Fee-Shifting, Financial Advisor Liability Among Likely Delaware Law Issues for 2015

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The Delaware courts weighed in on familiar issues of importance last year, including multiforum deal litigation and the emphasis on an independent board process, while also delving into relatively new territory such as fee-shifting bylaws. Meanwhile, significant changes to the benches of both the Delaware Court of Chancery and the Delaware Supreme Court in 2014 will undoubtedly shape the way Delaware jurisprudence develops in the coming years.

The courts: Last January, former Chancellor Leo E. Strine Jr. was confirmed as the new Chief Justice of the Supreme Court, and a few months later Chancellor Andre Bouchard was appointed as the new head of the Court of Chancery. Additionally, Justice Karen L. Valihura and Justice James T. Vaughn Jr. filled the vacancies created on the Supreme Court with the retirements of Justices Jack B. Jacobs and Carolyn Berger. Justice Henry DuPont Ridgely also is set to retire in January 2015, meaning that four of the five justices will have changed within the last 12 months.

Multiforum litigation: Stockholder plaintiffs filed claims after the announcement of nearly every significant public company transaction in 2014 and often attempted to litigate claims in multiple jurisdictions. The cost and inefficiency of this multiforum jurisdiction phenomenon has received widespread attention in recent years. One reaction by Delaware corporations has been to adopt forum selection bylaws choosing an exclusive forum for disputes — generally Delaware — as a way to reduce the risk of costly multijurisdictional stockholder litigation. Courts have largely upheld those bylaws, and stayed or dismissed lawsuits filed outside the selected jurisdiction. In *City of Providence v. First Citizens BancShares, Inc.*, 99 A.3d 229 (Del. Ch. 2014), Chancellor Bouchard followed the line of reasoning set forth by then-Chancellor Strine in *Boilermakers*, holding that a Delaware corporation may validly adopt a bylaw designating an exclusive forum, including a forum other than Delaware, for litigating intra-corporate disputes. Notably, the court also rejected a challenge to the timing of the adoption of the bylaw — which happened the same day the board of directors announced a merger transaction — reasoning that the timing is immaterial in the absence of any well-pleaded allegations demonstrating impropriety.

Fee-shifting bylaws: A new development in 2014 related to fee-shifting bylaws, which require unsuccessful stockholder plaintiffs to pay their adversaries' legal fees. In *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554 (Del. 2014), the Delaware Supreme Court found that such a provision in the bylaws of a Delaware nonstock corporation could be enforceable, setting off a flurry of reactions from Delaware corporations, practitioners and legislators that ranged from strong support, and even the adoption, of fee-shifting bylaws to fervent disapproval. Legislation that would effectively overrule *ATP Tour* was quickly proposed after the opinion was issued but then tabled for further consideration. The continuing development

of this legislation, and the reaction of Delaware courts as more corporations adopt these types of bylaws, will surely be a critical topic in 2015 as additional bylaws emerge.

The role of the board in transactions: Delaware courts also continued to focus on how board independence should be considered in deciding whether deferential business judgment review or the exacting entire fairness standard should be applied. In *KKR Financial Holdings LLC Shareholder Litigation*, Consol. C.A. No. 9210-CB (Del. Ch. Oct. 14, 2014), Chancellor Bouchard dismissed breach of fiduciary duty claims regarding the acquisition of KKR Financial Holdings LLC (KFN) by KKR & Co. L.P., which stockholders alleged was the controlling stockholder of KFN. The court held that KKR was not a controlling stockholder by virtue of a management agreement, and applied the business judgment rule after finding that a majority of KFN's board was disinterested and independent, and a majority of fully informed stockholders approved the merger.

In *Cornerstone Therapeutics Inc. Stockholder Litigation*, C.A. No. 8922-VCG (Del. Ch. Sept. 10, 2014), the court applied entire fairness at the pleadings stage to a controlling stockholder freeze-out merger, holding that disinterested directors entitled to exculpation under the company's charter could not prevail on a motion to dismiss. Applying the Supreme Court's decision in *Emerald Partners*, the court determined that the directors "must await a developed record, post-trial, before their liability is determined," despite the fact that no particularized allegations were brought against the directors. The Court of Chancery's decision in *In re Novell, Inc. Shareholder Litigation*, Consol. C.A. No. 6032-VCN (Del. Ch. Nov. 25, 2014), also is notable, because the court granted former directors' motion for summary judgment on a bad-faith claim alleging favorable treatment to one bidder over another. Despite the fact that the board was independent and disinterested, the court had initially denied a motion to dismiss the claim. In granting summary judgment in favor of the former directors, the court held that the plaintiffs failed to present evidence "that the board members were motivated by some improper purpose that makes their conduct culpable."

More recently, in *In re Rural/Metro Corp. Stockholders Litigation*, Consol. C.A. No. 6350-VCL (Del. Ch. Oct. 10, 2014), Vice Chancellor J. Travis Laster held post-trial that a financial advisor was liable for $75.8 million for aiding and abetting breach of fiduciary duty claims for, among other things, failing to oversee the board's special committee. The court also found that the directors of Rural/Metro Corporation breached their fiduciary duties in connection with the purchase of Rural/Metro at a premium, citing various conflicts of interest among management, the board and financial advisors. Before trial, the director defendants and another financial advisor had reached a settlement with the plaintiff on the same claims, leaving the financial advisor as the sole defendant in the lawsuit and subject to joint and several liability for damages. *Rural/Metro* highlights the caution that both directors and their financial advisors must take in ensuring that a board fulfills its obligations to remain fully informed and cautious of potential conflicts during a sale process. This matter may be the subject of an appeal, and one that all practitioners will be watching closely in 2015.

Finally, in *C&J Energy Services, Inc. v. City of Miami General Employees' & Sanitation Employees' Retirement Trust*, -- A.3d --, No. 655/657, 2014 (Del. Dec. 19, 2014), the

Delaware Supreme Court unanimously reversed a preliminary injunction issued by the Court of Chancery, holding that an active sale process is not automatically required for a target board to satisfy its fiduciary duties in a change of control transaction. The Delaware Supreme Court confirmed that a company selling itself in such a transaction is not per se required under *Revlon* and its progeny to shop itself to seek the highest immediate value, so long as the target board acts in good faith, tests the deal through a viable passive market check, and gives stockholders a fully informed opportunity to vote on the deal. The Court of Chancery subsequently relied on *C&J Energy* in *In re Family Dollar Stores, Inc. Shareholder Litigation*, Consol. C.A. No. 9985-CB (Del. Ch. Dec. 19, 2014), which addressed allegations that a target board had failed to satisfy its *Revlon* duties by turning down a higher-priced bid with potential antitrust issues in favor of a lower-priced bid with greater certainty of closing. The court held that *Revlon* requires a board to pursue the highest price reasonably attainable — not just the highest price offered, and that Delaware law is deferential to well-informed, disinterested boards that pursue a transaction in good faith.