

## Recent Chancery Court Opinions on Ripeness

By John Mark Zeberkiewicz and Stephanie Norman

Delaware Business Court Insider

December 10, 2014



John Mark Zeberkiewicz and Stephanie Norman

The Delaware Court of Chancery's ruling in *Pontiac General Employees Retirement System v. Ballantine*, C.A. No. 9789-VCL (Del. Ch. Oct. 14, 2014) (Transcript), is the most recent statement on so-called "dead hand" proxy puts—the provisions in credit agreements that trigger an acceleration of the borrower's indebtedness upon a change in a majority of its board within a specified timeframe. (An ordinary "proxy put" provides that the incumbent board may approve any non-incumbent nominee as a "continuing director" to ensure that the nominee will not be counted toward whether a change of control has occurred, while a "dead hand" proxy put provides that any person who has been nominated or elected as a result of an actual or threatened proxy contest will count toward a change of control, whether or not approved by the board.) Although the ruling is perhaps most notable as it relates to aiding and abetting claims against banks that negotiate for these provisions, it also raises interesting issues on the question of ripeness. The Delaware Supreme Court recently explained in *XL Specialty Insurance v. WMI Liquidating Trust*, 93 A.3d 1208, 1217-18 (Del. 2014) (footnotes omitted), that "generally, a dispute will be deemed ripe if 'litigation sooner or later appears to be unavoidable and where the material facts are static.' Conversely, a dispute will be deemed not ripe where the claim is based on 'uncertain and contingent events' that may not occur, or where 'future events may obviate the need' for judicial intervention." .

Notably, the stockholder plaintiff in *Ballantine* had not run its own slate of directors at any prior meeting of stockholders of Healthways Inc., the nominal defendant in *Ballantine*. Additionally, although the court noted that Healthways "faced, and continues to face, the risk of a proxy contest," there was no clear indication from the transcript that the plaintiff or any particular insurgent or group was actively seeking to run a slate of nominees at Healthways' upcoming annual meeting. Nevertheless, the plaintiff's challenge to the proxy-put provision in Healthways' credit agreement survived a motion to dismiss in the face of a ripeness defense.

The claims in *Ballantine* trace their roots to two earlier Chancery Court opinions, *San Antonio Fire & Police Pension Fund v. Amylin Pharmaceuticals*, 983 A.2d 304 (Del. Ch. 2009), and *Kallick v. Sandridge Energy*, 68 A.3d 242 (Del. Ch. 2013), addressing the use of proxy puts. Each of the companies in those cases was the subject of a proxy contest from an investor with the capacity to mount a serious campaign. Although it was not evident that a proxy contest, either at the behest of the plaintiff or any other party, implicating the proxy-put provision was threatened or under way at Healthways, the court was persuaded by the plaintiff's argument that the proxy-put provision operates as a "sword of Damocles," noting that any stockholder seeking a change in the board would be "bargaining in the shadow of the put." The court stated that "a truly effective deterrent is never triggered," and noted that if such a "deterrent is actually used, it has failed its purpose."

Since *Ballantine*, the court revisited the question of ripeness. In *In re Allergan Stockholder Litigation* (Del. Ch. Nov. 7, 2014), the stockholder plaintiffs challenged a provision in Allergan's certificate of incorporation and bylaws that permitted stockholders to remove directors at a special meeting, but not to elect their successors at such meeting, if

an election of directors had occurred within one year of the special meeting request. The plaintiffs sought a declaration that the similar item provision would not prohibit Allergan's stockholders from removing the entire board at a special meeting and simultaneously electing directors at the same meeting. The *Allergan* court held the plaintiffs' claim represented "a classic example of a request for an advisory opinion that is not ripe, and may never become ripe, for judicial review." Distinguishing *Ballantine*, the *Allergan* court held that Allergan's similar item provision could not "legitimately be characterized as a significant deterrent to the ability of Allergan's stockholders to exercise their franchise rights." That finding was "made plain" by the existence of an ongoing proxy contest seeking the removal of six of nine of Allergan's board members. As the *Allergan* court stated, "Allergan's stockholders have not been deterred from pursuing a proxy contest." Instead, the parties actually mounting the campaign elected to pursue a different strategy than the one the stockholder plaintiffs had proposed.

Interestingly, as in *Allergan*, the plaintiff in *Ballantine* was not only bringing claims for breach of fiduciary duty, but was also seeking a declaratory judgment as to the enforceability of the provision itself. Given that the credit agreement contained a severability clause, the plaintiff's declaratory judgment claim would seem, based on prior Chancery Court precedent, to be unripe. In *Wayne County Employees' Retirement System v. Corti*, (Del. Ch. July 24, 2009), for example, a stockholder plaintiff sought a declaration that a corporate opportunity provision in Activision Blizzard's certificate of incorporation was invalid on the grounds that it purported to exculpate directors from liability beyond the scope authorized by Section 102(b)(7) of the Delaware General Corporation Law. The *Corti* court held that the mere existence of the provision did not threaten harm sufficient to warrant a declaratory judgment on its facial validity, since the entire clause was "qualified by the phrase, 'to the fullest extent permitted by law,'" which precluded a construction "that would run afoul of Delaware law." It is unclear from the *Ballantine* transcript whether the court specifically ruled on the ripeness of the plaintiff's claim as to the proxy put's enforceability. "What I think is ripe now," the court stated, "is a claim that, based on the facts of this case, the board of directors breached its duties in a factually specific manner by adopting this ... dead hand proxy-put arrangement in the context of the facts and circumstances" present before the court.

While the court in *Ballantine*, unlike the court in *Allergan*, found that the plaintiff had brought a ripe claim (at least as to the adoption of the provision), it was careful to note that it was only ruling as to the defendants' motion to dismiss and was not "making any per se adjudication." The court stated that it was not making findings of fact on the underlying breach of fiduciary duty claims—specifically as to whether the proxy put was adopted in response to "stockholder pressure" or "some other driver." Nevertheless, when negotiating and entering into credit agreements and other instruments, corporations and their advisers should be aware of the potential implications of including proxy put and similar provisions in those instruments, such as the risk of litigation on what might otherwise appear to be a clear day.

---

*John Mark Zeberkiewicz* is a director, and *Stephanie Norman* is an associate, at Richards, Layton & Finger. The views expressed in this article are those of the authors and not necessarily those of Richards Layton or its clients.

Reprinted with permission from the December 10, 2014 issue of Delaware Business Court Insider. © 2014 ALM Media Properties, LLC. Further duplication without permission is prohibited. All rights reserved.