February 13, 2017

# Delaware Supreme Court Confirms Tender Offer and Vote Equivalence in Determining Standard of Review for Post-Closing Damages

## Delaware Supreme Court Summarily Affirms Court of Chancery Ruling

### SUMMARY

On February 9, 2017, in *Lax* v. *Goldman, Sachs & Co.*,[1] the Delaware Supreme Court summarily affirmed the Court of Chancery's decision in *In re Volcano Corp. Stockholder Litig.*[2] that held that business judgment review applied to a change of control transaction structured as a tender offer and merger under Section 251(h) of the Delaware General Corporation Law and was not subject to rebuttal once the Court concluded that a majority of fully informed, uncoerced, disinterested stockholders tendered into the offer.

The Delaware Supreme Court's affirmance of the Court of Chancery's decision makes clear that *Corwin* v. *KKR Fin. Holdings, LLC's*[3] standard of reducing post-closing review of transactions to business judgment in the face of a fully informed, uncoerced, and disinterested stockholder decision applies whether that decision is by vote or by a tender into a Section 251(h) offer. And, because waste is an almost futile claim (stockholders are not likely to approve waste), the approval of a transaction by a fully informed, disinterested and uncoerced vote is likely to lead to dismissal of any post-closing action.

The extension of the *Corwin* cleansing effect to a Section 251(h) transaction permits directors and others to avail themselves of the same post-closing protection of their decision-making that would be provided under a one-step merger process. In affirming the Court of Chancery's decision, the Supreme Court once again makes clear that the enhanced scrutiny of *Revlon* more properly should be exercised in the context

of pre-closing injunctive relief, and that Delaware courts increasingly will be reluctant to second-guess the judgment of fully informed and uncoerced stockholders.

## BACKGROUND

On December 16, 2014, Volcano Corporation entered into a merger agreement with Philips Holding USA Inc. Under the agreement, Philips agreed to tender for all of Volcano's outstanding shares at $18.00 per share through a two-step tender offer and merger transaction under Section 251(h) of the DGCL that does not require a stockholder vote. Philips commenced the tender offer on December 30, 2014. After stockholders sought to enjoin the merger, alleging, among other things, that the Volcano directors breached their fiduciary duties by omitting material information from Volcano's Schedule 14D-9 recommendation to stockholders, Volcano made supplemental disclosures, and those plaintiff stockholders withdrew their preliminary injunction motion.

More than 89% of Volcano's shares were tendered into the tender offer, and shortly thereafter the merger was consummated. On March 2, 2015, the plaintiff stockholders filed an amended complaint asserting, among other things, fiduciary duty claims against Volcano's directors, and seeking post-closing damages. On June 30, 2016, the Court of Chancery dismissed the complaint in its entirety.[4]

## THE CHANCERY COURT DECISION

The Court of Chancery (VC Montgomery-Reeves) dismissed the challenge, holding that consistent with the recently decided Delaware Supreme Court decisions in *Singh* v. *Attenborough*[5] and *Corwin*, the business judgment rule applies "irrebuttably" where a majority of a company's fully informed, uncoerced, disinterested stockholders have tendered into a tender offer. As a result, in the absence of waste, the Court of Chancery held, the plaintiffs' claims must be dismissed. The Vice Chancellor held that the cleansing effect of *Corwin* extended beyond stockholder-approved mergers to "voting" by tendering pursuant to a Section 251(h) merger. In so holding, the Court rejected plaintiffs' assertions that a first-step tender offer under Section 251(h) offers inferior protections to stockholders than those provided under a stockholder vote in a one-step merger and thus does not warrant business judgment review:

- A target corporation's board has the same fiduciary and disclosure obligations with respect to the transaction;
- Section 251(h) alleviates the coercion to which stockholders might otherwise be subject in a tender offer because the first-step tender offer is for all outstanding stock, the second-step must be effected as soon as practicable and for the same consideration as the first-step tender offer, and appraisal rights are available as an alternative challenge; and
- The policy considerations underlying the cleansing effect of a stockholder vote apply equally to a tender offer because "[a] stockholder is no less exercising her 'free and informed chance to decide on the economic merits of a transaction.'"[6]

Having determined that *Corwin* applied to a Section 251(h) transaction, the Court found as a factual matter that Volcano's stockholders were fully informed as to all material facts regarding the transaction, making business judgment the applicable standard of review, and leaving only what the Supreme Court has characterized as a "vestigial" waste challenge to the transaction. The plaintiffs failed to plead that the transaction constituted waste, and absent waste the Court found no basis for a breach of fiduciary duty claim against the Volcano directors.

On appeal, plaintiffs did not dispute that the Volcano stockholders were fully informed. Instead, plaintiffs challenged the notion that business judgment review "irrebuttably" applies in this context. At oral argument, the Delaware Supreme Court made clear that "irrebuttable" simply means that, once plaintiffs fail to plead a viable claim challenging the disclosures, the business judgment rule is irrebuttable to the extent that it may not be overcome through allegations that the transaction was tainted by breaches of fiduciary duty. Chief Justice Strine stated that "what that means in that context is that the game is over for [plaintiffs]. [Plaintiffs had the] chance to show [a failure in the approval process] and [plaintiffs] have not been able to do it."[7]

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[1] No. 372, 2016, slip op. at 1 (Del. Feb. 9, 2017).

[2] 143 A.3d 727, 738 (Del. Ch. 2016) (hereinafter *Volcano*).

[3] 125 A.3d 304 (Del. 2015) (hereinafter *Corwin*). For a previous publication, *see* SULLIVAN & CROMWELL LLP CLIENT MEMORANDUM, *Corwin v. KKR Financial Holdings LLC* (Updated Oct. 5, 2015).

[4] Sullivan & Cromwell LLP represented Philips in the pre-closing challenge, obtaining dismissal of Philips as a defendant, and represented Volcano in the post-closing challenge before the Court of Chancery and the Delaware Supreme Court.

[5] 137 A.3d 151 (Del. 2016).

[6] *Volcano*, at 743-45 (quoting *Corwin*, 125 A.3d at 312-13).

[7] For a video of the oral argument, *see* 2017-02-08 372, 2016 *Lax* v. *Goldman Sachs*, https://livestream.com/DelawareSupremeCourt/events/6961090/videos/148866238 (last visited Feb. 13, 2017).

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