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Extreme Takeover

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In his 39 years as a corporate lawyer, Andrew Bogen had seen his share of headstrong CEOs. So he wasn't especially surprised by the excitable man glaring at him across the room. Craig Conway, the president and chief executive officer of PeopleSoft, Inc., had good reason to be agitated. His company had just been targeted in a June 2003 hostile bid by software giant Oracle Corporation. To Conway, Oracle's bid had started an all-out war requiring the fiercest tactics. During an emergency meeting, Bogen, a partner at Gibson, Dunn & Crutcher, kept reminding Conway and the rest of PeopleSoft's board that there was this thing called Delaware law that required PeopleSoft to act carefully and deliberately and keep shareholder interests in mind.

Conway would have none of it. "I haven't heard a single creative thing," he snapped.

Bogen, a man with the lean, weathered look of a Clint Eastwood and a no-nonsense bluntness to match, wasn't about to be cowed by anyone, including a 50-year-old CEO. As usual, he didn't bother to sugarcoat his words. "I've been accused of a lot of things in my career," he answered. "But a lack of creativity isn't one of them."

The battle had just begun-and we're not just talking about the fight between Oracle and PeopleSoft. At crucial moments during the 18-month contest, PeopleSoft and its lawyers fought among themselves about as much as they jousted with Oracle. Lawyers and management clashed, and one by one they were shown the door; the lawyers fell first, and top executives followed. Classic ploys failed. PeopleSoft waived its lawyer-client privilege to make a point with a key Delaware judge and then sat back while a new counsel blunted its effect. It campaigned aggressively for the U.S. Department of Justice to intervene in the takeover, but then watched in horror as they drew one of the toughest judges in the West to preside over an antitrust suit. By the time it ended, the PeopleSoft battle had become the longest in U.S. history and the latest example of the tensions and wrenching choices faced by targets of mergers. Up against Oracle and its shrewd advisers from Davis Polk & Wardwell, even a united PeopleSoft team would have had trouble. But unity proved not to be an option.

Andy Bogen was already sweating when he heard about Oracle's bid. Early on the morning of June 6, 2003, he returned home from his daily jog through the streets of Santa Monica to find the light on his answering machine blinking. As he listened to the messages from his Gibson, Dunn partners, the 63-year-old lawyer learned about Oracle's unsolicited $5 billion tender offer. Its target, PeopleSoft, was a 15-year-old company based outside San Francisco in Pleasanton, California. It made the type of expensive "enterprise application software" that businesses use to manage tasks like payroll and accounts receivable. In effect, PeopleSoft, Oracle, and their principal competitor, SAP AG, had brought human resources into the high-tech age.

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Oracle offered $16 a share, a scant 89 cents above the stock's closing price the day before.

Bogen soon learned that not only were barbarians at the gate, but PeopleSoft had already stabbed itself in the foot. Caught off guard on a business trip to the Netherlands, CEO Conway had issued an incendiary press release without consulting with any legal advisers. "This is atrociously bad behavior from a company with a history of atrociously bad behavior," he stated. He later added that he "could imagine no price…to recommend accepting the offer." For good measure, he likened Oracle's chief executive officer, Lawrence Ellison, to Genghis Khan.

This, unfortunately, is the last thing a CEO should say when faced with a hostile bid-that is, if he wants to comply with the law of Delaware (where PeopleSoft was incorporated). To show that a company is concerned with the interests of shareholders, its leaders should initially state that the board will consider the bid and announce its position later. In Delaware, inciting a grudge match between CEOs is not, generally speaking, recommended.

Two days later, Bogen bluntly told the CEO that his intemperate statements had caused a problem. They were speaking for the first time during a PeopleSoft board meeting at Gibson, Dunn's Palo Alto office. Conway, still in Europe, was connected by speakerphone. Bogen had not worked for PeopleSoft before, although Gibson, Dunn was its regular corporate counsel. The board would have to go to extraordinary lengths to show that it was looking at this deal carefully, Bogen warned. It must proceed slowly, and deliberately, and be very cautious about any public pronouncements.

Conway passionately argued that he had to do whatever he could to save PeopleSoft. Ellison doesn't play by the book, he insisted. So neither could PeopleSoft.

Bogen, however, had helped write that book. In 1985 Bogen successfully led the defense team in arguably the most famous takeover case in the annals of Delaware law: Unocal Corporation's resistance to raider T. Boone Pickens. The Delaware Supreme Court upheld the company's novel defensive maneuvers, and laid out the standards that 20 years later still define the boundaries for a hostile bid defense. If the target can show that it reasonably perceives the bid to threaten its operations, the board can take defensive actions. But courts won't allow conduct that goes beyond what's considered reasonably proportionate to the threat, especially anything that suggests that management is principally concerned with "entrenching" itself.

For most of his life, Craig Conway was too busy moving ahead to spend much time thinking about entrenchment. The son of an American G.I. and a Sudanese mother, he grew up in the Midwest, in a working-class family that hopped from city to city, following jobs. A gift for math led him to the State University of New York, where he also found an outlet for his competitive streak: judo. A hard-charging engineer who was also a born salesman, Conway climbed the New Economy ladder, building and selling two companies. He took over PeopleSoft in 1999 from its beloved founder, the Hawaiian shirt-clad David Duffield. Conway revived the company, cutting costs and raising goals. In his view, he had only begun. Just before the Oracle bid, Conway had launched a friendly takeover effort of his own, signing a deal to acquire J.D. Edwards & Company, a smaller back-shop software outfit.

Conway knew Oracle well. He had worked at the Redwood City, California- based company for eight years, until he was fired in 1992. Conway's animus for Oracle-he called its executives "psychopaths" in an e-mail-surely fueled his hostility to Oracle's bid. But it's easy to understand why most companies wouldn't want to be become the prey of Ellison, a CEO infamous for his heavy-handed ways.

Oracle's bid had been triggered by PeopleSoft's announcement four days earlier that it planned to acquire J.D. Edwards. With this $1.7 billion deal, PeopleSoft would displace Oracle as the second-largest maker of enterprise application software. When Safra Catz, then an Oracle executive vice president, learned the news, she typed an e-mail to Ellison. "Now would be the time to launch on PSFT," she wrote, using PeopleSoft's stock trading symbol. "Just what I was thinking," replied Ellison.

Conway viewed Oracle's low bid as a diabolical scheme to cripple PeopleSoft, not as a legitimate offer to buy the company. And maybe Conway was right. Near the start of its bid, an investment banker advising Oracle wrote an e-mail to Catz in which he described the initial bid as a "twist in the wind" strategy. The banker, Joseph Reece from Credit Suisse First Boston LLC, advised Catz to stay with this low bid "to create doubts in the minds of the market." In time, he wrote, "we should see a decline in the price [of PeopleSoft]."

"There was a lot of skepticism about whether the bid was real," says Chris Varelas, the global head of technology, media, and telecom investment banking at Citigroup Inc., one of PeopleSoft's investment bankers. Companies doing friendly deals typically offer the target's shareholders in the range of a 25-30 percent premium over the trading price, he says, and hostile bids often require an additional 5-10 percent bump. Oracle's $16 bid was less than 6 percent over the previous day's price. At a minimum, Ellison seemed to be trying to thwart the J.D. Edwards deal. Or he might be trying to destroy PeopleSoft by scaring customers away.

PeopleSoft was much more vulnerable to a continuing hostile bid than most companies. Consumers won't stop buying their favorite soap if the maker is acquired: The soap still works. But PeopleSoft's customers required expensive technical support, which often cost more than the software itself. Who wants to buy software from a company that might not be around to service it next year? Ellison insisted that his company would give enhanced support to customers using PeopleSoft applications. But he had created enough uncertainty about what would happen to PeopleSoft and its products that several influential analysts and consultants advised customers to delay placing orders.

PeopleSoft was in a bind. If it didn't reassure customers that it would stay independent, sales could dry up. If it did reassure customers that it would stay independent, it would look like management wasn't concerned about maximizing shareholders' value. "From [a customer's] standpoint, what Craig said was exactly right," says director A. George "Skip" Battle about Conway's early rhetoric. "But from a Delaware court standpoint, it looked awful." At the first board meeting, Battle reinforced Bogen's admonition to Conway to tone down his public statements. "I told Craig, 'There is a point at which we'll sell to Oracle,' " he says.

That point was a long way off. The company and its counsel weren't looking for a deal. Instead, they searched for obstacles they could toss in Oracle's path.

At the first board meeting after Oracle's bid, PeopleSoft's chief financial officer, Kevin Parker, told the board about his idea for a novel "customer assurance program" that would keep sales flowing. The CAP, as it was called, would be written into software sales contracts and would require an acquiror to pay customers up to five times the software purchase price if the acquiror didn't offer similar support and products.

Also at that meeting, Bogen advised the board to form a "transaction committee" of independent directors. Such independent committees are not common in hostile deals, but Bogen believed the board should distance itself from Conway's comments. PeopleSoft's seven-member board had three directors considered insiders, including Conway and PeopleSoft's founder Duffield. The remaining four directors made up the transaction committee. They were led by Battle, the 61-year-old chairman and former CEO of the search engine company Ask Jeeves, Inc., who had previously been a managing partner at Andersen Consulting.

Bogen also explained to the board that PeopleSoft didn't have to be rushed into a decision. Even if PeopleSoft's shareholders thought the $16 bid was a good deal, they couldn't sell. Oracle's tender offer was contingent on PeopleSoft revoking its "poison pill." PeopleSoft, like thousands of corporations in America, had adopted this corporate device that made it prohibitively expensive for a hostile bidder to buy it. The poison pill allows the target to sell lots of cheap stock to its shareholders, inflating the purchase price an acquiror would have to pay. Delaware courts have upheld poison pills as a way to give targets some breathing room and bargaining leverage. PeopleSoft thought that if it could just hold on for a few months, Oracle would go away. Rarely do hostile bids last much longer. But with more than four times the revenue of PeopleSoft-most of its revenues comes from database software-Oracle could afford to hang on.

On June 11, 2003, the PeopleSoft board rejected Oracle's offer, citing the low price and a significant likelihood that the deal would not get antitrust approval from the government. Gibson, Dunn viewed antitrust issues as PeopleSoft's primary line of defense. A merger that united two of the three powerhouse players in this software market had a good chance of being blocked. A week later, Oracle raised its price to $19.50, which PeopleSoft again rejected.

Oracle dug in. Davis Polk's William Kelly, who led the Oracle corporate team, concedes that Oracle's bid wasn't generous. "Was the premium on the low end?" asks the 51-year-old Menlo Park partner. "Yeah." Still, he says that was no excuse for PeopleSoft's refusal to negotiate. "The notion that somebody starts with a modest premium, and you don't deal with them, I don't understand," he says. But PeopleSoft feared that if it made the slightest move toward negotiations, the word would leak out, and customers would stop buying its software.

Gibson, Dunn was preparing for battle, assembling a team of more than 25 lawyers to fight on several fronts simultaneously. The firm thought it was going to lead the antitrust effort, but PeopleSoft had another idea. Without consulting with Gibson, general counsel Anne Jordan hired Gary Reback as lead antitrust counsel. Brilliant and exceptionally intense, the 55-year-old lawyer is best known as the man who pursued an antitrust crusade against Microsoft Corporation on behalf of Netscape Communications Corporation. In 1996 Wired magazine put Reback on its cover and announced he was "the only man Bill Gates fears." In recent years, however, Reback had faded from

prominence. He left Wilson Sonsini Goodrich & Rosati in 2000, briefly headed a start-up, Voxeo Corporation, and, by the summer of 2003, was of counsel at Palo Alto's Carr & Ferrell, focusing more on writing than practicing law. General counsel Jordan says Reback was recommended by some partners at Carr & Ferrell, where she had previously worked.

Conway and Reback set off on a road show. They met first with Connecticut's governor and attorney general. Connecticut, like many states, used PeopleSoft products to run its operations. Conway's message: An Oracle takeover would cost the state millions, as it would be forced to switch to other products. Connecticut quickly sued to block a deal, followed eventually by nine other states. Starting in July 2003, Reback also began meeting with lawyers from the Justice Department, urging them to stop Oracle.

Conway and Reback admired each other's aggressiveness. "Gary and Craig had a very close relationship," says director Battle. "Craig had enormous confidence in Gary." But Reback's style did not mesh well with the careful Gibson, Dunn approach. Because Reback didn't bring a team of associates to assist him, the Gibson, Dunn antitrust lawyers functioned as his support. It's common for interested parties to petition the Justice Department to bring an antitrust case, but Gibson, Dunn worried that this hard sell might backfire. It could put off government officials, and give Oracle grounds to argue that PeopleSoft management wasn't open to getting a good deal for shareholders.

While Reback and Conway were jetting about the country, Gibson, Dunn's army was busy on multiple fronts. Bogen oversaw strategy on the hostile bid. The antitrust team, led by San Francisco partner Joel Sanders, worked to secure clearance for the J.D. Edwards merger, while also assisting Reback. A corporate team, led by San Francisco partner Douglas Smith, scrambled to restructure the J.D. Edwards deal so that it could close quickly without a vote by J.D. Edwards shareholders. (They hoped Oracle would drop its bid if PeopleSoft acquired the smaller company, which it believed Oracle didn't want.) Gibson litigators, meanwhile, led by Wayne Smith in Orange County, launched an unusual lawsuit in Oakland superior court, near PeopleSoft's headquarters. They alleged that Oracle's offer and tactics tortiously interfered with PeopleSoft's business opportunities and constituted unfair competition. Claims like these aren't novel, but this appears to have been the first time they've been used as a hostile takeover defense.

For its part, Oracle wasn't sitting back. On June 18 Davis Polk and Wilmington's Richards, Layton & Finger filed a lawsuit in Delaware Chancery Court seeking an injunction against the use of PeopleSoft's poison pill. They also asked the judge to invalidate the customer assurance program, labeling it an overreaching antitakeover defense. Outside of court, Davis Polk's Kelly was gearing up for a proxy fight to try to elect a majority of Oracle-friendly directors to PeopleSoft's board.

In this regard, PeopleSoft had a huge problem. Proxy contests are such a basic tactic in takeovers that many companies have "staggered" boards to prevent a bidder from gaining a majority of seats in one vote. Such boards are almost always structured so that only a third of a company's directors are elected each year. When PeopleSoft's board was structured in 1995 by Wilson Sonsini, the firm staggered the board in just two pieces. Half of its eight directors would be up for election in March 2004. (A director had been added from J.D. Edwards.) Wilson partner Henry Massey, Jr. says many Silicon Valley companies don't adopt anti-takeover devices and that PeopleSoft's board initially only had four or five directors.

By August of 2003, just two months into the fight, Gibson, Dunn wasn't getting along with its client. To bolster their arguments that Oracle's tactics had hurt PeopleSoft's sales, Gibson litigators wanted to interview customers. But general counsel Jordan said no; instead, she assigned that task to a small Chicago firm, Mandell Menkes & Surdyk, that had handled customer disputes for Jordan in the past. Jordan explains that the Chicago lawyers "were particularly effective in knowing where to get information."

But this didn't work for Gibson, Dunn. "I pleaded to be able to have our team contact customers," says litigation partner Wayne Smith. "[Jordan] had two partners from Chicago doing something that I would have put 12 lawyers on and done in a week to 12 days. Instead, it dragged on for weeks." And Smith says he had trouble getting access to the information that the Chicago firm did collect. As a result, he says, PeopleSoft's cases in Oakland and Delaware suffered.

Director Battle says he knew that Gibson, Dunn was frustrated and blames the general counsel. "Anne Jordan was overwhelmed in the sense of volume," he says. "She probably was not delegating as she might have been. Things were very slow getting done, causing Gibson, Dunn to be very concerned." Jordan says she and her legal department were stretched thin, especially since they were also juggling the J.D. Edwards deal, but that was to be expected in such an extraordinary situation. (She had 25 in-house lawyers when the hostile bid started and 35 after the J.D. Edwards merger closed in August 2003. But many were experienced drafters of licensing contracts, not corporate M&A experts or litigators.)

Conway remained as irrepressible as ever. At board meetings the CEO was brimming with ideas about ways to fend off Oracle. He suggested packing the board with more directors, or launching a hostile bid on the Oracle division that made applications software. An exasperated Bogen told him that these notions wouldn't work. "Craig wanted out-of-the-box thinking," says Citigroup's Varelas. "Craig said, 'Don't give me the playbook.' But a good defense can often be about executing the playbook well."

The bad chemistry strained strategy sessions. "I'm not sure Craig had the patience to sit through a lecture by Andy Bogen or anyone at Gibson, Dunn," says Jordan's deputy, David Chavez. He says the firm wanted to run everything, which didn't square with Conway's view of the world. "The institutional ego of Gibson, Dunn was equal, if not exceeded by, the ego of Craig Conway," Chavez says.

Conway continued to play up his personal war with Ellison. Soon after the bid, Conway had remarked that selling PeopleSoft to Oracle would be like asking him to sell his dog to Ellison, so that he could shoot it. Ellison responded: "If Craigy and [his dog] were standing next to each other and, trust me, I had one bullet, it wouldn't be for the dog." In September 2003 Conway walked onto the stage at a company sales conference with his black Labrador, Abbey. Both man and dog wore bulletproof vests. After a video replayed Ellison making his bullet comment, Conway joked that "Abbey and I decided we weren't taking any chances." The crowd laughed and applauded.

That was clever and amusing, but Conway's penchant for bold statements would get him in trouble. During a question-and-answer session with analysts that same month, Conway downplayed the effects of Oracle's bid. "It's a movie that's been playing a long time," the CEO commented. "I don't see it as a disruptive factor." To the salesman in

Conway, it was the perfect pitch. Unfortunately, he was undermining the company's litigation position that Oracle's tactics were crippling its business. Bogen confronted Conway: You should have cleared your remarks with your lawyers first, he said. Bogen expected the CEO to explode, but this time Conway agreed that Bogen was right.

By September 2003, the PeopleSoft legal team was in turmoil. The Gibson, Dunn lawyers working with Reback were ready to mutiny, straining under his demands for documents and files. Reback needed to respond to exhaustive requests from the Justice Department, which had asked for hundreds of customer contracts and other bid information. One Gibson, Dunn antitrust partner suffered a major heart attack, at the age of 45.

Conway was impatient and let his annoyance show. Litigator Wayne Smith recalls when his team prevailed in a discovery dispute and won an extraordinary order from Delaware vice-chancellor Leo Strine, Jr., that required an Oracle lawyer to affirm that he had personally searched the hard drives of all of Ellison's computers for relevant e-mails. Smith says that instead of being pleased, Conway was upset because Strine had set a 24-hour time limit for this search; Conway thought it should be done sooner. Conway, who agreed to answer selected questions for this article, says he does not remember responding this way.

At one point the CEO scribbled an undated handwritten note to prepare for a board meeting. He outlined the law firm's faults: "Big-slow, caliber is inconsistent; not strong leadership or coordination.…Andy is unglued and determined to find something harmful." In that same note Conway raved about Reback: "Established himself as an insider … high attention to detail … little tolerance/patience for incompetence-and he shows it." Assistant general counsel Chavez doesn't fault Gibson, Dunn, but notes, "Our CEO was becoming frustrated … and wanted something done to shake things up."

Conway thought he had found the answer: Joe Montana's former lawyer. With the board's approval, Conway hired Harvey Leiderman in September 2003 as PeopleSoft's special counsel for Oracle matters. A partner at San Francisco's 75-lawyer Steefel, Levitt & Weiss, Leiderman had no experience with hostile takeovers. The amiable lawyer did, however, have a fleeting personal relationship with Conway. The two had first met 25 years earlier through Conway's former neighbor, Montana, the famous ex-San Francisco 49er quarterback. Leiderman had represented the athlete in endorsement deals. When Conway needed a lawyer after his home slipped off its foundation during a rainy season, he called Leiderman. Though they had only sporadically been in touch since then, Conway still remembered that he felt comfortable with the lawyer. "Craig had the good fortune of not having to deal with attorneys most of his life," notes Leiderman. "[During the hostile bid] he soon found himself up to his ears in lawyers.… I think I was the only lawyer he trusted."

Leiderman, 57, essentially assumed the duties of a general counsel for the Oracle fight, even though Jordan was still at PeopleSoft. He promptly moved into an office on the company's executive floor, and his written job description outlined his mandate: develop master legal strategy; approve outside counsel tactical actions; approve and monitor legal budgets.

As one of his first tasks, Leiderman turned to the dysfunctional relationship with Gibson, Dunn. In September 2003 he invited nine partners, including Bogen, to participate in a

Saturday meeting at his firm. In a conference room overlooking the Golden Gate Bridge, he asked questions about the status of various legal matters and listened to their concerns and complaints. “The problem they had was that they were looking to a chain of command going into the general counsel’s office, and Anne Jordan was so engaged with the J.D. Edwards deal,” says Leiderman. “[The situation] lacked leadership.” He also thought that the Gibson, Dunn team wasn’t well organized for a protracted battle. “It was being run like an emergency room, rather than a full-service hospital,” says Leiderman.

In early November 2003, Gibson, Dunn litigator Wayne Smith succeeded in defeating a motion to dismiss brought by Oracle in the Oakland unfair competition case. When he called Leiderman to report the news, Leiderman asked Smith to meet him at PeopleSoft headquarters. Leiderman congratulated Smith on the result. Then he told Smith that he and his litigators were fired. New York’s Cleary Gottlieb Steen & Hamilton would take over the Delaware case. For the Oakland state court fight, Leiderman hired a small, highly regarded San Francisco litigation boutique, Folger Levin & Kahn.

Smith left the meeting and called his wife. “I just got out of jail,” he told her.

PeopleSoft didn’t jettison the whole Gibson, Dunn team. Bogen continued as lead M&A lawyer, his partner Douglas Smith kept handling the Securities and Exchange Commission filings, and the antitrust lawyers kept working under Reback. But most of them weren’t long for this battle.

Bogen soon crossed the line with Conway for the final time. The problem started in September 2003, when Bogen met with general counsel Jordan and CFO Parker. The two told him they had made a significant change to the language in the customer assurance program and sent out new contracts. Bogen was astounded. He chastised Jordan, telling her that the board should have approved those changes. Bogen feared that these revisions-which would have triggered the customer assurance program if there was a change in the composition in the company’s board-could be seen as an antitakeover defense that wouldn’t pass muster under the Unocal standard. “I don’t think there was ever a Delaware case where management [took defensive measures] on its own without the board being involved,” Bogen says. The language was soon corrected. Bogen told the board that Jordan should be relieved of duties related to the takeover defense.

Jordan counters in a recent interview that many people were involved in drafting and reviewing the CAP language. “It was a collective process, and no one group inside or outside the company can solely be credited with the final language,” she says. Jordan also adds, “The company and the board followed the advice of counsel as far as what was required under Unocal.”

Bogen was also concerned that PeopleSoft might not be able to record revenue from these contracts because of this contingent CAP obligation. Recording revenue for long-term software contracts is a complicated matter. He met with the company’s auditors, and with Battle and director Steven Goldby. (Bogen says the auditors at KPMG LLP concluded there wasn’t a problem.) Conway was upset when he found out about these meetings, according to these directors’ later testimony in Delaware. Bogen could fuss about Delaware law, but revenue recognition was a life-and-death matter for PeopleSoft.

In late November, Battle called Bogen: You're off the team, he said. The director, who had a good relationship with Bogen, told the lawyer that he liked him and his advice, but said he didn't have an effective relationship with management. Bogen was disappointed, but not really surprised. He understood, he said. The relationship had turned dysfunctional. In an interview in February, Battle says he would work with the Gibson, Dunn partner again "in a heartbeat." (In fact, earlier this year Battle hired Gibson, Dunn to handle the $2 billion sale of Ask Jeeves to Barry Diller's corporate group.) But, he says, "the day-to-day working relationship [with management] got to a point where we were frozen." (The lone Gibson, Dunn survivor, corporate partner Doug Smith, would still continue to handle securities filings.)

Though Battle says that Conway had objected to Bogen's talking directly to directors about this, Battle insists that the board didn't fire the lawyer at the CEO's insistence. Bogen had previously been keeping the transaction committee informed on a range of issues without Conway's clearance. "That bothered Craig a lot," notes Battle. "That didn't bother me." Contrary to the directors' sworn testimony, Conway insists he wasn't upset with Bogen. "I don't look back on my relationship with Andy as problematic," he says. "We were looking for a law firm that was more specialized."

In Bogen's place, Cleary Gottlieb partner Victor Lewkow emerged as PeopleSoft's new M&A adviser. A personable and slightly rough-around-the-edges New Yorker, the 55-year-old Lewkow had a better touch with Conway. He patiently listened to the CEO, and could talk him out of ideas without seeming harsh. "Vic is a very sweet and disarming man," says Battle. Lewkow's younger partner David Leinwand, who worked on this deal, says Lewkow has a forgiving personality. "Things roll off Vic's back," he says. "He keeps things in perspective, and his ego doesn't get bent out of shape easily."

That couldn't be said for Gibson, Dunn's antitrust team, which had reached its breaking point. In a December, 4, 2003, showdown before the board, they argued that Reback was too aggressive and they couldn't work with him. Reback appeared separately and explained his strategy for pushing the Justice Department to act. Cleary antitrust partner Mark Leddy, participating by phone from London, said he thought Reback should continue as the lead antitrust lawyer, and the board agreed. The Gibson antitrust team resigned and was replaced by Leddy and a Cleary team, with Reback remaining as the lead counsel.

The departures weren't over. Around this time, general counsel Jordan faded from the takeover battle. Battle would later testify that she was "removed" from her position. Jordan insists this isn't so, but agrees that she started focusing more on other legal matters besides the takeover. She eventually left PeopleSoft in July 2004, and was replaced by James Shaughnessy, a former in-house lawyer at Hewlett-Packard Company.

By the start of 2004, the new legal team was operating more smoothly. Leiderman was able to bring some order to what had been a chaotic situation. But two problems loomed. First, the Justice Department still hadn't decided whether to bring an antitrust suit. In January, Reback gave the Justice lawyers a lengthy "white paper"-provocatively entitled "A Hostage Taking"-that laid out the case for the government to block a deal. Reback and Cleary antitrust partner Leddy also had several meetings with senior Justice officials. Second, PeopleSoft's annual shareholder meeting was approaching in March, with Oracle's proxy fight the main attraction.

It was now seven months into this hostile bid, and PeopleSoft had never imagined it would still be fighting Oracle. To the surprise of many, Conway and his team had kept PeopleSoft's sales up. Revenue jumped as expected after the J.D. Edwards deal closed in the third quarter of 2003, and subsequent quarterly figures also rose. But the cost of the takeover defense was draining the bottom line. Net income in 2003 decreased 53 percent from the year before to $85 million, with more than half that decline-$46.2 million-spent on fees for lawyers, investment bankers, and others working on Oracle's bid.

In early February 2004, roughly a month before the annual shareholders meeting, Oracle threw down the gauntlet. To prevail in a proxy fight, it had to put an attractive offer on the table. It raised its bid by a hefty $6.50 a share to $26 and declared it the final offer. It was the first time since June 2003, the month the takeover started, that Oracle had lifted its price. Although this bid was 19 percent above the stock's trading price, PeopleSoft rejected it, calling the bid inadequate and citing the uncertainty of antitrust clearance.

PeopleSoft looked prescient: On February 26 the Justice Department filed United States of America v. Oracle Corporation in San Francisco federal court, seeking to block a merger. But almost immediately, the case looked less than rosy: Federal district court judge Vaughn Walker, 60, would hear the dispute. The former Pillsbury Madison & Sutro partner is well versed in antitrust, but he's also known as an independent thinker who wouldn't be deferential to the government. Walker set a tight schedule, with a trial to begin in three months.

Oracle abandoned its proxy contest when the Justice Department sued, deciding to await that outcome. About a month before trial, Oracle dropped its bid from $26 to $21, citing the drop in PeopleSoft's stock price. The offer, which still represented a 20 percent premium, was rejected.

The three-week trial began on June 7, 2004. Oracle, represented by Latham & Watkins, argued that the relevant market for PeopleSoft's software was more competitively robust than the Justice asserted [see "Dashed Dreams."]. Since PeopleSoft was not a party in this case, its leaders and lawyers had to watch passively from the sidelines. Reback, Conway, and Cleary's Leddy followed the proceedings from the front row.

But Reback didn't just sit there. Each night, he posted a daily trial blog on the PeopleSoft Web site. (Reback says the company initiated the idea for these communications, asking him to update its employees.) Reback's blog kept Lewkow busy, too. The Cleary partner figured that Reback's journal should be filed with the SEC as a company statement. So each night, the Cleary partner sat down to edit Reback's lengthy entry before it was posted, at times wrangling with him to tone down his language. In more than 31,000 words covering every day of trial and final arguments, Reback spun a relentlessly positive note. His entry for the last day of trial testimony boldly stated: "Oracle's case should be characterized as a complete failure of proof."

Judge Walker didn't agree. On September 9 Reback was walking into the lobby of a client's office when his cell phone rang. It was a reporter from The New York Times, telling him that Walker had ruled. "Who won?" Reback asked. "The government," the reporter responded at first. Reback was thrilled. But she quickly corrected herself and said that Oracle had won. Reback called Leiderman, who had seen the decision. "What

is it that Walker found the government failed to prove?" he asked. "Everything," Leiderman responded.

"It was the gloomiest period of the whole 18 months," recalls Citigroup's Varelas. Fifteen months into the hostile bid, PeopleSoft's most potent defense looked dead. Three weeks later, the government declined to appeal. And PeopleSoft's business was suffering. Somehow, miraculously, Conway had managed to keep sales rising, but income was tumbling. Earnings for the second quarter of 2004 came in 70 percent below the year before. Fees for lawyers and investment bankers were piling up at a rate of $4.5 million a month.

The same day that Walker released his devastating ruling, Andy Bogen walked into Davis Polk's Menlo Park office. He settled into a conference room to have his deposition taken by Davis Polk associate Zachary McGee.

Early in the litigation, PeopleSoft had decided to waive the attorney-client privilege for communications with its board. This choice, not unheard of in a hostile bid, would let the company argue that its directors had acted reasonably by relying on the advice of its counsel. But PeopleSoft hadn't counted on its lead M&A lawyer being fired.

During the videotaped session, McGee showed Bogen the Conway notes that disparaged Gibson, Dunn and labeled Bogen as "unglued." Bogen laughed. As the deposition wore on, Bogen's testimony wasn't always helpful to PeopleSoft. He said he'd told PeopleSoft's board that the CAP changes in the fall of 2003 had created a problem under Delaware law. "We really didn't have a record that in my view would sustain the Unocal test," he said. On the subject of his firing, Bogen's testimony was also potentially troublesome. Bogen said that while an accumulation of things led to his firing, it was brought to a head when he angered Conway with his decision to approach directors directly with concerns. This gave Davis Polk ammunition to argue that the PeopleSoft transaction committee wasn't insulated from Conway.

During the deposition, the lawyer representing PeopleSoft, Donald Wolfe of Wilmington's Potter Anderson & Corroon, repeatedly told Bogen not to answer questions about advice given to Conway and others outside of formal board meetings. (Bogen was not separately represented.) Davis Polk's McGee phoned partner Michael Carroll in New York to ask how to handle these objections. Carroll told the associate to let it go; he had an idea for how he'd throw this tactic back at PeopleSoft.

At a pretrial hearing, Carroll argued that PeopleSoft should be barred from using an advice of counsel defense because it had refused to disclose all communications between counsel and directors. PeopleSoft can't have it both ways, Carroll maintained. Vice-Chancellor Strine agreed. Thus, PeopleSoft had waived the attorney-client privilege for nothing, and in the process its lawyer had given testimony that Oracle could use to damage it. "They paid a price for using the defense, and then in the end they were not allowed to use it," says Carroll.

Wolfe, however, asserts that Bogen's testimony about the Unocal problem didn't amount to much, since the board had fixed the CAP problem by the time Bogen had relayed this warning. He also notes that Vice-Chancellor Strine ruled that Oracle's use of Bogen's testimony opened the door to let PeopleSoft use other statements from his deposition. "Andy also had some good testimony [for PeopleSoft] about the board process and the

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antitrust issues," says Wolfe, "and in the end I think that was more helpful."

Another deposition would cause even more turmoil. On August 26, 2004, Conway had been deposed by Carroll and David Balabanian, a partner at Bingham McCutchen who was defending Oracle in the Oakland case. (Discovery in the cases was coordinated.) Balabanian asked Conway about his statements to analysts in September 2003 that Oracle's bid wasn't hurting PeopleSoft. Conway didn't bother to finesse his answer.

"Did you make those statements?" Balabanian asked.

"Yes," Conway answered.

"Were they true?"

"No, they weren't true," Conway said.

Balabanian pressed the point.

"The statements were not true?"

"The statements were promotional," Conway said.

"True? False?"

"Absolutely not true," he bluntly answered.

Balabanian and Carroll were astounded; CEOs don't admit to baldly lying to the public every day. Was Conway poorly prepared, the Oracle lawyers wondered, or did he refuse to listen to his lawyers? Cleary litigation partner Max Gitter, who represented Oracle at the deposition, declines to comment about the preparation of Conway.

At that point, Carroll asked Conway if anyone represented him individually, besides the Cleary lawyers. Conway said no. Carroll asked if he had thought about consulting with lawyers of his own about the significance of a CEO making false statements. He said he had not.

Four weeks later, in late September, Leiderman received a large package from Oracle associate general counsel Dorian Daley, who was overseeing the takeover litigation. Included was a copy of Conway's original deposition with his troublesome statements highlighted. In a lengthy letter, she insisted that Leiderman give this to the board. Leiderman immediately called PeopleSoft's new general counsel, Shaughnessy. The two were puzzled. Why was Daley pushing the Conway deposition in front of the board? They suspected that Daley might be trying to set up PeopleSoft to look bad in the Delaware trial, set for October. Says Shaughnessy: "I can only think their calculation was to show that our board was so dominated by management, that even in the face of this nasty stuff-the CEO's testimony-they won't do anything."

Daley explains that she sent these materials because it wasn't clear that PeopleSoft's advisers were keeping the board properly informed. "Their legal team did not seem to be working together," she says. "They did not have the same cohesiveness that we did, and it was not clear who was running things." If PeopleSoft's board saw these materials,

From www.law.com/jsp/tal/PubArticleFriendlyTAL.jsp?id=1114798471468 6 October 2006

Oracle thought, they might strike a deal and avoid a trial in Delaware.

When director Battle saw the transcript, he was upset with Conway for what he said and with Cleary for not informing him of this bad testimony. “It would have been helpful if we had known earlier,” says Battle. Lewkow notes that the deposition transcript wasn’t ready for a week, and by then PeopleSoft was consumed with deciding what to do in the wake of Judge Walker’s decision. “It was an incredibly hectic time,” he says.

Soon after, Lewkow told Conway he should get separate counsel. Conway lined up Cooley Godward chairman Stephen Neal, who has represented such embattled public figures as Walter Hewlett and savings and loan operator Charles Keating, Jr.

Around 9 p.m. on September 30, Conway arrived at Gibson, Dunn’s Palo Alto office for a hastily called special meeting of the board. Gibson, Dunn corporate partner Doug Smith led him to a second-floor conference room. As Conway waited, PeopleSoft’s other directors met downstairs and voted unanimously to remove him as CEO. Around 11 p.m. directors Battle and Goldby went upstairs, and Battle delivered the news to Conway. Battle says that Conway acted professionally; Goldby would later testify that Conway was very quiet. Because he was fired without cause, he received a $13.7 million severance package. He also agreed to resign from the board.

Davis Polk’s carroll was talking to Safra Catz at Oracle headquarters on October 1 when they learned from news reports that Conway had been fired and replaced with 64-year-old founder Duffield. “Sometimes things happen, and you think it’s too good to be true,” recalls Carroll, who was preparing to begin trial in Delaware in three days. “Firing the CEO, that’s a pretty desperate move. No good comes of that.” Carroll suspected that a nervous PeopleSoft board thought that sacking the leader could establish its independence in court. That night the Davis Polk partner took a red-eye flight back east: “I remember thinking on the plane, let’s make sure there’s not some clever trick here, some sandbag.”

Not many hostile takeover cases go to trial, and the Delaware court hadn’t ruled on the validity of poison pills in years. Carroll would assert that PeopleSoft’s directors were not safeguarding shareholders’ interests. They lacked independence, he claimed, and had given management free rein to thwart the tender offer.

The case would be heard by Vice-Chancellor Strine, known as a bit of a maverick in Delaware for his willingness to shake up the state’s often-predictable corporate law. With nearly a year and a half having passed since Oracle’s initial bid, it was getting hard to argue that PeopleSoft’s poison pill was needed to give the company leverage to negotiate a fair deal. Just as interesting was how Strine would view the customer assurance program, which had created a $2.5 billion contingent liability.

When the trial started on Monday, October 4, the 48-year-old Carroll got right to the point. Without having done any depositions on Conway’s firing, the Davis Polk partner asked his first witness, director Goldby, the sort of open-ended question that trial lawyers rarely risk.

“Could you tell us, please, why Mr. Conway was fired?”

“Well, it’s a long story,” Goldby replied.

“I’ve got all day,” said Carroll.

Goldby explained there had been a gradual erosion of the board’s confidence in Conway. Carroll reminded Goldby that the board had known about Conway’s comments to analysts, made in 2003, for more than a year. The CEO’s deposition was relevant, Goldby said, but was not necessarily the reason for his firing. Goldby also explained that several senior executives were threatening to quit because of Conway’s abrasive style, and the board was worried about product development. In addition, the timing of the firing was driven by the board’s desire to wait until the close of the third quarter, which ended September 30.

“It’s not the case that you wanted to be able to show up for trial and defend your independence as a board member by being able to say that you had fired Mr. Conway?”

“My independence as a board member has never been in doubt, Mr. Carroll,” said Goldby, who insisted that the trial had nothing to do with Conway’s firing.

Carroll also took aim at other decisions by PeopleSoft’s board in an attempt to question their commitment to shareholders’ interests: the aggressive antitrust campaign, and the hiring of Conway “personal favorites” Leiderman and Reback. The Davis Polk partner also questioned the fact that the transaction committee didn’t have independent counsel. He read Bogen’s testimony about his warning to the board that it had a Unocal problem. He asked Goldby about Bogen’s firing, too.

“Mr. Conway was unhappy-angry-that Mr. Bogen had the nerve to go right to the board in private without talking to Mr. Conway and management first; correct?”

“Yes.”

“In fact, Mr. Conway voiced his anger at a board meeting so you knew it firsthand; correct?”

“Yes.”

“Do you think this is a very good board process we have going on here?”

“I think the board process has been an excellent one, Mr. Carroll.”

Conway took the stand on the third day of trial. Under Carroll’s questioning, he readily admitted that part of his strategy was to “vilify” Ellison. He also insisted that Bogen wasn’t fired for going to directors with his concerns. “He went to the board at will,” Conway said.

Director Battle appeared a week later and also insisted Bogen wasn’t fired for taking his concerns directly to the board. Bogen’s manner had irritated some, he explained. Battle criticized Bogen’s attentiveness: “Andy wasn’t spending enough time himself personally supervising the work for him to be as up to speed as he needed to be.” He also said Bogen had never told the board that its process violated the Unocal standard, despite Bogen’s deposition to the contrary.

Battle says his six hours on the stand were as hard as anything he'd ever done. "Mike Carroll is a very, very effective guy," he notes. When asked in February if Conway was fired to make the board look more independent, Battle smiled and responded, "It's hard to pursue a lack of independence [argument] if you've just fired a guy." But then he quickly added that the firing was triggered by several factors, including the deposition and the unhappiness of senior executives.

When the trial ended on October 15, Oracle was pleased. "If ever there was a case where a pill should be pulled, we had made that case," says associate general counsel Daley, who attended the proceedings.

Lewkow says that he and other counsel advised the board that it was unlikely that Delaware courts (including an appellate court, if necessary) would invalidate the poison pill. While the parties waited for Strine to rule, Oracle raised its bid on November 1 from $21 to $24 (still under the high-water mark of $26 made the previous February). The PeopleSoft board, supported by opinions from its financial advisers that it was inadequate, rejected it. Strine scheduled more depositions and hearings to explore this decision.

Oracle had something to worry about, too. That pesky tortious interference case in Oakland hadn't gone away. In fact, it was scheduled to start trial in January 2005, with Oracle facing damages of up to $2 billion, plus possible punitives. Although PeopleSoft's revenues had risen, the company maintained that it had been losing market share. A jury in economically strapped Oakland might not be sympathetic to megabillionaire Ellison and a company that planned to lay off thousands of local workers. "This case was getting a lot of traction," notes Battle. The PeopleSoft director praises the company's lead lawyer, Michael Kahn, of Folger Levin, by describing him as "every bit as good as Mike Carroll." He adds, "Mike Kahn was making it the only offense we had."

That November, Oracle's Catz had a bold idea: Oracle would test the waters to see how many PeopleSoft shareholders would accept a tender offer of $24 a share. (The poison pill prevented them from actually selling.) Oracle took a risk with this offer: If less than 50 percent approved the price, Oracle would walk away. More than 60 percent indicated they would sell at that price.

In early December, just a few days before Delaware hearings would resume, the PeopleSoft board authorized Gibson, Dunn's Doug Smith and Lewkow to try to strike a deal. The two lawyers called Kelly at Davis Polk. They insisted they weren't opening negotiations, but wanted to convey that PeopleSoft would be willing to accept $26.50, for a total of $10 billion. (Lewkow says a major PeopleSoft shareholder had learned that Oracle would be willing to pay this amount, and passed the information along.) A deal at this price could be seen as a face-saving, and litigation-saving, move for the board. They'd be able to say they got 50 cents a share more than the $26 bid Oracle had put on the table in February 2004 and withdrawn. Kelly soon called back and said they had a deal.

On December 12, PeopleSoft's board voted to accept the offer. The tally was short of unanimous: Duffield abstained, as did former executive Aneel Bhusri.

Looking back, Davis Polk's Kelly claims that PeopleSoft hurt itself with its missteps, including Conway's rash early comments and the company's strident antitrust efforts. "A

lot of their wounds were self-inflicted," he says. "We could have gotten to this result with a lot less pain and damage and resources consumed." He also adds, "In hindsight it's hard to question whether our bid was serious. We did write a check for $10 billion."

Maybe. But Oracle certainly didn't help matters with its ludicrously low opening offer. Cleary's Lewkow insists that PeopleSoft's valiant struggle forced Oracle to raise its bid to $26.50-which is 66 percent higher than where it started. That, he says, was a "home run." He also defends PeopleSoft's board: "This was a good board that worked hard."

In the wake of the merger, which was completed January 7, more than 5,000 workers have been let go from the two companies, with most of the layoffs at PeopleSoft. The lawyers and investment advisers on both sides walked away with more than $200 million in fees.

In the end, it was Duffield who had to break the news to PeopleSoft's 12,000 employees that the company he founded would soon be gone. On the morning of Monday, December 13, Duffield started to read a prepared statement and choked up. Separately, in a letter to all workers, he wrote: "You should know, and I hope you would expect, that I am deeply saddened by this outcome. We have come so far under such trying circumstances over the past 18 months.…I offer my sincere apologies for not figuring out a different conclusion."

Sorry, Dave, but under the cold hard reality of Delaware corporate law, the feelings and futures of company founders and workers don't count. Shareholder value trumps all.

Merger Scorecard

Number of law firms involved (both sides)	**12**
Number of days the hostile bid lasted	**555**
Common premium offered in a merger bid	**25—30%** above the stock price
Premium first offered by Oracle	**6%**
Amount Oracle's final offer exceeded its initial offer	**66%**
Number of words in Gary Reback's antitrust trial blog	**31,458**
Number of executives whose pet dogs sported a bulletproof vest	**1**
Fees for lawyers and investment bankers (both sides)	More than **$200 million**
Number of PeopleSoft and Oracle workers laid off postmerger	Around **5,000**