CLIENT ALERT

2022 Delaware Year-End Review: M&A and Shareholder Litigation

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It was another very busy year for M&A litigation in the Delaware courts. In addition to the many twists and turns that captured the world's attention in the high-profile, expedited *Twitter v. Musk* deal litigation, the Court of Chancery also had occasion over the last 12 months to issue its second opinion evaluating claims against SPAC sponsors and directors, and to analyze new challenges to the validity of several common bylaw and charter provisions. Additionally, as previously noted, in light of the steady growth over the last few years in both Section 220 books and records lawsuits and derivative actions asserting *Caremark* claims, the Court had the opportunity in 2022 to provide more guidance around the contours and limits of those actions. The Court of Chancery also permitted a "novel theory" for pleading a breach of fiduciary duty to survive a motion to dismiss, discussed the application of *Corwin* and *MFW*, and formally declared Delaware to be a pro sandbagging state. The Delaware Supreme Court also issued a number of important decisions, offering guidance on when "reliable" hearsay can be used to establish a proper purpose for a books and records demand, as well as the deference owed to legal opinions by counsel.

The Court of Chancery also welcomed some new faces. Nathan Cook, former managing partner of Block & Leviton, was sworn in as a Vice Chancellor in June, and Bonnie David was recently appointed as a Master in Chancery in the first few days of 2023. Looking forward, changes are also expected on the Delaware Supreme Court. Justice Tamika Montgomery-Reeves was confirmed in December and will join the Third Circuit Court of Appeals, and Justice James Vaughn announced his upcoming retirement in May.

Broken Deal Litigation and Material Adverse Effect ("MAE") Provisions

As readers are likely already aware, the headline news from the Court of Chancery in 2022 was the ***Twitter, Inc. v. Musk*** deal litigation, in which Elon Musk sought to terminate his purchase of Twitter for $54.20 per share.[1] Musk advanced a number of theories in support of his right to walk away from the deal, including most prominently that Twitter had understated the number of bot and spam accounts on the platform. Musk also sought to leverage a "whistleblower" complaint against Twitter claiming, among other things, that Twitter had violated a settlement with the Federal Trade Commission relating to Twitter's data security practices. The dispute, which was litigated before Chancellor McCormick, proceeded on an expedited schedule and resulted in a crush of filings and rulings. All told, in the four months from when Twitter filed suit in July to the actual closing of the transaction in late October, Chancellor McCormick adjudicated at least 15 disputed motions. Although the case never made it to trial, the Twitter action demonstrates the Court of Chancery's ability to handle cases of unprecedented size on a highly expedited basis, and serves as a useful guide for the timeline that the Court will set when a merger partner seeks to terminate a deal and the appropriate scope of discovery for busted deal litigation generally.

Beyond the Twitter dispute, the final broken deal lawsuit arising from the COVID-19 pandemic reached its conclusion last year. In ***Level 4 Yoga, LLC v. CorePower Yoga, LLC***, franchisors of the CorePower branded yoga studios were given a call option on 34 CorePower studios owned and operated by Level 4 Yoga, LLC.[2] In early 2019, the franchisors expressed an interest in exercising that option, but sought to delay the closing date. The parties eventually came to an agreement whereby closing would be pushed to April 1, 2020 in exchange for no closing conditions and the buyers assuming any market or industry-wide risk associated with the delayed closing. When April 1, 2020 rolled around, however, CorePower sought to terminate the acquisition, claiming that Level 4's closure of studios in response to COVID-related orders from government entities resulted in an MAE. Level 4 sued, seeking a declaratory judgment, specific performance, and damages for CorePower's refusal to close. After a week-long trial, Vice Chancellor Slights ordered the parties to close. The Court noted that the parties had agreed that a price adjustment would be the only recourse, and that "[t]he absence of any contractual condition to closing or express termination right is potent evidence of the parties' intent here." The Court also found that, in any event, there had been no MAE. On appeal, the Delaware Supreme Court summarily affirmed the decision.[3] Thus, this case ended much like virtually every other COVID broken deal case with the buyer remaining on the hook to close notwithstanding the disruptions to the target's business caused by the pandemic.

[1] C.A. No. 2022-0613-KSJM.
[2] *Level 4 Yoga, LLC v. CorePower Yoga, LLC*, 2022 WL 601862 (Del. Ch. Mar. 1, 2022).
[3] *CorePower Yoga, LLC v. Level 4 Yoga, LLC*, 2022 WL 16579468 (Del. Nov. 2, 2022).

SPAC Litigation

Last year, we wrote about the Court's *MultiPlan* opinion, where Vice Chancellor Will applied the entire fairness standard of review and sustained stockholder claims challenging a de-SPAC transaction based on the defendants' failure "to disclose information necessary for the plaintiffs to knowledgeably exercise their redemption rights."[4] But the Court left open a scenario in which the disclosures were adequate and the allegations rested "solely on the premise that the fiduciaries were necessarily interested given the SPAC's structure."[5]

In ***Delman v. GigAcquisitions3, LLC***, Vice Chancellor Will denied a motion to dismiss similar breach of fiduciary duty claims arising out of a de-SPAC transaction, through which a SPAC, GigCapital3, Inc., acquired Lightning eMotors, Inc.[6] As in *MultiPlan,* the complaint in *Delman* alleged that the SPAC's directors and the SPAC's sponsor, GigAcquisitions3, had acted disloyally by depriving stockholders of information necessary to exercise their redemption rights. The Court concluded that the breach of fiduciary duty claims were subject to entire fairness review because the SPAC sponsor was incentivized to undertake a value-decreasing transaction in conflict with its stockholders, and a majority of the board was controlled by the sponsor. *Delman* marks an evolution in the Court's SPAC jurisprudence because the Court determined for the first time that SPAC transactions may be structurally ineligible for *Corwin* cleansing through a disinterested, independent, and uncoerced stockholder vote.[7] The Court reasoned that a SPAC's public stockholders have "no reason to vote against a bad deal because they could redeem."[8] As a result, the Court held that, in the context of a de-SPAC transaction, the stockholder "vote was of no real consequence," and its "effect on the standard of review is equivalently meaningless."[9] The *Delman* case represents the second time that the Court has denied a motion to dismiss and—in stronger language than articulated in *MultiPlan*—implies that the Court may continue to subject de-SPAC transactions with relatively typical SPAC features to entire fairness review.

In ***In re P3 Health Group Holdings, LLC***, the Court of Chancery addressed certain novel issues arising out of a merger transaction involving a SPAC, Foresight Acquisition Corp., and a privately held limited liability company, P3 Health Group Holdings, LLC ("P3").[10] Hudson Vegas Investment SPV, LLC ("Hudson"), a minority investor in P3, brought an action alleging that the de-SPAC merger was designed to resurrect an earlier-attempted affiliate merger transaction (with the company's controller) that Hudson had previously vetoed under P3's LLC agreement. Hudson asserted numerous claims under various contractual and non-contractual theories against P3, its controller, and P3's directors and officers. Applying

[4] *In re MultiPlan Corp. S'holders Litig.*, 268 A.3d 784, 816 (Del. Ch. 2022).
[5] *Id*.
[6] *Delman v. GigAcquisitions3, LLC*, 2023 WL 29325 (Del. Ch. Jan. 4, 2023).
[7] *Corwin v. KKR Financial Holdings LLC*, 125 A.3d 304 (Del. 2015).
[8] *Delman*, at 20. Regardless, the Court further found that the disclosures issued in connection with the merger did not contain all material information, including with respect to the net cash per share that the SPAC would invest in the combined company and the value that the SPAC's stockholders would receive through the merger. *Id.* at 21-25.
[9] *Delman*, at 20.
[10] C.A. No. 2021-0518-JTL.

established principles of Delaware contract law, the Court dismissed Hudson's claims that the de-SPAC transaction stripped its governance and other rights under the pre-merger LLC agreement because no provision in that agreement preserved any such rights after a merger. The Court, however, sustained various other claims including, among other things, a breach of contract claim alleging that the de-SPAC transaction constituted the first step in a "series of transactions" with the controller that required Hudson's consent under the LLC agreement, a fraudulent inducement claim based on representations made to Hudson about P3's prospects at the time of its investment, and a claim for tortious interference against the SPAC and its sponsor for inducing P3's breach of the LLC agreement.

Transactions with Controlling Stockholders

Challenges to transactions with controlling stockholders remained a focus of litigation and the Court of Chancery continued to expand the range of transaction structures—beyond the traditional controlling stockholder "squeeze-out" merger—to which the dual-prong *MFW* framework can apply at the pleadings stage. In ***In re Match Group, Inc. Derivative Litigation***, the Court granted defendants' motion to dismiss claims challenging a reverse spinoff in which a controller obtained an alleged non-ratable benefit at the expense of the minority, finding that the transaction had complied with the *MFW* framework.[11] Similarly, in ***City Pension Fund for Firefighters and Police Officers in The City of Miami Beach v. The Trade Desk, Inc.***, the Court dismissed claims challenging a charter amendment extending the duration of the company's dual-class structure, and thereby the controlling stockholder's voting control, on the grounds that the complaint failed to adequately allege non-compliance with any of the *MFW* factors.[12] Both cases contain useful analysis of the factors that the Court will consider in assessing director independence as well as the appropriate level of disclosure required to comply with *MFW*.

These cases also serve as a reminder that the *MFW* framework provides a potent defense to controlling stockholders and other defendants in securing dismissal of lawsuits at the early pleadings stage. Absent that threshold defense, the Court will apply the significantly more onerous entire fairness standard, which all but guarantees denial of a motion to dismiss. In ***Manti Holdings LLC v. The Carlyle Group Inc.***, a minority stockholder challenged a sale on the basis that the company's controller pushed through an inadequately priced deal because it wanted to monetize and close an associated investment fund.[13] Applying the entire fairness standard, the Court declined to dismiss the breach of fiduciary duty claims in light of allegations that the controller's representatives expressed a strong desire to sell the company, that the controller received the bulk of the consideration from the sale through its ownership of preferred shares, and that the lone dissenting director was then allegedly excluded from the negotiations.

[11] C.A. No. 2020-0505-MTZ, 2022 WL 3970159 (Del. Ch. Sept. 1, 2022).
[12] C.A. No. 2021-0560-PAF, 2022 WL 3009959 (Del. Ch. July 29, 2022).
[13] C.A. No. 2020-0657-SG, 2022 WL 1815759, at *1 (Del. Ch. June 3, 2022).

However, even in circumstances where the *MFW* framework is found not to apply, cases this year showed that controlling stockholders can still overcome deal challenges and establish the entire fairness of a transaction at trial, notwithstanding a process that may be viewed as "imperfect." For example, in ***In re BGC Partners Inc. Derivative Litigation***, plaintiffs challenged a transaction where BGC acquired Berkeley Point Financial from an affiliate of its controlling stockholder.[14] Although the Court found that the controller "overstepped," including with respect to his involvement in the selection of advisors, the Court nonetheless concluded that he had extracted himself from the process sufficiently early on, that the special committee and its advisors were independent and had obtained meaningful concessions in the course of negotiations, and that the agreed price was within the range of fairness. And in ***In re Tesla Motors, Inc. Stockholder Litigation***, plaintiffs alleged that Elon Musk had caused Tesla to overpay for SolarCity, a company for which Musk served as Chairman and was its largest stockholder.[15] Although the Court found that Musk was "more involved" in the process than a conflicted fiduciary should be, it determined that Tesla's board had meaningfully vetted the acquisition and the evidence showed that Tesla paid a fair price. In particular, the Court noted the fact that the transaction was approved by a vote of disinterested stockholders—mostly consisting of sophisticated institutional investors—was persuasive evidence of a fair price.

***Corwin* Cleansing**

Under the *Corwin* doctrine, if fully informed, uncoerced and disinterested stockholders vote to approve a merger not involving a conflicted controlling stockholder, then the vote "cleanses" any breach of fiduciary duty and the business judgment rule will apply. This year, several cases required the Court to analyze whether plaintiffs had sufficiently alleged a material disclosure deficiency that would preclude *Corwin* cleansing.

In ***Galindo v. Stover***, stockholders of Noble Energy, Inc. ("Noble") voted to approve a merger with Chevron Corporation.[16] Plaintiffs challenged the transaction and argued that *Corwin* cleansing did not apply because the proxy failed to disclose a previous proposal to acquire certain of Noble's assets or the reasons the company amended its change in control severance payments for executives. Noting that "directors need not provide exhaustive information in seeking a stockholder vote," Vice Chancellor Glasscock found that the prior proposal was immaterial, because it was never seriously considered and occurred two years before the transaction, and that information about the change in control payments had been sufficiently disclosed in the merger proxy.[17] Accordingly, the Court found that *Corwin* applied, and based on the business judgment standard of review, granted the motion to dismiss.

[14] C.A. No. 2018-0722-LWW, 2022 WL 3581641 (Del. Ch. Aug. 19, 2022).
[15] C.A. No. 12711-VCS, 2022 WL 1237185 (Del. Ch. Apr. 27, 2022).
[16] C.A. No. 2021-0031-SG, 2022 WL 226848 (Del. Ch. Jan. 26, 2022).
[17] *Galindo*, at *7.

In ***Teamster Members Retirement Plan v. Dearth***, stockholders of Calgon Carbon Corp. voted to approve a cash out acquisition by Kuraray Co. Ltd. that offered a substantial premium.[18] The plaintiff filed suit criticizing the single-bidder process and, after successfully litigating a books and records action under Section 220, alleged that the stockholder vote was not fully informed due to three omitted or misleading disclosures. First, plaintiff claimed that the company should have used a 10-year instead of a 5-year forecast in order to capture projected earnings from a delayed project, but the Court found no disclosure violation because five-year forecasts are routine. Second, plaintiff claimed that the board adopted an adjustment to EBITDA so as to artificially depress the projections, but the Court found that the adjustment was requested by the financial advisor (rather than a director or officer), the adjustment was relatively small, and there were no facts suggesting that it was made under suspicious circumstances. Third, plaintiff claimed that certain information regarding the negotiations had been omitted, but the Court reaffirmed that "Delaware law does not require disclosure of a play-by-play of negotiations leading to a transaction or of potential offers that a board has determined were not worth pursuing."[19] Accordingly, the Court determined that the stockholders who approved the deal were fully informed, that *Corwin* applied, and that the case should be dismissed. The Delaware Supreme Court summarily affirmed Vice Chancellor Zurn's ruling.[20]

Shareholder Activism and Enforcement of Charter and Bylaw Provisions

Advance Notice Bylaws Strictly Enforced

Last year, we highlighted the Court of Chancery's decision in *Rosenbaum v. CytoDyn Inc.*, where the Court strictly enforced the terms of an advance notice bylaw.[21] This year saw another example of the Court carefully interpreting and enforcing an advance notice bylaw to the letter. In ***Strategic Investment Opportunities v. Lee Enterprises***,[22] the plaintiff, a beneficial owner of Lee Enterprises stock, failed to move its shares into record name by the advance notice deadline. In an attempt to remedy the fact that it held no shares in record name, plaintiff included a cover letter from Cede & Co. (as record holder of all public stock in the United States) when it submitted its nomination packet. The company rejected the plaintiff's nomination notice as deficient both on the basis of this issue as well as the plaintiff's failure to provide background information about its director nominees on the company's standard form as required by the bylaws. Plaintiff filed suit alleging breach of contract and breach of fiduciary duty.

Following expedited litigation and a trial on a paper record, Vice Chancellor Will held that the nomination notice failed to satisfy both the record holder and form requirements as a matter of contractual law and that equity did not require the Court to override the board's action. The Court reasoned that (a) the record holder requirement was adopted by the

[18] C.A. No. 2020-0807-MTZ, 2022 WL 1744436 (Del. Ch. May 31, 2022).
[19] *Dearth*, at *17.
[20] *Teamster Members Retirement Plan v. Dearth*, 2023 WL 125659 (Del. Jan. 9, 2023).
[21] C.A. No. 2021-0728-JRS, 2021 WL 4775140 (Del. Ch. Oct. 13, 2021).
[22] C.A. No. 2021-1089-LWW, 2022 WL 453607 (Del. Ch. Feb. 14, 2022).

board on a "clear day" long before the proxy threat; (b) the provision was not "empty formalism" because it ensured that the nominating party had "skin in the game"; (c) there was no evidence of any manipulative conduct by the board or that the board applied the bylaws unfairly; and (d) plaintiff's "own delay"—waiting until the weekend before the nomination deadline to consider the nomination requirements—was what ultimately prevented it from satisfying the record holder requirement, not any action by the board. The case serves as a reminder that stockholders planning any kind of action should begin preparing as early as possible, thoroughly review a company's governing documents, and ensure that they are in compliance in order to avoid disqualification on technical grounds.

Corporate Charters Cannot Mandate Business Judgment Deference

Totta v. CCSB Financial Corporation involved a board's decision to interpret a charter provision prohibiting a stockholder from exercising more than 10% of the company's voting power in an election as permitting the board to aggregate multiple stockholders' holdings if it perceived the stockholders to be acting in concert with one another.[23] Relying on that interpretation, the board instructed the inspector of elections not to count any votes above 10% submitted by an insurgent together with his slate of nominees, and an entity affiliated with a nominee's father, which resulted in the insurgent's nominees losing the election. In the ensuing lawsuit, the company argued for business judgment deference because the charter purported to provide the board with "conclusive and binding" authority to construe the voting provision as long as the board acted in good faith. Following a trial on a paper record, Chancellor McCormick rejected this argument, reasoning that constitutive agreements for a corporation—as opposed to agreements for other entities, such as partnerships or LLCs—cannot modify the standard of review for director conduct. Accordingly, applying enhanced scrutiny under *Blasius*,[24] the Court determined that the board's aggregation violated the letter of the 10% voting provision because there was not enough evidence to show that the stockholders were acting in concert, and also found that the board lacked a "compelling justification" for interfering with the election.

"Corporate Neutrality" Limits Company Statements in a Contested Election

In re AeroJet Rocketdyne Holdings, Inc. stemmed from a "soured relationship" between the Company's CEO and its Executive Chairman that spilled into a proxy fight.[25] The eight-person board was deadlocked: the Chairman and three directors had one slate of nominees, and the CEO and three other directors had another. As part of the proxy contest, the CEO issued a press release in the name of the Company that criticized the Chairman and his slate. The Chairman and the directors aligned with him sought a temporary restraining order and declaratory judgment that the CEO and the directors aligned with her were not authorized to speak for the Company in connection with the election. Vice Chancellor Will granted the TRO and held a trial on the merits. In ruling against the CEO-aligned directors, the Court noted that their actions were unauthorized because the "default standard under Delaware law" required majority board approval, as did

[23] C.A. No. 2021-0173-KSJM, 2022 WL 1751741 (Del. Ch. May 31, 2022).
[24] *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988).
[25] C.A. No. 2022-0127-LWW, 2022 WL 2180240 (Del. Ch. June 16, 2022).

the company's bylaws. Further, the Court found that the CEO aligned directors had violated the principle of corporate neutrality, which requires a corporation to "remain neutral when there is a legitimate question as to who is entitled to speak or act on its behalf."[26] The Court ordered certain corrective disclosures, including retracting the challenged press release and explaining that the company takes no position on the outcome of the pending director election.

"Novel" Theory for Pleading Shareholder Derivative Claims

In ***Garfield v. Allen***, the Court of Chancery sustained what it described as a "novel" theory for pleading a breach of fiduciary duty.[27] The case involved an award of performance shares to the company's CEO that, under certain circumstances, would exceed the annual limit for such awards under the operative equity compensation plan. A stockholder sent a demand letter bringing the issue to the board's attention, but the board rejected the demand and determined that the board's compensation committee was within its authority to interpret the plan. The stockholder sued alleging that the compensation committee (which approved the award) violated the terms of the plan and that the board as a whole breached its fiduciary duties by failing to undo the challenged awards. As to the first claim, the Court readily found that the committee members knowingly violated the unambiguous limit set forth in the plan. The second claim, however, presented a "novel" question: whether the failure to act in response to a stockholder demand itself constitutes a breach of fiduciary duty. Despite observing that he found it "disquieting" that a plaintiff could "manufacture" a fiduciary duty claim by means of a demand letter, Vice Chancellor Laster allowed the claim to proceed, analogizing it to a *Caremark* claim where the "conscious inaction" of a director in the face of knowledge of corporate wrongdoing may constitute a breach of fiduciary duty. But the Court admitted "trepidation" about the effects of the ruling, and cautioned that, going forward, the Court should not permit plaintiffs to use demand letters to create a new claim, extend their time to file and avoid a laches defense, or ensnare additional members of a board who would not otherwise be subject to litigation.

***Caremark* Claims**

Speaking of *Caremark*, Vice Chancellor Glasscock recently noted that "derivative claims against corporate directors for failure to oversee operations—so-called *Caremark* claims, once relative rarities—have in recent years bloomed like dandelions after a warm spring rain, largely following the Delaware Supreme Court's opinion in *Marchand v. Barnhill.*"[28] But two decisions this year underscored that there is still a high bar to pleading a *Caremark* claim, even in the context of headline-grabbing corporate trauma. To meet that bar, a plaintiff must plead particularized facts under which it is reasonably conceivable to infer that the board either (i) utterly failed to implement any reporting system or controls or (ii) having implemented such system or controls, consciously failed to monitor them or ignored red flags. In other words,

[26] *In re Aerojet*, at *13.

[27] 277 A.3d 296 (Del. Ch. 2022).

[28] *Construction Industry Laborers Pension Fund v. Bingle*, 2022 WL 4102492, at *1 (Del. Ch. Sept. 6, 2022) (citing *Marchand v. Barnhill*, 212 A.3d 805 (Del. 2019)).

even pleading gross negligence in violation of the duty of care is not enough; rather, a plaintiff must allege a lack of oversight so extreme that it amounts to scienter, demonstrating bad faith.

In ***Construction Industry Laborers Pension Fund v. Bingle***, Vice Chancellor Glasscock dismissed a *Caremark* claim arising out of the 2020 Russian cybersecurity attack on SolarWinds.[29] Plaintiffs alleged that the board had failed to adequately oversee cybersecurity risk, even though it was "mission critical" for the software company. The Court determined that plaintiffs had not alleged that the directors allowed the company itself (as opposed to third-party criminal actors) to violate any positive law, and that the company was a "victim of a major crime." This is a similar outcome to that reached in a case last year related to a data breach at Marriott.[30] Although plaintiffs alleged that the company had not followed cybersecurity guidance from the SEC and NYSE, the Court found that the guidance was not a binding requirement that the company was obligated to follow. The Court noted that it was an "open question" whether directors may be held liable "solely on failure to monitor business risk."[31] But the Court declined to resolve that question, because it also found that plaintiffs had failed to allege bad faith under either *Caremark* prong. The allegations established that the board had put in place a reporting system, even if it was alleged to be "subpar," because two committees were charged with oversight of cybersecurity and one had met and received a report on the topic. The Court further concluded that plaintiffs had not alleged that the directors ignored red flags, because warnings related to cybersecurity threats had not risen to the director level. Plaintiffs have appealed the decision to the Delaware Supreme Court.

City of Detroit Police and Fire Retirement System v. Hamrock involved an explosion in a natural gas pipeline system controlled by a former subsidiary of NiSource, Inc.[32] A stockholder-plaintiff brought a *Caremark* claim against NiSource directors under three theories, all of which Chancellor McCormick rejected. First, plaintiff alleged that defendants failed to implement any reporting or monitoring system to oversee pipeline safety, which was "mission critical" for NiSource's natural gas business. However, plaintiff's own allegations—supported by documents obtained from a Section 220 demand—revealed that the board had an active and functioning committee tasked with overseeing safety issues. Second, plaintiff alleged that the board violated positive law in pursuit of profit, analogous to *In re Massey Energy Co*.[33] But the Court found lacking the "degree of lawlessness" at issue in *Massey* because, notwithstanding allegations of repeated regulatory violations and a long timeline for implementation of a compliance program, it was not reasonably conceivable that NiSource was "in the business" of unlawful conduct. Third, plaintiff claimed that the board ignored red flags regarding NiSource's repeated violations of pipeline safety laws, a theory that the Court found had "more heft," but ultimately failed because the red flags were "simply too general or disconnected from the root causes of the" explosion to "place a reasonable observer on notice of the corporate trauma that ensued."[34] For example, although the complaint

[29] C.A. No. 2021-0940-SG, 2022 WL 4102492 (Del. Ch. Sept. 6, 2022).
[30] *Firemen's Ret. Sys. of St. Louis v. Sorenson*, 2021 WL 4593777 (Del. Ch. Oct. 5, 2021).
[31] *Bingle*, at *7
[32] C.A. No. 2021-0370-KSJM, 2022 WL 2387653 (Del. Ch. June 30, 2022).
[33] C.A. No. 5430-VCS, 2011 WL 2176479 (Del. Ch. May 31, 2011).
[34] *Hamrock*, at *1.

adequately alleged that the board was aware of general risks associated with recordkeeping violations, it failed to allege that the board was aware of any specific dangers at the subsidiary posed by the recordkeeping issues. Accordingly, the case was dismissed.

Books and Records Actions Under DGCL § 220

As previously noted, books and records demands under Section 220 have proliferated in recent years as the Delaware courts have encouraged plaintiffs to use this tool to investigate potential fiduciary misconduct before filing suit, and a number of cases concerning Section 220 disputes went to trial in 2022. Although the Court of Chancery has typically applied close scrutiny to the reasonableness of a corporation's response to a Section 220 demand, it has also laid down markers for stockholders to prevent abuse. In particular, the Court has continued to reject demands for "informal" board materials, such as emails, absent "atypical" circumstances (although in one notable case, it did order the production of informal materials).

For example, in ***Oklahoma Firefighters Pension and Retirement System v. Amazon.com, Inc.***, the Court ruled against a stockholder who made a Section 220 demand on Amazon to investigate possible mismanagement and wrongdoing relating to antitrust compliance.[35] Following trial on a paper record, Vice Chancellor Will held that the stockholder failed to make a credible showing of possible mismanagement. In particular, the Court found that the various government investigations and inquiries upon which the stockholder relied had either closed without a finding of wrongdoing or otherwise lacked probative value. These investigations thus lacked the type of evidentiary "plus factor" found in prior Court of Chancery decisions, such as the existence of a government settlement with relevant factual allegations or a related *qui tam* action. The Court also rejected the stockholder's request for informal board materials in the absence of "atypical circumstances necessitating a broader inspection" of such materials, such as a failure to "honor traditional corporate formalities" or evidence of "wide-ranging mismanagement."[36]

Similarly, in ***Frank v. National Holdings Corporation***, Vice Chancellor Zurn rejected a stockholder's request for the production of certain informal board materials following a merger.[37] Like in *Amazon*, the company produced much of the materials demanded, but refused to produce "informal" board and management communications. The Court found that even though the stockholder's purpose was proper, the requests for officer communications went beyond his stated needs, and explained that a stockholder is entitled to what is essential, but no more than what is sufficient. The Court found that the informal communications sought were not essential because neither of the "atypical" *Amazon* factors were at play, i.e., there was no evidence of vast and wide-ranging wrongdoing, and "extensive and sufficient" formal board

[35] C.A. No. 2021-0484-LWW, 2022 WL 1760618 (Del. Ch. June 1, 2022).
[36] *Amazon*, at *12.
[37] C.A. No. 2021-0160 (Del. Ch. Jul. 22, 2022) (transcript ruling).

materials had already been produced by the company in addition to existing detailed public records concerning the merger.

By contrast, in ***Loren Trent Hightower v. SharpSpring***, Chancellor McCormick ordered limited production of informal board materials where a stockholder demonstrated inconsistencies between the proxy materials and the board minutes concerning SharpSpring's sale to Constant Contact, Inc.[38] After concluding that the stockholder stated a proper purpose—by demonstrating a credible basis to infer that the sales process was tainted by conflicts of interest—the Court ordered production of informal board and officer-level materials because the proxy statement and the board minutes contained "inconsistent accounts" of the events leading up to the decision to sell the company, demonstrating that the stockholder needed "more information."[39] However, the Court specifically suggested that the email productions should be limited to a small number of document custodians and a narrow date range.

In a separate area of Section 220 jurisprudence, the Delaware Supreme Court held that a stockholder may use "reliable" hearsay to establish a proper purpose in ***NVIDIA Corp. v. City of Westland Police and Fire Retirement System***.[40] Hearing an appeal from a corporation that was ordered to produce certain documents in response to a Section 220 demand, the Delaware Supreme Court held that a prior decision, *Thomas & Betts Corp. v. Leviton Manufacturing Co.*, 681 A.2d 1026 (Del. 1996), created an exception to the hearsay rule in Section 220 cases where the proffered hearsay was "sufficiently reliable." Since neither party argued that *Betts* was wrongly decided or should be reconsidered, the Court declined to revisit that decision. Future litigants may take up that invitation in later cases to challenge *Betts* and argue against a special carve out for "reliable" hearsay in the Section 220 context. Nonetheless, the Delaware Supreme Court reversed and remanded on the facts, finding that NVIDIA had been deprived of an opportunity to test the reliability of the proffered hearsay evidence. Specifically, the stockholders "refus[ed] to cooperate with [NVIDIA] regarding the identification of trial witnesses or affiants" and essentially prevented NVIDIA from taking depositions.[41] The Court warned that if stockholders are going to rely on hearsay evidence to establish a proper purpose, they must communicate honestly and early with the company regarding their intent to do so.

[38] C.A. No. 2021-0720-KSJM, 2022 WL 3970155 (Del. Ch. Aug. 31, 2022).
[39] *SharpSpring*, at *10.
[40] 282 A.3d 1 (Del. 2022).
[41] *NVIDIA*, at 23.

Appraisal Actions

The default measurement of fair value in appraisal actions remains the adjusted deal price (deal price minus synergies), so long as the sales process exhibits sufficient indicia of reliability.[42] However, there are instances in which the Court will diverge from that measure.

For example, the appraisal statute requires the Court to determine the value of the company at closing, not signing.[43] We previously highlighted *In re Appraisal of Regal Entertainment Group*, an unusual appraisal action in which Vice Chancellor Laster found that the fair value of the target was 2.6% higher than the adjusted deal price, because changes in tax laws between signing and closing increased the seller's value.[44] This year, we saw another instance in which the Court of Chancery deviated from adjusted deal price because of significant changes in the value of the seller between signing and closing. ***BCIM Strategic Value Master Fund v. HFF, Inc.*** involved the sale of HFF, Inc. ("HFF") to Jones Lang LaSalle ("JLL") for a mix of cash and JLL stock with an aggregate deal value of $49.46 per share at signing, which subsequently declined by 7.3% to $45.87 at closing because JLL's stock price had declined.[45] The petitioner exercised its statutory right to appraisal, arguing that the sales process was ineffective and that the Court should employ a discounted cash flow valuation methodology. The respondent argued for the use of adjusted deal price, which it calculated at $44.29 per share. After a trial, Vice Chancellor Laster determined that the sales process was sufficiently reliable and agreed with the respondent that $44.29 per share represented fair value at signing, but found that the fair value of HFF had increased by $2.30 per share between signing and closing due to HFF's "significant and durable" outperformance of market expectations. To quantify the magnitude of the change in value of HFF between signing and closing, the Court relied on expert testimony showing a regression analysis of historical changes in HFF's stock price against the percentage by which HFF beat market expectations. Based on this analysis, the Court determined that fair value was $46.59 per share.

Separately, in ***Ramcell, Inc. v. Alltell Corp., d/b/a Verizon Wireless***, the Court of Chancery rejected the inputs of both sides' expert valuation models and instead created its own valuation model.[46] Jackson Cellular Telephone Co., Inc. ("Jackson") merged with and into Alltel (a subsidiary of Verizon Wireless), which owned 90% of Jackson's outstanding common stock. In the short-form merger under DGCL § 253, the petitioner's stock in Jackson was canceled and converted into the right to receive the merger consideration of $2,963 per share. The petitioner exercised its appraisal rights, and the case went to trial. Both sides agreed that Jackson should be valued exclusively using a discounted cash flow methodology. Respondent's expert opined that Jackson's per-share value was $5,690, while petitioner's expert opined that it was $36,016. Vice Chancellor Fioravanti concluded that neither side presented persuasive valuations.

[42] *See*, *e.g.*, *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128 (Del. 2019); *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 177 A.3d 1 (Del. 2017); *DFC Global Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346 (Del. 2017).

[43] 8 *Del. C.* § 262.

[44] C.A. No. 2018-0266-JTL, 2021 WL 1916364 (Del. Ch. May 13, 2021).

[45] C.A. No. 2019-0558-JTL, 2022 WL 304840, at *1 (Del. Ch. Feb. 2, 2022).

[46] C.A. No. 2019-0601-PAF, 2022 WL 16549259, at *1 (Del. Ch. Oct. 31, 2022).

Having rejected both models, the Court created two versions of its own model. The first used respondent's financial projections (derived from management) and received a weight of 70%. The second incorporated revenue projections from petitioner and received a weight of 30%. The Court ascribed more weight to respondent's projections because they were grounded in historical management models. The Court likewise employed a blended approach to determine the discount rate, and calculated the appropriate per share value that was four times the original consideration, at $11,464 per share.

Sandbagging

In ***Arwood v. AW Site Services***, the Court of Chancery held that "Delaware is a 'pro-sandbagging jurisdiction.'"[47] In this context, "sandbagging" is when a buyer knows that a representation or warranty made by the seller is false, but closes on a transaction anyway and then seeks damages for the breach after the close. In the case, the seller was financially unsophisticated, and had granted the buyer unfettered access to the business over the course of a months-long diligence process, so that the buyer could prepare a detailed set of financial statements for the seller and perform a valuation. After the close, the buyer discovered an issue, refused to release certain funds from escrow, and brought claims for breach of warranty. Vice Chancellor Slights held that the seller could not assert that the buyer had "sandbagged" it as a defense, especially because the terms of the purchase agreement expressly permitted sandbagging.[48] The Court explained that a sandbagging defense is "inconsistent with our profoundly contractarian predisposition," and unlike fraud claims, breach of contract claims do not require justifiable reliance or a showing of scienter.[49] The Court also held that the case before him did not actually implicate sandbagging, because sandbagging is only implicated where the buyer had *actual* knowledge of the misrepresentation before the closing, and whether the buyer should have known or was recklessly indifferent is irrelevant. Thus, sellers seeking to preserve the availability of a sandbagging defense likely must include specific "anti-sandbagging" provisions to that effect in their contracts.

Reliance on Counsel Legal Opinions

In ***Boardwalk Pipeline Partners, LP v. Bandera Master Fund LP***, the Delaware Supreme Court reversed the Court of Chancery's decision awarding approximately $690 million in damages for the breach of a partnership agreement.[50] Boardwalk Pipeline Partners, LP ("Boardwalk") was a holding company for subsidiaries operating interstate pipeline systems for natural gas. Loews Corporation ("Loews") controlled Boardwalk through its general partner. Boardwalk's partnership agreement contained a call right permitting Loews to acquire Boardwalk if two conditions were satisfied. The first condition required that Loews receive an opinion from counsel that the partnership's favored tax status "has or will

[47] C.A. No. 2019-0904-JRS, 2022 WL 705841 (Del. Ch. Mar. 9, 2022).
[48] *Arwood*, at *29 (discussing the "Risk Allocation" provision in the Asset Purchase Agreement that "expressly allow[ed]" for sandbagging).
[49] *Arwood*, at *3.
[50] 2022 WL 17750348 (Del. Dec. 19, 2022).

reasonably likely in the future have a material adverse effect on the maximum applicable rate that can be charged to customers."[51] The second condition was that Boardwalk's general partner was required to determine that the opinion of counsel was acceptable. In March 2018, the Federal Energy Regulatory Commission announced non-final regulatory policies that could have rendered master limited partnerships an undesirable investment vehicle for pipeline companies, and Loews caused Boardwalk's general partner to exercise the call right after receiving an opinion from counsel finding that changes in certain tax attributes of the partnership would be reasonably likely to have a material adverse effect on the rate of services that Boardwalk would be able to charge to its customers, and after Boardwalk's sole member determined that the opinion was acceptable.

In a lengthy post-trial opinion, Vice Chancellor Laster determined that neither condition had been satisfied.[52] With respect to the first condition, the Court of Chancery held that the opinion of counsel supporting the exercise of the call right had not been issued in good faith. The Court determined that the counsel issuing the opinion had "knowingly made unrealistic and counterfactual assumptions, knowingly relied on an artificial factual predicate, and consistently engaged in goal-directed reasoning to get the result that Loews wanted," including a knowingly false determination that the regulatory proposals were sufficiently final to trigger the call right.[53] The Court further observed that the "non-explained opinion" was rendered by a "non-Delaware firm" on a matter of Delaware law upon which Delaware attorneys had declined to opine. With respect to the second condition, the Court held that the partnership agreement required Boardwalk's general partner's board of directors to determine that the legal opinion was acceptable, rather than the Loews subsidiary that served as the general partner's sole member. The Court also found that the exculpatory provisions in the partnership agreement did not protect the general partner from liability because there had been willful misconduct in exercising the call right.

The Delaware Supreme Court disagreed, and took a far more deferential approach to the language of the partnership agreement, which granted broad discretionary authority to the general partner and provided a conclusive presumption of good faith when relying on advice of counsel.[54] The Supreme Court also noted that there had been clear disclosure provided to investors about that broad authority. The Supreme Court did not reach the issue of whether the legal opinion was provided in good faith, but ruled that the general partner had been reasonable in relying on it, based on a separate legal opinion it obtained from a different law firm. Accordingly, it found that Loews was exculpated under the agreement, and reversed. Justice Valihura issued a concurring opinion saying that the Court of Chancery had applied the wrong standard of review to the legal opinion, viewing it "through a *de novo* lens," when precedent required a more deferential

[51] *Boardwalk Pipeline Partners, LP*, at *1.
[52] *Bandera Master Fund LP v. Boardwalk Pipeline Partners, LP*, 2021 WL 5267734 (Del. Ch. Nov. 12, 2021).
[53] *Bandera Master Fund LP*, at *2.
[54] *See Boardwalk Pipeline Partners, LP*, at *1.

standard. Furthermore, the concurring opinion pointed to certain facts in the record that could support a conclusion that the legal opinion "was rendered in good faith, and at a minimum, was not rendered in bad faith."[55]

Equitable Defenses to Contractual Voidness

In ***XRI Investment Holdings LLC v. Holifield***, the Court of Chancery issued an instructive post-trial opinion regarding an analytically difficult corner of Delaware law regarding the availability of equitable defenses, including where parties contract in advance that an act shall be void.[56] In *XRI Investment*, the Court evaluated the validity of a transfer by a member of LLC units to a separate LLC he owned. XRI's LLC Agreement contained a provision generally prohibiting members from transferring their membership interests, and a separate provision specifying that any transfer in violation of the LLC Agreement was void. The Court held in this post-trial opinion that the transfer was void, citing the Delaware Supreme Court's precedent in *CompoSecure, L.L.C. v. CardUX, LLC*, in which the Delaware Supreme Court held that parties could contractually specify certain actions to be, effectively, incurably void.[57] Nevertheless, Vice Chancellor Laster specifically observed that this caused an "inequitable result," because the facts at trial demonstrated that the limited liability company had full knowledge of its rights and all material facts regarding the transfer, "yet remained inactive for more than two years as part of a calculated legal and business strategy."[58] The Court noted that, but for *CompoSecure*, it would have held that the disputed transfer was not void because the limited liability company had equitably acquiesced to the transfer. Accordingly, in dicta, the *XRI Investment* opinion proposes an alternative approach, where Delaware courts would restrict their determinations that corporate acts are "void *ab initio*" only "to those acts that contravene limitations imposed by the state" (such as those limits set forth in statute).[59] By contrast, agreements between private parties that corporate acts are void would remain subject to equitable defenses, including the defenses waiver, acquiescence, and estoppel, essentially rendering the act voidable, rather than void. It remains to be seen whether the Court of Chancery's proposed approach will be adopted by the Delaware Supreme Court. In the meantime, practitioners should heed the Court's caution that, under current law, contractually specifying that an act is void *ab initio* will eliminate the flexibility to later ratify the action if the parties desire to do so.

[55] *See Boardwalk Pipeline Partners, LP*, at *39.

[56] 283 A.3d 581 (Del. Ch. 2022).

[57] 206 A.3d 807 (Del. 2018).

[58] *XRI Investment Holdings LLC*, at 621.

[59] *Id.* at 666.

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