THE REVIEW OF
SECURITIES & COMMODITIES REGULATION
AN ANALYSIS OF CURRENT LAWS AND REGULATIONS AFFECTING THE SECURITIES AND FUTURES INDUSTRIES

Vol. 52 No. 8 April 24, 2019

DEVELOPMENTS IN M&A LITIGATION

The authors begin their article by discussing three Delaware decisions that have largely brought an end to multi-jurisdictional M & A litigation, sharply limited Revlon*-based preliminary injunctions, and disapproved most disclosure-only settlements. The result has been to shift most new M & A lawsuits to the federal courts, although these cases are almost always settled without litigation. The authors then turn to cases that continue to be litigated in Delaware state court, notably post-closing damages claims, cases involving controlling stockholders, books and records actions, and appraisal actions. They close by discussing examples of Delaware M & A litigation not brought by stockholder plaintiffs, namely "broken deal" litigation and the recent CBS/Redstone case.*

By Meredith Kotler and Mark McDonald *

Much has changed in M&A litigation over the last few years. Many of these changes were the result of Delaware judicial decisions responding to perceived abuses in the way M&A litigation proceeded in the past, including the pattern of plaintiffs quickly filing lawsuits in multiple jurisdictions once a deal was announced and then agreeing to resolve those suits by entering into "disclosure-only" settlements, with no apparent benefit to anyone other than fees for the plaintiffs' lawyers and broad releases for the defendants. The immediate result of these recent Delaware decisions, however, appears to have been simply to shift this type of litigation to the federal courts, where they continue to be filed in large numbers.

That is not to say that M&A litigation in Delaware has gone away. To be sure, recent decisions, including *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*[1] and *DFC Global Corporation v. Muirfield Value Partners, L.P.*,[2] which held that the deal price is entitled to substantial weight in determining "fair value" in an appraisal case, have substantially cut down on appraisal filings in Delaware. And decisions such as *Corwin v. KKR Financial Holdings LLC*[3] – which held that, in cases that do not involve a controlling stockholder, a fully informed and uncoerced vote of a majority of the disinterested stockholders invokes the business judgement rule – have made it more difficult for stockholder plaintiffs to successfully allege that the board breached its fiduciary duties in approving a merger. But recent Delaware decisions rejecting defendants' *Corwin* defense at the motion-to-dismiss stage have started to show limits of that precedent. In addition, more and more Section 220 "books and records" actions are filed as a means for stockholders to obtain pre-lawsuit discovery in order to plead a complaint that may stand a stronger chance of

[1] 177 A.3d 1 (Del. 2017).

[2] 172 A.3d 346 (Del. 2017).

[3] 125 A.3d 304 (Del. 2015)

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withstanding a motion to dismiss.

Delaware also continues to see a number of M&A cases that are not filed by stockholder plaintiffs. For example, in a closely watched case between a buyer and target, the Delaware courts recently held that the buyer properly invoked a "Material Adverse Effect" clause to terminate the merger agreement – the first decision so holding in Delaware. And CBS's recent proposal to dilute the Redstone family's controlling stake in CBS in response to a perceived threat that the Redstones were going to force a merger between CBS and Viacom (also controlled by the Redstones) also played out in the Court of Chancery. That case led to interesting decisions on the availability of preliminary injunctive relief and attorney-client privilege before it settled.

In short, M&A litigation has evolved dramatically in recent years. Many of the issues that used to plague M&A litigation have gone away, but other questions have sprung up in their place. Whether, and how, those new questions will be resolved remains to be seen. But one thing that is certain is that M&A litigation will continue apace.

THREE GROUNDBREAKING DELAWARE DECISIONS

Not long ago, M&A litigation involving public companies followed a familiar pattern. Shortly after a deal was announced, competing lawsuits seeking to enjoin the merger would be filed in multiple jurisdictions – usually, in the Delaware Court of Chancery where the target was incorporated and in the courts of the state where the target was headquartered (usually outside of Delaware).[4] It was widely acknowledged, even among the plaintiffs' bar, that this multi-jurisdictional litigation was wasteful and inefficient.[5] Defendants would seek to settle these lawsuits quickly, before the merger closed.[6] The result was often a settlement in which defendants made supplemental disclosures concerning the deal in advance of the stockholder vote, which typically were not material, and agreed to pay fees to the plaintiffs' lawyers in exchange for broad releases for the defendants.[7]

Three Delaware decisions between 2013 and 2016 fundamentally changed this practice. The first was then-Chancellor Strine's 2013 decision in *Boilermakers Local 154 Ret. Fund v. Chevron Corp.*[8] In that case, the court held that bylaw provisions designating Delaware state courts as the exclusive forum for litigation relating to a Delaware corporation's "internal affairs," including suits by stockholders alleging that the corporation's directors breached their fiduciary duties in connection with a merger – known as "forum-selection bylaws" – were permissible under Section 109(b) of the Delaware General Corporation Law ("DGCL").[9] The court further held that it was permissible under Delaware law for corporations, through their charters, to authorize the directors to unilaterally adopt such bylaws (i.e., without separate stockholder approval).[10] Accordingly, the court noted that these director-adopted "forum-selection bylaws" should be enforced by courts inside and outside Delaware just as any other contractual forum-selection clause.[11]

[4] *See, e.g.*, Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting the Peppercorn Settlement in Merger Litigation: An Empirical Analysis and a Proposal for Reform*, 93 Tex. L. Rev. 557, 558 (2015); Edward B. Micheletti & Jenness E. Parker, *Multi-Jurisdictional Litigation: Who Caused This Problem, And Can It Be Fixed?*, 37 Del. J. Corp. L. 1, 4 (2012).

[5] *See, e.g.*, Mark Lebovitch, "Improving Multi-Jurisdictional, Merger-Related Litigation," Harvard Law School Forum on Corporate Governance and Financial Regulation (May 19, 2011), *available at* https://corpgov.law.harvard.edu/2011/05/19/improving-multi-jurisdictional-merger-related-litigation/.

[6] Fisch, Griffith & Davidoff Solomon, *supra* note 4 at 565-66.

[7] *Id.* at 559; *see also id.* at 568 n.58.

[8] 73 A.3d 934 (Del. Ch. 2013).

[9] *Id.* at 939.

[10] *Id.*

[11] *Id.* at 940.

Particularly since *Boilermakers* was codified by the Delaware legislature in 2015,[12] many Delaware corporations have adopted forum-selection bylaws designating Delaware state courts as the exclusive forum for internal-affairs disputes, including state-law M&A claims (notably, claims under the federal securities laws are not covered, as will be discussed further below).[13] And decisions outside Delaware have generally enforced these forum-selection bylaws,[14] absent unusual circumstances.[15] As a result, it is now relatively rare for state-law M&A claims to be litigated in state courts outside of Delaware, at least where the target corporation is incorporated in Delaware.

The second Delaware decision that fundamentally altered the way M&A litigation used to be practiced was the Delaware Supreme Court's 2014 decision in *C&J Energy Services, Inc. v. City of Miami General Employees' & Sanitation Employees' Retirement Trust*.[16] In that case, the Delaware Supreme Court vacated a preliminary injunction issued by the Court of Chancery based on a "plausible" allegation that the target board had violated its "*Revlon* duties"[17] by failing to actively shop the company before or after closing.[18] In an opinion by Chief Justice Strine, the court first held that *Revlon* does not require target boards to "set aside [their] own view of what is best for the corporation's stockholders and run an auction whenever the board approves a change of control transaction" as long as "the transaction is subject to an effective market check under circumstances in which any bidder interested in paying more has a reasonable opportunity to do so."[19]

More importantly, the court indicated that the Court of Chancery should not enjoin a transaction – and thus take away from the stockholders the decision whether to approve the deal – based on the target board's alleged breach of its *Revlon* duties in the absence of a competing bid or a "barrier to the emergence of another bidder."[20] The Court of Chancery has since interpreted *C&J* effectively to preclude *Revlon*-based preliminary injunctions unless "there is a topping bid in the offing."[21] Because it is relatively rare for target boards to favor one bidder over another, the effect of *C&J* is to remove one of the primary grounds on which stockholder plaintiffs used to seek a preliminary injunction in most M&A cases, further reducing the incentive to bring such suits under Delaware law.

The third, and perhaps most impactful, decision was Chancellor Bouchard's January 2016 opinion rejecting a

[12] DGCL § 115 ("The certificate of incorporation or the bylaws may require, consistent with applicable jurisdictional requirements, that any or all internal corporate claims shall be brought solely and exclusively in any or all of the courts in this State."). In addition, DGCL § 115 specifies that "no provision of the certificate of incorporation or the bylaws may *prohibit* bringing such claims in the courts of this State." *Id.* (emphasis added).

[13] Helen Hershkoff & Marcel Kahan, *Forum-Selection Provisions in Corporate "Contracts,"* 93 Wash. L. Rev. 265, 274 (2018).

[14] *Id.* at 276 n.57 (citing cases).

[15] *Id.* at 276 ("The only court so far to have refused to enforce a forum-term is the California federal district court in *Galaviz v. Berg*, [763 F. Supp. 2d 1170, 1172 (N.D. Cal. Jan. 3, 2011),] which held that a forum-term unilaterally adopted by the board mid-stream 'after the majority of the purported wrongdoing is alleged to have occurred' was unenforceable because it lacked any showing 'of mutual consent' to the choice of forum.").

[16] 107 A.3d 1049 (Del. 2014).

[17] *Revlon v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

[18] *C&J*, 107 A.3d at 1052-54.

[19] *Id.* at 1067.

[20] *Id.* at 1070 ("[A]s the years go by, people seem to forget that *Revlon* was largely about a board's resistance to a particular bidder and its subsequent attempts to prevent market forces from surfacing the highest bid . . . . But in this case, there was no barrier to the emergence of another bidder and more than adequate time for such a bidder to emerge. The Court of Chancery was right to be 'skeptical that another buyer would emerge.'"); *id.* ("It is also contextually relevant that C&J's stockholders will have the chance to vote on whether to accept the benefits and risks that come with the transaction, or to reject the deal and have C&J continue to be run on a stand-alone basis.").

[21] Tr. of Oral Arg. on Pls.' Mot. for Expedited Proceedings at 18-19, *Chester Cty. Ret. Sys. v. Collins*, C.A. No. 12072-VCL (Del. Ch. Mar. 28, 2016) ("[I]n a post-*C&J* world . . . unless there is sufficient certainty to be able to enjoin the deal as a whole, which will really only exist if there is a topping bid in the offing, this is not the type of proceeding that is something that will end up in a preliminary injunction."); *see also* Tr. of Oral Arg. on Pls.' Mot. to Expedite Proceedings at 47, *Brigade Leveraged Cap. Structures Fund Ltd. v. Kindred Healthcare, Inc.*, Civil Action No. 2018-0165-SG (Del Ch. Mar. 15, 2018) ("March 15, 2018 *Brigade* Tr.") ("Let me turn, first, to the *Revlon* claims, the process claims. And I think in light of the *C&J* decision, it is a very difficult proposition to advance a preliminary injunctive relief claim where there is no one in the wings. . . . There's no one waiting in the wings. The choice is a binary choice and I am loath to take that away from the stockholders.").

disclosure-only settlement in *In re Trulia, Inc. Stockholder Litigation*.[22] In that case, Chancellor Bouchard noted the growing concerns of academics, practitioners, and other members of the Court of Chancery that the ubiquitous disclosure-only settlements "rarely yield genuine benefits for stockholders," and, because of the broad releases often granted to defendants in such settlements, they "threaten the loss of potentially valid claims that have not been investigated with rigor."[23] For these reasons, the court suggested that "practitioners should expect that disclosure settlements are likely to be met with continued disfavor in the future unless [i] the supplemental disclosures address a *plainly material* misrepresentation or omission and [ii] the subject matter of the release is narrowly circumscribed to encompass nothing more than disclosure claims and fiduciary duty claims concerning the sale process, if the record shows that such claims have been investigated sufficiently."[24] By "plainly material," the court said it meant that "it should not be a close call that the supplemental information is material as that term is defined under Delaware law."[25]

Because most pre-closing settlements before *Trulia* involved supplemental disclosures that were far from "plainly material," *Trulia* sent a message that settlements of such suits, including plaintiffs' counsel fees and broad releases, would be in significant doubt.

THE SHIFT TO FEDERAL COURTS

Following *C&J* and especially *Trulia*, the number of M&A cases filed in the Delaware Court of Chancery dropped dramatically. For example, the percentage of deals valued at $100 million or more litigated in Delaware declined from 37% in 2016 to just 7% in 2017.[26] Because of the 2013 decision in *Boilermakers* (and the 2015 amendment to the DGCL permitting Delaware corporations to adopt forum-selection bylaws), however, these cases generally did not migrate to other state courts.

Instead, they moved to the federal courts, in droves. In 2015 – the year before *Trulia* – just 34 M&A-related cases were filed in federal courts. In 2016, that number more than doubled to 85; in 2017, it more than doubled again to 198; and in 2018, it remained relatively high at 182.[27]

In these cases, plaintiffs generally assert claims that the target's proxy statement concerning the deal is materially false or misleading under Section 14(a) of the Securities Exchange Act of 1934. Such claims – because they arise under federal law (and must be brought in federal court by statute) – are not covered by Delaware corporations' forum-selection bylaws. Much like the previous generation of deal suits challenging disclosures, these claims are asserted in lawsuits filed shortly after the proxy statement becomes public, sometimes in multiple courts (except that these cases are limited to the federal courts, usually including the District of Delaware and the district in which the corporation is headquartered). And most such cases are resolved before the stockholder vote, with defendants agreeing to provide supplemental disclosures in exchange for plaintiffs withdrawing their claims, with a "mootness fee" for plaintiffs' counsel to be negotiated at a later date. In most such cases, defendants ultimately agree to pay plaintiffs' counsel a mootness fee that is typically less than what it would cost to litigate the fee issue.

Importantly, unlike the type of settlement that was rejected in *Trulia*, the vast majority of settlements in these federal actions involve no class-wide release of claims against defendants.[28] Instead, the plaintiffs, who almost never are appointed class representatives under the provisions of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), merely release their own individual claims. As a result, unless the parties litigate over the mootness fee (which rarely happens), the cases are voluntarily dismissed before the court has to do anything in them.

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[22] 129 A.3d 884 (Del. Ch. 2016).

[23] *Id.* at 887.

[24] *Id.* (emphasis added).

[25] *Id.*

[26] Cornerstone Research, *Shareholder Litigation Involving Acquisitions of Public Companies: Review of 2017 M&A Litigation* at 4, *available at* https://www.cornerstone.com/Publications/Reports/Shareholder-Litigation-Involving-Acquisitions-of-Public-Companies-Review-of-2017-M-and-A-Litigation.

[27] Cornerstone Research, *Securities Class Action Filings: 2018 Year in Review* at 5, *available at* https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2018-Year-in-Review.

[28] In cases involving settlements with a class-wide release, the federal courts were quick to adopt *Trulia*'s reasoning to reject such settlements. *E.g.*, *In re Walgreen Co. S'holder Litig.*, 832 F.3d 718, 724 (7th Cir. 2016) ("The type of class action illustrated by this case – the class action that yields fees for class counsel and nothing for the class – is no better than a racket.").

Federal courts do, however, have potentially powerful tools to police these kinds of disclosure-only cases. For example, one district court has held, in light of concerns about this type of litigation, that it would apply *Trulia*'s "plainly material" standard in deciding whether to approve plaintiffs' counsel's fees.[29] In addition, federal courts could hold that the PSLRA prohibits plaintiffs from seeking a class-wide injunction before a lead plaintiff is appointed or a class is certified,[30] or they could enforce the PSLRA's "mandatory sanctions" provisions for violations of Rule 11 of the Federal Rules of Civil Procedure.[31] And at least one court has held that the PSLRA bars plaintiffs' attorneys from being awarded fees at all where, as in virtually all of these cases, there is no monetary recovery to the class.[32]

Infrequently, Section 14 cases filed in the wake of a deal announcement actually proceed to litigation. One such case in which the stockholder plaintiff failed to obtain a preliminary injunction blocking the deal, but is now seeking post-closing damages based on alleged omissions in the target's disclosures, will shortly be heard by the United States Supreme Court.[33] In that case, the Ninth Circuit created a circuit split by holding that Section 14(e) of the Exchange Act – which is similar to Section 14(a), but governs disclosure claims made in connection with a tender offer rather than a stockholder vote – does not require scienter but instead only negligent misrepresentation.[34]

M&A LITIGATION IN DELAWARE COURTS TODAY

As noted above, the kind of routinized litigation resulting in disclosure-only settlements that used to be prevalent has largely been absent from the Delaware Court of Chancery since *Trulia*. But that does not mean Delaware is light on M&A litigation these days. On the contrary, the Delaware courts have been, and continue to be, busy adjudicating numerous interesting M&A disputes.

Preliminary Injunctions

As noted above, after *C&J*, preliminary injunctions based on *Revlon* claims are now relatively rare. But some stockholder plaintiffs still seek preliminary injunctions in Delaware based on disclosure claims, where particular incentives are present. For example, Brigade Capital, a hedge fund that had amassed a sizeable stake in Kindred Healthcare, Inc. ("Kindred"), and was vocally opposed to its proposed sale to a consortium of buyers that included TPG, Humana, and Welsh, Carson, filed suit last year in the Court of Chancery and sought to preliminarily enjoin the sale. Although the court denied Brigade Capital's motion for expedited proceedings with respect to its *Revlon* claim and most of its disclosure claims, the court permitted expedited proceedings on a single disclosure claim concerning a potential conflict of one of Kindred's directors.[35] Following expedited document discovery and a deposition of the director, Kindred filed supplemental disclosures concerning the board's process for addressing the director's potential conflict during the

[29] *House v. Akorn, Inc.*, No. 17 C 5018, 2018 WL 4579781, at *3 (N.D. Ill. Sept. 25, 2018). Interestingly, in that case, the plaintiffs and defendants had settled the fee issue, and stipulated to dismissal of the case. But a target stockholder filed a motion to intervene for the purpose of challenging plaintiffs' counsel's fees. *Id.* at *1. The district court's decision in this case is currently on appeal.

[30] *Rosenfeld v. Time Inc.*, No. 17cv9886 (DLC), 2018 WL 4177938, at *4 (S.D.N.Y. Aug. 30, 2018) (noting that this is "an open question in this Circuit").

[31] 15 U.S.C. § 78u-4(c)(1) ("In any private action arising under [the Exchange Act], upon final adjudication of the action, the court shall include in the record specific findings regarding compliance by each party and each attorney representing any party with each requirement of Rule 11(b) of the Federal Rules of Civil Procedure as to any complaint, responsive pleading, or dispositive motion."). *But see Rosenfeld*, *supra* note 30 at *5 (holding that this provision does not apply in cases where plaintiffs voluntarily dismiss their claims).

[32] 15 U.S.C. § 78u-4(a)(6) ("Total attorney's fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class."); *Mostaed v. Crawford*, No. 3:11-cv-00079-JAG, 2012 WL 3947978, at *7 (E.D. Va. Sept. 10, 2012) (noting that plaintiffs only achieved supplemental disclosures and "[did] not receive a monetary judgment, so [the PSLRA] clearly precludes them from seeking attorneys' fees based on alleged Securities and Exchange Act violations"); *see also Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423, 438 (2d Cir. 2007) (stating that while the PSLRA does not apply to the case, if it did, "[t]he PSLRA would not allow for the computation of fees on the basis of [] non-damage items" because "the statute speaks in terms of a percentage 'actually paid to the class'").

[33] Petition for a Writ of Certiorari at 6-8, *Emulex Corp. v. Varjabedian*, No. 18-459 (U.S. Oct. 11, 2018). The petition for a writ of certiorari was granted on January 4, 2019, and the case is scheduled for oral argument on April 15, 2019.

[34] *Varjabedian v. Emulex Corp.*, 888 F.3d 399 (9th Cir. 2018), *cert. granted*, No. 18-459, 2019 WL 98542 (Jan. 4, 2019).

[35] March 15, 2018 *Brigade* Tr. at 47-49.

deal negotiations. Brigade Capital, however, argued that these supplemental disclosures continued to be materially misleading. At a contested preliminary injunction hearing, Vice Chancellor Glasscock ruled that the supplemental disclosures were not misleading. Assuming without deciding the materiality of the supplemental disclosures, he ordered Kindred to hold open the stockholder vote on the merger for five business days to ensure that all stockholders had an adequate opportunity to perfect their appraisal rights.[36]

Because of the importance of protecting the integrity of the stockholder franchise, the Court of Chancery has gone out of its way to encourage more plaintiffs to file disclosure claims before the stockholder vote, rather than wait to raise such claims in post-closing litigation. In the *Kindred* case, for example, Vice Chancellor Glasscock "applaud[ed]" Brigade Capital for bringing its disclosure claims pre-close.[37] In fact, at times the court has asked the question – although not yet answered it – whether, if plaintiffs know of potential disclosure issues before the vote but fail to raise them at that time, they should be precluded from raising those issues to rebut a *Corwin*-based motion to dismiss in post-closing litigation. As in the *Tesla* litigation (a post-closing case), plaintiffs' counsel have asserted that it is in the best interest of the class not to raise disclosure issues before the vote, but to hold onto them in order to overcome a *Corwin*-based motion to dismiss.[38] Whether the Delaware courts continue to countenance this tactic, or whether more plaintiffs bring disclosure claims before closing, remains to be seen.

Post-Closing Damages Claims: The Corwin *Defense*

In *Corwin*, the Delaware Supreme Court held that arms-length transactions (i.e., ones that do not involve a controlling stockholder on both sides of the deal, as in a minority buy-out) approved by a fully informed, uncoerced vote of a majority of the disinterested stockholders will be reviewed under the deferential business judgment rule.[39] Subsequent decisions clarified that *Corwin* applies to two-step mergers under Section 251(h) of the DGCL (involving a tender offer followed by a short-form merger)[40]; that the business judgment presumption invoked by a fully informed and uncoerced vote is "irrebuttable"[41]; and that such presumption applies to extinguish all claims relating to the merger, including aiding and abetting claims against third parties.[42]

For a time, based on these and other decisions, *Corwin* was thought to signal the end of most post-closing damages cases in Delaware. But more recent decisions, including several denying motions to dismiss based on *Corwin*, may suggest that this view was premature. In these cases, three potential limits on the *Corwin* doctrine have emerged.

First, is there a controlling stockholder? In response to a *Corwin*-based motion to dismiss, plaintiffs' first tack is often to try to allege that the deal involved a controlling stockholder, because, if so, *Corwin*-cleansing does not apply.

[36] Tr. of Oral Arg. on Pls.' Mot. for Prelim. Injunction at 96-102, *Brigade Leveraged Cap. Structures Fund Ltd. v. Kindred Healthcare, Inc.*, Civil Action No. 2018-0165-SG (Del Ch. Mar. 27, 2018).

[37] March 15, 2018 *Brigade* Tr. ("I agree that these types of claims, to the extent they are meritorious, should be brought pre-close. So while there is a whiff of nostalgia about this argument for me, because there was a time a few years ago when I heard many more such cases, I applaud your decision, once you had reached a belief that there were meritorious disclosure and *Revlon* claims, to have brought them pre-close.").

[38] Tr. of Oral Arg. on Defs.' Mot. to Dismiss at 95-101, *In re Tesla Motors, Inc. Stockholder Litigation*, Consol. C.A. No. 12711-VCS (Del. Ch. Dec. 13, 2017) ("*Tesla* Tr.").

[39] 125 A.3d at 305-06.

[40] *In re Volcano Corp. Stockholder Litigation*, 143 A.3d 727 (Del. Ch. 2016), *aff'd*, 156 A.3d 697 (Del. 2017) (Table).

[41] *Singh v. Attenborough*, 137 A.3d 151, 151-52 (Del. 2016) (noting that, if business judgment presumption after fully informed and uncoerced vote were rebuttable, that "would give no standard-of-review-shifting effect to the vote"; instead, "[w]hen the business judgment rule standard of review is invoked because of a vote, dismissal is typically the result"); *Volcano*, 143 A.3d at 738 ("[R]ecent Supreme Court decisions confirm that the approval of a merger by a majority of a corporation's outstanding shares pursuant to a statutorily required vote of the corporation's fully informed, uncoerced, disinterested stockholders renders the business judgment rule irrebuttable."). The only exception is if plaintiffs can show waste. *Singh*, 137 A.3d at 152 ("[T]he vestigial waste exception [to the business judgment rule] has long had little real-world relevance, because it has been understood that stockholders would be unlikely to approve a transaction that is wasteful.").

[42] *Singh*, 137 A.3d at 152 ("Having correctly decided . . . that the stockholder vote was fully informed and voluntary, the Court of Chancery properly dismissed the plaintiffs' claims against all parties [including the board's financial advisor].").

In *Corwin* itself, the Delaware Supreme Court rejected plaintiffs' argument that the acquiror (KKR) was a controlling stockholder of the target (Financial Holdings) because a KKR affiliate managed Financial Holdings' day-to-day operations and because Financial Holdings' primary business was financing KKR's leveraged buyout activities.[43] In rejecting this argument, the court emphasized that KKR "owned less than 1% of [Financial Holdings], had no right to appoint any directors, and had no contractual right to veto any board action."[44] The court also noted that a controlling stockholder's fiduciary obligations arise from its "coercive power . . . over the board's ability to independently decide whether or not to approve the merger," not mere operating control of a company's business.[45]

More recently, in *In re Tesla Motors, Inc. Stockholder Litigation*, the Court of Chancery denied a motion to dismiss based on allegations that a 22.1% stockholder was the controlling stockholder.[46] The allegations in that case – which had to be assumed true at the pleading stage – were, however, unusual: In addition to being the founder and CEO of the company with allegedly outsized influence on the company and the board in particular, the court noted that the CEO/stockholder's alleged active participation in the transaction, and the fact that the board did not create a special committee to consider the transaction free from his influence, were relevant to the question of whether the CEO/stockholder was a controller for purposes of that transaction, even if he was not one generally.[47]

Second, who counts as disinterested? Plaintiffs have recently raised the argument that the votes of overlapping stockholders in the buyer and target should not be counted for purposes of *Corwin*, as *Corwin*-cleansing will only apply if a majority of the *disinterested* stockholders approves the transaction. This issue was raised but not decided in *Tesla*, for example.[48] If accepted, this argument could potentially limit the impact of *Corwin*, particularly in strategic mergers between two public companies, when it is common for there to be substantial overlap in the stockholder base of such companies. For this reason, some have argued that only the overlapping stockholders who actively participate in negotiating the deal should be counted as interested, not stockholders who have no direct involvement (such as index funds).[49]

Third, was the vote fully informed and uncoerced? In the first two years after *Corwin* was decided, a string of decisions granted defendants' motions to dismiss, finding that the vote was fully informed and not coerced. In 2018, however, the Delaware Supreme Court issued two opinions, both reversing a *Corwin*-based dismissal that seemed to signal a shift on this issue. In the first case, *Appel v. Berkman*, Chief Justice Strine wrote for the Court that the failure to disclose that the founder, largest stockholder, and chairman of the target privately told the board that, in his view, "it was not the right time to sell the Company," meant that the stockholders' vote on the deal was not fully informed.[50]

In the second case, *Morrison v. Berry*, Justice Valihura wrote for the Court that the failure to disclose "troubling facts regarding director behavior" in negotiating the deal, which "would have helped [stockholders] reach a materially more accurate assessment of the probative value of the [company's] sale process," precluded *Corwin*-cleansing in that case.[51] The Court emphasized that plaintiffs were not required to allege that the information, if disclosed, would have made a reasonable stockholder less likely to approve the deal; rather, it was enough to plead that "there is a substantial likelihood that a reasonable stockholder

[43] *Corwin*, 125 A.3d at 306-08.

[44] *Id.* at 306.

[45] *Id.* at 307.

[46] Consol. C.A. No. 12711-VCS, 2018 WL 1560293, at *2, 19 (Del. Ch. Mar. 28, 2018).

[47] *Id.* The *Tesla* case, and two similar decisions involving minority stockholders with "outsized influence," were discussed in the February 20, 2019 issue of The Review of Securities & Commodities Regulation. Melissa Sawyer and Emily Lichtenheld, *From Influential Stockholders to De Facto Controlling Stockholders: Recent Trends and Updates in Delaware*, 52 Rev. Sec. & Comm. Reg. 33, 37-38 (Feb. 20, 2019).

[48] 2018 WL 1560293, at *10 n.183 ("Plaintiffs contend that institutional stockholders who held equity positions in both Tesla and SolarCity should have been excluded from the vote tally for purposes of assessing the results and effect of the allegedly 'disinterested' vote. . . . In doing so, they rely on a document among the Section 220 Documents that purportedly reflects that among Tesla's top 25 institutional investors, those holding 45.7% of Tesla's stock (66,658,000 shares) also held SolarCity stock at the time of the Acquisition. . . . This issue may resurface in the event Defendants renew their ratification defense later in these proceedings.").

[49] *Tesla* Tr. at 39-40.

[50] 180 A.3d 1055, 1057-58 (Del. 2018).

[51] 191 A.3d 268, 283-84 (Del. 2018).

would have considered the omitted information important when deciding whether to tender her shares or seek appraisal."[52]

Recent Court of Chancery opinions have heeded these instructions. For example, in *In re Xura, Inc. Stockholder Litigation*, Vice Chancellor Slights held that claims against a CEO were not cleansed by the stockholder vote because alleged material facts purportedly showing his conflicted role in negotiating the transaction were not disclosed.[53] And in *In re Tangoe, Inc. Stockholders Litigation*, Vice Chancellor Slights held that claims against the target board were not cleansed by the stockholder vote because, among other things, allegedly material facts concerning an ongoing restatement process were not disclosed.[54]

Of course, notwithstanding these recent decisions, *Corwin* remains a powerful tool for defendants in post-closing damages litigation. Indeed, because of the significance of *Corwin*-cleansing, boards are routinely advised to disclose as many conceivably material facts as possible to the stockholders before they vote on the deal.

Cases Involving Controlling Stockholders

As explained in a recent article in these pages, until 2014, all controlling stockholder buyouts were evaluated under the onerous entire fairness standard regardless of the procedural protections used in the deal process.[55] But that changed with the Delaware Supreme Court's decision in *Kahn v. M&F Worldwide Corp.*, which held that the business judgment rule (not entire fairness) will apply if the controlling stockholder buyout is expressly conditioned *ab initio* on the approval of a special committee of the independent directors and approval of a majority of the disinterested stockholders (the "dual approval conditions").[56] In October 2018, the Delaware Supreme Court clarified that the "*ab initio*" requirement is satisfied as long as the dual approval conditions were in place before the onset of substantive economic bargaining, even if they were not included in the controller's initial offer.[57]

This framework also has been extended by the Court of Chancery beyond the controller buyout context. In *In re Martha Stewart Living Omnimedia, Inc. Stockholder Litigation*, the controlling stockholder was a seller to a third party along with the minority stockholders, but plaintiffs alleged that she received greater consideration for herself than the minority stockholders received.[58] In such a case, the court found that the business judgment rule would apply under *M&F Worldwide*, as long as the dual approval protections were in place at "the point where the controlling stockholder actually sits down with an acquiror to negotiate for additional consideration."[59]

The Rise of "Books and Records" Actions

In part in response to *Corwin* and *M&F Worldwide*, which raised the bar for plaintiffs in post-close damages actions to plead facts to survive a motion to dismiss, there has been a recent uptick in stockholder inspection demands under Section 220 of the DGCL, and actions brought in the Court of Chancery to compel the production of books and records pursuant to Section 220(c).[60] In the past year, some plaintiffs have used documents obtained in this way to plead a post-close damages complaint that survived a motion to dismiss, including in the *Appel* case discussed above.[61]

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[52] *Id.* at 286.

[53] Consolidated C.A. No. 12698-VCS, 2018 WL 6498677, at *1 (Del. Ch. Dec. 10, 2018).

[54] C.A. No. 2017-0650-JRS, 2018 WL 6074435, at *2 (Del. Ch. Nov. 20, 2018).

[55] Sawyer & Lichtenheld, *supra* note 47 at 34-35.

[56] 88 A.3d 635 (Del. 2014).

[57] *Flood v. Synutra Int'l, Inc.*, 198 A.3d 754 (Del. 2018).

[58] Consol. C.A. No. 11202-VCS, 2017 WL 3568089, at *2 (Del. Ch. Aug. 18, 2017).

[59] *Id.* at *19.

[60] DGCL § 220(c) ("If the corporation . . . refuses to permit an inspection sought by a stockholder . . . or does not reply to the demand within 5 business days . . . , the stockholder may apply to the Court of Chancery for an order to compel such production. The Court of Chancery is hereby vested with exclusive jurisdiction to determine whether or not the person seeking inspection is entitled to the inspection sought.").

[61] *Appel*, 180 A.3d at 1059 (noting plaintiff served Section 220 books and records demand before filing his post-closing damages suit). Notably, the material fact that the Delaware Supreme Court found was not disclosed in that case came from the target board's minutes. *Id.* at 1057 & n.1. The *Tesla* case is another example of a plaintiff using Section 220 to obtain documents in order to plead a complaint that survived a motion to dismiss. *Tesla*, 2018 WL 1560293, at *1 ("Tesla produced documents to Plaintiffs pursuant to [Section 220]. The parties have agreed that all Section 220 Documents shall be deemed

In a recent decision, the Delaware Supreme Court held that Section 220 may entitle stockholders to more than just minutes and other formal board materials, but only to the extent such formal materials are insufficient to satisfy the stockholder's proper inspection purpose.[62] The court explained that "if a company . . . decides to conduct formal corporate business largely through informal electronic communications [rather than through formal minutes and resolutions], it cannot use its own choice of medium to keep shareholders in the dark about the substantive information to which Section 220 entitles them."[63] But this "does not leave a respondent corporation . . . defenseless and presumptively required to produce e-mails and other electronic communications. If a corporation has traditional, non-electronic documents sufficient to satisfy the petitioner's needs, the corporation should not have to produce electronic documents."[64]

The Fall of "Appraisal Arbitrage"

Until recently, the past decade was marked by a notable increase in statutory appraisal filings in Delaware, driven by the "appraisal arbitrage" phenomenon.[65] This phenomenon was made possible largely by the generous statutory rate of interest on appraisal claims (5% over the Federal Reserve discount rate, compounded quarterly from the closing date of the merger[66]) and a 2007 Court of Chancery decision in *In re Appraisal of Transkaryotic Therapies, Inc.*[67] In that case, the court permitted investors who purchased publicly traded shares in the open market, when neither petitioner nor respondent knew whether those shares were voted in favor of the merger (which would disqualify them from seeking appraisal), to pursue appraisal so long as the total number of shares not voting in favor of the deal was greater than the number of shares pursuing appraisal.[68] Several appraisal decisions finding fair value materially above the merger price added to the increase in filings.[69]

Three more recent developments, however, have pumped the brakes on appraisal arbitrage. First, in 2016, Section 262(h) of the DGCL was amended to permit companies to cut off the accrual of statutory interest by pre-paying any amount to the petitioner. In addition, in response to the concern that small appraisal claims were being filed solely to extract nuisance settlements, Section 262(g) was amended to provide that appraisal would be unavailable in the case of a company whose stock was publicly listed if (i) the appraisal demands represent 1% or less of the stock outstanding and (ii) the total value of the demands (as implied by the deal price) is $1 million or less.

Second, in 2017, the Delaware Supreme Court reversed two appraisal awards – 7.5% above the deal price in *DFC Global*, and 28% above the deal price in *Dell* – in both cases because the lower court had given insufficient weight to the deal price.[70] As Chief Justice Strine explained in *DFC Global*, "economic principles" suggest that in open and arm's length mergers, "the best

footnoted continued from previous page…

incorporated within the Complaint whether or not expressly referenced or incorporated therein.").

[62] *KT4 Partners LLC v. Palantir Techs. Inc.*, No. 281, 2018, 2019 WL 347934, at *2 (Del. Jan. 29, 2019).

[63] *Id.*

[64] *Id.* at *12; *see also Inter-Local Pension Fund GCC/IBT v. Calgon Carbon Corp.*, C.A. No. 2017-0910-MTZ, 2019 WL 479082 (Del. Ch. Jan. 25, 2019) (holding that stockholder had proper purpose to inspect records, and that stockholder was entitled to e-mails because they were necessary and essential for that purpose).

[65] Cornerstone Research, *Appraisal Litigation in Delaware: Trends in Petitions and Opinions: 2006-2018* at 1, *available at* https://www.cornerstone.com/publications/reports/appraisal-litigation-delaware-2006-2018 ("Appraisal Litigation in Delaware") (noting appraisal filings steadily rose after 2009 until peaking in 2016).

[66] DGCL § 262(h).

[67] No. Civ.A. 1554-CC, 2007 WL 1378345 (Del. Ch. May 2, 2007).

[68] Scott Callahan, Darius Palia & Eric Talley, *Appraisal Arbitrage and Shareholder Value*, 3 J. Law, Fin. & Accounting 147, page 3 (2018) (describing how statutory interest rate in Section 262(h) and Court of Chancery's 2007 *Transkaryotic* decision led to "arbitrage opportunity": hedge funds may "accumulate shares in the target company after an announced merger, perfect appraisal rights, and put forward a sophisticated expert to challenge the merger consideration, possibly obtaining an award in excess of the merger consideration. And, even if the award fell short of the merger consideration, it would accrue interest at the statutory compounded rate, often far outpacing the risk-adjusted return on the deal consideration itself.").

[69] *E.g.*, *Towerview v. Cox Radio, Inc.*, C.A. No. 4809-VCP, 2013 WL 3316186 (Del. Ch. June 28, 2013) (finding fair value 20% above deal price); *Global GT LP v. Golden Telecom, Inc.*, 993 A.2d 497 (Del. Ch. 2010) (19.5% above deal price).

[70] *DFC Global*, 172 A.3d at 349-50; *Dell*, 172 A.3d at 5-6.

evidence of fair value [i]s the deal price."[71] The Court specifically rejected the arguments that regulatory uncertainty surrounding the target at the time of the transaction rendered the deal price unreliable and that the buyers' status as a financial sponsor rather than a strategic acquiror meant that it did not fully value the target.[72] In *Dell*, Justice Valihura echoed this reasoning, and extended it to a management buyout involving a relatively limited pre-signing bidding process.[73]

Both decisions left open that the deal price would not be entitled to significant weight in all cases, particularly those with an uncompetitive or otherwise flawed deal process. For that reason, even after *Dell* and *DFC Global*, the Court of Chancery has declined to place any weight on the deal price in at least two appraisal cases. But in both of those cases, the court looked to the deal price as a "check" on its fair value determination, which ultimately was very close to the deal price.[74]

Third, a separate line of appraisal cases has found fair value to be significantly *below* the deal price, due to the fact that synergies are excluded from the statutory fair value standard. For example, in *ACP Master, Ltd. v. Sprint Corp.*, Vice Chancellor Laster held that fair value was $2.13 per share, less than half the merger price of $5 per share.[75] Then, in *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*, Vice Chancellor Laster relied on the unaffected market price of the target's stock, which was 30% below the deal price, as the "most persuasive evidence of fair value."[76] The petitioners' appeal from that decision is currently pending.

Even before the Delaware Supreme Court decides the *Aruba* appeal, these developments have already led to a sharp decrease in appraisal actions, with new appraisal filings falling by approximately two-thirds from their peak in 2016.[77]

"Broken Deal" Litigation

In *Akorn, Inc. v. Fresenius Kabi AG*, the target (Akorn) sought to compel the buyer (Fresenius) to close on its acquisition of Akorn, while Fresenius sought a declaration that it had properly terminated the merger agreement based on the occurrence of a "Material Adverse Effect" or "MAE."[78] After expedited discovery and trial, Vice Chancellor Laster concluded that an MAE had occurred, and thus Fresenius had validly terminated and was not required to close. That decision was affirmed by the Delaware Supreme Court.[79]

Akorn is the first Delaware decision to release an acquiror from its obligation to close a transaction as a result of the occurrence of an MAE. Before *Akorn*, Delaware decisions had required the acquirors to close, often despite a significant diminution in the target's value. But the Court of Chancery's detailed recitation of the unusual facts of that case attest to the fact that MAEs remain difficult to establish, even after *Akorn*. Nonetheless, *Akorn* may embolden parties to litigate such cases in the future, where before the lack of precedent for finding an MAE may have discouraged them.

The CBS/Redstone *Case*

One of the most extraordinary Delaware cases in recent memory, *In re CBS Corporation Litigation*, led to two notable decisions from the Court of Chancery before it settled shortly before trial.

In that case, a special committee of the CBS Board of Directors called a special meeting of the full board on May 14, 2018 (to take place three days later, on May 17) to consider and vote on a stock dividend intended to dilute the voting control of National Amusements, Inc. ("NAI"), the Redstone family-owned company that, by virtue of CBS's dual class structure, owns approximately 10% of CBS's common stock and 80% of its voting

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[71] *DFC Global*, 172 A.3d at 349.

[72] *Id.* at 349-50.

[73] *Dell*, 172 A.3d at 31-35.

[74] *E.g.*, *Blueblade Cap. Opportunities LLC v. Norcraft Cos., Inc.*, C.A. No. 11184-VCS, 2018 WL 3602940, at *1-3 (Del. Ch. July 27, 2018) (refusing to give deal price any weight, finding fair value to be 2.5% above deal price); *In re Appraisal of AOL Inc.*, C.A. No. 11204-VCG, 2018 WL 1037450, at *2 (Del. Ch. Feb. 23, 2018) (also refusing to give deal price any weight, finding fair value to be 2.6% below deal price).

[75] C.A. No. 8508-VCL, 2017 WL 3421142, at *1 (Del. Ch. Aug. 8, 2017).

[76] C.A. No. 11448-VCL, 2018 WL 922139, at *2-4 (Del. Ch. Jan. 26, 2018).

[77] Appraisal Litigation in Delaware, *supra* note 65 at 1 ("Last year saw a drop in the number of appraisal petitions filed in the Delaware Court of Chancery. After steadily rising since 2009 and peaking at 76 in 2016, the number of appraisal petitions filed by shareholders declined to only 26 in 2018.").

[78] C.A. No. 2018-0300-JTL, 2018 WL 4719347, at *3 (Del. Ch. Oct. 1, 2018).

[79] *Akorn, Inc. v. Fresenius Kabi AG*, 198 A.3d 724 (Del. 2018).

power.[80] The special committee and CBS simultaneously filed a lawsuit against NAI in the Court of Chancery seeking approval of such dividend, alleging that it was necessary to prevent the supposed threat that NAI would remove CBS directors to force an allegedly unfair merger with Viacom, of which NAI is also the controlling stockholder. CBS also immediately moved for a temporary restraining order ("TRO") to prevent NAI from taking action to protect its controlling stake until the board had a chance to approve the proposed dividend at the special meeting.

Before a hearing on the TRO motion on May 16, NAI (which had no prior notice that the CBS special committee was considering such a drastic step) exercised its right to amend CBS's bylaws by written consent to require, among other things, that any dividend be approved by at least 90% of the CBS directors. Because three of the 14 CBS directors were affiliated with NAI, these bylaw amendments likely would preclude the declaration of the dilutive dividend.

After expedited briefing and a hearing on May 16, the Court of Chancery denied CBS's request for a TRO on May 17, the day of the special meeting. In so ruling, the Court of Chancery resolved an "apparent tension" in the law between, on the one hand, past decisions suggesting the possibility that a board might be justified in diluting a controlling stockholder in extraordinary circumstances (arguably implying that, in such circumstances, the board should be permitted to act without interference by the controlling stockholder) and, on the other hand, cases recognizing the right of a controlling stockholder to have the opportunity to take action to avoid being disenfranchised. The court found the well-established right of a controlling stockholder to take measures to protect its voting control "weigh[ed] heavily" against granting a TRO that would restrain it from doing so, and that "truly extraordinary circumstances" would therefore be required to support such a TRO.[81] At the same time, the court noted that it had the power to review and, if necessary, "set aside" any such action taken by the controlling stockholder after the fact (itself another reason why a TRO in these circumstances was not warranted).[82]

A second decision issued by the Court of Chancery in this case arose from a privilege dispute during discovery.[83] Among other things, NAI argued that, because the three NAI-affiliated members of the CBS board were joint clients of CBS's counsel (i.e., in-house and outside counsel representing the full board, not the special committee specifically), NAI was entitled to unfettered access to privileged communications with such counsel made prior to the filing of CBS's complaint on May 14. CBS, however, took the position that the NAI-affiliated directors were adverse to CBS management and other board members with respect to certain issues even separate from the proposed merger with Viacom (which the special committee was formed to consider) and prior to the commencement of the litigation. For example, CBS's outside counsel filed an affidavit acknowledging that over many years it had advised certain members of CBS management and the board (unaffiliated with NAI) about "the options available to CBS in dealing with its controller."[84]

In ruling on this issue, Chancellor Bouchard first held that, because the NAI-affiliated directors were joint clients of CBS's counsel, under existing Delaware jurisprudence they had the right to unfettered access to legal advice rendered by such counsel absent (i) an *ex ante* agreement among the parties; (ii) the formation of a special committee; or (iii) "sufficient adversity" between the director and the corporation "such that the director could no longer have a reasonable expectation that he was a client of the board's counsel."[85] The court determined that, as a result of the formation of a special committee by the CBS Board of Directors to consider the potential merger with Viacom, the NAI-affiliated CBS directors were not entitled to privileged communications with company counsel relating to the special committee's mandate. The court, however, held that the NAI-affiliated directors were entitled to communications with company counsel that were unrelated to special committee matters, finding that "no factual basis has been identified to support the conclusion that the NAI Affiliated Directors were made aware (or reasonably should have been aware) that CBS Counsel was not representing them jointly with the other

[80] *CBS Corp. v. Nat'l Amusements, Inc.*, Civil Action No. 2018-0342-AGB, 2018 WL 2263385, at *1-2 (Del. Ch. May 17, 2018).

[81] *Id.* at *6.

[82] *Id.* at *5

[83] *In re CBS Corp. Litigation*, Consol. C.A. No. 2018-0342-AGB, 2018 WL 3414163 (Del. Ch. July 13, 2018).

[84] *Id.* at *1.

[85] *Id.* at *4-5.

CBS directors with respect to any matter *other than the matters falling within the purview of the Special Committees for which CBS Counsel provided assistance*."[86] This decision shows that mere adversity between directors is not sufficient to exclude some directors from privileged communications with board counsel; rather, such adversity must be made "manifest" to the directors who are excluded.

CONCLUSION

By the numbers, most M&A cases these days are filed in federal courts, but those cases are rarely litigated (and perhaps soon will be a thing of the past). Most of the action remains in Delaware, where recent decisions exposing potential limits of the *Corwin* doctrine may embolden more stockholder plaintiffs to file post-closing breach-of-fiduciary-duty lawsuits. In the meantime, Delaware is likely to continue to see its fair share of litigation among "principals," such as *Akorn* and *CBS*, particularly given that an increasing percentage of merger agreements, and the bylaws of most Delaware corporations with respect to "internal affairs" disputes, require related litigation to be brought in Delaware state court. ■

[86] *Id.* at *7 (emphasis in original).