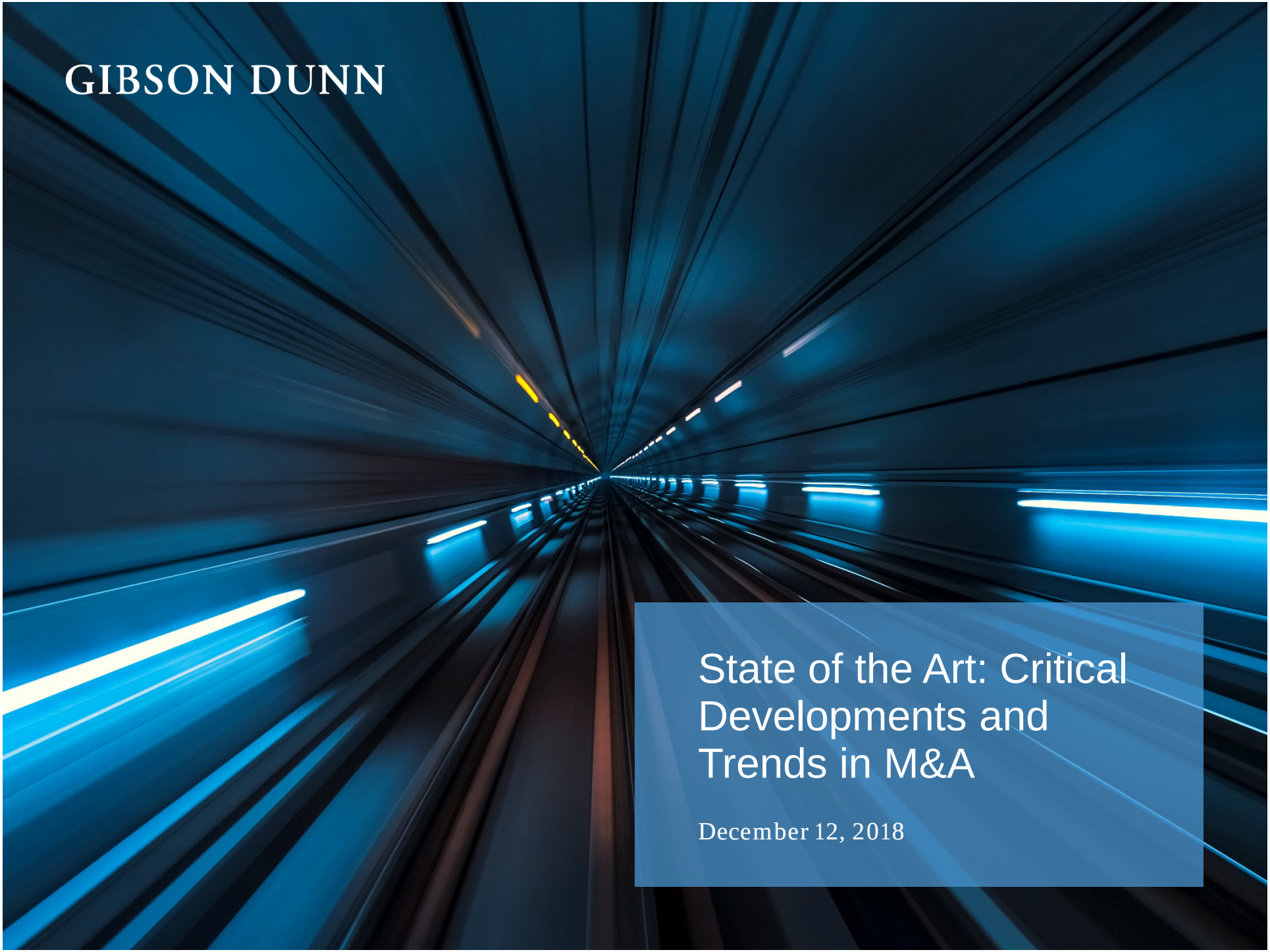

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State of the Art: Critical Developments and Trends in M&A

December 12, 2018

Today's Discussion

1. Private Equity Buyers: Latest Financing Constructs
2. The Future of MAE Clauses
3. Representation and Warranty Insurance Developments
4. Delaware Statutory Appraisal Actions
5. New Representations and Warranties in Purchase Agreements
6. Delaware Case Law Developments
7. Developments in Drag-Alongs

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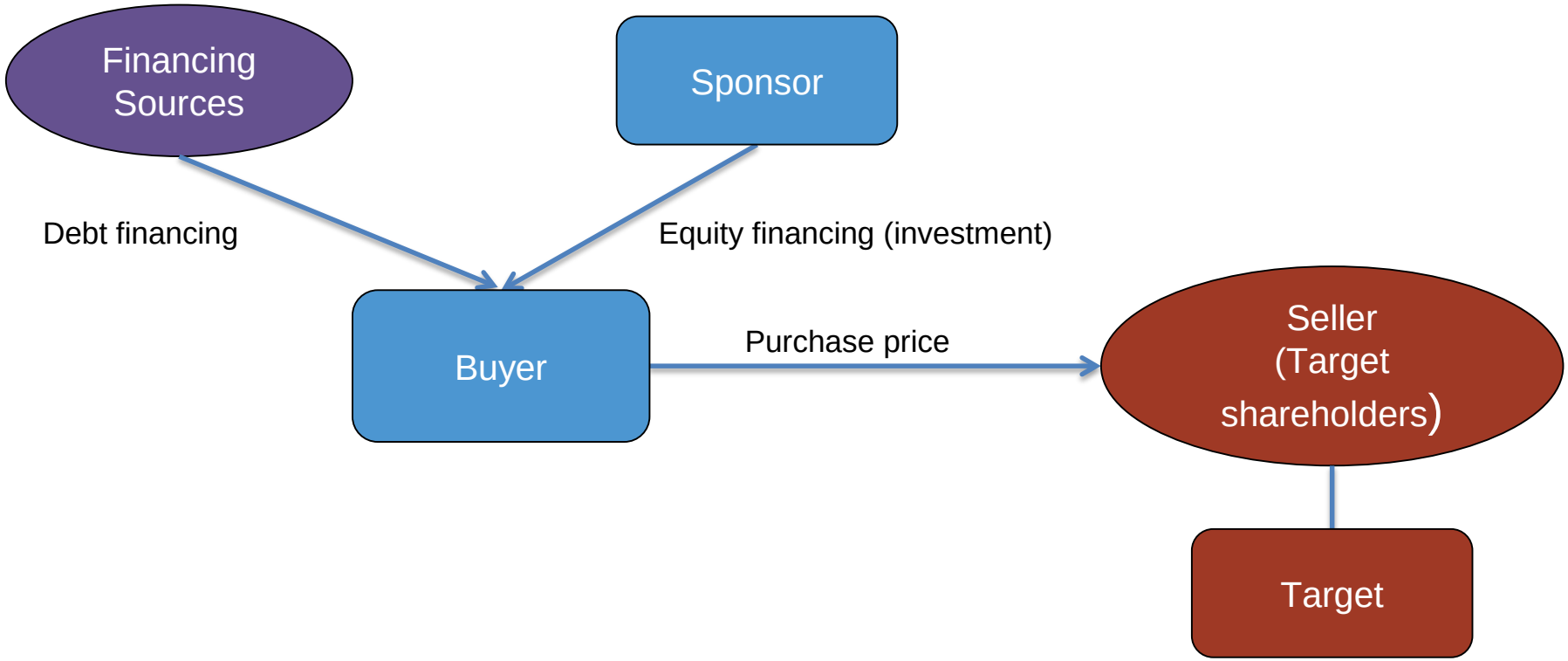
Private Equity Buyers: Latest Financing Constructs

Acquisition Financing Overview

Many acquisitions are funded with a combination of **equity financing** (Buyer or Buyer-affiliates) and **debt financing** (lenders):



Typical Private Equity Financing Construct

- At signing, Buyer provides debt commitment letters from lenders and an equity commitment letter from Sponsor
- The purchase agreement includes:
    - representations and warranties by Buyer regarding the debt and equity commitment letters
    - covenants by Buyer regarding obtaining the financing under the debt commitment letters
    - covenants obligating Seller and Target to cooperate in Buyer's financing efforts
    - termination right exercisable by Seller if (a) all conditions to closing are satisfied, (b) Seller is ready, willing and able to close and (c) Buyer fails to close
    - reverse termination fee payable by Buyer as liquidated damages (with possible exceptions for willful/intentional breach) if the purchase agreement is terminated by Seller as described in the immediately preceding bullet or when Seller terminates due to a Buyer breach
    - specific performance remedy available to Seller, as an alternative to reverse termination fee, to force Buyer to draw down on the equity commitment letter and close if (a) all closing conditions are satisfied, (b) the debt financing will fund at closing, (c) Seller is ready, willing and able to close and (d) Buyer fails to close
    - lender protective provisions
- At signing, Sponsor provides a limited guarantee for payment of the reverse termination fee

New Developments in Private Equity Financing Construct

- Sponsor provides an equity commitment letter for 100% of the purchase price
- Purchase agreement includes:
    - representations and warranties by Buyer regarding the equity commitment letter
    - covenants obligating Seller and Target to cooperate in Buyer's debt financing efforts
    - termination right exercisable by Seller if (a) all conditions to closing are satisfied, (b) Seller is ready, willing and able to close and (c) Buyer fails to close
    - reverse termination fee payable by Buyer as liquidated damages (with possible exceptions for willful/intentional breach) if the purchase agreement is terminated as described in the immediately preceding bullet or when Seller terminates due to a Buyer breach
        - reverse termination fee percentage of purchase price may be higher than the RTF in a typical PE financing construct deal
    - specific performance remedy available to Seller to force Buyer to draw down on the equity commitment letter and close if (a) all closing conditions are satisfied, (b) Seller is ready, willing and able to close and (d) Buyer fails to close
    - lender protective provisions
- At signing, Sponsor provides a limited guarantee for payment of the reverse termination fee

Considerations re. New Financing Construct

- Allows Buyer to eliminate some of the noise around financing uncertainty because Sponsor is on the hook for the entire purchase price
- Provides Seller with optionality to force closing through specific performance remedy (whether or not debt financing is prepared to fund) or collect a (potentially larger-than-normal) reverse termination fee
- Buyer still goes through its typical process of lining up debt commitment letters at signing to ensure that it has a debt financing source to fund the debt piece of the purchase price on acceptable terms
- Buyer needs to ensure that the purchase agreement (through HSR waiting period, designated interim period or otherwise) provides sufficient time for Buyer to negotiate and document the debt financing before closing is required to occur

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The Future of MAE Clauses

Fresenius: Is there a new MAE paradigm?

- Brief Background:
  - April 24, 2017, Fresenius Kabi AG agrees to acquire Akorn, Inc.
  - Shortly after stockholders approve merger, Akorn announced year-over-year declines in quarterly revenues, operating income and EPS of 29%, 84% and 96%
  - Declines persisted in every subsequent quarter
  - Late 2017 and early 2018, Fresenius received anonymous whistleblower letters
  - April 2018, Fresenius terminates merger agreement
- Chancery Court (V.C. Laster) in a 246-page decision marks first time a court has determined that a buyer validly terminated a merger agreement due to an MAE
  - MAE definition was typical formulation (general description of events that would create an MAE, followed by number of exclusions allocating risk between the parties)
  - V.C. Laster went to extraordinary lengths discussing the history between the parties (and the behavior of Acorn) before reaching his decision
    - Long-Term Business Downturn
    - Whistleblower Letters
    - Operational Changes

Fresenius: Is there a new MAE paradigm?

- On December 7, 2018, DE Supreme Court summarily affirmed Laster's decision
- Takeaways:
  - Continuing High Bar to Establishing an MAE
  - Highly Egregious Facts
  - MAE as Risk Allocation Tool
  - Target Evaluated on Stand-alone Basis
  - Parties Response to Perceived MAE (prior to termination)
- Drafting Considerations
  - Is status quo sufficient?
  - Words matter
  - Will parties now need to address risk allocation for "unknown/unforeseen" events (previously implied in the IBP decision)?
  - Should parties address synergies (in a strategic deal)?

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Representation and Warranty Insurance Developments

Representation and Warranty Insurance – General Overview

- Purpose: Alternative source of recovery for losses as a result of breaches of representations and warranties in connection with merger and acquisition transactions
- Availability: The insurance product was introduced in the 1990s and has increased in availability
- Industry Sectors: All
- General trends: Widely available, continuing decline in premiums (2-4% of coverage limit), most policies (80%+) are buy-side policies
- Prognostics: The R&W insurance policy market continues to be fluid as more insurers join the market and terms continue to evolve / change

Representation and Warranty Insurance – Trends

- Prevalence of R&W Insurance Policies: Of private target deals surveyed, 29% of deals included a R&W insurance policy (explicitly contemplated by purchase agreement). The number does not account for R&W insurance policies that were bought by buyer ex-agreement.(1)
- Sole Source of Recovery(2) – Private target deals surveyed are split on this issue of whether buyer can recover against seller if the R&W insurance policy recovery is exceeded or otherwise unavailable:
- R&W insurance policy is the sole source of recovery for all reps in 23% of agreements and for non-fundamental reps in 18% of agreements.
- Only 20% of surveyed agreements expressly state that RWI is not the sole source for recovery.

(1) 2017 Private Target Study
(2) 2017 Private Target Study

Representation and Warranty Insurance – Trends

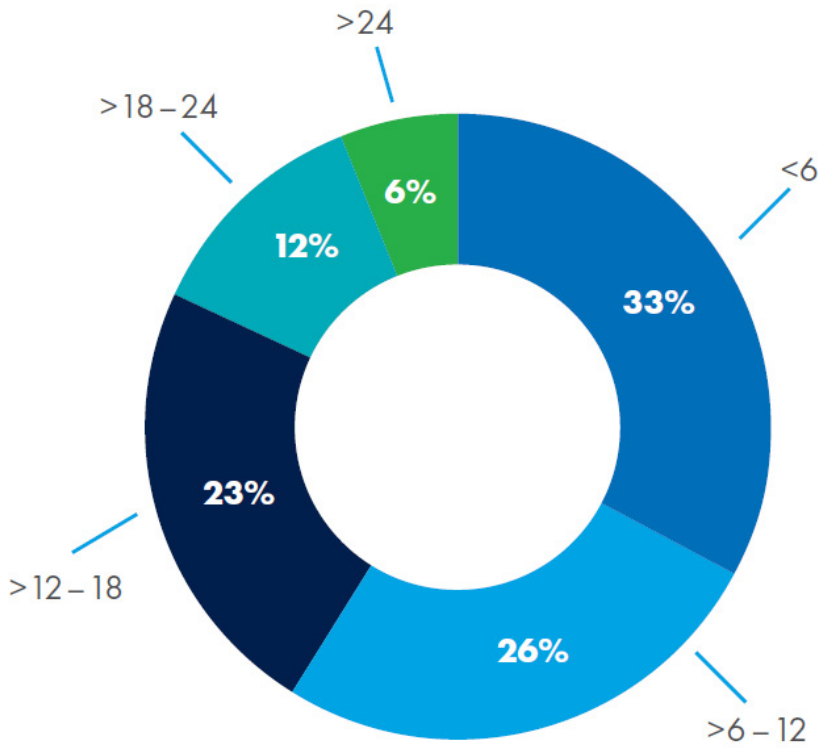
- **Zero Seller Recourse**
  - Buyer absorbs losses for the deductible / basket amount and the R&W insurance policy covers any losses in excess of that amount up to the coverage limit
  - Previously, the use of R&W insurance was predicated on the seller having "skin in the game" by requiring that the seller pay any retention under the R&W insurance policy
  - Increased competition among carriers providing R&W insurance policies leading to more policies being underwritten without recourse to seller without an increase to the premium of a similar R&W insurance policy with recourse to seller
- **Broader Scope of Coverage and Reduced Exclusions**
  - Historically, issues with known risk (e.g., regulatory matters, wage and hour liability, governmental payments, taxes) were excluded from coverage under R&W insurance policies
  - Trend today is to exclude specific issues rather than broad category exclusions
  - Insurers conduct thorough diligence to reduce exclusions as much as possible
- **More Claims**
  - The increase in R&W insurance policies has also led to an increase in claims filings – nearly one in five R&W insurance policies surveyed received a claim notification(1)

(1) AIG Claims Intelligence Series: M&A Insurance – The New Normal? Global MA Claims Intelligence 2018

Representation and Warranty Insurance – Trends

Timing of Claims – 80% of claim notifications are made within 18 months of closing[(1)]

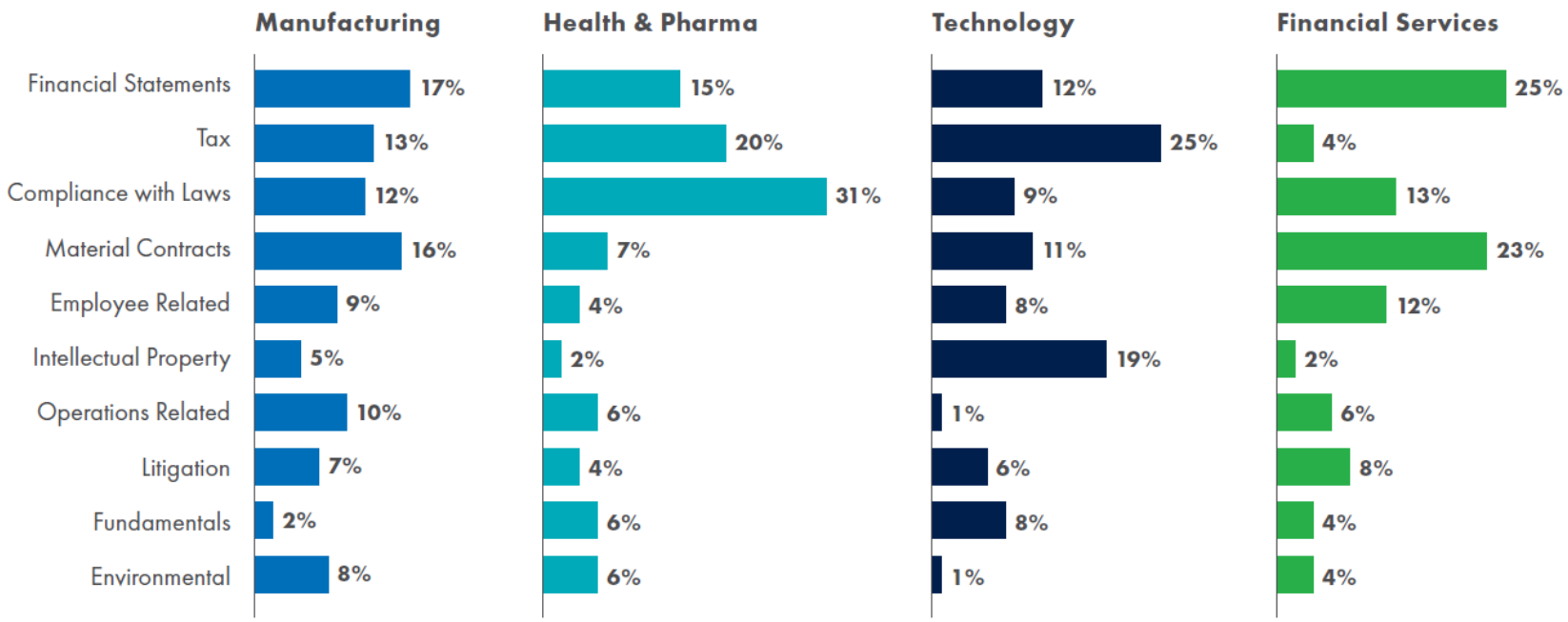
- 33% of claim notifications are made within the first 6 months of closing
- 26% of claim notifications are made between 6 and 12 months of closing
- 23% of claim notifications are made between 12 and 18 months of closing



(1) AIG Claims Intelligence Series: M&A Insurance – The New Normal? Global MA Claims Intelligence 2018

Representation and Warranty Insurance Trends

- Reported Incidents by Breach Type and Industry – Claims made are consistent with expected risk by industry(1)



(1) AIG Claims Intelligence Series: M&A Insurance – The New Normal? Global MA Claims Intelligence 2018

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Delaware Statutory Appraisal Actions

The Recent Judicial Response: Reorienting Towards Deal Price in Appraisal Actions

DFC Global Corporation v. Muirfield Value Partners, L.P.
(Delaware Supreme Court – August 2017)

- **Use of Deal Price:** Rejected judicial presumption in favor of deal price to determine fair value, but noted deal price is often "the best evidence of fair value" in cases involving an arm's-length deal with a fulsome sale process
- **Regulatory Uncertainty:** Rejected concept that regulatory uncertainty relating to target's industry casts doubt on deal price as indicative of fair value, given that market price incorporates public information about such uncertainty
- **No "Private Equity Carve Out" for Market Evidence:** Rejected Chancery Court's decision not to give dispositive weight to merger price on basis that the buyer was a financial buyer focused on "achieving a certain internal rate of return and on reaching a deal within its financing constraints, rather than on…fair value." Court noted that this so-called "private equity carve out," which has been raised in other Chancery Court opinions, is not "grounded in economic literature"
- **Valuation Methodologies:** Court must consider the reliability of appropriate factors and "explain," based on the "economic facts" before it and corporate finance principles, the weight it accords to the results of those methodologies

Dell v. Magnetar Global Event Driven Master Fund Ltd.
(Delaware Supreme Court – December 2017)

- **Use of Deal Price:** Reversed Court of Chancery's fair value determination because lower court's reasons for giving deal price no weight were not supported by that court's own factual findings
- **No "Valuation Gap":** Rejected Court of Chancery's conclusion that "investor myopia" and investor hangover from Dell's recent transformational efforts, which had not yet begun to generate anticipated results, had produced a "valuation gap"
- **No "Private Equity Carve Out" for Market Evidence:** As it did in *DFC*, Court rejected view that price paid by financial sponsors, who focus on achieving a particular internal rate of return, is incompatible or inconsistent with "fair value." Court reasserted its position in *DFC* that "all disciplined buyers, both strategic and financial, have internal rates of return that they expect"
- **Management Buyouts:** Rejected idea that threat of a "winner's curse" provided a valid basis for disregarding deal price as "extensive due diligence and cooperation from the Company helped address any information asymmetries that might otherwise imply the possibility of a winner's curse"

Aruba Networks and *Solera Holdings*: Fair Value Determinations in *Dell* Compliant Transactions

Verition Partners Master Fund Ltd. V. Aruba Networks
(Delaware Chancery Court – February 2018)

Fair Value Methodology: 30 Day Average Trading Price

Fair Value of $17.13/Share v. Deal Price of $24.67/Share

- **Reliance on "Market Indicators":** Interpreting *Dell* and *DFC* to express a preference for "market indicators over discounted cash flow valuations," the court concluded that the unaffected deal market price provided the most reliable indicator of fair value because it "provides a direct measure of the collective judgment of numerous market participants"
- **Key Inquiry in Appraisal Action:** "The issue in an appraisal is not whether a negotiator has extracted the highest possible bid. Rather, the key inquiry is whether the dissenters got fair value and were not exploited."
    - **Result:** Where the merger price is greater than the unaffected market price of the stock, "it is not possible to say" that the stockholders were exploited

In re Appraisal of Solera Holdings, Inc.
(Delaware Chancery Court – July 2018)

Fair Value Methodology: Deal Price Less Synergies

Fair Value of $53.95 /Share v. Deal Price of $55.85/Share

- **Reliance on Deal Price:** Chancery Court appraised fair value at deal price less merger synergies. In determining fair value in this regard, the Court relied on the guidance from *DFC* and *Dell*, noting that "those decisions teach that deal price is 'the best evidence of fair value' when there was an 'open process,' meaning that the process is characterized by 'objective indicia of reliability.'" In *Solera Holdings*, the Court pointed to (i) the opportunity of many potential bidders to bid, (ii) the Special Committee's role in actively negotiating an arm's length transaction and (iii) evidence that the market for Solera's stock was efficient and well functioning

AOL and *Norcraft* : Flawed Processes

In re Appraisal of AOL Inc. (Delaware Chancery Court – February 2018)

Fair Value Methodology: DCF Analysis

Fair Value of $48.70/Share (dropped to 47.08/Share on Rehearing in August 2018) v. Deal Price of $50/Share

- **Evidence of Deal Being "*Dell*-Compliant":** Court noted several features of the transaction being "*Dell*-compliant" (*i.e.*, that deal price is indicative of fair value), including (i) the fact that AOL was known to be in play, (ii) that directors complied with their fiduciary duties and (iii) the company spoke to numerous bidders
- **Deficient Features of the Sale Process Lead Court to Apply a DCF Analysis:** Court nonetheless found that a DCF analysis was appropriate because "the merger agreement was protected by a no-shop and matching right provisions" and because AOL's CEO had signaled to potential market participants that the deal was "done" and they "need not bother making an offer." Court, however, used deal price as "check" on its analysis given deal process was sufficiently robust

Blueblade Capital Opportunities, LLC v. Norcraft Companies, Inc. (Delaware Chancery Court – July 2018)

Fair Value Methodology: DCF Analysis

Fair Value of $26.16/Share v. Deal Price of $25.50 /Share

- **Deficient Features of the Sale Process Lead Court to Apply a DCF Analysis:** Chancery Court concluded that the deal price did not reflect Norcraft's fair value because there were "significant flaws" in the sales process, including "the absence of a pre-signing market check, failure to consider other potential merger partners, inclusion of deal protection measures that rendered the post-signing go-shop ineffective as a price discovery tool, and a lead negotiator for Norcraft who 'was at least as focused on securing benefits for himself as he was on securing the best price available for Norcraft." As a result, Court applied a DCF analysis

The Current State of Play

- After a period of significant uncertainty, it appears that the deal price should now be respected more often than not, at least in arms-length transactions with robust market checks
- Where there are significant flaws in the sales process, Delaware courts may continue to apply a DCF analysis
- A determination that the deal price is not a reliable indicator of fair value does not necessarily result in a fair value determination above deal price
  - Recent decisions have found fair value to be below deal price
  - In light of the recent decisions finding appraised value below deal price, stockholders may be discouraged from seeking appraisal
- The Supreme Court's position in *DFC* and *Dell* that a private equity carve-out is not grounded in economic literature or generally accepted financial principles — means that petitioners will be unable to argue that a deal price is not a reliable indicator of fair value simply based on the buyer's identity as a private equity buyer

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New Representations and Warranties in Purchase Agreements

The Impact of #MeToo

"#MeToo" M&A risk is coming to warrant its own separate consideration

Why:

- #MeToo represents a new M&A risk category, particularly for companies heavily dependent on key talent or personalities
- Public erosion of goodwill in companies with accused executives
- Reputational integrity is becoming its own valuation component
- Harassment claims or settlements may be material information required to be disclosed to shareholders, in turn triggering stock price decline

Who:

- The #MeToo inquiry will generally cover the directors, management team and other executives who supervise a significant number of employees

How:

- **Due diligence** – specific #MeToo diligence allows a buyer to assess the impact of potential claims on valuation of target
- **Reps and warranties** – #MeToo-based representations may be included in the acquisition agreement to address issues uncovered in diligence or hedge against potential harassment claims
  - Time period covered may exceed statute of limitations – reps are aimed at reputational harm, not specific litigation risk
  - In view of the potential reputational harm to both target and individual, information disclosed in connection with reps / disclosure schedules must be handled with discretion and care
  - May be MAE-qualified

The Impact of #MeToo (cont'd)

Examples of #MeToo Representations:

"Except as has not had and would not reasonably be expected to have, individually or in the aggregate, a Company Material Adverse Effect, to the Knowledge of the Company, (i) no allegations of sexual harassment have been made against (A) any officer or director of the Acquired Companies or (B) any employee of the Acquired Companies who, directly or indirectly, supervises at least eight (8) other employees of the Acquired Companies, and (ii) the Acquired Companies have not entered into any settlement agreement related to allegations of sexual harassment or sexual misconduct by an employee, contractor, director, officer or other Representative." — Verscend Technologies / Cotiviti Holdings Merger Agreement (June 2018)

"Except as set forth on Schedule 2.12(j), none of the Barteca Entities is party to a settlement agreement with a current or former officer, employee or independent contractor of any Barteca Entity resolving allegations of sexual harassment by either (i) an officer of any Barteca Entity or (ii) an employee of any Barteca Entity. There are no, and since January 1, 2015 there have not been any Actions pending or, to the Company's Knowledge, threatened, against the Company, in each case, involving allegations of sexual harassment by (A) any member of the Senior Management Team or (B) any employee of the Barteca Entities in a managerial or executive position." — Del Frisco's Restaurant Group / Barteca Merger Agreement (May 2018)

General Data Protection Regulation

GDPR significantly increases EU regulation of data privacy

What is GDPR?

- EU Regulation on the protection of natural persons with regard to processing and movement of personal data – enforceable since 5/25/18
- Sets forth strict new rules on collection and processing of personal information, guidelines for data management and individual consent rights

Applicability / jurisdiction

- Increased jurisdictional scope – will apply to an entity outside of the EU that offers goods or services or monitors behavior of individuals in the EU

Breaches / penalty

- A privacy breach must be notified to the supervisory authority within 72 hours after having become aware of it; high-risk breaches must also be communicated to the affected individuals without undue delay
- Failure to notify can result in an administrative fine of up to the greater of €10 million or 2% of total worldwide annual turnover (maximum fine under GDPR is the greater of €20 million or 4% of total worldwide annual turnover)
- A non-compliant company may be ordered to stop processing personal information altogether

Potential treatment in the acquisition agreement

- Reference to GDPR is typically included in general “compliance with laws” or privacy-related representation
- Nature or location of target’s business may warrant GDPR-specific representations

General Data Protection Regulation

Examples of GDPR Representations:

"Except as would not reasonably be expected to have a Company Material Adverse Effect, the Company and its Subsidiaries are fully compliant with all applicable requirements of EU General Data Protection Regulation EU/2016/679 and any Laws implementing or supplementing such regulation (collectively, GDPR), including that: (i) all processor agreements affecting Personal Information will be in compliance with Article 28 of the GDPR; (ii) all IT systems and Security Programs will meet the requirements of Chapter IV, Section 2 of the GDPR; (iii) the Company and its Subsidiaries will be able to fully respond to and fulfil the data subject rights under Chapter III of the GDPR; (iv) the Company and its Subsidiaries will have implemented data protection by design and by default for all of their products in accordance with Article 25 of the GDPR; (v) the Company Privacy Policy will be in compliance with Chapter III, Section 2 of the GDPR; and (vi) all new and prior consents from data subjects will be in compliance with Article 7 of the GDPR."

General Data Protection Regulation

Examples of GDPR Representations (cont'd):

"Except as would not, individually or in the aggregate, be reasonably expected to have a Company Material Adverse Effect, each of the Company and its Subsidiaries has ensured that all Processing of Personal Data carried out by the Company and its Subsidiaries on the basis of Article 6(1)(f) of the GDPR, to the extent applicable, is in compliance with the GDPR. For purpose of this Agreement, GDPR means Regulation (EU) 2016/679 of the European Parliament of the Council of 27 April 2016, and Personal Data Processing and Supervisory Authority shall each have the respective meaning set out in Article 4 of GDPR."

"The Company and its Subsidiaries are compliant in all material respects with all applicable requirements of the European Union's General Data Protection Regulation (GDPR) with respect to EU Personal Data."

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Delaware Case Law Developments

Controlling Stockholder Implications

Implications of Being a Controlling Stockholder

- Over the past few years, the Delaware Court of Chancery has issued several opinions addressing whether a less than majority stockholder may be a controlling stockholder
  - In *Kahn v. Lynch Communications Systems, Inc*. (Del. 1994), the Delaware Supreme Court observed that Delaware courts will deem a stockholder a controlling stockholder when the stockholder:
    - owns more than 50% of the voting power of a corporation; or
    - owns less than 50% of the voting power of the corporation but "exercises control over the business affairs of the corporation"
- The existence of a controlling stockholder has several implications under Delaware law, including:
  - Controlling stockholders owe fiduciary duties; and
  - Entire fairness standard of review will apply, unless the merger is conditioned *ab initio* upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders, in which case business judgment rule will apply. *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014)

Controlling Stockholder: Less Than a Majority Stockholder (Recent Delaware Chancery Court Opinions)

***In re Tesla Motors, Inc. S'holder Litig*., 2018 WL 1560293 (Del. Ch. Mar. 28, 2018)**

Chancery Court Decision

- Court found it reasonably conceivable that Musk, a 22.1% stockholder, was a controlling stockholder
- As Court noted, in citing to earlier Delaware Chancery Court opinions, "'there is no absolute percentage of voting power that is required in order for there to be a finding that a controlling stockholder exists.' Indeed, '[a]ctual control over business affairs may stem from sources extraneous to stock ownership.'"

Key Takeaways

- Stockholders with relatively low ownership stakes may be found to be controlling stockholders, but only if there are other factors that reflect control over the corporation
- Key factors in Court's decision:
  - Musk previously forced out the founder and then-CEO;
  - Tesla had some high votes in its bylaws that could have provided Musk holdup value;
  - Musk brought the transaction to the board three times, led the discussion of the acquisition, and engaged the advisors for the acquisition;
  - Musk had strong connections with the members of the Tesla Board and a majority of Tesla's Board was "interested" in the acquisition; and
  - Tesla acknowledged Musk's significant influence at Tesla in Tesla's public filings

Controlling Stockholder: Less Than a Majority Stockholder (Recent Delaware Chancery Court Opinions) (Cont'd)

***Basho Techs. Holdco B, LLC v. Georgetown Basho Investors, LLC* (Del. Ch. July 6, 2018)**

Chancery Court Decision

- Court finds that a less than majority stockholder is a controlling stockholder for purposes of a decision to approve a new round of financing, in part because the stockholder used its contractual rights to cut off access to other sources of financing
- As the Court noted, "The requisite degree of control can be shown to exist generally or with regard to the particular transaction that is being challenged"

Key Takeaways

- Mere blocking rights alone (e.g., to veto new financing) will typically not suffice to support a finding of control
  - "Lest sensitive readers fear that this decision signals heightened risk for venture capital firms who exercise their consent rights over equity financings, I reiterate that a finding of control requires a fact-specific analysis of multiple factors. If Georgetown only had exercised its consent right, that fact alone would not have supported a finding of control. The plaintiffs proved that Georgetown and Davenport did far more."
- Examples of sources of influence that could contribute to a finding of control over a particular decision include:
  - relationships with particular directors that compromise their disinterestedness or independence;
  - relationships with key managers or advisors who play a critical role in presenting options, providing information, and making recommendations;
  - exercise of contractual rights to channel the corporation into a particular outcome by blocking or restricting other paths; and
  - existence of commercial relationships that provide the defendant with leverage over the corporation, such as status as a key customer or supplier

Controlling Stockholder: Less Than a Majority Stockholder (Recent Delaware Chancery Court Opinions) (Cont'd)

***Basho Techs. Holdco B, LLC v. Georgetown Basho Investors, LLC* (Del. Ch. July 6, 2018)**

Key Takeaways (Cont'd)

- Broader indicia of effective control may also play a role in evaluating whether a defendant exercised actual control over a decision.
- Examples of broader indicia include:
  - ownership of a significant equity stake (albeit less than a majority);
  - the right to designate directors (albeit less than a majority);
  - decisional rules in governing documents that enhance the power of a minority stockholder or board-level positon; and
  - the ability to exercise outsized influence in the board room, such as through high-status roles like CEO, Chairman, or founder

Controlling Stockholder: Refinement of *MFW* Ab Initio Requirement

***Flood v. Synutra Int'l, Inc.*, No. 101, 2018 WL 4869248 (Del. Oct. 9, 2018)**

Delaware Supreme Court Decision

- Court finds *MFW* applied where the board considered a "preliminary non-binding proposal" that did not condition a potential transaction on the dual procedural protections because a follow-up letter, sent before the board had substantively evaluated the proposal, reaffirmed its initial offer and expressly conditioned the transaction on the approval of the special committee and a majority of the minority stockholders

Key Takeaways

- Court will favor a pragmatic, flexible approach to "*ab initio*" determination
  - However, we do not yet know what the outer limits of the Court's flexibility will be
    - In *Olenik v. Lodzinski*, 2018 WL 3493092 (Del. Ch. July 20, 2018), which is still in the appeal process, the Court of Chancery held that the *MFW* protections need not be in place before exploratory discussions between the parties, so long as they are in place at the outset of negotiations (which typically begin when a proposal is made by one party that, if accepted, would constitute a binding agreement)
    - If a controller wants to ensure it will receive the benefit of business judgment rule review, the prudent course is to indicate, in any expression of interest, no matter how early or informal, that adherence to *MFW* procedural safeguards is a pre-condition to any transaction

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Developments in Drag-Alongs

Drag-Along Right: Complications re: Fiduciary Duties

***In re Good Technology*, 2017 WL 2537347 (Del. Ch. May 12, 2017)**

Terms of Drag-Along

- In the event "that the Board and the holders of a majority of the outstanding shares of Preferred Stock . . . approve" a Sale of the Company . . . "each Investor and Common Holder hereby agrees . . . (ii) to vote (in person, by proxy or by action by written consent, as applicable . . . in favor of such Sale of the Company . . . (iii) to refrain from exercising any dissenters' rights or rights of appraisal under applicable law . . . and (iv) to execute and deliver all related documentation and take such other action in support of the Sale of the Company as shall reasonably be requested by the Company."

Key Points from Chancery Decision

- "It seems likely, for example, that an implied term of the drag right and appraisal waiver is that the board did not breach its fiduciary duties when approving the merger that triggers the drag."
- "A key purpose of conditioning a drag sale on board approval is "to require the board to consider its fiduciary duty to all of the company's owners." In light of this purpose, the parties may have regarded it as so obvious that the Company could only enforce the Drag-Along if the board complied with its fiduciary duties that it would have been "obvious and provocative" to include such a term explicitly. Assessing whether the parties intended to imply such a term will require a factual determination based on a full trial record."

Drag-Along Right: Abiding by the Particulars

***Halpin v. Riverstone Nat'l, Inc.*, 2015 WL 854724 (Del. Ch. Feb. 26, 2015)**

Terms of Drag-Along

- If the majority stockholder "*propose[d]*" to enter into a change-of-control transaction, the Company could require the minority holders to vote and/or tender their shares in favor of the transaction so long as the minority stockholders were provided advance notice thereof.

Holding

- Drag-along not specifically enforceable because the Company did not follow the procedures set forth in the stockholders agreement.
- Drag-along operated prospectively. That is, the minority holders agreed to vote or tender in favor of a "propose[d]" merger upon advance notice thereof. **The minority holders did not agree to consent to a consummated merger after the fact.**
- Thus, the minority holders were not bound to vote or consent in favor of the merger agreement and could exercise appraisal rights without breach of the stockholders agreement.

Drag-Along Right: Eliminating Appraisal Rights

Appraisal Rights—DGCL § 262(a)

- "Any stockholder . . . ***who has neither voted in favor of the merger or . . consolidation nor consented thereto in writing*** pursuant to § 228 of this title shall be entitled to an appraisal by the Court of Chancery . . . ."

Voting Agreements Generally Enforceable—DGCL § 218

- *Salamone v. Gorman*, 106 A.3d 354, 366 (Del. 2014) ("Section 218 of the DGCL explicitly permits stockholders 'to construct a contractual overlay on top of that mechanism to agree to vote their shares in accordance with [a] more specific scheme.'"); *In re Westech Capital Corp.*, 2014 WL 2211612, at *18 (Del. Ch. May 29, 2014).

Undecided Issue—*Halpin*

- "Although this case raises an interesting legal issue as to whether a common stockholder may contractually waive its statutory appraisal rights for consideration to be set later by a controlling stockholder, I do not find it necessary to resolve that legal question here."

Drag-Along Right: Eliminating Appraisal Rights

***Manti Holdings, LLC et al. v. Authentix Acquisition Co.*, 2018 WL 4698255 (Del. Ch. Oct. 1, 2018)**

Terms of Drag-Along

- In the event of a Company Sale, stockholders must consent to the sale and "refrain from the exercise of appraisal rights."
- "This agreement, and the respective rights and obligations of the Parties, shall terminate upon the . . . consummation of a Company Sale."

Holding

- The stockholders agreement was enforceable and plaintiffs could not pursue appraisal.
- The obligation to "refrain from the exercise of appraisal rights" did not terminate upon the consummation of the transaction.
    - "My finding is bolstered by the obvious fact that the 'exercise of appraisal rights' with respect to a transaction is meaningless until the transaction is accomplished."
- Enforcement of the stockholders agreement did not violate public policy or Section 151(a) of the DGCL (requiring limitations on classes of stock to be contained in the corporation's charter).
    - Enforcing the stockholders agreement is "not the equivalent of imposing limitations on a class of stock under Section 151(a) . . the Company . . . did not transform the Petitioner's shares of stock into a new restricted class via the SA; instead, individual stockholders took on contractual responsibilities in return for consideration."

GIBSON DUNN

Panelists

Andrew M. Herman

1050 Connecticut Avenue, NW, Washington, DC 20036
200 Park Avenue, New York, NY 10166
Tel: +1 202.955.8227
aherman@gibsondunn.com

Andrew M. Herman is a partner in the Washington, D.C. office of Gibson, Dunn & Crutcher. He is a member of the firm's Mergers and Acquisitions and Private Equity Practice Groups.

Mr. Herman's practice focuses on advising private equity sponsors and their portfolio companies on leveraged buyouts, growth equity investments and other transactions. He also advises public companies on mergers and acquisitions transactions, securities law compliance and corporate governance. He is experienced in advising on the acquisition and sale of sports franchises.

Mr. Herman's representative clients include MidOcean Partners, ATL Partners, Quad-C Management, Arlington Capital, Revolution Growth, Exelon Corporation, Tutor Perini and Monumental Sports and Entertainment (holding company of the Washington Wizards, Washington Capitals and Washington Mystics).

Mr. Herman has been recognized as a top lawyer by *Chambers USA* from 2011 to present. He also has been listed in the 2013-2018 editions of *Super Lawyers* and was recognized as a Notable practitioner in IFLR1000 2019. Prior to joining Gibson Dunn, Mr. Herman was a partner with Kirkland & Ellis.

Mr. Herman graduated in 1995 from Columbia University School of Law, where he was a Harlan Fiske Stone Scholar and the submissions editor of the *Journal of Transactional Law*. He received a master's degree with honors in accounting from the University of North Carolina, Chapel Hill in 1992.

Robert B. Little

2100 McKinney Avenue, Suite 1100, Dallas, TX 75201
Tel: +1 214.698.3260
rlittle@gibsondunn.com

Robert B. Little is a partner in Gibson, Dunn & Crutcher's Dallas office. He is a member of the firm's Mergers and Acquisitions, Capital Markets, Energy and Infrastructure, Private Equity, Securities Regulation and Corporate Governance, and Global Finance practice groups. Mr. Little serves on the Gibson Dunn Hiring Committee and is the hiring partner for the Dallas office.

Described by clients in *Chambers USA* 2017 as an "efficient, practical and proactive lawyer who is oriented to problem solving," Mr. Little's practice focuses on corporate transactions, including mergers and acquisitions, securities offerings, joint ventures, investments in public and private entities, and commercial transactions. He also advises business organizations regarding matters such as securities law disclosure, corporate governance, and fiduciary obligations. In addition, he represents investment funds and their sponsors along with investors in such funds. Mr. Little has represented clients in a variety of industries, including energy, retail, technology, transportation, manufacturing, and financial services.

Mr. Little received his law degree in 1998 with highest honors from The University of Texas School of Law, where he was named a Chancellor and a member of Order of the Coif and served as Articles Editor of the *Texas Law Review*. He also holds a B.A. from Baylor University, where he graduated *summa cum laude* in 1995. He previously served as a law clerk to The Honorable Patrick Higginbotham of the U.S. Court of Appeals for the Fifth Circuit.

Deepak Nanda

3161 Michelson Drive, Irvine, CA 92612
Tel: +1 949.451.4064
dnanda@gibsondunn.com

Deepak Nanda is a partner in Gibson, Dunn & Crutcher's Orange County office. His practice focuses on transactional and securities matters, including cross-border mergers and acquisitions, dispositions, privatization transactions, leveraged recapitalizations and buyouts; venture capital and private equity fund formation and portfolio company investment; public and private offerings of equity and debt securities; public corporation securities laws and reporting compliance; and structured finance transactions. Mr. Nanda is a member of the firm's Corporate and Mergers and Acquisitions practice groups.

Mr. Nanda has significant experience in the medical device, financial services, pharmaceutical, information technology and media and entertainment sectors. His clients have included medical device companies, financial institutions, multinational manufacturing and technology companies, and pharmaceutical companies in the United States, Europe and Asia. Mr. Nanda's practice has included representing clients with projects in the United States, Europe, the Middle-East, India, Singapore, China, South Korea, Canada, Latin America and Australia.

Mr. Nanda was recognized as a leading practitioner in *Legal 500* (2010-2011) and was previously selected for inclusion in the 2007 *Southern California Super Lawyers – Rising Stars*® list. In June 2010, *Diversity MBA Magazine* named Mr. Nanda to its list of "Top 100 under 50 Diverse Executive & Emerging Leaders."

Mr. Nanda is admitted to practice in California. He is also a member of the Los Angeles County and American Bar Associations. Mr. Nanda graduated from Loyola Law School of Los Angeles in 1997. In 1993, Mr. Nanda received his Bachelor of Arts degree, *cum laude*, from the University of California at Irvine, where he was a member of the Order of Merit.

Daniela Stolman

333 South Grand Avenue, Los Angeles, CA 90071
Tel: +1 213.229.7875
dstolman@gibsondunn.com

Daniela L. Stolman is an associate in Gibson Dunn's Los Angeles office and a member of the firm's Private Equity, Mergers and Acquisitions, Capital Markets and Securities Regulation and Corporate Governance practice groups.

She advises companies and private equity firms across a wide range of industries, focusing on public and private merger transactions, stock and asset sales, and public and private capital-raising transactions. Ms. Stolman also advises public companies with respect to securities regulation and corporate governance matters, including periodic reporting and disclosure matters, Section 16, Rule 144, and insider trading. She has been named as a Rising Star by Southern California *Super Lawyers* since 2014.

Ms. Stolman received her law degree in 2006 from the University of Southern California Law School, where she was elected to the Order of the Coif and was a Senior Editor of the *Southern California Law Review*. She earned a Bachelor of Arts degree in history and economics, *magna cum laude*, from the University of Pennsylvania in 2002.

Our Offices

Beijing
Unit 1301, Tower 1
China Central Place
No. 81 Jianguo Road
Chaoyang District
Beijing 100025, P.R.C.
+86 10 6502 8500

Brussels
Avenue Louise 480
1050 Brussels
Belgium
+32 (0)2 554 70 00

Century City
2029 Century Park East
Los Angeles, CA 90067-3026
+1 310.552.8500

Dallas
2100 McKinney Avenue
Suite 1100
Dallas, TX 75201-6912
+1 214.698.3100

Denver
1801 California Street
Suite 4200
Denver, CO 80202-2642
+1 303.298.5700

Dubai
Building 5, Level 4
Dubai International Finance Centre
P.O. Box 506654
Dubai, United Arab Emirates
+971 (0)4 318 4600

Frankfurt
TaunusTurm
Taunustor 1
60310 Frankfurt
Germany
+49 69 247 411 500

Hong Kong
32/F Gloucester Tower, The Landmark
15 Queen's Road Central
Hong Kong
+852 2214 3700

Houston
811 Main Street
Houston, Texas 77002
+1 346.718.6600

London
Telephone House
2-4 Temple Avenue
London EC4Y 0HB
England
+44 (0) 20 7071 4000

Los Angeles
333 South Grand Avenue
Los Angeles, CA 90071-3197
+1 213.229.7000

Munich
Hofgarten Palais
Marstallstrasse 11
80539 Munich
Germany
+49 89 189 33-0

New York
200 Park Avenue
New York, NY 10166-0193
+1 212.351.4000

Orange County
3161 Michelson Drive
Irvine, CA 92612-4412
+1 949.451.3800

Palo Alto
1881 Page Mill Road
Palo Alto, CA 94304-1125
+1 650.849.5300

Paris
166, rue du faubourg Saint Honoré
75008 Paris
France
+33 (0)1 56 43 13 00

San Francisco
555 Mission Street
San Francisco, CA 94105-0921
+1 415.393.8200

São Paulo
Rua Funchal, 418, 35°andar
Sao Paulo 04551-060
Brazil
+55 (11)3521.7160

Singapore
One Raffles Quay
Level #37-01, North Tower
Singapore 048583
+65.6507.3600

Washington, D.C.
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036-5306
+1 202.955.8500