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# Promises Made to be Broken? Standstill Agreements in Change of Control Transactions

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# PROMISES MADE TO BE BROKEN? STANDSTILL AGREEMENTS IN CHANGE OF CONTROL TRANSACTIONS

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## I. INTRODUCTION

Many promises are made in merger negotiations but not all promises are necessarily enforceable or consistent with a board of directors' fiduciary duties. This Article explores the enforceability of one such promise: the buyer's standstill agreement. When a publicly traded company explores a sale and allows potential buyers access to its confidential information, that company, the target, customarily requires each potential buyer to execute a confidentiality agreement containing a standstill provision.[1] A typical standstill[2] prevents potential buyers from publicly announcing a bid for the target, without the target's prior consent, for a period of approximately twelve to twenty-four months from the conclusion of the sales process or auction.[3] Standstills help targets control the bidding process, as well as prevent potential buyers from using the confidential information obtained during due diligence to make a bid outside of the formal sales process.[4]

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[1] *See* William G. Lawlor, *Taming the Tiger: Difficult Standstill Agreement Issues for Targets*, DEAL LAWYERS (July-Aug. 2007), at 7, *available at* http://www.dechert.com/files/Publication/c224a19d-bf74-40f8-96d1-38f2627a483d/Presentation/PublicationAttachment/e58245b1-30cb-4ee2-833a-3cedd2585bf3/C%26SLawlor-TamingtheTiger.pdf (explaining public target companies "almost always" have potential acquirers execute standstills when conducting bidding processes either for themselves or for a major asset); *see also* S. Union Co. v. Sw. Gas Corp., 180 F. Supp. 2d 1021, 1034 (D. Ariz. 2002) ("'In deals for public companies, it would be extraordinary for there not to be' a confidentiality and standstill agreement.").

[2] *See generally* Lawlor, *supra* note 1. Standstills can exist as a separate agreement but more typically are incorporated as a provision in a confidentiality agreement. The terms standstill, standstill agreement, and standstill provision will be used interchangeably in this Article despite whether the standstill appears as an individual standalone agreement or as a provision in a confidentiality agreement.

[3] *See infra* Part II.B.

[4] Lawlor, *supra* note 1, at 7 ("Th[e] [standstill] provision backstops the restrictions regarding the use of confidential information given by the target to prospective buyers. It also

Standstills also assure potential buyers that if they ultimately "win" the auction and execute a definitive acquisition agreement with the target company, any potential buyers who "lost" the auction will be contractually bound to not overbid.[5] This helps avoid hostile third-party bids after an acquisition is underway.[6]

The enforcement of standstills can cause a conflict between two fundamental principles of mergers and acquisitions ("M&A"). The first principle obligates the target's board of directors to maximize stockholder value when selling a controlling stake of a target company.[7] This obligation is known as a board's *Revlon* duties.[8] The second fundamental principle sanctions covenants within acquisition agreements aimed at thwarting third parties from overbidding between the signing and closing of a merger (or the pre-closing period).[9] These provisions are typically called "deal protection devices," and standstills are one variation of these devices.[10] The Delaware Supreme Court's decision in *Unocal Corp. v. Mesa Petroleum Co.*[11] and its progeny expressly allow deal protection devices under certain circumstances, and further announced the judicial standard of review for these devices.[12] A board's *Revlon* duties, along with the possible protections afforded to deal protection devices under *Unocal*, may create an irreconcilable conflict during the pre-closing period if a third party attempts to overbid.[13] At the same time, however, the promise of these devices may help a target satisfy its *Revlon* duties prior to the execution of an agreement

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provides a stable environment in which the sales process can be managed and controlled by the target.").

[5]*See infra* Part II.B.

[6]*See* Dennis J. Block, *Public Company M&A: Recent Developments in Corporate Control, Protective Mechanisms and Other Deal Protection Techniques*, *in* CONTESTS FOR CORPORATE CONTROL 2008: CURRENT OFFENSIVE AND DEFENSIVE STRATEGIES IN M&A TRANSACTIONS, at 93 (PLI Corp. Law & Practice, Course Handbook Series No. 13964, 2008) (stating standstills can restrict bidders from attempting hostile takeovers).

[7]Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986) (characterizing corporate directors as "auctioneers charged with getting the best price for the stockholders at a sale of the company").

[8]LOU R. KLING & EILEEN T. NUGENT, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 4.04[3], at 4-50 (2010) (describing the aforementioned obligation as the "Revlon duty").

[9]This Article will refer to the period between the execution of a definitive acquisition agreement and the closing of the transaction as the pre-closing period.

[10]*See, e.g.*, Block, *supra* note 6, at 91-93 (listing standstill provisions as a deal protection mechanism).

[11]493 A.2d 946 (Del. 1985).

[12]*See infra* Part II.A.2.

[13]*See* Lawlor, *supra* note 1, at 11 ("The limits placed on any interlopers…have yet to be fleshed out by the courts.").

during the pre-signing period.[14] As commonly argued, the availability and promise of these devices may encourage a potential buyer to pay more for the target because the covenants provide certain assurances that the executed merger agreement may not be overbid.[15] Thus, during the pre-signing period, a target's board may have good reason to agree to deal protection devices because the devices may pass under *Unocal*. However, pre-closing, the devices may inhibit the satisfaction of a board's *Revlon* duties if a higher bid were to emerge. Deal protection devices, including standstills, may prevent a board from considering a third party offer or discourage a third party from making an overbid in the first place.[16]

Although standstills have been used in M&A deals since at least the early 1980s, the scant Delaware case law provides little help to target boards in resolving the conflict described above.[17] Academics have paid very little attention to standstills over the past three decades, leaving a vast gap in academic literature regarding the potential conflict standstills create between *Revlon* and *Unocal*.[18] Despite this, a number of recent deals and cases mainly outside of Delaware highlight the need to answer these unanswered questions.[19] This Article begins to fill a thirty-year void in M&A literature by addressing the primary question found at the nexus between the *Revlon* duty to maximize stockholder value, and the board's ability to protect an executed transaction under *Unocal*. The conflict at the heart of this nexus is best illustrated by the hypothetical situation presented in the following paragraphs.

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[14] *See infra* Part IV.A.2.

[15] For example, Chancellor Leo Strine of the Delaware Court of Chancery indicated, while a Vice Chancellor, in *dicta*, that a standstill may be required in a pre-signing sales process to "to give the [target] leverage to extract concessions from the parties who seek to make a bid." *In re* Topps Co. S'holders Litig., 926 A.2d 58, 91 (Del. Ch. 2007).

[16] *See* Paul Povel & Rajdeep Singh, *Takeover Contests with Asymmetric Bidders*, 19 REV. FIN. STUD. 1399, 1402 (2006) ("These [deal protection] devices make the target less attractive to rejected bidders, thereby reducing their incentive to top up the winning bid."). *Contra In re* OPENLANE, Inc. S'holders Litig., 2011 WL 4599662, at *10 n.53 (Del. Ch. Sept. 30, 2011) (recognizing deal protection devices may discourage bidders but also indicating, in *dicta*, a fiduciary out clause may not be necessary when considering the fact that sophisticated bidders are already on notice that Delaware courts may not enforce an agreement lacking a fiduciary out if the bidder presents a board with a superior offer).

[17] *See* Guhan Subramanian, *Bargaining in the Shadow of Takeover Defenses*, 113 YALE L.J. 621, 659 n.164 (2003) (noting that standstill agreements "first appeared in the early 1980s"); Lawlor, *supra* note 1, at 7 ("Remarkably, while standstills have been prevalent for a long time, the case law in the area is relatively sparse.").

[18] Subramanian, *supra* note 17, at 659 ("Surprisingly, despite their important implications for the interplay between negotiated and hostile acquisitions, standstill agreements have not received attention from modern academic commentators.").

[19] *See infra* Part III.

To illustrate, assume a publicly-traded Delaware corporation ("Delaware Corp.") decides to put itself up for sale in an auction process. Delaware Corp. hires a financial advisor who contacts a number of potential bidders regarding their interest in participating in the auction. Six companies decide to partake in the auction. Before receiving confidential information, however, Delaware Corp. and its financial advisor require that each bidder execute a separate confidentiality agreement with Delaware Corp. Each confidentiality agreement includes a standstill provision, preventing the bidder "from making or announcing any bid outside of the auction process for a period of 18 months following the conclusion of the auction."[20]

Two of the six bidders make it to the final round of bidding and each submits a bid. "Bidder A" wins the auction by submitting an all-cash offer of $51 per share, beating out "Bidder B"'s $49 per share all-cash offer. Bidder A and Delaware Corp. enter into a merger agreement with closing expected to occur in a few months. The merger agreement contains a "fiduciary out" provision, allowing Delaware Corp. to enter into negotiations with, and provide information to, a third party who makes an offer that is, or is likely to become, superior in value to the agreement with Bidder A. Because of this provision, Delaware Corp. is allowed to terminate the agreement with Bidder A in order to accept a superior third party offer. The goal of these "fiduciary out" provisions is to allow the Delaware Corp. board to continue to satisfy its *Revlon* duties during the pre-closing period.

Now, assume that two weeks after Delaware Corp. executed the agreement with Bidder A, Bidder B submits an offer—in contravention of the previously executed standstill—of $53 per share. At this point, Bidder B's bid raises a number of questions: (1) whether under Delaware law Delaware Corp. may consider the $53 offer; (2) whether the standstill is enforceable; and (3) if the standstill is enforceable, who has the ability to enforce it— Delaware Corp. or Bidder A.[21]

Suppose during the pre-signing negotiations with A, in order to extract a higher price from Bidder A, Delaware Corp. promises not to waive all previously executed standstills. This promise further personifies a

[20] Ventas, Inc. v. HCP, Inc., 647 F.3d 291, 297 (6th Cir. 2011).

[21] For this final question, *see, e.g.*, William T. Allen, *Overview of Process Issues in Going Private Transaction*, *in* GOING PRIVATE 2011: DOING THE DEAL RIGHT, at 52 (PLI Corp. Law & Practice, Course Handbook Series No. 28673, 2011) (asking if "a Special Committee in an auction or quasi-auction process contractually obligates bidders not to overbid, is such a contract term enforceable, and if so, by whom?").

possible tension between the board's *Revlon* duties and its ability to protect an executed transaction under *Unocal*. Delaware courts, and most other courts, have not yet addressed whether a target board's promise not to waive a standstill is consistent with the board's fiduciary duties.[22] Furthermore, assume that Delaware Corp. and Bidder A's merger agreement contains a covenant providing for a breach of the agreement if Delaware Corp. did not seek all judicial relief in the event of an overbid made in contravention of a standstill. The Delaware courts have never addressed the validity of such a covenant.[23] Finally, assume that, while Delaware Corp. is negotiating with Bidder A, Delaware Corp. grants Bidder A the right "to enforce any existing Standstill Agreements with third parties" in the merger agreement.[24] Although a Canadian court upheld a similar grant,[25] whether Delaware courts would do the same is anything but clear.

This Article addresses how Delaware courts would likely answer the unanswered questions illustrated in the hypothetical above.[26] Part II provides an overview of the pre-signing sales process and a board's fiduciary duties in M&A transactions. In addition, it explores the roles of pre-signing sales agreements in the bidding process and specifically examines confidentiality agreements and standstills. Part II concludes by

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[22] *See, e.g.*, Lawlor, *supra* note 1, at 7 ("Given the target board's fiduciary duties and the questionable third party beneficiary status of the winning bidder, the enforceability of these provisions is not free from doubt."); Steven M. Davidoff, *Bidders Behaving Badly*, N.Y. TIMES DEALB%K (Sept. 14, 2009, 2:37 PM), http://dealbook.nytimes.com/2009/09/14/bidders-behaving-badly/ ("Delaware may or may not enjoin a bidder from breaching a standstill to offer a competing higher bid or otherwise allow a company to contractually override its fiduciary duties to consider a higher, competing bid."). As this Article went to print, the Delaware Court of Chancery issued a couple of rulings providing insight into how the court may rule on Don't-Ask-Don't-Waive standstills in the future. *See* The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction, *In re* Ancestry.com Inc. S'holder Litig., C.A. No. 7988-CS (Del. Ch. Dec. 17, 2012) (stating Don't-Ask-Don't-Waive standstills could be consistent with a board's fiduciary duties if the board uses them for a specific value maximizing purpose); Telephonic Oral Argument and the Court's Ruling, *In re* Complete Genomics, Inc. S'holder Litig., C.A. No. 7888-VCL (Del. Ch. Nov. 27, 2012) (finding that target board likely violated its fiduciary duties by agreeing to a Don't-Ask-Don't-Waive standstill as it prevented the board from "properly evaluat[ing] a competing offer, disclos[ing] material information, and mak[ing] a meaningful merger recommendation to its stockholders").

[23] *See* Allen, *supra* note 21, at 52 (questioning whether it is a breach of the merger agreement when a target fails to seek all available judicial relief against an overbidder where there was an agreement to not overbid).

[24] Ventas, Inc. v. HCP, Inc., 647 F.3d 291, 299 (6th Cir. 2011).

[25] Ventas Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. (3d) 254, para. 35 (Can. Ont. C.A.).

[26] This Article does not necessarily reflect my normative views of how these issues *should* be resolved. Instead, I argue that Delaware courts would apply and interpret *Revlon*, *Unocal*, and their progeny to decide these issues on a case-by-case basis.

exploring the role fiduciary outs play in the pre-closing period and their interplay with standstills. Part III examines standstill case law and unlitigated examples of overbids involving standstills. This part specifically focuses on overbids made in contravention of a previously executed standstill and emphasizes the interplay between standstills and target board's fiduciary duties. Part IV argues that, when ultimately presented with the questions illustrated above, Delaware courts will answer each question by examining the value maximization tools utilized by the board pre-signing to determine the reasonableness of the board's decision-making process. Moreover, in determining whether the board can decide not to consider an offer, agree not to waive a standstill, or grant the "winner" the right to enforce a standstill, the courts—in accordance with *Unocal*—will also consider the purpose of the board's actions under the circumstances of each case. Specifically, if a valid value maximization purpose is articulated and the board is not acting to further its own self-interests, then a Delaware court would likely find the board's actions to be reasonable and uphold the board's promises.

## II. STANDSTILLS IN THE BIDDING PROCESS & THE ROLE OF FIDUCIARY DUTIES

The types of standstills that are the subject of this Article are generally entered into during the pre-signing sales process and have a continuing effect during the pre-closing period. This Article refers to the activities taking place during the pre-signing period interchangeably as the "sales process" or the "bidding process."

During the pre-signing sales process and continuing into the pre-closing period, compliance with the target's board of directors' fiduciary duties controls the legitimacy of the acquisition and other ancillary agreements as well as the identity of the "winning bidder" if more than one bidder is seeking to acquire the target. As a result, the target board's fiduciary duties are a primary consideration when examining standstills and their role during the pre-closing period. This section provides an overview of the pre-signing sales process, a board's fiduciary duties in the context of M&A transactions, and the role of fiduciary outs during the pre-closing period.

### A. *Fiduciary Duties and the Pre-Signing Bidding Sales Process*

In the M&A world, the nature of the transaction drives many issues, including applicable statutory regulations and the appropriate standard that the target boards' actions must meet. Unless otherwise indicated, when referring to transactions in this Article, it is assumed that the transaction at issue involves a publicly traded target company, and further, that the target is being sold as an entire unit for cash, or a mix of cash and stock as consideration. In the public company realm, this type of transaction is typically accomplished by a merger.[27] The sale of the target as a unit differs from the sale of a major asset, division, or subsidiary as those sales may be accomplished by way of a variety of other transaction structures.[28] In addition, the execution of a contract involving a major asset, division, or subsidiary typically does not result in competition from third parties.[29] Hence, the overbidding fact patterns at issue in this Article generally would not arise in the sale of a major asset, division, or subsidiary.[30]

In negotiated M&A transactions, the board acts as a gatekeeper.[31] Under Delaware law, if a company is to be acquired by way of a merger, the required vote is by a majority of the outstanding voting shares.[32] However, the shareholders' right to vote only comes into play once the board has approved the merger and has entered into a definitive agreement.[33] That is, the "shareholders must be persuaded to approve the transaction."[34] Despite this, the board is vested with the initial decision as to whether the company should engage in an M&A transaction in the first place and, if so, in what manner and with whom that transaction should take place.[35]

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[27]*See* Robert T. Miller, *The Economics of Deal Risk: Allocating Risk Though MAC Clauses in Business Combination Agreements*, 50 WM. & MARY L. REV. 2007, 2017 (2009) ("[Transactions involving public companies] are almost invariably structured as statutory mergers . . . .").

[28]*See* Lawlor, *supra* note 1, at 7 (stating if a company sells a major asset, potential buyers will more than likely be asked to execute standstills). If a company were to sell a major asset, subsidiary, or division it would also have the bidders execute standstill agreements. However, this Article focuses on the sale of the target as an entire unit and standstills executed during those sales.

[29]KLING & NUGENT, *supra* note 8, § 16.01, at 16-3-16-4.

[30]Moreover, the enhanced scrutiny standards discussed in this Article do not apply to such transactions unless the asset, division, or subsidiary being sold constitutes all or substantially all of the assets of the target. *Id.* § 4.04[3], at 4-52.

[31]Stephen M. Bainbridge, *The Geography of* Revlon-*Land*, 81 FORDHAM L. REV. (forthcoming 2013) (manuscript at 8), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2115769.

[32]DEL. CODE ANN. tit 8, § 251(c) (1974).

[33]*See id.* §§ 251(b)-(c) (detailing the authorization process for merger agreements requiring shareholder vote); *see also* Christina M. Sautter, *Rethinking Contractual Limits on Fiduciary Duties*, 38 FLA. ST. U. L. REV. 55, 61-65 (2010) [hereinafter *Rethinking Contractual Limits*] (providing a detailed explanation of a board's adoption of a merger agreement and submission to the shareholders for a vote).

[34]Bainbridge, *supra* note 31, at 15-16.

[35]*Id.* at 20 ("[S]o long as the board of directors is disinterested and independent, it retains full decision-making authority with respect to the transaction.").

### 1. The Business Judgment Rule

Similar to other business decisions made by a company's board, the courts' default standard of review of a board's decisions in the M&A context is the business judgment rule.[36] Under this deferential standard, a court presumes "that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."[37] In other words, because the business judgment rule is a deferential standard, the board's decision will be upheld absent a showing it was "tainted by fraud, illegality, self-dealing, or some other exception to the rule."[38] However, because of the nature of some M&A transactions, there is a greater opportunity for directors to act in bad faith or to engage in self-dealing.[39] Thus, depending on the type of transaction involved, a court may subject the board's actions to an enhanced standard.[40]

### 2. *Unocal*, The *Revlon* Doctrine, and Transactions Triggering *Revlon*

Beginning in the 1980s, the Delaware Supreme Court began to recognize, in judicial opinions, that some fact patterns may call for an

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[36]*See, e.g.*, Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (characterizing the business judgment rule as an "acknowledgement of the managerial prerogatives of Delaware directors"), *overruled on other grounds*, Brehm v. Eisner, 746 A.2d 244 (Del. 2000).

[37]*Id.*

[38]Bainbridge, *supra* note 31, at 17.

[39]*See id.* at 15 (explaining board decisions that are structural in nature, i.e. corporate takeovers, "present a final period problem entailing an especially severe conflict of interest"). More specifically, as Professor Stephen Bainbridge explains, in some types of M&A transactions,

> [t]arget management is no longer subject to shareholder discipline because the target's shareholders will be bought out by the acquirer. Target management is no longer subject to market discipline because the target by definition will no longer operate in the market as an independent agency. As a result, management is no longer subject to either shareholder or market penalties for self-dealing. Accordingly, there is good reason to be skeptical of management claims to be acting in the shareholders' best interests. In turn, the resulting need in this context to hold the board accountable for its mistakes appropriately trumps the more usual tendency towards judicial deference to the board's authority.

Stephen Bainbridge*, Did Facebook's Mark Zuckerberg just have a Van Gorkom moment?* PROFESSORBAINBRIDGE.COM (Apr. 18, 2012, 11:06 AM), http://www.professorbainbridge.com/professorbainbridgecom/2012/04/did-facebooks-zuckerburg-just-have-a-van-gorkom-moment.html.

[40]*See, e.g.*, KLING & NUGENT, *supra* note 8, § 4.04[1], at 4-39 to 4-43 (summarizing enhanced scrutiny standards applicable to board action taken in response to a hostile takeover and transactions involving the sale of a company).

enhanced standard of review.[41] In particular, in *Unocal* the Delaware Supreme Court announced an enhanced standard specifically applicable to board action taken in response to hostile takeover activity.[42] More precisely, the court found that in these situations there is an "omnipresent specter that a board may be acting primarily in its own interests," thereby necessitating that the board show "they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership."[43] The court explained that a board could satisfy this burden by showing "good faith and [a] reasonable investigation."[44] However, the inquiry does not stop there.[45] Additionally, the defensive mechanism adopted by the board must also be proportional, or "reasonable in relation to the threat posed."[46] In a later case applying *Unocal*, the Delaware Supreme Court emphasized that this proportionality inquiry involves a two-step analysis.[47] Namely, the response taken must not be "draconian" (or in other words, neither "coercive [n]or preclusive"),[48] and secondly, the response must fall within a "range of reasonableness."[49]

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[41] *See generally id.* § 4.04[1], at 4-39 to 4-43 (describing the evolution of Delaware case law regarding the business judgment rule and enhanced scrutiny standards). Prior to the 1980s, courts regularly applied the business judgment rule outside of cases involving a "going private" transaction or a parent-subsidiary merger. *Id.* § 4.04[1], at 4-39. Furthermore, "[t]he board's *process* in an arm's length sale of a company to a third party was *rarely*, if ever, challenged, and attacks on the basis of the inadequacy or unfairness of price had to overcome the business judgment rule presumption . . . ." *Id.* § 4.04[1], at 4-38 (second emphasis added). However, the mid-1980s ushered in a new era for the Delaware courts beginning with *Unocal*. Professor Steven Davidoff has argued the Delaware Supreme Court switched gears in an attempt to prevent the Securities and Exchange Commission from promulgating federal regulations of takeover defenses. *See* Steven M. Davidoff, *The SEC and the Failure of Federal Takeover Regulation*, 34 FLA. ST. U. L. REV. 211, 240 (2007). However, Professor Davidoff also notes that once the SEC "released this pressure valve," the Delaware Supreme Court issued holdings limiting *Revlon*'s application. *See id.* Nevertheless, the result is that both hostile and friendly transactions may warrant a stricter level of review. *See id.*

[42] Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985).

[43] *Id.* at 954-55.

[44] *Id.* at 955.

[45] *Id.*

[46] *Unocal*, 493 A.2d at 955.

[47] *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1387-88 (Del. 1995) (emphasizing the bifurcated nature of the process).

[48] *Id*. The Delaware Supreme Court has further defined a coercive response to be one "aimed at forcing upon stockholders a management-sponsored alternative to a hostile offer." Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 935 (Del. 2003). A preclusive response is one that "deprives stockholders of the right to receive all tender offers or precludes a bidder from seeking control by fundamentally restricting proxy contests or otherwise." *Id.*

[49] *Unitrin*, 651 A.2d at 1387-88 (quoting Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34, 45 (Del. 1994)).

A year following its decision in *Unocal*, the Delaware Supreme Court issued another seminal decision—*Revlon v. MacAndrews & Forbes Holdings, Inc.*[50] Applying *Unocal*, the court in that case found Revlon's entry into an agreement with a white knight had effectively ended an active bidding contest for control of Revlon that had been occurring between the white knight and a hostile bidder.[51] The Delaware Supreme Court declared the deal protection devices in the agreement impermissible because they were entered into precisely when the "board's primary duty [had become] that of an auctioneer responsible for selling the company to the highest bidder."[52] The court further stated that, when the break-up of the company becomes inevitable, "[t]he directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company."[53] This auctioneering obligation has come to be known as a board's "*Revlon* duties."[54] However, the Delaware Supreme Court has since clarified that "there are no *special and distinct* '*Revlon* duties.'"[55] Instead, these so-called "*Revlon* duties" are simply a way of referring to "a particular application of the directors' general duties of care and loyalty" with the responsibility being "to maximize short term value" when a company is in "*Revlon* or sale mode."[56]

While *Revlon* actually involved a hostile bidder and the court was applying the *Unocal* standard of review, Delaware courts have extended these *Revlon* duties to negotiated transactions.[57] Moreover, although not

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[50]506 A.2d 173 (Del. 1986).

[51]*Id.* at 175-76.

[52]*Id.* at 184.

[53]*Id.* at 182.

[54]Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1288 (Del. 1989).

[55]*Id.* (emphasis added).

[56]KLING & NUGENT, *supra* note 8, § 4.04[3], at 4-50. The Delaware Supreme Court made this clear in *Mills Acquisition Co. v. Macmillan, Inc.*, saying:

> We stated in *Revlon,* and again here, that in a sale of corporate control the responsibility of the directors is to get the highest value reasonably attainable for the shareholders. Beyond that, there are no special and distinct "Revlon duties". Once a finding has been made by a court that the directors have fulfilled their fundamental duties of care and loyalty under the foregoing standards, there is no further judicial inquiry into the matter.

559 A.2d 1261, 1288 (Del. 1988) (citation omitted).

[57]KLING & NUGENT, *supra* note 8, § 4.04[3], at 4-51 (describing the willingness of the courts, as illustrated by Delaware jurisprudence, to apply the *Unocal* standard even to transactions bearing greater hallmarks of mutual intent); Clark W. Furlow, *Reflections on the Revlon Doctrine*, 11 U. PA. J. BUS. L. 519, 549 (2009) ("Over time, the fact that *Revlon* involved a specter of entrenchment lost its significance, and the '*Revlon* doctrine' came to stand for the idea that all challenged transaction [sic] involving the sale of the company must be subject to enhanced scrutiny.").

free from controversy, Delaware courts also have extended the *Unocal*-enhanced scrutiny standard to deal protection devices entered into during a negotiated transaction.[58] Hence, in negotiated transactions like the ones addressed in this Article, standstills are subject to the *Unocal*-enhanced scrutiny analysis while a board's sales process and actions during the pre-closing period may be subject to the enhanced *Revlon* standard.[59]

Of particular importance for this Article, a recurring question over the past couple of decades has been: what types of transactions trigger *Revlon duties*?[60] To answer this question, Delaware courts have focused on the type of consideration used in the transaction.[61] It is well accepted under Delaware law that an all-cash transaction triggers *Revlon*, as "there is no tomorrow" for the target's shareholders.[62] More specifically, the target's shareholders "will forever be shut out from future profits generated by the resulting entity as well as the possibility of obtaining a control premium in a subsequent transaction."[63] In addition, Delaware jurisprudence makes it clear that a stock-for-stock transaction will not trigger *Revlon* unless the end result of the transaction is that one entity or person acquires a controlling block of shares in the target, making the target's remaining shareholders minority owners in the surviving corporation.[64] But when the consideration

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[58] *See, e.g.*, Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 932 (Del. 2003). *But see* STEVEN M. DAVIDOFF, GODS AT WAR: SHOTGUN TAKEOVERS, GOVERNMENT BY DEAL, AND THE PRIVATE EQUITY IMPLOSION 236 (2009) (arguing Delaware Chancery Court decisions since *Omnicare* have narrowed its applicability "where controlling shareholders can't act by written consent immediately or the extreme circumstance . . . where a board of a company attempts to pass control to an unaffiliated third party without a shareholder vote").

[59] *See, e.g.*, *Omnicare*, 818 A.2d at 932 ("[Under *Unocal*] [d]efensive devices taken to protect a merger agreement executed by a board of directors are intended to give that agreement an advantage over any subsequent transactions that materialize before the merger is approved by the stockholders . . . . This is analogous to the favored treatment that a board of directors . . . give[s] to encourage an initial bidder when it discharges its fiduciary duties under *Revlon*.").

[60] *See, e.g.*, *In re* Smurfit-Stone Container Corp. S'holder Litig., 2011 WL 2028076, at *12 (Del. Ch. May 20, 2011) ("[A] question of much ongoing debate . . . is *when* does a corporation enter *Revlon* mode such that its directors must act reasonably to maximize short-term value of the corporation for its stockholders.").

[61] *See* DAVIDOFF, *supra* note 58, at 236 (describing the flexibility dealmakers have in stock transactions because *Revlon* is generally not applicable). *See also* Transcript of Court's Ruling on Plaintiffs' Motion for a Preliminary Injunction, at 4, Steinhardt v. Howard-Anderson, C.A. No. 5878-VCL (Del. Ch. Jan. 24, 2011) *available at* www.alston.com/files/docs/occam_Ruling.pdf. (recognizing Delaware jurisprudence focuses on change of control which results in debates regarding what amount of cash consideration triggers change of control).

[62] *See Smurfit-Stone*, 2011 WL 2028076, at *13.

[63] *Id.*

[64] *See, e.g.*, Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 42 (Del. 1994) ("In the absence of devices protecting minority stockholders, stockholder votes are likely to become mere formalities where there is a majority stockholder.") (footnote omitted).

used in the transaction is a mix of cash and stock, the Delaware courts have yet to establish a bright-line rule. For example, the Delaware Supreme Court has held that when the consideration is 33% cash, *Revlon* is not triggered, but it has not yet addressed deals in which cash exceeds 33%.[65] Recently, the Delaware Court of Chancery stated "even though the Delaware Supreme Court has not yet addressed this issue directly," a deal in which cash amounts to 50% of the consideration, likely triggers *Revlon*.[66] Moreover, the Court of Chancery has also held that where cash amounts to 62% of the consideration, *Revlon* is likely triggered.[67]

Despite the auctioneering language in *Revlon*, the Delaware Supreme Court has also acknowledged, "no single blueprint" exists for a board to satisfy its *Revlon* duties.[68] In addition, the Delaware courts have recognized that not every sale requires a full-blown auction process but rather the board's decision to sell the company to a particular bidder must meet "a reasonableness standard."[69] As the late, prominent M&A investment banker, Bruce Wasserstein, once wrote, "it can be helpful to think of the range of possibilities in terms of two types—the classic two-step auction and the negotiated sale."[70] Pursuant to Delaware case law, this latter type—the negotiated sale—can follow a more limited market canvass pre-signing or, in some cases, the target's board can rely exclusively on post-signing sales activities to ensure the negotiated sale reflects an adequate sale price.[71]

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[65] *See In re* Santa Fe Pac. Corp. S'holder Litig., 669 A.2d 59, 65, 70-71 (Del. 1995) (holding *Revlon* was not triggered in a transaction where cash accounted for 33% of consideration).

[66] *Smurfit-Stone*, 2011 WL 2028076, at *11.

[67] *In re* Lukens Inc. S'holders Litig., 757 A.2d 720, 725, 732 n.25 (Del. Ch. 1999).

[68] Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989).

[69] *See* Transcript of Court's Ruling on Plaintiffs' Motion for a Preliminary Injunction, at 6, Steinhardt v. Howard-Anderson, C.A. No. 5878-VCL (Del. Ch. Jan. 24, 2011) *available at* www.alston.com/files/docs/occam_Ruling.pdf. ("[Revlon] was a Cunian paradigm shift if there ever was one. We had language in there like 'auction duty, radically altered state,' really seemingly heavy duty stuff. We now know it's a reasonableness standard."); *see also In re* Netsmart Techs., Inc. S'holders Litig., 924 A.2d 171, 192 (Del. Ch. 2007) ("Unlike the bare rationality standard applicable to garden-variety decisions subject to the business judgment rule, the *Revlon* standard contemplates a judicial examination of the reasonableness of the board's decision-making process."); *Barkan*, 567 A.2d at 1286 ("*Revlon* does not demand that every change in the control of a Delaware corporation be preceded by a heated bidding contest.").

[70] BRUCE WASSERSTEIN, BIG DEAL: MERGERS AND ACQUISITIONS IN THE DIGITAL AGE 746 (2000).

[71] For a more detailed description of pre-signing market canvasses and post-signing market checks, see Christina M. Sautter, *Shopping During Extended Store Hours: From No Shops to Go-Shops - The Development, Effectiveness, and Implications of Go-Shop Provisions in Change of Control Transactions*, 73 BROOK. L. REV. 525, 539-53 (2008); *see also* DAVIDOFF, *supra* note 58, at 237-39 (discussing post-signing market checks in the context of a corporate board's *Revlon* duties). *See also In re* OPENLANE, Inc. S'holders Litig., 2011 WL 4599662, at *5 (Del. Ch. Sept.

Thus, an extensive bidding process does not necessarily precede every merger. However, if the target does not engage in a traditional value maximization tool like an auction or market check, "[the] board must possess an impeccable knowledge of the company's business for the Court to determine that it acted reasonably."[72] As such, as discussed in Part IV, a Delaware court may be more inclined to allow a target board to take certain actions, or not take certain actions, with respect to a standstill if the target engages in a more extensive pre-signing sales process.

### B. *The Roles of Confidentiality and Standstill Agreements in the Sales Process*

As is evident from the foregoing discussion, target companies that choose either a full-blown auction process or a more limited pre-signing bidding process are invariably presented with the question as to what procedures should be followed to ensure a fair bidding process that still guarantees the most value for the company.[73] Along these lines, target companies must also contend with the possibility of overbidding by losing bidders after the process has been completed and the winning bidder has entered into an agreement.[74] When targets are presented with these issues, the overwhelming majority of them choose to execute a confidentiality agreement including a standstill provision.[75]

Prior to gaining access to non-public information through due diligence pre-signing, most bidders must execute a confidentiality agreement.[76] The confidentiality agreement embodies two conflicting

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30, 2011) (describing traditional value maximization tools as including, inter alia, auctions).

[72]*In re* OPENLANE, Inc. S'holders Litig., 2011 WL 4599662, at *5.

[73]*See* Sautter, *supra* note 71, at 539-53 (acknowledging that although a public auction is the surest way to satisfy *Revlon*, there are scenarios where that sort of transaction is not desirable and therefore a corporate board may want to elect some other method, such as a more limited pre-signing market canvass, and thereafter discussing what transactions have been upheld by the Delaware courts).

[74]*See, e.g.*, *In re* Topps Co. S'holders Litig., 926 A.2d 58, 88 (Del. Ch. 2007) (discussing the complications that can arise in a multiple-bidder scenario, including access to proprietary information).

[75]In fact, Chancellor Strine has suggested—as Vice Chancellor—that a corporation running a bidding process may even be "mandated" to adopt procedures to ensure the confidentiality of information and an "orderly auction." *Id.* at 91. However, former Chancellor, now Professor William T. Allen recently asked whether participation in a market canvass or full auction should be "conditioned on willingness to sign a [confidentiality agreement], standstill or bid procedures letter . . . ." Allen, *supra* note 21, at 52.

[76]KLING & NUGENT, *supra* note 8, § 9.01, at 9-2 ("[T]he Buyer and the Seller ordinarily agree to enter into a confidentiality agreement which will establish the rules governing the Buyer's . . . examination and use of confidential information concerning the target Company.") (footnote omitted).

interests.[77] Namely, the target wants to facilitate the bidder's ability to make a "full bid," but the target also wants to protect itself from the possible repercussions of key business information disclosure.[78] Thus, confidentiality agreements have become "both standard and standardized" business practice in M&A transactions.[79] Furthermore, as the United States District Court for the Northern District of Texas notes, if confidentiality agreements could not be used and relied upon, "it could substantially disrupt the present process of negotiating and consummating business acquisitions and mergers."[80] Often a key component of a confidentiality agreement, which assists the negotiation process in running smoothly, is a standstill.[81]

Standstill agreements first surfaced "in the early 1980s," and appear to have been a direct answer to the hostile takeover activity prevalent during that period.[82] They developed as a basic contract between a corporation and a substantial stockholder that limited the ability of the shareholder to acquire and gain ownership of shares up to a certain amount.[83]

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[77] *Id.*

[78] *Id.*

[79] *See, e.g.*, David Marcus, *The Case of Travis Laster*, THE DEAL MAGAZINE, Mar. 25, 2011, *available at* http://www.thedeal.com/magazine/ID/038817/2011/the-case-of-travis-laster.php (stating that the use of confidentiality agreements in the M&A context are "both standard and standardized").

[80] Gen. Portland, Inc. v. LaFarge Coppee S.A., 1981 WL 1408, at *3 (N.D. Tex. Aug. 28, 1981).

[81] *See* Lawlor, *supra* note 1, at 7 (noting that standstill agreements involving publicy owned companies are prevalent in the M&A context and characterizing them as "corporate peace treaties").

[82] *See* Subramanian, *supra* note 17, at 659 n.164; *see also* Lawlor, *supra* note 1, at 7 (noting standstills have been used in M&A "for decades"). In his 2003 article, *Bargaining in the Shadow of Takeover Defenses*, Professor Guhan Subramanian noted outside of "technical discussions of standstill agreement mechanics in practitioner-oriented publications, . . . standstill agreements have been mentioned only in passing in the law review literature over the past ten years." Subramanian, *supra* note 17, at 659 n.164. In the same article, Professor Subramanian cited to three articles on standstills published in the 1980s: Joseph W. Bartlett & Christopher B. Andrews, *The Standstill Agreement: Legal and Business Considerations Underlying a Corporate Peace Treaty*, 62 B.U. L. REV. 143 (1982); Larry Y. Dann & Harry DeAngelo, *Standstill Agreements, Privately Negotiated Stock Repurchases, and the Market for Corporate Control*, 11 J. FIN. ECON. 275 (1983); and Steven A. Baronoff, Note, *The Standstill Agreement: A Case of Illegal Vote Selling and a Breach of Fiduciary Duty*, 93 YALE L.J. 1093 (1984). Subramanian, *supra* note 17, at 659 n.164. Professor Subramanian dedicated a small portion of *Bargaining in the Shadow of Takeover Defenses* to standstills, focusing on the role they play in negotiations. *See id*. at 659-62 (discussing standstills in the context of asymmetric information among bidders). However, I was unable to locate any other academic articles published since the three articles cited to by Professor Subramanian that provided a more in-depth analysis of standstills. Hence, this Article is the first academic article devoted solely to standstills to be published since the 1980s, according to this Author's research.

[83] *See, e.g.*, Dann & DeAngelo, *supra* note 82, at 276 (discussing the early evolution of the

Toward the latter half of the 1980s, standstill agreements began to be used in friendly acquisitions, and usually in connection with a confidentiality agreement.[84] Selling corporations in auctions and other pre-signing bidding processes began to ask bidders to execute a standstill in exchange for access to the seller's due diligence materials.[85] Today, most confidentiality agreements contain standstills or, if they do not, are accompanied by a standstill agreement separately executed as a stand-alone document.[86] No matter the form in which they appear, standstills are *de rigueur*.[87] For many target companies, a bidder's willingness to agree to a standstill in exchange for the provision of confidential, non-public information shows the target that the bidder is a serious one.[88] A former co-head of Global Mergers & Acquisitions at Lehman Brothers described standstills as "the cost of entry" into negotiations.[89] Some have even suggested that only the biggest M&A players can avoid executing a

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standstill).

[84]*See* Alan C. Stephenson, *Auctions: Companies in Play and at Work*, *in* 20TH ANNUAL INST. ON SEC. REGULATION, at 445 (PLI Corp. Law & Practice Group, Course Handbook Series No. B4-6846, 1988) (noting in 1988 that companies in an auction "may require any bidders execute a confidentiality and standstill agreement prior to the seller's delivery of confidential financial information to a bidder"); *see also* E. Norman Veasey et al., *The Delaware Business Judgment Rule: The Duty to Auction a Corporation and Lock-Ups in Contested Takeovers*, *in* HOSTILE BATTLES FOR CORPORATE CONTROL 1989, at 336 (PLI Corp. Law & Practice, Course Handbook Series No. B4-6869, 1989) (discussing Yanow v. Scientific Leasing, Inc., 1988 WL 8772 (Del. Ch. Feb. 5, 1988), *reprinted in* 13 DEL. J. CORP. L. 1273 (1988), where defendant, in its quest for a bidder, allowed potential bidders access to confidential information upon their signing of confidentiality and standstill agreements).

[85]*See* sources cited *supra* note 84; Subramanian, *supra* note 17, at 659-60 (explaining the functions of a standstill in a negotiation setting, where the potential acquirer agrees not to "increase its stake in the target, conduct a proxy contest to replace the target's board, or make a tender offer for the target's stock without the approval of the target board, for a specified period of time . . . [and] [i]n exchange, the acquirer gains access to the target's internal documents . . . allow[ing] it to conduct due diligence").

[86]*See* Lawlor, *supra* note 1, at 7 (noting most confidentiality agreements contain a standstill provision).

[87]*See supra* text accompanying note 1.

[88]*See* Nicole E. Clark, *Preliminary Agreements*, *in* DOING DEALS 2009: UNDERSTANDING THE NUTS & BOLTS OF TRANSACTIONAL PRACTICE, at 80-81 (PLI Corp. Law & Practice, Course Handbook Series No. 18777, 2009) (stating that the standstill agreement is of "primary concern" to the target company because it strives to thwart the potential acquirer from creating any disruptions to the negotiations process); Meryl S. Rosenblatt, *Letters of Intent and Exclusivity, Confidentiality and Standstill Agreements*, *in* DRAFTING CORPORATE AGREEMENTS 2004-2005, at 237 (PLI Corp. Law & Practice, Course Handbook Series No. B0-01K0, 2004) ("[A] target may require a potential buyer to enter into a standstill at the outset of merger negotiations to ensure that the buyer remains committed to a friendly negotiated transaction and is prevented from pursuing a hostile alternative.").

[89]Subramanian, *supra* note 17, at 660 (describing the understood expectation of a standstill agreement).

standstill.[90] Wasserstein summarized the view of many sellers in the M&A field when he wrote, "[t]he willingness to sign a standstill . . . serves as a kind of litmus test, an indication of a bidder's true intentions."[91] Essentially, the view among practitioners is that a potential buyer has a choice between preserving the right to bring a hostile transaction and foregoing that right by signing a standstill.[92]

The exact terms of standstills vary depending on factual context and are anything but boilerplate. Traditionally, standstill restrictions take the form of a combination of some or all of the following: 1) limitations on purchases of securities or assets of the target without the target's prior consent; 2) the solicitation of proxies to prevent the replacement of the target's management or from otherwise exercising control over management; and 3) making tender offers for the target's securities or making other unsolicited proposals for business combination transactions.[93] More simply, these restrictions are used to further the goals of "avoiding disruption" in negotiations, to control the bidding process, and to act as deal protection devices against later overbids.[94] To this end, although there are other situations in which a standstill may be used, this Article focuses on standstills executed "in connection with the exchange of confidential information as a prelude to a possible corporate combination."[95]

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[90] *Id.* ("As you might expect, the companies that can get away with [foregoing signing a standstill agreement] are the bigger gorillas in the jungle.") (quoting Interview by Guhan Subramanian with Stephen Munger, Co-Head of Global Mergers & Acquisitions, Morgan Stanley, in New York, N.Y. (June 3, 2003)).

[91] WASSERSTEIN, *supra* note 70, at 689.

[92] *See, e.g.*, Subramanian, *supra* note 17, at 662 (describing inevitable judgment call buyers must make when asked to execute a standstill agreement). A former Global Head of Mergers & Acquisitions at Bear Sterns best summarized the buyers' decision as:

> [Y]ou could preserve your flexibility to pursue a hostile deal, in which case you do not move forward with the bilateral discussions because the target is not willing to share confidential information with you unless you agree to the standstill. Alternatively, you try to modify the standstill as much as you can, but fundamentally give up the basic ability to launch an unsolicited offer.

*Id.* (quoting Interview by Guhan Subramanian with Louis P. Friedman, Former Global Head of Mergers & Acquisitions, Bear, Stearns & Co., in New York, N.Y. (June 2, 2003)).

[93] Marla A. Hoehn, *Letters of Intent, Confidentiality and Standstill Agreements*, *in* DRAFTING CORPORATE AGREEMENTS 2002-2003, at 78 (PLI Corp. Law & Practice Handbook Series No. B0-01K0, 2002).

[94] *See id.* at 79-80 (discussing how such protections facilitate smoother transactions); *see also* Robert E. Spatt & Peter Martelli, *The Four Ring Circus-Round Fifteen; A Further Updated View of the Mating Dance Among Announced Merger Partners and an Unsolicited Second or Third Bidder*, SIMPSON THATCHER & BARTLETT LLP 1, 35 (Mar. 17, 2011), http://www.stblaw.com/Four
RingCircus2011.pdf (noting that the intended goal of standstills is to prevent deal jumping).

[95] Kenneth J. Bialkin, *The Use of Standstill Agreements in Corporate Transactions*,

Alone, confidentiality agreements provide for a defense against hostile transactions because the "permitted uses and users" of confidential information in a confidentiality agreement generally do not include using such information to formulate a hostile offer.[96] Thus, despite the importance of standstills, a standstill provision can be removed from the confidentiality agreement, yet the confidentiality agreement can still stand and provide protection in some cases.[97] Conversely, a standstill provision can stand-alone and bind the parties, even when neither party has exchanged confidential information with the other, following the execution of a confidentiality agreement.[98] Thus, unless the agreement between the parties provides otherwise, a standstill will be effective as of the time of its execution.[99]

Although both confidentiality agreements and standstills can stand alone, confidentiality agreements do not fulfill the evidentiary function that standstill agreements do in the context of a hostile takeover.[100] More specifically, showing a violation of a standstill is easier than showing a violation of a confidentiality agreement.[101] In fact, some commentators have stated that courts "may view the mere existence of a standstill as eviden[ce] of the parties' intentions not to proceed on an unfriendly basis."[102] This may

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*in* THIRTEENTH ANNUAL INSTITUTE ON SECURITIES REGULATION 1983, at 34 (PLI Corp. L. & Practice, Course Handbook Series No. B2-1281, 1983).

[96]Rosenblatt, *supra* note 88, at 231, 237. Of particular significance is the recent Delaware Supreme Court case of *Martin Marietta Materials, Inc. v. Vulcan Materials Co.*, 2012 WL 2783101 (Del. July 10, 2012). There, Martin Marietta and Vulcan entered into two confidentiality agreements, neither of which contained an explicit standstill provision. *Id.* at *2, *7. The confidentiality agreements "permitted either party to *use* the other party's Evaluation Material, but '*solely for the purpose of evaluating a Transaction.*'" *Id.* at *2. Further, "'Transaction' [was defined] as 'a possible business combination transaction . . . between [Martin] and [Vulcan] or one of their respective subsidiaries.'" *Id.* The Supreme Court upheld the Court of Chancery's finding that a "possible business transaction between" the parties included only friendly, negotiated transactions. *Id.* at *7, *10 Thus, Martin Marietta was prevented from using Vulcan's confidential information in a hostile takeover of Vulcan. *Id.* at *56.

[97]*See* KLING & NUGENT, *supra* note 8, § 9.05, at 9-18 ("The message is clear that by signing a confidentiality agreement, even without a standstill provision, a Buyer may be foregoing its opportunity to proceed to acquire the Seller on any basis other than a friendly negotiated one in which the Seller will agree to the Buyer's disclosure of pertinent material information concerning the Seller in the Buyer's possession.").

[98]Aurizon Mines Ltd. v. Northgate Minerals Corp. (2006), 57 B.C.L.R. 4th 137, paras. 65-66 (Can. B.C. S.C.), *aff'd*, 55 B.C.L.R. 4th 203 (Can. B.C. C.A.); *see also Martin Marietta*, 2012 WL 2783101, at *8 ("Standstill prohibitions do not require, or in any way depend upon, a contracting party's use or disclosure of the other party's confidential, nonpublic information.").

[99]*Aurizon Mines Ltd.*, 57 B.C.L.R. 4th at para. 64.

[100]*See, e.g.*, Rosenblatt, *supra* note 88, at 237.

[101]*Id.*

[102]KLING & NUGENT, *supra* note 8, § 9.04, at 9-14.

account for one of the reasons these types of agreements have become so pervasive in the M&A realm.

Standstills usually span from one to five years, depending on factual context.[103] Typically, a target wants the standstill to last until the sales process ends or as long as the bidder has material non-public information.[104] Oftentimes, the bidder will demand the standstill expire either when a third party attempts to acquire the target, or upon the target's entry into an agreement with another party.[105] Generally, "auction-style standstill agreements last only one or two years, on the basis that the confidential information to be provided to the bidders will have useful currency for only a relatively short time."[106] Even shorter standstills with expirations between six months and one year are not uncommon; although, one year may be the norm.[107] As a result of these lengths, most standstills executed during the pre-signing period will last beyond the target's signing of a definitive acquisition agreement with another acquirer or a "winning bidder."[108] Thus, the standstill's interaction with provisions contained in the definitive merger agreement become of primary importance.

### C. *Fiduciary Outs & Their Correlation to Standstills*

Regardless of whether the target performs an auction or negotiates with only one bidder, the resulting merger agreement will be publicly

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[103] Rosenblatt, *supra* note 88, at 240.

[104] *Id.*

[105] *Id.* ("[A bidder may require the standstill] terminate . . . upon the filing of a Schedule 13D by a third party disclosing an acquisition of a specified threshold percentage of the target's voting securities, upon commencement of a tender offer or a proxy contest for the election of directors, or the execution of an agreement to acquire the target or its assets.").

[106] Lawlor, *supra* note 1, at 11. Some argue this one-to-two-year period may not be sufficient, depending on the type of information at issue. For example, practitioner William Lawlor argues this period may be "woefully short if the target is conveying crown jewel information." *Id.*

[107] Subramanian, *supra* note 17, at 660 & n.165; *see also The "Standstill Agreement" in Public Company Mergers: A Mock Negotiation*, *reprinted in* THE M&A JOURNAL, *available at* http://www.lawseminars.com/materials/07MACA/New%20Era%202007%20binder%20bkup%20docs/10%20%2The%20Standstill%20Agreement%20in%20Public%20Company%20Mergers-Mock%20Negotiation.pdf (participants at mock negotiation of standstill agreement stating between one year and two years is a normal standstill length and stating six months is not likely helpful). If the standstill relates to a significant shareholder, however, even if said shareholder is known as an activist shareholder, those standstills can last from five to ten years or even longer. Lawlor, *supra* note 1, at 11.

[108] Lawlor, *supra* note 1, at 7.

announced within a day or two of execution.[109] Once the agreement is publicly announced, there is a possibility that a third party may attempt to overbid.[110] Recent statistics reveal that when third parties submit competing offers during the pre-closing period, about a third of those third party offers have been successful.[111] But, even if the third party offer is unsuccessful, its mere presence tends to boost the price beyond the initial bid.[112]

A public company merger agreement normally contains a number of deal protection devices to prevent, or at least deter such overbids, but chief among them is a no-shop provision paired with a fiduciary out.[113] The no-shop provision, or non-solicitation provision, prevents the target from soliciting offers between signing and closing.[114] However, the fiduciary out allows a target's board of directors to negotiate with a third party who makes an unsolicited offer if the third party's offer is either a "Superior Offer," or if it is reasonably likely to become a "Superior Offer" as defined by the merger agreement.[115] In addition, the termination provisions typically work hand-in-hand with the fiduciary out and permit the target company to terminate the existing agreement in favor of a third party offer if the board determines it would be a violation of its fiduciary duties not to do so.[116] Many times the fiduciary out or the termination fee triggers will require that the unsolicited offer be a bona fide one.[117] In addition, this bona fide

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[109] Audra L. Boone & J. Harold Mulherin, *Do Termination Provisions Truncate the Takeover Bidding Process?*, 20 REV. FIN. STUD. 461, 475 (2007).

[110] Bainbridge, *supra* note 31, at 16 ("Where the target's board accepts a low initial offer, a second bidder may succeed by offering shareholders a higher-priced alternative.").

[111] Kelley D. Parker, *Deal Protection and Deal Jumping: Lessons Learned From the Recent Past*, *in* DOING DEALS 2011: THE ART OF M&A TRANSACTIONAL PRACTICE, at 329 (PLI Corp. Law & Practice, Course Handbook Series No. 28650, 2011) (stating in 2010 only three out of ten deals involved a third party bidder successfully breaking up an initial transaction).

[112] *See infra* Part III.A.1 (discussing an example of a case where an initial buyer increased its offer in the face of a third party overbid).

[113] Sautter, *supra* note 33, at 72-73.

[114] *Id.* ("[The no-shop] is a covenant preventing a target company from actively soliciting offers from third parties after the signing of a definitive acquisition agreement.").

[115] *Id.* at 73.

[116] *Id.* The standard for terminating an existing agreement will vary depending on the language of the fiduciary out, which itself varies from deal-to-deal. As an alternative to the "violation" language, some fiduciary outs require the action simply be "inconsistent" with the board's fiduciary duties. *Compare* Sun Microsystems, Inc., Preliminary Proxy Statement (Schedule 14-A), § 6.03(b) (May 12, 2009) ("[T]he failure to take such action would be *inconsistent with its fiduciary duties* under Applicable Law.") (emphasis added), *with* NetLogic Microsystems, Inc., Agreement and Plan of Merger Reorganization (Form 8-K), § 6.9(a), Exhibit 2.5 (June 4, 2009) (providing the target board may negotiate with or provide information to third parties upon the board's good faith determination, and failure to act without such a determination could result in a breach of fiduciary duties).

[117] An example of a no-shop fiduciary out conditioning performance on the unsolicited

language is often found in the definition of "Superior Offer" or "Superior Proposal," which plays a key role in whether a board may engage in negotiations with a third party, provide information to a third party, and possibly terminate the agreement in favor of the third party offer.[118] Delaware courts have yet to interpret the meaning of "bona fide" in the context of a third party offer. Accordingly, they have never addressed whether a third party offer made in contravention of a standstill could be a bona fide offer. Part IV.A of this Article addresses how Delaware courts might resolve this unanswered question.

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offer being bona fide is as follows:

> [O]nly until the Requisite Company Vote is obtained, the Company and its board of directors shall be permitted to:
>
> (i) (A) engage in discussions and negotiations with a Person who has made a *bona fide* unsolicited Company Takeover Proposal and (B) furnish or disclose any non-public information relating to the Company. . . , in each case if the board of directors of the Company determines in good faith, after consultation with the Company Financial Advisor, that such Company Takeover Proposal could reasonably be expected to lead to a Superior Proposal . . . .

SiRF Tech. Holdings, Inc., Agreement and Plan of Merger (Form 8-K) § 5.4(d), Exhibit 2.1 (Feb. 10, 2009) (emphasis added). In addition, an example of a termination fee trigger containing bona fide language is contained in HeartWare International, Inc.'s agreement to be acquired by Thoratec Corporation. That provision states:

> (iv) If this Agreement is terminated [because stockholder approval was not obtained then] . . . in the event that, (A) at any time after the date of this Agreement and prior to such termination any Third Party shall have publicly made, proposed, communicated or disclosed an intention to make a *bona fide* Acquisition Proposal, which *bona fide* Acquisition Proposal was not retracted or rescinded prior to such termination and (B) within twelve (12) months of the termination of this Agreement, the Company . . . enters into a definitive agreement with respect to an Acquisition Proposal . . . the Company shall pay . . . the Company Termination Fee, such payment to be made upon the earlier to occur of the execution of a definitive agreement relating to, or consummation of, such Acquisition Proposal.

HeartWare Int'l, Inc., Agreement and Plan of Merger (Form 8-K) § 8.03(a)(iv), Exhibit 2.1 (Feb. 13, 2009) (emphasis added).

[118] An example of bona fide language appearing in a Superior Proposal definition is present in SiRF Technology Holdings, Inc.'s merger agreement, which provides:

> "*Superior Proposal*" means any *bona fide* written Company Takeover Proposal . . . which the board of directors . . . determines in good faith (after consultation with its legal counsel and the Company Financial Advisor) to be more favorable to the stockholders of the Company from a financial point of view than the transactions contemplated by this Agreement, taking into consideration the conditions to the consummation of such Company Takeover Proposal and the financial, legal, regulatory and other aspects of such Company Takeover Proposal.

SiRF Tech. Holdings, Inc., Agreement and Plan of Merger (Form 8-K) § 8.1(y), Exhibit 2.1 (Feb. 10, 2009) (second emphasis added).

## III. STANDSTILLS IN ACTION

A limited number of cases have examined the validity of standstills in the sales process.[119] Courts that do take on the issue tend to address standstills as a part of the larger sales process, so that the validity or the alleged improper use of a standstill is usually only one of multiple challenges the court is addressing.[120] Thus, few cases have addressed standstills at length.[121] Courts have upheld a target's decision to have potential bidders execute a standstill as a precondition to obtaining access to confidential information, even when the deal results in a change of control and heightened scrutiny is applicable.[122]

### A. *Topping Bids in Contravention of a Standstill*

The Delaware courts have never addressed a target board's actions in the wake of a topping bid that violates an existing standstill. A few other U.S. courts, as well as Canadian courts, have confronted the issue.[123] This section explores those cases as well as other overbids made in contravention of a standstill that went unlitigated.

#### 1. The Importance of Contract Language and Bona Fide Offers

HCP, Inc. and Ventas, Inc.'s battle[124] for Sunrise REIT (hereinafter "Sunrise") illustrates a number of issues relating to standstills, including the requirement that a superior offer be bona fide and the promise not to grant a standstill waiver.[125] This contest began in late 2006, when Sunrise, a Canadian real estate investment trust whose units are traded on the Toronto

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[119] *See* City Capital Assocs. L.P. v. Interco Inc., 551 A.2d 787, 803 n.21 (Del. Ch. 1988) ("These [standstill] agreements which always play an important role . . . rarely get litigated.").

[120] *Id.* (remarking that the standstill is only one of several documents pertinent to a court's investigation into the matter at hand).

[121] *See e.g.*, *id.* (noting that courts often tend to side-step extensive discussion of standstill agreements in favor of focusing on other aspects of the deal).

[122] *See* Rosenblatt, *supra* note 88, at 241 ("[T]he validity of the standstill will be subject to heightened scrutiny but will likely be upheld so long as it is part of a good faith overall strategy to maximize shareholder value.").

[123] *E.g.*, Ventas, Inc. v. HCP, Inc., 647 F.3d 291 (6th Cir. 2011); Ventas, Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. 3d 254 (Can. Ont. C.A.).

[124] *Ventas*, 647 F.3d at 297-303 (recounting the contentious record between the two bidders).

[125] *Id.* at 321.

Stock Exchange, "conducted a confidential auction of its assets."[126] The auction was designed as a two-stage process with the goal of maximizing the value received for the units.[127] The first stage of the auction provided several possible buyers the opportunity to submit non-binding bids.[128] Sunrise then narrowed the field based on the non-binding bids, and allowed those participants to submit final bids for the second round.[129] As a part of the second stage of the auction, seven parties, including HCP and Ventas, executed confidentiality agreements containing a standstill provision.[130] HCP's standstill prevented it from making an offer to purchase the stock or assets of Sunrise for eighteen months without Sunrise's prior written consent.[131] Also as part of the standstill, HCP agreed not to request that Sunrise waive any portion of it.[132] The Ventas confidentiality agreement was substantially the same as HCP's, and also included a standstill.[133] But Ventas' standstill "ceased to apply if, amongst other things, Sunrise REIT entered into an agreement to sell more than 20% of its units or assets to a third party."[134] Neither HCP nor Ventas were parties to the other's confidentiality agreements.[135] With respect to waivers of the conditions contained in the confidentiality agreements, including presumably the standstill provision, the confidentiality agreements contained the following provision: "No provision of this agreement can be waived except by means of a written instrument that is validly executed on behalf of the party hereto granting the waiver and that refers specifically to the particular provision or provisions being waived."[136]

The bids submitted during the first stage of the auction were conditioned on reaching an agreement with Sunrise Senior Living, Inc. (SSL), a company that managed Sunrise's real estate.[137] Sunrise invited both HCP and Ventas to participate as the only bidders in the second stage of the

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[126] *Id.* at 297; *see also Ventas*, 85 O.R. 3d at para. 1 (stating Sunrise units were traded on the Toronto Stock Exchange).

[127] *Ventas*, 85 O.R. 3d at para. 2.

[128] *Ventas*, 647 F.3d at 297.

[129] *Id.*

[130] Ventas Inc. v. Sunrise Senior Living Real Estate Investment Trust (2007), 29 B.L.R. 4th 292, para. 4 (Can. Ont. Sup. Ct. J.).

[131] *Id.* at para. 5.

[132] *Id.*

[133] *Id.* at paras. 5-6.

[134] *Id.*

[135] Ventas, Inc. v. HCP, Inc., 647 F.3d 291, 297 (6th Cir. 2011).

[136] *Ventas*, 29 B.L.R. 4th at para. 5.

[137] *Ventas*, 647 F.3d at 297.

auction.[138] At this point, the problems seemed to begin. Ventas was able to reach an agreement with SSL, but HCP's negotiations with SSL "'blew up'" when another real estate portfolio that HCP owned but SSL managed "became intertwined in the Sunrise negotiations."[139] HCP did not submit a final bid for Sunrise and withdrew from the auction.[140] Ventas won the auction, agreeing to pay $15 per unit, or over $1.1 billion, pursuant to the Purchase Agreement announced on January 15, 2007.[141] The $15 figure represented a 50% premium over Sunrise's trading price prior to the deal announcement.[142]

The Sunrise-Ventas purchase agreement contained a no-shop provision preventing Sunrise from actively soliciting third party offers and from negotiating with or holding discussions with third parties regarding an actual or potential offer.[143] That provision was also paired with a fiduciary out for "Superior Proposals," a matching rights period of five business days, and a termination fee of $398 million.[144] Under the terms of the agreement, "Superior Proposal" meant "any unsolicited *bona fide* written Acquisition Proposal."[145] Moreover, the non-solicitation provision contained an anti-waiver clause that specifically stated Sunrise could not "release any Person from, or fail to enforce, any confidentiality or standstill agreement or similar obligations to Sunrise REIT or any of its Subsidiaries."[146]

Despite the non-solicitation provision, Sunrise's CEO "suggested to HCP['s] CEO . . . via email that HCP make a bid for Sunrise."[147] On

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[138] *Id.* This invitation was based on the preliminary bids that HCP and Ventas submitted during the first stage of the auction, in which HCP's preliminary bid was for $16.25 per unit and Ventas offered $13.25 per unit (both dollar amounts are in Canadian dollars). *Id.* & n.2. Hereinafter, unless otherwise noted, for the purposes of the Sunrise discussion, all dollar figures represent Canadian dollars.

[139] *Ventas*, 647 F.3d at 297-98. At trial in the United States District Court for the Western District of Kentucky, the parties could not agree as to who was at fault for the breakdown in negotiations. *Id.* at 298. On the one side, HCP argued that it had actually reached an agreement the week of January 8, 2007 with SSL, but then SSL "demanded 'concessions in separate negotiations concerning other properties.'" *Id.* From the other end, Ventas argued that the negotiations broke down because HCP was not acting in good faith and that HCP had submitted a counter-proposal to SSL at 8 p.m. the night before the final bid deadline containing "substantially different terms than [what] the parties had previously discussed." *Id.*

[140] *Ventas*, 647 F.3d at 298.

[141] *Id.* at 298-99.

[142] *Id.* at 299.

[143] Ventas Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 29 B.L.R. 4th 292, para. 13 (Can. Ont. Sup. Ct. J.).

[144] *Id.* at paras. 13-15.

[145] *Id.* at para. 14.

[146] *Id.* at para. 13.

[147] *Ventas*, 647 F.3d at 299.

February 14, 2007, HCP's CEO informed Sunrise's financial advisor that HCP was prepared to make an offer of $18 per unit.[148] HCP sent a letter to Sunrise including the details of its offer, as well as an unconditional but unsigned purchase agreement.[149] Although Sunrise requested that HCP not go public with its offer, HCP issued a press release announcing the offer.[150] The press release included a copy of the offer letter that HCP had sent to Sunrise, which contained a statement that it was "confident" that it would be able to reach an agreement "'with [SSL] on terms comparable to those entered into by Ventas.'"[151] However, after issuing the press release, HCP told Sunrise that reaching a deal with SSL was actually a condition of its offer.[152] On February 15, 2007, Sunrise's stock price increased to above $18 per unit despite a pre-market opening announcement by Sunrise that it would not consider HCP's offer "until 'such time as it receives a confirmation from HCP that their proposal is not conditional on [HCP] reaching an agreement with [SSL].'"[153]

Over the next seven days, Sunrise issued a number of press releases, including one referencing that HCP indicated it was ready to enter into an agreement with SSL that was "substantially similar" to the Ventas-SSL agreement.[154] This prompted Ventas to issue a press release on February 22, 2007 stating "that HCP's offer was barred by the Standstill Agreement, and was a conditional offer that was in fact less favorable than its own."[155] Also during this period, litigation involving the standstill agreement began.[156] First, on February 19, 2007, Sunrise filed an application in the Ontario Superior Court of Justice seeking a declaration clarifying whether HCP was allowed to negotiate with SSL.[157] On February 21, 2007, Ventas filed an application in the Ontario Superior Court "seeking a declaration that Sunrise was obligated to enforce its Standstill Agreement with HCP."[158]

Sunrise, Ventas, and HCP raised a number of arguments in support of their claims.[159] Sunrise argued that it had contracted for a fiduciary out in an

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[148] *Id.*
[149] *Id.*
[150] *Id.* at 299-300 (quoting HCP's press release announcing its proposal to acquire Sunrise).
[151] *Ventas,* 647 F.3d at 300.
[152] *Id.*
[153] *Id.* (noting that Feburary 15, 2007 was "the largest trading day in the history of Sunrise").
[154] *Id.*
[155] *Ventas,* 647 F.3d at 300.
[156] *Id.* at 301.
[157] *Id.*
[158] *Id.*
[159] *See* Ventas Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 29 B.L.R. 4th

attempt to maximize value for its unitholders.[160] Sunrise argued that Ventas' benefits from winning the auction were the matching rights and the $38 million termination fee.[161] Sunrise also argued that under the fiduciary out it "should be able to determine whether an Acquisition Proposal could be a Superior Proposal without being required to enforce a standstill provision."[162] It contended that, if Ventas wanted to prohibit a certain person who had taken part in the auction from submitting an offer, Ventas should have used "express language to do so."[163] HCP raised similar contentions as Sunrise but additionally argued that the no-shop and related fiduciary out did not prevent persons engaged in the auction process from making an offer.[164] HCP argued its offer was not made in violation of the no-shop provision as its offer was "unsolicited, and *bona fide*."[165]

Ventas took the opposite position to Sunrise and HCP.[166] It argued the standstill agreement had been entered into as part of the rules of the auction process, and one of the benefits of playing by the auction rules and winning was that Sunrise had a "binding obligation" to enforce HCP's standstill.[167] Ventas contended HCP's offer did not satisfy the requirements to trigger the fiduciary out provisions because the offer "w[as] not unsolicited or bona fide."[168] Ventas argued Sunrise and HCP should be held to their bargained-for contracts and that "[t]he rationale for deal protection devices such as the Standstill Agreement . . . is that, in a contested bidding situation, they encourage bidders to make their best bids."[169]

On March 6, 2007, the Ontario Superior Court issued its judgment ruling in favor of Ventas' application.[170] The court focused on the language of the non-solicitation provision and determined that Sunrise's promise not to waive the standstill agreement was unambiguous and express under the purchase agreement.[171] The court stated that "[b]ona fide means acting or done in good faith; sincere, genuine."[172] As a result, the court concluded that an offer made in violation of a "contractual obligation not to make such

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292, paras. 25-28 (Can. Ont. Sup. Ct. J.).

[160] *Id.* at para. 26.

[161] *Id.* (characterizing the benefits received by Ventas as "significant").

[162] *Id.*

[163] *Ventas*, 29 B.L.R. 4th at para. 26.

[164] *Id.* at para. 27.

[165] *Id.*

[166] *See id.* at paras. 25-27.

[167] *Ventas*, 29 B.L.R. 4th at para. 25.

[168] *Id.*

[169] *Id.*

[170] *Id.* at para. 46.

[171] *Ventas*, 29 B.L.R. 4th at para. 35.

[172] *Id.* at para. 37 (citing THE OXFORD ENGLISH DICTIONARY 379 (Oxford Univ. Press, 2d. ed. 2007)).

a proposal [could not] be considered . . . bona fide."[173] The court additionally stated the no-shop provision required that the third party offer not be made in violation of that particular provision[174] and further, HCP's offer had violated the no-shop because it was made in violation of the standstill.[175] The court also found that the "clear scheme" of the purchase agreement was to enforce standstills entered into during the auction.[176] This agreement, the court noted, "was a form of protection afforded to the purchaser, Ventas," and was "part of the package negotiated" between the parties.[177]

Less than three weeks after the Ontario Superior Court's decision, the Court of Appeal for Ontario affirmed.[178] Holding that the Sunrise-Ventas Purchase Agreement bound Sunrise to enforce the HCP standstill,[179] the court also affirmed the lower court's finding that HCP's proposal was not bona fide.[180] While the appellate decision delved into further detail, the Court of Appeal's analysis can be summarized as a rejection of both of Sunrise's assertions through relying on and heavily citing to the reasoning set forth in the Superior Court decision.[181]

Pertinent to this article is one particular point from the Court of Appeal for Ontario. HCP attempted to argue that, because the trial judge had neglected the importance of the trustees' fiduciary duty to maximize unitholder value, the trial judge had also failed to interpret the contract in a way "that accords with sound commercial sense."[182] HCP further urged that fiduciary outs should ensure that the trustees are able to consider other offers—even those submitted after Sunrise entered into a purchase agreement—that are potentially more favorable.[183] Interestingly, not only did the court reject HCP's argument, the analysis expressly stated:

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[173] *Id.*

[174] *Id.*

[175] *Ventas*, 29 B.L.R. (4th) at paras. 37-38.

[176] *Id.* at 38.

[177] *Id.*

[178] Ventas Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. 3d 254, para. 7 (Ca. Ont. C.A.).

[179] *Id.* at paras. 34-35 ("Sunrise's obligation to enforce its Standstill Agreements with third parties is not negated by the fiduciary out clause . . . . The fiduciary out clause does not apply where the unsolicited proposal is tendered in breach of the non-solicitation provisions of the Purchase Agreement, *i.e.*, in breach of a Standstill Agreement that Sunrise is obliged to enforce.").

[180] *Id.* at paras. 59-61.

[181] *See id.* at paras. 27-28, 35, 42, 48, 50-52, 60-61, 63-64 (agreeing with and defending the lower court's findings).

[182] *Ventas*, 85 O.R. (3d) 254 at para. 51.

[183] *Id.* at paras. 53 ("[HCP] placed great emphasis on the sanctity of the fiduciary out mechanism in acquisition agreements of this nature.").

> It is not necessary – nor would it be wise, in my view – to go as far as HCP[] suggests this court might go, and adopt the principle gleaned from some American authorities, that the target vendor can place no limits on the directors' right to consider superior offers and that any provision to the contrary is invalid and unenforceable: see *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34 (Del. 1994), and *ACE Ltd. v. Capital Re Corp.*, 747 A.2d 95 (Del. Ch. 1999), at p. 105. That is not what happened in this case.[184]

The appellate court found that Sunrise's trustees did not breach their fiduciary duty by agreeing to a contract restricting their ability to receive offers submitted by third parties who had executed standstills.[185]

Prior to the Court of Appeals of Ontario decision, Ventas contacted Sunrise, waiving the right under the Purchase Agreement to force the March 31, 2007 meeting of Sunrise's unitholders.[186] On April 11, Ventas submitted an increased offer of $16.50 "to salvage the deal and avoid injury to its reputation"; on April 19, the unitholders approved the offer.[187] Finally, on April 26, 2007, Sunrise and Ventas closed a deal.[188] Following the deal, Ventas commenced separate proceedings in the United States federal court system on May 3, 2007.[189] In the proceedings that followed, over two years lapsed before the United States District Court for the Western District of Kentucky ultimately found that HCP had tortiously interfered with Ventas' expectancies under the Sunrise-Ventas agreement.[190] On May 17, 2011, the United States Court of Appeals for the Sixth Circuit decided that just over a

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[184] *Id.* at para. 54.

[185] *Id.* at para. 55.

[186] Ventas, Inc. v. HCP, Inc., 647 F.3d 291, 327 (6th Cir. 2011).

[187] *Id.* at 301. Separately, the District Court detailed the circumstances surrounding this price increase as follows:

> HCP's announcement had also caused the trading price to increase, resulting in a new composition of unitholders. Following the Canadian litigation, Ventas sued Sunrise REIT for breach of contract based on Sunrise REIT's actions regarding HCP's interference. Through proxy voting, Ventas saw that the unitholders were overwhelmingly opposing its bid. During this time, Ventas and Sunrise REIT came to a resolution in their lawsuit that allowed Ventas to submit a bid for $16.50 with the support of the Sunrise REIT board.

Ventas, Inc. v. Health Care Prop. Investors, Inc., 635 F. Supp. 2d 612, 626 (W.D. Ky. 2009) (footnote omitted).

[188] *Ventas,* 647 F.3d at 301.

[189] *Id.*

[190] *Id.* at 301-03.

$101 million award of compensatory damages was appropriate.[191] Undoubtedly, the monetary value at stake had influenced both HCP and Ventas, spurring each party onward throughout the course of the extensive litigation process.[192]

In the context of this Article, two points of the tortious interference analysis are particularly pertinent. First, the courts' tortious interference analysis inquired into whether HCP *intentionally* interfered with Ventas's prospective business advantage.[193] Second, the court looked to whether HCP acted with improper motive and, more importantly, whether HCP was acting in good faith.[194] Because the issues of intent and good faith both relate to whether HCP's offer was bona fide, a few particular portions of the U.S. decisions seem noteworthy here.

In the first instance, evidence before the U.S. courts revealed a considerable amount of information proving HCP's intent to interfere—including a quote from one of HCP's investment bankers who apparently told his colleagues that, while HCP was still interested in acquiring Sunrise at the time they made the bid, "at a minimum, they plan[ned] on causing the other side to have to pay more."[195] Not only did this evidence support findings of tortious interference, it also provided further support for the conclusion that the HCP offer was not *bona fide*.[196]

Along those same lines, the aftermath that ensued after HCP's overbid also illustrates how a third party's contravention of a standstill can have severe consequences for the initial buyer.[197] Possibly the most glaring consequence in this case is highlighted by the jury's finding that HCP's improper interference prevented Ventas from successfully acquiring the target company for $15 per unit.[198]

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[191] *Id.* at 318.

[192] *See* Davidoff, *supra* note 22 (attributing this value as a possible explanation for why the parties had not settled, at least as of 2009, stating, "[a] $101 million verdict may just be HCP's price of doing business").

[193] *Ventas*, 647 F.3d at 306-07.

[194] Ventas, Inc. v. Health Care Prop. Investors, Inc., 635 F. Supp. 2d 612, 622-24 (W.D. Ky. 2009).

[195] *Ventas*, 647 F.3d at 321.

[196] *See id.*

[197] *See id.* at 317 (identifying jury's reasonable conclusion regarding the causal connection between HCP's overbid and Ventas's failure to acquire Sunrise at $15 per unit price). Additionally, Ventas alleged HCP caused its delay in dispensing units of stock that would raise the capital needed to finance the deal. *Ventas*, 635 F. Supp. 2d at 625. Ventas further alleged the harm caused by this delay amounted to a $155 to $180 million injury. *Id.* Ventas was not granted recovery on this theory because the damages were too speculative. *Ventas*, 647 F.3d at 324-25.

[198] *Ventas*, 647 F.3d at 317 ("In light of the totality of the evidence presented at trial, the

While the end result is that Sunrise's unitholders got more value for their respective units, the process used does not serve as an example of the procedural norm for the auction process. Although HCP's violation of the standstill agreement was not outcome determinative for purposes of the tortious inference case, that case, along with the Canadian proceedings, demonstrate why winners of auctions favor standstills.[199] At the same time, HCP's violation reveals there may be deals in which a target's shareholders could obtain additional value in a sale of control. Thus, the case displays the tension that standstills attempt to alleviate, more specifically, the desire of an auction winner to protect its executed transaction from being "jumped" and the desire of stockholders to obtain the highest price possible in a sale of control.

### 2. The Role of the Target in Responding to an Overbid

The Northrop Corporation ("Northrop") and Martin Marietta ("Marietta") fight for Grumman Corporation ("Grumman") further illustrates the interplay of standstill provisions, fiduciary duties, and good faith. This example shows that when a bidder appears to violate a standstill in the absence of bad faith—or at least when the bad faith occurs on the other side of the table—the validity of the standstill becomes questionable. When Northrop overbid, in violation of its standstill agreement with Grumman, it took the position that the standstill was unenforceable due to Grumman's failure to negotiate in good faith.[200] While still negotiating with Northrop, Grumman rushed to enter into an agreement with Marietta without encouraging Northrop to submit a bid or even notifying Northrop that it was negotiating with Marietta.[201]

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jury arrived at a reasonable conclusion regarding the element of causation. The jury had sufficient evidence to find that HCP's 'improper interference' caused injury to Ventas.").

[199] Davis Polk & Wardwell LLP partner, Paul Kingsley, has been quoted as saying,

> "I have on occasion heard bankers – not lawyers – say that standstills need not necessarily be respected because there are no damages to the target company or its shareholders from receiving a higher bid. That may be true, but that ignores, of course, circumstances like these in which the competing bidder – and auction winner – ended up having to shell out an extra $100 million plus to get its deal done."

David Marcus, *When Standstills Matter*, THE DEAL MAGAZINE (Jan. 8, 2010), *available at* http://www.thedeal.com/magazine/ID/032789/insights/safe-harbor/when-standstills-matter.php.

[200] Northrop Grumman Sys. Corp., Offer to Purchase (Schedule14-D1), Exhibit 99.A1, §§ 13, 15 (Mar. 14, 1994).

[201] *See id.* § 13.

On January 21, 1993, Northrop and Grumman entered into a confidentiality agreement with a standstill provision.[202] The standstill provided that each party agreed, unless specifically invited by the other, not to seek to acquire any securities of the other party or seek to effectuate any extraordinary transactions for a period of three years from the date of the letter.[203] The provision further provided that neither party would seek a waiver, directly or indirectly, under any provision of the standstill agreement.[204] The companies exchanged confidential information, but no serious discussions occurred.[205] In the fall of 1993, Northrop re-initiated discussions.[206] On January 19, 1994, Northrop forwarded a request for a thirty-day exclusivity period to engage in discussions.[207] Grumman declined the offer, but discussions continued between the two companies with Grumman telling Northrop that any transaction should involve a significant portion of cash consideration.[208] Northrop responded, indicating a preference for a transaction that minimized the amount of cash consideration.[209]

In early February 1994, Grumman reached out to Marietta.[210] Marietta stated it did not want to participate in an auction process, and would only negotiate on an exclusive basis.[211] The companies entered into a confidentiality agreement and standstill provision, similar to the one entered into between Grumman and Northrop, except the agreement only provided that neither party would *publicly* seek or *publicly* disclose a request for a waiver under the standstill provision.[212] Marietta indicated it would be able to go forward with a cash transaction maximizing value to Grumman's shareholders.[213] On February 17, Grumman's Board met and determined

[202] Grumman Corp., Solicitation, Recommendation Statements (Schedule 14-D9), at Item 4(b) (Mar. 9, 1994).

[203] Grumman Corp., Confidentiality Agreement (Schedule 14-D9), Exhibit 99.C13A, § 7 (Mar. 9, 1994).

[204] *Id.*

[205] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202, at Item 4(b).

[206] *Id.*

[207] *Id.*

[208] *Id.*

[209] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202, at Item 4(b).

[210] Lockheed Martin Inv. Mgmt. Co., Tender Offer Statement (Schedule 14D-1), Exhibit 99.A1, § 10 (Mar. 8, 1994).

[211] *Id.*

[212] Grumman Corp., Confidentiality Agreement (Schedule 14D-9), Exhibit 99.C14, § 7 (Mar. 9, 1994).

[213] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202, at

that it was not interested in pursuing a transaction with Northrop.[214] Grumman informed Marietta that it would agree to exclusive negotiations, but noted that "time was of the essence."[215]

On February 21, Marietta sent a letter that included an offer of $55 cash per share with the condition that negotiations proceed on an exclusive basis.[216] Grumman's Board authorized continued negotiations on the following understandings, based on Marietta's letter: a price of $55 per share, "until [Grumman] tells [Marietta] that the Company no longer wishes to continue discussions, [Grumman] does not intend to engage in discussions with another party regarding a business combination or invite or solicit such a transaction," and with respect to certain other terms of the letter, that the Board was only prepared to do what was "reasonable and consistent with the Board's fiduciary obligations."[217]

On February 24, Northrop communicated to Grumman they would be prepared to submit an offer of not less than $50 a share.[218] The following day, Northrop sent a letter further stating it would be prepared to submit a higher offer if Grumman would provide further information or analysis.[219] On February 28, Grumman's Board considered Northrop's letter and the possible effects that pursuing discussions would have on Marietta's offer.[220] Grumman determined not to pursue Northrop's letter after it was advised that Marietta's offer would likely produce a higher value under current market conditions.[221] Several days later, Grumman approved and executed the merger with Marietta.[222]

The merger agreement between Grumman and Marietta contained a no-shop paired with a fiduciary out, as well as a $50 million termination fee payable to Marietta in the event that Grumman terminated the agreement in favor of a third party's unsolicited overbid.[223] The confidentiality agreement between Grumman and Northrop contained a standstill provision prohibiting Northrop from making any offer for a period of three years, unless specifically invited by Grumman.[224] By the terms of the merger

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Item 4(b).

[214] *Id.*

[215] Lockheed Martin Inv. Mgmt. Co., Tender Offer Statement, *supra* note 210, § 10.

[216] *Id.*

[217] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202.

[218] *Id.*

[219] *Id.*

[220] *Id.*

[221] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202.

[222] Lockheed Martin Inv. Mgmt. Co., Tender Offer Statement, *supra* note 210, § 10.

[223] Grumman Corp., Tender Offer Statement (Schedule 14D-1), Exhibit 99.A1, § 6.2 (Mar. 8, 1994).

[224] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202, § 10.

agreement, Grumman could not solicit an offer from Northrop, and by the terms of the confidentiality agreement Northrop could not make an offer to Grumman.[225] Northrop commenced a tender offer, taking the position that the standstill provision of the confidentiality agreement was unenforceable.[226]

In a publicly filed letter accompanying the tender offer, the Chairman of Northrop complained that his company was not on a "level playing field."[227] Northrop was unaware Grumman was negotiating with another company based on Grumman's repeated assurances that it was "not for sale."[228] The letter asked why Northrop was not invited to submit an offer during negotiations while a request was made specifically to Marietta.[229] The Chairman pointed out that Northrop was not allowed the same confidential information as Marietta to complete its due diligence in order to refine its offer and additionally criticized the "lock up agreement" with Marietta as "improper and illegal."[230]

In response to the letter, Northrop was provided with the same non-public information that had been furnished to Marietta.[231] Marietta attempted to force Grumman to enforce the provisions of the standstill, but Grumman refused.[232] In a letter to the Chairman of Marietta, the Chairman of Grumman responded "in order to have a court enforce the Confidentiality Agreement's standstill provisions . . . it would be necessary to demonstrate the manner in which Grumman would be damaged if such standstill provisions were not enforced and, to secure injunctive relief, to demonstrate irreparable injury to Grumman."[233] He then invited Marietta's counsel to discuss the matter with Grumman's counsel.[234] Grumman proceeded to invite both companies to submit their highest bids.[235] Without any further protest or an upward bid revision from Marietta, Grumman paid the $50

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[225] *See supra* text accompanying notes 223-24.

[226] Grumman Corp., Tender Offer Statement (Schedule 14-D1), Exhibit 99.A1, § 10 (Mar. 14, 1994).

[227] Grumman Corp., Amended Solicitation, Recommendation Statements (Schedule 14-D9/A), Exhibit 99.C18 (Mar. 11, 1994).

[228] *Id.*

[229] *Id.*

[230] *Id.*

[231] *See* Grumman Corp., Amended Tender Offer Statement (Schedule 14-D1/A), Exhibit 99.C3 (Mar. 15, 1994).

[232] *See* Grumman Corp., Amended Solicitation, Recommendation Statements (Schedule 14-D9/A), Exhibits 99.C20, 99.C21 (Mar. 23, 1994).

[233] *Id.* at Exhibit 99.C21.

[234] *Id.*; *see also* Grumman Corp., Amended Tender Offer Statement (Schedule 14D-1/A), at 2 (Apr. 5, 1994) (confirming Grumman paid the $50 million termination fee).

[235] Grumman Corp., Definitive Proxy Statement (Schedule 14A), at 8 (May 3, 1994).

million termination fee and additional reimbursement expenses followed by acceptance of Northrop's offer.[236] Although this was a successful overbid in spite of a standstill provision, whether the standstill was actually enforceable (or used properly) is the $50 million dollar question.

3. Using a Standstill to Favor Board Members' Individual Interests

The story behind the Formation Capital Partners ("Formation") and Genesis Healthcare ("Genesis") merger tells a familiar story but raises different issues. Arguably, Genesis' board improperly entered into an agreement with Formation when another bidder, Fillmore Capital Partners ("Fillmore"), was present during a sales process that seemed to disregard shareholder value maximization and favor Formation.[237] When the Fillmore proposal was deemed to be more favorable, Genesis' board requested that Formation revise its proposal without asking Fillmore to do the same.[238] When it appeared the agreement would not be approved by Genesis' shareholders, Formation agreed to reduce the termination fee and to allow Genesis to release Fillmore from its standstill obligation.[239] After allowing Fillmore to continue to submit bids, Genesis then agreed to an increase in the termination fee to an amount near the original fee, further showing Genesis' preference to Formation.[240]

In November 2006, Genesis formed a special committee to commence a non-public solicitation process.[241] In early November, fourteen potential strategic and financial buyers were contacted, and several executed confidentiality and standstill agreements.[242] Fillmore and Genesis entered into a standstill agreement on November 15, 2006.[243] On December 1, Fillmore submitted an indication of interest to Genesis, suggesting it would be interested in retaining Genesis' senior management.[244] On December 6,

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[236] Grumman Corp., Amended Tender Offer Statement, (Schedule 14-D1/A), Exhibit 99.A11 (Apr. 5, 1994).

[237] *See* Genesis Healthcare Corp., Definitive Proxy Statement (Schedule 14A), at 20-21 (Mar. 7, 2007) (Fillmore is referred to as "Participant 2").

[238] *Id.* at 21.

[239] Genesis Healthcare Corp., Current Report (Form 8-K), at Item 1.01 (Apr. 20, 2007).

[240] Of note is that this is not the first time that Formation and Fillmore faced off. In 2005, Formation submitted a hostile bid in a failed attempt to disrupt Fillmore's buyout of Beverly Enterprises, Inc. *See* Spatt & Martelli, *supra* note 94, at 6.

[241] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 17.

[242] *Id.*

[243] *See* Genesis Healthcare Corp., Current Report (Form 8-K), Exhibit 99.1, at 1 (Apr. 26, 2007).

[244] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 18.

Formation Capital also submitted an indication of interest, revealing its intent to retain existing management.[245] The next week, Mr. Hager, Genesis' Chairman and CEO, informed Fillmore that he would not agree to work for their organization.[246] Fillmore's reply indicated that this decision would not discourage them from submitting a bid.[247]

Genesis received final proposals from both companies pursuant to the solicitation process on January 11 and 12.[248] Formation submitted an offer at $60 per share, while Fillmore's offer was $61 per share.[249] Genesis later stated the Fillmore offer proposed transaction agreements and financing commitments raised fewer issues than those of Formation, but the terms still required additional negotiation.[250] Genesis' board decided none of the bidders had distinguished themselves as the "clear winner," and requested revised bids.[251] Formation increased its bid to $62.50 per share, while Fillmore increased its offer to $63 per share.[252] Both offers included substantial improvements in regard to transaction agreements and financing commitments.[253]

At a meeting on January 15, Genesis' board was advised that the Fillmore offer was more favorable to the company's shareholders, and additionally suggested less risk of non-consummation compared with Formation's offer.[254] Mr. Hager, along with another executive, reiterated their unwillingness to work for Fillmore.[255] The non-executive directors were aware that Formation informed senior management of opportunities to own and run an independent company, though Formation had not disclosed any specific terms to the board or senior management.[256]

The special committee determined that entering into a transaction with either company would be in the best interests of Genesis.[257] After being contacted, Formation orally confirmed it would address open contract and financing issues and then raised its bid to $63 per share.[258] Immediately

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[245] *Id.*
[246] *Id.*
[247] *Id.*
[248] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 19.
[249] *Id.*
[250] *Id.* at 19-20.
[251] *Id.* at 20.
[252] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 20.
[253] *Id.*
[254] *Id.*
[255] *Id.* at 21.
[256] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 21.
[257] *Id.*
[258] *Id.*

afterward, the board of directors approved the merger agreement with Formation.[259] The merger agreement was subsequently announced the following morning.[260]

After a few months of shareholders publicly voicing disapproval of the process, Genesis stated it appeared unlikely the merger would be approved by shareholders based on a preliminary vote tally of proxies and communications with them.[261] On April 19, Genesis and Formation amended the merger agreement to increase the price to $64.25 per share, reduced the termination fee payable by Genesis to $15 million from $50 million, and permitted Genesis to release other parties, including Fillmore, from their standstill obligations.[262]

Then, in reliance on the waiver, Fillmore sent a proposal to acquire Genesis for $64.75 on April 24.[263] Fillmore and Formation continued outbidding one another until Fillmore finally withdrew following Genesis' acceptance of Formation's $69.35 offer, which included an increase in the termination fee to $40 million.[264] The CEO of Fillmore complained that there was not a level playing field, describing the process as "skewed and unfair," and called for "the Genesis Board to end the process yet again before its natural conclusion does not serve the interests of the Genesis shareholders."[265]

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[259] *Id.*

[260] Genesis Healthcare Corp., Definitive Proxy Statement, *supra* note 237, at 21.

[261] Genesis Healthcare Corp., Definitive Additional Proxy Soliciting Materials (Schedule 14A), at S-8 (Apr. 23, 2007).

[262] Genesis Healthcare Corp., Current Report, *supra* note 239, at Item 1.01. The merger agreement as previously executed contained a non-solicitation provision and required Genesis to cease all existing discussions and negotiations, but permitted either party to "waive compliance with any of the agreements or conditions contained for the benefit of such party contained herein." Genesis Healthcare Corp., Current Report (Form 8-K), Exhibit 2.1, at 61 (Jan. 18, 2007). The amendment provided:

> Parent and Merger Sub hereby acknowledge and agree that the Company may amend, waive, fail to enforce, and/or grant any consent with respect to the "standstill" provisions (and only the "standstill" provisions) under any confidentiality, standstill or similar agreement to which the Company is a party, and that any such action or non-action is permitted under the Merger Agreement and shall not constitute a violation by the Company of any term or provision of the Merger Agreement; provided, however, that any such amendment, waiver, period of non-enforcement or consent shall be time-limited so as to expire (and revert to its terms prior to any such amendment, waiver, failure to enforce or consent) if and when the Requisite Shareholder Vote is received.

Genesis Healthcare Corp., Current Report, *supra* note 239, at Exhibit 2.3, § 10.

[263] Genesis Healthcare Corp., Current Report (Form 8-K), at Item 1.01 (Apr. 26, 2007).

[264] Genesis Healthcare Corp., Current Report (Form 8-K), at Item 1.01 (May 22, 2007).

[265] Genesis Healthcare Corp., Current Report (Form 8-K), Exhibit 99.2, at 1 (May 10, 2007).

While Formation agreed to the release, this story nevertheless presents several questions pertinent to this Article. For example, what if Formation did not agree to release Fillmore from its obligation? What if there had been no waiver of that obligation, and Fillmore had made a bid in contravention of its standstill agreement? Would the lack of Formation's consent have required Genesis to uphold the standstill? In other words, would the standstill be enforceable in courts, despite the questionable manner in which the Genesis board favored Formation?

### B. *Target Board's Waiver of a Standstill*

#### 1. A Board's Refusal to Waive a Standstill

The Delaware Court of Chancery has most often examined standstills to determine whether the seller was using the provision for an inequitable purpose such as favoring one bidder over another, or favoring one bidder over the shareholders' interests.[266] The court made clear in *In re Topps Shareholders Litigation*[267] that a target company may not refuse to waive a standstill to "favor one bidder over another."[268]

In *Topps*, the target company, Topps Company, Inc. ("Topps"), entered into a merger agreement with a Michael Eisner-affiliated private equity firm ("Eisner").[269] The Topps merger agreement contained a go-shop provision[270] allowing Topps to actively shop the company for forty days following the execution of the merger agreement.[271] During the go-shop period, the Upper Deck Company ("Upper Deck")—Topps' prime competitor—expressed interest in Topps and "sought access to confidential information."[272] Before providing Upper Deck with access to its confidential information, Topps required Upper Deck to execute a

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[266] *See, e.g.*, *In re* J.P. Stevens & Co. S'holders Litig., 542 A.2d 770, 784 (Del. Ch. 1988) (considering whether target company favored the existing bidder to stockholders' detriment).

[267] 926 A.2d 58 (Del. Ch. 2007).

[268] *Id.* at 91.

[269] *Id.* at 62, 66.

[270] Sautter, *supra* note 71, at 557 & n.170 (explaining that unlike no-shop provisions, go-shop provisions allow a target company to actively solicit third party offers post-signing for a limited period of time).

[271] *Topps*, 926 A.2d at 61. *See generally* Sautter, *supra* note 71 (supplying an in-depth look at go-shop provisions in change of control dealings); Guhan Subramanian, *Go-Shops v. No-Shops in Private Equity Deals: Evidence and Implications*, 63 BUS. LAW. 729 (2008) (providing an analysis of the effectiveness of go-shop provisions in the sales process).

[272] *Topps*, 926 A.2d at 62, 66.

confidentiality agreement containing a standstill provision.[273] In particular, the standstill provision prevented Upper Deck from making "any public disclosure[s] with respect to any proposed transaction between Upper Deck and Topps," from disclosing that it was obtaining confidential information, and from making known that it had executed a standstill.[274] Additionally, under the standstill, "Upper Deck agreed for a period of two years not to acquire or offer to acquire any of Topps's common stock by way of purchase in the open market, tender offer, or otherwise without Topps's consent, or to solicit proxies or seek to control Topps in any manner."[275]

Upper Deck submitted formal offers for Topps both during and after the go-shop period.[276] Although each of Upper Deck's bids was higher than Eisner's bids, Topps never negotiated with Upper Deck regarding antitrust issues, price, or the reverse break-up fee offered by Upper Deck.[277] Topps released proxy statements containing material misstatements and omissions regarding Upper Deck's offers which "intentionally cast[ed] a negative light on Upper Deck's sincerity as a bidder."[278] Upper Deck requested that Topps waive the standstill so that Upper Deck could "make a tender offer on the terms it offered to Topps and . . . communicate with Topps's stockholders," but the Topps board of directors refused Upper Deck's request.[279]

Upper Deck, along with a group of Topps stockholders, sought a preliminary injunction seeking to enjoin the stockholder vote on the merger with Eisner, to mandate that Topps correct material misstatements in the proxy statement, and to order Topps to waive the standstill provision so that Upper Deck could communicate with stockholders or make a tender offer.[280] Then-Vice Chancellor Strine granted the preliminary injunction, finding that Topps was most likely "misusing the [s]tandstill" and that the "Topps board [was not] using the [s]tandstill to extract reasonable concessions from Upper Deck in order to unlock higher value."[281] Instead, Strine found that Topps's refusal to waive the standstill prevented Topps stockholders from hearing Upper Deck's version of events and from considering and accepting a higher offer.[282] Upper Deck was unable to seek antitrust clearance because

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[273] *Id.* at 66.
[274] *Id.*
[275] *Id.*
[276] *Topps*, 926 A.2d at 90.
[277] *Id.*
[278] *Id.* at 77-79 (describing Topps's proxy statement and other public statements as allegedly deficient and misleading with respect to Upper Deck's offers).
[279] *Id.* at 91-92.
[280] *Topps*, 926 A.2d at 84.
[281] *Id.* at 91.
[282] *Id.* at 92.

it could not commence a tender offer or have an executed merger agreement.[283] Ultimately, Vice Chancellor Strine found that the Topps board was "not using the [s]tandstill [a]greement for any apparent legitimate purpose."[284]

In the wake of *Topps*, then practitioner, now Vice Chancellor, Travis Laster, wrote the following:

> The questions created by aggressive standstill agreements and subsequent waivers have been part of the Delaware counseling mix for some time. Without any meaningful decisions on the issue, however, concerns regarding potential fiduciary duty issues were often given short-shrift. *Topps* confirms that the use of standstill agreements and reliance on them to foreclose subsequent bids are areas that must be approached with particular care.[285]

A board of directors' decision to waive or to refuse to waive an executed standstill so that a party can make a topping bid is a delicate subject.[286] A particularly sensitive question with respect to standstills is when a board of directors may legitimately promise *not* to waive the standstill provision.[287] In *Topps*, Vice Chancellor Strine alluded to such a situation by imagining a hypothetical final round auction with three bidders.[288] In that scenario, Strine suggested the target board might legitimately promise the highest bidder certain deal protection provisions including a promise not to waive the standstill.[289] However, because this

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[283] *Id.* Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18(a) *et seq.* (2006), before a company may file for antitrust clearance a definitive acquisition agreement or a letter of intent must have been executed. KLING & NUGENT, *supra* note 8, § 5.04[2], at 5-184.

[284] *Topps*, 926 A.2d at 92.

[285] Travis Laster, *Must Read Decision: VC Strine Enjoins Merger Vote* Topps *Case*, DEAL LAWYERS (June 18, 2007, 8:25 AM), http://www.deallawyers.com/blog/archives/000779.html.

[286] *See* Subramanian, *supra* note 17, at 659-62 (discussing the implications of a board of directors releasing non-public information during the sales process and the role a standstill plays in releasing non-public information).

[287] *See, e.g.*, Alexander B. Johnson, *Is Revlon Only Cosmetic?: Structuring a Merger in the mid-1990's*, 63 FORDHAM L. REV. 2271, 2283-84 (1995) (discussing the Delaware Supreme Court's holding in *Ivanhoe Partners v. Newmont Mining Corp.*, where the court found no *Revlon* triggering event occurred "because the remaining shareholders still controlled the corporation, as the standstill agreement retained in them the power to elect sixty percent of the company's board").

[288] *Topps*, 926 A.2d at 91 n.28.

[289] *Id.*

was only dicta, it remains unclear how extensive such an auction process must be before such a promise may be made.

An equally interesting issue is the enforceability of a promise made by a bidder not to request a waiver from the standstill provision, or "Don't-Ask-Don't-Waive" provisions. A few recent Delaware Court of Chancery cases involving the approval of class action settlements shed some light on the possible treatment of such provisions.

The first case, *In re Celera Corporation Shareholder Litigation*,[290] involved the sale of Celera Corporation ("Celera"). When first considering a transaction, Celera engaged financial advisor Credit Suisse Securities (USA) LLC ("Credit Suisse") to explore through "targeted discussions with potential counterparties" a sale of the company's individual assets, business segments, or the entire company.[291] Credit Suisse contacted nine potential bidders and five of the nine executed confidentiality agreements with Celera.[292] The confidentiality agreements contained a standstill preventing the bidders from "making offers for Celera shares without an express invitation from the Board."[293] The agreements also "contained a broadly worded provision preventing the signing parties from asking the Board to waive th[e] [standstill] restriction (the 'Don't-Ask-Don't-Waive Standstills')."[294]

After an extended sales process and several stops and starts, Celera eventually entered into a merger agreement with Quest Diagnostics, Inc., ("Quest") pursuant to which Quest would commence a twenty-one-day tender offer for Celera common stock at $8 per share.[295] The Celera-Quest merger agreement contained a $23.45 million termination fee amounting to 3.5% of the transaction's total value, "but [was] arguably as much as 10% of Celera's enterprise value"; a no-shop provision requiring Celera to end any "existing discussions, and not to solicit competing offers from, potential bidders other than Quest;" and a top-up option providing that if Quest obtained over 60% of Celera's voting power, it could then acquire as many shares as necessary to exceed 90% of Celera's voting stock.[296] After announcement of the merger agreement, a Celera shareholder brought a class action suit against Celera and Quest alleging, among other things, the

[290] *In re* Celera Corp. S'holder Litig., 2012 WL 1020471 (Del. Ch. Mar. 23, 2012).
[291] *Id.* at *2.
[292] *Id.* at *3.
[293] *Id.*
[294] *Celera*, 2012 WL 1020471, at *3.
[295] *Id.* at *5.
[296] *Id.* at *6.

Celera board had breached its fiduciary duties by entering into the agreement with Quest.[297]

Pursuant to the settlement negotiated with the lead plaintiff, Celera and Quest agreed, among other things, to reduce the termination fee to $15.6 million and to modify the no solicitation provision so that bidders subject to the Don't-Ask-Don't-Waive provision would be invited to submit bids.[298] In upholding the settlement agreement, Vice Chancellor Donald F. Parsons, Jr. was careful to state he was not declaring Don't-Ask-Don't-Waive standstills as generally unenforceable, and added that because of the prevalence of these provisions, any such judgment could only be in the context of an "appropriately developed record."[299] However, he stated the "[p]laintiffs have at least a colorable argument that these constraints collectively operate to ensure an informational vacuum."[300] Parsons further explained that once in the "informational vacuum," the board would not have any information pursuant to which it could evaluate whether continuing to comply with the merger agreement terms would violate the board's fiduciary duties.[301] As a result, he stated, "[c]ontracting into such a state conceivably could constitute a breach of fiduciary duty."[302]

In a settlement hearing held just weeks before the *Celera* decision was issued, Vice Chancellor Laster went further in his questioning of Don't-Ask-Don't-Waive standstills. In that case, *In re Rehabcare Group, Inc. Shareholders Litigation*, Vice Chancellor Laster stated:

> I do think it is weird that people persist in the "agree not to ask" in the standstill. When is that ever going to hold up if it's actually litigated, particularly after *Topps*? It's just one of those things that optically looks bad when you're reviewing the deal facts. It doesn't give you any ultimate benefit because you know that the person can get a *Topps* ruling making you let them ask, at a minimum, or can ask in a back channel way. Why would you hurt yourself in terms of the optics by asking for that? One of those strange things in life.[303]

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[297] *Id.*
[298] *Celera*, 2012 WL 1020471, at *7.
[299] *Id.* at *22.
[300] *Id.* at *21.
[301] *Id.*
[302] *Id.*
[303] Transcript of Settlement Hearing at 46, *In re* Rehabcare Group, Inc. S'holders Litig., C.A. No. 6197-VCL (Del. Ch. Sept. 8, 2011).

Although both Vice Chancellors Parsons and Laster's comments are essentially solely dicta, the comments do shed some light on Delaware's stance on Don't-Ask-Don't-Waive standstills. Such comments illustrate that a Delaware court is unlikely to uphold such a provision, particularly when it would result in the target's board being willfully blind to alternative bids that may maximize stockholder value.

Just as this Article was going to print, the Delaware Chancery Court issued two significant rulings that provide direct insight into the future of Don't-Ask-Don't-Waive standstills. On November 27, Vice Chancellor Laster had the opportunity to further review Don't-Ask-Don't-Waive standstills in *In re Complete Genomics, Inc. Shareholder Litigation*.[304] In that case, Laster compared Don't-Ask-Don't-Waive standstills to no-talk provisions declared invalid in *Phelps Dodge.*[305] In particular, Laster stated,

> So in my view, by analogy to Phelps Dodge, a Don't Ask, Don't Waive Standstill is impermissible because it has the same disabling effect as the no-talk clause, although on a bidder-specific basis. By agreeing to this provision, the Genomics board impermissibly limited its ongoing statutory and fiduciary obligations to properly evaluate a competing offer, disclose material information, and make a meaningful merger recommendation to its stockholders. With respect to the Don't Ask, Don't Waive Standstill provision, therefore, the plaintiffs have established a reasonable probability of success on the merits that that provision represents a promise by a fiduciary to violate its fiduciary duty, or represents a promise that tends to induce such a violation.[306]

Thus, at least if Vice Chancellor Laster has his way, Don't-Ask-Don't-Waive standstills may soon be history.

However, less than three weeks after Vice Chancellor Laster's ruling, Chancellor Strine weighed in on Don't-Ask-Don't-Waive standstills, calling them "the emerging issue of December of 2012," in *In re Ancestry.com Inc. Shareholder Litigation*.[307] In the ruling Chancellor Strine scrutinized Don't-

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[304] Telephonic Oral Argument and the Court's Ruling, *In re* Complete Genomics, Inc. S'holder Litig., C.A. No. 7888-VCL (Del. Ch. Nov. 27, 2012).

[305] *Id.* at 14-18.

[306] *Id.* at 18.

[307] The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction at 19, *In re* Ancestry.com Inc. S'holder Litig., C.A. No. 7988-CS (Del. Ch. Dec. 17, 2012).

Ask-Don't-Waive standstills, but was more careful to take a fact based approach and not make a per se ruling, limiting the precedential value of bench rulings generally and the potential reach of *Complete Genomics* and *Celera*.[308] Strine contemplated that Don't-Ask-Don't-Waive standstills could be used consistently with a board's fiduciary duties, but only if used to accomplish a specific value-maximizing purpose.[309] Strine went on to find that, had the board not waived the Don't-Ask-Don't-Waive provisions, it would not have been using the Don't-Ask-Don't-Waive standstill for a specific value-maximizing purpose.[310] In light of the waiver, Strine's order merely required disclosure of the circumstances surrounding the use and waiver of the Don't-Ask-Don't-Waive provision.[311]

### 2. Covenant to Cease All Existing or Previously Conducted Discussions

The example of the Marsh Supermarkets, Inc. ("Marsh") acquisition highlights a merger agreement that imposed contractual limitations on a target's ability to accommodate indications of interest pre-closing. In October 2005, after evaluating strategic alternatives for responding to economic pressure and declining profit margins, Marsh hired Merrill Lynch to begin gauging the interest of potential buyers and conduct an auction process.[312]

After Merrill Lynch had contacted twenty-seven strategic and financial parties in December of 2006, Marsh entered into confidentiality agreements with twenty-one of those parties—including Sun Capital Partners ("Sun").[313] In the process of the early bidding activity that followed, Marsh received preliminary indications of interest from ten of

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[308] *Id.* at 20-22 ("And the *Celera* case expressly went out of its way to say it's not making a per se rule. I think what *Genomics* and *Celera* both say, though, is Woah, this is a pretty potent provision.").

[309] *Id.* at 23-24 ("But the value-maximizing purpose has to be to allow the seller as a well-motivated seller to use it as a gavel, to impress upon the people that it has brought into the process the fact that the process is meaningful; that if you're creating an auction, there is really an end to the auction for those who participate.").

[310] *Id.* at 24-26 ("I think the plaintiffs have pretty obviously shown that this board was not informed about the potency of this clause. The CEO was not aware of it. It's not even clear the banker was aware of it. . . . None of the board seems to be aware of this. The only way it has value as an auction gavel is if it has the meaning I've just described. It was not used as an auction gavel. . . . I think that probabilistically is a violation of the duty of care.").

[311] *Id.* at 26.

[312] Marsh Supermarkets, Inc., Preliminary Proxy Statement (Schedule 14A), at 10, 23 (June 16, 2006).

[313] *Id.* at 23.

those parties, covering a broad price range from $7.50 to $18.00 per share.[314] Meanwhile, after the public announcement that Marsh was considering strategic alternatives, several unsolicited parties stepped forward to express interest.[315] On December 21, Cardinal Paragon, Inc. ("Cardinal")—one of these new bidders who had not been initially contacted by Merrill Lynch—reviewed public information and submitted an indication of interest that valued Marsh between $11.00 and $13.00 per share.[316] Marsh dismissed Cardinal's indication of interest in light of the previously mentioned indications that were more lucrative.[317]

Three other potential investors, including Sun, remained involved in the bidding process.[318] On February 22, 2006, Merrill Lynch requested that each party to submit its best and final offer by March 16.[319] Shortly thereafter, Cardinal re-entered the picture when it informed Merrill Lynch it was prepared to submit a revised indication much higher than its initial indication, and on March 13, Cardinal and Marsh signed a confidentiality agreement containing a standstill provision.[320] On March 17, Cardinal drastically increased their indication of interest, this time valuing Marsh between $18.00 and $20.00 per share.[321]

On March, 20, Sun stated that it was prepared to execute a cash deal that would pay Marsh between $10.00 and $13.00 per share.[322] While the offer was subject to Sun's completion of due diligence, Sun indicated it could finalize a definitive agreement within thirty days[323] and would only proceed if Marsh agreed to an exclusive negotiation period.[324] Although Marsh promptly rejected the exclusivity request, the two parties continued negotiations.[325]

In April of 2006, the negotiations heated up.[326] On April 3, an unnamed party submitted an indication interest valuing Marsh at $10.47 per share.[327] On April 7, Sun revised its estimate to $10.00 per share.[328] On

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[314] *Id.* at 23-24.
[315] *Id.* at 24.
[316] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 24.
[317] *Id.*
[318] *Id.*
[319] *Id.*
[320] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 25.
[321] *Id.* at 26.
[322] *Id.*
[323] *Id.*
[324] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 26.
[325] *Id.*
[326] *See id.* at 26-28.
[327] *Id.* at 26.

April 14, Merrill Lynch notified Cardinal that Marsh's board of directors would be meeting on April 18, and it would be prudent for Cardinal to submit a revised offer of value before the meeting took place.[329] Cardinal sent a response to Marsh explaining that, although it was undecided as to the current figure it was willing to offer, it estimated it would be between its December valuation ($11.00 to $13.00 per share) and its March valuation ($18.00 to $20.00 per share).[330] In the same correspondence, Cardinal stated it could revise its bid by the end of the following week, but it would only move forward on an exclusive basis.[331] Marsh rejected this exclusivity request, just as it had done to Sun's.[332] Meanwhile, also on April 14, Merrill Lynch continued its communication with Sun.[333] As a result of negotiations that took place between April 14 and April 18, Sun submitted a revised offer of $11.00 per share.[334]

On April 17, Merrill Lynch's communications with Cardinal revealed three pieces of information that likely contributed to the Marsh board's ultimate willingness to finalize an agreement with Sun.[335] Cardinal stated that committed financing could not be obtained without further information from Marsh, indicated that sixty days were needed to complete due diligence, and requested to be compensated for up to $1 million for their diligence efforts.[336] Marsh's board met on April 18 and, ultimately, after discussing its options, instructed Merrill Lynch to offer exclusivity to Sun if it could negotiate a deal for $12.00 per share.[337] In making its decision to move forward with Sun, the board considered, among other things, the fact that Sun had offered a firm price, and that Sun could execute the transaction without a financing condition.[338]

After further negotiation by Merrill Lynch, on April 20, Sun countered the $12.00 per share price with an offer to increase its price to $11.125 per share.[339] Sun conditioned its offer on the return of a signed letter of intent, which would have bound parties to a twenty-one day

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[328] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 26.
[329] *Id.*
[330] *Id.*
[331] *Id.*
[332] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 26.
[333] *Id.* at 27.
[334] *Id.*
[335] *Id.*; *see also* Marsh Supermarkets, Inc., Definitive Additional Proxy Soliciting Materials (Schedule 14A) (Sept. 7, 2006) (providing a simplified summary, via PowerPoint presentation, of reasons underlying the Marsh board's decision to proceed with Sun).
[336] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 27.
[337] *Id.*
[338] *Id.*
[339] *Id.*

exclusivity period so that Sun could complete diligence efforts and work towards finalizing the merger agreement.[340]

In response to Marsh's execution of a letter of intent with Sun, Cardinal re-entered the picture, this time with a partner; on April 27, Cardinal and its new partner jointly submitted a conditional, non-binding indication of interest to Merrill Lynch indicating a willingness to pay $13.625 per share.[341] Cardinal also indicated that it could be ready to finalize a definitive agreement, without a financing condition, within fifteen days.[342] On April 28, the Marsh board met to discuss their options.[343] It was clear that Cardinal's offer had the Marsh board's attention because it discussed the implications of violating its exclusivity agreement with Sun.[344] Ultimately, however, the board chose to proceed with Sun; the board was not willing to risk losing Sun as a prospective buyer, which it determined could have been the result if they pursued negotiations with Cardinal.[345]

After Marsh decided to proceed with Sun, the parties finalized the deal between Marsh and two affiliates of Sun, MSH Supermarkets and MS Operations, and executed a merger agreement on May 2, 2006.[346] Shortly after the announcement of the deal Cardinal responded and, pursuant to its aforementioned standstill, sought Marsh's permission to make a formal offer.[347] Reiterating the price of $13.625 per share, Cardinal communicated to Marsh that it was prepared to enter into a deal similar in structure to the one executed by Sun, but its offer was still subject to satisfactory completion of due diligence.[348] After consulting with its attorney, the Marsh board decided to seek Sun's permission to waive the standstill provisions of the Marsh-Cardinal confidentiality agreement.[349] Sun subsequently rejected the request for consent to waive, and Marsh then relayed that information to Cardinal.[350] Cardinal responded with a marked agreement with terms

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[340] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 27.

[341] *Id.* at 28. At this point in the negotiation process, Cardinal had partnered with Drawbridge Special Opportunity Investors, LLC and the two acted together for the remainder of the deal. *Id.* Cardinal and Drawbridge will be collectively referred to as "Cardinal."

[342] *Id.*

[343] *Id.*

[344] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 28.

[345] *Id.* ("The board . . . discussed the risk that if [Sun] walked away, there could be no assurance that a definitive agreement could be reached with Cardinal and Drawbridge or that the price per share in any such definitive agreement would equal or exceed $11.125.").

[346] *Id.* For purposes of this Article, MSH Supermarkets and MS Operations will be collectively referred to as "Sun."

[347] *Id.* at 29.

[348] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 29.

[349] *Id.*

[350] *Id.* at 29-30.

"substantially similar" to the agreement with Sun and also conveyed its position that Marsh was not required to obtain Sun's consent to waive the standstill provisions.[351] Cardinal maintained this position in the ensuing communications between the parties, during which Sun repeatedly sought to assert that Marsh would need its consent before granting Cardinal permission to make a formal proposal.[352]

On May 30, Marsh issued a press release publicly announcing its communication with Cardinal.[353] Pursuant to its agreement with Sun, Marsh was required to issue a press release within 10 business days stating its opposition to any publicly disclosed competing transaction; otherwise, Sun would have the right to terminate the agreement and collect a fee of $10 million.[354] On June 12, Marsh issued a press release expressing its opposition to the competing transaction from Cardinal.[355] Nevertheless, Marsh sought to consider Cardinal's indication of interest: on June 16, Marsh's board resorted to the Indiana Superior Court to clarify the interpretation of the Marsh-Sun agreement.[356]

As evidenced by the derivative suit that the shareholders eventually filed, Marsh's shareholders were interested in seeing whether Cardinal's indications of interest would develop into a superior offer.[357] With a potential $2.50 per share at stake, Marsh's board filed suit, naming as defendants Sun and Cardinal.[358] Faced with these competing interpretations of the merger agreement, the issue before the court was whether Marsh—under the provisions of the Marsh-Sun merger agreement—could "unilaterally consent to receive and consider Cardinal's indication of interest."[359]

The first provision at issue was Section 5.1(n), which stated in the pertinent part:

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[351] *Id.* at 29. Additionally, Cardinal indicated its willingness to enter into a definitive agreement within "a few days," again with a price of $13.625 per share. *Id.*

[352] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 29.

[353] *Id.* at 30.

[354] *Id.*

[355] *Id.* (speculating that, without such a press release, Sun could have proceeded to terminate the ensuing merger and collect the $10 million termination fee).

[356] Marsh Supermarkets, Inc., Preliminary Proxy Statement, *supra* note 312, at 30 ("[W]e filed a complaint in the Hamilton Superior Court, Hamilton County, Indiana, naming . . . [the] defendants.").

[357] *Id.* at 31.

[358] *See* Marsh Supermarkets, Inc., Additional Definitive Proxy Soliciting Materials (Schedule 14A), Exhibit 99.2 (Aug. 2, 2006).

[359] *Id.* at 3.

> [Marsh] covenants and agrees that, except (i) as expressly provided in this Agreement, (ii) with the prior written consent of [Sun] . . .
>
> (n) neither [Marsh] nor any of its Subsidiaries shall ***waive or fail to enforce*** any provision of any confidentiality agreement or standstill or similar agreement to which it is a party . . . .[360]

Based on its interpretation of this provision, the court held the Marsh board would not have "'waive[d]' any provision . . . by consenting to review Cardinal's indication of interest."[361] Furthermore, even if Marsh had granted Cardinal permission to make its offer, Marsh would not have been in violation of the explicit terms of Section 5.1(n) because it would not have waived or failed to enforce the standstill it had with Cardinal.[362]

The second provision at issue, Section 5.5(d), contained a no-shop paired with a fiduciary out.[363] However, this provision also contained a further limitation on Marsh's rights, as follows:

> [Marsh] will . . . *cease and cause to be terminated immediately all existing discussions or negotiations with any Persons conducted on or before the date hereof with respect to any Competing Transaction*.[364]

Marsh did not actively solicit Cardinal's conditional non-binding indication of interest and therefore, by the terms of a basic no-shop provision, Marsh would have been able to consider Cardinal's interest

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[360] *Id.* at 6.

[361] *Id.*

[362] Marsh Supermarkets, Inc., Additional Definitive Proxy Soliciting Materials, *supra* note 358, at 6.

[363] *See id.* Notably, the court's analysis implied Cardinal's indication of interest would have fallen into the merger's definition of a "competing transaction," which Marsh was prohibited from actively pursuing under section 5.5(a)(i). *See id.*, at 7 n.3. Nevertheless, the court found that when reading sections 5.5(a)(i) and 5.1(n) in tandem, Marsh was allowed to consider and review Cardinal's indication of interest without obtaining prior consent from Sun. *Id.* (concluding Marsh may "passively" receive and review indications of interest based on an analysis that "harmonize[d]" sections 5.1(n) and 5.5(a)(i)). Thus, according to the court, if Marsh had *actively* pursued Cardinal's indication of interest, such action by the board would have constituted a furtherance of a competing transaction. *Id.*

[364] Marsh Supermarkets, Inc., Additional Definitive Proxy Soliciting Materials, *supra* note 358, at 9 (emphasis added).

without violating Marsh's agreement with Sun.[365] In comparison to a typical no-shop provision, the court found that this covenant imposed more stringent limitations on Marsh.[366] The court found while Marsh's board could consider *some* unsolicited indications of interest, it could not consider any competing transaction proposals with parties who had engaged in discussions or negotiations prior to the signing of the merger agreement.[367] Consequently, "Marsh [could] not consider an indication of interest from Cardinal under any circumstances."[368] Based on the court's logic, on the date that Marsh signed the contract, Marsh agreed that it would not engage in negotiations or discussions with any person who had previously been a party to the auction process.[369] Because Marsh and Cardinal had been in prior discussions, Marsh had an obligation to Sun to terminate discussions with Cardinal as of the date of the merger agreement.[370]

As a last line of defense, Cardinal sought to assert that the court's decision would usurp the board's ability to fulfill its fiduciary duties to the shareholders.[371] Rejecting this contention, the court found that Cardinal did not have standing to assert the alleged injury suffered by Marsh's shareholders.[372] On September 22, the shareholders approved the merger agreement that Sun and Marsh had agreed upon over four months earlier.[373]

Of particular note is that in November of 2006, Cardinal entered into a $215 million sale/leaseback agreement with Sun, whereby Cardinal acquired Marsh's former real estate assets from Sun.[374] Thus, Sun went on

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[365] *See id.* at 7 n.3.

[366] *Id.* at 9.

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

[368] *Id*. at 12.

[369] *See* Marsh Supermarkets, Inc., Additional Definitive Proxy Soliciting Materials, *supra* note 358, at11-12.

[370] *Id.* Notably, section 5.1(n) of the agreement is seemingly rendered superfluous by section 5.5(d). If a target company enters into a definitive agreement with a buyer, it seems that the language within section 5.1(n), regarding waiving or enforcing standstills, presupposes that the target had previously entered into standstills with another party (or multiple parties). Moreover, if such a standstill is in place, while it may depend on how a court interprets the words "discussions or negotiations," the language of section 5.5(d) would likely preclude the target from considering any indications of interest from parties who had executed standstills prior to the merger agreement. Thus, perhaps section 5.1(n) has no effect at all when it is coupled with 5.5(d).

[371] *Id*. at 13.

[372] *Id*. at 14.

[373] Marsh Supermarkets, Inc., Current Report (Form 8-K), at Item 8.01 (Sept. 22, 2006).

[374] *See* Client List: Marsh Supermarkets, CARDINAL CAPITAL PARTNERS, http://www.cardinalcapital.com/clients.php?id=45 (last visited Sept. 7, 2012) ("To help finance its acquisition, Sun Capital sought a sale-leaseback partner to acquire all of Marsh's viable real estate assets for approximately $215 million, or two-thirds of Sun's acquisition price. . . . Cardinal

to realize the profits that could have been money in the pockets of Marsh's shareholders had the board been able to pursue Cardinal's offer.[375]

## IV. STANDSTILLS: PROMISES MADE TO BE BROKEN?

This Article assumes that standstills should be a part of the pre-signing sales process and the legitimacy of requiring a standstill to be executed pre-signing is not up for debate.[376] Despite that assumption, standstills raise a number of unanswered questions under Delaware law as described in Part I of this Article. Namely, those questions revolve around a target board's ability to consider a third party superior offer made in contravention of a standstill; its promise not to waive a standstill; and a board's ability to grant a "winning" bidder the right to enforce a previously executed standstill against a "losing" bidder. These questions bring to light a conflict between a board's *Revlon* duty to maximize stockholder value and its ability to protect an executed transaction under *Unocal*. This section addresses how Delaware courts would likely answer these questions and resolve this *Revlon-Unocal* conflict.

### A. *Promises Meant to be Broken? Offers Made in Contravention of a Standstill*

One of the overarching questions Delaware courts have yet to address is whether a target must enforce a previously executed standstill if a bidder makes a higher bid after the target has executed a merger agreement with another bidder. In other words, must a target enforce a standstill when a losing bidder has broken its promise not to submit an overbid?[377] This open question has been repeatedly articulated in recent literature.[378] As Professor Steven Davidoff pointed out during the HCP-Ventas battle for Sunrise, "Delaware may or may not enjoin a bidder from breaching a standstill to offer a competing higher bid or otherwise allow a company to contractually override its fiduciary duties to consider a higher, competing bid."[379] Moreover, commentators have also stated:

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Capital Partners successfully closed on the $215 million sale-leaseback in November 2006.").

[375] *Id.*

[376] Whether standstills should be part of the pre-signing sales process will be addressed in a separate work-in-progress tentatively entitled *Auction Theory and Standstills: Dealing with Friends and Foes in a Sale of Corporate Control*, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2207693.

[377] Davidoff, *supra* note 22 (framing the question in the context of the *Ventas* decision).

[378] *Id.*

[379] *Id.*

> [E]ven if a bidding participant in the sale process signs a standstill agreement, the agreement's enforceability may be open to question. The harm to shareholders of precluding a bidder who is subject to a standstill agreement from making a bid above that resulting from the auction process may lead a board or a court to decline to enforce, at least by an injunction, the standstill agreement, depending upon the circumstances of the situation.[380]

As seen in the various deals described throughout this Article, the circumstances of the situation can vary greatly from deal to deal and courts tend to address deal protection devices, including standstills, as part of the larger sales process. It follows that the circumstances of the situation may include facts pointing to the possibility the target board was acting out of its own self-interest in agreeing to proceed with one bidder over another or otherwise using the standstill as a way of favoring one bidder over another. When considering the individual circumstances of each deal, Delaware courts would likely consider the value maximization methods used pre-signing. That is, the Delaware courts are likely to consider how well "shopped" a deal was in determining whether a target must consider a third party's offer.

### 1. Evaluating the Target Board's Actions in Deciding Whether to Enforce a Standstill

As Vice Chancellor Laster recently stated, "Delaware has a strong interest in policing the behavior of fiduciaries who agree to final-stage transactions. This is particularly so when the illicit behavior is secretive and subversive, yet appears to elicit yawns from Wall Street players who regard it as par for the course."[381] This policy interest is all too applicable in the context of standstills. Although the Delaware courts have yet to define

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[380] Arthur Fleischer Jr. & Alexander R. Sussman, *Responses to Takeover Bids: Corporate, SEC, Tactical, and Fiduciary Considerations*, 6-4th CORP. PRAC. SERIES (BNA), § XII (2012), *available at* 2011 WL 121413; *see also* Soren Lindstrom & Cedric Powell, *Standstill Considerations in an M&A Context: Recent Developments and Some Practice Pointers*, K&L GATES LLP (Mar. 2, 2012), http://www.klgates.com/standstill-considerations-in-an-ma-context-recent-developments-and-some-practice-pointers-03-01-2012/ ("[I]t is difficult for a target to litigate a standstill if it has put itself up for sale, as it may very well be perceived as management entrenchment and preventing the shareholders from receiving maximum value.").

[381] *In re* Del Monte Foods Co. S'holders Litig., 25 A.3d 813, 842 (Del. Ch. 2011) (citation omitted).

the parameters of standstills, they have most often examined standstills to determine whether the target board was using the standstill for an inequitable purpose.[382] Along these lines, in *Topps*, then-Vice Chancellor Strine indicated that standstills will not be upheld when the standstill is not being used to further "any apparent legitimate purpose."[383] This is consistent with the *Unocal*-enhanced scrutiny standard applicable to deal protection devices.[384] However, what types of purposes must be articulated to qualify as "legitimate" is an open question. Moreover, a related issue arises once a purpose has been articulated. That is, would the articulation of a purpose such as maximizing stockholder value overcome questionable behavior by the target's board?

Two deals explored earlier in this Article provide further clarification of the facts a Delaware court may consider in determining whether a purpose is legitimate.[385] First, consider the Northrop-Marietta fight for Grumman during which the Grumman board stated that it favored Marietta because of its willingness to maximize the cash consideration in the deal.[386] Northrop alleged it should have been invited to submit an offer before an agreement was entered into with Martin-Marietta.[387] Thus, the question becomes whether the Grumman board's failure to ask Northrop to submit an offer and entering into a merger with a $50 million termination fee were meant to maximize stockholder value or were in bad faith. Viewing the transaction now, it appears the board's actions fall into the former category. This conclusion is particularly supported by the fact that when Marietta attempted to force Grumman to enforce the standstill, Grumman's Chairman responded by asking how Grumman would be damaged by Northrop's offer made in contravention of the standstill.[388] Any arguable impropriety did not involve the use of the standstill *itself*.

At least initially, Grumman did not use the standstill to further any favoritism towards Marietta, or otherwise improperly prevent Northrop from making an offer.[389] Northrop was given several months to negotiate

[382] *See generally In re* Topps Co. S'holders Litig., 926 A.2d 58 (Del. Ch. 2007) (elaborating on the potential misuse of standstill agreements in terms of both denying opportunity to stockholders, and obscuring the truth from them).

[383] *Id.* at 92.

[384] For a discussion of the *Unocal* standard of enhanced scrutiny, *see supra* Part II.A.2.

[385] *See also supra* Part III.B.1 (discussing legitimate purpose in the context of *Topps*).

[386] Grumman Corp., Solicitation, Recommendation Statements, *supra* note 202, at 10-11.

[387] Grumman Corp., Amended Solicitation, Recommendation Statements, *supra* note 227, Exhibit 99.C18, at 1.

[388] *See* text accompanying *supra* note 233.

[389] Grumman Corp., Solicitation, Recommendation Statements (Schedue 14-D9), at 12 (Mar. 9, 1994).

with Grumman and put its best offer forward.[390] It was only after Northrop seemingly could not produce a favorable offer and Grumman entered into the Marietta agreement that the standstill could have been used improperly.[391] Had Grumman not released Northrop from its standstill obligation, there may have been a different outcome, as the standstill would have prevented any further Northrop offers entirely.[392] When confronted with the issue, Grumman promptly refused to enforce the standstill to allow Northrop to make an offer.[393] Grumman did not use the standstill itself in a manner inconsistent with its fiduciary duties or otherwise for an "illegitimate" purpose.[394] Hence, a Delaware court would likely have found that, although not perfect, Grumman's actions were meant to extract value from Marietta and were intended to maximize stockholder value for Grumman shareholders.

On the opposite end of the spectrum is the Formation-Fillmore bidding war for Genesis. In that case, the Genesis board's actions pre-signing seemed to favor Formation over Fillmore because of management's preference to work for Formation rather than Fillmore.[395] At the same time, however, the Genesis board was advised that Fillmore's offer was more favorable than Formation's offer.[396] Despite this advice, Genesis entered into an agreement with Formation without providing Fillmore with an opportunity to increase its offer.[397] The Genesis board did amend the merger agreement to allow a waiver of any pre-existing standstills so that previous bidders, specifically Fillmore, could overbid.[398] But despite Fillmore's increased bid and the bidding contest that ensued between Fillmore and Formation, Fillmore's CEO alleged that Genesis again prematurely ended the bidding process by accepting Formation's offer of $69.35 along with an increased termination fee.[399] Had Fillmore's offer been made in contravention of the standstill, similar to Northrop's offer, a Delaware court would have likely found that the Genesis board had been using the standstill

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[390] *See supra* Part III.A.2 (describing Northrop's negotiations with Grumman).

[391] Grumman Corp., Solicitation, Recommendation Statements (Schedule 14-D9), at 3 (Mar. 25, 1994) (discussing potential breaches of the established merger agreement between the two entities).

[392] *See id.* at 4 (discussing not only the conditions for terminating negotiations, but also specifying damages).

[393] *Id.*

[394] *Id.*

[395] *See* Part III.A.3.

[396] *See supra* note 254 and accompanying text.

[397] *See supra* notes 257-59 and accompanying text.

[398] *See supra* note 262 and accompanying text.

[399] *See supra* notes 263-65 and accompanying text.

inappropriately in an attempt to favor Formation over Fillmore because of Genesis management's preference to work for Formation. If the standstill had not been waived, there would have been a considerable amount of value left on the table as evidenced by the number of upward bid revisions after the release.[400] When considered in light of the fact that the Genesis board clearly favored Formation, it would seem that the standstill, if not waived, would not have been used for a legitimate purpose.

### 2. The Consideration of Pre-Signing Value Maximization Methods in Determining Whether to Enforce a Standstill

In addition to considering whether a board used a standstill for a legitimate purpose, in the context of a change of control transaction the Delaware courts would consider the reasonableness of the board's decision-making process generally.[401] As explained in Part II.A.2, the Delaware courts will consider the "value maximization tool" used to determine whether a board has acted reasonably.[402] Decades of Delaware precedent in the wake of *Revlon* have established that an auction process or, even an active bidding process, need not precede a board's entry into a merger agreement.[403] However, at the same time, the more extensive the sales process pre-signing the more easily a board satisfies this reasonableness requirement. Thus, to determine whether a board may (or must) consider an offer made in violation of the standstill, the Delaware Chancery Court would likely examine the amount of "shopping" done by the board pre-signing. If a pre-signing auction was held, and a number of bidders submitted offers, a Delaware court would be more likely to find that the board had satisfied its *Revlon* duties pre-signing. In such a case, the court would likely find that the board would not have an obligation to waive the standstill post-signing.

At the same time, however, a question remains as to how much pre-signing shopping would be sufficient for a Delaware court to find that the

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[400] Genesis Healthcare Corp., Current Report (Form 8-K), Exhibit 99.2 (Apr. 26, 2007) (the contents of the letter indicate a number of revisions).

[401] *See supra* Part II.A.2 (discussing Delaware jurisprudence on a board's fiduciary duties in the context of a negotiated transaction).

[402] *See In re* OPENLANE, Inc. S'holders Litig., 2011 WL 4599662, at *5 (Del. Ch. Sept. 30, 2011).

[403] *See* Marc A. Alpert & Alison H. Kronstadt, *No Pre-Signing Auction Necessarily Required to Satisfy Revlon Duties*, LEXOLOGY (May 29, 2012), http://www.lexology.com/library/detail.aspx?g=63d2b0bc-e264-4b61-a6e3-7d224133760d (describing how courts allowed for more broad-base exploration of potential buyers by removing the shackles of these occasionally rigid requirements).

board does not have an obligation to consider a higher third party offer. As with most M&A cases, Delaware would likely evaluate the amount of shopping required on a case-by-case basis. A court would likely consider numerous factors including, but not limited to, the background and financial stability of the target, the industry in which the target operates, the market generally, and the length of sales process pre-signing. Hence, a Delaware court is unlikely to announce a bright-line rule in the context of a standstill.[404]

In determining whether a board may consider a third party offer made in contravention of a standstill, the Delaware courts will likely be forced to address the concept of a bona fide offer. When drafting fiduciary outs, superior offer definitions, and termination provisions, practitioners often include a requirement that the third party offer be a bona fide one.[405] Thus, a likely argument could be made by either a target board or an initial buyer that a third party overbid made in contravention of a standstill does not meet the bona fide offer requirement in the merger agreement.

### 3. The Fiduciary Out and Bona Fide Offer Requirement

Of the deals outlined above, the HCP-Sunrise-Ventas conflict provides the clearest illustration of how, during the pre-closing period, bona fide language can create a threshold that an offer made in contravention of standstill must pass.[406] While HCP argued that a bona fide Acquisition Proposal was "one that is 'genuine' or 'authentic' in the sense that it is not a sham and is reasonably capable of becoming a Superior Proposal," the court rejected HCP's argument.[407] In doing so, the appellate court followed the superior court decision, which defined the term bona fide as "acting 'in good faith; sincere, genuine,'" and, consequentially failed to address HCP's assertion that the meaning of bona fide depends on context.[408]

Essentially, the analysis below illustrates why a Delaware court would likely only assess one issue when determining if a bidder is bona fide

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[404] Vice Chancellor Parsons' comments in *In re Celera Corporation Shareholder Litigation* discussed in Part III.B.1 provide an excellent example of this hesitation. The Vice Chancellor was careful to state that any decisions declaring "Don't-Ask-Don't-Waive" standstills unlawful would have to be made only in the context of a well-developed factual record. *See supra* text accompanying note 299.

[405] *See supra* Part III.A.1 (discussing the HCP-Sunrise-Ventas conflict, where the issue of bona fide offer arose).

[406] *See supra* Part III.A.1.

[407] Ventas, Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. 3d 254, para. 61 (Can. Ont. C.A.).

[408] *Id.* at para. 60.

(sometimes referred to as "assessing a party's bona fides"): whether the bidder has a good faith intent and ability to close a deal with the target. Chancellor Strine and a few prominent Delaware practitioners recently co-authored an article, in which they noted, "[o]ur favorite examples of redundancy are when courts have used both good faith and its Latin equivalent bona fide in the same sentence."[409] In light of the frequent association of the terms "bona fide" and "good faith,"[410] they are used interchangeably in this section. While ample case law and scholarly commentary can be found discussing good faith as it relates to a corporate director's duties, very few corporate law discussions specifically address which facts or circumstances are relevant when determining whether a *bidder's* acts were in "good faith" or "bona fide."[411] Thus, despite the association of these two terms, when assessing a bidder any attempt to apply points from fiduciary duty discussions raises an issue yet to be resolved by Delaware courts: whether the meaning of bona fide depends on the particular factual context. Even if a Delaware court determined that the definition of bona fide should be context specific, the court would still face a second issue. Specifically, the court would have to grapple with which factors would, or should, be considered when determining which bids are bona fide in the context of a fiduciary out.

In his recent article, Chancellor Strine suggested a Delaware court would deviate from the Canadian courts and find "good faith" is a term that

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[409] Leo E. Strine, Jr. et al., *Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law*, 98 GEO. L.J. 629, 654 n.74 (2010).

[410] *See, e.g.*, BLACK'S LAW DICTIONARY 199 (9th ed. 2009) (defining bona fide as "1. Made in good faith; without fraud or deceit. 2. Sincere; genuine"); Strine, *supra* note 409, at 696 (recognizing that the terms "bona fide" and "good faith" are functionally equivalent); *see* text accompanying *supra* note 172 (identifying Ontario Superior Court's definition of bona fide as "good faith; sincere, genuine"). Also of note is that "good faith" has been defined as,

> A state of mind consisting in (1) honesty in belief or purpose, (2) faithfulness to one's duty or obligation, (3) observance of reasonable commercial standards of fair dealing in a given trade or business, or (4) absence of intent to defraud or to seek unconscionable advantage. — Also termed *bona fides*. Cf. BAD FAITH. — ***good-faith**, adj.*

BLACK'S LAW DICTIONARY 762 (9th ed. 2009). In addition to these definitions, Delaware case law also associates bona fide with good faith. *See* Smartmatic Corp. v. SVS Holdings, Inc., 2008 WL 1700195, at *3 n.23 (Del. Ch. Apr. 4, 2008) (stating bona fide offers are those "made in good faith, given [the offer's] structure and its terms").

[411] *See* Corinne Ball et al., *Advice for Corporate Directors*, *in* MERGERS & ACQUISITIONS 2010: TRENDS AND DEVS., at 137, 213-14 (PLI Corp. Law & Practice, Course Handbook Ser. No. B-1781, 2010) ("Restrictions on the nature of the bidders are common although frequently not litigated. Common examples are requirements that the third-party bidder be "bona fide" and that any such bid be fully financed or not subject to material conditions or conditions other than those in the primary agreement.").

is "relational" to the object and "requires a state of mind and resulting behavior faithful to one's contextual obligations."[412] It follows, based on the relationship between good faith and bona fide and Strine's intimate understanding of Delaware corporate law, that a Delaware court would likely agree with HCP's assertion that determining which bids are bona fide is a "decision [that] must be made in the context of the entire situation."[413]

Assuming a Delaware court would find the meaning of bona fide depends on context, the next issue to be addressed is what bona fide should mean in the context of fiduciary out provisions. Looking outside of the Canadian standard and Strine's good faith discussion, other sources indicate that, when determining whether a buyer is bona fide, an analysis of a bidder's bona fides should focus on whether the "purported [buyer]" has the ability and "intent [to] complet[e] the transaction."[414] If a Delaware court applied this standard (hereinafter, the "Intent to Close Standard") when assessing a bidder's bona fides, then any third party who exhibited intent and ability to close a deal with the target would be considered bona fide.[415]

The Intent to Close Standard is different than the standard applied by the Ontario courts (hereinafter, the "Canadian Standard"). For example, in contrast to the Canadian Standard, the Intent to Close Standard would allow the target board to transact with any bidder that is willing and able to execute a deal – regardless of whether the bid was made in contravention of a standstill.[416]

This author proposes a number of factors that could be considered by a board (and a court reviewing a board's decision) as indicators of a bidder's intent to close the deal. These factors include the existence of any financing

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[412]Strine, *supra* note 409, at 646.

[413]*Ventas*, 85 O.R. 3d at para. 60.

[414]Samuel C. Thompson, Jr., *Change of Control Board: Federal Preemption of the Law Governing a Target's Directors*, 70 MISS. L.J. 35, 100 (2000); *see also* James T. Halverson & Ronald C. Wheeler, *Negotiating Merger Consent Decrees*, 2 ANTITRUST 23, 27 (1988) (stating "bona fide" should be "interpret[ed] . . . in a similar fashion to 'qualified'").

[415]As such, bidders with a good faith intent to close a transaction could be distinguished from bidders that are either puffing or posturing with the sole intent to bump up the price for a competitor.

[416]Even though the initial buyer would not be protected by bona fide language in the case of a third party's breach of a standstill, the breach still exposes the third party bidder to the risk that either the target or initial buyer may still have a claim for tortious interference with contract.

*See* Ventas, Inc. v. Health Care Prop. Investors, Inc., 635 F. Supp. 2d 612, 618-19 (W.D. Ky. 2009) (articulating elements of tortious interference with contract, including third party bidder's intent to cause the target to breach an existing contract). In addition to its relevance for tortious interference *with contract*, breach of a standstill might also be relevant to a plaintiff's claim of tortious interference *with prospective business advantage*. *See id.* at 621.

conditions in the offer, completion of due diligence efforts by the bidder, size and other characteristics of the bidder as they relate to potential ability to fund the transaction, and other terms or conditions of the offer. Additionally, and particularly pertinent to this Article, the target board could consider even a buyer's prior willingness to execute a standstill when determining whether the buyer intends to complete the transaction.[417] Ultimately, under the Intent to Close Standard, when applied to mergers in the *Revlon* context, the basic question a court will face is whether the target board can justify its affirmative determination that a bidder has a bona fide intent and ability to close a deal that maximizes shareholder value.

One circumstance that could potentially complicate matters for the target board, or a reviewing judge, would be the existence of competition between the initial buyer and the party seeking to jump the deal.[418] A bidder could want to drive the price up for its competitor by submitting a bid during the pre-closing period. More problematically, if the bidder is careful, this intent to drive up the price could potentially be concealed because the average bidder probably would not be as disturbingly blatant as HCP was about non-bona fide intent. However, because it would hardly be surprising for a competitor to seek to acquire another competitor—in the absence of other indications that the party seeking to jump the deal lacks the intent to close the transaction—a court would likely find that the mere existence of competition between the parties should not be interpreted as a determinative indication that the party is not bona fide.

Thus, in sum, when confronted with a third party offer made in contravention of a standstill, a Delaware court will *not* likely follow the Ontario courts' reasoning that the offer is not bona fide simply because the offer was made in breach of a standstill.[419] Instead, the court will examine (or require a board to examine) whether the third party had an intent to close. Moreover, in determining whether a board has an obligation to consider that offer pursuant to its fiduciary duties, the courts will likely consider the value maximization tools used by the target board in deciding to sell the company, as well as the purpose articulated by the board in applying the standstill.

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[417] *See supra* Part II.B (describing how standstills can be indicators of a bidder's seriousness).

[418] *See* Ventas, Inc. v. HCP, Inc., 2009 WL 2912779, at *3-*4 (W.D. Ky. Sept. 8, 2009) (finding an existence of competition between Ventas and HCP and discussing how competition relates to tortious interference analysis).

[419] *See, e.g.*, Ventas, Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. 3d 254, para. 61 (Can. Ont. C.A.) (holding that violation of a standstill precludes an offer from being deemed bona fide).

### B. *An Enforceable Promise? Promises not to Waive a Standstill and a Board's Fiduciary Duties*

A related issue to the board's obligation to enforce a pre-existing standstill is the board's ability to agree not to waive a standstill. As when deciding on the validity of a standstill, when considering an agreement to not waive or fail to enforce a standstill, the Delaware courts would likely look to whether the provision was used for a legitimate purpose and the amount of shopping done prior to the agreement.[420] In *Topps*, then-Vice Chancellor Strine alluded that there may be situations where a target board may legitimately agree not to waive a standstill.[421] Specifically, Strine pointed to a multiple round auction involving three final round bidders all of which occurred after a broad market canvass.[422] Strine postulated in that scenario a target might be able to promise not to waive a standstill to extract additional value from the auction participants.[423] Strine again annunciated this idea in *Ancestry.com*, further stating that in the context of Don't-Ask-Don't-Waive standstills, a specific value-maximizing purpose should exist, and stated that such a purpose may exist if a "well-motivated seller . . . use[d] it as a gavel" to signal that "there is really an end the auction."[424]

Consistent with Chancellor Strine's hypothetical in *Topps*, a Delaware court may likely require the target's pre-signing shopping be more extensive when a board is agreeing pre-signing not to waive a standstill agreement in the future. Underlying Strine's view, the requirement of further shopping is necessary because of the greater restrictions that an agreement not to waive would impose on a board of directors to exercise its fiduciary duties under *Revlon*.[425]

The Cardinal-Sun battle for Marsh[426] provides a good illustration of the amount of shopping that may be required during the pre-signing before a target may enforce an agreement not to waive a standstill. Although Marsh's actions would be questionable under *Revlon* value-maximization principles, they must be considered in light of the significant amount of

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[420] *See, e.g.*, *In re* Topps Co. S'holders Litig., 926 A.2d 58, 91 n.28 (Del. Ch. 2007) (suggesting the potential validity of a board's express agreement to not waive a standstill).

[421] *Id.*

[422] *Id.*

[423] *Id.*

[424] The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction at 19, *In re* Ancestry.com Inc. S'holder Litig., C.A. No. 7988-CS, 23-24 (Del. Ch. Dec. 17, 2012).

[425] *See Topps*, 926 A.26 at 91 ("[T]he Topps board reserved the right to waive the Standstill if its fiduciary duties required. That was an important thing to do, given that there was no shopping process before signing . . . .").

[426] *See supra* Part III.B.2.

shopping done by Marsh. Because Marsh's board had engaged in an extensive sales process,[427] a court would likely find that its actions were reasonable, although not perfect. Cardinal had the opportunity to submit two indications of interest and refine its offer by the point Marsh entered into an agreement with Sun.[428] Cardinal was given ample time to negotiate and could be blamed for failing to use its time wisely.[429] Because Marsh had been dealing with Cardinal for a while, provided it the opportunity to define a more concrete proposal, and had been shopping for so long, the Marsh board knew Cardinal and knew the value of Marsh's shares.[430] While Marsh's reasons for agreeing to the merger agreement provisions when another bidder was present may have been weak, the Marsh board must have believed that the possibility for increasing value through entertaining the Cardinal offer was not as real as it seemed. A bird in the hand is better than two in the bush, and Marsh obtained the highest value *reasonably* attainable. If a Delaware court were reviewing the facts of this case, the court would likely uphold Marsh's promise not to waive the standstill.

Reconsider the hypothetical bidding war between Bidder A and Bidder B for Target and Target's promise not to waive all previously executed standstills, including the one with B.[431] The limited facts of the hypothetical appear to be very similar to those alluded to by Chancellor Strine in *Topps*; namely, an active auction process with three final round bidders.[432] Although in the A-B-Target hypothetical there are only two final round bidders, assuming the board and its financial advisor fairly enforced the auction rules and there was no self-dealing or entrenchment issues on the part of Target's board, a Delaware court could likely find that Target's promise not to waive the standstill is an enforceable one.[433] At the same

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[427] *See* Marsh Supermarkets, Inc., *supra* note 312, at 31 (describing, in detail, the voluminous number of steps and communications required to move the sale forward).

[428] *Id.* at 26.

[429] *E.g.*, *id.* at 31 (describing the six month period the company had to locate valid financing).

[430] *See supra* Part III.B.2.

[431] *See supra* Part I.

[432] *In re Topps Co. S'holders Litig.*, 926 A.2d at 91 n.28.

[433] This is how I believe a Delaware court would act based on previous cases and Delaware's application of *Revlon*, *Unocal*, and their progeny. I should note, however, that this is not how I believe the Delaware courts *should* act. In particular, in a previous article, *Rethinking Contractual Limits on Fiduciary Duties*, I argued that certain situations might call for a limitation on the board's ability to act post-closing in the context of a fiduciary out. Sautter, *supra* note 33, at 60. More specifically, I advocated for a narrower merger recommendation out in certain circumstances. *Id.* at 96-101. However, as I made clear in that article, I do not believe that a target's board of directors should be able to limit itself from withdrawing its recommendation in favor of a transaction in the event the target has received a superior offer. *Id.* at 98 n.251. Along

time, however, as indicated in *Celera*,[434] *Rehabcare*,[435] *Complete Genomics*,[436] and *Ancestry.com*,[437] the Target should exercise due care when requiring potential bidders like B to agree not to ask for a waiver. A Delaware court is likely to find that, absent a calculated goal, binding a bidder to such an agreement in advance prevents the target's board from exercising its ability to adequately weigh its options pre-closing should circumstances change.

### C. *An Enforceable Promise or a Promise Meant to be Broken? A Board's Grant to a Winning Bidder of the Right to Enforce a Standstill*

Another open issue under Delaware law is whether a target board may legitimately grant a winning bidder the right to enforce a standstill against an overbidder. As previously discussed, Sunrise granted Ventas such a right "to enforce any existing Standstill Agreements with third parties" in the Sunrise-Ventas definitive acquisition agreement executed after Ventas won the auction.[438] The Canadian court upheld the grant;[439] however, Delaware courts have yet to directly address this issue and it is unclear whether Delaware courts would do the same.[440]

The main concern with such a grant is that the winning bidder has "very different incentives than the target's Board" and thus could prevent a third party's rebid.[441] By granting a winning bidder the right to enforce a standstill against a third party overbidder, the target's board is essentially delegating its fiduciary duties to the third party. Such a delegation was

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these lines, the board also should not be able to completely limit itself from considering an overbid that is or may become a superior offer. By promising not to waive a standstill, a target would be doing exactly that.

[434] *In re* Celera Corp. S'holder Litig., 2012 WL 1020471, at *21 (Del. Ch. Mar. 23, 2012) (asserting that these sorts of agreements not to request a waiver, in combination with standstills, are more troublesome).

[435] Transcript of Settlement Hearing at 46, *In re* Rehabcare Group, Inc. S'holders Litig., C.A. No. 6197-VCL (Del. Ch. Sept. 8, 2011) (questioning the validity of agreements not to ask for a standstill waiver after *Topps*).

[436] Telephonic Oral Argument and the Court's Ruling, *In re* Complete Genomics, Inc. S'holder Litig., C.A. No. 7888-VCL (Del. Ch. Nov. 27, 2012).

[437] The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction, *In re* Ancestry.com Inc. S'holder Litig., C.A. No. 7988-CS (Del. Ch. Dec. 17, 2012).

[438] Ventas, Inc. v. HCP, Inc., 647 F.3d 291, 299 (6th Cir. 2011).

[439] Ventas, Inc. v. Sunrise Senior Living Real Estate Inv. Trust (2007), 85 O.R. 3d 254, paras. 34-35 (Can. Ont. C.A.).

[440] Former Chancellor, now Professor William T. Allen alluded to this very issue recently by asking,"[i]f a Special Committee in an auction or quasi-auction process contractually obligates bidders not to overbid, is such a contract term enforceable, and if so, by whom?" *See* Allen, *supra* note 21, at 52.

[441] Spatt & Martelli, *supra* note 94, at 37.

deemed to be invalid in the context of a no-shop provision in *Ace Ltd. v. Capital Re Corp.*[442] In that case, then-Vice Chancellor Strine stated a board may not agree to a provision that requires "an abdication by the board of its duty to determine what its own fiduciary obligations require at precisely that time in the life of the company when the board's own judgment is most important."[443] Although in many situations, in granting a winning bidder the right to enforce a standstill, the board is not explicitly allowing the winning bidder to step into the shoes of the target board; said board is *implicitly* doing just that. The winning bidder has, in most cases, an overwhelming interest in protecting the transaction for which it negotiated and, as such, it has profound reasons for not granting a waiver of a standstill to allow a rebid.

There are, however, limited circumstances in which a board could be able to curtail its power to entertain superior proposals in the context of a transaction that is subject to a shareholder vote.[444] Specifically, in *Ace*, Strine stated such a limited circumstance may be "where a board has actively canvassed the market, negotiated with various bidders in a competitive environment, and believes that the necessity to close a transaction requires that the sales contest end."[445] But at the same time, Strine noted that "where a board has not explored the marketplace with confidence and is negotiating a deal that requires stockholder approval and would result in a change in stockholder ownership interests, a board's decision to preclude itself—and therefore the stockholders—from entertaining other offers is less justifiable."[446]

In his December 2012 bench ruling in *Ancestry.com*, Chancellor Strine seemed to follow his reasoning in *Ace* with respect to the grant of the right to enforce a standstill.[447] Specifically, he stated if the board decided to use a Don't-Ask-Don't-Waive standstill as a "gavel" then the shareholders should be informed

> that the board made the cost/benefit trade-off that the best way to get the value was to draw the highest bid out from those people while they were in the process; that in order to do that,

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[442] 747 A.2d 95 (Del. Ch. 1999).

[443] *Id.* at 106.

[444] *See id.* at 107 (noting that, in the case *sub judice*, that the board's complete refusal to consider another offer was well outside the range of such circumstances).

[445] *Id.* at 107 n.36.

[446] *Ace*, 747 A.2d at 107 n.36.

[447] The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction at 19, *In re* Ancestry.com Inc. S'holder Litig., C.A. No. 7988-CS, 27-28 (Del. Ch. Dec. 17, 2012).

> it had to incur the cost of giving to the winner the right to enforce it.[448]

If the Delaware courts were to extend Strine's reasoning in *Ace* and his suggestion in *Ancestry.com*, a court considering a third party's right to enforce the standstill would likely again engage in the same examination of the pre-signing shopping process as previously described throughout this section.[449] Applying this analysis in the case of A and B's battle for Target, a Delaware court would likely uphold A's ability to enforce the standstill as granted and promised by Target. Thus, when ultimately presented with the various issues addressed in this Article, a Delaware court is likely to find that standstills, and other promises relating to standstills, are enforceable promises under the facts and circumstances of many cases.

## V. CONCLUSION

Standstill agreements are a common promise made during the sale of a company. However, standstills can create a conflict between a target board's duty to maximize stockholder value in a sale of control, or *Revlon* duty, and the board's ability to protect an executed agreement as permitted by the Delaware Supreme Court's decision in *Unocal* and its progeny. The conflict is particularly evident after the target has executed a merger agreement with a "winning bidder" and a "losing bidder" makes a higher offer for the target in contravention of the standstill.

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[448] *Id.*

[449] Although the Delaware courts would likely extend Strine's reasoning in *Ace* so that the pre-signing sales process may be considered, I do not believe from a normative perspective this should be the case. These limited circumstances should not even be considered in providing the winning bidder with the contractual right to enforce the standstill. The target's grant of this type of right extends the delegation of power at issue in *Ace* to a new level. More specifically, the no-shop provision at issue in *Ace* prevented the target board from providing information to a third party who made an overbid and from engaging in discussions or negotiations with the third party until certain requirements were satisfied. *Ace*, 747 A.2d at 98. Among these requirements was that the target board had to make the determination "based on the *written advice of its outside legal counsel*, that participating in such negotiations or discussions or furnishing such information [was] required in order to prevent the Board of Directors of the Company from breaching its fiduciary duties to its stockholders . . . ." *Id.* (emphasis added). In contrast to the written opinion in *Ace* that was found to be an improper delegation of the board's fiduciary duties, granting a winning bidder the right to enforce a pre-existing standstill is a far more extreme delegation of a board's fiduciary duties. By granting a winning bidder such a right, the board is in essence granting the winning bidder the right to determine when a third party overbid is or is not a Superior Offer under the terms of the no-shop fiduciary out. As such, by promising the winning bidder this right, the target board is making an unenforceable promise.

This overbid, or the potential for it, raises a number of questions that Delaware courts, and academics alike, have yet to address. Those questions revolve around a target board's ability to consider a third party superior offer made in contravention of a standstill; its promise not to waive a standstill; and a board's ability to grant a "winning" bidder the right to enforce a previously executed standstill against a "losing" bidder. When ultimately presented with these questions, Delaware courts will answer each question by examining the value maximization tools utilized by the board during pre-signing to determine the reasonableness of the board's decision-making process. Namely, the court will consider the extent to which the board "shopped" the company pre-signing. Moreover, in determining whether the board can decide not to consider an offer, agree not to waive a standstill, or grant the "winner" the right to enforce a standstill, the courts, in accordance with *Unocal*, will also consider the purpose of the board's actions under the circumstances of each case. Specifically, if a valid value maximization purpose is articulated and the board is not acting to further its own self-interests, then a Delaware court would likely find the board's actions to be reasonable and uphold the board's promises. In addressing these questions, this Article attempts to fill a thirty-year void in academic literature regarding the interplay of standstills and a board's fiduciary duties during the pre-closing period.