M&A Perspectives

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Troutman Sanders is pleased to present its latest issue of *M&A Perspectives*, a publication featuring analysis of U.S. mergers & acquisitions market and legal developments.

Table of Contents

M&A Buyers Say #MeToo 3
Spotting Bigfoot: The Mythical MAE 5
Recent CFIUS Reform 11
Recent Developments in Delaware Law 14
Troutman Sanders by the Numbers 18
Recent Transactions 19

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M&A Buyers Say #MeToo

By: Coby Beck, Clayton De Arment and Sarah Rust Pylant

Over a year into the #MeToo movement, the impact has been significant. The Weinstein Company LLC is bankrupt, a U.S. senator and several congressmen have resigned and dozens of figures in the public eye with substantial employment contracts have been removed from their posts. Companies and their shareholders have felt the ramifications of #MeToo claims.

Fortune 500 companies have lost billions of dollars in market capitalization, had senior executives forced out and suffered employee walkouts. Significant financial and reputational damages resulting from #MeToo claims have led to corporate M&A attorneys advising clients as to proactive measures to avoid or mitigate future #MeToo damages. These measures include targeted due diligence and the inclusion of "Weinstein clauses" in acquisition agreements and key executive employment agreements.

With respect to #MeToo claims, as with other areas of risk, due diligence serves as the first step in appropriately allocating liability between a seller and a potential buyer in M&A transactions. If a buyer is able to identify existing or contingent liabilities as part of its due diligence, the buyer in a private company transaction can exclude the liability or seek a specific indemnity related to the liability. In a public or private company acquisition, the buyer can factor an identified #MeToo liability into its valuation of the target and its decision as to whether to proceed with the transaction. A buyer's due diligence traditionally includes reviewing the target's employment policies and practices as well as past and pending claims and litigation. The #MeToo movement has highlighted the need for a buyer to also consider conducting due diligence focused on understanding a target's corporate culture, conducting background checks on key executives and identifying the target's use of settlement agreements and non-disclosure agreements stemming from allegations of sexual harassment or sexual misconduct. This level of due diligence is particularly important if the target's business (a) is well-known to the public (media, entertainment, etc.), (b) is in a traditionally male-dominated field (e.g., technology), or (c) is closely identified by its "celebrity CEO" or otherwise has notable individuals on its board, in its executive ranks or in its advertising. Due diligence lists, investigations and reviews should be modified to incorporate these specific #MeToo concerns.

The acquisition agreement provides another opportunity for buyers to allocate liability stemming from #MeToo claims. The representations and warranties in an acquisition agreement generally serve as part of a buyer's due diligence process as well as a way to allocate risk between the buyer and the seller. With respect to sexual misconduct

#MeToo claims are often rooted in allegations and internal company complaints that may have occurred in the distant past and may not have risen to the level of a pending or threatened claim against the target.

claims, acquisition agreement representations and warranties typically address pending and threatened claims under labor and employment laws and often address historical claims for a limited look-back period. However, in today's environment, these traditional representations and warranties may not provide sufficient protection for a buyer. #MeToo claims are often rooted in allegations and internal company complaints that may have occurred in the distant past and may not have risen to the level of a pending or threatened claim against the target. The potential risk to a buyer is no longer determined by whether the target may have exposure to a potential claim during the applicable statute of limitations period. The risk now includes fundamental and reputational risk that is not bound by time.

To address the heightened risk to buyers of past sexual misconduct by a target's representatives, M&A practitioners have started to require representations and warranties that are commonly referred to as "#MeToo representations" or "Weinstein clauses." Although the language of these representations varies, these clauses generally exceed the traditional representations regarding pending or threatened employment law claims to specifically include any allegations of sexual harassment or misconduct looking back for much longer periods of time or even indefinitely.

Here is an example of such a representation in a recent public company transaction:

> *"To the Knowledge of the Company, (i) no allegations of sexual harassment have been made against (A) any officer or director of the Company or any of its Subsidiaries or (B) any employee of the Company or any of its Subsidiaries who, directly or indirectly, supervises at least eight (8) other employees of the Company or any of its Subsidiaries, as applicable, and (ii) neither the Company nor any of its Subsidiaries has entered into any settlement agreement related to allegations of sexual harassment or sexual misconduct by an employee, contractor, director, officer or other representative."*[1]

As is the case with all representations and warranties, the buyer and seller will be faced with the typical negotiating points with respect to this representation—the duration of the look-back period: the scope of the "Knowledge" definition; the appropriateness of materiality qualifiers; and, in non-public transactions, how the #MeToo representation is addressed in the indemnification provisions with respect to survival, baskets, caps, escrows and the like.

We recommend that buyers in M&A deals consider the potential financial and reputational damage that could reasonably be expected as a result of a #MeToo claim and then ensure that the due diligence process appropriately investigates the potential risks. Similarly, a buyer that identifies meaningful risk in the due diligence process from such a claim should include a "#MeToo representation" and, in a private company transaction, related indemnification. In a public company transaction, the buyer will need to carefully consider any identified risks as part of its valuation of the target and its decision whether to proceed with the transaction given that indemnification is generally not available. «

[1] Midatech Pharma PLC. (2018). September 27, 2018, Form 6-K. Retrieved from www.sec.gov/edgar.shtml.

Spotting Bigfoot: Delaware Court of Chancery Finds the Mythical Material Adverse Effect

By: Sean Ehni

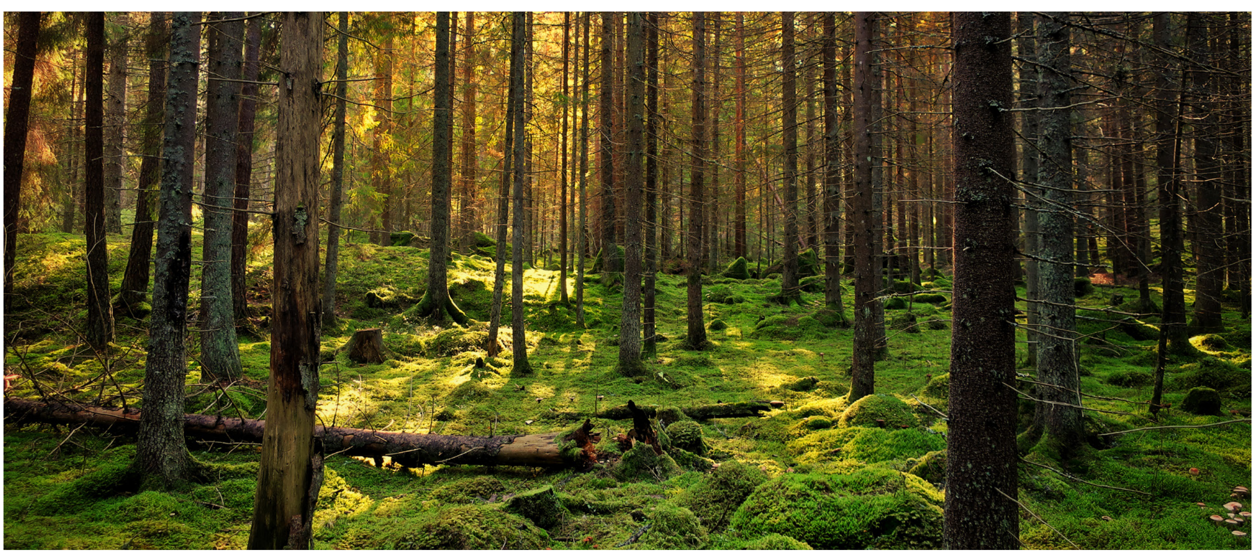
In most M&A transactions, material adverse effects (MAE) clauses, are utilized in representations and warranties and closing conditions as a risk allocation tool and to narrow diligence issues. MAEs are rarely expected to be operative or used by one party to terminate a merger or acquisition agreement. One former colleague, an experienced M&A attorney, routinely waved away MAEs as largely irrelevant, saying, “I’ve never seen Bigfoot, and I’ve never seen an MAE,” emphasizing that we should save our dry powder for more important negotiated points.

However, the Delaware Court of Chancery recently found Bigfoot. In *Akorn, Inc. v. Fresenius Kabi AG*, C.A. No. 2018-0300-JTL (Del. Ch. Oct. 1, 2018), the Court held for the first time that a buyer properly terminated an acquisition agreement on the basis of an MAE and refused the seller’s request for specific performance of the merger agreement. In a one-page ruling on December 7, 2018, the Delaware Supreme Court affirmed the lower Court’s *Akorn* decision. In this article, we describe the background of *Akorn*, analyze the Court’s decision and provide some key takeaways for negotiating future M&A transactions under Delaware law.

Background

The Deal

On April 24, 2017, Fresenius Kabi AG, a German pharmaceutical company, agreed to acquire Akorn, Inc., an Illinois-based publicly traded specialty generic pharmaceutical company, in an all-cash deal where each share of Akorn stock would be converted into the right to receive a cash payment of $34 at closing. As is customary, Fresenius’s obligation to close was conditioned on Akorn’s representations having been true and correct both at signing



and closing, except where failure to be true and correct would not reasonably be expected to have an MAE. Fresenius's obligation to close was also conditioned on Akorn not having suffered an MAE in the interim period between signing and closing. Akorn also agreed to use commercially reasonable efforts to continue to operate its business in the ordinary course after signing.

Akorn's Decline

In the quarter after signing, Akorn's business performance quickly deteriorated. Akorn announced year-over-year declines for the quarter of 29% in revenue, 84% in operating income and 96% in earnings per share. Akorn's executives attributed the poor results to unexpected new market entrants competing with Akorn's key products. This competition exceeded Akron's projections in its 2017 forecast. Fresenius executives met with Akorn management to understand the nature of the decline and began to explore Fresenius's options under the merger agreement, including possible termination of the agreement. Akorn management assured Fresenius that the downturn was only temporary, but Akorn's performance continued its downward trajectory in July and August of 2017.

Regulatory Compliance Issues

In late 2017, Fresenius received several letters from anonymous whistleblowers asserting that Akorn's product development process failed to comply with regulatory requirements, including with respect to FDA regulations. Akorn was an FDA-regulated company, so these allegations were particularly concerning and called into question the accuracy of Akorn's regulatory compliance representations and warranties and whether Akorn had breached its covenant to operate in the ordinary course of business. Fresenius began investigating the allegations and uncovered serious and pervasive data integrity problems. Fresenius concluded that Akorn's representations and warranties about its regulatory compliance would reasonably be expected to result in an MAE and that Akorn had failed to conduct its business in the ordinary course.

As the Court noted, employees in Akorn's quality and IT functions were informed that some of the 2017 quality control initiatives would cease as a result of the pending acquisition.

Akorn also made fundamental changes to its quality control and information technology processes without the consent of Fresenius. As the Court noted, employees in Akorn's quality and IT functions were informed that some of the 2017 quality control initiatives would cease as a result of the pending acquisition. This included replacing certain regular internal audits with "verification" audits, which were less stringent and focused only on addressing prior audit findings as opposed to identifying any potential new issues.

Fresenius Demands Out

In April 2018, Fresenius sent Akorn a letter stating that the conditions to closing could not be met and identifying Fresenius's contractual bases for terminating the merger agreement. In an effort to help resolve the issues, Fresenius offered to extend the outside date by which the merger could be closed if Akorn believed further investigation could help resolve its difficulties. Akorn declined, however, and Fresenius gave notice it was terminating the merger agreement shortly thereafter. Fresenius terminated the merger agreement on three grounds:

1. Akorn's representations regarding regulatory compliance were so incorrect as would reasonably be expected to result in an MAE;

2. Akorn had suffered a general MAE; and
3. Akorn failed to use commercially reasonable efforts to operate in the ordinary course of business.

Analysis

The Court ruled that Fresenius validly terminated the merger agreement on all three grounds, and that Fresenius had not been in material breach of its own obligations under the agreement.

Regulatory Compliance MAE

The Court conducted a qualitative and quantitative analysis of Akorn's compliance with its regulatory representations and warranties. The standard analysis for determining if an MAE has occurred is whether the alleged violation would be considered "material when viewed from the longer-term perspective of a reasonable acquirer."

In its qualitative analysis, the Court determined that compliance with FDA regulatory requirements was essential to Akorn's business because the value of Akorn's existing and developing products depended on its ability to meet FDA requirements.

In its quantitative analysis, the Court extensively reviewed the financial impact of Akorn's pervasive regulatory compliance issues. The Court concluded that $900 million was the most credible estimate of the financial impact of Akorn's data integrity issues, or 21% of the implied $4.3 billion equity value of Akorn under the terms of the merger agreement. After a lengthy discussion of what would be considered "material" under Delaware law and in the broader corporate context, the Court concluded that "an expense amounting to 20% of Akorn's value would be material to a reasonable acquirer," and that, as a result, the regulatory issues would reasonably be expected to result in an MAE. However, the Court took great pains to emphasize that under no circumstances should 20% be viewed as establishing a bright-line test or that revenue and profitability metrics are determinative to an MAE analysis.

General MAE

The Court described general MAE clauses as a risk allocation device, typically allocating general market or industry risk to the buyer and target-specific risks to the seller. As noted above, with respect to a general MAE, the standard is whether the MAE is "material when viewed from the longer-term perspective of a reasonable acquirer." The Court explained that a buyer "faces a heavy burden when it attempts to invoke a material adverse effect clause in order to avoid its obligation to close," and "a short-term hiccup in earnings should not suffice." In order for an MAE to exist, the effect in question should substantially affect the overall earnings potential of the target in a "durationally-significant manner," which requires an intensive fact-based inquiry accounting for many variables, including seasonality, industry trends and a detailed analysis of the target's business.

The Court analyzed the decline in Akorn's business and found it to be durationally significant due to the decline in revenue, operating income and earnings per share in each of five straight quarters. The Court also noted that the decline showed "no sign of abating" based on contemporary analyst valuations of Akorn at between $5 and $12 per share, a far cry from the $34 per share offered by Fresenius. Akorn's peers had not endured a similar decline, which supported Fresenius's case.

Akorn presented a counterargument asserting that its decline in performance should be assessed against its synergistic value to Fresenius, as opposed to as a standalone entity. The Court flatly rejected this argument and cited the language of the merger agreement that the MAE referred to the "results and operations of the Company and its Subsidiaries, taken as a whole." In the Court's view, if the parties wanted the MAE to apply to the synergistic value of Akorn to Fresenius, it would have said so and referenced the combined company.

The Court also rejected Akorn's argument that it was the victim of an industry-wide decline, which was a risk assumed by Fresenius under the terms of the merger agreement. According to the Court, Akorn's decline was disproportionate to its peers and a specific business risk that should be borne by the target company. Major contributors to Akorn's decline were new market entrants and the loss of a key customer contract, both of which were specific to Akorn and not industry-wide concerns.

Ordinary Course Covenant Failure

In the merger agreement, Akorn committed to use "commercially reasonable efforts to carry on its business in all material respects in the ordinary course of business." The Court broke this obligation down into its component parts and determined that Akorn had breached this covenant, leaving Fresenius free to validly terminate the merger agreement.

First, the Court discussed what “in all material respects” means when considering the breach of a covenant. The Court relied on a formulation familiar in securities law and held that “in all material respects” requires only a “substantial likelihood that the…[breach] would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information.” The Court noted, however, that this was a lower standard than the MAE built into the regulatory compliance representation.

Second, the Court discussed what “commercially reasonable efforts” entail. The Court summarized the common distinctions M&A attorneys make between different efforts standards, including “best efforts," “reasonable best efforts,” “reasonable efforts,” “commercially reasonable efforts,” and “good faith efforts.” The Court found these distinctions essentially meaningless and not supported by case law. Instead, the Court reaffirmed the Delaware Supreme Court’s view that efforts covenants in general “impose obligations to take all reasonable steps” in order to accomplish the applicable action. In the case of Akorn, the covenant required that Akorn "'take all reasonable steps' to maintain its operations in the ordinary course of business.”

Finally, the Court applied the standards above to the facts and determined that Akorn had indeed breached the ordinary course covenant. The Court focused on Akorn’s most egregious actions, including its departure from its regular audit assessments, failure to maintain data integrity and submission of FDA regulatory filings based on fabricated data. The Court concluded that Fresenius would not have agreed to buy Akorn if it understood that Akron would not address these issues in the interim period between signing and closing, which altered the total mix of information available to Fresenius at the time of the merger agreement and which made the breach material. The Court also doubted that the breach was curable since Akorn estimated it would take three years to cure its regulatory issues, well beyond the bounds of the outside date for completion of the merger.

Key Conclusions

MAEs Remain a Fact-Intensive Inquiry

Despite the Court’s ruling, it seems unlikely that we will see a marked increase in MAE terminations in the future. Buyers still bear a heavy burden to prove an MAE has occurred, and the Court emphasized that it was not setting any bright-line standards or blazing a new trail. Any dispute over an MAE will be fact-intensive and require egregious circumstances for the Court to determine that an MAE exists. As noted, a temporary dip in financial performance is insufficient to trigger an MAE. The decline must be serious and sustained. Therefore, buyers should not begin looking for an exit based on a single quarter of poor target financial results, and sellers likewise should not worry if poor results are seasonal or cyclical or if the seller’s performance fluctuates consistent in magnitude with a broader industry trend.

MAEs Can Be Operative, but Buyers Should Monitor Their Conduct

Buyers can take comfort that MAEs, under the right circumstances, are enforceable and operative under Delaware law. If the facts are egregious enough, buyers may be able to validly terminate an agreement based on an MAE. However, buyers should take care to monitor their own conduct between signing and closing to ensure they are not vulnerable to a seller counterclaim that the buyer is merely experiencing buyer’s remorse or looking for any way to exit the deal. TThe Court took special note of Fresenius’s conduct throughout the process and emphasized that Fresenius attempted to cooperate and work with Akorn while Akorn experienced business and regulatory difficulties, largely of its own making. Fresenius also explored its options under the merger agreement but continued to publicly affirm the transaction and perform its obligations. It may be a fine line between exploring termination rights under the merger agreement and actively trying to scuttle a deal, so buyers would do well to consult with legal if there is the possibility of an MAE or a violation of an MAE-qualified representation in the interim period between signing and closing.

Sellers Shouldn't Count Their Chickens

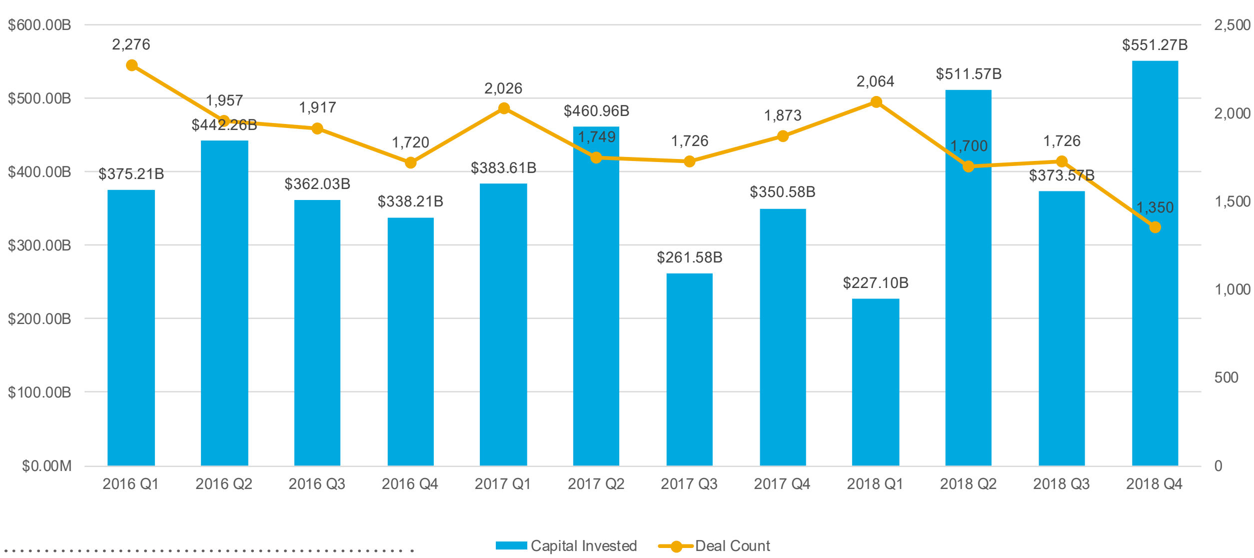
Sellers should be cognizant that MAEs are not a get out of jail free card. The Court in Akorn determined that a 20% decline in the target's total equity value based on a violation of a representation resulted in an MAE. While the Court emphasized this was in no way a bright-line test, this threshold is the only guidepost we have under Delaware law and will be one baseline for future MAE-related litigation. Additionally, Akorn did itself no favors here. It attempted to paper over the cracks in its compliance regime and actively departed from its prior internal audit procedures, practically inviting the Court to make its ruling. A seller may help avoid a similar outcome by operating as if it would continue to be a standalone company in the future, including adapting to changing business environments, as opposed to halting certain compliance functions due to a major pending transaction. If major changes are contemplated, communication with the buyer is essential and a seller should err on the side of requesting consent from the buyer to make such changes.

One Effort Standard

The Court also indicated that the traditional hierarchy of efforts standards employed by M&A attorneys ("best efforts," "reasonable best efforts," "reasonable efforts," "commercially reasonable efforts," etc.) may be irrelevant. It did not distinguish between the various efforts standards and instead applied a single standard that requires a party to "take all reasonable steps" to adhere to its obligations. This may save buyers and targets some time and fees in the future as M&A attorneys may no longer have to spend the time (and brain damage) arguing over the various efforts distinctions.

However, the Court did recognize that hell-or-high-water clauses were a separate standard and still required Fresenius to "take all actions necessary" to secure antitrust approval of the transaction. Therefore, it seems we may be moving to a two-tier standard comprised of reasonable efforts on the one hand and a hell-or-high-water clause on the other. «

U.S. M&A Market Snapshot: Capital Invested & Deal Count



Source: PitchBook

Recent CFIUS Reform Sets the Stage for Increased Restrictions on Foreign Investments

By: Kevin Christmas, Dan Anziska and Brett Hubler

The Committee on Foreign Investment in the United States (CFIUS) has undergone recent reforms that increase restrictions on foreign investment in U.S. businesses. The reforms will require certain mandatory filings for specified transactions in a wide range of industries, significantly expanding the reach of what was previously a voluntary process with a more limited scope. In this article, we discuss certain aspects of these reforms and the implications for M&A transactions going forward.

The CFIUS Regulatory Framework and Reform

CFIUS is an interagency body comprising nine members and chaired by the Secretary of the Treasury. The committee reviews certain transactions involving foreign investment in the U.S. As a result of that review, the president may suspend or block transactions that present a risk to U.S. national security.

Although CFIUS has the power to initiate review unilaterally, CFIUS disclosure historically has been considered voluntary and somewhat limited in application. However, following the recent passage of the Foreign Investment Risk Review Modernization Act (FIRRMA) and the Department of the Treasury's introduction of a pilot program implementing certain temporary regulations under FIRRMA (the "Pilot Program"), CFIUS's jurisdiction has been significantly expanded and filings are now mandatory for "pilot program covered transactions." Failure to comply with the mandatory filing requirements can result in stiff penalties up to an amount equal to the value of the transaction in question.

"Pilot program covered transactions" include (i) any transaction that could result in foreign control of a "pilot program U.S. business" and (ii) certain non-controlling, non-passive investments by foreign persons in a "pilot program U.S. business."

The Pilot Program broadly defines a "pilot program U.S. business" as any U.S. business that produces, designs, tests, manufactures, fabricates or develops critical technology that is either (1) utilized in connection with the U.S. business's activity in a specified set of 27 industries (the "Pilot Program Industries") or (2) designed by the U.S. business for use in one or more Pilot Program Industries. The complete list of Pilot Program Industries is linked here.

According to the Department of the Treasury, the Pilot Program Industries were "carefully developed" to cover industries for which "certain strategically motivated foreign investment could pose a threat to U.S. technological superiority and national security."[1] The full breadth of the Pilot

[1] U.S. Department of Treasury "Fact Sheet: Interim Regulations for FIRRMA Pilot Program" dated October 10, 2018, https://home.treasury.gov/system/files/206/Fact-Sheet-FIRRMA-Pilot-Program.pdf.

Program Industries is beyond the scope of this article, but such industries include biotechnology research and development, computer manufacturing, computer storage device manufacturing, chemical manufacturing, aircraft manufacturing, battery manufacturing, radio and television broadcasting, wireless communications equipment manufacturing and nuclear electric power generation.

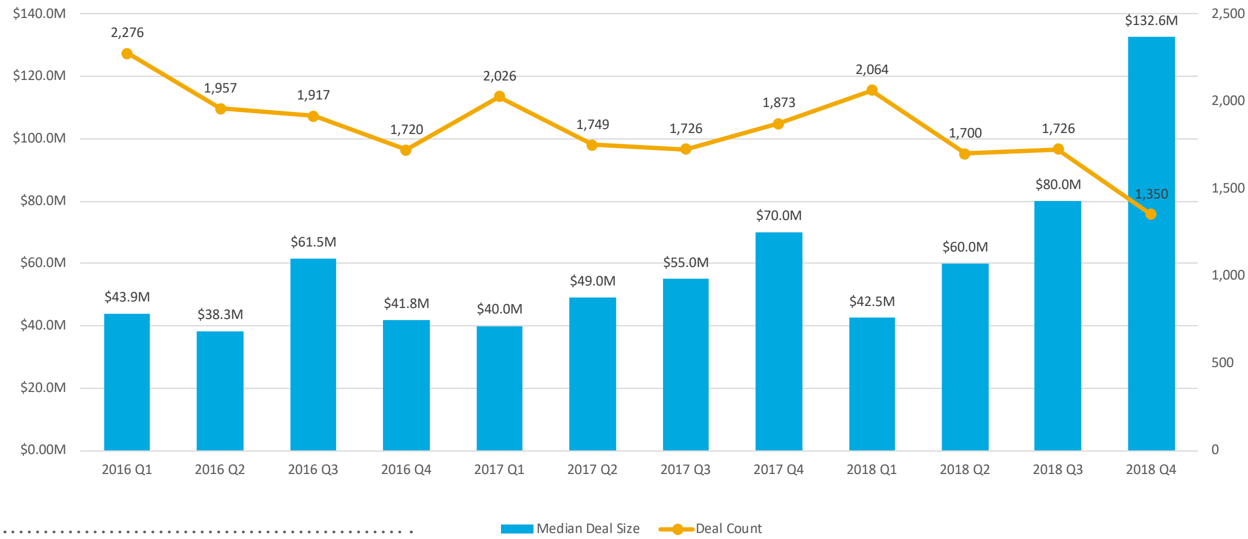
Although the Pilot Program is set to expire on or before March 5, 2020, the program is expected to inform and guide the full implementation of FIRRMA in the future. Therefore, it is critical for dealmakers to both comply with the Pilot Program during its period of effectiveness and consider its broader implications on a going-forward basis. Potential deal parties should be aware that the Pilot Program is not limited to transactions involving buyers from a subset of high-risk countries. The Pilot Program and its mandatory filing requirements apply if a transaction constitutes a "pilot program covered transaction," regardless of the buyer's country of origin.

Suggestions for Addressing CFIUS Risk

In light of the significant expansion of CFIUS's reach under FIRRMA and the Pilot Program, it is more important than ever for deal professionals to evaluate the applicability of CFIUS at the earliest possible stage of a proposed transaction and consider the costs, timing and associated execution risk if a CFIUS filing is triggered. As a part of this evaluation, a seller should conduct due diligence on the proposed buyer and its controlling shareholders to assess perceived national security concerns and the level of risk of a prolonged CFIUS review or potential block by the president. A seller's diligence should include dialogue with the buyer to understand the buyer's and its advisors' awareness of and experience with the CFIUS process. An inexperienced or unprepared buyer can cause significant delays and related issues when responding to CFIUS requests.

In addition to due diligence, for potential high-risk transactions (in particular those involving Chinese buyers) we strongly recommend that the parties engage with CFIUS, either formally or informally, at the letter of intent or term sheet stage if possible. Engaging with CFIUS before negotiating definitive deal agreements helps proactively address risks before incurring significant deal costs. In the case of a U.S. public company, before moving forward with any such early filing, the parties should evaluate whether the filing would trigger

U.S. M&A Market Snapshot: Median Deal Size & Deal Count



Source: PitchBook

reporting requirements with the U.S. Securities and Exchange Commission. If reporting is required, then confidentiality and related issues will likely outweigh the benefits of early engagement with CFIUS.

As the parties move forward with the negotiation of definitive deal agreements, they should pay careful attention to the contractual allocation of CFIUS-related risks between the buyer and seller. Sellers should push for a reverse termination fee triggered by failure to obtain CFIUS clearance. Although we have seen an increase in such fees over the last few years, we expect to see more pushback from buyers, particularly those from perceived high-risk countries such as China, in light of the expanded scope of CFIUS and the perceived uncertainty arising out of the current geopolitical climate. Alternatives to a full reverse termination fee trigger are (i) a two-tiered fee structure with a lower fee triggered by any CFIUS-related termination other than those resulting from willful misconduct or a material breach by the buyer or (ii) an obligation by the buyer to reimburse the seller for its full deal expenses (subject to a cap) upon any CFIUS-related termination.

Regardless of the contractual risk allocation agreed on, sellers need to give careful consideration to the potential difficulties associated with recovering on claims against non-U.S. buyers. In order to mitigate these difficulties, a seller should consider requiring an escrow, deposit or other credit support to cover the buyer's obligations with respect to the reverse termination fee or other payments. These credit support mechanisms can be phased in throughout the transaction to help spread the risk and address the potential burdens of foreign exchange controls.

Buyers should be aware that insurers have recently shown a willingness to provide insurance coverage for potential CFIUS-triggered reverse termination fees. Although it remains to be seen whether this insurance coverage will continue to be available following the recent reforms, buyers should consider engaging an insurance broker early in the deal process to evaluate the options.

As the market continues to evolve and respond to the impact of FIRRMA and the Pilot Program, potential deal parties should remain diligent, work with counsel to monitor further changes and attempt to address CFIUS-related risk at the earliest stages of a proposed transaction. «

Recent Developments in Delaware Law

By: John Bradley and Christine Kim

During the second half of 2018, Delaware courts issued opinions in a number of cases and the Delaware Legislature enacted statutory amendments that will affect many mergers and acquisitions (M&A) transactions. This article summarizes three influential Delaware cases and two statutory amendments to the Delaware General Corporation Law (DGCL).

MFW's *Ab Initio* Condition

Kahn v. M&F Worldwide Corp., 88 A.3d 635 (Del. 2014) (MFW) established a Delaware court's standard of review in controlling stockholder take-private transactions, holding that the deferential business judgment rule applies in lieu of the stringent entire fairness standard if the controlling stockholder commits in advance to approval by both an independent, adequately empowered special committee of the subject company's board that fulfilled its duty of care, and an uncoerced, informed majority of the non-controlling stockholders.

In Flood v. Synutra Int'l, Inc., 195 A.3d 754 (Del. 2018), the Delaware Supreme Court clarified that the controlling stockholder must commit to MFW's two procedural protections prior to economic negotiations in order to achieve the more favorable business judgment rule standard of review.

Synutra's controlling stockholder proposed to take Synutra private but did not commit or condition its initial proposal *ab initio* on MFW's procedural protections. After Synutra's board formed a special committee for the proposed transaction, the controlling stockholder sent a follow-up proposal including the same economic conditions as well as MFW's procedural protections. Importantly, the follow-up proposal was made prior to the special committee engaging its financial advisor, before financial projections were made available and in advance of any price negotiations.

The claimant in Synutra argued that MFW's *ab initio* requirement was unfulfilled because the controlling stockholder failed to include MFW's procedural protections in its initial proposal. The Delaware Supreme Court rejected this rigid application and clarified a more flexible test, allowing for the business judgment rule standard of review provided that the controlling stockholder commits to MFW's procedural protections prior to economic negotiations. The Court reasoned that the key concern articulated in MFW—"ensuring that controllers could not use the [MFW] conditions as bargaining chips during economic negotiations"—is still addressed if MFW's procedural protections are in place before economic negotiations commence.

Practitioners, controlling stockholders, target company boards of directors and special committees should give due attention to timely conditioning proposals on and implementing MFW's procedural protections consistent with MFW and Synutra while paying close attention to when substantive "economic negotiations" are to commence. Additionally, since Delaware courts seem disinclined to use bright-line temporal tests in this context, participants should seek to follow MFW's procedural safeguards as early as possible to avoid future complications and a higher standard of review.

Contractually Overriding Appraisal Rights

In Manti Holdings LLC v. Authentix Acquisition Co., C.A. No. 2017-0887-SG (Del. Ch. Oct. 1, 2018), the Delaware Court of Chancery held that waivers of statutory appraisal rights in stockholder agreements are enforceable as a matter of law provided that the stockholders voluntarily entered into the agreement in return for consideration.

Authentix's stockholders entered into a stockholder agreement to support a third-party investment. The stockholder agreement included "drag-along" rights requiring the stockholders to agree to a sale or merger of Authentix if approved by holders of a majority of Authentix's outstanding stock. The stockholder agreement also required that the stockholders party to the agreement refrain from exercising any appraisal rights related to such a transaction. Holders of a majority of Authentix's outstanding stock later resolved in writing to sell Authentix to a third party through a merger transaction, resulting in some stockholders receiving only nominal or no consideration in the transaction.

The claimant stockholders, although having signed the stockholder agreement, sought to perfect statutory appraisal rights under Section 262 of the DGCL, arguing that they had not waived their appraisal rights. The claimants argued that the language of the stockholder agreement—that they would "refrain from exercising" any appraisal rights, as opposed to "waiving" those rights—did not extinguish the rights but merely delayed their right of exercise until after closing. The Court disagreed, finding the claimants' interpretation unreasonable, and held that the stockholder agreement unambiguously extinguished their appraisal rights, stating that "no contracting party, agreeing to the quoted language, would consider itself free to exercise appraisal rights . . ."

The claimant stockholders also argued that an appraisal rights waiver is in any event unenforceable under DGCL Section 151(a), which requires that limitations on a class of stock must be set forth in or derived from a corporation's certificate of incorporation. The Court disagreed, finding that the contractual obligations did not transform the subject stock into a new class of stock, and that enforcing a contractual appraisal rights waiver is not equivalent to imposing limitations on a class of stock.

Practitioners and investors should take comfort in the certainty provided by Authentix while at the same time ensuring that drag-along provisions and waivers of appraisal rights are drafted with precision to succeed against or avoid a challenge to their effectiveness based on interpretation and ambiguity.

Delaware Court Upholds MAE Termination

In Akorn, Inc. v. Fresenius Kabi AG, C.A. No. 2018-0300-JTL (Del. Ch. Oct. 1, 2018), the Delaware Court of Chancery held for the first time that a buyer properly terminated an acquisition agreement on the basis of a material adverse effect (MAE).

Fresenius agreed to acquire Akorn under a merger agreement that included, among other notable provisions, customary seller representations and warranties, a MAE condition to closing and another condition to closing requiring Akorn's representations and warranties be true and correct except as would not reasonably be expected to have a MAE. Shortly after signing the merger agreement, Akorn's business performance plummeted. Fresenius ultimately terminated the merger agreement and Akorn subsequently sued to compel Fresenius to close the transaction.

The Court held that Fresenius properly terminated the merger agreement, finding that Akorn breached several representations, warranties and covenants, and experienced a MAE. The Court focused extensively on the highly detailed factual record in determining that Akorn experienced a MAE, including

On December 7, 2018, the Delaware Supreme Court upheld the Delaware Court of Chancery's finding that Fresenius properly terminated the merger agreement.

a company-specific lengthy and severe business downturn, widespread regulatory non-compliance and Akorn's failure to operate its business in the ordinary course.

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Practitioners, buyers and sellers should be mindful of the particularly egregious and case-specific facts while heeding the Court's emphasis on the high threshold for establishing a MAE. M&A parties should also understand that any alleged failure to satisfy a MAE condition to closing will be examined both qualitatively and quantitatively without bright-line rules for financial performance. The Akorn case presents an excellent primer on Delaware courts' approach to MAE analysis while reinforcing the importance of drafting and negotiating MAE clauses with utmost precision.

For a more in-depth analysis of the Akorn case, see Spotting Bigfoot: Delaware Court of Chancery Finds the Mythical Material Adverse Effect on pages 5-10 of *M&A Perspectives*.

DGCL Amendments

Amendments to Sections 204 and 262 of the DGCL became effective on August 1, 2018.

Ratification of Defective Corporate Acts

Amendments to Section 204 clarify the circumstances under which corporations may use Section 204 to ratify defective corporate acts.

Section 204(c) has been amended to confirm its availability even when no valid stock is outstanding, whether because the corporation has not validly issued any shares or because all shares are putative stock, even if ratification would otherwise require stockholder approval under Section 204(c).

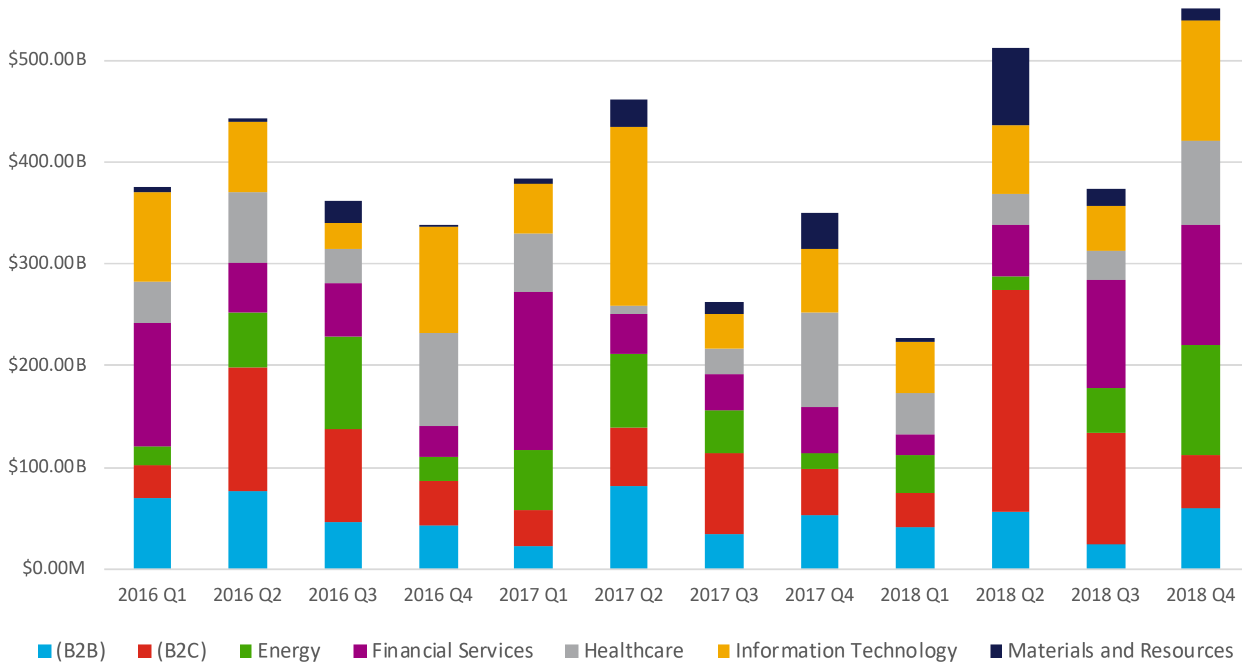
Section 204(d) has been amended to clarify that in the event a stockholder vote is scheduled to ratify a defective corporate act that involved a record date, the required notice may be sent to all holders of valid or putative stock as of the record date originally established for approval of the defective corporate act. Section 204(g) has been amended to permit public companies to fulfill the stockholder notice requirements through documents publicly filed with the Securities and Exchange Commission.

Section 204(h)(1) has been amended to clarify that any act taken within a corporation's general powers may be ratified under Section 204 despite the failure to approve the act in accordance with the DGCL or the corporation's certificate of incorporation or bylaws. Importantly, the Delaware Court of Chancery still may refuse to validate a defective corporate act ratified under Section 204 if the initial failure of authorization involved a deliberate withholding of any consent or approval required under the DGCL or the corporation's certificate of incorporation or bylaws. The amendments also clarify that ratification under Section 204 may cure the failure of an act or transaction resulting from deficiencies in any proxy statement or consent solicitation.

Statutory Appraisal Rights

Amendments to Section 262 extend the "market out" exception to appraisal rights to an "intermediate form" merger. An intermediate form merger involves an exchange offer followed by a back-end

U.S. M&A Market Snapshot: Capital Invested by Primary Industry Sector



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merger consummated without a stockholder vote in accordance with Section 251(h). The market out exception applies under Section 262(b)(1) when the target's stock is listed on a national securities exchange and held by more than 2,000 holders of record. Section 262(b)(2) makes appraisal rights nevertheless available when target stockholders receive consideration consisting of anything other than shares of stock of the surviving corporation or depository receipts in respect thereof, shares of stock of any other corporation or depository receipts in respect thereof that at the merger effective time will be listed on a national securities exchange or be held by more than 2,000 holders of record, cash in lieu of fractional shares or fractional depository receipts, or any combination of the foregoing.

Additionally, amendments to Section 262(b)(3) eliminate the carve-out for intermediate form mergers, treating intermediate and long-form mergers the same with respect to appraisal rights under Section 262.

Finally, Section 262(e) clarifies that the statement by the surviving corporation required to be furnished to dissenting stockholders in connection with an intermediate-form merger under Section 251(h) must set forth the number of shares that were not tendered for purchase or exchanged in connection with a tender or exchange offer. Section 262(e) previously called for disclosure of the number of shares "voted" for the merger; however, no shares are in fact "voted" in a transaction under Section 251(h) for the adoption of a merger agreement. «

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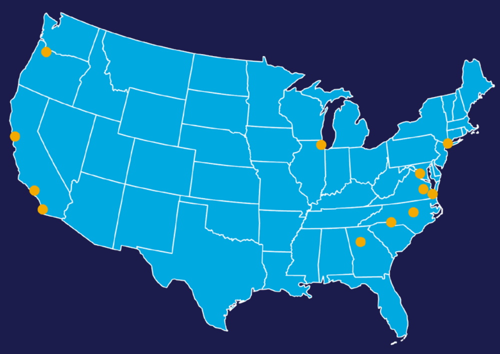

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$7,400,000,000 ARRIS Acquisition by CommScope	$1,500,000,000 Dominion Energy Sale of 50% interest in Blue Racer to First Reserve	$1,540,000,000 conEdison Development Acquisition of Sempra Energy subsidiary	$610,000,000 ACCESS NATIONAL CORPORATION Acquisition by Union Bankshares Corporation
Value Not Disclosed Mikart Acquisition by Nautic Partners LLC	$7,000,000 GAF Gastroenterology Associates Of Fredericksburg Acquisition of interest in Physicians Endoscopy, LLC	Value Not Disclosed Audio precision Acquisition by Battery Ventures LP	$75,500,000 ConversionPoint TECHNOLOGIES Acquisition of Inuvo, Inc.
$5,400,000 envirostar Acquisition of Washington Automated, LLC	Value Not Disclosed HARGRAY Do More. Live Better. Acquisition of the Alabama assets of USA Communications	$520,000,000 BRINKS Acquisition of Dunbar Armored, Inc.	Value Not Disclosed brightree Acquisition of Apacheta Corporation
$452,900,000 BRANDBANK Merger with Renasant	Value Not Disclosed MANGROVE EQUITY PARTNERS Sale of Readylift Holdings, LLC to WheelPros, LLC	$55,100,000 pb VIRGINIA PARTNERS BANK Acquisition of stock by Delmar Bancorp	$34,200,000 White Birch Paper Acquisition of Bear Island Paper Mill by Cascades, Inc.