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DOJ AND FTC RELEASE FINAL RULE EXPANDING HSR PREMERGER FILING REQUIREMENTS

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The Federal Trade Commission ("FTC") unanimously issued a final rule expanding the requirements of premerger filings under the Hart-Scott-Rodino Antitrust Improvements ("HSR") Act of 1976. The HSR Act requires parties to certain mergers and acquisitions to make premerger notification filings with the U.S. Department of Justice ("DOJ") and FTC, and to observe statutory waiting periods, prior to consummating their transaction. The final rule is a compromise that pares back many administrative burdens in the FTC's June 2023 draft rule.[1]

Although the final rule scaled back several of the initial proposed requirements, it still: (i) introduces novel obligations to address substantive antitrust issues in HSR filings; and (ii) requires submission of additional data and documents compared to the current HSR form. The final rule takes effect on February 10, 2025 (90 days after it was published in the Federal Register). Therefore, parties expecting to file on or after February 10, 2025, will need to file under the new rules.

Most HSR filings will take more time to prepare, which dealmakers should reflect in transaction covenants. Dealmakers also need to consider the effect of substantive disclosure obligations on risk of a DOJ or FTC investigation. It is not all bad news, however: The Commission also announced it would lift its February 2021 suspension of HSR waiting period "early terminations" for deals without antitrust concerns.

Substantive Antitrust Issues

The most significant change is the obligation to identify certain substantive antitrust issues in the HSR filing, including a "brief" description of horizontal overlaps and vertical supply relationships. Certain acquisitions unlikely to involve overlaps and deals involving products or services generating less than $10 million in revenue are excepted from this obligation.

Product Descriptions and Horizontal Overlaps. The final rule requires merging par-

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ties to describe the "principal categories" of products and services they offer, "as reflected in documents created in the ordinary course of business" of the company. Parties also must list and describe current or known planned products or services that compete or "could compete" with the other party to the transaction if those products or services are mentioned in the documents submitted with the filing.

For each competitive or potentially competitive product or service, parties are required to provide the sales (in dollars) for the most recent year. The rule also requires parties to provide a description of all categories of customers that purchase or use the product or service and the top 10 customers (as measured in dollars) in the most recent year for each overlap product or service and each category identified.

Non-Horizontal (or Supply) Relationships. The final rule also requires parties to list products, services, or assets that are sold, licensed, or otherwise supplied to the other party or any other business that competes with the other party. These disclosures also require information about sales to the other party or any competitors and the top 10 customers for these products.

Strategic Rationale. The final rule requires each party to explain the strategic rationale for the transaction and identify any documents included in the filing that confirm or discuss the rationale.

New Document, Data, and Information Disclosures

The most significant disclosure obligation for many companies will be submission of regularly prepared business plans provided to the company's CEO "that analyze market shares, competition, competitors, or markets pertaining to any product or service of the acquiring person also produced, sold, or known to be under development by" the other party to the transaction. This obligation is limited to documents prepared or modified within one year of the filing.

The final rule adds a requirement to submit so-called 4(c) and 4(d) documents, which analyze the transaction with respect to competition issues if those documents are prepared by or for the supervisory deal team lead.

Additional submission obligations are listed below:

- Translations for all foreign language documents.
- "Doing business as" (or "d/b/a") names for entities at the time of filing.
- Organize legal entities by operating business.
- Describe the business operations of the acquiring entity.
- Transaction diagram (if one exists).
- All exhibits and schedules to the transaction agreement.

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- Pending awarded procurement contracts with the Department of Defense or any member of the U.S. intelligence community (defined by statute) valued at $100 million or more (if an overlap exists).
- Identify merger control filings outside the United States (now mandatory rather than voluntary).
- Disclose (via checkbox) the existence of licensing arrangements, non-competes, and non-solicits between the parties.
- Identify officers and directors of the acquiring person in overlap industries and certain limited partners with management rights.
- Identify other entities for which identified officers and directors serve as an officer or director.
- Disclose more information about minority investments.
- Identify subsidies from any "foreign entity or government of concern."

HSR Filings Based on a Letter of Intent. The HSR regulations require parties to submit an affidavit attesting they have executed a contract, letter of intent ("LOI"), or agreement in principle, and have the good-faith intent to complete the transaction. Historically, a simple nonbinding LOI sufficed.

The new rules still permit merging parties to file even if they have not executed a definitive agreement but only if the merging parties provide more detail about the transaction compared to the existing requirement. The new HSR rules will require a dated document that describes some combination of the parties' identities, the transaction's structure, the scope of the acquisition, the calculation of the purchase price, an estimated closing timeline, employee retention policies, post-closing governance, and transaction expenses or other material terms.

Upcoming Developments to Watch

In a November 12, 2024, blog post, the FTC acknowledged that the upcoming changes to the HSR form and instructions will involve adjustments for practitioners. In recognition of the changes, the agency stated that the Premerger Notification Office ("PNO") will soon provide a detailed overview of the new requirements and will then invite practitioners to submit any questions. PNO staff will post answers to any questions on the FTC's website. The blog post also noted that the PNO plans to update other HSR form-related guidance and tips, including instructions on how to submit the newly required materials.

Five Key Takeaways

1. Most HSR filings can be prepared within about two weeks, and many within a week. Filings under the new rules will take longer to prepare; however, the burden will not be as significant for deals with no overlap or no vertical relationships. Deals involving numerous or complex overlaps or vertical relationships may require much more time and effort to explain. The FTC estimates its rule will increase the number of hours to prepare HSR filings by 84% on average and by more than 225% for complex deals.
2. The HSR rule will take effect on February 10, 2025, meaning that companies should begin planning now. The new HSR Form calls for detailed information, perhaps in a format the merging parties may not ordinarily maintain.
3. Dealmakers should consider the effect of the rule on deal timing in the transaction covenants. Companies may need more time to produce information for the HSR filings, particularly if certain employees who keep information responsive to the expanded filing obligations are not "under the tent."
4. With additional information on horizontal overlaps and vertical relationships, the agencies may open more preliminary investigations to determine if they require further inquiry. In some cases, upfront information might help DOJ and FTC come to quick conclusions that no issues exist. However, in

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other cases, faced with additional upfront information to sort through, enforcers may require more time to reach a conclusion about a given transaction.

5. In recent years, unanimity has been infrequent at the FTC. The Republican commissioners supported the new HSR rule because the Commission rejected some of the most burdensome obligations in the draft rule. Lifting the ban on early termination, in place since February 2021, will likely allow many deals with no substantive issues to close more quickly.

The views and opinions set forth herein are the personal views or opinions of the authors; they do not necessarily reflect views or opinions of the law firm with which they are associated.

ENDNOTES:

[1]The Commission eliminated some of the more onerous requirements, including production of certain drafts of documents analyzing the deal, labor market information, and certain ordinary course documents.

CHARTER'S SUPERMAJORITY VOTE REQUIREMENT FOR AMENDMENTS IS INAPPLICABLE IN THE CONTEXT OF A REINCORPORATION TO NEVADA—*GUNDERSON V. TRADE DESK*

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In *Gunderson v. The Trade Desk, Inc.*,[1] the Delaware Court of Chancery held that only a majority stockholder vote was required to approve the proposed reincorporation of The Trade Desk, Inc. (the "Company") from Delaware to Nevada through a corporate conversion (the "Conversion"). The court held that, although Article X of the Company's charter (the "Charter") required a supermajority vote for amendment or repeal of the Charter, and although the Conversion as a substantive matter would result in amendment or repeal of the Charter, Article X was inapplicable because the language as drafted did not state that the Supermajority Vote requirement applied to amendment or repeal of the Charter *as a result of a conversion*.

Key Points

- **Critical drafting point for charter amendment provisions**. The decision reiterates the precise guidance provided in previous cases for corporate drafters when they seek to extend a protective supermajority (or other special) vote requirement for amendment or repeal of a charter that is effected through a corporate transaction such as a merger, consolidation, or conversion. For the vote requirement to extend to charter amendment or repeal in such cases, the charter amendment provision must explicitly state that the vote requirement applies to amendment or repeal of the charter *whether by merger, consolidation, conversion, or otherwise*. (We note that the decision bodes well for Tesla, Inc. in the pending litigation challenging its majority stockholder vote on its reincorporation to Texas pursuant to a conversion, as Tesla's amendment charter provision was similar to Trade Desk's.)

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- **Potency of the doctrine of independent legal significance**. The court's result was based on the doctrine of independent legal significance—which holds that legal action authorized under one section of the DGCL is not invalid because it causes a result that would not be achievable if pursued through other action under other provisions of the statute. While over the years there has been some uncertainty among practitioners as to the continued force of the doctrine, the court emphasized in *Gunderson* that it is "a bedrock of Delaware corporate law and should not easily be displaced."

- **Narrow opinion, however**. The court addressed in this opinion only the question whether the Conversion would be *legally authorized* if approved by a majority rather than a supermajority vote. Noting that director action is "twice-tested, first for legal authorization, and second by equity," the court reaffirmed that the doctrine of independent legal significance cannot bar fiduciary or equitable claims. The court indicated that the Plaintiff's equitable claims challenging the substantive fairness of the Conversion may be addressed at a subsequent stage of the litigation.

- **Continued judicial emphasis on technical formalities**. We note that the decision is consistent with the trend of the court in recent years toward an emphasis on technical formalities in a variety of contexts. The court focused on the formal transaction structure the board utilized (a conversion) rather than the transaction's substantive effect (repeal of the Charter); the technical requirements under the Delaware statute applicable to the transaction; and the precise language of the Charter.

- **Few reincorporations from Delaware**. Due to certain controversial decisions issued by the Delaware courts in the past couple of years (including *Crispo*, *Moelis*, *Activision*, *Tornetta*, and *Match Group*), there has been much discussion about the possibility of Delaware corporations deciding to reincorporate to states that impose lower fiduciary standards for corporate directors. Our research indicates, however, that, since 2021, only eight Delaware corporations have reincorporated to other states—and each of them was a controlled company. We note, further, that the decision in the appeal of *TripAdvisor*[2] is expected imminently. In *TripAdvisor*, the Court of Chancery held at the pleading stage of the litigation that a reincorporation from Delaware to Nevada was subject to entire fairness review (Delaware's strictest standard). If *TripAdvisor* is overturned, it is possible there would be some increase in interest in reincorporation from Delaware.

Background

The Company is a Delaware corporation with a dual class stock structure. The Company's founder, Jeff Green, is a controlling stockholder. In September 2024, the board of directors approved a resolution to reincorporate the Company as a Nevada corporation, through a conversion to be effected pursuant to DGCL Section 266. In the proxy statement for the stockholders' vote on the Conversion, the Company stated that, under Section 266, a majority vote was required to approve the Conversion. The stockholder-Plaintiff brought suit, claiming that a supermajority vote was required because Article X of the Company's Charter required a supermajority vote for amendment or repeal of the Charter and the Conversion would result in amendment or repeal of the Charter. Vice Chancellor Fioravanti held that only a majority vote would be required and granted summary judgment in favor of the Company, Green and the director-Defendants. At a special meeting on November 14, 2024, the stockholders approved the Conversion by a majority vote.

Discussion

The doctrine of independent legal significance. This doctrine has been described by the Delaware Supreme Court as providing that "action taken under one section of [Delaware law] is legally independent, and its validity is not dependent upon, nor to be tested by the requirements of[,] other unrelated sections under which the same final result might be attained by different means." The

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doctrine provides certainty to corporate planners—as a transaction structured to comply with a section of the DGCL will not be invalidated for its failure to comply with a different section of the DGCL. The paradigm application of the doctrine is where a corporate action is taken pursuant to a specific statute and there is an alternative statute with which the corporation could have complied to accomplish the same result.

Application of the doctrine to amendment or repeal of a charter. The Conversion will have the substantive effect of amending or repealing the Company's Charter. DGCL Section 266 requires a majority vote for approval of a conversion. DGCL Section 242 (which provides general authorization for amendment or repeal of corporate charters) requires a majority vote for amendment or repeal of a charter unless the charter provides for a greater vote. Article X of the Charter required a 66 2/3% vote for amendment or repeal of the Charter. In addressing whether the Conversion required a majority vote under Section 266 or, instead, a supermajority vote under Section 242 in light of Article X, the Plaintiff urged the court to focus on the substantive effect of the Conversion (*i.e.*, amendment or repeal of the Charter) rather than on the formality as to the specific type of transaction pursuant to which that result would be obtained (*i.e.*, a conversion). The court rejected this argument, writing: "[T]he entire field of corporation law has largely to do with formality." And such formality, the court stated, "has significant utility for business planners and investors." The court concluded that, under the doctrine of independent legal significance, and based on a long-standing line of precedential decisions, a majority vote would be required to approve the Conversion, as Article X did not expressly and clearly provide that it applied to amendments or repeal of the Charter effected through a corporate transaction such as a conversion. In the absence of such explicit language extending the reach of Article X, the court concluded, Article X applied only to Company action to amend or repeal the Charter pursuant to DGCL Section 242 and not to amendments or repeal effected through corporate transactions (such as mergers or conversions) authorized under sections of the DGCL *other than* Section 242.

Clear guidance under precedential cases. The critical consideration for the court in *Gunderson*, in not applying a substantive analysis to determine the intent of the drafters of Article X, was that there is a long line of precedential cases—*Warner Communications v. Chris-Craft*[3] and *Elliott Associates v. Avatex*,[4] and their progeny—that has provided "clear guidance to practitioners" with respect to drafting special vote requirements for charter amendments such that they would extend to amendments effected as a result of corporate transactions. In *Warner*, the Court of Chancery held that a merger could proceed under DGCL Section 251 without a class vote of the company's preferred stock even though the merger could have an adverse effect on the preferred stock that would have triggered a class vote under DGCL Section 242. In *Avatex,* the Delaware Supreme Court held that preferred stockholders had a vote on a merger that would have adversely affected their rights set forth in the company's charter because—in contrast to the charter provision in *Warner*—the Avatex charter granted the preferred stockholders a vote on amendment or repeal of the charter "whether by merger, consolidation or otherwise." The court emphasized in *Gunderson* that, given the decades-long precedent containing explicit guidance to drafters, if the language endorsed by the court is absent, the court will infer that its absence is intentional on the part of the drafters.

Potential viability of equitable claims notwithstanding the doctrine of independent legal significance. Even when the doctrine of independent legal significance applies, it cannot preclude equitable review, under which the court could determine to recharacterize a transaction even if the parties have complied with the applicable statutes. The court confirmed that, notwithstanding application of the doctrine of independent legal significance, "a substantive analysis [(*i.e.*, looking through a transaction's form to its substantive effect)] may prove necessary" when evaluating equitable claims, for example "to determine drafters' intent in adopting a particular provision." The court indicated that the Plaintiff's claims challenging the substantive fairness of the Conversion—which the Plaintiff added to the Complaint during the parties' briefing of the Plaintiff's

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motion to expedite hearing of the parties' summary judgment cross-motions—may be considered at a subsequent stage of the litigation. This opinion, narrowly, considered only the legal question relating to the required stockholder vote necessary for the Conversion.

Reincorporation from Delaware. An appendix to the Company's proxy statement provides a table of proxy filings by Delaware corporations that have recently proposed reincorporations to other states. The table, prepared by Professor Steven Davidoff Solomon, indicates that, from January 1, 2021 to August 19, 2024, 18 Delaware corporations proposed to reincorporate to other states—of those, 14 were proposals for reincorporation to Nevada; two (one of which is Tesla) for reincorporation to Texas; one for reincorporation to Colorado; and one for reincorporation to Maryland. Our research indicates that only eight of the 18 Delaware corporations that proposed to reincorporate to other states have actually reincorporated (six to Nevada and two to Texas)—and all of these companies appear to have a controlling stockholder. (We note that the Appendix also reflects that there were 18 corporations during that period that proposed to reincorporate *to Delaware*—two of which were Nevada corporations and one of which was a Texas corporation.)

***TripAdvisor* appeal**. The appeal of the Court of Chancery's *TripAdvisor* decision was heard by the Delaware Supreme Court on October 30, 2024, and a decision is expected imminently. In *TripAdvisor*, the Court of Chancery held that reincorporation from Delaware to a state imposing lesser fiduciary standards on directors offers a non-ratable benefit to directors (namely, more protection against personal liability) and so will be subject to entire fairness review if challenged. The decision indicated that, while a Delaware corporation is free to reincorporate to a lower-fiduciary-standard state, a board's fiduciary duties may require that the stockholders be compensated in some way (potentially in the form of monetary damages) for the diminishment of their "litigation rights" as a result of the reincorporation. Notably, in *TripAdvisor*, the company asserted that Nevada law provides for lower fiduciary standards than Delaware—allegedly, without carefully examining the Nevada statute; and there was, allegedly, substantial evidence that obtaining the benefit for directors of lower fiduciary standards was the primary reason for the company's proposing the reincorporation. If the Supreme Court overturns *TripAdvisor*, this may stimulate more interest in reincorporation from Delaware. If *TripAdvisor* is upheld, the Supreme Court's decision may provide needed guidance on open issues, such as whether compensation would not be owing to stockholders if the board seeks reincorporation for reasons that provide benefit to the corporation and its stockholders as a whole rather than to provide directors with lesser exposure to fiduciary claims.

Practice Points

Consider whether to include "*Avatex* language" in charter provision requiring a supermajority (or class or other special) vote for charter amendments. The court-endorsed language—which is protective of stockholders—would state that the supermajority (or class or other special) vote requirement applies to any amendment or repeal of the charter "whether effected through a merger, consolidation, conversion, or otherwise." We note that this issue arises not only in the context of conversions and mergers, but often in the context of the issuance of preferred stock and a charter provision requiring a class vote of the holders for charter amendments that would adversely affect the rights and preferences of the preferred stock.

Monitor Delaware decisions for court-endorsed language in other contexts. It should be kept in mind that, where the court has clearly and over a long period endorsed specific language to be used in a specific context to effect a certain result, the absence of such (or similar) language may be interpreted by the court as being intentional, indicating that the drafter did not intend to effect such result.

Reincorporation from Delaware. Pending and subject to any guidance that may be offered in the upcoming decision in the appeal of *TripAdvisor*, corporations considering reincorporation from Delaware should:

- Examine carefully the statutes and policies of the

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proposed new state to determine if they provide lower fiduciary standards for corporate directors, officers or controllers—rather than simply assuming as much;

- Keep in mind that entire fairness review may be applicable; that the stockholders may be owed compensation for a decrease in their "litigation rights" if the fiduciary standards are lower in the new state than in Delaware; and that it is unclear what form that compensation can take and, if monetary damages, how they would be calculated; and

- Establish a record reflecting that the reasons for proposing the reincorporation are based on benefits to the corporation and its stockholders as a whole—for example, lower franchise fees. (We note that, as one example, Gaxos.ai Inc. disclosed in its proxy statement relating to its reincorporation that, based on its current capital structure, it would pay franchise taxes of $200,000 in Delaware for 2024, while in Nevada it would pay only $675.) Other potential reasons for reincorporation that would redound to the benefit of the corporation and its stockholders as a whole include, for example: greater ability to attract and retain management and employees in the new state; lower exposure to product liability claims under the new state's legal regime; a political climate in the new state that better aligns with the corporation's culture and values; and being located in the state where the corporation's primary facilities or operations are located.

Of course, companies considering reincorporation from Delaware should keep in mind the potentially significant disadvantages—including less predictability on legal matters due to more limited case law in the new state; and potential investor unease to the extent the law and policies in the new state are viewed as being less developed, less understood, and/or less protective of stockholder rights than Delaware's laws and policies.

ENDNOTES:

[1]*Gunderson v. The Trade Desk, Inc.,* C. A. 2024-1029-PAF (Nov. 7, 2024).

[2]*Palkon v. Maffei*, 311 A.3d 255 (Del. Ch. 2024), certification denied, 2024 WL 1211688 (Del. Ch. 2024) ("*TripAdvisor*").

[3]*Warner Communications Inc. v. Chris-Craft Industries, Inc.*, 583 A.2d 962 (Del. Ch. 1989), order aff'd, 567 A.2d 419 (Del. 1989).

[4]*Elliott Associates, L.P. v. Avatex Corp.*, 715 A.2d 843 (Del. 1998).

U.S. TREASURY CREATES THE "REVERSE CFIUS" PROGRAM, A (LIMITED) GREAT WALL ON OUTBOUND INVESTMENT

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The Department of the Treasury ("Treasury") has released a final rule imposing restrictions on U.S. outbound investment in Chinese companies active in developing certain national security technologies ("Final Outbound Rule").

The rule, which was released on October 28, 2024, and takes effect on January 2, 2025, imposes additional diligence responsibilities, record-keeping and notification requirements, and restrictions on U.S. persons and

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their controlled foreign entities engaging in certain transactions with foreign persons in "countries of concern" (currently limited to China) that perform defined activities related to semiconductors and microelectronics, quantum information technologies or artificial intelligence ("AI") (together, "sensitive sectors").

Unlike the Committee on Foreign Investment in the United States ("CFIUS"), the Final Outbound Rule—which has been referred to as a "reverse CFIUS" program—does not create a transaction-specific screening and review mechanism.

Instead, it outsources the primary regulatory compliance burden to the relevant U.S. investor or investment management professional.

As shown in the chart below, the Final Outbound Rule requires U.S. citizens, lawful permanent residents and entities (including limited partners, or LPs, and U.S. individuals serving in key management roles in non-U.S. entities) (together, "U.S. Persons") to notify, abstain from or take action to prohibit certain transactions ("covered transactions") related to Chinese companies or related companies engaged in specified activities in sensitive sectors ("covered activities"). (Companies engaged in covered activities are "covered foreign persons.")

Below, we highlight key features of the Final Outbound Rule with the not-insignificant caveat that because this rule is not based on legislation, the incoming Trump administration will be free to modify or withdraw the rule. Given that at least some Republican members of Congress have already criticized the rules as inadequate, we expect the Trump administration will be inclined to give these rules a very hard look.

Covered Transactions

The Final Outbound Rule applies to the following types of investment or investment-related transactions (both direct and indirect):

- acquisition of equity or a contingent equity interest;
- provision of certain debt financing;
- conversion of contingent equity interest into equity interest;
- involvement in greenfield or brownfield investment;
- entrance into a joint venture; or
- acquisition of a limited partner interest in non-U.S. fund.

Whether a transaction is a covered transaction depends on whether the U.S. Person has "knowledge" at the time of the transaction, to include undertaking "a reasonable and diligent inquiry," that a specific transaction is a covered transaction—*i.e.*, whether the transaction involves a covered foreign person engaging in a covered activity.

The Final Outbound Rule places ongoing notification requirements on U.S. Persons if a U.S. Person learns after closing that the transaction was a "covered transaction," putting a spotlight on the adequacy of any pre-transaction diligence.

While obtaining representations and warranties is a factor in satisfying the "reasonable and diligent inquiry" standard, this factor is not dispositive, nor does the Treasury Department identify specific representations or warranties that would be sufficient to meet this requirement.

Rather, the Final Outbound Rule suggests that a more individualized review may be required. It does so by identifying a non-inclusive list of factors such as diligence questions asked of a target, analysis of publicly available information, the presence of "warning signs" such as evasive diligence responses and efforts to obtain nonpublic information relevant to transaction, as relevant to determining whether a U.S. Person had "knowledge" the transaction was a "covered transaction."

The Final Outbound Rule includes some exceptions and safe harbors for transactions that do not typically provide investment targets with the type of intangible benefits of U.S. Person investments that the Final Outbound Rule was designed to regulate.

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For example, the rule exempts the acquisition of publicly traded securities, as well as passive U.S. LP investments into non-U.S. funds below $2 million (or where the LP obtains contractual guarantees that its capital will not be used in a prohibited/notifiable transaction). The Final Outbound Rule also exempts some intracompany transactions between a U.S. Person parent and its subsidiary that may otherwise be a covered foreign person, as well as certain debt and derivative transactions.

Additionally, most agreements entered into prior to January 2, 2025, are not captured, although any subsequent, related transactions on or after January 2, 2025, would need to be carefully reviewed under the Final Outbound Rule.

Covered Foreign Persons

The Final Outbound Rule defines "covered foreign persons" to include any person or entity that "engages in" a covered activity who is:

- a citizen or permanent resident of China and not a U.S. citizen or permanent resident;
- (if an entity) headquartered or with its principal place of business in China, or incorporated or organized under Chinese law;
- a Chinese government party; or
- any entity, wherever located, where 50% or greater voting interests, board interests or equity interests are held by persons described above ("persons of a country of concern").

The term also includes any person, including U.S. Persons, who holds certain equity, voting or governance interests in a covered foreign person, from which such person derives a majority of their income or incurs a majority of their expenditures or expenses (*e.g.*, variable interest entities).

Thus, U.S. Persons must look beyond investments in China to transactions with covered foreign persons in third countries and must also consider whether their investments may be used to establish a covered foreign person. U.S. investors will need to ensure that their investments into non-Chinese targets in sensitive sectors do not inadvertently create an indirect notifiable or prohibited transaction.

Moreover, because the Final Outbound Rule does not set a *de minimis* level of activity that would qualify as "engag[ing] in a covered activity," determining whether a person of a country of concern "engages in" a covered activity is likely to be a key diligence challenge.

Notifiable and Prohibited Transactions

The Final Outbound Rule defines two different classes of covered transactions—notifiable transactions and prohibited transactions—based on the type of activity in a sensitive sector in which a covered foreign person engages. (See table below.)

An obligation to notify the Treasury Department of a transaction is triggered where a covered foreign person engages in:

- designing, fabricating or packaging integrated circuits ("ICs") (where the transaction is not a prohibited transaction), or
- developing AI systems (1) designed for military or government intelligence or mass surveillance uses, (2) intended to be used for cybersecurity applications, digital forensics, penetration testing or control of robotic systems, or (3) trained using a defined threshold of computing power.

A transaction is prohibited if it involves sensitive sector activities implicating:

- certain advanced technologies (*i.e.*, those technologies exceeding certain performance or power thresholds) or military or intelligence end uses, or
- foundational and related technology (design software for ICs, developing or producing semiconductor fabrication or packaging equipment, and a range of actions related to quantum computing and related activities).

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Covered activities include research and initial development or design work as well as modification and certain testing activities.

Further complicating an investor's diligence burden, even an entity that outsources these activities can be considered "engaging in" the covered activity in addition to making the third-party entity providing those services a potential covered foreign person.

Activities by U.S. Persons in Non-U.S. Companies

Although the obligations in the Final Outbound Rule extend to U.S. Persons, they can impact non-U.S. funds and other companies in several ways.

For example, a U.S. Person must take "all reasonable steps" to ensure their controlled (*i.e.*, greater than 50% voting interest) foreign subsidiaries ("controlled foreign entity") do not engage in prohibited transactions and must report notifiable transactions by their controlled foreign subsidiaries. A U.S. Person who holds certain executive functions at a foreign entity but is not otherwise a "parent" of the entity must not "knowingly direct" a transaction that would be a prohibited transaction if engaged in by a U.S. Person.

The Final Outbound Rule provides safe harbor to such U.S. Persons who recuse themselves from certain decision-making activities with respect to the would-be covered transaction.

Finally, passive U.S. LPs investing more than $2 million will have diligence requirements when investing in foreign funds and in certain circumstances must obtain contractual assurances that the non-U.S. fund will not engage in covered transactions.

Penalties

The Final Outbound Rule does not establish independent penalties but relies more broadly on penalty amounts authorized under the International Emergency Economic Powers Act, similar to the penalties available under economic sanctions programs administered by Treasury's Office of Foreign Assets Control.

Civil penalties can be imposed to the greater of either $250,000 (adjusted for inflation, currently $368,136) or twice the value of the transaction that serves as the basis of the violation.

Persons who willfully violate the Final Outbound Rule may be subject to a fine of up to $1 million and be imprisoned for up to 20 years.

The secretary of the Treasury can also take actions to require divestment for any prohibited transaction. Where an investor believes a violation may have occurred, they may submit a voluntary self-disclosure to Treasury that will be taken into account in assessing any penalties.

A More Complicated U.S. Regulatory Landscape

The thresholds and covered activities established in the Final Outbound Rule complement, and were informed by, adjacent U.S. regulatory regimes, but do not perfectly match them.

For example, technical thresholds in the Final Outbound Rule are not a perfect match to technical thresholds established in the Export Administration Regulations or International Traffic in Arms Regulations for ICs and related hardware.

Covered activities are also not a perfect match to activities associated with a "critical technology U.S. business" under the CFIUS regulations, and the Final Outbound Rule covers a much broader set of transactions than those regulated by CFIUS.

While the Final Outbound Rule does make some effort to conform definitions with some other national security regulatory regimes (*e.g.*, the definition of "AI system" with Executive Order 14110, on the "Safe, Secure and Trustworthy Development and Use of Artificial Intelligence"), investors will need to carefully analyze the Final Outbound Rule's definitions against a prospective target's technology to determine applicability.

Takeaways

The Final Outbound Rule is broad in capturing U.S.

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Persons, wherever located, and in defining covered foreign persons to include their subsidiaries abroad and those with significant financial relationships. But the rule is limited in that it narrowly tailors the scope of covered activities to defined activities within sensitive sectors.

We expect that the Final Outbound Rule may have a limited impact on investments and related transactions, due in part to the de-risking in relevant Chinese markets already being undertaken by U.S. investors and tech companies in response to current and anticipated U.S. regulatory restrictions.

They include:

- Reporting requirements and restrictions in relation to the Commerce Department's Information and Communications Technology and Services regulations.
- Mitigation restrictions as a result of receiving CHIPS Act funding.
- Risk factors for CFIUS and ex-U.S. foreign direct investment screening regimes.
- Export controls on semiconductor, AI and quantum computing-related hardware and technology.
- Forthcoming regulations such as a rule restricting access to U.S. bulk data.

All together, these new and anticipated regulatory regimes will work to restrict or prohibit U.S. Person involvement in sensitive sectors in China and any other country of concern that the U.S. president may name.

Nonetheless, the Final Outbound Rule may impose significant diligence and related compliance obligations, directly or indirectly, on U.S. investors, U.S. companies engaging in cross-border transactions implicating the sensitive sectors and similarly situated non-U.S. firms with U.S. management personnel.

The Final Outbound Rule may not be the last word on regulating U.S. outbound investment. As noted in the rule, several pending bills in Congress could supersede portions of the Final Outbound Rule. Moreover, and as previously noted, the incoming Trump administration may expand the scope of the restrictions or otherwise change the rule.

Additionally, the U.S. may not be alone for long in imposing such restrictions. The European Commission has expressed some interest in exploring parallel outbound restrictions for European Union investors—though there appears to be much less appetite for pursuing them than has been the case in the U.S.

Is the Transaction Prohibited or Notifiable?

The flowchart below illustrates what types of transactions are prohibited, notifiable or require no notification to the Treasury Department.

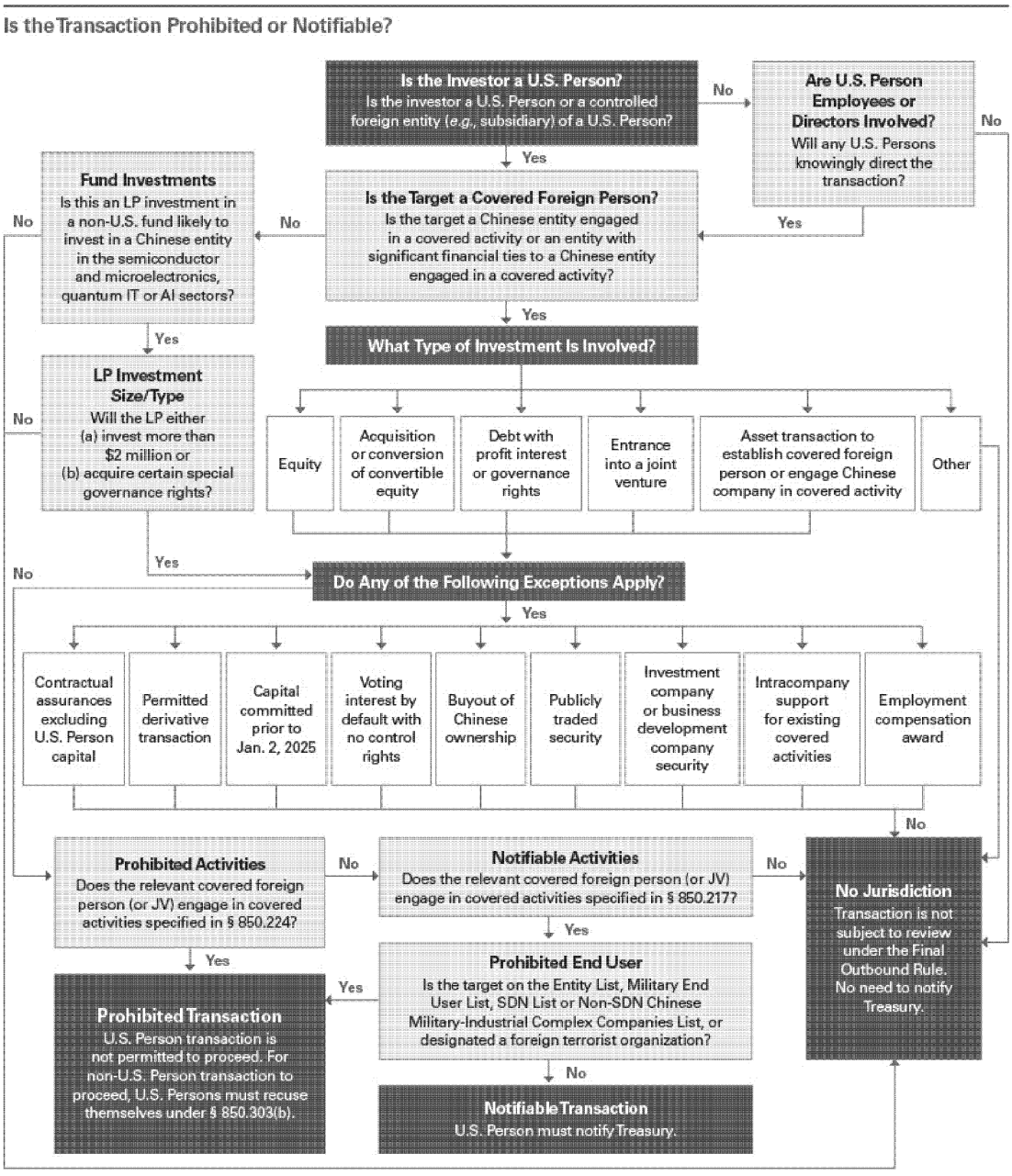
The key questions are:

- **Is the Investor a U.S. Person?** Is the investor a U.S. Person or a controlled foreign entity (*e.g.*, subsidiary) of a U.S. Person?
- **What Type of Investment Is Involved?**
- **Do Any of the Following Exceptions Apply?**

The flowchart runs the reader through yes/no options to reach one of three conclusions:

- **Prohibited Transaction**. U.S. Person transaction is not permitted to proceed. For non-U.S. Person transaction to proceed, U.S. Persons must recuse themselves under Section 850.303(b).
- **Notifiable Transaction**. U.S. Person must notify Treasury.
- **No Jurisdiction**. Transaction is not subject to review under the Final Outbound Rule. No need to notify Treasury.

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Please note that this graphic is provided solely as a quick reference guide to general jurisdictional principles and is not intended to comprehensively reflect the final regulations' requirements or jurisdictional reach.

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COVERED ACTIVITIES		
SECTOR	**PROHIBITED**	**NOTIFIABLE**
Semiconductors and Microelectronics	Development or production of: ▪ Certain electronic design automation software. ▪ Certain fabrication or advanced packaging tools. Design or fabrication of: ▪ Certain advanced ICs (*e.g.*, those classified at ECCN 3A090.a and certain logic ICs, NAND memory ICs, gallium-based compound semiconductors, ICs using graphene transistors or carbon nanotubes; ICs for operation at or below 4.5 kelvins). ▪ Advanced packaging techniques for ICs. Development, installation, sale or production of certain supercomputers enabled by advanced ICs.	Design, fabrication or packaging of ICs not otherwise covered in "prohibited" category.
Quantum Technologies	Development of quantum computers or production of any critical components required to produce a quantum computer. Development or production of: ▪ Certain quantum sensing platforms. ▪ Certain quantum networks or quantum communication systems.	N/A
AI	Development of any AI system: ▪ Designed to be exclusively used for, or intended to be used for, certain end uses. ▪ That is trained using a quantity of computing power greater than 10^25 computational operations or trained using primarily biological sequence data and a quantity of computing power greater than 10^24 computational operations.	Development of any AI system not otherwise covered by the prohibited transaction definition, where such AI system is: ▪ designed or intended to be used for certain end uses or applications; or ▪ trained using a quantity of computing power greater than 10^23 computational operations.

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MIDDLE MARKET M&A: RECOVERY AROUND THE CORNER?

Mergers and acquisitions of middle-market companies have faced the same issuance downtrends as the overall M&A market in the 2023-early 2024 period. So could middle-market deals help lead the way to a fresh wave of deal activity in 2025?

"For the entire M&A market, 2023 was absolutely a down year—that goes without saying. For the first half of 2024, overall deal volumes have been static but value has somewhat increased due to mega-deals," said Seyfarth Shaw LLP partner Andrew Lucano, who is co-chair of the firm's M&A practice. "Middle market deals have fared somewhat better in terms of volume. The general consensus is that the growth we've had in the first half of 2024 still trailed the expectations many people had at the beginning of this year. While the expected recovery hasn't come to total fruition yet, things have certainly picked up in the last few months and there is optimism for very positive activity in 2025."

There are a number of reasons for optimism, he said. "For one thing, the interest rate cuts, and the expected future cuts is a helpful sign, but not the entire story. There are reduced inflationary numbers, and increased pressure from limited partners for private equity firms to continue generating returns. Private equity activity has been much slower during 2023 and the first half of 2024, so there is certainly some pent-up demand. Limited partners are getting anxious and want to start seeing a return of deal activity to generate returns. Of course, there is still certainly no shortage of cash sitting of the sidelines waiting to be deployed, which is always a good sign."

What remains true, regardless of year-by-year volume trends, is that "M&A is the most proven method for accelerated growth for a company," Lucano said. "M&A is a well-traveled path for companies trying to keep pace with their competition. I also think there's more confidence brewing right now. People have been worried about 'when is the recession coming?' but it never came, and that fear has alleviated in a big way for the time being."

Seyfarth Shaw's latest Market M&A SurveyBook[1] (the "Survey") analyzes key transaction terms from over 130 middle market private target acquisition agreements that were signed in 2023 and the first half of 2024.[2]

The Survey attributes 2023/early 2024 volume declines and plateaus to a number of factors, including still-historically-high inflation and geopolitical uncertainties. Another key factor: buyers becoming more disciplined in engaging in transactions, refusing to overextend themselves to acquire targets, and moving to lower levels of the middle market amid uncertainty.

"When rates were low in 2021, which helped inspire a frenzy of M&A deals, there was just so much competition for deals that they were going quick—you would often see bidders come over the top with their purchase price proposals in deals marketed through an auction process in order to win the deal," said Lucano, who is based in Seyfarth Shaw's New York office. "In the current environment, even with rates coming down, buyers are more cautious and deliberate. It's not that they weren't doing expansive diligence in 2021, but it just seemed like there was a greater willingness to move quick to close deals."

"With the increase in the cost of capital, deals have become more expensive to do, the ROI is more narrow," he added. "Buyers are taking more time, running all the traps to uncover hidden issues, trying to make sure it's the best deal they can get. Buyers are not just jumping into deals. If buyers feel like they are paying a premium in order to be the winning bidder, they will be more cautious in their approach to make sure they are not com-

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pounding a potential overpayment by buying a problem missed in diligence."

Deal Terms

The Survey focuses on essential deal terms in middle-market deals, including those comprising the "indemnity package" at the heart of many private target acquisition agreements—terms that address a seller's potential post-closing liability to a buyer and which set the parameters of a buyer's ability to claw back purchase price from a seller.

Representation and warranty ("R&W") insurance remains quite popular in private middle market M&A transactions. Approximately 57% of the transactions reviewed in the 2023/2024 Survey included R&W insurance, compared to approximately 58% in the 2022/2023 Survey. Not surprisingly, the terms of the typical "indemnity package" differ substantially when R&W insurance is utilized.

"R&W insurance is a great product—it's tried and true, it's here to stay, and it's going to continue to be a valuable tool for M&A deals," Lucano said. "I wouldn't say there has been a plateau in use this year, as the M&A market in general has been slower. Also, there are some parties in deals that philosophically don't like to buy insurance products—they think they're never going to use the coverage. That's one reason we will likely never see complete saturation of deals using R&W insurance. But when the deal market gets hot again, we will continue to see heavy use of R&W insurance due to the 'win-win' nature of the product for both buyers and sellers."

Any upcoming decrease in R&W usage, he said, "could occur if there's a trend of insurance companies not paying claims—that would definitely dampen the R&W market, but current data does not support that trend. Of course, if the price of the product materially increases or if there are increased policy exclusions, or if it takes more time to put a policy in place—all of these are reasons why you could see a decrease in usage, but I do not believe we will head in that direction."

As per the Survey, the median general survival period for non-insured deals surveyed was 16.5 months, consistent with the 2022/2023 Survey. The vast majority (approximately 82%) of non-insured deals surveyed had a survival period of 12-18 months in 2023/2024. Roughly 16% of non-insured deals had survival periods of greater than 18 months, generally consistent with 2022/2023 and with prior years where such deals represented only a small percentage of the total number of deals surveyed.

The median general survival period for insured deals surveyed was 12 months, slightly down from 14 months in the 2022/2023 Survey. Roughly 92% of insured deals surveyed had a survival period of 12-18 months in 2023/2024, which is generally consistent with the length of the majority of indemnity escrow periods in 2023/2024. And approximately 8% of insured deals had survival periods of greater than 18 months, down from about 15% in 2022/2023.

With respect to "no survival" private target acquisitions in which representations and warranties of the seller terminate at closing, the Survey found a material decrease in "no survival" deals for the first time in several years when R&W insurance is used, while "no survival" deals for transactions not involving R&W insurance remained stable. In the scenario of a "no survival" deal, recourse to R&W insurance is often a buyer's only remedy.

"It makes sense that if you don't buy R&W insurance and don't have a remedy through a policy, the buyer has to look directly to the seller to be made whole in the event that the seller breaches its representations and warranties," Lucano said. "Buyers will most often demand an indemnity escrow to secure a seller's indemnity obligations when R&W insurance is not in play and generally not be willing to do a deal on no-survival terms. Our most recent M&A survey showed that even when parties bought R&W policies there was a material decrease in "no survival" deals, signaling a shift to more buyer-friendly terms."

"No-survival deals had been increasing over the past several years—this is the first decrease in some time," he added. "It's an indication of buyers taking a more cautious approach, wanting sellers to have some skin in the

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game and to stand behind their representations and warranties. In the end, it's always about the leverage of the parties in a particular transaction and the specific facts and circumstances applicable to the subject transaction. If the seller has an A class asset with great appeal to drive competition among multiple buyers, the leverage will lean toward the seller and you will be more likely to see a no-survival deal. On the other hand, when the buyer has more leverage, it is more likely that a no-survival deal format will not be used."

Other Survey findings included:

- Of the middle-market deals surveyed in 2023/2024, approximately 15% included earnouts, as compared to 17% in 2022/2023. And of the deals surveyed in 2023/2024 with earnouts, approximately 50% provided for earnout amounts in excess of 30% of the purchase price while roughly 30% of such deals provided for earnout amounts less than 5% of the purchase price.

- Of the middle-market deals surveyed in 2023/2024, about 76% used a "Material Adverse Effect" ("MAE") qualifier for the representations and warranties bring-down closing condition, compared to about 81% in 2022/2023. Approximately 17% used an "in all material respects" qualifier for the representations and warranties bring-down closing condition, compared to roughly 13% in 2022/2023. The high percentage of deals using the MAE qualifier for the representations and warranties bring-down closing condition is a seller-friendly term that increases certainty of closing for sellers, Seyfarth Shaw said.

ENDNOTES:

[1]For articles on previous editions of this survey, *see The M&A Lawyer*, October 2023, Vol. 27, Issue 9; *The M&A Lawyer*, April 2022, Vol. 26, Issue 4; *The M&A Lawyer*, May 2020, Vol. 24, Issue 5; *The M&A Lawyer*, May 2019, Vol. 23, Issue 5,

[2]*See* https://www.seyfarth.com/dir_docs/documents/flipbooks/2024_MA_SurveyBook.pdf.

NOMINEE DIRECTORS AND CONFIDENTIAL INFORMATION UP NORTH: WHAT U.S. PRIVATE EQUITY AND VENTURE CAPITAL SHOULD KNOW

By Marie-Christine Valois, Perry Feldman, Gesta Abols, Marco Maduri and Paul Blyschak

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Nominee directors are central to private equity and venture capital investment strategies. Significant investors expect to gain meaningful visibility and strategic input into the investee company, and thus routinely negotiate for the right to appoint one or more nominee directors. But what should take precedence: the confidentiality of board deliberations or the investors' expectation of information?

Earlier this year in *Illumina*,[1] the Delaware Court of Chancery (the "Court") confirmed when company confidential information can be shared by a nominee director with the nominating shareholder under Delaware law. As Canada is regularly among the top five destinations for outbound U.S. transactions by both deal value and volume, U.S. cross-border lawyers will be interested to know that Canadian corporate law differs somewhat from Delaware on this important issue.

We highlight what U.S. investors in the Canadian market, and their nominee directors, need to know about the sharing of confidential company information in Canada. We then provide key practice points to consider when selecting nominee directors as part of Canadian investment transactions.

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Delaware: Nominee Directors, Dual Fiduciaries and Designation Rights

At issue in *Illumina* was whether a company director who was employed by an activist shareholder could share confidential board communications with the activist shareholder.

The Court confirmed that Delaware has a "long line of caselaw dating back to 1992" that only permits a nominee director to share confidential company information with the nominating shareholder in "certain limited circumstances."[2] These are:

- When the director "serves as a controller or fiduciary of the stockholder,"[3] because of the impossibility of compartmentalizing information obtained through the board position from the director's responsibilities in their other fiduciary role. OR
- When the "stockholder has the right to designate [the] director, either by contract or through its voting power."[4] Here there is a presumption that, by virtue of a stockholder or shareholder agreement with nominating rights, the nominee will share information with the nominating entity, and thus the company should not expect confidentiality from such nominee.

In *Illumina*, the Court ruled that neither of these tests were satisfied in the circumstances. The director was not a controller or fiduciary of the activist shareholder, only a mere employee. The director had not been appointed as the result of any designation right in favour of the activist shareholder, but by the ordinary vote of shareholders. Nor did the activist shareholder have the right to appoint the director via its voting power, holding only a 2% interest in the company.

Canada: Nominee Directors and the Primacy of the Company's Interests

How do things stand north of the border? An immediate caveat is that Canadian corporate law does not benefit from nearly the same depth of judicial consideration of confidentiality issues that Delaware does. Simply put, no Canadian court has definitively ruled on whether, or to what extent, a nominee director can share company confidential information with the nominating shareholder.

Nonetheless, it remains useful to compare and contrast relevant Canadian corporate law and the clear test set forth in *Illumina*.

One point relates to the notion of a "dual-fiduciary" as recognized in Delaware. This underlies the first test under *Illumina*, whereby a nominee director can share confidential information with a nominating shareholder where the director is also a fiduciary of the nominating shareholder. The rationale is that, because a director only has "one brain," it is "simply not realistic or practical to believe that any information to which [the director] may become privy as a result of [her director status] could be segregated from her thought process in her other capacity."[5]

Canadian courts have not yet had occasion to directly consider this issue. When addressing the duty of loyalty provided for in corporate statutes and the Civil Code of Québec, Canadian courts often emphasize that the duty is owed only to the company, and not to any particular stakeholder (including nominating shareholders).[6] They also indicate that a director must avoid conflicts of interest with the company, avoid abusing their position to gain personal benefit and maintain the confidentiality of information they acquire by virtue of their position.[7] Accordingly, should the interests of the company and any stakeholder conflict, the interests of the company must prevail.[8] This should give nominee directors and their nominating shareholders pause before relying on "dual fiduciary" arguments in Canada.

A second noteworthy comparison between Delaware and Canada relates to the exception arising from a shareholder's right to nominate the director either by contract or through its voting power. While Canadian corporate law does not address the specific circumstance of a shareholder having sufficient voting power to elect a nominee director, it is generally uncontroversial that the company and the nominating shareholder can contract

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for the sharing of confidential company information (*e.g.*, in a shareholder agreement).[9]

That said, unlike in Delaware, in Canada the mere right of the nominating shareholder to appoint a nominee director may not be enough to trump the director's duty of confidentiality. In Delaware this logic is multifaceted. One justification is that the right to appoint a director results in a presumption that information will be shared by the director with the shareholder such that the company has no expectation of confidentiality.[10] Another justification is that the right to appoint a director effectively makes the director a representative of the shareholder, entitling the shareholder to the same information as the director.[11] Writing in *The Business Lawyer*, Vice Chancellor Laster has also advocated for this approach based on the "practical realities" of fund investment structures and investment management.[12]

As Canadian courts often consider Delaware rulings related to M&A and corporate governance, it is not impossible that a Canadian court may give weight to this reasoning in finding a similar implied right to confidential company information arising from a board nomination right. However, this would conflict with principles repeatedly affirmed by caselaw,[13] including decisions of the Supreme Court of Canada.

The third noteworthy comparison between Delaware and Canada is that a Canadian appellate court (in *PWA Corp. v. Gemini Group*) has ruled that, in exceptional circumstances, a nominee director may be obligated to share information *concerning the nominating shareholder* with the company on whose board the director sits.[14] Specifically, the court held that this duty may arise where the nominee director learns of information regarding the nominating shareholder that threatens a "serious loss" to a "vital aspect" of the company to whom the director owes fiduciary duties.

We are not aware of a similar result in the 30 years since the decision, and two aspects of the case may limit the likelihood of this occurring.[15] First, the nominee directors were part of the nominating shareholder's negotiating team pursuing the transaction that would be damaging to the company. Second, the nominee directors actively concealed from the company the fact that the nominating shareholder was pursuing the transaction. This included signing non-disclosure agreements prohibiting them from disclosing the existence of the negotiations, a circumstance that, according to the court, placed the directors in an "untenable position of conflict of interest" they could only resolve by resigning.[16] Although the court underscored the unique facts of the case, prudence warrants that the risk posed by *PWA Corp. v. Gemini Group*., even if arguably remote, is considered when appointing a director to the board of a portfolio company.

Key Practice Points Regarding Nominee Directors and Confidentiality in Canada

The foregoing variations between Canadian and Delaware corporate law highlight the need to approach nominee directors in Canada in a thoughtful and deliberate manner, including taking reasonably available precautions given the different issues presented. Key practice points to consider both when choosing who will serve as a nominee director and the terms of the nominating shareholder's right to appoint the director include:

- Best practice is to expressly address the sharing of confidential company information by the nominee director with the nominating shareholder in a written agreement between the company and the nominating shareholder (*e.g.*, a shareholders agreement). It is possible that company consent to the sharing of confidential information can be implied, but this will depend on the specific circumstances, and no Canadian court has yet done so. A clear written framework is thus preferable.

- Among other things, the agreement should (i) specify the nominating shareholder will maintain the confidentiality of any information received by its nominee, (ii) identify which of the nominating shareholder's personnel can have access to the information, and (iii) require the nominating shareholder to maintain protocols that will prevent the sharing of the information beyond permitted personnel. For example, care should be taken that

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the information is not shared with any of the nominating shareholder's personnel who sit on the board of a competitor of the company.

- If the company is a reporting issuer, it may be prudent to establish an internal wall between the nominee director and personnel responsible for trading shares of the company owned by the nominating shareholder. That said, it is important to note that Canadian insider trading rules apply to both public and private companies and cannot be waived by written agreement or otherwise.[17]

- Consider including an express acknowledgment in a written agreement providing that the nominee director is under no obligation to share any confidential information of the nominating shareholder with the company. While this may not provide a complete defence to the risk raised by *PWA Corp. v. Gemini Group*, it may militate against a claim by the company that it had a reasonable expectation to such information.

- The risk raised by *PWA Corp. v. Gemini Group* will be amplified where there is tension between the interests of the nominating shareholder and those of the investee company. In case of a material conflict of interest, nominee directors should weigh all options, including potentially resigning from their board position.

- Bear in mind that, notwithstanding the sharing of company information, the duties of confidentiality and loyalty will endure and continue to prevent the nominee director and/or nominating shareholder from using company confidential information for any improper purpose. Nor will the nominee director's duty of confidentiality regarding company confidential information received during the director's tenure expire when the director ceases to serve on the company board.[18]

- Alberta is the only jurisdiction in Canada that allows for corporate opportunity waivers of the kind afforded under Delaware General Corporation Law s.122(17).[19] As such, except where the investee company is incorporated in Alberta and has adopted a corporate opportunity waiver, a nominee director and/or the nominating shareholder may be liable to the investee company for exploiting a business opportunity that should have first been offered to the company.

Concluding Comments: Mind the Different Fiduciary Landscape Up North

While nominee directors play a pivotal role in the relationship between significant investors and investee companies, the guardrails around company confidential information require careful navigation. The Court of Chancery's decision in *Illumina* provides valuable guidance regarding Delaware law on this point, but U.S. investors must appreciate the different legal landscape at play in Canada to ensure the adoption of appropriate risk mitigation procedures by both nominee directors and nominating shareholders.

ENDNOTES:

[1]*Icahn Partners LP et al v. Francis deSouza et al and Illumina Inc.*, C.A. No. 2023-1045-PAF (Del. Ch. Jan. 16, 2024) ["*Illumina*"].

[2]*Illumina* at p. 12.

[3]*Illumina* at p. 13.

[4]*Illumina* at pp. 12-13.

[5]*Illumina* at pp. 20-21, quoting *Hyde Park Venture Partners Fund III, L.P. v. FairXchange, LLC*, 292 A.3d 178 (Del. Ch. 2023) and *In re CBS Corporation Litigation*, 2018 WL 3414163 (Del. Ch. 2018).

[6]*See* Markus Koehnen, *Oppression and Related Remedies* (Toronto: Thomson Carswell, 2004) at 204; Carol Hansell, *Directors and Officers in Canada: Law and Practice* (Toronto: Thomson Reuters, 2024); *Hawkes v. Cuddy*, [2009] EWCA Civ 291 at paras. 32-33 (Ch).

[7]*Peoples Department Stores Inc. (Trustee of) v. Wise*, para. 35.

[8]*See, e.g., Brockman v Valmont Industries Holland B.V.*, 2021 BCSC 500 (CanLII) at para. 115: "Shareholders have a reasonable expectation that the directors of a company will act in the best interests of the company. . . [T]hat principle would be fundamentally undermined if a majority shareholder's nominees to the board of direc-

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tors were to prefer the interests of that majority shareholder to the interests of the Company as a whole."

[9]*See* B. Reiter et al, *Directors' Duties in Canada* (Seventh Edition) (LexisNexis Canada, 2021) at 4.13-4.14.

[10]*Illumina* at pp. 14-15, citing *Moore Business* Forms.

[11]*Illumina* at pp. 16-17, citing *Kalisman v. Friedman*, 2013 WL 1668205 (Del. Ch. 2013).

[12]See J. Travis Laster & John Mark Zeberkiewicz, "The Rights and Duties of Blockholder Directors" 70 *The Business Lawyer* 33 (2015).

[13]*See*, for example, *PWA Corp. v. Gemini Group Antomated Distribution Systems Inc*., 1993 CanLII 9401 (ON SC): "A director nominated by a particular shareholder of the corporation is not in any sense relieved of his or her fiduciary duties to the corporation. A nominee director is not accorded an attenuated standard of loyalty to the corporation. The director must exercise his or her judgment in the interests of the corporation and comply with his duties of disclosure, and must not subordinate the interests of the corporation to those of the director's patron."

[14]*See PWA Corp. v. Gemini Group Automated Distribution Systems Inc*., 1993 CanLII 8475 (ON CA).

[15]Note also that the court split on this point with the dissenting justice finding no breach of fiduciary duty by the nominee directors for failing to disclose the shareholder information to the investee company.

[16]*PWA Corp. v. Gemini Group Automated Distribution Systems Inc*., 1993 CanLII 9401 (ON SC) at 177.

[17]*See*, for example, *Canada Business Corporations Act*, RSC 1985, c C-44 at s. 131(4).

[18]*See Bulk Steel & Salvage Ltd. v. Love*, [1984] O.J. No. 329 (H. Ct. J.).

[19]For further discussion, *see* S. Gingrich, B. Schneider, G. McGlaughlin, C. Rose and P. Blyschak, "Delaware's Corporate Opportunity Waiver Comes to Canada," *The M&A Lawyer*, Vol. 27, Issue 9, October 2023.

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FROM THE EDITOR

Post-Election: A New Era Begins (Take Two)

Donald Trump returns to the White House in January 2025, and along with him comes the substantial potential of an invigorated M&A market, one whose volumes have underperformed expectations since the post-COVID burst of deals in late 2021 and 2022.

Our year-in-review issue, coming in January, will go into greater depth as to how Trump 2.0 could play out in terms of federal antitrust review, along with its other implications for M&A. But predictions got fully underway within days of Trump's victory over VP Kamala Harris in early November.

There are two broad schools of thought about what the second Trump term will mean for mergers. One is essentially the "open the floodgates!" theory—that the M&A market, whose issuers have felt constrained by the Biden-era FTC and DOJ, are going to welcome what's generally perceived as a more M&A-friendly administration, which could produce a tidal wave of new deals in 2025.

"We know where the world is headed in a Trump environment because we've seen it before," Jeffrey Solomon, president of TD Cowen, said on CNBC's "Money Movers" in mid-November. "I think the regulatory environment will be much more conducive to economic growth. There will be lighter and targeted regulation."

And Jared Holz, health-care equity strategist for Mizuho, told CNBC that "whether or not Lina Khan is bounced day one is a key consideration, but even if fewer changes at the FTC take place, there is no doubt this [incoming] administration—at least on paper—will be far more amicable when it comes to business combinations."

Then there's the "deals will return, but so could chaos" perspective. Some M&A market observers agree with expectations that the market in the Trump restoration is likely to see increases in deal volume and value, in the short term. But they also predict that the administration has a substantial risk of creating economic uncertainty—such as trade wars with China and Europe and overall increased protectionism. Depending on the administration's tax and tariff plans, the U.S. could face renewed, and possibly substantial, inflationary pressures. Any of these factors could flatten M&A in the medium-term, they argue.

This is the last issue of *The M&A Lawyer* for 2024. We'll return in early January with our look back at the year, as well as a look ahead at 2025. We hope that all of our readers have a safe and happy holiday season, and a happy New Year.

Chris O'Leary

Managing Editor

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