

Delaware Courts Expand **Corwin** Line of Cases

On March 7, 2017, Vice Chancellor Laster of the Delaware Court of Chancery dismissed the action *In re Columbia Pipeline Group, Inc.*, C.A. No. 12152-VCL. Stockholders of Columbia Pipeline Group, Inc. (“CPG”) claimed that CPG’s directors, Chief Executive Officer and Chief Financial Officer (collectively, the “defendants”) structured the sale of CPG to TransCanada Corp. (“TRP”) in a particular manner to enrich themselves at the expense of the stockholders. Based on the seminal decision *In re KKR Fin. Hldgs. LLC S’holder Litig.*, 101 A.3d 980 (Del. Ch. 2014), *aff’d sub nom. Corwin v. KKR Fin. Hldgs. LLC*, 125 A. 3rd 304 (Del. 2015), Vice Chancellor Laster, applying the business judgment rule, dismissed the action because plaintiffs had not pled a viable disclosure claim.

Related Capabilities

- Corporate Governance & Compliance

Relevant Facts in *Columbia*

CPG had been a wholly owned subsidiary of NiSource, Inc. Prospective buyers had expressed their interest in acquiring CPG from NiSource. Although the defendants had change-of-control benefits with NiSource, the sale of CPG directly by NiSource would not trigger such benefits because CPG comprised a relatively small percentage of NiSource’s assets.

Instead of selling CPG, NiSource spun off CPG on July 1, 2015. Two senior officers and a number of CPG’s directors stayed with CPG. Their change-of-control benefits were transferred to CPG, on a dollar-for-dollar basis, even though CPG was a considerably smaller company than NiSource.

Approximately nine months later, on March 17, 2016, TRP and CPG entered into a merger agreement (the “Merger Agreement”) pursuant to which TRP would acquire CPG. CPG’s board, with the help of two financial advisors (Goldman, Sachs & Co. and Lazard Freres & Co. LLC), approved the transaction and recommended it to CPG’s stockholders. In connection with soliciting stockholder approval of the transaction, CPG filed its preliminary proxy statement on April 8, 2016 and its definitive proxy statement on

May 17, 2017 (the “Proxy Statement”). Finally, on June 22, 2016, CPG’s stockholders, representing more than 95% of the total outstanding shares of CPG, voted in favor of the merger, which closed on July 1, 2016.

Corwin: Securing the Business Judgment Rule Standard with a Stockholder Vote

Vice Chancellor Laster held that the *Corwin* analysis governed this action. In *Corwin*, the Delaware Supreme Court made clear that, where a transaction that is not subject to the entire fairness standard of review has been approved by a majority of the disinterested stockholders in a fully informed, uncoerced vote, the business judgment rule applies and insulates the transaction from all other attacks, other than on the grounds of waste. Since the *Corwin* decision, Delaware courts have further reinforced and expanded *Corwin* in a number of respects, including as follows:

- **Waste:** The Delaware Supreme Court further explained the *Corwin* test as follows: “When the business judgment rule standard of review is invoked because of a vote, dismissal is typically the result. That is because the vestigial waste exception has long had little real-world relevance, because it has been understood that stockholders would be unlikely to approve a transaction that is wasteful.” (*Singh v. Attenborough*, 137 A.3d at 152 (Del. 2016) (ORDER))
- **Entire Fairness:** In response to the plaintiffs’ argument that transactions subject to the entire fairness standard for any reason cannot be cleansed under *Corwin*, the court stated that the only transactions subject to entire fairness review that cannot be cleansed by proper stockholder approval are conflicted transactions with controlling stockholders (*Larkin v. Shah*, 2016 WL 4485447 (Del. Ch. Aug. 25, 2016)).
- **Revlon:** In response to the plaintiffs’ argument that the board’s conduct of the sale process and decision to approve the merger calls for enhanced scrutiny under *Revlon*, the Court cited *Corwin* in stating that *Revlon* was “primarily designed to give stockholders and the Court of Chancery the tool of injunctive relief to address important M&A decisions in real time, before closing,” and was not a tool “designed with post-closing money damages claims in mind.” Thus, the business judgment rule applied. (*In re Solera Hldgs. S’holder Litig.*, 2017 WL 57839, at *7-8 (Del. Ch. Jan. 5, 2017)).
- **Burden of Proof:** Chancellor Bouchard held that, in addressing the question of who has the *burden to plead* disclosure deficiencies in the first place to test whether the vote was fully-informed in *Solera*, it made more sense for the plaintiff challenging the transaction approval to first identify a deficiency in the operative disclosure document. Then, the burden would fall on the defendants to show that the alleged deficiency fails as a matter of law in order to secure the cleansing effect of the vote.
- **Tender Offers:** In rejecting the plaintiffs’ post-closing damages claim arising from a transaction, the Court found that a medium-form merger under Section 251(h) of the Delaware General Corporation Law that results from a sufficient percentage of shares being tendered by stockholders in a tender offer has the same cleansing effect as a stockholder vote in favor of that merger. Since the stockholders were fully informed as to all material facts regarding the merger at the time of the tender offer, the plaintiffs were subject to the irrebutable presumption of the business judgment rule. (*In re Volcano Corp. S’holder Litig.*, 143 A.3d 727, 741 (Del. Ch. 2016)).

Thus, the *Corwin* line of cases has, in transactions without a controlling stockholder, established a high threshold for plaintiffs seeking a post-closing damages claim. In

response to a disclosure deficiency identified by a plaintiff, if the defendant establishes the sufficiency of disclosure made to stockholders for the purposes of obtaining such stockholders' ratification of the transaction, then the approved transaction can only be challenged on the basis of waste. Such a claim is very unlikely to succeed because, in the view of the Delaware Courts, fully informed, uncoerced stockholders would not likely vote in favor of a wasteful transaction.

Application of *Corwin* in *Columbia*

In *Columbia*, plaintiffs alleged that the defendants breached their duty of loyalty by engineering a sale of CPG following its spinoff as part of a self-interested plan to obtain lucrative change-in-control benefits that would not have been realized had NiSource directly sold CPG to a buyer. In other words, the defendants had planned all along to sell CPG, but wanted to do so in a manner that triggered the payment of their change-of-control benefits, which diverted consideration away from the public stockholders. Vice Chancellor Laster found that the allegations in support of the plaintiffs' theory were sufficiently detailed to state a pleadings-stage claim for breach of loyalty against the defendants.

In applying *Corwin*, Vice Chancellor Laster stated that, if the stockholders approved the conflict-of-interest after full disclosure, the business judgment rule would apply. Thus, the plaintiffs claimed that the Proxy Statement failed to disclose the defendant's self-interest in engineering the spinoff to generate change-of-control benefits. Thus, the key issue was whether the CPG stockholders were fully informed of the alleged conflict-of-interest prior to their vote approving the transaction.

Were the CPG Stockholders Fully Informed?

Citing prior Delaware cases, Vice Chancellor Laster stated that the duty of disclosure demands that fiduciaries disclose facts, but not legal conclusions as to the inferences to be drawn from those facts. He stated that "when a proxy statement describes the facts that create differing incentives for fiduciaries, it need not explain how those differing incentives could produce a self-interested outcome."

The Proxy Statement disclosed CPG's preparation for potential acquisition offers, engagement of two financial advisors, comprehensive review of its strategic alternatives and process leading up to the Merger Agreement. Moreover, the basic terms of the defendants' compensation packages were publicly available and the Proxy Statement disclosed that the total value of change-of-control benefits that two of the defendants earned through the merger was higher than would have been received if NiSource simply sold CPG without the spinoff. Essentially, the plaintiffs argued that the defendants were obligated to disclose that they acted for selfish and self-interested reasons. Vice Chancellor Laster noted that there was no requirement for "the defendants to aver that they acted for that purpose," which if true, "would be to force them to engage in self-flagellation." He concluded that "[t]he material facts were disclosed. That is all Delaware law requires."

Financial Advisor Conflict

The *Columbia* plaintiffs also alleged that the Proxy Statement failed to disclose that Goldman had a conflicting financial interest because Goldman and its affiliates collectively owned approximately \$28.4 million in TRP stock. Vice Chancellor Laster noted that Goldman and its affiliates also owned approximately \$50.4 million of CPG stock and approximately \$30.1 million of Columbia Pipeline Partners limited partnership units. Therefore, he concluded that one could not infer from these positions that Goldman's interests favored TRP.

While Vice Chancellor Laster noted that there was no obligation to disclose these positions, because they were available in Goldman's publicly filed Form 13F, *in dicta* he noted that he would favor a disclosure regime that requires a proxy statement for a merger to disclose the positions that the sell-side investment advisors and its affiliates held in the sell-side entity, the acquirer and any other participant in the sale process. In his view, it would be preferable to have these matters set out in a table in the proxy statement, rather than expecting stockholders to uncover the information in other lengthy filings.

Conclusion

Since the plaintiffs had not pled a viable disclosure claim, and the stockholder vote was therefore fully informed and uncoerced, the business judgment rule applied and the action was dismissed. This decision appears to further broaden the *Corwin* line of cases by applying to circumstances where a board conflict-of-interest exists, but the material facts of such conflict have been adequately disclosed. In other words, the Delaware Chancery Court appears to have now concluded that, as long as stockholders know the facts giving rise to the conflict-of-interest when they vote for the deal, if they approve of the deal in such vote, the board and the company will receive the benefit of the business judgment rule.