

## Recent Developments

### Recent Decisions Reaffirm That Merger Terminates Derivative Standing Under Delaware Law

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The Delaware Supreme Court has long recognized that a merger terminates the standing of the target corporation's former shareholders to maintain a derivative action on the target's behalf, with two narrow exceptions: if the merger is fraudulently designed solely to eliminate derivative standing or if it is merely a "reorganization" that does not affect the shareholders' ownership of the enterprise. Despite efforts by the plaintiffs' bar to circumvent this rule, two recent decisions relating to the Countrywide-Bank of America merger have reaffirmed these fundamental principles.

In January 2008, when Countrywide agreed to merge with a Bank of America subsidiary, Countrywide's directors and officers faced a number of derivative suits in California. As is typical, shareholder class actions challenging the merger were filed in the Delaware Court of Chancery. The Delaware litigation was eventually settled on the basis of supplemental proxy disclosures, and the deal closed in July 2008. Although the derivative claims were not settled, the California federal court dismissed them for lack of standing. The California derivative plaintiffs objected to the Delaware settlement, asserting that it improperly released claims that Countrywide's board had breached its fiduciary duties by failing to "value" or "preserve" the derivative claims before agreeing to the merger. The Court of Chancery approved the settlement, holding that the objectors' "novel" claims were "functionally worthless." *In re Countrywide Corp. S'holders Litig.*, 2009 WL 846019, at \*7, \*9-10 (Del. Ch. Mar. 31, 2009). The Delaware Supreme Court affirmed, holding that "Delaware corporate fiduciary law does not require directors to value or preserve

piecemeal assets in a merger setting." *Ark. Teacher Ret. Sys. v. Caiafa*, 2010 WL 2103027, at \*1 (Del. May 21, 2010). The Supreme Court also noted that the merger "extinguish[ed] [plaintiffs'] standing to pursue derivative claims" under Delaware law. *Id.*

The objectors nevertheless returned to California and sought reconsideration of the dismissal of their derivative claims for lack of standing. The objectors relied on *dicta* in the Delaware Supreme Court's opinion that, they claimed, expanded the "fraud" exception to the loss of derivative standing to include situations in which a merger was necessitated by allegedly fraudulent conduct on the part of the acquired company's board. But the federal court adhered to its ruling, holding that the Delaware Supreme Court "did not change Delaware law regarding the loss of derivative standing after a merger." *In re Countrywide Fin. Corp. Deriv. Litig.*, No. 07-cv-06923 (C.D. Cal. June 22, 2010).

One can expect the plaintiffs' bar to continue its efforts to keep derivative claims alive in the post-merger context. The Delaware Supreme Court has recently agreed to hear argument on an important related legal issue—whether, and under what circumstances, the shareholders of an acquired company may pursue a so-called "double derivative" claim following a stock-for-stock merger.

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