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EXPERT ANALYSIS

Delaware Curbs Frivolous Merger Suits With More Critical Review of Disclosure-Only Pacts

By Gardner Davis, Esq., and Neda Sharifi, Esq.
Foley & Lardner

The Delaware Chancery Court, in a recent memorandum decision, *In re Riverbed Technology Inc. Stockholders Litigation*, 2015 WL 5458041 (Del. Ch. Sept. 17, 2015), has taken a long-overdue step toward curbing frivolous litigation in big-ticket mergers and acquisitions.

The court promised greater judicial scrutiny of the common practice of settling quickly by agreeing to make supplemental disclosures in the merger proxy statement — which are of no meaningful value to stockholders — and to pay a generous fee to plaintiffs' counsel. In exchange, defendants typically receive a global release from all potential claims.

The proliferation of stockholder litigation challenging mergers involving publically traded target companies is well docu-mented.[1] In 2013 plaintiffs filed lawsuits challenging 97.5 percent of deals valued at more than $100 million, and each of those transactions triggered seven separate lawsuits, on average.[2] In the great majority of these cases, the plaintiffs' lawyers were the greatest beneficiaries. Almost all the cases that survive a motion to dismiss are quickly settled without any money being paid to the stockholders. In 81 percent of the lawsuits filed in 2012, the defendants settled by agreeing only to provide supplemental disclosure in the merger-related proxy statement.[3] Another 13 percent settled by agreeing to make changes to the merger agreement, most often to the deal-protection provisions, but with no additional money paid to stockholders.[4]

In disclosure-only settlements, plaintiffs' lawyers received an average fee of about $500,000.[5]

Although plaintiffs' lawyers claim the additional disclosures provide value to stockholders, in fact the disclosures don't appear to make any difference at all. A recent empirical study of 453 mergers announced between 2005 and 2012 found that the additional disclosures provided by disclosure-only settlements had no impact, positive or negative, on the stockholder vote, suggesting the additional disclosures were a complete waste of resources.[6]

In several recent rulings from the bench, members of the Delaware Chancery Court have questioned what benefit disclosure-only settlements provide to stockholders and whether the benefit justified the global releases typically provided to defendants.[7]

Against this backdrop, *Riverbed* recently came before the Delaware Chancery Court. The question before the court stemmed from settlement of a class-action lawsuit brought by the stockholders of Riverbed Technology Inc. in connection with the company's acquisition by Thoma Bravo LLC and Teachers' Private Capital, an affiliate of Ontario Teachers' Pension Plan, for around $3.6 billion. The plaintiffs initially sought to enjoin the merger, alleging that the sale process undervalued the company and had been tainted by conflicts of interest. The plaintiffs also raised a number of disclosure claims, some of which were mooted by the definitive proxy.

EXPEDITED DISCOVERY, QUICK SETTLEMENT

Shortly after filing the definitive proxy, the Chancery Court granted expedited discovery on the claims regarding disclosure of potential conflicts of interests regarding Goldman Sachs, a financial adviser to Riverbed. About 10 days later, the parties executed a settlement agreement pursuant to which the company made supplemental disclosures in the SEC filings prior to the stockholder vote on the merger. As part of the deal, the defendants received a broad release of all known and unknown potential claims arising from the transaction, including claims both under fiduciary common law and federal statutory law. The deal awarded a fee of $500,000, representing $713 per hour, to plaintiffs' counsel.

However, *Riverbed Technologies* differed from the usual case in one significant way. In *Riverbed*, Sean Griffith, a law professor who has written about the merger litigation problem, purchased stock in the company and objected to both the settlement and award of attorney fees. Griffith argued that "like other disclosure-only settlements, the parties here propose to trade an expansive global release for supplemental disclosures … that provided no value to the [stockholders]."[8]

Vice Chancellor Sam Glasscock III's ruling focused on "the motivations of counsel for the class representative in prosecuting [M&A stockholder class action] litigation, and how the interests of the attorney, and the class representative plaintiff, diverge from that of the corporate shareholders."

The additional disclosure was of virtually no practical value to the Riverbed stockholders, the Vice Chancellor wrote.

First, the Vice Chancellor examined the settlement's benefit to stockholders. The additional disclosure was of virtually no practical value to the Riverbed stockholders, the Vice Chancellor wrote, pointing out that among the shares voting on the merger, 99.48 percent voted in favor of the merger despite the disclosures. In fact, some of the additional disclosures produced by the settlement arguably made the transaction more attractive to stockholders.[9]

Next, the court looked at the potentially divided loyalties facing the lawyer represent-ing the plaintiff class: "A plaintiff's attorney may favor a quick settlement where the additional effort required to fully develop valuable claims on behalf of the class may not generate an additional fee as lucrative to the plaintiff's attorney as accepting a quick and moderate fee, then pursuing other interests. The interest of the principal — the individual plaintiff/stockholder — is often so small that it serves as scant check on the perverse interest described above, notwithstanding that the aggregate interest of the class and pursuing litigation may be great — the very problem that makes class litigation appropriate in the first instance."[10]

'CONFLICTED' INTERESTS

Vice Chancellor Glasscock then pointed out the conflicted and somewhat counter-intuitive interest of the defendants in the context of disclosure-only settlements: "[t]he adversarial system provides little comfort that mal-alignments between the interests of the class and its counsel resulting from perverse incentives will be revealed and addressed, because the defendants' interest is largely subsumed within that of the successor entities' interest, which is commonly in the consummation of the deal and the termination of any further litigation threat. Where the defendants' interest may be captured via a broad release, inexpensive disclosures and a modest — in light of the value of the merger — fee award, there is little incentive for the defendants to engage in further litigation even if the claims are weak; and every reason to go forward to obtain by settlement what one member of this court has deemed 'deal insurance,' the broadest release possible."[11]

SELF-INTEREST ON BOTH SIDES

According to this line of thinking, the self-interest of both the plaintiffs lawyers and defendants have contributed to the flood of frivolous merger litigation. Stockholders are the only real losers in this legal frenzy, as potentially meritorious claims are probably being released without serious examination or any meaningful benefit to the stockholders.

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Vice Chancellor Glasscock noted that "[i]n combination, the incentives of litigants may be inimical to the class: the individual plaintiff may have little actual stake in the outcome, her counsel may rationally believe a quick settlement and modest fee is in his best financial interest, and the defendant may be happy to 'purchase,' at the bargain price of disclosures of marginal benefit to the class and payment of the plaintiffs' attorney fees, a broad release from liability."[12]

To counteract the assertion that stockholders received dubious value in the settlement, plaintiff's counsel strenuously argued that although the fiduciary duty claims in the complaint were robust, the plaintiff's expert could not opine that the merger price was unfairly low.

Therefore, while the settlement released viable fiduciary duty claims, they were not claims that would have resulted, if pursued, in any benefit to the stockholders. Further, plaintiff's counsel represented that he did not identify any viable claims under federal securities laws. Put another way, plaintiff's counsel appeared to concede that the claims were frivolous and presumably should never have been pursued in the first place. As Vice Chancellor Glasscock more diplomatically noted: "According to the plaintiffs, the 'give' from the class in connection with the settlement was basically nil."

In opposing the settlement Griffith argued that there may be valuable unknown claims extinguished by the release and that the lack of a full record should cause the court to reject the settlement, leaving the parties to pursue further litigation or attempt to reach a settlement with a much narrower release. Vice Chancellor Glasscock found that "this, in light of the rather meager benefit achieved by the settlement for the class, as well as the broad release bargained for, is a serious objection."

Vice Chancellor Glasscock telegraphed that he might accept this objection in the future: "In another factual scenario it might well carry the day."[13]

The defendant may be happy to 'purchase,' at the bargain price of disclosures of marginal benefit to the class and payment of the plaintiffs' attorney fees, a broad release from liability, the judge said.

NOT BUSINESS AS USUAL

Vice Chancellor Glasscock approved the settlement in the *Riverbed* litigation because "given the past practice of this court in examining settlements of this type, the parties in good faith negotiated a remedy — additional disclosures — that has been consummated, with the reasonable expectation that a very broad, but hardly unprecedented release negotiated in return would be approved by this court."[14] However, Vice Chancellor Glasscock sent the loud and clear message that this reliance on past practice will not carry the day in the future: "I note that factor, while it bears some equitable weight here, will be diminished or eliminated going forward in light of this memorandum opinion and other decisions of this court."[15]

And Vice Chancellor Glasscock noted that, notwithstanding the unique circumstances of this case, "the breadth of the release is troubling. It is hubristic to believe that upon this record I can properly evaluate, and dismiss as insubstantial, all potential federal and state claims. If it were not for the reasonable reliance of the parties on formerly settled practice of this court, … the interests of the class might merit rejection of a settlement encompassing a release that goes far beyond the claims asserted and the results achieved. However, in the specific circumstances presented, I find the settlement fair to the class and approve it."

The vice chancellor reduced the $500,000 fee award agreed upon by the parties in the settlement to $300,000 because "the result is too modest a benefit to justify the fees sought." He specifically noted that his decision "will incentivize the amount and quality of litigants that will follow in similar cases." And the vice chancellor suggested that the *Riverbed* award might be larger than otherwise warranted because "expectations reasonably based upon prior court practice are entitled equitable consideration."[16]

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TAKEAWAYS

The take-away from Vice Chancellor Glasscock's *Riverbed* opinion, particularly considered in conjunction with other unreported bench rulings, is that plaintiffs lawyers and defense counsel can no longer rely on the Chancery Court's formerly settled practice of routinely approving disclosure-only settlements which provide for global releases that go far beyond the claims asserted and the results achieved. Moreover, the dubious benefits that stockholders receive from these settlements will no longer support the generous legal fees historically awarded to plaintiff's counsel. Collectively, we hope these changes will strengthen defendants' resolve to resist frivolous litigation and force plaintiffs' lawyers to be more selective in deciding which merger challenges to pursue.

NOTES

[1] Robert M. Daines & Olga Kopumrian, Cornerstone Research, Shareholders Litigation Involving Mergers And Acquisitions, *available at* http://cornerstone.com/Publications/Reports/shareholder-Litigation-Involving-Mergers-and-Acqui; Matthew D. Cain & Steven M. Davidoff, Takeover Litigation in 2013, Moritz Coll. Of Law Ctr. For Interdisciplinary Law and Policy Studies, Public Law and Legal Theory Working Paper Series No. 236, 2014, *available at* http://ssrn.com/abstract=2377001; Jill E. Fisch, Sean J. Griffith and Steven Davidoff Solomon, *Confronting The Peppercorn Settlement in Merger Litigation: An Empirical Analysis & A Proposal For Reform,* 93 Tex. L. Rev 557 (February 2015); Sean J. Griffith, *Correcting Corporate Benefit: How to Fix Shareholder Litigation By Shifting The Doctrine on Fees,* 56 B. C. L. Rev 1 (January, 2015); Sean J. Griffith & Alexandra D. Lahav, The Market for Preclusion in Merger Litigation, 66 VAND. L. Rev. 1053 (2013).

[2] Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting The Peppercorn Settlement in Merger Litigation: An Empirical Analysis and A Proposal For Reform,* 93 Tex. L. Rev 557, 559 (February 2015), citing Matthew D. Cain & Steven M. Davidoff, "Takeover Litigation in 2013, Moritz Coll. Of Law Ctr. For Interdisciplinary Law and Policy Studies, Public Law and Legal Theory Working Paper Series No. 236, 2014, *available at* http://ssrn.com/abstract=2377001.

[3] Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting The Peppercorn Settlement in Merger Litigation: An Empirical Analysis and A Proposal For Reform,* 93 Tex. L. Rev 557, 566 (February 2015), citing Robert M. Daines & Olga Kopumrian, Cornerstone Research, *Shareholders Litigation Involving Mergers And Acquisitions, available at* http://cornerstone.com/Publications/Reports/shareholder-Litigation-Involving-Mergers-and-Acqui.

[4] Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting The Peppercorn Settlement in Merger Litigation: An Empirical Analysis & Proposal For Reform,* 93 Tex. L. Rev 557, 566 (February 2015), citing Sean J. Griffith & Alexandra D. Lahav, *The Market for Preclusion in Merger Litigation,* 66 VAND. L. Rev. 1053, 1093(2013).

[5] Jill E. Fisch, Sean J. Griffith & Steven Davidoff Solomon, *Confronting The Peppercorn Settlement in Merger Litigation: An Empirical Analysis & a Proposal for Reform,* 93 Tex. L. Rev 557, 568 (February 2015).

[6] *Id.*

[7] *In re Susser Holdings Corp. S'holder Litig.,* No. 9613-VCG (Del. Ch. Sept 15, 2015). *Acevedo v. Aeroflex Holding Corp.,* No. 9730-VCL (Del Ch. July 8, 2015); *In re Intermune Inc. S'holder Litig.,* No. 10086-VCN (Del. Ch. Jul 8, 2015).

[8] Objection of Sean Griffith to Proposed Settlement & Application for Attorneys' Fees and Expenses filed in *Riverbed Tech. Stockholders Litig.*

[9] *In re Riverbed Tech. Stockholders Litig.,* 2015 WL 5458041 at *5 (Del. Ch. Sept. 17, 2015).

[10] *Id.* at *3.

[11] *Id., see In re InterMune Inc. S'holder Litig.,* No. NL 10086-VCN (Del. Ch. Jul 8, 2015).

[12] *In re Riverbed Tech. Stockholders Litig.* at *4.

[13] *Id.* at *6.

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[14] *Id.*

[15] *Id.* at *6. *See* generally *In re Susser Holdings Corp. S'holder Litig.,* No. 9613-VCG (Del. Ch. Sept. 15, 2015); *Acevedo v. Aeroflex Holding Corp.,* No. 9730-VCL (Del. Ch. July 8, 2015); *In re InterMune Inc. S'holder Litig.,* No. 10086-VCN (Del. Ch. July 8, 2015).

[16] *Id.* at *7.


Gardner Davis (L) is a partner in the transactional & securities practice of **Foley & Lardner**. He frequently represents buyers and sellers in M&A transactions and advises boards of directors and special committees in regard to fiduciary duty issues in various contexts. He be reached at (904) 359-8726 or gdavis@foley.com. **Neda Sharifi** (R), an associate with Foley & Lardner, focuses her practice on corporate and securities laws matters, including M&A and securities law compliance counseling. She can be reached at (904) 359-8719 or NSharifi@foley.com.

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