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THE SPOTLIGHT

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WELCOME TO THE SPOTLIGHT

BROUGHT TO YOU BY ROBINS KAPLAN LLP'S WEALTH PLANNING, ADMINISTRATION, AND FIDUCIARY DISPUTES GROUP

The Spotlight strives to provide a forum to discuss the latest news and compelling issues impacting fiduciaries and those to whom fiduciaries owe duties. Whether you are an officer, director, trustee, beneficiary, trust officer, attorney, financial advisor, or anyone impacted by the law governing fiduciaries, we hope that you will find this newsletter interesting, informative, and perhaps at times even a bit entertaining.

Fiduciary disputes come in many varieties, but they share some consistent themes that involve the erosion of trust, high emotion, and opportunities—sometimes missed—for creative approaches to avoid or resolve litigation. As practitioners and teachers of fiduciary law, our attorneys have built a reputation for excellence in meeting the needs of individuals and organizations facing complex fiduciary issues, starting with the transactional and estate planning work that can mitigate risk from the beginning. We counsel individuals and business owners in a broad range of fiduciary issues, from estate planning and business succession, to dispute resolution and litigation when unavoidable.

Is there a topic affecting your practice that you would like us to discuss in an upcoming issue of The Spotlight? Let us know at all_marketing@robinskaplan.com.

– Denise S. Rahne and Steven K. Orloff

UNINTENDED **CONSEQUENCES**

DON'T FORGET THE LITIGATION RISKS WHEN GETTING A DEAL DONE

BY ANNE M. LOCKNER AND HEATHER CHANG

Transactional attorneys play a key strategic role in drafting essential documents, such as corporate formations and contracts, on behalf of corporate clients. With a client's current needs at the forefront—often accompanied by the excitement and pressures of getting a deal done—a drafting attorney's priority may not be on future, hypothetical litigation. And drafting decisions without an adequate eye toward litigation may inadvertently create challenges and complexities in litigation that could have been mitigated at the drafting stage.

Large (and even not-so-large) corporate deals often involve multiple entities, some of which are affiliated with other parties and nonparties to the deal; multiple owners, officers, and directors; and multiple legal documents to effectuate the deal. Often these multiple documents are compiled and circulated in a "deal book." The attorneys sometimes even make themselves "deal toys" to commemorate the "deal" (sometimes to the envy of trial attorneys, where such toys aren't a thing).

Behind this plethora of documents usually lie complex legal and business reasons involving tax benefits, IP ownership, investor requirements, other strategic decisions, and sometimes good old-fashioned horse trading that drive the ultimate structure of a deal. Yet the justification for these well-thought-out strategies and their corresponding effects on the documentation of the ultimate deal often disappear over time.

For example, years after an exciting deal has consummated, it sours, and disputes arise. Party A to the deal wants to sue Party B. Enter the litigator, who—after carefully considering her client's identity and how to ensure privilege protection —analyzes the operative documents and develops a legal theory under one of the contracts, noting the agreement requires that Illinois law apply to any disputes arising from the contract and that the exclusive resolution venue be the Northern District or state courts of Illinois. But the litigator also discovers a viable fiduciary-duty claim against a Party A director who's also affiliated with Party B, complicated by Party A's certificate of incorporation requiring that all fiduciary claims against directors be brought in Delaware. So where should she file suit?

Not wanting to voluntarily enter a two-front war, she advises the client to move forward with just the fiduciary-duty claim in the Delaware Court of Chancery and hold fire on the contract claim for now. But litigation is not a game of solitaire, and one's adversary often has a say in which battles will be fought. And—looking for leverage—the adverse party, Party B, decides it has a claim against an affiliate of Party A, under yet a third agreement in the deal book that contains a nonexclusive venue provision allowing claims to be brought in Minnesota, Party B's home state. So, Party B files suit against A's affiliate in Minnesota. Now our intrepid counsel, who represents Party A and now A's affiliate, is effectively fighting a two-front war while reserving A's unfiled contract claim against B, which must be filed in Illinois.

Even assuming that, as a legal matter, all parties have diligently maintained and respected the corporate distinctions among the various entities and no basis exists for piercing the client-privilege barrier, as a practical matter, two sides clearly exist: those aligned with Party A and those aligned with Party B—regardless of which individuals or affiliates are named in the various lawsuits. And no settlement will get done without a global resolution of all the disputes between Party A and Party B and all their respective affiliates. But a global resolution often does not happen immediately. Usually, a certain amount of motion practice and discovery must happen before both parties are ready to come to the table at all—let alone be willing to come to a deal.

In the meantime, litigation is costly. And litigating on multiple fronts is even worse. Depending on whether the case is in federal or state court, a court might consider transferring venue so the cases can be either consolidated or, at least, coordinated. But transfer may not be possible when issues of personal jurisdiction or exclusive jurisdiction render one of the venues inappropriate. It also may not be an option if one or more cases are in state court, without the ability to remove to federal court where there might be more venue-transfer mechanisms. And a judge may deny a motion to stay when parties, though aligned, are not identical with those of the other matter. Even with the means to make such motions, you are fighting about where to have a fight—and, even if you win this battle, you still must win the actual war.

For unavoidable multiple-front wars, it usually makes sense to assign one lead counsel to oversee all matters, but there will likely be a need to hire local counsel in one or more jurisdictions. The alternative is to hire separate counsel for each matter, but it will require close coordination to ensure counsel takes consistent positions. Coordination will also result in higher fees.

Likewise, discovery is often the most expensive part of litigation, and undertaking it and paying for it twice or more is not an efficient use of anyone's capital. Further, the ability to coordinate discovery could be limited if the cases come before different judges with different timelines. In addition to direct costs, your officers and employees may have to sit for multiple depositions, further taking time away from running the actual business. And since some of the factual issues will likely overlap, inconsistent rulings and findings from the courts become a risk, as well.

Looking back, was there a strategy behind the venue decision? Or was it just a remnant from an earlier version used as a template or thrown in without much thought? Perhaps there was a reason for this decision. But if the drafting parties and counsel cannot identify strategic rationale for varying venue and jurisdiction provisions, then they should think twice and consider making them consistent. Otherwise, all the other benefits they so carefully structured could be undermined by the unnecessary cost of a multifront conflict. While the war may not be avoidable, with some advance forethought and planning, you can contain the theater in which you fight it.

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DO WE HAVE TO SHARE **THAT INFORMATION?**

ATTORNEY-CLIENT PRIVILEGE IN THE MULTI-ENTITY CONTEXT

BY ERICA ROSENBAUM

A bedrock feature of the attorney-client relationship is the privilege protecting legal-advice communications from prying eyes. Confidential communications between a client and her lawyer are protected to a degree not found in almost any other relationship. The same is true even when the client is a corporation—although, as the Supreme Court has recognized, "The administration of the attorney-client privilege in the case of corporations . . . presents special problems."[1] While a corporation is a person for purposes of the law, it is not a person in the practical sense. An attorney cannot talk directly to a corporate entity; she must speak to the corporation's representatives. Thus, in the seminal case *Upjohn v. United States*, 449 U.S. 383 (1981), the Supreme Court held that, in the corporate context, the attorney-client privilege extends to any communication between counsel and a corporate employee that was made for the purpose of obtaining legal advice on behalf of the corporation, regardless of the employee's seniority within the corporation. And the directors of a corporation generally have a near-absolute right to information concerning the corporation, including privileged information.

But what happens when the same individuals who serve as directors of an entity become adverse or arguably adverse to the entity? In such a scenario, the question of who holds the privilege and who is entitled to access privileged information becomes more complicated to answer.

Take, for example, the case of a joint venture ("Umbrella Venture") between two closely held corporations, "Acme Co." and "Beta Co." Adams is the owner and a director of Acme, while Brown is the owner and a director of Beta. Both Adams and Brown, on behalf of Acme and Beta, respectively, decide to form Umbrella Venture and become the directors of the new entity. In the course of Umbrella's business, it enters into contracts with both Acme and Beta. As long as the parties get along, attorney-client-privilege (not to mention competing fiduciary-duty) issues should not arise, despite Adams' and Brown's dual roles serving as directors of separate corporate entities. To the extent Umbrella Venture seeks legal counsel, Adams and Brown would both fall within the scope of Umbrella's attorney-client privilege and be entitled to access all communications, including legal advice, received by Umbrella Venture.

However, as so often happens in corporate relationships (and life), matters can go awry. What if Acme sues Umbrella Venture, alleging breach of the contract between the two entities? Or what if Brown decides that Adams' actions constitute a breach of his fiduciary duty to Umbrella Venture and wants Umbrella's counsel to undertake an investigation of Adams? What entitlement to Umbrella's privileged communications with corporate counsel does Adams, as simultaneous director of Umbrella Venture and owner and director of Acme, have?

The answer may not always be clear. In Delaware, for example, the Court of Chancery recognizes only three limitations on a director's ability to access privileged information: First, a director's access can be limited by *ex ante* agreement. Second, a board of directors can appoint a special (sub)committee of the full board, which would be free to retain separate legal counsel and whose communications with that counsel would be privileged from the remainder of the board. Third, a board of directors "can withhold privileged information once sufficient adversity exists between the director and the corporation such that the director could no longer have a reasonable expectation that he was a client of the board's counsel." *Kalisman v. Friedman*, C.A. No. 8447-VCL, 2013 WL 1668205, at *5 (Del. Ch. Apr. 17, 2013).

If *Kalisman* applied to our breach-of-contract hypothetical case, Brown might argue that Adams is not entitled to Umbrella's privileged communications with counsel because Acme's suit against Umbrella Venture created "sufficient adversity" between Adams and Umbrella Venture. Nevertheless, relying on a determination of "sufficient adversity" could be a risky position, especially in the context of a hotly contested dispute. And the breach-of-fiduciary-duty scenario is even more fraught because the adversity is less clear. Therefore, Brown and the rest of the board would be wise to appoint a special committee to investigate Adams' conduct so as to better protect the privilege (and the integrity of the investigation).

As always, the better way to prevent Adams from accessing Umbrella's privileged communications during an investigation or adverse litigation is by having such contingencies already anticipated in Umbrella Venture's operating agreement—i.e., by forming an *ex ante* contract about each director's entitlement to privileged information in the event of adversity arising between a director and/or their respective company on the one hand and Umbrella Venture on the other.

As these examples illustrate, an attorney representing an individual or entity in a messy scenario like this should proceed with caution, examining the operative documents, researching the caselaw in the applicable jurisdiction, and, if appropriate, discussing the scope of privilege with opposing counsel as soon as possible. Perhaps more importantly, though, attorneys who assist with the drafting of such corporate documents should include provisions that govern corporate privilege with the understanding that even the best-laid plans of corporations and men often go awry.

ERICA ROSENBAUM is an attorney in the firm's Business Litigation Group. Her practice emphasizes complex commercial and healthcare litigation. Prior to joining the firm, she spent two years as a judicial law clerk for Chief Judge Patrick J. Schiltz in the U.S. District Court for the District of Minnesota.

[1] *Commodity Futures Trading Com'n v. Weintraub*, 471 U.S. 343, 348 (1985).

SELLERS OF A BUSINESS **KNOW THYSELF.**

BY PETER FOUNDAS

So, you have decided to sell your business. Often this process starts with an inward reflection. You may have identified a good reason to sell, but many questions remain. Sellers at this early point often look to hire a broker or financial advisor to help get answers to their major questions. Don't stop the introspection here. Continue to think hard about what your business looks like from the inside and what additional advisor can help you get the best return. Retaining legal counsel early in the process – preferably before a letter of intent or term sheet is signed – can help you scrutinize major aspects of your business and secure a deal in your desired price range.

Experienced counsel can guide you through an effective presale internal diligence process to spot issues before a potential buyer does and deliver maximum return on what you have built. Any sophisticated buyer will do the same. Identifying issues early on can help reduce negotiating points, avoid unwanted holdbacks, and get to a closing with reduced tension. Here are some of the major areas where presale seller-side legal diligence can help identify and fix problems to avoid unintended consequences such as a buyer demanding a lower price, or worse, walking away.

IT ALL STARTS AT THE TOP – ADDRESS OWNERSHIP ISSUES

You may want to sell, but are you the only owner? Are you sure all your co-owners or other equity holders are on board? Any hint of problems or dissent at the ownership level can cause significant disruption to business operations during a sales process.

For instance, do some want to stay on as advisors or employees when a new buyer takes over? Do some have a preferred buyer in mind? Is there a sentimental or emotional issue at play that will require some level of insight or control into the business post-closing, such as retention of a board seat? Are there any company loans, bonuses, or other monies owed to or by an owner? Does everyone understand exactly how the sale proceeds will be divided under the governing documents of your company? These questions are just some of the issues that can cause a deal to fall apart if not fully vetted before a buyer starts negotiating.

A good strategy is to have experienced counsel on hand to help address these issues behind closed doors. A united front and a clear list of conditions for a buyer's consideration as the parties negotiate the term sheet will set the stage for an honest and direct negotiation process. Big asks like post-closing employee or consulting agreements, retention of favored employees, or exclusion of certain assets from the deal will need to be factored into the asking price. Dealing with these disparate interests among your ownership group at an early stage can avoid an embarrassing fracture in front of the buyer.

Other ownership-level issues sometimes overlooked are corporate records and registration. Counsel can clean up any required corporate resolutions, assemble board minutes, and ensure all prior equity transfers are properly documented so a buyer cannot question who rightfully owns the business and can authorize the sale. Counsel can also assist in ensuring your business is registered in all jurisdictions where it operates, and in reviewing any license or permitting issues.

HANDSHAKES BACKED BY HARD COPY – REVIEW YOUR KEY RELATIONSHIPS

For many companies, their strategic relationships with suppliers, vendors, customers, distributors, or service providers are critical to profitability. Before allowing those relationships to come under a buyer's scrutiny, think about whether all your relationships are properly documented, and if so, whether you need to renegotiate or update terms. It is possible, for instance, that a years-long master services agreement has grown obsolete and needs updating to reflect a changed business environment. Make sure you've documented any favorable terms, such as volume or bulk discounts from key suppliers, because a buyer cannot count on a handshake deal to last. Another important consideration is whether any of these agreements prevent assignment to a new buyer without written consent. Many leases, for instance, contain strict prohibitions on assignment without landlord's express written consent, which can be triggered either in an asset sale or equity deal where a substantial portion of the ownership equity is changing hands.

SECURE THE SECRET SAUCE – PROTECT YOUR INTELLECTUAL PROPERTY

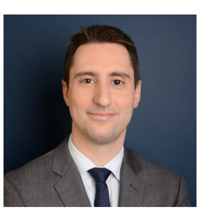
For many startups and technology businesses, intellectual property is the crown jewel of the company. Any problems uncovered by a buyer in this area will likely affect the closing process. Depending on the nature of your business, an expert can help you navigate a variety of legal issues, with some examples including registering (or renewing) your major trademarks or copyrights, ensuring you have legal right or title to use your website domains or licensed software, analyzing your patent portfolio's strength to withstand a challenge, and evaluating security measures (cyber and physical) in place to protect customer lists or other trade secrets. A robust review of the legal protections in place over your IP can instill confidence in a buyer and ensure that the purchaser can utilize these assets to their fullest post-closing potential. Strong protections here can lead to higher returns.

PREPARE YOUR PEOPLE – EMPLOYEE CONSIDERATIONS

The sale process can make many employees feel uneasy about their future at the company and could lead to departures or early retirements. One possible mitigation plan is having top managers or other crucial talent sign confidentiality and invention assignment agreements. Keep in mind that non-compete clauses may only be enforceable under limited circumstances, or perhaps not at all in your jurisdiction, so it is important to confer with legal counsel to understand whether you can or should include these clauses or whether your existing agreements offer effective protections. If you want certain individuals to stay on through a transition period, perhaps you need to think about incentive bonuses or an earn-out at closing.

CONCLUSION

Due diligence is not just a buyer's purview. A small upfront investment on the seller side can shield buyers from latent problems lurking beneath the surface and avoid an unintended consequence of a less-than-optimal deal for the sale of your business. A good attorney will help you deal with these issues and command top dollar for your business.



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