Client Alert

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Delaware Chancery Court Rejects Disclosure-Only Settlement in Trulia/Zillow Merger Litigation, Making Clear Such Settlements Will Be Subject to "Increasingly Vigilant" Scrutiny

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On January 22, 2016, Delaware Chancellor Andre C. Bouchard rejected a proposed "disclosure-only" settlement in *In re Trulia Stockholder Litigation*.[1] The decision confirms the Chancery Court's growing skepticism for disclosure-only settlements in merger litigation.

In *In re Trulia*, the Delaware Chancery Court rejected a proposed disclosure-only settlement of a shareholder suit challenging the merger between Trulia and Zillow. In declining to approve this proposed settlement, Chancellor Bouchard explained that "to the extent that litigants continue to pursue disclosure settlements, they can expect that the Court will be increasingly vigilant in scrutinizing the 'give' and the 'get' of such settlements to ensure that they are genuinely fair and reasonable to the absent class members."[2]

In re Trulia continues the recent trend in Delaware closely scrutinizing disclosure-only settlements of merger cases. For example, in *In re Riverbed Technology, Inc. Stockholders Litigation*, Vice Chancellor Glasscock approved a proposed disclosure-only settlement, but expressed concern about the practice of settling merger challenges (and releasing shareholders' claims) based on supplemental disclosures. The Court noted that reliance on the Court's previous practice of approving these settlements "will be diminished or eliminated going forward in light of this Memorandum Opinion and other decisions of this Court."[3] Vice Chancellor Glasscock explained that, in the future, "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."[4]

BACKGROUND

In re Trulia involved a proposed settlement of a stockholder class action challenging Zillow, Inc.'s acquisition of Trulia, Inc. in a stock-for-stock merger that was announced in July 2014 and closed in February 2015. Under the merger agreement, Zillow would acquire Trulia for approximately $3.5 billion in stock.

After the announcement of the merger, in four nearly identical class action complaints, Trulia stockholders sought to enjoin the proposed merger alleging breaches of fiduciary duties by Trulia directors in approving the proposed merger at an unfair exchange ratio. On October 13, 2014, the court granted an unopposed motion to consolidate the four cases into one action and to appoint lead counsel.

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[1] *In re Trulia, Inc. Stockholder Litig.*, C.A. No. 10020-CB, 2016 Del. Ch. LEXIS 8 (Del. Ch. Jan. 22, 2016).

[2] Id. at *4-*5.

[3] C.A. No. 10484-VCG, 2015 Del. Ch. LEXIS 241, at *20 (Del. Ch. Sept. 17, 2015).

[4] *In re Trulia Stockholder Litig.*, 2016 Del. Ch. at *21-*22.

Nearly four months after these challenges, the parties reached an agreement-in-principle to settle. On November 19, 2014, the parties entered into a Memorandum of Understanding detailing the agreement-in-principle to settle the litigation for certain disclosures to supplement those contained in the proxy. Under the proposed settlement, Trulia, Inc. agreed to provide additional information in its proxy materials, and plaintiffs agreed to drop their motion to preliminarily enjoin the merger and would provide a release of claims on behalf of a proposed class of Trulia's shareholders. After receiving briefing and an affidavit from plaintiffs advocating for approval of the settlement, on September 16, 2015, Chancellor Bouchard held a hearing to consider the fairness of the proposed settlement.

THE COURT'S ANALYSIS

In a January 22, 2016, decision, Chancellor Bouchard wrote that "[u]nder Court of Chancery Rule 23, the Court must approve the dismissal or settlement of a class action," and that "the fiduciary character of a class action requires the Court to independently examine the fairness of a class action settlement before approving it."[5] The Court added that "[i]n doing so, the Court evaluates not only the claim, possible defenses, and obstacles to its successful prosecution, but also the reasonableness of the 'give' and the 'get,' or what the class members receive in exchange for ending the litigation."[6]

The Court highlighted the difficulties of evaluating the fairness of a proposed settlement when "little or no motion practice has occurred and the discovery record is sparse, as is typically the case in an expedited deal litigation leading to an equally expedited resolution based on supplemental disclosures before the transaction closes."[7] The Court pointed out that "[i]n this case, . . . no motions were decided . . . , and discovery was limited to the production of less than 3,000 pages of documents and the taking of three depositions . . . ."[8] This "lack of an adversarial process often requires that the Court become essentially a forensic examiner of proxy materials so that it can play devil's advocate in probing the value of the 'get' for stockholders in a proposed disclosure settlement."[9]

The Court offered that "the optimal means by which disclosure claims in deal litigation should be adjudicated is outside the context of a proposed settlement so that the Court's consideration of the merits of the disclosure claims can occur in an adversarial process where the defendants' desire to obtain a release does not hang in the balance."[10]

Under these circumstances, the Court held that the proposed settlement was not fair or reasonable to Trulia stockholders. The Court found that none of the four specific supplemental disclosures in this matter "were material or even helpful to Trulia's stockholders."[11] Chancellor Bouchard explained that "[a]s such, from the

[5] Id. at *13.

[6] Id. at *13 (internal quotation marks omitted).

[7] Id. at *21.

[8] Id. at *21.

[9] Id. at *22.

[10] Id. at *29.

[11] Id. at *60; *see also* id. at *39-*40 (identifying the supplemental disclosures as solely concerning a section of the proxy summarizing a financial analysis of the transaction, "providing additional details concerning: (1) certain synergy numbers in . . . value creation analysis; (2) selected comparable transaction multiples; (3) selected public trading multiples; and (4) implied terminal EBITDA multiples for a relative cash flow analysis.").

perspective of Trulia's stockholders, the 'get' in the form of the Supplemental Disclosures does not provide adequate consideration to warrant the 'give' of providing a release of claims to defendants and their affiliates . . . ."[12]

Most significantly, the Court warned practitioners of "enhanced judicial scrutiny" of disclosure settlements and that "practitioners should expect that the Court will continue to be increasingly vigilant in applying its independent judgment to its case-by-case assessment of the reasonableness of the 'give' and 'get' of [disclosure] settlements . . . ."[13] An exception, however, might be "supplemental disclosures address[ing] a plainly material misrepresentation or omission" where "the subject matter of the proposed release is narrowly circumscribed."[14]

CONCLUSION

In *In re Trulia*, Chancellor Bouchard explained that Delaware courts will closely scrutinize disclosure settlements and will assess the reasonableness of the "give" and "get" of such settlements. Chancellor Bouchard stressed that "the historical predisposition that has been shown towards approving disclosure settlements must evolve," and future proposed disclosure-only merger litigation settlements will likely be met with significant skepticism in Delaware. Thus, while the court stated that "[t]he percentage of settlements in Delaware based solely on supplemental disclosures was 63.6% in 2013 and 70.6% in 2014,"[15] this may be a declining trend in Delaware in years to come.

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[12] Id. at *60.

[13] Id. at *35.

[14] Id. at *35.

[15] Id. at n.28.