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If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

This issue focuses on important, developing areas of Delaware corporation law and deal litigation, including common questions facing boards of directors during the COVID-19 crisis, the status and procedures of Delaware state and federal courts amid the pandemic, the Delaware Supreme Court's ruling in *Salzberg v. Sciabacucchi*, two Court of Chancery appraisal decisions following *Aruba*, *Dell* and *DFC*, and a Court of Chancery ruling that reaffirms bedrock principles of law governing relationships between parent and subsidiary corporations.

Q&A: Directors' Delaware Law Questions During the Pandemic

Contributor

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Skadden partner Edward Micheletti, who heads the litigation practice of the firm's Wilmington office, answers common Delaware law questions facing boards of directors during the COVID-19 crisis.

Many boards of directors of Delaware corporations are facing extreme circumstances due to the COVID-19 pandemic. In addition to the crisis' general economic impact and the demands of day-to-day decision-making, boards are being forced to address employee health concerns and government-mandated shutdowns of core business operations. What guidance does Delaware law offer boards facing such unprecedented circumstances?

Delaware law offers straightforward, basic principles that guide boards of directors and provide them with flexibility when addressing even the most unique and complicated circumstances. These include the well-defined fiduciary duties of care and loyalty (which encompass disclosure and oversight responsibilities) and the deferential business judgment rule, which prevents a court from second-guessing good faith, well-informed decisions by boards comprised of a majority of disinterested and independent directors. Focusing on these core Delaware corporate law principles, whether as part of normal business operations or during a time of crisis, such as the COVID-19 public health emergency, should help directors make good faith decisions for their business in real time and protect against exposure to potential liability. For more information, see our February 19, 2020, client alert, "Directors' Fiduciary Duties: Back to Delaware Law Basics."

The COVID-19 health emergency has had an unexpected, negative impact on many corporations, having implications on assessment of value. Many boards have been forced into "crisis mode," requiring them to engage in damage control and make very difficult decisions about the business and affairs of a company. How should boards approach these issues?

Again, boards should rely on core Delaware corporation law principles to tackle these problems. Boards can, for example, inform themselves by listening to management about the impact COVID-19 is having (or is anticipated to have) on the company's business operations. Boards can also ask legal or financial advisors to provide their insight as well. When the board makes well-informed, good faith determinations, without self-interest, that are in the best interest of the company and its stockholders, such decisions — even out of the ordinary decisions addressing COVID-19's impact on business operations or corporate value — should be afforded the benefit of the business judgment rule. I suspect that boards will be considering the impact of COVID-19 on business operations and corporate value throughout 2020, even after "stay at home" orders and other government-mandated closures have been lifted. Boards will need to make decisions as facts and circumstances develop and exercise their business judgment consistent with their fiduciary duties to address them.

How does the duty of oversight come into play?

From an oversight standpoint, boards should be aware that, in times of crisis, it is important to focus on maintaining, or even augmenting, board-level reporting and oversight structures so that the board receives the information it needs to assess and address business risks. For example, boards (or applicable board committees) may conclude that more frequent meetings and reports from management, or further augmentation of existing controls, may be warranted to address COVID-19 related concerns. A further discussion on considerations for boards of directors on the COVID-19 crisis can be found in our March 20, 2020, client alert, "Thoughts for Boards of Directors on the COVID-19 Crisis."

In addition to navigating the day-to-day business impact of COVID-19, some directors face the additional challenge of managing the pandemic's effect on their efforts to close a pending merger or acquisition. What issues do directors of buyers and sellers face?

Along with managing COVID-19's impact on a company's day-to-day business, employees and customers, some boards must also manage a number of important issues relating to pending mergers or other transactions. This has been a significant topic of interest for both buyers and sellers with pending deals over the last several weeks in particular. Whether the COVID-19 pandemic has had a "material adverse effect" (MAE) on or may constitute a "material adverse change" (MAC) to a particular business is a determination guided by the specific language of the transaction agreement at issue and fact-specific considerations. Among other things, one critical challenge in demonstrating an MAE or MAC is that, under Delaware law, a party must be able to show a durationally significant adverse impact on a company's fundamental value. Given that COVID-19's impact on the United States in general, and its businesses and economy in particular, arguably manifested itself during the past few months, there will be debate over whether it has been durationally significant enough to support an argument that an MAE or MAC has occurred. Similarly, predicting any long-term impact of COVID-19 will require parties, for example, to analyze the facts and circumstances for an individual business and the industry in which it operates. Other context-specific issues related to COVID-19 include whether the MAE definition in a particular merger agreement directly or indirectly excludes an impact from COVID-19. The exclusions to the MAE or MAC definition can differ in each merger agreement, and merger parties will need to examine the particular language of those exclusions to determine whether a COVID-19-related impact is excluded. Similar issues also may arise when a transaction participant looks for a way out of the deal, for example, by examining a seller's compliance with interim operating covenants and a buyer's conduct in withholding, conditioning or delaying consent for the seller to take certain specified actions to address COVID-19.

Are there any recent Delaware law decisions that address these issues?

Again, these types of issues, including whether a court would order specific performance of any covenant obligations and/or consummation of the transaction, are fact-driven and their resolution may vary from case to case. Two recent post-trial decisions by the Court of Chancery involving MAE/MAC issues help illustrate the matter. In *Akorn, Inc. v. Fresenius Kabi AG*, Vice Chancellor J. Travis Laster denied a seller's request for specific performance of a merger agreement and determined that the buyer did not have to close the deal because it had made the showing necessary to establish an MAE, including based on the seller's significant downturn in performance over five quarters. In *Channel Medsystems, Inc. v. Boston Scientific Corp.*, Chancellor Andre G. Bouchard granted a seller's request for specific performance and determined that the buyer wrongfully terminated the merger agreement. The court held that concerns about potential products liability litigation, competitive harm and future regulatory action were unsubstantiated and did not demonstrate that an MAE was reasonably expected to occur. As MAE/MAC cases are litigated in response to COVID-19, a recurring debate will be whether the particular facts are closer to those in *Akorn* or *Boston Scientific*.

Has COVID-19 resulted in an increase in stockholder litigation at this point, and what should boards do to stay prepared?

Not yet. However, given COVID-19's impact on business and the economy, it would not surprise me at all to see a wave of stockholder litigation arise from this situation. One early indicator would be an uptick in stockholder demands for books and records to investigate "wrongdoing" focused on the board's response to COVID-19. These demands are usually a precursor to a derivative action, which is how most oversight claims are raised. Board-level materials, such as minutes or board presentations, are almost always requested, but a recent trend has emerged in which stockholders try to push the envelope beyond such formal records and attempt to access board communications in emails or even text messages. Keeping accurate, formal records of board decision-making in response to COVID-19 is important, and may help defeat or limit a stockholder's request to access such electronic communications.

Are there any other developing stockholder litigation trends that bear mentioning?

Another trend that began to develop shortly before COVID-19 is using Section 220 demands to explore whether officers, in addition to boards of directors, were involved in any "wrongdoing." This has been of significant interest to plaintiff lawyers because under Delaware law, officers owe fiduciary duties of care and loyalty, but unlike directors, officers are not covered by a company's Section 102(b)(7) exculpatory provision for money damages stemming from breaches of the duty of care.

Checking In With Delaware Courts Amid the COVID-19 Crisis

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While Delaware's "stay at home" order remains in place amid the COVID-19 pandemic, the Delaware Supreme Court and Court of Chancery are still operational, and legal services providers, which are deemed "essential," may continue to conduct business. Given the state's prominence in establishing and enforcing corporate laws, businesses should note that corporate litigation pending in Delaware continues with relatively minimal interruptions and new matters may be filed in the state or federal courts when the need arises. Below are key highlights regarding the courts' current status and procedures. While the situation continues to evolve, Delaware's courts are well-positioned to operate in the current climate.

Parties May Continue To File Documents With the Courts

From a corporate and commercial perspective, filings are largely proceeding without interruption. Delaware courts are better prepared than many to deal with the current crisis. Long before COVID-19 surfaced, the Delaware state and federal courts mandated electronic filing for virtually all corporate and commercial matters. Thus, the recent disruption caused by the pandemic has not prevented litigants from filing pleadings and other documents in Delaware or the courts from receiving them.

"The Delaware Supreme Court has taken steps to adjust procedural requirements that could have curtailed a litigant's ability to file papers." For example, many types of filings, including complaints and counterclaims in the Delaware Court of Chancery, require notarized verifications or affidavits to be included in support of the filing. Gaining access to a notary in the current environment could present substantial challenges. As a result, the Delaware Supreme Court has temporarily suspended the need for notarized documents and instead allowed litigants to submit declarations made under penalty of perjury.[1]

All Delaware Courts Continue To Issue Decisions, and Several Are Scheduling Telephonic Hearings

Although all state courthouses in Delaware are closed to the public until May 14, 2020, the Court of Chancery continues to schedule hearings and hear telephonic arguments from litigants, and the Delaware Supreme Court continues to issue decisions on pending cases.[2] Delaware federal courts are also open for official business and holding hearings telephonically, including for commercial disputes.[3]

The Court of Chancery is conducting virtually all hearings telephonically. The court has a long tradition of accommodating parties and counsel by holding hearings telephonically, positioning it to minimize disruption as a result of COVID-19. If conducting a

[1] Similarly, the U.S. Bankruptcy Court in Delaware has temporarily suspended the requirement for physical signatures from a debtor for any documents filed electronically, subject to certain requirements.

[2] The Delaware Superior Court, including its Complex Commercial Litigation Division (the CCLD), has announced that civil jury trials are suspended through and including May 29, 2020. The court has also announced that all "nonessential" proceedings, including all commercial disputes, are postponed until further notice. However, the CCLD and the Superior Court as a whole continue to issue opinions.

[3] Individual judicial officers in the District of Delaware have discretion to continue to hold hearings and other proceedings by telephone, videoconferencing or otherwise. All civil jury trials in the District of Delaware scheduled to begin before May 31, 2020, have been continued indefinitely. The U.S. Bankruptcy Court continued all matters that are not time sensitive until after May 18, 2020, and any proceedings necessary prior to May 18, 2020, are conducted telephonically or by videoconference. All deadlines under federal or local rules, or existing scheduling orders, are to remain in effect unless modified by the court.

hearing telephonically is not practicable, the hearing shall be continued in person. A party may request by motion that the court conduct an in-person hearing in the event of an exigent need. The Court of Chancery has also expressed a willingness to hold trials electronically, if necessary. Because trials in the Court of Chancery do not involve juries, it has more flexibility to conduct trials remotely. Unlike many courts, the Court of Chancery largely relies on the parties to agree to an order detailing the schedules governing briefing on motions and other pretrial procedures. These scheduling orders remain in effect. However, the Court of Chancery has stated that it will consider any requests for relief from these scheduling orders related to COVID-19 issues, and anecdotal evidence to date suggests that the court is routinely granting such requests.

The Delaware Supreme Court announced that all oral arguments scheduled through the end of May 2020 are canceled and that the court will decide those appeals on the briefs. The court has allowed parties to file a motion requesting oral argument.

Certain Deadlines and Statutes of Limitation and Repose Have Been Tolled

While courts continue to proceed with as little disruption as possible under the current circumstances, the Delaware Supreme Court has provided relief to potential litigants facing a looming statute of limitations. In an April 14, 2020, administrative order, the court extended its earlier order from March 22, 2020, and stated that:

> Deadlines in court rules or state or local statutes and ordinances applicable to the judiciary that expire between March 23, 2020 and May 14, 2020 are extended through June 1, 2020. Statutes of limitations and statutes of repose that would otherwise expire during the period between March 23, 2020 and May 14, 2020 are extended through June 1, 2020. Deadlines, statutes of limitations, and statutes of repose that are not set to expire between March 23, 2020 and May 14, 2020 are not extended or tolled by this order.

As a result, litigants with deadlines imposed under court rules or potential litigants in Delaware state courts who were required to file claims between March 23, 2020, and May 14, 2020, or risk being barred now have until June 1, 2020, to file their papers. For now, litigants with rule-imposed or statutory deadlines after May 14, 2020, still must file by the applicable state or local deadline. Note that, as described above, this does not alleviate deadlines imposed by scheduling orders.

Takeaways

- The governor of Delaware has declared that legal services providers are "essential" and the state and federal courts in Delaware are operational. Litigation continues to proceed and litigants may continue to bring new disputes to the courts.
- Parties may continue to file pleadings and other papers with the state and federal courts via electronic filing.
- The Delaware courts continue to issue decisions. The Court of Chancery and the Delaware federal courts are continuing to schedule new hearings telephonically, though leeway is being granted to amend schedules for COVID-19-related reasons. Parties should anticipate that any hearing scheduled between now and (at a minimum) mid-May 2020 will be held telephonically.
- The Delaware Supreme Court has tolled deadlines set by state statutes or court rules, including statutes of limitations, that would otherwise expire during the period between March 23, 2020, and May 14, 2020. These deadlines have been extended through June 1, 2020. However, this extension does not apply to deadlines agreed to or imposed in existing scheduling orders. Relief from those deadlines is considered on a case-by-case basis by the court.

Delaware Supreme Court Upholds Validity of Provisions Designating Federal Courts as Exclusive Forum of 1933 Act Claims

Contributor

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In *Salzberg v. Sciabacucchi*, No. 346, 2019 (Del. Mar. 18, 2020), the Delaware Supreme Court upheld the validity of corporate charter provisions designating federal courts as the exclusive forum for the litigation of claims under the Securities Act of 1933. The opinion may provide a tool for tempering the wave of state court 1933 Act claims post-*Cyan*.

Background

In *Cyan, Inc. v. Beaver County Employees Retirement Fund*, No. 15-1439 (U.S. Mar. 20, 2018), the U.S. Supreme Court held that federal and state courts have concurrent jurisdiction over class actions based on claims brought under the 1933 Act, and that such claims are not removable to federal court. Following *Cyan*, the filing of 1933 Act cases in state courts escalated. In response, corporations began adopting forum selection provisions in their charters that designated the federal courts as the exclusive forum for such claims.

The Court of Chancery's Opinion in *Sciabacucchi v. Salzberg*

In December 2017, a stockholder of Blue Apron Holdings, Inc., Roku, Inc. and Stitch Fix, Inc. filed an action in the Court of Chancery seeking declaratory judgment that the companies' forum selection provisions requiring stockholder-based federal securities claims to be brought exclusively in federal court are invalid.

The Roku and Stitch Fix certificates of incorporation, which contained substantively identical provisions, provided that "[u]nless the Company consents in writing to the selection of an alternative forum, the federal district courts of the United States of America shall be the exclusive forum for the resolution of any complaint asserting a cause of action arising under the Securities Act of 1933. Any person or entity purchasing or otherwise acquiring any interest in any security of the Corporation shall be deemed to have notice of and consented to [this provision]."

Blue Apron's certificate of incorporation was slightly different and provided that "the federal district courts of the United States of America shall, *to the fullest extent permitted by law*, be the sole and exclusive forum for the resolution of any complaint asserting a cause of action arising under the Securities Act of 1933."

On December 19, 2018, in *Sciabacucchi v. Salzberg*, C.A. No. 2017-093-JTL (Del. Ch. Dec. 19, 2018), the Delaware Court of Chancery held that such charter provisions were invalid because "constitutive documents of a Delaware corporation cannot bind a plaintiff to a particular forum when the claim does not involve rights or relationships that were established by or under Delaware's corporate law," and that federal forum selection provisions attempted to accomplish that and were therefore invalid. Skadden discussed the Court of Chancery's opinion in the December 21, 2018, client alert, "Delaware Court of Chancery Invalidates Forum Selection Provisions Regulating Claims Under the Securities Act of 1933."

The Delaware Supreme Court's Opinion

On appeal, the Delaware Supreme Court reversed the Court of Chancery, and held that federal forum provisions (FFPs) are facially valid under Delaware law.

The court began by analyzing 8 Del. C. § 102, which governs matters contained in a corporation's charter. Section 102(b)(1) authorizes two broad types of charter provisions: "any provision for the management of the business and for the conduct of the affairs of the corporation" and "any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the stockholders, or any class of the stockholders ... if such provisions are not contrary to the laws of this State." The court held that an FFP "could easily fall within either of these broad categories, and thus, is facially valid."

The court also remarked that such provisions "can provide a corporation with certain efficiencies in managing the procedural aspects of securities litigation following the United States Supreme Court's decision in *Cyan, Inc. v. Beaver County Employees Retirement Fund*." The court pointed to the escalation of 1933 Act claims being brought in state courts post-*Cyan* and remarked that:

> When parallel state and federal actions are filed, no procedural mechanism is available to consolidate or coordinate multiple suits in state and federal court. The costs and inefficiencies of multiple cases being litigated simultaneously in both state and federal courts are obvious. The possibility of inconsistent judgments and rulings on other matters, such as stays of discovery, also exist. By directing 1933 Act claims to federal courts when coordination and consolidation are possible, FFPs classically fit the definition of a provision "for the management of the business and for the conduct of the affairs of the corporation."

The court then looked to the 2015 amendments to the DGCL to add Section 115, which explicitly allowed corporations to adopt forum selection provisions designating Delaware as the exclusive forum for internal corporate claims. The court found that the amendments further supported the view that FFPs are valid under Delaware law, and that Section 115 did not implicitly amend Section 102(b)(1).

The court also held that FFPs do not violate the policies or laws of Delaware, given that the DGCL "allows immense freedom for businesses to adopt the most appropriate terms for the organization, finance and governance of their enterprise." The court further held that FFPs do not violate federal law or policy. The court referred to the U.S. Supreme Court's decision in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, where the U.S. Supreme Court held that federal law has no objection to provisions that preclude state litigation of Securities Act claims. The Delaware Supreme Court remarked, "The holding in *Rodriguez* provides forceful support for the notion that FFPs do not violate federal policy by narrowing the forum alternatives available under the Securities Act."

The Delaware Supreme Court also discussed the implications of its decision, something that the parties had extensively briefed. The court noted that "the most difficult aspect of this dispute is not with the facial validity of FFPs, but rather, with the 'down the road' question of whether they will be respected and enforced by our sister states." The court remarked that the question of enforceability is a separate analysis that should not drive the initial facial validity inquiry but recognized it as a "powerful concern," remarking:

> Delaware historically has, and should continue to be, vigilant about not stepping on the toes of our sister states or the federal government. But there are persuasive arguments that could be made to our sister states that a provision in a Delaware corporation's certificate of incorporation requiring Section 11 claims to be brought in federal court does not offend principles of horizontal sovereignty — just as it does not offend federal policy.

The court ultimately concluded its opinion by stating:

> FFPs are a relatively recent phenomenon designed to address post-*Cyan* difficulties presented by multi-forum litigation of Securities Act claims. The policies underlying the DGCL include certainty and predictability, uniformity, and prompt judicial resolution to corporate disputes. Our law strives to enhance flexibility in order to engage in private ordering, and to defer to case-by-case law development. Delaware courts attempt "to achieve judicial economy and avoid duplicative efforts among courts in resolving disputes." FFPs advance these two goals.

Takeaways

- The Delaware Supreme Court's opinion may provide a tool for companies to avoid duplicative litigation of securities claims in certain federal and state courts and to temper the wave of claims under the 1933 Act brought in state court.
- Private companies that are considering going public should evaluate amending their charter to include similar federal forum provisions.
- Public companies whose charters contain such federal forum provisions should consider raising the provision as a defense early on in state court litigations.
- The provisions at issue in *Salzberg* were contained in the corporations' charters, and the court's opinion largely turned on the interpretation of 8 Del. C. §102(b)(1), which governs the contents of corporate charters. Moreover, amendments to corporate charters must be approved by a stockholder vote. Thus, it remains to be seen whether such provisions would be valid if they were solely in the corporation's bylaws, which are governed by a different provision of the DGCL and which do not, in general, require a stockholder vote to be amended.
- *Salzberg* involved a facial challenge to the validity of forum selection charter provisions. While the court found that such provisions are facially valid, an "as applied" challenge to such provisions may be possible. To that end, the court remarked in its opinion that "charter and bylaw provisions that may otherwise be facially valid will not be enforced if adopted or used for an inequitable purpose."
- Companies should consult with outside counsel regarding the appropriate form of FFP, whether the FFP should be in a charter or bylaw, and other related issues before adopting such a provision.

Court of Chancery Continues To Rely on Market-Based Metrics in Appraisal Decisions

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In recent decisions, the Delaware Court of Chancery continued to follow the Delaware Supreme Court's mandate from *Aruba*, *Dell* and *DFC* to rely on market-based metrics, when available, to determine fair value in appraisal cases.

In *In re Appraisal of Panera Bread Company* (Del. Ch. Jan. 31, 2020), the court found that deal price minus synergies was the most reliable indicator of fair value because the deal process exhibited sufficient objective indicia of reliability.[1] This was similar to the court's decisions last year in both *In re Appraisal of Columbia Pipeline Group* (Del. Ch. Aug. 12, 2019) and *In re Appraisal of Stillwater Mining* (Del. Ch. Aug. 21, 2019), in which the court also found that each deal process was characterized by objective indicia of reliability sufficient to make deal price the most reliable metric of fair value. In addition, in *In re Appraisal of Jarden* (Del. Ch. July 19, 2019), the court determined that flaws in the deal process undermined its reliability, but found that the unaffected market price was the best evidence of fair value.[2] *Stillwater* is currently on appeal to the Delaware Supreme Court.

In *Manichaean Capital, LLC v. SourceHOV Holdings, Inc.* (Del. Ch. Jan. 30, 2020), the court appraised SourceHOV, which was a privately held entity prior to a business combination whereby it became a publicly traded company. Only after determining that market-based metrics were unreliable or unavailable, the court resorted to a DCF valuation.

An analysis of the 2020 opinions follows.

Panera

In *Panera*, the court found that the $315 deal price minus $11.56 in synergies was the most reliable indicator of fair value. The court noted that "[t]here is no checklist or set of minimum characteristics for giving weight to the deal price." Instead, the court determined that the following objective indicia (similar to *Columbia Pipeline* and *Stillwater*) outweighed the petitioners' argument that certain aspects of the deal process undermined the reliability of the deal price:

- The merger was an arm's-length transaction with a third party;
- Panera's board, its CEO and primary negotiator, and its advisers were not conflicted;
- Panera's board used its "impeccable knowledge of the market" and its advisers' advice to engage all logical buyers;
- The buyer, JAB Holdings, B.V. (JAB), conducted due diligence and received confidential insights about Panera's value;
- JAB also assessed Panera's value using Panera's extensive public information, which was accessible to other potential bidders;
- Panera negotiated with JAB and extracted multiple price increases;
- Panera's passive post-signing market check offered interested bidders a reasonable chance to bid, where Panera's deal protections (a no-shop provision with a fiduciary

[1] Skadden represented Panera Bread Company.

[2] *See* Jenness E. Parker, Kaitlin E. Maloney and Daniel S. Atlas, "Chancery Relies on Market-Based Metrics in Recent Appraisal Decisions," Delaware Business Courts Insider, October 16, 2019, for an examination of the 2019 decisions.

out, matching rights and a 3% termination fee) fell within what Delaware courts have held to satisfy enhanced scrutiny; and

- No bidders emerged post-signing.

Also, the court agreed with Panera that several factors provided "conclusive evidence" that Panera's stock traded in an efficient market, which supported giving dispositive weight to deal price: Panera had many stockholders; no controlling stockholder; highly active trading; a large market capitalization; substantial public float and trading volume; a low bid-ask spread; a high number of equity analysts; and a rapid response to transaction rumors. In addition, information about the company was widely available and easily disseminated to the market.

The court disregarded the petitioners' three alternative valuation methodologies as unreliable in the face of a reliable market-based deal price. The court rejected the petitioners' proffered DCF valuation because it exceeded the deal price by $39 per share and suggested that over a billion dollars was left on the table. The court found that the petitioners' expert "weaken[ed] his credibility" by shifting his investment rate and failing to adjust his DCF to accommodate that shift. The court also rejected the petitioners' comparable companies and precedent transactions analyses for lack of a suitable peer group.

The court deducted $11.56 in cost savings and tax synergies from the deal price. The court found that a "preponderance of the evidence demonstrate[d] that JAB formed its bid in anticipation of applying its management playbook" for cost and cash savings, including re-leveraging Panera's balance sheet to increase debt and resulting tax savings. The court recognized that JAB had successfully implemented similar working capital changes at other companies it had acquired, noting that several bankers' presentations cited JAB's "long track-record" of delivering expected cost savings. In addition, the court noted that Panera's valuation expert agreed with these synergies and that internal documents reflected that JAB anticipated them and factored them into its valuation of Panera. The court rejected the petitioners' argument that the synergies were not merger-specific because management theoretically could have made the changes. The court found instead that "Panera's management culture and priorities did not support the changes JAB intended to make."

Panera sought a refund of the synergies amount because it had prepaid the full deal price pursuant to the appraisal statute. However, as a matter of first impression, the court denied the request, stating that "Section 262(h) does not explicitly contemplate any refund" and the parties had not stipulated to a clawback provision in their prepayment agreement, even though Panera had reserved all rights to request the refund.

Manichaean Capital

In *Manichaean Capital*, which involved an appraisal of SourceHOV, a privately held company at the time of the business combination, the court noted that "[i]n the wake of recent guidance from our Supreme Court, this Court typically begins its statutory appraisal function by focusing on market-based evidence of fair value." Even though the "parties agree[d] that market evidence is not useful because SourceHOV was privately held and its managers made no real effort to run a 'sale process,'" the court summarily considered the deal process and found that the circumstances surrounding SourceHOV's business combination disqualified market-based evidence as reliable metrics for two reasons.

First, the court agreed with the parties that the deal price was not reliable because SourceHOV did not engage in a sales process prior to the business combination. For example, SourceHOV did not hold a single board meeting to consider the potential business combination, nor did it solicit offers from third parties after it received the initial overture. Second, the court held that it could not look to unaffected market price because as a private company, SourceHOV had no publicly traded stock.

The parties also agreed that there were no sufficiently comparable companies or transactions with which to perform either a trading multiples or a transaction multiples analysis.

Therefore, the court resorted to a DCF analysis to determine SourceHOV's fair value. Noting that the DCF valuations proffered by the parties' experts were "solar systems apart," the court relied solely on the DCF valuation proffered by the petitioners' valuation expert because the inputs were reasonable and supported by credible evidence. Conversely, the court found that the DCF submitted by the respondent was not credible because the respondent disagreed with its own expert and proffered a valuation that came in "well below even its own expert's appraisal," relied on witnesses whose credibility was impeached and employed a novel approach to calculate SourceHOV's equity beta, which was unsupported by the record.

Takeaways

- The Delaware Court of Chancery continues to examine market-based metrics of fair value in the first instance and resorts to a DCF analysis where market-based evidence is unreliable or unavailable.
- Petitioners may have difficulty rebutting the reliability of the deal price where alleged "flaws" in the process do not outweigh the objective indicia of reliability and where no money was left on the table.
- Delaware courts may find that a passive post-signing market check confirms the reliability of the deal price where potential bidders had an opportunity to come forward and where a merger agreement contains reasonable deal protection provisions that would survive enhanced scrutiny.
- Delaware courts may deduct synergies where there is sufficient record evidence that the buyer quantified, anticipated and included those synergies in its valuation of the target company.
- Where synergies comprised a portion of the deal price, companies may consider prepaying an amount lower than the deal price or stipulating to a clawback provision in a prepayment agreement.
- As exemplified by *Panera*, Delaware courts are increasingly skeptical of DCF analyses that result in fair values well above the deal price and are declining to rely on comparable analyses without a suitable peer group.

Court of Chancery Dismisses Consent and Unconscionability Claims Challenging Contract Between Parent and Wholly Owned Subsidiary

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On March 30, 2020, in *The Chemours Company v. DowDuPont Inc., et al.*, C.A. No. 2019-0351-SG (Del. Ch. Mar. 30, 2020), the Delaware Court of Chancery issued an important decision reaffirming bedrock principles of Delaware corporate and contract law governing the relationship between parent and subsidiary corporations. In *Chemours*, the Court of Chancery upheld the validity of a separation agreement entered into by a parent corporation and its wholly owned subsidiary and enforced the delegation clause of a mandatory arbitration provision in the parties' separation agreement. Specifically, the Court of Chancery held that agreements between a parent and subsidiary corporation do not fail for lack of contractual "consent" and are not procedurally unconscionable simply because the parent company dictates the terms of the contract. Under settled Delaware law, wholly owned subsidiaries are expected to operate for the benefit of their parent corporations, and Delaware will not invalidate contracts because the parties operate accordingly.

The decision in *Chemours* reaffirms a foundational element of parent-wholly owned subsidiary jurisprudence and preserves an integral part of corporate structuring by expressly acknowledging the validity of parent-wholly owned subsidiary contracts under Delaware law.

Background of the Parties' Dispute

In *Chemours*, the parties' dispute arose out of the 2015 spin-off of The Chemours Company (Chemours) from its former parent, E.I. du Pont de Nemours and Company (DuPont).[1] The terms of the spin-off were governed by a separation agreement (the Separation Agreement), which was approved by Chemours' board and signed by a Chemours officer prior to the spin-off. The Separation Agreement assigned certain assets and liabilities to Chemours, including historical environmental liabilities for which Chemours is obligated to indemnify DuPont.

The Separation Agreement also contained a mandatory arbitration provision requiring confidential arbitration of any disputes arising among the parties relating in any way to the Separation Agreement. Moreover, a "delegation provision" in the Separation Agreement stated that the parties "expressly agree" that "all issues of arbitrability … shall be finally and solely determined by the Arbitral Tribunal."

In 2019, four years after the spin-off, Chemours filed a lawsuit in the Delaware Court of Chancery seeking to invalidate or limit its obligation to indemnify DuPont (and others) under the Separation Agreement. Chemours claimed that, at the time of the spin-off, the value of Chemours' indemnification obligations had been underestimated by DuPont and, if properly estimated, would have rendered Chemours insolvent at the time of the spin-off, in violation of Delaware law. Chemours sought an order from the court declaring the indemnification provisions of the Separation Agreement unenforceable, or imposing caps on its indemnification obligations. In the alternative, Chemours sought the return of a $3.91 billion dividend paid to DuPont in connection with the spin-off.

Summary of the Court of Chancery's Analysis

Citing the mandatory arbitration provision, DuPont moved to dismiss Chemours' claims for lack of subject matter jurisdiction. In opposition, Chemours argued it was not required to arbitrate its claims because (i) it did not consent to arbitration, and (ii) the arbitration

[1] Skadden represented DuPont and the other defendants.

provision was unconscionable. The Court of Chancery rejected both of Chemours' arguments and dismissed its claims for lack of subject matter jurisdiction.

Unless specified otherwise in the agreement, agreements to arbitrate disputes involving interstate commerce, like the Separation Agreement, are governed by the Federal Arbitration Act (FAA). Under the FAA, issues of contract formation, like consent, are governed by principles of state contract law.

Chemours first argued that "as a subsidiary, pre-Spin-Off Chemours had no will of its own; it was animated solely by the will of its parent, DuPont, and thus was unable to independently and effectively consent to arbitration." Chemours alleged, among other things, that it had no opportunity to bargain with DuPont regarding the terms of arbitration and was not permitted to retain counsel, and that the arbitration provision was "conceived, drafted, and executed by DuPont alone." The Court of Chancery disagreed that these alleged facts rendered Chemours unable to consent. Applying Delaware law, the court found that "[w]hile Chemours challenges its consent to arbitration in this 'real world' or intuitive sense, it cannot show that it did not consent in the *contractual* sense required by the FAA." The court explained: "Simply because the parent dictates terms to its wholly-owned subsidiary is *not* grounds under Delaware law to infer lack of consent such that the contract would be unenforceable." Rather, consent is measured at the time of contract formation, and Chemours' board resolution and its acting vice president's signature on the Separation Agreement (even though all such parties were DuPont employees) evidenced Chemours' "overt manifestation of assent — and, therefore, Chemours's consent — to the Separation Agreement."

Chemours also argued that the arbitration provisions should not bind Chemours because the Separation Agreement was akin to a foundational document, such as a corporate charter, and thus not really a contract at all. The Court of Chancery again disagreed, finding that Chemours' argument would "violate the FAA's equal treatment principle," which required courts to place arbitration provisions on equal footing with other contracts. The Court of Chancery also explained that "Delaware law recognizes no subspecies of consent applicable to agreements such as the Separation Agreement," and thus "[a] rule that requires an elevated level of consent for purposes of an arbitration agreement ... would derivate from Delaware law contract principles."

Next, the Court of Chancery rejected Chemours' argument that the delegation provision was substantively and procedurally unconscionable. Chemours argued that the mandatory arbitration provision of the Separation Agreement was substantively unconscionable because, among other reasons, the Separation Agreement "den[ies] the arbitrator any 'authority or power to limit, expand, alter, amend, modify, revoke or suspend any condition or provision' of the Separation Agreement." Thus, Chemours argued, the arbitrator would have no power to take any action should it agree with Chemours that the arbitration provisions were unconscionable because any action would require the arbitrator to "modify" or "revoke" a provision of the Separation Agreement. The court rejected this argument, explaining that Chemours had failed to articulate a substantive unconscionability argument that was specific to the delegation clause (and that, in all events, the provisions Chemours complained about did not operate on the delegation clause, and therefore did not render the delegation clause substantively unconscionable).

Finally, the Court of Chancery rejected as a matter of Delaware law Chemours' argument that the Separation Agreement was "procedurally unconscionable." Similar to its consent arguments, Chemours argued the arbitration provisions were procedurally unconscionable because, according to Chemours, they were "'written into the Separation Agreement over Chemours's express objection.'" The Court of Chancery noted that unconscionability is measured at the time of contract formation, and that Chemours was a wholly owned subsidiary of DuPont at the time the Separation Agreement was executed. Reaffirming long-standing principles of Delaware corporate law, the Court of Chancery found that, even if the delegation clause were the product of procedural unfairness, "it cannot be procedurally unconscionable because such a finding cannot be squared with settled Delaware law that 'wholly-owned subsidiary corporations are expected to operate for the benefit of their corporations; that is why they are created.'" The court stated that "the spirit of procedural unconscionability ... is wholly inconsistent with the routine enforcement of parent-subsidiary contracts," and "to find such a contract unenforceable based on procedural unconscionability would be nonsensical."

Chemours has appealed the decision to the Delaware Supreme Court. The briefing on the appeal is scheduled to conclude in July 2020.

Takeaways

- Parent-subsidiary contracts are presumptively valid under Delaware law, even where the parent dictates the terms.
- As a general matter, agreements between a parent and wholly owned subsidiary cannot be procedurally unconscionable because wholly owned subsidiaries are created solely for the benefit of the parent.
- Companies should be in close contact with outside counsel in navigating these types of issues.

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