

# Securities Litigation Alert

## Court of Chancery's *Volcano* Decision Extends *Corwin* Rule to Two-Step Mergers

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The Delaware Court of Chancery's June 30, 2016 decision in *In re Volcano Corporation Stockholder Litigation*, C.A. No. 10485-VCMR, extends to a two-step merger under Section 251(h) of the Delaware General Corporation Law the rule set forth in *Corwin v. KKR Financial Holdings, LLC*, 125 A.3d 304 (Del. 2015), that when a majority of a company's disinterested, fully informed, and uncoerced stockholders approve a merger with an acquirer that is not the company's controlling stockholder, the business judgment rule applies and insulates the transaction from all challenges other than waste.

*Volcano* is the latest installment in what has become a recurring litigation topic over the past two years—the effect of fully informed, uncoerced, and disinterested stockholder approval on the standard of review. In addition to *Corwin*, recent cases addressing this topic include *In re KKR Financial Holdings LLC Shareholder Litigation*, 101 A.3d 980 (Del. Ch. 2014), *In re Zale Corp. Stockholders Litigation*, 2015 WL 5853693 (Del. Ch. Oct. 1, 2015), *In re Zale Corp. Stockholders Litigation*, 2015 WL 6551418 (Del. Ch. Oct. 29, 2015), and *Singh v. Attenborough*, 2016 WL 2765312 (Del. May 6, 2016) (ORDER).

### Background

On December 15, 2014, the Board of Directors of Volcano Corporation ("Volcano") approved a cash-out merger with Philips Holding USA Inc. pursuant to which Volcano's stockholders received \$18 per share in cash (the "Merger"). The Merger was consummated as a two-step transaction under Section 251(h) of the Delaware General Corporation Law ("DGCL"). The first-step tender offer commenced on December 30, 2014, and closed on February 17, 2015, with 89.1% of Volcano's outstanding shares having tendered. The second-step merger was then consummated.

Shortly thereafter, Volcano stockholders brought suit, alleging that the members of Volcano's board of directors breached their fiduciary duties of care and loyalty by not running a better process and not obtaining a better price, and that the board's financial advisor, Goldman, Sachs & Co. ("Goldman Sachs") aided and abetted the alleged breaches of fiduciary duties.

Defendants moved to dismiss the complaint on the basis that, among other things, the fully-informed, uncoerced decision by the majority of Volcano's disinterested stockholders to tender their shares insulated the transaction from all challenges other than waste (a claim the plaintiffs did not assert).

## The Court of Chancery's Decision

The Opinion, authored by Vice Chancellor Montgomery-Reeves, is the first to directly address whether the rule set forth in *Corwin* applies to a two-step transaction under Section 251(h). In holding that it does, the Court examined the procedures involved in effectuating a merger under Section 251(h) and the policy rationale of *Corwin*.

First, the Court examined the requirements of Section 251(h) and determined that the target board's role in negotiating a two-step merger under Section 251(h) is substantially similar to its role in negotiating a merger subject to a stockholder vote and that the board has the same disclosure obligations as it would in any other communication with stockholders. Second, the Court held that there is nothing inherently coercive about a two-step transaction effectuated pursuant to Section 251(h) because, among other things, the tender offer must be for all of the target's outstanding shares, the second-step merger must be for the same consideration as that offered in the tender offer, and appraisal rights are available. Third, the Court analyzed the policy considerations underlying the Delaware Supreme Court's holding in *Corwin* and concluded that the rationale—namely judicial deference to stockholders who exercise their “free and informed chance to decide on the economic merits of a transaction”—applied equally to a two-step transaction under Section 251(h). Finally, the Court looked to case law equating stockholder acceptance of a tender offer with a stockholder vote in favor of a merger, and concluded that the common law weighed in favor of extending *Corwin* to two-step mergers.

The Court therefore determined that the effect of tendering shares by fully informed, disinterested, uncoerced stockholders representing a majority of a corporation's outstanding shares in a two-step merger under Section 251(h) is to insulate the transaction from all challenges other than waste. Because plaintiffs had not alleged that the tendering stockholders were interested or coerced, the Court solely addressed plaintiffs' contention that stockholders had not been fully apprised of the extent of Goldman Sachs' alleged conflict of interest, which allegedly motivated Goldman Sachs

to consummate a deal before certain options expired. The Court rejected plaintiffs' argument, holding that the defendants had satisfied their burden of demonstrating that Volcano's stockholders were fully informed when deciding whether to tender their shares because the existence of the alleged conflict was adequately disclosed. Accordingly, and because plaintiffs failed to allege waste, the Court held that the complaint failed to state a claim for breach of fiduciary duty against the Volcano board. In so concluding, the Court also echoed the Supreme Court's statement in *Singh* that it is logically difficult to imagine a circumstance in which a plaintiff could prove a waste claim in the face of a fully-informed, uncoerced majority vote.

The Court also dismissed plaintiffs' aiding and abetting claim against Goldman Sachs on the grounds that plaintiffs had failed to state a claim for an underlying breach of fiduciary duty and that even if plaintiffs had stated a claim for breach of fiduciary duty, the allegations against Goldman Sachs were insufficient to establish the requisite scienter.

## Key Takeaways

In 2014, amendments to Section 251(h) lowered the threshold for effectuating the back-end “short form” merger from 90% to a simple majority. Directors of companies considering such a transaction can take comfort in knowing that the Court of Chancery will afford directors the same level of deference when disinterested, uncoerced, and fully informed stockholders tender their shares as part of a two-step merger as directors are afforded when stockholders vote to approve a single-step merger. Consistent with *Corwin* and other recent decisions, the *Volcano* decision highlights the importance of robust disclosure in promoting deal certainty and enabling early dismissal of post-closing deal litigation. This decision should also further assuage the concerns of financial advisors following the Supreme Court's holding in *RBC Capital Markets v. Jervis*, 129 A.3d 816 (Del. 2015), as it, like the Supreme Court's holding in *Singh*, reiterates the high level of culpability required for aiding and abetting claims against financial advisors to survive dismissal.

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