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Increased Use of M&A Deterrents May Spur Rise in D&O Litigation
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The recent proliferation of "poison pills" — shareholder rights provisions adopted by companies' boards to discourage hostile takeover bids — could lead to more directors and officers liability litigation, experts say.

Furthermore, the increased number of the provisions means companies anticipate more mergers and acquisitions activity, which is often followed by D&O litigation, these observers say.
More poison pills are being announced. According to data compiled by law firm DLA Piper, there were 17 traditional poison pills adopted in March by U.S. companies, while the previous monthly high since January 2017 was three. By April 22, the total had increased to 41, according to the law firm.

Driving the increase, experts say, is the recent stock market turmoil that has been fueled by the coronavirus pandemic, which has left company boards feeling vulnerable to hostile takeovers (see related story).

The wide variety of companies that have adopted the provisions include Tulsa, Oklahoma-based pipeline operator Williams Cos.; Grand Prairie, Texas-based Six Flags Entertainment Corp.; and Dallas-based restaurant chain Dave & Buster's Entertainment Inc.

In addition to those that have already introduced poison pills, a "vast number" more have them on the shelf, ready to use should the need arise, said Sanjay M. Shirodkar, of counsel at DLA Piper in Washington, who is co-head of the firm's public company and corporate governance practice.

"It's clear that there are more poison pills that are being implemented now than during the prior 12 months, and the coronavirus, in most instances, is the reason for it," said Kirk D. Dillman, a principal with McKool Smith in Los Angeles, who specializes in complex litigation.
Boris Feldman, a partner with Wilson, Sonsini, Goodrich & Rosati in Palo Alto, California, who represents businesses, said with "everybody's stock in the toilet" companies may become short-term takeover targets and want to protect themselves against opportunistically timed bids.

"In recent years, in part because of activist pressure, companies discarded some of the arrows in their defensive quiver," including poison pills. "I think they're now going to rearm," he said.
Gregory V. Gooding, a partner with Debevoise & Plumpton LLP in New York, who is a member of his firm's M&A group, said poison pills are being introduced because "boards view their stock as being significantly undervalued as a result of the recent price declines."

This creates "the possibility that somebody could build a large position in their shares for a lot less money than it could have done three months ago," he said.
Thomas O. Gorman, a partner with Dorsey & Whitney LLP in Washington, whose practice includes defending companies in Securities and Exchange Commission investigations and enforcement actions, said it can be assumed if a long-standing company has just introduced a poison pill "they have some concerns about a takeover bid" that may lead to shareholder litigation.

Michael P. McCloskey, a partner with Wilson Elser Moskowitz Edelman & Dicker LLP in San Diego, who is a member of his firm's securities and commercial litigation practices, said if a poison pill discourages a deal that a minority shareholder feels he would have benefited from "you've got yourself a lawsuit."

Some observers believe courts may be sympathetic to companies if poison pills lead to litigation filed against them.

Historically, corporate activists have been given a lot of latitude by the courts, Mr. Feldman said. But there may be a "sea change" in how courts respond to litigation filed by activist shareholders against poison pills.

"I think you may see a reversal in judicial sentiment, to be less accommodating to activist investors," Mr. Feldman said. He said he was not referring to institutional investors, who "have a lot of credibility in court" but to plaintiff attorneys who are seeking "to make a quick buck."
Dan A. Bailey, a member of law firm Bailey Cavalieri LLC in Columbus, Ohio, who represents directors and officers and insurers, said, "There's quite a bit of case law that's developed over the last 20 years about what those poison pills should and should not say, what circumstances should or should not exist in order to justify the adoption of those poison pills, so there's a pretty good road map for counsel in evaluating whether it is appropriate to adopt a poison pill."
Many times, it is appropriate, he said. "As a general matter, they're recognized as appropriate" if they are done in a way that is "consistent with that line of cases," Mr. Bailey said.
Meanwhile, some observers believe the poison pills themselves are a portent of M&A activity, which in turn often leads to D&O litigation.

Shareholders litigated 82% of M&A deals valued at over $100 million in 2017 and 2018, according to a report issued in September by San Francisco-based Cornerstone Research.
Poison pills are intended to discourage hostile takeovers. "We haven't seen a large volume of hostile acquisitions in many years," Mr. Bailey said. If they do increase, they are likely to result in more D&O litigation, he said.

"The question is whether the D&O litigation we see is going to be severe and result in significant loss payments by carriers or whether it's just going to be nuisance litigation," Mr. Bailey said, adding, "The big majority are nuisance claims."