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Tulane Corporate Law Institute Part II

M&A Practice In a New Age

The first panel at the Tulane Corporate Law Institute discussed what lies ahead for dealmakers after the high number last year of failed deals, the recent Delaware cases of *Corwin* and *Trulia*, and the effect of the new administration so far on M&A and how to navigate through the uncertain times that may soon be here. The panelists included Chief Justice Leo E. Strine, Jr. of the Delaware Supreme Court; Ted Yu, chief of the SEC's Office of Mergers & Acquisitions; Kurt Simon, global chairman of M&A at J.P. Morgan Chase; Gar Bason on Davis Polk & Wardwell; Bill Lafferty of Morris, Nichols, Arsht & Tunnell; and moderator Eileen Nugent of Skadden. "Frankly, you almost can't talk about M&A without talking about these changes," Ms Nugent said. "In my own view, there were a lot of gut feelings of boards and CEOs, and emotions, that are affecting dealmaking maybe more than they have in the past."

As the panel discussion began, there was one empty seat. "Ah, there he is!" Ms Nugent, "Always a happy fixture here," she said as the Delaware chief justice walked in, carrying a heavy bag over one shoulder, having been directed to the Crescent Ballroom at the Roosevelt Hotel. "Is that at a different hotel?" Ms Nugent asked. Said His Honor: "No, it's right beyond the breakfast. But it's empty and it's a long walk." The conference had graduated to a larger place, Ms Nugent explained, with its more than 600 attendees, yet another record broken in the days of busy but complicated M&A.

Davis Polk's Gar Bason opened the discussion with a look another record—the highest number of abandoned takeovers since 2010. "Failed deals are far more common," Mr. Bason said. "It's getting very tough to do transactions." The dollar value of deals that did not reach closing came in at well over $800 billion dollars. "That's a lot." Seventy percent were U.S. transactions, which fell into two categories, deals that were inversions and those that ran afoul of antitrust regulators.

An inversion, Mr. Bason explained, involves a company that is going overseas to avoid U.S. tax jurisdiction. "What starts, when these deals start to fail, as a straightforward Treasury revenue reaction, which is how do we stop this happening because we'll lose a lot of tax revenue, morphs pretty quickly into a somewhat more populistic

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"I liked the original Pilgrims, but this new crowd can't talk about anything but dealmaking."

M&A Practice

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reaction, which is to say: 'This is unpatriotic. This is bad. What are these companies doing?' I'll leave it to all of you to see if that populistic danger has become better or worse in the last three months." As for the antitrust hurdle, there were 35 deals challenged in 2016. Twenty-seven of those were settled before litigation, one was abandoned before a court hearing, and seven were litigated, generally with unhappy results for the deal parties.

Mr. Bason, in looking ahead to 2017 for a sense of what will happen to inversions, suggested that one should think of that "great tax lawyer, Clint Eastwood." Chief Justice Strine interrupted to say, "He is actually the White House ethics counsel," a remark that brought down the house. Mr. Bason, resuming his thought, said that Mr. Eastwood would say to dealmakers, "Do you feel lucky?" Mr. Bason said that for the next year he does not see a large number of big company transactions "willing to stand in the way of a freight train that not only combines reducing revenue payable to the Treasury but moving offshore with all the baggage that contains." CEOs, he pointed out, read the papers. "The worst thing about the current administration, in many respects, for dealmaking is we do have a president who takes to tweeting what his reaction is to a particular transaction. That is every CEO's nightmare."

Turning to antitrust and the question of why deals are having regulatory problems, Mr. Bason asked whether this is because regulators have had a number of notable victories and are feeling emboldened. "That could be," he said. Is it because all the easy deals have been done? "That also could be—or is it because activist investors are pushing companies to do M&A transactions and as a general rule, when a target is faced with a high premium, unsolicited offer, there is a usually an enormous amount of intolerance from the shareholder base for an antitrust defense."

Ms Nugent said she believes these difficulties are caused in large part by the fact that many deals have been done. "There is a great deal of significant consolidation going on in some industries," she said. "But I think you're right that people have gotten used to the concept that you can get approval ultimately after doing a couple of divestitures here and there. Boards don't want to hear that the deal can't get through, but there is growing evidence that deals either are much harder to get through or there is a lot more regulatory activity."

Mr. Bason then posed the question to the Delaware lawyers and Delaware's senior jurist on the panel: "How do you feel about a board member that says, 'I think this is a heavy lift as a regulatory matter. I think there is a meaningful chance, if not a probability, that this deal won't get done. But I'm worried about getting thrown out of office next May if I don't do the deal.' " A board should balance that reaction with how strong the protections for the transaction might be negotiated, whether it is a sizeable break-up fee or reverse break-up fee, Mr. Lafferty of Morris Nichols submitted. He cited the Shire/Abbvie deal, which was shot down because of the inversion regulations that came down from the government. Shire walked away with a very large break fee. "I think there the board the right thing," Mr. Lafferty said. "It got the protections they needed for the company."

Ms Nugent responded by saying that during "the dark ages" when she began practicing law, it was considered a disaster if a deal were to fall apart. "It was just a horrible thing. Maybe it's because people understand deals more, maybe it's because of the media and the attention that deals get. It's just a much more well educated financial marketplace when it comes to M&A deals. Companies don't fall apart." Break-up fees also make it easier to accept. "Gee, this is nice" is often a buyer's reaction when a failure to close triggers a large fee. Mr. Bason agreed: "What we're learning is that the sun actually does rise after a deal fails."

Chief Justice Strine pointed out that it is called the business judgment rule for a reason. "Ultimately, you get credit for having an explicable business justification for what you do and if your actions match your rationale, you have little danger of getting in trouble." Boards may well make the decision that a deal in question is a significant opportunity that may not come their way again, even given the risks that may be involved. "If you're backing into something because of market pressure—we know that happens—that's when you have to realize you're not going to get any sympathy from the institutional investors. It's like when GM did every goo-goo thing in the world, right? It had like a seventy-five page manual on good governance. And then when the stock price went down, it was, 'Well, don't we get credit for the manual?' No. The same people who pushed you into the deal, if it goes wrong and you didn't get adequate protections, are going to sue your ass off, criticize you to the press, head out to the CNBC terminal and diss you. So you might as well from the beginning do what you think is correct. But then, there are real risks of uncertainty. Are you pricing them? I think one of the reasons why the market is accepting deals is they're seeing boards match the deal architecture to the risks that are being confronted when they see a reverse termination fee and other provisions that actually seem to sensibly price the risk. Then you get your stockholder base to go on the ride. I view it as heartening."

Protectionism

The chief justice then expressed disdain for protectionism. "I would ask you guys on this uncertainty thing—just like on the playground, the U.S. is not the only one with a basketball or a soccer ball. We don't get to pick up our ball and go home. If we go protectionist on some dimension, we don't get to call, 'Well, that's the only dimension on which we go protectionist, which is tax.' You mentioned antitrust risk and this relates to that especially. Protectionist, nativist impulses where we don't work with the European Union and others on one dimension—do you fear that for example if we decide to be more protectionist about deal motivations around things like tax and don't do it in concert with the EU, that there can be individual nations using their competition rules and other things as a response? One move invites another. You can play a hockey game like Putin, right—where all the stooges on the other side let you score. I had not known that was global capitalism."

Ms Nugent felt moved to stand up for boards, particularly since the crash. "As a lawyer, I've never had board members pay such close attention to risk as they do now, including the risk of a deal not closing. That part of the agreement, with all the miscellaneous provisions as to exactly how the fees work—you would take a board through all that, and they listened, but there's nothing like years of a downturn and an awful lot of litigation that came out of it. I've never had as much attention from boards when you talk about what the remedies are if the deal doesn't close. Historically, lawyers worried about this and maybe nobody else did."

A failed deal not only affects the board, noted Mr. Simon of J.P. Morgan Chase. "A CEO's reputation is also incredibly important here too. CEOs who have failed deals? That has a big impact on their psyche, how they feel about future deals. It's not just the board that are impacted by failed deals." Chief Justice Strine asked, "CEOs have vulnerable psyches in your experience?" Mr.

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Strine Moments

Chief Justice Strine: I have been asked by the president to . . . um—

Eileen Nugent: Just stop right there! [*laughter*]

Chief Justice Strine: Have any of you noticed my wrist band? See, some of you are not sympathetic. You're looking right through it. It's the clear arm band that signals the suffering that comes with male-pattern baldness. Although President Trump himself has a very full and interesting head of hair, he is empathetic and he has asked me to lead a moon shot to eradicate male pattern baldness. And he has authorized me to announce this at the Tulane Corporate Law Institute where many of the participants can empathize.

Ms Nugent: O—KAY [*laughter*] Clear arm bands? I can't deal with it.

Chief Justice Strine: Again, failure of empathy.

Ms Nugent: I know. It's just awful.

On disclosure-only shareholder suits...

Chief Justice Strine: You would get the intergalactic release and you would get to pay three or four hundred thousand dollars. It had nothing to do with the law. Then the Court of Chancery began to examine these stinky-as-cheese cases, and they weren't stinky cheese in a good way—they were just skanky. It's not Bourbon Street when you're having fun. It's Bourbon Street the next morning when the last thing you need to do is to smell something bad that just puts you over the line that holds it together. . . . They were not a class of cases Delaware ever wanted or believed should exist."

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Simon did not miss a beat: “We all do. Present company included.”

CFIUS

Mr. Bason posed the question of regulatory risk when your only bidder is from China. You look at the CFIUS risk associated with that. You get the best reverse termination fee and covenants you can, but even so you realize that the risk of failure is high, he posited. This is a particularly apt issue under the Trump administration, the panelists agreed. “This is not rocket science, to use a CFIUS-loaded term,” Mr. Bason said. “Things that are trending down include any cross-border deals from certain companies—that would be China, and that would be Russia. Plus, anything that involves large job losses. ‘Synergies’ is frequently a polite way of saying ‘We’re going to reduce the number of employees.’ When those numbers are large, that’s concealing a very large personal tragedy for many people. Certainly, there is a reasonable possibility in this environment that that becomes a populist problem. It can be quite complicated to deal with that, if synergies are a big part of your story to the street.”

As for those forces that are trending up, Mr. Bason turned to Janis Joplin: “Get it while you can.” With interest rates low, he said, there may be those who say, ‘There’s an opportunity and I’m going to pounce on it.’ ” The chief justice jumped in and asked the audience, “Does that describe last night [in New Orleans] for any of you?”

Five of the top ten big deals were announced within three weeks of the election, Mr. Simon noted, which he described as remarkable. Was that driven by a sense that the buyer should move fast because things could get worse? Mr. Simon described it as simply a long-term view that it was better to bid rather than wait for months to see what the tea leaves in Washington might look like. “The deals matured at the right time,” he said, “and people got comfortable with the uncertainty. We haven’t really seen a deal get tested on antitrust yet or CFIUS frankly. We’ll see.”

Tax Reform

What about tax reform? Mr. Simon described the issue as “a near-term negative” that might defer certain types of deals into 2018. The buyer is faced with the difficulty of assessing the value of a target. “You look at scenarios. You look at probabilities,” Mr. Simon noted. “You get comfortable with the price on the table—is it high enough to compensate you for the prospect of tax reform?” Would a target be moving too fast if it were to try to do an immediate deal? “Post-health care and what’s happened there,” Ms Nugent said, in answer to her own question, “now I have no idea what’s going to happen. When you talk about scenarios, one of them has to be nothing happens until 2018. Maybe in some ways that’s better.” Dealmakers may have time to ponder and to see what transpires rather than to rush into a transaction, the fate of which is unpredictable.

Ms Nugent pointed out that all the present uncertainty might have led to a stronger domestic M&A market than the prospects for cross-border deals. “But this proves why I’m really bad at making these predictions,” she said, “because that’s entirely wrong. To date, people are concentrating on cross-border deals. I think there is another factor with some of these decisions. There has been a lot of buying. There has been a lot of activity. Two very strong years. There are at least some companies out there—it’s like a game of musical chairs—there aren’t that many really good consolidations left. That, Gar, goes to the get-it-while-you-can approach.”

Mr. Simon asserted that he and his colleagues at J.P. Morgan Chase do not take a dire view of dealmaking over the next year. Quite the contrary: tech, industrials, energy and healthcare are the sectors to watch. Tech, he said, is still a relatively fragmented industry. He has been struck, for example, by the number of industrial companies looking to buy software companies, which he described as “staggering.” He said healthcare is due for a rebound. “There has been a lot of pent-up demand there,” he said. Energy, if we see stability in pricing, he described as ‘ripe for consolidation” as well.

Corwin

This is how Chief Justice Strine described what has become known as the Corwin Doctrine: “One thing I want to say about this whole “doctrine” thing is: Love one another as you wish to be loved. In tribute to me, they called it the Strine Rule. It’s not the Strine Rule. It’s the Golden Rule. It goes back. It has a lot of lineage. There was a guy named Jesus who said it. Maimonides echoed it about, I think, a thousand years later. It’s still a rule. If you read the footnote in *Corwin*, where there’s 57 prior cases cited, there’s nothing new about this. And it’s nothing new either that it applies to tender offers or to the vote, because the prior cases, if you read the old law—the old time religion—if you accepted the benefits of the transaction, you could not stultify yourself and then sue on the transaction. Those were cases that dealt with tenders.

"From a Delaware standpoint, analytically, the issue of what the standard of review is going to be, is going to [depend on] the question of whether the disinterested electorate knowingly accepted the benefits of the transaction in a fully informed and uncoerced way. I'm not sure, Ted, that everybody uniformly agrees that what you guys are doing on the tender offer is necessarily within your department to the same extent as other things, But in terms of what you're trying to get under state law certainty, I think you need to look at your tender offer disclosures to your stockholders, Bill, in the same way you look at it if you're getting a vote, wouldn't you say, for the old time religion?" Mr. Lafferty answered with one word: "Absolutely."

Ms Nugent chose to address the issue of Chief Justice Strine's ruling in *Corwin* from the point of view of the adviser. "How does [the decision] affect counseling and advising a board? How does it affect dealmaking, if at all? The combination of *Corwin* and *Trulia* has meant that litigation, as it has proceeded in deals over the last several years, is changing and significantly changing. How does that affect how you look at a deal, what you advise boards, how you ask them to structure deals, whether you're as worried about standards of review as a practitioner, and advising boards on how to do deals?

To Ms Nugent's questions about the effect of the decision on advisers, Mr. Lafferty began his answer by saying that he was glad the chief justice had clarified the fact that *Corwin* has always been the law. He noted the rising panic that as a result of the ruling the Delaware courts are on the brink of shutting down. He assured the audience that the case is an evolution and not a revolution.

"Despite *Trulia*, because of which there are no more disclosure-only settlements, and now the power of the stockholder of vote in *Corwin*, there are still good cases being brought in Delaware," Mr. Lafferty said. "The courts in Delaware are as busy as ever. Some of the chancery judges will confirm that. The reality is that we're left with real cases. Litigators like me now are busier than ever because now we have to litigate real cases, post-closing deal cases where there are conflicts, loyalty issues at play. And so, those are the ones that are really going forward. In terms of how I advise clients when they're in a process considering selling the company, I honestly don't think it has impacted one iota how directors are thinking about dealmaking. They have their basic duties of care and loyalty and as they think about how to structure the selling of the company, I don't think they're thinking about standards of review at the back end and a *Corwin* stockholder vote. They're thinking about whether it's the right thing to do to go out and shop pre-signing, or do we have some legitimate business reason why we're going to do a single bidder strategy subject to a post-signing go-shop. They're not thinking about it in terms of getting protection at the back end."

Mr. Simon agreed. "I actually think it's good practice. I think the truth will set you free here. If boards aren't comfortable hiring me because of my personal relationships or firm relationships, then we'll step aside and I'd rather do that up front. I think this has made our practice better. I think it's made boards come to better decisions and I think it's been a really good development."

As for the *Trulia* decision, here is the view of the chief justice: "Historical context is important here. When I was first on the Court of Chancery and when I was in practice, these cases were regularly dismissed without consideration going to the plaintiffs' lawyers. The forum shopping changed the game. You used to get sued in three or four different states for disclosing something that was meaningless and would not endanger the vote. You would get the intergalactic release and you would get to pay three or four hundred thousand dollars. It had nothing to do with the law. Then the Court of Chancery began to examine these stinky-as-cheese cases, and they weren't stinky cheese in a good way—they were just skanky. It's not Bourbon Street when you're having fun. It's Bourbon Street the next morning when the last thing you need to do is to smell something bad that just puts you over the line that holds it together. . . . They were not a class of cases Delaware ever wanted or believed should exist."

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M&A Practice: 2017
A Summary

Getting Deals Done is Getting Harder

Failed deals are more common. 2016 saw the largest number of abandoned takeovers since 2010. Withdrawn M&A by value reached an eight-year high of $804.7 billion. Deals for U.S. targets accounted for 70 percent of that figure.

- **Inversion Problems**
- **Antitrust Problems**: 35 deals challenged in 2016; 27 settled prior to litigation; 1 abandoned prior to litigation; 7 litigated; outcomes generally negative for deal parties
- **Abandoned deals**: Shire/Abbvie; Pfizer/Allergan; CF Industries/OCI; GE/Electrolux; Baker Hughes/Halliburton; Time Warner/Comcast; Aetna/Humana; Cigna/Anthem; Staples/Office Depot; Lam Research/KLA-Tencor

Why? Will These Trends Continue?

Inversions —Inversion deals are not impossible, but there are probably not a large number of parties that are going to be willing to step in front of the controversy associated with leaving the United States for tax purposes.

Antitrust —Why are so many deals having antitrust problems? Is it that:

- Regulators are feeling stronger?
- All the easy deals have been done?
- Activist investors are forcing deals on targets and promptly penalize targets that fight an offer on antitrust grounds?

What Does it Mean?

- The potential of any deal failing addressed sooner and more often in deals—in the agreement and in Board room discussions.
- If you are a seller's board and you are willing to interact, you are deeply focused on what antitrust covenants to extract from the buyer. Above all, you are focused on getting a reverse termination fee if there is an antitrust fail. If you are the buyer's board, expect the target to push strongly for all of the above. Same analysis occurs in connection with other regulatory hurdles.
- How do companies react?
- With lots of failed deals, many companies find themselves starting over again—and often, the world doesn't look so bad. Despite what we all may say as sell-side counsel, the world doesn't end if the deal fails.
- Can we expect those companies to be loathe to try again?

Dealmaking Under the Trump Administration

How does uncertainty factor in?

Trending down?

- Any cross border deal from certain countries.
- Any deal whose economics count on large scale job losses, or moving operations overseas.

Trending up?

- Is the theory of "do it while you can," coupled with (for now) continued low interest rates going to prevail?

Which way does potential tax reform cut?

- If rate cuts seem likely, will that delay deals?
- Can targets be valued appropriately in an uncertain tax climate?

What about border-adjustment taxes?

- Will that chill deal flow from highly multinational deals?
- Potential effects of protectionism.

Effect of *Corwin* on Deals

- ". . . *Unocal* and *Revlon* are primarily designed to give stockholders and the Court of Chancery the tool of injunctive relief to address important M&A decisions in real time, before closing. They were not tools designed with post-closing money damages in mind . . ."

- A "*Revlon*" transaction before a stockholder vote—one subject to enhanced scrutiny—is protected by the business judgment rule after approval by uncoerced, fully informed and disinterested holders of a majority of the Corporation's shares.
- *Corwin* applies to two-step transactions as well as one-step mergers (tendering shares given similar effect as stockholder vote).
- *Corwin* may also cut off related aiding and abetting claims.

What is the Effect of *Corwin* on Dealmaking

Advising target boards of directors after *Corwin*:

- How does it affect advisory boards, if at all?
- Is this a logical result—one that directors might expect—in the context of third-party deals without conflicts of interest?
- "No single blueprint"—will directors change practices with respect to designing sale processes?

Buyers:

- How will buyers react—any effect on purchase price?

Financial advisors

- Will the decrease in likelihood of aiding and abetting claims change opinion practices or other forms of advice rendered by financial advisors?

MA

Delaware Developments
Perspectives on Corwin

Where have all the plaintiffs gone?
Short time passing.
Where have all the plaintiffs gone?
Dismissed under Corwin, every one.
O! When will they ever learn?
Gone into the appraisal game, every one.

("Sung" by Ted Mirvis of Wachtell at Tulane)

Theodore N. Mirvis, a partner in the Litigation Department at Wachtell, Lipton, Rosen & Katz, examined the aftermath of Chief Justice Leo Strine's *Corwin* decision. Vice Chancellor Glasscock, who has decided a number of cases under Corwin, then responded to the "interesting doctrinal points" that Mr. Mirvis raised. This was followed by Joel Friedlander of Friedlander & Gorris, who looked at trends in Delaware jurisprudence and practice from a plaintiff's point of view.

He was part of the Delaware Developments panel that included Potter Anderson's Peter Walsh as moderator, Vice Chancellor Samuel Glasscock III, Elena Norman of Young Conaway Stargatt & Taylor, and Lisa Schmidt of Richards, Layton & Finger and Joel Friedlander of Friedlander & Gorris. Mr. Mirvis was described by Donald Wolff of Potter Anderson, co-head of the planning committee of the Tulane Corporate Law Institute as "vivacious and surprisingly spry."

Peter Walsh, the moderator of the Delaware developments panel, introduced Mr. Mirvis: "You probably heard the chief justice say, in speaking about the *Corwin* case, that nothing has changed. While that may be true as a matter of law, I think members of the panel would certainly agree that this past year has seen some very, very significant developments in Delaware corporate law. The impacts of those developments I think are something that, whether you are a litigator or a deal lawyer, are going to be very important to your practice in the ensuing months and years. Ted is going to start us off with perspectives on *Corwin*."

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Ted Mirvis: I'm actually going to start by singing the first slide. This is my best singing voice: *Where have all the plaintiffs gone? Short time passing. Where have all the plaintiffs gone? Dismissed under Corwin, every one. O! When will they ever learn? Gone into the appraisal game, every one.*

Corwin is a remarkably clear opinion. I think it's admirable to see what has happened once *Gantler* was cabined to quote/unquote "ratification." I'll go through some of the cases that have flung out of *Corwin*—that's a bad word—that have been decided since. I think they create a pretty remarkable tapestry in relatively short order. But first I

I'll put *Corwin* in context.

I think *Corwin* can be seen as part of, if not a trend then of a movement of some kind, which involves all the things on this slide [see: *Corwin* Context: Stockholder/Market Power!!]. All of which share in some way in the notion that the Delaware courts have recognized in various contexts, including appraisal, but in various contexts, the changing nature of the stockholder base and have been willing to, I won't say cede authority, but I would say incorporate into legal doctrine to a greater degree than previously, the effect of informed stockholder voting.

Before I start tweeting about "we're winning so much, we're getting sick of winning" [*laughter*]—I don't even really know what tweeting is. If we just look at some of the decisions that have come under *Corwin*, *Corwin* #1 has put new emphasis on the notion of whether plaintiffs can withhold litigation disclosure claims and just assert them post-closing to defeat *Corwin*. I don't think there is a definitive answer to the question. You see here some of the cases [see *Corwin* #1: Use it or Lose It?]. I put *Transkaryotic* at the bottom because that was a pre-*Corwin* case, which many people read to say that if the disclosure claim is not brought pre-closing that it's lost. I think courts have expressed—and understandably so—their preference that disclosure claims be raised pre-closing so that if disclosure violations occur they can be remedied.

One of the big issues that arose immediately after *Corwin* was to what degree does the Mr. Clean of *Corwin* cleanse conflicts. Does it cleanse loyalty claims and other potential claims that stockholders might have with respect to a transaction? Initially, it wasn't all that clear, but I think it is, certainly in the Court of Chancery, I think it's fair to say that a consensus has developed that a *Corwin*-type approval—that is an uncoerced, fully informed stockholder vote—will end all claims with respect to the directors' conduct in the transaction, including duty of loyalty or conflict claims other than claims in which there is a controlling stockholder.

This has built up to the most recent opinion on that point, which is *Columbia Pipeline* by Vice Chancellor Laster only a very short time ago, in which the vice chancellor said that the business judgment rule and dismissal would be required, even if a complaint sufficiently alleged a claim for the breach of the duty of loyalty. It was quite a very specific claim, that the defendant directors and management had engaged in a spin-off and then a sale in order to trigger personal benefits for themselves in the form of change-in-control payments.

Larkin has been cited by many of the Chancery Court cases. It's a decision by Vice Chancellor Sleights and it makes what I thought was the very interesting point, which is summarized on this slide under Policy—attempting to harmonize *Corwin* with the policy rationales that undergird all of Delaware jurisprudence on controlling stockholders and referred to the effect of stockholder approval as being "proportionate to their situational legitimacy." [see *Corwin* #2] In the controlling stockholder context, the court said all that derives from shareholder approval is burden-shifting. But it restores the business judgment deference in other contexts that otherwise would implicate entire fairness review, and therefore led to the conclusion that board-level conflicts or due care issues can be cleansed by the vote of disinterested stockholders, leaving as the uncleansed categories controller squeeze-outs and third-party deals where controllers receive differential or favorable treatment.

Another issue [see *Corwin* #2.1] arose from the question of whether, once *Corwin* applies and you're in business judgment rule territory, is the business judgment rule rebuttable or irrebuttable? I think a great degree of clarity was brought by the Supreme Court's affirmance in *Attenborough*, which is actually *Zale 2*—called *Attenborough* for reasons that are best known only to denizens of Dover (there must be a reasons but I don't know what they are). And then you see a series of cases that made the same point, that once the business judgment rule applies, the only potential claim in a deal case is the waste exception and, of course the comment that stockholders are unlikely to approve the transaction that's wasteful.

Another issue that has arisen and already been decided is whether *Corwin* applies outside of stockholder votes on mergers and also to tendering and tender offers at least when they are constructed in a form of follow-on merger transactions under Section 251. An opinion by the Court of Chancery that has been affirmed by the Delaware Supreme Court, in holding that stockholder approval of a merger under Section 251 by accepting a tender offer will have the same cleansing effect as a vote in favor of the merger.

The fifth, or fourth interesting question is what about aiding and abetting claims? We know from *Rural Metro* that a claim against directors that is non-actionable because of exculpation under Section 102(b)(7) can nonetheless be the predicate for an aiding and abetting claim against investment bankers and potentially other advisers. What about a claim that is dismissable under *Corwin*? Does that claim still have enough life in it to be a predicate for aiding and abetting? I think the answer to that is clearly, no. Both in *Corwin* and *Zale 2*, that statement was made, and then most recently in *Comstock*.

That led me to think about the difference in language that the Supreme Court used in *Corwin* as compared to *Rural Metro* and whether or not, nigh on thirty years later, what's left of *Revlon*? Is it dead? Is it just a ghost stalking the halls? How does it work? I can't answer this question, but to me the descriptions in the two cases are intentional. In *Corwin*, the court emphasized the point that *Unocal* and *Revlon* are primarily tools to be used at the pre-closing stage for injunctive relief. The court said that they were not tools designed with post-closing money damages in mind.

And yet, in *Rural Metro*—which is earlier, but not much earlier and from the same court—the court held that a violation of what is referred to as a situational duty under *Revlon*, not a breach of the duty of care or the duty of loyalty, was a sufficient predicate for post-closing aiding and abetting liability against the sell-side banker. If anyone has an answer to this tension, I would be happy to meet them right after this panel.

This is a list of questions [see *Corwin* #6] that occurred to me about what we should look for in the case law as the doctrine develops. It's been a really very intense period of doctrinal development as the courts, on a case by case basis, sort out the implications of *Corwin*. Are courts getting tougher on disclosure claims than they might otherwise have been because more hangs in the balance? If they find that it's a good disclosure claim, then *Corwin* doesn't work. Are plaintiffs in fact holding back on litigating disclosure claims because they don't want them to be cured pre-closing by the target company and therefore allow a *Corwin* dismissal? Are plaintiffs able to keep their disclosure claims close to the vest and raise them post-closing, maybe not as direct claims if *Transkaryotic* is back in power. But is it good enough even if they're not litigating them as disclosure claims, can they still assert them to defeat dismissal under *Corwin*?

Can we think of *Corwin* as a case that really reinterprets the Delaware interested director statute at Section 144(a)? Is it really going to hold up—and I do think it has up to this point—that when a case is dismissable or a claim is dismissable under *Corwin*, it has a different impact on aiding and abetting claims for whatever reason? There may be good policy reasons behind it. We can have a conversation about that I think—why claims dismissed under *Corwin* should be treated differently for aiding and abetting purposes than claims dismissable under Section 102(b)(7).

And now, Joel will explain why we should leave no claim behind.

Peter Walsh: Thanks Ted. You've certainly raised some questions that I think Joel will have some thoughts on. Vice Chancellor, do you have any thoughts on *Corwin*? You have authored a number of cases based on *Corwin* and you may have some thoughts on Ted's presentation.

Vice Chancellor Glasscock: When I saw Ted's slides I was pretty exercised and there were a lot of things I wanted to say but I'm now so full of red beans and rice and jambalaya that I can't really get it together about anything. Let me just say a couple of things that are interesting about what Ted has raised. He's hit some interesting doctrinal points. First of all, with respect to *Revlon*. My understanding of *Revlon*, and I'm speaking for myself and not the court, is that the intermediate level of scrutiny is a tool. It's a tool to allow the court to get past the first prong of a preliminary injunctive relief request. It relieves the court from a finding that is more likely than not that there is a breach of fiduciary duty and allows the court, in a pre-merger situation, to remedy either unreasonable sales techniques or, more importantly, to remedy disclosure violations without addressing whether those arose from some breach of duty.

It doesn't seem to me it fits well at all in a post-closing damages claim. So I do think that our current case law has clarified that point. *Revlon* and *Unocal* really are pre-closure standards. For that very reason, another practice point that somewhat concerns me, is the idea that we have created an incentive for plaintiffs

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continued

to not bring disclosure claims so that they will have leverage to prevent *Corwin* cleansing after the merger has closed. To the extent that is happening, it's not a social good because there is no remedy for disclosure that can make the stockholders fully whole other than remedying a maldisclosure. The quasi-appraisal remedy or other post-closing damages remedies are not fully available—they are not the equivalent of restoring an informed vote. I don't know if we've done that. I don't know if it is happening. But I suspect if we do see it happening that there will be a reaction from the court that would tend to either apply laches principles or waiver or something else to prevent that social bad from happening.

The only other thing I'll say is I'm interested to watch the law develop around *Corwin*. The *Columbia Pipeline* case has made me think about hypotheticals. You could imagine a case where the binary choice that is presented to stockholders is to either accept a deal with a premium but discard a corporate asset, which is a viable breach of fiduciary duty action, or reject the deal and its certainty and pursue the breach of fiduciary action. Someone will present an argument that that is really a coercive choice in a revival of *Gantler*. Where that goes I don't know, but it's an interesting question to me. Maybe the answer is just that the value of that breach of fiduciary duty action is taken into account by the stockholders when they make their vote and it's cleansed. But I think at least it raises an interesting question where two things are being accomplished by the stockholder vote—both the acceptance or rejection of a deal premium and keeping or discarding an asset of the corporation.

Mr. Walsh: Thanks Vice Chancellor.

MA

A Guide from Ted Mirvis

Corwin: Where have all the plaintiffs gone?

Even in a transaction otherwise subject to Revlon standard review . . .

". . . when a transaction not subject to the entire fairness standard is approved by a fully informed, uncoerced vote of the disinterested stockholders, the business judgment rule applies." [*Corwin v. KKR Fin. Holdings LLC*, 125 A.3d 304, 309 (Del. 2015)].

". . . dismissal is typically the result." [Singh v. Attenborough, 137 A,3 151, 152 (Del. 2016)].

Corwin in Context

Exclusive forum by-laws

Trulia: end of disclosure-only settlement

MFW: roadmap to dismissal of controller squeeze-outs via majority-of-minority vote.

Appraisal: merger price = fair value in non-controlling/non-conflict cases: 6 – 0 (*BMC, Ramtron, CKx, Ancestry.com, AutoInfo, Lender Processing*).

Corwin #1
Use it or Lose it?

Can a plaintiff withhold pre-close litigation of disclosure claims and assert post-close to defeat *Corwin* dismissal?

Comstock: "[P]reference under Delaware law for disclosure claims to be litigated before a stockholder vote so that if a disclosure violation exists, it can be remedied by curing the informational deficiencies . . . ." [*City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Trust v. Comstock*, 2016 WL 4464156, at *9 (Del. Ch. Aug. 24, 2016) (CB), aff'd, C.A. No. 482, 2016 (Del. Mar. 23, 2017) (Order)].

Barrett: [C]laim should be brought pre-close, not post-close . . . [A] salutary incentive could be provided by considering claims based on disclosure, pled but not pursued pre-close, to be waived." [*Nguyen v. Barrett*, 2016 WL 5404095, at *7 (Del. Ch. Sept. 28, 2016)(VCG)].

Transkaryotic: "[O]nce this irreparable harm has occurred—i.e., when shareholders have voted without complete and accurate information—it is, by definition, too late to remedy the harm. [*In re Transkaryotic Therapies, Inc.*, 954 A.2d 346, 360-62 (Del. Ch. 2008)(CC)(emphasis added).

Corwin #2
Cleansing Conflicts—But Not Controllers?

KKR Fin.: BJR applies "even if [the] plaintiffs had pled facts from which it was reasonably inferable that a majority of [the company's] directors were not independent. [*In re KKR Fin. Holdings*, 101 A.3d 980, 1003 (Del. Ch. 2014)(CB), *aff'd, Corwin v. KKR Fin. Holdings LLC*, 125 A.3d 304 (Del. 2015)].

Chelsea Therapeutics: "unclear that the rule in *Corwin* . . . would cleanse a bad-faith act, even if disclosed." [*In re Chelsea Therapeutics Int'l Ltd. Stockholders Litig.*, 2016 WL 3044721, at *6 (Del. Ch. May 20, 2016)(VCG).]

Comstock: "suggesting that *Corwin* requires dismissal "unless plaintiff can establish a basis for applying entire fairness." [*City of Miami*, 2016 WL 4464156, at *7.]

Solera: noting that under *Larkin*, "the only transactions that are subject to entire fairness that cannot be cleansed by proper stockholder approval are those involving a controlling stockholder." [*In re Solera Holdings, Inc. Stockholder Litig.*, 2017 WL 57839, at *6 n. 28 ("CB).]

Columbia Pipeline: BJR applies (and dismissal required) notwithstanding allegations "sufficiently detailed to state a pleadings-stage claim for breach of the duty of loyalty" (that defendants engineered spin-off and then sale to trigger change-in-control benefits). [*In re Columbia Pipeline Grp., Inc. Stockholder Litig.*, C.A. No. 12152-VCL , at 5 (Del. Ch. Mar. 7, 2017)(Order)].

***Larkin*: applying *Corwin* to duty of loyalty claims:**

Corwin: BJR should apply if vote approving "a transaction with a party other than a controlling stockholder." [*Corwin*, 125 A.3d at 306.]

Policy: "harmonizes *Corwin* with the policy rationales that animate Delaware controlling stockholder jurisprudence"—effect of stockholder approval is **proportionate to their situational legitimacy**": "burden shifting in the controlling stockholder context"; "restoration of business judgment deference in other contexts that would otherwise implicate entire fairness review"; board-level conflicts or lapses of due care" can be cleansed by disinterested stockholders. [*Larkin*, 2016 WL 4485447, at *12 (emphasis added).]

Not cleansed: (1) controller squeeze-outs; (2) third-party deals where controller receives differential/favorable treatment.

Corwin #2.1:
BJR Rebuttable or Irrebuttable

Zale: duty of care/gross negligence claim still possible. [*In re Zale Corp. Stockholders Litig.*, 2015 WL 65511418, at *2 (Del. Ch. Oct. 29, 2015)(VCP)].

Attenborough: "employing this same standard after an informed, uncoerced vote of the disinterested stockholders would give no standard-of-review-shifting effect to the vote."

— only "the vestigial waste exception" remains.

— "stockholders would be unlikely to approve a transaction that is wasteful." [*Singh v. Attenborough*, 137 A.3d 151, 151-52 (Del. 2016)].

Volcano: vote "renders the business judgment rule irrebuttable" [*In re Volcano Corp. Stockholder Litig.*, 143 A.3d 727, 738 (Del Ch. 2016), *aff'd*,--A.3d--, 2017 WL 563187 (Del. Feb. 9, 2017) (Order)].

Larkin: effect is "review under the irrebuttable business judgment rule" [*Larkin*, 2016 WL 4485447, at *1.]

OM Group: "irrebuttable" BJR and insulates board from all attacks other than waste [*In re OM Grp., Inc. Stockholders Litig.*, 2016 WL 5929951, at *10 (Del. Ch. Oct. 12, 2016)(VCS).]

Corwin ➔

Corwin

continued

Corwin #3
Tender Offers/Section 251(h)?

Volcano: "[S]tockholder approval of a merger under section 251(h) by accepting a tender offer has the same effect as a vote in favor of [the] merger." [*In re Volcano Corp.*, 143 A.3d at 738.]

Section 251(h) "permit[s] a merger agreement to include a provision eliminating the requirement of a stockholder vote" if the tender offer results in acquirer ownership of at least the percentage of shares needed to adopt the merger agreement. *Id.* At 741 (citation omitted). Section 251(h) eliminates concerns that a tender offer "arguably is more coercive" than a merger vote. Id. At 743.

Corwin #4:
Aiding and Abetting

Can a claim dismissable under *Corwin* support an aiding and abetting claim against advisors—a la claim dismissable under DGCL Section 102(b)(7)?

NO.

Corwin: aiding and abetting "may be summarily dismissed." [*In re KKR Fin. Holdings LLC*, 101 A.2d 980, 1003 (Del. Ch. 2014) (CB).]

Attenborough: dismissal of claims "against all parties." [Singh, 137 A.3d at 153.]

Comstock: aiding and abetting claims "cannot survive." [*City of Miami Gen. Emps.' and Sanitation Emps.' Ret. Trust v. Comstock*, 2016 WL 4464156, at *23 (Del. Ch. Aug. 24, 2016)(CB), aff'd, C.A. No. 482, 2016 (Del. Mar. 23, 2017)(Order).]

Corwin #5:
Revlon R.I.P.?
1985-2015?

Corwin: "*Unocal* and *Revlon* are primarily designed to give stockholders and the Court of Chancery the tool of injunctive relief to address important M&A decisions in real time, before closing. *They were not the tools designed with post-closing money damages claims in mind.*" [*Corwin*, 125 A.3d at 312 (emphasis added).

Rural Metro: "sufficient predicate" for post-closing aiding and abetting damages liability against sell-side ibanker where board "violated its situational duty [under *Revlon*] by failing to take reasonable steps to attain the best value reasonably available to the stockholders"—in absence of gross negligence. [*RBC Capital Mkts., LLC v. Jervis*, 129 A.3d 816, 857)(Del. 2015) (emphasis added).]

Corwin #6
(Un)intended Consequences

1. Courts getting tougher on disclosure claims—materiality?
2. Plaintiffs holding back on alleging/litigating disclosure claims pre-close?
3. Plaintiffs able to raise disclosure claims solely to defeat *Corwin* post-close—not as direct claims—and avoid waiver/laches arguments?
4. Is *Corwin* really a re-reading of DGLC Section 144(a) on "interested director" transactions?
5. Is *Corwin* negation different in kind or impact than DGCL Section 102(b)(7) exculpation?

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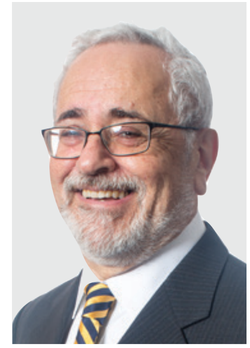
A Sleepy Topic
The Return of Appraisal Rights



Cleary's Victor Lewkow

Victor Lewkow of Cleary Gottlieb opened the panel on appraisal rights by saying this has been "the sleepiest topic for some time." He said that in the 15 years that he has been attending the Tulane Corporate Law Institute he could not remember the experts "ever more than mentioning it in passing." No longer.

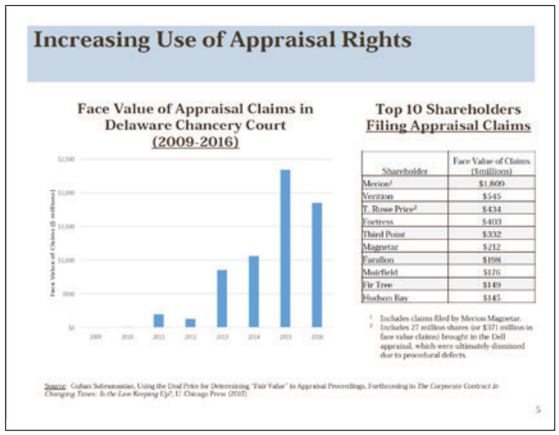
The panel included moderator Mr. Lewkow; The Honorable Andre G. Bouchard, the chancellor of the Court of Chancery; Ballad Spahr's David J. Margules; Skadden's Robert S. Saunders; and Simpson Thacher's Eric M. Swedenburg.

What are Appraisal Rights?

DGCL Section 262 provides holders of unlisted stock not held by more than 2000 holders of record with the right to demand a judicial appraisal of the "fair value" of their stock. In general, holders of listed stock (or stock held by more than 2000 holders of record) also have appraisal rights if they are required to accept as merger consideration anything other than (i) stock of the surviving company, (ii) listed stock of any other corporation or (iii) cash in lieu of fractional shares. This right is subject to *de minimis* exception adopted in 2016.

In general, to exercise appraisal rights a stockholder must: deliver a written demand prior to the vote; not have voted in favor of the merger; continuously hold the stock through closing; perfect appraisal rights after closing. A stockholder need not have owned the shares as of the deal announcement or even as of the record date for the vote.

Stockholder will receive the appraised fair value in cash together with interest at a rate of five percent over the Fed discount rate (compounded quarterly) from merger closing until paid—subject to the company's prepayment rights instituted in a 2016 statutory amendment. (See Emerging Issues, page 15.)



Statutory Underpinning

"[T]he Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors."

8 Del. C. Section 262 (h).

Putting it in Context

"[T]he standard 'Delaware block' or weighted average method of valuation, formerly employed in appraisal and other stock valuation cases, shall no longer exclusively control such proceedings. We believe that a more liberal approach must include proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court, subject only to our interpretation of 8 De. C. Section 262(h), *infra*. *See also* D.R.E. 702-05. This will obviate the very structured and mechanistic procedure that has heretofore governed such matters."

Weinberger v. UOP, 457 A.2d, 701, 712-713 (Del. 1983).

Appraisal Rights ➔

Appraisal Rights

continued

Broad Mandate, Critically Applied

"Our Supreme Court has clarified that, in appraisal actions, this Court must not begin its analysis with a presumption that a particular valuation method is appropriate, but must instead examine all relevant methodologies and factors, consistent with the appraisal statute."

Merion Capital LP v. BMC Software, Inc., C.A. No. 8900-VCG, 2015 Del. Ch. LEXIS 268, at *2 (Del. Ch. Oct. 21, 2015) (citing *Global GT LP v. Golden Telecom, Inc.*, 11 A.3d 214, 217-18 (Del. 2010).

"Although this Court frequently defers to a transaction price that was the product of an arm's-length process and a robust bidding environment, that price is reliable only when the market conditions leading to the transaction are conducive to achieving a fair price. Similarly, a discounted cash flow model is only as reliable as the financial projections used in it and its other underlying assumptions. The transaction here was negotiated and consummated during a period of significant company turmoil and regulatory uncertainty, calling into question the reliability of the transaction price as well as management's financial projections. Thus, neither of these proposed metrics to value DFC stands out as being inherently more reliable than the other."

In re Appraisal of DFC Global Corp., C.A. No. 10107-CB, 2016 Del. Ch. LEXIS 103, at *2 (Del. Ch. July 8, 2016).

Discounted Cash Flow Analysis

"The DCF method is frequently used in [Chancery Court] and, I, like many others, prefer to give it great, and sometimes even exclusive, weight when it may be responsibly."

Andaloro v. PFPC Worldwide, Inc., C.A. No. 20336 Del. Ch. LEXIS 125, at *35 (Del. Ch. Aug. 19, 2005) (Chancellor Strine).

"Although I believe my DCF analysis to rely on the most appropriate inputs, and thus to provide the best DCF valuation based on the information available to me, I nevertheless am reluctant to defer to that valuation in this appraisal. My DCF valuation is a product of a set of management projections, projections that in one sense may be particularly reliable due to BMC's subscription-based business. Nevertheless, the Respondent's expert, pertinently, demonstrated that the projections were historically problematic, in a way that could distort value. The record does not suggest a reliable method to adjust to these projections."

Merion Capital LP v. BMC Software, Inc., C.A. No. 8900-VCG, 2015 Del. Ch. LEXIS 268, at *65 (Del. Ch. Oct. 21, 2015).

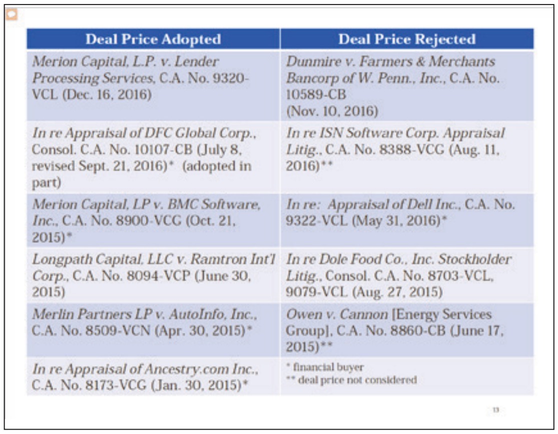
Emerging Issues: Role of Deal Price

"Requiring the Court of Chancery to defer—conclusively or presumptively—to the merger price, even in the face of a pristine, unchallenged transactional process, would contravene the unambiguous languages of the statute and the reasoned holdings of our precedent. It would inappropriately shift the responsibility to determine 'fair value' from the court to the private parties . . . .Therefore, we reject . . . [the] call to establish a rule required the Court of Chancery to defer to the merger price in any appraisal proceeding."

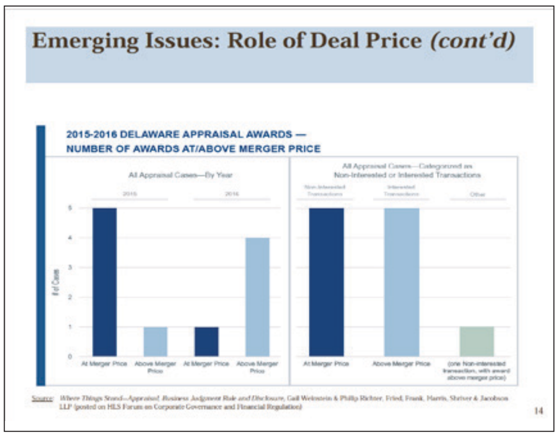
Golden Telecom, Inc. v. Glob. GT LP, 11 A.3d 214, 217-18 (Del. 2010).

"What is the fair value of an asset? For a simple asset—a piece of real property, for instance—it is the market value. If a trustee were to sell property held in trust, such a sale could be challenged by the beneficiary on a number of grounds. It would be odd, however, if the sale were an arms-length, disinterested transaction after an adequate market canvas and auction, yet the challenge was that the price received did not represent "fair" value. It would be odder still if the beneficiary presented as evidence of this proposition a post-sale appraisal, relying on speculative future income from the property not currently being realized, and stating that, notwithstanding the sales price, the true value was more than twice that received; and if the trustee's rebuttal involve a second post-facto appraisal indicating that the sales price was higher than the fair value of the parcel. In such a case the appraisals would be viewed by this Court, not as some Platonic ideal of "true value," but as estimates—educated guesses—as to what price could be achieved by exposing the property to the market. A law-trained judge would have scant grounds to substitute his own appraisal for those of the real estate valuation experts, and would have no reason to second-guess the market price absent demonstration of self-dealing or a flawed sales process."

Huff Fund Inv. P'ship v. Ckx, Inc., C.A. No. 6844-VCG, 2013 Del. Ch. LEXIS 262, at *1-2 (Del Ch. Oct. 31, 2013).



Deal Price Adopted	Deal Price Rejected
Merion Capital, L.P. v. Lender Processing Services, C.A. No. 9320-VCL (Dec. 16, 2016)	*Dunmire v. Farmers & Merchants Bancorp of W. Penn., Inc.*, C.A. No. 10589-CB (Nov. 10, 2016)
In re Appraisal of DFC Global Corp., Consol. C.A. No. 10107-CB (July 8, revised Sept. 21, 2016)* (adopted in part)	*In re ISN Software Corp. Appraisal Litig.*, C.A. No. 8388-VCG (Aug. 11, 2016)**
Merion Capital, LP v. BMC Software, Inc., C.A. No. 8900-VCG (Oct. 21, 2015)*	*In re: Appraisal of Dell Inc.*, C.A. No. 9322-VCL (May 31, 2016)*
Longpath Capital, LLC v. Ramtron Int'l Corp., C.A. No. 8094-VCP (June 30, 2015)	*In re Dole Food Co., Inc. Stockholder Litig.*, Consol. C.A. No. 8703-VCL, 9079-VCL (Aug. 27, 2015)
Merlin Partners LP v. AutoInfo, Inc., C.A. No. 8509-VCN (Apr. 30, 2015)*	*Owen v. Cannon* [Energy Services Group], C.A. No. 8860-CB (June 17, 2015)**
In re Appraisal of Ancestry.com Inc., C.A. No. 8173-VCG (Jan. 30, 2015)*	* financial buyer ** deal price not considered



"Depending on the facts of the case, a variety of factors may undermine the potential persuasiveness of the deal price as evidence of fair value."

- "For one, in a public company merger, the need for a stockholder vote, regulatory approvals, and other time-intensive steps may generate a substantial delay between the signing date and the close date."
- "Writing as a Vice Chancellor, Chief Justice Strine observed that even for purposes of determining the value of individual shares, where the stock market is typically thick and liquid, the proponents of the efficient capital markets hypothesis no longer make the strong-form claim that the market price actually determines fundamental value; at most they make the semi-strong claim that market prices reflect all available information and are efficient at incorporating new information. The M&A market has fewer buyers and one seller, and the dissemination of critical, non-public due diligence information is limited to participants who sign confidentiality agreements. . . . It is perhaps more erroneous to claim that the thinner M&A market generates a price consistent with fundamental efficiency, when the same claim is no longer made for the thicker markets in individual shares."

In re Appraisal of Dell Inc., C.A. No. 9322-VCL, 2016 Del. Ch. LEXIS 81, at *70-77 (Del. Ch. May 31, 2016).

In *Dunmire*, the Court "place[d] no weight on the Merger price as an indicator of fair value" because the Merger was not the product of an auction, the record did not "inspire confidence" that the negotiations of the Special Committee were truly arm's-length, and the transaction was not conditioned on obtaining the approval of a majority of the minority stockholders of F&M."

Dunmire v. Farmers & Merchs. Bancorp of W. Pa., C.A. No. 10589-CB, 2016 Del. Ch. LEXIS 167, at *19-22 (Del. Ch. Nov. 10, 2016).

Emerging Issues: Appraisal Standard v. Fiduciary Standard

"Because the standards differ, it is entirely possible that the decisions made during a sale process could fall within *Revlon*'s range of reasonableness, and yet the process still could generate a price that was not persuasive evidence of fair value in an appraisal. Put differently, even if a transaction passes fiduciary muster, an appraisal proceeding could result in a fair value award."

In re Appraisal of Dell Inc., C.A. No 9322-VCL, 2016 Del. Ch. LEXIS 81, *70-77 (Del. Ch. May 31, 2016).

Emerging Issues: Synergies

"The Company argued belatedly that the court should make a finding regarding the value of the combinatorial synergies and deduct some portion of that value from the deal price to generate fair value. That is a viable method. . . . Having taken these positions, it was too late for the Company to argue in its post-trial briefs that the court should deduct synergies."

Merion Capital L.P. v. Lender Processing Services, C.A. No. 9320-VCL, 2-16 Del. Ch. LEXIS 189, at *89-90 (Del. Ch. Dec. 16, 2016).

Appraisal Rights ➔

Appraisal Rights

continued

Appraisal Rights' Impact on Deal Considerations and Process

Seller's focus, meanwhile, continues to be centered on: maximizing price/value; maximizing deal certainty.

Satisfaction of fiduciary duties remains the primary driver of a seller's construction of the deal process. Satisfaction of fiduciary duties does not, however, eliminate the appraisal/price certainty risk facing a buyer. *Absent an appraisal condition*, appraisal is a post-closing risk that is borne by the buyer.

Putting it all together, how does appraisal risk impact the mating dance and deal documentation?

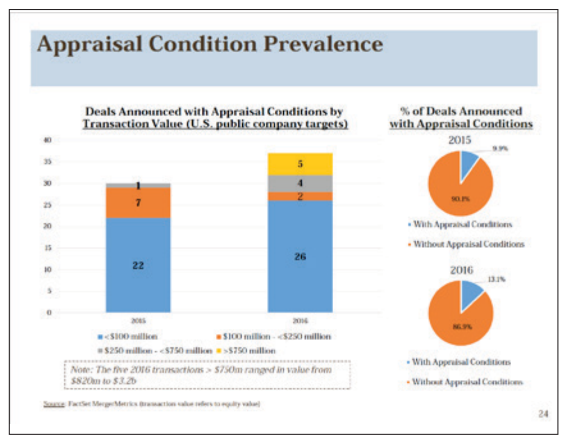
Appraisal Conditions—What's Old is New?

The perception of a heightened appraisal risk (and related buyer anxiety) is evidenced by the increased consideration by buyers of seeking an appraisal condition and some increase in the actual inclusion of such a condition.

Since adoption of DGCL Section 251(h), appraisal conditions have become possible in two-step deals. Traditional appraisal conditions have provided that: buyer need not close if initial appraisal notices given by holders of >X% of target's shares (typically 10-20%); condition measured as of proposed closing (not as of date of vote); buyer may waive the condition at or prior to closing; neither buyer nor target has termination right, until drop-dead date; no fee or expense reimbursement obligations triggered by failure of condition.

In deals with other closing conditions that remain unsatisfied post vote (*e.g.*, antitrust/regulatory, this formulation can create a limbo period between vote and drop-dead date—as stockholders may withdraw their appraisal claims at any time before closing. In the event of such a period: buyer remains obligated to continue to use agreed "efforts" to obtain approvals; target remains subject to ordinary course and other business covenants. To avoid a long limbo period, both parties may prefer a more tailored appraisal condition, which may include: buyer termination right if threshold remains exceeded for specified period after vote, with target being able to seek to obtain withdrawal of appraisal notices during that period; if appraisal cap still exceeded at end of such period and buyer doesn't waive condition within specified period, target has termination right for some period.

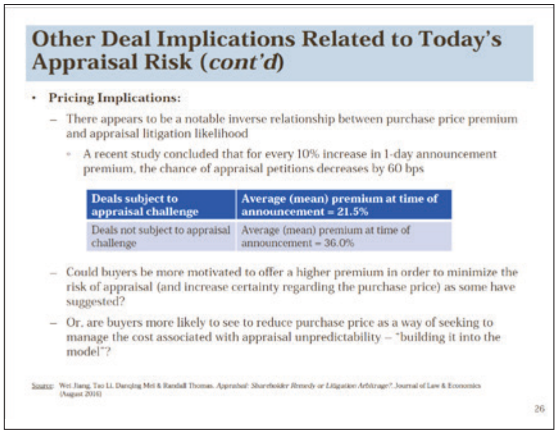
In a DGCL Section 251(h) tender offer, buyer may want to extend offer rather than make an immediate waiver decision, and target may want to require extension, in either case if the condition would be triggered. In negotiating appraisal cap percentage, parties should consider the implications of a major stockholder who may be likely to demand appraisal. In negotiating an appraisal cap, either party could seek expense reimbursement or a termination fee under specified circumstances.

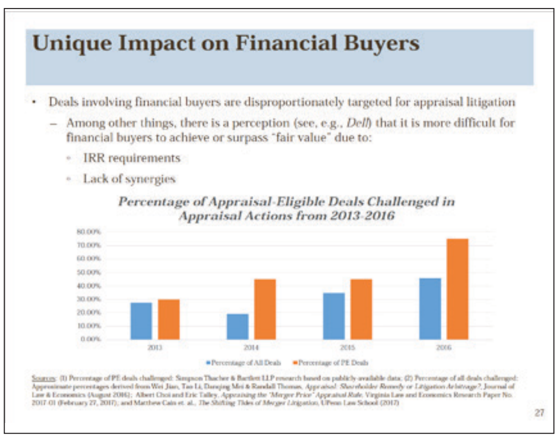


Other Deal Implications Related to Today's Appraisal Risk

The Exclusivity Discussion: Exclusive negotiations = less pre-signing price discovery = more perceived risk of drawing appraisal litigation and having it result in a valuation that is materially in excess of deal price. Despite increased risk of appraisal litigation (and the corollary of less overall price certainty), a buyer may nonetheless pursue a strategy of seeking to engage in exclusive negotiations with the seller. In response, the seller may look to seek buyer's agreement to not demand an appraisal condition. Query as to practical enforceability?

Impact on Deal Protection Negotiations: The more robust the sale process, the more likely a court will defer, at least in part, to the merger price in appraisal litigation. Accordingly, the threat of appraisal could theoretically soften, somewhat, buyer deal-protection related demands. Similarly, the presence of an appraisal condition could incentivize the seller to demand a more robust market check (pre- and post-signing). Query whether use of a go-shop could help mitigate appraisal risk??





Unique Impact on Financial Buyers

Appraisal claims pose unique challenges for financial buyers. When the aggregate purchase price will not be known until post-closing:

- How does this impact financing commitments at signing?
- How to accurately model the investment?
- Issues with navigating capital calls?

Silver (or Grey?) lining: Financial buyer may be able to reduce capital invested at closing and until resolution of appraisal litigation.

- Can change the leverage profile immediately post-closing.
- Other advantages and disadvantages?

Appraisal Prepayment

In 2016, legislation was adopted in Delaware permitting the "prepayment" of appraisal demands in order to cut off claims for interest on the prepaid amounts. Statutory amendments also limited appraisal to cases involving a minimum aggregate share value of $1 million or 1 percent of the outstanding stock of the company.

Anecdotal indications regarding the use of the pre-funding option to limit the interest rate exposure (5 percent over the Federal Reserve discount rate) are a mixed bag. Some buyers have used the option. Other buyers, however, pass on the opportunity, weighing factors such as:

- Cost of capital associated with prepaying (particularly poignant concern of financial buyers)
- Whether depriving an appraisal petitioner of liquidity by not prepaying could reduce overall appraisal actions and/or offer a buyer leverage in settlement negotiations with appraisal petitioners.

When buyers are considering pre-funding, the key decision points become when to pre-fund and how much.

- Benefit of preserving some downside risk for petitioners.

Final Observations

Further Judicial Guidance: Deal world anxiously awaits Delaware Supreme Court decisions in *Dell* and *DFC Global*. Impact on other notable appraisal litigations pending in the Chancery Court (*e.g.*, *Petsmart*).

Possible Future Legislative Developments?

The following reforms have been proposed and/or discussed in various circles as a result of the appraisal arbitrage phenomenon:

Reduction of Statutory Interest Rate—Reduce the statutory pre-judgment interest rate paid on the amount awarded in any appraisal proceeding.

Shareholder Disqualification—Disqualification of shareholders from appraisal if they were not owners as of the record date, or perhaps even as of the date on which the merger was announced.

Potential appraisal-friendly reforms have been discussed as well, such as: eliminating the exception for stock-only deals; enhanced disclosure requirements to give shareholders additional information needed to conduct an independent valuation.

No indication that the appraisal trend will abate. The appraisal arbitrage community, by all accounts, have achieved attractive rates of return to date employing the strategy. Based on

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continued

a study of appraisal petitions from 2000 to 2014, one study estimates that the average annualized net return on appraisal petitions (not including settlements) was approximately 25 percent, and it appears that appraisal arbitrage funds have subsequently continued to generate attractive returns.

Corwin and (if controllers use it) *MFW* and their progeny (and *Trulia*) may also increase the likelihood of appraisal litigation. Appraisal now one of the few avenues open to plaintiffs to seek post-closing remedies. Recent studies have suggested that the limitation on remedies in merger challenges has been correlated with an increase in appraisal claims. Although statutory reforms were recently adopted to reduce appraisal litigation, practitioners have not been surprised that they have not dissuaded the appraisal arbitrage community.

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Impediments to Stealth Acquisitions by Activists

By Ethan A. Klingsberg, Steven J. Kaiser and Elizabeth K. Bieber of Cleary Gottlieb Steen & Hamilton LLP

A settlement on July 12, 2016 by the DOJ with ValueAct for violations of the HSR Act's notification requirements and an interpretation of the Exchange Act's beneficial ownership reporting rules posted by the SEC staff on July 14, 2016 combine to have an impact on shareholder activism and engagement.

These developments at the DOJ and SEC matter because the effectiveness of hedge fund activism is directly related to the extent to which the funds may engage in "under the radar" accumulations of equity positions. Enhanced enforcement of the requirement to obtain HSR Act clearance in advance of accumulations in excess of $[fill in] of publicly traded shares with a non-passive intent and the threat of a $40,000 per day fine for violations will drive activist funds to use American-style, stock-settled options to accumulate shares as these arrangements will not count as beneficial ownership for HSR purposes until the options are exercised and the fund actually holds voting power (as opposed to the right to acquire voting power). But an important limitation on the effectiveness of this approach to stealth accumulations is that the SEC's beneficial ownership reporting rules, in contrast to the HSR rules, will consider these options to constitute "beneficial ownership" even if the funds do not have the right to control the vote over the underlying shares until after exercise of these options. Under the SEC regime, once an activist's fund group has beneficially owned such options or outright shares representing in excess of 5% of the outstanding shares for at least 10 calendar days, the activist must publicly report the ownership on Schedule 13D and thereafter promptly update upon any material changes.

At the heart of these new developments is a struggle by these two governmental agencies to determine where to draw the line between active vs. passive investing, albeit under rules using different language and against backdrops of different statutory regimes, for purposes of determining when a shareholder's level of engagement is "active" enough that the investment ceases to qualify for a passivity exemption from the requirement to make an HSR Act notification or a filing of a Statement of Beneficial Ownership on Schedule 13D. See "Activist 13G Filers," (page 20) some of whom do not have non-activist divisions and which have regularly disclosed their 5%+ holdings on Schedule 13G in reliance on Rule 13d-1(b)'s passive investor exemption from Schedule 13D that entitles the filer to delay filing until as late as the 45th calendar day after the end of the calendar year in which the shares were purchased. These requirements to make an HSR notification and file a Schedule 13D, especially when combined with each other, can impede meaningfully the ability of an activist shareholder to buy under the radar in many scenarios.

The DOJ's complaint that ValueAct failed to qualify for the exemption from the HSR Act notification was based on allegations not only that ValueAct was communicating opinions on strategic matters to the issuers in question, but also that ValueAct coupled these communications with a self-promoted reputation as an activist that uses disruptive tactics, including proxy contests and other efforts to change board composition, to assure that issuers implement its opinions. We noted, at that time, that the SEC staff may use a similar rationale to view activist hedge funds as ineligible to rely on a Schedule 13G passivity exemption from Schedule 13D filing requirements when these funds are conveying opinions to boards even though they are holding off on threatening proxy contests. Accordingly, we hypothesized that the ValueAct complaint and any adherence by the SEC staff to a similar approach in analyzing Section 13(d) matters should not stand for the proposition that HSR Act notifications or Schedule 13D filings are required when "non-activist" institutional investors communicate substantive opinions to issuers without any express or background threats to lead the charge on a change to board composition.

The ValueAct settlement with the DOJ, however, does not go so far as to require that ValueAct, so long as it holds itself out as an activist with a proud history of causing changes to the compositions of boards and senior managements, must file an HSR Act notification whenever it holds in excess of the applicable HSR Act threshold (currently $80.8 million worth of voting stock) in an issuer to which it intends to communicate any substantive views. Instead, the settlement focuses on the specific subject matter of proposals that trigger an HSR Act notification if ValueAct either "intends" to make any such proposal or has an investment strategy specific to the issuer in question that "identifies circumstances in which ValueAct may" make such proposals. The types of proposals covered would include formal shareholder proposals for inclusion in a proxy statement, as well as all types of oral or written communications to any director or officer, but would arguably not cover the publication of proposals in white papers addressed to broad audiences, such as a hedge fund conference, or commentary aimed at the general market via the press or social media. The subject matter includes:

- proposals that the company merge with a third party, acquire a third party, or sell itself to a third party, or similar proposals to the third party for such a transaction with the company if ValueAct owns any equity in the third party;
- proposals to modify or pursue an alternative to the company's publicly announced merger or acquisition transaction;
- proposals to change the corporate structure that would require shareholder approval; and
- proposals to change the company's strategies regarding the pricing of any products or services, production capacity, or production output.

Notably missing from this list are proposals relating exclusively to changes to executive compensation, even though the DOJ's complaint against ValueAct highlighted alleged efforts by ValueAct to change an issuer's compensation structures.

To what extent do shareholders need to be wary when venturing into communications with a company that touches upon these areas? The claims in the ValueAct complaint arise from a particularly bad set of alleged facts. According to the complaint, ValueAct allegedly took numerous steps, as a shareholder of both Halliburton and Baker Hughes in excess of the threshold for HSR Act notification, to pressure directors and officers of each company to pursue strategic options in connection with navigating and reacting to the difficult antitrust review process that the pending Halliburton-Baker Hughes merger was undergoing. Moreover, ValueAct apparently had a history of alleged failures to make required HSR Act notifications. While a perfect storm of alleged entanglement with the DOJ's antitrust review of a merger is what caused ValueAct to grab the attention of the DOJ, all shareholders – even those with neither a self-promoted reputation as an activist nor any intent ever to get involved with leading a campaign to change the composition of the board or management – should consider the parameters of the ValueAct settlement in determining whether they have active or passive intent for HSR purposes.

By contrast, the SEC staff's release was designed more pointedly to give comfort that those investors, which do not traditionally consider themselves to be activist or that merely consider themselves to be "good governance activists," may continue with their issuer engagement strategies without triggering a Schedule 13D filing obligation. Additionally the SEC staff's statement reinforces that the typical subject matter of hedge fund activist approaches definitely do merit a Schedule 13D filing when the applicable ownership threshold is met. On the SEC

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staff's list of topics that, on their own, do not render an investor ineligible to rely on the passivity exemption from filing a Schedule 13D:

- executive compensation, social or public interest issues (including environmental policies) and
- corporate governance topics (including staggered boards, majority voting standards, and elimination of poison pills) where the discussion is part of a "broad effort . . . for all its portfolio companies."

But specifically calling for the sale or restructuring of the company, sale of significant assets, or a proxy contest would definitely put the shareholder into Schedule 13D territory.

The results of these "passive vs. active" line drawing efforts by the DOJ and the SEC —in pursuit of different policy objectives and without coordination, but with similar and inter-related impacts— will become increasingly tricky and significant as a handful of traditional money managers and institutional investors continue to show up among the top shareholders of almost all publicly traded companies while, in parallel, these money managers and institutional investors become more directly involved in influencing these companies and arguably position themselves to become the heirs to the campaigns run nowadays by hedge fund activists.

"Activist" 13G Filers[1]

	Voting Power	"Activist"	Company	Date of 13G filing
1.	18.8%	Pershing Square	Restaurant Brands International Inc.	1/5/2015
2.	13.4%	Pershing Square	Fortune Brands Home & Security, Inc.	10/18/2011
3.	11.8%	Marcato Capital Management	CyrusOne Inc.	3/28/2013
4.	11.0%	Pershing Square	Burger King Worldwide, Inc.	6/22/2012
5.	9.67%	Marcato Capital Management	Aerojet Rocketdyne Holdings, Inc.[2]	2/14/2012
6.	8.9%	Pershing Square	Family Dollar Stores, Inc.	6/9/2011
7.	8.6%	Pershing Square	Alexander & Baldwin, Inc.	7/6/2012
8.	8.6%	Pershing Square	Matson, Inc.	7/6/2012
9.	8.25%	Corvex Management	Nomad Foods Ltd.	2/16/2016
10.	8.0%	Pershing Square	General Growth Properties, Inc.	1/3/2013
11.	7.19%	Marcato Capital Management	Cincinnati Bell Inc.	10/25/2012
12.	7.1%	Marcato Capital Management	Vail Resorts, Inc.	2/14/2014
13.	6.59%	Marcato Capital Management	Trinity Place Holdings Inc.[3]	2/14/2012
14.	6.55%	Third Point	Citadel Broadcasting Corporation	2/11/2011
15.	6.52%	Corvex Management	B/E Aerospace Inc.	2/17/2015
16.	6.50%	Corvex Management	Lamar Advertising Company	2/14/2014
17.	6.4%	Marcato Capital Management	Macquarie Infrastructure Company LLC	2/14/2014
18.	5.42%	Third Point	Ally Financial Inc.	2/13/2015
19.	5.36%	Third Point	Swift Transportation Company	2/11/2011

[1] This chart lists only those initial Schedule 13G filings over a five year period by well-known activists where they have filed pursuant to Rule 13d-1(b), which requires that the filer be both passive and meet one of the criteria for being a qualified institution, such as being a registered investment advisor, broker-dealer or investment company. There are additional "activist 13G filings" that are not in this chart where the activist claims passivity but fails to be a qualified institution and therefore takes advantage of the short-form disclosure of Schedule 13G, but is not entitled to the delayed timing for the filing applicable for Rule 13d-1(b) filers.

[2] Formerly GenCorp Inc.

[3] Formerly Syms Corp

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