DELAWARE CORPORATE LAW BULLETIN

Delaware Chancellor Again Invokes *Corwin* in Granting Directors' Motion to Dismiss Breach of Fiduciary Duty Claim

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Discusses potential application of Corwin *in the context of allegedly unreasonable deal protections included in merger agreement*

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INTRODUCTION

The "cleansing" device confirmed by the Delaware Supreme Court in its October 2015 decision in *Corwin v. KKR Financial Holdings LLC*[1] has proven an effective shield for corporate directors to defeat

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post-closing damages claims in connection with M&A transactions. The *Corwin* court ruled that certain directorial breaches of fiduciary duties may be "cleansed" by a fully informed, uncoerced, and disinterested stockholder approval of the underlying transaction. There are two principal grounds that plaintiff/stockholders can cite to avoid application of *Corwin*: *first*, that the stockholder approval relied on by defendant/directors was not "fully informed" and, *second*, that it was coerced.

The former ground has been explored by the Delaware Court of Chancery (the "*Chancery Court*") on several occasions, and it would appear that the bar is quite high for plaintiffs to establish that a particular stockholder approval was not fully informed. For instance, in *In re Saba Software, Inc. Stockholder Litigation*,[2] Vice Chancellor Joseph R. Slights III wrote that "[t]he so-called *Corwin* doctrine . . . only applies 'to fully informed, uncoerced stockholder votes, and if *troubling facts* regarding director behavior were not disclosed that would have been material to a voting stockholder, then the business judgment rule is not invoked.' "[3] The "troubling facts" that led Vice Chancellor Slights to refuse to apply *Corwin* in *Saba Software* were indeed extreme: "[T]here was an elephant in the [Saba Software] boardroom from 2012 forward. The Company had engaged in fraud."[4]

The latter ground—the stockholder vote was coerced—has received less attention from the Chancery Court. In refusing to grant defendant/directors' motion to dismiss in *Saba Software*, Vice Chancellor Slights explained that "[t]he court will find wrongful coercion where stockholders are induced to vote 'in favor of the proposed transaction for some reason other than the economic merits of the transaction.' "[5] The important question for this analysis is "whether the stockholders have been permitted to exercise their franchise free of undue external pressure created by the fiduciary that distracts them from the merits of the decision under consideration."[6] Further, the Vice

1. 125 A.3d 304 (Del. 2015) ("*Corwin*"). For a discussion of the *Corwin* decision and follow-on decisions, see Robert S. Reder & Tiffany M. Burba, *Delaware Courts Confront Question Whether "Cleansing Effect" of* Corwin *Applies to Duty of Loyalty Claims*, 70 VAND. L. REV. EN BANC 187 (2017).

2. C.A. No. 10697-VCS, 2017 WL 1201108 (Del. Ch. Mar. 31, 2017) ("*Saba Software*"). For a discussion of the *Saba Software* decision, see Robert S. Reder, *Delaware Court Refuses to Invoke* Corwin *to "Cleanse" Alleged Director Misconduct Despite Stockholder Vote Approving Merger*, 70 VAND. L. REV. EN BANC 199 (2017).

3. *Saba Software*, C.A. No. 10697-VCS, 2017 WL 1201108 at 7 (Del. Ch. Mar. 31, 2017) (emphasis added).

4. *Id.* at *20.

5. *Id.* at *14.

6. *Id.* at *15.

Chancellor explained that "[i]nequitable coercion can exist . . . when the fiduciary *fails to act* when he knows he has a duty to act and thereby coerces stockholder action."[7]

Alleged coercion of a stockholder vote was at the heart of plaintiffs' attempt to avoid application of *Corwin* in another recent decision of the Chancery Court, *In re Paramount Gold and Silver Corp. Stockholders Litigation*.[8] This time, however, Chancellor Andre G. Bouchard found no coercion and, for that reason and others, granted the defendant/directors' motion to dismiss the fiduciary duty claims brought against them. The Chancellor's opinion also tees up, but does not attempt to resolve, a potential conflict between an earlier Delaware Supreme Court decision and *Corwin*.

I. FACTUAL BACKGROUND

Paramount Gold and Silver Corporation ("*Paramount*") was "a precious metals exploration company" whose common stock traded on the New York Stock Exchange.[9] Paramount owned two "advanced stage mining projects," one located in Mexico (the "*Mexico Project*") and the other located in Nevada (the "*Nevada Project*").[10]

For a number of years, Coeur Mining, Inc. ("*Coeur*") sought to acquire the Mexico Project, but not the Nevada Project. Over this period, the two companies held numerous discussions and negotiations, focusing on several different permutations for structuring a transaction in which Coeur would acquire the Mexico Project and Paramount stockholders would retain their interest in the Nevada Project. These talks culminated on December 15, 2014 with the signing of a merger agreement pursuant to which Paramount would become a wholly-owned subsidiary of Coeur, but *only after* spinning off the Nevada Project into a new company referred to as SpinCo ("*SpinCo*"). In exchange for their Paramount shares, Paramount stockholders would receive (i) shares of publicly-traded Coeur common stock and (ii) shares of SpinCo common stock representing a 95.1% interest in SpinCo. Coeur would receive the remaining 4.9% interest in SpinCo in exchange for a $10 million cash infusion into the new company. The merger agreement promised Coeur a $5 million termination fee (the "*Termination Fee*") if, following announcement of an alternative proposal by a third party, Paramount stockholders refused to approve the transaction and, within

7. *Id.* at *16 (emphasis added).

8. C.A. No. 10499CB, 2017 WL 1372659 (Del Ch. Apr. 13, 2017) ("*Paramount Gold & Silver*").

9. *Id.* at *2.

10. *Id.*

12 months thereafter, Paramount finalized such an alternative transaction. Paramount stockholders ultimately approved the transaction, which closed on April 17, 2015.[11]

On the same day the merger agreement was signed, Paramount and Coeur entered into a royalty agreement granting Coeur a "perpetual royalty" for a portion of future "net smelter returns" generated by the Mexico Project (the "*Royalty Payment*") in exchange for a cash payment of $5.25 million. The Royalty Payment was not conditioned on completion of the merger, and would continue in place whether or not the transaction closed.

Although various Paramount stockholders brought suit in the Chancery Court after initial announcement of the transaction, they did not seek an injunction and allowed their action to linger for several months. Finally, in August 2016, plaintiffs amended their complaint to seek post-closing damages, alleging breach of fiduciary duty on the part of the Paramount directors and challenging various disclosures made in the solicitation materials for the stockholder vote. At the heart of plaintiffs' claims was their contention that *Corwin* was not available to cleanse the directors' conduct because (i) the combination of the Termination Fee and the Royalty Payment represented a " 'preclusive and *per se* unreasonable' deal protection device 'rendering the vote coerced,' " and (ii) "the stockholder vote was uninformed."[12] As such, plaintiffs contended, the directors' conduct should not be given the deference of the business judgment rule but rather should be "reviewed under the *Unocal* enhanced judicial scrutiny standard."[13]

The Paramount directors asked Chancellor Bouchard to dismiss plaintiffs' action. Following a hearing, the Chancellor granted the motion to dismiss.

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11. *Id.* at *4.

12. *Id.* at *5.

13. *Id.* at *6. *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) ("*Unocal*"). Chancellor Bouchard explained the relevance of *Unocal*'s enhanced scrutiny standard of review to deal protection measures as follows:

> Our Supreme Court has held that a 'board's decision to protect its decision to enter a merger agreement with defensive devices against uninvited competing transactions that may emerge is analogous to a board's decision to protect against dangers to corporate policy and effectiveness when it adopts defensive measures in a hostile takeover contest,' and thus should be reviewed under the *Unocal* enhanced judicial scrutiny standard.

Paramount Gold & Silver, C.A. No. 10499CB, 2017 WL 1372659 at *6 (quoting Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 932 (Del. 2003)).

II. CHANCELLOR BOUCHARD'S ANALYSIS

A. Applicability of Corwin

At the outset, Chancellor Bouchard was faced with a possible conflict between *Corwin* and an earlier Delaware Supreme Court decision, *In re Santa Fe Pacific Corporation Shareholder Litigation*.[14] The *Santa Fe* court ruled that "a fully informed stockholder vote approving a merger *did not* preclude review of certain deal protection devices under *Unocal*" in the context of a post-closing challenge.[15] This ruling was premised on the notion that "Santa Fe stockholders did not vote in favor of the precise measures under challenge in the complaint. Here, the defensive measures had allegedly already worked their effect before the stockholders had a chance to vote."[16] Consequently, the *Santa Fe* court "decline[d] to find ratification in this instance."[17]

This was precisely the issue confronting Chancellor Bouchard: plaintiffs claimed that the combination of the Termination Fee and the Royalty Payment—which they alleged represented a termination penalty equivalent to 7.02% of the transaction's value—did not pass muster under a *Unocal* analysis. Accordingly, they argued, consistent with *Santa Fe*, *Corwin* was inapplicable. After pointing out that the *Corwin* court "did not discuss or expressly overrule this aspect of *Santa Fe*," the Chancellor wrote that he "need not address the apparent tension between *Corwin* and *Santa Fe* . . . because it is apparent from the face of the Complaint and documents incorporated therein that the provisions challenged here do not constitute an unreasonable deal protection device."[18] This "apparent tension" between *Santa Fe* and *Corwin,* therefore, is an open question that the Delaware Supreme Court will need to address at some point.

B. Unocal Analysis

Chancellor Bouchard acknowledged that a termination fee of the magnitude alleged by plaintiffs indeed "would be problematic."[19] However, the Chancellor disagreed with plaintiffs' assertion that the Termination Payment and the Royalty Payment should be linked or that the Royalty Payment could properly be characterized as a deal

14. 669 A.2d 59 (Del. 1995) ("*Santa Fe*").
15. *See Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *6.
16. *Santa Fe*, 669 A.2d at 68.
17. *Id.*
18. *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *6.
19. *Id.* at *7.

protection measure. The Chancellor pointed out that (i) the arrangements underlying the Royalty Payment were, unlike typical deal protection measures, "not contingent on consummation of the Merger," (ii) there was no suggestion by plaintiffs "that a superior bidder had any obligation to buy out Coeur's royalty interest in the [Mexico] Project . . . in order to propose or consummate a transaction with Paramount," (iii) "plaintiffs do not allege that Paramount received inadequate consideration in exchange for" the royalty arrangements, and (iv) Coeur "did not have a 'block right' under the Royalty Agreement to veto an alternative transaction to the Merger . . . ."[20] Thus, regardless of whether *Corwin* cleansing was available, enhanced scrutiny of the Paramount directors' conduct was not required under either *Unocal* or, for that matter, *Revlon*.[21]

C. Paramount Stockholder Vote

Next, to determine whether *Corwin* could be properly invoked, Chancellor Bouchard examined the disclosures challenged by plaintiffs. Initially, the Chancellor noted that when corporate boards solicit stockholder approval of a transaction, they "must 'disclose fully and fairly all material information within the board's control.' "[22] For this purpose, a "fact is material only 'if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote.' "[23] Further, he noted that "a board's disclosure obligation is 'not boundless,' and that the board need not disclose information simply because it 'might be helpful.' "[24]

For *Corwin* purposes, the Chancellor explained that "the 'plaintiff challenging the [stockholders'] decision to approve a transaction must first identify a deficiency in the operative disclosure document, at which point the burden would fall to defendants to establish that the alleged deficiency fails as a matter of law to secure the cleansing effect of that vote.' "[25] To this end, plaintiffs raised three

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20. *Id.* at *7, *9.

21. *See* Revlon v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986) ("*Revlon*"). Plaintiffs did not argue that *Revlon* should apply, presumably because Paramount and Coeur had structured "a stock-for-stock transaction." *See Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *14. Further, although plaintiffs originally suggested that Paramount's 15.7% stockholder was a "controller," they ultimately did not ask the Chancellor to apply an entire fairness analysis. *Id.* at *5 n.13.

22. *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *9 (quoting Stroud v. Grace, 606 A.2d 75, 84 (Del. 1992)).

23. *Id.* (quoting Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985)).

24. *Id.* (quoting Skeen v. Jo-Ann Stores, Inc., 750 A.2d 1170, 1174 (Del. 2000)).

25. *Id.* (quoting *In re* Solera Holdings, Inc. S'holder Litig., C.A. No. 11524-CB, 2017 WL 57839 at *7-8 (Del. Ch. Jan. 5, 2017) ("*Solera*")). For a discussion of the *Solera* decision, see Robert S.

objections to disclosures in the documents furnished to Paramount stockholders relating to (i) analysts' price targets for Paramount, (ii) the role of a financial advisor who attended only one board meeting, and (iii) the fee arrangement for the financial advisor formally retained to assist with the Coeur transaction. The Chancellor found none of these issues to be material and therefore ruled that "plaintiffs' disclosure challenges are without merit and thus the stockholder vote approving the Merger was fully informed."[26] Consequently, he ruled that plaintiffs' complaint "must be dismissed for failure to state a claim for relief under the *Corwin* doctrine."[27]

D. Breach of Fiduciary Duty

Finally, Chancellor Bouchard explored the issue whether, even if *Corwin* could not properly be invoked, plaintiffs had stated a "non-exculpated" claim for breach of fiduciary duty that would warrant his not granting directors' motion to dismiss. Like so many other public corporations, Paramount exculpated its directors from personal liability for breach of their duty of care through a provision in its certificate of incorporation authorized by section 102(b)(7) of the Delaware General Corporation Law ("*DGCL §102(b)(7)*"). Accordingly, the Chancellor focused on potential breaches of the directors' duty of loyalty, which cannot be exculpated under DGCL §102(b)(7).

Because plaintiffs did not "challenge the independence or disinterestedness of a majority of the [Paramount] board" or state "any conceivable basis for a loyalty claim other than to assert 'bad faith,' " the question for Chancellor Bouchard was whether plaintiffs' allegations supported a pleading stage finding of bad faith.[28] This in turn required plaintiffs to "show either an extreme set of facts to establish that disinterested directors were intentionally disregarding their duties, or that the decision under attack is so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[29] Plaintiffs' attacks on the deal

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Reder & Tiffany M. Burba, *Delaware Courts Confront Question Whether "Cleansing Effect" of* Corwin *Applies to Duty of Loyalty Claims*, 70 VAND. L. REV. EN BANC 35 (2017).

26. *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *14.

27. *Id.*

28. *Id.* at *1, *14.

29. *Id.* at *14 (quoting *In re* Chelsea Therapeutics Int'l Ltd. S'holders Litig., C.A. No. 9640-VCG, 2016 WL 3044721 at *7 (Del. Ch. May 20, 2016) ("*Chelsea*")). For a discussion of the *Chelsea* decision, see Robert S. Reder & Tiffany M. Burba, *Delaware Court Dismisses Duty of Loyalty Claim Against Disinterested, Independent Directors*, 69 VAND. L. REV. EN BANC 235 (2016).

protections included in the merger agreement,[30] the disclosures made to Paramount stockholders,[31] the sales process,[32] the deal price,[33] and the fairness opinion delivered by the board's financial advisor[34] all were, in the Chancellor's estimation, wholly insufficient to satisfy the high bar to successfully pleading bad faith.

CONCLUSION

Chancellor Bouchard's *Paramount Gold & Silver* opinion does not break new ground in the rapidly-developing *Corwin* jurisprudence. On the other hand, the opinion does exemplify the difficult burden faced by plaintiffs who bring post-closing damages claims for directorial breach of fiduciary duty in connection with M&A transactions. Relatively extreme facts must be pled if such claims are to survive defendant/directors' motion to dismiss. Notably, however, the Chancellor's opinion points to one important question that will need to be resolved, perhaps ultimately, by the Delaware Supreme Court: in light of *Santa Fe,* will a fully informed, uncoerced vote of disinterested stockholders that passes muster under *Corwin* ever be available to "cleanse" a board's approval of a merger agreement containing deal protection measures that a court finds unreasonable for purposes of *Unocal* and its progeny?

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30. "[T]he Royalty Agreement plainly did not operate as a deal protection device and the termination fee by itself was reasonable . . . ." *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *15.

31. Plaintiffs' complaint was "devoid of any facts from which one reasonably could infer that Paramount's directors intentionally disregarded their duties or otherwise acted in bad faith with respect to the disclosures" made to stockholders. *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *15.

32. "There is a vast difference between an inadequate or flawed effort to carry out fiduciary duties and a conscious disregard for those duties." *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *15 (quoting Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 243 (Del. 2009)).

33. "[T]he Court would need to conclude that the price was so far beyond the bounds of reasonable judgment that it seems inexplicable on any ground other than bad faith." *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *15 (quoting *In re* Crimson Expl. Inc. S'holder Litig., C.A. No. 8541-VCP, 2014 WL 5449419 at *23 (Del. Ch. Oct. 24, 2014)). "Plaintiffs have failed to allege facts from which I reasonably could infer that the Merger consideration, representing a '19.8% premium over the last day of trading,' satisfies this 'demanding standard.' " *Id.*

34. "The plaintiffs cannot simply quibble with the inputs used in the fairness opinions." *Paramount Gold & Silver*, C.A. No. 10499CB, 2017 WL 1372659 at *15 (quoting *In re* Morton's Rest. Gp. Inc. S'holders Litig., 74 A.3d 656, 673–74 (Del. Ch. 2013)).