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Delaware Chancellor Raises the Standard for Pricing Mootness Fees for Supplemental Disclosures

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In a precedential decision on July 6, 2023, the Delaware Court of Chancery lowered stockholder-plaintiffs' incentives to pursue meritless deal litigation by raising the standard that supplemental disclosures must meet to justify an award of attorneys' fees from "helpful" to "material." *Anderson v. Magellan Health, Inc., et al.* -- A.3d ---, C.A. No. 2021-0202-KSJM.

Much ink has been spilled regarding the shift in merger-related disclosure claims to federal court after the Delaware Court of Chancery announced in *Trulia* that it would approve disclosure-only settlements only where the additional information is "plainly material." Because the merger tax levied by these strike suits continues to plague Delaware corporations—typically now in the form of a "mootness fee" to settle stockholder claims on an individual, rather than class-wide, basis—Delaware Chancellor Kathaleen St. J. McCormick recently announced in *Anderson v. Magellan Health, Inc.* that the Court of Chancery is raising the standard for pricing supplemental disclosures in mootness-fee proceedings from merely "helpful" to "material." The Chancellor also provided guidance regarding the corporate benefit doctrine and how Delaware courts interpret case law applying it.

Under the corporate benefit doctrine, Delaware courts may award fees to plaintiffs' counsel for the beneficial results they produce for a defendant corporation even without a favorable adjudication. In *Magellan*, the Court of Chancery revisited standards for pricing corporate benefits that it adopted in 2016. The Chancellor's decision will likely reduce the overall amount of attorneys' fees and expenses paid by corporations to resolve stockholder litigation providing no discernable benefit to stockholders, and may reduce the volume of meritless disclosure demands in M&A transactions.

Factual Background

The complaint filed in *Magellan* challenged Magellan Health, Inc.'s (the "Company") 2021 acquisition by a managed care company (the "Buyer"). A Company stockholder claimed that certain deal protections from an abandoned sale process in 2019 impeded the more recent sale to the Buyer and were inadequately described in the Company's proxy. The Company responded by loosening the deal protections and issuing supplemental disclosures, which mooted the plaintiff's claims. Loosened deal protections and supplemental disclosures are common forms of non-monetary benefits.

In subsequent mootness-fee proceedings, the plaintiff petitioned the Court of Chancery for an award of attorneys' fees and expenses. The plaintiff argued that its litigation resulted in corporate benefits worth more than $1 million. The Company argued in opposition that the benefits were worth approximately $100,000. After reexamining Delaware's standards for pricing non-monetary corporate benefits, the court sided with the Company and awarded only $75,000 in fees and expenses.

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Loosened Deal Protections

Delaware law recognizes a corporate benefit in this context because, "[a]s a theoretical matter, loosening deal protection devices makes topping bids more likely." In *Magellan*, the plaintiff sought over $1 million in fees for causing the Company to waive don't-ask-don't-waive provisions that continued to bind three potential bidders from an abandoned 2019 sale process. Rejecting the plaintiff's application of Delaware law, the court found that the waivers "d[id] not justify a fee award" because "the increased likelihood of a topping bid was close to zero."

The court rejected the plaintiff's application of Delaware law for two reasons. First, the plaintiff improperly omitted "the qualitative evaluation of the increased likelihood of a topping bid *due to the plaintiff's efforts*." Under a proper reading of Delaware precedent, the plaintiff was not entitled to full credit for the likelihood of a topping bid, only "the increased likelihood (if any) of a topping bid generated by the [w]aivers." The plaintiff also erred in assuming the waivers increased the likelihood of a topping bid. In the court's analysis of the likelihood of a topping bid, it found that two potential bidders had not expressed serious interest in the Company and the waiver released the third bidder only one day early.

Second, the plaintiff improperly relied on Court of Chancery decisions issued in 2014 or earlier for the resolution of claims challenging don't-ask-don't-waive provisions. The court found the plaintiff's reliance on these decisions was misplaced because (i) they were "issued at a time when Delaware courts were still developing their views on don't-ask-don't-waive provisions," (ii) "[e]ach involved far greater effort from the plaintiffs' counsel than [the plaintiffs] invested in this case," and (iii) "each achieved far more than [the plaintiffs] achieved here." Finally, and perhaps most importantly, the court criticized the plaintiffs' reliance on precedent decisions predating doctrinal shifts in 2015 and 2016—including the court's decision in *Trulia*—and it characterized such precedents as "less useful in determining the value of otherwise comparable benefits."

Supplemental Disclosures

Supplemental disclosures also can provide a compensable corporate benefit under Delaware law. According to the court, however, "developments in deal litigation since" 2016 warrant reexamining "the standard for pricing that benefit."

In 2016, the Court of Chancery announced new standards for pricing supplemental disclosures in settlement-approval proceedings and mootness-fee proceedings. In *Trulia*, the court held that it would only approve disclosure-only settlements where the disclosures were "plainly material"—that is, where the supplemental disclosures procured met a higher materiality standard than the one applied when determining whether a disclosure claim is adequately pleaded. The court also concluded that mootness-fee proceedings were a preferable mechanism for pricing the corporate benefit resulting from the supplemental disclosures. In mootness-fee proceedings a few months later, however, the court declined to apply the defendant-friendly "plainly material" standard announced in *Trulia*. Instead, in *Xoom*, it "ratchet[ed] down the standard from 'material' to 'helpful.'"

The effect of these decisions was significant. *Trulia* incentivized plaintiffs to repackage fiduciary duty claims as federal securities claims and file them in federal courts, which limited the Court of Chancery's opportunities to clarify Delaware policy on disclosure-based mootness fees. *Xoom* incentivized plaintiffs to pursue weak or meritless disclosure claims expecting that defendants would rather issue supplemental disclosures and pay a mootness fee than expend the resources necessary to defend weak or meritless litigation.

Troubled by "a rule that seems to encourage the pursuit of legally meritless disclosure claims" and the resulting "merger tax of deal litigation" that "continues to plague Delaware corporations" in other courts, the Chancellor announced a new standard for pricing supplemental disclosures in mootness-fee proceedings. Barring disagreement by

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the Delaware Supreme Court, “mootness fees based on supplemental disclosures” are available under Delaware law “only when the information is material.”

Because the parties in *Magellan* had not argued for the heightened standard, however, the court applied *Xoom* one last time. The supplemental disclosures at issue were “marginally helpful” because they “provided a more easy-to-read summary of the existence, terms, and operation of the standstills, including why Magellan did not believe that certain of its standstill obligations impeded the sale process.” Based on “one post-*Trulia* academic survey” and “the limited set of court-ordered mootness fees awards post-*Trulia*,” the court valued the Company’s supplemental disclosures at $75,000.

Key Takeaways

Chancellor McCormick wrote the precedential decision in *Magellan* in response to the plaintiff’s “eye-popping request for $1,100,000,” which caught the attention of two professors who filed amicus briefs urging the Court of Chancery to “issue a written decision to warn other courts applying Delaware law of these policy concerns.” The following key takeaways should guide practitioners and jurists applying Delaware law.

- When pricing mootness fees, courts applying Delaware law should apply a “materiality” standard rather than the “helpful” standard originally announced in *Xoom*. Because Delaware has adopted the federal standard for materiality in the stockholder disclosure context, this means that courts will only award mootness fees “if there is a substantial likelihood that a reasonable shareholder would consider” the supplemental disclosures “important in deciding how to vote” or tender shares.
- Chancellor McCormick clearly instructed courts applying Delaware law to give less weight to corporate benefit cases pre-dating *Trulia*, because “*Trulia* and other doctrinal changes in Delaware law adopted around that time” drove “an overall decline in settlements and fee awards” that “renders pre-*Trulia* precedent less useful in determining the value of otherwise comparable benefits.” Practitioners and non-Delaware courts should be mindful of this guidance when relying on pre-*Trulia* corporate benefit cases applying the materiality standard.
- It is hornbook law that plaintiffs are only entitled to compensation for the incremental value of a corporate benefit they cause. In *Magellan*, the Court of Chancery clarified how practitioners and courts should analyze the incremental value of loosened deal protections. In this context, pricing the incremental value created by a plaintiff requires a fact-specific “*qualitative* evaluation of the increased likelihood of a topping bid,” implicating the range of protections loosened, the nature and effect of each loosened protection, and the nature and extent of interest expressed by potential bidders who benefited from the loosened protections.
- The decision will likely reduce the overall amount of attorneys’ fees and expenses paid by Delaware corporations to settle stockholder litigation providing no discernable benefit to stockholders. The falling price may also reduce the overall volume of demands for supplemental disclosures.

The Court’s opinion is available here.

The following Gibson Dunn attorneys assisted in preparing this client update: Jonathan D. Fortney, Brian M. Lutz, and Mark H. Mixon, Jr.

Gibson Dunn lawyers are available to assist in addressing any questions you may have regarding the developments in the Delaware Court of Chancery. Please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any of the following leaders and members of the firm’s Securities Litigation, Securities Regulation and Corporate Governance, Mergers and Acquisitions, or Private Equity practice groups:

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