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FTC IMPOSES RECORD FINE ON TEXAS ENERGY COMPANIES FOR HSR "GUN JUMPING"

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In early January, the Federal Trade Commission ("FTC") announced that Texas energy companies have agreed to pay a record $5.6 million civil penalty to settle allegations they engaged in pre-merger coordination, known as gun jumping, in violation of the Hart-Scott-Rodino Act ("HSR Act"). During antitrust review between M&A signing and closing, HSR rules restrict an acquiror from beginning to control the target's business.

Government is closely watching transaction parties' adherence to gun-jumping rules. This new action led to a significant fine for pre-closing conduct, including allegations of early control of the target; aggressive pre-closing covenants; and loose information sharing. Compliance with antitrust protocols limits legal risk and potential penalties, especially where the deal may raise information-exchange or other gun-jumping issues.

"Gun jumping" is an enforcement priority for the Department of Justice and Federal Trade Commission. A recent enforcement action against three Texas oil producers challenged several types of alleged gun jumping that the government emphasizes companies should avoid between signing and closing a merger or acquisition.

The federal merger notification statute, the HSR Act, requires parties to large M&A transactions to make "HSR" filings and delay closing to allow the government an opportunity to review their transaction under substantive antitrust law. The HSR waiting period lasts 30-60 days, unless the government extends its investigation by issuing a "second request" for additional information. Until that waiting period expires, an acquiror cannot take "beneficial ownership," including by allowing the acquiring company to begin to exercise control over the target's operations—"gun jumping"—whether or not that will have an anticompetitive effect.

The XCL Transaction

Sister companies XCL Resources and Verdun

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Oil agreed to pay $1.4 billion to acquire target EP Energy, a crude producer in the Texas Eagle Ford and Utah's Uinta Basin. The parties signed their acquisition agreement in July 2021. They then made HSR filings and delayed closing to allow the HSR waiting period to expire.

- However, according to the government's complaint, their agreement required that the target immediately halt its crude development activities so the acquirors could control plans to use its drilling assets moving forward. This led to shortages, so the acquirors began working with the target's customers for alternate supply. This allegedly gave the acquirors access to the target's customers and customer contracts.

- The government also alleged the acquirors used nonpublic information obtained in due diligence to influence the target's operations. For example, a Verdun employee allegedly used customer pricing and contract terms obtained from the data room to suggest changes to the target's pricing to customers.

- The agreement also required the target to obtain acquiror approval for all expenditures above $250,000, which the government alleged effectively transferred control of day-to-day operations to the acquirors.

In October 2021, FTC issued a "second request," extending its investigation and the HSR waiting period. At that point the parties amended the purchase agreement, removing the acquirors' early control rights.

After investigating, the FTC alleged the transaction would lessen competition in Uinta Basin waxy crude sold to Salt Lake City refiners. In a 2022 settlement of the FTC's antitrust challenge to the transaction, the acquirors agreed to divest the target's Utah business to a third party. The government's gun-jumping investigation continued until 2025.

Enforcement Action

In *XCL*, the government challenged the following alleged pre-closing conduct by the acquirors:

1. ***Control of the target business.*** The acquirors allegedly secured the right to control—and then controlled—much of the target's ordinary-course business decisions, daily operations, and customer interactions. This included pausing the target's well-development activities, changing its site design plans and vendor selections, and taking control over some operations.

2. ***Exchanging competitively sensitive information***. The acquirors' pre-closing involvement led to the target allegedly providing acquiror personnel with nonpublic information on the target business,

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including customer contracts and pricing, production reports, business plans, and other nonpublic information, which the acquirers then disseminated and used within its own business.

3. ***Control over expenditures***. The acquisition agreement's pre-closing covenants required that the target submit for approval by acquirors all expenditures above $250,000. The government alleged that this dollar amount covered many of the target's ordinary-course expenditures and itself effectively transferred control over much of the target's daily operations.

The companies agreed to settle the enforcement action and pay a $5.6 million fine, a gun-jumping record. (HSR Act violations are subject to a ~$52,000 daily penalty.)

Lessons Learned

This action highlights the importance of understanding gun-jumping principles. Much of the *XCL* conduct reflects routine concerns in M&A transactions. For example, many merger agreements require acquiror approval for significant pre-closing expenditures. The government's complaint acknowledges this practice, but asserts the $250,000 threshold was too low for an oil producer, such that (in the government's view) the acquirors obtained control of the target's day-to-day business. Likewise, the complaint asserted the target made little effort to control use of competitive information in its data room.

Whether or not the parties are competitors, failure to comply with gun-jumping rules can lead to delays in merger review and substantial fines. It is therefore important to work closely with inside and antitrust counsel in advance of signing a transaction agreement, especially where it may raise information-exchange or other gun-jumping issues

Key Takeaways

1. Recognizing and avoiding gun-jumping risk is critical: an acquiror may not take control of the target business pre-closing and should respect limits on competitively-sensitive information.

2. Appropriateness of pre-closing covenants may depend on the nature of target industry and business, calling for careful consideration.

3. Attention to antitrust protocols during due diligence and antitrust review can limit legal risk and delay.

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.

DELAWARE COURT OF CHANCERY HOLDS THAT CONTROLLER LACKED LIQUIDITY-BASED CONFLICT

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In a recent post-trial opinion in *Manti Holdings, LLC* v. *The Carlyle Group Inc.*,[1] the Delaware Court of Chancery, after initially declining to dismiss the case, held that the business judgment rule applied to the third-party sale of a controlled company because the private equity controller did not have a liquidity-based conflict and its interests were aligned with the minority in the sale. In what may be his last opinion before retiring, Vice Chancellor Glasscock confirmed the high bar that plaintiffs

must overcome to prove a private equity controller's liquidity-based conflict triggering entire fairness review of a transaction.

Background

In 2017, Authentix Acquisition Company, Inc. was sold to Blue Water Energy LLP following a year-long process. At the time of the sale, affiliates of the Carlyle Group Inc. ("Carlyle") controlled Authentix, owning through a fund 70% of Authentix's preferred stock and 52% of its common stock. The fund's partnership agreement provided for a fund life of 10 years (expiring in 2017), but there was no obligation to exit any particular investment at that time, and the fund was extended after the sale of Authentix. Plaintiffs, minority stockholders of Authentix, brought claims on the argument that Carlyle had sought a fire sale of Authentix in a process that was unfair to the minority and from which Carlyle extracted a unique benefit, namely liquidity and a timely exit for its fund. In an earlier opinion,[2] the court denied the defendants' motion to dismiss the complaint, finding that Carlyle was sufficiently alleged to be a controller of Authentix. Then drawing plaintiff-friendly inferences at the pleadings stage, the court held that the complaint adequately pled that Carlyle had acted to achieve a non-ratable benefit that was denied to the minority, and therefore entire fairness presumptively applied.

Analysis

After trial, the court held that while Carlyle was a controller, its interests were aligned with the minority and it did not have conflicts of interest that triggered entire fairness review. Therefore, the business judgment rule applied. Specifically, the court held as follows:

Carlyle did not have a liquidity conflict. First, the court held that Carlyle did not have a liquidity conflict resulting from the fund's expiration or any investor pressure for returns. Although the facts demonstrated that Carlyle wished to exit its Authentix investment in 2017, it did not *need* to exit the investment, nor was it driven by time pressure that would cause it to accept less than fair value for its investment. Even though the fund's initial term was set to expire in 2017, it could continue to hold investments after expiration, the term could be extended, Authentix was not the fund's only remaining asset and there was no pressure from fund investors to engage in a quick sale of Authentix. The court wrote, "[t]o prove a liquidity-driven conflict of a controller, it is not enough to show a general interest in investors that a fund adhere to a timeline; a plaintiff must show sufficient evidence 'of a cash need' that explains why 'rational economic actors have chosen to short-change themselves.' " The court also noted that the "comprehensive marketing and sales process" of Authentix, which lasted a year and consisted of contacting 127 potential buyers, was evidence that Carlyle did not have liquidity pressure in this regard.

Second, Carlyle did not seek liquidity to avoid disgorgement under a clawback mechanism operative under the fund documents, which would have required Carlyle to return excess carried interest if the fund failed to achieve certain returns. Instead, the court found that the clawback created an incentive structure that motivated Carlyle to sell investments that may be likely to decline in value (like Authentix), and that it would be best for all stockholders, regardless of the clawback, to sell before any further decline in value.

Carlyle's receipt of consideration for its preferred stock was not a non-ratable benefit triggering entire fairness. Plaintiffs alleged that Carlyle, through its ownership of 70% of Authentix's preferred stock, received a non-ratable benefit in the sale due to the preferred stock's liquidation preference, which ensured that the preferred stockholders received the first $70 million in consideration. Rejecting this argument, the court noted that Carlyle, which also held 52% of the company's common stock, had the most to gain from a high sale value, as Carlyle would be paid approximately half of every dollar in consideration over the $70 million liquidation preference. Therefore, its interests were aligned with the minority in extracting as high of a price as possible for Authentix.

Takeaways

Manti reaffirms that liquidity-based conflicts of con-

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trollers can be difficult to prove under Delaware law. Plaintiffs must show strong evidence as to why a controller would choose to short change itself in a sale, and allegations based on '' '[s]weeping characterizations' of the '[private equity] industry writ large' '' are unlikely to overcome this burden. Notwithstanding this high bar, as in *Manti*, liquidity-based controller conflict claims stemming from facts that likely would not support a post-trial finding of liability may nonetheless survive a motion to dismiss due to the plaintiff-friendly standards applied at that stage. Controllers and their representatives should be mindful of not developing a record suggesting that liquidity needs are more dire than they actually are to minimize risk of a plaintiff's success.

ENDNOTES:

[1]*Manti Holdings, LLC, et al. v. The Carlyle Group, Inc., et al.,* C.A. No. 2020-0657-SG (Del. Ch. January 7, 2025) (https://courts.delaware.gov/Opinions/Download.aspx?id=373720).

[2]*Manti Holdings, LLC, et al. v. The Carlyle Group, Inc., et al.,* C.A. No. 2020-0657-SG (Del. Ch. June 3, 2022) (https://courts.delaware.gov/Opinions/Download.aspx?id=333690).

PRACTICE POINTS ARISING FROM ALBERTSONS' CLAIMS AGAINST KROGER FOR BREACH OF THEIR MERGER AGREEMENT

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On December 10, 2024, two courts, on antitrust grounds, enjoined the planned $24.6 billion merger pursuant to which Kroger was to acquire Albertsons. After the injunctions were issued, Albertsons terminated the parties' Merger Agreement and filed suit against Kroger in the Delaware Court of Chancery. Albertsons alleges that, post-signing, Kroger had a case of buyer's remorse; and then, to derail the deal, willfully breached its obligations under the Merger Agreement to seek to obtain the antitrust approvals needed to close the deal. Albertsons is seeking the $600 million reverse termination fee ("RTF") delineated in the Merger Agreement, as well as all legally available damages (including the lost merger premium). Kroger, in turn, has asserted that Albertsons breached the Merger Agreement and is not entitled to the RTF.

These developments are reminiscent of other busted deal situations, such as the 2017 $54 billion planned merger between Anthem and Cigna, which was enjoined on antitrust grounds. In that case, after trial, the Court of Chancery found that Cigna (the target company) had a post-signing change of heart about the deal and then actively worked against Anthem's regulatory strategy in breach of the merger agreement—but that Cigna owed no damages to Anthem because the merger likely would have been enjoined in any event. In that case, the court determined that, in light of Cigna's breach, it was not entitled to receive the RTF provided for in that transaction.

While some or all of the allegations in the Kroger/Albertsons dispute may or may not be found to be true, they prompt consideration as to how a target company can best protect itself against the possibility that a buyer may not timely and effectively comply with its obligations to pursue the necessary regulatory approvals for a deal.

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Key Point

- ***The typical merger agreement provisions relating to obtaining regulatory approvals may not operate effectively in the case of a buyer who is not fully eager to close.*** Usually, the typical efforts, cooperation, and termination fee provisions relating to obtaining regulatory approvals are sufficient, as both parties have a unity of interest in the necessary regulatory approvals being obtained so the deal can close. However, where a buyer has a change of heart about the deal post-signing or determines that the divestiture requirements necessary to obtain regulatory clearance are too steep, the typical provisions may not be sufficient to prevent the buyer from subtly sabotaging the regulatory approval process. Thus, under certain circumstances, a target may wish to consider negotiating for additional, less usual agreement provisions to protect against such scenarios. See "Practice Points" below.

Background

In October 2022, Kroger agreed to acquire Albertsons in a merger, subject to antitrust clearance by the Federal Trade Commission. The parties understood from the outset that it could be challenging to obtain antitrust clearance and that, at a minimum, Kroger would have to make significant divestitures of supermarket stores to resolve antitrust issues.

According to Albertsons' Complaint, Kroger proposed to the FTC the divestiture of hundreds of stores, but the FTC found the divestiture package inadequate—stressing the "hodgepodge" nature of the list of stores to be divested and the inexperience and other weaknesses of the proposed divestiture purchaser. After a roughly two-year process, the FTC (joined by eight states) sued in federal court to enjoin the merger; and the States of Washington and Colorado filed separate suits to block the merger in those states. On December 10, 2024, a federal district court in Oregon granted the FTC a preliminary injunction blocking the merger, and a federal court in Washington issued an injunction blocking the merger in that state. Both courts found that the transaction raised antitrust issues and that the proposed divestiture package failed to resolve those issues.

Soon thereafter, Albertsons terminated the Merger Agreement and sued Kroger, asserting that Kroger sought to derail the deal due to strongly negative market and political reactions upon announcement, and decreased grocery store profits as people had shifted to more restaurant (rather than home) eating post-pandemic. Albertsons claims that Kroger willfully breached its contractual efforts obligations to obtain the required regulatory approvals for the merger. Kroger has publicly alleged that Albertsons breached the Merger Agreement, and therefore its termination is invalid and it is not entitled to the RTF; and Kroger separately sent a termination notice to Albertsons.

Discussion

The Merger Agreement

- **Efforts obligation.** The Merger Agreement sets forth a variety of different efforts standards. First, Kroger and Albertsons each were obligated to use "reasonable best efforts" to take all actions necessary, proper or advisable to satisfy the closing conditions as promptly as reasonably practicable, including by taking actions necessary to eliminate all antitrust impediments. Second, Kroger was required to use "best efforts" to take all actions necessary to eliminate all antitrust impediments to the merger, including by divesting assets, to enable closing to occur as promptly as practicable.

  Third, the Merger Agreement had a further provision under which Kroger was obligated, in the event a regulator threatened or instituted any Proceeding (defined to include "any investigation"—which, we note, potentially could include a "Second Request" from the FTC) challenging the merger on antitrust grounds, to take "any and all actions" to (i) contest the Proceeding to avoid the entry of an injunction and (ii) "eliminate each and every impediment under any Antitrust Law" to closing the merger before the end date. Albertsons'

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Complaint contends that this last provision amounted to a "hell or high water" commitment on the part of Kroger, subject only to the Divestiture Cap. The court, therefore, will have to determine whether this provision imposed an independent "hell or high water" obligation on Kroger beyond the already high "best efforts" obligation, or only obligated Kroger to contest any Proceeding using "best efforts."

- **Divestiture Cap.** Under the Merger Agreement, Kroger was not obligated to make divestures that would result in the divestiture of more than 650 stores. (Allegedly, Albertsons agreed to sign the Merger Agreement only after the CEO of its largest stockholder obtained the personal assurance of Kroger's CEO that Kroger would divest 650 stores.)

- **Control over the process; obligation to cooperate.** Kroger was obligated to "cooperate" with Albertsons in the process; consult with Albertsons before communicating or meeting with regulators; give Albertsons the opportunity to attend and participate in meetings with regulators; and "work together" with Albertsons to resolve disagreements. However, if the parties could not agree after working together in good faith, Kroger had the principal responsibility for devising and implementing the strategy to obtain antitrust approval.

- **Termination fee; damages.** If the merger failed to close by a specified end date—and all of the non-antitrust closing conditions (including that Albertsons had materially complied with its obligations under the Merger Agreement) were satisfied—a $600 million termination fee (2.5% of total merger consideration) was payable by Kroger to Albertsons. Further, if Kroger committed any "Willful Breach" of the Merger Agreement, Albertsons could seek, in addition to the termination fee, all legally available damages, including the lost merger premium.

Kroger's Alleged Willful Breach of its Efforts Obligations

- **Inadequate divestiture proposal.** Albertsons alleges that the divestiture package Kroger proposed to the FTC (as initially crafted, and as revised over time) was facially inadequate to meet antitrust concerns, and that Kroger knew that it would not pass muster with the FTC. In addition, Albertsons alleges that Kroger did not comply with its best efforts/hell-or-high-water obligation under the Merger Agreement, as the divestiture package did not include 650 stores. According to the Complaint, Kroger's own economic expert admitted that even with the divestiture package Kroger proposed, the merger would still be presumptively anticompetitive in at least 22 geographic markets; and the FTC had stated that this fact was "on its own. . .sufficient to find that the divestiture will not mitigate the merger's anticompetitive effects. . . ."

- **Non-responsiveness to the FTC.** Albertsons alleges that Kroger repeatedly dragged its feet when dealing with the FTC and other regulators, including by not responding to their comments and concerns or even their routine questions, and by doubling down on the divestiture package it proposed to the FTC even in the face of ongoing advice from Albertsons and repeated feedback from the FTC that the package was not sufficient to resolve antitrust concerns.

- **Non-cooperation with Albertsons.** Albertsons alleges that Kroger failed to adequately inform and cooperate with Albertsons in the process, including by ignoring Albertsons' advice, not including Albertsons in meetings, and ignoring Albertsons' repeated pleas that Kroger be more responsive to the FTC's concerns.

Albertsons' Specific Complaints about the Proposed Divestiture Package

- **Cherry-picked, nonviable stores.** Albertsons alleges that Kroger cherry-picked a "hodge-podge"

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of stores for divestiture, so that it could retain for itself the most valuable stores and off-load the least valuable stores—rather than selecting stores that, based on objective and neutral economic analysis, would be likely to address antitrust concerns.

- **Number of stores.** Albertsons complains that Kroger initially proposed divestiture of only 238 stores, and then increased that number ultimately to 541 stores, which was still short of the 650 stores cap.
- **Unacceptable divestiture purchaser.** Albertsons alleges that Kroger waited for months to begin the process of selecting a proposed purchaser of the to-be-divested stores, and then selected among the many interested bidders a company that the regulators were not likely to approve—a grocery wholesaler with little experience operating retail supermarkets, a history of selling retail locations soon after acquiring them, and a need for significant new financing to acquire the stores.
- **Insufficient non-store assets.** Albertsons alleges that Kroger did not include in the divestiture package sufficient *non-store* assets (such as store trade names, private label brands, and technology) for the divested business to thrive as an effective competitor.

The Anthem-Cigna Failed Merger

Similar to the Kroger-Albertsons situation, in 2017 a federal court, on antitrust grounds, issued a temporary injunction blocking Anthem's acquisition of Cigna. In that case, Anthem (the buyer) then sued Cigna (the target), claiming that Cigna had a post-signing change of heart about the deal and then worked to sabotage the regulatory approval process. Cigna attempted to terminate the merger agreement, and sued Anthem for breach of its obligations under the antitrust covenants in the merger agreement. Cigna sought the $1.85 billion RTF delineated in the agreement, as well as $13 billion in damages. In turn, Anthem sued Cigna for breach of its obligations under the merger agreement, alleging that Cigna had actively worked against Anthem's regulatory strategy (including even providing testimony in court that allegedly supported the FTC's position against the deal). Anthem sought damages of $20 billion. Five years after that deal's announcement, and over a year after the deal was enjoined, the Court of Chancery decided the breach of contract claims. The court held that neither Cigna nor Anthem was liable to the other. The court found that Cigna had breached its obligation to use reasonable best efforts to seek the regulatory approvals, but that Anthem had not been damaged by Cigna's actions because the merger likely would have been enjoined even if Cigna had fulfilled its obligations. The court also found that Anthem had adopted a reasonable regulatory strategy. Importantly, the court also found that Cigna was not entitled to the RTF given its own breaches.

Practice Points

Under certain circumstances, a target may wish to consider negotiating for less usual provisions that could provide additional protection against a remorseful buyer derailing the regulatory approval process. These circumstances might include, for example: a high level of antitrust risk; a buyer with a history of busted deals; a deal that is expected to provoke negative market, political, or credit rating agency reaction; an environment in which significant post-signing economic or market changes are expected or possible; and/or a pre-signing divergence of views between the parties as to the regulatory approval strategy. As indicated by the Anthem-Cigna failed merger, a *buyer* also may wish to seek greater protections against a *target* that may become reluctant post-signing and attempt to derail the regulatory approval process.

A more specific efforts provision may be more protective. A merger agreement often provides that the parties will use reasonable best efforts to obtain the regulatory approvals required for closing; and, specifically, that the buyer must use reasonable best efforts, or will take all actions necessary, to make divestitures needed to secure regulatory clearance. Many agreements also provide for specific limitations on the efforts obligation, such as a cap on the divestitures that the buyer

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would be obligated to make. Often, the limit is tied to a material adverse effect standard, which may be measured against the target, the buyer, or the combined company. As these efforts standards and limitations are often undefined, and materiality may be difficult to establish, a target may obtain added protection from provisions that set forth specific buyer obligations that are viewed as critical, with the parties agreeing in the merger agreement that breach of any of them would be deemed to be material. Depending on the facts and circumstances of the given situation, such obligations could include, for example, that the buyer must:

- Select assets for divestiture based on their value in resolving antitrust issues, rather than on any other objectives the buyer may have;
- Identify upfront specific assets that must be part of a divestiture package, unless the target or the regulator agrees otherwise—such an approach has the downside of reducing the buyer's leverage with the regulator, as it may provide a regulator with a "roadmap" of problematic assets, but may be useful where it is relatively clear from the outset that certain specific assets will have to be divested to meet antitrust rules or concerns;
- Include in the package of divested assets specified ancillary assets that would help the divested business operate as a strong competitor—such as, in the Kroger-Albertsons case, the divested stores' trade names, private label brands, and technology;
- Divest assets *at* the divestiture cap, if by a certain date the regulator has not accepted a lesser divestiture package;
- Select as the proposed divestiture purchaser a party who meets specified criteria;
- Select a specified investment banker to be responsible for running the divestiture process, and provide that both parties must be allowed to participate in substantive meetings with the banker;
- Agree to have disputes between the parties over compliance with efforts obligations relating to the divestiture package refereed and resolved by independent, experienced antitrust counsel and/or an economist; and/or
- Perform certain tasks within specified timeframes—such as, deadlines for the buyer and the target to certify substantial compliance with any Second Request, and for the buyer to propose a divestiture package to regulators, commence the process for locating a divestiture buyer, enter into a divestiture agreement, enter into consent decree, and so on.

The agreement could set forth specific consequences for breach of any of these specific obligations. Such consequences could include, for example: shifting to the target some (or primary) control over the regulatory approval process; and/or a right of the target to terminate the deal (which it might want to do if it has lost all hope that the buyer will do what is necessary to obtain the approvals). Also, the agreement could provide that, if certain deadlines during the process are missed, or if the regulatory process drags out beyond certain points, that failure would not constitute a breach, but the buyer would have to make specified payments to the target, or to make such payments into an escrow with the escrowed funds released to the target if regulatory approvals ultimately are not obtained—essentially a "pay-for-delay" construct. Under this type of arrangement, if a buyer thought it could obtain a better outcome by continuing to negotiate with regulators, it could do so, but at a predetermined price; and the buyer would effectively be prepaying the RTF, with the benefit to the target that it would not have to litigate after the deal breaks to obtain the RTF. In addition, as an RTF typically is not payable if the target breached its obligations under the merger agreement, a target may seek to negotiate, for this purpose, a higher standard of breach than usual or a breach only of specific obligations.

A target should seek maximum flexibility in the interim operating covenants. A merger agreement often provides that, between signing and closing, the target must act in the ordinary course of business and cannot

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take certain specified actions, without the buyer's consent. Many agreements provide that the buyer cannot withhold such consent unreasonably. Although the buyer and the target have a unity of interest in ensuring that the target operates effectively pending closing, their views may well diverge with respect to what constitutes effective operation. Also, particularly in the case of a remorseful buyer, the buyer's incentives may be skewed. Thus, the consent provision, even if consent cannot be withheld unreasonably, may not offer the target sufficient flexibility.[1]

A target should consider seeking to obtain the highest possible reverse termination fee. Albertsons alleged that, in negotiating with Kroger, it traded a lower-than-usual RTF in exchange for the highest-possible standard of buyer efforts. Certainly, Albertsons' thinking was that it would prefer that Kroger offer the FTC a significant remedy and obtain the approvals, rather than the deal failing to close and Albertsons receiving a large termination fee. Given the potential for a buyer's breach of its efforts obligations, however, and the possible difficulty of proving willful breach, a target may not always be advantaged by prioritizing the efforts obligation over the termination fee. The decision may depend on the level of antitrust risk, as well as the level of the target's trust in the buyer and its commitment to the deal. The parties should keep in mind that RTFs payable by a buyer are not subject to the same type of fiduciary duty issues as deal protection breakup fees payable by the target. Accordingly, the size of an RTF can exceed the typical 3%-4% range for deal protection termination fees. A Practical Law study of 2023 deals with antitrust-related RTFs reflects that, in 72% of the 39 public and private transactions in this dataset (with a value over $100 million), the RTF was 6% or more of the total merger consideration, with the average for all the deals being 4.8%. For deals valued over $5 billion in this dataset, most of them had RTFs above the 2.5% fee in the Kroger-Albertsons deal.

The parties should seek to ensure clarity in their agreement with respect to efforts obligations. First, drafters must pay special attention to the interaction of the various sections of a merger agreement, so that the parties' intentions are properly and clearly reflected. The interaction of multiple efforts standard is a common trouble spot in merger agreements. Second, in some decisions in recent years, the Court of Chancery has indicted that, without further definition, all efforts standards could, in practice, impose a similar obligation—that is, to take all reasonable steps to solve problems and consummate the transaction. Accordingly, where parties agree on a "best efforts" standard, they should consider whether they intend this standard to require even actions that are not "commercially reasonable"—and, if so, they should expressly so provide. Where parties agree on a "hell or high water" commitment, the agreement language should be clear that the parties intend that the buyer is obligated to take any and all actions to resolve antitrust issues, including making any divestitures and agreeing to any conduct restrictions—that is, that they intend to require the highest possible level of efforts that is judicially sustainable.

Antitrust counsel should be consulted early in the process. A critical part of the initial decision whether to pursue a sale or merger transaction involving a competitor is a determination as to the likelihood that antitrust approval can be obtained, and, importantly, whether it can be obtained in a timeframe and on terms that are acceptable to the parties. Also, success in securing antitrust approvals for a deal, and crafting appropriate deal terms relating to antitrust matters, relies to a great extent on planning in the very earliest stages of the deal, guided by antitrust counsel.

A target should consider carefully what the impact of non-approval by regulators would be. If regulatory approvals are not obtained, the target—in addition to having endured ongoing distraction and losing the merger premium—will have been subject, possibly for a lengthy period, to restrictions on its interim operations. In addition, in planning for the deal and the subsequent integration, the target will have shared detailed information with the buyer (who may be a competitor), including with respect to its plans and ideas for the future.

Merger parties should carefully consider the level

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and type of divestitures likely to be required by regulators—and the buyer should consider whether, realistically, it will find such divestitures to be acceptable. The parties may not wish to provide specifics as to exactly how many or precisely which assets the buyer will be obligated to divest if necessary to obtain antitrust approval—as such information could influence the regulators' view as to what they should require. However, the buyer may want to negotiate for a cap on the divestitures it has to offer and/or the exclusion of certain specified assets; and the target may want to negotiate for a minimum and/or the inclusion of certain specified assets. Generally, the antitrust regulators will be skeptical of large and complex divestiture packages comprised of mix-and-match assets.

Generally, providing a sufficient divestiture package to the antitrust regulators early in the process is a better strategy than proposing an initially weak package and then negotiating it over a lengthy period. In some circumstances, although this is not common, it may even be possible to present to the antitrust regulators at the outset a divestiture package with a divestiture purchaser and appropriate support agreements already lined up. Also, although unusual, there may be circumstances where a buyer, to address a divestiture purchaser's needs for support, could consider providing upfront cash support to the purchaser instead of support agreements that would entail a lengthy period of co-dependence on a competitor.

A buyer could consider a spinoff instead of divestiture. Spinoffs have rarely been used for required antitrust divestitures, but, under appropriate circumstances, a spinoff, with appropriate support from the buyer, may be an effective option for meeting business objectives (indeed, the availability of a viable spinoff alternative should increase the buyer's negotiating leverage with potential third-party purchasers of the to-be-divested assets); and, if properly crafted and presented, a spinoff may be acceptable to the regulatory agencies. A spinoff could offer the advantages that a suitable purchaser would not have to be found and that the arrangements would be self-executing (*i.e.*, the company would determine the arrangements without having to negotiate with a third party). Also, it should be easier to provide to a spinco, rather than to a third- party buyer of assets, the agreements and other support that would ensure that the spinco would be a strong competitor. Most importantly, all of the value delivered to the spinco would be captured by the merger party's stockholders (rather than by a third party, in what is often the equivalent of a "fire sale" due to the pressure to divest to obtain the approvals).

A buyer could consider signing an agreement to sell the overlapping assets prior to the Hart-Scott-Rodino ("HSR") filing, and submit the HSR filing only for the acquisition of assets that would remain after the divestiture. With this approach, the buyer can focus the antitrust agencies (and potentially a court) on the as-fixed transaction upfront, rather than as a potential remedy to an otherwise anticompetitive transaction. In contrast, in Kroger-Albertsons, the HSR filings submitted by the parties were for Kroger's acquisition of all of Albertsons, and the FTC was easily able to show in their prima facie case that the transaction as filed was anticompetitive across hundreds of geographies. Only at the rebuttal stage did the defendants have the opportunity to show how the proposed divestiture would mitigate the anticompetitive harms.

A buyer should not ignore the target's input if there is a cooperation obligation. If the parties' agreement, as would be typical, grants the buyer control over crafting and implementing the regulatory approval strategy but requires the buyer to cooperate or consult with the target, the buyer does not have to follow the target's advice or suggestions, but should not simply ignore the target. A record should be maintained of the consultations or conversations with the target and, possibly, the reasons for disagreeing with the target's advice.

Antitrust law and policy is in flux. Notably, the federal court enjoining the Kroger-Albertsons merger endorsed the FTC's embrace of important new components of the 2023 Merger Guidelines that have been controversial—including narrower definition of relevant markets; consideration of labor markets as a relevant antitrust market; and low levels of concentration (as low

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as 30%) as establishing a presumption that a transaction is anticompetitive. We expect that the antitrust agencies, under new leadership in the Trump administration, are likely to revert to a more traditional approach to mergers than has been the case under the Biden administration, with less focus on novel theories of harm such as the impact on labor, and possibly revision or withdrawal in whole or in part of the 2023 Merger Guidelines.

ENDNOTES:

[1] *See* our article, *A Postpandemic Framework for Ordinary Course and MAE Provisions in Merger Agreements: Reviewing Recent Market Practice Changes and Addressing Skewed Incentives*, published online in The Yale Law Journal.

FTC ANNOUNCES 2025 HSR THRESHOLDS AND FILING FEES AS CHALLENGES TO NEW HSR RULES LOOM

By Kenneth B. Schwartz, Rita Sinkfield Belin and F. Joseph Ciani-Dausch

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On January 10, 2025, the Federal Trade Commission ("FTC") announced revised notification thresholds and filing fees under the Hart-Scott-Rodino Act ("HSR Act"), as required by Section 7A of the Clayton Act. If a proposed merger, acquisition of stock, assets or unincorporated interests, or other business combination meets certain thresholds, the parties must notify the FTC and the Antitrust Division of the Department of Justice ("DOJ"), and observe a 30-day waiting period before consummating the transaction.

While these adjustments are largely administrative and will go into effect without opposition, the same cannot be said for the new rules promulgated by the FTC on October 10, 2024, dramatically expanding the information and documents required to be submitted with HSR filings.[1]

Although these rules are scheduled to become effective on February 10, 2025, recent developments could impact the start date. First, a lawsuit was filed on January 10, 2025, by the U.S. Chamber of Commerce and other plaintiffs alleging that the rules violate the Administrative Procedure Act ("APA"). Second, following his inauguration, President Trump signed an executive order, that if implemented, could delay the effective date. Third, the new rules also could face a challenge under the Congressional Review Act now that Republicans are in control of both houses of Congress and the White House.

Revised Thresholds

The new minimum filing threshold will be $126.4 million, up from $119.5 million. The new thresholds were published in the Federal Register on January 22, 2025, and will become effective on February 21, 2025.

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Original Threshold	Current Threshold	Revised Threshold
$10 million	$23.9 million	$25.3 million
$50 million	$119.5 million	$126.4 million
$100 million	$239.0 million	$252.9 million
$110 million	$262.9 million	$278.2 million
$200 million	$478.0 million	$505.8 million
$500 million	$1.195 billion	$1.264 billion
$1 billion	$2.39 billion	$2.529 billion

These new thresholds will affect the jurisdictional requirements and certain exemptions under the HSR Act, as well as the HSR Act's filing fee schedule. For example, if the value of a transaction does not exceed the revised minimum notification threshold of $126.4 million, the transaction will not need to be reported, and if a transaction value is at least $505.8 million, the HSR size-of-person test (which exempts deals from the notification requirement if the parties' annual revenues and total assets are below specified levels) will not apply to the transaction.

In addition, the FTC has announced the revised jurisdictional dollar thresholds applicable to Clayton Act Section 8, which prohibits competing companies from having interlocking officers or directors. The revised thresholds are $51.38 million for Section 8(a)(1) and $5.138 million for Section 8(a)(2)(A). These new thresholds took effect immediately upon publication in the Federal Register on January 22, 2025. Finally, the maximum civil penalty amount that can be imposed for violations of the HSR Act increased from $51,744 per day to $53,088 per day, effective January 17, 2025.

Revised Filing Fees

The FTC also announced updated merger filing fees for transactions subject to the HSR Act.

Size of Transaction	Filing Fee
Greater than $126.4 million to $179.4 million	$30,000
$179.4 million to $555.5 million	$105,000
$555.5 million to $1.111 billion	$265,000
$1.111 billion to $2.222 billion	$425,000
$2.222 billion to $5.555 billion	$850,000
$5.555 billion or more	$2.39 million

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The updated filing fees will also become effective on February 21, 2025.

Challenges to New HSR Rules

HSR changes of far greater consequence are scheduled to take effect on February 10, 2025. As we wrote in our October 2024 alert, these new HSR rules would dramatically increase the information and documents that parties will need to submit with an HSR filing. However, a new lawsuit filed on January 10, 2025, by the U.S. Chamber of Commerce in the U.S. District Court for the Eastern District of Texas seeks to set aside the new rules on the basis that they violate the APA. The Chamber's complaint argues that:

- The information required by the new rules is not "necessary and appropriate" to determine whether the transaction may violate the antitrust laws, as required by the HSR Act.
- The benefits of the new rules are greatly outweighed by the costs they will impose on filing parties.
- The FTC failed to offer sufficient evidence of deficiencies in the current HSR regime to justify a significant departure from longstanding policy.
- The FTC did not sufficiently explain why it could not fill any alleged information gaps through other, more targeted methods.

Plaintiffs have already been successful in challenging the FTC's proposed ban on non-compete agreements, convincing a judge in the U.S. District Court for the Northern District of Texas to set aside that rule in August 2024 (a decision that is currently on appeal). If the Chamber's suit is successful, the new HSR rules would similarly be set aside, and filing parties would continue to use the HSR Form currently in place.

Another avenue of challenge that bears watching is the potential use of the Congressional Review Act ("CRA"). Enacted in 1996, the CRA enables Congress to overturn certain administrative rules after they are promulgated by a federal agency. This procedure requires the passage of a joint resolution of Congress and signature by the President (or a congressional override of his or her veto), so in practice it requires broad bipartisan consensus or, as is now the case, one-party control of the legislative and executive branches.

Importantly, if a rule is overturned pursuant to the CRA, the relevant agency may not issue a substantially similar rule in the future without specific congressional authorization. However, there is a time limitation established by the CRA for disapprovals: Starting on the 15th legislative day of a new session, Congress must act within 60 legislative days or its authority to overturn the rule expires.

Finally, President Trump signed an executive order on January 20, 2025, ordering all executive departments and agencies to "consider postponing for 60 days . . . any rules that have been published in the Federal Register, or any rules that have been issued in any manner but have not taken effect, for the purpose of reviewing any questions of fact, law, and policy that the rules may raise." The new HSR rules meet that description, so depending on whether or not the FTC decides to implement this regulatory freeze, the effective date of the rules could potentially be pushed back to March 20, 2025, or some later date.

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ENDNOTES:

[1] *See* our October 17, 2024, client alert "Final HSR Rules: Major Changes Ahead for Premerger Filings" (https://www.skadden.com/insights/publications/2024/10/final-hsr-rules-major-changes-ahead-for-premerger-filings).

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EXCHANGEABLE SHARE STRUCTURES IN CROSS-BORDER M&A: WHAT U.S. BUYERS OF A CANADIAN TARGET SHOULD KNOW

By Quentin Lageix, Kristian Zimmerman, Enoch Chang, Paul Blyschak and Marco Maduri

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Exchangeable share structures can be a tax-efficient way for U.S. buyers to offer equity consideration to a Canadian seller, and are a valuable tool for U.S. buyers considering the acquisition of a Canadian target. This is particularly true for U.S. private equity buyers, as an exchangeable share structure can help facilitate the rollover of a Canadian seller's equity.

As Canada is regularly among the top five destinations for outbound U.S. transactions by both deal value and volume, we provide a concise overview of this tried and tested deal mechanism that has been a common feature of U.S. investment into Canada for several decades. We also explain why U.S. dealmakers should be familiar with the structure to remain competitive with any Canadian bidders interested in the same target.

Tax-Deferred Treatment

The impetus for a U.S. buyer of a Canadian target agreeing to an exchangeable share structure is tax based. A sale of shares in a Canadian company by a Canadian-resident shareholder, in exchange for shares of a Canadian entity, whether a corporation or a partnership (with only Canadian-resident partners), is generally eligible for tax-deferred treatment when the appropriate election is made under the *Income Tax Act* (Canada).

Where this election is unavailable or otherwise not made, a Canadian resident who disposes of shares of a Canadian company will be considered to have disposed of such shares for proceeds of disposition equal to the fair market value, at the time of the disposition, of the shares acquired in the exchange.

By contrast, Canadian-resident shareholders cannot exchange shares of a Canadian corporation for shares of a U.S. (or other foreign) buyer on a tax-deferred basis under Canadian tax law. Without an exchangeable share structure, Canadian sellers could find themselves with tax liability, while at the same time receiving U.S. buyer stock with little or no liquidity.

The primary benefit for the U.S. buyer is therefore a means to increase the attractiveness of its bid to the Canadian sellers and/or to remain competitive with any Canadian bidders interested in the same target. The primary benefit for the Canadian seller(s) is the ability to secure deferral of Canadian capital gains taxes on the equity consideration received for the sale of the Canadian target to the U.S. buyer. The tax-deferral lasts until the exchangeable shares are exchanged for the corresponding stock in the U.S. buyer, typically on a liquidity event of the buyer (such as a change of control or listing).

U.S. Private Equity Buyers

For private equity buyers, this exchangeable share structure offers the same benefits rollover equity brings, providing: (1) a means to help bridge any valuation gap between the parties, (2) better alignment between management and the sponsor going forward, and (3) improved financing terms through a reduced closing cash payment and lower leverage. Also, if desired, exchangeable shares can be structured to be exchangeable into limited partnership or LLC membership interests, rather than shares of a corporate buyer.

Structure, Entities and Material Rights

An exchangeable share structure can be implemented in different ways, but the essential objective is to provide the Canadian seller(s) with shares in a new Canadian corporation that are the economic equivalent of stock in

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the U.S. buyer (*i.e.*, which mirror all rights attaching to the U.S. buyer's stock, including dividend and liquidation entitlements).

The structure is achieved through the incorporation of two new Canadian corporate entities. First, a direct Canadian subsidiary of the U.S. buyer, typically called "CallCo." Second, a Canadian subsidiary of CallCo or the U.S. buyer, typically called "ExchangeCo."

Upon acquiring the Canadian target, ExchangeCo issues the exchangeable shares—on a tax-deferred basis—to the Canadian sellers. Thereafter, upon any liquidation or dissolution event of the U.S. buyer, the Canadian sellers are entitled to exchange the exchangeable shares for stock in the U.S. buyer on a one-for-one basis. The Canadian sellers are also provided a "retraction right" whereby they can require that ExchangeCo redeem the exchangeable shares for stock in the U.S. buyer on the same basis. Similarly, ExchangeCo has a "redemption right" whereby it can redeem the exchangeable shares, in certain limited circumstances, on the same basis.

CallCo is also provided with an "overriding call right," entitling it to purchase the exchangeable shares from the Canadian sellers in exchange for stock in the U.S. buyer on a one-for-one basis. This purchase right may be preferable to redemption—whether in the case of a liquidation event, retraction or redemption—for avoiding adverse Canadian deemed dividend tax consequences to the Canadian sellers that may arise upon a redemption of the exchangeable shares.

Key Deal Points and Documents

Because the Canadian seller(s) will effectively become stockholder(s) of the U.S. buyer, acquirors should expect corresponding due diligence by the Canadian seller(s), including the review and negotiation of shareholder agreements to which the U.S. buyer is a party, ExchangeCo's constating documents, and the "support and exchange agreement" (discussed below). Due diligence is also necessary to ensure proper alignment from a mechanical perspective.

Key negotiation points can include whether the sellers will be granted, where reasonably viable, special voting rights in the U.S. buyer to put them on the same footing as regular holders of the U.S. buyer's stock, such as through the issuance by the U.S. buyer of special voting stock to a share trustee (or other intermediary), who will hold the special voting shares on behalf of the Canadian sellers. The Canadian sellers, through a share trustee (or other intermediary), may also desire to be made a party to any stockholder (or similar) agreement of the U.S. buyer. The intent here is for the Canadian sellers to benefit from material stockholder rights under such agreements (*e.g.*, rights of first refusal, tag-along rights, access to information rights, and liquidity rights). The U.S. buyer and Canadian sellers may also desire a sunset clause whereby an exchange of the shares is automatically triggered after a set period of time (*e.g.*, 10 years) or upon specified events such as prior to an initial public offering or an adverse change in tax laws.

The Canadian sellers, CallCo and ExchangeCo typically enter into a "support and exchange agreement" with the U.S. buyer. The key terms under this agreement include undertakings by the U.S. buyer to (1) provide ExchangeCo with sufficient funds to pay the Canadian sellers dividends equal to those paid to regular stockholders of the U.S. buyer, and (2) issue stock in itself to satisfy the exchange of the exchangeable shares into its stock, whether upon a liquidation event or the exercise of the seller's retraction right, ExchangeCo's redemption right, or CallCo's call right.

Advantages and Disadvantages

Before deciding to adopt an exchangeable share structure, their advantages and disadvantages in the particular circumstances should be weighed and balanced. At a high level, these include:

Advantages:

- Canadian sellers enjoy the option of tax deferral on the share consideration received, while preserving an economic interest equivalent to direct ownership in the U.S. buyer.

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- It is still possible for U.S. buyers to provide mixed consideration that includes the desired combination of taxable securities of the U.S. buyer and tax-deferred shares of ExchangeCo, which can be desirable when Canadian sellers have tax losses.
- Achieves similar tax treatment between Canadian-resident sellers (who are not otherwise entitled to a tax deferral) and non-Canadian sellers who may be entitled to a tax deferral.
- If properly structured, may allow for earnout/reverse earnout mechanisms to be layered into the acquisition structure while preserving tax deferral for the Canadian sellers.

Disadvantages:

- Exchangeable share structures increase transaction complexity and add costs related to implementation and maintenance, including accounting implications.
- Some sellers may not benefit from the structure's advantages, including non-taxable and non-resident entities and Canadian residents able to deduct losses against the capital gains realized.
- Some additional future complexity is added, *i.e.,* in connection with unwinding the structure or potentially preserving it should any Canadian rollover shareholders be rolled over again.
- Additional considerations and structures may be required to deal with other securities, such as convertible notes issued by the Canadian target, that are to remain outstanding following the closing of the transaction.[1]

Concluding Comments

Canadian buyers are able to offer Canadian sellers equity on a tax deferred basis. As such, to remain competitive in the Canadian market, and particularly in a competitive bid scenario, prospective U.S. buyers should familiarize themselves with exchangeable share structures and the planning, buyer due diligence, and associated negotiation points and deal documents necessary to implement them.

While adopting an exchangeable share structure increases transaction costs, these additional costs may be offset by the competitive gains attained and other potential attendant benefits such as a smaller cash component of the purchase price, reduced debt financing costs and, in the case of a U.S. private equity buyer, synergy between the exchangeable share structure and rollover equity.

ENDNOTES:

[1]For example, by amending the terms of such securities to allow them to be converted into shares of the U.S. buyer (where a taxable transaction is desired) or ExchangeCo (where a tax-deferred transaction is desired)

SECTION 205: INTENT MATTERS

By Kevin Rudolph

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In late August 2024, Vice Chancellor Lori W. Will of the Delaware Court of Chancery issued an opinion in *Falcon I, LLC, et al. v. Golden Mountain Financial Holdings, et al*[1] that will guide corporate counsel and their clients on the use of Section 205 petitions to cure defective corporate acts.

In *Falcon*, private equity fund TS Falcon I notified the Golden Mountain board of its intent to exercise its option to increase its stake in Golden Mountain.[2] Three days later, the Golden Mountain board met in executive session, excluding Falcon's observers, and resolved to reschedule the Golden Mountain annual meeting and set the record date to one day before Falcon attempted to exercise its option.[3] Falcon sued Golden Mountain and its board, seeking a declaration of its voting power under 8 *Del. C. §* 225 and asserting a violation of the annual meeting statute, 8 *Del. C. §* 213(a).[4] As the trial record

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reflected, the Section 213(a) violation was undisputed—a board cannot fix a record date that "precede[s] the date upon which the resolution fixing the record date is adopted."[5]

Golden Mountain answered and filed a petition under 8 *Del. C.* § 205 to validate that clear statutory violation.[6] Section 205 dates back to 2013, and was part of a statutory scheme to permit corporations to ratify otherwise defective corporate acts and stock, curing otherwise incurable voidness.[7] The proposed changes were meant to fix what otherwise were "the draconian effects of prior Delaware case law that made acts void under law incurable in equity."[8]

The statute provides that "no defective corporate act or putative stock shall be void or voidable solely as a result of a failure of authorization if ratified" under Section 204 or Section 205.[9] Section 204 provides for self-help ratification, and Section 205 provides for judicially-approved ratification.

Less than a year after its effective date, the Court of Chancery had the opportunity to interpret the new law in *In re Numoda Corporation Shareholders Litigation*.[10] As the first judicial officer interpreting the new statute, Vice Chancellor Noble took the opportunity to frame what the new statute was and wasn't. Vice Chancellor Noble summarized the new law as allowing the Court "to facilitate correction of mistakes made in the context of a corporate act without disproportionately disruptive consequences."[11] Vice Chancellor Noble cautioned that although the language the General Assembly enacted was seemingly broad, the Court should construe the statute narrowly, and warned practitioners not to read the new statute "as a license to cure just any defect."[12]

Later that same year, Vice Chancellor Parsons issued *In re Genelux Corp.*, in which the Court rejected a petitioner's attempt to use Section 205 to *invalidate* a corporate act.[13] In rejecting the petition, Vice Chancellor Parsons called Section 205 a method "to correct a technical defect and thereby remedy incidental harm."[14] Not a method to invalidate an otherwise valid corporate act.

In the years following *In re Numoda* and *In re Genelux*, practitioners have used and the court has ratified defective corporate acts caused by mistakes in the board room. For example, in *In re 8x8, Inc.*, Chancellor McCormick granted a Section 205 petition where the board had, more than a decade earlier, mistakenly issued a proxy preceding a vote on increasing the amount of authorized shares that contained incorrect information as to that vote.[15] Because the 2012 proxy contained an error, there was uncertainty as to whether the 2012 vote and subsequent stock authorization was valid. The petitioner argued—and the Court agreed—that Section 205 was the appropriate method to cure the board's mistake, which had created intolerable uncertainty about the corporation's capital structure.

Returning to *Falcon*, Golden Mountain sought Section 205 relief to cure its intentional decision to set the record date for the annual meeting to precede the date Falcon gave its notice of intent to exercise its option, thereby curbing Falcon's influence.[16]

In determining whether Section 205 relief was appropriate, the Court first asked whether the defective corporate act fell within the statute—specifically was the petition to cure a failure of authorization?[17] The Court concluded that the defective corporate act was a failure of authorization and thus proceeded to the non-exhaustive list of factors that the General Assembly instructed the Court to evaluate when deciding a Section 205 petition.[18] That list is:

> (1) Whether the defective corporate act was originally approved or effectuated with the belief that the approval or effectuation was in compliance with the provisions of this title, the certificate of incorporation or bylaws of the corporation; (2) Whether the corporation and board of directors has treated the defective corporate act as a valid act or transaction and whether any person has acted in reliance on the public record that such defective corporate act was valid; (3) Whether any person will be or was harmed by the ratification or validation of the defective corporate act, excluding any harm that would have resulted if the defective corporate act had been valid when approved or effectuated; (4) Whether any person will be harmed by the failure to ratify or validate the defective corporate act; and (5) Any other factors or considerations the Court deems just and equitable.[19]

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Applying those factors, the Court concluded:

- Factor #1 (belief in validity) weighed heavily against ratification because Golden Mountain "purposefully" sought to set the record date to a time before Falcon gave its notice of intent.[20]
- Factor #2 (treatment of the act as valid) weighed in favor of ratification but weighed in favor only slightly because (1) Golden Mountain's defective act had only been treated as valid for a "short time in connection with a single" transaction, and (2) Golden Mountain's violations were "flagrant."[21]
- Factor #3 (harm from validation) weighed against ratification because there was a "non-zero risk of harm" to Falcon if the defective ratification date was ratified.[22]
- Factor #4 (harm absent validation) weighed in favor of ratification because, at the very least, the corporation would need to send a new proxy and hold a new annual meeting, which would create additional expenses.[23]
- Factor #5 (other considerations) did not apply.

Weighing the factors together, the Court concluded that Section 205 relief was not warranted.[24] Of particular note, the Court placed significant weight on the first two factors, and the first factor most of all. The Court's finding about Golden Mountain's intent led the Court to give less weight to the second factor. Specifically, the Court found that although the second factor weighed in favor of ratification, the temporal duration and "*flagrant violation*" gave less weight to that factor.[25]

Given the seeming proliferation of Section 205 petitions and in light of *Falcon* and recent Section 205 case law, practitioners should take note that:

- **Satisfying Factor #1 is paramount.** The Court in *Falcon* gave Factor #1 the greatest weight and applied the conclusions it made under Factor #1 when evaluating the other four factors.
- **Factor #1 is intent dependent.** The Court in *Falcon* found that Golden Mountain *intended* to set the retroactive record date to prohibit Falcon from exercising its option.[26] It was that intent that led the Court to conclude Golden Mountain could not have believed it was following Section 213(a).[27] But what if a future petitioner had set a retroactive record date due to a scrivener's error? The defect would be the same, but the intent, and likely the Court's reception, would be different.
- **Mistakes happen.** As the Court in *Falcon* implied, Section 205 can fix a "foot fault," but not an intentional act meant to limit or harm an identified person or entities' rights.[28]

Practitioners should first examine the intent of the petitioner when the petitioner was pursuing the defective corporate act. If the defective corporate act was the product of a mistake, then Section 205 will likely be an appropriate remedy. If the defective corporate act was the product of an attempt to limit or harm an identified person or entities' rights, then Section 205 will likely not be an appropriate remedy.

To note, practitioners should also be aware that Section 205 is not a cure-all. It can cure statutory violations, but it cannot cure common law fiduciary duty violations. Applied here, whether the resolution setting the record and annual meeting dates violated Section 213(a) or not, Section 205 cannot protect against a claim for breach of fiduciary duty for taking those actions.[29]

ENDNOTES:

[1]*TS Falcon I, LLC v. Golden Mountain Financial Holdings Corp.*, 2024 WL 3942255 (Del. Ch. 2024), judgment entered, 2024 WL 4182881 (Del. Ch. 2024).

[2]*Id.* at *3.

[3]*Id.*

[4]*Id.* at *4.

[5]*Id.*; 8 *Del. C. §* 213(a).

[6]*TS Falcon I, LLC v. Golden Mountain Financial Holdings Corp.*, 2024 WL 3942255, at *4 (Del. Ch. 2024), judgment entered, 2024 WL 4182881 (Del. Ch.

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2024).

[7]John W. Noble, *Fixing Lawyers' Mistakes: The Court's Role In Administering Delaware's Corporate Status*, 18 U. Pa. J. Bus. L. 293, 310 (2016).

[8]Kathaleen S. McCormick & Daniel M. Kirshenbaum, *Key Decisions of 2015 In Delaware Corporate Law*, 16 Del. L. Rev. 91, 147 (2016) (citing *In re Genelux Corporation*, 126 A.3d 644, 667 (Del. Ch. 2015), vacated in part, 143 A.3d 20 (Del. 2016) (TABLE)); C. Stephen Bigler & John Mark Zeberkiewicz, *Restoring Equity: Delaware's Legislative Cure For Defects In Stock Issuances And Other Corporate Acts*, 69 Bus. Law. 393, 394-402 (2014).

[9]8 *Del. C. §* 204(a); Del. H.B. 127, 147th Gen. Assem., 79 Del. Laws ch. 72 (2013).

[10]*In re Numoda Corporation Shareholders Litigation*, 2015 WL 402265 (Del. Ch. 2015), judgment entered, 2015 WL 1056143 (Del. Ch. 2015) and judgment aff'd, 128 A.3d 991 (Del. 2015) (TABLE).

[11]*Id.* at *8.

[12]Id.

[13]*In re Genelux Corporation*, 126 A.3d 644 (Del. Ch. 2015), vacated in part, 143 A.3d 20 (Del. 2016) (TABLE).

[14]*Id.* at 669.

[15]*In re 8x8, Inc.*, C.A. No. 2024-0154-KSJM, Dkt. 7 (Del. Ch. Apr. 4, 2024); *see id.*, Dkt. 1 (Del. Ch. Feb. 20, 2024).

[16]*TS Falcon I, LLC v. Golden Mountain Financial Holdings Corp.*, 2024 WL 3942255, at *4 (Del. Ch. 2024), judgment entered, 2024 WL 4182881 (Del. Ch. 2024).

[17]*Id.* at *5.

[18]*Id.* at *5-6.

[19] 8 *Del. C. §* 205(d).

[20]*Id.* at *6-7.

[21]*Id.* at *8.

[22]*Id.*

[23]*Id.*

[24]*Id.*

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

[26]*Id.* at *6.

[27]*Id.*

[28]*See TS Falcon I, LLC v. Golden Mountain Financial Holdings Corp.*, 2024 WL 3942255, at *9 (Del. Ch. 2024), judgment entered, 2024 WL 4182881 (Del. Ch. 2024); *see, e.g.*, *In re Lordstown Motors Corp.*, 290 A.3d 1, 12-13 (Del. Ch. 2023); *In re Mullen Auto. Inc. S'holder Litig.*, C.A. No. 2022-1131-LWW, at 58 (Del. Ch. June 8, 2023) (TRANSCRIPT); John W. Noble, *Fixing Lawyers' Mistakes: The Court's Role In Administering Delaware's Corporate Status*, 18 U. Pa. J. Bus. L. 293, 310 (stating Section is "a means to fix a mistake, to correct a wrong, or to arrive at a fair and just outcome"); *id.* at 314 ("this legislation provides methods for correcting mistakes").

[29]*See* H.B. 127 syn., 147th Gen. Assem. (2013) ("Ratification of a defective corporate act under § 204 is designed to remedy the technical validity of the act or transaction; it is not intended to modify the fiduciary duties applicable to either the approval or effectuation of a defective corporate act or transaction or any ratification of such act or transaction. Defective corporate acts, even if ratified under this section, are subject to traditional fiduciary and equitable review.").

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FROM THE EDITOR

Continuity Amidst Disruption

President Trump has begun his second term with a seemingly endless flurry of executive orders, with which he intends to transform how Washington has operated in the past few decades. For M&A antitrust enforcement, however, there have been more signs of continuity with the outgoing administration than there have been severe breaks in policy—at least so far.

It's still early days, of course. Gail Slater, the president's nominee to lead DOJ's Antitrust Division, has yet to be confirmed. However, Omeed Assefi, who was appointed the temporary DOJ antitrust head, recently offered a measure of approval for the Biden administration's antitrust efforts. Reportedly, Assefi, who worked in the first Trump administration, told antitrust staff that he would continue the previous administration's "aggressive" stance in re antitrust and that there would reportedly be no "relaxation" of enforcement.

Another sign of continuity: the DOJ suing to block Hewlett Packard Enterprise's $14 billion acquisition of Juniper Networks—a deal investigated under the Biden administration and, as of now, a challenge allowed to proceed by the Trump administration.

Unlike more novel antitrust theories advanced by Biden regulators, the DOJ's case here is a standard argument that HPE regarded Juniper, which sells an AI-fueled technology called Mist, as a threat to its business and embarked on an acquisition to remove a prime competitor from the board, with potential negative results for wireless tech consumers in terms of pricing and competitive offerings.

"The threat this merger poses is not theoretical. Vital industries in our country—including American hospitals and small businesses—rely on wireless networks to complete their missions. This proposed merger would significantly reduce competition and weaken innovation, resulting in large segments of the American economy paying more for less from wireless technology providers," Assefi said in a statement announcing the DOJ's case. Should the deal go through, the DOJ claimed it could create a duopoly, with HPE/Juniper and Cisco Systems controlling over 70% of the U.S. market, the DOJ claimed, and thus "decreas[ing] pressure on HPE to discount and innovate in the future."

HPE pushed back by claiming that U.S. antitrust enforcers define the wireless tech market too narrowly, and that HPE faces stiff competition from many wireless networking companies. In an interview, HPE CEO Antonio Neri said the DOJ's case is flawed "because they think there is a market of three going down to two vendors. [But] there are at least three or four that have the exact same market share as Juniper. . .The barriers to compete are very low, and they are all disrupters."

Chris O'Leary

Managing Editor

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