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IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE VOLCANO CORPORATION STOCKHOLDER LITIGATION MELVIN LAX, MELISSA GORDON and MOHAMMED MUNAWAR, Plaintiffs Below, Appellants, vs. GOLDMAN, SACHS & CO., KIERAN T. GALLAHUE, LESLEY H. HOWE, R. SCOTT HUENNEKENS, SIDDHARTHA KADIA, ALEXIS V. LUKIANOV, RONALD A. MATRICARIA, LESLIE V. NORWALK, DANIEL J. WOLTERMAN, AND VOLCANO CORPORATION. Defendants Below, Appellees.	No. 372, 2016 On Appeal from C.A. No. 10485-VCMR in the Court of Chancery of the State of Delaware

APPELLANTS' REPLY BRIEF TO VOLCANO DEFENDANTS-APPELLEES' ANSWERING BRIEF

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I. THE COURT OF CHANCERY ERRED IN FINDING THAT THE BUSINESS JUDGMENT RULE IRREBUTTABLY APPLIED TO THE MERGER AND BARS PLAINTIFFS' CLAIMS

Appellees spill much ink urging this Court that the doctrine of *stare decisis* applies under the "final and settled Delaware law" established in *Singh*[1] and legally forces the business judgment standard of review to irrebuttably apply following stockholder ratification and completely bar all claims but waste.[2] To the contrary, the doctrine of *stare decisis* further supports Appellants' contention that a fully informed, uncoerced, and disinterested stockholder vote in favor of a merger simply shifts the burden of proof to plaintiffs to then rebut.

First, prior to the Court of Chancery's holding below in the instant case, no Delaware Court – including the Court in *Singh* – had ever specifically held that stockholder ratification rendered the business judgment rule irrebuttable. *Second*, any interpretation to the contrary is explicitly at odds with multiple earlier opinions by the Delaware Supreme Court (specifically, *Stroud v. Grace*,[3] *Williams v. Geier*,[4]

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1 *Singh v. Attenborough*, 137 A.3d 151 (Del. 2016).

2 Volcano Defendants-Appellees' Ans. Br. at 24-25 [hereinafter Def. Ans. Br.].

3 606 A.2d 75 (Del. 1992).

4 671 A.2d 1368 (Del. 1996).

and *In re Santa Fe*[5]) and by the Court of Chancery in *Wheelabrator*,[6] each of which remain good law. Accordingly, and as even acknowledged by Appellees at length in their brief, an irrebuttable business judgment rule is inconsistent with the historical effect of ratification – a historical effect "which is not afterwards to be departed from or lightly overruled or set aside."[7]

To be clear, Appellants are not asking this Court to overrule its prior decisions in *Singh* and *Corwin*.[8] Rather, Appellants respectfully take issue with the characterization of *Singh* and *Corwin* offered by Appellees and the Court of Chancery below – specifically, that "[i]n [*Singh*]…the Supreme Court held that upon a fully informed vote by a majority of a company's disinterested, uncoerced stockholders, ***the business judgment rule irrebuttably applies***."[9] In Appellants' view, *Singh* simply held that "a fully informed, uncoerced vote of the disinterested stockholders invoked the business judgment rule standard of review."[10] Nowhere in *Singh* did this Court specifically hold that the business judgment rule was

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5 *In re Santa Fe Pac. Corp. S'holder Litig*., 669 A.2d 59 (Del. 1995).

6 *In re Wheelabrator Tech. S'holders Litig*., 663 A.2d 1194 (Del. Ch. 1995).

7 Def. Ans. Br. at 24.

8 *Corwin v. KKR Fin. Holdings LLC*, 125 A.3d 304 (Del. 2015).

9 Def. Ans. Br. at 19 (emphasis added).

10 137 A.3d at 151.

irrebuttable following stockholder ratification. Moreover, *Singh* emphasized that the implication of stockholder ratification was burden-shifting, rather than burden deletive.[11]

Similarly, in *Corwin*, this Court held that "when a transaction . . . is approved by a fully informed, uncoerced vote of the disinterested stockholders, the business judgment rule applies"[12] – a holding Appellants do not contest. The *Corwin* Court cited – in a footnote – a portion of the underlying decision in *KKR*,[13] which referenced waste. Importantly, however, the Court did not discuss nor hold that the business judgment rule applied irrebuttably or that all claims would be extinguished and that waste would be a plaintiff's only remedy.[14] As detailed in Appellants' Opening Brief, just referencing what another court said does not make new law, particularly when the parties below did not address, much less dispute, the issue.

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[11] *Id*. ("Employing this same standard after an informed, uncoerced vote of the disinterested stockholders would give no ***standard-of-review-shifting effect to the vote***.") (Emphasis added).

[12] 125 A.3d at 306.

[13] *In re KKR Fin. Holdings LLC S'holder Litig*., 101 A.3d 980 (Del. Ch. 2014).

[14] *Cf*. Def. Ans. Br. at 20 (arguing *Corwin* affirmed *KKR*'s "holding that the effect of such [stockholder] approval extinguishes all claims but waste."); *KKR*, 101 A.3d at 988, n.19.

Moreover, *Singh* did not overrule this Court's prior precedent in *Stroud*, *Williams*, and *In re Santa Fe*, or the Delaware Chancery's decision in *Wheelabrator*. Appellees urge, in turn, that the extensive quotations provided by Appellants from these cases are, in every instance, selectively taken out of context.[15] Relying on contrived language and propositions simply not present in the written text of these opinions, Appellees further urge that these cases demonstrate that only a certain extremely narrow scope of duty of loyalty claims subject to entire fairness review can survive stockholder ratification.[16] Appellees are wrong. Each of these cases, when read in their entirety and in the proper context, further support the broader principle that the business judgment rule is rebuttable and more than just claims of waste should survive stockholder ratification.

For example, relying on *Wheelabrator*, Appellees contend that the Court of Chancery "***expressly endorsed*** the application of the irrebuttable business judgment rule" in cases not implicating entire fairness review.[17] Actually, however, the Court of Chancery in *Wheelabrator* expressly found that entire

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15 Def. Ans. Br. at 26.

16 *See, e.g.*, *Id.* (surmising *Wheelabrator* "expressly endorsed" an irrebuttable business judgment rule).

17 *Id.* at 26 (emphasis added).

fairness review was not implicated but permitted plaintiffs' duty of loyalty claims to survive summary judgment regardless:

> The plaintiffs argue that their duty of loyalty claim is governed by the entire fairness standard, with ratification operating only to shift the burden on the fairness issue to the plaintiffs. That is incorrect, because ***this merger did not involve an interested and controlling stockholder . . . Accordingly, the review standard applicable to this merger is business judgment, with the plaintiffs having the burden of proof . . . For the foregoing reasons, the defendants' motion for summary judgment*** (1) is granted as to the disclosure claim, (2) is granted as to the duty of care claim, and (3) ***is denied as to the duty of loyalty claims***.[18]

Appellees similarly contrive holdings for *Stroud* and *Williams*. For instance, while Appellees urge that *Stroud* "***expressly states*** that the usual effect of fully informed, uncoerced, and disinterested stockholder approval is dismissal,"[19] they conveniently ignore that both *Stroud* and *Williams* acknowledge that the business judgment rule may be rebutted and by evidence of more than just waste.[20] And while Appellees further argue that *Stroud* is "generally inapposite to the present

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[18] 663 A.2d at 1205 (emphasis added).

[19] Def. Ans. Br. at 27.

[20] *See Stroud*, 606 A.2d at 92 ("In sum, after finding that the stockholder vote was fully informed, ***and in the absence of any fraud, waste, manipulative or other inequitable conduct***, that should have ended the matter of basic principles of ratification.") (emphasis added); *Williams*, 671 A.2d at 1380 ("[T]he stockholder vote, ***being both fully informed and devoid of any fraud, waste, manipulative or other inequitable conduct***, effectively implemented the board recommendations adopting amendments.") (emphasis added).

action" because it was adjudicated under entire fairness review,[21] *Stroud* was heavily cited – virtually wholesale – by the *Williams* Court, which refused to apply entire fairness review.[22]

Consistent with the foregoing, Appellants contend that stockholder approval, even where informed and uncoerced, cannot: (1) render the business judgment rule irrebuttable; or (2) summarily extinguish all claims and insulate the transaction from all attacks other than on the grounds of waste. To the extent the Court of Chancery below concluded otherwise, that holding is not consistent with the Supreme Court's decisions in *Stroud, Williams*, and *In re Santa Fe* (nor the Chancery Court's decision in *Wheelabrator*) and it should therefore be overruled.

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21 Def. Ans. Br. at 27.

22 671 A.2d at 1378.

II. THE COURT OF CHANCERY ERRED IN EXTENDING "*CORWIN*-BASED CLEANSING" TO TENDER OFFERS, THEREBY SHIELDING THE TRANSACTION FROM ENHANCED JUDICIAL SCRUTINY

Appellees, attempting to incorrectly reframe the narrative in their favor, mischaracterize several of Appellants' arguments. Ultimately, there are differences between tender offers and mergers involving a stockholder vote – even after the passage of Delaware General Corporation Law § 251(h). And while Section 251(h) is ostensibly an effort to bring several of the stockholder protections afforded by mergers involving a vote to tender offers, several disadvantages to minority stockholders remain, including potentially reduced target-board bargaining powers, reduced opportunity for the emergence of topping bidders, less opportunity for stockholder activists to gain traction in expressing deal disapproval, and lower regulatory controls and scrutiny. Considered together, these conditions present potentially significant disadvantages to minority stockholders – concerns which are only magnified by the various colorable conflict of interest claims specifically alleged by the Appellants herein.

Moreover, while Appellees take issue with Appellants' characterization of a "long-standing body of case law," the fact is that the lower court's decision in this case is the first time such a standard of review shift has been specifically applied to

tender offers.[23] With the various surrounding changes to the ratification doctrine, in its formal or informal sense, Appellants contend that this Court consciously abstained from extending its holding in *Corwin* to tender offers, erring on the side of caution vis-à-vis minority stockholders.[24] Contrary to Appellees' claims, Appellants do not necessarily contend that tender offers are necessarily more "coercive" than mergers involving a stockholder vote. Rather, Appellants simply stress to this Court that tender offers present certain disadvantages to minority stockholders and that, especially at the motion to dismiss stage in the proceedings, *Corwin*-based cleansing should not be applied to tender offers.

Contrary to Appellees' contentions, Appellants do not contend that a target board's fiduciary duties are fundamentally different depending on whether a merger is tailored as a tender offer or one involving a stockholder vote. Rather, Appellants argued that while target directors are ostensibly held to the same

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[23] *See* Appellants' Op. Br., at 33, n.31 ("no Delaware case has held that burden-shifting in a fairness inquiry can be accomplished by a tender of shares rather than by an actual vote.") (quoting *In re Emerging Communs., Inc. S'Holders Litig.*, 2004 Del. Ch. LEXIS 70, *1 (Del. Ch. May 3, 2004)); *see also In re Cencom Cable Income Partners, LP*, 2000 Del. Ch. LEXIS 90 (Del. Ch. May 5, 2000) ("Ratification can effectively occur only where the specific transaction is clearly delineated to the investor whose approval is sought and that approval has been put to a ***vote***.") (emphasis added).

[24] As noted in Apellants' Opening Brief, the only case cited by the Court in *Corwin* which involved a tender offer was *Morton's*. *See* Appellants' Op. Br. at 33, n.31. In citing to *Morton's*, a case which in *dicta* noted the potential question of a standard of review shift, it appears likely that the Court considered specifically whether to extend its holding to tender offers, and chose not to. *See id.*

fiduciary duties in either case, tender offers may reduce the bargaining power of a target board, or even set the stage for anti-competitive behavior, for reasons further discussed *infra* and in the Opening Brief.[25] And though Appellees disregard Chancellor Bouchard's caution in *Zuckerberg*, the "lack of any explicit role in the General Corporation Law for a target board of directors responding to a tender offer," coupled with the potential for lowered bargaining power or anti-competitive behavior, and the various well-pled conflicts of interests in this case, created conditions ripe for tainted negotiations – a scenario that would be well-served by increased judicial scrutiny.

Appellees also misrepresent the speed advantage of tender offers over mergers involving a stockholder vote.[26] Appellants did not argue that tender offers

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[25] *See* Erik Devos, William B. Elliott, & Hilmi Songur, *Top-up Options and Tender Offers*, at 3 (2014) ("Our evidence is most consistent with the anti-competitive hypothesis."). This is an empirical question, and though it is largely understudied, Appellants contend that because minority stockholder interests are at hand, it is worth consideration. *Id.* at 6 ("Yet, much is still unknown about the actual bargaining process leading up to . . . a merger."); *see also* Appellants' Op. Br. at 30.

[26] Appellees' incorrectly contend that several arguments should be disregarded under Supreme Court Rule 8 on the basis that they were not adequately argued by Appellants below. *See, e.g.*, Appellant's Op. Br. App. at A336-38 (Plaintiffs' Supplemental Brief in Further Opposition to Defendants' Motion to Dismiss) (arguing that tender offers and stockholder ratification are not analogous). Moreover, the instant case involved numerous references to the speed of the negotiations and deal, allegedly to the detriment of the stockholders. *See, e.g.*, *id.* at A177 (for example, MTD Opp at page 10 ("worked swiftly to complete the deal"). In any event, Appellants contend that this Court should fully consider our

fail to provide adequate time for stockholders to make a decision on whether to tender. Rather, Appellants' focus was on the implications, and potential disadvantages to minority stockholders, of the faster overall tender offer process.[27] From start (signing of merger agreement) to finish (tender offer close or stockholder vote), the completion time of tender offers "is from 35 to 65 days shorter than the completion time of mergers."[28] The graphic below is illustrative of the timing differences between a tender offer and a merger involving a stockholder vote:[29]

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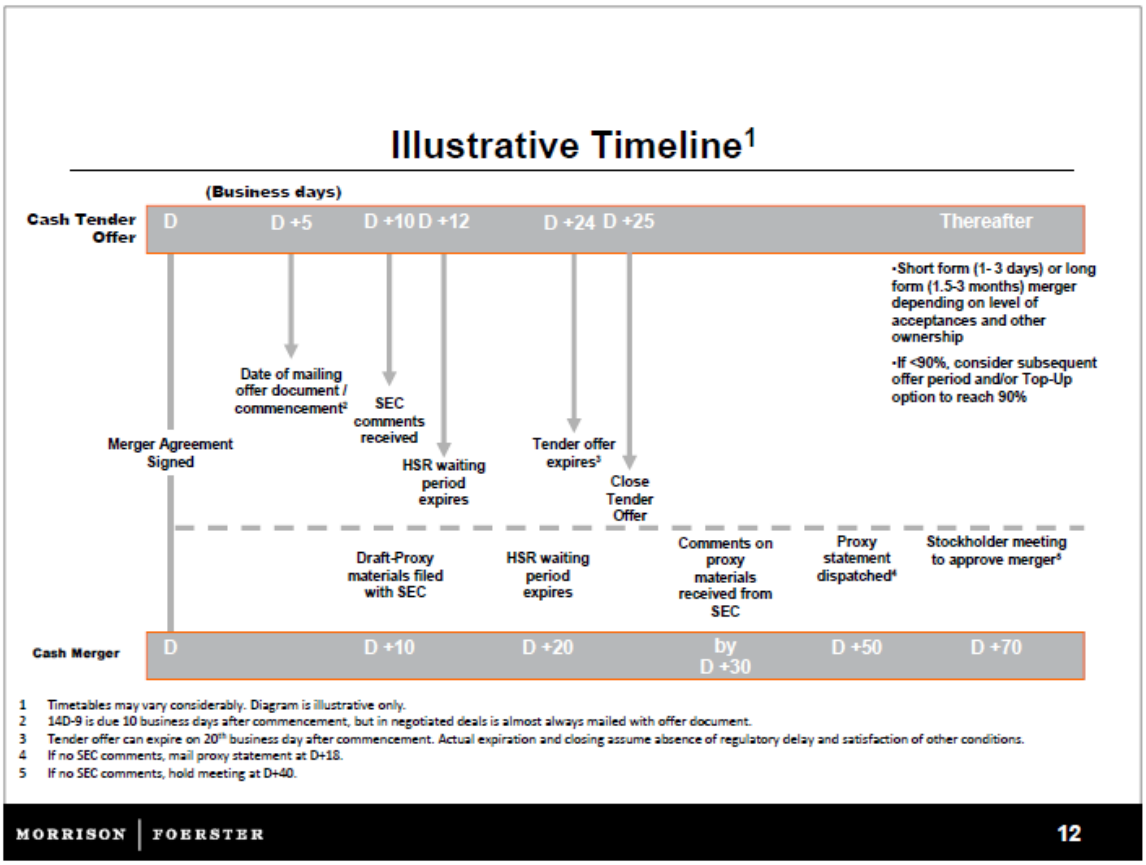
arguments here because they are relevant to Volcano stockholders and doing so furthers the "interests of justice." *See* Del. Supreme Ct. R. 8. ("Only questions fairly presented to the trial court may be presented for review; provided, however, that when the interests of justice so require, the Court may consider and determine any question not so presented.").

[27] *See* Appellants' Op. Br. at 30-32 (discussing the disadvantages stockholders have in a tender offer).

[28] Offenberg, D. and C. Pirinsky, *How do acquirers choose between mergers and tender offers?*, Journal of Financial Economics, Volume 116, Issue 2, 331–348 (May 2015) (hereafter, "Offenberg").

[29] Mergers and Acquisitions Committee Business Combinations and Proxy Statements Subcommittee, *Tender Offers: The New Paradigm and SEC M&A Updates*, https://media2.mofo.com/documents/130809-tender-offers-new-paradigm-sec-ma-updates.pdf, at 12 (August 9, 2013). Of note, though stockholder voter "proxy materials must be filed with, **and cleared by**, the SEC before the target company uses the proxy materials to solicit the votes of its stockholders," there is no such regulatory approval necessary with tender offers. Ann Beth Stebbins & Alan C. Myers, *International Comparative Legal Guides to: Mergers & Acquisitions* 319 (2009) *available at* https://www.skadden.com/sites/default/files/publications/Publications1776_0.pdf;



(emphasis added); *see also* Sullivan & Cromwell LLP, *Recent Amendments to Delaware Corporation and LLC Statutes: Adoption of Section 251(h) Facilitates Tender and Exchange Offers; Fiduciary Duties Obtain in LLC Absent Elimination; Public Benefit Corporations Authorized*, at 3, n.4 (September 17, 2013), *available at* https://www.sullcrom.com/siteFiles/Publications/SC_Publication_Recent_Amendments_to_Delaware_Corporation_and_LLC_Statutes.pdf. Moreover, while the "FTC and DOJ have 30 days to review a merger or exchange offer for antitrust concerns under the Hart-Scott-Rodino Act," they "only have 15 days for a cash tender offer." Offenberg, *supra* note 28, at 6-7. The speed and reduced regulatory oversight present additional risk to minority stockholders – risk which could and should be offset by heightened judicial scrutiny.

The expediency of tender offers potentially negatively impacts minority stockholder interests for several reasons, including a lower chance of a topping bidder emerging and less of an opportunity for stockholder activists to gain traction with any concerns about the deal, in the hope of receiving a price increase.[30] Because a target board's "fiduciary out" extinguishes upon completion of the tender offer, potential competitor bidders have significantly less time to formulate a topping bid to the benefit of minority stockholders.[31]

Lastly, Appellees misrepresented Appellants' position regarding "top-up" provisions, couching it as a gripe about the protections afforded by "[Section] 251(h)'s 50% approval threshold."[32] Appellants did not make the argument that

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30 *See* Appellant's Op. Br. at 30-32.

31 Chief Justice Strine, then serving as Vice Chancellor, earlier acknowledged the "practical difficulty for a competing bidder to enter into a definitive agreement within a 25-day period, calling it 'almost impossible to do' given the time delays accompanying that process, namely, allowing the initial bidder to match the alternate proposal, causing the board to terminate the existing agreement, conducting due diligence, and negotiating the terms of the definitive agreement." John Mark Zeberkiewicz and Blake Rohrbacher, *The Shops Are Open: Delaware's New Take on Go-Shop Provisions* under *Revlon.* Insights: The Corporate & Securities Law Advisor, Volume 21 Number 7 (July 2007) (citing *Berg v. Ellison*, C.A. No. 2949-VCS, at 5-6 (Del. Ch. June 12, 2007) (TRANSCRIPT). The lack of protection provided by a very brief "go-shop" period coupled with Appellants' allegations that the Board failed to conduct an active market check, especially in the later stages in the sales process, cumulatively demonstrates the risks of a tender offer "go-shop" period. *See* CAC ¶¶ 11-12, 28-29, 81-90.

32 Def. Ans. Br. at 39.

stockholders are prejudiced by the voter threshold amount, but rather that pre-Section 251(h) tender offers, with "top up" provisions, offered a rare potential advantage in bargaining power to minority stockholders – one which could potentially off-set some of the various disadvantages, discussed above,[33] inherent to tender offers. Specifically, Appellants argued that, in rendering obsolete "top-up" provisions, Section 251(h) also – perhaps inadvertently – mitigated target board bargaining powers because, as noted in Appellants' Opening Brief,[34] the effectiveness of "top-up" provisions are "constrained by the amount of authorized, but unissued, shares of common stock" that a target company has available.[35] Therefore, a tender offer that received over 50% of the shares outstanding but well under the 90% threshold, might not have enough authorized shares to issue to the acquiring company to reach the 90% threshold necessary to complete the short-

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33 *See* Appellant's Op. Br. at 30-32.

34 *Id*. at 30, 33, n.25.

35 Devos, *supra* note 25, at 2-3. And note that although the authors' focus is on the effect of "top-up" provisions, they postulate that 251(h) serves to only increase any findings of risk to minority stockholder value. *Id* at 3 ("although top-up options are no longer necessary, studying their use in tender offers is important, as the findings of our paper extend to the manner in which tender offers, under DGCL amendment (Section 251[h]), are currently conducted. Thus, any potential negative impact on stockholder wealth which may have been associated with the use of top-options prior to August 1, 2013 is likely to still exist after that date, calling into doubt the fairness, to stockholders, of the DGCL amendment . . . . The amendment gives an acquirer an advantage similar to that from the top-up option, without the need for a large number of unissued, authorized shares.").

form merger. As a result, the parties would need to resort to a long-form merger – which entails a stockholder vote, with all the customary regulatory oversight and none of the greater expediency effect of a tender offer. To avoid such an undesirable scenario, a target board could wield enhanced bargaining power to extract a more favorable deal for minority stockholders, therefore one more likely to garner a higher tender percentage. Section 251(h) removed "top-up" provisions from common use and in-so-doing may have lessened target boards' bargaining powers.

Ultimately, the differences between tender offers and mergers involving stockholder votes involve many empirical questions – most of which remain largely understudied.[36] Nevertheless, as presented above, there exist various distinctions and potential disadvantages to minority stockholder interests inherent to tender offers. Therefore, Appellants respectfully request that the Court err of the side of protecting stockholder interests by refusing to apply *Corwin*-based cleansing to tender offers, and allowing the protections of *Revlon* enhanced judicial scrutiny to remain intact in appropriate circumstances.

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[36] *See* Devos, *supra* note 25, at 6; Sandra Betton, B. Espen Eckbo, & Karin S. Thorburn, *Corporate Takeovers*, in HANDBOOK OF CORPORATE FINANCE*:* EMPIRICAL CORPORATE FINANCE, 316 (2008) ("Systematic empirical evidence on the choice of merger versus tender offer is only beginning to emerge.").

CONCLUSION

For the reasons stated herein, the Court should reverse the Court of Chancery's decision below and reinstate Appellants' claims against Appellees.

Dated: October 21, 2016

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