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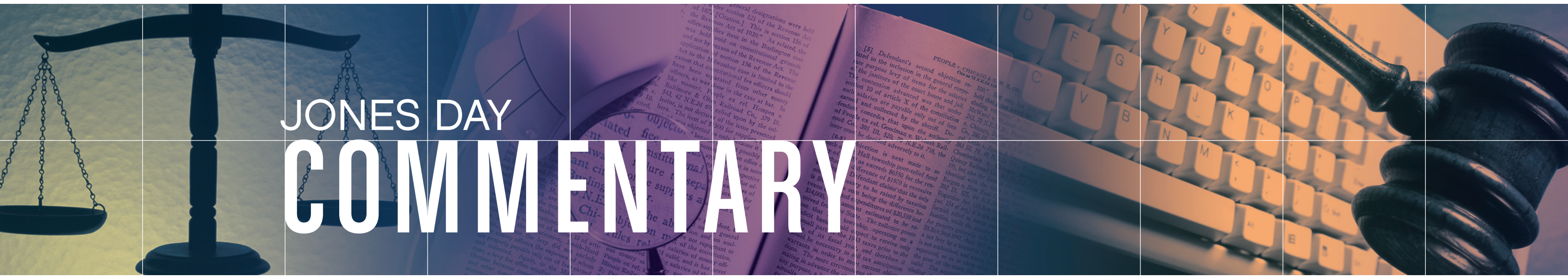

CONFLICTS OF INTEREST CONTINUE TO DOMINATE IN RECENT M&A LITIGATION

In re Delphi Financial Group Shareholder Litigation is the second Delaware decision in as many weeks eschewing injunctive relief in favor of post-deal remedies in single-bidder transactions. In *Delphi*, Vice Chancellor Glasscock declined to enjoin the sale of Delphi Financial Group, Inc. ("Delphi") to Tokio Marine Holdings, Inc. ("TMH"), even in the face of an allegedly suspect process, because the harm would be "largely, if not completely, remediable by damages." *In re Delphi Fin. Group S'holder Litig.*, C.A. No. 7144-VCG (Del. Ch. Mar. 6, 2012).

BACKGROUND

Delphi founder and CEO Robert Rosenkranz took Delphi, an insurance holding company, public in 1990. After the initial public offering, two classes of stock were created. Class A stock represented one vote per share, and Class B stock represented 10 votes per share. Rosenkranz and his affiliates own some Class A stock and all of the Class B stock, meaning that Rosenkranz is the controlling stockholder of Delphi despite owning only 12.9 percent of the outstanding shares. A voting agreement caps Rosenkranz's voting power at 49.9 percent, and a Delphi charter provision prohibits Class B stockholders from receiving a premium not shared by Class A stockholders in the event of a merger.

TMH approached Delphi in 2011 about a possible acquisition. Rosenkranz negotiated with TMH on behalf of Delphi. As a result of these negotiations, TMH offered $45 per share for all of the Class A and Class B shares. Rosenkranz then informed the board that he was unwilling to vote in favor of the deal without obtaining a premium for his Class B shares. The board created a Special Committee to evaluate any differential consideration, and after a negotiation process, TMH and Delphi ultimately agreed that Class A stockholders would receive approximately $45 per share and Class B stockholders would receive approximately $54 per share. Each price represented a substantial premium over the market price. The merger agreement required approval of the deal by a majority of disinterested Class A stockholders and approval of an amendment to the Delphi charter exempting the transaction from the requirement that Class A and Class B stock receive equal merger consideration.

POST-CLOSING DAMAGES, NOT AN INJUNCTION, AS THE MORE APPROPRIATE REMEDY

Vice Chancellor Glasscock was most concerned by Rosenkranz's alleged violation of his duties to Class A stockholders "in negotiating for disparate consideration and only agreeing to support the merger if he received it." It troubled the court that Rosenkranz and other Delphi officers allegedly worked together "to formulate a plan, not to maximize, via the [m]erger, return to the stockholders, for whom they are fiduciaries, but to maximize return to Rosenkranz himself."

Additionally, Vice Chancellor Glasscock concluded that Rosenkranz already had "sold his right to a control premium to the Class A stockholders via the Charter" to retain voting control after the initial public offering and that allowing Rosenkranz to receive a control premium in the deal with TMH would render the charter provision prohibiting disparate merger consideration "illusory." The Delphi charter could be amended, and "clear of any impending sale," Rosenkranz could have negotiated for his control premium back. Absent that amendment, however, the court was critical of Rosenkranz's attempt to sell "the same control premium again in connection with [the] [m]erger."

Vice Chancellor Glasscock concluded that the plaintiffs had demonstrated a likelihood of success on the merits, but he refused to grant a preliminary injunction, in light of the large premium the TMH deal would provide to Delphi stockholders and the absence of any other potential purchasers of the company. The vice chancellor further concluded that "[m]uch of the alleged misconduct of which the Plaintiffs complain is remediable by readily ascertainable damages," and he stated that he would be inclined to order disgorgement of any improper consideration received by Rosenkranz.

CONCLUSION

As mentioned above, *Delphi* is the second recent Delaware decision declining to halt an allegedly flawed single-bidder process pursuant to which shareholders stand to receive a significant premium over market price and post-closing damages are available. *See In re El Paso Corp. S'holder Litig.*, C.A. No. 6949-CS (Del. Ch. Feb. 29, 2012). Like the *El Paso* court, Vice Chancellor Glasscock scrutinized the alleged actions of the company's CEO and found them to be "troubling." Also like *El Paso*, the court nevertheless declined to grant the injunction, concluding that "money damages can largely remedy the threatened harm." Another example of a Delaware court turning to post-deal damages as a remedy for a flawed deal process is Vice Chancellor Laster's 2009 decision allowing NACCO Industries, Inc., a losing bidder, to seek expectation damages for the target's no-shop and prompt notice breaches. *See NACCO Indus., Inc. v. Applica Inc.*, 997 A.2d 1 (Del. Ch. 2009).

Delphi further evidences the preference of Delaware courts for stockholders to make their own determination as to whether to approve a proposed transaction and collect a premium for their shares or whether to voice their disapproval through a negative vote. In certain situations, such as *Delphi*, the stockholders may feel pressure to vote affirmatively for an attractive transaction to collect the substantial premium, despite any imperfections in the process or the existence of potential conflicts of interest (and, in fact, the *El Paso* shareholders did just that, with 95 percent of the shares that voted on the merger approving the deal). In recent decisions, such as *Delphi* and *El Paso*, Delaware courts have balanced those competing interests by indicating the availability of post-closing damages. As a result, even successful bidders may face substantial liability for problematic transactions and, accordingly, may seek conditions precluding closings in the face of a *Delphi* or *El Paso* finding.

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