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Delaware Court Addresses Ability to Sue Buyers for Lost Premiums in M&A Deals

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The Delaware Court of Chancery recently addressed an important issue — whether a target company's stockholders could sue a buyer for monetary damages representing the lost premium they would have received if the merger closed. The court reached a sensible result under the circumstances that the stockholders could not bring that claim. But in doing so, the court muddied the waters in an area that many practitioners believed was more clear and has possibly taken away an M&A provision that significantly discourages buyers from breaching merger agreements.

Background

In *Crispo v. Musk*,[1] a Twitter stockholder brought suit against Elon Musk based on his alleged breach of the merger agreement in which he had agreed to purchase Twitter.[2] Musk eventually completed the transaction, which led to the unusual posture of this case — the plaintiff sought a $3 million "mootness fee" on the theory that his action was causally related to Musk's decision to close. Mootness fees can be awarded where there is a resulting corporate benefit causally related to a lawsuit, but the suit must have been meritorious when filed.[3]

Court of Chancery's Opinion

The Court of Chancery concluded that the plaintiff was not entitled to a mootness fee, because his suit was not meritorious when filed. The merger agreement included a provision (the "Lost-Premium Provision") that termination of the merger agreement would not:

> … relieve any party hereto of any liability or damages (which the parties acknowledge and agree shall not be limited to reimbursement of Expenses or out-of-pocket costs, and, in the case of liabilities or damages payable by [buyer], would include the benefits of the transactions contemplated by this Agreement lost by [the target]'s stockholders) (*taking into consideration all relevant matters, including lost stockholder premium*, other combination opportunities and the time value of

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[1] *Crispo v. Musk*, C.A. No. 2022-0666-KSJM, mem. op. (Oct. 31, 2023).

[2] The merger agreement was entered into on April 25, 2022. On July 8, 2022, Musk purported to terminate the merger agreement. Musk later agreed to consummate the merger on its original terms before Twitter's or the stockholder's claims went to trial.

[3] *See United Vanguard Fund, Inc. v. TakeCare, Inc.*, 693 A.2d 1076, 1079 (Del. 1997).

money), which shall be deemed in such event to be damages of such party, resulting from any knowing and intentional breach of this Agreement prior to such termination … (emphasis added).

The court held that there were two competing interpretations of the Lost-Premium Provision, neither of which supported the plaintiff's lawsuit. Under one interpretation, the court said the Lost-Premium Provision would be unenforceable because it did not specifically make the stockholders third-party beneficiaries of the provision and, therefore, the target would be recovering damages (*i.e.*, the lost premium) for consideration that it had no right or expectation to receive had the merger agreement been performed. Viewed that way, lost-premium damages would be an unenforceable penalty under contract law unless the merger agreement made the stockholders third-party beneficiaries.[4]

Under the other interpretation, the Lost-Premium Provision made the target stockholders third-party beneficiaries whose rights to bring claims directly against the buyer would accrue only if the merger agreement had been terminated and specific performance was unavailable. Because the merger agreement was never validly terminated and the transaction ultimately closed, the plaintiff's right to bring a suit never vested.

The court concluded that, under either interpretation, the plaintiff lacked standing to enforce the merger agreement at the time he filed the complaint. The complaint, therefore, was not meritorious when filed and the petition for a mootness fee was denied.

Analysis and Implications

Lost-premium provisions — also called "*ConEd* provisions" after a 2005 decision in the Second Circuit — have been employed in M&A transactions for almost 20 years.[5] Many practitioners believed these provisions might be unnecessary in Delaware, however, because Delaware courts presumably would allow a target company to pursue lost-premium damages on behalf of its stockholders even without a specific authorization in the merger agreement.[6] Indeed, one reason the *Crispo* decision is surprising is that many buyers have long accepted that, in the absence of an express limitation on a target's remedy (such as a reverse termination fee as the sole and exclusive remedy), there was potential exposure for lost-premium damages.

The court's analysis raises several issues. First, the court was clear that, as drafted, the Lost-Premium Provision would not be enforceable by Twitter itself.[7] The court reasoned that only a target company's stockholders — not the target

[4] *See Crispo* at 27 ("Because only the target stockholders expect to receive a premium in the event a merger closes, a damages-definition defining a buyer's damages to include lost-premium is only enforceable if it grants stockholders third-party beneficiary status.").

[5] *Consol. Edison, Inc. v. Ne. Utilities*, 426 F.3d 524 (2d Cir. 2005). The *ConEd* court held that the merger agreement conferred certain third-party beneficiary rights on the target company's shareholders, but that such rights were limited to enforcing the buyer's obligation to pay the merger consideration to the shareholders *after* the effective time (which never occurred). For a comprehensive review of *ConEd*, see Kevin Miller, *The ConEd Decision — One Year Later: Significant Implications For Public Company Mergers Appear Largely Ignored*, The M&A Lawyer (Oct. 2006).

[6] *See*, *e.g.*, Ryan D. Thomas and Russell E. Stair, *Revisiting Consolidated Edison—A Second Look at the Case That Has Many Questioning Traditional Assumptions Regarding the Availability of Shareholder Damages in Public Company Mergers*, 64 Bus. Law. 329, 357 (2009) (quoting remarks of then-Vice Chancellor Leo E. Strine, Jr. at the Securities Regulation Institute Seminar at the Northwestern University School of Law (Jan. 24, 2008)); Matthew D. Cain and Steven M. Davidoff, *Delaware's Competitive Reach*, 9 J. Emp. L. Studies 92 (2012) (theorizing that all-cash transactions would migrate to Delaware and away from New York due to certainty of law after *ConEd*).

[7] *See Crispo* at 27 ("To the extent that a damages-definition provision purports to define lost-premium damages as exclusive to the target, therefore, it is unenforceable.").

company itself — have any right or expectation to receive the merger consideration, including the premium, and therefore awarding lost-premium damages to the target would result in an unenforceable penalty under hornbook contract law.[8]

Second, and in our view most importantly, the court indicated in dicta that even if target company stockholders are third-party beneficiaries of a lost-premium provision — thereby avoiding the unenforceable penalty issue discussed above — allowing the target to pursue damages on the stockholders' behalf may not be enforceable because the stockholders did not appoint the target as their agent. Citing to two secondary sources which acknowledged the legal uncertainty, the court noted that the agency approach "rested on shaky [legal] ground."[9] Given Delaware's pro-contractarian approach to private ordering, it is not clear why, when a buyer and target create and bestow a third-party beneficiary right, they cannot also condition or proscribe the manner in which that right may be enforced. If it is an all-or-nothing proposition, the result may be that target company stockholders are worse off in M&A deals because they will be less likely to be made third-party beneficiaries of merger agreements.

With respect to the court's second interpretation, which would allow the target stockholders to sue the buyer but only if specific performance is unavailable, the court did not indicate whether the stockholders' right to seek damages would depend on whether the target had actually sought specific performance or obtained a definitive ruling that the buyer breached the merger agreement. As discussed below, this could be left to private ordering in merger agreements.

The court's holding presents numerous issues for transaction counterparties. First, many buyers may resist giving target stockholders a direct right of action against them.[10] Buyers will fear that any failed deal will result in multiple lawsuits from the plaintiffs' bar, similar to the numerous disclosure-related lawsuits routinely brought against target companies, which will seek compensation on a contingency fee basis. Obviously, not every failed deal involves a buyer's willful breach, but the economics of stockholder litigation will still incentivize lawsuits.

Similarly, targets have been reticent to empower stockholders with direct enforcement rights.[11] Reserving that right for the board of directors, which owes fiduciary duties to the stockholders, is consistent with Delaware's board-centric regime. Admittedly, the prospect of target stockholders suits seeking lost-premium damages is a powerful disincentive for the buyer to breach. But if stockholders can sue buyers, the target board's ability to negotiate or settle with buyers over failed transactions may be curtailed. In fact, there may be situations where the target's board of directors does not believe it is in the best interests of the target to sue the buyer (*e.g.*, where the target company may have breached its covenants or potentially suffered a material adverse effect). After all, the target's board of directors is best situated to judge the merits of any claim

[8] *See id.* at 26-27.

[9] *Id.* at 22 (citing 2 Arthur Fleischer, Jr. *et al.*, *Takeover Defense: Mergers and Acquisitions* § 19.06[C] at 209-10 (9th ed. 2017); Victor I. Lewkow and Neil Whoriskey, *Left at the Altar: Creating Meaningful Remedies for Target Companies*, The M&A Lawyer (Oct. 2007)).

[10] Of course, if *Crispo* stands, whether a buyer agrees to allow stockholders to bring lost-premium claims will be a function of the parties' negotiating leverage.

[11] *See*, *e.g.*, Lewkow and Whoriskey, *supra* (noting that the "[t]arget will want to preserve for itself the right to control this critical litigation including the right to settle such litigation … and [b]uyer will not want to negotiate/litigate with potentially unorganized and uncoordinated groups of shareholders should a breach be alleged").

against the buyer under the agreement.[12] Target stockholder-initiated litigation will be even messier if the buyer counterclaims against the target seeking damages from the target's alleged breach of the agreement.

Second, if buyers are unwilling to agree to give target company stockholders the right to bring lost-premium damages claims, then a rule prohibiting targets from seeking lost-premium damages directly will create a significant imbalance in leverage in enforcing a merger agreement. The prospect of lost-premium damages is a powerful disincentive for a buyer to breach. Whether a buyer could be liable for lost-premium damages versus only the target's out-of-pocket costs factors greatly into that buyer's analysis of whether to breach. It likewise affects the target's decision to enter into a transaction with a buyer, as well as whether to sue for monetary damages after weighing the expense of litigating the claim against the likelihood of recovery. While already important and typically the preferred remedy, specific performance — which may not always be available[13] — will be particularly critical if targets lack a meaningful damages claim.

Legal Arguments in Favor of Lost-Premium Provisions

Despite the dicta in *Crispo* regarding a target's ability to seek lost-premium damages on behalf of its stockholders, there are reasons why a Delaware court could uphold a lost-premium provision similar to the one in this case. First, it is important to remember the unusual context of this case (*i.e.*, a plaintiff seeking a mootness fee after suing a buyer during the pendency of litigation between the merger parties). A Delaware court may reexamine the issue more closely in a post-termination lawsuit brought by a jilted target against a buyer for a willful breach of a merger agreement. Delaware courts also have previously suggested lost-premium damages could be recovered.[14] As one treatise observes, "common sense would suggest that this is a rational and appropriate means of achieving an equitable and intended result."[15]

Second, there is support for lost-premium provisions under the Delaware General Corporation Law. For one, Section 251(b)(6) states that a merger agreement can contain such "details or provisions as are deemed desirable."[16] Delaware is a pro-contractarian state, vesting decision-making in the board of directors to agree on those details and provisions. For another, Section 251(b) provides that "the terms of the agreement of merger … may be made

[12] *Cf. Dolan v. Altice USA, Inc.*, 2019 WL 2711280 (Del. Ch. June 27, 2019) (noting that the plaintiffs actively participated in the merger negotiations independent of the target company and negotiated the contract terms which they sought to enforce). For all of the reasons described above, a target's lawsuit over a failed deal is fundamentally different from a stockholder's third-party beneficiary rights to receive the merger consideration after closing. *See Amirsaleh v. Bd. of Trade of City of New York, Inc.*, 2008 WL 4182998, at *4 (Del. Ch. Sept. 11, 2008).

[13] For example, consider a situation where the buyer may have the financial wherewithal to satisfy a damages award but would be rendered insolvent if forced to acquire the company. In addition, the Court of Chancery recently declined to award specific performance in a decision involving extraordinary findings. *See 26 Capital Acq. Corp. v. Tiger Resort Asia Ltd.*, C.A. 2023-0128-JTL (Del. Ch. Sept. 7, 2023).

[14] *See In re IBP, Inc. S'holders Litig.*, 789 A.2d 14, 83 (Del. Ch. 2001) ("[T]he determination of a cash damages award will be very difficult in this case. And the amount of any award could be staggeringly large. No doubt the parties would haggle over huge valuation questions …"); *see also* note 6 *supra*.

[15] Fleischer, *supra*, at § 19.06[C].

[16] 8 Del. C. § 251(b)(6).

dependent upon facts ascertainable outside of such agreement."[17] The term "facts" includes "a determination or action by any person or body, including the corporation."[18] Such provisions have supported, for example, the use of post-closing stockholders' representatives.[19]

Possible Responses to the Ruling

In the absence of a Delaware court revisiting the dicta, practitioners will need to consider how best to deal with remedies and lost-premium damages. Potential options, among others, may include:

- Stockholders' Appointment of Target as Agent. Stockholders could approve the agent-principal appointment by virtue of their adoption of the merger agreement. Similar language is often included in merger agreements appointing sellers' representatives, typically, but not exclusively, in the private company context.[20] We expect to see more such language in public company merger agreements. In practice, this seems workable but some questions remain. For one, what happens if the buyer's breach and termination occur before the stockholder vote?[21] For another, *Crispo* did not address whether a majority of the stockholders can approve the agency appointment for all stockholders.[22] Consideration will also need to be given to how the appointment might be addressed in a tender offer (*e.g.*, through language in transmittal documents).
- Conditioning Third-Party Beneficiary Rights in Merger Agreements. While this is an evolving area of the law, parties might draft merger agreements to condition the stockholders' third-party beneficiary status and concomitant enforcement right.[23] One approach based on *Crispo* is to provide clearly that the damages claim may only be brought if the target has terminated the merger agreement due to buyer's breach. This would allow the target to pursue specific performance and avoid stockholder lawsuits until after the target has abandoned the transaction. Another possibility to be considered is whether the merger agreement could require that the board of directors affirmatively declare that the third-party beneficiary rights have vested, which would give the target's board even greater control over the settlement negotiations. Yet another possibility might provide that the stockholder claim can only be brought if the target's board has obtained a final judgment that the buyer breached the agreement but did not obtain specific performance. That approach would give the target's board the greatest control over whether to litigate with the buyer.

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[17] *Id.* § 251(b).

[18] *Id.*

[19] *See Aveta Inc. v. Cavallieri*, 23 A.3d 157 (Del. Ch. 2010); *see also Houseman v. Sagerman*, 2021 WL 3047165, at *6 (Del. Ch. July 20, 2021), *aff'd sub nom. Houseman v. Whittington*, 287 A.3d 227 (Del. 2022).

[20] *See In re Openlane, Inc.*, 2011 WL 4599662, at *3 (Del. Ch. Sept. 30, 2011) (noting that a merger agreement approved by a majority of stockholders by written consent appointed a stockholder's representative).

[21] In that situation, would the target update its disclosure accordingly and proceed with the stockholder vote on the theory that the agreement has not been validly terminated by the buyer?

[22] If a majority of the stockholders cannot bind all of the stockholders, it would still seem that the target could pursue lost-premium damages on behalf of those stockholders who did approve the agency appointment.

[23] *See* Tina L. Stark, *Negotiating and Drafting Contract Boilerplate* § 5.03 at 100 (2003) (noting that the contract can determine when the third-party beneficiary right vests).

- Adding Provisions to Organizational Documents. The court queried whether a charter provision could authorize the target to act as an agent in merger transactions.[24] Unfortunately, this will not be practicable for most existing public companies. It may also raise some drafting challenges when adopted in the abstract (*e.g.*, addressing which stockholders would receive the recovery if shares were transferred after the breach) and there may be timing considerations if adopted in connection with a specific transaction (*e.g.*, when the breach occurs before the vote on the charter amendment). In addition, a transaction structured as a tender offer would not involve a stockholder vote to approve a charter amendment. Practitioners might explore, however, whether this could pass muster as a board-adopted bylaw.[25]
- Reverse Termination Fees as Liquidated Damages. Targets may look to reverse termination fees as liquidated damages. This is a valid approach, but there are notable limitations on the size of the fee. Generally, a liquidated damages provision will be enforced when damages are difficult to calculate, the amount is a reasonable forecast of damages and the fee is not coercive or unconscionable.[26] Lost-premium damages, however, ordinarily will far exceed the amount of a customary reverse termination fee payable for, say, a regulatory or financing failure. Thus, if a reverse termination fee payable as liquidated damages for a buyer's willful breach is not large enough, it risks transforming the agreement into an "option" for the buyer. Factors that might support a larger than normal reverse termination fee in the context of a buyer's willful breach include the target's lost opportunities, the risk of losing customers and employees during the interim period, and the reputational harm of not consummating the transaction, along with out-of-pocket costs. Nevertheless, case law will place limits on the size of the fee that probably prevent it from approximating lost-premium damages.
- Legislative Response. Given the importance of this issue and the significant uncertainty it raises for public company M&A, the Delaware legislature could amend the DGCL to authorize corporations to pursue claims on behalf of their stockholders in connection with mergers and similar transactions.

Delaware Chancery Addresses Section 271 of DGCL's 'Substantially All of the Assets' Requirement

By John Jenkins, Managing Editor of DealLawyers.com

When I taught law school, I guaranteed each of my students that if they went into corporate law, at some point in their career they would be asked by a partner or other senior lawyer to research the issue of whether a particular transaction involved a sale of "substantially all" of a Delaware

[24] *Crispo* at 22 n.86.

[25] *See*, *e.g.*, 8 Del. C. § 109(b) ("The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees."). Although not directly on point, note that boards have often adopted forum-selection bylaws in connection with merger agreements that bind all stockholders.

[26] *Brazen v. Bell Atlantic Corp.*, 695 A.2d 43, 50 (Del. 1997).

corporation's assets, thus requiring stockholder approval under Section 271 of the Delaware General Corporation Law. America's law firms and law departments are extremely well stocked with such memos, almost all of which conclude with some mushy variation of, "Who knows?"

The reason for that conclusion is that Delaware case law in this area has historically not been a model of clarity, but the Court of Chancery's 2023 decision in *Altieri v. Alexy* does a better job than most in illuminating what asset transactions are likely to trigger a stockholder vote under Section 271. The funny thing about this decision is that it is not really a formal opinion — it is just an order, which does not have precedential value, but because Chancellor Kathaleen McCormick reviews key Delaware precedent and distinguishes the sale at issue in that case from those involved in cases cited by the plaintiff, it is nevertheless a helpful resource for thinking through the issues surrounding the "substantially all of the assets" question.

Section 271 of the DGCL

Section 271(a) of the DGCL requires stockholder approval of a sale of substantially all of the assets of a Delaware corporation.[1] The first thing you notice about this statute when you compare it to the merger statute is its brevity. Section 271 does not include the detailed procedural requirements that are contained in the provisions of the statute governing mergers. For example, Section 271 says nothing about what has to be in the asset purchase agreement and does not require any filings with the government for the transaction to become effective. It simply says that the board of directors has to deem the transaction expedient and in the best interests of the corporation, and the holders of a majority of the outstanding shares have to authorize it.[2]

In Delaware and in most other states, a sale of "substantially all" of a corporation's assets is regarded as being the kind of organic change that requires shareholder approval. But, since directors and management generally have dominion over the assets of a corporation, the question becomes, when does a sale of assets become the kind of organic event that shareholders have to approve?

If you answer that solely from a quantitative perspective, then companies like restaurants and supermarkets might have to start every day with a shareholders meeting since a big chunk of their assets consists of perishable inventory, which gets sold in a matter of days. Since this is the case, courts tend to evaluate whether a transfer involves "substantially all" of the assets in both quantitative and qualitative terms. In the leading Delaware case, *Gimbel v. Signal Companies*, the Chancery Court said that the answer depended on "whether the sale of assets is quantitatively vital to the operation of the corporation and is out of the ordinary and substantially affects the existence and purpose of the corporation."[3]

One of the challenges in applying the *Gimbel* test is assessing how its quantitative and qualitative components should be weighed in deciding whether a particular asset sale triggers a stockholder vote under Section 271.[4] It is the

[1] 8 Del. Code §271.

[2] *Id.*

[3] *Gimbel v. Signal Companies*, 316 A.2d 599 (Del. Ch. 1974).

[4] Perhaps the most perplexing decision in this regard is *Hollinger v. Hollinger International*, 858 A.2d 342, (Del. Ch. 2004), in which then-Vice Chancellor Leo Strine held that the sale of a "crown jewel" business representing more than 55% of a company's value did not trigger a stockholder vote under Section 271. In reaching this conclusion, he noted that the business represented less than half of the company's revenues and less than 40% of the book value of its assets. Taking these quantitative figures into account, he observed that "if the assets to be sold are not quantitatively vital to the corporation's life, it is not altogether apparent how they can 'substantially affect the existence and purpose of the corporation.'" *Id.* at 377.

relationship between these two prongs of the *Gimbel* test that Chancellor McCormick's effort to work through Delaware precedent and to distinguish the cases cited by the plaintiff in *Alexy* helps to illuminate.

Altieri v. Alexy: Sale Does Not Involve "Substantially All" of the Company's Assets

Alexy involved a challenge to cybersecurity firm Mandiant's sale of its FireEye line of business. The plaintiff contended that the transaction involved substantially all of Mandiant's assets and from a quantitative perspective, this excerpt from the order suggests that the plaintiff's claim appeared to be fairly strong:

> In 2019 and 2020, the FireEye Business accounted for 62% and 57% of the Company's overall revenue, respectively. Further, the Company's Form 10-Q for the fiscal quarter ended June 30, 2021, listed $1 billion in goodwill, approximately $500 million of which is alleged to be attributable to the FireEye Business. The FireEye Business also had a strong social media presence relative to Mandiant's other offerings.[5]

However, Chancellor McCormick noted that when evaluating quantitative metrics, no one factor is necessarily dispositive. Instead, the deal "must be viewed in terms of its overall effect on the corporation, and there is no necessary quantifying percentage."[6] Applying this standard, she concluded that the FireEye sale didn't satisfy the substantially all test, noting that the company's public filings indicate total assets of approximately $3.2 billion as of December 2020 and $3.1 billion as of June 30, 2021, and that the $1.2 billion sale price represented less than 40% of each of those figures.[7]

The Chancellor also concluded that the FireEye assets did not meet the substantially all test from a qualitative perspective:

> When considered qualitatively, the Sale does not satisfy the substantially-all test. Although the FireEye Business was an important aspect of Mandiant, Plaintiff has not pled that it affects the "existence and purpose" of the Company. Mandiant was a cybersecurity company before the Sale. It is a cybersecurity company after the Sale. Although selling the FireEye Business may alter course in how the Company operates, the change is not qualitatively so significant as to "strike a blow" to Mandiant's "heart." Although the Sale was out of the ordinary, it does not satisfy the "substantially all" test from a qualitative perspective.[8]

Applying *Gimbel*: Chancellor McCormick Shows Her Work

If Chancellor McCormick ended her discussion there, we would just have another bowl of judicial mush to add to the "substantially all" muddle. Fortunately, she did not do that. Instead, Chancellor McCormick addressed four Delaware decisions cited by the plaintiff in which the Delaware courts had to weigh qualitative and quantitative factors and distinguished those decisions from the facts of *Alexy*. She also addressed the reasons why her decision was consistent with the *Hollinger* decision.[9]

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[5] *Altieri v. Alexy*, CA No. 2021-0946-KSJM (Del. Ch. May 22, 2023) at 2.

[6] *Id.* at 6.

[7] *Id.* at 7.

[8] *Id.* at 7-8.

[9] *Id.* at 7-12.

The cases cited by the plaintiff in support of her argument that the quantitative and qualitative aspects of the FireEye sale were sufficient to characterize it as involving a sale of substantially all of Mandiant's assets were *Katz v. Bregman*, 431 A.2d 1274, 1275–76 (Del. Ch. 1981); *Thorpe v. CERBCO, Inc.*, 1995 WL 478954, at *9 (Del. Ch. Aug. 9, 1995); *B.S.F. Co. v. Phila. Nat'l Bank*, 204 A.2d 746, 750 (Del. 1964); and *Winston v. Mandor*, 710 A.2d 835 (Del. Ch. 1997).

Chancellor McCormick found all four cases to be distinguishable. She noted that in the first case, *Katz*, the court determined that a deal that was not outsized from a quantitative perspective satisfied the substantially all test based primarily on qualitative factors. The business line being disposed of in that case represented only 51% of the company's assets, 45% of its revenue and 52% of its pre-tax net operating income, but the sale involved an effort by the company to "shift its overall business strategy by 'embark[ing] on the manufacture of plastic drums' that 'represent[ed] a radical departure from [the company's] historically successful line of business, namely steel drums.'"[10]

In contrast, she concluded that the sale of the FireEye line of business did not involve a "stark departure" from the company's traditional line of business. The company's business focused on cybersecurity services before and after the sale of FireEye, and it retained several additional businesses following its divestiture. *Katz* is distinguishable, because the transaction at issue in this case did not represent a stark departure from the company's historic line of business. As the Chancellor put it, "Mandiant was a cybersecurity company before the Sale. It is a cybersecurity company after the Sale. Although selling the FireEye Business may alter course in how the Company operates, the change is not qualitatively so significant as to 'strike a blow' to Mandiant's 'heart.'"[11]

Turning to the next two cases cited by the plaintiff, *Thorpe* and *B.S.F.*, the Chancellor noted that in both cases, quantitative factors resulted in the court concluding that the transactions involved substantially all of the assets. *Thorpe* involved the sale of a subsidiary pipeline services business representing 68% of the company's overall assets and the parent company's "primary income generating asset"[12] and absent the subsidiary's business, the parent holding company "would have been left with a substantial amount of cash, a small subsidiary that was about to be liquidated, and a single operating company … that was minimally profitable."[13] Similarly, in *B.S.F.*, the asset sale at issue involved 75% of the company's assets and represented its "only substantial income [] producing asset[.]"[14]

Chancellor McCormick distinguished *Thorpe* and *B.S.F.* based on the fact that the quantitative metrics involved in the FireEye transaction were not nearly as compelling. Although the revenue metrics were similar, only 38% of Mandiant's assets were represented by the FireEye business and the plaintiff did not plead facts suggesting that the company was left without the ability to generate income as a result of the sale. In that regard, she noted that Mandiant realized total revenues of nearly $122 million in the fiscal quarter following the divestiture.[15]

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[10] *Id.* at 5, citing *Katz*.

[11] *Id.* at 7.

[12] *Id.* at 9, citing *Thorpe*.

[13] *Id.* at 9, citing *B.S.F.*

[14] *Id.*, citing *B.S.F.*

[15] *Id.* at 9-10.

While the outcome in *Katz* turned primarily on qualitative factors and the outcome in *Thorpe* and *B.S.F.* turned primarily on quantitative factors, in the final case cited by the plaintiff, *Winston*, both qualitative and quantitative factors led the court to conclude that it was reasonably conceivable that a sale involved substantially all of the company's assets. The plaintiff in *Winston* alleged that the sale resulted in a shift in the company's primary business away from direct ownership of real property to ownership of real-estate related securities, and that the assets involved in the sale represented 60% of the company's net assets.[16]

Chancellor McCormick distinguished the sale at issue in *Winston* from the one challenged in *Alexy* in two ways. First, the FireEye divestiture did not fundamentally change Mandiant's "core practice in the cybersecurity space."[17] Furthermore, as previously noted, the FireEye business represented only 38% of the company's net assets, much less than the 60% involved in *Winston*.[18]

After distinguishing the decisions that the *Alexy* plaintiff pointed to as supporting her argument that the FireEye divestiture involved substantially all of Mandiant's assets, she turned to another key Delaware precedent that the plaintiff attempted to distinguish from her situation — then-Vice Chancellor Strine's decision in *Hollinger*. In that case, Vice Chancellor Strine held that a media company's sale of its Telegraph Group asset did not require stockholder approval under Section 271. He reached that conclusion despite the fact that the Telegraph Group was the company's "single most valuable asset" and accounted for more than 55% of the company's overall asset value.[19]

He observed that from a qualitative perspective, even after the sale, the company's stockholders would remain investors in a business with profitable operating assets, including "a well-regarded tabloid newspaper of good reputation and large circulation, a prestigious newspaper in Israel, and other valuable assets." Accordingly, although the sale of the Telegraph Group was "important," it did not "strike a blow to [the company's] heart" — even if it was the company's single most valuable asset.[20]

In reaching this conclusion, the Vice Chancellor pointed out that the Telegraph Group assets involved in the sale accounted for less than half of the company's revenues and represented less than 40% of its book value. Essentially, the Vice Chancellor concluded that to require a vote here would be to transform the "substantially all" requirement into an "approximately half" requirement, which he declined to do.[21]

Chancellor McCormick concluded that the sale of the FireEye business was similarly important to Mandiant's business, but, like the divestiture at issue in *Hollinger*, did not strike a blow to the company's heart. She rejected various efforts by the plaintiff to distinguish *Hollinger*, including the plaintiff's argument that "the presence of strong qualitative factors weighing in her favor distinguishes *Hollinger*, which—unlike here—was not a close call on the qualitative dimension of the *Gimbel* test."[22] In particular, she noted that

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[16] *Id.* at 10.

[17] *Id.* at 11.

[18] *Id.*

[19] *Hollinger*, 858 A.2d at 379-380.

[20] *Id.* at 385.

[21] *Id.* at 386.

[22] *Alexy* at 12.

the qualitative analysis did not weigh in Plaintiff's favor, since, as discussed above, the FireEye business was just one part of the company's corporate identity and the complaint did not support a reasonable inference that it was the "heart" of the company's existence and purpose.[23]

Key Takeaways from *Altieri v. Alexy*

Decisions about whether a stockholder vote under Section 271 will be triggered by a particular asset transaction will always involve an intensely fact-based inquiry. Nevertheless, Chancellor McCormick's review of Delaware precedent in *Alexy* does provide insights that are helpful to keep in mind when considering that issue.

- Satisfying the Qualitative Prong Requires a "Fundamental Shift" in Business. If a plaintiff is to prevail on an argument premised primarily on qualitative factors, Delaware precedent indicates that the asset transaction at issue must involve a fundamental change in the business in which the stockholders have invested in order to trigger a stockholder vote. *Alexy* and *Hollinger* make it clear that simply disposing of a crown jewel asset, even if that asset represents more than half of the company's value, revenue or operating income, will not always be sufficient to trigger a stockholder vote if the court concludes that there has not been an accompanying fundamental change in its operations that "strikes at the heart" of the company's business.
- Shifts in Degree vs. Shifts in Kind. Chancellor McCormick's review of precedent indicates that a transaction may "strike at the heart" of the company's business for purposes of *Gimbel's* qualitative prong if it involves a fundamental change in either the scope of its business operations or in the kind of business that it operates. However, *Alexy* and the precedent the Chancellor sites in that decision suggest that if quantitative factors are also not compelling, a fundamental change in the *kind* of business the company operates is more likely to satisfy *Gimbel's* qualitative side.

  For example, in *Katz*, a sale of 51% of the company's assets was sufficient to trigger a stockholder vote, because the court concluded that the deal also involved a fundamental change in the kind of business the company conducted. The court characterized the associated departure from the company's metal drum business and its decision to embark on the manufacture of plastic drums as involving a "radical departure" from its overall business strategy.

  In contrast, the *Hollinger* case involved a change in the scope of the company's business, but not in the kind of business the company operated. In concluding that a stockholder vote was not required, Vice Chancellor Strine noted that although the company disposed of a crown jewel asset representing more than 55% of its value, after the sale, it retained substantial operations in the same general business that it had operated in historically.
- Quantitative Prong Considers Multiple Metrics on a Holistic Basis. The language of Section 271 focuses on whether a transaction involves a sale of substantially all of the company's assets, but the metrics Delaware courts will use to evaluate that issue go beyond the balance sheet. While

[23] *Id.* at 12-13.

the relative book value of the assets being disposed of and those being retained will be evaluated, so will the overall market value of those assets and the percentage of the overall market value of the company that they represent. In addition, the percentage of revenues and operating income attributable to those assets, and the company's ability to generate income going forward after the sale, are additional factors that may be considered by the Delaware courts in deciding whether a stockholder vote is required.

It does not appear that any one quantitative metric is necessarily dispositive, but that Delaware courts will consider them holistically, as part of an evaluation of whether the company remains able, after the transaction, to conduct a viable business operation. The logical corollary of this is that, as the precedent reviewed by Chancellor McCormick highlights, the greater the size of the transaction across a variety of key metrics, the more likely it is that *Gimbel's* quantitative prong will be satisfied.

- Neither the Quantitative nor Qualitative Prong Stands Alone. The cases cited in *Alexy* make it clear that, in most cases, neither the quantitative nor qualitative prong of the *Gimbel* test will stand alone; however, it also seems fair to say that qualitative factors will need to be particularly robust to trigger stockholder approval of a transaction that is borderline from a quantitative perspective, and that when a transaction is large from a quantitative perspective, the hurdles imposed by the qualitative side of *Gimbel* are easier to surmount.

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