

# DELAWARE BUSINESS COURT INSIDER

## Chancery Upholds Shareholder Representative Structure and Refuses to Treat Sellers as Real Parties in Interest

In *Fortis Advisors v. Allergan W.C. Holding*, the counterparty sought to bypass the agreed-upon shareholder representative by moving to treat the selling stockholders as parties for purposes of discovery and trial.

By **Barry M. Klayman and Mark E. Felger** | June 10, 2020



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Selling stockholders in a buy-sell agreement typically designate a shareholder representative to act as their agent and attorney-in-fact with respect to all matters relating to the agreement, including acting on their behalf in connection with any claims under the agreement. The shareholder representative structure promotes efficiency in closing the deal and in adjudicating post-closing disputes. In *Fortis Advisors v. Allergan W.C. Holding*, C.A. No. 2019-0159-MTZ (Del. Ch. May 14, 2020), the counterparty sought to bypass the agreed-upon shareholder representative by moving to treat the selling stockholders as parties for purposes of discovery and trial. Vice Chancellor Morgan T. Zurn denied the motion, holding that the merger agreement’s shareholder representative structure identified the shareholder representative as the real party in interest and did not give the shareholder representative control over the selling stockholders’ discoverable material.

The case arose out of the merger between Allergan and Oculeve. Under the merger agreement, the selling stockholders appointed Fortis Advisors to be the shareholder representative, acting as their “sole, exclusive, true and lawful agent, representative and attorney-in-fact” with respect to any and all matters relating to the merger agreement, including contingent payments. The agreement provided that “all actions, notices, communications and determinations” by or on behalf of the selling stockholders would be made by the shareholder representative. The agreement did not give the shareholder representative access to the individual sellers’ books and records.

A dispute arose between Allergan and Fortis over the selling stockholders' entitlement to post-closing milestone payments under the merger agreement. For the selling stockholders to earn the milestone payment, Allergan's medical device had to achieve a specific approval from the FDA within a specified deadline. After the FDA gave its approval, Allergan refused to make the milestone payment on the grounds that the FDA's authorization did not meet the contractual requirements. Fortis, as the shareholder representative, filed suit against Allergan and claimed that Allergan had materially breached the merger agreement by failing to make the milestone payment and by not using commercially reasonable and good faith efforts to achieve the specific FDA approval by the contract deadline.

Allergan served document requests on Fortis that purported to require Fortis to produce documents in the possession of the sellers, which included over 50 individual, nonparty former stockholders in Oculeve. Fortis objected to the requests on the grounds that the sellers were not parties to the action, and said it would limit its response and any production of documents on behalf of itself only. Allergan then moved for an order requiring the former Oculeve stockholders to participate in discovery as real parties in interest and be subject to trial subpoenas as parties, or in the alternative, compelling Fortis to obtain and produce documents and testimony from the former stockholders.

Zurn focused her analysis on the language of the merger agreement, since Delaware law presumes that the parties are bound by the language of the agreement they negotiated. The merger agreement appointed Fortis as the sole and exclusive shareholder representative to act on behalf of the selling shareholders with regard to all matters pertaining to the agreement. It did not empower Fortis to compel stockholder participation in litigation; instead, it appointed Fortis to litigate in the stockholders' stead.

The vice chancellor noted that the contractual appointment of a shareholder representative to bring certain actions makes the representative the real party in interest in those actions. This structure is helpful to both buyers and sellers as it enables them to resolve post-closing disputes efficiently. Buyers also benefit from the fact that the structure makes a judgment against the representative binding on all the selling stockholders. To hold that the stockholders must participate in discovery as real parties in interest would be contrary to the language and purpose of the merger agreement's shareholder representative structure. Allergan bargained for structural efficiency in closing the merger and in adjudicating post-closing disputes, and may not avoid that structure because third-party discovery introduces some tangential inefficiency in litigating against the former stockholders.

Also, the merger agreement did not give the shareholder representative any right to compel the selling stockholders to produce documents. The parties acknowledged that there was no Delaware authority addressing the scope of a shareholder representative's control over individual stockholders' documents. Allergan relied on several cases from the federal district courts in Nevada and New York holding that administrative agents under credit agreements were required to produce documents in the principal lenders' possession, custody and control. However, none of the underlying credit agreements in those cases included the litigation arrangements that were present in the merger agreement. The credit agreements were silent as to litigation responsibilities, while the merger agreement specified that Fortis was to act for the selling stockholders with regard to all matters pertaining to the contingent payments. Allergan agreed to the shareholder representative structure in

the merger agreement, which did not include the discovery rights it sought to enforce against the individual sellers.

As a makeweight, the vice chancellor added that upholding the terms of the shareholder representative structure in the merger agreement would not significantly prejudice Allergan in the litigation. Allergan said that it was seeking the discovery from the individual sellers to see what Oculeve's investors thought about the merger. The vice chancellor said that this issue did not appear to be central to the parties' dispute and could be adequately explored through third-party discovery if really necessary to Allergan's case. The weak rationale proffered by Allergan for the discovery from the individual selling stockholders further undermined its efforts to displace the shareholder representative structure that the parties had negotiated in the merger agreement.

The court's rationale and refusal to disregard the shareholder representative structure underscore the structure's utility in buy-sell agreements to the parties. The opinion suggests that Allergan could have sought in the merger agreement to require the selling stockholders to give the shareholder representative the right to compel them to testify or produce documents in any ensuing proceeding. However, such a provision would have undermined the value of the shareholder representative structure to the sellers. It is doubtful that the result would have differed even if Allergan had proffered a more compelling need for the discovery from the selling stockholders. Moreover, nothing in the opinion forecloses Allergan's ability to pursue third-party discovery from the selling stockholders, albeit at a greater cost and inconvenience.

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