the acquisition of a public company listed on a U.S. stock exchange with a market capitalization of over \$100 million (Source: Capital IQ).

UPSTREAM PUBLIC COMPANY M&A*

LAST 5 YEARS (2014- 2018)

UPSTREAM (cont'd)

Announced Date	Transaction Value (\$USDmm)	Target	Buyer	Legal Advisors
3/28/2018	\$9,627	RSP Permian, Inc. (NYSE:RSPP)	Concho Resources Inc. (NYSE:CXO)	Target: V&E Buyer: Sullivan & Cromwell
11/21/2017	\$2,500	Stone Energy Corporation (NYSE: SGY)	Talos Energy	Target/Seller: Akin Gump Buyer: V&E
11/15/2017**	\$741	Bonanza Creek Energy, Inc. (NYSE: BCEI)	SandRidge Energy, Inc. (NYSE: SD)	Target: Kirkland & Ellis Buyer: V&E
6/19/2017	\$10,670	Rice Energy (NYSE: RICE)	EQT Corporation (NYSE: EQT)	Target: V&E Buyer: Wachtell
1/16/2017	\$3,357	Clayton Williams Energy, Inc. (NYSE: CWEI)	Noble Energy, Inc. (NYSE: NBL)	Target: Latham & Watkins Buyer: Skadden
7/21/2016	\$2,090	InterOil Corporation (NYSE:IOC; POMSoX:IOC)	Exxon Mobil Corporation (NYSE:XOM)	Target: Wachtell Buyer: Davis Polk

 = V&E involvement

*Includes all transactions in the upstream energy industry since 2014 involving the acquisition of a public company listed on a U.S. stock exchange with a market capitalization of over \$100 million (Source: Capital IQ).

**Transaction terminated

UPSTREAM PUBLIC COMPANY M&A*

LAST 5 YEARS (2014- 2018)

UPSTREAM (cont'd)

Announced Date	Transaction Value (\$USDmm)	Target	Buyer	Legal Advisors
7/22/2016	\$1,000	Centennial Resource Development (NASDAQ: CDEV)	Silver Run Acquisition Corporation (NASDAQ: SRAQ)	Target: V&E Buyer: Latham & Watkins
5/16/2016	\$6,882	Memorial Resource Development (NasdaqGS:MRD)	Range Resources Corporation (NYSE:RRC)	Target: V&E Buyer: Sidley Austin
5/21/2015	\$664	Eagle Rock Energy Partners (NasdaqGS:EROC)	Vanguard Natural Resources (NasdaqGS:VNR)	Target: V&E Buyer: Paul Hastings
5/11/2015	\$3,898	Rosetta Resources (Nasdaq:ROSE)	Noble Energy (NYSE:NBL)	Target: Latham & Watkins; Davis Polk Buyer: Skadden; Bracewell#
4/20/2015	\$535	LRR Energy (NYSE:LRE)	Vanguard Natural Resources (NasdaqGS:VNR)	Target: Latham & Watkins; Hunton Andrews Kurth Buyer: Paul Hastings
10/3/2014	\$433	Apco Oil & Gas International (NASDAQ:APAGF)	Pluspetrol Resources	Target: Weil, Gotshal; Maples and Calder Buyer: Cleary Gottlieb; Appleby

 = V&E involvement

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Bracewell partner is now a partner at V&E

UPSTREAM PUBLIC COMPANY M&A*

LAST 5 YEARS (2014- 2018)

UPSTREAM (cont'd)

Announced Date	Transaction Value (\$USDmm)	Target	Buyer	Legal Advisors
9/29/2014	\$6,980	Athlon Energy (NYSE:ATHL)	Encana (TSX:ECA)	Target: Latham & Watkins; Akin Gump Buyer: V&E ; Paul, Weiss; Blake, Cassels & Graydon
7/24/2014	\$2,867	QR Energy (NYSE:QRE)	Breitburn Energy Partners (NasdaqGS:BBEP)	Target: V&E Buyer: Latham & Watkins
7/13/2014	\$6,129	Kodiak Oil & Gas (NYSE:KOG)	Whiting Petroleum (NYSE:WLL)	Target: Dorsey & Whitney; Alston & Bird Buyer: Foley & Lardner; Simpson Thacher;
5/6/2014	-	Forest Oil (NYSE: FST)	Sabine Oil & Gas	Target: Wachtell Buyer: V&E
3/12/2014	\$2,187	EPL Oil & Gas (NYSE:EPL)	Energy XXI (NasdaqGS:EXXI)	Target: Sidley Austin Buyer: V&E

 = V&E involvement

*Includes all transactions in the upstream energy industry since 2014 involving the acquisition of a public company listed on a U.S. stock exchange with a market capitalization of over \$100 million (Source: Capital IQ).

THE TEXAS LAWBOOK: 2018 IN REVIEW

THE TOP 10 TEXAS M&A DEALS

V&E worked on **4** of the top **10** M&A deals of 2018 as reported by Texas Lawbook.

Energy Transfer Equity's \$62 billion purchase of Energy Transfer Partners

"No doubt, Energy Transfer Equity's acquisition of affiliate Energy Transfer Partners, which closed in November, was a blockbuster in terms of numbers. It involved \$27 billion in stock and \$35 billion in debt assumption to create a \$90 billion energy infrastructure giant."

Led by V&E Partners Lande Spottswood & Stephen Gill

RSP Permian's \$9.5 billion sale to Concho

"As oil prices moved upward earlier in the year, so did a wave of mergers between oil and gas explorers and producers. Concho Resources' \$9.5 billion purchase of RSP Permian announced in March was the first big one out of the gate."

Led by V&E Partners Steve Gill, Doug McWilliams & Lande Spottswood

Chesapeake's \$4 billion purchase of WildHorse

"Oklahoma oil and gas producer Chesapeake Energy Corp. surprised industry observers when it announced its \$4 billion purchase of WildHorse Resource Development Corp. in October."

Led by V&E Partners Steve Gill & Doug McWilliams

GIP's \$3.12 billion acquisition of Devon's EnLink interests

"Another surprise deal was Global Infrastructure Partners' \$3.12 billion purchase of Devon Energy's interests in EnLink Midstream Partners LP and EnLink Midstream LLC in June for \$3.12 billion."

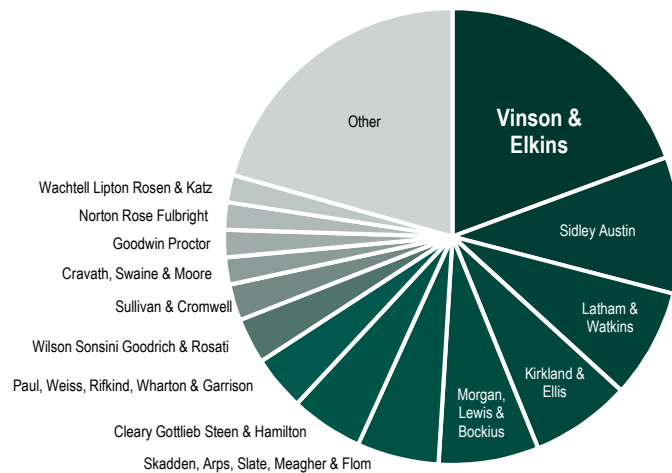
Led by V&E Partner Ramey Layne

SHAREHOLDER ACTIVISM

ACTIVISM DEFENSE LEAGUE TABLES

While not always applicable in a public M&A transaction, activism is becoming increasingly relevant. Activism can be a catalyst for a merger and can also result after signing, in opposition to a merger. Because it is difficult to predict whether activism will matter, it behooves public companies to have M&A counsel who is deeply experienced in shareholder activism defense.

Activist Insight's 2018 Intermediary Awards
Breakdown of law firm representation of issuers in 2018



Activist Insight Shareholder Activism Scorecard 2018
(by Number of Campaigns)

RANK	ADVISOR NAME	2018
1	V&E	30
2	Sidley Austin LLP	15
3	Latham & Watkins	12
4	Kirkland & Ellis	11
4	Morgan Lewis	11
5	Skadden	9

Wall Street Journal/FactSet SharkRepellent Activism Scorecard 2018 /2017
(by Number of Campaigns)

RANK	ADVISOR NAME	2018	2017
1	V&E	27	25
2	Wachtell	25	22
3	Latham & Watkins	15	8
4	Sidley Austin	14	7
5	Kirkland & Ellis	9	7
6	Morgan Lewis	7	11
6	Wilson Sonsini	7	6

THANK YOU

Austin
T +1.512.542.8400

Beijing
T +86.10.6414.5500

Dallas
T +1.214.220.7700

Dubai
T +971.4.330.1800

Hong Kong
T +852.3658.6400

Houston
T +1.713.758.2222

London
T +44.20.7065.6000

New York
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Richmond
T +1.804.327.6300

Riyadh
T +966.11.250.0800

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T +1.415.979.6900

Tokyo
T +81.3.3282.0450

Washington
T +1.202.639.6500

