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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

Christina M. Sautter[†]

BUD FOX: How much is enough?

GORDON GEKKO: It's not a question of enough, pal. It's a zero-sum game, somebody wins and somebody loses.

—*Wall Street*¹

I. INTRODUCTION

The question “How much is enough?” has likely resonated through boardrooms for decades in the wake of the Delaware Supreme Court’s 1986 landmark decision, *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,² announcing that once the sale of a company becomes inevitable, the board must take steps to ensure the maximization of value for the benefit of the stockholders.³ The Supreme Court forever altered the corporate sales process by further stating that directors should foster competitive bidding to obtain the highest price possible

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¹ WALL STREET (Amercent Films, American Entertainment Partners L.P., Twentieth Century-Fox Film Corp. 1987).

² 506 A.2d 173 (Del. 1986).

³ *Id.* at 182.

for stockholders.⁴ Initially, this appeared to signal a movement toward a purer auction model, or at least a more competitive bidding process in the market for corporate control.⁵ Over the past twenty years, however, dealmakers have devised various tactics and sale methods in response to this perceived movement.⁶

Similar to Delaware's takeover jurisprudence, corporate sale methods are not formed in a vacuum, but are products of the periods in which they are developed. *Revlon*, for example, is a direct result of the mergers and acquisitions ("M&A") landscape of the 1980s, which for many is best exemplified by the 1987 movie *Wall Street*. This period was marked by unprecedented deal volume, highly leveraged transactions, hostile takeovers, and corporate raiders, like Gordon Gekko, who often challenged entrenched management.⁷ The buyout boom of the 1980s left a lasting impression on corporate case law, as the Delaware courts issued a number of watershed opinions addressing a board's obligations to stockholders as well as management and board greed. The cases stemmed from stockholder allegations that boards and management resisted deals offering large premiums in an effort to maintain their jobs.⁸

⁴ *Revlon*, 506 A.2d at 183.

⁵ See Mark J. Loewenstein, *Toward an Auction Market for Corporate Control and the Demise of the Business Judgment Rule*, 63 S. CAL. L. REV. 65, 66-68 (1989) (describing the movement toward an auction model for corporate control).

⁶ The focus of this Article is on post-signing market checks and go-shop provisions. For in-depth discussions of these sale methods, see *infra* Part II.C-E.

⁷ See Jason M. Klein, *When the Board Should Just Say Yes to Management: The Interplay Between the Decision of Whether to Conduct an Auction and Transaction Structure*, 5 STAN. J.L. BUS. & FIN., Aug. 1999, at 45, 45-46 (describing the M&A environment in the 1980s); Joseph S. Allerhand & Bradley R. Aronstam, *New Wave of M&A Litigation Attacks Private Equity Deals*, 238 N.Y.L.J. 9 (July 9, 2007) ("[M]erger and acquisition activity in the 1980s was epitomized by hostile takeovers and the 'omnipresent specter' of entrenched management . . ."). During the early 1980s, management buyouts ("MBOs") were characterized by the sales of divisions of larger companies, but the trend shifted in the mid-1980s to highly leveraged MBOs of complete companies rather than divisions. Klein, *supra*, at 45-46. The trend shifted again during the late 1980s when management utilized MBOs as defensive tactics against corporate raiders. *Id.* at 46; see also Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1022 (1997) (stating that management obtained job security through MBOs).

⁸ See Peter Lattman & Dana Cimilluca, *Court Faults Buyouts—Delaware Rulings Raise Disclosure Questions in Topps, Lear Deals*, WALL ST. J., July 12, 2007, at C1 (describing the legal claims arising from the 1980s buyout boom and recognizing corporate raiders offered stockholders large premiums and promised to remove boards and management).

The furious dealmaking activity of the last few years has led some to compare the current M&A environment to that of the 1980s.⁹ In many respects, the comparison is a fair one as there has been a resurgence of leveraged buyouts (“LBOs”),¹⁰ management buyouts (“MBOs”),¹¹ and hostile takeovers.¹² There are, however, a number of subtle but important developments that highlight the differences between the two decades. Unlike the hostile transactions of the 1980s that were generally led by corporate raiders, today’s hostile takeover attempts are increasingly launched by strategic buyers and, more recently, private equity buyers.¹³ In addition, corporate raiders have been replaced by, or have simply transformed themselves into, stockholder activists.¹⁴ For example, Carl Icahn, the quintessential corporate raider—and real-life Gordon Gekko

⁹ See Rik Kirkland, *Private Money*, FORTUNE, Mar. 5, 2007, at 50 (comparing the current prevalence of private equity leveraged buyouts to leveraged buyouts in the 1980s); Joe Nocera, *From Raider to Activist, But Still Icahn*, N.Y. TIMES, Feb. 3, 2007, at C1 (quoting Peter J. Solomon, a prominent New York investment banker, as stating, “We are in a carnivorous wave . . . The last one was about greenmailing and corporate raiding. This one is about private equity and activists.”).

¹⁰ An LBO is a takeover of a company in which an acquirer uses borrowed funds to finance the transaction. Typically, the target company’s assets are used as security for the debt the acquirer incurred in purchasing the target. In an LBO, the acquirer profits by taking the company public with an initial public offering, or by selling the company to another acquirer.

¹¹ An MBO is a transaction in which the target company’s management purchases the target’s publicly held shares and takes the company private. An MBO is typically financed as a leveraged buyout.

¹² See Philip Mills & Mutya Harsch, *Hostile Takeovers: How to Avoid the Jump*, INT’L FIN. L. REV., Dec. 2006, at 44, 44-45 (describing increases in financial sponsored deals and hostile activity globally).

¹³ See Igor Kirman, *Takeover Law and Practice*, in DOING DEALS 2007: UNDERSTANDING THE NUTS & BOLTS OF TRANSACTIONAL PRACTICE 9, 22 (PLI Corp. Law & Practice Handbook Series No. 1594, 2007) (contrasting today’s hostile activity involving strategic buyers to hostile deals in the 1970s and 1980s); see also *In re Netsmart Techs., Inc. S’holders Litig.*, 924 A.2d 171, 198 (Del. Ch. 2007) (recognizing that, in the early part of this decade, strategic buyers jumped competitors’ deals and that the current trend is for private equity firms to outbid strategic buyers); *In re Toys “R” Us, Inc. S’holder Litig.*, 877 A.2d 975, 1008 (Del. Ch. 2005) (recognizing that a marketplace exists “where strategic buyers have not felt shy about ‘jumping’ friendly deals crafted between their industry rivals”); ROBERT E. SPATT, THE FOUR RING CIRCUS—ROUND ELEVEN; A FURTHER UPDATED VIEW OF THE MATING DANCE AMONG ANNOUNCED MERGER PARTNERS AND AN UNSOLICITED SECOND OR THIRD BIDDER 1, 1-9 (Mar. 17, 2007), available at http://stblaw.com/content/publications/publications23_0.pdf (listing examples of U.S. and foreign transactions from 1994 to early 2007 in which a deal was jumped or a jump was attempted).

¹⁴ See Kirman, *supra* note 13, at 27-28 (discussing increase in stockholder activism).

figure of the 1980s—has now embraced the role of stockholder activist.¹⁵

Recent years have seen the unprecedented growth of M&A activity and the re-emergence of private equity firms playing an enhanced role in M&A deals. For example, in 2006, global deal volume totaled \$3.79 trillion with private equity buyouts accounting for nearly a fifth of all deals.¹⁶ Dealmakers began 2007 at an even more accelerated pace. During the first half of the year, deal volume totaled \$1.005 trillion in the United States alone, representing a 36% increase from the same period in 2006 and marking the first time that M&A activity has ever reached that level in the first half of any year.¹⁷ During the first half of 2007, private equity firm-sponsored LBOs accounted for \$644 billion worth of deals worldwide.¹⁸ This is up 95.1% from 2006 and accounts for 34% of the \$1.005 trillion of U.S. deal activity and nearly a quarter of all merger activity worldwide.¹⁹ Although recent months have seen turmoil in the credit markets that are so vital to private equity transactions and dealmaking generally, record transaction volume demonstrates that we have been in the midst of a distinctive time for deal activity over the past few years.

Like the unique takeover activity of the 1980s, the recent M&A boom has prompted the Delaware courts to address the actions, and sometimes the alleged greed, of

¹⁵ See Nocera, *supra* note 9, at C1 (describing Icahn's transition from corporate raider to stockholder activist); see also William W. Bratton, *Hedge Funds and Governance Targets*, 95 GEO. L.J. 1375, 1377-79 (2007) (describing recent example of Icahn's stockholder activism during proposed Mylan Laboratories-King Pharmaceuticals deal).

¹⁶ Heather Timmons, *The Year That Made Deal Makers Giddy*, N.Y. TIMES, Jan. 5, 2007, at C6 (citing Thomson Financial statistics regarding 2006 deal flow and indicating that another statistics firm, Dealogic, has stated that 2006 deal flow was worth even more, at \$3.98 trillion). According to Thomson Financial, the \$3.79 trillion figure represents an increase of 38% from 2005. *Id.*

¹⁷ See Jessica Hall, *U.S. Merger Volume Hits Record Despite Soft June*, REUTERS, June 28, 2007, <http://www.reuters.com/article/mergersNews/idUSN2837929220070628> (citing Dealogic statistics).

¹⁸ Grace Wong, *Private Equity: Scrooge No Longer*, CNNMONEY.COM, July 10, 2007, http://money.cnn.com/2007/07/10/markets/pe_philanthropy/index.htm (citing Thomson Financial statistics).

¹⁹ *Id.* (citing Thomson Financial statistics that the number of private equity deals accounted for a quarter of all M&A deals worldwide and represented a 95.1% increase from the previous year); Grace Wong, *Private Equity: The Beat Goes On*, CNNMONEY.COM, July 4, 2007, http://money.cnn.com/2007/07/04/markets/pe_what_next/index.htm (citing Dealogic statistics that private equity buyouts accounted for 34% of \$1 trillion U.S. deal activity in the first six months of 2007).

corporate management and boards.²⁰ This time the cases often involve allegations by stockholders that boards have favored private equity buyers who are seeking to retain management with enhanced compensation packages.²¹ Like the 1980s, today's high deal volume and new dealmakers are creating a new set of issues for courts to address, including new sale methods that purportedly enable boards to better satisfy their *Revlon* duties.²²

Perhaps the most prominent and controversial among these new deal tactics are go-shop provisions. Unlike "no shop" or "window shop" provisions—deal protection devices which prevent a target company from actively soliciting bids following the signing of a definitive agreement—go-shop provisions permit a target company to *actively* solicit alternative bidders for a limited period *after* entering into a definitive agreement with an acquirer.²³ Since *Revlon*, dealmakers have relied primarily on pre-signing public auctions or targeted market canvasses in an effort to obtain the highest possible price for stockholders.²⁴ Because these sale methods are completed pre-signing, M&A agreements generally include a "fiduciary out"²⁵ that enables the target board to consider unsolicited third party offers received between signing and receipt of stockholder approval. However, the board may only consider the third

²⁰ This Article focuses solely on Delaware law because of Delaware's well-developed body of corporate case law, its continuing influence over other states' corporate laws, and its dominant position in the incorporation market. For example, over 50% of U.S. corporations that are currently traded on the New York Stock Exchange and NASDAQ, and 61% of Fortune 500 companies, are incorporated in Delaware. DIVISION OF CORPORATIONS, DEL. DEP'T OF STATE, 2006 ANNUAL REPORT, <http://www.corp.delaware.gov> (search for "2006 Annual Report").

²¹ See Lattman & Cimilluca, *supra* note 8, at C1 ("In the current buyout craze, many buyout firms retain the management by offering rich pay packages and a stake in the newly private entity.").

²² See Grace Wong, *Rival Bidders Emerge for Big Buyouts*, CNNMONEY.COM, Mar. 19, 2007, http://money.cnn.com/2007/03/19/markets/pe_deals/index.htm [hereinafter *Rival Bidders*] ("The deal landscape may be growing more intense, but private equity firms—considered some of the savviest deal makers on Wall Street—undoubtedly are looking out for ways to stay one step ahead of their rivals.").

²³ 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 2007: CURRENT OFFENSIVE & DEFENSIVE STRATEGIES IN M&A TRANSACTIONS, at 7, 106-07 (PLI Corp. Law & Practice, Course Handbook Series No. 1584, 2007) (differentiating no shops and go-shops).

²⁴ See *infra* note 69 and accompanying text (discussing how public auctions and market canvasses are the best ways to ensure the maximization of stockholder value).

²⁵ For a description of "fiduciary out" provisions, see *infra* Part II.A.2.

party offer if it is, or may become, a superior offer.²⁶ Thus, in the typical deal, a target is “closed for business” and must ignore advances from third parties unless an unsolicited superior proposal is received. By contrast, go-shop provisions effectively allow a target to extend its typical “store hours” and actively seek a better deal during the time in which it otherwise would have been officially closed for business.

Although go-shop provisions initially surfaced during the late 1980s, the provisions received scant attention from the M&A community until dealmakers began utilizing the provisions with increasing frequency over the past three years. This increased use of go-shop provisions has triggered a debate among commentators as to the effectiveness of the provisions and have led some to question whether the provisions are merely “window dressing” enabling boards to claim that they have satisfied their duty to maximize stockholder value.²⁷

This Article demonstrates, through an examination of the go-shop provision’s development, that despite *Revlon*, Delaware courts have failed to take affirmative steps to promote the maximization of stockholder value. Furthermore, this Article argues that the ability of a company to extend its “store hours” by actively shopping post-signing has the same end result with respect to value maximization as the typical post-signing market check that relies solely on a no shop provision coupled with a fiduciary out. Part II of the Article explores the evolution of go-shop provisions.²⁸ The section begins with a general discussion of deal protection devices with a particular focus on no shop and window shop provisions, the predecessors to the go-shop, and then moves into a more specific description of the Delaware courts’ treatment of post-signing market checks in light of *Revlon* and its progeny.²⁹ The

²⁶ See *infra* notes 50-51 and 86 and accompanying text (describing fiduciary outs and use of fiduciary outs). Merger agreements differ on what constitutes a “superior offer,” with factors such as the form of consideration, certainty of closing, and regulatory issues often playing an important role. However, this Article assumes that the principal determination of whether an offer is superior is the value of consideration paid.

²⁷ See Mark A. Morton, Partner, & Roxanne L. Houtman, Assoc., Potter Anderson & Corroon LLP, *Go-Shops: Market Check Magic or Mirage?* 1, 7-8 (May 2007), www.potteranderson.com/assets/attachments/Potter_Anderson_Go-Shops_rev.pdf (questioning whether go-shop provisions are effective or are “window dressing”). For a further discussion regarding the effectiveness of go-shop provisions, see *infra* Part III.A.

²⁸ See *infra* Part II (describing the evolution of the go-shop).

²⁹ See *infra* Part II.A-C.

section ends with a discussion of the development of go-shop provisions.³⁰ Part III discusses the effectiveness of go-shop provisions, including critics' arguments that the provisions have a chilling effect on the bidding process.³¹ This section also includes an examination of *In re Topps Co. Shareholders Litigation* and *In re Lear Corp. Shareholders Litigation*, the most recent Delaware cases to specifically address and validate go-shop provisions.³² Part IV of this Article contends that, despite facial differences, go-shop provisions and post-signing market checks are effectively the same.³³ The Delaware courts' continuing validation of both post-signing market checks and go-shop provisions reveal the courts' hesitancy in disrupting signed transactions and has resulted in a movement away from Delaware's policy that directors should act as auctioneers and conduct a sale process that will result in the maximization of stockholder value. Thus, I contend that this continued trend in Delaware jurisprudence, including the Delaware Court of Chancery's validation of go-shop provisions, signals the death of the policies, originally set forth in *Revlon*, promoting a more competitive sale process, and, ultimately, higher value realization for stockholders.

II. THE RISE OF GO-SHOP PROVISIONS

A. *Deal Protection Generally*

To fully appreciate no shops, market checks, and go-shops, one must first understand the reasons that dealmakers use deal protection devices generally and how typical deal protection devices are used in combination. In classic consumer shopping situations, once a consumer finds and selects a desired product at a price he or she is willing to pay, the consumer can generally rest assured that the time spent and money invested thus far is not for naught. In such situations, the time between the selection of a product and the exchange of money and ownership is usually limited, and thus the risk that an interloper will upset the transaction is likewise extremely small or, in most cases, nonexistent. However, the same does not hold true in the M&A world.

³⁰ See *infra* Part II.D-E.

³¹ See *infra* Part III.A.

³² See *infra* Part III.B.

³³ See *infra* Part IV.

Unlike everyday consumer transactions, the purchase of a public company cannot be completed prior to the fulfillment of certain closing conditions. These conditions include stockholder approval, the preparation and filing of a proxy statement, and, in many cases, regulatory approval, including antitrust approvals, the registration of securities to be issued in connection with the transaction and other required third party consents.³⁴ Because of the time needed to accomplish these required closing conditions, the interim period between signing the transaction agreement and closing the transaction can stretch anywhere from several weeks to several months, or beyond.³⁵

By the time of signing, the acquirer has devoted a significant amount of time and money to identifying the target and to assessing the target's value.³⁶ In addition to traditional sunk costs that are associated with identifying and assessing the value of the target, commentators have also identified operational costs and reputational costs that the initial acquirer may incur in the event that the transaction is not completed. For example, Professor Guhan Subramanian has argued that if a deal is not completed, the initial acquirer may suffer a decrease in its own stock price and may be viewed as "weak" in the market for corporate control.³⁷ Such a reputation for weakness may result in the reduction of future profit opportunities for the acquirer because other bidders may be more willing to enter into a future bidding contest against a "weak" bidder.³⁸ Because of these potential costs, the acquirer will seek to prevent its proposed transaction from being interrupted, or "jumped," by a third party.

³⁴ See Stephen M. Bainbridge, *Exclusive Merger Agreements and Lock-Ups in Negotiated Corporate Acquisitions*, 75 MINN. L. REV. 239, 241 n.3 (1990) (listing closing conditions).

³⁵ See *id.* at 241 (explaining there is generally a two to four month period between signing and closing); John C. Coates IV & Guhan Subramanian, *A Buy-Side Model of M&A Lockups: Theory and Evidence*, 53 STAN. L. REV. 307, 310 (2000) (stating that the period between signing and closing ranges from a minimum of thirty days to up to six months).

³⁶ See Bainbridge, *supra* note 34, at 242 (describing purchaser's sunk costs).

³⁷ See Guhan Subramanian, *The Drivers of Market Efficiency in Revlon Transactions*, 28 J. CORP. L. 691, 701-02 (2003) (describing potential operational and reputational costs that acquirer may incur in the event of a failed deal).

³⁸ See *id.* at 702 (describing reputational costs); see also Coates & Subramanian, *supra* note 35, at 360 (stating that bidders may decide not to enter future auctions if a "tough" bidder has already entered the bidding contest, or may drop out if a tough bidder enters).

On the other hand, the target's board has an obligation to act in the best interests of the business and must fulfill its fiduciary duties to the corporation's stockholders.³⁹ In some cases, this may mean considering options that arise after the signing of a definitive transaction agreement as a result of a deal being "jumped." In addition, the target's stockholders may not approve the proposed transaction for any reason, including the existence of a superior third party bid. Thus, a definitive agreement between the initial acquirer and the target is not necessarily a "sure thing" because it does not effectively bind the target to the transaction.⁴⁰ This tension between the initial acquirer's costs and the non-binding nature of the agreement on the target and its stockholders has given rise to deal protection devices. As the name suggests, deal protection devices include a variety of contractual terms that are incorporated into a definitive agreement with the goal of protecting a deal from being "jumped" by a third party by making the third party's bid riskier and more expensive.⁴¹ The inclusion of at least some combination of deal protection devices has become de rigeur in public M&A transactions.⁴²

The following section is a brief summary of some typical deal protection devices, including no shops, window shops, no talk provisions, termination or break-up fees, and matching rights. In addition, this section also focuses on "fiduciary outs," which act as important exceptions to deal protection devices. This section, as well as the remainder of this Article, addresses how dealmakers use these devices in combination and how the Delaware courts have treated the results of such combinations.

³⁹ For a discussion of a board's fiduciary duties in a change of control context, see *infra* notes 63-71 and accompanying text.

⁴⁰ See note 86 and accompanying text. There also are reasons why the target may want a binding definitive agreement. For example, if the acquirer backs out, the target risks being left "in play" without another buyer. Sean J. Griffith, *Deal Protection Provisions in the Last Period of Play*, 71 *FORDHAM L. REV.* 1899, 1900-01 (2003) (describing a target's reasons for avoiding non-binding agreements). In addition, an unsolicited bid from a financial buyer may not present the same opportunities for synergy that the signed deal with a strategic buyer may be capable of. See *id.*

⁴¹ See *id.* at 1902-03 (describing why deal protection mechanisms are used); see also *McMillan v. Intercargo Corp.*, 768 A.2d 492, 506 n.62 (Del. Ch. 2000) (stating that deal protection devices make "it more difficult and more expensive to consummate a competing transaction and . . . provid[e] compensation to the odd company out if such an alternative deal nonetheless occurs").

⁴² See Block, *supra* note 23, at 89 (stating that acquirers and targets will often bargain for deal protection devices); Coates & Subramanian, *supra* note 35, at 315 (indicating that, by 1998, lock-ups appeared in 80% of deals and termination fees appeared in 70% of deals).

1. No Shop Provisions, Window Shop Provisions, and No Talk Provisions

Although the term “no shop” can refer to a variety of covenants in an M&A agreement, pure no shop provisions prevent a target’s board from *actively* soliciting bids after the target has entered into a definitive agreement with an initial acquirer.⁴³ Similarly, window shop provisions prevent a target from actively soliciting bids from third parties after the signing of a definitive agreement.⁴⁴ However, a window shop provision contains a fiduciary out that allows the target’s board to negotiate with, provide due diligence materials to, and, if appropriate, ultimately accept a bid from a third party that makes an unsolicited offer if taking such action is necessary to avoid a breach of the board’s fiduciary duties.⁴⁵ Typically, window shop provisions require that the unsolicited third party bid meet certain criteria in order to exercise the fiduciary out; among these requirements is that the third party bid be deemed a superior proposal to that of the incumbent bidder.⁴⁶ Although technically slightly different, the terms “no shop” and “window shop” are frequently referred to interchangeably and will be referred to interchangeably throughout this Article.

Conversely, no talk provisions prevent the target from actively soliciting potential third party bids and from negotiating with, or providing due diligence or other information to, a third party who has submitted an unsolicited offer, despite the terms of the unsolicited offer.⁴⁷ In essence, as the name suggests, no talk provisions prevent targets from speaking with interested third parties altogether, unless the target has permission from the initial acquirer. Practitioners have viewed no talk provisions that do not contain fiduciary outs as per se invalid because they can prevent a target’s board

⁴³ Block, *supra* note 23, at 91. Block indicates that pure no shops are generally not permissible in transactions resulting in a change of control of the target unless the target’s board has already fulfilled their *Revlon* duties by conducting an auction. *Id.* at 93. For a further discussion of a board’s *Revlon* duties and related sale methods, see *infra* notes 63-86 and accompanying text.

⁴⁴ Block, *supra* note 23, at 91.

⁴⁵ *Id.* For a further discussion of fiduciary out clauses, see discussion *infra* Part II.A.2.

⁴⁶ See Block, *supra* note 23, at 92 (listing typical window shop fiduciary out requirements).

⁴⁷ See *id.* at 91 (describing no talk provisions); Thanos Panagopoulos, *Thinking Inside the Box: Analyzing Judicial Scrutiny of Deal Protection Devices in Delaware*, 3 BERKELEY BUS. L.J. 437, 446 (2006) (same).

from fulfilling their fiduciary duties, which the Delaware Court of Chancery has stated is the “legal equivalent of willful blindness.”⁴⁸

Delaware courts analyze the validity of no shop provisions based on the particular facts and circumstances of a given case. Accordingly, courts will uphold no shop provisions where they “do not foreclose other offers, but operate merely to afford some protection to prevent disruption of the Agreement by proposals from third parties that are neither bona fide nor likely to result in a higher transaction.”⁴⁹

2. Fiduciary Outs

Although fiduciary outs are not deal protection devices, fiduciary outs are used with deal protection devices to ensure the validity of the devices. Fiduciary outs are contractual clauses that allow the target to perform an act that the agreement otherwise forbids (or to refrain from doing an act that the contract requires) if the performance of the forbidden act (or non-performance of the required act) would otherwise result in a violation of a board’s fiduciary duties.⁵⁰ When a board exercises its fiduciary out, the resulting act, or failure to act, is not considered to be a contractual breach.⁵¹ Thus, the fiduciary out acts as a safe harbor to the deal protection mechanism.

3. Termination or Break-Up Fees

No shops are often paired with termination or break-up fees that are payable by the target to the incumbent bidder

⁴⁸ *Phelps Dodge Corp. v. Cyprus Amax Minerals Co.*, Nos. CIV. A. 17398, CIV. A. 17383, CIV. A. 17427, 1999 WL 1054255, at *1 (Del. Ch. Sept. 27, 1999) (“No-talk provisions . . . are troubling precisely because they prevent a board from meeting its duty to make an informed judgment with respect to even considering whether to negotiate with a third party.”); *see also* *Ace Ltd. v. Capital Re Corp.*, 747 A.2d 95, 106-09 (Del. Ch. 1999) (suggesting that no talk provisions are invalid); Karl L. Balz, *No-Shop Clauses*, 28 DEL. J. CORP. L. 513, 545 (2003) (describing the validity of no talk provisions and scenarios where no talk provisions may be deemed valid).

⁴⁹ *Matador Capital Mgmt. Corp. v. BRC Holdings, Inc.*, 729 A.2d 280, 291 (Del. Ch. 1998).

⁵⁰ *See* William T. Allen, *Understanding Fiduciary Outs: The What and the Why of an Anomalous Concept*, 55 BUS. LAW. 653, 653-54 (2000) (defining fiduciary outs).

⁵¹ *See id.* at 654.

upon the occurrence of specific circumstances.⁵² Typical triggering events include the termination of an agreement following (1) the target board's withdrawal, modification or change in its recommendation of the proposed transaction; (2) the target board's recommendation of a competing proposal; (3) the target board's exercise of a fiduciary out in favor of a superior proposal; or (4) the stockholders' failure to approve the proposed transaction.⁵³ Delaware courts have upheld termination fees ranging from 1% to 6% of the target's equity value.⁵⁴ Generally, however, dealmakers include termination fees ranging from 1% to 5% of transaction value, with a median of approximately 2.6% to 3%.⁵⁵

In the event that a deal falls through, termination fees guarantee that the initial acquirer will at least be compensated for the fees and expenses that it incurred in negotiating the underlying agreement.⁵⁶ Although the target incurs the termination fee, the fee is considered a transaction cost for

⁵² Termination fees can also be payable by an acquirer to the target in certain situations, including where the acquirer breaches an agreement and fails to consummate the transaction. Fees payable by the acquirer to a target are known as reverse termination fees.

⁵³ See Block, *supra* note 23, at 115-16 (describing typical triggering events for termination fees).

⁵⁴ See *id.* at 110 (describing current practices relating to termination fees). The courts treat termination fees as liquidated damages and rely on authority stating that liquidated damage provisions equal to between 1% and 5% of the proposed acquisition price are reasonable. See *Kysor Indus. Corp. v. Margaux, Inc.*, 674 A.2d 889, 897 (Del. Super. Ct. 1996) (citing Bainbridge, *supra* note 34, at 245). Despite treating termination fees as liquidated damages, the Delaware courts refuse to issue a bright-line rule regarding the acceptable percentage of termination fees. See *La. Mun. Police Employees' Ret. Sys. v. Crawford*, 918 A.2d 1172, 1181 n.10 (Del. Ch. 2007) ("Though a '3% rule' for termination fees might be convenient for transaction planners, it is simply too blunt an instrument, too subject to abuse, for this Court to bless as a blanket rule."). However, in dicta, the Delaware Court of Chancery has indicated that a termination fee of 6.3% "certainly seems to stretch the definition of range of reasonableness and probably stretches the definition beyond its breaking point." *Phelps Dodge*, Nos. CIV. A. 17398, CIV. A. 17383, CIV. A. 17427, 1999 WL 1054255, at *2. For further examples of termination fees that the Delaware Court of Chancery have upheld, see *infra* note 112.

⁵⁵ See Block, *supra* note 23, at 110 (describing typical termination fees).

⁵⁶ See *Kysor Indus.*, 674 A.2d at 897 (stating that termination fees act as a form of reimbursement for the initial bidder's lost opportunities and expenditures); Panagopoulos, *supra* note 47, at 445 (describing the purposes of termination fees). Generally, "the more closely a fee resembles the actual and economic costs incurred by a party the more likely it is to be upheld by a court." Gregory V. Varallo & Srinivas M. Raju, *A Process Based Model for Analyzing Deal Protection Measures*, 55 BUS. LAW. 1609, 1613 (2000).

the topping bidder.⁵⁷ Thus, termination fees may act as disincentives for third parties who are considering “jumping” a deal because they make the topping bid more expensive.⁵⁸

4. Matching Rights

In addition to termination fees, no shops are commonly paired with matching rights, also referred to as topping or last-look rights. Matching rights require the target to inform the incumbent bidder of a superior proposal and allow the incumbent bidder a period during which the incumbent bidder may match, or exceed, the unsolicited superior proposal.⁵⁹ Thus, matching rights have the capability of creating a post-signing bidding war between the initial acquirer and one or more interlopers who have submitted superior proposals.

Matching rights act as deal protection devices because they deter potential bidders from “jumping in” post-signing since potential bidders are aware that the initial acquirer may submit another bid matching, or exceeding, the superior proposal.⁶⁰

5. Go-Shop Provisions

As previously discussed, go-shop provisions appear to be the opposite of no shop provisions.⁶¹ Go-shops allow a target to *actively* solicit buyers after the target has already entered into a definitive agreement with a purchaser. Although commentators tend to refer to go-shop provisions as deal protection devices, I contend that go-shops are more similar to fiduciary outs because they allow the target company to

⁵⁷ See *Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914, 938 (Del. 2003) (“To the extent that defensive measures are economic and reasonable, they may become an increased cost to the proponent of any subsequent transaction.”).

⁵⁸ See Panagopoulos, *supra* note 47, at 445; Judd F. Sneirson, *Merger Agreements, Termination Fees, and the Contract-Corporate Tension*, 2002 COLUM. BUS. L. REV. 573, 581-82 (providing examples illustrating how termination fees deter topping bids).

⁵⁹ See Block, *supra* note 23, at 117 (describing typical matching rights). Generally, matching rights also require the target to inform the initial acquirer of the identity of the person who submitted the superior proposal. *Id.* In addition, the initial acquirer is typically given three business days’ notice of a possible termination. *Id.* Once the initial acquirer is given notice, the matching rights provision usually requires that the target negotiate in good faith with the initial acquirer so that the initial acquirer may make a superior proposal. *Id.*

⁶⁰ *Id.*

⁶¹ See *infra* Part IV.

actively solicit other bidders following signing and could result in the termination of an agreement in favor of a superior proposal.⁶² A more in-depth discussion of the typical characteristics of go-shop provisions is set forth in Part II.E.

B. *Fiduciary Duties of the Board*

Over the past several years, practitioners, academics, and jurists have wrestled with the judicial standard of review applicable to deal protection devices, an issue that this Article does not seek to address.⁶³ However, it is clear since *Revlon* that once a board of directors contemplates a transaction that will cause either a change in corporate control⁶⁴ or a breakup of the corporate entity, the board is obligated to seek the best present value reasonably available to stockholders.⁶⁵

⁶² See, e.g., Block, *supra* note 23, at 91, 106 (grouping go-shop provisions with deal protection devices).

⁶³ See Gregory V. Varallo & Srinivas M. Raju, *A Fresh Look at Deal Protection Devices: Out from the Shadow of the Omnipresent Specter*, 26 DEL. J. CORP. L. 975, 975-76 (2001) (stating that academics, practitioners, and jurists have long debated the appropriate standard of review for deal protection devices and noting that the Delaware Court of Chancery has struggled with the issue); see also Balz, *supra* note 48, at 527-44 (analyzing the appropriate standard of review applicable to no shop provisions); Stephen J. Lubben & Alana J. Darnell, *Delaware's Duty of Care*, 31 DEL. J. CORP. L. 589, 627 (2006) (arguing that the duty of care standard should be applied to deal protection devices unless the merger is a defensive measure); Panagopoulos, *supra* note 47, at 448-71 (examining and critiquing the judicial standards applicable to deal protection devices). See generally Symposium, *Judicial Standards of Review of Corporate Fiduciary Action*, 26 DEL. J. CORP. L. 995, 1059-82 (2001) (transcript of a symposium session at which jurists, practitioners, and scholars debated the standards of review applicable to corporate actions and, in particular, to deal protection devices).

⁶⁴ This Article does not seek to define what constitutes a "change of control transaction," which Delaware jurists recognize to be an unanswered question. See William T. Allen et al., *Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 26 DEL. J. CORP. L. 859, 895 n.130 (2001) (former chancellor and his co-authors recognizing that courts have yet to fully address what constitutes a change of control under Delaware law); see also *In re TW Servs., Inc. S'holders Litig.*, CIV. A. Nos. 10427, 10298, 1989 WL 20290, at *8 (Del. Ch. Mar. 2, 1989) (asking when *Revlon* duties apply).

⁶⁵ See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986) (holding that a board's act of authorizing management to negotiate a merger or buyout is a recognition that the company is for sale and changes the board's duty from the "preservation of . . . a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit"); see also Allen et al., *supra* note 64, at 894 ("Where directors have decided to commit the corporation to a change of control transaction, their actions must be evaluated solely by reference to their duty to obtain the highest value reasonably available."). The Delaware Supreme Court has held that *Revlon* duties attach

when a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear break-up of the company. . . . [or where], in response to a bidder's offer, a target abandons its

Additionally, a board's favoritism of a particular bidder over another is permitted only if the board's objective is to maximize the stockholders' value of their shares.⁶⁶ However, the board need not maintain a "level playing field" at all times.⁶⁷ The Supreme Court has recognized that, because today's corporate and financial environment is continuously evolving, "no single blueprint" exists for a board to satisfy its *Revlon* duties.⁶⁸

Although "no single blueprint" exists, a transaction with the highest bidder following a full public auction is the most desirable way in which a board can satisfy *Revlon*'s enhanced scrutiny test.⁶⁹ In fact, the Delaware Supreme Court held that in a change of control situation, "a board's primary duty becomes that of an auctioneer responsible for selling the company to the highest bidder."⁷⁰ The board is also required to take steps that foster, rather than impede, bidding, which will presumably result in the maximization of stockholder value.⁷¹

Following *Revlon*, the Delaware courts have held that a full-blown public auction is not necessarily a requirement for change of control transactions for all corporations under Delaware law.⁷² Indeed, there are certain situations in which

long-term strategy and seeks an alternative transaction involving the breakup of the company.

Paramount Comm'ns, Inc. v. Time Inc., 571 A.2d 1140, 1150 (Del. 1990) (citation omitted).

⁶⁶ *In re Topps Co. S'holders Litig.*, 926 A.2d 58, 64 (Del. Ch. 2007).

⁶⁷ *See In re TW Servs.*, 1989 WL 20290, at *7 (holding that there is no duty to conduct an auction or maintain a "level playing field" when a company is for sale).

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

⁶⁹ *See Morton & Houtman, supra note 27*, at 1 (stating that transactions with the highest bidder after either a full public auction or a slightly more limited market check in which a number of bidders are contacted directly and participate in bidding likely satisfies a board's *Revlon* duties); Mark W. Peters et al., *Emergence of the "Go-Shop,"* 11 WALLSTREETLAWYER.COM: SEC. ELECTRONIC AGE 7 (2007) (indicating that the most desirable way for the board of a target to fulfill its *Revlon* duties is to conduct a full public auction and enter into an agreement with the bidder making the highest offer). However, even when a full-blown public auction is conducted, the definitive agreement must still contain a fiduciary out. *See infra* note 86 and accompanying text.

⁷⁰ *Revlon*, 506 A.2d at 184.

⁷¹ *See id.* at 183 (stating that the result of the lock-up in *Revlon* "was not to foster bidding, but to destroy it").

⁷² *See 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."); *In re Toys "R" Us, Inc. S'holder Litig.*, 877 A.2d 975, 1000 (Del. Ch. 2005) ("[T]he [Delaware] Supreme Court has held that the duty to take reasonable steps to secure the highest immediately available price does not invariably require a board to conduct an auction process or even a targeted market canvass in the first instance, emphasizing that there is 'no single blue-print' for fulfilling the duty to maximize value."). However, small micro-cap companies may not be able to rely on a limited

a public auction is not desirable, as boards may view public auctions as placing the company at a competitive disadvantage.⁷³ For example, if a company conducts a public auction, the company risks losing employees, customers and suppliers.⁷⁴ In addition, the company also runs the risk of being viewed by the market for corporate control as “damaged goods” if the company does not receive any indications of interest or if the board determines that the offers it receives are inadequate.⁷⁵ Thus, in the event of a failed auction, it may take some time for a company to successfully sell itself.⁷⁶ Furthermore, although potential bidders are required to execute confidentiality agreements before being provided with a confidential offering memorandum or commencing due diligence, companies also risk disclosure of proprietary or sensitive information to the public and to other competitors.⁷⁷ In addition, in some cases, the target may have already been approached by a potential purchaser whose bid may be lost if the target board were to choose to engage in a full blown auction.⁷⁸ As a result, target boards may be faced with a situation in which they are interested in exploring change of control possibilities but do not desire to actively pursue a public auction.

In these situations, targets often choose to engage in a more limited pre-signing market canvass.⁷⁹ That is, a target, or

public auction or post-signing market check. *See infra* notes 83-85 and accompanying text.

⁷³ The Delaware Court of Chancery also recognizes the potential risks involved with a public auction. *See In re MONY Group Inc. S’holder Litig.*, 852 A.2d 9, 21 (Del. Ch. 2004) (recognizing benefits to single bidder approaches).

⁷⁴ *See Peters et al.*, *supra* note 69 (listing reasons why boards choose not to conduct public bidding processes).

⁷⁵ Heath Price Tarbert, *Merger Breakup Fees: A Critical Challenge to Anglo-American Corporate Law*, 34 LAW & POLY INT’L BUS. 627, 633-34 (2003) (internal quotation marks omitted) (citing F. George Davitt, *Orchestrating Takeover Talks: The Corporate Board*, SF86 ALI-ABA 677 (2001)) (describing the possibility that customers, suppliers, and potential acquirers may view a target as “damaged goods” upon the failure of a transaction).

⁷⁶ *See Embarking on the Sale Process*, in ABA COMMITTEE ON NEGOTIATED ACQUISITIONS, *THE M&A PROCESS: A PRACTICAL GUIDE FOR THE BUSINESS LAWYER* 93, 93-94 (2005) (detailing the disadvantages of auctions, including the length of time it takes to sell a company after a failed auction).

⁷⁷ *See In re Topps Co. S’holders Litig.*, 926 A.2d 58, 62 (Del. Ch. 2007) (noting the target’s “legitimate proprietary concerns” about turning over information to a competitor).

⁷⁸ *See, e.g., id.* at 61 (stating that the buyer’s bid was contingent on the target not conducting a public auction); *In re Lear Corp. S’holder Litig.*, 926 A.2d 94, 104 (Del. Ch. 2007) (same).

⁷⁹ *See Morton & Houtman*, *supra* note 27, at 1 (stating that a transaction with the highest bidder occurring after a more limited market check in which a number

more likely its financial advisor, will contact a select group of potential bidders, who may be interested in purchasing the target. Because only a limited number of potential purchasers are contacted, the risks associated with a pre-signing market canvass are not as great as with a public auction since the target company has not been placed “on the auction block.”

In addition to a public auction or a more limited pre-signing market canvass, Delaware courts have repeatedly validated a target board’s more exclusive reliance on a no shop with a fiduciary out or a window shop provision,⁸⁰ also known as a post-signing market check. This alternative, as previously discussed,⁸¹ permits the target to terminate the definitive agreement in favor of an unsolicited proposal that would result in a better deal with a third party. As Part II.C will demonstrate, the Delaware courts’ repeated blessing of a target’s reliance on post-signing market checks in the absence of a public auction or targeted market canvass has made the post-signing market check a third sale method for targets. It is worth noting, however, that recent Delaware jurisprudence indicates that small micro-cap companies⁸² may need to engage in a more complete targeted market canvass rather than rely on a post-signing market check.⁸³ In such a situation, the rationale for a more complete pre-signing market canvass is that micro-cap companies do not attract as much attention from the market for corporate control as their large-cap counterparts attract and micro-cap companies are less likely to

of bidders are contacted directly and participate in bidding likely satisfies a board’s *Revlon* duties).

⁸⁰ See, e.g., *In re* MONY Group Inc. S’holder Litig., 852 A.2d 9, 23-24 (Del. Ch. 2004); *In re* Pennaco Energy, Inc., 787 A.2d 691, 705-07 (Del. Ch. 2001); *In re* Fort Howard Corp. S’holders Litig., Civ. A. No. 9991, 1988 WL 83147, at *12-13 (Del. Ch. Aug. 8, 1988).

⁸¹ See discussion *supra* Part II.A.1 (describing no shop and window shop provisions).

⁸² According to the Securities and Exchange Commission’s proposed regulation of smaller companies, micro-cap companies are “companies whose outstanding common stock (or equivalent) in the aggregate comprises the lowest 1% of total U.S. equity market capitalization” or, in other words, those companies whose market capitalization is less than approximately \$128.2 million. Exposure Draft of Final Report of Advisory Committee on Smaller Public Companies, 71 Fed. Reg. 11,090, 11,092 (May 3, 2006). Under the same recommendation, large-cap companies are those companies whose outstanding common stock (or equivalent) accounts for 94% of total U.S. equity market capitalization or, in other words, those companies whose market capitalization is more than approximately \$787.1 million. See *id.* (table).

⁸³ See *In re* Netsmart Techs., Inc. S’holders Litig., 924 A.2d 171, 197-99 (Del. Ch. 2007) (finding that targeting of private equity buyers and not strategic buyers was likely a breach of *Revlon* duties).

be hostile takeover targets.⁸⁴ Thus, the Delaware Court of Chancery found that a micro-cap company's limited pre-signing market canvass and the reliance on a post-signing market check did not adequately fulfill a board's duties to maximize stockholder value.⁸⁵ Nonetheless, even when a large-cap or micro-cap company has engaged in a public auction or limited pre-signing market check, agreements must still contain a fiduciary out in order to allow the target board to fulfill its *Revlon* duties between signing and the stockholders' approval of the proposed transaction.⁸⁶

C. *Before the Rise of the Go-Shop: Post-Signing Market Checks*

In the wake of *Revlon*, Delaware courts have repeatedly addressed the intensity of the post-signing market check necessary to satisfy a board's *Revlon* duties in the absence of a public auction or other pre-signing market canvass, or in the event that a target conducted only a very limited market canvass.⁸⁷ However, the courts, and in particular the Delaware Court of Chancery, are constrained by the context in which these cases arise. The plaintiffs in these cases are typically the

⁸⁴ *Id.* at 197-98; see also *In re Lear*, 926 A.2d at 123 n.22 (stating that strategic buyers of micro-cap companies in niche markets are not likely to make unsolicited proposals without prior discussions or information).

⁸⁵ *In re Netsmart*, 924 A.2d at 199.

⁸⁶ See *Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914, 938 (Del. 2003) ("The directors of a Delaware corporation have a continuing obligation to discharge their fiduciary responsibilities, as future circumstances develop, after a merger agreement is announced."). In *Omnicare*, the majority opinion made it clear that the target company's board of directors was required to negotiate a fiduciary out clause to protect its stockholders in the event that the proposed transaction became an inferior offer. *Id.* The majority stated that by failing to include a fiduciary out clause, the target board had effectively "disabled itself from exercising its own fiduciary obligations at a time when the board's own judgment is most important, i.e., receipt of a subsequent superior offer." *Id.*

⁸⁷ See, e.g., *In re MONY Group Inc. S'holder Litig.*, 852 A.2d 9, 23-24 (Del. Ch. 2004); *In re Pennaco Energy, Inc. S'holders Litig.*, 787 A.2d 691, 705-07 (Del. Ch. 2001); *Kohls v. Duthie*, 765 A.2d 1274, 1285 (Del. Ch. 2000); *Goodwin v. Live Entm't, Inc.*, No. Civ.A. 15765, 1999 WL 64265, at *23 (Del. Ch. Jan. 25, 1999); *Matador Capital Mgmt. Corp. v. BRC Holdings, Inc.*, 729 A.2d 280, 291 (Del. Ch. 1998); *In re MCA, Inc. S'holders Litig.*, 598 A.2d 687, 693 (Del. Ch. 1991); *In re Vitalink Commc'ns Corp. S'holders Litig.*, Civ. A. No. 12085, 1991 WL 238816, at *7 (Del. Ch. Nov. 8, 1991); *Roberts v. Gen. Instrument Corp.*, Civ. A. No. 11639, 1990 WL 118356, at *8-9 (Del. Ch. Aug. 13, 1990); *Braunschweiger v. Am. Home Shield Corp.*, Civ. A. No. 10755, 1989 WL 128571, at *6-7 (Del. Ch. Oct. 26, 1989); *In re KDI Corp. S'holders Litig.*, Civ. A. No. 10,278, 1988 WL 116448, at *5-7 (Del. Ch. Nov. 1, 1988); *In re Fort Howard Corp. S'holders Litig.*, Civ. A. No. 9991, 1988 WL 83147, at *12-13 (Del. Ch. Aug. 8, 1988).

stockholders of a target company or a scorned third party bidder who raise challenges to the market check in a motion seeking to enjoin an impending merger. The courts thus view these cases from the position of a Monday morning sports commentator, attempting to determine whether the board's actions were reasonable, not perfect, in light of the circumstances at the time of the decision.⁸⁸ In the words of Vice Chancellor Strine of the Delaware Court of Chancery, "[T]his reasonableness review is more searching than rationality review, and there is less tolerance for slack by the directors."⁸⁹ As a result, the trend in Delaware jurisprudence is to consider the sale process as a whole. The courts consider a variety of factors to determine whether the sale process used resulted in a transaction that maximizes stockholder value. Among these factors are the target's pre-signing market position;⁹⁰ whether the special committee, if one was formed, was truly independent and how the special committee conducted the sale process;⁹¹ whether a truly independent financial advisor was engaged;⁹² and whether the stockholders were fully informed of the sale process.⁹³

The emphasis on this myriad of factors appears to have shifted the Delaware courts' attention away from taking affirmative steps to promote the maximization of stockholder value. As mentioned previously, Delaware jurisprudence over

⁸⁸ See *Paramount Commc'ns, Inc. v. QVC Network, Inc.*, 637 A.2d 34, 45 (Del. 1994) ("[C]ourt[s] applying enhanced judicial scrutiny should be deciding whether the directors made a reasonable decision, not a perfect decision. If a board selected one of several reasonable alternatives, a court should not second-guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the board's determination." (emphasis omitted)); *In re Lear*, 926 A.2d at 118 ("Reasonableness, not perfection, measured in business terms relevant to value creation, rather than by what creates the most sterile smell, is the metric.").

⁸⁹ *In re Netsmart*, 924 A.2d at 192.

⁹⁰ See, e.g., *In re Lear*, 926 A.2d at 118-19 (considering investments made in the company and elimination of poison pill as indications to the market that the company was for sale); *In re Pennaco*, 787 A.2d at 705 (considering the target's position in the market for corporate control, including whether strategic buyers had expressed interest in the company).

⁹¹ See, e.g., *In re Fort Howard*, 1988 WL 83147, at *12 (examining special committee's actions).

⁹² See, e.g., *In re Toys "R" Us, Inc. S'holder Litig.*, 877 A.2d 975, 1006 n.46 (Del. Ch. 2005) (commenting on fees that the investment bank stood to gain if the target chose to go with a particular transaction and stating that "[i]n general . . . it is advisable that investment banks representing sellers not create the appearance that they desire buy-side work").

⁹³ See, e.g., *In re Lear*, 926 A.2d at 110-14 (evaluating whether the extent of stockholder disclosure met fiduciary requirements); *In re Topps Co. S'holders Litig.*, 926 A.2d 58, 91-92 (Del. Ch. 2007) (scrutinizing stockholder disclosure).

the past twenty years reveals that as long as the deal protection devices do not effectively lock up the transaction, the Delaware courts will bless whatever sale method is used. A detailed description of significant market check cases follows to clearly demonstrate the direction of Delaware Court of Chancery jurisprudence regarding stockholder value maximization over the past two decades.

1. *In re Fort Howard Corp. Shareholders Litigation*

In 1988, two years after the Delaware Supreme Court's decision in *Revlon*, the Court of Chancery first addressed the validity of a post-signing market check in *In re Fort Howard Corp. Shareholders Litigation*.⁹⁴ In that case, Fort Howard's board, fearing that the company may be vulnerable to a takeover attempt while its stock was temporarily depressed, sought advice from its financial advisor, Morgan Stanley, regarding steps the company could take to protect its stockholders.⁹⁵ Over the course of several meetings, Morgan Stanley and Fort Howard determined that an LBO of the company involving Morgan Stanley acting as a principal and Fort Howard's senior management also participating would create a greater value than other alternatives.⁹⁶ After

⁹⁴ *In re Fort Howard*, 1988 WL 83147, at *1. Some commentators cite to a preceding case, *Yanow v. Scientific Leasing, Inc.*, 1988 WL 8772 (Del. Ch. Feb. 8, 1988), as having first addressed the validity of a post-signing market check. Although the merger agreement in that case contained a window shop provision and the target company only seriously negotiated with one bidder prior to signing the agreement, the plaintiffs did not specifically challenge the target's reliance on a post-signing market check but rather challenged the validity of the pre-signing auction process. *Yanow*, 1988 WL 8772, at *3-4. In particular, the plaintiffs challenged the target's decision to only negotiate with one bidder without having first conducted an auction or, at least, having discreetly contacted third parties that had previously expressed an interest in the target. *Id.* at *4. In addition, then-Vice Chancellor Jacobs also focused on the pre-signing market canvass in finding that although it was not clear that the market was fully informed that the target was for sale, the "undisputed evidence [was] that for the last two years, the relevant 'players' in the industry were aware that [the target] was willing to (and, indeed, had) entertained acquisition proposals." *Id.* at *6.

⁹⁵ *In re Fort Howard*, 1988 WL 83147, at *2.

⁹⁶ *Id.* During the initial meeting on March 30, 1988, Fort Howard's CEO asked about a wide range of transactions, including recapitalizations, spin-offs, acquisitions and other transactions. *Id.* Morgan Stanley described the structure and mechanics of different types of recapitalizations and then mentioned that an LBO of the company with Morgan Stanley acting as a principal was also an alternative. *Id.* On May 3, Fort Howard management requested Morgan Stanley to evaluate the company's possible alternatives and, three weeks later, Morgan Stanley presented a written report at a meeting with management. *Id.* During this meeting, Morgan Stanley indicated that in its opinion an LBO of the company would result in the greatest

management presented the LBO proposal to the board, the board formed a special committee that initially elected to keep the buyout proposal confidential, although the company later issued press releases regarding the negotiations.⁹⁷ The special committee retained an independent financial advisor, who advised that if the board accepted an LBO proposal, the proposal should provide for a market test to determine whether a third party could make a better offer.⁹⁸

Ultimately, Fort Howard and the Morgan Stanley group entered into a merger agreement that included a no shop provision allowing Fort Howard to receive third party proposals but prevented management from actively soliciting alternative offers.⁹⁹ The agreement also included a topping fee and expense reimbursement provision capped at \$67 million, which represented 1.9% of the equity value of the transaction.¹⁰⁰ Pursuant to the terms of the agreement, the tender offer would be publicly known for thirty business days, or forty-three calendar days.¹⁰¹ Thus, the agreement essentially provided for a forty-three day market check period, which came to be standard in transactions following *Fort Howard*.

Upon execution of the merger agreement, Fort Howard issued a press release that announced the transaction and specifically stated that management was available to receive

stockholder value and again stated that Morgan Stanley would be interested in participating in such a transaction with Fort Howard's senior management. *Id.*

⁹⁷ *Id.* at *3-5. On June 22, 1988, after the company received a telephone inquiry regarding a rumor that there was a buyout being negotiated, Fort Howard issued a press release stating that "members of [Fort Howard's] management intend to seek a proposal with third parties to acquire the Company in a leveraged buyout." *Id.* at *5 (internal quotation marks omitted). On June 24, the company issued another press release stating that it was engaged in negotiations with a group consisting of members of its senior management and an affiliate of Morgan Stanley for an LBO, but that there was no assurance that the transaction would come to fruition. *Id.* at *6-7.

⁹⁸ *Id.* at *4-5. After receiving Morgan Stanley's initial draft merger agreement that included a proposal to purchase all of the outstanding company shares for \$50 per share and provided for a broad prohibition against shopping the company, the special committee demanded a market test and indicated that it would not go forward with the LBO unless there was time to test the market and there were fewer restrictions on its ability to do so. *Id.* at *5-6. Among the other provisions in the initial draft that the Special Committee rejected were provisions allowing for unspecified break-up fees, unlimited expense reimbursement, and "a provision acknowledging Morgan Stanley's right to commence and complete any tender offer with[in] twenty days from the announcement of its [definitive] agreement." *Id.* at *5.

⁹⁹ *Id.* at *7.

¹⁰⁰ *Id.*; see also Morton & Houtman, *supra* note 27, at 2 (explaining the Fort Howard deal's protection provisions).

¹⁰¹ *In re Fort Howard*, 1988 WL 83147, at *6.

inquiries from interested parties.¹⁰² Following the press release, the company received eight inquiries from third parties, but only two of the eight pursued the transaction further, including a competitor of Fort Howard that ended up being the only third party to seriously pursue a transaction with Fort Howard.¹⁰³ When the competitor requested additional information beyond the information provided to the other potential bidders, the special committee expressed concerns that the competitor would face significant antitrust problems and possibly financing problems in acquiring Fort Howard.¹⁰⁴ As a result of these alleged concerns, the confidentiality/standstill¹⁰⁵ agreement that the committee sought to have the competitor execute contained several provisions that did not exist in the Morgan Stanley confidentiality agreement. These provisions included a fee of \$67.8 million that the competitor would have to pay if, after being provided with the additional confidential information, the competitor did not make a bid, Morgan Stanley's tender offer did not close, and another bidder did not appear.¹⁰⁶

Fort Howard stockholders challenged the deal, arguing, *inter alia*, that the independent committee had engaged in a course of conduct that would never effectively allow it to shop

¹⁰² *Id.* at *7. In particular, the press release provided:

Notwithstanding its recommendation, and consistent with the terms of the merger agreement, the Special Committee directed the Company's management and the First Boston Corporation to be available to receive inquiries from any other parties interested in the possible acquisition of the Company and, as appropriate, to provide information and, in First Boston's case in conjunction with the Special Committee, enter into discussions and negotiations with such parties in connection with any such indicated interest.

Id. Following the press release, the Fort Howard transaction was prominently featured in the business section of several publications, including the *New York Times*, *Wall Street Journal*, and *Los Angeles Times*. *Id.* at *8.

¹⁰³ *Id.* at *8. The Special Committee instructed its financial advisor to screen the proposed bidders to determine if they were capable of completing a transaction of this size. *Id.* After it was determined that all eight bidders could be considered serious contenders, each received additional materials that had previously been provided to Morgan Stanley. *Id.*

¹⁰⁴ *Id.*

¹⁰⁵ A standstill provision in a confidentiality agreement "prevents a subsequent bidder who enters from becoming hostile to the target. The subsequent bidder will typically be restricted from making a public tender offer and will, rather, join a process in which the target's board is not only included, but will ultimately choose its merger partner." Block, *supra* note 23, at 93.

¹⁰⁶ *Id.* at *9. During later negotiations, the special committee removed the \$67.8 million fee and offered another alternative that required the competitor to submit a bid by August 5. *Id.*

the company and that the market check period was really a sham, pointing to the confidentiality/standstill agreement as proof that the special committee favored the management-affiliated transaction.¹⁰⁷ In denying the plaintiffs' request for a preliminary injunction, then-Chancellor Allen noted that there may be grounds for suspicion regarding the special committee's good faith, but under the totality of the circumstances, there was not enough to find the shareholders' argument persuasive.¹⁰⁸ Instead, Chancellor Allen focused on whether the special committee's post-signing market check was a mere formality or whether it actually checked the market for superior offers. The Chancellor blessed the post-signing market check, finding that it "was reasonably calculated to (and did) effectively probe the market for alternative possible transactions" because it was not overly burdened by lock-ups, termination fees, topping fees, time, or administrative complications "to permit the inference that [the] alternative was a sham designed from the outset to be ineffective or minimally effective."¹⁰⁹ The court focused on the company's press release, the fact that a number of potential bidders quickly expressed interest, and the company's prompt provision of information to bidders.¹¹⁰

Following its seminal decision in *Fort Howard*, the Court of Chancery continued to consider the effectiveness of post-signing market checks in a number of cases.¹¹¹ The post-signing market checks of the late 1980s and early 1990s were modeled after the *Fort Howard* market check and came to be

¹⁰⁷ See *id.* at *10.

¹⁰⁸ *Id.* at *12. Among other things, Chancellor Allen looked with suspicion on the fact that the CEO, in effect, chose the members of the special committee and the special counsel for the committee. *Id.*

¹⁰⁹ *Id.* at *13. It is interesting to note, however, that Chancellor Allen found the special committee's initial decision to keep the management's buyout proposal secret to be suspicious, describing it as "a decision to sell the Company to management if it would pay a fair price, but not to inquire whether another would pay a fair price if management would not do so." *Id.* at *12. Chancellor Allen explained that this decision implied a bias on the part of the special committee. *Id.*

¹¹⁰ *Id.* at *13.

¹¹¹ See, e.g., *Kohls v. Duthie*, 765 A.2d 1274, 1285 (Del. Ch. 2000); *Goodwin v. Live Entm't, Inc.*, No. Civ.A. 15765, 1999 WL 64265, at *23 (Del. Ch. Jan. 25, 1999); *Matador Capital Mgmt. Corp. v. BRC Holdings, Inc.*, 729 A.2d 280, 291 (Del. Ch. 1998); *In re Vitalink Commc'ns Corp. S'holders Litig.*, Civ. A. No. 12085, 1991 WL 238816, at *7 (Del. Ch. Nov. 8, 1991); *Roberts v. Gen. Instrument Corp.*, Civ. A. No. 11639, 1990 WL 118356, at *8-9 (Del. Ch. Aug. 13, 1990); *Braunschweiger v. Am. Home Shield Corp.*, Civ.A. No. 10755, 1989 WL 128571, at *6-7 (Del. Ch. Oct. 26, 1989); *In re KDI Corp. S'holders Litig.*, Civ. A. No. 10,278, 1988 WL 116448, at *5 (Del. Ch. Nov. 1, 1988).

characterized by termination fees ranging from 1.9% to 3.83%¹¹² and, often times, press releases announcing, or at least implying, that the company was open to receiving inquiries from other bidders.¹¹³ In addition, in these transactions, matching rights were not necessarily always provided to the initial acquirer.¹¹⁴ There appears to have been a seven-year gap during which the Court of Chancery was not presented with a case involving post-signing market checks but the court began to address them again in 1998.

2. *In re Pennaco Energy, Inc.*

More recently, in 2001, the Court of Chancery again visited post-signing market checks in *In re Pennaco Energy, Inc.*¹¹⁵ In that case, Pennaco Energy's stockholders challenged the board's decision to not actively shop the company and to

¹¹² See, e.g., *Kohls*, 765 A.2d at 1285 (refusing to enjoin a deal with a termination fee of 2.25% of the equity value of the transaction); see also *Kenetech Corp., Agreement and Plan of Merger* (Form 8-K, exhibit 2), at 1, 14, 44 (Oct. 26, 2000) (filing Merger Agreement, dated October 25, 2000, containing capitalization representation stating that 31,970,164 shares of common stock were issued and outstanding, merger consideration of \$1.04 per share and termination fee of \$750,000); *Goodwin*, 1999 WL 64265, at *20 (refusing to enjoin a deal with a termination fee equal to 3.125% of the merger value plus \$1 million in expenses for a total percentage of 4.16%); *Matador Capital Mgmt.*, 720 A.2d at 291 (refusing to enjoin a deal with a termination fee of approximately 3.83% of the equity value of the transaction); *In re Vitalink*, 1991 WL 238816, at *7 (finding that a termination fee equal to 1.9% of the equity value of the transaction did not prevent a market canvass); *Roberts*, 1990 WL 118356, at *9 (refusing to enjoin a deal with a termination fee equal to 2% of the equity value of the transaction); *Braunschweiger*, 1989 WL 128571, at *7 (refusing to enjoin a deal with a termination fee equal to \$0.25 per share, or 1.9% of the equity value of the transaction).

¹¹³ Compare *Kenetech Corp.*, Press Release (Form 8-K, exhibit 99.1), at 1 (Oct. 26, 2000) (explicitly stating that Kenetech's financial advisor was available to receive unsolicited inquiries), and *In re KDI*, 1988 WL 116448, at *4 (summarizing a press release stating that the target's special committee and its financial advisor would continue to be available to receive inquiries and would negotiate with third parties), with *Roberts*, 1990 WL 118356, at *6 (quoting a press release stating that the incumbent bidder would be paid a termination fee if the target receives an unsolicited offer and accepts the offer in accordance with the board's fiduciary duties), and *Braunschweiger*, 1989 WL 128571, at *9 n.13 (quoting a press release stating that the incumbent bidder would be paid a termination fee if the target's board withdraws its stockholder recommendation and accepts another offer in accordance with its fiduciary duties). But see *BRC Holdings Inc.*, Press Release (Form SC 14D1, exhibit 9), at 1 (Oct. 23, 1998) (filing a press release containing no indication, either explicit or implicit, that the company was willing to entertain offers from third parties). The BRC Holdings transaction became the subject of the litigation in *Matador Capital Management*, 729 A.2d at 291.

¹¹⁴ See, e.g., *In re MCA, Inc. S'holders Litig.*, 598 A.2d 687, 693 (Del. Ch. 1991) (no matching rights); *In re Vitalink*, 1991 WL238816, at *7, 10 (same); *In re KDI*, 1988 WL 116448, at *3 (same).

¹¹⁵ 787 A.2d 691, 705-07 (Del. Ch. 2001).

rely exclusively on a post-agreement market check.¹¹⁶ Unlike *Fort Howard*, Pennaco concerned a strategic transaction—not an LBO. In November 2000, Pennaco and a subsidiary of Marathon Oil entered into a confidentiality agreement after Marathon expressed an interest in acquiring Pennaco.¹¹⁷ After entering into the confidentiality agreement, Pennaco’s board focused solely on Marathon and did not attempt to canvass the market even though the confidentiality agreement did not prohibit Pennaco from doing so.¹¹⁸ A little over a month after entering into the confidentiality agreement, the parties executed a merger agreement.¹¹⁹ The merger agreement included a relatively non-restrictive no shop provision that allowed Pennaco to speak with and provide information to any third party who could reasonably “be expected to make a superior offer that could be consummated without undue delay.”¹²⁰ In addition, Marathon was granted matching rights that allowed Marathon a three-day period during which it could match a superior proposal.¹²¹ The agreement also contained a termination fee equal to 3% of Pennaco’s equity

¹¹⁶ *Id.* at 692.

¹¹⁷ *Id.* at 698.

¹¹⁸ *Id.* at 699. Pennaco also did not hire an investment bank to canvass the market for it. *Id.* However, Pennaco’s management identified investment bankers for possible retention should a transaction arise with Marathon or another party, and Pennaco received pitch books from two of the banks that it contacted, including Credit Suisse First Boston (“CSFB”). *Id.* CSFB provided Pennaco with preliminary valuation analyses and indicated a range in value for Pennaco between \$17.88 and \$20.81 per share. *Id.*

¹¹⁹ *Id.* at 702. After completing three weeks of due diligence, Marathon submitted its initial bid of \$17 per share. *Id.* at 700. The Pennaco board determined that Marathon’s bid was too low, given CSFB’s preliminary valuation, and instructed Pennaco’s CEO to reject the \$17 offer and “to seek a price ‘north of \$20 a share.’” *Id.* A week after its initial offer, Marathon increased its bid to \$19 per share. *Id.* at 701. The board again met and instructed the CEO “to see if there was ‘any more room above the \$19 a share.’” *Id.* At that meeting, the board also hired Lehman Brothers as its investment bank. *Id.* After Marathon indicated that \$19 a share was its absolute best and final offer, the board authorized Lehman to begin working on a fairness opinion and discussed its fiduciary duties and possibilities for a post-agreement market check with its outside counsel. *Id.* Lehman gave an oral presentation to the board regarding its fairness opinion, during which it presented net asset valuations based on three different “base cases,” the most aggressive of which produced a range of value of \$15.14 to \$18.89 per share. *Id.* at 702 (internal quotation marks omitted). Following its presentation, Lehman gave an oral opinion that Marathon’s \$19 per share offer was fair and the board then formally approved a sale of Pennaco to Marathon at \$19 per share. *Id.*

¹²⁰ *Id.*

¹²¹ See Pennaco Energy, Inc., Agreement and Plan of Merger (Form 8-K, exhibit 2.1), at 38-39 (Dec. 27, 2000), (filing Agreement and Plan of Merger, dated as of December 22, 2000, that included a three-business-day matching rights period in Section 8.01(d)).

value and slightly less than 3% of the value of its combined debt and equity as measured by the transaction value.¹²² Furthermore, in order to allow sufficient time for third parties to review the transaction and make competing offers, the Pennaco board obtained an agreement from Marathon that it would not commence its tender offer until the second week of January 2001.¹²³

In addressing the Pennaco stockholders' challenges that the Pennaco board breached their *Revlon* duties by solely negotiating with Marathon and by relying on a post-agreement market check with a termination fee, Vice Chancellor Strine first noted that "one would not commend the Pennaco board's actions as a business school model of value maximization" before finding that the board's actions were reasonable.¹²⁴ Strine validated the board's single bidder strategy because the board ensured that a post-agreement market check would occur and because the termination fee and matching rights did not act as substantial barriers to third parties.¹²⁵ Although he found the board's actions to be reasonable, it is noteworthy that Vice Chancellor Strine indicated that had the board agreed to more onerous deal protection devices that prevented competing bids from emerging, his decision would likely have been different.¹²⁶

3. *In re MONY Group Inc. Shareholder Litigation*

Three years after its decision in *Pennaco*, the Delaware Court of Chancery again addressed the necessity of a pre-signing auction and the adequacy of a post-signing market check in *In re MONY Group Inc. Shareholder Litigation*.¹²⁷ Like *Pennaco*, *MONY* also did not involve an LBO but rather a

¹²² *In re Pennaco*, 787 A.2d at 702, 702 n.16.

¹²³ *Id.* at 703.

¹²⁴ *Id.* at 705. In reaching the conclusion that the board's actions were not unreasonable, Strine relied on numerous factors, including: (1) Pennaco's market posture, including that the company was a "source of industry interest"; (2) Pennaco's recent search for a joint venture partner that had "brought the company to the attention of twenty to thirty industry players"; (3) the company's "reincorporation into Delaware to facilitate its participation in the mergers and acquisitions market"; and (4) the board members' expertise and experience in the industry. *Id.* at 705-06.

¹²⁵ *Id.* at 707 (holding that the fact that no higher bids emerged "is itself evidence that the directors, in fact, obtained the highest and best transaction reasonably available" (quoting *Matador Capital Mgmt. Corp. v. BRC Holdings, Inc.*, 729 A.2d 280, 293 (Del. Ch. 1998)).

¹²⁶ *Id.* at 707.

¹²⁷ 852 A.2d 9, 20-21, 23-24 (Del. Ch. 2004).

strategic transaction. In *MONY*, MONY Group Inc. stockholders challenged the proposed stock-for-cash merger of MONY and a wholly-owned subsidiary of AXA Financial, Inc.¹²⁸ After MONY posted losses in 2001 and 2002, the company's board of directors authorized its CEO, Michael I. Roth, to explore strategic opportunities but rejected the idea of a public auction of the company.¹²⁹ Approximately ten months after Roth first met with AXA, MONY and AXA announced they had signed a merger agreement pursuant to which MONY stockholders would receive \$31 cash for each share of MONY stock.¹³⁰ The merger agreement contained a window shop provision which prohibited MONY from *actively* soliciting offers during the five-month market check period but allowed the board to pursue proposals that were, or were reasonably likely to constitute, a more favorable business combination to stockholders and that was reasonably capable of being completed on the proposed terms.¹³¹ In addition, AXA was granted a five-day period during which it could match a superior proposal.¹³² The merger agreement also contained a termination fee of \$50 million, which represented 3.3% of MONY's total equity value and 2.4% of the total transaction value.¹³³ The MONY stockholders challenged the board's decision to forego a pre-signing auction or solicitation process and also challenged the adequacy of the post-signing market check.¹³⁴

In finding that the board's decision not to pursue a pre-agreement auction was reasonable, Vice Chancellor Lamb stated that "[s]ingle-bidder approaches offer the benefits of protecting against the risk that an auction will be a failed one, and avoiding a premature disclosure to the detriment of the

¹²⁸ *Id.* at 14-15.

¹²⁹ *Id.* at 16. In November 2002, the board met with its financial advisor, CSFB, to discuss MONY's financial issues. *Id.* CSFB's report to the board suggested twelve potential partners and acquirers for MONY, including AXA Financial. *Id.*

¹³⁰ *Id.* at 18. This price represented a 7.3% premium over MONY's then-current trading price of \$28.89. *Id.*

¹³¹ *Id.* at 23 n.31.

¹³² See The MONY Group Inc., Agreement and Plan of Merger (Form 8-K, exhibit 2.1), § 9.1(h), at 59-60 (Sept. 18, 2003) (filing Agreement and Plan of Merger, dated as of September 17, 2003, that included a five-business-day matching rights period).

¹³³ *In re MONY*, 852 A.2d at 18.

¹³⁴ *Id.* at 20, 23.

company's then-ongoing business."¹³⁵ In addition, the court held that the five-month period between the merger agreement signing and the date on which the MONY stockholders brought suit was more than adequate for a competing bidder to emerge and complete due diligence.¹³⁶

Although the Court of Chancery continued to scrutinize the board's activities in light of the totality of the circumstances, there were a number of facts that differentiated the more recent market checks validated in *Pennaco* and *MONY* from the first market check that the court upheld in *Fort Howard*.¹³⁷ Unlike *Fort Howard*, neither *Pennaco* nor *MONY* issued a press release explicitly stating that the target's management was available to field third party inquiries.¹³⁸ In addition, some practitioners have noted that the termination fees upheld in both *Pennaco* and *MONY* were not only higher than the *Fort Howard* termination fee but were also significantly higher than termination fees contained in other deals involving post-signing market checks in the absence of a market canvass.¹³⁹ Finally, unlike in *Fort Howard*, the initial bidders in both *Pennaco* and *MONY* received matching rights in the event of a superior third party proposal.¹⁴⁰ A practitioner

¹³⁵ *Id.* at 21. Vice Chancellor Lamb indicated that the MONY board considered several factors in deciding not to engage in an active solicitation process. *Id.* These factors included (1) the previous attempt by another company engaged in the same industry whose business and stock market performance suffered after undergoing a public auction; (2) the risk that MONY's employees would seek alternative employment; (3) the risk that competitors would gain a competitive advantage after performing due diligence on MONY and would seek to employ MONY's career agency force; and (4) the knowledge that a post-agreement market check was a possibility. *Id.*

¹³⁶ *Id.* at 23-24.

¹³⁷ See *Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1286 (Del. 1989) (stating that a board's actions "must be evaluated in light of relevant circumstances to determine if they were undertaken with due diligence and in good faith").

¹³⁸ Compare text at *supra* note 102 (quoting a *Fort Howard* press release that explicitly stated that management was available to field unsolicited third party offers) with *Pennaco Energy, Inc.*, Current Report (Form 8-K) (Dec. 27, 2000) (press release that does not mention management's availability to field unsolicited third party offers, nor does the press release mention the inclusion of a window shop provision in the merger agreement), and *The MONY Group Inc.*, Current Report (Form 8-K) (Sept. 18, 2003) (same).

¹³⁹ See *Morton & Houtman*, *supra* note 27, at 3-4 (noting that the *Pennaco* fee of 3% and the *MONY* fee of 3.3% were higher than the *Fort Howard* fee of 1.9% and were much higher than similar situations in the past involving a sale of control to a single bidder without a pre-signing market canvass).

¹⁴⁰ See *The MONY Group Inc.*, Current Report (Form 8-K), at 59-60 (Sept. 18, 2003) (filing Agreement and Plan of Merger, dated as of September 17, 2003, that included a five-business-day matching rights period in Section 9.1(h)); *Pennaco Energy, Inc.*, Current Report (Form 8-K), at 38-39 (Dec. 27, 2000) (filing Agreement and Plan of

at one Delaware law firm theorized that the differences between *Pennaco*, *MONY* and *Fort Howard* are a result of *Pennaco* and *MONY* involving strategic buyers while *Fort Howard* involved an MBO.¹⁴¹ In any event, some commentators believe that this liberalization of market checks paved the way for the recent prevalence of the go-shop provision.¹⁴²

D. 2004-2007: *The Development of the Go-Shop*

Until recently, the window shop provision was the medium of choice for boards seeking to ensure the maximization of stockholder value in the absence of a public auction or targeted market canvass. Dealmakers rarely used go-shop provisions, and when they chose to use them it was generally only under special circumstances.¹⁴³ Richard E. Spatt, a partner at Simpson Thacher & Bartlett LLP, has indicated that these “special circumstances” include situations “where an insider or fiduciary/board member is the buyer” or where the price terms of a deal have been renegotiated downward.¹⁴⁴

The Delaware Court of Chancery first addressed go-shops in its 1989 opinion, *In re Formica Corp. Shareholders Litigation*.¹⁴⁵ The go-shop provision in that case arose during the MBO of Formica Corp. and permitted the unlimited solicitation and negotiation of competing acquisition proposals during the thirty business day, or forty-seven calendar day, period that the tender offer was open.¹⁴⁶ The deal, entered into after a very limited market canvass, included a \$5 million termination fee representing approximately 2.14% of the equity value of the transaction and a provision capping expense

Merger, dated as of December 22, 2000, that included a three-business-day matching rights period in Section 8.01(d)).

¹⁴¹ See Michael K. Reilly, *The Post-Agreement Market Check Revisited* (Mar. 2004), available at <http://www.potteranderson.com/news-publications-40-45.html> (arguing that differences between the three cases are a result of *Pennaco* and *MONY* involving a strategic third party who may not be as familiar with the target and as a result incurring higher sunk costs).

¹⁴² See Morton & Houtman, *supra* note 27, at 5 (stating that following *Pennaco* and *MONY* post-signing market checks “began fading into the background and a new approach—the go-shop provision—started to take hold”); see also Spatt, *supra* note 13, at 33 (stating that go-shops are natural extensions of no shops).

¹⁴³ See Spatt, *supra* note 13, at 33-40 (describing the rise of the go-shop provision).

¹⁴⁴ *Id.*

¹⁴⁵ CIV.A. No. 10598, 1989 WL 25812 (Del. Ch. Mar. 22, 1989).

¹⁴⁶ *Id.* at *8.

reimbursement at \$5.5 million.¹⁴⁷ The press release announcing the transaction explicitly stated that Formica's financial advisor had been instructed to "actively solicit competing bids."¹⁴⁸

The stockholders challenged the post-signing market test as being incapable of resulting in a meaningful auction, arguing that the length of the market test period was an insufficient time for incoming bidders to arrange complex foreign financing.¹⁴⁹ However, then-Vice Chancellor Jacobs rejected this argument for several reasons. First, Jacobs noted that bidders do not require foreign financing unless they need debt financing and, even then, bidders could make their bids subject to securing financing and temporarily finance the acquisition using a bridge loan.¹⁵⁰ Second, Jacobs stated that there was "no evidence that any potential bidder . . . complained that the . . . period [was] too truncated to enable a bid to be made."¹⁵¹ Finally, Vice Chancellor Jacobs compared the go-shop provision to the no shop provision in *Fort Howard* and found the facts of *Formica* to be "more compelling" because the target could actively solicit potential bidders, the target's financial advisor had contacted 125 potential bidders and was engaged in discussions with four of them, and "the market test period [was] one week longer than the one employed in *Fort Howard*."¹⁵²

Following *Formica* in 1989, only a handful of deals over the subsequent decade and a half contained go-shops.¹⁵³ This

¹⁴⁷ *In re Formica Corp. S'holders Litig.*, 1989 WL 25812, at *3-4, *8 (describing the exploratory discussions and the terms of the final merger agreement). The special committee considered holding an auction but rejected the idea, fearing that it may not end up with any bids. *Id.* at *6.

¹⁴⁸ *Id.* at *7.

¹⁴⁹ *Id.* at *12.

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² *Id.* The tender offers in *Formica* and *Fort Howard* both remained open for thirty business days although the *Formica* tender offer was open for four calendar days longer than the *Fort Howard* tender offer. Compare *In re Fort Howard S'holders Litig.*, Civ. A. No. 9991, 1988 WL 83147, at *6 (Del. Ch. Aug. 8, 1988) (stating that the tender offer would remain open for thirty business days or forty-three calendar days) with *In re Formica*, 1989 WL 25812, at *8, *12 (stating that the tender offer would remain open for thirty business days or forty-seven calendar days and such time constituted the market check period).

¹⁵³ See, e.g., Spatt, *supra* note 13, at 33 (indicating that the 1991 acquisition by non-executive chairman of National Gypsum included a go-shop provision); Kemper Corp., Current Report (Form 8-K), at 2-3 (July 1, 1994) (summarizing a merger agreement allowing for a ten-day go-shop period with a bifurcated termination fee pursuant to which Kemper could terminate the agreement in favor of a third party).

scarce use of go-shops is likely a product of the collapse of the high-yield bond market and the resulting substantial decline in LBOs in 1989 and 1990.¹⁵⁴ Then, beginning in 2004, dealmakers began including go-shops in a rising number of deals.¹⁵⁵ During 2006, dealmakers included go-shops in at least fifteen deals.¹⁵⁶

This sudden increased use of go-shops may lead one to ask: what has changed that dealmakers are turning to go-shops? The answer to this question is likely the result of a combination of factors. As discussed in Part I, over the past three years, there has been a resurgence in the number of private equity firms entering the playing field.¹⁵⁷ In contrast to transactions with strategic players, private equity firms often bring different considerations to the negotiating table. Private equity firms frequently deal with targets that have not necessarily considered themselves as being for sale.¹⁵⁸ Private equity firms, like other buyers, prefer having private negotiations with the target company and thus often avoid competitive auctions, which frequently result in increasing the purchase price of the target.¹⁵⁹ Accordingly, a private equity firm may make its proposal contingent on the target not shopping the deal prior to entering into a definitive agreement.¹⁶⁰ However, in return for abstaining from shopping

¹⁵⁴ See Steven N. Kaplan, *The Evolution of U.S. Corporate Governance: We Are All Henry Kravis Now*, J. PRIVATE EQUITY, Fall 1997, at 7, available at <http://faculty.chicagogsb.edu/steven.kaplan/research/govern.pdf> (discussing the decline of LBOs and the reasons for the decrease).

¹⁵⁵ See, e.g., The Chalone Wine Group, Ltd., Current Report (Form 8-K) (Nov. 1, 2004) (filing merger agreement with a go-shop provision and press release announcing Chalone may continue to solicit bids); Hollywood Entertainment Corp., Current Report (Form 8-K) (Oct. 14, 2004) (filing amended merger agreement with go-shop provision and press release announcing that according to amended merger agreement that included a renegotiated price, Hollywood Entertainment was permitted to entertain competing proposals); US Oncology, Inc., Current Report (Form 8-K) (Mar. 22, 2004) (filing merger agreement with a go-shop provision and press release announcing that US Oncology may continue to solicit competing bids).

¹⁵⁶ See Morton & Houtman, *supra* note 27, at app. 7-18 (listing transactions that included go-shop provisions in their agreements).

¹⁵⁷ See *supra* Part. I (discussing increase in private equity deals).

¹⁵⁸ See Peters et al., *supra* note 69 (“[A] target board may be faced with a situation in which, although it has no intention to sell, it is approached by an unsolicited bidder who makes an offer that the board is compelled to consider.”).

¹⁵⁹ See Thomas J. Dougherty, *Takeovers*, in ALI-ABA COURSE OF STUDY: SECURITIES LITIGATION: PLANNING AND STRATEGY 327, 330 (2007) (“[O]nce p-e [private equity] players commit to a potential deal, they would rather proceed from a bear hug offer that dazzles management through to deal closure with as little competitive bidding as possible.”).

¹⁶⁰ See, e.g., *In re Lear Corp. S’holder Litig.*, 926 A.2d 94, 104 (Del. Ch. 2007) (recognizing that the private equity buyer indicated that it would pull its bid if a “full-blown auction” were conducted).

the deal pre-signing—and in recognition that the target board has an obligation to fulfill its *Revlon* duties—private equity firms will agree to go-shop provisions.¹⁶¹ Because the private equity firm has secured its place as the initial acquirer it is able to benefit from the other deal protection devices that the agreement often contains, including termination fees and matching rights. Furthermore, although the target is, in effect, conducting an auction post-signing, go-shop periods are not generally as long as public auctions.¹⁶² Therefore, the initial acquirer is able to avoid a pre-signing bidding war, secure an agreement and then the target is put on the auction block for a more limited period.

In addition to the private equity buyers' avoidance of public auctions, the target board may harbor concerns that a public auction or pre-signing market canvass will not be effective in inducing bids when a private equity firm has already made a proposal. Boards may fear that third parties will be hesitant to compete with a buyout group that includes target insiders, or that management may not cooperate with a public auction because it is already aligned with the private equity buyer.¹⁶³ Furthermore, boards also may be concerned about the market for corporate control's perception that the

¹⁶¹ See Michael Weisser & Michael Cubell, *Go-Shops: Are Sponsors Giving Away the Store?*, PRIVATE EQUITY ALERT (Weil, Gotshal & Manges LLP), Dec. 2006, at 1, 3-4, [http://www.weil.com/wgm/cwgmhomep.nsf/Files/PEADec06/\\$file/PEADec06.pdf](http://www.weil.com/wgm/cwgmhomep.nsf/Files/PEADec06/$file/PEADec06.pdf) (describing reasons that private equity buyers agree to go-shop provisions).

¹⁶² See Mills & Harsch, *supra* note 12, at 45 (recognizing the time differences required for public auctions and typical go-shop periods).

¹⁶³ See Stephen I. Glover & Jonathan P. Goodman, *Go-Shops: Are They Here to Stay?*, M&A LAW., June 2007, at 1 (describing reasons boards may agree to go-shop provisions when a private equity firm has made a buyout proposal). This argument may have some weight, as Professor Guhan Subramanian, in an article summarizing an empirical study of go-shop provisions, states that:

The fact that no higher bidder has emerged in an MBO go-shop to date (after nearly two years of experience with go-shops, in a frenzied deal environment) suggests that third parties may be wary of entering a bidding contest, or that bankers might not conduct as thorough and energetic a search, when management has already picked its preferred buyout partner. A management team with difficult-to-acquire firm-specific skills and knowledge can use their inherent advantage to buy the company from the public shareholders at a lower price, by effectively committing to its favored buyout group and making clear its unwillingness to work with any other buyout group that might emerge during the go-shop process.

Guhan Subramanian, *Go-Shops v. No-Shops in Private Equity Deals: Evidence and Implications* (forthcoming BUS. LAWYER, May 2008).

board itself is favoring the private equity buyer.¹⁶⁴ In the opinion of the board, the inclusion of a go-shop provision in the final agreement helps to mitigate the perception that the board or management may be biased in favor of the private equity buyer.¹⁶⁵

In addition to the increased role that private equity firms are playing in the M&A world and the related issues that LBOs and MBOs raise, stockholder activism also has been on the rise.¹⁶⁶ Stockholders are increasingly willing to challenge deals that, in their opinion, do not maximize stockholder value.¹⁶⁷ Although stockholder suits overall have decreased in recent years, suits challenging deals involving private equity firms have doubled over the past three years.¹⁶⁸ As a result, boards are increasingly turning to go-shop provisions in an effort to show that they have and are continuing to fulfill their *Revlon* duties.¹⁶⁹

E. Typical Characteristics of Go-Shop Provisions

As mentioned previously, go-shops allow the target company to actively solicit other bidders post-signing for a limited period, generally ranging from fifteen to fifty days.¹⁷⁰ Agreements containing go-shop provisions also typically contain deal protection devices such as termination fees and matching rights. Termination fees are often bifurcated; that is,

¹⁶⁴ See Glover & Goodman, *supra* note 163.

¹⁶⁵ See *id.*

¹⁶⁶ See generally *Battling for Corporate America—Shareholder Democracy*, THE ECONOMIST, Mar. 11, 2006, at 63 (describing an environment of shareholder activism).

¹⁶⁷ Christopher Palmeri, *Saying No to an LBO*, BUS. WEEK, July 23, 2007, at 26.

¹⁶⁸ *Id.*; see also Wong, *Rival Bidders*, *supra* note 22 (stating that stockholders increasingly react with hostility toward private equity deals).

¹⁶⁹ See Dan Freed, *They've Shopped, But Haven't Dropped: First-Half M&A Sizzled, and the Second Half Is Already Off to a Fast Start. Is It Too Much of a Good Thing?*, INV. DEALERS' DIG., July 9, 2007 ("The emergence of the 'go shop' appears to be symptomatic of a larger concern among boards that they be seen as doing whatever they can on behalf of shareholders."); Glover & Goodman, *supra* note 163 ("Yet another factor explaining the rise of the go-shop is increased shareholder activism by institutional investors and hedge funds.")

¹⁷⁰ See Morton & Houtman, *supra* note 27 (providing a table listing transactions containing go-shop provisions, including details regarding the length of the go-shop periods). Typically, go-shop provisions do not limit who may be solicited during the go-shop period. Glover & Goodman, *supra* note 163. However, in a few deals targets have been limited to contacting a select group of strategic buyers or a limited number of bidders generally. *Id.*

a lower termination fee will apply during the go-shop period than following the go-shop period. The lower termination fee generally ranges from 40% to 60% of the base termination fee.¹⁷¹ Some deals have allowed the lower termination fee to apply only if the target terminated the original agreement “prior to the expiration of the go-shop period,” while other deals permit the lower termination fee to apply so long as the target company terminated the original agreement in favor of a superior proposal that was received during the go-shop period.¹⁷² Go-shop provisions are also often paired with matching rights, allowing the initial acquirer an opportunity to match any bids received as a result of a target’s solicitation during the go-shop period.¹⁷³ Finally, following the expiration of the go-shop period, target companies are subject to no shop and fiduciary out provisions.¹⁷⁴ Therefore, following the expiration of the go-shop period, the target may no longer actively solicit bids. Although the target may consider superior proposals, the higher base termination fee would apply to bids received after the expiration of the go-shop period.¹⁷⁵

III. EFFECTIVENESS OF GO-SHOP PROVISIONS AND RECENT DELAWARE JURISPRUDENCE

A. *Intended Advantages and Related Criticisms of Go-Shop Provisions*

As the use of go-shop provisions increases, so has the attention that the provisions are receiving from the M&A community. Law firms have issued a number of client memoranda discussing and often questioning the efficacy of go-shops.¹⁷⁶ The rise of the go-shop has not been lost on the business press, which has also expressed skepticism regarding

¹⁷¹ See Glover & Goodman, *supra* note 163 (describing bifurcated termination fees).

¹⁷² See Kevin M. Schmidt, *Private Equity: Current M&A Issues for Buyers*, in EIGHTH ANNUAL PRIVATE EQUITY FORUM 99, 106, 110 (PLI Corp. Law & Practice, Course Handbook Series No. 1614, 2007) (summarizing transactions containing bifurcated termination fees).

¹⁷³ See *id.* at 110 (describing recent transactions including go-shops and matching rights).

¹⁷⁴ See *id.* at 105, 106.

¹⁷⁵ See *id.* at 106, 110.

¹⁷⁶ See, e.g., Paul Kingsley & Mutya Harsch, *Go-Shop Provisions: A New Trend?*, PRIVATE EQUITY NEWSL. (Davis Polk & Wardwell), Dec. 2006, at 1, available at http://www.dpw.com/1485409/dpw/12_07_06_PrivateEquityNews_dec_06.pdf; Morton & Houtman, *supra* note 27, at 6-7; Weisser & Cubell, *supra* note 161, at 4-5.

the benefits of go-shop provisions. In particular, commentators have debated the effectiveness of go-shop provisions in inducing third party bids and have questioned a board's ability to adequately fulfill its *Revlon* duties by utilizing the provisions. This section seeks to summarize the purported advantages and related criticisms of go-shops.

1. Effectiveness of Go-Shop Provisions in Inducing Third Party Offers

One of the purported benefits of go-shop provisions is that they enable the target company to have a form of insurance in change of control transactions. In other words, go-shop provisions allow the target to conduct an open auction, but because a signed deal already exists, the target avoids the risks involved with a potentially failed public auction.¹⁷⁷ However, a full-blown pre-signing auction and a post-signing auction are not created equal. In contrast to public auctions where all bidders are on equal footing, post-signing market checks, particularly those resulting from go-shop provisions, provide several advantages to the incumbent bidder. The foremost advantage is that the initial acquirer begins the auction in first place and, thus, gains the benefits derived from its first place position, including the traditional deal protection devices contained in the definitive merger agreement.¹⁷⁸ Therefore, critics argue that third party bidders are less likely to emerge post-signing because of the protections conferred upon the initial acquirer in the merger agreement.¹⁷⁹ However, proponents contend that go-shop provisions may be more effective than traditional market checks because bidders are more likely to emerge post-signing if they are actively solicited.¹⁸⁰

¹⁷⁷ See *Go-Shop*, POCKET MBA (PLI), Aug. 8, 2007 (stating that go-shops provide targets with the benefits of an open auction without risk).

¹⁷⁸ See Kingsley & Harsch, *supra* note 176 (stating that the initial acquirer is in an "enviable first place position as the preferred buyer").

¹⁷⁹ *Id.* at 7-8 (summarizing arguments that go-shop provisions do not induce third party bidders).

¹⁸⁰ *Id.* at 6-7 (stating that some proponents contend that third parties are more likely to propose a bid post-signing if they are actively solicited to do so). In addition, commentators point out that, in contrast to the typical fiduciary out provision where companies have to wait for unsolicited superior proposals, "[g]reater transparency and openness is accomplished when the target is allowed to actively pursue other offers." Block, *supra* note 23, at 108 (summarizing advantages and disadvantages of go-shop provisions).

Because go-shop provisions have traditionally been used in LBOs and MBOs, critics assert that there are additional reasons that the provisions are not successful in adequately maximizing stockholder value. Specifically, they argue that both private equity firms and strategic buyers may be hesitant in making a proposal when the initial acquirer is a private equity firm. In particular, some experts have suggested that private equity firms operate on an unwritten gentlemen's agreement that they will not jump another private equity firm's signed deal.¹⁸¹ That is, they act on a sort of "what goes around comes around" mentality, most likely because they tend to engage in several deals a year, and the possibility exists that they could see the same private equity firm on the next deal.¹⁸² Vice Chancellor Strine referenced this mentality recently, stating that it is "a reality that there is not a culture of rampant topping among the larger private equity players, who have relationships with each other that might inhibit such behavior."¹⁸³ Nonetheless, in the aggressive world of M&A participants, it is hard to imagine that, given the right circumstances, a private equity group would not jump a deal for fear of future retribution, even if they consider it to be in bad form to do so.¹⁸⁴ In fact, it already appears as if the market is heading in that direction. Recently, an affiliate of Apollo Management L.P., a private equity firm, successfully jumped

¹⁸¹ See Janet Morrissey, *A Private Equity Peak?*, TIME, July 19, 2007 (stating that the deal jumping among private equity firms is considered a faux pas and quoting Chris Young, Director of M&A Research at Institutional Shareholder Services, as saying, "It has long been suspected that there is an unwritten gentleman's agreement among private-equity firms to refrain from jumping each other's deals"); see also Freed, *supra* note 169 (noting that private equity firms have not outbid other private equity firms in the context of a go-shop provision). Rob Kindler, Vice Chairman of M&A at Morgan Stanley, has stated, "If boards are told go shops' [sic] are likely to make other private equity firms outbid a signed private equity deal, they're being misinformed." *Id.*

¹⁸² See Glover & Goodman, *supra* note 163 (stating that private equity firms may be reluctant to jump a signed deal when they may see the other private equity buyer in the next deal). The same sort of unspoken or unwritten gentlemen's agreement does not appear to exist among strategic players in today's M&A environment. Even the Court of Chancery has recognized that "strategic buyers have not felt shy about 'jumping' friendly deals crafted between their industry rivals." *In re Toys "R" Us, Inc. S'holder Litig.*, 877 A.2d 975, 1008 (Del. Ch. 2005). This is likely because strategic buyers are not engaging in the same number of transactions as private equity firms.

¹⁸³ *In re Lear Corp. S'holder Litig.*, 926 A.2d 94, 121 (Del. Ch. 2007).

¹⁸⁴ Vice Chancellor Strine also has expressed doubt as to whether "such a culture . . . can persist given the powerful countervailing economic incentives at work." *Id.*

an MBO of EGL, Inc., a global freight transportation provider.¹⁸⁵

Like private equity buyers, strategic buyers may also be hesitant in jumping a signed LBO or MBO. In particular, critics argue that strategic buyers may decide not to jump deals where the target company's management is already aligned with the private equity buyer who is planning to retain management and who may be offering management additional equity stakes following completion of the proposed transaction.¹⁸⁶ Therefore, a strategic buyer may harbor concerns that it will not have enough time to assemble a different management team or that its offer would not be successful because it is not willing to offer management the same potential benefits.¹⁸⁷

Others simply contend that go-shop provisions are unnecessary, pointing out that because of the media scrutiny that going-private transactions receive, potential strategic and financial buyers are fully aware that the target company is "in play."¹⁸⁸ As a result, there is no need for the target company to actively solicit bids post-signing and the boards can simply rely on the traditional window shop provision.¹⁸⁹

Still others point out that go-shop provisions make the incumbent bidder a stalking horse for its own transaction which they argue actually makes the target company more desirable to third parties.¹⁹⁰ In addition, the target company is

¹⁸⁵ See EGL, Inc., Current Report (Form 8-K), May 24, 2007 (describing EGL's termination of a merger agreement with a CEO-led group and entry into a merger agreement with an Apollo Management affiliate after EGL determined that the Apollo affiliate's offer constituted a superior proposal).

¹⁸⁶ See Glover & Goodman, *supra* note 163; see also *In re Netsmart Tech., Inc. S'holders Litig.*, 924 A.2d 171, 198 (Del. Ch. 2007) ("[S]trategic buyers might sense that CEOs are more interested in doing private equity deals that leave them as CEOs than strategic deals that may . . . not."). Vice Chancellor Strine has indicated that in deciding whether to submit a bid, strategic buyers consider the profits that management is likely to obtain in a proposed deal. See *id.*

¹⁸⁷ See Glover & Goodman, *supra* note 163.

¹⁸⁸ See Weisser & Cubell, *supra* note 161, at 3-4 (describing factors that initial acquirers weigh before agreeing to go-shop provisions); Michael Weisser & Matthew Cammack, *Shepherding the Deal*, THE DEAL, Mar. 30, 2007 ("[M]any question the practical need of go-shop provisions, particularly when private equity deals grab headlines and pricing and other material terms are often spelled out on the front pages of financial and other publications, thus drawing competing bids with little or no solicitation by the target.").

¹⁸⁹ See Weisser & Cubell, *supra* note 161, at 3-4; Weisser & Cammack, *supra* note 188 (stating that because of the extensive publicity most private equity deals have, competing bids are obtained with "little or no solicitation by the target").

¹⁹⁰ See Kingsley & Harsch, *supra* note 176 (describing the role the initial acquirer assumes as a "stalking horse").

able to lock in a sale price. That is, the initial acquirer's bid sets the floor for any third party bids.¹⁹¹ However, incoming third party bidders still must determine whether to submit a bid while taking into account the value of the underlying transaction and the related deal protection devices in the signed agreement. Thus, to have an opportunity to be a successful bidder post-signing, the third party's bid must at least meet the initial acquirer's bid plus an additional amount taking into account the termination fee for the transaction.¹⁹²

Proponents of go-shops argue that the provisions may actually aid the target in achieving maximum stockholder value. They reason that once the initial acquirer agrees to the inclusion of a go-shop provision, the initial acquirer is incentivized to offer the highest possible price in order to avoid a post-signing bidding war and the possibility that the deal may be successfully "jumped."¹⁹³

2. Sufficiency of the Go-Shop Period in Preparing Superior Proposals and Other Timing Considerations Relating to Go-Shops

Commentators also consider the ramifications of the go-shop period. For instance, some question whether a third party has the legitimate opportunity to prepare a competitive superior proposal during the limited go-shop period. For example, a bid that is higher than the proposed transaction but is contingent on "obtaining financing" would likely not be deemed a superior proposal to a fully financed pre-existing LBO.¹⁹⁴ However, the typically limited duration of the go-shop period may not provide a third party with sufficient time to secure financing.¹⁹⁵ Furthermore, there is a risk that financing may not be available because the initial acquirer has already

¹⁹¹ See Andrew Ross Sorkin, *Looking for More Money, After Reaching a Deal*, N.Y. TIMES, Mar. 26, 2006, at 34 (stating that initial acquirer acts as a "stalking horse" and sets the base price for potential bidders).

¹⁹² For a further discussion of how termination fees work in practice, see *supra* Part II.A.3.

¹⁹³ See Glover & Goodman, *supra* note 163 (arguing that a small number of topping bids may be due to an initial acquirer's incentive to pay full price fearing that the deal may be lost during a go-shop period).

¹⁹⁴ See Dougherty, *supra* note 159, at 331 ("[I]f such competitors overbid 'subject to obtaining financing,' they run the risk that their premium priced bid will be deemed 'not-superior' to the fully financed p-e bid in the hand.").

¹⁹⁵ See *id.* at 330 (stating that the typical go-shop period may not provide a buyer with enough time to arrange financing).

taken advantage of the existing financing opportunities or has engaged the limited number of banks that can offer such a financing package to the point where the banks are conflicted from working with another buyer.¹⁹⁶ Thus, in such a situation, the go-shop provision will not result in a superior proposal.

In addition, the professed timing benefits of go-shop provisions may not be that great. Go-shop provisions purportedly allow parties to streamline the purchase process by permitting parties to forego a public auction or pre-signing market canvass. Instead, the parties can first enter into a definitive agreement and then the target company can begin the auction process while also working to satisfy the closing conditions with the initial acquirer.¹⁹⁷ However, critics point out that go-shops force the target's management to balance its time between the post-signing auction and the fulfillment of closing conditions, including the time-consuming tasks of proxy preparation and other filing preparations.¹⁹⁸ As a result, although time may be saved on the front-end, critics contend that the period between signing and closing may be longer than in traditional post-signing market check situations.¹⁹⁹

Another timing consideration is that by quickly entering into a deal that includes a go-shop provision, the initial acquirer may immediately begin taking steps towards closing, including preparing regulatory filings and advancing the stockholder approval process.²⁰⁰ Thus, the initial acquirer is able to place itself in a position to be able to close the proposed transaction faster than a third party that enters post-signing.²⁰¹ As a result, go-shop provisions *may* have the unintended impact of making the target's management and board favor the initial acquirer over a third party because the initial acquirer is in a more competitive position to close the transaction.

¹⁹⁶ See *id.* (“[A] financed competitive bid assumes that financing has not been ‘dried up’ in advance by a p-e bidder team that strategically pre-shopped financing opportunities to the market’s main financing sources but not the bid itself.”).

¹⁹⁷ Schmidt, *supra* note 172, at 107 (describing purported timing advantages of go-shops).

¹⁹⁸ See *id.*

¹⁹⁹ *Id.*

²⁰⁰ See Mills & Harsch, *supra* note 12, at 46 (describing possible time benefits for the initial acquirer).

²⁰¹ See *id.*

3. Effectiveness of Go-Shop Provisions in Reducing Stockholder Litigation

As previously discussed, boards are turning to go-shop provisions in an effort to avoid increasingly active stockholders challenging proposed transactions and specifically challenging whether the boards have fulfilled their *Revlon* duties. Some commentators argue that the provisions allow boards to more easily fulfill their fiduciary duties because they remain open to higher offers.²⁰² However, other commentators argue that the provisions are illusory and that the provisions are simply “window dressing,” the inclusion of which allows boards to argue that they have fulfilled their duty to maximize stockholder value although the boards may not be making additional efforts to do so.²⁰³ It appears that go-shop provisions will not shield boards from stockholder suits as two recent Delaware Court of Chancery cases demonstrate: in both cases the stockholders challenged the adequacy of the market check when the boards relied on the inclusion of go-shop provisions.

B. *Recent Delaware Court of Chancery Decisions Allowing Companies to “Shop Like Paris Hilton”²⁰⁴ During Extended Store Hours*

Despite expressing skepticism regarding the value of go-shop provisions less than three months earlier at the Tulane Corporate Law Institute, Vice Chancellor Strine issued two back-to-back opinions that, like then-Vice Chancellor Jacobs’ decision nineteen years earlier in *Formica*, seemingly blessed the use of go-shop provisions as a technique for maximizing stockholder value.²⁰⁵

1. *In re Topps Co. Shareholders Litigation*

The first, *In re Topps Co. Shareholders Litigation*, involved the Michael Eisner-led private equity buyout of Topps

²⁰² See Block, *supra* note 23, at 108 (detailing arguments in favor of go-shops).

²⁰³ See *id.* at 108-09 (describing criticisms of go-shop provisions).

²⁰⁴ *In re Topps Co. S’holders Litig.*, 926 A.2d 58, 86 (Del. Ch. 2007).

²⁰⁵ See David Marcus, *The New Auction Rules*, DAILY DEAL, Apr. 16, 2007 (stating that Vice Chancellor Strine recognizes that go-shops “rarely produce much of anything for anyone, including shareholders”); David Marcus, *Auctions, Conflicts and Go-shops, Oh My!*, DAILY DEAL, Apr. 20, 2007 (recounting the highlights of the 2007 Tulane Corporate Law Institute conference and describing Vice Chancellor’s Strine’s statements regarding go-shops provisions).

Co., a manufacturer of baseball cards and the distributor of Bazooka gum.²⁰⁶ Although the deal was not technically an MBO, the Eisner proposal ensured the retention of the majority of the company's key employees and senior management, including the CEO and Chairman's son-in-law who served as the company's President and Chief Operating Officer.²⁰⁷ Topps's ten-member board included three directors nominated by an insurgent stockholder whom Strine referred to as the "Dissident Directors" because the three directors did not agree with the "Incumbent Directors" on many issues, including the Eisner proposal.²⁰⁸

Under Eisner's proposal, a pre-signing auction or market check was not acceptable although Eisner was willing to accept a go-shop provision.²⁰⁹ As a result, the merger agreement included a provision that "gave Topps the chance to shop the bid for 40 days after signing, and the right to accept a 'Superior Proposal' after that, subject only to Eisner's receipt of a termination fee and his match right."²¹⁰ The agreement also included a bifurcated termination fee that amounted to 3.0% of the transaction value during the go-shop period and 4.6% of the transaction value after the go-shop period.²¹¹

The board formed an executive committee, which consisted solely of the five Incumbent Directors, to evaluate offers during the go-shop period.²¹² The only responsibility the entire board, including the Dissident Directors, had with respect to the go-shop period was to evaluate whether a competing offer was actually a superior proposal or was likely to become one.²¹³ At the beginning of the go-shop period, Topps's financial advisor "contacted 107 potential strategic and financial bidders, [of which] five expressed interest in Topps

²⁰⁶ *In re Topps*, 926 A.2d at 60-61 (describing Topps's business and the merger agreement between Eisner and Topps).

²⁰⁷ *Id.* at 60, 61, 73-74. This is of particular consequence because Topps had previously been the subject of a proxy contest designed to remove three directors, including CEO and Chairman, Arthur Shorin, who was also the grandson and nephew of the company's founders. *Id.* at 60-61, 68. In fact, Eisner first approached Shorin during the proxy contest. *Id.* at 61, 68.

²⁰⁸ *Id.* at 61. The board approved the Eisner merger 7-3, with the Dissident Directors making up the three dissenting votes. *Id.* at 71.

²⁰⁹ *Id.* at 61, 70.

²¹⁰ *Id.* at 61.

²¹¹ *Id.* at 66.

²¹² *Id.* at 71. The board formed the executive committee after the majority of the board determined that the Dissident Directors could not sufficiently represent the company's interests because they had voted against the Eisner merger. *Id.*

²¹³ *Id.*

and began a due diligence review.”²¹⁴ The only bidder that seriously continued to pursue Topps was Upper Deck—the one true competitor of Topps—who submitted a bid two days before the expiration of the go-shop period.²¹⁵ The Topps board met after the go-shop period expired and determined that Upper Deck was not an “Excluded Party” under the terms of the agreement, which would have allowed Upper Deck and Topps to continue talks past the expiration of the go-shop period.²¹⁶ The Topps board based its decision on concerns regarding Upper Deck’s ability to finance the transaction, the risk that the transaction may be delayed or prevented by antitrust authorities, and Upper Deck’s failure to sufficiently assume the antitrust risk and the small reverse termination fee proposed by Upper Deck.²¹⁷ Following the board’s decision, Upper Deck made a new, unsolicited offer that was accompanied by a letter from Upper Deck’s financial advisor and potential lender stating that it was “highly confident” that it could finance the transaction.²¹⁸ Upper Deck’s new proposal also offered to divest key licenses if required to do so by antitrust regulators and also was accompanied by an antitrust expert’s letter addressing Topps’s unspecified antitrust concerns.²¹⁹ The Topps board determined that the unsolicited offer was not a superior proposal for similar reasons.²²⁰ The board also rejected Upper Deck’s request to be released from the standstill agreement that prevented Upper Deck from making public any information about its discussions with Topps and also prevented Upper Deck from launching a tender offer for Topps shares without the Topps board’s permission.²²¹

²¹⁴ *In re Topps*, 926 A.2d at 71.

²¹⁵ *Id.* The Upper Deck bid was for \$10.75 cash per share, \$1 more per share than the Eisner proposal. *Id.* Upper Deck’s proposed merger agreement was based on the Eisner merger agreement but deleted all representations and warranties relating to Upper Deck’s ability to finance the merger, deleted a covenant requiring Upper Deck to divest assets in order to obtain regulatory and antitrust approvals, and included an affirmative right not to be required to divest assets in order to obtain regulatory approval. *Id.* In addition, Upper Deck included a “due diligence out” provision pursuant to which Topps would have to provide Upper Deck with any additional information that Upper Deck requested and that conditioned the transaction on Upper Deck’s satisfactory review of due diligence. *Id.*

²¹⁶ *Id.* at 72.

²¹⁷ *Id.*

²¹⁸ *Id.*

²¹⁹ *Id.* at 90.

²²⁰ *Id.* at 72-73.

²²¹ *Id.* at 62.

Although Vice Chancellor Strine granted Upper Deck's motion for a preliminary injunction, Topps "won" with respect to the deal protection devices, including the go-shop provision, which Strine found to be reasonable.²²² Despite his earlier questioning of go-shops,²²³ Strine did not acknowledge that the Delaware courts had not addressed these provisions in recent years, nor did he cite to *Formica* in upholding the go-shop provision. Instead, Strine appeared to treat the go-shop provision as if it were a *Fort Howard* post-signing market check and stated that because the board had not performed a pre-signing market check, it properly obtained a go-shop provision.²²⁴

Strine indicated that go-shops may be useful in inducing other bids because the existence of a "credible, committed" initial acquirer may act as a form of "sucker's insurance" for others to take the leap and submit a bid.²²⁵ Thus, Strine adopted the argument urged by proponents of go-shops that the provisions foster positive psychological effects in helping to stimulate bids.²²⁶ In addition, Vice Chancellor Strine stated that although Eisner had been granted a matching right, the right was not a barrier to other bidders because matching rights have been overcome in the past.²²⁷ Strine also recognized that although a target might want a longer go-shop period or a lower break-up fee, the deal protection devices "left reasonable room for an effective post-signing market check. For 40 days, the Topps board could shop like Paris Hilton."²²⁸

Although Strine did not scrutinize the board's reliance on a go-shop provision, he looked at the board's actions during the go-shop period more closely. Strine found that the board's

²²² *Id.* at 86-87, 93.

²²³ *See supra* note 205 and accompanying text (describing Strine's questioning of go-shop provisions).

²²⁴ *In re Topps*, 926 A.2d at 86.

²²⁵ *Id.* at 87.

²²⁶ *Id.*

²²⁷ *Id.* at 86.

²²⁸ *Id.* Pursuant to the terms of the agreement, after the expiration of the go-shop period, Topps could no longer talk to bidders "unless the bidder had already submitted a 'Superior Proposal' or the Topps board determined that the bidder was an 'Excluded Party'" (i.e., a party that the board determined was "reasonably likely to make a Superior Proposal"). *Id.* at 65. Topps could also consider bids after the forty-day period, if the bid was a superior proposal or was "reasonably likely to lead to one." *Id.* Strine also found that if a bidder felt as if it needed more time, it could obtain the information it needed during the go-shop period and then submit an offer after the period expired and resume the process. *Id.* at 86-87. Thus, Strine seemed to imply that the two periods worked in tandem to create a longer go-shop period. *See id.*

decision not to treat Upper Deck as an “Excluded Party” so that it could negotiate further with Upper Deck after the go-shop period was “highly questionable” and suggested that the Incumbent Directors favored Eisner who promised to retain management.²²⁹ Strine further criticized Topps’s lack of a good faith effort to negotiate with Upper Deck and Topps’s misrepresentation of facts regarding Upper Deck’s offer that were included in Topps’s public disclosure, including public criticism of Upper Deck’s offer.²³⁰ Furthermore, Strine determined that Topps’s refusal to release Upper Deck from the standstill threatened Topps’s stockholders’ informed decision-making because Upper Deck was unable to tell its own version of the story.²³¹ As a result, Strine granted a preliminary injunction delaying the merger vote until Topps granted Upper Deck a waiver of the standstill so that that Upper Deck could make a tender offer and communicate with Topps stockholders.²³²

2. *In re Lear Corp. Shareholders Litigation*

A day after *Topps*, Vice Chancellor Strine issued a second opinion, *In re Lear Corp. Shareholders Litigation*, in which the Vice Chancellor again issued a preliminary injunction delaying the merger vote until additional disclosure could be made, but blessed the parties’ inclusion of a go-shop provision in the merger agreement.²³³ That case stemmed from a Carl Icahn-led LBO of Lear Corp., a troubled company in which Icahn had obtained a 24% holding in 2006.²³⁴ In November 2006, concerned about his personal financial security, Lear’s long-time CEO, Robert E. Rossiter, approached Lear’s compensation committee about accelerating his retirement benefit payments which had a fully vested value of \$14.6 million.²³⁵ The compensation committee hired a compensation

²²⁹ *In re Topps*, 926 A.2d at 89-90. Strine also emphasized that when Upper Deck proposed a materially higher price than the Eisner proposal, the board seemed “more bent on coming up with obstacles to securing that higher value” rather than reacting with enthusiasm at the possibility of enhancing stockholder value. *Id.* at 88.

²³⁰ *Id.* at 91.

²³¹ *Id.* at 92.

²³² *Id.* at 92-93.

²³³ *In re Lear Corp. S’holder Litig.*, 926 A.2d 94, 97-98 (Del. Ch. 2007).

²³⁴ *Id.* at 97, 100. Icahn planned to use an affiliated entity, American Real Estate Partner, LP, to consummate the transaction. *Id.* at 102.

²³⁵ *Id.* at 100. The retirement benefits would vest in 2011 when Rossiter turned 65; however, Rossiter could access \$10.4 million of his SERP benefits by mid-2007 if Rossiter retired. *Id.*

consulting firm that “presented five potential options to allow Rossiter to liquidate his retirement assets quickly while keeping his job.”²³⁶ The consulting firm indicated that no matter which option Rossiter were to choose, he was likely to face criticism from investors for accelerating his own benefits during a difficult period for the company.²³⁷ Rossiter, however, did not have to choose among the five options because, in January 2007, Icahn proposed a going-private transaction in which existing management would be retained.²³⁸ The special committee that was formed following Icahn’s proposal allowed Rossiter to negotiate price terms without the presence of Lear’s financial advisor or the special committee.²³⁹

The Lear board debated whether the company should engage in a formal auction but ultimately rejected the idea fearing that it would disrupt business and that, more importantly, Icahn may pull his offer as Icahn had indicated that he would do if the company engaged in a full-blown auction.²⁴⁰ The board instead directed Lear’s financial advisor to engage in a four-day limited pre-signing canvass by contacting eight financial buyers who had an interest in the automotive sector, the industry in which Lear engages.²⁴¹ Five of the financial buyers who were contacted expressed “tepid ‘maybes,’” but none made a preliminary proposal or expressed a desire to pursue due diligence.²⁴² A few days after the limited market canvass, Lear entered into a merger agreement with Icahn that included a forty-five day go-shop provision and fiduciary out that allowed Lear to accept a superior proposal following the expiration of the go-shop period.²⁴³ In addition, the agreement contained a bifurcated termination fee amounting to 2.79% of the equity value of the deal if the agreement was terminated during the go-shop period, or 3.52% of the deal equity value if the agreement was terminated following the expiration of the go-shop period.²⁴⁴ Icahn also was granted

²³⁶ *Id.* at 100-01.

²³⁷ *Id.* at 101.

²³⁸ *Id.*

²³⁹ *Id.* at 102-03.

²⁴⁰ *Id.* at 104.

²⁴¹ *Id.* at 104-05.

²⁴² *Id.* at 105.

²⁴³ *Id.* at 105, 107.

²⁴⁴ *Id.* at 107. The agreement also provided that a termination fee was payable if the Lear board withdrew its recommendation for the merger or failed to reconfirm its support for the merger if it were requested to do so. *Id.*

matching rights which allowed Icahn ten days to determine whether to increase his offer to match a superior proposal.²⁴⁵ Lear's financial advisors began to contact potential buyers as soon as the merger agreement was executed.²⁴⁶ They contacted a total of forty-one potential buyers, twenty-four financial sponsors and seventeen strategic buyers, of which only eight buyers entered into confidentiality agreements to begin due diligence.²⁴⁷ However, unlike in *Topps*, none of the buyers contacted ultimately made a preliminary bid nor did Lear receive any unsolicited bids during the go-shop period.²⁴⁸

Lear stockholders sought a preliminary injunction arguing that the Lear board did not disclose all material facts necessary for the stockholders to decide whether to approve the merger and that the Lear board failed to make a reasonable effort to maximize stockholder value.²⁴⁹ With respect to the *Reylon* claims, Strine stated that Rossiter should have informed the board of Icahn's proposal earlier and that the special committee should have taken a larger role in the negotiation process, particularly in light of Rossiter's personal interests in the going-private transaction.²⁵⁰ However, Strine concluded that the overall approach taken by the special committee appeared to have been reasonable.²⁵¹ In finding that the Lear board's decision not to engage in a full public auction was reasonable, Strine indicated that Lear's elimination of its poison pill and Icahn's investment in Lear were signals to the market that it was "perfectly obvious that Lear was open to invitations."²⁵²

Vice Chancellor Strine likewise rejected the plaintiffs' argument that the go-shop provision combined with the other deal protection devices had the effect of chilling bids.²⁵³ However, in reaching that determination, Strine admittedly

²⁴⁵ *In re Lear*, 926 A.2d at 108. Icahn's offer was for \$36 per share. *Id.* at 105. If the superior proposal was greater than \$37 per share, Icahn only had one chance to match. *Id.* at 108. However, if the superior proposal was not greater than \$37 per share, Lear had to give Icahn "three days to match each successive [superior] proposal." *Id.* If Icahn decided not to match a superior proposal, Icahn agreed to vote his block of shares in favor of the superior proposal. *Id.*

²⁴⁶ *Id.* at 105.

²⁴⁷ *Id.* at 106.

²⁴⁸ *Id.* at 106-07.

²⁴⁹ *Id.* at 109-10.

²⁵⁰ *Id.* at 118.

²⁵¹ *Id.*

²⁵² *Id.* at 118-19.

²⁵³ *Id.* at 120.

gave the bifurcated, or two-tiered, termination fee “relatively little weight.”²⁵⁴ Strine acknowledged that most bidders would have been able to take advantage of the lower termination fee offered during the go-shop provision because it required the third party to “get the whole shebang done within the 45-day window.”²⁵⁵ Strine found that the 3.52% termination fee was reasonable because it was not of the level that would deter a serious bid.²⁵⁶ Strine treated Icahn’s matching rights similarly stating that matching rights “are hardly novel” and have been upheld even when coupled with termination fees.²⁵⁷

Like his decision in *Topps*, Vice Chancellor Strine treated the Lear plaintiffs’ disclosure claims with skepticism.²⁵⁸ Although Strine was careful to say that Rossiter did not act inappropriately, Strine found that Rossiter’s personal motivations for favoring a going-private transaction should have been included in the proxy statement.²⁵⁹

3. Impact of *Topps* and *Lear*

Although Strine continually stresses that Court of Chancery decisions are not intended to create bright-line rules

²⁵⁴ *Id.* at 119.

²⁵⁵ *Id.* at 119-20. To take advantage of the lower termination fee, Strine stated that the third party would have to

do adequate due diligence, present a topping bid with a full-blown draft merger agreement, have the Lear board make the required decision to declare the new bid a superior offer, wait Icahn’s ten-day period to match, and then have the Lear board accept that bid, terminate its agreement with Icahn, and “substantially concurrently” enter into a merger agreement with it. All of these events had to occur within [the forty-five-day go-shop provision]

Id. at 119.

²⁵⁶ *Id.* at 120.

²⁵⁷ *Id.* In reaching this conclusion, Strine relied on the defendants’ citation of over fifteen transactions that were jumped despite a termination fee exceeding 3% paired with matching rights. *Id.* at 120 n.21; *see also* The AREP Defendants’ Memorandum of Law in Opposition to Plaintiffs’ Application for a Preliminary Injunction at 28-29, *In re Lear*, 926 A.2d 94, 2007 WL 2125317. The majority of the deals cited by defendants involved traditional no shop and window shop provisions rather than go-shop provisions. Affidavit of Daniel R. Fischel, exhibit O, *In re Lear*, 926 A.2d 94, 2007 WL 2801493.

²⁵⁸ *In re Lear*, 926 A.2d at 114-15.

²⁵⁹ *Id.* at 114. On July 16, 2007, Lear’s stockholders voted against the Icahn buyout. *See* Lear Corp., Current Report (Form 8-K, exhibit 99.1) (July 17, 2007) (filing press release announcing that Lear stockholders had voted against the Icahn merger). This stockholder vote represents only the eighth U.S. deal (out of more than 1000 U.S. deals requiring consent) that stockholders have voted against since 2003. *See* Terry Kosdrosky, *Lear Vote Is Big Bet on Detroit*, WALL ST. J., July 17, 2007, at A2.

that dealmakers must follow in every deal, Strine's cursory review of the go-shop provisions in *Topps* and *Lear* send a signal to dealmakers that go-shops are acceptable provisions to depend upon in future transactions.²⁶⁰ However, as the next section details, the effect of go-shop provisions is likely not that different than that of traditional post-signing market checks with respect to value maximization. In fact, both sale methods reveal that the Delaware courts are moving in the opposite direction from the purer bidding process announced in *Revlon*.

IV. SHOPPING DURING "EXTENDED STORE HOURS": NOT SO DIFFERENT FROM NOT SHOPPING AFTER ALL

Although commentators have noted Strine's cursory review of the go-shop provisions in *Topps* and *Lear*, they have failed to recognize Strine's implicit recognition that we have come full circle since the 1980s when the Delaware Supreme Court announced that the board should act as auctioneers in sale of control transactions. Neither in *Formica*, nor in *Lear* and *Topps*, did either vice-chancellor draw a distinction between go-shop provisions and the post-signing market checks blessed in the *Fort Howard* line of cases that relied on deal protection devices, such as no shop and window shop provisions.²⁶¹ I contend that this was not simply an oversight on the part of the Delaware Court of Chancery. Instead, it reflects the simple acknowledgment that despite all of the hoopla surrounding the recent prevalence of go-shop provisions, and the questioning of their effectiveness, the end result of the go-

²⁶⁰ See Sheri Qualters, *Strine Theory*, NAT'L L.J., July 30, 2007, at 1 (summarizing Vice Chancellor Strine's opinion that deal tactics must change as companies' circumstances change). Strine's cursory review and failure to differentiate go-shops from no shops may well be a result of the lag time that frequently occurs between the use of a particular deal mechanism and the courts' opportunity to review the mechanism. Because of the dynamic nature of M&A and the fact that dealmakers are often utilizing new deal tactics and new twists on transaction structures before they are blessed by the courts, many deals close prior to the courts having an opportunity to review the actions of dealmakers. In a similar context, Professor Edward R. Rock has commented that as a result of this lag time, Delaware courts are placed in the position of not being able to deem the dealmakers' tactics or new transaction structures per se illegal. Rock, *supra* note 7, at 1096-97 (theorizing that because of the significant number of MBOs in the 1970s and 1980s, by the time the Delaware Court of Chancery could have an "opportunity to articulate standards," the court could not find MBOs per se illegal). Beyond finding a particular deal tactic per se illegal, Delaware courts are presented with the situation where the actions or tactics used in a deal are not necessarily ideal but the courts may be hesitant to issue an injunction without a great showing of unreasonableness.

²⁶¹ For a discussion of the *Fort Howard* line of cases, see Part II.C.

shop provision is the same as the post-signing market check with respect to value maximization.

As described previously, a no shop provision with a fiduciary out, or a window shop provision, does not allow the active solicitation of third party offers. However, a no shop accompanied by a fiduciary out permits a target board to participate in negotiations with a third party who submits an unsolicited offer that is, or may become, a superior proposal. In contrast, the go-shop provision allows the active solicitation of such offers and effectively moves the auction process to the post-signing. However, these facial dissimilarities are where the differences between the two sale methods end.

Targets have relied exclusively on both the post-signing market check and go-shop provisions in situations where they have negotiated solely with one bidder pre-signing, or conducted only a limited pre-signing market canvass, as in *Fort Howard*, *Pennaco*, *MONY*, *Lear*, and *Topps*. According to one survey, which analyzed thirty transactions including go-shop provisions, the target companies in nearly every transaction surveyed did not first conduct a pre-signing market canvass prior to entering into the merger agreement.²⁶² Similarly, Delaware courts have upheld post-signing market checks when the target did not first conduct a pre-signing market canvass.²⁶³ Thus, the same criticisms regarding the favoritism of boards and management and resulting bid chilling effects of go-shop provisions can be equally applied to post-signing market checks. For example, the possibility remains that using go-shop provisions to fulfill a board's *Revlon* duties could "permit management to insulate its last period decisions from the constraint of the market for corporate control."²⁶⁴ There is a risk that management and boards who may have ulterior motives could use go-shop provisions to go with the suitor of their choice rather than the bidder who may present a superior offer. Stated differently, go-shop provisions present the danger of allowing a board to "hide" behind a go-shop despite not having shopped the company pre-signing. However, the same risks exist in the now standard post-signing market check situation,

²⁶² See Morton & Houtman, *supra* note 27, at 1 n.1 (describing results of survey).

²⁶³ See, e.g., *In re MCA, Inc. S'holders Litig.*, 598 A.2d 687, 693 (Del. Ch. 1991) (upholding reliance on post-signing market check after initial merger agreement was publicly negotiated for two months and no other bidders came forward).

²⁶⁴ Griffith, *supra* note 40, at 1963.

and the Delaware Court of Chancery addressed such allegations of favoritism in *Fort Howard*.²⁶⁵

Moreover, critics' arguments that go-shops are ineffective at inducing superior proposals because of barriers to entry that a signed transaction present also hold true in situations where the target relies only on a post-signing market check. Like third parties who are contacted during a go-shop period, third parties that enter during a post-signing market check also encounter deal protection devices like termination fees and matching rights and also are constrained by the pre-closing period. The Delaware courts, however, address only whether these mechanisms are too onerous that they would completely prevent bidders from "jumping" in post-signing.

In fact, as we have seen, the continuing trend in the Delaware courts is to consider the sale process as a whole and, in particular, the reasonableness of the board's decisions in light of the totality of the circumstances. As the Delaware courts have done since the 1980s, *Lear* and *Topps* demonstrate the courts' continued focus on the role of management in negotiations. For example, the courts scrutinize whether there were conflicts of interest present and whether the management's decisions were motivated by entrenchment.²⁶⁶ Although the Delaware courts may express skepticism and suspicion regarding a board's or special committee's actions, the courts are, in effect, powerless to prevent such an action without a very persuasive showing of bad faith by the plaintiffs.²⁶⁷ The same powerlessness applies no matter if a post-signing market check or a go-shop provision is utilized to determine whether the board has selected the best deal for the target's stockholders.²⁶⁸ Instead, the Delaware courts tend to

²⁶⁵ See *In re Fort Howard Corp. S'holders Litig.*, Civ. A. No. 9991, 1988 WL 83147, at *10-11 (Del. Ch. Aug. 8, 1988) (summarizing plaintiffs' arguments that the special committee favored the management-affiliated transactions).

²⁶⁶ See *supra* Part III.B.

²⁶⁷ See, e.g., *In re Fort Howard*, 1988 WL 83147, at *12-13 (finding the good faith of the special committee to be suspect, but that the committee's actions were not enough to indicate bad faith); see also *supra* note 108 and accompanying text (describing Chancellor Allen's suspicion in *Fort Howard* of the CEO's and special committee's activities and Allen's finding that the showing of bad faith was not sufficient).

²⁶⁸ Although it is beyond the scope of this Article, what really may be needed in order to curb the possibility of a board or management's own selfish greed is, in the words of former U.S. Securities and Exchange Commission Chairman Donaldson,

a change in mindset—one that fosters not only a "culture of compliance" but also a company-wide environment that fosters ethical behavior and decision-

use their decisions to comment on behavior that they find to be suspicious so that dealmakers will tend to shy away from such activity in future transactions.²⁶⁹

As a result of this trend in Delaware jurisprudence, over the past two decades we have moved from an initial focus on fully shopped deals that include fiduciary outs simply to ensure that the directors do not violate their post-signing fiduciary duties, to a more exclusive reliance on the fiduciary out model to sell the company. We then moved from the fiduciary out model to go-shop provisions that in effect allow an auction to be conducted post-signing. This movement appears to be in direct opposition to *Revlon* where the Delaware Supreme Court chastised the parties for ending a heated bidding contest and held that a fiduciary out must be included in the definitive agreement. Although *Revlon* seemed to be the start of a trend towards fostering a more competitive bidding process, the Delaware courts' decisions allowing much, if not all, of the sale process to take place post-signing does not foster such a heated bidding process when deal protections in the merger agreement act to discourage bids. Realistically, what board of directors would not be inclined to rely on go-shop provisions in the

making. Creating that culture means doing more than developing good policies and procedures . . . It means instilling an ethical culture—a company-wide commitment to do the right thing, this time and every time—so much so that it becomes the core of what I call the essential “DNA” of the company.

William H. Donaldson, Chairman, SEC, Remarks to the National Association of Securities Dealers (May 12, 2004), *transcript available at* <http://www.sec.gov/news/speech/spch051204whd.htm>.

²⁶⁹ See Rock, *supra* note 7, at 1095-96 (stating that the advisory opinion-like nature of Delaware opinions are helpful to dealmakers in planning transactions, but they are problematic because of their fact-specific nature); Qualters, *supra* note 260, at 1 (quoting Vice Chancellor Strine as stating, “People learn from the cases, that’s what’s good about them . . . It’s a low-cost opportunity.” (internal quotation marks omitted)). Professor Rock has theorized:

This reactive stance, combined with what I claim to be a fairly self-conscious attempt by the courts to shape the standards of conduct in a rapidly developing transactional form, may be the driving force behind judicial attempts to surpass it. Thus, the “preachiness” of Delaware MBO opinions, the pattern of criticizing conduct even when no injunction is issued, and judges’ extrajudicial utterances can all be read as attempts to be heard on a critical matter in the absence of a case raising just the right issue and in the absence of the articulation (or articulability) of a governing rule. Such utterances are, in a literal sense, advisory opinions.

Rock, *supra* note 7, at 1095.

absence of a public auction or targeted market canvass?²⁷⁰ The long-term implications of the go-shop provision could very well be that the pre-signing public auction or more limited market canvass may go by the wayside as the Delaware courts have allowed such processes to be conducted post-signing.

V. CONCLUSION

In many ways we have come full circle since the merger wave of the 1980s and the Delaware Supreme Court's landmark opinion in *Revlon*. The 1986 ruling in *Revlon* appeared to begin a movement toward a "pure" auction process that would result in achieving the best possible price for stockholders. The Delaware courts have recognized that a public auction or, at least, a targeted market canvass that occurs pre-signing, are the best ways to achieve value maximization. These methods allow potential buyers to bid on a target company before deal protection devices and other concerns work to inhibit bidding. However, less than two years after *Revlon*, the Delaware Court of Chancery authorized the almost exclusive reliance on no shop provisions coupled with fiduciary outs, or, in other words, a post-signing market check, to achieve value maximization. The Delaware courts have continued to validate these post-signing market checks while focusing on the sale process as a whole.

Over the past three years, the passive post-signing market check has given way to go-shop provisions allowing target companies to *actively* shop themselves post-signing, when they would have otherwise been prevented from doing so. In effect, these provisions permit targets to extend their "store hours" and have moved the auction process post-signing. Critics have attacked these provisions as ineffective at maximizing stockholder value for various reasons, including that the provisions do not induce bids because of pre-existing deal protection devices and because the provisions allow target companies to favor the initial bidders, who are often private equity firms that are seeking to retain management or are providing management with certain compensation packages or

²⁷⁰ An exception likely exists for small micro-cap companies, who after the Delaware Court of Chancery's ruling in *Netsmart*, need to engage in a more complete targeted market canvass rather than rely on a post-signing market check as a sale method. For a discussion of sale methods with respect to micro-cap companies, see *supra* notes 83-85 accompanying text.

other incentives following closing. This Article contends, however, that the end result of the go-shop is really no different from the more passive post-signing market check that permits a company to terminate the agreement in favor of a superior proposal but does not allow the target to actively shop the company. The same criticisms can apply equally to both sale methods and active bidding can be inhibited due to deal protection devices when either sale method is utilized. The implications of this movement in Delaware jurisprudence toward reliance on post-signing market checks and go-shops results in the failure to use methods that encourage an active bidding process and the maximization of stockholder value. Because the Delaware courts do not focus on these sale processes but rather only check that the methods used are not so onerous that they would result in locking up a transaction, the courts have shifted their attention away from the policies promoted by *Revlon*. The exclusive reliance on go-shop provisions to sell a company and achieve the highest price for stockholders signals the death of the movement toward a purer competitive bidding process that first began over twenty years ago in *Revlon*.