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Delaware Court of Chancery Dismisses Post-Closing Disclosure Claims for Failure to Show Disloyalty or Bad Faith

In *Nguyen* v. *Barrett*, the Delaware Court of Chancery dismissed post-closing claims that the board acted disloyally or in bad faith by failing to make the challenged disclosures. The Court also reiterated Delaware's strong preference that plaintiffs assert and pursue disclosure claims pre-closing so there is an opportunity to remedy these concerns prior to the stockholder vote.

The plaintiff challenged disclosures made in connection with the acquisition of Millennial by AOL, Inc. Prior to closing, the plaintiff sought a preliminary injunction of the merger based on Millennial's failure to disclose its financial advisor's unlevered, after-tax free cash flow ("UFCF") projections. Even though banker-prepared projections typically need not be disclosed under Delaware law, the plaintiff argued that Millennial should disclose the UFCF projections because they were based on components provided by Millennial management. After review of the proxy and precedent, however, the Court of Chancery concluded that management did not prepare the UFCF projections and denied plaintiff's request for a preliminary injunction. The Delaware Supreme Court denied plaintiff's request for an interlocutory appeal of such holding.

After the merger closed, the plaintiff elected to continue pursuing just two disclosure claims: one challenging the failure to disclose the UFCF projections and another challenging Millennial's proxy disclosures relating to its financial advisor's contingent fee arrangement.

In granting the defendants' motion to dismiss, the Court made several holdings that serve as helpful reminders when litigating disclosure claims.

- *Where a board is exculpated for duty of care claims pursuant to 8 Del. C. § 102(b)(7), a plaintiff pleading post-closing disclosure claims must allege facts making it reasonably conceivable that there has been a non-exculpated breach of fiduciary duty by the board.*

  - The Millennial board was exculpated for duty of care claims under 8 *Del. C.* § 102(b)(7). Therefore, to sustain a breach of fiduciary duty claim against the Millennial board, the plaintiff had to demonstrate a breach of the board's duty of loyalty. This required a showing that a majority of the board was not disinterested or independent, or was otherwise disloyal or acted in bad faith in failing to make the alleged material disclosures.

  - The only conflict or bad faith action that the plaintiff alleged with regard to a majority of the directors, however, was that they were motivated to enter into the transaction with AOL to accelerate the vesting of their options to avoid unspecified "risk." The Court found that this allegation did not demonstrate board disloyalty with regard to either disclosure claim, and that it is "well-settled that where the interests of the directors and stockholders are aligned, as here, the accelerated vesting of shares in a merger does not create a conflict of interest."

- *The Court reiterated that the preferred method for pursuing disclosure claims is pre-closing while there is still an opportunity to remedy such concerns prior to a stockholder vote.*

  - The Court noted that, because of the judicial interest in ensuring that stockholder votes are fully informed, it was more likely to find that plaintiffs had waived the right to pursue any disclosure claim post-closing that had been pled but that plaintiffs had failed to pursue pre-closing.

  - Here, the plaintiff had pled the claim relating to disclosure of the financial advisor's contingent fee arrangement prior to closing, but then failed to pursue the claim. The Court ultimately did not reach a conclusion as to whether the plaintiff had waived the claim, as it determined that the claim failed on its merits.

- *Disclosure that a "substantial portion" of a financial advisor's fee was contingent on completion of a merger is generally sufficient, absent some indication that the fee is exorbitant, unusual or otherwise improper.*

  - The Court distinguished *In re Atheros Communications, Inc.*, where the company's disclosure that its advisor's fee was "substantially contingent" on the deal's closing was found to be insufficient. In *Atheros*, nearly all (98%) of the advisor's fee was contingent, which the *Atheros* court found to "exceed[] both common practice and common understanding of what constitutes 'substantial,'" and "may fairly raise questions about the financial advisor's objectivity and self-interest." Thus, the Court in *Nguyen* noted that *Atheros* does not undermine the body of case law holding that disclosure that a "substantial portion" of a fee is contingent is sufficient under a more standard set of facts.

  - Here, the plaintiff did not allege any facts indicating that the fee at issue fell outside the general rule, and therefore, the Court found the disclosure that a "substantial portion" of the advisor's fee was contingent to be sufficient.

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