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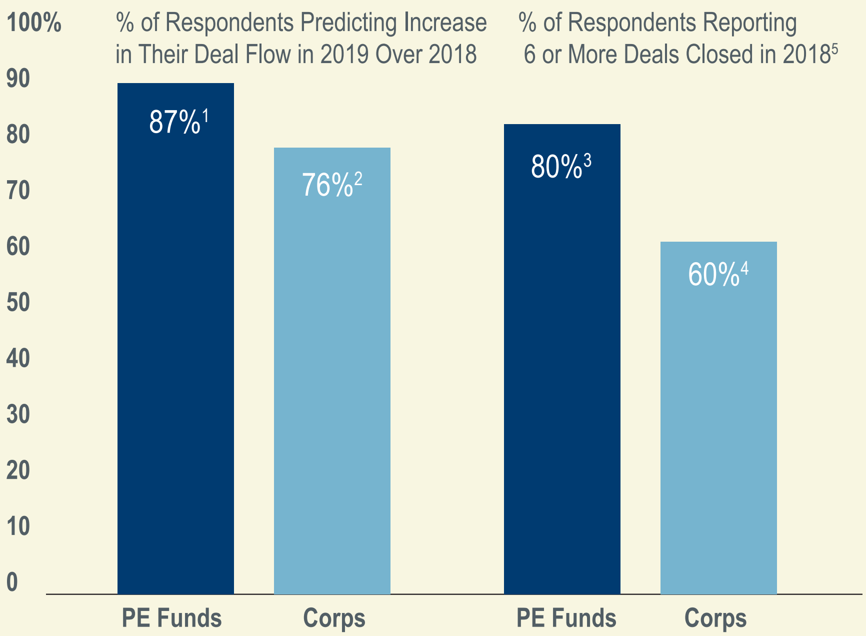
M&A/PE *QUARTERLY*

A quarterly round-up of key M&A/PE developments

April 2019

Number & Size of M&A/PE Deals Are Expected to Increase in 2019

Despite a significant uptick in deal flow from 2017 to 2018, the vast majority of U.S.-based corporate and PE executives expect a further increase in their deal flow in 2019. Further, 70% of respondents predict that deal sizes will be larger in 2019 than 2018.



Data from Deloitte survey of 1,000 executives at a variety of U.S.-based PE Funds and corporations. [1]Up from 76% that expected an increase in 2018 over 2017. [2]Up from 69% that expected an increase in 2018 over 2017. [3]Up from 60% in 2017. [4] Up from 50% in 2017. [5]Further, a majority reported a significant increase in the total value of their deals in 2018 over 2017.

The Increasing Risk for Companies of Being Required to Produce Emails and Texts in Section 220 Actions—Papa John's *and* Palantir

Two recent Delaware decisions, *Schnatter v. Papa John's* (Jan. 15, 2019) and *KT4 Partners LLC v. Palantir Technologies* (Jan. 20, 2019), highlight an increased willingness by the Delaware courts, in Section 220 actions, to order that directors' and officers' emails and/or texts be produced. This trend is evolving against a backdrop of significantly expanded use of emails and texts in connection with modern business practices and recordkeeping. We note that, due to the real-time nature of and oftentimes more informal and less guarded approach with respect to email and text communications, when produced, they often provide critical evidence that is rarely discovered through more traditional written records and communications (such as board presentations and meeting minutes).

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Key Points

- **These decisions reflect an expansion of the court's willingness to order the production of emails**. While there is no bright-line test for determining whether emails (and other non-traditional forms of communication) will have to be produced in response to a Section 220 action, their production was ordered in these cases against a backdrop of the courts' observation that "the reality of today's world" is that corporate communications are increasingly by email and text. In *Palantir*, the Delaware Supreme Court ordered production of corporate emails based on the company's failure to observe corporate formalities that would have resulted in evidence being available from the production of traditional written records. In *Papa John's*, the Court of Chancery went further, ordering the production of personal emails and texts on directors' and officers' personal email accounts and personal devices on the basis that the communications "relate[d] to the rights and obligations of the corporation" (rather than being purely personal) and "the need for the information sought outweigh[ed] the burdens of production and the availability of the information from other sources."

- ***Papa John's* also clarifies that a director's "proper purpose" for a books and records demand will not be undermined by his *also* having a personal purpose.** A director will have a "proper purpose" if his purpose "relates to his duties as a director." That proper purpose will not be undermined by his also having a personal purpose—such as, in the case of a director with whom the company has sought to sever its ties due to the director's alleged misconduct, to restore his public reputation and/or to retain his position by establishing that the board acted improperly).

- **It cannot be emphasized enough that directors and officers, when communicating by email or text (including on their personal accounts and devices when the communications relate to corporate business), should keep in mind that the communications may be producible in response to Section 220 demands or in other litigation.**

Section 220. DGCL Section 220 permits a *stockholder* to inspect the company's books and records for any "proper purpose." What constitutes a proper purpose for a stockholder is not specified in the statute (but has been developed by case law); and the burden of proof is on the stockholder to prove that she has a proper purpose. Section 220(d) permits a *director* to inspect the company's books and records for any proper purpose. The statute defines a proper purpose for a director as "a purpose reasonably related to the director's position as a director"; and the burden of proof is on the company to prove that a director does not have a proper purpose. (An officer would not have any right under Section 220 to inspect the books and records unless she were also a shareholder or a director.) It is well established that, under Section 220, a director's right to obtain corporate books and records is broader than a stockholder's right.

Palantir. In *Palantir*, a Section 220 demand was made by a major stockholder for the purported purpose of investigating possible fraud, mismanagement and breach of fiduciary duty by company executives in connection with amendments to the company's Investors Rights Agreement and representations that may have been made by the company to the other stockholders relating to the amendments. The Court of Chancery (Feb. 22, 2018) found that the plaintiff-stockholder had a proper purpose for the demand of both written and electronic books and records, but the court specifically rejected the demand for emails. Vice Chancellor Slights reasoned that the production of emails was not essential to fulfilling the plaintiff's purpose given that traditional, non-email books and records existed that could be produced.

On January 29, 2019, the Delaware Supreme Court overturned that part of the Court of Chancery's decision and ruled that the emails had to be produced because there were no non-email documents that were responsive to the Section 220 request. The Supreme Court emphasized that the plaintiff had shown that the company generally had not observed corporate formalities (including by having repeatedly not held an annual meeting of stockholders), and had indeed conducted business by email (and, in one case, by a LinkedIn message). Chief Justice Strine wrote that companies that "document their actions through board minutes, resolutions and official letters" should be able to satisfy a Section 220 request with these documents and not have to produce emails and texts. However, he wrote further, the issue must be decided "in light of companies' actual and evolving record-keeping and communications practices." He observed as a general matter: "Today, emails and other electronic communications do much of the work of the paper correspondence of yore" and "[a company] cannot use its own choice of medium to keep stockholders in the dark about the substantive information to which §220 entitles them." The Supreme Court also rejected the company's contention that a plaintiff had to prove by "compelling evidence that emails are necessary to a proper purpose."

Papa John's. In *Papa John's*, in response to a director's Section 220 demand, the Court of Chancery granted access to directors' *personal* emails and text messages (*i.e.*, communications on their *personal* email accounts and devices rather than just their corporate email accounts). Although it declined to impose a bright-line rule for considering §220 requests for information from personal accounts and devices, the court emphasized the need to "apply its discretion on a case-by-case basis to balance the need for the information sought against the burdens of production and the availability of the information from other sources . . .."

JS, a Papa John's director who was the founder, largest stockholder, recent Chair, and long-time public face of the company, provoked intense negative media attention after stating on an earnings call his view that the company's revenues had declined due to the National Football League's mishandling of the players' protests during the playing of the national anthem. (Papa John's was then the NFL's exclusive pizza sponsor.) Subsequently, a magazine article reported that JS had spoken a racial slur during an internal training session. In the wake of these events, the company's stock price fell significantly; the board removed JS as CEO and Chair and requested that JS resign as a director (which he refused to do); and the company terminated its contractual arrangements with JS relating to his marketing services and use of office space.

JS filed a Section 220 demand with the stated purpose of determining whether, in severing ties with him, the directors had breached their fiduciary duties to act in the best interests of the stockholders. According to JS, the board's actions had a significant negative impact on the company and were undertaken without the board having interviewed him or investigated his conduct. Chancellor Bouchard ruled that JS was entitled to the access he sought. Thereafter, activist firm Starboard acquired 10% of the company's shares; JS set up a proxy fight by nominating himself for reelection to the board; and, after many months, the company and JS reached an agreement pursuant to which JS will resign from the board and be replaced by an independent director. As part of the agreement, the company has agreed to share with JS all of the company's records, giving him the option to sue if the documents reveal wrongdoing by the company.

The court focused on whether the communications that were sought constituted "corporate books and records." The court stated that, if the company's directors, CEO and General Counsel had "used personal accounts and devices to communicate about changing the Company's relationship with [JS], they should expect to provide that information to the Company." Notably, the court emphasized "the reality of today's world" that people communicate frequently by emails and texts. The court wrote: "Although some methods of communication (e.g., text messages) present greater challenges for collection and review than others, and thus may impose more expense on the company to produce, the utility of Section 220 as a means of investigating mismanagement would be undermined if the court categorically were to rule out the need to produce communications in these formats."

Other cases. The issue of the discoverability of emails and texts of directors, executives and/or bankers has figured prominently in other recent high-profile cases, with ensuing negative publicity for the companies and persons involved and apparently negative impact for them in the litigation. These litigations have involved, for example, Rent-A-Center Inc., Kate Spade, Facebook, Uber, Xerox, Aruba Networks and Viacom. In one notable case, *Transperfect*, Chancellor Bouchard viewed a smiley-face emoticon in a party's texts as evidence of the party's malign intent.

Practice Points

- **Critically, directors and officers should anticipate the possibility of corporate and personal emails having to be produced in response to a Section 220 demand or otherwise in litigation.** It cannot be emphasized enough that email communications should be (and so often are not) written and used with this possibility kept in mind. Appropriate use of and attention to emails should be a routine part of corporate training for directors.

- **Directors and officers generally should seek to refrain from conducting corporate business on their personal email accounts or devices.** Directors generally should use a dedicated email account for company business and should consider obtaining a corporate-issued email account for their board service and related work. Personal emails and texts (including on a director's or officer's personal devices) may be producible in a Section 220 action if there is more than mere suspicion that corporate business was conducted in this way. Factors that may create more than mere suspicion could include the company not regularly keeping traditional books and records (such as minutes), the directors not having corporate email accounts, and/or the company not having a policy expressing that directors should not use their personal email accounts for corporate business. Companies should consider (i) providing officers and directors with corporate email accounts and cellphones or other mobile devices for their communications regarding company business and (ii) maintaining a written policy expressing that the company considers communications on directors' and officer's personal accounts and devices to be "'personal unrestricted information' outside the control of the company."

- **Companies should expect that, when the board seeks to sever ties with a director for alleged offensive misconduct, in addition to contractual, defamation and fiduciary claims, the director is likely to make a books and records demand.** We note that generally a board cannot force a director off the board. *Papa John's* has potentially broad applicability in the current era of increased sensitivity to allegations of sexual harassment or racism. As *Papa John's* illustrates, once a director has established a proper purpose for a Section 220 demand (which could include to investigate whether the board mismanaged the company), the directors' access to books and records is essentially unfettered (and should not be thwarted by the director also having a personal purpose in seeking, for example, to restore his reputation, retain his position and/or increase his leverage in negotiating a separation settlement). Clearly, a board should carefully weigh, based on the specific facts and circumstances, the advantages of taking quick action to seek to sever ties with (or, in particularly sensitive situations, to isolate) a director who allegedly has engaged in offensive misconduct versus taking time to conduct an internal or external investigation into the allegations.

- **In contrast to a stockholder, a director can successfully pursue a derivative lawsuit contemporaneously with a Section 220 demand.** A stockholder's filing of a derivative lawsuit generally in considered to be a concession by the stockholder that inspection of the company's books and records is not necessary or essential to pursuit of the claims he or she is making. However, when a director-shareholder files a Section 220 demand (as a director) and simultaneously files a derivative suit (as a shareholder), the court does not automatically assume such a concession. Generally, a director need not establish that books and records he or she seeks are necessary or essential to his or her proper purpose in seeking them because, given a director's fiduciary duties to the company and its stockholders, a director is accorded very broad access rights to books and records and in any event is subject to obligations not to misuse the information. In *Papa John's*, JS agreed with the court that materials he obtained in the Section 220 action would not be used in the derivative lawsuit he was pursuing in his interest as a stockholder.

- **A Section 220 demand may still be successful even when the underlying fiduciary claims are likely to be dismissed.** Notably, in *Papa John's*, any duty of care violation by the Papa John's board would have been exculpated under the company's charter; and a duty of loyalty violation generally would be untenable where the directors, as in that case, were independent.

See our Briefing*, Court of Chancery Grants the Books and Records Demand of a Director Whose Ties With the Company Were Severed by the Board After His Allegedly Offensive Conduct*—Schnatter v. Papa John's (Jan. 24, 2019).

Court of Chancery Rules that a Merger Termination, After the Other Party "Simply Forgot" to Provide an Extension Notice, Is Valid—Vintage Rodeo v. Rent-A-Center

In *Vintage Rodeo Parent, LLC v. Rent-A-Center, Inc*. (March 14, 2019), the Delaware Court of Chancery ruled that Rent-A-Center, Inc.'s termination of the merger agreement pursuant to which it was to be acquired by Vintage Rodeo Parent, LLC was valid. Rent-A-Center terminated the agreement after Vintage apparently "simply forgot" to provide a formal notice of extension of the merger agreement.

The merger agreement provided that, if the transaction had not closed after six months (the "end date"), either party could terminate the agreement by providing notice; but that, if at the end date, antitrust clearance review for the transaction was still ongoing, thereafter either party could provide a notice of extension of the agreement for an additional period. The notices were to be in writing and provided to specified addresses. Until the end date, the parties had been working toward obtaining antitrust clearance, arranging financing, and planning for integration (as they were contractually required to do). Their actions relating to antitrust clearance reflected that they expected that the clearance would not be obtained by the end date and that they would continue to seek the clearance after the end date. After the agreement was signed, there were no discussions between the parties about extension or termination of the agreement. At the end date, neither party provided an extension notice. A few days after the end date, Rent-A-Center (whose performance apparently had improved since the parties had agreed to the merger) sent notice of termination of the agreement and a demand for payment of the $127.6 million reverse termination fee.

Vice Chancellor Glasscock held that the termination was valid and he has sought supplementary briefs from the parties on the issue of payment of the reverse termination fee. The court emphasized that, generally, contracts will be judicially enforced in accordance with their express terms—which, in this case, required formal written notice to the other party to extend the merger agreement.

The court rejected Vintage's various arguments that the termination was invalid. First, Vintage argued that the parties' actions that contemplated a delayed closing and continued efforts beyond the end date to obtain antitrust approval indicated that notice of extension of the agreement had been effectively provided or waived. Second, Vintage argued that the implied covenant of good faith, and the parties' express covenant to use reasonable efforts to close the transaction, required that Rent-A-Center provide some "warning" to Vintage that Rent-A-Center wanted to terminate the agreement or that Vintage apparently was forgetting the notice requirement for extending the agreement. The court (i) emphasized that the express, unambiguous terms of the contract will govern, and that, in this case, the terms required formal written notice to the other party to extend the agreement; (ii) stated that there is no general "duty to warn" a counterparty that one is considering termination of an agreement or that there is an upcoming deadline for extension or termination of an agreement; and (iii) clarified that an "efforts" covenant does not override an express right to terminate an agreement.

It remains to be seen whether the court will find that the reverse termination fee is payable by Vintage. Because the parties expected that the transaction might not close due to antitrust clearance not being obtainable, the merger agreement provided for a reverse termination fee (RTF) to be paid by Vintage if the transaction did not close and antitrust approval had not been obtained. The court has asked for supplemental briefing on the issue "whether the implied covenant of good faith and fair dealing should apply to liability for a reverse breakup fee in these circumstances, where the buyer remains willing and able to proceed toward closing." The Vice Chancellor offered that he was "dubious" whether the parties intended the fee to be payable when the termination of the agreement was due to Vintage's forgetting to give notice of extension of the agreement rather than due to antitrust issues.

Practice Points

- **Awareness of deadlines.** Obviously, it is imperative that parties have a system for reminding themselves of deadlines set forth in their agreements. This is true for deadlines with respect to the right to terminate or extend an agreement, as well as deadlines for taking specified required actions, making indemnification claims (in private deals), and other matters.

- **Effect of course of conduct.** Where a party believes that its and/or its counterparty's course of conduct has effected an implicit change in the provisions of an agreement, the party should consider whether it would be prudent to seek a formal amendment to (or waiver from) the terms of the agreement.

- **Reverse termination fees.** The risk of not ultimately obtaining antitrust approval is sometimes (in antitrust-sensitive deals, often) dealt with through a provision requiring the payment of a "reverse termination fee" by the buyer to the target company (or, in a private deal, to the sellers) if antitrust approvals are not received by the end date (or, if applicable, permitted extensions of the end date), or antitrust approval cannot be obtained without divestiture of assets beyond an agreed limit. *Rent-A-Car* underscores the importance of an RTF provision being drafted so that it accurately reflects the parties' intention with respect to when it would and would not be payable. With respect to the size of an RTF, the fiduciary duty issues relating to breakup fees as deal protection mechanisms are not applicable, Thus, the amount of the fee is generally a contractual matter, with challenge being possible if the amount may constitute unreasonable liquidated damages. While the size of RTFs has generally been somewhat above the usual 3-4% range of deal protection fees, conceivably the court in *Rent-A-Car* could be influenced by the size of the RTF (15% of the deal value—which the court called "enormous") as it decides whether the fee is payable in the unusual circumstances under which the agreement was terminated.

- **Interrelationship of termination provision and efforts commitment**. A merger agreement should expressly provide that the exercise of a right to terminate the agreement will not in and of itself constitute a breach of the covenant to use efforts to consummate the proposed transaction.

- **Notice provisions.** A merger agreement should be clear with respect to the timing, content, and method of delivery for meeting any notice requirements in the agreement.

Delaware Forum Selection Clauses, Control Groups and Dilution of Early-Stage Investors—Reminders and Practice Points Arising from Sheldon v. Pinto *and* Plaze v. Callas

Two recent Court of Chancery decisions—*Sheldon v. Pinto* (Jan. 28, 2019) and *Plaze v. Callas* (Feb. 28, 2019)—break no new legal ground, but serve as a salient reminder of a number of key points relating to forum selection clauses. In addition, *Sheldon* reinforces longstanding principles regarding the establishment of control groups. Finally, the court's opinion appears to reflect an attitude of general skepticism by the court of dilution claims by early-stage investors after a significant increase in a company's valuation.

Sheldon. In *Sheldon*, the court dismissed the plaintiffs' fiduciary claims against certain directors and officers of IDEV Technologies, Inc. that were based on the plaintiffs having suffered severe dilution of their interest in the company after it effected a financing in which the plaintiffs chose not to invest. The plaintiffs had brought the suit initially in a Texas court; and the Texas court enforced the Delaware forum selection clause in the parties' Shareholders Agreement. The claims were then filed in the Court of Chancery. The Court of Chancery subsequently dismissed the case on the basis that the claims were derivative in nature and that demand had not been made on the board.

The key ruling by the Court of Chancery was its rejection of the plaintiffs' argument that the defendants were estopped from arguing that the claims were derivative because the Texas court (when determining the enforceability of the Delaware forum clause for disputes "arising out of" the Shareholders Agreement) had determined that the underlying dispute between the parties had in fact arisen out of that agreement. The plaintiffs contended that, because that ruling indicated that the claims were contract-based rather than fiduciary-based, it was settled that they were direct and not derivative (and the plaintiffs could not take a contrary position in the Delaware litigation). The Court of Chancery, disagreeing with the plaintiffs' conclusion, reasoned that the Texas court's finding as to the contractual nature of the claims had been made for the "limited purpose" of determining the enforceability of the forum selection clause and not for determining whether the claims were direct or derivative. The Court of Chancery observed that the Texas court had not addressed and decided whether the claims were direct or derivative and, indeed, had characterized the claims as sounding in tort (not contract) which indicated that the Texas court actually had viewed the claims as derivative.

Plaze. In *Plaze*, the Court of Chancery held that a Delaware forum selection clause in a purchase agreement did not apply to certain parties because, as drafted, the clause applied to "the Parties" and that term as defined in the agreement did not include the parties at issue—even though those parties were signatories to and had obligations under the purchase agreement and the underlying dispute related to an ancillary lease agreement entered into contemporaneously with the purchase agreement. The court emphasized its deference to the precise drafting of the forum selection clause in determining who was covered by it.

Key Points

- **Most importantly, the decisions highlight the need for careful drafting of forum selection clauses.** *Sheldon* underscores the need for the drafting to be clear as to *what types of legal actions* are and are not covered by the clause (and to seek to avoid there being unanticipated adverse consequences that flow from adjudication of the issue of enforceability of the clause). *Plaze* obviously serves as a reminder of the need for the drafting to be clear as to *which parties* are and are not covered by the clause.

- ***Sheldon* underscores that a common investment history, alone, does not necessarily establish the existence of a control group.** The defendants owned, in the aggregate, 60% of the outstanding stock, had the right to appoint half or more of the board, had a history of investing together and had acted in concert to effect the financing that led to the dilution of the plaintiffs' interests. The court nonetheless rejected the plaintiffs' contention that the defendants constituted a control group and had caused the company to take the dilutive actions. The court focused on the facts that the defendants did not have a "long history of coordination and cooperation," had not been "intertwined, collaborative and exclusive" with one another, and had never identified themselves as a group.

- ***Sheldon* also highlights the vulnerability of early stage investors to subsequent dilution—and appears to reflect a general judicial skepticism of "after-the-fact" claims of unfair dilution** by shareholders who choose not to participate in a financing and, years later, following a substantial increase in value of the company, "try [through a claim of unfair dilution] to increase their share."

Background—*Sheldon*

The *Sheldon* plaintiffs ("JS" and "AK") obtained common and preferred stock in IDEV Technologies (a medical device manufacturer) soon after the company was created in 1999. JS was the founder and initial CEO; AK had invented technology that was licensed to IDEV and he had served over a long period as a consultant. Over several years, IDEV raised capital in several rounds to support its growth. In 2009, new management was installed and created a strategic plan to obtain long-term capital. In that connection, in early 2010, the company met with more than fifteen venture capital and strategic investors. The company selected a proposal for raising new capital from both new and existing investors (the "Financing").

In July 2010, IDEV implemented the first part of the plan to set the stage for the capital raise. At this time, the plaintiffs owned a total of less than 4% of the company's total outstanding stock. Some of the company's venture capital stockholders, who then owned over 60% of the outstanding stock (the "VC Defendants"), voted to (i) convert the company's preferred stock (the "Preferred Stock") into common stock, (ii) effect a 100 to 1 reverse stock split of the common shares, and (iii) authorize a new series of preferred stock (the "New Preferred Stock"). At the same time, the company and the VC Defendants amended the Shareholders Agreement to eliminate preemptive rights held by certain stockholders, including JS.

The company then implemented the second part of the plan, in which the new capital was raised. The company raised $27 million by issuing shares of New Preferred Stock to new and existing investors—including each of the VC Defendants and (apparently at the plaintiffs' choice) not including the plaintiffs. There was also an exchange offering in which previous holders of Preferred Stock could convert their common stock back into Preferred Stock so long as they also purchased shares of New Preferred Stock (which the plaintiffs did not do). The company's Information Statement warned stockholders that the Financing would result in significant dilution to the previous holders of Preferred Stock and that the dilution would be "significantly increased" as to those holders who did not participate in the Financing.

Thereafter, IDEV was acquired by Abbott Laboratories for over $310 million. In 2013, the plaintiffs sued the VC Defendants and members of IDEV's board of directors and management, alleging breaches of fiduciary duties, aiding and abetting of the breaches, and unfair enrichment by them in connection with the Financing. The plaintiffs alleged that, in the Abbott acquisition, they would have received almost $8 million and $4 million, respectively, if the Financing had not occurred; but, given the Financing, they would receive only about $15,000 and $7,500, respectively.

The plaintiffs brought their suit in Texas state court. The defendants (who were in Texas) sought to enforce the forum selection provision of the Shareholders Agreement, which required that "any dispute arising out of" the agreement be litigated in Delaware. Ultimately, the Texas Supreme Court ruled that the forum selection provision was applicable and Delaware jurisdiction was required. The plaintiffs complied and brought this litigation before the Court of Chancery. The defendants moved to dismiss on the basis that the primary fiduciary claims were derivative in nature, demand had not been made on the board, and the plaintiffs had not pled that demand would have been futile. The plaintiffs responded that the defendants were estopped from arguing that the claims were derivative because that argument was contrary to the Texas court's finding (in deciding on the enforceability of the forum selection clause) that the claims arose out of the Shareholders Agreement. That finding indicated that the claims were contractual in nature and so were direct claims, the plaintiffs asserted. Alternatively, they argued, under *Gentile v. Rosette* (Del. 2006), the claims were direct because, they alleged, the VC Defendants constituted a control group.

Vice Chancellor Morgan Zurn dismissed the case. She ruled that (i) the defendants were not estopped from arguing that the claim was derivative and (ii) *Gentile* did not apply because, based on the plaintiffs' allegations, it was not reasonably conceivable that the VC Defendants were a control group.

Discussion—*Sheldon*

The Texas court's finding that the forum selection provision was applicable was based on the specific drafting of the provision—specifically, the use of the word "dispute" rather than "claim." The Shareholders Agreement provided for exclusive Delaware jurisdiction for any "dispute arising out of" the Shareholders Agreement. The plaintiffs argued that their claims arose out of *fiduciary breaches* by the VC Defendants, the directors and management—rather than out of breaches of the Shareholders Agreement. The Texas court focused on the fact that the clause encompassed any "*dispute*" rather than any "*claim*." This distinction, the Texas court reasoned, meant that the coverage of the clause was "necessarily broader than claims based solely on rights originating exclusively from the contract." This "meant Plaintiffs' tort claims arose out of the Shareholders Agreement and Plaintiffs [therefore] needed to file in Delaware." In other words, the court interpreted the phrase "any dispute arising out of" the agreement to include disputes relating to fiduciary claims that flowed from breaches of the contract. The court's analysis should be kept in mind when drafting a forum selection clause (see Practice Points below).

The court's characterization of the claim as derivative determined the outcome. Generally, a claim is derivative if the harm was to the shareholders generally and is direct if the harm was specifically to the plaintiff-shareholders. Derivative claims belong to the corporation and generally will be dismissed if the plaintiffs did not make a demand on the board to bring litigation on behalf of the corporation (unless the plaintiffs establish that making the demand would have been futile). A breach of contract claim (which reflects a harm to the specific parties to the contract) generally would be direct in nature. Claims of unfair dilution of stockholdings (as were at issue in this case) classically would involve harm to the stockholders generally and so would be derivative in nature; however, under *Gentile v. Rosette* (Del. 2006), a dilution claim may also become a direct claim if a control stockholder or group caused the company to effect the dilution. In this case, the Court of Chancery held that the claims were not direct claims because the plaintiffs had not pled facts sufficient to support an inference that actions to improperly dilute the plaintiffs' ownership of shares were taken by a control group of stockholders (nor for an inference that the IDEV board lacked a disinterested and independent majority).

A non-Delaware court's decision that a Delaware forum selection clause is enforceable may estop the parties from making certain arguments in the litigation when brought in Delaware. A party cannot make an argument in the Delaware litigation that is contrary to arguments that it made in the non-Delaware litigation *which "persuaded" the non-Delaware court with respect to the holdings reached*. Thus, whether a party is estopped from making a particular argument by virtue of the non-Delaware court's decision will depend on a "careful and literal reading" of the decision, taking the context into account. In this case, the Vice Chancellor concluded that the Texas court's conclusion that the claim "arose out of" the Shareholders Agreement was made "for the limited purpose" of determining whether the Delaware forum selection clause in that agreement applied. Moreover, the Vice Chancellor observed, the Texas language used by the Texas court in its decision "painstakingly made clear [the Texas court's view] that Plaintiffs were asserting claims sounding in tort, not contract." The Vice Chancellor concluded that the Texas court had not determined that (nor even considered whether) the claims were direct or derivative. Therefore, she ruled, the defendants were not now estopped from arguing that the plaintiffs' claims were derivative. The Vice Chancellor cited as "the most helpful precedent" for its analysis the Court of Chancery's decision in *First Interstate Bancorp Litigation* (1998). In that case, the plaintiffs argued that the defendants could not contest whether the plaintiffs' claims were direct or derivative because the non-Delaware court had entered the parties' stipulation certifying a class. The Court of Chancery rejected that argument on the basis that the class certification order was not a determination that the claim was direct or derivative but "merely [had] determined a procedural issue."

A common investment history should not result in the court finding that a control group existed unless there are additional factors evidencing actual coordination. The plaintiffs argued that, under *Gentile*, the claims were direct claims because a control group had caused the company to effect the allegedly unfair dilution. The plaintiffs alleged that the VC Defendants were a control group at the time of the Financing because they: (i) collectively controlled over 60% of the then outstanding stock; (ii) were parties to an agreement that gave them the right to appoint three directors to the company's six-person board, with those three directors choosing an additional two (and the third being the CEO); (iii) had a "long and close relationship of investing together for their mutual benefit"; and (iv) acted in concert to effect the Financing (allegedly, "to extract economic benefit for their own selfish gain"). The court found that, based on the plaintiffs' allegations at the pleading stage, it was *not* reasonably conceivable that the VC Defendants constituted a control group, notwithstanding the "concurrence of their self-interest." The Vice Chancellor observed that a history of common investments can reflect simply that "venture capital firms in the same sector crossed paths in a few investments."

The court distinguished Hansen Medical, Inc. Stockholders Litigation *(2018) (where the court found that a control group existed)*. The court focused on the fact that the VC Defendants did not have the "long history of coordination and cooperation" of the control group members in *Hansen* and had not been as "intertwined, collaborative and exclusive" with one another. By contrast, the *Hansen* investors had worked together for over twenty years. In connection with the initial investment in *Hansen*, the investors had "entered into a voting agreement and declared themselves to the SEC as a 'group' of stockholders." They had coordinated their investment strategy in at least seven different companies. They were the only participants in the private placement that made them the company's largest stockholders. When the company in which they had invested was acquired, the acquiror identified the alleged control group members as "Key Stockholders" and entered into agreements that allowed them, and only them, to negotiate directly with the acquiror. These agreements also obligated them to vote in favor of the merger and permitted them to roll over their shares into equity of the acquiror while the minority stockholders received only cash. The *Hansen* court concluded that each of these factors alone, and "perhaps even less than all of them together," would be insufficient to successfully allege a control group—but that all of them, taken together and considered in light of the twenty-year "coordinated investment history," made it reasonably conceivable that they had functioned as a control group with respect to the merger.

In *Sheldon*, the court noted that, by contrast, (i) subsets of the alleged control group in IDEV had invested in four different companies but they had not all invested in any other company; (ii) other investors also had been involved in the Financing (and IDEV's previous financings); (iii) the investors were not contractually bound to pursue the Financing (as the Shareholders Agreement covered only their appointment of directors and otherwise they retained the right to vote their shares in their sole discretion); and (iv) there were seventy signatories to the Shareholders Agreement (and "no explanation for why the [VC] Defendants are members of an alleged control group while the numerous other signatories [were] not").

The court found this case similar to van der Fluit v. Yates *(2017) (where the court found that a control group did not exist).* In van der Fluit, the supposed members of the alleged control group were two of the company's founders, who were directors and owned a total of 30% of the company's stock; a venture capital investor who owned 16.7% and appointed one director; and another venture capital investor who owned 3%—so, a total of just under 50% of the stock, with the right to appoint three of the seven board seats. They were parties to an investor rights agreement that provided registration and informational rights to early investors, but no voting or decision-making agreement that related to the challenged transaction. The *Van der Fluit* court found that these entities were not a group and "simple appear[ed] to be "early venture capital investors selected by Plaintiff as an attempt to increase the stock ownership of the purported group." The Vice Chancellor wrote in *Sheldon*: "The same is true here for the [VC] Defendants as bound by the Shareholders Agreement, which in no way related to the Financing." She noted also that, although the issue whether a control exists is facts-intensive, it can be decided at the motion to dismiss stage when, as in *Van der Fluit* and here, the plaintiffs have not pled facts that make the conclusion reasonably conceivable.

Early-stage investors can be vulnerable to later severe dilution—and the court may be skeptical of "after-the-fact" claims of unfair dilution. *Sheldon* highlights the potential for severe (possibly unanticipated) dilution in venture capital and private equity situations. In *Sheldon*, it appears that at least one of the two plaintiff-investors initially had preemptive rights, but that the Shareholders Agreement was amendable by a 60% majority of the outstanding shares and the preemptive rights were in fact eliminated by amendment prior to the Financing. A stockholder obviously is not protected by contractual provisions that can be amended by other stockholders without that stockholder's consent. (It also appears from the court's description of the background facts that, irrespective of the preemptive rights, the plaintiff-investors were free to participate in the financing round that resulted in their dilution if they had wanted to, but chose not to.)

The *Sheldon* opinion appears to reflect a general skepticism by the court when early-stage investors, years after their investment and following a significant increase in the company's value, claim that their interests were unfairly diluted (and particularly so, of course, where, as here, they plaintiffs apparently had the opportunity to participate in the dilutive financing but chose not to). The court characterized the lawsuit as an attempt by the plaintiffs (after the $300 million sale of the company in which they were severely diluted) "to increase their share by suing." Also, the court observed that "IDEV's success [in connection with the sale] was bitter for Plaintiffs because the Financing had diluted their previously significant holdings." Further, the court noted that the plaintiffs "chose not to seek a contractual remedy for violation of the preemptive right or the anti-dilution provisions of the shareholders agreements, which contained a Delaware forum selection clause."

Background—*Plaze*

Like *Sheldon*, the *Plaze* decision also featured a focus on drafting issues relating a Delaware forum selection clause. The factual background was as follows: Plaze Inc. purchased Apollo Industries, a Georgia-based business, from three parties (the "Callases") pursuant to a stock purchase agreement (the "SPA"). Three Apollo production facilities were not acquired and, instead, Plaze and Apollo leased those facilities from Callas-affiliated entities (the "RE Holdcos") pursuant to lease agreements (the "Leases"). After a few years, the RE Holdcos sued Plaze and Apollo in Georgia state court alleging violations by them relating to the leased facilities. In response, Plaze and Apollo filed this action seeking a preliminary injunction of the Georgia suit, arguing that the SPA's Delaware forum selection clause, which covered any claims "arising out of or relating to the sale," applied to the RE Holdcos. Vice Chancellor Montgomery-Reeves held that the forum selection clause, as drafted, did not apply to the RE Holdcos and she granted the injunction.

Discussion—*Plaze*

The court relied on the precise drafting of the forum selection clause to determine who was covered by it. The forum selection clause in the SPA stated that it applied to "the Parties." The SPA defined a "Party" as "each of Buyer, the Company, the Administrator and each Seller." The court wrote: "It does not name the RE Holdcos as Parties, despite their status as signatories and despite imposing other obligations on them." Moreover, the court stated, the forum selection clause "uses the term Parties three times, evidencing an intent"; "this intent is consistent with the overall contractual scheme, which limits the RE Holdcos obligations"; and this intent is "also consistent with the language in the Leases suggesting an expectation to litigate disputes related to the Leases in Georgia." The court rejected the plaintiffs' argument that it would be "absurd and unfair" to require the plaintiffs to litigate claims arising from the SPA in Delaware while not holding the RE Holdcos to the same requirement. The court reasoned that the parties were free to contract for the clause to apply to whomever they chose and they did so. The court also rejected the plaintiffs' argument that the SPA and the Leases should be "read together" as a "single agreement." "[T]he single agreement theory does not apply to bind a party to a provision it never agreed to," the court wrote. The court also observed that no public policy reasons favor litigating a Georgia property dispute in Delaware (and, in fact, that Georgia courts are best positioned to apply Georgia law to injuries related to Georgia property).

Practice Points

- **Drafting a forum selection clause—Use of the word "dispute" vs. "claim."** As highlighted in *Sheldon* and *Plaze*, a forum selection clause should be drafted clearly with respect to which types of actions and which parties are subject to the clause. A party that seeks to include a forum selection clause in an agreement typically will want the clause to cover, as clearly as possible, *all* potential litigation. Of note, *Sheldon* indicates that the court may view a clause that provides that it covers any "*dispute*" arising out of an agreement as providing broader coverage than a clause that provides that it covers any "*claim*" arising out of the agreement. Thus, the word "dispute" should be used—preferably, with other language that further clarifies the parties' intent with respect to the breadth of litigation that will be subject to the clause.

- **Judicial estoppel—Arguments made when adjudicating the enforceability of a forum selection clause.** As illustrated by *Sheldon*, litigants should keep in mind the potential for a court's adjudication of the enforceability of a forum selection clause to estop a party from making contrary arguments in future proceedings if and when the litigation moves to Delaware. Judicial estoppel applies in Delaware when (i) a litigant advances a position that is inconsistent with a position the litigant took in the same or earlier legal proceeding and (ii) the court "was persuaded to accept the previous argument as a basis for its earlier ruling." A determination as to whether the court was "persuaded" in this way requires a "careful and literal reading [by the court] of the arguments and decision in the earlier matter." Thus, for example, a plaintiff's argument that the defendant is estopped from contending that claims are derivative (and therefore must be dismissed unless demand was made) would be undermined to the extent that the court in the prior enforceability proceeding may have characterized the claims as sounding in tort rather than contract.

- **No tolling of the statute of limitations.** The Delaware statute of limitations is not tolled pending an adjudication of the enforceability of a forum selection clause. In *Sheldon*, the court noted that the defendants in *Huffington v. T.C. Group* (Del. Sup. Ct. 2012) had persuaded a Massachusetts court to enforce a Delaware forum selection clause and, when the case was later filed in Delaware Superior Court, the defendants moved to dismiss on the basis that the Delaware statute of limitations had expired. The plaintiff argued that by persuading the Massachusetts court that the plaintiff could sue in Delaware and that Delaware would properly apply Massachusetts law, the defendants had implied to the Massachusetts court that the claims were not time-barred. The Delaware court rejected the plaintiff's argument on the basis that nothing in the Massachusetts court's decision addressed the statute of limitations—which (the Vice Chancellor observed in *Sheldon*) was appropriate given that the Delaware statute of limitations had "nothing to do with" the issue before the Massachusetts court, which was the enforceability of the forum selection clause. In this connection, it is possible that parties to a shareholders agreement containing an exclusive forum selection clause might seek to have the company agree to a tolling of any statute of limitations during the pendency of an action determining the enforceability of the clause.

- **Appropriate shareholder protections in shareholder agreements.** As illustrated by *Sheldon*, careful attention is required with respect to the drafting of and interrelationships among various provisions in shareholders agreements, including rights with respect to the dilution of shares, conversion of shares, participation in future financings, election of directors, and, perhaps most importantly, amendment of the agreement. Early stockholders' anti-dilution and related rights will depend primarily on the parties' respective negotiating leverage, the company's anticipated need for additional subsequent capital, and then-prevalent market terms with respect to anti-dilution. In addition to these basic business factors, relatively weak anti-dilution protection for early investors frequently can result from (i) faulty assumptions that the friendly and collaborative relations among the founders or original investors will provide protection down the road, and/or (ii) in the case of small startup ventures, a general lack of attention paid to legal formalities and the details of corporate agreements.

Another Reminder that Buyers Generally Do Not Have An Obligation to Seek to Maximize Earnout Payments — Glidepath v. Beumer

Earnouts, while often used to bridge valuation differences between parties to an agreement to acquire a private company, frequently lead to post-closing disputes. A common dispute relates to a seller's contentions that, during the earnout period, the buyer did not take appropriate actions to support the realization and maximization of the earnout. The courts have consistently endorsed a very limited approach to application of the implied covenant of good faith and fair dealing (which adheres to every contract), and have found that a buyer did not meet its obligations only when the buyer did not satisfy its express contractual commitments or acted purposefully to frustrate realization of the earnout (such as by artificially moving revenues to a period outside the earnout period).

In *Glidepath Limited v. Beumer Corporation* (Feb. 21, 2019), the Court of Chancery recently reaffirmed that, during an earnout period, a buyer has no obligation to seek to maximize the amount of earnout consideration that will be triggered (absent an express contractual commitment to the contrary). In *Glidepath*, the Beumer Corporation (the "Buyer") first acquired 60% of the membership interests in and took control of management of *Glidepath*. After a few years of shared ownership, the Buyer called the remaining 40% interest (pursuant to a reciprocal put-call provision that permitted Glidepath to put or Beumer to call the remaining interest). Most of the purchase price took the form of contingent payments based on the company's performance over a three-year period. The plaintiff-seller brought suit when the company's performance did not warrant any contingent payment.

The plaintiff claimed that the Buyer and the two individual defendants had breached terms of the acquisition agreement, the implied covenant of good faith, and their fiduciary duties, each of which (alone) warranted damages equal to the full contingent consideration amount. The court found that there were breaches of the agreement but rejected the theory that the contingent payment amount constituted the appropriate damages and awarded modest damages for breaches. The court acknowledged that the Buyer had fiduciary duties to the company and its members and agreed with the plaintiff that, during the earnout period, the Buyer had a conflict of interest given its earnout obligation (which meant that its actions, if challenged, would be reviewed under the entire fairness standard). However, the court stated, a buyer's fiduciary duties are to seek to maximize the *long-term value* of the company (rather than the value of the earnout assets). In this case, the court found, the Buyer established that that was its motivation and, indeed, the effect of its actions. The Buyer's fiduciary duties "did not include any obligation to ensure that the plaintiffs received the contingent consideration," the court wrote.

The parties' operating agreement called for the Buyer to "support the Company with the realization of the [mutually agreed] Business Plan by way of its bonding line." The plaintiff's complaint was based on the Buyer (i) having changed the company's strategy to focus on bigger, higher-margin projects rather than following the company's traditional course and (ii) not having provided the company with the benefit of the buyer's bonding line so that the company could have bid for more projects. Numerous problems developed with respect to the new strategy during the earnout period, with essentially none of the company's bids being successful. Then, just after the end of the earnout period, two projects which had floundered during the earnout period became successful (either one of which, if it had been successful during the earnout period, would have triggered the maximum contingent payment).

The court found that the parties' agreement specifically authorized the Buyer to determine the strategy to achieve the Business Plan. The court noted that the Manager was obligated to update the Business Plan each year; and, indeed, that the sellers knew during the sale process that the Buyer intended to shift the strategy as they ultimately did. The court found that the projects' success falling outside the earnout period was "due to events beyond the parties' control." Further, the court found, the Buyer did not have its own bonding line until well into the earnout period. Prior to that, it had obtained bonds through its parent company. However, the court emphasized that the agreement did not obligate the Buyer's *parent* to provide bonding nor obligate the Buyer to cause its parent to provide bonding. The court noted that the Buyer did try to obtain bonding from its parent at times, that the parent had provided bonding on some occasions, and that there were "legitimate reasons" for the Buyer not providing bonding when it did not.

Statistics on Earnouts. Based on the last statistics available (in the 2017 ABA Private Target Study), earnouts were utilized in about 28% of the U.S. private target transactions with purchase prices between $30 million and $500 million. This rate is consistent with the rate generally over the past decade, which has ranged from 20-30% (with a spike to 38% in 2014). With respect to these agreements:

- 21% included an express covenant requiring the buyer to run the business consistent with past practice, and 33% expressly permitted the buyer to operate post-closing in its discretion;
- 8% included an express covenant requiring the buyer to seek to maximize the earnout;
- 5% included an express acceleration of the earnout payment(s) on a change of control (in recent prior years, 11-27% of agreements with earnouts included this type of acceleration);
- 51% expressly permitted the buyer to offset indemnity payments against the earnout (in recent prior years, 58-81% of agreements with earnouts expressly permitted offsets); and
- 32% provided for calculation of the earnout based on revenues, 27% based on earnings/EBITDA, and none based on a combination of revenues and earnings.

Practice Points. The key practice point arising from *Glidepath* is that, if a seller anticipates that the support of a buyer's parent, subsidiary or other affiliate will be required during the earnout period, that support should be specified in the purchase agreement covenants (rather than assuming that the buyer will choose to seek the support from its affiliate). Also, **see our Briefing**, *Earnout Period Pitfalls* (Sept. 4, 2018), in which we provide extensive practice points relating to earnouts generally (and discuss an earlier ruling in *Glidepath* where the court rejected the plaintiffs' request for reformation of the acquisition agreement to change the dates of the earnout period based on a delay in signing and closing the agreement (which had led to the anomalous result of the earnout period commencing *before* the closing)).

In Its Most Recent Appraisal Decision (Involving an Unusual Factual Context), the Court of Chancery Relies on DCF and the Result is Close to the Valuation Suggested by Market-Based Data—Trussway

In its seminal 2017 *DFC Global* and *Dell* decisions, the Delaware Supreme Court held that, in an appraisal case following a merger that was negotiated at arm's-length in a robust sale process, the Court of Chancery should rely solely or primarily on the deal price itself to determine appraised "fair value." The practical result of this approach is that there would be no benefit from seeking appraisal in this context of an arm's-length merger. Since *DFC Global* and *Dell*, in certain contexts, the Court of Chancery has sometimes relied solely or primarily on the DCF methodology (rather than a deal price or other market-based data) to determine fair value even in cases arguably involving an arm's-length merger or where there is relevant market-based data available. However, the court's appraisal results in these cases—*whether* relying primarily on the merger price *<u>or</u>* the DCF methodology—have tended to be close to or below the merger price. These results, as would be expected, have had a chilling effect on the filing of appraisal claims. The number of appraisal claims filed in Delaware, which had increased steadily from 2009 through 2016, decreased from a peak of 76 petitions filed in 2016 to only 26 filed in 2018.

Silver Spur Capital Partners v. Trussway Holdings LLC (Feb. 28, 2019) **is another case (albeit involving an unusual factual context) in which the court determined that the available market-based data was not reliable and relied instead on the DCF methodology—and reached a DCF result that in fact was close to the valuation suggested by market-based data (in contrast to the court's DCF results in past years which typically exceeded the merger price).**

The primary relevance of reliance on the DCF methodology is that the appraisal result is less certain. Not only is a DCF result the product of various subjective inputs, but small changes in one or more of the inputs can significantly affect the analysis. Accordingly, to the extent that the court may rely on the DCF methodology rather than the merger price, there is an incentive to file appraisal claims because there is a potential that the appraisal result may be higher (possibly significantly higher) than the merger price.

Notably, in cases involving arm's-length mergers where the court has relied on the merger price, the results post-*Dell *have been sometimes at the merger price, but also sometimes have been below (even well below) the merger price. This result has been the product of a new emphasis by the court on the statutory requirement that appraised fair value must exclude any value arising from the merger itself (*i.e.*, the value of anticipated merger synergies—which value is by definition included in the merger price). Also of note is that, post-*Dell*, in cases involving arguably arm's-length mergers where the court has relied on the DCF methodology, the court's recent results also have been close to or below the merger price.

In* Trussway*, the court relied on the DCF methodology, as it viewed the market-based data from the company's extensive sale process as "too preliminary" to be reliable. *Trussway* involved an unusual factual context. The merger at issue (the "Merger") was effected in order to convert the corporation, Trussway Holdings Inc. (the leading manufacturer of pre-made steel trusses for the multi-family housing industry), to a limited liability company. Thus, there was no merger price, just an exchange of each common share for an LLC unit. Although the Merger was effected by the 95% stockholder-controller of Trussway, prior to and for a time following the conversion Merger Trussway was simultaneously engaged in an extensive sale process. Trussway Holdings had engaged a banker in July 2016 to conduct a sale process for its main asset (its wholly-owned subsidiary, "TII"). The banker contacted 76 parties, 27 of whom executed nondisclosure agreements and received confidential information presentations. The seven parties that submitted expressions of interest by the November 2016 deadline then received further information, including the management's projections (the "Projections"). In early December 2016, while the sale process was "ongoing," Trussway effected the Merger. Apparently there were no further efforts made thereafter to sell the company. In February 2017, Trussway received one definitive offer (the "Offer"), although the Offer was withdrawn four days after it was made. The banker's engagement ended in March 2017.

Trussway's two minority stockholders dissented from the Merger and sought appraisal of their shares. The Court of Chancery viewed the indications of interest and the Offer received in the sale process as too "preliminary" to be reliable in determining appraised fair value—because the Offer had been withdrawn and apparently the sale process was not further pursued after the Merger. Therefore, as there was no merger price in the Merger and only "preliminary" market-based data was available from the sale process, the court decided to rely solely on the DCF methodology, while stating that the Offer price could be "useful only as a very rough reasonableness check" on the court's DCF result.

However, the court's DCF result was close to the valuation suggested by the market-based data. The valuation range that Trussway's banker had established for it in connection with the sale process was about $200-300 million. The third-party arm's-length Offer that was made and then withdrawn was for $170 million—which, one might argue, suggested that the company's value was equal to or (more likely) *below* $170 million. The court's DCF result was $180 million—that is, reasonably close to the Offer price (and much lower than the banker's valuation). The case thus underscores the diminishing incidence—whether the court relies on the merger price or even on a DCF analysis—of appraisal results that are significantly above a deal price or other market-based valuation data.

In this case, the appraisal result (which was only slightly higher than the respondent company's proposed result) likely reflected in part the unusual factual context. The challenged merger, although it involved a controller, did *not* involve a cashing-out or other termination of the investment as in the typical case of a merger with a third party. In this case, the merger did not effect a sale of the company but a change in corporate form—and the minority investors would have retained the same interest in the same company, presumably with the same (limited) rights. The result may also reflect the influence of market-based data even when the court purports not to rely on it.

The parties' and the court's valuations. The petitioner contended that Trussway's fair value was $387.82 per share. The respondent company contended that it was $225.92 per share. Vice Chancellor Glasscock determined it to be $236.52 per share—which reflected a value for TII of $183.3 million (and, given that Trussway's other assets and liabilities reflected net liabilities, a value for Trussway of $143.3 million).

- ***The petitioner.*** The petitioner's expert relied (a) 60% on a DCF analysis that utilized the Projections, with a 1% discount applied to the Projections to reflect the uncertainties discussed above; (b) 30% on a comparable companies analysis; and (c) 10% on a precedent transactions analysis.

- ***The respondent.*** The respondent's (Trussway's) expert relied (a) 25% on a DCF analysis that utilized the Projections and, (b) to reflect the uncertainties with respect to the Projections discussed above, relied 75% on a DCF analysis that utilized projections that "manipulated" the Projections to cover only a five-year timeframe (the "Manipulated Projections").

- ***The court.*** First, with respect to the petitioner's approach, the court rejected the 1% discount to the Projections as arbitrary. "[T]he record…does not demonstrate why this particular adjustment is appropriate," the court wrote. Second, the court rejected the comparable companies analysis because the sixteen guideline companies were not sufficiently comparable (given Trussway's "unique" focus on the multi-family housing market). Finally, the court rejected the precedent transaction analysis because it included only one precedent transaction. The court decided to conduct two DCF analyses—the first of which utilized the Projections and the second of which utilized the Manipulated Projections, with each accorded a 50% weighting. This approach largely mirrored the respondent's approach, but the court increased—to 50% (from 25%)—the weighting accorded to the DCF analysis based on the Projections. The value of TII under the court's first DCF was $197.8 million, and under the second DCF was $168.8 million, with an average of the two (based on the 50-50 weighting) of $183.3 million. (Adding this value to Trussway's other stipulated assets and liabilities resulted in a value for Trussway of $143.3 million.)

The following factors relating to the court's DCF analysis should be noted:

- ***Projections time period***. The decision indicates that a long timeframe for projections, while potentially justifiable for a cyclical business, may nonetheless provoke judicial skepticism. In its DCF analysis, the court relied 50% on a DCF that utilized the Management Projections (which were nine-year projections) and, due to the considerable uncertainties inherent in those projections given the lengthy period covered, relied 50% on an alternate DCF that utilized projections that were derived from a "manipulation" of the Management Projections to reduce the time period covered to five years. The court acknowledged that long-term projections are appropriate to smooth out distortions when a company operates in a cyclical industry (as Trussway did), and concluded that the Management Projections indeed constituted the "best estimate" of the company's future performance. However, at the same time, the court expressed strong skepticism about predictions of corporate performance nine years out and rejected sole reliance on the Management Projections in its DCF analysis.

- ***Additional skepticism about the projections***. Notably, the court's skepticism about the lengthy time period covered apparently was augmented by other factors—*i.e*., the inclusion in the projections of significant "strategic initiatives" the implementation of which had not yet commenced; and the facts that management had prepared the projections in part for the sale process, that the projections were more optimistic than the management's prior internal projections, and that the projections had been downgraded during the sale process because the company's performance was not matching what had been anticipated.

- ***Strategic initiatives not yet commenced.*** The court viewed "strategic initiatives" that the company had planned and budgeted, but had not yet commenced, as part of the company's pre-merger "operative reality" that would be included in appraised fair value. The initiatives, which accounted for 43% of EBITDA at the end of the projections period, were within the company's "unilateral control," the court stated. The court distinguished an acquisition whose closing is "far off—which would *not* be part of a company's pre-merger operative reality (apparently because the acquisition would not be in the company's unilateral control).

Practice Points

- **As discussed, there is now a greater risk than in the past of appraisal results being close to or below (even significantly below) the merger price—particularly in cases in which the court relies on the merger price but even in cases where the court relies on the DCF methodology.**

- **A petitioner may argue that the court should consider planned "strategic initiatives" to be part of the company's pre-merger "operative reality" even if the initiatives have not yet commenced.** Note that in previous cases the court has stated that an acquisition that "is far from being completed" is not part of the pre-merger operative reality. In *Trussway*, the court distinguished the company's strategic initiatives (involving building a plant and expanding into new product, segment and geographic markets) on the basis that the initiatives had been "planned and budgeted" and were within the company's "unilateral control."

- **A company should be mindful that a lengthy timeframe on projections can provoke judicial skepticism.** In *Trussway*, the court rejected the approach of an “arbitrary” 1% discount to the projections to reflect the inherent uncertainties. The court preferred instead the approach of utilizing a blend of management’s long-term (nine-year) projections and alternate shorter-term projections. The court may have been far less skeptical of the projections if they had not included strategic initiatives that had not yet been commenced, had not been prepared in connection with the sale process, and had not already been downgraded due to the company’s actual performance.

See our Briefing, *The Most Recent Appraisal Decisions (One Above, and One Below, the Deal Price) Should Further Discourage Appraisal Claims in Arm’s-Length Merger Cases*—Norcraft *and* Solera (Aug, 14, 2018).

M&A/PE and Governance Update

Court of Chancery Enjoins a Controller-Led Merger Pending Corrective Disclosures—*FrontFour v. Medley Capital*

In *FrontFour Capital Group, LLC et al v. Brooke Taube et al [Medley Capital]* (March 11, 2019), the court determined that, based on the precedent set in the Delaware Supreme Court’s 2014 *C&J Energy* decision, it could order only a disclosure remedy and not more substantive relief (such as ordering that the company be shopped) in the context of what it viewed as a controller-led merger of three affiliated entities in a “deeply flawed” sale process. The judicial outcome turned on the court’s finding that the plaintiff had not proved (indeed, had offered no evidence whatsoever to prove) that the acquiring entity had aided and abetted what the court viewed as fiduciary breaches by the target company’s board. Vice Chancellor McCormick indicated that if the plaintiff *had* proved the aiding and abetting claim, then *C&J* would not have precluded the court from ordering a “curative shopping process.” The decision may be expected to encourage plaintiffs to make (and try hard to substantiate) aiding and abetting claims to avoid this application of *C&J*.

Financial Advisor and Legal Counsel are Sued for Aiding and Abetting a Target Board’s Alleged Fiduciary Breaches—*Morrison v. Berry*

In this longstanding litigation regarding a take-private transaction, the plaintiff, after document discovery, filed an Amended Complaint (made public on March 14, 2019) that added as defendants the target board’s highly regarded outside financial advisor and legal counsel. The plaintiff claimed that the advisors aided and abetted the target board’s alleged fiduciary breaches in connection with the sale process.

Vice Chancellor Laster Asserts Delaware Jurisdiction Based on Directors’ “Sufficient Involvement” in a Merger—and Suggests a New Framework for Analysis in Controller Cases, With Deference to “Enhanced-Independence Directors”—*Pilgrim Pride*

In *In re Pilgrim’s Pride Corp. Deriv. Litig.* (March 15, 2019), the Court of Chancery rejected the defendants’ motion to dismiss the derivative suit by minority stockholders against the parent company-controller of Pilgrim’s Pride Corp. (JBS, S.A., a company organized under the laws of Brazil). The suit challenged Pilgrim’s 2017 $1.3 billion acquisition of Moy Park, Ltd., which was owned by JBS. The court disagreed with the plaintiffs’ argument that certain Pilgrim directors (all of whom were also executive officers of JBS or its controlled subsidiaries) had not been sufficiently involved in the transaction to be subjected to Delaware jurisdiction. These directors argued that a special committee had been appointed to act with respect to the merger and these directors had only voted on the merger to avoid the triggering of a covenant in the company’s debt. According to the court, however, two of these directors actually had been involved in the deal talks. As to the other three directors, the court stated that their only having approved the board resolution approving the deal was a “slim reed” on which to base jurisdiction, but that, at the pleading stage, it constituted “sufficient involvement by conflicted fiduciaries in the effectuation of a self-dealing transaction” to warrant denying their motion to dismiss. The court also asserted jurisdiction over JBS, which had argued that its only contact with Delaware was its ownership of Pilgrim. The court found that Delaware had jurisdiction over the claims against JBS under a Delaware forum selection bylaw adopted by the Pilgrim board. The court noted that JBS had appointed and exercised control over a majority of the directors on the Pilgrim board and that the board had adopted the forum selection bylaw the same day that it approved the Moy Park transaction.

An interesting aspect of the decision is that Vice Chancellor Laster, citing a recent article by Professors Lucien Bebchuk and Assaf Hamdani, proposed a possible new framework for evaluating claims in conflicted controller transactions. While a challenged conflicted controller transaction currently is evaluated under the stringent “entire fairness” standard, the Vice Chancellor suggested that perhaps it should be evaluated under the deferential business judgment standard when, as in *Pilgrim Pride*, under the company’s corporate governance system, the minority stockholders have the power to elect directors and those directors comprise a majority of the special committee that approved the transaction. This framework would provide another path to business judgement review for controller transactions (in addition to the existing *MFW* framework, which requires that a transaction was, from the outset, conditioned on approval by both an independent special committee and a majority of the minority stockholders). Vice Chancellor Laster observed that, while the *MFW* framework “works well for major transactions like squeeze-out mergers, its significant requirements undermine its utility for other types of interested transactions involving a controller.”

The Vice Chancellor explained in the opinion that, based on his knowledge of the Bebchuk-Hamdani article, he had raised *sua sponte* with the parties in *Pilgrim Pride* whether the suggested approach (which he characterized as the “enhanced independence approach”) should apply in this case and he had asked the parties to provide supplemental briefs on the issue. In their supplemental brief, the plaintiffs “identified a series of questions of first impression that this court would have to confront, as well as tensions with other areas of Delaware law, and argued that the standard should be applied only in a case where the defendants specifically rely on it and provide the court with full briefing on the subject.” The Vice Chancellor agreed that “the current record” in this case did not provide “an adequate basis for assessing the many questions of first impression raised by the enhanced independence approach” (such as whether the “enhanced- independence directors” would in fact be free of the controller’s “influence”). He “therefore [did] not consider th[e] approach any further.”

Due to the Vice Chancellor’s discussion of the proposed approach over two full pages in the body of his opinion, controllers in some cases may consider having a governance system under which some directors are elected by the minority stockholders, with those directors constituting a majority of the special committee evaluating (specific, or all) conflicted transactions between the controller and the company. We note that controlled companies’ implementing a structure that would permit application of Laster’s suggested standard would be a significant new development. A controller would want to weigh the advantages of obtaining the business judgment safe harbor against the disadvantages of minority-stockholder elected directors controlling the approval process for affiliated transactions.

Delaware Supreme Court Affirms a Dismissal of Claims for Misuse of Trade Secrets by a PE Owner—*Alarm.com*

In *Alarm.com v. ABS Capital Partners* (Feb. 7, 2019), the Delaware Supreme Court upheld a Court of Chancery (June 2018) decision dismissing claims by Alarm.com Inc. that private equity firm ABS Capital Partners, a major investor in Alarm.com with designees on its board, had misused and misappropriated Alarm.com’s trade secrets after ABS invested in and joined the board of an Alarm.com competitor. Alarm.com had unsuccessfully sought an injunction to bar ABS from investing in two companies—a startup that was a direct competitor and an industry supplier. The investments occurred about a year after the general partner of ABS left his longtime position as Chairman of Alarm.com’s board and the ABS managing partner (who never had served on the alarm.com board) joined the board of the competitor. The Court of Chancery emphasized that unrelated corporate agreements between Alarm.com and ABS made clear that Alarm.com had not negotiated for non-competition commitments from ABS (indeed, the agreements suggested that competition was permitted). The Supreme Court panel emphasized that Alarm.com had advanced a theory of “inevitable use” of trade secrets rather than specific allegations of any actual use. Chief Justice Strine suggested that Alarm.com was “just…upset that [ABS is] a prior private equity sponsor who [Alarm.com] agreed could go into a competing business, and did.”

Court of Chancery Finds an Officer-Founder Who Bought a Building Next to the Company's Offices Had Usurped the Company's Corporate Opportunity to Buy It for Expansion Purposes —*Personal Touch*

In *Personal Touch v. Glaubach* (Feb. 25. 2019), the Court of Chancery held that EG, the founder and President of Personal Touch Inc. (a closely held corporation engaged in providing home healthcare services), usurped a corporate opportunity when he personally acquired a building next door to the company's offices in Jamaica, Queens and then rented the building to the company. The company had been wanting to acquire the building to expand its space. Two months after EG acquired the building, the company terminated his employment for that and other reasons. The company then brought suit seeking (i) a declaratory judgment that the termination of EG's employment was valid under his employment agreement and (ii) damages for alleged breaches by EG of his fiduciary duties, including a usurpation of corporate opportunity by his acquiring the building. The suit involved, in the court's words, a "wide-ranging mishmash of issues" relating to cross-allegations of illegality, self-dealing and harassment in the running of Personal Touch.

The court held that EG had usurped a corporate opportunity. By hiding his actions from the company and putting his personal interests ahead of the company's corporate interests, he had intentionally breached the duty of loyalty, the court held. The court awarded the company damages of $2,735,000 (which represented the difference between the building's market value at the time of the trial and the price that EG had paid for it). The court also granted the company a declaration that its terminating EG was valid under his employment agreement, which provided for termination in the event of EG's "willful misconduct." The court stated that the usurpation of corporate opportunity constituted "willful misconduct," "material dishonesty" and a "material breach of trust" under the agreement.

The key part of Chancellor Bouchard's decision is his clarification that the four-part analysis set forth in *Broz*—the critical case in determining whether there has been a usurpation of corporate opportunity—is to be conducted with each of the factors "weighed…on a holistic basis." The court emphasized that the analysis is not to be "technical" or "narrow" but, rather, is to be based on "broad considerations of corporate duty and loyalty," with "a balancing of the equities of [the] individual case."

In *Broz* (1996), the Delaware Supreme Court, relying on its seminal *Goth v. Loft* decision (1939), articulated that a corporate director or officer may not take a business opportunity for his or her own if (i) the corporation is financially able to exploit the opportunity; (ii) the opportunity is within the corporation's line of business; (iii) the corporation has an interest or expectancy in the opportunity; and (iv) by taking the opportunity for his or her own, the corporate fiduciary will thereby be placed in a position inimical to his or her duties to the corporation. The court wrote that, although the *Broz* test is stated "in the conjunctive," *Broz* and later cases emphasize that the test involves a *weighing* of the four factors, "with no one factor [being] dispositive and all [of the] factors [being] taken into account insofar as they are applicable."

The court found, first, that the record established that the company had been "keenly interested in, and had a reasonable expectation of" acquiring the building right up through the time that EG acquired it and was financially able to do so. Second, the court rejected EG's contention that, because the company was a home healthcare business, not a commercial real estate venture, acquisition of the building was not within the company's line of business. The court stated that the line of business inquiry is to be applied "flexibly" such that an opportunity to acquire a building with a highly desirable location that could be used to expand operations is an opportunity that "fits within the Company's existing line of business." An "equally sensible" view, the court wrote, would be to view the line of business factor as "simply not relevant" in a case where, as here, the company had "a clear interest and expectancy" in acquiring the building and "the opportunity presented concern[ed] an operational decision about how to manage or expand [the] existing business." Finally, the court found that taking the opportunity to buy the building placed EG in a position "inimical to his duties"—that is, his taking the opportunity resulted in a conflict between his fiduciary duties to the corporation and his own self-interest "as actualized by the exploitation of the opportunity." The court observed that EG knew of the unique value of the building to the company given its location, knew of the company's interest in and expectancy of acquiring the building, concealed his activities with respect to the building from the company until after he had closed the deal, and sought to lease the building to the company almost immediately after he acquired it.

Delaware Supreme Court Upholds the Non-Dismissal of Claims Against a Controller for Self-Dealing—*Straight Path*

The Delaware Supreme Court, in a one-page order (issued Feb. 22, 2019), upheld the Court of Chancery decision that allows a suit by two minority investors in Straight Path Communications Inc. against the controlling stockholder to proceed. The plaintiff-stockholders alleged that HJ, the controller of Straight Path's controlling stockholder IDT Corp., had secured personal benefits for himself in the $3.1 billion merger between Straight Path and Verizon. In 2013, IDT had spun Straight Path off and IDT agreed to indemnify the spun-off entity for any regulatory liabilities arising from conduct that occurred prior to the spinoff. Subsequently, an FCC investigation resulted in a $614 million penalty relating to pre-spinoff fraudulent reporting activities (and thus the fine would have been covered by the indemnification agreement). The minority investors filed suit in July 2017, alleging that HJ had exerted his control over both IDT and Straight Path to avoid the indemnification by refusing to approve any merger that would have included a sale of the claim. Instead, at the same time as the $3.1 billion sale of Straight Path to Verizon in May 2017, Straight Path, had settled the $614 million claim by accepting $10 million from IDT and selling its intellectual property to HJ for $6 million. In June 2018, Vice Chancellor Glasscock refused to dismiss the plaintiffs' claims, finding that they had adequately pled that they were harmed by the settlement with IDT when they could have retained the indemnification claim as part of a litigation trust that would have survived the Verizon deal. The Supreme Court upheld that decision, rejecting IDT counsel's contentions during oral argument that the claims against HJ, to the extent valid at all, were derivative and therefore belonged to Straight Path and could not be asserted directly by the minority investors.

Board Diversity Is Expected To Be a Focus in the 2019 Proxy Season

It is expected that gender and racial diversity issues will play a key role in the 2019 proxy season. Proxy advisor Glass Lewis announced in late 2018 that, for meetings held after January 1, 2019, Glass Lewis will generally recommend voting against the nominating committee chair of a board that has no female members. Glass Lewis may extend this recommendation to vote against other nominating committee members depending on several factors, including the company's size, industry and governance profile. Glass Lewis's new policy does not necessarily apply to companies outside the Russell 3000 index or those that have provided a robust explanation for not having any female board members.

Other developments on diversity. In this connection, California recently required that publicly held companies based in California have at least one female director by the end of 2019 (and, depending on the size of the board, additional female directors by the end of 2021). Bills are being introduced in New York and New Jersey that would require companies to disclose data on dive. In addition, institutional investors including State Street, CalPERS and BlackRock, have made public demands for greater gender diversity on boards. The Spencer Stuart Board Index, an annual survey on board composition at S&P 500 companies, reported that, in 2018, 40% of new board seats went to female directors; and women now represent 24% of all S&P 500 directors (up from 16% in 2008). Minority men represented only 10% of new board seats in 2018 (down from 14% in 2017). Minority men and women now represent 17% of directors in the top 200 of the S&P 500 (up only slightly from 14% in 2008).

Shareholder Resolutions on Board Gender Diversity. On a related note, Arjuna Capital, an investment firm specializing in sustainable and ethical investing, is engaged in a campaign to induce twelve banks and technology companies to disclose their median pay gaps for women (a number that arguably indicates the extent of underrepresentation of women in higher paying positions at a company). In response, Citigroup disclosed on January 16, 2019 that median pay at the company for women globally was 71% of the median pay for men. Citigroup disclosed further its goals to increase, by the end of 2021, representation at the assistant vice president through managing director levels to at least 40% for women on a global basis and 8% for black employees in the U.S. Arjuna has been orchestrating shareholder resolutions requiring the disclosure, which would be voted on at the companies' 2019 annual meetings. Wells Fargo and Bank of America both tried to block the resolutions, arguing that they are an attempt to "micromanage" the company; however, on February 21, 2019, the SEC staff disagreed and permitted the resolutions. MasterCard's request to block the resolution it received is pending at the SEC.

New SEC C&DI on Board Diversity Disclosure. The Division of Corporate Finance released Compliance and Disclosure Interpretations 116.11 and 133.13 on February 6, 2019, which address the disclosure of self-identified diversity characteristics with respect to board members and nominees under Regulation S-K, Items 104 and 107. They provide that, to the extent a company's board nominating committee considers self-identified diversity characteristics such as race, gender, ethnicity, religion, disability, sexual orientation or cultural background, the SEC would expect the company's disclosure to include "identifying those characteristics and how they were considered."

Companies Should Consider Designating a Particular EU Subsidiary or Entity as the Company's "Main Establishment" for the Processing of EU Personal Data—*Google*

In its first enforcement action under the EU's General Data Protection Regulation, the French data protection authority ("CNIL"), on Jan. 21, 2019, imposed a €50 million (about US$56.8 million) penalty against Google LLC for violating disclosure and consent requirements under the GDPR relating to the processing of users' personal data for the purpose of developing targeted advertising. Google has announced that it will appeal the decision to France's highest Administrative Court. (The highest fine previously imposed under the GDPR was €400,000, in December 2018. Notably, for certain violations, the GDPR provides that the maximum fine is the *higher* of €20 million or 4% of the entity's annual revenue.) CNIL alleged that, while Google had disclosed a significant volume of data processing information to its users, it had failed (i) to provide notice in an easily accessible form, using clear and plain language, and (ii) to obtain users' valid consent to process their personal data for the purpose of developing personalized advertising. CNIL contended that Google's disclosure was not easily accessible for users and was spread across various documents; and that the description of the purposes of use of data, and the type of data that would be used for these purposes, was too "generic and vague."

Of note, Google had argued that France does not have jurisdiction over it under GDPR. The GDPR provides a "one stop shop" mechanism for companies that operate in multiple EU countries. The country where the company has its "main establishment" in the EU has primary responsibility for enforcement. Google contended that Ireland had jurisdiction because the company's Irish subsidiary is its main establishment in the EU—as it has been the headquarters for the company's EU operations since 2003, oversees administrative and financial functions for Europe region, and is the signing party on all contracts with advertising agencies located in the EU. CNIL took the position that Google had not established any "main establishment" with respect to the processing of personal EU data and that, therefore, CNIL (or *any* other EU authority) had jurisdiction under the GDPR. Based on the evidence provided by Google, CNIL determined that the Irish subsidiary had decision-making authority only with respect to Google's financial, advertising and commercial functions in the European region and had not been identified in Google's privacy policy as the company deciding the means and purposes of processing personal data in the EU. Accordingly, to avoid uncertainty as to which jurisdiction will have authority under the GDPR, a company should consider specifically assigning authority to a particular EU subsidiary or entity to act as its "main establishment" for the processing of EU personal data and should identify that entity in its privacy policy.

HSR and Director Interlock Thresholds Are Adjusted

The Federal Trade Commission announced on Feb. 15, 2019 the annual update of reporting thresholds for mergers and acquisitions under the Hart-Scott-Rodino Antitrust Improvements Act and director interlock prohibitions under Section 8 of the Clayton Act. The HSR threshold is revised annually based on the annual change in gross national product. The minimum size of a transaction requiring an HSR filing has been raised to $90 million (up from $84.4 million). The revised threshold is applicable to all transactions that close on or after April 3, 2019. The interlocking directorate thresholds prohibit a person from serving as a director or officer of competing corporations unless the parties' sales of the competing products or services are below certain *de minimis* thresholds. Under these revised thresholds, which are effective immediately, simultaneous service as a director or officer of two corporations, each with capital, surplus, and undivided profits of $36,656,400 or more, will be prohibited (subject to several exceptions). Companies should keep in mind that effective Section 8 compliance requires that a corporation annually review the outside affiliations of its directors and officers to assess whether, for example, sales growth, entry into new markets, or a decline in sales or exit from a non-competing business may trigger potential issues under the statute. For further discussion, including the other adjustments made, **see our Briefing**, *FTC Revises Thresholds for HSR Filings and Interlocking Directorates* (Mar. 4, 2019).

European Commission, for the First Time, Alleges Breach by a Company of the Commitments It Made in Obtaining Antitrust Clearance—*Telefonica Deutschland*

The European Commission, on Feb. 22, 2019, filed a formal objection to the implementation by Telefonica Deutschland of its commitments made when applying for competition clearance in connection with its 2014 acquisition of E-Plus (which had been the German mobile telecomm business of KPN, the Dutch telecomm operator). The Commission has never previously taken such an action. Telefonica had agreed to offer wholesale 4G services to all interested parties at "best prices under benchmark conditions." The Commission found that Telefonica did not properly implement the commitment because it did not include in the benchmark certain existing wholesale deals (thereby curtailing the ability of third parties to compete in the German market for mobile services). Telefonica's other commitments had included a sale of up to 30% of the merged company's network capacity and an offer to divest radio wave spectrum and certain other assets, initially to a new network operator or subsequently to virtual operators. The Commissioner in charge of competition policy wrote in the release announcing the objection: "We need full compliance and take very seriously any case where companies may have failed to comply with their commitments, which is why we have sent today's statement of objections."

The objection comes on the heels of an October 2018 dismissal by the European Court of Justice (the EU's highest court) of three cases brought by companies that had sought to buy network capacity that Telefonica was obligated to sell under its commitment to the Commission. (The court ruled that the Commission's decisions, as they are not legally binding, created no appeal rights for companies that sought to acquire network capacity that Telefonica agreed to offer for sale when obtaining antitrust approval.) Following a response by Telefonica, if the Commission concludes that the company did not respect the commitment made as part of obtaining antitrust clearance, the Commission could impose a fine of up to 10% of Telefonica's annual revenue and possibly could revoke the clearance decision.

Fried Frank M&A/PE Briefings Issued 1Q 2019

(*Please click on the title to see the Briefing*)

- ***Court of Chancery Grants the Books and Records Demand of a Director Whose Ties With the Company Were Severed by the Board After His Allegedly Offensive Conduct—Schnatter v. Papa John's*** (Jan. 24, 2019). In *Papa John's*, the Court of Chancery ruled that a director had the right, under DGCL Section 220, to inspect the corporate books and records that related to the board's determination to seek to sever ties with him based on his conduct involving the use of racial slurs. The director was also the founder, largest stockholder, Chairman, recent CEO, spokesperson and longtime "public face" of the company. As discussed in our Briefing, the decision potentially has broad applicability in the current era of increased sensitivity to directors' misconduct related to sexual harassment or racism. Boards should expect that, when they seek to sever ties with a director based on offensive conduct, in addition to fiduciary, contractual and/or defamation claims, a books and records demand is likely to be made and may provide another tool available to the director to increase his or her leverage in the situation. In the Briefing, we analyze the decision and offer related practice points.

- ***The Road Ahead for Shareholder Activism After a "Record Year"*** (Jan. 22, 2019). Many commentators have cited 2018 as a "record year" for activism in terms of number of campaigns, capital deployed, number of activists involved, first-time activists, and board seats obtained. In our Briefing, we review the 2018 year-end statistics and note that they do not tell the whole story. Despite the record statistics, the growth of activism from 2017 to 2018 was modest, particularly when campaigns against an announced merger and short seller campaigns are excluded. In addition, first time targets in the US represented less than 43% of financial activist's targets. Although we expect that activism will continue to evolve and will remain a prominent feature of the corporate landscape and that new themes and changing market conditions will create opportunities for activists, we believe the road ahead contains many pitfalls for activists. We discuss these and other issues in the Briefing, including the likelihood of (i) a concentration of the ranks of activists, (ii) workplace issues such as sexual harassment becoming a catalyst for activism, and (iii) increased aggressiveness of activists in connection with M&A-related campaigns.

- ***Impact of the Federal Government Shutdown on M&A Transactions, SEC and Investment Adviser Filings and Registrations, Government Contracts, and Litigation*** (Jan. 9, 2019).

- ***FTC Revises Thresholds for HSR Filings and Interlocking Directorates*** (Mar. 4, 2019).

- ***Recent OFAC Enforcement Actions Highlight Sanctions Risk in Cross-Border M&A Activity*** (Feb. 19, 2019). OFAC recently issued two enforcement actions for activities conducted by foreign subsidiaries that violated US sanctions laws. As discussed in our International Trade & Investment Alert, these settlements highlight the importance of US companies conducting enhanced sanctions due diligence on foreign targets during the M&A process, and implementing sanctions compliance policies at the new foreign subsidiaries. It is equally important that foreign subsidiaries' compliance with US sanctions laws and internal policies be monitored. Failure by foreign subsidiaries to comply with OFAC regulations could result in significant penalties for the parent as well as the subsidiaries

Fried Frank M&A/PE *Round-Up*

Fried Frank's M&A practice advises clients on some of the largest and most complex US and global deals, providing counsel to a full spectrum of companies on sophisticated transactions that are often multi-jurisdictional and, in some cases, transformational. With over eighty attorneys in four offices, our team has deep experience advising public and private companies, special committees, audit committees, and boards of directors in complex negotiated and contested situations, including negotiated mergers, hostile takeovers and takeover defense, proxy contests, financial adviser representations, and restructuring transactions.

Corporate partners Philip Richter and Warren de Wied and corporate senior counsel Gail Weinstein received the **2019 Burton Awards' Law360 Distinguished Legal Writing Award** for their article published in Law360, titled "Recent Trends In Shareholder Activism." This is the second consecutive year that both Mr. Richter and Ms. Weinstein have received the honor.

Highlights of Our 2019 First Quarter Work Include Representations of:

GreenOak Real Estate

Counsel to GreenOak Real Estate in its signing of an agreement with Bentall Kennedy to merge the two firms into a leading global real estate investment platform.

Laurel Road Bank

Counsel to Laurel Road Bank in the sale of its digital lending business to KeyBank National Association.

Special Committee of Safety, Income & Growth Inc. (SAFE)

Counsel to the Special Committee of Safety, Income & Growth Inc. (SAFE) in connection with the investment by iStar Inc. of an additional US$250 million in SAFE in the form of an acquisition of partnership units of SAFE's operating partnership.

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