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Delaware Insider:

Court of Chancery Orders a "Fairer Price" Based on Controller's Malfeasance

By Joanna J. Cline, James H.S. Levine and Christopher B. Chuff

In a recent post-trial opinion, Vice Chancellor J. Travis Laster of the Delaware Court of Chancery held that a company's CEO and controlling stockholder, and the company's president, COO, and general counsel, who was working for the benefit of the controlling stockholder, breached their fiduciary duties by obstructing the work of an independent committee in connection with the controlling stockholder's effort to take the company private. In *In re Dole Food Company, Inc.*, the court found the controller, David Murdock, and his top lieutenant, C. Michael Carter, jointly and severally liable for over $148 million in damages in connection with their efforts to interfere with and obstruct the independent committee of Dole's board that considered (and ultimately recommended) the going-private transaction. That award represents $2.74 per share, a 20.4 percent premium over the proposal amount of $13.50. Vice Chancellor Laster concluded that Murdock and Carter had acted in bad faith, and that Carter had committed outright fraud. Because fiduciary breaches of this nature are neither exculpable nor indemnifiable under Delaware law, Murdock and Carter are personally liable for the damages imposed.

Background

Murdock's history with Dole began in 1985, when a company of which he was CEO merged with Dole's parent. In 2003, Murdock took Dole private in a leveraged buyout. The company and Murdock both felt the squeeze of the 2008 financial crisis, and Dole was forced to refinance its debt at a very high interest rate. To pay down the company's debt (and Murdock's personal debt), Dole conducted an initial public offering in October 2009, which reduced Murdock's ownership stake in the company from 100 percent to approximately 40 percent.

But Murdock was not satisfied with partial control of Dole. Witnesses testified that he "seemed frustrated with boards," and the court concluded that he "was an old-school, my-way-or-the-highway controller, fixated on his authority and the power and privileges that came with it." Beginning in 2011, Murdock began the machinations to take Dole private once again. He planned to separate two of the company's three businesses, buy out the remaining stockholders, and run the third business privately. The first steps of the plan came to fruition in 2012 and 2013. The company sold two of its businesses, and Murdock and Carter became CEO and president, respectively.

The court determined that after his appointment as president, Carter deliberately and calculatingly depressed Dole's stock price to facilitate Murdock's proposed going-private transaction. He publicly underestimated potential cost savings and undervalued certain of the company's assets, portraying Dole as less valuable than it was. Carter next cancelled a board-approved share repurchase plan without informing the board, claiming that the company could not afford to continue the plan while also embarking on additional capital expenditures to support its operations. Vice Chancellor Laster determined, however, that Carter's explanation was pretextual, and that the company could have proceeded with both the share repurchase and the capital expenditures. Dole's stock price tumbled by 10 percent or more after each of Carter's announcements.

While Carter was actively working to devalue Dole's stock, Murdock proposed to acquire all of the company's shares that he did not own for $12.00 per share (the stock then traded at $10.20 per share, due to Carter's efforts). Murdock's proposal was conditioned upon (1) the approval of a special committee consisting of disinterested and independent Dole directors, and (2) an affirmative majority-of-the-minority stockholder vote, which the Court of Chancery in *In re MFW Shareholders Litigation*, C.A. No. 6566, (May 29, 2013) deemed necessary conditions to preserve business judgment review of a going-private transaction involving a controlling stockholder. Murdock's proposal also described Murdock as "a buyer, not a seller" to prevent the board from seeking a higher bid from a third party interested in buying the entire company.

The board formed the special committee, which engaged independent legal and finan-

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cial advisors, and ultimately negotiated an increase in Murdock's offer to $13.50 per share, which fell toward the higher end of the special committee's financial advisor's valuation range. The committee, believing it had negotiated the highest possible price, recommended Murdock's proposal to the board. The proposal also contained a 30-day go-shop period, and provided for a minimal breakup fee. The board approved the proposal, and no competing bidder emerged during the go-shop period. A scant majority – 50.9 percent – of the minority stockholders approved the buyout, and the transaction closed on November 1, 2013.

Plaintiffs brought suit, arguing that the merger was not entirely fair and that Murdock, Carter, and others had breached their fiduciary duties.

The Court's Ruling

Vice Chancellor Laster concluded that although Murdock and Dole had enacted the safeguards prescribed by *MFW*, and that the special committee was independent and took its job seriously, the process was inescapably tainted by Murdock and Carter's interference and misconduct. Specifically, the court concluded that Carter, acting in furtherance of Murdock's efforts to pay the lowest price possible, provided financial information to the special committee that contained numerous false statements or omitted material information, and which deviated substantially from the data the company had distributed to the board a few weeks prior to the special committee's deliberations, and that he repeatedly refused to comply with the special committee's directives.

The court determined that Carter's misconduct rose to a fraudulent level, which permeated the entire process and "rendered useless and ineffective the highly commendable efforts of the Committee and its advisors to negotiate a fair transaction that they subjectively believed was in the best interests of Dole's stockholders." Carter intentionally took measures to depress Dole's stock price to make it cheaper for Murdock to eliminate the minority stockholders. He deliberately misled the market about the company's potential cost savings, and unilaterally cancelled the stock repurchase program, even though the company was financially able to support it contemporaneously with the capital expenditures. Carter's fraud vitiated the entire process, rendering it necessarily unfair to Dole's stockholders.

Carter further intentionally deceived the special committee about the true nature of the company's financial picture, withholding pertinent information about Dole's cost savings and expected increases in EBITDA from its operations. The projections the company's management prepared at Carter's direction were "knowingly false. Carter intentionally tried to mislead the Committee for Murdock's benefit."

Although the merger price fell within the range of fairness established by the special committee's financial advisor, the court concluded that Carter's fraud made it impossible for the committee to develop an accurate valuation of Dole, and that had the committee had accurate information, its valuation likely would have been quite different. "If the Committee and Lazard [the financial adviser] had not been misled, then the Committee's negotiations and Lazard's analysis would have provided powerful evidence of fairness. But Carter's actions tainted both the negotiation process and Lazard's work product." Carter's subterfuge made it impossible for the special committee and its financial advisor to do their jobs, which resulted in an inaccurate valuation of the company. "[A]ssuming for the sake of argument that the $13.50 price still fell within a range of fairness, the stockholders are not limited to a fair price. They are entitled to a fairer price designed to eliminate the ability of the defendants to profit from their breaches of the duty of loyalty. . . . By engaging in fraud, Carter deprived the Committee of its ability to obtain a better result on behalf of the stockholders, prevented the Committee from having the knowledge it needed to potentially say 'no,' and foreclosed the ability of the stockholders to protect themselves by voting down the deal."

Vice Chancellor Laster found Murdock liable both as a controller and as a director. As a controlling stockholder, he derived an improper personal benefit from the transaction, and as a director, he breached his duty of loyalty by "orchestrating an unfair, self-interested transaction." He further found Carter liable as an officer and a director, as he knew about Murdock's buyout plan and consistently acted to promote Murdock's interest instead of the best interests of Dole and its stockholders. Although Dole's certificate of incorporation indemnifies directors to the extent permitted by Delaware law, the court noted that the nature of Murdock and Carter's breaches as directors was not subject to the protections of the exculpation clause, and that neither of them could be exculpated for their breaches as controlling stockholder and officer, respectively. Both were held personally liable for their bad faith conduct to the detriment of the company and its stockholders.

Conclusion

Unlike in *In re Trados Inc. Shareholder Litigation* where the court concluded that the unfair sale process still resulted in a fair price, *In re Dole Food Company, Inc.* demonstrates that Delaware courts will not hesitate to award substantial damages to stockholders where the unfairness of a sale process is caused by bad faith and fraud. "[W]hat the stockholder vote could not cleanse, and what even an arguably fair price does not immunize, is fraud." Controlling stockholders who seek to cleanse their transaction by following the *MFW* safeguards must conform to not only the form, but the substance of those procedures to enjoy the protection of the business judgment rule.

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