December 4, 2017

Delaware Court of Chancery Dismisses Fiduciary Duty Claims Despite Inapplicability of *Corwin*

Recently in *van der Fluit* v. *Yates*, the Delaware Court of Chancery dismissed fiduciary duty claims brought against the board of Opower, Inc. in connection with the company's acquisition by Oracle Corporation, even though the court concluded that the defendants were not entitled to the irrebuttable presumptions of the business judgment rule under *Corwin* due to the shareholder tender offer not being fully informed. Applying the familiar *Revlon* standard post-closing, the court concluded that the board nevertheless acted reasonably and did not commit a non-exculpated breach of fiduciary duty in connection with the transaction, despite, among other things, allegations that that the two-week market check was rushed.

Background

Oracle and Opower, a provider of cloud-based software for the utility industry, engaged in negotiations regarding a possible transaction on two separate occasions in 2014, both before and after Opower's April 2014 IPO. In both instances, negotiations ceased before reaching an agreement. In March 2016, Oracle submitted a bid to acquire Opower for $9.00 to $10.00 per share. Following Oracle's bid, Opower's financial advisor conducted a two-week market check, which included 14 potential strategic buyers. Four potential buyers entered into confidentiality agreements, but each eventually withdrew from the process.

The Opower board rejected Oracle's initial bid and sought an increase to $11.00 per share. Oracle revised its offer to $10.30 per share, and thereafter, Opower granted Oracle the right to exclusive negotiations. The parties settled on $10.30 per share with the following terms: (i) a $20 million termination fee and up to $5 million in expense reimbursement; (ii) the right for certain members of Opower management to convert a portion of their unvested Opower options into comparable unvested Oracle options; (iii) a waiver by each of the Opower CEO and president of 10% of their portion of the merger compensations unless and until each had worked one full year at Oracle; and (iv) an agreement by management and certain other stockholders to tender their shares to Oracle. The transaction was structured as a two-step merger under Section 251(h) of the Delaware General Corporation Law ("DGCL"), with the Opower stockholders "overwhelmingly tender[ing]" their shares to Oracle.

Analysis

In the opinion by Vice Chancellor Montgomery-Reeves granting the defendants' motion to dismiss, the court made the following key holdings:

- *Due to material omissions in the offer disclosures, the business judgment rule is not irrebuttably invoked per* Corwin. In *Corwin* v. *KKR Financial Holdings LLC* (discussed here), the Delaware Supreme Court held that in situations where entire fairness review does not automatically apply (*e.g.*, a merger without a controlling stockholder that extracted personal benefits), a transaction that is approved by a fully-informed, uncoerced vote of disinterested stockholders will irrebuttably invoke the business judgment rule absent a showing of waste. The rule from Corwin was extended to first step tender offers under Section 251(h) in *In re Volcano Corp. Stockholder Litigation* (discussed here).

  - The court concluded that no control group existed. The tender and support agreements relating to the merger and an earlier investor rights agreement were insufficient to establish an alleged control group among Opower's co-founders and early stage venture capital investors. According to the court, the investor rights agreement (which was signed pre-IPO and related to certain registration and information rights) did not create a control group because it contained no voting, decision-making or other agreements relating to the merger with Oracle. With regard to the tender and support agreements in which various Opower stockholders committed to tender their shares to Oracle, the court found that the plaintiff failed to show that these agreements evidenced a control group rather than simply a "concurrence of self-interest among certain stockholders." Moreover, the court questioned why the plaintiff included certain early stage venture capital investors in the alleged control group, but did not include numerous other stockholder signatories to these agreements, suggesting that the venture capital investors were selected by plaintiff in an attempt to increase the stock ownership of the alleged control group. Additionally, plaintiff did not plead sufficient facts to show an alleged control group only among the co-founders (management members who together only held 30% of Opower's stock at the time of the transaction). The alleged facts did not demonstrate meaningful connections between the co-founders besides their concurrent interests or that they exercised control over Opower as a group.

  - The court also concluded that *Corwin* was inapplicable to the transaction because stockholders were not fully informed. The tender offer documents failed to disclose that the Opower representatives negotiating the deal included the company's CEO and the president, each of whom received post-transaction employment and the conversion of unvested Opower options into unvested Oracle options. This amounted to a material omission because stockholders are entitled to know when fiduciaries' interests deviate from their own interests.

- *The plaintiff failed to state non-exculpated claims against the board, however; thus the claims were dismissed.* Opower's certificate of incorporation contained a provision under Section 102(b)(7) of the DGCL that exculpates the board from monetary liability for duty of care violations. Therefore, without the benefit of *Corwin* dismissal, the plaintiff was required to show a non-exculpated breach of the duty of loyalty.

- The court concluded that all breaches of the duty of loyalty alleged by defendants were unsupported by the facts, including conclusory allegations that the director defendants favored Oracle in the bidding process, that the directors sought to maximize their own pre-IPO investments rather than stockholder value, and that the termination fee was unreasonably high.[1]

- The court also rejected plaintiff's claims that the board unreasonably rushed the two-week market check to favor Oracle, and therefore breached its duty of loyalty. The court distinguished the case from its decision in *In re Answers Corp.*, which held a two-week market check to be unreasonably rushed. In that case, the plaintiff made non-conclusory allegations that the market check was unreasonably rushed, citing various warnings from the company's financial advisor, including that it was not a "real" market check. Here, the court found that the plaintiff did not make any such non-conclusory allegations.

- Finally, the plaintiff failed to sufficiently state a duty of loyalty claim through allegations of conflicts of interests that tainted a majority of the board. The court first concluded that the board did not breach its *Revlon* duties (which duties "are only a specific application of directors' traditional fiduciary duties of care and loyalty in the context of a control transaction"). Second, the court concluded that the board did not act outside of its business judgment, holding that the plaintiff failed to allege facts showing that interested directors comprised a majority of the board, dominated the other directors, or failed to inform the other directors of their alleged conflicts.

- Notably, the court's application of *Revlon* to the post-closing damages claims here arguably is inconsistent with reasoning in *Corwin* and its line of cases that enhanced reasonableness standards of review, such as *Revlon* and *Unocal*, are better suited to the preliminary injunction context, perhaps suggesting *Revlon* should no longer apply to post-closing, damages-only claims. In a footnote, the court acknowledged this potential deviation, but noted that it need not decide the applicable standard of review due its conclusion that the plaintiff failed to state a claim under either enhanced scrutiny or the business judgment rule.

- *Plaintiff failed to state an aiding and abetting claim against Oracle.* Plaintiff failed to allege Oracle's knowing participation in any alleged breach of fiduciary duty by the board; therefore the court dismissed aiding and abetting claims against it.

* * *

[1] Plaintiff argued that the termination fee, which he calculated to be 4.699% of the transaction value, was unacceptably high. The court found, however, that this termination fee was based on plaintiff's miscalculation of the total deal value and his failure to consider that, per the merger agreement, any expense reimbursement would be credited against any obligation to pay the termination fee. Accordingly, the court found that the termination fee was capped at 3.62% of the transaction value, which it found to be "a number in line with Delaware case law."

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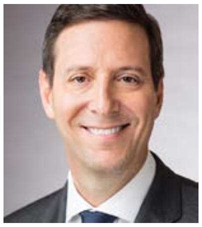

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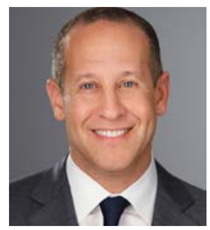

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