

[原著論文]

M&A Litigation in Delaware Courts from January to June 2018

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Abstract

This paper presents an overview of some of the most important decisions handed down by the Delaware Supreme Court and the Delaware Court of Chancery from January 2018 to June 2018 in lawsuits arising out of Merger and Acquisition (M&A) transactions.

I. Introduction:

Following closely on the heels of a spurt in M&A transactions in the final quarter of 2017, several factors were expected to influence M&A activity in 2018. Among these were major changes in the U.S. tax code, uncertainty regarding antitrust enforcement, and record levels of funds at the disposal of private equity funds. Ever since the Delaware Chancery Court's decision in *In re Trulia, Inc. Stockholders Litigation*,¹ whereby the Court had laid down stringent conditions for the approval of disclosure-only settlements, there has been a perceptible migration of "disclosure-only" lawsuits to other courts, including the federal courts.² However, due to a multitude of factors – among them the fact that Delaware is the corporate domicile for a large number of corporations – the Delaware Courts continue to hold their pre-eminent status in matters relating to corporate litigation. Following is a brief outline of the most important Merger and Acquisition cases decided by the Delaware Court of Chancery and the Delaware Supreme Court in the period from January to June 2018.³

II. A brief overview of significant Merger and Acquisition cases decided by the Delaware Courts in the first six months of 2018:

1) *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*⁴

This case involved an appraisal proceeding in connection with the 2015 acquisition by Hewlett-Packard Company ("Hewlett-Packard") of Aruba Networks, Inc. ("Aruba") for a consideration price of \$24.67 per share. The petitioners were shareholders of Aruba who sought appraisal of their shares under Section of 262 of the General Corporation Law of the State of Delaware. In a post-trial decision, the Chancery Court determined that the fair value of the shares was \$17.13 per share – considerably less than the merger price. The Court arrived at this figure on the basis of Aruba's thirty-day average unaffected market price after considering three alternative methods of valuation that were argued before the Court, namely: (i) the unaffected market price, (ii) the merger price, and (iii) a discounted cash flow analysis.

This was the Court of Chancery's first appraisal decision after the Delaware Supreme Court's decisions in *DFC Global*⁵ and *Dell*⁶ in which the Delaware Supreme Court had invoked the Efficient Capital Markets Hypothesis as providing a basis for the reliability of market prices. The Chancery Court,

¹ *In re Trulia, Inc. Stockholders Litigation*. Consolidated C.A.No. 10020-CB. Decided by the Court of Chancery of the State of Delaware on January 22, 2016. Opinion available at: <https://courts.delaware.gov/opinions/download.aspx?ID=235370>.

² One such case decided during the first six months of 2018 was *Varjabedian v. Emulex Corp.* where the Ninth Circuit ruled that in order to assert a claim under Section 14(e) of the Securities Exchange Act of 1934, the plaintiff would have to show negligence. See: *Varjabedian v. Emulex Corp.*, 888 F.3d 399.

³ One significant non-Delaware decision issued during this period was in *In re Xerox Corporation Consolidated Shareholder Litigation*, by the Supreme Court of the State of New York granting a preliminary injunction in respect of a public company deal. Index No. 650766/18 (Doc.No.488, April 27, 2018). Another significant M&A decision was issued by the New York Supreme Court in May 2018 in *In re Handy & Harman Ltd. Stockholder Litigation* (Index No. 654747/2017, in the Supreme Court of the State of New York, New York County, Commercial Division). The Court considered the applicability of Delaware's "MFW" standard in respect of a Delaware corporation in New York.

⁴ *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.* C.A. No. 11448-VCL, decided by the Court of Chancery of the State of Delaware on February 15, 2018. Memorandum Opinion available at: <https://www.appraisalrightslitigation.com/files/2018/02/Chancery-Court-Hands-Down-Ruling-in-Aruba-Networks-Aruba-Post-Trial-FINAL-2-15-18.pdf>.

⁵ *DFC Global Corp. v. Muirfield Value Partners, L.P.*, 2017 WL 3261190 (Del. Aug.1, 2017).

⁶ *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 2017 WL 6375829 (Del. Dec. 14, 2017).

in this case found that the market for Aruba's shares had the attributes that the Delaware Supreme Court had considered to be sufficient to constitute an efficient market in *DFC Global* and *Dell*⁷ and that this unaffected stock price was the most compelling evidence of fair value. The Court of Chancery rejected the competing discounted cash flow valuations proffered by the two sides on the footing that they were to be accorded due weightage only where the acquired company was not public or the sale had not been conducted in an open market. Neither of these conditions applied in the present case. Similarly, the Court refused to countenance the deal price on the footing that it incorporated an uncertain subjective judgment about the anticipated synergies, and though it had to be considered considerable weight, it was not determinative of fair value. The Court further determined that a proper appraisal of fair value should also exclude the value of reduced agency costs. On the basis of these factors, the Court awarded the petitioners \$17.13 per share.

This decision is significant inasmuch as it was the first handed down by the Delaware Court of Chancery in an appraisal action in the wake of the Delaware Supreme Court's decisions in *DFC Global* and *Dell*. The decision highlights the caveat that the possibility of receiving an amount lower than the merger price is a factor to be considered by those seeking to file appraisal actions.⁸

2) In re Appraisal of AOL Inc.:⁹

This, too, was an appraisal case involving Section 262 of the General Corporation Law of the State of Delaware, in which the Court made extensive reference to the Delaware Supreme Court's opinions in *DFC Global* and *Dell* and discussed their ramifications.¹⁰ The case arose out of the merger of AOL with Verizon for a deal price of \$50 per share. Petitioners were stockholders of AOL who sought appraisal of their shares. At the outset, the Court considered whether the sales process was in conformity with the factors set out by the Delaware Supreme Court in *DFC Global* and *Dell* as constituting a sufficient basis for the determination of the deal price as indicative of fair value. In the Court's view, these factors

⁷ *Verition Partners Master Fund Ltd. V. Aruba Networks, Inc*, *Supra* note 4, at internal pages 60- 63 of the Court's Opinion.

⁸ However, it should be pointed out that on appeal the Delaware Supreme Court by its decision issued on April 16, 2019 reversed and remanded the Court of Chancery's judgment. The Supreme Court held that the Court of Chancery judgment was based on an erroneous finding of fact and ordered that on remand the Court of Chancery enter judgment for the petitioner-appellants in a sum of \$19.10 per share which represented the deal price less a part of the synergies, plus interest. See: *Verition Partners Master Fund Ltd. V. Aruba Networks, Inc.* No. 368, 2018. Decided by the Supreme Court of the State of Delaware on April 16, 2019. Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=288480>.

⁹ *In re Appraisal of AOL Inc.*, C.A.No.11204-VCG. Decided by the Court of Chancery of the State of Delaware on February 23, 2018. Memorandum Opinion available at:<https://courts.delaware.gov/Opinions/Download.aspx?id=269440>.

¹⁰ Regarding the weight to be accorded to the transaction price in determining fair value, the Court here pithily summed up the essence of the Supreme Court's opinions thus:

“Where information necessary for participants in the market is widely disseminated, and where the terms of the transaction are not structurally prohibitive or unduly limiting to such market participation, the trial court in its determination of fair value must take into consideration the transaction price as set by the market. ... In sum, while no presumption in favor of transaction price obtains, a transaction that demonstrates and unhindered, informed, and competitive market value is at least first among equals of valuation methodologies in deciding fair value. ...”

would be satisfied “where (i) information was sufficiently disseminated to potential bidders, so that (ii) an informed sale could take place, (iii) without undue impediments imposed by the deal structure itself.”¹¹ Upon a detailed examination of the circumstances of the sale, the Court was of the view that it was not in full compliance with what was set out by the Delaware Supreme Court in *DFC Global* and *Dell*. The Court noted that no auction had been conducted, that the deal protection terms included a no-shop, a 3.5% break-up fee, and matching rights. and one fact in particular, namely, a statement made by the AOL CEO in a TV interview where he made the statement that he was “committed to the deal with Verizon...” and that he had given Verizon his “word” that the deal would happen.¹² The Court was of the view that this statement that he had given his “word” to Verizon, could have served to ward off other potential bidders and this fact coupled with the other circumstances in the case rendered the deal price an unreliable indicator of fair value.¹³ The Court concluded that given the circumstances, a discounted cash flow (DCF) analysis would be the best mode of evaluating fair value. As is common, a vast gulf separated the competing figures proffered by the experts of the two sides. According to the DCF analysis of the petitioners’ expert, \$69.98 per share was the fair value of AOL stock. In contrast, based on the DCF analysis of the respondent’s expert, \$44.85 per share was the fair value. The Court conducted its own DCF analysis and arrived at a figure of \$48.70 as being the fair value on the date of valuation.

Thus, once again, the petitioners were awarded an amount lower than the deal price, albeit through the use of a different mode of evaluating fair value than that used in the *Verition v. Aruba*¹⁴ case. Both cases emphasized the importance of market evidence, and could serve as a deterrent to appraisal seekers in public company mergers.¹⁵

3) *Christopher Miller et al v. HCP & Company et al.*:¹⁶

This case arose out of a sale of an LLC, Trumpet Search to an unaffiliated third party. The minority

¹¹ *In re Appraisal of AOL Inc., id.*, at internal page 20 of the Court’s Opinion.

¹² *In re Appraisal of AOL Inc., id.* Transcript of the TV interview at internal pages 16 and 17 of the Court’s Opinion.

¹³ The Court summed up the disabling circumstances as:

...[A] *no-shop* provision, combined with (i) the declared intent of the acting CEO to consummate a deal with Verizon, (ii) the CEO’s prospect of post-merger employment with Verizon, (iii) unlimited three-day matching rights, and (iv) the fact that Verizon already had ninety days between expressing interest in acquiring the entire company and signing the Merger Agreement, including seventy-one days of data room access.

In re Appraisal of AOL Inc., id., at internal pages 22 and 23 of the Court’s Opinion.

¹⁴ *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc, supra* note 4.

¹⁵ It is noteworthy that on February 23, 2018, that is, the same day on which the Delaware Court of Chancery handed down its ruling in the *AOL* case, the Delaware Supreme Court issued a ruling in an appraisal case affirming the decision of the Court of Chancery whereby the Court had determined fair value as being below the merger price. This decision was significant inasmuch as it was the first time since the advent of “appraisal arbitrage” that the Delaware Supreme Court affirmed a decision of the Court of Chancery setting the valuation clearly below the merger price. See: *Merlin Partners, LP and AAMAF, LP v. SWS Group, Inc. and Hilltop Securities Holdings LLC v. Lone Star Value Investors, LP and Lone Star Value Co-Invest II, LP*. No. 295, 2017. Decided by the Supreme Court of the State of Delaware on February 23, 2018. Order, available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=269400>.

¹⁶ *Christopher Miller et al v. HCP & Company et al.* C.A. No. 2017-0291-SG. Decided by the Court of Chancery of the State of Delaware on February 1, 2018. Memorandum Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=268570>.

unitholding members brought an action against the majority unitholding members claiming that the sale had been conducted in breach of the implied covenant of good faith and fair dealing. The plaintiffs alleged that the sale had been approved without conducting an open auction that would have resulted in a much higher sales price and thereby the unitholding members did not receive the maximum value of their units. Defendants brought a motion to dismiss the complaint under Rule 12(b)(6) of the Rules of the Court of Chancery of the State of Delaware.

Under the Operating Agreement, every unitholding member was required to consent to a sale that had been approved by the majority-dominated Board, which was vested with sole discretion to determine the manner of the sale, subject to only one condition, which was properly met. The gravamen of the plaintiffs' case was that the priority of distribution set out in the Operating Agreement was such that the majority unitholding members had no incentive to negotiate a price above a certain figure. According to the plaintiffs, the defendants, that is, the majority unitholding-member had, as might be expected, acted in alignment with their incentives. The plaintiffs contended that notwithstanding the fact that under the Operating Agreement all fiduciary duties on the part of the members and the Board had been waived, there was an implied covenant of good faith and fair dealing that made it incumbent upon the Board to conduct an open market sale or auction to get the highest price and thereby maximize the value of the units held by all the members. In light of the express terms of the Operating agreement, the Court refused to read an implied covenant of good faith and fair dealing.

The Court of Chancery succinctly outlined the principles to be gleaned from the Court's precedents regarding the invoking of the implied covenant of good faith and fair dealing.¹⁷ The Court determined that the conditions for successfully invoking the implied clause of good faith and fair dealing were not met in the present case. Finally, noting that the plaintiffs could have adequately safeguarded their interests by means of suitable provisions in the Operating Agreement, but that they had not done so, the Court granted the defendants' motion to dismiss. The Court's Opinion highlights the necessity for parties to pay careful heed to the terms of the Operating Agreement at the time of negotiation, because resort to implied covenants cannot be easily had when a party gets disgruntled by the implications of those terms at a later date.

4) *Appel v. Berkman et al.*:¹⁸

¹⁷ *Christopher Miller et al v. HCP & Company et al. id.*, At internal pages 22 and 23 of the Court's Opinion, the Court summed up the principles thus:

“The implied covenant applies only when one party “proves that the other party has acted arbitrarily or unreasonably, thereby frustrating the fruits of the bargain that the asserting party reasonably expected.” A party's reasonable expectations are measured as of the time of contracting, and any implied terms must address “developments or contractual gaps that the asserting party pleads neither party anticipated.” The Court will not rewrite a contract simply because a party now wishes it had gotten a better deal. ... “[G]ood faith” in the implied covenant context entails “faithfulness to the scope, purpose, and terms of the parties' contract.” Similarly, “fair dealing” ... simply means actions consonant “with the terms of the parties' agreement and its purpose.””
[Internal citations omitted.]

¹⁸ *Appel v. Berkman et al.* No.316, 2017, C.A. No. 12844—VCM. Decided by the Supreme Court of the State of Delaware on February 20, 2018. Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=269180>.

This was a ruling handed down by the Delaware Supreme Court regarding a decision of the Chancery Court whereby the Chancery Court had granted a motion to dismiss a stockholder's suit challenging the sale of Diamond Resorts International ("Diamond Resorts") to Apollo Global Management ("Apollo") by means of a two-step merger transaction under Section 251 (h) of the State of Delaware General Corporation Law. The stockholder's suit called into question the fairness of the merger and alleged that the Diamond Resorts International Board had omitted to disclose all material information to the stockholders in respect of the tender offer.

The Founder-Chairman of Diamond Resorts had abstained from voting in favor of the merger because he had reservations about the price and the timing of the sale.¹⁹ In its Schedule 14D-9 filing with the Securities and Exchange Commission, Diamond Resorts mentioned that the Chairman had abstained from voting and also that he was yet to determine whether he would tender his shares. However, no reasons were given for his abstention or his yet-to-be-determined stance regarding the tendering of his shares. The Court of Chancery dismissed the plaintiffs' damages claim on the ground that the shareholders' vote in favor of the tender offer was fully informed.

At issue before the Delaware Supreme Court was whether the omission in the proxy statement regarding the Chairman's abstention from the vote was materially misleading. The Delaware Supreme Court disagreed with the reasoning of the Chancery Court and reversed and remanded for further proceedings.²⁰

The Court's opinion highlights the importance of disclosing the reasons for a director's abstention or dissension in cases where a vote to sell a company is not unanimous. Omission to do so could also disentitle a company from claiming the protection of the business judgment rule under *Corwin*.²¹

5) *In Re Rouse Properties, Inc. Fiduciary Litigation*:²²

This case arose in connection with the merger of Rouse Properties Inc. ("Rouse") with Brookfield

¹⁹ The relevant part of the Minutes of the Board of Directors Meeting as quoted in the Court's Opinion reads:

"he was disappointed with the price and the Company's management for not having run the business in a manner that would command a higher price, and that in his view, it was not the right time to sell the company."

Appel v. Berkman et al. id., at internal page 4 of the Court's Opinion.

²⁰ The Court explained its reasoning thus:

Precisely because Delaware law gives important effect to an informed stockholder decision, Delaware law also requires that the disclosures the board makes to stockholders contain the material facts and not describe events in a materially misleading way. Here, the founder and Chairman's views regarding the wisdom of selling the company were ones that reasonable stockholders would have found material in deciding whether to vote for the merger or seek appraisal, and the failure to disclose them rendered the facts that were disclosed misleadingly incomplete.
[Internal citations omitted]

Appel v. Berkman et al. id., at internal page 2 of the Court's Opinion.

²¹ See *Corwin v. KKR Financial Holdings LLC*, 125 A.3d 304 (Del.2015).

²² *In Re Rouse Properties, Inc. Fiduciary Litigation*. Consolidated C.A.No.12194—VCS. 2018 WL 1226015 (Del. Ch. Mar.9, 2018). Decided by the Court of Chancery of the State of Delaware on March 9, 2018. Memorandum Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=269960>.

Asset Management, Inc. (“Brookfield”). A group of companies affiliated to Brookfield collectively owned 33.5% of Rouse’s shares, being its largest stockholder. Plaintiffs were stockholders of Rouse who brought suit against the members of the Special Committee constituted by Rouse in connection with the merger and its largest stockholder, Brookfield, alleging breaches of fiduciary duties.

Brookfield, the 33.5% stockholder offered to acquire all the shares of Rouse that it did not hold. After weeks of negotiation between Brookfield and Rouse’s Special Committee, a price of \$18.25 per share was decided upon, which was approved by Rouse’s Special Committee and its Board. The proposed deal was then presented to Rouse’s shareholders for approval. The plaintiffs initially sought to enjoin the merger transaction before the stockholder vote, alleging shortcomings in the sales process, but the motion was denied. Following the denial, 82.4% of the non-Brookfield shares voted in favor of the merger. The merger transaction thereupon closed. Plaintiffs then filed an amended complaint seeking post-closing damages alleging breaches of fiduciary duties on the part of Brookfield as the controlling stockholder and the members of the Special Committee, and also alleging aiding and abetting on the part of Brookfield. Defendants sought dismissal under Court of Chancery Rule 12 (b)(6).

The Court’s analysis first addressed the question as to whether Brookfield was a controller. Relying upon precedent, the Court noted:

Under Delaware law, a stockholder is a controller *only* if he “(1) owns more than 50% of the voting power of a corporation or (2) owns less than 50% of the voting power of the corporation but *exercises control* over the business affairs of the corporation.”²³
(Internal citation omitted)

In support of their case, the plaintiffs sought to argue, inter alia, that two members of the Special Committee were not independent of Brookfield, and that the Special Committee had tilted the deal conditions in Brookfield’s favor. Upon a detailed consideration of the facts and circumstances of the case, however, and the law as it prevailed under the Court’s precedents, the Court rejected plaintiffs’ contention that Brookfield was a controlling shareholder. Absent a controller, the transaction would be subject to the business judgment rule under *Corwin*²⁴ unless the plaintiff had adequately pleaded that the stockholder vote was coerced or uninformed. On this point, too, the Court found that the plaintiffs had not adequately so pled.

Further, the Court found no substance in the plaintiffs’ aiding and abetting claim as the Court had already found that there was no breach of fiduciary duty, nor was any knowing participation in any such alleged breach properly pled. On that basis, the Court granted the Defendants’ motion to dismiss.

²³ *In Re Rouse Properties, Inc. Fiduciary Litigation. Id.* at internal page 30 of the Court’s Opinion. The Court here cited *In Re KKR Financial Holdings LLC*, 101 A.3d 980 (2014) at 991.

²⁴ *Corwin v. KKR Financial Holdings LLC.*, 125 A.3d 304 (Del.2015). While upholding the judgment of the Court of Chancery, the Delaware Supreme Court stated at the outset of the Court’s Opinion as follows:

In a well-reasoned opinion, the Court of Chancery held that the business judgment rule is invoked as the appropriate standard of review for a post-closing damages action when a merger that is not subject to the entire fairness standard of review has been approved by a fully-informed, uncoerced majority of the disinterested stockholders.

The detailed examination of the nature of Brookfield’s stockholding indicates that a court’s determination as to whether a large, but less-than-a-majority shareholder is a controlling shareholder will be done through a fact-specific inquiry.

6) *In Re Tesla Motors, Inc. Stockholder Litigation*:²⁵

This case arose out of the 2016 acquisition by Tesla, Inc. (“Tesla”) of SolarCity Corporation (“SolarCity”). Elon Musk was the largest stockholder of Tesla (owning about 22.1% of Tesla’s common stock) and its Chairman of the Board, CEO, and Chief Product Architect. Elon Musk was also the largest stockholder of SolarCity (owning about 21.9% of SolarCity’s common stock) and its Chairman of the Board. The Tesla Board had not constituted a special committee to consider the acquisition in spite of some apparent conflicts. Upon the announcement of the proposed acquisition, Plaintiffs, who were the stockholders of Tesla, filed multiple suits challenging the transaction. Tesla stockholders, excluding interested stockholders, later voted to approved the merger. Plaintiffs contended that Elon Musk was a conflicted controller, and alleged, inter alia, that the Tesla Board and Elon Musk had committed breaches of fiduciary duties in approving the transaction. The Defendants brought a motion to dismiss, contending that in light of the fully informed, uncoerced vote of the disinterested stockholders, the deferential business judgment standard of review would apply. The crux of the case was whether Elon Musk was a controlling stockholder despite owning only 22.1% of Tesla shares.²⁶

The Court examined four factors which the Plaintiffs proffered in support of their contention that Elon Musk was a controlling shareholder, namely: “1.Musk’s Control of the Vote”²⁷; “2. Musk’s Control Over Tesla’s Board”²⁸; “3.The Board Level Conflicts”²⁹; “4. Musk and Tesla Acknowledge Musk’s Influence.”³⁰ In the Court’s analysis, it was the sum total of all the circumstances which were determinative of whether Elon Musk in fact controlled the company.³¹ Upon a consideration of all the factors, the Court concluded as follows:

[T]he combination of well-pled facts relating to Musk’s voting influence, his domination of the Board during the

²⁵ *In Re Tesla Motors, Inc. Stockholder Litigation*. Consolidated C.A.No. 12711 – VCS. Decided by the Court of Chancery of the State of Delaware on March 28, 2018. Memorandum Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=270830>.

²⁶ *In Re Tesla Motors, Inc. Stockholder Litigation*, *id.* at internal page 39 of the Court’s Opinion, the Court formulated the substance of the required pleading thus:

“...[T]he plaintiff may plead either (or both) of the following: that the minority blockholder actually dominated and controlled the corporation, its board or the deciding committee with respect to the challenged transaction or (2) that the minority blockholder actually dominated and controlled the majority of the board generally.”

[The Court here cited *In Re Rouse Props., Inc. Fiduciary Litig.*, 2018 WL 1226015, at *12 (Del. Ch. Mar.9, 2018).

²⁷ *Id.*, at pages 41-45 of the Court’s Opinion.

²⁸ *Id.*, at pages 46-50 of the Court’s Opinion.

²⁹ *Id.*, at pages 50-53 of the Court’s Opinion.

³⁰ *Id.*, at pages 54-56 of the Court’s Opinion.

³¹ *Id.* at page 43 of the Court’s Opinion, the Court cited and quoted the following passage from *Superior Vision Servs.*, 2006 WL 2521426 at *4 (emphasis added by the Court in the present case)(Square brackets, too, supplied by the Court in the present case: “[T]he focus of the [controller] inquiry [is] on the *de facto* power of a significant (but less than majority) shareholder, which, when *coupled with other factors*, gives that shareholder the ability to dominate the corporate decision-making process.”

process leading up to the Acquisition against the backdrop of his extraordinary influence within the Company generally, the Board level conflicts that diminished the Board's resistance to Musk's influence, and the Company's and Musk's own acknowledgement of his outsized influence, all told, satisfy Plaintiffs' burden to plead that Musk's status as a Tesla controlling stockholder is reasonably conceivable.³²

Since the Court found it "reasonably conceivable" at the motion stage that Elon Musk was a controlling stockholder of Tesla, if this were proven to be so, then the transaction would be subject to the entire fairness standard of review. In the circumstances, the Court denied the motion to dismiss. The Court deemed the issue of exculpation which the Defendants had tepidly raised to have been waived for the purpose of the motion in question.

The Court's opinion is significant, inasmuch as it highlights the possibility that even a stockholder with a small – though sizable – stockholding can be considered to be a "controlling stockholder" if the surrounding supplemental facts indicate predominance over the affairs of the company. In the present case, the circumstantial evidence considered by the Court included the terms of the merger deal, Elon Musk's previous actions and his status within the company at the relevant time, and public statements issued on behalf of Tesla. These are useful pointers to be considered when a potential problem relating to control is likely to be an issue. It is to be noted that the Tesla Board had not constituted a Special Committee to consider the acquisition. It remains a question whether the approval of an independent, properly empowered Special Committee that performed its duty of care, coupled with the fully informed, uncoerced vote of the disinterested stockholders which was duly done in this case, would have ensured the protection of the business judgment rule.

7) *City of North Miami Beach General Employees' Retirement Plan et al. v. Dr. Pepper Snapple Group, Inc. et al.*:³³

The case arose out of the merger of Dr. Pepper Snapple Group, Inc. ("Dr. Pepper") and Keurig Green Mountain, Inc. ("Keurig") by means of a reverse triangular merger whereby a parent company acquires a target company through a subsidiary which in turn is absorbed by the target company. Under the merger deal in the present case, a subsidiary of Dr. Pepper would merge into Keurig with Keurig becoming the surviving wholly-owned subsidiary of Dr. Pepper. The stockholders of Keurig would get the right to receive newly issued Dr. Pepper stock. Stockholders of Dr. Pepper were to retain their shares and would receive a special cash dividend of \$103.75 per share which would be partly funded by a \$9 billion cash dividend to be paid by the parent of Keurig to Dr. Pepper. After completion of the merger, the holding of the original stockholders of Dr. Pepper would collectively represent 13% of the combined company whereas the original stockholders of Keurig would receive shares collectively representing 87% of the combined company. The approval of the Dr. Pepper stockholders was sought in respect of certain transactions that were to be prerequisites to the effectuation of the merger. The proxy statement filed by Dr. Pepper with the SEC in that connection stated that the stockholders would have no appraisal rights under Section 262 of the Delaware

³² *Id.*, at page 57 of the Court's Opinion.

³³ *City of North Miami Beach General Employees' Retirement Plan et al. v. Dr. Pepper Snapple Group, Inc. et al.* C.A. No. 2018-0227-AGB. Decided by the Court of Chancery of the State of Delaware on June 1, 2018. Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=273770>.

General Corporation Law. Plaintiffs were stockholders of Dr. Pepper who claimed that they were entitled to an appraisal of their shares in connection with the merger. Plaintiffs and two defendants – namely, Dr. Pepper and the parent of Keurig – filed cross- motions for summary judgment.

The Court viewed the case as turning on the interpretation of Section 262 of the Delaware General Corporation Law (“DGCL”) which deals with appraisal rights. Under the Court’s interpretation, plaintiffs were not entitled to appraisal rights. The Court based its ruling on two grounds, namely: (i) Dr. Pepper was not a “constituent corporation” under Section 262 (b) of the DGCL; and (ii) as the stockholders of Dr. Pepper were to retain their shares and not relinquish them, they could not avail of the provisions of Section 262 (b) of the DGCL.

The Court based its reasoning on the interpretation of the statutory language of the relevant provisions of the DGCL. Firstly, Section 262 (b) expressly mentions that appraisal rights can be availed of in respect of shares of a “constituent corporation.”³⁴ To determine the meaning of the term “constituent corporation,” the Court examined the use of the term in other sections of the the DGCL, specifically in Section 251 (a)³⁵ and Section 262 (b)(1)(ii),³⁶ and the interpretation of the term in the Court’s precedents and concluded that it “means only an entity that actually is being merged or combined with another entity in a merger or consolidation and thus does *not* include a parent of such entities.”³⁷ Since this was a reverse triangular merger in which the subsidiary of Dr. Pepper was to merge with the parent stockholding entity of Keurig, the Court ruled that the stockholders of Dr. Pepper would not be entitled to appraisal rights.

³⁴ Specifically, the opening lines of § 262 (b) read as follows:

(b) Appraisal rights shall be available for the shares of any class or series of stock of a constituent corporation in a merger or consolidation to be effected pursuant to § 251 (other than a merger effected pursuant to § 251 (g) of this title), § 252, § 254, § 255, § 256, § 257, § 258, § 263 or § 264 of this title: ...

City of North Miami Beach General Employees’ Retirement Plan et al. v. Dr.Pepper Snapple Group, Inc. et al.,id., cited at page 12 of the Court’s Opinion. Statutory text available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=273770>.

³⁵ The provisions of § 251 (a) read as follows:

(a)Any 2 or more corporations of this State may merge into a single surviving corporation, which may be any 1 of the constituent corporations or may consolidate into a new resulting corporation formed by the consolidation, pursuant to an agreement of merger or consolidation, as the case may be, complying and approved in accordance with this section.

City of North Miami Beach General Employees’ Retirement Plan et al. v. Dr.Pepper Snapple Group, Inc. et al., id.. Cited at page 13 of the Court’s Opinion. Statutory text available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=273770>.

³⁶ The relevant portion of §262 (b)(1)(ii) reads as follows:

...[F]urther provided that no appraisal rights shall be available for any shares of stock of the constituent corporation surviving a merger if the merger did not requires for its approval the vote of the stockholders of the surviving corporation as provided in § 251 (f) of this title.

City of North Miami Beach General Employees’ Retirement Plan et al. v. Dr.Pepper Snapple Group, Inc. et al., id. Cited at page 14 of the Court’s Opinion. Statutory text available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=273770>.

³⁷ *City of North Miami Beach General Employees’ Retirement Plan et al. v. Dr.Pepper Snapple Group, Inc. et al., id.* at page 21 of the Court’s Opinion.

Furthermore, the Court ruled that under the provisions of Section 262 (b) of the DGCL, “stockholders are only entitled to appraisal of their share *when those shares* are being taken from them in *certain, statutorily specified* types of transactions.”³⁸ Since the stockholders in this case retained their shares, the Court ruled that the stockholders were not entitled to appraisal rights under Section 262 (b).³⁹

On that basis, the Court granted defendants’ motion for summary judgment, and denied plaintiffs’ cross-motion for summary judgment.

The Court’s Opinion highlights the paramount importance accorded by the Court in appraisal actions to the express language of the statute even in a case such as this where the actual end result of the transaction was that the original stockholders of Dr. Pepper would be ceding control of Dr. Pepper to the parent of Keurig.

8) *Edinburgh Holdings, Inc. v. Education Affiliates, Inc.*:⁴⁰

This case arose out of a dispute over an “earn-out” provision in an agreement relating to the sale of a business. An “earn-out” clause in an agreement provides that the buyer will pay further post-closing consideration upon the fulfillment of specified conditions. Its purpose is to facilitate the closing of the transaction where the parties cannot reach an agreement about the sale price due to uncertainty about the post-closing performance of the acquired company.

The plaintiff in this case, operating under a previous name, sold its education business to a subsidiary of Education Affiliates, Inc. Under the purchase agreement, Education Affiliates, Inc. was required to pay a fixed price at the time of closing, and then pay further post-closing amounts on the condition that the acquired business achieve specified revenue targets after the closing. The Agreement also provided that the pre-closing managers of the plaintiff would continue to manage the business post-closing and that they would do so, inter alia, “consistent with its past practices.” The earn-out period was to run for a period of four years after closing, and payments were to be made annually each year. Education Affiliates duly made the required payments for the first three years but refused to do so for the fourth year, alleging managerial misconduct. Plaintiff brought suit against Education Affiliates and a related party seeking the remaining additional payments. Defendants filed a counterclaim and third-party claims alleging fraud and breaches of contractual and fiduciary duties. Plaintiff and defendants to the original suit filed cross motions to dismiss. The Court granted the original defendants’ motion to dismiss one count of the original plaintiff’s complaint whereby the original plaintiff had alleged “breach of the implied covenant of good faith and fair dealing,”⁴¹ on the ground that it was a redundant duplication of the original plaintiff’s claim for “breach of contract.”⁴² The Court also granted the original plaintiff’s motion in respect of one of the original defendants’ claims, namely that relating to “fraudulent inducement and breach of fiduciary duty,”⁴³ but denied the original plaintiff’s motion regarding the “breach of contract”⁴⁴ claim.

Regarding the breach of implied covenant claim in the original plaintiff’s complaint, the Court

³⁸ *City of North Miami Beach General Employees’ Retirement Plan et al. v. Dr. Pepper Snapple Group, Inc. et al.*, *id.* at page 24 of the Court’s Opinion. (Italics as given in the text of the Opinion.)

³⁹ The Court further spelled out, arguendo, additional reasons why appraisal rights would not be available to the plaintiffs under Section 262 (b) of the DGCL.

⁴⁰ *Edinburgh Holdings, Inc. v. Education Affiliates, Inc.* C.A. No. 2017-0500-JRS. Decided by the Court of Chancery of the State of Delaware on June 6, 2018. Memorandum Opinion available at: <https://courts.delaware.gov/Opinions/Download.aspx?id=274020>.

⁴¹ *Id.*, at internal page 3 of the Court’s Opinion.

⁴² *Id.*, at internal page 3 of the Court’s Opinion.

⁴³ *Id.*, at internal page 3 of the Court’s Opinion.

⁴⁴ *Id.*, at internal page 3 of the Court’s Opinion.

stated that it could only be invoked in respect of matters that were not clearly covered by the express terms of the contract.⁴⁵ Since the original plaintiff's right to receive the additional payments was clearly stated in the purchase agreement, the original plaintiff's attempt to rely upon the implied covenant was merely a duplication of the plaintiff's contractual claim. For that reason, the Court dismissed the original plaintiff's implied covenant claim. Regarding the fraud claim in the original defendants' counterclaim and third party claims, the Court held that the facts necessary to sustain such a claim were insufficiently pled and on that ground, dismissed defendants' fraud claim. Regarding the original defendants' breach of contract claim, however, the Court determined that it needed a resolution of what the "past practices" of the business were and whether they had been adhered to post-closing. According to the Court, this would entail a fact-intensive inquiry that could not be resolved on a motion. For that reason, the Court refused to dismiss the original defendants' breach of contract claim. One count of the original defendants' counterclaim and third-party complaint was based on a claim of breach of fiduciary duty. The Court dismissed this claim on the ground that it duplicated the breach of contract claim.

This case is a useful pointer to the ways in which earn-out provisions can lead to post-closing disputes. In particular, the case highlights the need for greater clarity in spelling out the rights and duties of the parties rather than relying on general, broadly-worded clauses.

9) *Glidepath Limited v. Beumer Corporation*:⁴⁶

This case, too, related to an earn-out provision. This case arose in connection with the sale by the plaintiffs of a 60% stake in the equity of Glidepath LLC to the defendants, under an Acquisition Agreement. The Acquisition Agreement postulated, inter alia, a period of shared management by the plaintiffs and the defendants under the provisions of a separate Operating Agreement. A part of the payment price was to be paid as an earn-out over a period of three years from the anticipated date of the closing of the sale which was recorded in the agreement. For various legitimate reasons, the actual closing of the sale was delayed by a period of about nine months beyond the originally anticipated closing date. However, the relevant dates of the earn-out period as recorded in the agreement were not changed. Later, the defendants refused to make any earn-out payments beyond the date mentioned in the agreement. Plaintiffs contended that the agreement postulated an earn-out period that would run for three years after the date of closing. Defendants disputed the plaintiffs' claim. Thereupon, plaintiffs filed the present suit alleging breach of contract and breach of fiduciary duty. One of the principal contentions advanced by the plaintiffs was that the dates of the three-year period as recorded in the Acquisition and Operating Agreements should be "reformed" to reflect the actual dates of the closing and the three-year period

⁴⁵ The Court stated:

The implied covenant is available only where the terms to be implied are missing from the contract; it "cannot be invoked to override the express terms of a contract. Thus, if the contract at issue expressly addresses a particular matter, an implied covenant claim respecting that matter is duplicative and not viable.
(Internal citations omitted.)

Edinburgh Holdings, Inc. v. Education Affiliates, Inc., *supra* note 40, at internal page 21 of the Court's Opinion.

⁴⁶ *Glidepath Limited v. Beumer Corporation*. C.A.No.122220-VCL. Decided by the Court of Chancery of the State of Delaware on June 4, 2018. Memorandum Opinion available at: <https://www.klgatesdelawaredocket.com/wp-content/uploads/2018/06/Glidepath-Limited-and-Sir-Ken-Stevens-KNZM-v.-Beumer-Corporation-et-al.-memorandum-opinion-180604.pdf>.

thereafter. Consequently, such reformation would also extend the earn-out period by a period of about nine months. By the present opinion, the Court addressed the “reformation” question as it would have a direct bearing on other claims in the suit.

The Court addressed this question by clearly setting out what the plaintiffs would need to do in order to get the Agreement reformed. The Court stated:

The party seeking reformation first must show that it was mistaken about the contents of the final, written agreement. The proponent must show either that its counterparty was similarly mistaken (mutual mistake) or that its counterparty “knew of ...[the]mistake and remained silent” so as to take advantage of the error. Finally, the party seeking reformation must prove the existence of a specific meeting of the minds regarding a term that was not accurately reflected in the final, written agreement.⁴⁷
(Internal citations omitted.)

Upon a detailed examination of the facts of the case, the Court concluded that the plaintiffs were not entitled to the sought reformation of the terms of the Agreement.

The case highlights yet another potential cause of dispute that can arise with relation to an earn-out provision. Specifically, it is a reminder that in the event of a closing being deferred to a date beyond that which the parties had anticipated, it is essential that the relevant dates set out in the Agreement be revisited and suitably revised where necessary.

III. Conclusion:

In spite of the drop in M&A-related litigation in Delaware Courts in recent years,⁴⁸ the Delaware Court of Chancery and the Delaware Supreme Court continue to hold their reputational primacy for their expertise in matters relating to corporate law. The cases decided by the Delaware Courts in the first six months of 2018 have been important steps in the continuing evolution of M&A jurisprudence.⁴⁹

Received date May 28, 2019

Accepted date August 1, 2019

⁴⁷ *Glidepath Limited v. Beumer Corporation, id.*, at internal page 24 of the Court’s Opinion. (Internal quotation marks, brackets, and parentheses are as set out in the text of the Court’s Opinion.)

⁴⁸ Three cases in particular have played a large role in bringing about this decline, namely: *C&J Energy*, 107 A.3d 1049 (Del. 2014); *Corwin*, 125 A.3d 304 (Del.2015); and *Trulia*, 129 A.3d 884 (2016).

⁴⁹ One decision not outlined in the present paper is the Delaware Court of Chancery’s March 2018 decision relating to an injunction of a stockholder vote sought by a stockholder-plaintiff in *Brigade Leveraged Capital Structures Fund Ltd. v. Kindred Healthcare, Inc.*