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Merger Objection Cases: Toothless Tigers

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Mergers and Acquisition (M&A) cases have become the bane of public companies and securities practitioners across the country. In the last decade, the percentage of lawsuits filed following the announcement of a merger or other fundamental transaction has skyrocketed. In 2012, 93% of deals valued over $100 million were challenged.[1] In 2013, 94% of deals valued over $100 million were challenged.[2] The format of the cases is rote: plaintiffs' firms issue announcements looking for plaintiffs whenever a public company deal is announced, and bring suit shortly thereafter, often using one of a stable of serial plaintiffs they have on standby; the lawsuits seek expedited discovery and a hearing date for a preliminary injunction; if the parties agree, or discovery is ordered, the plaintiffs take three to five depositions, review a handful of board minutes and bankers books; and then, prior to a hearing on a preliminary injunction, the plaintiffs demand corrective disclosures and an agreement on fees for their counsel. More often than not, the cases settle, not because of any malfeasance by the companies or their directors but because the companies are unwilling to incur the risk that a court will issue a preliminary injunction delaying the shareholder vote and, thus, jeopardizing the acquisition.[3]

We realized, anecdotally, however, that in the vast majority of cases, when defendants take a firm stand, refuse to compromise with the plaintiffs, and insist on fighting expedited discovery, they are successful. Indeed, it was our view that, if one were to examine the merger objection cases brought in the preceding years, the number of actual wins for plaintiffs' lawyers (as opposed to the number of cases in which plaintiffs were able to extract a settlement) would be low.

We set out to test that thesis by reviewing every lawsuit brought to enjoin every public company transaction in 2012 and the first half of 2013. We reviewed lawsuits filed in connection with 226 discrete transactions, and found substantive information regarding at least some aspects of 70% (158) of the deals. We were able to de-

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[1] 2013 Cornerstone Research Study, http://www.cornerstone.com/getattachment/9d8fd78f-7807-485a-a8fc-4ec4182dedd6/Shareholder-Litigation-Involving-Mergers-and-Acqui.aspx (last accessed March 24, 2014) ("2013 Cornerstone Study").

[2] 2014 Cornerstone Research Study, http://www.cornerstone.com/getattachment/73882c85-ea7b-4b3c-a75f-40830eab34b6/Shareholder-Litigation-Involving-Mergers-and-Acqui.aspx (last accessed March 24, 2014) ("2014 Cornerstone Study").

[3] 2014 Cornerstone Study at 4 ("Overall, the majority of M&A litigation settled, consistent with prior years.").

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termine the outcome of the request for expedited relief in 68% of (153) cases. Of them, the court issued a decision on the temporary restraining order or preliminary injunction motion in 28% of the (43) cases. We were able to determine attorney's fee amounts in 30% of (47) the cases. The other cases were in state courts, where docket information was not readily accessible.[4] When cases went forward in multiple courts, we tracked the lead case.[5]

Courts Rarely Grant Injunctions, and When They Do, it Is Generally for Predictable Issues. As expected, when the court ruled on a motion for expedition or a motion for a preliminary injunction, defendants were successful in the vast majority of cases. Courts ruled on emergency relief in 28% (43 of 153) of the cases we were able to track through summary judgment (the others were either dismissed voluntarily (13% of cases) or settled before a decision on expedition or preliminary injunction (59% of cases)). The court denied expedited relief 91% of the time (39 cases).

About 30% of the time (12 cases) the court refused to allow expedited discovery or to set a hearing date for a preliminary injunction, making the initial determination that the plaintiffs' claims, as alleged, were not colorable. In 69% of cases (27 cases) the defendants defeated a preliminary injunction. Remarkably, over the 18-month time period we surveyed, the court granted injunctive relief only *four* times.

Not only was it rare for a court to grant an injunction, when injunctions were issued, the results were not dire. The court enjoined the stockholder vote on a merger in only one case, *First Financial Holdings*, which was brought in New York state court. Even there, the parties reached an agreement that allowed the merger vote to go forward as planned in exchange for changes to the deal terms.

In the other three cases in which injunctive relief was granted, the courts ordered changes to the terms of the merger, or additional disclosures, but did not order a delay of the shareholder vote. In addition, the injunctions were issued for relatively predictable issues. The Delaware Court of Chancery issued only two injunctions, and both—*Ancestry.com* and *Complete Genomics*—involved a ''don't ask, don't waive'' (DADW) provision. A DADW provision requires that a potential suitor agree in a nondisclosure agreement, before receiving confidential information, that it will not attempt a hostile takeover if its offer price is rejected by the board. The Delaware Court of Chancery has recognized that ''DADW provisions can have value, in that they produce pressures to bid high akin to those achieved in a sealed bid action.''[6] In *Ancestry.com*, then-Chancellor Leo E. Strine noted that a DADW provision can be ''value maximizing'' when ''there really is an end'' and potential acquirers know ''you should bid your fullest because, if you win, you have the confidence of knowing you actually won.''[7]

Still, DADW provisions have been referred to by the Delaware Court of Chancery as ''potent,'' and the chancellors have expressed concern over their use.[8] In *Complete Genomics*, Vice Chancellor Laster suggested that DADW provisions might be *per se* invalid.[9] In the subsequent *Ancestry.com* decision, however, Chancellor Strine indicated that DADW provisions could serve a legitimate purpose so long as the board's deliberation regarding them was fully disclosed.[10] Later, when considering the fee petition in *Ancestry.com,* Vice Chancellor Laster adopted Chancellor Strine's view that the provisions were acceptable so long as fully disclosed as an alternate means for courts to address the provisions.[11] In both *Ancestry.com* and *Complete Genomics*, the Court of Chancery ordered a change in deal terms, or disclosures, but did not enjoin the shareholder vote.

In *Parlux*, the final case in which injunctive relief was granted, a Florida state court ordered corrective disclosures after discovery revealed that a statement in the proxy—that management had provided its free cash flow projections to the financial advisors—was incorrect. Again, as in the Delaware cases, this did not result in a delay to the deal. The bottom line, then, is that even in cases in which an injunction is issued, it is extremely rare for the injunction to be anything worse than what the parties would agree to during a settlement.

Plaintiffs Are Not Getting the Sort of 'High Value' Settlements We Would Expect if the Meritorious Cases Were Being Settled to Avoid Litigation. It is encouraging to note that the courts, as a rule, are reluctant to interfere with a merger. Still, we wondered, was it possible that ''messier'' cases were being resolved through settlement, and not through litigation. To answer this, we looked at the 90 cases that settled with a motion for expedition or preliminary injunction pending, and checked to see how many resulted in a change in deal terms or a settlement of over $1 million. Only 7% of settled cases met this criteria. Three involved DADW provisions, which the companies waived after the Delaware Court of Chancery made its skepticism for the clauses known. One involved an extended appraisal period. The other three involved a reduction in the termination fee, though interestingly, the termination fees initially negotiated in those cases were below 5%. This, to us, suggests that plaintiffs may be insisting on a reduction in termination fees to help justify higher attorney's fees than they could obtain from a disclosureonly settlement.

In general, the settlement value (almost always in the form of an agreement to pay fees to plaintiffs' counsel) was not high. All but a handful of the cases we looked at settled for fees in the $250,000–$500,000 range. Only three settled for more than $1 million in fees, and in each of those, the plaintiff was able to negotiate a

[4] We obtained information from PACER, state court websites, and disclosures filed on SEC.gov.

[5] According to Cornerstone, ''[t]he most active courts for M&A litigation in the last four years (after Delaware Court of Chancery) were: New York County, NY; Santa Clara County, CA; and Harris County, TX.'' 2014 Cornerstone Study at 3. We observed the same in our study.

[6] *Koehler v. NetSpend Holdings Inc.*, 2013 BL 133760, at *21, n. 235 (Del. Ch. May 21, 2013).

[7] *In re Ancesry.com Inc. S'holder Litig.* C.A. No. 7988CS, at 23 (Del. Ch. Dec. 17, 2012) (TRANSCRIPT).

[8] *Ancestry.com*, C.A. No. 7988CS at 21; *Complete Genomics, Inc.*, Del. Ch., Cons. C.A. No. 7888VCL, at 1418 (Nov. 27, 2012) (TRANSCRIPT).

[9] *Complete Genomics, Inc.*, Cons. C.A. No. 7888VCL, at 1418.

[10] *See Ancestry.com*, No. 7988CS at 23.

[11] *In re Complete Genomics, Inc.*, C.A. No. 7888VCL, at 50 (Oct. 2, 2013) (TRANSCRIPT).

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change in deal terms (elimination of the DADW provision in one, extension of the appraisal period in another, and a lower termination fee in the third). We did not observe any instance in which the plaintiffs obtained fees in excess of $1 million with a disclosure-only settlement.

A Victory During Expedition Is Likely to Translate to Total Victory. We also tracked cases, after the decision on a motion for expedition or preliminary injunction, to see what happens after the plaintiffs lose. We were able to track activity in 31 of the 39 cases in which the court rejected expedited relief. The plaintiffs voluntarily dismissed 55% of the cases, without further substantive litigation. Courts dismissed another 13% at pleading stage. Sixteen percent settled for undisclosed or nominal attorney's fee awards (these cases involved either federal Section 11 claims or instances in which the defendants made voluntary disclosures while preliminary injunction motions were pending, allowing the plaintiffs' counsel to claim a benefit even after a loss). The remaining cases are still being litigated. Of note, however, no court in the last 18 months has allowed a *Revlon* claim to continue past the pleading stage after denying expedited relief. The repercussions of this are obvious: a win on expedition should, in most cases, translate into a win on the merits.

Conclusion. After surveying cases filed in the preceding 18 months, we have determined that, in the vast majority of cases, the best tactic when litigating a meritless merger objection suit is to oppose either expedited discovery or a preliminary injunction. In Delaware, where courts require plaintiffs to plead a ''colorable'' claim before obtaining expedited discovery, the best approach is generally to oppose expedition. This gives the company the opportunity to either win the case early without imperiling its merger vote and to preview the court's view of the issues. If the case is in a jurisdiction where courts allow expedited discovery more readily, or if the defendants prefer to avoid the initial fight of expedited proceedings, the risk of opposing a preliminary injunction is also minimal; though the stakes are high, when only four cases in 18 months result in an injunction, that suggests that a large number of meritless cases (which can be won early) are being brought. In almost all cases where the defendants defeat either expedition or a preliminary injunction, the plaintiffs dismiss their case. This, of course, is a general theory for the general case; in instances where the transaction has disfavored terms, or where disclosures are inaccurate, a company would be wise to settle early before the plaintiffs' counsel can claim greater success and thus higher fees. If companies were in most instances to contest these cases, rather than usually settling them early, it is quite possible that we would see the end of this blight of cases.