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PERSPECTIVE

Disclosures when approval not required

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In *Doppelt v. Windstream Holdings Inc.*, the Delaware Court of Chancery considered the adequacy of disclosures made in connection with a stockholder vote on certain proposals, approval of which permitted a corporation to enter into another transaction that was not subject to a stockholder vote. The court's opinion sheds light on the disclosure obligations related to transactions that are not subject to stockholder approval but are closely tied to transactions that require stockholder approval and the issues with disclosing information to the public without directly disclosing it to stockholders.

Windstream Holdings decided to spin-off certain assets into an independent, publicly traded real estate investment trust. Windstream would retain 19.9 percent of the REIT and distribute the remainder to Windstream's stockholders. Windstream touted that the spin-off would reduce its debt by \$4 billion, increase its cash flow, and pay an attractive dividend to its stockholders, but did not explain how the spin-off would create those benefits. Furthermore, to avoid a \$600-\$800 million tax burden, Windstream proposed converting an operating subsidiary from a corporation to a limited liability company, which could not be effected without the approval of Windstream's stockholders. As a result, Windstream's board of directors sought its stockholders' approval of a proposal to eliminate that voting right. Additionally, Windstream's board of directors sought its stockholders' approval of a one-for-six stock split following the spin-off.

Windstream sent a proxy statement to the stockholders disclosing information regarding the two proposals but without disclosing certain material information regarding the spin-off, which could be effected without stockholder approval.

On Feb. 19, 2015, in an oral ruling, the Delaware Court of Chancery denied a preliminary injunction to enjoin a special meeting of stockholders to vote on the two proposals because the stockholder-plaintiffs could not show

a reasonable likelihood of success on the merits. The court found that much of the information that the stockholder-plaintiffs sought to have Windstream disclose was disclosed in public filings, Windstream's board of directors was independent and disinterested and stockholder adoption of the two proposals was not necessary to effect the spin-off.

Subsequently, the same stockholders alleged, among other things, that the members of Windstream's board of directors breached their fiduciary duties by failing to disclose certain material information prior to the stockholder meeting to adopt the two proposals.

In response, the directors filed a motion to dismiss arguing, among other things, the proxy statement contained all facts material to the vote on the two proposals and other public filings contained any other information sought by the stockholder-plaintiffs.

The court considered whether the disclosures made in the proxy statement and outside of the proxy statement were sufficient to grant the directors' motion to dismiss. The court rejected the directors' argument that the information relating to the spin-off was not material because it was reasonably conceivable the two proposals and the spin-off were the same transaction. The court distinguished *In re Novell Inc. Shareholder Litigation*, in which the duty of candor was found not to extend to matters that may be related, but are not subject, to a stockholder vote. Unlike in *Novell* where two transactions, though negotiated together, held value independent of one another, the court found it reasonably conceivable that the two proposals were of no value other than in connection with the spin-off.

Moreover, the fact that all of the reasons provided in the proxy statement for the stockholders to vote in favor of the two proposals related to benefits of the spin-off and that the background of the transaction in the proxy statement listed the rationale for and benefits of the spin-off, supported the right of Windstream's stockholders to all material information regarding the spin-off before voting on the two proposals at the special meeting.

The court also rejected the direc-

tors' argument that, to the extent any material information was not provided in Windstream's proxy statement, the information was disclosed through various press releases, investor presentations, information statements and other means. The court noted that "while Delaware law recognizes that '[p]roxy statements need not include facts known or reasonably available to the stockholders,' misrepresentations or omissions are not 'cured by reason that [they] could be uncovered by an energetic shareholder reading an SEC filing.'" Where the disclosure violations were at least conceivably material, excluded from direct communications of Windstream with its stockholders and involved arguably misleading statements, the court concluded that the information was not reasonably available to Windstream's stockholders. Based on the foregoing conclusions, the court held that it was at least reasonably conceivable that the plaintiff-stockholders' disclosure violations were material, relevant to the two proposals and inadequately disclosed at the time of the special meeting. Therefore, the directors' motion to dismiss the fiduciary duties claims against them for failing to disclose certain material information was denied.

This decision is instructive in several respects. The right of stockholders to vote on a transaction is not the controlling factor when determining whether disclosure of the material facts related to that transaction is required. The fundamental reason for requiring disclosure of a transaction that does not require stockholder approval is the materiality threshold that triggers all disclosure obligations. Although the court in *Doppelt* analyzed whether the two proposals were the same transactions as the spin-off, that analysis only determined the materiality of the spin-off relative to the two proposals. *Doppelt* establishes that where a transaction requiring stockholder approval has value only insofar as that which is created by a transaction that does not require stockholder approval, the latter transaction likely is material to the stockholders' decision on the former transaction and material information regarding that

transaction should be disclosed.

In addition, Delaware law does not burden stockholders with a duty to discover information that is not directly disclosed to them by the corporation. In the case of public companies, this means the proxy statement should disclose all material facts. If it comes to light that certain material information was omitted from the proxy statement, then the proxy statement should be supplemented. A public corporation should not rely on investors presentations or other materials filed on the Securities and Exchange Commission's website that are not disclosed directly to the stockholders to satisfy disclosure requirements or supplement existing disclosures.

In the case of private companies, best practice is to disclose all material facts in any disclosure document sent to stockholders when seeking their approval. However, all private Delaware corporations with more than a handful of stockholders should consider obtaining all of the stockholders' consents to all forms of electronic notice pursuant to Section 232 of the General Corporation Law of the State of Delaware. After obtaining those consents, any disclosures may be sent by email or, assuming the stockholders all have access to it, may be posted on the corporation's intranet (if separate notice of the posting is given to the stockholders). Obtaining stockholder consent to electronic transmissions significantly reduces the risk of litigating the claims brought in *Doppelt*.

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