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WHAT'S INSIDE

CONTEST FOR CONTROL

Delaware high court appeal centers on validity of CEO removal

The outcome of a boardroom battle for control of Allegro Development Corp. will turn on the Delaware Supreme Court's decision as to whether the risk management software firm's directors' surprise removal of the CEO was "void" or only "voidable."

Klaassen v. Allegro Development Corp. et al., No. 583, 2013, opening brief filed (Del. Nov. 11, 2013).

In an opening brief to the high court, founder Eldon Klaassen says his enemies on the board of directors improperly ambushed him with a secret removal action that violated company bylaws and was therefore void — clearly invalid and of no effect.

He's appealing an Oct. 11 Chancery Court ruling in which Vice Chancellor J. Travis Laster found that the board's Nov. 1, 2012, removal action was only voidable, meaning it could be challenged and possibly proven to be invalid. *Klaassen v. Allegro Dev. Corp. et al.*, No. 8626, 2013 WL 5739680 (Del. Ch. Oct. 11, 2013).

Klaassen later used his majority stock holdings to replace one of the opposing directors and hold on to his director position, according to the vice chancellor's opinion. However, Klaassen

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Representations and warranties insurance: An innovative solution

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FIRREA: The Justice Department's expansive (and expensive) tool of choice

Allyson B. Baker and Andrew Olmem of Venable LLP warn that federal regulators plan to use a series of favorable court rulings to dramatically expand their use of a little-known provision of the Financial Institutions Reform, Recovery and Enforcement Act to accelerate investigations and prosecutions of bank officials for financial crisis claims.

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Representations and warranties insurance: An innovative solution

By D. Stephen Antion, Esq., and Philip Lang, Esq.
Katten Muchin Rosenman LLP

One of the most contentious and negotiated aspects of an acquisition transaction is the allocation of risk for post-closing breaches of the seller's representations and warranties, and the remedies available to the buyer for such breaches. The buyer will want to be protected and indemnified for any liabilities arising from a breach, while the seller will prefer a clean break at closing with minimal holdback of the purchase consideration and without responsibility for unknown contingent liabilities. The actual representations and warranties of the seller will also be heavily negotiated to ensure they work with the indemnification provisions to properly reflect the agreed upon allocation of post-closing risk.

To help bridge the distance between the buyer and seller and mitigate risk exposure, more and more buyers and sellers are turning to representations and warranties insurance, as well as other types of transaction liability insurance. Though representations and warranties insurance was first introduced in 1998, in the past few years, the market has seen a surge in the number of transactions using transactional insurance products. Although representations and warranties insurance is still in relatively limited use in the U.S., it has seen widespread use in Europe, Asia and Australia, with about 90 percent of Australian private equity deals utilizing such insurance. Other transactional insurance products can be utilized with representations and warranties insurance to address specific risks for a particular transaction.

HOW IS REPRESENTATIONS AND WARRANTIES INSURANCE USED?

Representations and warranties insurance, whether buyer-side or seller-side, can be used as a backstop or supplement for the seller's indemnification obligations under the purchase agreement. It may also be used as a substitute remedy for indemnification that serves as the buyer's sole recourse in the event of breaches of the seller's representations and warranties. For the payment of a one-time premium, the insurer takes on the risk for breaches of the seller's representations and warranties and pays the buyer or the seller, as appropriate.

> More buyers and sellers are turning to representations and warranties insurance, as well as other types of transaction liability insurance.

Buyer-side representations and warranties insurance is more common and provides for the direct payment by the insurer to the buyer to cover losses due to breaches of the seller's representations and warranties. This insurance can be used as a supplement to a negotiated indemnification provision, in which case the insurance can provide additional coverage and protection beyond the negotiated indemnification caps and survival periods. In the alternative, the parties may agree to delete the concept of indemnification in the purchase agreement and list recourse to the representations and warranties insurance as the sole remedy for a breach of the seller's representations and warranties. As one can imagine, this is very attractive to sellers and may be used competitively by buyers seeking an edge in an auction process.

Seller-side representations and warranties insurance is typically used as a backstop to the seller's indemnification obligations under the purchase agreement in situations where the buyer demands indemnification and an escrow from the seller. With such a policy, the insurer will indemnify and pay sellers for any losses they are contractually required to indemnify the buyer for under the purchase agreement. One significant difference between seller-side and buyer-side representations and warranties insurance is that a seller-side policy will not provide coverage for breaches due to the seller's fraud, whereas such breaches are covered in a buyer-side policy. In addition to providing less comprehensive coverage, this policy leaves sellers in the middle and requires them to respond to and deal with post-closing claims from the buyer. Also, the terms of this policy may not completely mirror the terms of the representations and indemnities in the purchase agreement, so there could be a gap in coverage.

As a result, the policy can be beneficial but is likely to be used only where the buyer refuses to accept a buyer-side policy as its sole recourse.


D. Stephen Antion (L) is a partner and **Philip Lang** (R) is an associate at **Katten Muchin Rosenman LLP**. Antion heads the Los Angeles corporate group and represents private equity firms, entrepreneurial businesses and families in a wide range of transactions with an emphasis on mergers and acquisitions, corporate finance, and securities law. Lang represents private equity firms, private and public companies and private investors in a variety of corporate transactions, including mergers and acquisitions, joint ventures, corporate finance, and international transactions.

Structuring an acquisition with a representations and warranties insurance policy can greatly expedite the process by removing the lengthy negotiations of the indemnification and liability provisions. A policy can also be issued very quickly, usually in two to three weeks. As representations and warranties insurance has grown in usage, insurers have become more sensitive to the timing concerns in acquisition transactions and are, in turn, streamlining the insurance underwriting and issuance process.

COVERAGE AND PRICING

Representations and warranties insurance policies typically provide coverage up to a cap of 10 percent to 20 percent of the enterprise value of the target company, with higher coverages structured through multiple insurers. The premiums for representations and warranties insurance policies have decreased through the years and are now generally priced in an amount equal to 2.5 percent to 3.5 percent of the coverage amount. Similar to a "basket" in an indemnification provision, a representations and warranties insurance policy will also include a modest retention amount or deductible, with the insurer only required to pay when losses exceed the deductible.

The coverage period for representations and warranties insurance will generally mirror the survival periods for the representations and warranties in a typical purchase agreement. General representations and warranties have a shorter coverage period of up to two years, while certain fundamental representations and tax representations have a longer coverage period of up to six years. Although the liability of the seller for the representations and warranties in the purchase agreement may not survive the closing, the insurer will continue to cover losses for breaches of the seller's representations and warranties during the coverage period. As the use of representations and warranties insurance has continued to grow and develop, some insurers are now offering, for an increased premium, a coverage period of up to six years for all representations and warranties.

Every representations and warranties insurance policy has certain exclusions from coverage. Typical exclusions include the following:

- Losses arising from facts and circumstances of which the buyer had previous knowledge.
- Items included in the buyer's due diligence reports or listed on the disclosure schedules to the purchase agreement.
- Losses due to the breach of any of the seller's covenants and any post-closing purchase price adjustment.

It is important to note these exclusions may be disadvantageous to the buyer as compared to a traditional negotiated indemnification provision.

> One significant difference between seller-side and buyer-side representations and warranties insurance is that a seller-side policy will not provide coverage for breaches due to the seller's fraud.

CONSIDERATIONS FOR THE BUYER

In determining whether a representations and warranties insurance policy is the right approach, the buyer will need to consider the benefits and disadvantages of the policy in the context of the particular facts and circumstances of the contemplated transaction.

Are there concerns over the ability to collect from the seller?

A representations and warranties insurance policy can provide the buyer comfort and security in situations where the seller could present a credit risk or where there are concerns over the ability to collect for losses directly from the seller.

Is the target company a public company?

A representations and warranties insurance policy can be used in the acquisition of a public company for protection not otherwise available in typical public acquisitions, where individual shareholders do not stand behind the company's representations and warranties post-closing.

Are continuing members of management selling shareholders?

Representations and warranties insurance can ease some of the tension that may arise in a situation where the buyer seeks indemnification claims from former shareholder management members of the target company who are employed by the buyer after the closing.

Does the buyer insist that the seller provide an indemnity?

If the buyer insists that the seller or sellers stand by the representations and warranties and provide indemnification for the buyer, representations and warranties insurance may still provide benefits to the buyer. If the seller will only provide indemnification up to lower-than-desired limits, a representations and warranties policy can bridge any gaps in coverage.

Does the buyer want a longer period of coverage?

With the broad six-year representations and warranties insurance policy now being offered by certain insurers, a buyer could have a longer coverage period than what could be negotiated in an indemnification provision, which is usually one to two years.

Are there any potential significant liabilities known to the buyer?

As discussed above, a representations and warranties insurance policy excludes from coverage losses arising out of facts or circumstances that were known to the insured prior to the closing. In addition, losses arising out of matters that are described in any due diligence reports or disclosed in the disclosure schedules to the purchase agreement are also excluded. For example, in a situation where it is known and disclosed to all parties that there is pending litigation that may result in significant damages, a representations and warranties insurance may not provide any protection. The buyer would need specific line item indemnification of the litigation to ensure it is protected regardless of prior knowledge and disclosure of such matter.

A separate transactional insurance policy could be used together with a representations and warranties insurance policy to provide coverage that would otherwise be excluded, but such transactional insurance policies come at a higher price.

Are there concerns over sharing any diligence reports with the insurer?

As part of the underwriting process, the buyer will need to provide the insurer with copies of all diligence reports, including legal, financial and environmental reports.

Are there concerns about breaches of "fundamental representations" that could result in significant liabilities?

In a typical representations and warranties insurance policy, all claims will be subject to the same maximum cap on coverage and basket or deductible, regardless of the specific representation or warranty breached. In many purchase agreements with indemnification provisions, however, certain fundamental representations of the seller- such as organization, authority and capitalization, and representations relating to taxes- are excluded from the maximum cap and basket. The reasoning behind this is that consequences of breaching such representations may result in significant and irreparable damage to the buyer. Thus, the scope of the coverage may be less than what would be negotiated with a seller.

Does the seller have material post-closing covenants?

While a traditional indemnification provision will usually cover breaches of post-closing covenants, such covenant breaches are excluded from coverage under representations and warranties insurance. In the event a seller breaches a post-closing covenant, such as a non-compete or non-solicit provision, the only remedy for the buyer may be to sue such a seller for breach of contract.

Is the buyer involved in a competitive bidding process?

Given the benefits a representations and warranties insurance policy presents a seller, a buyer can make its bid more appealing to the seller by proposing a "clean break" deal structure that incorporates a representations and warranties insurance policy.

CONSIDERATIONS FOR THE SELLER

For a seller, the use of a representations and warranties insurance policy can be a very attractive way to structure a transaction.

The seller can have a clean exit.

From the seller's perspective, one of the key advantages of representations and warranties insurance is that it provides the confidence of a clean exit without contingent post-closing liabilities or any holdback or escrow of the purchase price. This is particularly true for private equity fund sellers where the absence of an escrow will enhance the fund's IRR by avoiding the delayed receipt of the escrowed proceeds. It may be critical if the fund is at the end of its term and needs to exit and distribute the proceeds to its limited partners.

Avoid issues that arise relating to joint and several liability with multiple sellers.

In an acquisition involving multiple sellers, a key point of contention is whether the sellers are subject to joint and/or several liability. A representations and warranties insurance policy can address the sellers' concerns and protect minority or passive sellers who may have minimal knowledge and/or control of the target company.

Propose a representations and warranties insurance policy from the onset.

Given the significant advantages, a seller may want to incorporate representations and warranties insurance into the proposed deal structure in its marketing materials and bid package when marketing the company to potential buyers. A number of private equity funds are now doing this as a matter of policy.

OTHER TRANSACTIONAL INSURANCE PRODUCTS

As the insurance industry has expanded its transactional insurance products, insurers are now able to offer specific products to address a variety of concerns, including tax, contingent liability, litigation buyout, fraudulent conveyance, successor liability and environmental insurance.

These products can be utilized to cover legacy liability concerns known to the buyer and excluded under a representations and warranties insurance policy. These types of transactional insurance policies may be more expensive than the premium for a representations and warranties insurance policy, though. For example, a tax insurance policy may have a premium of 4 percent to 6 percent of the coverage amount, while a litigation buyout insurance policy may have a premium equal to 10 percent of the coverage amount.

CONCLUSION

Incorporating a representations and warranties insurance policy in an acquisition transaction can be an excellent way to both expedite the process and address the concerns of both parties over the allocation of risk in the event of post-closing breaches. Whether used as a supplement to or a substitute for traditional indemnification provisions, such a policy can be issued quickly and without the protracted negotiations of an indemnity. Plus, it substitutes the uncertainty of future contingent liabilities with a set, one-time premium payment. The buyer has a credit worthy source of recovery for breaches and will deal with an entity that is experienced in processing claims, unlike most sellers. Accordingly, deal participants should carefully consider whether to utilize this insurance product at the outset of their transactions. WJ

FIRREA: The Justice Department's expansive (and expensive) tool of choice

By Allyson B. Baker, Esq., and Andrew Olmem, Esq.
Venable LLP

A series of recent court rulings has effectively expanded the Department of Justice's authority to investigate and prosecute banks for claims related to the financial crisis.

These rulings have broadly interpreted a little-known provision of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 to allow the DOJ to seek millions of dollars in penalties from federally insured financial institutions for violations of criminal fraud statutes. Under Section 951 of FIRREA, codified as 12 U.S.C. § 1833a, the DOJ need only rely on a civil burden of proof to prove criminal fraud, provided that the alleged fraud "affects" a federally insured financial institution.

Although the provision was originally viewed as a measure to protect banks from fraud by third parties, three separate courts have recently construed this "affects" requirement broadly and affirmed that a bank can be both a "victim of" and a "participant in" the predicate fraud that gives rise to a FIRREA claim. As a result, FIRREA has become the DOJ's statute of choice when proceeding against financial institutions. Given the serious consequences of a FIRREA suit, financial institutions should be aware of its unique reach and legal standards.

REUTERS/Chip East

The Justice Department's use of FIRREA suits has been linked closely to its role on the Financial Fraud Task Force, which comprises more than 20 federal agencies, including the SEC and the IRS.

FINANCIAL CRISIS FRAUD FORCE

The DOJ's use of FIRREA suits has been linked closely to its role on the Financial Fraud Task Force. President Barack Obama formed the task force in 2009 in response to the financial crisis. The task force comprises more than 20 federal agencies, including the Department of Justice, the Consumer Financial Protection Bureau, the Securities and Exchange Commission, the Internal Revenue Service, and the banking regulatory agencies and consists of several working groups on areas including consumer protection and mortgages.

A recent press release describes the task force as "the broadest coalition of law enforcement, investigatory and regulatory agencies ever assembled to combat fraud." Although the task force comprises numerous federal agencies, it operates under the leadership and guidance of the Department of Justice, as Attorney General Eric Holder serves as its chair.

Allyson Baker (L), a partner in the Washington office of **Venable LLP**, is a trial attorney and was, until recently, an enforcement attorney with the Consumer Financial Protection Bureau, where she served as lead counsel on one of the first enforcement actions that also resulted in the largest agency settlement to date. Venable partner **Andrew Olmem** (R) just finished up a seven-year tenure as Republican chief counsel and deputy staff director at the Senate Banking Committee. He was lead Senate staff negotiator during the passage of Dodd-Frank and he was involved with the Housing and Economic Recovery Act and the TARP Act.

RELYING ON FIRREA

The DOJ has relied on FIRREA heavily in conjunction with its work on the Financial Fraud Task Force because of the statute's broad reach, lower burden of proof, substantial penalties and long limitations period. Specifically, FIRREA provides that the DOJ may seek civil penalties for violations of 14 different federal criminal laws, including mail and wire fraud statutes, 18 U.S.C. §§ 1341, 1343. Certain of those violations, including the most commonly alleged predicate violations, such as mail and wire fraud, must also affect federally insured financial institutions. *See* 12 U.S.C. § 1833a.

Under FIRREA, however, the DOJ need only prove that there was a violation of one of these 14 predicate criminal offenses "by a preponderance of the evidence," which is a civil evidentiary burden. 12 U.S.C. § 1833a(f). If the DOJ successfully proves a violation of one or more predicate offenses, then under FIRREA, a court can impose a civil penalty that is as much as $1 million for each violation. But in the case of continuing violations a civil money penalty can be imposed that is the lesser of $1 million a day or a total of $5 million. *See* 12 U.S.C. §§ 1833a(b)(1), (2).

However, many of the larger FIRREA cases the DOJ is currently prosecuting against banks alleging mortgage fraud seek penalties well in excess of these numbers, because FIRREA also imposes a penalty if there is a finding that "any person [including any corporation] derives pecuniary gain from the violation," or if the violation results in a loss to a person other than the violator. "[T]he amount of the civil penalty may exceed the amounts [described above] but may not exceed the amount of such gain or loss." 12 U.S.C. § 1833a(b)(3).

NEW POWERS

Furthermore, under FIRREA, the DOJ can gather evidence through formal process in advance of filing a civil action. FIRREA allows the DOJ to issue administrative subpoenas seeking documents and testimony in connection with a civil investigation initiated "in contemplation of a civil proceeding under" FIRREA. 12 U.S.C. § 1833a(g)(1). This investigative authority is akin to the enforcement authority of other agencies like the SEC, the CFPB and the Federal Trade Commission.

In addition, FIRREA has a 10-year limitations period; this allows the DOJ to investigate conduct alleged to have occurred several years earlier during the financial crisis, further enhancing the appeal of FIRREA in the eyes of the DOJ. In recent years, the DOJ has brought numerous FIRREA cases and pursued even more investigations under FIRREA.

> A series of recent court rulings has effectively expanded the Department of Justice's authority to investigate and prosecute banks for claims related to the financial crisis.

The DOJ's current use of FIRREA has, in many ways, strayed from the statute's origins. Congress passed FIRREA in response to the savings and loan crisis of the late 1980s. The statute's legislative history suggests that Congress focused little if any debate on Section 1833a. Rather, the congressional debate indicates that Congress was focused more on expanding authority to bring enforcement actions against individuals and related parties whose fraudulent activities caused the failure of savings and loan institutions.

CONCLUSION: LIMITING FIRREA?

As the DOJ has increased its use of FIRREA suits, courts have increasingly examined the question of whether there are limits on its scope and application. In several high-profile matters pending in the U.S. District Court for the Southern District of New York, banks that are defendants in FIRREA cases have contended that their cases should be dismissed on grounds that the banks could not — as a matter of FIRREA's plain language and intent — engage in self-inflicting conduct. In other words, they could not engage in alleged wrongdoing that "affects" themselves.

The courts, however, have disagreed. On Sept. 24, in *United States v. Wells Fargo Bank*, No. 12-civ-7527, 2013 WL 5312564 (S.D.N.Y. 2013), a case alleging that Wells Fargo engaged in fraudulent mortgage underwriting, the court held that a "financial institution, through its own misconduct, can affect itself within the meaning of FIRREA." This holding builds on an earlier and even more expansive opinion issued by Judge Lewis Kaplan in *United States v. Bank of New York Mellon*, 2013 WL 1749418 (S.D.N.Y. Apr. 24, 2013), and has further validated the DOJ's expansive use of FIRREA and made it the tool of choice for bringing civil fraud cases against banks in the aftermath of the financial crisis. WJ

Shareholder suit against Healthways directors survives dismissal

A shareholder derivative suit accusing a health care cost-management firm's directors of giving the company president too many stock options in violation of its stock incentive plan can proceed in Delaware Chancery Court.

Pfeiffer et al. v. Leedle et al., No. 7831, 2013 WL 5988416 (Del. Ch. Nov. 8, 2013).

In a Nov. 8 opinion, Vice Chancellor Donald F. Parsons held that because plaintiff Milton Pfeiffer had raised reasonable doubts about the independence of Healthways' board of directors, he did not have to bring his complaints to the board's attention before filing suit, as Delaware law usually requires.

The judge also found that the business judgment rule, which normally shields directors from liability for the consequences of their ordinary business discretion, did not apply to Pfeiffer's claims because the board allegedly violated an express and unambiguous provision of the corporate stock plan.

"[W]hen a plaintiff presents particularized factual allegations that indicate that the board clearly violated an unambiguous provision of a stock plan, it is proper to infer that such violation was committed knowingly or intentionally and, therefore, that demand should be excused," Vice Chancellor Parsons wrote, citing *Sanders v. Wang*, 1999 WL 1044880 (Del. Ch. 1999).

Pfeiffer's suit claims breach of fiduciary duty against Healthways' directors and company President Ben Leedle Jr. in connection with 734,000 stock options the board allegedly gave Leedle between 2011 and 2012.

According to the complaint, the board in both years violated the company's stock incentive plan, which prohibits any participant from receiving more than 150,000 shares of stock options or stock appreciation rights in any calendar year.

The suit also alleges unjust enrichment against Leedle and seeks disgorgement of his profits.

The defendants moved to dismiss in November 2012, arguing that Pfeiffer had failed to make a pre-suit demand on the board asking it to take action itself, as Delaware law normally requires. Healthways is a Delaware corporation.

Pfeiffer countered that such a demand would have been futile because the Healthways' board is self-interested rather than disinterested.

Vice Chancellor Parsons applied the two-part test the state Supreme Court articulated in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), for determining whether a pre-suit demand would have been futile.

Under *Aronson*, the plaintiff does not have to make a pre-suit demand if his or her allegations create a reasonable doubt that the directors are disinterested and independent or that their actions were otherwise the product of valid business judgment.

Citing *Sanders*, the judge found that Pfeiffer had raised significant doubts about the applicability of the business judgment rule.

Under *Sanders*, a company's directors cannot claim the protection of the business judgment rule if they departed from clear corporate rules knowingly or intentionally.

If Healthways' directors indeed violated an express an unambiguous provision of the corporate stock plan, they met that standard, Vice Chancellor Parsons said.

Courtesy of Delaware Chancery Court

When the directors are accused of violating an unambiguous corporate stock plan, the plaintiff does not have to make a pre-suit demand on the board, Vice Chancellor Donald F. Parsons said.

Pfeiffer therefore did not have to make a pre-suit demand because he satisfied the second prong of the *Aronson* test, the judge held, declining to dismiss his claims. WJ

Attorneys:

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Defendants: William M. Lafferty and D. McKinley Measley, Morris Nichols Arsht & Tunnell, Wilmington; Wallace W. Dietz, Bass Berry & Sims, Nashville, Tenn.

Related Court Document:
Opinion: 2013 WL 5988416

Child labor stain can't cross Atlantic to taint Hershey board, court master says

Even if West African farms that supply cocoa to Hershey Co. abuse child laborers, there's no proof that wrongdoing infects the chocolatier's board of directors, according to a master's report advising the Delaware Chancery Court to dismiss a shareholder's records inspection action.

Louisiana Municipal Police Employees' Retirement System v. Hershey Co., No. 7996, master's final report filed (Del. Ch. Nov. 8, 2013).

Abigail LeGrow, one of the masters who act as fact finders to help Chancery Court judges resolve issues and speed up litigation, said in her final report Nov. 8 she found no "reasonably conceivable set of circumstances" in which the suit could link the board with the abuse.

Without that link, a Hershey shareholder cannot show it has more than mere suspicion on which to base its claim that the directors breached their duty to the company by allegedly exposing it to liability in an international child labor abuse scandal, the report said.

Therefore, the investor, a municipal retirement fund, has no credible basis for a demand to search corporate records for evidence of wrongdoing by the board, and the records access demand should be dismissed, LeGrow recommended.

The Louisiana Municipal Police Employees' Retirement System filed a books-and-records action asserting its right as a shareholder of a Delaware-chartered company to inspect board minutes and correspondence for evidence of wrongdoing. Hershey's directors said the lawsuit was without foundation and moved to dismiss it.

In a preliminary report released Aug. 16 on whether LMPERS' suit had enough substance to survive a motion to dismiss, LeGrow said the suit was not based on "credible evidence" of wrongdoing, as required by the law of Delaware, Hershey's state of incorporation.

Without evidence that the Hershey directors knew of specific cocoa purchases that tainted their products with child labor abuses, LMPERS' basis for a records request "melts away," she wrote in the preliminary report.

However, LMPERS filed a reply brief Oct. 25 in support of its motion for reconsideration on the draft report's conclusions before LeGrow submitted her final report.

REUTERS/Kwasi Kpodo

A family of cocoa growers helps with drying cocoa beans in Akim Akooko, Ghana. In a lawsuit a shareholder of Hershey Co. said the company directors are hiding behind middlemen in making cocoa purchases from West African farmers it knew were abusing child laborers.

The books-and-records suit is often an opening-round action to gather ammunition for a follow-up breach-of-duty lawsuit against a board of directors for alleged wrongdoing.

In its reply brief, the pension fund argued to no avail that the preliminary report allowed Hershey's directors to hide behind middlemen in making cocoa purchases from farmers it knew were abusing child laborers.

LMPERS said Hershey's board knows what it needs to do to make its chocolate abuse-free but does not want to take the steps necessary to do that.

LeGrow's final report says the plaintiff's reasoning is essentially guilt by association.

No one alleges that Hershey violated the law or is under investigation for its business dealings in the West African cocoa industry, the report says.

LeGrow notes that even if Hershey has not gone as far as it could to enforce a code of conduct for cocoa suppliers, an industry agreement it signed "does not require that a company take particular, or even any, action to address illegal labor within its supply chain."

"LMPERS' philosophical disagreements with the effectiveness of Hershey's supplier code of conduct do not amount to credible evidence," the final report says.

Since the Chancery Court usually endorses the recommendations of masters' final report, this shareholder action — which generated numerous headlines about corporate social responsibility and the ethics of dealing with abusive cocoa plantations — will likely die in its infancy. WJ

Attorneys:
Plaintiff: Michael J. Barry and Justin K. Victor, Grant & Eisenhofer, Wilmington, Del.

Defendants: Srinivas Raju and Robert L. Burns, Richards, Layton & Finger, Wilmington

Related Court Document:
Reply brief in support of exceptions:
2013 WL 5823686

See Document Section B (P. 42) for the reply brief.

DEBT SECURITIES

Delaware justices seek debt-security opinion from New York's high court

A lawsuit against a credit-default-swap underwriter, its officers and directors, and its largest equity holder must await guidance from New York's highest court, the Delaware Supreme Court has decided.

Quadrant Structured Products Co. Ltd. v. Vertin et al., No. 338, 2012, 2013 WL 5962813 (Del. Nov. 7, 2013).

The Delaware Supreme Court will await the New York Court of Appeals' answer to certified questions it has sent before ruling on Quadrant Structured Products' appeal of a Chancery Court opinion dismissing the complaint.

The New York high court must interpret a no-action clause in documents that are central to Quadrant's case, the Delaware Supreme Court found.

The clause, which New York state law governs, identifies the circumstances under which Quadrant can sue Athilon Capital Corp., its corporate affiliates and its executives.

Quadrant obtained an ownership interest in Athilon debt securities in 2011, the opinion says.

According to the Delaware Supreme Court's opinion, until the 2008 financial crisis, Athilon's business was underwriting credit default swaps, a kind of financial insurance policy for debt securities. Its corporate documents limited its business to underwriting these swaps.

In the years before the crisis, Athilon underwrote more than $50 billion in credit default swaps. The company's leverage ratio on the swaps reached a high point of 506-to-1, meaning a 0.2 percent loss on its swaps could put the company out of business, according to the Delaware high court's opinion.

Athilon began to experience problems during the financial crisis when it lost its investment-grade credit rating and had to pay millions of dollars to swap counterparties. In 2010 the company entered a permanent "runoff" mode: It could not contract new business and could only pay off previous swaps.

The same year, investment firm EBF & Associates acquired 100 percent of Athilon's equity and put in place its own board of directors, according to the state court's opinion. EBF also bought a majority of the Athilon debt securities, which were trading at a fraction of their original value.

Quadrant sued in the Delaware Chancery Court, accusing EBF, through the Athilon board, of embarking on a risky business strategy that might benefit junior note holders like EBF in the short term but which harmed Quadrant as a senior note holder.

That is irresponsible and self-serving, Quadrant said, arguing that Athilon should be protecting its senior note holders by preserving its value for an orderly liquidation in 2014.

Athilon moved to dismiss Quadrant's complaint, claiming the investor could not overcome the no-action clause in the note agreements.

The Chancery Court agreed, dismissing the suit. Quadrant appealed the decision to the state Supreme Court.

Instead of deciding the motion in its Nov. 7 opinion, Delaware's high court found that New York law governs the note agreements and sent certified questions to the New York Court of Appeals asking it to determine whether the no-action clause bars Quadrant's litigation. WJ

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Related Court Document:
Opinion: 2013 WL 5962813

Shareholder suit: Mindspeed board failed to get best price

A shareholder of semiconductor manufacturer Mindspeed Technologies has filed a class action in Delaware seeking to halt a merger with M/A-Com Technology Solutions that she says ignores Mindspeed's potential for future growth and the significant synergies MACOM will realize.

Pogal v. Mindspeed Technologies Inc. et al., No. 9076, complaint filed (Del. Ch. Nov. 12, 2013).

Lead plaintiff Beatrice Pogal also claims in her Nov. 12 Chancery Court complaint that the merger agreement announced Nov. 5 includes unreasonable deal-protection devices that effectively bar Mindspeed from seeking a better offer.

According to the lawsuit, MACOM, a leading provider of high-performance analog semiconductor solutions for wireless and wired applications, would purchase all outstanding shares of Mindspeed at $5.05 per share in a deal valued at about $270 million.

But Pogal says the merger undervalues Mindspeed, which is poised to reap financial rewards after years of work driving industry innovations, including advanced processing for long-term-evolution mobile networks.

Though the company saw some setbacks in the current fiscal year, the suit says, Mindspeed has continued to bring a stream of new innovations to the market. For instance, in September the company introduced the industry's lowest-power and smallest-footprint CDR device, as well as a new laser drive that allows for transmitting error-free broadcast video over longer distances, according to Pogal.

While the $5.05-per-share offer is 66 percent higher than Mindspeed's Nov. 4 closing price of $3.04, the complaint notes that Mindspeed shares closed at $5.23 last February and $6.87 per share in January 2012.

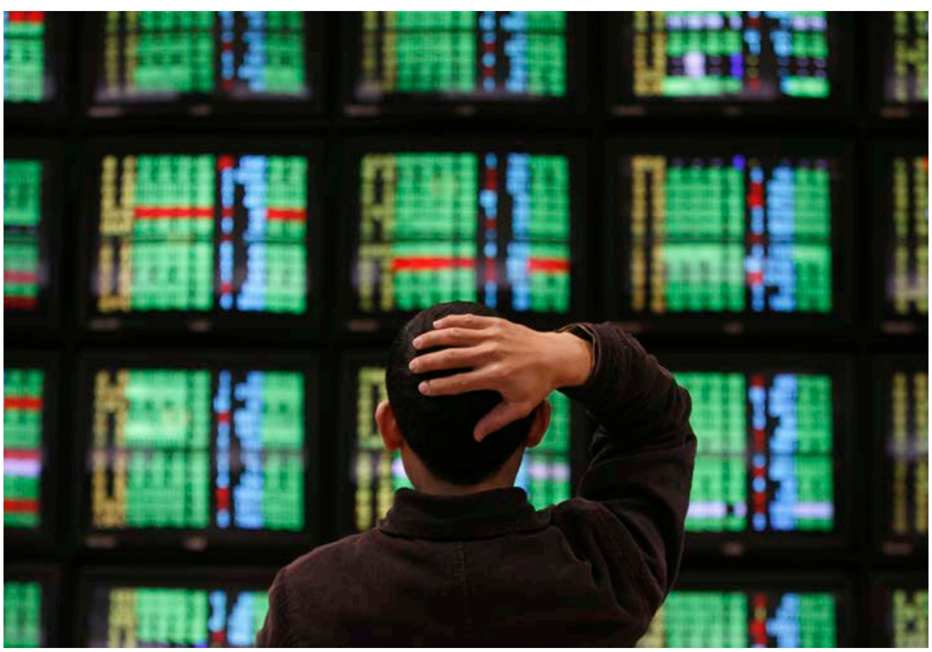
"Mindspeed's recent financial setbacks and consequent drop in share price do not properly indicate the company's strong past and future financial values," the suit says.

The deal also fails to take into account everything the buyer would walk away with, according to Pogal. While MACOM has a strong U.S. presence, most of Mindspeed's revenue comes from the Asia–Pacific region, the complaint says, and that customer footprint would presumably transfer with the merger, significantly expanding MACOM's business.

The agreement also prohibits Mindspeed from seeking any additional bidders and would allow MACOM to match any unsolicited bids that might materialize. Given MACOM's advantage over competitors, Pogal says, it is unlikely any other bids will come in.

Moreover, should Mindspeed walk away, the company would have to pay a $9.5 million termination fee to MACOM. That clause essentially requires any competing bidder to place a high, up-front premium on its offer, the suit says.

"Mindspeed's recent financial setbacks and consequent drop in share price do not properly indicate the company's strong past and future financial values," the suit says.



REUTERS/Nicky Loh

Pogal claims breach of fiduciary duties by eight Mindspeed board members, including Chairman Dwight W. Decker, who she says failed to find stockholders the best possible share price.

She also alleges aiding and abetting against Mindspeed, MACOM and a subsidiary, Micro Merger Sub Inc.

The suit seeks class certification, a court order blocking the merger, damages, costs and fees. WJ

Attorneys:
Plaintiff: Ryan M. Ernst, O'Kelly, Ernst & Bielli, Wilmington, Del.

Related Court Document:
Complaint: 2013 WL 6003138

MERGER CHALLENGE

$2.6 billion merger a steal for Salix, shareholder suits say

Six dissident shareholders of specialty drug maker Santarus Inc. have filed virtually identical class-action complaints asking the Delaware Chancery Court to halt a $2.6 billion merger with Salix Pharmaceuticals that they claim does not adequately compensate stockholders.

Rodriguez v. Santarus Inc. et al., No. 9074, complaint filed (Del. Ch. Nov. 12, 2013).

Clark v. Santarus Inc., No. 9075, complaint filed (Del. Ch. Nov. 12, 2013).

Grignon v. Santarus Inc., No. 9092, complaint filed (Del. Ch. Nov. 15, 2013).

Khalil v. Santarus Inc., No. 9093, complaint filed (Del. Ch. Nov. 15, 2013).

King v. Santarus Inc., No. 9094, complaint filed (Del. Ch. Nov. 15, 2013).

Korhonen v. Santarus Inc., No. 9095, complaint filed (Del. Ch. Nov. 15, 2013).

The suits, filed between Nov. 12 and Nov. 15, say Santarus has put up impressive financial results in the past year, and they argue that the proposed sale price of $32 a share cuts shareholders out of the company's future earnings.

The merger also ignores the significant synergies Salix is expected to realize in the deal and includes preclusive measures intended to deter any competing offers, the plaintiffs in all six suits claim.

Santarus announced the deal Nov. 7. The company simultaneously declared that third-quarter revenues for 2013 were up 81 percent over 2012, with net income rising to $30.3 million from $9 million the previous year.

Cash and cash equivalents were also up to $168.7 million as of Sept. 30 — an increase of $74 million over the $94.7 million Santarus posted in December 2012, according to the lawsuits.

Moreover, Santarus is currently focused on five commercial products, with two others in the later stages of development, the suits claim, which could make the merger extremely lucrative for Salix. Salix CEO Carolyn Logan has allegedly said the acquisition would be "transformative, both commercially and financially."

The proposed merger also includes provisions that make it difficult for Santarus to get a better deal, according to the complaints. Under the agreement, Santarus allegedly cannot solicit other offers and must communicate any unsolicited bids to Salix, which would then have the chance to match.

Should Santarus decide to walk away from the deal, it would have to pay Salix an $80 million termination fee, according to the lawsuits. Salix has also entered into support agreements with several Santarus board members, who together own about 12 percent of all outstanding shares and have pledged to vote against any other proposals, the plaintiffs claim.

The complaints allege breach of fiduciary duties by eight Santarus board members, including Chairman David F. Hale. They also accuse Santarus and Salix of aiding and abetting that breach.

The suits seek class certification, a court order blocking the merger, damages, costs and fees. WJ

Attorneys:
Plaintiffs: Seth D. Rigrodsky, Brian D. Long and Gina M. Serra, Rigrodsky & Long, Wilmington, Del.

Related Court Documents:
Rodriguez complaint: 2013 WL 6003134
Clark complaint: 2013 WL 6047741
Grignon complaint: 2013 WL 6094881
King complaint: 2013 WL 6061295
Korhonen complaint: 2013 WL 6094888

Delaware judge OKs attorney fees award in Quest buyout dispute

By Brett Goncher, Esq., Senior Content Writer, Westlaw Daily Briefing

Quest Software Inc. shareholders can recover $1 million in attorney fees for their challenge to a proposed merger with another software company because it helped spur Quest to accept a better offer from Dell Inc., a Delaware judge has ruled.

In re Quest Software Inc. Shareholders Litigation, No. 7357, 2013 WL 5978900 (Del. Ch. Nov. 12, 2013).

Although the lawsuit became moot when Quest found a better deal, there was a close enough connection between the litigation and the resulting corporate benefit, Vice Chancellor Sam Glasscock III of the Delaware Chancery Court said in a written opinion.

He rejected the Quest board of directors' argument that the suit had no impact on the company's eventual agreement to merge with Dell, explaining that "bald denial" cannot defeat a presumption that the plaintiffs' action compelled them to accept a better offer.

$283 MILLION CORPORATE BENEFIT

The dispute stemmed from Quest's proposed merger agreement in March 2012 with Insight Holdings Corp. that would have netted shareholders $23 per share and included a 60-day "go-shop" period where the company could solicit other potential takeover bids.

During the go-shop period, Quest shareholders initiated a consolidated lawsuit asserting the deal undervalued the company and that Quest's CEO and chairman had engaged in self-dealing because he owned an interest in Insight, according to the judge's opinion.

After a month of negotiations, Quest accepted a $28-per-share offer from Dell to acquire all of Quest's outstanding stock in a deal that resulted in $283 million more than the proposed Insight buyout, the opinion says.

After their suit was dismissed as moot, plaintiffs' co-lead counsel, including law firm Grant & Eisenhofer PA, requested an attorney fee award of $2.8 million.

'RAPTORIOUS AND UNBLINKING' EYES IN OVERSIGHT

The vice chancellor explained that Delaware's "corporate benefit" doctrine allows attorney fee awards in mooted cases if the plaintiff shows its suit was meritorious when filed, the defendants took beneficial action before a judicial resolution was achieved and the resulting benefit has a causal connection to the lawsuit.

In addition, a plaintiff is entitled to a rebuttable presumption that a corporate benefit resulted from its mooted lawsuit, he said.

The judge found the shareholders' suit was meritorious when filed and would have survived a motion to dismiss because their allegations illustrated a merger process with a company associated with a Quest insider.

He rejected the defendants' argument that the suit had no impact on the go-shop period that was already underway and the eventual bid from Dell.

"The record makes it clear that the board was well aware of the eyes, raptorious and unblinking in oversight, of the plaintiffs' counsel, and responded accordingly," the judge said.

The judge reasoned that the suit contributed 5 percent to the $283 million corporate benefit and calculated that plaintiffs' counsel was entitled to an award of roughly 7.5 percent of the benefit, or $1 million.

Plaintiffs' counsel billed more than 2,000 hours to the case, resulting in a fee of about $441 per hour, he said, noting the award was adjusted for the overlap among work performed on five separate complaints that were eventually consolidated. WJ

Related Court Document:
Opinion: 2013 WL 5978900

Delaware judge: Don't sue in Delaware to enforce forum clauses

By Alison Frankel

With Chancellor Strine's ruling in *Boilermakers v. Chevron* entrenched, at least for now, as Delaware precedent, Davis Polk asked, is there any reason why businesses shouldn't rush to adopt forum-selection provisions? *Boilermakers Local 154 Ret. Fund et al. v. Chevron Corp. et al.*, No. 7220; *IClub Inv. P'ship v. FedEx Corp. et al.*, No. 7238, 73 A.3d 934 (Del. Ch. June 25, 2013). According to the firm, about 120 corporations, mostly in Delaware, have done just that.

But Davis Polk also said there are a couple of reasons to wait. For one thing, shareholders may look askance at forum selection provisions, and could even try to extract revenge against board members who push for them. And for another, it's not clear that judges in jurisdictions outside of Delaware will obey the law according to Leo Strine.

"The non-Delaware judge considering the motion may be influenced, but will not be bound, by the *Chevron* decision," the Davis Polk post said. "We may imagine, and some have confidently predicted, that over time a body of law will develop upholding these provisions under the internal affairs doctrine. But that day has not yet arrived, and in the meantime companies will have to fund some level of litigation to defend their position. These companies may, like Chevron and FedEx, have the satisfaction of having moved the law in a positive direction, but others may be happy to have the trailblazers reap the honor."

Vice Chancellor Travis Laster of Delaware Chancery Court raised an obstacle for forum-selection trailblazers in a ruling from the bench Nov. 5 in *Edgen Group v. Genoud*, No. 9055, *bench ruling issued* (Del. Ch. Nov. 5, 2013), a case in which Edgen was trying to enforce a provision in its corporate charter that requires shareholders to litigate claims in Delaware. According to Vice Chancellor Laster, companies with forum-selection clauses shouldn't expect Delaware judges to block their colleagues in other states from hearing shareholder cases, at least until the corporations have asked judges outside of Delaware to enforce the provisions and dismiss shareholder suits.

Vice Chancellor Travis Laster of Delaware Chancery Court raised an obstacle for forum-selection trailblazers in a ruling from the bench Nov. 5 in *Edgen Group v. Genoud*.

"When I review the *Chevron* decision," Vice Chancellor Laster wrote, "it is seemingly apparent on the face of that decision that Chancellor Strine contemplated, at least for purposes of his ruling in that case, that the forum selection provision would be considered in the first instance by the other court."

The judge declined to grant Edgen an anti-suit injunction to block a shareholder suit in Louisiana, even though Edgen's lawyers (from Morris James and Dechert) warned that the case could potentially interfere with Sumitomo Corp.'s $12-per-share offer for the drilling equipment company — and even though Vice Chancellor Laster called the underlying shareholder claim "exceedingly weak" and castigated plaintiffs' lawyers at Robbins Geller Rudman & Dowd for "unsatisfying and, dare I say, pathetic representational contortions" seemingly designed to preserve an argument that Delaware doesn't have personal jurisdiction over the shareholder who sued in Louisiana.

The Delaware Supreme Court made clear in its decision last spring dismissing a derivative suit against Allergan's board that it expects Chancery Court to respect rulings by sister state and federal courts under the Full Faith and Credit Clause of the U.S. Constitution. *Pyott et al. v. La. Mun. Police Employees' Ret. Sys.et al.*, No. 380, 2012, 2013 WL 1364695 (Del. Apr. 4, 2013).

Vice Chancellor Laster's decision in the *Edgen* case shows that Chancery took to heart the state Supreme Court's admonitions about intrastate comity, even when corporations have specified Delaware as their forum of choice.

For Edgen, Vice Chancellor Laster's ruling means that it must attempt to win the dismissal of the Louisiana case before it can get help from Chancery Court. That suit was filed by a Canadian shareholder named Jason Genoud after Edgen announced in October that it had agreed to Sumitomo's $12-per-share offer. The offer represents a 55 percent premium over Edgen's trading price and treats Edgen's controlling shareholders no differently from minority owners, but Genoud nevertheless sued the board for breach of fiduciary duty in state court in Baton Rouge, where the company is headquartered.

In a Nov. 6 letter to Vice Chancellor Laster, Genoud counsel Randall Baron of Robbins Geller explained that the shareholder wanted to challenge Edgen's forum-selection provision, which was "unilaterally adopted" in an amendment to offering documents in Edgen's IPO in April 2012.

"We believed that the civil law system in Louisiana would allow the court to assess the validity of the provision under Louisiana contract law without undue reliance on the Delaware precedent in *Boilermakers* that we

Alison Frankel updates her blog, "On the Case," multiple times throughout each day on WestlawNext Practitioner Insights. A founding editor of Litigation Daily, she has covered big-ticket litigation for more than 20 years. Frankel's work has appeared in The New York Times, Newsday, The American Lawyer and several other national publications. She is also the author of "Double Eagle: The Epic Story of the World's Most Valuable Coin."

do not believe should be followed outside of Delaware," Baron wrote.

Edgen sued Genoud in Delaware, seeking an injunction to bar the Louisiana case from moving forward. Unless Vice Chancellor Laster enforced Edgen's forum-selection clause, the company argued, it risked irreparable harm if the Louisiana court enjoined the Sumitomo deal. That injunction, Edgen said, could even come before a decision on the company's motion to dismiss Genoud's case under its forum selection clause.

"Common sense suggests that there would be some sequence in Louisiana that would have our forum motion decided prior to the injunction motion, but there is no guarantee as to sequence," Edgen counsel Joseph Slights of Morris James told Vice Chancellor Laster. "And if this transaction is enjoined in Louisiana — we don't think it should be, but if it is, it's too late for us to really seek to invoke our exclusive forum provision at that point."

Vice Chancellor Laster was sympathetic, especially because he was so skeptical about Genoud's claims. "This case really exemplifies the interforum dynamics that have allowed plaintiff's counsel to extract settlements in M&A litigation and that have generated truly absurdly high rates of litigation challenging transactions," he said. "It also demonstrates why corporations have seen fit to respond with forum selection provisions in an effort to reduce the ability of plaintiff's counsel to extract rents from what is really a market externality."

The vice chancellor was also notably irritated that Robbins Geller insisted it did not represent Genoud in the Delaware case, although it is handling the Louisiana case for him. Genoud had refused to accept service of Edgen's case, and Vice Chancellor Laster implied that Robbins Geller made a tactical decision to contest the Delaware court's jurisdiction over the shareholder. Vice Chancellor Laster called that strategy "quite disappointing behavior from a firm that otherwise has done a great deal to build up reputational capital and credibility with the Delaware courts."

The Louisiana suit, he said, clearly violated Edgen's forum-selection clause. But Vice Chancellor Laster concluded that precedent on forum-selection clauses, whether in bylaws or corporate charters, is simply too undeveloped to grant anti-suit injunctions as a first recourse for Edgen.

"It may be that in the right case an anti-suit injunction is appropriate, but I do think that *Chevron* suggests that primacy should be given in the first instance to the non-contractually selected forum," he said.

Wachtell, Lipton, Rosen & Katz, which has championed forum-selection clauses, chose to regard Vice Chancellor Laster's decision as a glass half-full, emphasizing the judge's finding that Edgen's charter provision is presumptively valid. But in a phone interview, Baron of Robbins Geller told me Vice Chancellor Laster appropriately concluded that it's up to non-Delaware courts to decide how much deference to give to forum selection clauses.

For Edgen, the judge's ruling means that it must attempt to win the dismissal of the Louisiana case before it can get help from Chancery Court.

"We know the bylaws are valid in Delaware," he said. "The next question is to what extent each jurisdiction is obligated to give full faith and credit to those holdings."

In an email, Baron also responded to Vice Chancellor Laster's comments about his firm's strategy. "Vice Chancellor Laster is one of the best jurists in the country and clearly an expert in Delaware law," he said. "I understand his desire to have Delaware courts hear issues on Delaware law. That said, our client was legally entitled to file and have the forum selection clause issue decided in the principle place of business of Edgen. And our client is legally entitled to assure that Defendants properly served him and had personal jurisdiction over him before subjecting him to orders in the forum of their choice."

Edgen counsel at Morris James didn't respond to my phone messages. WJ

NEWS IN BRIEF

DEVELOPER ASKS COURT TO KICK FACEBOOK'S COUNTERCLAIMS

After Kickflip Inc. sued Facebook for allegedly monopolizing the virtual currency market for online gaming, the social networking site lodged vague counterclaims against the software developer that the Delaware federal court should toss, according to a Nov. 12 filing. Facebook answered Kickflip's antitrust suit in October, asserting that the developer, which does business as Gambit, committed fraud and induced others to breach contracts around four years ago. These counterclaims, however, have a three-year statute of limitations; therefore, they are time-barred, Kickflip says in its dismissal motion. Additionally, Facebook fails to specify any fraud that Kickflip allegedly committed or describe any improper conduct that the software company did with the intent to induce third parties to breach any contracts with Facebook, the developer adds. Therefore, the court should toss the counterclaims because they have no merit and fail to meet the required pleading standards.

Kickflip Inc. v. Facebook Inc., No. 12-1369, motion to dismiss filed (D. Del. Nov. 12, 2013).

WARRANT NEEDED FOR GPS SEARCH, 3RD CIRCUIT RULES

Law enforcement officers needed to obtain a warrant before affixing a GPS tracker to a car whose owner they suspected was involved in a wave of pharmacy burglaries in three states, a federal appellate panel in Philadelphia has ruled. The GPS tracker installed on Harry Katzin's car allowed for targeted monitoring of his movements and continuous police presence and therefore implicated Fourth Amendment privacy concerns, the 3rd U.S. Circuit Court of Appeals ruled in a 2-1 opinion. Even if law enforcement officials had probable cause to suspect Katzin was involved in the burglaries, it had no reason to avoid the U.S. Constitution's requirement to obtain a warrant before installing the GPS tracker and conducting the search, the court said. The majority therefore affirmed a Pennsylvania federal judge's decision to suppress the evidence police obtained from Katzin's vehicle in the criminal trial against him and his brothers. The dissenter, Circuit Judge Franklin S. Van Antwerpen, said suppression was not the appropriate remedy.

United States v. Katzin et al., No. 12-2548, 2013 WL 5716367 (3d Cir. Oct. 22, 2013).

Related Court Document:
Opinion: 2013 WL 5716367

3RD CIRCUIT: LACK OF EXPOSURE HISTORY DOOMS MDL ASBESTOS PLAINTIFFS

Plaintiffs in four asbestos lawsuits who failed to provide defendants with exposure histories correctly had their cases dismissed with prejudice, the 3rd U.S. Circuit Court of Appeals has affirmed. The plaintiffs were "in seeming denial" that a federal judge would take this "drastic" step if they failed to follow the requirement of showing medical diagnoses based on their occupational exposure history, the panel said in an Oct. 17 opinion. Instead of complying with the order issued by Judge Eduardo C. Robreno of the U.S. District Court for the Eastern District of Pennsylvania, who oversees the asbestos multidistrict litigation, these plaintiffs argued that the judge's interpretation of his own order was incorrect, the appeals panel said. The panel said Federal Rule of Civil Procedure 41(b) gives the District Court the right under these circumstances to order a dismissal that "operates as an adjudication on the merits."

In re Asbestos Products Liability Litigation, Nos. 12-3822, 12-3823, 12-3824 and 12-3825, 2013 WL 5651289 (3d Cir. Oct. 17, 2013).

Related Court Document:
Opinion: 2013 WL 5651289

CEO removal

CONTINUED FROM PAGE 1

was outmaneuvered in his bid to oust all his enemies on the board and win back his CEO job, the opinion said.

In a subsequent Nov. 7 decision, the vice chancellor acknowledged that the void-or-voidable issue was a proper issue for the state high court to consider on appeal, but he refused to impose a boardroom truce or litigation stay while the justices considered the case. *Klaassen v. Allegro Dev. Corp. et al.* No. 8626, 2013 WL 5951762 (Del. Ch. Nov. 7, 2013).

CORPORATE LAW SORE SPOT

The interpretation of the void-or-voidable issue has been a recurring problem for the Chancery Court in deciding challenges to the validity of corporate actions, said professor **Lawrence Hamermesh**, who heads the corporate law department at the **Widener University School of Law**.

"The *Klaassen* case highlights a recurring sore spot in Delaware's corporate law doctrine: namely, distinguishing between corporate actions that are void and actions that are merely voidable, and determining what difference that makes," he said in emailed comments.

"While voidable actions can be cured after the fact, void actions are thought to be irredeemable, beyond repair and indefensible on equitable grounds," Hamermesh said.

That made all the difference in this battle. If Klaassen had been given no notice at all of the board meeting at which he was removed (rather than just no notice of the removal vote itself), he would have had a much easier time establishing that the board's action was simply void.

In that case, the strength of Klaassen's attack on that vote would not have mattered, Hamermesh pointed out.

The battle for control of the Dallas-based developer of energy trading and risk management software stemmed from the dissatisfaction among board members over the company's failure to perform financially as Klaassen allegedly promised when they made significant capital investments.

Klaassen filed this declaratory judgment action in Delaware, where Allegro is incorporated, seeking a court ruling that he was the rightful CEO and that he had validly removed his rival board members.

> The interpretation of the void-or-voidable issue has been a recurring problem for Delaware courts in deciding challenges to the validity of corporate actions, Widener University law professor Lawrence Hamermesh said.

JUST 'VOIDABLE'

In his Oct. 11 opinion, Vice Chancellor Laster found that Klaassen did not get proper notice of the board's plan for a vote to remove him as CEO. He said, however, that type of failure of notice is not the same as if he got no notice of the meeting at all, which could have rendered the board's action void rather than simply voidable.

The judge found that based on past cases, Klaassen did not prove his removal was void or show valid reasons for contesting a voidable action.

The vice chancellor had to "wrestle mightily" with the fine points of this void-vs.-voidable issue in both opinions, Hamermesh said.

In his appeal brief, Klaassen argued that he had been excluded from the board meetings in which the directors decided to remove him and drew up paperwork to that effect, so the action was clearly void and need not be challenged.

However, Hamermesh said Klaassen has a tough row to hoe on appeal.

'NOT CRYSTALLINE'

"I think the vice chancellor got it right: the claim of lack of notice was premised on the idea that Klaassen was equitably entitled to notice because he was also a majority stockholder and capable of throwing out the board before they got a chance to fire him as CEO," he said.

"The vice chancellor, however, recognized that the case law on the subject of voidness and voidability is anything but crystalline, and it's an area that the Delaware Supreme Court could usefully try to clarify." WJ

Attorneys:
Plaintiff: R. Judson Scaggs Jr., Kevin M. Coen and Frank R. Martin, Morris, Nichols, Arsht & Tunnell, Wilmington, Del.; George P. Young and Kelli Larsen Walter, Haynes & Boone, Fort Worth, Texas

Defendants: Peter J. Walsh Jr. and Ryan T. Costa, Potter Anderson & Corroon, Wilmington; Van H. Beckwith, Jonathan R. Mureen and Jordan H. Flournoy, Baker Botts LLP, Dallas

Related Court Documents:
October opinion: 2013 WL 5739680

November opinion: 2013 WL 5951762

See Document Section A (P. 21) for the October opinion.

CHANCERY COURT CASES

CAPTION	CASE NO.	NATURE OF ACTION	DATE	ATTORNEY
Knowles v. Advanced Photonix	9064	Director election	Nov. 6, 2013	Kurt Hayman
Mehta v. Tellabs	9066	Breach of duty	Nov. 6, 2013	Seth Rigrodsky
Treeck v. Brazil Fast Food	9068	Breach of duty	Nov. 7, 2013	Seth Rigrodsy
Merlin Partners v. ORHI	9069	Appraisal	Nov. 7, 2013	Ronald Brown Jr.
Charlot v. Brazil Fast Food	9071	Breach of duty	Nov. 7, 2013	Ryan Ernst
Robitaille v. Goergen	9072	Breach of duty	Nov. 8, 2013	Seth Rigrodsky
Rodriguez v. Santarus	9074	Breach of duty	Nov. 12, 2013	Seth Rigrodsky
Clark v. Santarus	9075	Breach of duty	Nov. 12, 2013	Seth Rigrodsky
Pogal v. Mindspeed	9076	Breach of duty	Nov. 12, 2013	Ryan Ernst
Pfeiffer v. Activision	9077	Books & records	Nov. 12, 2013	David Jenkins
Ruckett v. Nucor	9078	Attorney fees	Nov. 13, 2013	Joel Friedlander
Hudson Bay v. Dole	9079	Appraisal	Nov. 13, 2013	Stuart Grant
Durand v. Decker	9080	Breach of duty	Nov. 14, 2013	Carmella Keener
Merion Capital v. Dole	9081	Appraisal	Nov. 14, 2013	Steven Margolin
Emerging Acquisition v. Sommer	9082	Indemnification	Nov. 14, 2013	Catherine Gaul
Backus v. Healthwarehouse	9083	Advancement	Nov. 14, 2013	Jon Abramczyk
Potter v. Santarus	9084	Breach of duty	Nov. 14, 2013	Ryan Ernst
RATL v. Brazil Fast Food	9086	Breach of duty	Nov. 15, 2013	Edmond Johnson
Vandrevala v. Hirco	9088	Advancement	Nov. 15, 2013	Edmond Johnson
Johns Manville v. CCG Group	9089	Breach of merger pact	Nov. 15, 2013	Kurt Heyman
Christie v. Crowder	9090	Misappropriation	Nov. 15, 2013	Christopher Curtin
Feiner v. VitaSpring	9091	Books & records	Nov. 15, 2013	Leslie Spoltore
Grignon v. Santarus	9092	Breach of duty	Nov. 15, 2013	Seth Rigrodsky
Khalil v. Santarus	9093	Breach of duty	Nov. 15, 2013	Seth Rigrodsky
King v. Santarus	9094	Breach of duty	Nov. 15, 2013	Seth Rigrodsky
Korhonen v. Santarus	9095	Breach of duty	Nov. 15, 2013	Seth Rigrodsky
Tassa v. Mindspeed	9096	Breach of duty	Nov. 15, 2013	Seth Rigrodsky
Zwang v. Autoliv	9098	Breach of duty	Nov. 18, 2013	Blake Bennett

CASE AND DOCUMENT INDEX