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Recommended Citation
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Resolving the Crisis in U.S. Merger Regulation: A Transatlantic Alternative to the Perpetual Litigation Machine

Dan Awrey,[†] Blanaid Clarke,[‡] and Sean J. Griffith[*]

Regulation by litigation has driven U.S. merger regulation to crisis. The reliance on private lawsuits to police disclosures and potential conflicts of interest in mergers, takeovers, and other control transactions has resulted in the filing of claims after every major transaction. However, it has failed to achieve meaningful benefits for shareholders and has instead deprived them of potentially valuable rights. Regulation by litigation has devolved into attorney rent-seeking, and the raft of substantive and procedural reforms aimed at resolving the crisis has failed.

There is an alternative to regulation by litigation. Drawing upon the code and panel-based models of merger regulation in the United Kingdom and Ireland, this Article explores whether a regulatory model might be better at protecting shareholder interests in merger transactions. A regulatory alternative holds a number of significant advantages, including greater speed, responsiveness, certainty, and lower administrative costs. In light of these potential advantages, it is remarkable that no U.S. state has experimented with a code and panel-based model of merger regulation. We explain the persistent difference between the U.S. and Anglo-Irish models by reference to interest group politics and, in particular, the power of the bar to influence corporate law reforms in the United States.

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Introduction

The American model of corporate law is regulation by litigation. This model relies upon private lawsuits to oversee managerial conduct in mergers, takeovers, and other control transactions and to ensure the adequacy of disclosure to shareholders.[1] No regulatory body oversees the negotiation and consummation of these transactions.[2] Rather, shareholders' right to sue corporate managers for breach of fiduciary duty in connection with merger transactions leads judges to "regulate" mergers by deciding the cases brought before them.

But there is a well-known crisis in merger litigation in the United States.[3] In spite of generating lawsuits in virtually every deal, the system generates no

1. For brevity, we will refer to these transactions simply as "mergers" and, except where otherwise provided, to regulation or litigation relating to these matters simply as "merger regulation" or "merger litigation."

2. The role of securities law and the Securities and Exchange Commission ("SEC") in these transactions is described in more detail at *infra* notes 31-34 and accompanying text.

3. *See* JOHN C. COFFEE, JR., ENTREPRENEURIAL LITIGATION: ITS RISE AND FALL AND FUTURE 90 (2015) (noting that in the context of merger class actions, "incentives to sue have become excessive, and litigation is growing out of control, like algae in a petri dish"); *see also* Stephen Bainbridge, *Fee-Shifting: Delaware's Self-Inflicted Wound*, 40 DEL. J. CORP. L. 851, 852 (2016) (contending that merger litigation is a "problem that has reached crisis proportions"); James D. Cox & Randall S. Thomas,

real litigation. Instead, suits are brought for their nuisance value and settled for non-monetary relief, typically in the form of supplemental disclosures in the proxy statement. The shareholder class receives nothing, but the lawyers on both sides collect fees from the corporation. Judges no longer decide cases but rather approve settlements, essentially trading their gavels for rubber stamps. The devolution of merger litigation is a concern not only for the shareholders who are made to waive valuable rights for worthless settlements, or for the corporations that fund the perpetual litigation machine. The crisis may be most concerning for corporate law itself, which has been thoroughly discredited in the process.[4]

There is an alternative to regulation by litigation—that is, simply, regulation. The alternative regulatory model thrives on the other side of the Atlantic Ocean where both the United Kingdom and Ireland have adopted a model based on the application of detailed ex ante codes to the conduct of bidders, targets, and other market participants in takeovers and merger transactions. These codes are drafted, interpreted, and enforced by expert panels comprised of bankers, lawyers, institutional investors, and other market professionals. Litigants, courtrooms, and judges are rarely involved. In spite of

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Corporate Darwinism: Disciplining Managers in a World with Weak Shareholder Litigation, 95 N.C. L. REV. 19, 27 (2016) (noting that "litigation against publicly-held companies that undertake deals is now of epidemic proportions"); Jill E. Fisch et al., *Confronting the Peppercorn Settlement in Merger Litigation: An Empirical Analysis and a Proposal for Reform*, 93 TEX. L. REV. 557, 558 (2015) (noting that "[d]eal litigation is pervasive in the United States"); Joel E. Friedlander, *How* Rural/Metro *Exposed the Systemic Problem of Disclosure Settlements*, 40 DEL. J. CORP. L. 877, 883 (2016) ("Disclosure settlement practice has operated as a shadow, parallel legal system within the Court of Chancery competing for judicial resources with a full docket of adversarial litigation. The institutionalization of routine disclosure settlements parodied the procedures for adjudicating claims of breach of fiduciary duty."); Sean J. Griffith, *Correcting Corporate Benefit: How to Fix Shareholder Litigation by Shifting the Doctrine on Fees*, 56 B.C. L. REV. 1, 2 (2015) ("The defects of shareholder litigation have long been known."); Charles R. Korsmo & Minor Myers, *The Structure of Stockholder Litigation: When Do the Merits Matter?*, 75 OHIO ST. L.J. 829, 840-41 (2014) (emphasizing indicia of litigation agency costs in merger class actions and arguing that the merits count for little in such claims); Brian J.M. Quinn, *Shareholder Lawsuits, Status Quo Bias, and Adoption of the Exclusive Forum Provision*, 45 U.C. DAVIS L. REV. 137, 155 (2011) (discussing merger lawsuits as "cookie-cutter complaints"); David H. Webber, *Private Policing of Mergers and Acquisitions: An Empirical Assessment of Institutional Lead Plaintiffs in Transactional Class and Derivative Actions*, 38 DEL. J. CORP. L. 907, 909 (2014) ("The debate over transactional class and derivative actions continues to rage both inside and outside academia."); Marianna Wonder, *The Changing Odds of the Chancery Lottery*, 84 FORDHAM L. REV. 2381, 2382 (2016) (noting that the volume of merger filings and the "similarity between so many of these cases . . . indicates that M&A litigation has become routine, regardless of actual merit"); Matthew D. Cain & Steven D. Solomon, *Takeover Litigation in 2015* (Berkeley Ctr. for Law, Bus. & the Econ., Working Paper, 2017), http://ssrn.com /abstract=2715890 [http://perma.cc/Y9U5-5NGM] (providing empirical evidence of litigation activity and outcomes); Olga Koumrian, *Recent Developments in Shareholder Litigation Involving Mergers and Acquisitions*, CORNERSTONE RES. 1 (2012), http://www.cornerstone.com/files/upload/Shareholder _MandA_Litigation.pdf [http://perma.cc/JF63-GVT4] (providing empirical evidence of litigation activity and outcomes).

4. *See* Transcript of Settlement Hearing at 65-66, Acevedo v. Aeroflex Hldg. Corp., No. 9730-VCL, 2015 WL 4127547 (Del. Ch. July 8, 2015) (No. 9730) (noting that "omnipresent litigation undercuts the credibility of the litigation process" and leads observers to "look askance at stockholder litigation without remembering that stockholder litigation is actually an important part of the Delaware legal framework," ultimately undercutting "Delaware's credibility as an honest broker in the legal realm").

this—or perhaps because of it—these code and panel-based regimes are generally viewed as highly successful: offering flexibility, speed, and certainty at relatively low administrative cost.[5] In light of the success of the Anglo-Irish model, the obvious question becomes whether a similar approach might work in the United States. Remarkably, it has not been tried.

The divergence in regulatory modalities between the United States and the Anglo-Irish systems is especially striking given the similarities between the underlying legal and economic systems. The legal systems in all three countries are based on common law principles. All three countries have highly developed stock markets with dispersed ownership of publicly traded firms.[6] All three take agency costs as the central problem of corporate governance.[7] And all three—especially the United States and the United Kingdom—experience high levels of takeover and merger activity in comparison with other countries.[8] Yet, in spite of the American federal system and its fifty "laborator[ies]" of democracy,[9] each with a strong incentive to compete for corporate charters,[10] no state has yet been tempted to adopt the Anglo-Irish model of merger regulation. Instead, all fifty states apply a form of regulation by litigation.

This Article explores the two models of merger regulation, tracing the development and current operation of each and exploring their relative costs and benefits. This part of our analysis addresses comparative law questions, including how such closely related legal and economic systems developed widely divergent approaches to merger regulation and, more importantly, why these divergent approaches have persisted in an era of convergence and globalization. This comparative analysis is not merely descriptive, but rather serves as a springboard for our larger normative inquiry comparing the relative efficiency of the Anglo-Irish and the U.S. systems. After weighing these considerations in the abstract, we propose a hybrid regulatory model to address the crisis in U.S. merger litigation.

In presenting this account, our Article intersects several lines of scholarly debate. First, in offering an alternative to regulation by litigation, we contribute to the corporate and procedural law literature focusing on how litigation effectively (or ineffectively) serves regulatory objectives, addressing the

5. *See infra* Part II.

6. *See generally* Rafael LaPorta et al., *Corporate Ownership Around the World*, 54 J. FIN. 471 (1999).

7. *See* John Armour et al., *What is Corporate Law?*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 29-31 (Reinier Kraakman et al. eds., 2017) (explaining that the general function of corporate law in terms of controlling conflicts of interest can be understood as a series of agency problems).

8. Of the 23,123 completed public takeovers reported in the ZEPHYR corporate information database as of July 18, 2016, 6,675 (28.87%) took place in the United States and 2,911 (12.59%) took place in the United Kingdom. The reported figure for Ireland was 304.

9. New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932) ("It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.").

10. *See infra* Section IV.A.

promise and peril of ordinary shareholders serving as "private attorneys general."[11] Second, we engage the law and economics literature, analyzing the costs and benefits of alternative models of regulation and applying these to the real world context of shareholder litigation. Third, in addressing why no U.S. state has experimented with a regulatory alternative to merger litigation, we contribute to the corporate law literature on interstate competition for corporate charters, shedding light on how the "race to the top" or "race to the bottom" might actually work. Fourth, we apply insights from the interest group theory of corporate law to highlight the dominance of the corporate bar as the Achilles heel of Delaware corporate law. Fifth and finally, we contribute to the comparative law literature by demonstrating how the form of legal regulation can be as important in determining outcomes as the substance of the rules.

From this Introduction, the Article proceeds as follows. The first half—Parts I and II—is largely descriptive. Part I describes the American system of regulation by litigation through the lens of the dominant producer of American corporate law, Delaware, and analyses the forces leading to the current crisis in shareholder litigation and the state's various efforts to address it. Part II explores the key substantive and procedural features of the code and panel-based modes of merger regulation adopted in the United Kingdom and Ireland, the rationales underpinning their emergence and development, and the experience of those regimes to date. The second half of the Article—Parts III and IV—is more normative. Part III engages the literature comparing the costs and benefits of litigation versus regulation and articulates a code and panel-based system of merger regulation that could be adopted by any state as an alternative to regulation by litigation. Part IV then explores the persistence of the regulation by litigation paradigm in an era of cross-border convergence and globalization, asking why no state has experimented with this alternative regulatory modality, and ultimately identifying the key obstacles that need to be surmounted in order to finally resolve the crisis in U.S. merger litigation. The Article then closes with a brief summary and conclusion.

I. Regulation by Litigation and the Crisis in U.S. Merger Litigation

In the United States, corporate law governs the internal affairs of the corporation—the relationship between shareholders and managers—which is, in general, a matter of state law.[12] U.S. companies can organize in any U.S. state, without regard to residence or principal place of business.[13] As a result,

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11. *See* COFFEE, *supra* note 3.

12. Edgar v. MITE Corp., 457 U.S. 624, 645 (1982); *see also* Frederick C. Tung, *Before Competition: Origins of the Internal Affairs Doctrine*, 32 J. CORP. L. 33 (2006) (explaining the internal affairs doctrine and the role of the states in corporate law).

13. *See* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 212 (1991) ("Managers may incorporate in any state, no matter where the firm's assets, employees, and investors are located.").

corporations effectively choose the state law under which their internal affairs will be governed when they decide where to incorporate.[14] And they overwhelmingly choose Delaware.[15] More than half of all public companies and an even larger share (65.6%) of Fortune 500 companies are incorporated in Delaware.[16]

Corporations choose Delaware for its law, yet the Delaware General Corporation Law contains few mandatory terms.[17] Instead, it is broadly "enabling."[18] Nevertheless, the statute does have a central idea—that is, the conferral of managerial authority upon the board of directors.[19] Shareholders unhappy with management's use of this authority can sell their shares, vote the board out of office, or sue.[20] Hence, insofar as Delaware regulates the internal affairs of American corporations, it does so principally through the shareholder suit. Delaware law, in other words, constitutes regulation by litigation.

This part explores the implications of this regulatory modality, which is shared by every other U.S. state, demonstrating how it has come to police both managerial motives and the adequacy of disclosures in merger transactions. Section I.A reviews shareholder litigation in Delaware, focusing on merger litigation as the paradigmatic example. Section I.B describes the crisis in shareholder litigation in Delaware and the spread of the crisis to other U.S. states. Section I.C reviews attempts by Delaware to address this crisis.

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14. *See* Roberta Romano, *The Market for Corporate Law Redux*, *in* 2 OXFORD HANDBOOK OF LAW AND ECONOMICS 1, 2 (Francesco Parisi ed., 2017) ("This arrangement provides firms with a choice, they can select their governing law from among the states regardless of their physical location; thus the notion that states offer a product that corporations purchase, by means of incorporation fees . . . .").

15. *See, e.g.*, Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 885, 887 (1990) (noting that "over forty percent of the New York Stock Exchange-listed companies and over fifty percent of the Fortune 500 companies" incorporate in Delaware and that "eighty-two percent of the firms that reincorporate move to Delaware"); *see also* Lucian A. Bebchuk & Alma Cohen, *Firms' Decisions Where to Incorporate*, 46 J.L. ECON. 383, 389 (2003); Robert Daines, 62 J. FIN. ECON. 525, 538 (2001) (noting that Delaware leads in a study of IPOs); Roberta Romano, *Law as a Product: Some Pieces of the Incorporation Puzzle*, 1 J.L. ECON. & ORG. 225, 244 (1985) (providing a significant study of re-incorporations and jurisdictional choice of companies).

16. Div. Corps, *Why Incorporate in Delaware?*, ST. DEL., http://corp.delaware.gov [http://perma.cc/Z2PF-EMFD].

17. *See, e.g.*, Bernard S. Black, *Is Corporate Law Trivial?: A Political and Economic Analysis*, 84 NW. U. L. REV. 542, 543 (1990) (arguing that the optional nature of all but the most basic procedural requirements makes the corporate statute "trivial").

18. Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416, 1417 (1989) ("The corporate code in almost every state is an 'enabling' statute.").

19. *See* Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 DEL. J. CORP. L. 673, 675 (2005) ("The central idea of Delaware's approach to corporate law is the social utility of an active, engaged central management. That idea is expressed by our statute, which states the fundamental principle that the 'business and affairs of the corporation are managed by or under the direction of a board of directors.'" (quoting DEL. CODE ANN. tit. 8 § 141(a) (2015))).

20. WILLIAM T. ALLEN ET AL., COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 177 (2d ed. 2007).

A. The Emergence of Delaware Corporate Law

Before Delaware, there was New Jersey. Building upon advantages conferred by the early abolition of special chartering in favor of general incorporation and the state's proximity to both New York City and Philadelphia, New Jersey took the early lead in the interstate market for corporate charters when it passed a series of statutes between 1888 and 1893 that expressly authorized corporations to own shares of other corporations.[21] While New Jersey was not the first state to allow holding companies, the state's unambiguous statutory commitment to the holding company structure offered refuge to transaction planners at a time when business conglomerates were generally under siege.[22] A few years later, in 1896, New Jersey amended its statute to grant corporations the power, with few exceptions, to engage in "any lawful business or purpose whatsoever" and to provide for perpetual corporate existence.[23] Companies flocked to New Jersey in the wake of these amendments,[24] and, by 1900, New Jersey had become the dominant state of incorporation in the United States, especially for large businesses, providing the state with a significant source of revenue.[25] Nevertheless, other states, notably Delaware and Maine, remained competitive by enacting corporate legislation mimicking the New Jersey statute.[26]

Governor Woodrow Wilson destroyed New Jersey's dominance in the market for corporate charters when he insisted on aligning New Jersey corporate law with federal antitrust policy.[27] In 1913, Wilson pushed a series of enactments

21. *See* Charles M. Yablon, *The Historical Race: Competition for Charters and the Rise and Decline of New Jersey: 1880-1910*, 32 J. CORP. L. 323, 331-45 (2007) (discussing the 1889 statute's passage); John C. Brinkerhoff Jr., Note, *Ropes of Sand: State Antitrust Statutes Bound by Their Original Scope*, 34 YALE J. ON REG. 353, 371 n.104 (2017) (discussing the statutes and their effect on New Jersey's competitive advantage). The 1889 statute, the primary source catalyzing the growth in New Jersey's incorporation rate, allowed corporations to "purchase . . . property necessary for their business, *or the stock of any company or companies* owning . . . property necessary for their business." 1889 N.J. Laws 412, 414 (emphasis added).

22. Federal hostility to large-scale mergers and acquisitions was expressed in antitrust (competition) policy. *See* ALFRED D. CHANDLER, JR., THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS 316 (1977); HANS B. THORELLI, THE FEDERAL ANTITRUST POLICY: ORIGINATION OF AN AMERICAN TRADITION 108-232 (1955).

23. An Act Concerning Corporations, 1896 N.J. Laws 277, 279-80 (1896).

24. *See* Yablon, *supra* note 21, at 344-45.

25. Joel Seligman, *A Brief History of Delaware's General Corporation Law of 1899*, 1 DEL. J. CORP. L. 249, 267 (1976) (noting that "95 percent of the nation's major corporations were chartered in New Jersey").

26. *See* Yablon, *supra* note 21, at 358-63.

27. Then-Governor Woodrow Wilson said:

> The corporation laws of the state notoriously stand in need of alteration. They are manifestly inconsistent with the policy of the Federal Government and with the interests of the people in the all-important matter of monopoly, to which the attention of the nation is now so earnestly directed. The laws of New Jersey, as they stand, so far from checking monopoly actually encourage it.

known as the Seven Sister Acts through the legislature, each of which "drastically tightened [New Jersey] law relating to corporations and trusts."[28] The new laws restricted stock issuances, regulated mergers, and, critically, reversed the statutory authorization of the holding company structure, introducing new restrictions on the ability of corporations to hold shares in other business entities.[29]

By 1913, Delaware corporate law was already a substantive copy of New Jersey corporate law.[30] But Delaware did not follow New Jersey in adopting the regulatory framework of the Seven Sisters Acts. Instead, Delaware invited New Jersey corporations to migrate one state south, and the corporations accepted the invitation. It did not matter that New Jersey repealed most of the Seven Sisters provisions in 1917. New Jersey's credibility was destroyed. The corporations stayed in Delaware.

In the wake of the Great Crash of 1929, the federal government assumed a larger regulatory role in corporate affairs, most notably with the enactment of the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act").[31] Broadly speaking, both statutes focus on fraud and disclosure in the securities market, with the Securities Act regulating the primary market—transactions involving a corporate issuer—and the Exchange Act regulating secondary market trading.[32] The creation of regulatory power over these transactions also gave the federal government authority to regulate what might otherwise be viewed as core corporate governance functions—functions previously governed solely by state law. For example, in the merger context, the federal securities laws now prescribe tender offer procedures and the form and content of disclosures provided in connection with shareholder voting.[33] Perhaps most importantly, the federal government could, and many have argued should, subsume all corporate governance regulation.[34] So far, however, it has not gone down this path. As a result, state corporate law remains the principal source of law governing merger activity, a role it performs by means of the shareholder suit.

New Jersey's Corporation Laws, 96 NATION 91 (1913).

28. William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 664 (1974).

29. *See* 1913 N.J. Laws 23-31.

30. *See* Seligman, *supra* note 25, at 271-74.

31. Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74 (codified as amended at 15 U.S.C. § 77(a) (2012)); Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (codified as amended at 15 U.S.C. § 78(a) (2012)).

32. *See* Seligman, *supra* note 25.

33. The Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified as amended at 15 U.S.C. §§ 77-78 (2012)).

34. *See* Santa Fe Indus. v. Green, 430 U.S. 462 (1977); Cary, *supra* note 28.

B. Merger Litigation in Delaware

Although shareholders can sue over almost anything managers do,[35] application of the business judgment rule ensures that they will generally lose.[36] As long as a board is not conflicted, its business decisions are not subject to judicial second-guessing, and shareholder challenges are quickly dismissed.[37] A major exception to this principle, however, occurs when shareholders challenge mergers—a context in which the business judgment rule does not apply. These transactions instead receive a heightened form of judicial scrutiny, either "enhanced scrutiny" or, in the case of clear conflicts, "entire fairness."[38]

Enhanced judicial scrutiny has its origins in one of the first Delaware cases to consider takeover defenses. In 1964, the Court of Chancery heard *Cheff v. Mathes*, a derivative suit challenging a company's actions to ward off a takeover attempt.[39] Although it ultimately favored management, *Cheff* nevertheless highlighted a context—mergers—in which management disinterest could not be casually assumed.[40] This nascent suspicion of management's motives in control transactions later bloomed in the Delaware Supreme Court's 1985 decision in *Unocal v. Mesa Petroleum,*[41] applying enhanced scrutiny to takeover defenses, and the court's 1986 opinion in *Revlon, Inc. v. MacAndrews & Forbes Holdings*,[42] applying enhanced scrutiny to mergers.[43] In either case, the court

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35. *See* Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133 (2004) (explaining that this type of litigation generally occurs in the form of a derivative suit but that when the injury is to the shareholder directly—such as actions impacting voting rights or the consideration received in a merger transaction—shareholder suits may be brought as class actions).

36. *See* Sean J. Griffith, *Good Faith Business Judgment: A Theory of Rhetoric in Corporate Law Jurisprudence*, 50 DUKE L.J. 8, 11-13 (2005) (describing operation of the business judgment rule).

37. *See* Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 83 (2004).

38. Weinberger v. UOP, Inc., 457 A.2d 701, 711-15 (Del. 1983) (requiring fair dealing and fair price in non-arm's length transactions); *see also* Kahn v. M & F Worldwide Corp., 88 A.3d 635, 644 (Del. 2014) (holding that the involvement of a special committee and a majority of the minority vote may shift the standard of review to the business judgment rule). *But see* Transcript of Oral Argument at 20-21, Swomley v. Schlect, No. 9355-VCL (Del. Ch. Aug. 27, 2014), 2014 WL 4470951 (granting a motion to dismiss on the basis of procedural protections and noting that "the whole point of encouraging [the M & F Worldwide] structure was to create a situation where defendants could effectively structure a transaction so that they could obtain a pleading-stage dismissal against breach of fiduciary duty claims").

39. 199 A.2d 548 (Del. 1964).

40. *Id.* at 554 (holding that defensive action was proper, as long as entrenchment was not the board's sole or primary motivation).

41. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) ("Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.").

42. 506 A.2d 173, 185 (Del. 1986).

43. *See* Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 37 (Del. 1993) (incorporating the diffuse-to-controlling shareholder aspect of the standard).

requires the board to justify the transaction in light of shareholder—rather than management—interests.[44]

In addition to heightened judicial scrutiny of management's motives in planning and executing control transactions, Delaware law also provides for judicial scrutiny of the sufficiency of the information provided to shareholders.[45] This cause of action is an implicit corollary to shareholders' statutory right to vote on the transaction.[46] Because the failure to disclose all material information in connection with a transaction effectively deprives shareholders of their statutory voting rights, target boards have an implied duty to disclose.[47] As a result, in addition to policing conflicts of interest, corporate law courts have a role in determining whether the disclosures provided to shareholders are adequate to enable them to make an informed decision on the transaction. Hence, the two principal "regulatory" functions of corporate law courts are to police conflicts of interest in the transaction process and ensure the adequacy of corporate disclosures.[48]

Merger litigation invokes both of these core regulatory functions.[49] Cases are brought on a class basis, often with a single shareholder representing the rights of all shareholders as a class.[50] Complaints begin by using *Revlon* to challenge the merger process, thereby laying the foundation for setting aside the

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44. *See* J. Travis Laster, Revlon *Is a Standard of Review: Why It's True and What It Means*, 19 FORDHAM J. CORP. & FIN. L. 5 (2013); *accord* Reis v. Hazelett Strip-Casting Corp., 28 A.3d 442, 457-60 (Del. Ch. 2011) (describing the range of situations to which enhanced scrutiny may apply). *But see* Stephen M. Bainbridge, *The Geography of* Revlon-*Land*, 81 FORDHAM L. REV. 3277, 3337-38 (2013) (disputing the extension of enhanced scrutiny into non-traditional applications).

45. *See, e.g.*, Stroud v. Grace, 606 A.2d 75, 84 (Del. 1992) ("[D]irectors of Delaware corporations are under a fiduciary duty to disclose fully and fairly all material information within the board's control when it seeks shareholder action.").

46. *See, e.g.*, DEL. CODE ANN. tit. 8, § 251 (2012) (providing for a shareholder vote in a long form merger transaction).

47. *See* Sean J. Griffith, *The Omnipresent Specter of* Omnicare, 38 J. CORP. L. 753, 780-85 (2013) (discussing the implied duty to inform shareholders fully in connection with the merger vote).

48. *See* LARRY E. RIBSTEIN, THE RISE OF THE UNCORPORATION (2010) (treating the fiduciary duties imposed by states on corporate managers as a form of government regulation).

49. Our reference to "merger litigation" here and throughout the Article is to fiduciary duty litigation brought to enforce shareholder rights in the context of merger transactions, not litigation brought to enforce shareholders' statutory appraisal rights. Although implicated by the same underlying transaction, appraisal actions are substantively and procedurally distinct from fiduciary duty claims. We therefore treat appraisal actions and the potential reform of Delaware's approach to appraisal as outside the scope of this article. *See* DEL. CODE ANN. tit. 8, § 262 (2012); *see also,* Charles R. Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 WASH. U. L. REV. 1551 (2015).

50. Because the issues will be common to all shareholders, merger claims can be—and almost always are—brought on a representative basis, typically in the form of a class action. Thompson & Thomas, *supra* note 35, at 168 (reporting the results of a multiyear study of Delaware Chancery Court litigation finding that "[a]lmost all (94 percent: 772 of 824) class action suits arise in an acquisition setting whereas almost all (90 percent: 123 of 137) of the derivative suits arise in a non-acquisition setting"). Formally, class action plaintiffs represent the interest of shareholders as a group, and derivative suit plaintiffs represent the corporation. *See* Griffith, *supra* note 3, at 37-44.

business judgment rule in favor of enhanced judicial scrutiny.[51] But once the provisional proxy statement is released, complaints are amended to incorporate this information and include disclosure allegations. Because the Delaware standard for awarding expedited discovery requires a "colorable claim and . . . a possibility of . . . irreparable injury,"[52] and shareholders can always argue that they will be irreparably injured by the failure to disclose material information prior to the shareholder vote,[53] shareholder plaintiffs are virtually assured of expedited discovery.[54] Unfortunately, this is where the adversarial process typically ends. As explained by the Court in *In re Trulia*:

> Once the litigation is on an expedited track and the prospect of an injunction hearing looms, the most common currency used to procure a settlement is the issuance of supplemental disclosures to the target's stockholders before they are asked to vote on the proposed transaction. The theory behind making these disclosures is that, by having the additional information, stockholders will be better informed when exercising their franchise rights. Given the Court's historical practice of approving disclosure settlements when the additional information is not material, and indeed may be of only minor value to the stockholders, providing supplemental disclosures is a particularly easy "give" for defendants to make in exchange for a release.[55]

Rather than engaging in serious adversarial discovery, the parties settle.

The impetus for settlement is spurred by the hold-up value inherent in every merger claim.[56] Every case, if seriously pursued, has the potential to impose burdensome discovery on defendants and, should unfavorable information be

51. Most complaints arising out of merger transactions allege some defect in the sale process, such as an insufficiently competitive auction or excessive deal-protection discouraging subsequent offers. *See* Koumrian, *supra* note 3, at 1 ("Common allegations include the deal terms not resulting from a sufficiently competitive auction, the existence of restrictive deal protections that discouraged additional bids, or the impact of various conflicts of interests, such as executive retention or change-of-control payments to executives. Complaints also typically allege that a target's board failed to disclose sufficient information to shareholders to enable their informed vote. Insufficient disclosure allegations have focused on information related to the sale process, the reasons for the board's actions, financial projections, and the financial advisors' fairness opinions.").

52. Giammargo v. Snapple Beverage Corp., No. 13845, 1994 WL 672698, at *2 (Del. Ch. Nov. 15, 1994).

53. Sinchareonkul v. Fahnemann, No. 10543, 2015 WL 292314, at *1 n.1 (Del. Ch. Jan. 22, 2015) ("[T]he standard for expedition, colorability, which simply implies a non-frivolous set of issues, is even lower than the 'conceivability' standard applied on a motion to dismiss." (quoting *In re* BioClinica, Inc. S'holder Litig., No. 8272, 2013 WL 5631233, at *1 (Del. Ch. Oct. 16, 2013))); *In re* BioClinica, 2013 WL 5631233, at *4 n.46 ("The standard for a motion to expedite is colorability and the standard for a motion to dismiss under Rule 12(b)(6) is reasonable conceivability–in my view, a higher, although still minimal, pleading burden.").

54. As a result of this argument and the anticipated outcome under the Delaware standard, most defendants agree to some form of expedited discovery. *See* Sean J. Griffith & Anthony A. Rickey, *Objections to Disclosure Settlements: A "How To" Guide*, 70 OKLA. L. REV. 281 (2017).

55. *In re* Trulia, Inc. Stockholder Litig., 129 A.3d 884, 892-93 (Del. Ch. 2016).

56. *See, e.g.*, *In re* Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604, 605 (Del. Ch. 2005) ("[E]ach *Lynch* case has settlement value, not necessarily because of its merits but because it cannot be dismissed.").

unearthed, enjoin the transaction at least until such information can be disseminated to shareholders.[57] Because time is of the essence in most control transactions, defendants regard any potential delay as a serious threat. Moreover, settlement provides defendants with a class-wide release of claims precluding litigation of any claim arising from the same underlying facts, a benefit that the most resonant courtroom victory could not provide.[58] Defendants therefore have an incentive to settle every case, however frivolous.

Intuiting defendants' incentives and the clear pathway to settlement present in every merger claim, plaintiffs' lawyers similarly have little incentive to invest substantial effort in any one case.[59] Instead, they go through the motions, accepting the production of "core documents" from defendants, engaging in desultory "confirmatory discovery," then settling for supplemental disclosures and, of course, attorneys' fees.[60] Because plaintiffs' lawyers can find a client in every major transaction,[61] cases can be—and are—brought against virtually every deal.[62]

C. The Crisis in Shareholder Litigation

The crisis in shareholder litigation is not merely that there is a suit brought against every deal. Nor is it that shareholders obtain no meaningful relief in exchange for the release of potentially valuable litigation rights. Nor is it the "deal tax" imposed upon transacting parties. While these are all aspects of the crisis, the core problem is that merger litigation is not "litigation" at all.[63] Instead, merger litigation has devolved into a non-adversarial process in which attorneys on both sides of the "v" extract rents from corporations and their shareholders. The promise of serious judicial scrutiny over merger transactions has all but disappeared, replaced instead by a system that ensures a source of revenue for the corporate bar.

The most commonly cited statistics demonstrating the crisis in shareholder litigation highlight the frequency of merger litigation. In each year from 2009

57. *See, e.g.*, Fresh Del Monte Produce Inc. v. Del Monte Foods Co., 933 F. Supp. 2d 655 (S.D.N.Y. 2013).

58. Courtroom victory can only result in dismissal as to the named complainants. Because the class is never certified, other shareholders are not precluded from raising the same claims.

59. *See* Friedlander, *supra* note 3, at 909 (explaining that the exception may be cases with a clear potential for monetary recovery, such as controlling shareholder transactions or cases with clear conflicts of interest).

60. *See* Griffith & Rickey, *supra* note 54 (describing the process).

61. Plaintiffs' clients typically come either through a relationship with a public pension fund plaintiff or through advertising to individual shareholders. *See id.* (discussing attorney advertising in the context of merger litigation).

62. *See infra* text accompanying notes 64-68.

63. *Cf.* Polk Cty. v. Dodson, 454 U.S. 312, 318 (1981) ("The system assumes that adversarial testing will ultimately advance the public interest in truth and fairness."); Mackey v. Montrym, 443 U.S. 1, 13 (1979) ("[O]ur legal tradition regards the adversary process as the best means of ascertaining truth and minimizing risk of error.").

through 2015, somewhere between eighty-five and ninety-five percent of all merger transactions valued at over $100 million attracted litigation, in comparison with thirty-nine percent a decade ago.[64] Preliminary evidence suggests that lawsuit filings were down somewhat in 2016, yet they are still roughly twice the historical average.[65]

The frequency of lawsuit filings, taken on its own, does not necessarily prove the existence of a crisis. After all, claims must be filed to get access to discovery, without which prospective litigants cannot know whether they have a valuable claim. A high frequency of litigation activity may thus merely reflect the necessary investigatory effort, after which plaintiffs should presumably pursue strong claims and drop weak ones. However, when the statistics on litigation frequency are combined with the statistics on outcomes, the crisis comes into sharp relief. Most merger claims settle,[66] but the vast majority of these settlements provide no monetary recovery to the plaintiff class.[67] Instead, merger claims typically result in nothing more than supplemental disclosures—so called "disclosure settlements."[68] The shareholders are made to waive their *Revlon* claims at settlement along with any conceivable claim arising from the same underlying facts in exchange for mere words.[69] Moreover, any additional disclosures are typically provided only a few days before the voting deadline, usually in the form of an SEC filing rather than a document disseminated to all

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64. *See* Cain & Solomon, *supra* note 3, at 2.

65. *See* Ravi Sinha, *Shareholder Litigation Involving Acquisitions of Public Companies,* CORNERSTONE RES. 2 (2016), http://www.cornerstone.com/Publications/Reports/Shareholder-Litigation-Involving-Acquisitions-2016.pdf [http://perma.cc/6RPA-L2HB] (reporting first half of 2016 statistics showing that merger suits were filed in 64% of all deals worth over $100 million).

66. Koumrian, *supra* note 3, at 8 (noting that approximately 70% of merger cases settle with the rest being dismissed, and finding that 69% of the 565 suits for which the authors could track the resolution resulted in settlement, while 27% were voluntarily dismissed by plaintiffs, and 4% were dismissed with prejudice); Matthew D. Cain & Steven Davidoff Solomon, *A Great Game: The Dynamics of State Competition and Litigation*, 100 IOWA L. REV. 465, 477 (2015) ("[L]itigation with respect to transactions is dismissed by the court 28.4% of the time. The other 71.6% of transaction litigations result in some type of settlement.").

67. *Id.* at 10 (reporting that nine out of 190 settlements sampled resulted in payments to shareholders, while 82% resulted in disclosure-based settlements); *id.* ("Settlements which only require disclosure constitute 55.1% of the settlement types in the sample and are the most common type of settlement.").

68. A small fraction of settlements (approximately 13%) resulted in changes to the merger agreement, most often to the deal-protection provisions, but none of these changes resulted in a higher bid for the target. Koumrian, *supra* note 3, at 10 ("Other merger agreement changes included the terms of top-up option and appraisal rights. Eleven settlements (6%) involved other terms, most often a delay of the shareholder vote."). Cases resolved for disclosures alone are sometimes referred to as "disclosure only" settlements, while cases resolved for disclosures and additional non-pecuniary relief, such as a reduction in the termination fee, are sometimes referred to as "disclosure plus" settlements. *See* Fisch et al., *supra* note 3, at 586. Here we follow Friedlander in referring to both forms simply as "disclosure" settlements. *See id.*

69. Broad releases can extinguish meaningful claims. For example, *In re Rural Metro Corp.*, 88 A.3d 54 (Del. Ch. 2014), which ultimately resulted in a payment of $93 million to the shareholder class, was first presented to the Court of Chancery as a disclosure settlement. The settlement was rejected over the objection of other shareholders, but many other such settlements may not attract motivated objectors. *See* Griffith, *supra* note 3, at 26 ("There is no way of knowing how many such cases are silently extinguished by a release in a prior shareholder suit.").

holders, and rarely amounts to the kind of information that would cause a rational shareholder to reevaluate the transaction.[70] And indeed, prior research has found no evidence of a shareholder response to supplemental disclosures released in connection with the settlement of merger litigation.[71]

At the root of the crisis in shareholder litigation is the absence of meaningful incentives on either side to protect shareholder rights. Plaintiffs' lawyers seeking disclosure settlements happily trade litigation rights into which they have invested little, if any, real investigative effort. Meanwhile, defense counsel, who also collect fees ultimately funded by shareholders, set up the settlements that result in the abandonment of shareholder rights. The disclosure settlement dynamic may also lead defense counsel to take a more cavalier approach to potentially serious conflicts or other complications. In the words of a prominent member of the Delaware plaintiffs' bar:

> The widespread availability of disclosure settlements created perverse pressures on transactional counsel and defense counsel. Lawyers for target corporations and their fiduciaries, financial advisors and purchasers rationally expected that much M&A litigation can be resolved by means of a disclosure settlement. This knowledge lessened the influence of transactional counsel to uncover or police conflicts of interest while a sale process or transaction is pending and to ensure the prompt, full disclosure of material facts. When litigation began, defense counsel were incentivized to devote their talents to drafting supplemental disclosures amenable to a negotiated resolution, and guiding litigation along a path of least judicial oversight. Successful merits-based litigation by plaintiffs' counsel empowers transactional counsel to avoid, police, and disclose conflicts of interest. Disclosure settlements do not.[72]

The real crisis in shareholder litigation, in other words, is the collapse of the adversarial process. Lawyers don't litigate claims. They negotiate settlements that not only fail to serve shareholders' interests, but also fail to deter managerial misconduct.[73]

Still, before any settlement can become binding on absent class members, the law requires a hearing before a judge who is empowered to reject inadequate or otherwise unfair settlement outcomes.[74] But there is no adversarial interest to

70. *See* Fisch et al., *supra* note 3, at 566.

71. *See id.* (providing an empirical study of shareholder voting patterns in response to supplemental disclosures and finding no statistically significant shareholder reaction to the release of supplemental disclosures in connection with the settlement of merger litigation).

72. *See* Friedlander, *supra* note 3, at 882-83.

73. *See* Griffith, *supra* note 3, at 26 (explaining that the "common perception that such claims lack merit—a view fueled by the high volume of filings and the dearth of significant recoveries—itself diminishes the reputational impact of being made to defend such a suit").

74. Howard M. Erichson, *The Problem of Settlement Class Actions*, 82 GEO. WASH. L. REV. 951, 968-69 (2014) ("What binds the class is not the *agreement* between the defendant and the lead plaintiffs or class counsel, but rather the court's *judgment* approving that agreement. The binding effect of a class settlement, in other words, must be understood as a function of judicial power."); William B. Rubenstein, *The Fairness Hearing: Adversarial and Regulatory Approaches*, 53 UCLA L. REV. 1435,

frame the problem for the judge.[75] Instead, as described by Fiss in his classic polemic, *Against Settlement*, "[t]he contending parties have struck a bargain, and have every interest in defending the settlement and in convincing the judge that it is in accord with the law."[76] Or, as Macey and Miller more colorfully described the problem, settlement hearings are "pep rallies jointly orchestrated by plaintiffs' counsel and defense counsel."[77] Questionable assertions of fact and law are not scrutinized by opposing counsel. Experts are not cross-examined or even questioned. And opposing experts are not presented. Instead, judges acting alone must conduct what amounts to a forensic examination of the proxy statement to determine whether the settlement disclosures materially altered the total mix of information available to shareholders.[78] It would not be surprising if many judges, considering their already crowded dockets, decided to skip the exercise and simply approve the settlement to which the parties have agreed. Busy judges, deprived of adversarial proceedings, make bad gatekeepers.[79]

While class action merger litigation is the paradigmatic example of the crisis in shareholder litigation, derivative suits largely mirror these patterns.[80] Derivative suit filings are common and cluster around public events, often a regulatory investigation, an enforcement action, or a securities filing.[81] Settlement patterns are dictated not by the plaintiffs' investigatory efforts, but by timing considerations of the underlying enforcement or regulatory action. As with merger litigation, cases typically settle for non-pecuniary relief and no monetary recovery to the plaintiffs' class.[82] Only the lawyers get paid. Moreover, although the process theoretically follows Delaware law, proceedings are often brought outside of Delaware.[83]

1444 (2006) ("If class action attorneys sell out their clients, the judge should perceive that the settlement does not live up to the value of the claims and reject it accordingly. Conversely, if class action attorneys file a frivolous case, the judge should perceive that the settlement is merely a nuisance payment, reject it for that reason, and dismiss the case.").

75. Griffith, *supra* note 3, at 21-23 (emphasizing information asymmetries in the settlement hearing).

76. Owen M. Fiss, *Against Settlement*, 93 YALE L.J. 1073, 1082 (1984).

77. Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 46 (1991).

78. Griffith & Rickey, *supra* note 54.

79. *But see* Hillary A. Sale, *Judges Who Settle*, 89 WASH. U. L. REV. 377 (2011) (arguing for a gatekeeping role for judges in settlement).

80. *See* D. Rosenberg & S. Shavell, *A Model in Which Suits Are Brought for Their Nuisance Value*, 5 INT'L REV. L. & ECON. 3 (1985) (discussing nuisance suits as suits that settle after little real litigation activity for a de minimus recovery for the class).

81. *See* Stephen J. Choi et al., *Piling On? An Empirical Study of Parallel Derivative Suits* (U. Mich. Law & Econ., Research Paper No. 16-001, 2017), http://papers.ssrn.com /sol3/papers.cfm?abstract_id=2703509 [http://perma.cc/2CM5-CTZ5].

82. *See* Jessica Erickson, *Corporate Governance in the Courtroom*: *An Empirical Analysis*, 51 WM. & MARY L. REV. 1749 (2010); Macey & Miller, *supra* note 77, at 26.

83. *See, e.g.*, *In re* Walmart Stores, Inc. Del. Derivative Litig., C.A. No. 7455-CB, 2016 WL 2908344 (Del. Ch., May 13, 2016) (holding that a Delaware derivative action was precluded by a dismissal in Arkansas court involving the same underlying facts).

D. Attempts to Address the Crisis

Recognizing the crisis in shareholder litigation, Delaware has moved to address it principally through its judiciary. Attempts to respond to the crisis have included fee shifting bylaws, a heightened standard of review at the fairness hearing, exclusive forum bylaws, and ultimately the hardening of jurisprudential attitudes toward shareholder suits. However, none of these attempts has thus far worked to correct the problem and, worse, the hardening of judicial attitudes toward shareholder litigation may further damage Delaware's system of regulation by litigation by throwing good claims out with the bad.

1. Fee Shifting

The first major effort to address the crisis came when the Delaware Supreme Court suggested, in its 2014 ruling in *ATP Tour, Inc.* v. *Deutscher Tennis Bund*, that corporations could adopt bylaws to shift attorneys' fees and litigation costs to unsuccessful plaintiffs.[84] Delaware corporations, in other words, could use bylaw amendments to adopt "loser pays" rules for shareholder suits.[85] Because most shareholder plaintiffs sue in a representative capacity, forcing the class representative (or her lawyer) to bear the risk of defense-side legal fees would likely deter most shareholder claimants from filing.[86] The *ATP Tour* ruling thus represents a potentially promising strategy for quelling the growth in shareholder litigation.

Precisely for that reason, however, the decision did not stand for long.[87] Instead, the Delaware legislature quickly adopted a statutory provision unambiguously prohibiting any provision that would shift to a shareholder the corporation's fees and expenses incurred "in connection with an internal corporate claim."[88] The reasons for this legislative reversal are explored in greater detail below.[89] For present purposes, it is enough to note that legislation now precludes a fee shifting strategy to correct the crisis in shareholder litigation.[90]

84. *See* 91 A.3d 554, 556 (Del. 2014) (noting the claimant was obligated to pay "all fees, costs, and expenses of every kind and description (including, but not limited to, all reasonable attorneys' fees and other litigation expenses)" of the opposing party in the event that the claimant "does not obtain a judgment on the merits that substantially achieves, in substance and amount, the full remedy sought").

85. *See infra* Section II.D (discussing the indemnity principle in the British and Irish systems).

86. Choi, *supra* note 81.

87. *See infra* text accompanying note 376 (discussing the interest group theory).

88. *See* DEL. CODE ANN. tit. 8, § 109(b); *see also id.* tit. 8, § 115.

89. *See infra* Section III.B.

90. *See, e.g.*, Solak v. Sarowitz, No. 12299-CB, 2016 Del. Ch. LEXIS 194, at *21-22 (Del. Ch. Dec. 27, 2016) (holding that a fee shifting provision, adopted to apply only to extra-forum litigation filed and maintained in contravention of an exclusive forum provision, nevertheless violated the ban on fee shifting provisions in § 109(b)).

2. A Heightened Standard at the Fairness Hearing

After a series of *sua sponte* settlement rejections criticizing plaintiffs for providing no meaningful benefit to the shareholder class,[91] the Court of Chancery in *In re Trulia* clarified that it would apply a heightened standard for the approval of disclosure settlements.[92] Reaffirming the longstanding but inconsistently applied principle of materiality,[93] the *Trulia* court emphasized that

> practitioners should expect that disclosure settlements are likely to be met with continued disfavor in the future unless the supplemental disclosures address a *plainly material misrepresentation or omission* . . . . In using the term "plainly material," I mean that *it should not be a close call that the supplemental information is material* as that term is defined under Delaware law.[94]

In applying a high standard of materiality as a condition for the approval of disclosure settlements, *Trulia* announced that such settlements are no longer welcome in Delaware.

Trulia changed litigation patterns in Delaware and across the United States. As a qualitative matter, Delaware disclosure settlements converted into mootness

91. *See, e.g.*, *In re* Aruba Networks, Inc. Stockholders Litig., No. 10765-VCL, slip op. at 73 (Del. Ch. Oct. 9, 2015) (denying settlement approval and emphasizing that representation is inadequate where counsel files litigation when "there wasn't a basis to file in the first place" but subsequently fails to aggressively litigate when discovery turns up valuable information); *In re* Riverbed Tech., Inc. Stockholders Litig., No. 10484-VCG, 2015 Del. Ch. LEXIS 241, at *20 (Del. Ch. Sept. 17, 2015) (approving settlement but noting that "[i]f it were not for the reasonable reliance of the parties on formerly settled practice in this Court . . . the interests of the Class might merit rejection of a settlement encompassing a release that goes far beyond the claims asserted and the results achieved"); Acevedo v. Aeroflex Holding Corp., No. 9730–VCL, slip op. at 73 (Del. Ch. July 8, 2015) (rejecting a disclosure-only settlement where plaintiffs settled for "precisely the type of nonsubstantive disclosures that routinely show up in these types of settlements"); *In re* Theragenics Corp. Stockholders Litig., No. 8790-VCL, slip op. at 15 (Del. Ch. May 5, 2014) (refusing to approve settlement and noting that "when a fiduciary action settles, I have to have some confidence that the issues in the case were adequately explored, particularly when there is going to be a global, expansive, all-encompassing release given"); Rubin v. Obagi Med. Ptrods., Inc., No. 8433-VCL, slip op. at 7 (Del. Ch. Apr. 30, 2014) (refusing to approve settlement and noting that "there are unknown unknowns in the world, and the type of global release . . . in this case and [similar] disclosure settlements provides expansive protection for the defendants against a broad range of claims, virtually all of which have been completely unexplored by plaintiffs"); *In re* Medicis Pharm. Corp. S'holder Litig., No. 7857-CS, slip op. at 8 (Del. Ch. Feb. 26, 2014) (refusing to approve settlement and noting that "giving out releases lightly is something we've got to be careful about"); *In re* Transatlantic Holdings Inc. S'holders Litig., No. 6574-CS, 2013 WL 1191738 (Del. Ch. Mar. 8, 2013) (refusing to approve settlement for lack of any real investigation, disclosure of additional background information, and in light of the overwhelming vote in favor of the transaction).

92. *In re* Trulia, Inc. Stockholder Litig., 129 A.3d 884 (Del. Ch. 2016).

93. *See* Arnold v. Soc'y for Sav. Bancorp., 650 A.2d 1270, 1277 (Del. 1994); Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985) (adopting standard of *TSC Industries, Inc.* v. *Northway*, *Inc.*, 426 U.S. 438, 449 (1976), that information is material if it significantly alters the total mix of information available); Chrysler v. Dann, 223 A.2d 384 (Del. 1966); Hoffman v. Dann, 205 A.2d 343, 345 (Del. 1964).

94. 129 A.3d at 898-99 (emphases added).

proceedings.[95] And quantitatively, Delaware began to see less merger litigation. This was not because lawyers decided to abandon claims—but because they decided to pursue them elsewhere. In the fourth quarter of 2015 and first half of 2016, the percentage of litigated deals with claims filed in Delaware fell from 61% to 26%.[96] Similarly, in the first half of 2016, complaints involving Delaware-incorporated targets were filed in Delaware just 36% of the time, down from 74% in 2015.[97] During this same period, merger objection lawsuits filed in federal court increased substantially.[98]

The shift of claims to courts in other jurisdictions highlights a fundamental weakness underlying *Trulia* in particular, and with the system of regulation by litigation more generally. Delaware courts can control only what happens in Delaware. Yet shareholders of a Delaware-incorporated company typically can bring suit in Delaware, in the state in which the company is headquartered, and in federal court.[99] Even if Delaware substantive law applies to the underlying claim, there is thus no guarantee that the court in the alternative jurisdiction will follow *Trulia*.[100] Moreover, considering that neither party to the settlement has any incentive to instruct the judge in the alternative forum about the existence of *Trulia*—much less to encourage the judge to follow it—it is possible that judges in other jurisdictions will go on approving disclosure settlements without regard to the decision. Worse, courts in other states may choose not to follow *Trulia* in

95. *See, e.g.*, *In re* Xoom Corp. S'holders Litig., No. 11263-VCG, 2016 WL 4146425, at *5 (Del. Ch. Aug. 4, 2016) (awarding plaintiffs' attorney's fees totaling $50,000 in connection with a mootness dismissal).

96. *See* Sinha, *supra* note 65, at 3.

97. *Id.*

98. *Id.* (finding that merger lawsuits filed in federal court increased by 167% in the second half of 2015); *accord* Stefan Boettrich & Svetlana Starykh, *Recent Trends in Securities Class Action Litigation: 2016 Full Year Review*, NERA ECON. CONSULTING 4-6 (2017), http://www.nera.com/publications/archive/2017/recent-trends-in-securities-class-action-litigation--2016-full-y.html [http://perma.cc/MU3V-XFK4]. The NERA study expressly connects the increase in merger objection claims in federal court to the increased difficulty in reaching disclosure settlements in state court:

> [T]he record number of [federal securities] filings this year was largely attributable to new merger-objection cases, which numbered 88. The jump likely stemmed from federal merger-objection suits that would have been filed in other jurisdictions but for various state-level decisions limiting "disclosure-only" settlements . . . . Mergers and acquisitions (M&A) activity does not appear to be the primary driver of federal merger-objection case counts because the number of federal merger-objection filings generally fell between 2010 and 2015, despite increased M&A activity over this period. In 2016, notwithstanding a 13% year-over-year drop in M&A deals targeting US companies, merger-objection suits doubled from 2015 levels.

Boettrich & Svetlana, *supra*, at 4.

99. *See* Sean J. Griffith & Alexandra D. Lahav, *The Market for Preclusion in Merger Litigation*, 66 VAND. L. REV. 1053, 1066-67 (2013).

100. *See* Sean J. Griffith, *Private Ordering Post-*Trulia*: Why No Pay Provisions Can Fix the Deal Tax and Forum Selection Provisions Can't*, *in* THE CORPORATE CONTRACT IN CHANGING TIMES (Steven D. Solomon & Randall S. Thomas eds., 2017) (providing a comprehensive analysis of inter-jurisdictional dynamics in merger cases).

order to attract litigation to their state.[101] Federal district courts, for their part, have a record both pre- and post-*Trulia* of approving disclosure settlements,[102] but the Seventh Circuit, in an opinion by Judge Posner, did adopt the *Trulia* standard for review of disclosure settlements.[103] It remains to be seen, however, what other federal courts will do. The one thing that is clear, however, is that Delaware courts have literally lost control of the problem.

3. Exclusive Forum Bylaws

Delaware responded to the movement of corporate law litigation to other jurisdictions by explicitly endorsing exclusive forum bylaws—first in judicial rulings, then by statute.[104] Companies can specify Delaware as the exclusive forum for intra-corporate litigation and then move for the dismissal of litigation in the alternative forum as a violation of the exclusive forum provision.[105] However, it now appears that exclusive forum provisions will not solve the crisis in shareholder litigation. The reason, essentially, is that the provision is not self-enforcing. Because defendants retain discretion over whether to invoke the provision, and because defendants have strong incentives to settle merger claims for disclosures or other insubstantial relief, exclusive forum provisions are unlikely to bring merger litigation back to Delaware where, post-*Trulia*, it is harder to settle a case for disclosures.[106]

Defense counsel have been remarkably forthright in counseling clients on preserving their settlement options. As explained by one prominent law firm:

> [A] company may wish to . . . adopt the bylaws now and then eliminate them if it becomes clear that other jurisdictions will continue to approve disclosure-only settlements. Further, a company may wish to adopt the bylaws and then waive them in the context of an approved transaction when the company would prefer

101. *See, e.g.*, Gordon v. Verizon Commc'ns Inc., 148 A.D.3d 146, 159 (2017) (reversing the trial court decision and adopting a standard of "some benefit" for disclosure settlements in the face of Delaware's plainly material standard).

102. *See In re* Meadowbrook Ins. Grp., Inc. S'holder Litig., No. 5:15-CV-10497-JCO-RSW, 2016 WL 8200510 (E.D. Mich. Apr. 7, 2016); Leitz v. Kraft Foods Grp., Inc., No. 3:15-CV-262-HEH, 2016 WL 1043021 (E.D. Va. Mar. 10, 2016); McGill v. Hake, No. 1:15-cv-00217-TWP-DKL, 2015 U.S. Dist. LEXIS 22440 (S.D. Ind. Mar. 10, 2016); Li v. Bowers, 1:15-cv-373 (M.D. N.C., Mar. 22, 2016); Taxman v. Covidien, No. 1:14-cv-12949 (D. Mass., Sept. 21, 2015).

103. *See In re* Walgreen Co. Stockholder Litig., 832 F.3d 718 (7th Cir. 2016).

104. *See* City of Providence v. First Citizens Bancshares, Inc., 99 A.3d 229, 242 (Del. Ch. 2014); Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 936 (Del. Ch. 2013); *see also* DEL. CODE ANN. tit. 8, § 115 (authorizing the certificate of incorporation or bylaws of a Delaware corporation to include a forum selection clause requiring that lawsuits asserting "internal corporate claims," including derivative actions, be brought solely and exclusively in the Delaware courts).

105. *See, e.g.*, Roberts v. TriQuint Semiconductor, Inc., 364 P.3d 328 (Or. 2015) (en banc) (recognizing the validity of the exclusive forum provision).

106. *See supra* Section I.D.2.

> the certainty of a quick resolution over the prospect of lengthier litigation for vindication on the merits.[107]

There is at least one example of a case settling for non-pecuniary relief in an alternative jurisdiction expressly to avoid Delaware.[108] However, looking only at companies that settled in an alternative forum in spite of a previously adopted exclusive forum provision likely underrepresents the full extent of the problem because firms can adopt exclusive forum provisions without shareholder approval at virtually any time.[109] Every firm should thus be regarded as having the provision in place. In light of this, the fact that there are many disclosure settlements outside of Delaware post-*Trulia* can only mean that such outcomes are a revealed preference of defendants.

4. The Hardening of Jurisprudential Standards

Finally, Delaware courts have reacted to the crisis in shareholder litigation through a series of discernable shifts in the underlying jurisprudential standards.

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107. *See Delaware's Effort to Reduce Wasteful M&A Litigation*, FRIED FRANK 5 (Feb. 9, 2016), http://www.friedfrank.com/siteFiles/Publications/Final%20-2-9-2016-MA%20Briefing-Trulia.pdf [http://perma.cc/5TEF-ZU97].

108. The case is the CytRx derivative litigation filed both in Delaware and in federal court in California, where rather than enforcing its exclusive forum provision in favor of Delaware, the defendant asked a California federal court to set aside a prior dismissal of the case in order to settle there. However, the court refused, noting that it was

> skeptical of the Parties' motivation for attempting to settle here. The Delaware Court of Chancery has gained a reputation for rejecting shareholder class action and derivative settlements that do not have a monetary component yet include a broad release of claims and an award of attorneys' fees, similar to the proposed settlement here . . . . It is reasonable to infer that a motivation for seeking vacatur may be to avoid a forum that reviews critically the general type of settlement proposed by the Parties here. This inference is made all the more reasonable by Plaintiffs' counsel's recent failure to receive approval of a non-monetary settlement in the Chancery Court. We cannot ignore the possibility that the current Motion may be an attempt to shop for a more hospitable forum in which to settle the dispute.

In re CytRx Corp. S'holder Derivative Litig., CV-14-6414-GHK-PJW, slip op. at 7-9 (C.D. Cal. Aug. 17, 2016).

109. The problem is analogous to measuring takeover defenses by looking only at firms that have adopted poison pills. As with the poison pill, forum selection bylaws are adopted by unilateral board action. Thus, surveying the number of firms that have adopted the provision fails to count those firms that could have the provision at their disposal in a moment's notice—as soon as the company receives a hostile bid, in the case of a poison pill, or as soon as the company signs a merger agreement or engages in other transactions likely to lead to shareholder suits, in the case of a forum selection bylaw. In the same way that every Delaware company has a "shadow" pill, so every Delaware company should also be regarded as having a "shadow" exclusive forum provision. *See* John C. Coates, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271 (2000); *see also* Emiliano M. Catan, *The Insignificance of Clear-Day Poison Pills* (N.Y.U. Sch. of Law, Working Paper No. 16-33, 2016), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2836223 [http://perma.cc/PSE8-EJ53].

Earlier Delaware cases expressed skepticism of single-bidder auctions,[110] subjected stringent deal protections to rigorous scrutiny,[111] and invalidated contracts made in violation of fiduciary duty.[112] More recent Delaware jurisprudence, however, tolerates single-bidder merger processes, accepts no-shop provisions and other deal protections as routine, places greater emphasis on the contractual rights of bidders, demonstrates a reluctance to issue injunctions, and defers to the stockholder vote as the principal check on deal practice.[113] Although there are several possible reasons for these shifts—including director independence, the de-staggering of boards, and greater involvement of institutional and activist investors—one possible cause is the recognition that older jurisprudential standards may have led to, or at least failed to prevent, the crisis in shareholder litigation.[114]

The watering down of jurisprudential standards in response to the crisis in shareholder litigation implies a failure to distinguish good and bad claims and, ultimately, a failure to police managerial misconduct.[115] The substantive changes described above suggest less protection for shareholders even in the case of genuine managerial failures. Foreclosing litigation in such cases may, in a system of regulation by litigation, pave the way for more self-serving transactions by management and an overall reduction in shareholder welfare.

II. Administrative Regulation and the Anglo-Irish Alternative

In 1887, Oscar Wilde, an Irishman, wrote that the English "have really everything in common with America nowadays, except, of course, language."[116] If he were alive today, he might have added, "and merger regulation." In spite of the strong cultural affinities between British, Irish, and American societies and

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110. *See, e.g.*, Barkan v. Amsted Indus., 567 A.2d 1279, 1287 (Del. 1989) ("A decent respect for reality forces one to admit that . . . advice [of an investment banker] is frequently a pale substitute for the dependable information that a canvas of the relevant market can provide.").

111. *See, e.g.*, Paramount Commc'ns. Inc. v. QVC Network Inc., 637 A.2d 34, 49 (Del. 1994) ("[T]he Paramount Board clearly gave insufficient attention to the potential consequences of the defensive measures demanded by Viacom.").

112. *Id.* at 51 (finding that a sophisticated contracting party "cannot be now heard to argue that it obtained vested contract rights by negotiating and obtaining contractual provisions from a board acting in violation of its fiduciary duties").

113. *See* J. Travis Laster, *Changing Attitudes: The Stark Results of Thirty Years of Evolution in Delaware M&A Litigation* 27 (unpublished manuscript) (on file with author) (analyzing the Delaware Supreme Court's decision in *C & J Energy Services, Inc. v. Miami General Employees' & Sanitation Employees' Retirement Trust*, 107 A.3d 1049 (Del. 2014), as a paradigmatic example of this shift).

114. *Id.* at 44-47 (documenting "the avalanche of lawsuits produc[ing] comparably minimal value for stockholders"); *accord* Joel E. Friedlander, *Vindicating the Duty of Loyalty: Using Data Points of Successful Stockholder Litigation as a Tool for Reform* 45-51 (U. Penn. Inst. for Law & Econ., Research Paper No. 17-1, 2016) (criticizing the expansion of the business judgment rule as a means of controlling nuisance litigation).

115. *See id.* at 51 (warning that overzealous application of the business judgment rule "creates an incentive for controllers to commit fraud").

116. OSCAR WILDE, THE CANTERVILLE GHOST 6 (2011).

the deep structural similarities between their legal and economic institutions—common law legal systems, developed stock markets, dispersed ownership, and active takeover markets[117]—these countries have chosen two sharply divergent approaches to regulating merger activity.[118] While the United States has steadfastly pursued a system of regulation by litigation, the United Kingdom and Ireland have successfully experimented with a system based around expert panels of market professionals applying codified bodies of rules that govern transactions as they unfold. These code and panel-based regimes have largely supplanted litigation in the context of public takeover bids. In the Anglo-Irish system, takeover panels effectively preside over what in the United States are the core preoccupations of judges in merger suits: the conduct of the sale process, the adequacy of disclosure to shareholders, and the permissible role of the target board in responding to takeover bids.

This Part describes the core features of the Anglo-Irish model of merger regulation. It frames the important differences between this model and the U.S. system of regulation by litigation as a function of divergent institutional interests and structural constraints operating on either side of the Atlantic. These code and panel-based regimes, along with a concomitant set of procedural rules discouraging entrepreneurial litigation, work to constrain the development of shareholder litigation while still protecting shareholder rights in merger transactions.

A. *The Emergence of Anglo-Irish Takeover Regulation*

The approach to merger regulation in the United Kingdom and Ireland grew out of a longstanding tradition of self-regulation in financial markets. The preference for self-regulation implied a particular model of regulation. Because both government intervention and the imposition of jurisprudential standards are antithetical to self-regulatory norms, the Anglo-Irish system adopted a system whereby expert panels of market participants wrote, interpreted, and enforced a set of rules agreed among the participants themselves. The development of this system is described in greater detail below.

Public takeover bids appeared in the United Kingdom in the early 1950s. These first bids reflected the confluence of several factors, including post-war inflation on real estate and other fixed assets, dividend restrictions on public companies, and improvements in financial reporting.[119] The emergence of public

117. *See supra* notes 6-10 and accompanying text (reviewing the economic and legal similarities between the United States, United Kingdom, and Ireland).

118. *See* Paul Davies & Klaus Hopt, *Control Transactions*, in THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH, *supra* note 7, at 225 (describing the different policy choices of the United States and United Kingdom in the area of mergers, acquisitions and other control transactions).

119. *See* John Armour et al., *The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets*, 52 HARV. INT'L L.J. 219, 233 (2011); Les Hannah, *Takeover Bids in Britain Before 1950: An Exercise in Business 'Pre-History,'* 16 BUS. HIST. 65 (1974); Andrew Johnston,

takeover bids during the 1950s and 1960s represented a clear threat to the directors and management of target companies. Target boards responded with a range of defensive tactics. High profile examples include the takeover contests for the Savoy Hotel and British Aluminium.[120]

In the contest for the Savoy, the bidder sought to acquire the target in order to convert one of its flagship properties, The Berkeley Hotel, into commercial offices.[121] The target board responded with a classic "lock-up" defense: transferring ownership of The Berkeley to a shell corporation whose voting shares were then allotted to the trustees of the Savoy's employee pension fund, one of whom was the chairman of the target board. This strategy proved highly controversial, with many Savoy shareholders viewing it as depriving them of their right to consider the bid on its merits. This view was subsequently affirmed by the U.K. Board of Trade,[122] which issued a report concluding that the board's actions were invalid as they had the effect of irrevocably denying any future owner of the ability to sell or alter the use of The Berkeley.[123]

The contest for British Aluminium was even more controversial.[124] The controversy began when two prospective bidders privately approached the target board: one a partnership between Tube Investments and Reynolds Metal Company ("TI-Reynolds"), the other the Aluminum Company of America ("Alcoa"). Without publicly disclosing either approach, the board rejected the TI-Reynolds bid and agreed to a deal that involved the issuance of a significant number of new shares to Alcoa.[125] When it became clear that TI-Reynolds planned to make a direct offer to shareholders, the target board then disclosed the earlier approaches and sought to secure shareholder approval for the Alcoa deal by increasing the firm's dividend.[126] The revelation of the board's decision to issue a block of new and undervalued shares to Alcoa attracted significant opprobrium from shareholders, many of whom sold out to TI-Reynolds.[127]

Takeover Regulation: Historical and Theoretical Perspectives on the City Code, 66 CAMBRIDGE L.J. 422, 426-27 (2007).

120. *See generally* Richard Roberts, *Regulatory Responses to the Rise of the Market for Corporate Control in Britain in the 1950s*, 34 BUS. HIST. 183, 187 (1992) (describing the early English jurisprudence arising in connection with the emergence of public takeover bids).

121. *See* Laurence C.B. Gower, *Corporate Control: The Battle for the Berkeley*, 68 HARV. L. REV. 1176 (1955) (providing a more detailed description of the takeover contest for the Savoy).

122. The Board of Trade was the predecessor to the current Department for Business, Energy and Industrial Strategy.

123. *See* BD. OF TRADE, THE SAVOY HOTEL LIMITED AND THE BERKELEY HOTEL COMPANY LIMITED: INVESTIGATION UNDER SECTION 165(B) OF THE COMPANIES ACT, 1948: REPORT OF EDWARD M. HOLLAND, Q.C. (1954).

124. For a more detailed description of the takeover contest for British Aluminium, see Armour et al., *supra* note 119, at 235; and John Armour & David A. Skeel, *Who Writes the Rules for Hostile Takeovers and Why?: The Peculiar Divergence of US and UK Takeover Regulation*, 95 GEO. L.J. 1727, 1758 (2007).

125. *See Battle for British Aluminium*, ECONOMIST, Dec. 6, 1958, at 913.

126. *See Statement of the British Aluminium Board*, TIMES LONDON, Dec. 6, 1958, at 11; *British Aluminium Reveals Contract with Alcoa*, TIMES LONDON, Nov. 29, 1958, at 12.

127. *See British Aluminium: A Reply Under Pressure*, ECONOMIST, Dec. 27, 1958; *Letters to the Editor*, TIMES LONDON, Dec. 11, 1958; *Letters to the Editor*, TIMES LONDON, Jan. 9, 1959.

Indeed, the shareholder reaction to the board's conduct was so powerful that a number of other public companies committed not to issue new shares without prior shareholder approval.[128]

The controversies surrounding the takeover contests for the Savoy and British Aluminium provoked widespread calls for regulation prescribing the range of actions that target boards would be permitted to take in response to takeover bids.[129] In July 1959, the Bank of England responded by convening a committee representing large commercial banks, merchant banks, and institutional investors, along with the London Stock Exchange, to draft a set of rules governing the conduct of takeover bids.[130] The result was the *Notes on Amalgamation of British Businesses* ("*Notes*"), a series of principles, supplemented by procedural rules, "concerned primarily to safeguard the interests of shareholders."[131] These principles emphasized, for example, that there should be no interference in the free market for shares, that shareholders should receive sufficient information, and that it was up to shareholders—not the target board—to decide on the merits of a bid.[132] The obligation of the target board to provide information to shareholders represented a significant change from the common law position, which did not require the board to provide information to assist shareholders in evaluating the bid.[133] The *Notes* are thus credited with articulating the basic principle of shareholder primacy that survives in the United Kingdom to this day.[134]

Ultimately, the *Notes* proved less than successful as a mechanism for constraining abuse within the U.K. takeover market. As a preliminary matter, the principles provided by the *Notes* were often extremely vague: suggesting, for example, that "every effort" should be made to avoid market disturbance, that shareholders should be given "adequate time (say three weeks)" for accepting an offer, and that it was "desirable" that the offer be made for all of the target's outstanding shares.[135] Perhaps more importantly, there was no oversight body responsible for monitoring or enforcing compliance with the *Notes*.[136]

By the late 1960s, the use of defensive tactics—combined with the relative impotence of the *Notes*—was also beginning to provoke shareholder litigation.

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128. *British Aluminium Reply*, TIMES LONDON, Dec. 20, 1958, at 9.

129. *See* Armour & Skeel, *supra* note 124, at 1758; Armour et al., *supra* note 119, at 236; David Kershaw, *Corporate Law and Self-Regulation* 12 (London Sch. of Econ. Law, Soc'y & Econ., Working Paper No. 05/2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2574201 [http://perma.cc/4YS4-MXLD].

130. *See* LOUISE GULLIFER & JENNIFER PAYNE, CORPORATE FINANCE LAW: PRINCIPLES AND POLICY 568 (2015); Armour et al., *supra* note 119, at 236.

131. *See* Armour & Skeel, *supra* note 124, at 1759.

132. *See* Johnston, *supra* note 119, at 432.

133. *See In Re* Evertite Locknuts Ltd., [1945] Ch D 220 (UK).

134. *See* Armour & Skeel, *supra* note 124, at 1759.

135. *See* Kershaw, *supra* note 129, at 13.

136. *See* Armour & Skeel, *supra* note 124, at 1759.

The leading case from this period is *Hogg* v. *Cramphorn*.[137] Citing a long line of precedents, the court held that the defensive tactics in question were voidable because their primary purpose was to thwart a potential takeover bid. The court's reasoning in *Hogg* thus echoed the "sole or primary purpose" test enunciated in *Cheff v. Mathes*,[138] decided in Delaware at approximately the same time.[139] Importantly, like *Cheff v. Mathes*, the test in *Hogg* necessitated a fact-driven investigation into the board's motives for adopting defensive tactics. From the perspective of bidders and target shareholders, therefore, applying to a court for relief was likely to be a time consuming, costly, and uncertain process.[140]

The influence of *Hogg* as a precedent for future cases was largely forestalled by the introduction of the *City Code on Takeovers and Mergers* ("City Code").[141] The introduction of the City Code is generally viewed as a response to two related threats to the City's shareholder-friendly reputation. The first was the threat of government intervention following a spate of high profile takeover disputes in the late 1960s. These disputes reinforced the perception that the *Notes* were an ineffective mechanism for constraining abusive conduct and practices.[142] The second was the delay and uncertainty associated with the common law approach to the resolution of these disputes as embodied by the court's decision in *Hogg*.[143] For the second time in less than a decade, the Bank of England responded by convening a committee of bankers, institutional investors, and other market participants. On March 28, 1968, the committee unveiled the new City Code: a collection of ten general principles supplemented by thirty-five more detailed rules governing the U.K. public takeover market. Like its predecessor, the City Code was drafted by market participants concerned primarily with protecting the interests of target shareholders. The key difference in terms of the effectiveness of the City Code relative to the *Notes* was the creation of the U.K. Panel on Takeovers and Mergers.[144]

The United Kingdom's decision to adopt a self-regulatory code and panel-based takeover regime can be attributed to two principal factors. The first was

137. Hogg v. Cramphorn, [1967] 1 Ch 254, 266-67 (UK) (citing Piercy v. Mills, [1920] 1 Ch. 77 (UK), and Fraser v. Whalley (1864) 71 Eng. Rep. 361; 2 H & M 10).

138. 199 A.2d 548 (Del. Ch. 1964).

139. *See supra* text accompanying notes 39-40.

140. *See* Johnston, *supra* note 119, at 436.

141. PANEL ON TAKEOVERS & MERGERS, THE TAKEOVER CODE 2016 [hereinafter City Code]; Johnston, *supra* note 119, at 441. This is not to suggest that the introduction of the City Code completely forestalled the development of subsequent case law in this area. *See* Criterion Props. plc v. Stratford Props. UK plc, [2004] UKHL 28, 1 W.L.R. 2108; Howard Smith v. Ampol Petroleum, [1974] AC 821 (PC).

142. *See* Armour & Skeel, *supra* note 124, at 1759; Kershaw, *supra* note 129, at 16. This threat was notably framed in terms of the creation of a British Securities and Exchange Commission. *See The Case for a British SEC*, ECONOMIST, Jan. 7, 1967; *Back to the Jungle*, ECONOMIST, July 22, 1967.

143. *See* Johnston, *supra* note 119, at 442-44.

144. *See* John Armour et al., *A Comparative Analysis of Hostile Takeover Regimes in the US, UK and Japan (with Implications for Emerging Markets)* 18 (Colum. Law & Econ., Working Paper No. 377), http://ssrn.com/abstract=1657953 [http://perma.cc/R7FM-WRJJ].

the United Kingdom's longstanding tradition of self-regulation.[145] Perhaps nowhere has this tradition been more observable than in connection with the regulation of financial markets.[146] Indeed, before the dramatic structural changes introduced by the so-called "Big Bang"[147] and the enactment of the Financial Services Act of 1986,[148] the United Kingdom relied almost exclusively on market participants, customary understandings, and moral suasion on the part of the Bank of England as sources of financial regulation. The second factor was the influence of institutional shareholders. Insurance companies, pension funds, and other institutional investors began accumulating significant stakes in U.K. public companies long before the same trend emerged in the United States. Between 1957 and 1969, the percentage of U.K. share ownership by institutional investors more than doubled from under 20% to approximately 45%.[149] As demonstrated by the impact of their rebuke of the board's conduct in the takeover contest for British Aluminum, along with their subsequent role in the development of the *Notes* and City Code, the rise of institutional shareholders in the United Kingdom enabled them to exert coordinated influence over the regulatory environment in which public companies operated.[150] As these shareholders began to perceive that common law courts would prove too slow, too unpredictable, and potentially afford inadequate protection to their interests, they found themselves in an advantageous position to leverage this influence to shape the substantive obligations enshrined in the City Code. Importantly, the speed, certainty, and level of protection that institutional shareholders desired also suggested a particular mode of merger regulation: an expert panel responsible for writing, interpreting, and enforcing a set of detailed rules, in real time, and with limited recourse to courts.

The U.K. Takeover Panel operated as a self-regulatory body until 2006,[151] when the Companies Act of 2006 codified the City Code and provided the U.K.

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145. *See* Rob Baggot, *Regulatory Reform in Britain: The Changing Face of Self-Regulation*, 67 PUB. ADMIN. 435, 442-43 (1989).

146. BRIAN R. CHEFFINS, COMPANY LAW: THEORY, STRUCTURE AND OPERATION 365-66 (1997); LAURENCE GOWER, REVIEW OF INVESTOR PROTECTION: A DISCUSSION DOCUMENT (1982).

147. "Big Bang" (never "the Big Bang") refers to the October 27, 1986 restructuring of the London Stock Exchange (LSE). Formerly a private and autonomous association, Big Bang brought the LSE within the scope of the Financial Services Act 1986, abolished minimum commissions, and eliminated the longstanding distinction between stockbrokers and stockjobbers. Big Bang also saw the removal of restrictions respecting the organization and ownership of LSE member firms, thus facilitating the acquisition of significant interests in members by other financial intermediaries for the first time.

148. Financial Services Act 1986, c. 60 (UK).

149. Armour & Skeel, *supra* note 124, at 1769.

150. *See* G.P. STAPLEDON, INSTITUTIONAL SHAREHOLDERS AND CORPORATE GOVERNANCE, at chs. 3, 4, 5 (1996); Armour & Skeel, *supra* note 124, at 1793-94; Bernard S. Black & John C. Coffee, Jr., *Hail Britannia?: Institutional Investor Behavior Under Limited Regulation*, 92 MICH. L. REV. 1997, 2035-36 (1994).

151. In 2006, the United Kingdom implemented the European Union Takeover Directive, which was in large part modeled on the City Code. Directive 2004/25/EC, of the European Parliament and of the Council of 21 April 2004 on Takeover Bids, 2004 O.J. (L 142) 12. Ultimately, the United Kingdom provided statutory underpinning for the U.K. Panel in order to ensure full implementation of the Takeover Directive. *See* Blanaid Clarke, *The Takeovers Directive: Is a Little*

Panel with a range of formal powers.[152] Today, the City Code is organized around six General Principles,[153] thirty-eight rules, and comments providing guidance on each rule. The notes are of considerable importance and, in many cases, are treated as prescriptive by the Panel.[154] The City Code applies to all offers made for companies that have their registered office in the United Kingdom whose securities have been admitted for trading on a regulated market or multilateral trading facility in the United Kingdom.[155] The primary purpose of the City Code is to ensure that target shareholders are treated fairly, afforded equivalent treatment by bidders, and not denied an opportunity to decide on the merits of a bid. Ultimately, however, neither the City Code nor the U.K. Panel are concerned with value judgments as to the merits of a bid.

In Ireland, the U.K. Panel regulated takeover offers for registered companies until 1997. In response to incoming EU legislation, the Irish Stock Exchange withdrew from the International Stock Exchange of the United Kingdom and Republic of Ireland in 1995. As a result, the continued oversight of Irish listed companies by the U.K. Panel was no longer appropriate. However, the Irish experience with the U.K. Panel had been very positive. As such, there was a preference to retain a self-regulatory system modeled on the U.K. Panel. At the same time, it was felt that statutory powers were required in order to ensure the effectiveness of the new regime. The Irish Panel was thus established as a statutory body pursuant to the Irish Takeover Panel Act of 1997 ("Takeover Act").[156]

The Irish Panel regulates the conduct of takeovers of Irish registered companies listed on the Irish Stock Exchange, London Stock Exchange, New York Stock Exchange, or Nasdaq ("relevant companies").[157] The inclusion of companies listed on U.S. exchanges has meant that approximately one-quarter of the eighty companies overseen by the panel are former U.S. companies that

Regulation Better Than No Regulation?, 15 EUR. L.J. 174, 177 (2009); Blanaid Clarke, *Takeover Regulation: Through the Regulatory Looking Glass* 6 (Comparative Research in Law & Political Econ., Research Paper No. 18/2007), http://ssrn.com/abstract=1002675 [http://perma.cc/M5CV-RN9E].

152. Companies Act 2006, c. 46 § 954 (UK).

153. These five General Principles are the same principles that are set out in Article 3 of the Directive.

154. The Appendices contain more detailed guidance notes on specific issues such as mandatory bid waivers and auction procedures. Thirty practice statements on controversial issues such as shareholder activism and irrevocable undertakings are also appended to the Code.

155. City Code, *supra* note 141, § 3(a)(i), at A3. The City Code also applies to certain offers where: (i) the takeover panel considers the target firm as having its central management and control in the United Kingdom, *id.* § 3(a)(ii)), or (ii) the United Kingdom shares jurisdiction with another jurisdiction in the European Economic Area, *id.* § 3(a)(iii). The City Code also applies to certain companies supervised by the U.K. Panel by virtue of Article 4 of the E.U. Takeover Directive.

156. Irish Takeover Panel Act 1997 (Act No. 5/1997) (Ir.), http://www.irishstatutebook.ie/eli/1997/act/5/enacted/en/html [http://perma.cc/Z9NK-LFMC] [hereinafter 1997 Takeover Panel Act]; *see also* BLANAID CLARKE, TAKEOVERS AND MERGERS LAW IN IRELAND, at ch. 3 (1999) (providing a description of the background to the introduction of the 1997 Takeover Panel Act).

157. The Irish Panel may also be responsible for supervising certain other EU companies by virtue of Article 4(2) of the EU Takeover Bids Directive 2004/25/EC.

have undergone corporate inversions or restructurings. The ownership of these companies tends to be dominated by foreign shareholders, with the management and lead advisers in connection with any takeover also likely to be from outside Ireland. Between July 2012 and June 2016, six of the thirteen takeovers supervised by the Irish Panel involved U.S. listed companies.[158] Although Irish law applies to these transactions, the U.S. listings, large U.S. shareholder bases, and the residency of many of the principal parties have ensured that the SEC and U.S. courts have also played a role in these transactions.

The Takeover Act sets out seven General Principles applicable to the conduct of takeovers, the first six of which are identical to those contained in the City Code.[159] The Irish Rules promulgated under the Takeover Act are similarly based substantially on those in the United Kingdom.[160] While not a self-regulatory body, the Takeover Act imbues the Irish Panel with significant flexibility, allowing it, for example, to waive or derogate from any of the Irish Rules in exceptional circumstances.[161] Although most of the initial differences with the City Code could be attributed to the statutory nature of the Irish Rules, a small number of disparities have since arisen in the regulation of various issues. Ultimately, however, the objectives of the Irish Rules are the same as those of the City Code,[162] and neither the Irish Rules nor Panel are concerned with the merits of a bid.

B. The City Code and the Irish Rules

In the United States, bidders enjoy a great deal of freedom in the context of public takeover bids. Target companies are likewise free to erect procedural barriers to these bids, subject only to the board's fiduciary duties and the requirement that takeover defenses be "reasonable in relation to the threat posed."[163] The City Code and Irish Rules, in contrast, add to these fiduciary duties prescriptive rules governing almost every aspect of the conduct of both bidders and target companies. These rules prescribe, among other matters: the timetable for bids; the content of announcements, offering documents, and management circulars; restrictions on dealing in target shares; the nature of bid consideration; the use of conditional bids; agreements with target management; the circumstances in which target boards will be required to seek independent advice; and the role and duties of financial advisers.

158. *See Annual Reports 2012-2017*, IRISH TAKEOVER PANEL App. 2, http://irishtakeoverpanel.ie/about/annual-reports [http://perma.cc/H9TY-PSVV].

159. City Code, *supra* note 141, General Princ., at B1. The seventh principle regulates substantial acquisitions of securities which are no longer regulated by the U.K. Panel.

160. IRISH TAKEOVER PANEL, TAKEOVER RULES AND SUBSTANTIAL ACQUISITION RULES, 2013, (Ir.) [hereinafter Irish Rules].

161. 1997 Takeover Panel Act, *supra* note 156, § 8(7).

162. Irish Rules, *supra* note 160, Intro., at 1.

163. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985).

From the perspective of our comparison with the U.S. model of regulation by litigation, four sets of rules stand out as particularly important. The first relates to the timetable of the offer, which is strictly regulated in the United Kingdom and Ireland. Once a bidder has announced a firm intention to make an offer, in general, it must post a formal offer to shareholders within twenty-eight days[164] and have the offer accepted within a further sixty days.[165]

The second important set of rules relates to the financial and other information that bidders and target boards are required to provide target shareholders. General Principle 2 states that "[t]he holders of the securities of an offeree company must have sufficient time and information to enable them to reach a properly informed decision on the bid."[166] This principle is fleshed out by a series of more detailed rules identifying the information that must be provided to shareholders. Information that must be disclosed by the bidder includes audited accounts; strategic plans for the target firm; the bidder's intentions with regard to the target's business, employees, and pension schemes;[167] a description of the relevant financing arrangements; and any interests or dealings of the bidder, its directors, or those acting in concert in the securities of the target.[168] Target boards, meanwhile, are required to provide shareholders with a circular setting out the board's opinion on the bid, including its views on the impact of the proposed merger on the firm's interests, employment, and the location of the firm's place of business. All information tendered by a bidder or target must be made equally available to all shareholders as nearly as possible to the same time and in the same manner.[169] These detailed requirements are then augmented by a more general duty on bidders, target boards, and their advisers to ensure that each document, announcement, statement, or other information released during the course of a bid complies with the highest standards of care and accuracy.[170] Further, all documents and advertisements published in connection with the offer must contain statements to the effect that the directors of the bidder or target (as applicable) accept responsibility for the information contained therein and that it is, to the best of their knowledge, accurate and complete.[171]

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164. City Code, *supra* note 141, r. 24.1, at J2; Irish Rules, *supra* note 160, r. 30.2(a), at 9.2.

165. City Code, *supra* note 141, r. 31.6, at N3; Irish Rules, *supra* note 160, r. 31.4, at 9.4.

166. City Code, *supra* note 141, General Princ., at B1; Irish Rules, *supra* note 160, r. 23, at 7.3.

167. The Irish Rules do not explicitly refer to pensions.

168. City Code, *supra* note 141, r. 24, at J2; Irish Rules, *supra* note 160, r. 24, at 7.4.

169. City Code, *supra* note 141, r. 20.1, at I9; Irish Rules, *supra* note 160, r. 20.1(a), at 6.10.

170. City Code, *supra* note 141, r. 19.1, at I1; Irish Rules, *supra* note 160, r. 19.1, at 6.2 (helping to avoid acrimonious disputes between the parties, as only where a statement is expressly stated to be an opinion may it be included without verification and a statement of source).

171. City Code, *supra* note 141, r. 19.2, at I2; Irish Rules, *supra* note 160, r. 19.2, at 6.2.

The third set of rules impose significant constraints on the range of actions that target boards can take in response to a takeover bid. The most important of these constraints—especially in comparison with the position in the United States—is the "no frustration" rule. General Principle 3 states that "[t]he board of an offeree company must act in the interests of the company as a whole and must not deny the holders of securities the opportunity to decide on the merits of the bid."[172] Rule 21 gives effect to this principle by prohibiting target boards from taking any action that may result in the frustration of a bid, or deprive shareholders of the opportunity to decide on its merits, without first obtaining shareholder approval.[173] This prohibition encompasses (but is not limited to) the creation or issuance of shares, options, or other rights in connection with the target's shares (e.g. "poison pills"), the acquisition or disposal of material assets (e.g. "lock up" defenses), and the entering into of any contract other than in the ordinary course of business.[174] Following Kraft's successful takeover bid for Cadbury in 2011, the scope of the prohibition in the City Code was expanded to include, subject to very narrow exceptions, break fees, inducement fees, and other deal protection measures.[175] In Ireland, such potentially defensive measures are still permitted subject to panel consent.[176] In marked contrast with the United States, the role of target boards in defending against a takeover bid is thus limited to the identification of potential alternative bidders—so called "white knights"—and to persuading shareholders that the bid does not fully reflect the value of the firm. Perhaps most importantly for the present purposes, the no frustration principle substitutes a bright line rule constraining defensive action for the fact-driven common law test articulated in *Hogg*.[177]

The City Code's prohibition against frustrating action is also reflected in the U.K. Panel's approach toward tactical litigation. The U.K. Panel has referred to tactical litigation for the purposes of preventing a bid from being considered on its merits as "highly undesirable and potentially gravely damaging to the orderly conduct of bids" [178] and something the shareholders should have an opportunity to consider and vote upon at a general meeting. It is presently not clear whether the Irish Panel would adopt a similar approach to tactical litigation.

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172. City Code, *supra* note 141, General Princ. 3, at B1.

173. *Id.* R. 21.1(a), at I18; Irish Rules, *supra* note 160, r. 21.1(a), at 6.14.

174. City Code, *supra* note 141, r. 21.1(b), at I18; Irish Rules, *supra* note 160, r. 21.1(a), at 6.14 (explaining that the panel may consent to an otherwise restricted action if the action relates to a pre-existing obligation, or if a decision to take the proposed action was taken before the offer was imminent and that decision has either been partly or fully implemented or is in the ordinary course of business).

175. City Code, *supra* note 141, r. 21.2, at I21.

176. Irish Rules, *supra* note 160, r. 21, at 6.14-15 (explaining that consent will generally only be given in connection with arrangements covering specific quantifiable third party costs, subject to an upper limit of one percent of the value of the bid and confirmation by the target's financial adviser that the arrangement is in the shareholders' best interests).

177. *See* TAKEOVER PANEL, CONSOLIDATED GOLD FIELDS PLC, 1989, at 9 (UK) (acknowledging and disapproving of the use of tactical litigation itself as a defensive tactic).

178. *Id.*

On the one hand, preventing a board from taking legal action might be viewed as a breach of the company's constitutional right to access to the courts.[179] On the other hand, Rule 21 does not represent an outright prohibition against frustrating action, but simply a requirement that shareholder approval be obtained before any action is taken.

The prohibition against frustrating action is only triggered during the course of an offer or at any earlier time at which the board has reason to believe that a bona fide offer may be imminent.[180] However, even where no bid is imminent, target boards in the United Kingdom and Ireland still face a number of significant constraints on their ability to proactively implement defensive measures. Under the U.K. Companies Act 2006 and Irish Companies Act 2014, for example, the issuance of new shares necessary to implement a poison pill would require shareholder authorization.[181] Shareholders also possess the mandatory right to remove directors by ordinary resolution, thereby rendering staggered boards an ineffective entrenchment mechanism.[182] In theory, of course, defensive action might also constitute a breach of the directors' duties to act in the interests of the company[183] and to exercise their powers for proper purpose.[184]

The prohibition against frustrating action places severe constraints on the ability of a target board to take any actions in response to a takeover bid that might conflict with the interests of shareholders. This prohibition is supplemented by a fourth set of rules dealing more specifically with conflicts of interest. Rule 3.1 requires a target company to obtain independent advice regarding whether the financial terms of any offer are fair and reasonable and to disclose this advice to shareholders.[185] Rule 3.2 imposes an equivalent obligation on bidders in the context of reserve takeovers or where the directors face a conflict of interest.[186] The financial advisers providing this advice must similarly not have a significant interest in, or connection with, either the bidder or target

179. McCauley v. Minister for Posts & Teles. [1966] IR 345 (Ir.) (recognizing that companies have this right).

180. City Code, *supra* note 141, r. 21.1, at I18; Irish Rules, *supra* note 160, r. 21.1, at 6.14.

181. Companies Act 2006, *supra* note 152, c. 46, §§ 549-551; Companies Act 2014 (Act No. 38/2014), § 1021 (Ir.), http://www.irishstatutebook.ie/eli/2014/act/38/enacted/en/html [http://perma.cc/PC3Z-MCJM] [hereinafter Companies Act 2014].

182. Companies Act 2006, *supra* note 152, c. 46, § 168; Companies Act 2014, *supra* note 181, § 146.

183. Companies Act 2006, *supra* note 152, c. 46, § 172(1); Companies Act 2014, *supra* note 181, § 228(1)(a).

184. Companies Act 2006, *supra* note 152, c. 46, § 171; Companies Act 2014, *supra* note 181, § 228(1)(c).

185. City Code, *supra* note 141, r. 3.1, at D21; Irish Rules, *supra* note 160, r. 3.1, at 1.13 (referring only to "advice on [the] offer").

186. City Code, *supra* note 141, r. 3.2, at D21-22; Irish Rules, *supra* note 160, r. 3.2, at 1.13 (noting that a conflict of interest will exist for these purposes "for instance, when there are significant cross-shareholdings between an offeror and the offeree company, when there are a number of directors common to both companies or when a person has a substantial interest in both companies").

company that would create a conflict of interest.[187] Finally, where a member of the target board has a conflict of interest, that director should not normally join the remainder of the board in the expression of its views on the bid as part of the management circular.[188] The nature of the conflict to be clearly explained to shareholders.[189]

C. The Takeover Panels

Introduced alongside the City Code, the U.K. Takeover Panel serves two key functions. The first is broadly legislative: writing, periodically reviewing, and updating the City Code.[190] The second is essentially judicial: giving guidance and rulings on the interpretation, application, and effect of the City Code's principles, rules, and notices.[191] The U.K. Panel also monitors compliance with the City Code and investigates and enforces potential breaches. In furtherance of its rulemaking, investigatory, and enforcement functions, the U.K. Panel is empowered by statute to "do anything that it considers necessary or expedient."[192] This includes the power to compel disclosure of information, impose sanctions, and apply to a court to enforce compliance with the City Code.[193]

Responsibility for the U.K. Panel's legislative function rests with the panel's Code Committee.[194] The Code Committee is composed of representatives drawn from the panel's membership of institutional shareholders, corporate executives, legal and financial advisers, and other stakeholder groups.[195] The committee meets several times a year to discuss market developments and determine whether any amendments to the City Code are necessary.[196] In most cases, the committee will undertake a consultative process akin to the SEC's notice and comment period soliciting the views of interested stakeholders in connection with any proposed amendments. In exceptional cases, the committee may also amend the City Code without prior consultation where

187. City Code, *supra* note 141, r. 3.3, at D22; Irish Rules, *supra* note 160, r. 3.3, at 1.14 (noting that advisers may be disqualified on the basis of a conflict by arrangements–such as success fees–contingent on the failure of a bid).

188. City Code, *supra* note 141, r. 25.2, at J17 n.4; Irish Rules, *supra* note 160, r. 3.1(a)(ii), at 1.13.

189. *Id.*

190. Companies Act 2006, *supra* note 152, c. 46, §§ 943-44.

191. *Id.* § 945.

192. *Id.* § 942(2).

193. *Id.* §§ 947, 952, 955.

194. City Code, *supra* note 141, § 4(b), at A9 (UK).

195. *Id.*

196. *See* Armour & Skeel, *supra* note 124, at 1749; *see also Annual Reports (2012-2016)*, TAKEOVER PANEL http://www.thetakeoverpanel.org.uk/statements/reports [http://perma.cc/FY4A-2TUY] (noting that between 2012 and 2016, the Code Committee met four to five times per year on average).

an expedited response to market developments is deemed necessary and appropriate.[197]

Frontline responsibility for the U.K. Panel's judicial function rests with its executive. The executive is staffed by a mix of fulltime employees and professionals on secondment from law firms, investment banks, and other City institutions.[198] For each deal, the panel will assign a case officer to oversee the bid process.[199] The parties will then be required to liaise with the case officer on a regular basis. Where one of the parties has a question about the interpretation or application of the City Code, or a compliant about the conduct of another party, it will approach the executive for guidance or a ruling. Thus, for example, a bidder might lodge a complaint that the target's board has failed to provide it with sufficient disclosure or engaged in impermissible defensive tactics. Where warranted, the panel will then direct the target board to provide the requisite information or cease and desist from any action contravening the 'no frustration' principle.

Importantly, the City Code expressly contemplates that the executive will interpret and apply the General Principles and rules on the basis of both their technical letter and underlying spirit.[200] The executive seeks to respond to any questions or complaints in real time: with most decisions communicated to the parties by telephone within twenty-four hours.[201] While parties are often asked to provide information, there are no formal rules of evidence and most interactions with the panel consist of oral communications. Moreover, while the parties are often represented in these communications, it is typically by their financial—as opposed to legal—advisers.[202] As John Armour and David Skeel have observed, the panel's adjudication process is thus "untrammeled by the procedural and precedential niceties of the courtroom."[203] This procedural informality, combined with the executive's expert staff and close involvement throughout the bid process, enable the U.K. Panel to interpret and apply the City Code on an expert and dynamic basis in response to the unique facts of each transaction.[204]

Residing in the background of this informal adjudication process is the threat that the U.K. Panel will impose a wide range of sanctions in response to violations of the City Code. At the more informal end of the enforcement

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197. *See* City Code, *supra* note 141, § 4(b), at A9 (explaining that the Code Committee will then typically undertake a consultation on the expedited rule and subsequently make further amendments as necessary).

198. *Id.* § 5-6.

199. *See* Kershaw, *supra* note 129, at 23.

200. City Code § 2(b).

201. *See* Armour & Skeel, *supra* note 124, at 1929; *see also* Emma Armson, *Models for Takeover Dispute Resolution: Australia and the UK*, 5 J. CORP. L. STUD. 401, 421 (2005) (discussing the U.K. procedures).

202. *See* Armson, *supra* note 201, at 421.

203. Armour & Skeel, *supra* note 124, at 1729.

204. *Id.* at 1745; *see also* Johnston, *supra* note 119, at 448.

spectrum, these sanctions include either a private reprimand or public censure.[205] In response to more egregious conduct or repeat offences, the panel can also issue what is known as a 'cold shoulder' statement. The effect of a cold-shoulder statement is to require any person or firm authorized by the Financial Conduct Authority (FCA) to cease working with the offending party in connection with any takeover bid for a specified period of time.[206] At the more formal end of the enforcement spectrum, the panel is empowered to require individuals violating certain provisions of the City Code to compensate affected shareholders.[207] The panel can also seek a court order to enforce compliance with the City Code[208] and report potential misconduct to the FCA.[209] Finally, it is a criminal offence for a person who knew or was reckless to the fact that any bid documentation did not comply with the City Code and who failed to take reasonable steps to ensure compliance.[210] While there have been relatively few instances in which any of these sanctions have been imposed—only four cold shoulder statements have been issued in the panel's forty-eight-year history—this enforcement regime is widely viewed as an effective deterrent against violations of the City Code.[211]

Decisions of the U.K. Panel's executive are subject to both internal and external review. Where a party with sufficient interest in the matter wishes to contest a decision of the executive, this party is entitled to request that the panel's Hearings Committee review the matter.[212] Any party to a hearing before the Hearings Committee (or any person denied such a hearing) may then appeal against the decision to an independent Takeover Panel Board.[213] Consistent with the U.K. Panel's general approach, hearings before both the Hearings Committee and Takeover Panel Board are largely informal, typically taking place in person and in private, and without formal rules of evidence or the involvement of legal counsel.[214] Decisions of the Hearings Committee and Takeover Panel Board are communicated to the parties in writing as soon as practicable and then usually published on the panel's website.[215]

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205. City Code, *supra* note 141, § 11(b)(i)-(ii), at A15 (UK).

206. *Id.* § 11(b)(v), at A15 (noting that where any authorized person or firm fails to comply with a "cold-shoulder statement," they will themselves face sanctions including, *in extremis*, loss of authorization).

207. *Id.* § 10(c), at A14; *see also* TAKEOVER PANEL, TAKEOVER PANEL REQUIRES GUINNESS TO MAKE PAYMENTS TO FORMER DISTILLERS SHAREHOLDERS, 1989/13, at 1 (UK) (requiring that Guinness pay approximately £85 million in compensation for failing to make a cash alternative available to shareholders in connection with its bid for Distillers Company).

208. Companies Act 2006, *supra* note 152, c. 46, § 955.

209. City Code, *supra* note 141, § 11(b)(iv), at A14.

210. Companies Act 2006, *supra* note 152, c. 46, § 953.

211. *See* Armour & Skeel, *supra* note 124, at 1784-90; Kershaw, *supra* note 129, at 22-23.

212. City Code, *supra* note 141, § 7(a), at A12.

213. *Id.* § 8, at A12.

214. *Id.* §§ 7, 8, at A12.

215. *Id.*

The decisions of the U.K. Panel are also technically subject to judicial review. In practice, however, judicial review of the panel's decisions is relatively uncommon for two reasons. First, English courts have carefully limited the scope of any review of the panel's decisions. The Court of Appeal in *ex parte Datafin* determined that the panel must be given "considerable latitude" in the performance of its functions.[216] Consistent with this approach, the court advised the panel to ignore applications for leave to apply for judicial review in order to prevent applications from being used as "a mere ploy" in takeover contests.[217] Second, the strategy of seeking judicial review is unlikely to pay tactical dividends in the context of an ongoing takeover bid. As a preliminary matter, parties will be required to comply with the panel's decisions while in the process of seeking judicial review.[218] Perhaps more importantly, the Companies Act 2006 provides that contravention of the City Code will not affect the validity or enforceability of the relevant transactions or give rise to a breach of statutory duty.[219] Reflecting this restrictive approach to the available remedies, courts have been reluctant to intervene during the course of an active bid.[220] As a result, decisions of the U.K. Panel are typically the final word on the interpretation, application, and enforcement of the City Code.

In contrast with the U.K. Panel, the Irish Panel has been a statutory body since its inception. The statutory duties of the Irish Panel are twofold. First, the panel monitors and supervises takeovers and other relevant transactions[221] in order to ensure compliance with the provisions of the Takeover Act and Irish Rules.[222] Second, it makes rules in relation to matters within its jurisdiction.[223] The Takeover Act and EU Takeover Directive identify a number of issues that must be regulated, but the panel has considerable discretion to design and implement specific rules. For example, the panel is entitled to introduce any rules for the purpose of "ensuring that takeovers and other relevant transactions comply with the [General Principles] and the other provisions of this Act."[224] The Irish Panel

216. Regina v. Panel on Take-Overs and Mergers, *Ex parte* Datafin [1987] QB 815, 841 (Eng.). Donaldson MR suggested that the court should grant certiorari and mandamus only where there had been a breach of natural justice and that in all other cases contemporary decisions of the panel should take their course and the relationship of the court and panel should be "historic rather than contemporaneous." *Id.*

217. *Id.* at 840.

218. *Id.* at 840-41.

219. Companies Act 2006, *supra* note 152, c. 46, §§ 956, 961 (noting that the panel itself is also exempt from any liability save for acts committed in bad faith or which contravene the United Kingdom's Human Rights Act).

220. *See* GULLIFER & PAYNE, *supra* note 130, at 574-75.

221. 1997 Takeover Panel Act, *supra* note 156, §§ 5(1)(a), 7(1).

222. *Id.*

223. *Id.* §§ 5(1)(b), 8.

224. *Id.* § 8(1)(b).

reviews its rules from time to time—often following changes to the City Code—and generally consults with the public on any proposed changes.[225]

The functions of the Irish Panel are divided between its board and permanent executive. The day-to-day work of the Irish Panel is carried out by the executive. Although, like its U.K. counterpart, the executive bears frontline responsibility for providing guidance on the interpretation and application of the Irish Rules, it does not issue rulings.[226] The executive is available to respond to email or telephone enquiries from both the parties to a takeover and the general public. The executive is also responsible for monitoring dealings in the securities of relevant companies to ensure compliance with the Irish Rules and General Principles.

The board is responsible for making formal decisions on the application, interpretation, and enforcement of the Irish Rules and General Principles. As with the U.K. Panel, board members are drawn from the financial, business, and legal communities with each member appointing a director to the board.[227] The Governor of the Central Bank of Ireland is responsible for appointing two further directors who serve as the deputy chairperson and chairperson to the board.[228] Once appointed, all directors carry out their functions independently of their nominators.[229]

Parties may apply to the board for a ruling on whether aspects of a transaction comply with the Irish Rules either as a prophylactic measure or alleging that another party has breached the rules. The vast majority of applications are made by the legal or financial advisers to the target or bidder. These applications often include a request for the panel to give specific directions to remedy alleged breaches. Save where the panel deems a hearing necessary, only written representations are accepted. To ensure compliance, the panel may give a "direction" to any party to do or to refrain from doing anything that the panel specifies in its direction.[230] This may include, for example, a direction to acquire or dispose of securities, refrain from exercising voting rights attached to securities, make an offer on specified terms, or disclose any information. Where

225. It should be noted that § 8(5) of the Takeover Act provides that the approval of the Minister for Jobs, Enterprise and Innovation is needed before changes may be made to the rules relating to competition legislation and the Substantial Acquisition Rules.

226. *But see id.* §§ 8(5), 6(2) (noting that it may, however, exercise certain functions delegated to it by the board).

227. *Id.* § 6. (indicating that the members are drawn from the Law Society of Ireland, the Irish Association of Investment Managers, the Banking and Payments Federation Ireland, the Irish Stock Exchange, and the Consultative Committee of Accountancy Bodies–Ireland).

228. *See id.* § 6(e) (providing that appointment by the members and Governor of alternate directors ensures that there is a quorum at each meeting, which is important in a small country with a small and relatively tight-knit business and legal community); *see also id.* § 6(d) (providing resources where the expertise available to the panel is considered deficient in the circumstances of any particular takeover). This provision has been invoked only rarely.

229. *Id.* § 6(3) (prohibiting members of the Panel from instructing directors on how to carry out of their duties under the Act).

230. *Id.* § 9(2)(a).

it has reasonable grounds to believe that there has or will be a contravention of the Irish Rules or the General Principles, the Irish Panel may initiate an inquiry into the conduct of any person.[231] It may do so on its own initiative, or at the request of either the Irish Stock Exchange or a party to a transaction. Following this enquiry, the panel may "advise, admonish or censure" a person in public or private.[232] Notably, however, not every ruling finding a breach results in the issuance of advice, admonishment, or censure. Additionally, the Irish Panel may hold a statutory hearing.[233] This might be done, for example, where there is conflicting evidence that needs to be resolved in order to make a ruling. For the purposes of the hearing, the panel has the same powers, rights, and privileges as are vested in the High Court in relation to compelling attendance, examination on oath, and compelling the production of documents.[234] At the hearing, the parties may call witnesses, invite statements from the attendees, and present arguments. Parties and their advisers are entitled to be present throughout and to see papers submitted to the panel in connection with the hearing. To date, there has only been one statutory hearing.[235]

Notably, despite the statutory nature of Irish merger regulation, "efforts were made to ensure that this would not give rise to increased litigation, particularly tactical litigation."[236] Although there is nothing to prevent a party inviting the Irish Panel to review a ruling or direction, the Takeover Act provides that the sole method of questioning the validity of a rule, ruling, or direction, including any derogation or waiver thereof,[237] is by means of judicial review.[238] The restriction attempts to strike a balance between the protection of shareholders and ensuring that takeovers are not unnecessarily impeded.[239] The decision of the court is final and leave to appeal will only be granted where the court certifies that its decision involves a point of law of "exceptional public importance" and that it is desirable in the public interest that an appeal should be taken.[240] In addition, an applicant must seek leave from the court to apply for judicial review, generally within seven days of the date when the relevant ruling

231. *Id.* § 10.

232. *Id.* § 10(2)-(3).

233. *Id.* § 11.

234. *Id.* § 11(4) (indicating that a witness before the panel is also entitled to the same privileges and immunities as they would before the High Court).

235. *Annual Report 1998*, IRISH TAKEOVER PANEL 13, http://irishtakeoverpanel.ie/wp-content/uploads/2010/02/ITP-Annual-Report-1998.pdf [http://perma.cc/3S3V-LV9Q] (describing a hearing that arose in connection with a complaint that certain directors in a target company had conflicts of interest in relation to a particular takeover and thus should have been excluded from participating in the formulation and communication of advice to shareholders, and ruling that the parties were not conflicted within the meaning of the Irish Rules).

236. *Id.* at 8.

237. 1997 Takeover Panel Act § 13(2) (providing that a rule may only be challenged where the Panel has made a ruling or given a direction based on that particular rule).

238. *Id.* § 13.

239. 149 Seanad Deb. (Feb. 6 1997) col. 1692 (Ir.).

240. 1997 Takeover Panel Act, *supra* note 156, § 13(6). This would not prevent a party challenging the constitutionality of the law pursuant to Section 13(7).

or direction is made.[241] This strict time limit demonstrates the commitment of the legislature to the swift settlement of any disputes. It is also consistent with the recognition by the English Court of Appeal in *Datafin* of the importance of speed in the resolution of financial market disputes. Finally, to ensure certainty, the Takeover Act provides that where transactions have been completed, the provisions of the Act cannot be used to have them unwound.[242] Given these constraints, it is perhaps not surprising that in its twenty years of operation, the Irish Panel has only been the subject of a judicial review application on three occasions.[243]

D. Obstacles to Shareholder Litigation in the United Kingdom and Ireland

Importantly, the code and panel-based takeover regimes in the United Kingdom and Ireland have developed against the backdrop of substantive and procedural rules that dramatically reduce the prospect of shareholder litigation.[244] These rules differ from those in the United States in several important respects. First, as a substantive matter, the statutory duties of directors in the United Kingdom and Ireland are explicitly owed to the company itself—not its shareholders.[245] Consistent with this approach, courts tend to treat losses suffered by both shareholders and the company stemming from the same underlying facts as reflective losses,[246] for which the company—and not individual shareholders—is entitled to recover.[247] While fiduciary and other

241. *Id.* § 13(3)(a). Section 13(5) provides that this period may only be extended where the delay was not caused by the default or neglect of the applicant or any person acting for him and where an extension would not cause injustice to any other concerned party. *Id.* § 13(5). Section 13(8) provides that while an application for leave to apply for judicial review is pending or during the seven-day period within which such an application may be made, the panel may apply to the court for an order providing for appropriate interim or interlocutory relief. *Id.* § 13(8).

242. *Id.* § 15. The only circumstances in which a transaction could potentially be unwound would be where the panel itself applies to the court to annul a transaction that had been carried out otherwise than in accordance with a ruling or direction, or where a ruling or direction was made on the basis of false or misleading information provided by a party to the takeover.

243. In neither of the first two cases did the matter proceed to a hearing. In the third case, the court reached the stage of making a determination on an application for leave to apply for judicial review made by Aer Lingus Group ("Aer Lingus") in respect of a hostile bid by Ryanair Holdings. Aer Lingus sought to review a decision of the Irish Panel on the duration of a moratorium imposed on Ryanair under the Irish Rules preventing it from making another offer for Aer Lingus, with Aer Lingus claiming that the moratorium should have been longer. The High Court refused the leave application on the basis that Aer Lingus had not established substantial grounds because it had not shown that the interpretation of the rule by the panel was wrong or even questionable. An order for costs was made by the High Court in favor of the panel. *See* Aer Lingus Group PLC v. Irish Takeover Panel [2013] IEHC 428 (Ir.).

244. For a survey of these procedural rules, see Armour et al., *supra* note 124, at 262-64.

245. Companies Act 2006, *supra* note 152, c. 46, § 170 (UK); Companies Act 2014, *supra* note 181, § 227(1).

246. *See* Johnson v. Gore Wood & Co. [2002] 2 AC (HL) 1, 51 (UK).

247. *See* PAUL L. DAVIES & SARAH WORTHINGTON, PRINCIPLES OF MODERN COMPANY LAW 610-12 (2012).

duties may also arise at common law,[248] courts have historically been extremely reluctant to extend directors' duties to individual shareholders.[249] As Paul Davies and Sarah Worthington have observed, special facts and circumstances warranting such an extension are especially unlikely to arise in the context of public companies with large and dispersed shareholder bodies.[250]

Second, shareholders in public companies face significant obstacles in bringing a derivative action on behalf of a company. The common law rule articulated in *Foss* v. *Harbottle* severely limits the circumstances in which shareholders in the United Kingdom and Ireland would have standing to bring a derivative action.[251] Perhaps most importantly for the present purposes, shareholders would be required to establish that a controlling blockholder had perpetrated a fraud on minority shareholders.[252] Understandably, this requirement is often extremely difficult to satisfy in the case of public companies. In the United Kingdom, shareholders can also bring a statutory derivative action.[253] However, shareholders seeking to bring a statutory derivative action must apply to the court for permission.[254] In determining whether to grant permission, the court must take into consideration whether the applicant is acting in good faith and in accordance with their duty to promote the success of the company, whether the company has decided not to pursue the claim, and whether the conduct gives rise to a cause of action that the shareholder could pursue in their own right.[255] The court is also required to refuse permission where it is satisfied that a person acting in accordance with their duty to promote the success of the company would not seek to continue the claim, or where the conduct giving rise to the action has been authorized or ratified by the corporation.[256] As with the rule in *Foss v. Harbottle*, the U.K. Companies Act 2006 thus erects significant hurdles for shareholders seeking to bring a derivative action in connection with the conduct of a target board.

Third, as a procedural matter, one of the defining features of the legal systems in the United Kingdom and Ireland is the relative absence of U.S.-style class action lawsuits. The closest equivalents in the United Kingdom are what

248. Peskin v. Anderson, [2002] 2 EWCA (Civ.) 326, *aff'd*, [2001] 1 B.C.L.C. 372 (UK).

249. *See* DAVIES & WORTHINGTON, *supra* note 247, at 467; THOMAS COURTNEY, THE LAW OF COMPANIES 744 (2016).

250. See DAVIES & WORTHINGTON, *supra* note 247, at 469.

251. Foss v. Harbottle (1843) 67 Eng. Rep. 189; 2 Hare 462. For a discussion of the impact of this case. see DAVIES & WORTHINGTON, *supra* note 247, at 595, and COURTNEY, supra note 249, at 674.

252. *See* Birch v. Sullivan [1957] 1 W.L.R. 1247 (Ch.); Crindle Inv. v. Wymes [1998] 4 IR 567, 569 (Ir.).

253. Companies Act 2006, *supra* note 152, c. 46, §§ 260-63.

254. *Id.* § 261.

255. *Id.* § 263(2).

256. *Id.* § 263(3).

are known as group litigation orders[257] and in Ireland, representative actions.[258] Like U.S. class actions, group litigation orders and representative actions allow courts to consolidate and manage multiple related claims.[259] However, unlike U.S. class actions, where shareholders will typically be automatically included in any securities class action unless they opt out, group litigation orders and representative actions require shareholders to expressly opt into the action. Plaintiffs in group litigation orders and representative actions are also prevented from deposing witnesses before trial, thereby depriving them of potentially valuable investigative opportunities.[260] Accordingly, while group litigation orders and representative actions have recently been used in connection with a number of high profile cases in the United Kingdom and Ireland,[261] these avenues of redress are unlikely to yield the same benefits for shareholders as U.S.-style class actions.[262]

A second potentially significant procedural obstacle to shareholder litigation in the United Kingdom and Ireland is the "loser pays" principle. This principle envisions that where a court is required to make an award at trial, the unsuccessful party will be required to pay the successful party's costs.[263] When assessed on the standard basis in the United Kingdom,[264] these costs include litigation expenses "reasonably and proportionately incurred" and "reasonable and proportionate in amount."[265] In Ireland, meanwhile, these costs include all costs reasonably incurred in the prosecution of a claim or the defense of the

257. UK R. CIV. P. 19.11.

258. Representative actions allow a party to sue on behalf of specified persons who have authorized the application and who have the "same interest" in the claim. *See* Order 15, Rule 9 of the Rules of the Superior Courts 1986; *see also* Niall Collins et al., *Class/Collective Actions in Ireland*, PRAC. L. GLOBAL GUIDE (2016), http://uk.practicallaw.thomsonreuters.com/9-618-0420 [http://perma.cc/PL4R-MWTL] for a fuller discussion on this point. Any settlement of a representative action is binding on all the authorizing parties. Notably, these actions cannot be used for tort claims and remedies are limited to injunctive and declaratory relief.

259. UK R. CIV. P.19.10 (stipulating that these claims must "give rise to common or related issues of fact or law").

260. *See* Kurt Hunciker & Jake Nachmani, *The State of International Shareholder Litigation: Comparing Outlooks in the US and UK*, ADVOCATE 3 (Feb. 6, 2015), http://www.blbglaw.com/news/publications/data/00179/_res/id=File1/Adv_Fall2014_Hunciker_Nachmani.pdf [http://perma.cc/Z52D-F4H6]

261. *See Guidance: Group Litigation Orders*, H.M. CTS. & TRIBUNAL SERVS. (Aug. 7, 2015), http://www.gov.uk/guidance/group-litigation-orders [http://perma.cc/C8PQ-NCF8] (providing a list and brief summary of all outstanding group litigation orders granted in the United Kingdom to date; in total, ninety-five group litigation orders have been granted since 2000).

262. *See* Hunciker & Nachmani, *supra* note 260, at 4-5.

263. *See* U.K. R. CIV. P. 44.2; SUPERIOR COURTS RULES COMM., IRISH RULES OF THE SUPERIOR COURTS (1986), r. 1(3).

264. U.K. R. CIV. P. 44.3 (noting that costs can also be assessed on an "indemnity" basis where the costs were "unreasonably incurred" or "unreasonable in amount").

265. *Id.*

proceedings.[266] Courts in both the United Kingdom and Ireland retain the discretion to deviate from the loser pays principle on a case-by-case basis.[267]

Finally, both the United Kingdom and Ireland impose relatively tight restrictions on the use of contingency fee arrangements. In the United Kingdom, so-called "conditional fee agreements" are permitted subject to a cap on any success fee equal to 100% of legal costs.[268] Any success fee is payable by the client in accordance with the terms of the agreement. Barristers and solicitors in the United Kingdom can also use so-called "damage-based agreements," entitling them to a proportion of any sums recovered in successful litigation. Like contingent fee agreements, however, these damaged-based agreements are subject to a cap: typically 50% of the recovered sum in commercial cases.[269] In Ireland, meanwhile, contingency fee arrangements are unenforceable.[270]

Collectively, these rules make it relatively difficult for shareholders in the United Kingdom and Ireland to use litigation as a means of compelling disclosure or constraining conflicts of interest in the context of public takeovers. The fact that directors' duties are owed directly to the corporation, along with the jurisprudential and statutory safeguards around derivative actions by shareholders, serve to limit the scope of actionable claims. Compounding matters, the practice of forcing the loser to pay increases the costs of litigation, deterring shareholders from commencing actionable claims—especially where the legal costs are likely to be high in relation to the expected damage awards.[271] The absence of U.S.-style class actions further increases the upfront costs of litigation for both shareholders and their legal counsel, while restrictions on contingency fees dilute the incentives of entrepreneurial counsel who might otherwise be willing to assume the risk of initiating group litigation.[272] Viewed from this perspective, the broader legal environment in the United Kingdom and Ireland thus serves as something of a complement to the prevailing mode of merger regulation, deterring nuisance litigation and entrenching the U.K. and Irish Panels as the principal adjudicators of shareholder rights in connection with public takeover bids.

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266. The Taxing Master of the High Court is an independent officer of the Court who provides an independent and impartial process of assessment of legal costs, seeking to achieve a balance between the costs involved and the services rendered.

267. UK R. CIV. P. 44.2 (noting that in exercising this discretion, courts in the United Kingdom are required to take into consideration the conduct of the parties, whether the unsuccessful party has been successful in any aspect of the case, and any admissible settlement offers).

268. The Conditional Fee Agreements Order 2013, SI 2013/689, § 3.

269. The Damages-Based Agreements Regulations 2013, SI No. 609, § 4(3).

270. Solicitors (Amendment) Act 1994 (Act No. 68/1994) (Ir.), http://www.irishstatutebook.ie/eli/1994/act/27/section/68/enacted/en/html [http://perma.cc/5DGL-DHZE]; BAR OF IR., CODE OF CONDUCT FOR THE BAR OF IRELAND § 12(e) (2014).

271. *See* Michael R. Baye et al., *Comparative Analysis of Litigation Systems: An Auction-Theoretic Approach*, 115 ECON. J. 583 (2005); James W. Hughes & Edward A. Snyder, *Litigation and Settlement Under the English and American Rules: Theory and Evidence*, 38 J.L. & ECON. 225 (1995); Edward A. Snyder & James W. Hughes, *The English Rule for Allocating Legal Costs: Evidence Confronts Theory*, 6 J.L. ECON. & ORG. 345, 345-48 (1990).

272. Armour et al., *supra* note 119, at 262-264.

III. Assessing the Efficiency of Alternative Modes of Regulation

The previous Part outlined two distinctive models for regulating mergers: the U.S. system of regulation by litigation and the Anglo-Irish regulatory system of detailed codes written, interpreted, and enforced by expert panels. This part compares the relative efficiency of the two approaches. After reviewing the economic literature on regulation versus litigation and applying it to the specific context of merger regulation, this part articulates an alternative to the current U.S. approach that draws both on the theoretical literature and the Anglo-Irish example.

A. The Costs and Benefits of the Current U.S. Model

Much of the prior work comparing the relative costs and benefits of regulation versus litigation focuses on a single aspect of the comparison—for example, (regulatory) rules versus (judicial) standards, or ex ante (regulation) versus ex post (litigation) scrutiny.[273] Yet there are at least two accounts—one by Richard Posner, the other by Steven Shavell—that offer a more comprehensive framework for assessing the efficiency of regulation versus litigation.[274] Each of these accounts frames the comparison as a tradeoff between four key factors. Posner emphasizes: (1) the use of rules versus standards; (2) whether these rules or standards are designed to act as ex ante prophylactics versus ex post deterrents; (3) whether they are designed and implemented by experts versus generalists; and (4) whether the enforcement process is public versus private. Shavell, meanwhile, emphasizes: (1) any special knowledge that private parties or regulators possess in relation to the relevant risks; (2) the capacity of private parties to pay for any harm stemming from the materialization of these risks; (3) the likelihood that the materialization of these risks would result in a lawsuit; and (4) administrative costs. Many of the factors identified by Posner and Shavell are closely related, if not overlapping.

The first two factors in Posner's framework—ex ante versus ex post and rules versus standards—typically come together as a single package. Paradigmatic regulatory decision making proceeds ex ante and according to a body of rules, while litigation proceeds on the basis of ex post adjudication according to a set of broad standards. For example, when fire inspectors enter a

273. *See, e.g.*, Robert Innes, *Enforcement Costs, Optimal Sanctions, and the Choice Between Ex-Post Liability and Ex-Ante Regulation*, 24 INT'L REV. L. & ECON. 29, 35 (2004) (explaining the cost and benefits of ex ante versus ex post scrutiny); Samuel Issacharoff, *Regulating After the Fact*, 56 DEPAUL L. REV. 375, 377 (2007) (explaining the costs and benefits of ex ante versus ex post systems).

274. *Compare* Richard A. Posner, *Regulation (Agencies) Versus Litigation (Courts): An Analytical Framework*, *in* REGULATION VERSUS LITIGATION: PERSPECTIVES FROM ECONOMICS AND LAW 11, 13 (Daniel P. Kessler ed., 2011), *with* Steven Shavell, *Liability for Harm Versus Regulation of Safety*, 13 J. LEGAL STUDS. 357, 357 (1984). Shavell is more specifically focused on the efficiency of regulatory rules versus liability in tort. However, this question largely overlaps with the question of regulation versus efficiency.

building, they conduct their inspection according to a codified set of procedures prior to the start of any fire. When a warehouse burns down due to a neighbor's alleged negligence, the judge decides the case after the fact according to a general standard of care. The tradeoff between these two modes of regulation hinges on the level of technical specificity involved in deciding each case. Ex ante analysis is largely categorical, grouping problems according to type and excluding details not previously specified in the rules.[275] In Posner's words, the use of ex ante rules thus "buys precision at the cost of excluding case-specific information that the promulgators of the regulation either did not anticipate or excluded in order to keep the regulation simple."[276] Ex post litigation, on the other hand, takes these case-specific details into account—thereby increasing accuracy, but often at the cost of considerable time and administrative expense. However, Posner emphasizes that litigation may also economize on administrative costs by intervening on a sporadic rather than a constant basis—with costs incurred only when claims are actually brought.[277]

Posner's analysis on these first two points largely overlaps with Shavell's consideration of the likelihood that a lawsuit will be brought and the associated administrative costs. In addition to litigation costs being incurred only when claims are actually filed, Shavell also emphasizes that litigation may distribute costs more efficiently by concentrating costs on those parties most likely to cause harm. In Shavell's view, this stands in contrast with administrative regulation, which typically spreads these costs across a class of actors that may or may not engage in harmful conduct.[278] Furthermore, with regard to the likelihood that a suit will be brought, Shavell emphasizes that regulation may be especially appropriate in those situations where injured parties might fail to bring suit, thereby leaving the harmful conduct unregulated. Posner captures the same concern in his consideration of the public nature of regulation versus the private nature of litigation: because litigation is privately financed, important claims may not be advanced.[279]

The current U.S. system of regulation by litigation does not measure up well against these first two factors. The fact that litigation is brought in virtually every transaction belies the notion of administrative savings from sporadic legal interventions. The near certainty of litigation also suggests that costs are not concentrated on those most likely to have caused harm. Imposing costs on all transacting parties functions as an indiscriminate levy rather than a targeted

275. However, as we explain, this issue can be addressed by establishing processes that facilitate the refinement of existing rules, along with the adoption of new rules, in response to developments in the real world.

276. *See* Posner, *supra* note 274, at 14.

277. *Id.* at 15 (explaining that ex post regulation "economizes on administrative expense because intervention is sporadic, and utilizes both case-specific information . . . and adversary procedure, which may increase accuracy").

278. *See* Shavell, *supra* note 274, at 373.

279. *See* Posner, *supra* note 274, at 26.

sanction aimed at deterring harmful conduct. The settlement aspect of merger litigation, however, might suggest more of a hybrid system. Judicial review of merger activity typically occurs at a settlement hearing prior to the close of the transaction. At the same time, the non-adversarial nature of settlement hearings suggests that the benefit of extracting case-specific information via litigation is also absent.[280] Judges must either accept the settlement that the parties put forward or scrutinize the settlement without the benefit of either adversarial briefing or the kind of detailed code or rulebook that a similarly situated regulator might possess.

In Delaware, at least, the accretion of precedent in this context has enabled judges to formulate a kind of rubric for disclosure settlements. For example, disclosures must be plainly material,[281] which typically involves a previously undisclosed conflict of interest[282] or a withheld piece of financial information that would change how the company is valued.[283] However, it should not be taken for granted that other courts will benefit from either the accumulation of precedent or the judicial expertise necessary to work through what is, in effect, a kind of regulatory analysis. And at least so far, Delaware has been unable to ensure jurisdiction over all merger litigation, even for Delaware incorporated companies. Furthermore, the "plainly material" standard remains a standard, susceptible to varying interpretations by different judges and courts.[284] The lack of a clear ex ante rulebook thus increases transactional uncertainty, thereby imposing costs on transacting parties.

The current hybrid, in other words, may be the worst of both worlds. It has the high costs of litigation—applied indiscriminately and in every case—with the general lack of precision associated with regulatory systems. Worse, the judicial application of standards rather than regulatory rules leads to unpredictability and makes compliance difficult to achieve without frequent resort to litigation.[285] Finally, because bringing a claim in this context is not the same as pursuing truly adversarial litigation, conduct resulting in substantial harm may not be seriously scrutinized.[286] All of this suggests that it may be worth considering an alternative approach to merger regulation in the United States.[287]

280. *Id.*

281. *In re* Trulia, Inc. Stockholder Litig., 129 A.3d 884, 899 (Del. Ch. 2016).

282. *In re* Sauer-Danfoss, Inc. S'holders Litig., 65 A.3d 1116, 1136 (Del. Ch. 2011).

283. *In re* Netsmart Techs., Inc. S'holders Litig., 924 A.2d 171, 203 (Del. Ch. 2007).

284. Wonder, *supra* note 3, at 2410.

285. *See* Posner, *supra* note 274, at 14 (explaining that the ability to make clear ex ante rules weighs in favor of regulation because "compliance may be achieved without frequent enforcement proceedings," thus lowering marginal costs).

286. *See* Friedlander, *supra* note 3, at 883 (noting that routine approval of disclosure settlements may amount to "the routine release of absent class members' claims without due process of law").

287. *See generally* Andrei Shleifer, *Efficient Regulation*, *in* REGULATION VERSUS LITIGATION, *supra* note 274, at 27, 29 (articulating a theory of regulation in which the purpose of regulation is to correct courts' failures to solve social problems).

Another parallel between Posner's and Shavell's frameworks is the relevance of experts and expertise. According to Posner, expert administrative bodies are better at accumulating a body of specialized knowledge. Because they are unbound by precedent, these administrative bodies are also able to adopt more responsive and flexible approaches to changing real world problems. However, a downside to highly flexible administrative regulation, described in greater detail below, is the possibility of regulatory capture.[288] Courts of general jurisdiction, in contrast, are thought to be largely immune from interest-group pressure, but may also be less flexible due to the lack of specialized knowledge, limited investigatory resources, and "cumbersome and to a degree antiquated procedures."[289] Like Posner, Shavell emphasizes special knowledge but focuses, in the first instance, on the parties themselves rather than the ultimate decision-maker. According to Shavell, where the parties possess special knowledge relevant to the underlying risk, liability rules may be superior insofar as they allow the parties to strike an informed bargain around that risk.[290] If, on the other hand, knowledge about the underlying risk is generalizable, then an administrative body could attain sufficient expertise to regulate the risk without excessive risk of error.[291]

In the context of merger transactions, shareholders are generally concerned about two things. First, they must be provided with adequate information to make an informed decision on the merits of the proposed transaction. Second, they are likely to be concerned about the prospect of a management conflict that has the effect of suppressing the value of the company at sale. The first concern is eminently generalizable. Indeed, it has largely been generalized in Delaware precedents relating to the value of individual disclosures in connection with merger litigation. Hence, there is no barrier to the distillation of these types of information into a set of rules and principles on merger disclosure, rules which have largely been written not only by the U.K. and Irish Panels, but also in large part by the SEC.[292]

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288. *See infra* Section IV.A.

289. Posner, *supra* note 274, at 20.

290. *See* Shavell, *supra* note 274, at 359 ("Where private parties have superior knowledge of these elements, it would be better for them to decide about the control of risks, indicating an advantage of liability rules, other things being equal.").

291. *Id.* at 359 ("[I]f the information possessed by a regulator is superior to private parties and the courts . . . the use of direct regulation would be more attractive than liability.").

292. *See* Securities Exchange Act of 1934, 15 U.S.C. § 78 (2012) (describing how in the United States the federal securities laws authorize the SEC to promulgate rules relating to disclosures in mergers and takeovers); *see also* Reports, Opinions, Appraisals, and Negotiations, 17 C.F.R. § 229.1015(a) (2016) (requiring disclosure in going-private transactions of "[a]ny report, opinion or appraisal relating to the consideration or the fairness of the consideration to be offered to security holders or the fairness of the transaction to the issuer or affiliate or to security holders who are not affiliates"). *See generally* David Friedman, Note*, The Regulator in Robes: Examining the SEC and the Delaware Court of Chancery's Parallel Disclosure Regimes*, 113 COLUM. L. REV. 1543, 1556 (2013) (comparing SEC rules to Delaware disclosure cases).

Managerial conflict of interest, however, presents a distinct rule-making challenge. Although the type of problem—the existence of a conflict of interest—may be readily generalizable, these conflicts can arise in a wide range of circumstances and in myriad forms. The determination of whether the problem is present in any given case thus necessarily demands the kind of a fact-intensive ex post investigation to which common law courts are well suited. Accordingly, common law courts may retain a comparative advantage over regulatory systems in policing conflicts of interest. We do not want to overstate this advantage, however, as both the U.K. and Irish Panels retain ex post investigative powers over breaches of both the General Principles as well as detailed rules, thus at least partially offsetting the advantages of ex post litigation in this regard.

Finally, both Posner and Shavell consider the capacity of private parties to pay for any harm stemming from the materialization of the relevant risks. Their principal insight is that, if the potential liability exceeds the defendant's ability to pay, then liability rules will not create sufficient incentives to meet the desired standard of care.[293] Regulation would therefore be preferable in this situation.[294] Of all the factors considered by Shavell and Posner, this is the most difficult one to apply in the context of merger activity. Merger transactions do not map neatly onto the standard tort paradigm in which the prospect of damages leads parties to take care. In the merger context, the greatest threat to the transacting parties is the possibility of an injunction and the resulting collapse of the proposed transaction. While there is also the risk of liability for fraud or conflict of interest on the part of individual officers or directors, these are secondary considerations at best.[295] When injunctive relief is the real risk, ability to pay is not relevant.

On balance, then, application of these factors suggests that regulation by litigation is not a particularly efficient mode of merger regulation. However, it is also clear that the present system of merger regulation—at least in Delaware—is a hybrid system, with some attributes typical of regulation and others typical of litigation. Hybrid systems, of course, are highly likely to emerge in the real world. And both Posner and Shavell suggest that hybrid systems may often be preferable. Posner emphasizes regulation and litigation as complements rather than substitutes.[296] Shavell likewise suggests that a "complete solution to the problem of the control of risk should involve the joint use of liability and

293. *See* Posner, *supra* note 274 (discussing the same in the context of limited liability); Shavell, *supra* note 274, at 360-61 (explaining that "parties would treat losses caused that exceeded their assets as imposing liabilities only equal to their liabilities").

294. *See* Shavell, *supra* note 274, at 361 (noting that "the greater the likelihood of harm much larger than assets, the greater the appeal of regulation").

295. *See* DEL. CODE ANN. tit. 8, § 102(b)(7) (2015); Black & Coffee, *supra* note 150; Lyman P.Q. Johnson & Robert Ricca, *The Dwindling of* Revlon, 71 WASH. & LEE L. REV. 167 (2014) (arguing that *Revlon* is extremely unlikely to be the basis of judicial sanctions).

296. *See* Posner, *supra* note 274, at 23 (using antitrust as an example to emphasize that a hybrid system "exploits complementarities between agencies and courts . . . antitrust judges fine-tune Justice Department or FTC merger guidelines; and judges review the rulings of administrative agencies for compliance with statutes and with principles of fair procedure").

regulation, with the balance between them reflecting the importance of the determinants."[297] We sketch one possible hybrid approach in the next section.

B. Towards an Administrative Alternative for U.S. Merger Regulation

In this Section, we propose a regulatory alternative to the current litigation-centric model of U.S. merger regulation. This alternative draws on both the theoretical considerations canvassed above and, importantly, the Anglo-Irish example. Our alternative is a hybrid. We propose an ex ante regulatory panel to guarantee a basic level of disclosure and procedural fairness in merger transactions. Panel approval, however, would not foreclose the right of shareholders to bring suit ex post in connection with serious harms. To control the threat of nuisance claims in this context, we recommend the adoption of procedural rules to ensure that cases are only pursued when there is evidence of substantial wrongdoing, rather than minor deficiencies in corporate disclosure.

It is important to emphasize that we are sketching out a procedural model for merger regulation without regard to the underlying substance of the law. The underlying substance of takeover law could, for example, permit takeover defenses (as in the United States) or prohibit them (as in the United Kingdom and Ireland). Our model remains agnostic on this and other substantive choices, such as whether to prescribe a strict schedule for responding to takeover bids (as in the United Kingdom and Ireland) or to leave the matter to the discretion of the target board (as in the United States). Here we are focused purely on the procedural mode of merger regulation.

Finally, although we think our alternative offers significant advantages over the current system of regulation by litigation, ours is but one way of conceiving a regulatory alternative. Many more could be imagined. Any U.S. state could adopt a regulatory approach as part of its state corporate law. Alternatively, the regulatory model could be made a part of federal securities regulation. While the discussion that follows assumes a model adopted under state corporate law, it would also apply (with minor modifications) to the federal context.

1. The Administrative Panel

Following the Anglo-Irish example, the frontline work in our regulatory model would be performed by an administrative panel reviewing each merger transaction. Like the U.K. and Irish models, the panel would be staffed by experts—perhaps including prominent M&A practitioners, current or former members of the judiciary, representatives from institutional investors, investment bankers, accountants, and academic lawyers and economists. The panel would write, interpret, and enforce rules and principles to govern the merger process, including conflicts of interest and the timing and content of

297. Shavell, *supra* note 274, at 365.

required disclosures. Parties to the transaction would also be able to approach the panel with questions and concerns. Like the U.K. and Irish panels, the panel would aim to provide real-time answers to questions and to review and respond to submissions as quickly as possible. Importantly, our panel would be responsible for conducting a general review of preliminary proxy statements for the adequacy of disclosures. The completion of an initial review, however, would not bar the panel from revisiting disclosure issues in the event of a complaint or the subsequent revelation of new information. The panel would also be empowered to investigate potential conflicts of interest with the goal not of improving the economics of the transaction but of ensuring full disclosure.

Structured in this way, our administrative approach to merger regulation would provide several advantages. The first set of advantages stems from the scrutiny of transactions by expert panels. Although most deals currently attract litigation, it is far from clear that those claims subject transactions to serious oversight.[298] In contrast, the panel approach would ensure that every transaction is reviewed by experts with specialized knowledge in the field. Every deal would receive a threshold level of ex ante scrutiny, enabling the panel to implement corrective disclosure where necessary prior to the shareholder vote. The threat that the panel would require parties to make corrective disclosures—and the potential impact this would have on shareholders' view of the reputations of the parties, the credibility of these disclosures and, ultimately, the outcome of the transaction—would incentivize parties to disclose all potentially material information as quickly as possible.

Second, the panel's review would proceed according to a clear set of rules regarding what specific information—such as financial valuations—must be disclosed in particular types of transactions, and which potential issues—such as conflicts—may require more detailed discussion. Clear ex ante rules enhance certainty, and improve the ability of transaction planners to structure and quickly close deals. These rules could include "disclose or explain" obligations, requiring transacting parties to reveal information to the panel that they would, perhaps for competitive reasons, withhold from the proxy statement.[299] Moreover, the body of rules would make the panel's analysis more predictable to transaction planners, leading them to incorporate the information into their disclosures and thereby obviating the need for extensive regulatory involvement in many cases. At the same time, while operating on the basis of a clearly articulated body of rules, our panel, like the U.K. and Irish Panels, would be empowered to enforce General Principles and, like the U.K. Panel, seek

298. *See supra* Part I.

299. For an analysis of the effectiveness of "comply and explain" approaches generally, see Sridhar Arcot et al., *Corporate Governance in the UK: Is the Comply or Explain Approach Working?*, 30 INT'L REV. L. & ECON. 193, 201 (2010); Luca Enriques & Paulo Volpin, *Corporate Governance Reforms in Continental Europe*, 21 J. ECON. PERSPS. 117, 130 (2007); and Iain MacNeil & Xiao Li, *"Comply or Explain": Market Discipline and Non-Compliance with the Combined Code*, 14 CORP. GOVERNANCE 486, 486 (2015).

compliance with the spirit as well as the letter of the law. This would allow the panel's interpretations to take new developments and idiosyncrasies of individual cases into account.[300]

Third, in contrast to the reactive nature of common law rulemaking,[301] which relies heavily on the incentives of the parties to unearth and litigate issues,[302] our panel system—like its U.K. and Irish models—would continuously monitor market developments and proactively evaluate whether developments warrant refinement to the underlying code and rules.[303] Any such changes could be implemented quickly. In addition, our proactive regulatory approach would curb the strategic incentive of defendants to withhold information from their preliminary proxy statements in order to set up a disclosure settlement later.[304] These practices degrade the quality of corporate disclosures if the deal is never challenged or, more likely, if plaintiffs' counsel does not seek disclosure of the particular information withheld. Under our approach, there would be no incentive to withhold information and every incentive to disclose all material information immediately in order to guarantee a quick regulatory review and avoid any reputational damage from being compelled by the panel to make additional disclosures.

A fourth advantage of the panel system is speed. While Delaware courts are doubtlessly some of the fastest in the world, most cases still take several weeks from filing to completion—and in some cases significantly longer. Parties to a transaction in the United Kingdom or Ireland, meanwhile, need only telephone the executive for immediate guidance. Similarly, a ruling may be obtained from the executive in the United Kingdom or the panel in Ireland in a matter of days or less.

Fifth, in terms of administrative costs, we expect that our approach will be less costly overall than the present system that allows attorneys on both sides to seek rents in every transaction. The regulatory approach would move from litigation in virtually every deal to, we expect, ligation in very few deals.[305] The

300. City Code, *supra* note 141, Intro. § 2(b), at A2 (explaining that in the United Kingdom, the executive is expressly empowered to apply the City Code on the basis of its underlying spirit); 1997 Takeover Panel Act, *supra* note 156, General Principles (noting that the panel still has a considerable degree of latitude despite the statutory nature of the Irish rules).

301. *See* Armour & Skeel, *supra* note 124, at 1730 (noting that rulemaking within common law systems involves an incremental and largely uncoordinated process of articulating, refining, and distinguishing precedents).

302. *See supra* Section IV.B; *see also* Paul Rubin, *Micro and Macro Legal Efficiency: Supply and Demand*, 13 SUP. CT. ECON. REV. 19 (2005); Todd Zywicki, *The Rise and Fall of Efficiency in the Common Law: A Supply-Side Analysis*, 97 NW. L. REV. 1551 (2003).

303. The two panels are thus designed to proactively intervene to ensure that the rules evolve to reflect changes in the takeover process. As one court has put it, the panel "acts as a sort of fire brigade to extinguish quickly the flames of unacceptable and unfair practice." Regina v. Panel on Takeovers & Mergers, *Ex parte* Guinness Plc (1988) 4 BCC 325, 338 (UK).

304. *See supra* Section IV.B.

305. Insofar as our model moves the United States towards the Anglo-Irish system, it may be useful to compare the litigation rates of the United States and the United Kingdom in mergers and acquisitions transactions.

operations of the panel would not be free, of course, but there is reason to believe that companies would pay far less for panel review than they currently pay in attorneys' fees to litigate and settle merger claims. In the United Kingdom, for example, the operations of the U.K. Panel are funded by way of small "document charges" levied in connection with formal offers exceeding £1 million, fees on block transactions in shares listed on the London Stock Exchange, sales of the City Code, and other minor charges.[306] These charges are likely a small fraction of plaintiffs' attorneys' fees, defense attorneys' fees, and court costs in the U.S. system. In the United Kingdom, for example, a transaction worth £1 billion would cost £175,000 ($215,000) in document charges. The Irish Panel, meanwhile, charges a fee of €62,500 ($66,520) on all offers over €125 million, with a reduced fee for lower value offers but an additional charge where the bidder is not a relevant company. In the United States, by contrast, plaintiffs' attorney's fees alone typically run over $400,000 in disclosure settlements.[307] Defense attorneys' fees are undisclosed but are likely similarly high (or higher).[308] A straightforward comparison of administrative expenses thus plainly favors the Anglo-Irish system.

The more significant cost associated with administrative regulation may be the upfront costs of drafting a set of rules and procedures for merger review. However, a clear rubric of principles already exists under Delaware law,[309] SEC rules,[310] the Takeovers Directive, and in the rules and principles of takeover panels around the world.[311] While this drafting exercise would not be costless, states would be starting from a relatively clear set of blueprints reflecting tried and tested provisions.

The other potential cost of administrative regulation is the risk of regulatory capture.[312] Moving from judicial regulation to a form of administrative

306. *See* City Code, *supra* note 141, at A17 (UK); *Annual Statement*, TAKEOVER PANEL (2016), http://www.thetakeoverpanel.org.uk/statements/reports [http://perma.cc/WN95-HLN5].

307. *See* Cain & Solomon, *supra* note 3, at 5 (reporting median plaintiffs' attorneys' fees of $410,000 for disclosure settlements in 2015).

308. Corporations typically retain transaction advisors and, when claims are filed, separate litigation counsel, who charge a separate (substantial) fee. *See* Griffith & Lahav, *supra* note 99, at 1081 n.122 (reporting that the defense side cost to brief and argue a preliminary injunction motion could run to $1.5 million).

309. *See, e.g.*, Maric Capital Master Fund, Ltd. v. Plato Learning, Inc., 11 A.3d 1175, 1179 (Del. Ch. 2010).

310. *See supra* text accompanying note 292. Although a comparison of the substance of the SEC rules with the City Code or the Irish Rules is beyond the scope of this Article, it should be noted that the two systems are not incompatible. In practice, any conflicts may be resolved by the panels exercising their broad regulatory discretion to waive or derogate from a rule once there is compliance with the General Principles.

311. These would include, for example, the City Code, the Irish Rules, the Singapore Code on Take-Overs and Mergers, and the Corporations Act of 2001.

312. Regulatory capture occurs when a special interest persuades a regulator to deviate from the public interest in order to delivery private benefits to the interest group, as for example when a regulated industry persuades a government regulator to erect barriers to entry. *See, e.g.*, George J. Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3, 3 (1971).

regulation would seem to increase the risk of capture.[313] In the context of merger regulation, the standard source of this critique is management.[314] The fear would thus be that a regulatory panel might be more subject to capture from managerial interests than a judicial decision-maker. In response to this critique, we would point out first that our proposed code and panel-based system is neutral with regard to the substance of corporate law—neutral, that is, with regard to the appropriate balance between managerial versus shareholder interests. It is a recommendation only with regard to process or form. Thus, insofar as a state adopted our model of merger regulation but imposed a rule structure that excessively favored management interests, we would expect the standard mechanism—competition in the market for corporate law and investors' interest in efficient corporate governance rules—to correct any imbalance in due course.[315] Moreover, the standard focus on the special interests of management fails to account for the role of another interest group—the bar—on the development of corporate law.[316] As described in further detail below, the current shape of Delaware corporate law generally, and takeover jurisprudence in particular, largely reflects the interest of the corporate bar.[317] Thus, insofar as our model moves regulatory authority away from courtrooms and lawyers, it should reduce rather than increase this kind of capture. Further, the risk of capture could be further contained by carefully choosing the interests represented on the panel board.[318]

2. Procedural Reforms to Prevent Nuisance Suits

Because regulatory review does not replicate true adversarial litigation, we do not recommend that the panel review fully replace ex post litigation. While the panel can adequately address disclosure issues, including the disclosure of information suggesting possible conflicts of interest, it may be unable to uncover or provide relief for extensive harm to shareholders from conflicted or otherwise unfaithful managers. As a result, shareholder litigation remains an important outside option, even in a code and panel-based takeover regime.

313. *See* Posner, *supra* note 274.

314. *See, e.g.*, Cary, *supra* note 28 (claiming that Delaware law caters to management interests over the interests of shareholders and the public).

315. *See* Ralph K. Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251, 254 (1977); *see also* ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATION LAW 144 (1993) (describing the impact of charter competition on the structure of the rules governing the market for corporate control in the United States).

316. *See* Macey & Miller, *supra* note 77, at 46.

317. *See infra* Part IV.

318. The risk of regulatory capture is mitigated in Ireland and the United Kingdom by ensuring that the members of the U.K. and Irish Panels representing interest groups, once appointed, are completely independent. Should a conflict of interest arise with any particular member in a specific transaction, the member in question steps aside. *See* City Code, *supra* note 141, § 4 App. 9.5; Irish Rules, *supra* note 160, tbl.10.

However, given the demonstrated tendency of merger claims to devolve into nuisance litigation, we would build in a set of procedural protections—again mimicking the Anglo-Irish system—to prevent lawyers and litigants from imposing these costs on shareholders, corporations, and the corporate law. In particular, we would recommend a set of procedural rules implementing a modified fee shifting rule or, at a minimum, a provision barring corporations from paying plaintiffs' side fees. Fee shifting remains highly controversial in the United States, in large part because the system relies upon private litigation to right what are effectively public wrongs.[319] The statutory invalidation of fee shifting in Delaware, however, may say more about the political economy of Delaware corporate law than it does about the desirability of fee shifting per se.[320] Fee shifting, along with the absence of U.S.-style class action lawsuits, works well to control the extent of shareholder litigation in Ireland and the United Kingdom. Crucially, however, the takeover regimes in these jurisdictions provide an effective substitute to litigation as a mechanism for the basic protection of shareholder rights.[321] The panel in our model would play a fundamentally similar role. The backstop protection offered by the panel means it would no longer be necessary to rely on shareholder litigation as the sole means of protecting shareholder rights.

If the abolition of the shareholder class action or the imposition of fee shifting rules appear too extreme, a similar result might be attained by adopting a basic No Pay provision that would preclude the corporation from paying attorneys' fees and costs for specified outcomes in representative litigation. Corporations customarily pay such fees and costs in connection with shareholder class actions on the basis of the "corporate benefit" doctrine, a corollary to the "common fund" doctrine in equity.[322] The near certainty of a fee award under the corporate benefit doctrine has played a large part in fueling the explosive growth of merger litigation.[323] The obvious corrective, therefore, is a corporate law with the opposite default rule.[324]

Nothing prevents a state from adopting a statute to preclude the corporation from paying plaintiffs' attorneys' fees in connection with shareholder litigation unless the litigation recovered meaningful relief for shareholders, such as

319. *See* Choi, *supra* note 81.

320. *See infra* Section IV.A.

321. *See supra* Section II.C.

322. *See* Griffith, *supra* note 3, at 38-40 (noting that the common fund doctrine entitles plaintiffs' counsel to be paid from funds recovered in representative litigation); *id* at 3 (explaining that the corporate benefit doctrine extended the logic of the common fund doctrine to the derivative suit context, and that when a derivative suit results in non-monetary relief, the common benefit doctrine allows plaintiffs' counsel to be paid by the corporation, the recipient of the benefit and the party on whose behalf the lawyer was technically working); *id.* at 2 (noting that a further expansion of the doctrine led courts to apply the corporate benefit rationale to non-pecuniary relief in class actions as well as derivative suits).

323. *Id.*

324. *See* Griffith, *supra* note 100, at 16.

monetary recovery or, perhaps, monetary recovery of a specified amount.[325] Unlike fee shifting provisions, No Pay provisions do not seek to punish plaintiffs' lawyers. They simply refuse to pay for failure and force the shareholders to bear their own fees and costs. The likely effect of such a rule would be to cause entrepreneurial lawyers to abandon all but the most profitable claims—that is, those claims most likely to return a monetary award to shareholders at least equal to the statutory threshold amount. In a system where litigation is the only means of acquitting shareholder rights, such a rule may raise concerns. However, in a system such as the one we propose, where low-value and non-pecuniary shareholder rights are protected by means of an administrative panel, it is less of a risk to limit litigation to high value claims.[326]

Under our model, shareholder litigation would be reserved only for fraud or similarly grievous wrongs, precisely those claims that entrepreneurial plaintiffs' lawyers—that is, those who are not members of the "disclosure settlement bar"[327]—are willing and able to finance. Without expressly limiting litigation rights, the additional regulation will merely add a layer of additional cost to what is already widely acknowledged as a crisis in shareholder litigation. At the same time, administrative regulation should not be viewed simply as a substitute for shareholder litigation. It is a complement.[328] The goal here is to strike a balance that preserves litigation rights only for those claims that are worth preserving. In our view, this is best accomplished with a No Pay provision keyed to a common fund at a specified threshold value.

IV. Convergence Versus Persistence

Our account of the different modes of regulation employed in the American and the Anglo-Irish systems explained the evolution of those differences as a function of the divergent institutional interests and structural constraints operating within these systems.[329] After the takeover wave of the 1950s and 1960s, the influence of institutional shareholders and tradition of self-regulation pushed the United Kingdom to develop a system of administrative panels for takeover regulation. The United States, meanwhile, after ceding market regulation to the federal government in the 1930s, responded through

325. The common benefit doctrine is a common law default rule which can be altered by statute. *See* WILLIAM N. ESKRIDGE, JR., INTERPRETING LAW: A PRIMER ON HOW TO READ STATUTES AND THE CONSTITUTION 180 (2016) (noting that there is no longer a presumption against statutory derogation of common law and that statutes can override common law principles); *see also* A.W. Fin. Servs., S.A. v. Empire Res., Inc., 981 A.2d 1114, 1123 (Del. 2009) (acknowledging several ways in which statutory enactments can supplant the common law).

326. Additionally, we would advise states to adopt such statutes as default rather than mandatory provisions, allowing corporations to opt out through the corporate charter. However, we expect that this opt-out right would be rarely, if ever, invoked.

327. *See* Friedlander, *supra* note 3, at 909.

328. *See* Posner, *supra* note 274.

329. *See supra* Parts I & II.

amendments to the securities laws and the development of corporate law jurisprudence.[330] While this story may account for the emergence of different regulatory regimes, it does not account for their remarkable persistence. Path dependency weakens as an explanatory theory when the underlying institutional structures change.

In the intervening half-century, institutional investors have risen to prominence in the U.S. market to a point where they now hold the vast majority of the shares of the thousand or so largest companies.[331] Barriers to communication between institutional investors have also largely disappeared, and institutions now coordinate through organizations such as the Council on Institutional Investors (CII) and Institutional Shareholder Services (ISS).[332] Moreover, institutional investors and activists alike have shown a willingness to coalesce around corporate governance reforms, such as the dismantling of staggered boards and greater representation of independent directors on boards.[333] In light of the disappearance of these structural distinctions and the emergence of the crisis in merger litigation, why has the U.S. model not moved closer to the Anglo-Irish model? Alternatively, given the proliferation of cross-border mergers and acquisitions, global capital markets, and the spread of U.S.-style litigation, why has the Anglo-Irish system not moved closer to the U.S. system of regulation by litigation? Why, in other words, have the modes of regulation remained dissimilar in an era of convergence and globalization?

In this part, we consider the failure of convergence. We lay the blame not with any defect in the market for corporate charters but rather in the relative strength of different interest groups. The first section evaluates the strength of the interstate market for corporate charters in the United States. The second section considers the interests of the different interest groups that empower—and are empowered by—the alternative modes of regulation, focusing on the pivotal role of the corporate bar within the U.S. system. The third and final section briefly considers the ways in which the Anglo-Irish model may be moving closer to the litigation-centric U.S. model and asks whether further convergence in this direction is likely.

330. In turn, the institutional interests represented in the self-regulatory model, on the one hand, and the litigation model, on the other, may explain the differing substance of takeover regulation. *See* Armour & Skeel, *supra* note 124.

331. Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863 (2013) ("[T]he Berle-Means premise of dispersed share ownership is now wrong. In 2011, for example, institutional investors owned over 70% of the outstanding stock of the thousand largest U.S. public corporations.").

332. *See generally* COUNCIL OF INSTITUTIONAL INVS., http://www.cii.org/ [http://perma.cc/KD2R-S9LY]; INSTITUTIONAL SHAREHOLDER SERVS., http://www.issgovernance.com/ [http://perma.cc/MH9M-PGLU].

333. *See* Mira Ganor, *Why Do Managers Dismantle Staggered Boards?*, 33 DEL. J. CORP. L. 149, 151 (2008).

A. Barriers to Competition in the Market for Corporate Charters

The institutional context for corporate law change in the United States has been the interstate market for corporate charters and the threat of SEC pre-emption of state corporate lawmaking. Any state that wanted to adopt a regulatory structure similar to the one we articulated above could do so, as could the federal government by amendment to the securities laws. Moreover, if the structure promises the efficiencies we have claimed, the market for corporate charters would seem to give states a strong incentive to adopt a regulatory model similar to the one we have articulated in order to raise revenue by "selling" more corporate charters. The fact that no state has done so may belie the efficiencies that we have claimed. Or it may point to defects in the U.S. market for corporate charters.

Some have doubted the dynamism of competition in the market for corporate charters, observing that few states behave as if they are seeking to win business from Delaware.[334] Nevertheless, states do clearly react to retain corporations chartered in their state by adapting their corporate law in response to changes in other states.[335] Moreover, the idea that states neither compete to attract corporate charters, nor have anything to gain from doing so, is contradicted by the example of Nevada. Nevada actively and successfully competes with Delaware for corporate charters.[336] Because Nevada competes by providing broad exculpation for managers—for everything short of outright fraud[337]—it is cited as an example of the "race to the bottom."[338] Others dispute this characterization, arguing that Nevada law allows firms to save on the monitoring and litigation costs imposed by Delaware,[339] savings which may be of special appeal to smaller firms that are less able to absorb such costs.[340]

334. *See, e.g.*, Marcel Kahan & Ehud Kamar, *The Myth of State Competition in Corporate Law*, 55 STAN. L. REV. 679, 679 (2002).

335. Roberta Romano, *The States as a Laboratory: Legal Innovation and State Competition for Corporate Charters*, 23 YALE J. ON REG. 209, 237 (2006).

336. When Nevada flipped the default provision in its corporate law statute, changing exculpation from an opt-in right to an opt-out right, it enjoyed a significant net inflow of corporations in spite of also raising its franchise fee by 10,000%. Michal Barzuza, *Market Segmentation: The Rise of Nevada as a Liability-Free Jurisdiction*, 98 VA. L. REV. 935, 948-49 (2012).

337. *See* NEV. REV. STAT. § 78.037 (2010) (allowing exculpation of directors and officers for all but intentional misconduct); *cf.* DEL. CODE ANN. tit. 8, § 102(b)(7) (2011) (allowing companies to opt-in to exculpation except for allegations involving breach of the duty of loyalty, lack of good faith, intentional misconduct, knowing violations of law, or transactions in which the directors receive an improper personal benefit).

338. *See* Barzuza, *supra* note 336, at 940, 994 (describing Nevada as a haven for managers seeking private benefits of control); *see also* Michal Barzuza & David C. Smith, *What Happens in Nevada? Self-Selecting into Lax Law*, 27 REV. FIN. STUD. 3593 (2014) (finding that firms incorporated in Nevada are 30-40% more likely to restate their financial results than firms incorporated in other states).

339. *See* Bruce H. Kobayashi & Larry E. Ribstein, *Nevada and the Market for Corporate Law*, 35 SEATTLE U. L. REV. 1165 (2012).

340. *See* Ofer Eldar & Lorenzo Magnolfi*, Regulatory Competition and the Market for Corporate Law* 4 (Yale Law & Econ. Working Paper No. 528, 2016), http://papers.ssrn.com/sol3

Putting aside the debate over which state has better law, it is clear that Nevada and Delaware compete.

But even if the market for corporate charters is somewhat competitive, there may still be significant barriers to entry into the market. Delaware has been the dominant state of incorporation for more than a century. New entrants would encounter switching costs and network effects as well as commitment problems. As described in greater detail below, these barriers center around the pivotal role of Delaware law, the advantages of Delaware's judiciary, and the influential role of the Delaware corporate bar.

1. Switching Costs and Network Externalities

Switching costs arise in markets where repeat buyers require similar or compatible products.[341] The buyers' need for interoperable products creates economies of scope for the provider of such products and imposes a cost on firms for switching away from that provider.[342] In the market for corporate charters, the repeat buyers are not the corporations themselves, but rather the corporate lawyers that advise them.[343] Most corporate lawyers are familiar with Delaware law—often only with Delaware law—and would accordingly experience significant costs if forced to learn and apply a different set of rules.[344] Delaware's continued dominance, in other words, may result as much from lawyers' path dependence as it does from a superior corporate law product.[345]

Closely related to switching costs are network effects. Network effects arise when a product becomes more valuable as the number of users increase.[346] As

/papers.cfm?abstract_id=2685969 [http://perma.cc/DZZ3-J69G] (finding that firms that choose Nevada are predominantly smaller firms with low institutional shareholdings).

341. Joseph Farrell & Paul Klemperer, *Coordination and Lock-In: Competition with Switching Costs and Network Effects*, *in* INDUSTRIAL ORGANIZATION HANDBOOK 1967, 1971 (Mark Armstrong & Robert Porter eds., 2007) ("Switching costs arise if a consumer wants a group, or especially a series, of his own purchases to be compatible with one another: this creates economies of scope among his purchases from a single firm.").

342. *Id.*

343. Firms typically choose where to incorporate only once and therefore do not anticipate purchasing a series of charters from the state. The lawyers advising them, however, may steer firms to one state or another, and their familiarity with the law of various jurisdictions may play a decisive role.

344. William J. Carney et al., *Lawyers, Ignorance, and the Dominance of Delaware Corporate Law*, 2 HARV. BUS. L. REV. 123, 129 (2012) (providing survey evidence showing that lawyers' ignorance of other states' laws leads them to recommend Delaware incorporation).

345. Robert Anderson IV & Jeffrey Manns, *The Delaware Delusion*, 93 N.C. L. REV. 1049, 1052 (2015) (providing empirical evidence to argue that "Delaware's appeal is driven by lawyers' default decision making based on Delaware's past preeminence and reflects lawyers' failure to assess the value added by Delaware compared to other states"); *see also* Brian J. Broughman & Darian M. Ibrahim, *Delaware's Familiarity*, 52 SAN DIEGO L. REV. 273, 291 (2015) (arguing from IPO data that investor familiarity rather than network externalities explains Delaware's dominance).

346. *See* Farrell & Klemperer, *supra* note 341, at 1971 ("Network effects arise when a user wants compatibility with other users so that he can interact or trade with them, or use the same complements; this creates economies of scope between different users' purchases."); *see also* DAVID

people begin to use telephones, email accounts, or Facebook pages, they generate "network externalities," attracting new users not only by the inherent qualities of the product itself but also by virtue of its widespread use.[347] Michael Klausner has posited the existence of network effects in connection with Delaware corporate law, focusing largely on judicial opinions.[348] In his words:

> A judicial opinion that interprets one corporation's contract term in effect embeds that interpretation in the contracts of all firms that use the same term. The more firms that have adopted a particular term, the more likely it is the term will be litigated, and therefore the more likely that future judicial interpretations will be provided.[349]

Delaware corporate law is valuable, in other words, because the large number of firms incorporated in Delaware ensures that its courts will have occasion to provide guidance on a large number of corporate law concerns, affecting not only the litigants in the particular dispute, but all firms incorporated in Delaware. Furthermore, the reduction in uncertainty may attract further incorporations in the state, a feedback loop described by Roberta Romano:

> [T]he more firms there are in Delaware, the more legal precedents will be produced, further providing a sounder basis for business planning, which attracts even more firms to that state. Finally, the more corporate law cases that are brought, the greater will be the expertise of the Delaware judges, as will be the value to an individual from developing such expertise as a member of the judiciary.[350]

The principal network externality of Delaware corporate law is thus the current existence and future assurance of a large body of judicial precedent. Furthermore, Delaware may increase its advantage by devising a particularly difficult to copy body of precedent.[351]

SINGH GREWAL, NETWORK POWER: THE SOCIAL DYNAMICS OF GLOBALIZATION (2008) (noting how network growth makes norm defection prohibitively costly).

347. Farrell & Klemperer, *supra* note 341, at 43-44.

348. *See* Michael Klausner, *Corporations, Corporate Law, and Networks of Contracts*, 81 VA. L. REV. 757, 761 (1995) (suggesting that network effects may reduce the cost of legal services due to lawyers' familiarity with Delaware law). Although this is a theoretical possibility, the legal costs of Delaware incorporation once litigation exposure is factored in seem to be substantial. Legal services may therefore fit better as a switching cost, discussed above.

349. *Id.* at 776 ("[T]he expected quantity and frequency of judicial interpretations is positively related to the number of firms that adopt the term. Thus, to the extent that future judicial interpretations are beneficial, they are network benefits associated with particular corporate contract terms.")

350. ROMANO, *supra* note 315, at 44.

351. Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908, 1910 (1998) ("Delaware law may be less determinate than is optimal."). Kamar goes on to note, "Although indeterminacy diminishes the value to corporations of Delaware law, it diminishes the value of rival laws to a greater extent by stymying their compatibility with Delaware law." *Id.*

Switching costs and network externalities suggest that even if another state were to introduce improvements on the substantive corporate law, perhaps by reducing the cost of nuisance litigation, firms might be reluctant to reincorporate in the other state and their lawyers might be even more reluctant to advise them to do so.

2. Commitment Problems

A second barrier to entry is the difficulty other states may encounter in making a credible commitment to maintaining a superior corporate law product. Firms shopping for a state of incorporation might reasonably fear that states will defect, as New Jersey did, from an otherwise public, pro-corporate orientation.[352] Likewise, corporations may fear that states will raise the cost of incorporation, perhaps by succumbing to the pressure of the corporate bar, once firms locate there—effectively adopting the "bargain-then-rip-off" pricing strategy made famous by retailers everywhere.[353] Delaware, by contrast, has a special ability to credibly commit not to behave opportunistically in the making of corporate law.

Delaware's commitment not to behave opportunistically is credible because the state derives such a large portion of its revenues from corporate franchise fees, the loss of which would throw the state into an immediate fiscal crisis.[354] The loss of franchise fee revenue would force legislators to make up the shortfall either by cutting services or by raising taxes on the electorate—both unpalatable options. The obvious importance of avoiding this outcome makes Delaware's commitment to corporate responsiveness highly credible.

It may be difficult for other states to match the credibility of this commitment. In particular, larger states with other significant sources of revenue may be able to weather the loss of franchise tax revenue better than Delaware. The less dependent a state is on franchise tax revenue, the less credible that state's commitment will be to maintaining a responsive, pro-corporate regime. This theory suggests that Delaware's most effective competitors may be relatively small states with few outside sources of revenue and few dominant in-state businesses.[355] States such as Rhode Island, Maine, and Idaho, for example, would thus seem more likely competitors than California, New York, and Illinois.

Nevertheless, as the Nevada example illustrates, these barriers to entry are not insurmountable. States do compete for corporate charters and there is the

352. *See supra* Section I.A.

353. *See* Farrell & Klemperer, *supra* note 341, at 8.

354. *See* Michael Barzuza, *Price Considerations in the Market for Corporate Law*, 26 CARDOZO L. REV. 127, 181-82 (2004) (noting that "Delaware's revenues from its franchise tax amount to approximately twenty percent of its total revenues" and providing further statistics on Delaware's corporation-related revenues and costs).

355. In-state businesses can lead to distortions that equally affect outside incorporations. Pennsylvania, for example, adopted a strong anti-takeover law in the 1980s at the behest of the steel industry.

potential to generate significant revenue from this competition. So what explains the failure of states to respond to the crisis in shareholder litigation, if not with the exact package we have proposed, then perhaps with a set of proposals designed to arrive at a similar outcome? The explanation, we argue below, lies with the set of interests in each system that controls corporate law innovation.

B. Interest Group Capture

Interest groups have a large role in determining the form and content of any regulatory regime. Aside from their managerial and shareholder clients, the corporate bar is the interest group with the largest stake in the development of U.S. corporate law.[356] The corporate bar, of course, has a strong interest in maximizing fee income from both deal flow and litigation. And the corporate bar, as we explore, exerts decisive influence over the development of Delaware corporate law. In Delaware, as in other U.S. states, "[l]egislative initiatives in corporate law originate with the corporate bar."[357]

Not only is the bar a politically powerful interest group, organized into guilds and associations to lobby for their interests, the corporate bar controls the corporate law. "Delaware lawyers . . . *are* the Delaware legislature, at least insofar as corporate law is concerned."[358] Changes to the Delaware statute typically originate with the Delaware bar and receive no legislative resistance or even review.[359] The formal organ through which the bar exerts this authority is the Corporation Law Section of the Delaware State Bar Association and, in particular, the governing body of that group, the "Council."[360] As described in greater detail by a member of that organization:

> The Council currently consists of twenty-one members, formally elected annually by the members of the Corporation Law Section. A number of informal traditions guide the selection of nominees to the Council. As a matter of practice, and in recognition of the size of their corporate practice groups, seven of the large commercial law firms in Wilmington have nominated two members each; the other members practice in smaller firms (or in my case, teach), all in Wilmington. The members are about evenly distributed between those whose practices

356. Jonathan R. Macey & Geoffrey P. Miller, *Toward an Interest-Group Theory of Delaware Corporate Law*, 65 TEX. L. REV. 469, 491 (1987).

357. ROMANO, *supra* note 315, at 11.

358. Larry E. Ribstein, *Delaware, Lawyers, and Contractual Choice of Law*, 19 DEL. J. CORP. L. 999, 1009 (1994).

359. Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 885, 898 (1990) (explaining that changes to the statute originate with the Senate Judiciary Committee but reporting a committee member's view that "if a corporate law bill has the support of the Delaware Bar Association and the Secretary of State's office, then it is passed without amendment or debate"); Lawrence Hamermesh, *The Policy Foundations of Delaware Corporate Law*, 106 COLUM. L. REV. 1749, 1754-55 (2006) ("The members of the Delaware General Assembly . . . have not taken on any significant role in initiating or drafting changes to the DGCL. Nor are those amendments the product of any legislative staff, or of any lobbyists engaged by individual businesses.").

360. *See* Hamermesh, *supra* note 359, at 1755.

> concentrate on litigation and those whose practices gravitate toward transactional counseling. Also as a matter of practice, the members of the Council include a number of lawyers—a small minority, to be sure—whose litigation practice is dominated by representation of shareholder plaintiffs. In 2005, after one Wilmington firm had developed an ongoing client base of public institutional investors, the size of the Council was expanded to permit that firm to nominate a member. Notably absent from the Council, on the other hand, are any in-house lawyers (i.e., lawyers employed by and primarily representing a single business), any non-Delaware lawyers, and with one exception, any lawyers from firms not principally based in Delaware.[361]

This guild of local corporate practitioners controls amendments to the Delaware General Corporation Law. Although they work subject to the norm that they "leave parochial client interests behind when proposing corporate legislation,"[362] their deliberations are secret.[363] It would therefore not be unreasonable to suppose that even when they succeed in leaving behind client interests, they do not leave behind their own.

A stark example of the Council's work is the recent legislative overruling of fee shifting bylaws. Immediately after the *ATP Tour* decision authorized fee shifting bylaws,[364] the Delaware bar, recognizing the existential threat, responded in less than two weeks with a proposed amendment to the Delaware General Corporation Law that would restore the status quo ante.[365] The amendment, which imposed a per se ban on fee shifting,[366] was formally introduced into the Delaware State Senate on June 3, 2014 with every expectation that it would soon pass.[367] The hasty process was derailed, however, after significant lobbying from the Chamber of Commerce produced a resolution holding up the legislation for "continued examination" of the issue.[368] This

361. *Id.* at 1755-56.

362. LEWIS S. BLACK, JR., WHY CORPORATIONS CHOOSE DELAWARE 4 (1999).

363. Hamermesh, *supra* note 359, at 1756.

364. *See supra* Section I.D.1.

365. S.B. 236, 147th Gen. Assemb., Reg. Sess. (Del. 2014) (noting that the amendment "is intended to limit applicability of [*ATP Tour*] to non-stock corporations").

366. *See id.* § 331 ("Notwithstanding any other provision of this chapter, neither the certificate of incorporation nor the bylaws of any corporation may impose monetary liability . . . on any stockholder of the corporation.").

367. *Id.* (contemplating an August 1 effective date); *see also* Daniel Fisher, *Is Delaware Law a Favor to Plaintiff Lawyers, or Shareholder Protection?*, FORBES (June 10, 2014), http://www.forbes.com/sites/danielfisher/2014/06/10/is-delaware-law-a-favor-to-plaintiff-lawyers-or-protection-for-capitalists/ [http://perma.cc/5WZ6-2DCQ] (describing the path of Senate Bill 236 through the Delaware legislature, including that S.B. 236 was "drafted with near-unanimous approval by the members of the Council and Senate sponsors").

368. *See, e.g.*, Letter from C. Michael Carter, President & Chief Operating Officer, Dole Food Co., Inc., to Bryan Townsend, Senator, Del. Gen. Assembly (June 9, 2014) (on file with author); Letter from Lisa A. Rickard, President, Inst. for Legal Reform, U.S. Chamber of Commerce to Members of the Del. Gen. Assembly (June 9, 2014) (on file with author); Letter from Andrew Wynne, Dir. of State Legislative Affairs, U.S. Chamber of Commerce, to Bryan Townsend, Senator, Del. Senate (June 5, 2014) (on file with author); *see also* S.J. Res. 12, 147th Gen. Assemb., Reg. Sess. (Del. 2014) (calling on "the Delaware State Bar Association, its Corporation Law Section, and the Council of that Section . . . to

resulted in a nine-month delay, after which, on June 11, 2015, the Delaware legislature enacted the exact same provision that had been proposed nine months before, without any change in substance or in wording. Tellingly, there was no evidence of "continued examination" in the twelve-page memorandum the Council released defending its actions.[369] The memorandum contained no serious analysis of fee shifting or any discussion of alternatives. None of the voluminous literature on the effects of fee shifting on litigation was cited.[370] The only citations to secondary literature were to three short pieces written by practitioners.[371] Rather than demonstrating careful study of the issue, the memorandum reads like rhetorical cover for an entrenched group exerting control to protect its interests.

We assume the bar's principal interest in corporate law reform lies in protecting its fee revenue.[372] This interest will not necessarily produce a corporate law that is unbalanced in favor of either managers or shareholders. Delaware law, it is often said, must retain a balance between shareholder and managerial interests, and balance is in the bar's interest as well.[373] If the corporate law becomes too slanted toward shareholder interests, management may seek to move the corporation from Delaware to a friendlier jurisdiction.[374] Fewer Delaware corporations means fewer potential clients and lower expected fee revenues. Likewise, if the corporate law becomes too slanted toward managerial interests, the federal government may intervene by effectively taking all or a part of the corporate law away from the state.[375] Federal preemption reduces the scope of matters on which the Delaware bar can advise, also eroding its fee base. The Delaware bar's interests thus are largely aligned with the state's in making changes to the corporate law to maximize the number of incorporations. However, if the problem is the volume and typical outcome of litigation itself—what we have described as the crisis in U.S. shareholder

continue its ongoing examination of the State's business entity laws with an eye toward maintaining balance, efficiency, fairness and predictability").

369. *See* DEL. STATE BAR ASS'N, EXPLANATION OF COUNCIL LEGISLATIVE PROPOSAL (2015).

370. *See* Avery W. Katz & Chris W. Sanchirico, *Fee-Shifting*, *in* 2 PROCEDURAL LAW & ECONOMICS, ENCYCLOPEDIA OF LAW AND ECONOMICS 271-72 (Chris William Sanchirico ed., 2012) (surveying the extensive literature on the effects of fee shifting and summarizing "the main lesson" as "the effects of cost shifting on the amount and intensity of litigation are substantially more complicated than a superficial consideration of the matter might suggest").

371. *See* DEL. STATE BAR ASS'N, *supra* note 369.

372. *See* Macey & Miller, *supra* note 77, at 3.

373. *See, e.g.*, Sean J. Griffith, *Good Faith Business Judgment: A Theory of Rhetoric in Corporate Law Jurisprudence*, 55 DUKE L.J. 1, 69 (2005) (describing how the importance of balance has been expressed in Delaware corporate law decisions).

374. *See* Jeffrey N. Gordon, *Corporations, Markets, and Courts*, 91 COLUM. L. REV. 1931, 1959 n.95 (1991) (noting that practitioners threatened to leave Delaware for more hospitable domiciles).

375. *See* Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 616 (2003) (emphasizing Delaware's competition with the SEC); *see also* Griffith, *supra* note 373 (analyzing the evolution of jurisprudential standards in Delaware in light of the threat of federal pre-emption)

litigation—the bar would seem to be significantly less motivated to correct it, especially when no other state is promoting itself as a jurisdiction serious about limiting nuisance litigation.[376] Even Nevada, in spite of its emphasis on minimizing the threat of managerial liability, has proven to be a haven for merger litigation and disclosure settlements.[377] This likely reflects the interests of the Nevada bar—as long as managerial liability is not a real risk, as in disclosure settlements, litigation can serve the interests of the bar without compromising the basic promise of Nevada incorporation.

The situation in the United Kingdom and Ireland is markedly different because there "the lawyers miraculously disappear."[378] The tradition of self-regulation in the United Kingdom has meant that a different and broader constituency has had a hand in designing the substantive law, thus limiting the opportunity for the corporate bar to exert control in furtherance of its own interests. From a process perspective, meanwhile, the entire system was devised to avoid the general courts and, not coincidentally, litigators. Although, as noted above, corporate lawyers together with financial advisers play an important role in ensuring compliance with the City Code and Irish Rules and in liaising with the panels and making submissions on behalf of their clients, this generally remains a less confrontational exercise than in the United States. In addition, with limited recourse to judicial review, the U.K. and Irish Panels are generally the final arbiters, and the entire process involves less time and legal expense. The result is a radically different interest group dynamic that counterbalances the influence of the bar, preventing lawyers from using the regulatory process to extract rents.

Back in the United States, the interests of the corporate bar in maximizing fee revenue from shareholder litigation can only raise the cost of Delaware incorporation.[379] At some point, these costs might grow to a level that spurs managers and shareholders to reconsider their options.[380] But before this can happen, another state needs to be able to offer a credible alternative, such as our proposal, that is less vulnerable to being commandeered by the bar. Unfortunately, this kind of innovation seems possible only where a state's

376. The interests of the bar may also explain the highly fact-specific nature of Delaware jurisprudence, always in need of a lawyer to interpret it. *See* Douglas M. Branson, *Indeterminacy: The Final Ingredient in an Interest Group Analysis of Corporate Law*, 43 VAND. L. REV. 85, 112-13 (1990).

377. *See* Jeffrey S. Rugg, *Strike Suit Certainty Remains the Status Quo in Nevada*, LAW360 (Aug. 11, 2015), http://www.law360.com/articles/689917/strike-suit-certainty-remains-the-status-quo-in-nevada [http://perma.cc/3CVM-W5E9] (describing several merger class actions brought in Nevada that ended in disclosure settlements).

378. *See* Armour & Skeel, *supra* note 124, at 1744.

379. *See* Macey & Miller, *supra* note 77, at 3.

380. Stephen M. Bainbridge, *Fee-Shifting: Delaware's Self-Inflicted Wound*, 40 DEL. J. CORP. L. 851 (2016); Paul Atkins, *CA Has Hollywood, TX Has Oil, Delaware Corporations*, REAL CLEAR MKTS., (June 11, 2015), http://www.realclearmarkets.com/articles/2015/06/11/ca_has_hollywood_tx_has_oil_delaware_corporations.html [http://perma.cc/Q422-33E2].

corporate law is not already captured by the bar, as indeed it may be in most, if not all, U.S. states.

C. A Larger Role for Litigation in the Anglo-Irish System?

There is no movement in either Ireland or the United Kingdom to move closer to U.S. corporate law in matters of substance. The "no-frustration" rule, for example, is safely ensconced in Ireland and the United Kingdom, and both countries remain committed to an open market for corporate control.[381] But U.S. lawyers and U.S.-style litigation have made some inroads on the other side of the Atlantic.

While it remains highly unusual for any litigation to be initiated in the U.K. or Irish courts in relation to the takeover or merger of public companies,[382] the takeover of former U.S.-based companies incorporated in Ireland by way of corporate inversions may have increased the likelihood of U.S.-style litigation in Ireland.[383] For example, in 2013, such a company, the subject of a hostile bid, sought an injunction prohibiting a bidder from distributing a proxy statement filed in the United States on the basis that it did not comply with the Irish Rules. The parties ultimately agreed in court that the matter should be resolved by the panel pursuant to the Irish Rules.[384] Revealingly, the Chairperson of the Irish Panel used its 2013 *Annual Report* to express the panel's hope that this case was not the start of a trend towards a more litigious approach to public takeovers. In his words:

> If parties do resort to the courts more frequently to resolve issues arising in connection with takeovers, such actions may introduce legal uncertainty into the takeover process and may run the risk of prolonging the bid timetable all of which is unlikely to be in the best interests of shareholders and the market in general. The Panel is an expert group with significant experience in applying its own rules and in dealing with issues arising during the course of a takeover. Since its

381. Although debated following the 2010 takeover of UK-based Cadbury by the U.S. conglomerate Kraft, the no-frustration rule remained in place, and the government adamantly rejected "economic nationalism." *See* Dep't for Bus., Innovation & Skills, *Getting the UK Takeover Framework Right*, U.K. GOV'T (June 1, 2010), http://www.gov.uk/government/news/getting-the-uk-takeover-framework-right [http://perma.cc/Y639-LQ8G] (reporting Minister Vince Cable's comments on the Panel's consultation).

382. Shareholders do in theory retain statutory rights of action against directors for oppression or unfair prejudice. *See* Corporations Act 2006, c. 46, § 994 (UK); Corporations Act 2014, § 212 (Ir.). However, the authors are not aware of any such actions in the context of a takeover regulated by either panel. Furthermore, as noted above, judicial review of panel actions in both the United Kingdom and Ireland is restricted. The options for further litigation are thus limited.

383. *See* Eric L. Talley, *Corporate Inversions and the Unbundling of Regulatory Competition*, 101 VA. L. REV. 1649 (2015) (discussing the flood of corporate inversions and its implications for U.S. corporate governance).

384. IRISH TAKEOVER PANEL, *supra* note 160, at 5 (Chairperson's Statement).

> establishment the Panel has sought to ensure that matters arising during the course of a takeover are dealt with expeditiously.[385]

This statement reveals the value that the Irish Panel and its core constituencies place on speed, certainty, and expertise in the context of public takeover bids as well as the concern that these values would be imperiled by a trend towards greater litigation in common law courts. Nevertheless, there is evidence that the trend continued. Two years later, another inverted company, Perrigo Company, sought declaratory and injunctive relief against a hostile bidder in a case featuring multiple class action suits filed in the United States against the hostile bidder, its directors, and later, Perrigo and its former CEO.[386] Similar actions against companies undergoing inversions regulated by the Irish panel have ended in disclosure settlements in U.S. courts.[387] A panel-based model does not necessarily foreclose litigation.

In spite of the tendency of U.S.-style litigation to follow U.S. companies overseas, there is no real pressure in the United Kingdom or Ireland to reform legal procedures to introduce class actions. Although the Irish Law Reform Commission in 2005 acknowledged certain advantages afforded by the U.S.-style class action procedure, it identified more significant disadvantages including a loss of autonomy for class members, arbitrary results, high legal costs, and "a litigious climate" that "target[s] 'deep-pocket' defendants."[388] It recommended instead a formal multi-party action procedural structure, which would operate on an opt-in basis.[389] These recommendations have not yet been acted upon.

Conclusion

We have articulated an alternative form of merger regulation to the dominant U.S. model of regulation by litigation. Our code and panel-based proposal, built on the U.K. and Irish examples, offers numerous advantages to the standard litigation-centric model. These advantages include enhanced predictability, speed, and flexibility, with lower overall administrative expense. Delaware's Court of Chancery promises some of these same advantages, but Delaware is unique among state courts in this regard. Many states do not have the corporate law caseload to build a comparable body of precedent or similar

385. *Id.* at 6.

386. Mylan N.V., Quarterly Report (Form 10-Q) 52-53 (2015). The actions against Perrigo and its former CEO include *Roofers Pension Fund v. Papa,* No. 2:16-cv-02805-MCA-LDW, 2017 WL 1099226 (D.N.J. Mar. 20, 2017), and *AMI – Government Employees Provident Fund Management Co. v. Papa,* No. 1:16-cv-04752 (S.D.N.Y. July 12, 2016).

387. *See, e.g.*, Taxman v. Covidien, No. 1:14-cv-12949 (D. Mass. Sept. 21, 2015).

388. *Report: Multi-Party Litigation*, LAW REFORM COMM'N 56 (2005), http://www.lawreform.ie/_fileupload/Reports/Report%20Multi-party%20litigation.pdf [http://perma.cc/LQ5S-Y8LR].

389. *Id.* at 3.

depth of judicial expertise. A code and panel-based model may thus present a more efficient model for another state seeking to compete with Delaware in the market for corporate charters. Moreover, the code and panel-based model would allow a state to copy Delaware's signal advantages without also importing its principal weakness—that is, capture by the interests of the corporate bar.

That no state has experimented with a code and panel-based model may reflect the central role played by the bar in most law reform efforts. Because its principal source of savings comes from limiting the ability of the corporate bar to extract rents, the impetus for developing a code and panel-based regime of merger regulation will likely need to come from outside the practicing bar. However, given the current crisis in shareholder litigation, the time may be ripe for reform.