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Delaware Chancery Allows Buyer Aiding and Abetting and Other Fiduciary Breach Claims to Proceed

In an opinion that touches on a number of important issues related to acquisitions of public companies, the Court of Chancery in *In re Answers Corp. Shareholders Litigation*, Consol. C.A. No. 6170-VCN (Del. Ch. Apr. 11, 2012), denied motions to dismiss claims against a target's board of directors and the private equity acquiror of the target. While the opinion was issued in the context of a motion to dismiss, which in Delaware requires only that a complaint state "reasonably conceivable" claims, we nevertheless find the opinion interesting in particular for the court's refusal to dismiss the aiding and abetting claims against the buyer.

In early 2010, Answers' 30% stockholder, Redpoint Ventures, desired to sell its stake in Answers. The complaint alleged that the only way Redpoint Ventures could sell its interest was through a sale of the entire company because the public float was too thin to absorb the holder's 30% stake. In pursuit of a company sale, two company directors affiliated with Redpoint Ventures allegedly began soliciting interest, leading eventually to negotiations with an affiliate of Summit Partners, a private equity fund. There was allegedly no discussion as to whether a private sale of the stake was considered or possible. Negotiations with Summit Partners proceeded throughout 2010.

In late 2010, with the parties nearing agreement on terms and price, Answers disclosed projections showing a positive outlook for the remainder of 2010 and through 2011. Thereafter, Summit Partners allegedly pressed for a swift conclusion of negotiations because of the positive outlook and a brief two-week post-signing market check. The board allegedly acquiesced to the rushed process and failed to adequately assess whether the company's stock price would appreciate in response to the eventual disclosure of the positive company projections to such an extent that the company would be worth more remaining as a standalone publicly-traded company.

The court acknowledged its skepticism of certain factual allegations, but given the stage of the proceedings, it was required to accept all of plaintiffs' factual allegations as true so long as they passed the low "reasonably conceivable" hurdle. As such, the court held that if the allegations were true, they would support claims for breach of fiduciary duty against the directors and for aiding and abetting those breaches of fiduciary duty by the acquiror.

In particular, the court found that the following claims were reasonably conceivable:

- That directors affiliated with a 30% stockholder had a conflict of interest arising from the stockholder's desire for liquidity which could only be achieved through a sale of the company and not through a public market sale of the stock due to the company's thin float.

- That directors who were otherwise independent violated their duties of loyalty by agreeing to a brief two-week market check in order to avoid the rising stock price overtaking the contemplated deal price.

- That the target CEO, who was also a director, pushed for a sale of the company because he believed that he would retain his position only if a sale were accomplished.

- That a buyer knowingly participated in a breach of fiduciary duty by pressuring the board to agree to the brief market check after receiving non-public company projections showing positive results that might cause the company's stock price to overtake the contemplated deal price.

While additional facts may be entered into the record that will ultimately refute these allegations, the litigation continues for now.

This decision raises a number of concerns for directors of public companies evaluating potential sale transactions. The allegations against the two Redpoint-affiliated directors—if eventually supported by evidence—would form the basis of a breach of the duty of loyalty because the allegations were that the directors acted in the interests of the large stockholder and not the interests of the company or its other stockholders. Further, the allegations against the outside directors—that they allowed the transaction to proceed at a pace that was not in the interests of the corporation or the non-Redpoint stockholders—would also state a claim for breach of the duty of loyalty. Such breaches, if ultimately found, would be non-exculpable and, thus, the directors would then be litigating with personal liability at stake.

This decision also raises concerns for private equity firms – both when supporting a sale as an existing stockholder with affiliated directors on the board and when acquiring a public company. It is noteworthy that the claims of aiding and abetting against the private equity buyer survived based on a sequence of events that may not be infrequent: a private equity buyer receives confidential projections from the target that show a positive outlook and later pushes for a quick end to the process and customary deal protections in the definitive agreement.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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