M&A Litigation

Contributing editors
William M Regan, Jon M Talotta and Ryan M Philp

Hogan Lovells

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GETTING THE DEAL THROUGH

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First edition

Getting the Deal Through is delighted to publish the first edition of M&A Litigation, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to William M Regan, Jon M Talotta and Ryan M Philp of Hogan Lovells US LLP, the contributing editors, for their assistance in devising and editing this volume.

GETTING THE
DEAL THROUGH

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Introduction

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Hogan Lovells US LLP

M&A transactions typically are transformational corporate events. From comparatively small private company transactions involving tens of millions of US dollars, to the largest multinational public company deals worth more than US$100 billion, the purchase or sale of any company involves significant risks and many uncertainties. M&A transactions impact the participants – directors, officers, employees, stockholders, creditors and customers – at every level of the corporate enterprise. And even the most strategic and well-planned M&A transactions sometimes fail to deliver the economic benefits that the parties anticipated at signing. These factors individually and collectively make M&A transactions ripe for litigation.

M&A litigation also raises many important policy issues, ranging from the appropriate role of corporate directors and stockholders both in making business decisions and in pursuing internal corporate misconduct, to the enforceability of contract provisions allocating various risks in connection with private company deals. The individual chapters that follow this introduction summarise how key jurisdictions around the world address these policy issues, and the extent to which they permit, encourage or limit M&A litigation. A survey of these chapters reveals a number of significant similarities, but also a number of important differences.

Common themes in global M&A litigation

Across common law and code law countries, there are a number of striking similarities with respect to how different jurisdictions address M&A litigation issues. For example, nearly every country addressed in this book expressly or impliedly embraces some form of what in the US is called the 'business judgment rule'. Whether characterised as a formal legal presumption or simply the inherent reluctance of judges to interfere with discretionary business decisions, jurisdictions around the world show a strong tendency to protect or defer to corporate decision-making in the M&A context where the board acts in good faith, on an informed basis and without conflicts of interest.

Similarly, nearly every jurisdiction requires that corporate actors in the M&A context comply with some variation of the duty of care and the duty of loyalty. To uphold a challenged M&A decision, courts broadly require that directors and management make decisions on a fully informed basis, acting with the care of a reasonably prudent person under the applicable facts and circumstances. Jurisdictions consistently require that corporate representatives disclose or avoid conflicts of interest, such that M&A decisions are made in good faith in the best interests of the corporate enterprise, and not in the personal interests of any individual director or officer.

Another commonality across jurisdictions concerns the impact of a stockholder vote. After a board has approved an M&A transaction, separate approval by the stockholders is often required before the transaction can close. In most jurisdictions, where the stockholder vote is made on a fully informed basis, subsequent claims challenging the deal or the directors' conduct in connection with the deal typically will be barred. This may be under a theory that the stockholder vote 'ratified' the board's decision, that the vote 'cleansed' the transaction of any fiduciary duty issues or that stockholders are 'estopped' from challenging a transaction approved by a majority of investors.

One final recurring theme is that nearly every jurisdiction applies additional scrutiny with respect to responsive or defensive measures taken by a board in response to unsolicited takeover proposals. Some jurisdictions impose heightened judicial scrutiny on such measures, while others require separate stockholder or regulatory approval. But in all cases, jurisdictions recognise the increased risks and potential conflicts when a board acts in response to an unsolicited offer.

Notable differences in M&A litigation across jurisdictions

There also are a number of stark differences in M&A litigation across jurisdictions. For example, outside of the United States, few jurisdictions allow individual stockholders to pursue broad class or collective actions on behalf of all similarly situated investors, and, in particular, few jurisdictions permit class actions that require investors to affirmatively 'opt-out' to avoid being bound by a judgment. Jurisdictions also vary significantly on the extent to which they permit individual investors to pursue 'derivative' actions to recover damages incurred by the corporation (some allow broad derivative rights, some do not recognise the procedure at all, and still others provide for minimum ownership requirements or court approval before an investor will be permitted to proceed).

Similarly, few jurisdictions permit stockholders to take broad pre-trial discovery in M&A litigation, although most recognise some form of a books and records inspection right. The majority of courts also limit the ability of corporate defendants to resolve M&A litigation through early dispositive motion practice.

Jurisdictions also follow significantly varying approaches with respect to whether a corporation may limit liability for directors involved in M&A transactions through exculpatory by-law or corporate charter provisions. Some jurisdictions broadly allow such provisions; others find them void as against public policy; and others permit them for certain types of claims (eg, claims sounding in ordinary negligence or claims by outside third parties).

One final notable difference is the extent to which jurisdictions permit corporations to require stockholders to bring M&A litigation in particular forums. Certain jurisdictions permit corporations to mandate that stockholders bring M&A litigation in particular courts or even in arbitration, while others apply their general jurisdiction and venue rules.

Conclusion

Public company M&A litigation is most common in the United States and certain other countries discussed in this book. This appears to be because of class action and discovery mechanisms that permit an individual investor to pursue claims on behalf of other similarly situated investors. It is important to note, however, that US public company M&A litigation is currently undergoing significant changes. Certain leading courts have changed the law to afford greater deference to arms-length transactions approved by a stockholder vote. These changes appear to have brought US law more in line with that of other jurisdictions permitting collective actions. Following these decisions, there has been a slight reduction in the overall number of suits filed, along with changes to the types of claims being asserted and the venues where cases are being filed. The ultimate impact of these recent changes remains to be seen, however, both within and outside the United States.

United States

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1 Identify the main claims shareholders in your jurisdiction may assert against corporations, officers and directors in connection with M&A transactions.

The claims typically asserted by shareholders in connection with M&A transactions arise out of the fiduciary duties owed by boards of directors to companies and their constituents. Corporate directors owe a corporation and its shareholders two principal fiduciary duties: the duty of care and the duty of loyalty. These two duties generally encompass a number of related duties, such as the duty of disclosure (or candour), the duty of oversight and the duty of good faith.

After an M&A transaction is announced, the seller's shareholders frequently assert breach of fiduciary duty claims alleging that the board of directors agreed to sell the company for an inadequate price following the conclusion of an unfair and/or conflicted sales process. In addition, shareholders often challenge the adequacy of the seller's disclosures in connection with a transaction, including, in particular, disclosures provided in the materials used to solicit shareholder votes on the transaction.

The law governing a board of directors' fiduciary duties is the law of the state where the company is incorporated. In the United States, the majority of large public companies are incorporated in Delaware, which has a well-developed and widely followed body of case law concerning M&A transactions. Other states have broadly similar fiduciary duty rules, but may differ on particular points of law. In the interest of brevity, this chapter discusses the most common or generally applicable US legal concepts in the context of an M&A litigation and not the law of any particular state.

2 For each of the most common claims, what must shareholders in your jurisdiction show to bring a successful suit?

To successfully bring a breach of fiduciary duty claim, shareholders generally must show the existence of a fiduciary duty and a breach of that duty. For claims alleging a breach of the duty of care, shareholders must show that the defendant did not use the amount of care that an ordinarily careful and prudent person would use in similar circumstances. For claims alleging a breach of the duty of loyalty, shareholders must show that the defendant failed to act in the best interest of the corporation and its shareholders. To successfully bring a disclosure claim under state law, shareholders must show that the defendant failed to disclose fully and fairly all information that is material to a shareholder's decision.

In recent years, many courts have become increasingly sceptical of disclosure claims brought under state fiduciary duty law. As a result, many shareholders now bring disclosure claims under the US federal securities laws. Such claims require shareholders to demonstrate that a disclosure document failed to accurately disclose material information relating to an M&A transaction. In certain cases, the false or misleading statement must be intentional and not merely negligent or inadvertent.

3 Do the types of claims that shareholders can bring differ depending on whether the corporations involved in the M&A transaction are publicly traded or privately held?

Yes. In the context of public M&A transactions, shareholder claims typically are brought derivatively, on behalf of the corporation, or as a class action, and the claims are premised on the fiduciary duties owed by the company's directors to the company or the requirements of US federal securities laws governing disclosures to shareholders. By contrast, in the context of privately held corporations, claims typically are brought by the buyer or buyers, or the seller or sellers, and arise out of the parties' contract or direct dealings. Claims in private M&A transactions most frequently involve purchase price adjustment or earn-out disputes, indemnification disputes arising from contractual representations and warranties, and fraud claims based on alleged misstatements or omissions that induced one party to enter into the contract.

4 Do the types of claims that shareholders can bring differ depending on the form of the transaction?

In certain cases, yes, but not in others. For example, in the public M&A context, shareholder claims alleging state law breach of fiduciary duty will not necessarily differ if a transaction is structured as a merger instead of a tender offer. For disclosure claims brought under federal law, however, shareholder claims will vary depending on the structure of the transaction. For example, shareholders challenging disclosures in connection with a tender offer under section 14(e) of the Securities Exchange Act of 1934 typically must show that the speaker acted with *scienter* or the intent to deceive investors and otherwise satisfy heightened pleading standards. In contrast, in a merger structure where shareholders challenge proxy disclosures under section 14(a) of that same statute, most courts hold that shareholders do not need to establish that a false or misleading statement was intentional.

5 Do the types of claims differ depending on whether the transaction involves a negotiated transaction versus a hostile or unsolicited offer?

As a general matter, the fiduciary duties of a board of directors do not differ depending on whether the transaction is negotiated or is the result of a hostile or unsolicited offer. In both circumstances, the board is required to act in a fully informed manner, with the requisite level of care, and in the best interests of the company and its shareholders. In the context of a hostile or unsolicited offer, it is generally accepted that a target board may, in appropriate circumstances, act consistently with its fiduciary duties by resisting or rejecting a hostile or unsolicited offer. However, where shareholders challenge affirmative conduct by a company to resist a hostile or unsolicited offer, such as the implementation of a 'poison pill' or shareholder rights plan, the board's conduct will be evaluated under more rigorous standards of review designed to ensure that the board is acting to protect shareholder interests.

6 Do the types of claims differ depending on whether the loss is suffered by the corporation or by the shareholder?

Yes. Claims for losses suffered by a corporation typically belong to the corporation. Therefore, for the shareholder to bring claims on behalf of the corporation – that is, derivatively – the law imposes several threshold requirements that a shareholder must satisfy to have standing to bring corporate claims. Shareholder derivative actions seek recovery for the benefit of the corporation as a whole. In contrast, where the loss is suffered by shareholders, as distinct from the corporation itself, one or more shareholders may seek to pursue direct recovery from the alleged wrongdoers. Such 'direct' actions frequently seek recovery on behalf of a group (or class) of shareholders, and thus must satisfy different procedural requirements that apply to class actions. Recovery in a class action belongs to the shareholders, not the corporation.

In M&A transactions, courts typically hold that shareholders have direct claims when asked to vote based on misleading disclosures or when forced to exchange shares for inadequate consideration.

7 Where a loss is suffered directly by individual shareholders in connection with M&A transactions, may they pursue claims on behalf of other similarly situated shareholders?

Yes. In instances where a loss is suffered directly by individual shareholders, as distinct from losses suffered by the corporation, shareholders may seek to bring a class action lawsuit on behalf of themselves and other similarly situated shareholders. To commence a class action lawsuit, the named plaintiff must meet several requirements designed to ensure that prosecution of claims on a class-wide basis is necessary and practical, and that the named plaintiff is properly situated to act on behalf of the class.

Among other things, a proposed class representative must show that:

- the class members are so numerous that it would be impracticable to join them all in a single litigation;
- there are common questions of law or fact applicable to all class members;
- the proposed representative's claims are typical of all class member claims; and
- the proposed representative will adequately represent the interests of the absent class members.

In addition, the proposed class representative must show that common questions predominate over any individualised issues applicable to the class members.

8 Where a loss is suffered by the corporation in connection with an M&A transaction, can shareholders bring derivative litigation on behalf or in the name of the corporation?

Yes. Where a loss is suffered by the corporation, rather than shareholders individually or as a group, shareholders may bring derivative actions on behalf of the corporation. To have standing to bring a derivative claim on behalf of the corporation, a shareholder must meet strict requirements intended to determine whether it is appropriate to vest the shareholder with authority to bring claims belonging to the corporation. A shareholder must either make a demand on the board that is wrongfully refused, or demonstrate in the complaint that any such demand would have been futile. Further, a derivative plaintiff must remain a shareholder from the time of the challenged transaction until the conclusion of the litigation.

Derivative claims arise more frequently in connection with failed M&A transactions (eg, where a board of directors terminates a deal or changes its recommendation and thereby causes the company to pay a substantial termination fee to the counterparty).

9 What are the bases for a court to award injunctive or other interim relief to prevent the closing of an M&A transaction? May courts in your jurisdiction enjoin M&A transactions or modify deal terms?

Due to the impracticability of unwinding a transaction after it has closed, US courts have the discretion to issue an injunction to prevent the closing of an M&A transaction in certain circumstances, including where the disclosures fail to provide shareholders with adequate information, or the deal protection provisions in the M&A agreement improperly preclude other potential bidders from coming forward or coerce shareholders into voting in favour of the transaction. Although the injunction standard differs slightly from jurisdiction to jurisdiction, most courts consider whether there is a reasonable probability that the movant will succeed on its claim, whether the movant will suffer imminent and irreparable harm, and the balance of the equities. Rather than enjoin a transaction, courts also in limited circumstances may strike objectionable deal terms.

10 May defendants seek early dismissal of a shareholder complaint prior to disclosure or discovery?

Yes. Defendants may seek early dismissal of a shareholder complaint by filing a motion to dismiss. Defendants may seek dismissal of shareholder derivative and class actions on the ground that the shareholder plaintiffs fail to meet one or more of the procedural requirements for commencing such an action. Defendants also may seek dismissal of shareholder claims on the ground that the complaint fails to adequately state an actionable claim.

11 Can shareholders bring claims against third-party advisers that assist in M&A transactions?

Yes. Claims against third-party advisers have become increasingly common in recent years – in particular, claims based on financial advisers' undisclosed conflicts of interest. Typically, such claims have been asserted on the theory that conflicted financial advisers aided and abetted breaches of fiduciary duty by the board of directors. For example, shareholders have asserted claims against financial advisers who provided fairness opinions to the target, but had undisclosed financial incentives related to the buyer.

12 Can shareholders in one of the parties bring claims against the counterparties to M&A transactions?

Yes. Generally, efforts to achieve a better deal through arm's-length negotiations will not give rise to liability, but liability for aiding and abetting may arise in very limited circumstances where, for example, a party intentionally creates or exploits a conflict of interest. In addition, shareholders may bring claims against a counterparty based upon allegedly false or misleading disclosures, such as where a joint proxy is issued or in connection with a tender offer.

13 What impact do the corporation's constituting documents have on the extent board members or executives can be held liable in connection with M&A transactions?

Many state corporation statutes permit corporations to include in their charter a provision eliminating director monetary liability for breaches of the duty of care. Such provisions make it difficult for shareholders to prevail in post-closing damages cases where the core contention is that the directors should have or could have obtained a better price when selling the company.

However, exculpatory provisions of this kind do not eliminate director monetary liability for breaches of the duty of loyalty or for actions undertaken in bad faith. Nor do these provisions prevent a shareholder from pursuing a claim for non-monetary relief (eg, an injunction against consummation of an M&A transaction), or from pursuing a claim for monetary damages for actions undertaken by an officer of the corporation.

14 Are there any statutory or regulatory provisions in your jurisdiction that limit shareholders' ability to bring claims against directors and officers in connection with M&A transactions?

As a general matter, there are no statutory or regulatory provisions precluding such claims, but as noted above there are procedural rules applicable to shareholder class and derivative actions challenging M&A transactions. A shareholder class action asserting claims under the federal securities laws also must comply with the requirements of the Private Securities Litigation Reform Act of 1995.

15 Are there common law rules that impair shareholders' ability to bring claims against board members or executives in connection with M&A transactions?

Under traditional common law, most decisions by disinterested directors receive the protections of the business judgment rule. This doctrine provides a presumption that directors making a business decision acted on an informed basis, in good faith and in the honest belief that the action was taken in the best interests of the company. A plaintiff can rebut the business judgment rule by demonstrating a breach of the directors' obligations of good faith, loyalty or due care (eg, by proving corporate waste). When the business judgment rule applies and is not rebutted, a court will not second-guess director decisions.

16 What is the standard for determining whether a board member or executive may be held liable to shareholders in connection with an M&A transaction?

There are three primary standards for assessing director conduct in M&A transactions: the business judgment rule, enhanced scrutiny and entire fairness.

Business judgment rule
As discussed above, when the business judgment rule applies, courts generally will not second-guess the decisions of directors.

Enhanced scrutiny
An intermediate standard of review applicable to M&A transactions involving control of a company that requires directors to satisfy certain conditions before they will enjoy the benefits of the business judgment rule. For example, forms of enhanced scrutiny apply to transactions involving a break-up of a corporation and to defensive measures adopted by directors in response to a potential change-in-control.

Entire fairness
Courts will require directors to prove the entire fairness of an M&A transaction in which a majority of directors are interested or that involves a controlling shareholder. The defendants bear the burden of proving entire fairness.

In many litigations involving M&A transactions, the standard of review that the court chooses to apply will be dispositive. Where a court applies the business judgment rule, decisions made by a board of director are upheld in the vast majority of cases. In contrast, an entire fairness review strongly favours plaintiff shareholders because it forces the directors to affirmatively prove that all aspects of the process and price were fair.

17 Does the standard vary depending on the type of transaction at issue?

Yes, in certain cases. For example, enhanced scrutiny applies and 'Revlon duties' are implicated when a company initiates an active bidding process involving a clear break-up of the company; when, in response to an offer, a target abandons its long-term strategy and seeks an alternative transaction; or when approval of a transaction results in a 'change of control'.

Interested transactions (eg, a going private transaction with a controlling shareholder) are subject to the entire fairness test. Other M&A transactions (eg, a merger of equals between two public corporations with no controlling shareholder) generally are subject to the business judgment rule.

18 Does the standard vary depending on the type of consideration being paid to the seller's shareholders?

Yes, in certain cases. In a cash-out merger where shareholders will have their investment in the ongoing enterprise terminated, Revlon duties will apply and courts will consider whether directors have taken reasonable steps to provide shareholders with the best transaction reasonably available. A stock-for-stock merger in which control of the combined entity will remain in a fluid market, by contrast, generally will not trigger enhanced scrutiny. Transactions involving a mixture of cash and stock are assessed on a case-by-case basis, although enhanced scrutiny will generally apply when 50 per cent or more of the consideration that shareholders receive is in cash.

19 Does the standard vary if one or more directors or officers have potential conflicts of interest in connection with an M&A transaction?

A transaction in which a majority of directors are interested will be subject to the test of entire fairness. Under the entire fairness test, the burden of proof is on the board of directors to show that the transaction was the product of an arm's-length fair process that resulted in an objectively fair price. The entire fairness test is fact-intensive by nature and often requires resolution by trial (and not pre-trial motion practice).

20 Does the standard vary if a controlling shareholder is a party to the transaction or is receiving consideration in connection with the transaction that is not shared ratably with all shareholders?

Yes. A transaction in which a controlling shareholder is a party or has an interest different from other shareholders ordinarily will be scrutinised under the entire fairness test. However, the business judgment rule can apply to a transaction with a controlling shareholder if the transaction is conditioned upon approval by a fully empowered special committee of disinterested and independent directors; and the transaction is conditioned upon approval by an informed and non-coerced vote by a majority of the minority shareholders.

Where only one of these two conditions is met, the entire fairness test will continue to apply, but the burden will shift to the plaintiff to prove the unfairness of the transaction.

21 Does your jurisdiction impose legal restrictions on a company's ability to indemnify, or advance the legal fees of, its officers and directors named as defendants?

Indemnification may be required, permitted or prohibited depending on the facts and circumstances of a particular case. To the extent a director or officer has been successful on the merits in connection with an M&A litigation, indemnification for attorneys' fees and expenses is typically mandatory. At the other extreme, directors and officers may not be indemnified for a claim, issue or matter in which they are found to be liable to the corporation (eg, a shareholder derivative action) absent court approval. In all other cases, directors and officers may be indemnified if it is determined that they acted in good faith in a manner reasonably believed to be in, or not opposed to, the best interests of the corporation and, in a criminal action or proceeding, where there is no reasonable cause to believe the person's conduct was unlawful.

Corporations may advance legal fees to a director or officer if the person receiving advancement furnishes an undertaking agreeing to repay the corporation if it is ultimately determined that the standard for indemnification has not been met.

22 Can shareholders challenge particular clauses or terms in M&A transaction documents?

Yes, shareholders challenging an M&A transaction often will focus on deal-protection devices (eg, termination fees, matching rights, 'no-shop' clauses). These devices will be evaluated under the enhanced scrutiny standards described above. Courts generally allow parties to include such devices in their M&A transaction agreements provided that they do not, separately or in the aggregate, preclude other bidders from making offers to acquire the seller or coerce shareholders into approving a transaction favoured by management.

23 What impact does a shareholder vote have on M&A litigation in your jurisdiction?

In a transaction that does not involve a controlling shareholder, a fully informed and uncoerced shareholder vote approving the transaction will result in the irrebuttable application of the business judgment rule. Courts conclude that such a vote will 'cleanse' any breach of fiduciary duty that took place in connection with the deal approval process.

In transactions involving a controlling shareholder, and absent satisfaction of the other prerequisites described above, shareholder approval will shift the burden to a plaintiff to prove the unfairness of a transaction.

24 What role does directors' and officers' insurance play in shareholder litigation arising from M&A transactions?

Companies typically have insurance for their directors and officers that will cover the types of claims generally asserted in shareholder litigation arising from M&A transactions. The most important role of directors' and officers' insurance is minimising the risk that a director or officer will be subject to personal liability in connection with shareholder litigation. Directors' and officers' insurance also can influence the parties' willingness or ability to settle shareholder claims. Insurers generally play a small role in the preliminary phases of litigation, but may become more involved if a matter progresses or enters into formal settlement negotiations, such as mediation.

Update and trends

M&A litigation in the US has changed significantly in recent years, largely driven by several notable decisions issued by the Delaware Supreme Court and the Delaware Court of Chancery. For example, in the public company M&A litigation context, many shareholder suits previously were resolved through 'disclosure-only' settlements. In a typical case, a shareholder plaintiff would file a complaint alleging that the target's board of directors breached its fiduciary duties of care and loyalty in approving an unfair merger, and that the target's proxy statement seeking shareholder approval was misleading or failed to disclose important information. The parties often resolved such cases by causing the target to provide its shareholders with supplemental disclosures regarding the proposed transaction (but not an increase in the sale price or other material changes to the deal terms). The defendants in turn would receive a broad release binding on all of the target's shareholders, while paying a substantial attorneys' fee award to the plaintiffs' counsel. Such disclosure-only settlements contributed to a widely publicised increase in the number of public company M&A deals that were challenged in litigation: at one time, more than 90 per cent of large public company transactions in the US resulted in shareholder lawsuits.

In *In re Trulia, Inc Shareholder Litigation*, the Delaware Court of Chancery concluded that disclosure-only settlements typically failed to provide real benefits to shareholders and would no longer be approved by the Court unless the alleged disclosure deficiencies were 'plainly material.' The Chancery Court reasoned that the supplemental disclosures provided to shareholders frequently addressed unimportant background details that did not aid shareholders in deciding whether to approve the transaction. Plaintiffs' counsel and defendants, on the other hand, received substantial benefits in the form of attorneys' fees and broad releases, respectively. The *Trulia* decision caused an initial decline in the total number of M&A suits filed. In addition, *Trulia* has caused many shareholders to challenge M&A transactions under US federal securities law rather than through state fiduciary duty and disclosure claims.

Another important recent development concerns the impact of a shareholder vote on M&A litigation disputes. In *Corwin v KKR Financial Holdings LLC*, the Delaware Supreme Court held that certain M&A transactions would be reviewed under the deferential business judgment standard once the transaction was approved by an uncoerced and fully informed shareholder vote. Owing to the 'cleansing' effect of a shareholder vote, the *Corwin* decision has made it more difficult for shareholders to pursue post-closing damages claims against target boards.

The combined impact of the *Trulia* and *Corwin* decisions has caused certain shareholders to pursue a different strategy. Rather than challenge M&A transactions prior to a vote, a number of shareholders are now first pursuing statutory books and records demands in order to obtain internal company documents and other non-public material relating to the transaction. These shareholders then use the documents obtained through the books and records process to craft more detailed complaints asserting that important details were not disclosed to shareholders, and therefore that the *Corwin* business judgment analysis should not apply. These cases are working their way through the court system.

Another important decision that has changed the M&A litigation landscape is *Kahn v M&F Worldwide Corp*, where the Delaware Supreme Court affirmed a Delaware Court of Chancery ruling that going-private mergers with a controlling shareholder, which typically had been reviewed under the strict 'entire fairness' test, instead would be subject to a deferential business judgment review if certain procedural protections were part of the deal structure. First, the controlling shareholder must agree at the outset that the transaction will be subject to approval by a fully informed and independent special board committee empowered to retain its own financial and legal advisers and, if necessary, decline the transaction. Second, the transaction must be conditioned at the outset on a 'majority of the minority' vote, meaning that a majority of shareholders who are unaffiliated with the controlling shareholder must separately vote in favour of the deal. The M&F decision makes it more difficult for shareholders to challenge going-private transactions structured in accordance with this framework.

One final current trend in US M&A litigation that merits mention involves the appraisal process. As noted above, in many US M&A transactions, shareholders have statutory appraisal rights, which allow dissenting shareholders to petition a court to determine the fair value of their ownership interest. Previously, certain investors pursued an 'appraisal arbitrage' strategy in which the investor would purchase stock upon the announcement of a deal, and then pursue an appraisal claim. The goal was to obtain a court award finding that the fair value was substantially in excess of the deal price, while also taking advantage of favourable statutory interest rates, with the deal price serving as a worst-case floor for the investment. Several recent appraisal cases, most notably the Delaware Supreme Court's decision in *Dell, Inc v Magnetar Global Event Driven Master Fund Ltd*, have resulted in the investor being awarded substantially less than the deal price. In addition, recent cases emphasise that in the public company context, courts in most instances should give significant weight to the deal price as evidence of fair value and less to after-the-fact valuations created for the purpose of appraisal litigation. Collectively, the recent cases have increased the risk to investors pursuing appraisal arbitrage strategies.

In recent years, many insurance carriers have substantially increased the deductible or retention applicable to M&A litigation such that a significant part of defence costs and early-stage settlement payments are made by the insured.

25 Who has the burden of proof in an M&A litigation – the shareholders or the board members and officers? Does the burden ever shift?

The business judgment rule protects the decisions of officers and directors of a corporation if those decisions are made in good faith, informed and believed to be in the best interests of the corporation. Where the business judgment rule applies, the plaintiff has the burden to rebut the presumption. The plaintiff may do so by showing, for example, that the board of directors failed to consider relevant material information or rushed to a decision without a legitimate business justification. If a plaintiff is able to overcome the business judgment rule presumption, then the burden shifts to the defendants, who must demonstrate 'entire fairness', which requires that the transaction be entirely fair to the corporation and its shareholders.

26 Are there pre-litigation tools that enable shareholders to investigate potential claims against board members or executives?

Shareholders have a qualified, statutory right to inspect a corporation's books and records. To do so, a shareholder must make a demand that includes a proper purpose for the inspection. A proper purpose is one reasonably related to an individual's interest as a shareholder, such as investigating alleged mismanagement or corporate waste. If the shareholder can state a proper purpose, then he or she may seek books and records that are necessary to accomplish that proper purpose. The scope of documents available to a shareholder pursuant to a books and records demand is narrower than is available during discovery between litigation parties.

Shareholders increasingly are making books and records demands in response to M&A transactions (rather than proceeding directly to litigation) for two reasons. First, Delaware courts have encouraged shareholders to obtain books and records in order to plead more detailed complaints. Second, to successfully proceed with a post-closing damages case, shareholders need to show that a vote or tender was not made on an informed basis or was the product of material conflicts.

27 Are there jurisdictional or other rules limiting where shareholders can bring M&A litigation?

A shareholder must bring M&A litigation in a forum that has subject matter jurisdiction over the claims as well as personal jurisdiction over the parties. A federal court generally may exercise subject matter jurisdiction over state law claims if a shareholder also asserts valid federal claims or if the parties' citizenship is diverse. A state court generally does not have subject matter jurisdiction over federal claims. Personal jurisdiction over a corporation exists, at a minimum, in its state of incorporation and principal place of business, and may exist elsewhere depending on the corporation's business contacts with the jurisdiction. Whether a court has personal jurisdiction over a director or officer is a more detailed inquiry, and turns on the contacts between that director or officer and the forum. A corporation also may control where suits can be brought by adopting a forum selection clause in its by-laws or articles of incorporation.

28 Does your jurisdiction permit expedited proceedings and discovery in M&A litigation? What are the most common discovery issues that arise?

Shareholders may seek expedited proceedings for the purpose of setting expedited discovery deadlines and the date for an injunction hearing. The court generally has broad power to permit expedited proceedings, and the plaintiff's burden is relatively minimal, that is, the plaintiff need only demonstrate a colourable claim and a sufficient possibility of irreparable harm to obtain expedition. When expedited discovery is allowed, the seller typically is required to produce presentations from its financial adviser, board minutes relating to the transactions, and management projections or forecasts, among other things.

The most common discovery issues concern attorney–client privilege. Some jurisdictions recognise a fiduciary exception to the attorney–client privilege, which, under certain circumstances, allows shareholders to invade the corporation's attorney–client privilege to prove fiduciary breaches by officers and directors upon a showing of good cause. In addition, if the corporation is based outside of the US, issues may arise regarding applicable blocking or privacy statutes.

29 How are damages calculated in M&A litigation in your jurisdiction?

Damages typically are designed to restore the shareholder to the position he or she would have been in if the alleged misconduct had not occurred. In M&A litigation, shareholders generally seek the difference between the deal price and what the deal price would have been absent the alleged misconduct. To litigate damages, plaintiffs and defendants usually retain experts, who typically employ one or more generally accepted valuation methodologies (eg, discounted cash flow analysis, an analysis of comparable transactions) to support an opinion that the deal price should have been higher or lower (on the plaintiffs' side) or that the deal price was fair and reasonable (on the defendants' side).

30 What are the special issues in your jurisdiction with respect to settling shareholder M&A litigation?

Settlements of shareholder class actions and derivative cases require court approval. Typically, the plaintiff shareholder, through counsel, will file a motion seeking the court's preliminary approval of the proposed settlement. The motion will request that the court approve, among other things, a process for providing notice to the shareholders; the content of a notice to be mailed or published in a newspaper or trade journal, or both; and the deadline for shareholders to object in writing, at a final approval hearing, or both.

Often, the lawyers for the shareholder plaintiff also will seek the court's approval of an attorneys' fees award to be paid from the common settlement fund. At a final settlement hearing, the court will assess whether the settlement is fair and reasonable, subject to any objections it receives.

Over the past decade, M&A litigation has become increasingly common. At one point, complaints were filed in connection with approximately 95 per cent of public company deals valued at more than US$1 billion. These filings often were followed by what became known as 'disclosure-only' settlements in which the seller's shareholders received supplemental disclosures prior to a vote or tender, the defendants received a broad class-wide release covering all claims relating to the transaction and plaintiffs' counsel received a substantial fee award.

US courts have become increasingly sceptical of disclosure-only settlements, concluding that shareholders receive no real benefit in the majority of cases. As a result, courts now prefer in most instances that parties pursue mootness resolutions without court involvement in which the defendants agree to address the shareholders' disclosure claims, the release given to defendants is narrowed and the attorneys' fees paid to shareholders' counsel are lower.

31 Can third parties bring litigation to break up or stop agreed M&A transactions prior to closing?

Third parties – increasingly, activist hedge funds – can employ a variety of strategies to stop or break-up proposed M&A transactions, some of which involve filing litigation (in their capacity as shareholders) and some of which do not (such as publicly criticising the transaction or soliciting shareholder proxies opposing the transaction). Activist investors may seek to enjoin a proposed transaction by, among other things, attacking the motives and financial interests of the target company's board of directors and management team, challenging deal-related disclosures or asserting that deal protection measures agreed to with the buyer interfere with or preclude a superior bid. In certain circumstances, activist investors may pursue one or more of these strategies in collaboration with other financial or strategic buyers.

In addition, potential purchasers have in the past pursued M&A litigations to break-up agreed transactions and acquire the target away from the preferred buyer. Purchasers in such situations typically need to be shareholders in the target company to have standing. Such cases have become less common in recent years as courts have clarified the law concerning permissible anti-takeover and deal protection measures.

32 Can third parties in your jurisdiction use litigation to force or pressure corporations to enter into M&A transactions?

Activist investors also may pursue litigation or other tactics to force or pressure corporations to enter into unsolicited transactions. Generally, defensive measures taken by a board of directors to resist unsolicited offers are subject to enhanced judicial scrutiny, and thus are subject to challenge by shareholders who wish to see the transaction proceed. In addition, activist investors may pursue non-litigation alternatives to exert pressure, such as instituting a proxy contest to obtain board control or making an unsolicited offer in the hopes that additional, superior offers will emerge.

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33 What are the duties and responsibilities of directors in your jurisdiction when the corporation receives an unsolicited or unwanted proposal to enter into an M&A transaction?

As a general matter, the fiduciary obligations of a target company's management and directors in response to an unsolicited or unwanted proposal are to act in good faith, with due care and loyalty, in what they believe to be the best interests of the corporation. A board of directors has no fiduciary duty to negotiate or sell in response to an unsolicited offer – the board also may 'just say no'. In appropriate circumstances, the board of directors may implement defensive measures to resist an offer that the board believes represents a threat. However, to be upheld by a court, such defensive measures must be in response to a legitimate threat to corporate interests, and must be reasonable and proportional in relation to the threat. Once a company elects to consider an alternative involving a break-up of the company or initiates an active bidding process, the board is required to take steps reasonably calculated to obtain the best price available.

34 Shareholders aside, what are the most common types of claims asserted by and against counterparties to an M&A transaction?

In the context of private M&A transactions, the most common claims arise out of the terms of the purchase agreement, including claims for breaches of contractual representations, covenants and warranties. These claims often are subject to indemnity provisions, and may be made against merger consideration held in escrow. In addition, purchase agreements frequently contain a mechanism for a post-closing purchase price adjustment whereby the purchase price may be adjusted to account for variations in the target's value or a depletion of its working capital. These claims typically are resolved by arbitration. In addition, buyers may assert claims premised on fraud, including claims for fraud in the inducement.

35 How does litigation between the parties to an M&A transaction differ from litigation brought by shareholders?

Shareholder litigation arising out of M&A transactions generally is commenced in a representative capacity, that is, by an individual shareholder as a class action (on behalf of a larger class of shareholders) or as a derivative action (on behalf of the company), and seeks to enforce fiduciary duties owed by a company's board of directors to the shareholders. In contrast, litigation between parties to an M&A transaction is brought directly between the parties. Private M&A litigation typically relates to the terms of the negotiated agreements and the veracity of the representations made by the parties prior to closing. Contractual counterparties do not owe each other fiduciary duties.

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