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Shifts seen in the way M&A cases are litigated

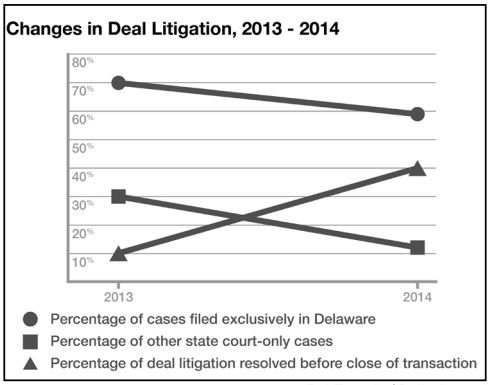
By Koji Fukumura

The convergence of a number of forces is changing the way M&A lawsuits are litigated and resolved. First, there are a growing number of public companies whose foundational documents contain an exclusive forum provision in favor of the Delaware Chancery Court. Second, courts throughout the country (including Delaware) have expressed increasing hostility to so-called "disclosure-only" settlements reached prior to the close of a transaction. Finally, there has been an increase in the number of cases being litigated beyond the closing of the transaction at issue. An escalation in the number of post-close cases will naturally increase substantially litigation costs and the risk of a settlement exceeding the attorney fee awards in disclosure-only settlements. Accordingly, public company boards and their advisors should assume in crafting and executing the sales process that their deals will be actively litigated.

Exclusive Forum Provisions

Exclusive forum provisions (in a corporation's bylaws or charter) designate a specific court to serve as the exclusive venue for intra-corporate litigation — e.g., derivative suits; actions (including class actions) asserting breach of fiduciary duty by a director, officer or other employee to the corporation or its shareholders, and other disputes asserting claims under the internal affairs doctrine. These provisions are intended to address multi-forum litigation — a well-known and particularly vexatious problem in the context of mergers and acquisitions and derivative suits.

In June 2013, in *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*, the Delaware Chancery Court upheld the facial validity and enforceability of an exclusive forum bylaw provision. 73 A.3d 934 (Del. Ch. 2013). Then-Chancellor Leo Strine (now chief justice of the Delaware Supreme Court) ruled that the boards of directors of Chevron and FedEx (Delaware corporations) were authorized unilaterally to amend the company's bylaws to designate a specific court as the "exclusive forum" for certain intra-corporate litigation (e.g., derivative actions, breach of fiduciary duty claims, actions under the DGCL, cases involving the internal affairs doctrine). Plaintiffs appealed the decision to the Delaware Supreme Court, but subsequently abandoned that appeal (presumably to avoid a binding precedent from the highest court, who many expected to uphold the decision).



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In the first six months after the *Chevron* decision, over 150 Delaware corporations adopted or announced plans to adopt such a provision. (See, e.g., Claudia Allen, "Trends in Exclusive Forum Bylaws," Director Notes of the Conference Board Governance Center, January 2014.) Given that throughout 2014 many law firms routinely advised their public company clients to amend their bylaws to include an exclusive-forum provision (existing public companies) or to include such a provision in their certificate of incorporation (new public companies), the number of public companies whose foundational documents contain an exclusive-forum provision is likely well over 300.

Since June 2013, courts in New York, Texas, Louisiana, Illinois, California, Delaware, Alabama and Ohio have upheld exclusive forum selection provisions and dismissed or transferred shareholder litigation as a result. See, e.g., *HEMG Inc. v. Aspen Univ.*, No. 650457/13, 2013 WL 5958388 (N.Y. Sup. Ct. Nov. 4, 2013); *Genoud v. Edgen Group Inc.*, No. 625,244, slip op., 2014 WL 2782221 (La. Dist. Ct. Jan. 17, 2014); *Miller v. Beam Inc.*, No. 2014 CH 00932, Tr. of Oral Arg., at 38-47 (Ill. Cir. Ct. Mar. 5, 2014); *Groen v. Safeway Inc.*, No. RG14716641, slip op., at 1-2, 2014 WL 3405752 (Cal. Super. Ct. May 14, 2014); *Providence v. First Citizens BancShares Inc.*, 99 A.3d 229 (Del. Ch. 2014) (upholding the validity of an exclusive-forum bylaw provision of a Delaware corporation in favor of courts in North Carolina); *North v. McNamara*, No. 13-cv-833, 2014 WL 4684377 (S.D. Ohio Sept. 19, 2014); *Golovoy v. MetroPCS Communications Inc.*, No. CC-12-06144-A (Tex Cnty Ct Apr. 18, 2014), *Edelman v. Protective Life Corp*, No. CV-2014-902474 (Cir Ct of Jefferson Cnty, Ala, Sept. 19, 2014).

The effect of exclusive forum provisions on deal litigation is no longer theoretical. According to a report issued last week by Cornerstone Research Inc., cases filed exclusively in Delaware have increased substantially — from 10 percent in 2013 to 40 percent in 2014. The total incidence of cases in Delaware (compared to other jurisdictions combined) is at an all-time high of 88 percent. Similarly, the incidence of other state court-only cases is down to 12 percent in 2014 compared to 30 percent in 2013. Further, the percentage of deal cases filed in transactions below $1 billion has dropped below 90 percent.

Be Careful What You Wish For

While exclusive-forum provisions are having their intended effect of curbing abusive multi-forum litigation, it may also be increasing the number of cases being litigated beyond the closing of a transaction. The Cornerstone Report notes that from 2009 through 2013, over 70 percent of deal litigation was resolved prior to the close of a transaction (virtually all by entry into disclosure-only settlements). In 2014, that number decreased to 59 percent — which is the lowest level since 2008.

This decrease in the number of pre-close settlements may be attributed to a perception in plaintiff's bar that the Delaware Chancery Court (among others) has become increasingly hostile to disclosure-only settlements. Plaintiffs firms may believe that, in the disclosure-only context, a court might either reduce significantly any fee award or refuse to award them a fee at all. That belief, coupled with several recent high-profile, large-dollar settlements may be motivating plaintiff's lawyers to eschew a disclosure-only settlement in favor of post-close litigation.


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