Second Quarter 2015

The Ropes Recap

Mergers & Acquisition Law News

A quarterly recap of mergers and acquisition law news from the M&A team at Ropes & Gray LLP.

Contents

News from the Courts

Delaware Chancery Court Finds That Dispute Over Accounting Methodology Is Subject to Arbitration Procedures

Post-closing purchase price and working capital adjustments are common in mergers and acquisitions, as are disputes between the transaction parties regarding such adjustments. Given the technical nature of these provisions, transaction agreements often provide that these disputes are to be resolved by a neutral arbitrator, such as an independent accounting firm, instead of courts through traditional litigation. In *Alliant Techsystems, Inc. v. MidOcean Bushnell Holdings, L.P.*, the Chancery Court decided a case in which the parties contested the question of whether their dispute over accounting methodology, arising in connection with working capital adjustment procedures, was to be heard by an independent accounting firm or a court. This opinion, together with other recent Delaware cases considering arbitration provisions, such as *Weiner v. Milliken Design, Inc.* and *Garda USA v. SPX* described in the First Quarter 2015 and 2013 editions of the Ropes Recap, respectively, highlights the need for drafters to carefully consider the scope of review that arbitrators may undertake in resolving disputes over purchase price adjustments.

The dispute arose as parties were working through the post-closing purchase price adjustment mechanics set out in the purchase agreement. Alliant Techsystems, Inc. ("ATK") challenged MidOcean Bushnell Holdings L.P.'s estimate of net working capital, contending that MidOcean's estimate did not comply with GAAP. When the parties could not reach an agreement on the net working capital amount, ATK sought to have an independent accounting firm arbitrate the dispute, as provided for by the purchase agreement's provisions governing the purchase price adjustment process. MidOcean countered that disputes over accounting methodology had to be resolved by a court under the Agreement's indemnification provisions. According to MidOcean's theory, ATK needed to allege that MidOcean breached its contractual representations that the financial statements were prepared in accordance with GAAP, and could not bring such a dispute under the agreement's purchase price adjustment provisions. ATK asked the Chancery Court to order specific performance, compelling MidOcean to submit the accounting dispute to arbitration, while MidOcean sought a declaration that the dispute be resolved under the agreement's indemnification provisions.

Chancellor Bouchard found in favor of ATK, finding that the agreement required the parties to submit their dispute to arbitration. The Chancellor observed that the agreement required MidOcean's pre-closing estimate of net working capital to conform to the definition of "net working capital" in the agreement, and this definition provided that net working capital was to be "calculated in accordance with GAAP and otherwise in a manner consistent with the practices and methodologies used in the preparation of the Financial Statements." Therefore, in preparing its post-closing calculation of net working capital, also in accordance with the definition of "net working capital" in the agreement, ATK was not bound to follow the methodology used in the

Financial Statements to the extent that such methodology was not consistent with GAAP, and the resulting discrepancy in the parties' net working capital calculations properly fell within the purchase price adjustment procedures of the agreement. Given this conclusion, the provision in the agreement stating that purchase price disputes must be arbitrated by an accounting firm applied, and the court entered an order for specific performance, compelling the parties to submit their dispute to arbitration. In reaching this decision, Chancellor Bouchard rejected claims from MidOcean that the parties intended for the accounting firm to resolve only issues of "pure mathematics," that an exclusive remedy provision in the Agreement's indemnification provisions should have governed the dispute and that prior precedents required disputes over accounting methodologies to be decided under indemnification provisions in acquisition agreements.

This decision highlights the care that practitioners must use in crafting purchase price adjustment provisions in order to prevent unwanted outcomes with respect to post-closing disputes. Parties may wish to specify in the purchase price adjustment provisions whether questions of accounting methodology will be resolved using the arbitration mechanism or by the courts .

Alliant Techsystems Inc. v. MidOcean Bushnell Holdings LP, C.A. No. 9813-CB (Del Ch. Apr. 24, 2015, rev. Apr. 27, 2015).

Delaware Supreme Court Finds Purchaser Did Not Breach Earn-Out Provision

In *Lazard Technology Partners, LLC v. Qinetiq North America Operations LLC*, the Delaware Supreme Court upheld a Chancery Court ruling holding that a purchaser did not violate the terms of a merger agreement's earn-out provision.

The case concerned a merger agreement through which Qinetiq North America acquired Cyveillance, a cyber technology company. The agreement provided for a $40 million up-front payment, plus up to another $40 million if Cyveillance's revenues reached a specified level (the "Earn-Out Payment"). The agreement also included a provision that prohibited Qinetiq from taking "any action to divert or defer [revenue] with the intent of reducing or limiting the Earn-Out Payment."

After Cyveillance failed to achieve sufficient revenue to generate an Earn-Out Payment, former Cyveillance stockholders sued, alleging that Qinetiq failed to take actions that would have caused the Cyveillance's revenue to reach the Earn-Out threshold. The stockholders also contended that Qinetiq violated the implied covenant of good faith and fair dealing by failing to take such actions. The Chancery Court rejected those claims, finding that the plaintiff had not proven that any of Qinetiq's business decisions were motivated by a desire to avoid an Earn-Out Payment.

On appeal, the Supreme Court upheld the Chancery Court's ruling. In so doing, the Supreme Court rejected the stockholders' contention that Qinetiq was prohibited from taking actions that it knew would negatively affect the likelihood that the stockholders would receive the Earn-Out Payment. The Court noted that the relevant contractual provision required "intent" to reduce or limit the Earn-Out Payment, which only precluded conduct that was, at least in part, "specifically motivated by a desire to avoid the earn-out." Conversely, the agreement did not prohibit acting with mere knowledge that Qinetiq's conduct may limit the Earn-Out Payment.

The Court also rejected the stockholders' claim that Qinetiq violated the implied covenant of good faith and fair dealing. The Court noted that, in the course of negotiating the merger agreement, the sellers attempted to negotiate for several affirmative post-closing obligations, and Qinetiq rejected all of these attempts, with the parties instead agreeing to the general prohibition against actions taken with the intent of reducing the Earn-Out Payment. Given this history, the Court refused to apply the implied covenant to give the stockholders the protections that they had failed to obtain when they negotiated the agreement.

The *Qinetiq* opinion highlights the Court's willingness to rely on the language of the contract, rather than give effect to extra-contractual claims. Additionally, the opinion demonstrates that the Delaware courts will look skeptically at attempts to use the implied covenant of good faith and fair dealing to prevail on points that a party was unable to win at the negotiating table.

Lazard Technology Partners, LLC v. Qinetiq North America Operations LLC, No. 464, 2014 (C.A. No. 6815-VCL) (Del. Apr. 23, 2015).

Delaware Chancery Court Closely Scrutinizes Director Compensation

In a recent Chancery Court opinion (*Calma v. Templeton)*, Chancellor Bouchard applied the entire fairness standard of review in principally denying director defendants' motion to dismiss a derivative plaintiff's challenge to equity compensation awards issued to the non-employee directors of Citrix Systems, Inc.

The lawsuit was initiated by an individual Citrix stockholder, who challenged the award of certain restricted stock units to Citrix's non-employee directors between 2011 and 2013. Those RSUs were issued pursuant to the company's 2005 Equity Incentive Plan, which had been approved by the Citrix stockholders. However, that equity compensation plan did not state the amount or form of compensation that could be awarded to non-employee directors, specifying only that no plan beneficiary could receive more than one million RSUs in any given year.

Between 2011 and 2013, all determinations concerning director compensation were made by the compensation committee of the Citrix board of directors. The committee was composed exclusively of non-employee directors, who thus determined their own compensation. During that time period, the committee awarded over $1 million in cash compensation and RSUs to the company's non-employee directors, which the plaintiff contended was excessive in comparison with director compensation at peer corporations. The plaintiff filed derivative breach of fiduciary duty and corporate waste claims against the directors, and the directors in turn moved to dismiss those claims on the basis that such payments were previously ratified by the company's stockholders.

The Court first concluded that the stockholder plaintiff did not have to make a pre-suit demand on the Citrix board requesting that they pursue claims relating to the RSU grants. Rather, demand was excused because the Citrix directors were "interested" with respect to claims that concerned those directors' compensation. The Court also did not require the plaintiff to show that the RSUs were material to the company's non-employee directors, because "the law is skeptical that an individual can fairly and impartially consider whether to have the corporation initiate litigation challenging his or her own compensation, regardless of whether or not that compensation is material on a personal level."

The Court then found that more than half of the directors who approved the challenged compensation awards were not disinterested with respect to those awards. Stating that "self-compensation decisions are conflicted transactions that 'lie outside of the business judgment rule's presumptive protection,'" the Court determined that such decisions must be reviewed under the entire fairness standard, which requires the directors to establish that the transaction at issue was the product of fair dealing and was effected at a fair price. The Court did, however, distinguish between director self-compensation decisions and disinterested directors approving the compensation of other directors, which decisions would be presumed to be subject to the business judgment rule.

Seeking to avoid the entire fairness standard of review, the director defendants argued that the stockholders had ratified the 2005 Equity Incentive Plan pursuant to which the challenged compensation had been awarded. However, a ratification defense is typically available only where the stockholders have approved a "specific decision." Chancellor Bouchard concluded that the Citrix stockholders had not ratified the challenged compensation because the 2005 Equity Incentive Plan did not establish any specific amounts of director compensation or set any meaningful limits on the compensation that any beneficiary could receive in a given year. Chancellor Bouchard noted the policy benefits of companies seeking stockholder approval of specific aspects of director compensation, which "ensure[s] integrity in the underlying principal-agent relationship."

To protect against stockholder challenges to compensation paid to directors, companies should consider including realistic limits, such as dollar value caps, on non-employee director equity grants under stockholder-approved equity plans, which would help directors establish a ratification defense against director compensation-related claims.

Calma v. Templeton, C.A. No. 9579-CB (Del. Ch. April 30, 2015).

Delaware Chancery Court Finds Restriction on Poison Pills Under Prior Parent Corporation's Settlement Agreement Does Not Necessarily Apply to Spun-Off Entity

In *Miramar Police Officers' Retirement Plan v. Murdoch*, Chancellor Bouchard rejected a stockholder's challenge to a stockholder rights plan adopted by News Corporation, finding that a settlement agreement entered into by its former parent entity was not binding upon News Corporation.

This case originated with a 2006 settlement agreement between News Corporation ("Old News Corp") and its stockholders, in which Old News Corp agreed that, for the 20-year period following the date of the settlement agreement, Old News Corp would not maintain a stockholder rights plan for longer than one year without obtaining stockholder approval.

In 2013, Old News Corp transferred its newspaper and publishing business to a wholly-owned subsidiary ("New News Corp") and then spun off New News Corp to its stockholders, pursuant to the terms of a Separation and Distribution Agreement. Later in 2013, the New News Corp board adopted a one-year stockholder rights plan, and subsequently extended that plan for an additional year without obtaining stockholder approval of the plan. Plaintiff, a New News Corp stockholder, brought an action against New News Corp, arguing that New News Corp, as a transferee or assignee of Old News Corp, was bound by the terms of the settlement agreement and thus prohibited from extending the term of the rights plan without stockholder consent.

Chancellor Bouchard's ruling included a detailed review of both the settlement agreement and the separation agreement. The settlement agreement provided that the terms of the agreement would be binding upon the "transferees, successors and assigns" of Old News Corp and upon "any corporation, partnership, or other entity into or with which any party or person may merge or consolidate." The Court noted that this language identified several types of corporate transactions that would result in a non-party entity being bound by the settlement agreement. However, a spin-off was not one of those identified transactions, suggesting the parties did not intend to include a spin-off within the scope of that provision. The Court also rejected a claim that the assignment of Old News Corp assets to New News Corp made New News Corp a transferee or assignee for purposes of the settlement agreement. The Court noted that such a broad interpretation would lead to absurd results, by making any party that acquired assets from Old News Corp subject to the settlement agreement. Instead, the Court found that New News Corp would only be subject to the settlement agreement if Old News Corp specifically assigned its rights and obligations under the settlement agreement to New News Corp.

The Court next reviewed the terms of the separation agreement to determine whether the settlement agreement was assigned to New News Corp as part of the spin-off transaction and determined that it was not so assigned.

Based on that analysis, the Court found that New News Corp was not bound by the terms of the settlement agreement, and dismissed the plaintiff's claims.

This opinion clarifies that the Delaware courts are reluctant to apply contractual obligations to spun-off entities, absent a clear contractual basis in the spin-off documents for doing so.

Miramar Police Officers' Retirement Plan v. Murdoch, C.A. No. 9860-CB (Del. Ch. Apr. 7, 2015).

Board's Refusal to Seat a Director Represented by Opposing Litigation Counsel is Consistent with its Fiduciary Duty

In a recent case (*Partners Healthcare Solutions Holdings L.P., et al.* v. *Universal American Corp.),* Vice Chancellor Glasscock held that a party's refusal to seat a major stockholder's board designee represented by opposing litigation counsel was consistent with the board's fiduciary duties and did not constitute a breach of the company's Board Seat Agreement with the stockholder.

Partners Healthcare Solutions Holdings L.P. had sold a subsidiary to Universal American Corp. As part of that transaction, Partners became one of Universal's largest stockholders and was entitled to designate a director to the board of Universal pursuant to a Board Seat Agreement. After the closing, the subsidiary performed poorly, and Universal brought fraud claims against Partners. After Partners' initial board designee resigned, Partners sought to seat a successor designee to the board, but Universal refused to seat the director until he signed an agreement that the firm representing Partners in the litigation would not advise him in his director role. The director refused to sign the agreement. Partners and Universal eventually settled the dispute by arranging for the law firm to enact an ethical wall between the attorneys advising the director and the attorneys involved in the litigation and then seating the designee, but Partners continued to pursue its claims against Universal for breach of the Board Seat Agreement.

Vice Chancellor Glasscock dismissed Partners' claims, ruling that Universal had not breached the Board Seat Agreement. Even though the Board Seat Agreement did not include any requirement that Partners' designee sign a confidentiality agreement or agree to any other conditions, the board of directors has a fiduciary duty not to provide opposing litigation counsel access to the sort of information that a director is privy to. Thus, the board's unwillingness to seat the Partners designee until he signed the confidentiality agreement did not constitute a breach. This case illustrates the complications that a board of directors can face in the midst of a dispute between parties represented on the board and the conflicts that can be raised when appointed directors have responsibilities to adverse constituencies.

Partners Healthcare Solutions Holdings L.P., et al. v. *Universal American Corp.*, C.A. No. 9593-VCG (Del. Ch. June 17, 2015).

Plaintiffs Strike Out in Two Recent Delaware Appraisal Actions

The Delaware Chancery Court has twice in the past few months ruled in statutory appraisal actions that the negotiated transaction price was the most reliable indicator of value.

In an April 30, 2014 Delaware Chancery Court decision (*Merlin Partners LP and AAMAF, LP v. AutoInfo, Inc.*) deciding a statutory appraisal action, the Court found that the price paid for the buyout of AutoInfo by funds affiliated with private equity firm Comvest Partners was fair to AutoInfo's stockholders.

The Court found that the $1.05 per share price, negotiated through a special committee of independent directors after an extensive sale process that involved multiple competing bidders, was the best estimate of AutoInfo's value at the time of the transaction. The Court was unpersuaded by the plaintiffs' reliance on a discounted cash flow ("DCF") analysis and multiple forms of comparable company analysis, each of which lead to higher valuations. The Court found that the companies used in the plaintiff's comparable company analysis were not sufficiently comparable, and that the plaintiffs' DCF analysis was not credible given the reliance on management projections, which the Court found to be unreliable.

While weight is often given in appraisal proceedings to management's projections prepared in the ordinary course of business, management projections may be disregarded when their use was unprecedented, they were produced in anticipation of litigation, they differed in form or duration from those customarily prepared or they were produced in order to obtain benefits outside the ordinary course of business.

Similarly, on June 30th, the Delaware Chancery Court relied primarily on the negotiated purchase price in determining fair value in the statutory appraisal proceeding of case of *LongPath Capital, LLC v. Ramtron Int'l Corp.* (Del. Ch. June 30, 2015). In this case, a hedge fund plaintiff acquired shares after announcement of the deal in order to pursue the appraisal claim. This plaintiff advocated following a discounted cash flow (DCF) analysis that supported a significantly higher valuation. In a context where the $3.10 per share merger price represented a significant (71%) premium to the pre-announcement trading price, and the record demonstrated substantial price negotiations with the purchaser and extensive (albeit ultimately unsuccessful) sales efforts in an attempt to solicit potential alternative buyers to try to top the initially hostile bid, Vice Chancellor Parsons was skeptical of the DCF analysis dependent on management projections and a dearth of "comparable transactions," and noted that "in the situation of a proper transactional process likely to have resulted in an accurate valuation of an acquired corporation, this Court has looked to the merger price as evidence of fair value and, on occasion, given that metric one hundred percent weight." Finding that the negotiated merger price ($3.10 per share) represented the fair value of shares, the court applied a $0.03 (roughly 1%) reduction for purposes of appraisal attributable to the synergies of the deal in accordance with DGCL Section 262 which requires that "fair value" for purposes of appraisal exclude any element of value arising from the merger itself.

AutoInfo and *LongPath* are part of a continuing trend of Delaware appraisal case law demonstrating the risk to activist shareholders in bringing appraisal actions in the face of transactions that have been arrived at after a robust and properly conducted sale process. *See, e.g.*, *Huff Fund Investment Partnership v. CKx, Inc.*, C.A. 6844-VCG (Del. Ch. May 19, 2014) (covered in the First Quarter 2014 edition of the Ropes Recap) and *In re Appraisal of Ancestry.com, Inc.*, C.A. 8173-VCG (Del. Ch. Jan. 30, 2015) (covered in the First Quarter 2015 edition of the Ropes Recap.) Of course, where the record does not demonstrate a robust and fair sale process, the Delaware courts will not generally defer to the deal price and are more likely to determine fair value for purposes of appraisal by reference to valuation analyses and methodologies that are generally considered acceptable in the financial community such as discounted cash flow analysis. *See, e.g., Owen v. Cannon,* C.A. No. 8860-CB (Del. Ch. June 17, 2015) (involving closely held corporation where two principal stockholders squeezed out third principal stockholder in a deal where defendants failed to establish fair process).

LongPath Capital, LLC v. Ramtron International Corporation, C.A. No. 8094-VCP (Del. Ch. June 30, 2015).

Merlin Partners LP v. AutoInfo, Inc., No. 8509-VCN (Del. Ch. Apr. 30, 2015).

Delaware Chancery Court Approves Settlement Agreement for $275 Million in Derivative Suit Relating to Activision Restructuring

On May 20, 2015, in I*n re Activision Blizzard, Inc. Stockholder Litigation*, the Chancery Court approved a $275 million derivative settlement, describing it as the largest cash derivative settlement in history. The case involved videogame maker Activision Blizzard, Inc. ("Activision").

Facing liquidity problems in 2012, Vivendi S.A. ("Vivendi"), Activision's controlling stockholder prompted Activision's board of directors to explore strategic alternatives. A restructuring was negotiated pursuant to which the Chairman and the CEO of Activision, along with co-investors, agreed to acquire the equity from Vivendi. A consolidated derivative action alleging breach of fiduciary duty settled a month before trial. Under the terms of the settlement agreement, the defendants agreed to (a) pay $275 million directly to Activision (*i.e.*, not to the plaintiff Class members), (b) reduce a cap on the voting power exercised by the Chairman and the CEO and (c) expand the Activision board to include two independent directors unaffiliated with either the Chairman or the CEO of Activision. A number of stockholders subsequently challenged the settlement.

In assessing the adequacy of settlement consideration, a reviewing court will consider multiple factors, including, "(1) the probable validity of the claims, (2) the apparent difficulties in enforcing the claims through the courts, (3) the collectability of any judgment recovered, (4) the delay, expense and trouble of litigation, (5) the amount of the compromise as compared with the amount and collectability of a judgment, and (6) the views of the parties involved, pro and con."

In supporting an award of $72.5 million in fees and expenses to lead counsel, the Court considered a number of factors, including the results achieved, the time and effort of counsel and the contingency risk assumed by counsel. "While the size of the award implies a generous hourly rate," the Court noted, "in this case it is justified by the effort."

In re Activision Blizzard, Inc. Stockholder Litigation, Cons. C.A. No. 8885-VCL (Del. Ch. May 20, 2015).

Delaware Chancery Court Describes Standards for Attorneys' Fees

In *In re Jefferies Group, Inc. Shareholders Litigation*, Chancellor Bouchard discussed the appropriate amount of attorneys' fees and held that attorneys' fee awards should be calculated based upon the gross settlement value.

The action arose from a 2013 stock-for-stock merger of Jefferies Group, Inc. and Leucadia National Corporation. The shareholder plaintiffs alleged that certain of Jefferies' directors had been conflicted in the transaction and negotiated for leadership positions with the combined company at the expense of Jefferies' stockholders. The plaintiffs argued that as a result of that conflict the directors must demonstrate that the transaction satisfied the entire fairness standard, while the defendants contended that the business judgment rule should apply. Ultimately, the parties settled five weeks before trial was scheduled to begin, after the plaintiffs had survived a motion to dismiss and a motion for summary judgment.

The defendants' Delaware counsel sought attorneys' fees of $27.5 million, which would have been approximately 27.5% of the gross value of the settlement, after taking into account the requested fees and expenses. The defendants argued that the fee award should be based instead on the net value of the settlement, and that an award of 22.5% of such amount was appropriate.

Chancellor Bouchard determined that the award should be based on the gross settlement value, which, in his view, is how the Chancery Court has traditionally determined awards. However, he noted that defendants are typically indifferent to the percentage of a gross settlement awarded for plaintiffs' counsel, as defendants' exposure is typically capped at an agreed maximum fee award. From a policy perspective, the Court found that it is preferable for the parties to agree on a net payment to stockholders without an agreement on the maximum fee award, because defendants will have an incentive to oppose fee requests and the amount of such awards would be "subject to adversarial inquiry to provide the Court with a better record with which to evaluate the *Sugarland* factors, in particular the quality of the benefit achieved in a proposed settlement."

The Court then turned to determining the amount of fees to be awarded to the plaintiffs' counsel, relying upon the *Sugarland* factors, "(1) the results achieved; (2) the time and effort of counsel; (3) the relative complexities of the litigation; (4) any contingency factor; and (5) the standing and ability of counsel involved." After evaluating each of the factors, the Court noted that fee awards "usually max out at one-third" of a settlement fund and that the typical fee award for a case that settled at the same stage as *In re Jefferies* range from 22.5% to 25% of the benefit conferred. Ultimately, the Court awards the plaintiffs' counsel 23.5% of the gross value of the award (or $21.5 million).

In re Jefferies Group Shareholders Litigation, Cons. C.A. No. 8059-CB (Del. Ch. June 5, 2015).

Delaware Legislative Update

On June 24, 2015, Delaware Governor Jack Markell signed into law Senate Bill 75, which contained several amendments to the General Corporation Law of the State of Delaware (the "DGCL"). Perhaps the two most notable changes were a new prohibition on fee shifting provisions and new provisions authorizing the use of certain forum selection clauses. Both sets of amendments will become effective on August 1, 2015.

Fee Shifting Provisions.

The bans on fee shifting provisions in certificates of incorporation and corporate bylaws are codified in Sections 102(f) and 109(b), respectively, of the DGCL. Each section prohibits the adoption of any provision that would make a stockholder responsible for the attorneys' fees or other expenses of the corporation or any other party arising out of an unsuccessful "internal corporate claim."

The kinds of "internal corporate claims" to which the new ban applies include those brought in the right of the corporation (i.e. a shareholder derivative claim), and consist of those that are based on a violation of a duty by any current or former director, officer, or stockholder.

However, the ban is limited in several important ways. It does not apply to non-stock membership corporations. Additionally, the ban only prevents the use of fee shifting provisions in certificates of incorporation and corporate bylaws; such provisions are still valid if included in other documents to which stockholders may be subject, including stock purchase agreements or stockholders' agreements.

As we noted in the First Quarter 2015 edition of the Ropes Recap, the amendments were proposed in response to recent Delaware litigation. In *ATP Tour, Inc., v. Deutscher Tennis Bund*, 91 A.3d 554 (Del. 2014), the Delaware Supreme Court ruled that a bylaw making the members of a non-stock corporation responsible for the legal expenses of the corporation in certain internal corporate claims was facially valid. Indeed, the Court even held that adopting such provisions with the intent to deter litigation would not necessarily render them unenforceable. While the business in question in *ATP Tour* was a non-stock corporation, the case's holding could logically be extended to apply to stock corporations as well, and this prompted the Delaware Legislature to enact these amendments. The effect of the new amendments is to limit the holding in *ATP Tour* to non-stock corporations.

Forum Selection Clauses.

Similar to the fee shifting provisions discussed above, the DGCL amendments regarding forum selection clauses were also developed in response to Delaware litigation. In *Boilermakers Local 154 Retirement Fund v. Chevron Corporation*, 73 A.3d 934 (Del. Ch. 2013), the Delaware Chancery Court held that certificates of incorporation and corporate bylaws can specify that internal corporate claims must be brought solely and exclusively in the Delaware courts, including Delaware federal court. The new Section 115 of the DGCL codifies this holding; Delaware corporations may now include provisions in their bylaws or certificate of incorporation that designate Delaware courts as the sole forum for certain intra-corporate claims. The types of intra-corporate claims covered are the same as those covered by Sections 102(f) and 109(b).

However, the DGCL's authorization of forum selection clauses is subject to several limitations. Section 115 does not specifically authorize or prohibit corporations from designating additional forums outside of the Delaware courts. It does, however, prohibit the selection of forums outside of Delaware on an exclusive basis. This limitation would seem to overrule Chancery Court's holding in *City of Providence v. First Citizens Bancshares, Inc. et al.*, C.A. No. 9795-CB (Del. Ch. Sept. 8, 2014), where the court upheld a forum selection clause requiring claims to be brought only in North Carolina courts.

As with Sections 102(f) and 109(b), Section 115 applies only to provisions included in a corporation's certificate of incorporation or bylaws. As a result, corporations are free to designate non-Delaware forums as the sole forum for litigation or arbitration in stockholders' agreements or other documents.

Despite Section 115, Delaware corporations may still face difficulties when attempting to enforce forum selection clauses in non-Delaware jurisdictions. For example, as we reported in the Third Quarter 2014 edition of the Ropes Recap, an Oregon state court recently declined to enforce a Delaware forum selection bylaw adopted as part of the merger challenged by the plaintiffs in the same case. *See Roberts v. TriQuint Semiconductor, Inc.*, 342 P.3d 88 (Or. 2014).

Notable Deals

Acquiring a Competitor: The Impact of "Foreign" on HSR Act Analysis

Absent an exemption, acquisitions resulting in a person holding in excess of $76.3 million of voting securities (and meeting the size of parties threshold) are subject to the reporting requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "HSR Act"). The parties to such a transaction must report it to federal antitrust authorities and observe a waiting period while the agencies evaluate the possible anti-competitive effects of the contemplated acquisition. Recently, the HSR Act has taken center stage in a takeover battle being waged between two pharmaceutical companies, Teva Pharmaceutical Industries Ltd. ("Teva") and Mylan N.V. ("Mylan"). At issue is whether the companies are sufficiently "foreign" such that the acquisition by Teva of a non-controlling stake in Mylan – even when valued in excess of the HSR Act's dollar threshold – does not trigger mandatory premerger reporting.

As of May 27, 2015, Teva held a 1.35% stake, which exceeded $460 million based on the lowest recent closing price of Mylan's stock; more than six times higher than the HSR Act threshold. On June 1, 2015, Mylan sent Teva a letter contending that Teva's recent acquisitions of Mylan's stock violated the HSR Act, as ostensibly Teva had not received clearance prior to this acquisition. Teva responded that it had conferred with U.S. antitrust authorities and had no reason to believe its purchases violated the HSR Act.

The Teva-Mylan saga revolves around the applicability of the HSR Act's "foreign issuer" exemption. This exemption distinguishes between foreign and U.S. persons as acquiring parties and foreign and U.S. issuers as acquired parties, giving greater latitude to foreign persons acquiring shares of foreign issuers on the basis that the U.S. nexus – and therefore likely impact on competition in U.S. markets – is much more tenuous. As such, acquisitions of foreign issuers are not reportable where the issuer does not have the requisite U.S. sales or assets. Generally, a foreign person may acquire an unlimited dollar amount of a foreign issuer's shares so long as its aggregate holdings represent less than 50% of the issuer's issued and outstanding shares. As such, a foreign person can acquire up to 49.9% of a foreign issuer's shares, without triggering the HSR Act's notification requirements. In contrast, a foreign person acquiring a stake in a competing U.S. corporation will likely have its holdings capped at $76.3 million (absent another exemption), and a U.S. person acquiring shares of a foreign issuer will need to further analyze whether the issuer has sufficient U.S. sales or assets to trigger HSR Act reporting. Additionally, unlike the "passive investor" exemption – which permits aggregate acquisitions of less than 10% of an issuer's outstanding shares solely for investment purposes so long as the person is not a competitor – the foreign issuer exemption can be used even where the buyer intends to launch a takeover.

Determining the availability of the foreign issuer exemption requires focusing on the term "foreign issuer." Under the HSR Act, an issuer is foreign if it is incorporated outside the U.S., not organized under the laws of the U.S., and has its principal offices outside of the U.S.

Although the first two prongs are easily determinable, the last requires investigation and is not specifically defined within the regulations. The Premerger Notification Office of the FTC (the "PNO"), which administers the premerger reporting program, offers guidance in determining an issuer's principal office location. The PNO gives greatest weight to the location of a company's officers, but also considers where binding documents are signed and, in the absence of directors or officers, the location of those exercising control over the decision-makers. By contrast, the PNO appears to discount the issuer's legal address, the location of the company's directors, the location of board meetings, and where an entity holds itself out as being principally located.

Determining whether Mylan is a "foreign issuer" is further complicated by its recent structural inversion, as a result of which, Mylan is now incorporated in and organized under the laws of the Netherlands, with its principal executive offices located in the U.K. Mylan is foreign for tax purposes, but Mylan claims to be a U.S. issuer for HSR Act purposes. This adds to questions about principal office location and is seemingly supported by Mylan's website, which suggests Mylan's Chief Executive Officer and other executive officers manage Mylan's worldwide businesses from the its Canonsburg, Pennsylvania offices. Further complicating the analysis is Mylan's poison pill-type scheme that allows the indefinite transfer of voting control from its stockholders to a stichting, in order to block a Teva bid. This would effectively transfer Mylan's decision-making power to the stichting's board in the Netherlands, which could bolster support for Mylan as a foreign issuer but could also block Teva from purchasing more than 20% of Mylan's stock, as larger purchases would require the stichting board's approval.

Navigating the HSR Act rules and determining "principal offices" can, in certain circumstances, be quite challenging, but it can also give a strategic advantage when used to help a foreign person acquire a toe-hold position (or more) in a competitor or as a blocking technique when questioning HSR Act compliance of a potential acquirer.

London Update

High Court Decision Provides Guidance on Avoiding Pitfalls When Serving Notice: IPSOS S.A. v. Dentsu Aegis Network Limited

1. **Summary**

This recent decision of the High Court provides a cautionary tale to any purchaser who contemplates bringing a claim for breach of warranty under a share sale agreement. The takeaway point for a purchaser is to ensure that any notice of claim is clear and informative and complies fully with the requirements set out in the sale agreement.

The Court noted that the requirements of a notification clause will, ultimately, turn on its own wording, but confirmed that in carrying out an assessment of a purported notice, four propositions will help determine whether it is effective or not:

(a) Whether the notice ensures that sellers know in sufficiently formal terms that a claim for breach will be brought and of the particular grounds upon which the claim is based so that the seller can make financial provisions;

(b) How the purported notice wold be understood by a reasonable recipient with knowledge of the context in which it was sent;

(c) Whether the notice specifies that a claim is actually being made (as opposed to indicating the possibility that a claim may be made in the future); and

(d) Whether the notice complies with the agreement's requirements with respect to specificity.

2. **Facts**

Ipsos had purchased shares in companies in the Synovate Group from Aegis Limited. Aegis had limited its liability for breach of warranty in a fairly standard way: (i) a notice of claim for breach of warranty had to be brought within two years of completion of the deal; (ii) this claim notice was required to specify in reasonable detail the matter giving rise to the claim, the nature of the claim and, so far as reasonably practicable at the time of the notification, the amount claimed; and (iii) proceedings would then need to be issued within six months of the date of the claim notice. In addition, under a separate limitation provision, the agreement required the purchaser to notify the seller if it became aware of any third party claim that might lead to a claim for breach of warranty or a claim under a separate indemnity contained in the sale contract. Failure to comply with this additional notification requirement would not bar a subsequent claim for breach of warranty, but might reduce the level of damages that could be recovered.

Ipsos issued proceedings against Aegis for breach of warranty some two and half years after completion. Aegis resisted the claim on the grounds that Ipsos had failed to notify the claim and to initiate proceedings within the timeframe specified in the sale agreement. The central point for discussion was whether Ipsos had served an effective notice of claim:

(a) Ipsos had sent a preliminary notification to Aegis of various employment law claims against a target group company. This letter stated on its face that it was intended to be a notification of third party claim, as required under the agreement and also stated that it was not a notification of warranty claim. Aegis responded to this letter to the effect that further information was required for an effective notification of a third party claim.

(b) Ipsos wrote a further letter to Aegis about a year later just prior to the end of the two-year period for notifying claims. This letter referred to the previous correspondence and provided further detailed information in relation to the relevant claims, including a discussion of quantum. In this letter, Ipsos indicated that it would follow up with a further breakdown of what losses it might recover under either an indemnity contained in the sale agreement (to cover losses relating to disclosed litigation) or which it would claim or might claim from Aegis as damages for breach of warranty. This letter invited further clarification from Aegis as to which claims should come within scope of the indemnity. The letter did not state that it was a notification of claim for breach of warranty.

The court had to consider whether this second letter was sufficient to constitute an effective notice of claim.

3. **Decision**

The Court concluded that Ipsos had failed to give an effective notice of a warranty claim in the manner required under the agreement because:

(a) a reasonable recipient of the notice with the knowledge of the context in which it was sent would not have understood the letter to be a claim notice (the court referred, in particular, to the ambiguity that arose as a result of the separate obligation to notify a third party claim);

(b) the letter did not specify the matter which gave rise to the claim in sufficiently clear terms; and

(c) the letter did not specify the nature of the claim in ‘reasonable detail’, as was required in the contract.

This case confirms the importance, when serving a notification of this kind, to observe the contractual requirements associated with such notice: not only must a claim notice be served within the timeframe stipulated by the contract, but also it must be clear on its face that it is a notice of warranty claim (especially in circumstances where separate notifications of third party claims are required) and, furthermore, to the extent required by an agreement (as is customarily the case), the notice must provide details of the claim.

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Contributors

Partners:	Associates:
Jason Freedman (San Francisco) jason.freedman@ropesgray.com	Zachary Blume (Boston) zachary.blume@ropesgray.com
Jane Goldstein (Boston/New York) (co-head of M&A) jane.goldstein@ropesgray.com	James Davis (Chicago) james.davis@ropesgray.com
Howard Glazer (San Francisco) howard.glazer@ropesgray.com	Greg Demers (Boston) gregory.demers@ropesgray.com
James Lidbury (Hong Kong) (co-head of M&A) james.lidbury@ropesgray.com	Jacob Silberberg (Boston) jacob.silberberg@ropesgray.com
Carl Marcellino (New York) (co-head of M&A) carl.marcellino@ropesgray.com	Justin Voeks (Chicago) justin.voeks@ropesgray.com
Philip Sanderson (London) philip.sanderson@ropesgray.com	Peter Wang (San Francisco) peter.wang@ropesgray.com
Peter Welsh (Boston) peter.welsh@ropesgray.com	Christian Westra (Boston) christian.westra@ropesgray.com
Marko Zatylny (Boston) marko.zatylny@ropesgray.com	**Contract Attorneys:** Amanda N. Muller (Boston) amanda.muller@ropesgray.com
Counsel: Martin Crisp (New York) martin.crisp@ropesgray.com	**Summer Associates:** Reggie Guy (Chicago)
Deidre J. Johnson (Boston) deidre.johnson@ropesgray.com	Jim O'Neill (Boston)
Chief of Legal Knowledge Management: Patrick Diaz (Boston) patrick.diaz@ropesgray.com	Graham Rogers (Boston)
Professional Support and KM Lawyers: Fay Anthony (London) fay.anthony@ropesgray.com	
Marc Feldhamer (New York) marc.feldhamer@ropesgray.com	