stockholders, the more advisable to include meaningful time limitations to enhance the likelihood of enforceability without these separate undertakings.

The merger structure should continue to provide an effective means for acquirors to proceed quickly and confidentially to a definitive acquisition agreement with privately held targets that locks in the target to a sale of 100% of the equity, especially when these targets have numerous non-insider stockholders. A well-advised acquiror should be able to craft an approach to the merger agreement and ancillary support agreements in ways that do not leave the acquiror with a bleak choice between a merger agreement structure that provides inadequate post-closing protections, and a stock purchase agreement structure that is characterized by unacceptable risks of failing to acquire 100% of the equity as well as impediments from the perspectives of speed and confidentiality.

Courts Increasingly Skeptical of the Value of Disclosure-Only Settlements

By Tim Mast, Tom Bosch, and Nicholas Howell of Troutman Sanders LLP

In 2013 and early 2014, courts in Delaware and other jurisdictions increasingly began to scrutinize attorneys' fee awards in disclosure-only settlements resolving shareholder challenges to merger transactions.[1] In several decisions, courts reduced or denied plaintiffs' attorneys' fees because the settlements involved only nonmaterial additional disclosures. Delaware courts have been relatively quiet on this issue since the Court of Chancery's February 2014 decision in *In re Medicis Pharm. Corp., S'holders Litig.*;[2] however, several recent decisions from the New York Supreme Court's Commercial Division and one decision from the Northern District of California indicate that courts will continue to eschew the practice of "automatic" fee awards in favor of awarding fees based on the benefit that the additional disclosures provide to shareholders and, in appropriate circumstances, rejecting settlements and fee requests.

Reduction of Fees. In June 2014, after certifying a class for settlement purposes, Judge Charles E. Ramos of the New York Supreme Court's Commercial Division rejected a request by plaintiff's counsel for $465,000 in fees in *Schumacher v. NeoStem, Inc.*[3] Although Judge Ramos believed that plaintiff's counsel had "undoubtedly achieved value" for the class by securing additional disclosures and several corporate governance reforms, he opined that the benefit to shareholders was "limited" because the settlement did not provide the shareholders any monetary relief.[4] Consequently, Judge Ramos reduced the fee award to $125,000.[5]

Several months later, in *West Palm Beach Police Pension Fund v. Gottdiener*, Judge Marcy Friedman of the Commercial Division approved a disclosure-only settlement, but applied the lodestar method to reduce an unopposed fee request from the $500,000 requested to $379,566.50 plus $36,637.65 in unreimbursed expenses.[6] Judge Friedman declined to apply a multiplier to increase the amount of the fees awarded because "the contingency risk that the plaintiff faced was insubstantial, given the ubiquity of settlements in shareholder derivative actions challenging mergers based on insufficient disclosures."[7]

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[1] *See* Tim Mast, Tom Bosch, and Mary Weeks, *Attys' Fees Under Increasing Scrutiny In M&A Settlements*, Law360 (Apr. 3, 2014), http://www.law360.com/articles/524910/attys-fees-under-increasing-scrutiny-in-m-a-settlements.

[2] *See In re Medicis Pharm. Corp. S'holders Litig.*, No. 7857-CS (Del. Ch. Feb. 26, 2014).

[3] *Schumacher v. NeoStem, Inc.*, 993 N.Y.S.2d 646, 646 (2014).

[4] *Id.*

[5] *Id.*

[6] *W. Palm Beach Police Pension Fund v. Gottdiener*, 2014 N.Y. Misc. LEXIS 4686, at *10 (N.Y. Sup. Ct. Oct. 22, 2014).

[7] *Id.* at *8-9.

Similarly, in *St. Louis Police Retirement System v. Severson*, Judge Yvonne Rogers of the Northern District of California also approved a disclosure-only settlement and used the lodestar method to reduce a fee request of $1,650,000 to $543,018.75.[8] Although Judge Rogers found that the defendants failed to make "full disclosures of material facts bearing on the shareholders' proxy vote," she applied only a 1.5 multiplier—rather than the requested 2.8—because the case did not involve extraordinary risk, complexity, or effort on behalf of plaintiff's counsel.[9] Judge Rogers also scrutinized the plaintiff counsel's request for $51,231.89 in expenses and awarded only $36,410.78.[10]

Denial of Settlements. In December 2014, in *Gordon v. Verizon Communications, Inc.*, Judge Melvin L. Schweitzer of the New York Supreme Court's Commercial Division rejected a proposed disclosure-only settlement and request for attorneys' fees because the additional disclosures were immaterial.[11] Judge Schweitzer described the supplemental disclosures as "unnecessary surplusage" that "individually and collectively fail[ed] to materially enhance the shareholders' knowledge" of the merger. Thus, he held that any award of legal fees would constitute a misuse of corporate assets.[12] Noting the "tsunami of litigation" and the "suspect disclosure-only settlements associated with public acquisitions today," Judge Schweitzer denied the proposed settlement because approving it would have made him "an enabler of an unwarranted divestiture of shareholder rights by virtue of plaintiff's release, as well as a misuse of corporate assets were plaintiff's legal fees to be awarded."[13] The plaintiff's appeal of the court's denial of the settlement is pending.

Most recently, in *City Trading Fund v. Nye*, Judge Shirley W. Kornreich of the Commercial Division also denied approval of a disclosure-only settlement. Judge Kornreich criticized the plaintiffs' claims for their "downright frivolity" because the plaintiffs neither alleged material omissions nor settled for material supplemental disclosures.[14] She also denied the plaintiffs' request for attorneys' fees totaling $500,000.[15] Despite acknowledging that the company wished to settle, Judge Kornreich determined that she could not certify the class for settlement purposes because doing so would undermine the public interest, incentivize plaintiffs to file frivolous disclosure suits, and levy unnecessary costs on shareholders.[16] The plaintiffs responded by voluntarily dismissing their claims.

When considered alongside the prior decisions from Delaware, these cases signal courts' (1) growing frustration with the deluge of frivolous or questionable shareholder merger challenges, and (2) increasing willingness to override defendants' decisions to settle merger challenges on a disclosure-only basis. Even if this trend continues, it remains to be seen whether it will stem the tide of merger challenge lawsuits, which appears to be one of the courts' goals in rendering these decisions, or simply make merger litigation more difficult to settle, which could put companies in a precarious position when trying to consummate mergers.

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[8] *St. Louis Police Ret. Sys. v. Severson*, No. 12-CV-5086 YGR, 2014 U.S. Dist. LEXIS 110984, at *21 (N.D. Cal. Aug. 11, 2014).

[9] *Id.* at *20-21.

[10] *Id.* at *23.

[11] *Gordon v. Verizon Commc'ns, Inc.*, 2014 N.Y. Misc. LEXIS 5642, at *11 (N.Y. Sup. Ct. Dec. 19, 2014).

[12] *Id.* at *16, *21.

[13] *Id.* at *19, *21.

[14] *City Trading Fund v. Nye*, 2015 N.Y. Misc. LEXIS 11, at *32, *41 (N.Y. Sup. Ct. Jan. 7, 2015).

[15] *Id.* at *37.

[16] *Id.* at *33.