PENN STATE LAW REVIEW

Oral Arguments in a Hypotehtical Appeal of *Air Products v. Airgas* to the Deleware Supreme Court[1]

Participants:

Samuel C. Thompson, Jr.,[2] Moderator
Stephen P. Lamb,[3] Presiding Justice
William M. Lafferty,[4] Counsel for Petitioner
Kevin R. Shannon,[5] Counsel for Respondent

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1. An edited transcript of a presentation given in New York City on October 13, 2011, as part of the 8th Annual Institute on Corporate, Securities, and Related Aspects of Mergers and Acquisitions.

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I. INTRODUCTION

SAMUEL THOMPSON: (Moderator)

As indicated earlier, our luncheon program is a mock argument before a fictitious Delaware Supreme Court consisting of you, our audience, of an appeal of the *Airgas* case.[6] In *Airgas*, Chancellor Chandler of the Delaware Court of Chancery upheld Airgas's poison pill.

First, let me introduce the person who will be acting as the Chief Justice of the Delaware Supreme Court, Stephen Lamb, sitting in the middle, formerly a Vice Chancellor of the Delaware Court of Chancery and now a partner with Paul Weiss, where he focuses on Delaware corporate law and governance issues.

Representing the appellant, Air Products, is William Lafferty, of the firm Morris, Nichols in Wilmington, who focuses on litigation involving M&A, proxy contests, and shareholder class and derivative actions. Bill represented Air Products in the Chancery Court. At Penn State, we are particularly proud of Bill. He's a graduate of The Dickinson School of Law, which has become the Penn State Dickinson School of Law.

Representing the appellee, Airgas, is Kevin Shannon of the firm Potter Anderson in Wilmington, where he specializes in shareholder class and derivative actions in M&A and other complex transactions. Kevin represented Airgas in the Chancery Court.

Chief Justice Lamb, I will now turn the time over to you.

6. Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48 (Del. Ch. 2011).

STEPHEN LAMB: (Presiding Justice)

Thank you, Sam. I'm going to give a very brief introduction of what the case is about and then turn it over to Mr. Lafferty.

Air Products and Airgas are both Delaware corporations. Both corporations are headquartered in Pennsylvania and are in the industrial gas business.[7] Between October 2009 and February 2010, Air Products made a series of purchase offers to the Airgas Board, first at $60 per share and then at $62. Airgas rejected each offer. Air Products followed up on February 11, 2010, with a $60 all-cash, all-share tender offer to the Airgas stockholders. The Airgas Board recommended against the offer as inadequate and refused to redeem its poison pill.

The Board would adhere to these positions as Air Products raised its offer in the coming months. Under the Airgas charter, the board of nine members was classified into three classes. Air Products quickly announced its intention to solicit proxies for a slate of independent nominees to occupy three of those seats that were up for election at the Airgas annual meeting then scheduled for September 15, 2010.

Air Products' slate was duly elected. Air Products also asked the stockholders of Airgas at that meeting to vote on an amendment to the Airgas bylaws to move the date of the next Airgas annual meeting from September 2010 to January 18, 2011, a mere four months after the 2010 annual meeting. That bylaw amendment passed by a 52% majority of the shares voting.

Airgas then asked the Chancery Court to declare the bylaw invalid on the theory that the

7. The following summarizes the Chancery Court's findings of facts. *Id.* at 59-91.

> Airgas charter required a vote of 67% of the outstanding shares to approve a bylaw that was inconsistent with the charter's classified Board provision. Airgas argued that the bylaw was, in fact, inconsistent because the classified Board provision contemplated a full three-year term for each class of directors, and that the by-laws shift in the annual meeting date shortened the incumbent's term by eight months.
>
> Chancellor Chandler ruled for Air Products, finding the charter provision to be ambiguous and able to be interpreted either to bestow a full three-year term or to hold a term until the third annual meeting after which you were elected. Chancellor Chandler resolved the ambiguity in the bylaws in the bylaws' favor rather than in the charter's favor by reference to an interpreted preference for the shareholder franchise.
>
> The Delaware Supreme Court reversed that holding, agreeing with Airgas that the charter provision was ambiguous, and agreeing with the court in part, but finding that most charters are drafted in the same way. The court took notice of extrinsic evidence to the effect that classified board provisions are generally understood to import three-year terms—that is, full three-year terms or nearly three-year terms.
>
> Airgas and Air Products continued to negotiate a possible combination while this litigation was taking place. In November 2010, the Airgas Board stated its position: the board wanted to see $78 per share on the table for negotiations to proceed. Meanwhile, the new directors elected in September 2010 got up to speed, and the board agreed to the new director's request to hire a third outside valuation expert to give an opinion and to hire their own legal counsel.

> The company retained Credit Suisse as the third banker.
>
> Air Products then announced its highest and best offer of $70 per share. The Airgas board, including the three new members who had been elected at Air Products' urging, unanimously rejected this offer as inadequate. It then remained for Chancellor Chandler to rule on the *Unocal*[8] or *Moran*[9] question, whether the Airgas Board's refusal to redeem its poison pill was appropriate; that is, whether the refusal was disproportionate to the threat posed by the Airgas offer.
>
> In a remarkable opinion, the Chancellor sustained the Airgas board. The environment was informationally rich, so there was no chance that the shareholders would tender under a misapprehension regarding the company's value.[10]
>
> Still, the threat was found to lay instead in the combination of an inadequate price and a stockholder majority which, by that point, consisted of arbitrageurs who were ready to tender. The good faith board, the court held, was free to maintain its defense.[11] After this decision, Air Products withdrew its offer.[12] For the purposes of today's discussion, however, they haven't withdrawn their argument. Instead, Air Products has taken an appeal to the Delaware Supreme Court. Mr.

8. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).
9. Moran v. Household Int'l, Inc., 500 A.2d 1346 (Del. 1985).
10. *Airgas*, 16 A.3d at 104-06.
11. *Id.* at 111-13.
12. *See* Jef Feeley & Phil Milford, *Air Products Drops Hostile Bid After Airgas Wins on Poison Pill*, BLOOMBERG.COM (Feb. 16, 2011), http://www.bloomberg.com/news/2011-02-15/air-products-loses-court-bid-to-invalidate-airgas-defense-against-takeover.html.

Lafferty will present argument for Air Products.

II. ARGUMENT BY PETITIONER

WILLIAM LAFFERTY: (Counsel for Petitioner)

Thank you. May it please the court, I'm pleased to present argument today on behalf of Air Products in the *Air Products v. Airgas* case. On page 1 of his opinion, the former chancellor[13] framed the issue before the court as follows:

> Can a Board of Directors acting in good faith and with reasonable factual basis for its decision, when faced with a structurally non-coercive, all cash, fully-financed tender offer directed to the stockholders of the corporation, keep a poison pill in place so as to prevent stockholders from making their own decision about whether they want to tender their shares—even after the incumbent board had lost one election, a full year had gone by since the offer was first made public, and the stockholders were fully informed as to the target board's views on the inadequacy of the offer?[14]

While the former chancellor correctly framed the issue, I respectfully submit that he got the answer to that question wrong, and I'm going to turn to the two main reasons why I believe that to be the case.

First, I respectfully submit that the chancellor incorrectly applied Delaware law in concluding that the power to defeat an inadequate, hostile

13. Former Chancellor William B. Chandler III left the Delaware Court of Chancery in 2011, serving from 1989-2011. JUDICIAL OFFICERS OF THE COURT OF CHANCERY, http://courts.delaware.gov/chancery/judges.stm (last visited Jan. 25, 2012).

14. *Airgas*, 16 A.3d at 54.

> offer ultimately lies with the Board. Second, even if the Board does have such power to defeat a tender offer, it can only do so after it has affirmatively identified and investigated the nature of the alleged threat and determined that the continued maintenance of the poison pill was a proportionate response to that threat. The Airgas Board here did neither.
>
> Now before I turn to those two points, I want to step back for a moment and just put some of this in perspective. The Delaware General Corporation Law (the "DGCL") does not regulate tender offers, nor does the DGCL contemplate director action with respect to tender offers at all. As explained by former Chancellor Allen in the *T.W. Services* case, tender offers, even when aggregated into a single changing control transaction, require no corporate action, and state law traditionally has accorded directors no statutory role whatsoever with respect to a public tender offer, even for a controlling number of shares.[15]
>
> Instead, a federal regulatory scheme governs tender offers. The Williams Act requires disclosure of information and requires directors to make a recommendation on a tender offer, but once they have disclosed information and made a recommendation under federal law, the directors' role is done.[16]
>
> Now in the early to mid-1980's, we saw the emergence of coercive, two-tiered, front-end-loaded tender offers, a tactic used by corporate raiders. Simply providing information and a recommendation as the Williams Act requires did not provide adequate protection from the

15. TW Servs., Inc. v. SWT Acquisition Corp., Nos. 10427 & 10298, 1989 WL 20290, at *1189 (Del. Ch. Jan. 31, 1989).

16. *See* 15 U.S.C. § 78n(d), (f) (2010).

> structurally coercive offers of that era. Thus, in response to those types of offers, boards began adopting poison pills to delay or prevent takeovers.
>
> In 1985, this court, in *Moran v. Household*,[17] sanctioned the use of a poison pill to respond to a threat such as a two-tiered, front-end-loaded tender offer, but it did so only with the fundamental promise to stockholders that a rights plan is not absolute and would not prevent stockholders from receiving tender offers, because a Board's decision to put in a pill would be reviewed under *Unocal*[18] and would be subject to judicial review.[19] And less than a year ago, the Delaware Supreme Court, in the *Selectica*[20] case, reaffirmed the fundamental promise from *Moran* that a pill is not absolute.[21] I will now turn to the reasons why I believe the Chancellor misapplied that promise.
>
> Under *Unocal*, a board has the burden to show a reasonable grounds for believing that a danger to corporate policy and effectiveness existed, and second, that the board's response to that threat is neither preclusive nor coercive and was reasonable in relation to the threat.[22] The chancellor, in his opinion below, wrote that his *Unocal* analysis came down to two cases: the *Paramount v.Time-Warner*[23] case

17. Moran v. Household Int'l, Inc., 500 A.2d 1346 (Del. 1985).

18. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (holding that adoption of a defensive measure will be protected by the business judgment rule as long as the board had reasonable grounds for believing that a danger to corporate policy and effectiveness existed and the board's defensive response was reasonable in relation to the threat posed).

19. *Moran*, 500 A.2d at 1354.

20. Versata Enters., Inc. v. Selectica, Inc., 5 A.3d 586 (Del. 2010).

21. *Id.* at 599.

22. *Unocal*, 493 A.2d at 955.

23. Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1990).

> and the *Unitrin*[24] case. I'd like to take a look at both of those cases briefly in light of some other precedents that are out there: *Interco*[25] and *Chesapeake*.[26]
>
> In the *Interco* decision—possibly the last case where the court ordered a pill to be pulled—Chancellor Allen was faced with a similar factual scenario. Interco was defending itself, using a poison pill, against a $74 tender offer, and the board in turn was attempting a restructuring that could result in a higher value for stockholders.[27] While Chancellor Allen didn't use substantive coercion, which has now become a common phrase, in his opinion, he did identify the threat to the company as the possibility that the board's financial advisors were incorrect in how they valued the restructuring plan, and that a majority of the Interco shareholders may not accept that fact and may incorrectly tender and be injured.[28]
>
> In his opinion below, Chancellor Chandler identified the threat similarly as the threat that a majority of the stockholders—in this case, arbitrageurs—might be willing to tender their shares regardless of whether the price was adequate.[29] Basically, that the stockholders weren't smart enough to figure this out for themselves.
>
> The Chancellor expressed much skepticism about whether this concept of a threat was a cognizable threat under *Unocal*, and he stated point-blank that he had a hard time believing that an inadequate price alone in the context of

24. Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361 (Del. 1995).
25. City Capital Assocs. Ltd. P'ship v. Interco, Inc., 551 A.2d 787 (Del. Ch. 1988).
26. Chesapeake Corp. v. Shore, 771 A.2d 293 (Del. Ch. 2000).
27. *Interco*, 551 A.2d at 794.
28. *Id.* at 798.
29. Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 111-12 (Del. Ch. 2011).

> a non-discriminatory, all-cash, all-shares, fully-financed offer could pose a threat—particularly given the wealth of information that the stockholders already had to make their decision.[30] Based on his reading of *Paramount* and *Unitrin*, however, the Chancellor reluctantly concluded that under existing Delaware law, it apparently does pose a threat.[31]
>
> Your Honor, I share the Chancellor's skepticism that an inadequate price alone can constitute a valid threat, especially one that is not time-limited. Our law presumes that stockholders are competent to buy stock. *Unitrin* itself presumes stockholders are competent to sell stock into a stock repurchase program.[32] Our law further presumes that stockholders are smart enough and competent enough to elect directors. If stockholders are competent to make those decisions, why does our law deem them incompetent or too ignorant to decide whether to accept or reject a structurally non-coercive, premium offer? I respectfully submit that our law should not ascribe a rubelike quality to stockholders.
>
> Even more troubling is that if an inadequate price in and of itself is a continuous threat, and as this court held in *Unocal*, directors have a fundamental duty and obligation to protect the corporate enterprise from harm that they reasonably perceive,[33] then directors would be breaching their fiduciary duty by not using the poison pill to prevent stockholders from deciding on a tender offer that the directors

30. *Id.* at 56-57.
31. *Id.* at 99-101.
32. *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1372 (Del. 1995) (noting stock repurchase programs, enacted outside of the context of defensive measures, are reviewed under the business judgment rule).
33. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985).

> believe may be inadequate. In my opinion, that just cannot and should not be our law.
>
> But like the Chancellor below, I acknowledge that, as our law presently exists, this form of substantive coercion is a recognized threat in Delaware. The question wherein I believe the Chancellor erred is that: How can a Board respond to that threat? I submit that the answer is found in Chancellor Allen's decision in *Interco*. There, Chancellor Allen ordered the Board to redeem the pill, notwithstanding this identified price threat, and specifically, in an important part of the holding, Chancellor Allen said:
>
> To acknowledge that directors may employ the recent innovation of "poison pills" to deprive stockholders of the ability effectively to choose to accept a non-coercive offer after the [B]oard has had a reasonable opportunity to explore or create alternatives or attempt to negotiate on the shareholders' behalf, would, it seems to me, be so inconsistent with widely shared notions of appropriate corporate governance as to threaten to diminish the legitimacy and authority of our corporation law.[34]
>
> Now, fast-forward 18 months after the *Interco* decision to the *Paramount* case. It's important to note that *Paramount*, which was so heavily relied on by the chancellor, did not involve the question of whether the Board ought to pull a poison pill in response to Paramount's offer.
> In *Paramount*, Time had entered into a stock-for-stock merger agreement with Warner. When Paramount came on the scene with this blockbuster, all-cash tender offer, Time amended its merger agreement with Warner in

34. City Capital Assocs. Ltd. P'ship v. Interco, Inc., 551 A.2d 787, 799-800 (Del. Ch. 1988).

> a number of ways in order to defend its transaction.[35] Paramount sought to enjoin Time's tender offer for Warner stock so as to give Time stockholders a chance to accept Paramount's bid.[36]
>
> The Supreme Court in *Paramount* did discuss the *Interco* case by Chancellor Allen briefly, and it overruled a portion of Chancellor Allen's opinion in *Paramount*. The portion of *Interco* overruled in *Paramount*, however, dealt with the forms of threat, or threats that may exist, not whether the continued use of a poison pill is a disproportionate response to a tender offer.[37]
>
> Indeed, the academic article upon which the *Paramount* decision relies to support this concept of substantive coercion[38] acknowledges that the concept of substantive coercion is a slippery, slippery concept, and relies on the notion that recognizing such a threat would be reviewed by a court under the proportionality test of *Unocal*.[39]
>
> After identifying a number of threats arising from the Paramount tender offer, the court there did apply a proportionality test, and the court's proportionality analysis in *Paramount* turned expressly on the fact that the revised agreement and its accompanying safety devices did not preclude Paramount from making an offer for the combined Time-Warner company.[40] Such a holding is quite far afield, I

35. Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140, 1144-49 (Del. 1990).
36. *Id*. at 1149-50.
37. *Id*. at 1152-53.
38. *See id*. at 1153 n.17 (quoting Ronald J. Gilson & Reinier Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247, 267 (1989)).
39. Gilson, *supra* note 37, at 274.
40. *Paramount*, 571 A.2d at 1154-55.

> submit, from binding the chancellor in this case to conclude that the power to defeat a tender offer ultimately lies with the Board.
>
> Vice Chancellor Strine—now Chancellor Strine—in *Chesapeake*, was faced with an argument that substantive coercion from a hostile bid justified the implementation of a super-majority bylaw. Chancellor Strine, as Chancellor Chandler did here, acknowledged that the concept of substantive coercion is binding precedent in Delaware, but went on to note that the so-called "threat of substantive coercion" could be invoked as a justification for aggressive defensive measures and could easily be subject to abuse.[41]
>
> Chancellor Strine went on to discuss the application of the second prong of *Unocal*, in light of such a threat of abuse, as a method to police such potential abuse of the substantive coercion threat as an excuse for justifying defensive measures.[42] Chancellor Strine's comments here were instructive. He said that:
>
> One might imagine that the response to this particular type of threat might be time-limited and confined to what is necessary to ensure that the board can tell its side of the story effectively. That is, because the threat is defined as one involving the possibility that stockholders might make an erroneous investment or voting decision, the appropriate response would seem to be one that would remedy that problem by providing stockholders with adequate information. The corporate [B]oard has, of course, many tools to accomplish that, but may legitimately need

41. Chesapeake Corp. v. Shore, 771 A.2d 293, 327 (Del. Ch. 2000).
42. *Id.* at 327-29.

more time to ensure that it could get its message out to the marketplace.[43]

I respectfully submit, Your Honors, that Chancellor Strine's analysis of the second prong of *Unocal* in light of this concept of substantive coercion being a threat is the proper one that Delaware ought to follow.

Now briefly, let me turn . . .

STEPHEN LAMB: (Presiding Justice) Mr. Lafferty, I know your time is almost up, but how did it influence the chancellor's opinion that the three directors that your client caused to be elected basically drank the Kool-Aid?

WILLIAM LAFFERTY: (Counsel for Petitioner) Well, I certainly think it did have an impact, Your Honor, but I think in the wrong direction.

STEPHEN LAMB: (Presiding Justice) Well, why wouldn't it affect this court's analysis as well?

WILLIAM LAFFERTY: (Counsel for Petitioner) I think I would say the following, Your Honor. My point is that this concept of substantive coercion that was relied upon here is one that frankly is even further undermined by the fact that three independent directors who were nominated by my client actually joined the other side. That actually supports the notion that the stockholders have every piece of information they could possibly need, and it quite frankly undermines the notion that, somehow, stockholders are going to make a misinformed or misguided voting decision.

STEPHEN LAMB: (Presiding Justice) Well, that would be true except for the finding by the chancellor that a majority of the

43. *Id.* at 324-25.

shareholders consisted of short-term traders who would be more than happy to take $70, even if $80 or $78 was the minimum adequate price.[44] So, didn't the chancellor's decision turn on his determination that the Board acted in good faith?

WILLIAM LAFFERTY: (Counsel for Petitioner)

I believe it did, Your Honor. At the end of the day, I think he looked at what the Board did and its process. I want to turn to one important process point that was swept under the rug: the proportionality review. The Board is obligated to actually look at whether there is a continuing threat and to actually make an assessment about whether they ought to keep the pill in place. Here, and Mr. Shannon will acknowledge it—I believe he will have to after two trials and around 40 depositions—there was one mention of the pill ever at an Airgas board meeting. The mention was an aside made by one of the new directors, Mr. Clancey, that "[w]e have to protect the pill."[45] That is the only time there was ever any discussion by the directors about keeping the pill in place or anything like it, and indeed, people commented that they didn't even know what Mr. Clancey was talking about.

I would also submit that the Board was obligated to actually think about these things. This notion about the arbitrageurs wanting to maybe mistakenly tender, or tendering no matter what the price was, was again not something the Board can decide. They never talked about that issue whatsoever. That was a post-hoc justification thrown up at trial by Airgas's expert.

44. Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 121 (Del. Ch. 2011).
45. *Id.* at 58.

STEPHEN LAMB: (Presiding Justice) Thank you. I think your time is up. Mr. Shannon?

III. ARGUMENT BY RESPONDENT

KEVIN SHANNON: (Counsel for Respondent) Thank you, Your Honor. May it please the court, I'm making the argument on behalf of Airgas and its Board of Directors, which is comprised overwhelmingly of outside, independent directors, including, as Mr. Lafferty pointed out, three directors nominated by Air Products. The Airgas board, with the advice of three independent investment bankers, unanimously concluded that the $70 Air Products offer was inadequate. The Airgas Board also unanimously concluded that the company's defenses, including its rights plan, should remain in place, and that Air Products' inadequate offer should be resisted.

STEPHEN LAMB: (Presiding Justice) Mr. Shannon, what's the record citation, or what's the citation in the chancellor's opinion for the assertion that the Board of Directors of your client actually made an affirmative decision to retain the poison pill?

KEVIN SHANNON: (Counsel for Respondent) There are a number of citations. A number of board presentations actually show the percentage of shares held by arbitrageurs over time. That issue that was repeatedly raised with the Board; and the implications were addressed with the board. In fact, as Mr. Lafferty already pointed out, it was one of Air Product's nominees, Mr. Clancey, who, after hearing a presentation, including the presentations by the three investment bankers, said that not only was the offer inadequate, to which all the investment bankers agreed, but that the pill needs to be protected.[46]

46. *Id.*

STEPHEN LAMB: (Presiding Justice) — But was there ever a vote taken on that issue? Did the Board of Directors of Airgas ever actually, in a meeting, determine that in light of their finding of inadequacy, that it was incumbent upon them and part of their fiduciary responsibility, to leave this poison pill in place?

KEVIN SHANNON: (Counsel for Respondent) — Your Honor has pointed out that the Board determined repeatedly, based on good faith investigation and advice, that the offer was inadequate. Based on that determination, they did not elect to redeem the pill. Whether they actually made an affirmative vote on that, there isn't a record, but clearly, what they repeatedly determined, and what the court found . . .

STEPHEN LAMB: (Presiding Justice) — Well, your firm and Wachtell were advising the Airgas Board, were they not?

KEVIN SHANNON: (Counsel for Respondent) — They were, Your Honor.

STEPHEN LAMB: (Presiding Justice) — So the fact that there is no reference in the minutes to this happening, I take to mean that it didn't happen. Am I wrong?

KEVIN SHANNON: (Counsel for Respondent) — What happened was a determination that the offer was inadequate, and they would not facilitate it. Ultimately, Your Honor, that is the question before the Court, and it may get lost in the semantics. But the question before the Court . . .

STEPHEN LAMB: (Presiding Justice) — Why is that the question? Why aren't the directors obligated to make a decision about whether, even in light of the finding of inadequacy, it is not appropriate, or it would be a breach of duty on their part, essentially, to permit this offer to go forward?

KEVIN SHANNON: (Counsel for Respondent) — In fact, Your Honor, that was the question before the Court. Did the Airgas Directors breach their fiduciary duty? Did they have a duty to pull the pill in order to facilitate an offer that they unanimously deemed inadequate? Or as Mr. Lafferty would suggest, did they have a duty at some point of time to simply step aside and allow the Court to do that? What they determined is that the offer was inadequate and they did not pull the pill.

STEPHEN LAMB: (Presiding Justice) — All right, I'll stop badgering you, but doesn't Moran at least suggest that the directors have an obligation at some point after an offer's been extended to actually make an affirmative decision to leave the poison pill in place, or not to redeem it? The Board must have been asked by Air Products to redeem the pill.

KEVIN SHANNON: (Counsel for Respondent) — There was certainly a suit filed, and what *Moran* says is the duty, and Mr. Lafferty suggests as much, to keep the pill in place, or the ability, is not absolute.[47] And whether you keep that pill in place will be evaluated under *Unocal*, and what the court did was to evaluate under *Unocal* whether they met that burden.

STEPHEN LAMB: (Presiding Justice) — I gather there is no "resolution" in the minutes of the Board in the last six months of this transaction to the effect that, in light of their findings and the conclusions they've reached, that it is their judgment that the poison pill should remain in place?

KEVIN SHANNON: (Counsel for Respondent) — No, what you will see in the record is a determination repeatedly that the offer is inadequate and it should be resisted. Is there a specific resolution that, "We shall maintain the poison pill"? I have not seen that, nor is the question before the Court whether there is a

47. *See supra* notes 16-20 and accompanying text.

resolution stating that the directors will not pull the pill. In fact, what the Board did is not pull the poison pill after being requested because they made a good-faith determination that the offer was not adequate.

STEPHEN LAMB: (Presiding Justice) Apparently without discussing the ramifications of the pill and its effect on the offer. Was it even discussed after the three new members were admitted? Was there a discussion as reflected in the Board minutes of the purpose of the pill and how the Board is using it?

KEVIN SHANNON: (Counsel for Respondent) Well, I think it was very clear that the pill—there was a suit outstanding.

STEPHEN LAMB: (Presiding Justice) That's not my question. I will leave you alone to proceed as you want.

KEVIN SHANNON: (Counsel for Respondent) Ultimately, Your Honor, the question—and Your Honor has already alluded to it—before this Court isn't a broad, theoretical question, but rather a specific question: Did this Board breach its fiduciary duties? And the question—as Your Honor has already highlighted—is whether they have a duty, having determined that the offer was inadequate, to pull the pill, or, as I mentioned a minute ago, whether they have a duty to step aside and allow the shareholders to decide whether and when the company would be sold?

And I will tell you that is not currently Delaware law and nor should it be. Section 141(a) of the DGCL, to which Mr. Lafferty referred, clearly vests the power to manage the business and affairs of the corporation in the hands of the directors.[48] *Van Gorkom* makes

48. 8 DEL. CODE ANN. tit. 8, § 141(a) (West 2011).

clear that the directors' duty is unyielding and that they have an affirmative duty to protect the shareholders.[49]

In *Paramount*, and Mr. Lafferty referred to some of the *Paramount* holdings, the court stated that, "The fiduciary duty to manage a corporate enterprise includes the selection of a timeframe for the achievement of corporate goals. That duty may not be delegated to the stockholders."[50] The Court also explained that Directors are not obligated to abandon a deliberately conceived corporate plan for short-term shareholder profit unless there is clearly no basis to sustain the corporate strategy.[51]

This was also addressed in *Unitrin*, where this Court held that the Unitrin board had not only the power, but the duty, to protect Unitrin shareholders from an all-cash, all-shares offer they deemed inadequate.[52] The directors' duty to protect the shareholders doesn't have a time limit. The duty does not change because the shareholders are informed or not informed. It does not change because the shareholders are sophisticated or unsophisticated. And most important, the duty cannot be delegated to the shareholders. There is no reason for this Court to change that well-established law. As Mr. Lafferty noted, the shareholders have a right to elect directors. They do not have a right to manage the company or force the Board to engage in a sale.

STEPHEN LAMB: (Presiding Justice) Mr. Shannon, Mr. Lafferty suggested that the upshot of this is that a board in your clients' situation would breach its fiduciary duty if the board, after concluding that a transaction was

49. Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985).
50. Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140, 1154 (Del. 1990).
51. *Id.*
52. Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1389-90 (Del. 1995).

inadequate, either didn't institute or agreed to pull a pill. Do you agree with that?

KEVIN SHANNON: (Counsel for Respondent) There's a very good argument for that, Your Honor. From *Van Gorkom*, *Paramount*, and *Unitrin*, the court has made clear that there is, as I mentioned before, an unyielding, unremitting, and affirmative duty to protect the shareholders.[53] And there is a very good reason for that.

STEPHEN LAMB: (Presiding Justice) But does that extend to a duty to use a poison pill to do that?

KEVIN SHANNON: (Counsel for Respondent) I think, Your Honor, that this is one of the things that I'll point to the testimony of Air Products' own directors. When Chancellor Chandler asked them at trial, "If faced with an inadequate offer, what would you do?" And the director said, "I'd have to use every legal mechanism available to hold out for the best price."[54] The poison pill is one of those mechanisms that they would have to use. There is a duty, an unremitting duty, to protect the shareholders, and a board faced with an offer they unanimously determined to be inadequate based on the advice of three independent bankers, has to follow that duty. And there is a very good reason for that.

STEPHEN LAMB: (Presiding Justice) What if three of the nine didn't agree? Would that change the fiduciary duties of the other six?

KEVIN SHANNON: (Counsel for Respondent) Would it change? No, I think the directors have to act in accordance with their fiduciary duty. And, Your Honor, there's a very important point here. When the directors are acting, Mr. Lafferty and Air Products suggest

53. *See supra* notes 48-49 and accompanying text.

54. *See* Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 58 (Del. Ch. 2011) (quoting Transcript of Supplemental Evidentiary Hearing at 104, *id.* (No. 5256-CC)).

that the board should step aside and let the shareholders decide. But in deciding whether to accept or reject a tender offer, the shareholder is deciding only one thing: Do I want to sell my shares? They are not deciding to sell the company. The shareholder can have any number of reasons to sell their shares and are making individual investment decisions without any consideration of how their personal decisions will affect the shareholders.

The Board, and only the Board, has a duty to make the decision in the best interest of the company and all of the shareholders. Only the Board has the duty to maximize value if there's a sale, and when the Board approves a sale, it's approving a sale that will force out other shareholders. That is a fundamental and critical difference between allowing the shareholders to decide whether and when to sell the Company, and why Delaware law always has vested that power in the Board.

STEPHEN LAMB: (Presiding Justice) It's really an exaggeration to say, "always had," because this poison pill business didn't start until the mid-80's. But would a Board be breaching its duties if it adopted a pill that only lasted six months?

KEVIN SHANNON: (Counsel for Respondent) If the Board restricted its ability to extend the pill, certainly.

STEPHEN LAMB: (Presiding Justice) What if the board adopted a pill that said, "Anyone who makes an all-cash, all-shares offer with a minimum condition of two-thirds of the shares being tendered does not have to worry about the pill." Would that breach the board's fiduciary duties?

KEVIN SHANNON: (Counsel for Respondent) — Yes, if the Board included in the pill that that it didn't have the ability to exercise its fiduciary duty and address the facts as they were presented at the time.

STEPHEN LAMB: (Presiding Justice) — And if that language is not included, just saying, "This is the pill we adopt and this is what it says." Is that a breach of fiduciary duty?

KEVIN SHANNON: (Counsel for Respondent) — I don't believe that would be a breach of duty per se, as long as the Board had the ability to revisit the pill if there were changes. *Quickturn* would tell you that the Board can't commit itself to do something in the future without knowing the facts.[55]

STEPHEN LAMB: (Presiding Justice) — I'm not making any assumptions about what the Board might do later if circumstances changed. Just, at the time, would a Board be entitled to adopt a pill of that structure?

KEVIN SHANNON: (Counsel for Respondent) — A pill said that it will withdraw if 67% of the shares are tendered?

STEPHEN LAMB: (Presiding Justice) — No, rather that there will be no pill if there is an all-cash, all-shares offer with a minimum condition of two-thirds of the shares being tendered.

KEVIN SHANNON: (Counsel for Respondent) — Arguably, a Board could adopt such a pill, but the Board would have to reserve the right to amend it in the face of any change in circumstances.

STEPHEN LAMB: (Presiding Justice) — So why would that not be delegating the decision about transferring the company to the stockholders?

55. Quickturn Design Sys., Inc. v. Shapiro, 721 A.2d 1281, 1291-92 (Del. 1998).

KEVIN SHANNON: (Counsel for Respondent) It's not because the Board is reserving the right based on a . . .

STEPHEN LAMB: (Presiding Justice) And if the circumstances don't change, the Board doesn't exercise that right. The Board left it up to the stockholders by a two-thirds majority to decide whether or not to change control.

KEVIN SHANNON: (Counsel for Respondent) In my view, if the Board had determined that the offer is inadequate. The Board has a duty, an unyielding, unremitting, and affirmative duty to protect the shareholders.

STEPHEN LAMB: (Presiding Justice) If the Board determines the pill is inadequate, it couldn't adopt a pill like I just described.

KEVIN SHANNON: (Counsel for Respondent) The Board would have to be able to show how the adoption of the pill is consistent with their fiduciary duties to the shareholders. And I think the other thing you have to recognize—the reason that a pill is so important and so powerful—is that it forces a bidder to deal with the Board. The Board, and only the Board, is in the position to negotiate effectively for the shareholders, with the pill providing the negotiating power. The pill forces the bidder to deal with the Board, and if the bidder could unilaterally avoid the pill by deeming its offer "best and final" or putting a time limit on it, that would render the pill essentially useless. That's why Chancellor Chandler, after considering the extensive factual records, expressly and correctly held, that in order to have any effectiveness, the pill does not and cannot have a set expiration date,[56] which I think would get back to your question. In theory, you could have a pill that has limited powers, but I think the Board

56. *Airgas*, 16 A.3d at 129.

would always have to reserve its rights to protect the shareholders, and the law from *Van Gorkom* has been consistent on that.

Your Honor—I know my time is up—in conclusion, the Court of Chancery went through the *Unocal* analysis. The court made express factual findings that each of those elements were satisfied. The court didn't simply hold that the Board did not breach its duties, the court held that this Board was the quintessential example of the good faith and compliance with fiduciary duties that are expected of Delaware directors. In fact, Air Product's own directors suggested that they would do the exact same thing as Airgas's directors.

There is no basis on this factual record and established Delaware law to find that these directors breached their duty. Nor should this court change the law and hold that, at a point in time, the Directors who are charged with protecting the company and all of its shareholders should simply step aside and let the shareholders decide when and whether to sell the company based on their own personal interests, not the interests of the company as a whole. For all these reasons, Your Honor, I request and believe that the Court of Chancery's opinion should be affirmed.

IV. REBUTTAL BY PETITIONER

WILLIAM LAFFERTY: (Counsel for Petitioner)

I want to leave you with one parting thought. I want to come full circle. The upshot of the chancellor's opinion was that the power to defeat an inadequate tender offer lies with the Board of Directors. That holding comes in the context of a federal regulatory scheme in the Williams Act, whose stated purpose is to require full and fair disclosure for the benefit

of the stockholders, while at the same time providing management an equal opportunity to present their case.[57] In this era of concern over federal encroachment into state corporation law—in the face of Sarbanes-Oxley and Dodd-Frank—does this court really want to opine that, in light of the stated purpose of the federal regulations, that Delaware has nonetheless placed the power to totally defeat a hostile tender offer into the hands of the board? I respectfully submit that it should not, and that this Court should reverse the chancellor's decision. Thank you.

STEPHEN LAMB: (Presiding Justice) Thank you, Mr. Lafferty. We will now convene in chambers to take a vote.

57. *See* 15 U.S.C. § 78b (2010).