

ClientAlert

Mergers & Acquisitions

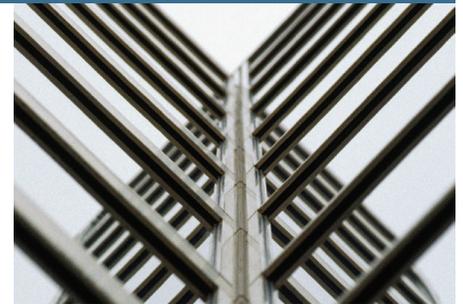
October 2014

Delaware Court Decides Damages in Breach of Fiduciary Duty Aiding and Abetting Case

In March 2014, Vice Chancellor Laster of the Court of Chancery of the State of Delaware issued an opinion finding Rural/Metro Corporation's lead financial advisor liable for aiding and abetting breaches of fiduciary duty by Rural's board of directors in connection with Rural's 2011 sale to an affiliate of Warburg Pincus LLC (the "Liability Opinion"). ([Click here](#) for the White & Case Client Alert on the Liability Opinion.) Vice Chancellor Laster has now set such financial advisor's liability to Rural's former stockholders at approximately US\$75.8 million (*In re Rural/Metro Corporation Stockholders Litigation*, C.A. No. 6350-VCL (Del. Ch. Oct 10, 2014)). According to the Court, this amount represents 83% of the total damages that former Rural stockholders suffered.

Vice Chancellor Laster applied a "quasi-appraisal" approach in fashioning relief, holding that money damages equal to the "fair" or "intrinsic" value of the common stock held by Rural stockholders at the time of the merger less the price actually received by such stockholders for such stock was the appropriate remedy. In the Liability Opinion, the Court adopted the discounted cash flow model presented by the plaintiffs' expert as the general framework for its valuation analysis and instructed the parties to submit revised expert valuations using certain inputs identified by the Vice Chancellor. On that basis, and with supplemental submissions and evidence presented at trial, the Court determined that the value of Rural common stock on the merger date was US\$21.42 per share. As Rural stockholders received US\$17.25 per share in the 2011 sale, Vice Chancellor Laster found that Rural stockholders suffered an out-of-pocket loss of US\$4.17 per share. This resulted in a finding of total damages of approximately US\$91.3 million.

The Court then addressed the lead financial advisor's claim that it was entitled to a settlement credit under the Delaware Uniform Contribution Among Tortfeasors Law ("DUCATA"). While the Court concluded that there was no bright-line rule barring the financial advisor from claiming a settlement credit even though, in the Court's view, the financial advisor knowingly participated in the directors' breach, the Court held that the doctrine of "unclean hands" vis-a-vis the other alleged joint tortfeasors prevented the financial advisor from claiming settlement credit with respect to damages related to (i) the board's failure to disclose material information in the definitive proxy statement and (ii) the board's breaches of its fiduciary duty in approving the merger. In the Court's view, these breaches of fiduciary duty resulted from affirmative misrepresentations and disclosure omissions by the financial advisor toward the individual defendant directors. The Court, however, permitted the financial advisor to claim settlement credit for aspects of the sale process that did not involve such misrepresentations or omissions.



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The Court next analyzed whether any of the settling defendants were “joint tortfeasors,” entitling the lead financial advisor to a right of contribution under DUCATA. In determining whether the director defendants were joint tortfeasors, the Court considered whether “the proposed contributor could have “common liability”—in the sense of an obligation to pay money damages—for the injury to the plaintiff.” As Rural’s certificate of incorporation contained an exculpatory provision for directors as permitted under Section 102(b)(7) of the Delaware General Corporation Law, those directors who breached solely their duty of care to Rural would not be deemed joint tortfeasors and would be protected from liability. Ultimately, the Court found that two directors would not have been entitled to exculpation under Section 102(b)(7). Accordingly, these directors would have shared a common liability with the lead financial advisor, thereby entitling the financial advisor to a reduction in its liability equal to the share of responsibility attributable to those directors.

As for allocation of responsibility, the Court determined that the financial advisor was solely responsible for the failure to disclose certain material information in the definitive proxy statement, to which the Court allocated 50% of the stockholders’ damages, and the board’s fiduciary duty breaches related to the board’s final approval of the merger, to which the Court allocated 25% of the stockholders’ damages. The remaining 25% of the damages was attributed to the board’s breaches of fiduciary duty resulting from the special committee’s decision to commence a sale process before obtaining the full board’s approval. The Court allocated 8% of such damages to the lead financial advisor and 17% to the applicable directors. Based on these determinations, the Court held that 17% of the responsibility for the damages suffered by the class was attributable to the actions of two of the director defendants, and ultimately reduced the damages assessed against the lead financial advisor by 17%.

This decision, along with the Liability Opinion, again highlights the scrutiny given by Delaware courts to potential conflicts of interest. Companies must ensure that board and committee members are properly empowered, and advisors must be vigilant in monitoring potential conflicts of interest and in keeping the board apprised of developments as appropriate.

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