



Do the plaintiff attorneys suing Harbin Electric (Nasdaq: HRBN) know more about the risk of Harbin's \$24-per-share acquisition closing than the rest of the market? It sure seems so.

Late last night Harbin filed a curious 8-k detailing the settlement terms of the Nevada state class-action lawsuit seeking to enjoin Harbin from closing the buyout transaction with Abax and Tienfu Yang (Harbin's Chairman and CEO). [The 8-k can be found [here](#)] This settlement was to be expected as the company had already dealt with lawsuits pending in New York State and Nevada Federal courts.

The details of the settlement include additional disclosure in an amendment to the proxy [[Link to this amendment can be found here](#)] being mailed to shareholders. As is typical with such settlements the plaintiff attorneys will have the right to be awarded fees and expenses once they've certified the class of shareholders they represent. While the filing doesn't hint at the size of such award, in my experience it could range anywhere from a mid-six figure sum to a few million dollars. In general the more incentive the company in question has to settle, the higher the fee award they would agree to. Knowing that Harbin desperately wishes to pursue the pending \$24 buyout it is safe to assume the amount would be on the higher rather than lower side.

With \$87.5 million in cash plus an additional \$17.5 million restricted as per the June 30th, 2011 10-Q on the surface it would seem Harbin's ability to pay such fees wouldn't be in doubt. Yet, buried in the 8-k is an additional concession the plaintiff's attorneys wrung out of Harbin – namely, lowering the breakup fee (from \$22.5m to 19.75m) payable to Tienfu Yang (via his Tech Full vehicle) and Abax in the event Harbin Electric fails to close the buyout under certain circumstances.

This breakup was originally negotiated between the Harbin Special Committee and Tienfu/Abax. It works to Tienfu's disadvantage to lower that amount. Why would the plaintiff attorney's demand this as part of the settlement?

Usually during a pending acquisition a shareholder friendly group would look to lower the breakup fee payable to the acquirors because you want to incentivise other bidders to join the fray and consider raising the offer. That, to me, is obviously not the case with Harbin given the lack of interest from the dozens of acquirors previously contacted and Tienfu's inability to work with any of them (documented oh-so nicely



HARBIN ELECTRIC LOWERS BREAKUP FEE PAYABLE TO TECH FULL 10-11-2011



by Morgan Stanley's report to the Special Committee [See the Link here for a gripping read!] – my favorite gem, on page 9, is “On Multiple Occassions Mr. Yang stated directly to the special committee and to third-parties that he is unwilling to sell / relinquish control”)

If you dig deeper into Harbin's cash position it becomes clear that the attorneys had good reason to fear be able to get paid in the event the \$24 offer falls through. How so? Cash on hand plus restricted cash equals \$105 million. But those funds are deposited with a bevy of Chinese banks that have also lent Harbin \$36.9 million on short term revolvers, alongside an additional \$36.8 million in short term notes outstanding. Net cash is therefore only \$31.3 million of which more than half of that is restricted. Paying \$22.5 million would be a stretch for Harbin and leave little left over for the possibly million dollar plus settlement to the attorneys. And what are the odds these Chinese banks would allow Harbin to operate at a net cash deficit? Lowering the number payable to Tienfu/Abax by \$2.75 million, close to what I believe is the high estimate of legal fees payable, would give Harbin enough wiggle room to get both Tienfu and the attorneys paid in a timely fashion. (Of course that leaves nothing left for the \$23 million down payment on the latest land 'purchase' – all the more reason to believe that deal doesn't get done either.)

One could argue that agreeing to lower the amount payable to himself is Tienfu's way of showing his confidence in the \$24 deal closing – after all, giving up something of nothing is an easy way to settle any lawsuit. But one has to wonder exactly what the plaintiff attorneys had in mind when demanding this change. As in any litigation, they have had most likely extensive conversations with Harbin and its' counsel. If the plaintiff attorneys felt the chances of the \$24 Harbin acquisition falling apart were negligible then why push to lower the breakup fee?

Harbin shareholders today have an opportunity to sell their stock at \$21 and change. That's not too far from the \$24 takeout price and a long way above where this stock would be trading, in my opinion, if the acquisition does fall through. So again, I ask you this question – What do the plaintiff attorneys know about Harbin that the investing public does not?

Disclosure : As of the publishing of this report, I am short Harbin Electric.