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Delaware Court of Chancery Finds It "Reasonably Conceivable" That Two Minority Stockholders Form Control Group

Recently in *In re Hansen Medical, Inc. Stockholders Litigation*, the Delaware Court of Chancery declined to grant defendants' motion to dismiss, finding that plaintiff stockholders had sufficiently pled a "reasonably conceivable" claim that two minority stockholders of Hansen Medical, Inc. constituted a control group (the "Controller Defendants") and extracted a non-ratable benefit from the company's acquisition by Auris Surgical Robotics, Inc., in which case the entire fairness standard would apply to the transaction. Vice Chancellor Montgomery-Reeves based her holding on allegations of a lengthy history of investment cooperation and coordination by the Controller Defendants, their entering into voting agreements and proxies with Auris, and their decision to roll over their shares in the transaction, which constituted a non-ratable benefit unavailable to other stockholders.

Background

In 2016, Auris acquired Hansen for $4.00 per share. In connection with the merger, certain key stockholders, including the Controller Defendants, negotiated directly, and entered into voting agreements and proxies, with Auris and rolled over their shares. The Controller Defendants (the two constituent groups of which held 34% and 31% of Hansen's stock prior to the merger) had a 21-year history of investment cooperation and coordination. Plaintiffs brought claims for breach of fiduciary duty against the Controller Defendants and two directors of the company, who also served as CEO and interim CFO, respectively. Additionally, plaintiffs asserted a claim against Auris for aiding and abetting the alleged fiduciary duty breaches.

Analysis

In its opinion addressing the defendants' motion to dismiss for failure to state a claim, the court determined that plaintiffs had stated a reasonably conceivable claim that the merger should at this stage be considered under the entire fairness standard of review because it was a conflicted transaction involving controllers.

- *It was reasonably conceivable that the Controller Defendants were a control group due to their history of cooperation and coordination in investing.* The court found that plaintiffs made well-pled factual allegations regarding the Controller Defendants' history of investment cooperation and coordination, including that they invested together in at least seven different companies, having declared themselves to the SEC as a "group" in connection with their investment in one such company. The Controller Defendants invested as the sole participants in a private placement by

Hansen that made them the largest stockholders of the company and participated in two later private placements by Hansen in which they were defined together as the "Principal Purchasers," including having rights (*e.g.*, to determine the closing date and to amend the agreement) that were unavailable to other investors. Additionally, they both entered into proxies and a voting agreement with Auris in connection with the merger.

- *Plaintiffs made well-pled allegations that the Controller Defendants received a non-ratable benefit unavailable to the minority, namely the opportunity to roll over their shares.* Therefore, plaintiffs stated a reasonably conceivable claim that the merger should at this stage be considered under the entire fairness standard because it was a conflicted transaction involving controllers.

  Notwithstanding the foregoing, the court acknowledged that the Controller Defendants, who argued that they should not be considered a control group, "offer[ed] reasonable explanations for some of the connections" between them, and that "one might even argue that they offer a more compelling version of events" and may prevail at a later stage in the litigation. However, because the motion-to-dismiss standard is "minimal," the court was required to deny the motion unless plaintiffs could not recover under any "reasonably conceivable set of circumstances."

Additionally, the court made the following key holdings:

- *Plaintiff stated reasonably conceivable non-exculpated claims against the director defendants based on allegations of material misstatements in the proxy statement relating to the merger*. In particular, the proxy statement included three valuation ranges calculated using discounted cash flow analyses that were based on three separate management projections. One range was well above the transaction price and the other ranges were at or below the transaction price. While the proxy represented that all three sets of projections reflected "management's best available estimates and judgments regarding [Hansen's] future financial performance," deposition testimony from one of the directors (who prepared the projections as interim CFO) indicated that the projections yielding the highest valuation range were the most likely scenario, and that the other two sets of projections were included only to "keep the CFO from 'looking stupid.'" The court concluded that it was reasonably conceivable that the director/interim CFO knew that the proxy was materially misleading and that plaintiffs therefore stated a non-exculpated claim against him. Additionally, the court determined that plaintiffs stated a non-exculpated claim against the director who signed the proxy in his capacity as CEO, as it was reasonably conceivable that he was aware of material misstatements in the proxy.

- *Plaintiffs did not state a reasonably conceivable claim against Auris for aiding and abetting a breach of fiduciary duty.* Plaintiffs did not plead facts to show that Auris knowingly participated in any purported breach by the other defendants, and therefore, the court dismissed the claim against it.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Matthew W. Abbott
Partner
New York Office
+1-212-373-3402
Email

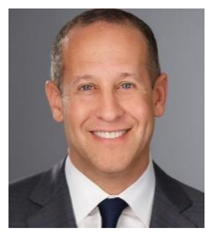
Scott A. Barshay
Partner
New York Office
+1-212-373-3040
Email

Ariel J. Deckelbaum
Partner
New York Office
+1-212-373-3546
Email

Ross A. Fieldston
Partner
New York Office
+1-212-373-3075
Email

Justin G. Hamill
Partner
New York Office
+1-212-373-3189
Email

Stephen P. Lamb
Partner
Wilmington Office
+1-302-655-4411
Email



Jeffrey D. Marell
Partner
New York Office
+1-212-373-3105
Email

Taurie M. Zeitzer
Partner
New York Office
+1-212-373-3353
Email

Counsel Frances F. Mi and legal consultant Cara Grisin Fay contributed to this memorandum.

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