Chancery Court Addresses Aiding and Abetting Claims

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In *Virtus Capital v. Eastman Chemical*, C.A. No. 9808-VCL (Del. Ch. Feb. 11, 2015), the Delaware Court of Chancery denied a motion to dismiss a complaint for lack of personal jurisdiction in a suit related to the 2011 sale of Sterling Chemicals Inc. to Eastman Chemical Co. that was allegedly orchestrated by Sterling's controlling stockholder, Martin D. Sass. In the process of finding that the defendants were subject to personal jurisdiction in Delaware, Vice Chancellor J. Travis Laster indicated that the complaint contained allegations sufficient to state a claim that Sass had breached his fiduciary duties by allegedly causing Sterling to be sold at a "fire-sale" price and that Eastman had aided and abetted Sass' breaches of fiduciary duty.

Although the case was at a preliminary stage procedurally, plaintiff Virtus Capital L.P. had engaged in substantial discovery during an appraisal proceeding related to the merger prior to bringing its fiduciary duty and aiding and abetting claims. Sass moved to dismiss the complaint for lack of personal jurisdiction. The court denied Sass' motion, concluding that Virtus had made a factual showing that the elements of the conspiracy theory of jurisdiction had been satisfied.

The court found the first two elements of the conspiracy theory of jurisdiction—that a conspiracy existed and that Sass was a member in the conspiracy—had been satisfied because the complaint alleged a claim for breach of fiduciary duty and a related claim against Eastman for aiding and abetting that breach. Specifically, Virtus alleged the sale of Sterling was primarily motivated by Sass' desire to monetize his investment in Sterling before he lost majority voting control over Sterling.

After Eastman approached Sterling about a potential transaction, Sass allegedly breached his fiduciary duties by steering Sterling toward a sale of the whole company through his control over members of the Sterling board of directors and the chairman of the special committee charged with negotiating the deal. Virtus also alleged that Eastman aided and abetted Sass' breach by using information leaked by a Sterling employee regarding the sale process and Sass' desire to seek a short-term sale to negotiate for a deal at a below-market price. The court found the other elements of the conspiracy theory of jurisdiction were satisfied because activities in furtherance of the conspiracy occurring in Delaware were either taken by or were attributable to Sass, and because Sass was a sophisticated investor who knew or should have known that his conduct could subject him to jurisdiction in Delaware for purposes of challenges to the merger.

Eastman Chemical is notable because it is the third recent case in which Laster has addressed aiding and abetting claims. In *In re Rural/Metro Stockholders Litigation*, 88 A.3d 54 (Del. Ch. 2014), Laster held a financial adviser liable for a judgment of approximately $75.8 million for aiding and abetting breaches of fiduciary duty of a board of directors in connection with a merger. More recently, in *Pontiac General Employees Retirement System v. Ballantine (Healthways)*, C.A. No. 9789-VCL (Del. Ch. Oct. 14, 2014), Laster denied a motion to dismiss aiding and abetting

claims against a bank that allegedly facilitated the entrenchment motives of a board of directors by negotiating for a dead hand proxy-put provision in a loan agreement while the company was under the threat of a proxy contest.

The Chancery Court's recent focus on aiding and abetting claims could be cause for concern for buyers who find themselves with superior leverage during M&A negotiations. As the Delaware Supreme Court stated in *Malpiede v. Townson*, attempts by a third party to achieve a better deal through arm's-length negotiations generally do not give rise to liability for aiding and abetting. However, as the Supreme Court noted in *Malpiede* and the Chancery Court indicated in these recent decisions, a third party could face liability as an aider and abettor for creating or exploiting a conflict of interest in the board of directors to further its own interests.

Contrasting the alleged conduct of the third-party negotiators in *Eastman Chemical* and *Healthways* with the alleged conduct of the acquirer in *In re Comverge Shareholders Litigation*, C.A. No. 7368-VCP (Del. Ch. Nov. 25, 2014), demonstrates the fine line between aggressive, arm's-length negotiations and aiding and abetting a fiduciary breach.

In *Comverge*, Vice Chancellor Donald F. Parsons Jr. dismissed aiding and abetting claims against HIG Capital LLC related to HIG's acquisition of Comverge Inc. HIG gained significant leverage over Comverge during merger negotiations by acquiring notes issued by Comverge that gave HIG the right to accelerate Comverge's debt. HIG used its leverage to negotiate for a deal that was below Comverge's then-current trading price and to secure deal-protection devices that the Chancery Court found could have had an impermissibly preclusive effect on alternative bidders. The court recognized that HIG's "hard-nosed and aggressive" negotiating strategy was designed to take advantage of Comverge's weakened financial position, but ultimately concluded that HIG's conduct, while potentially suspect, did not rise to the level of aiding and abetting liability.

The distinction between *Comverge* and *Eastman Chemical* may be that, in seeking to get a better deal, HIG allegedly took advantage of the company's financial distress, while Eastman allegedly took advantage of the controlling stockholder's desire for liquidity. From a buyer's perspective, both situations resulted in a transaction between a willing buyer and a motivated seller, but, due to the identity of the party motivated to sell, one transaction may carry with it the risk of aider and abettor liability and the other does not.

While the Chancery Court will likely continue to explore the contours of aiding and abetting liability in future decisions, potential acquirers in M&A transactions should be aware of the risk that hard bargaining and informational advantages could be recast by an opportunistic plaintiff as an aiding and abetting claim.

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