COHEN
ZIFFER
FRENCHMAN
& MCKENNA

LAW360: Del. Court Rules Against Insurers in Harman 'Bump-Up' Case

In a closely watched ruling on directors and officers insurer denials of mergers and acquisitions cost "bump-up" payouts, a Delaware judge sided on Friday with Harman International Industries' claims that insurance providers unjustifiably denied coverage for a $28 million settlement of challenges to Harman's 2017 merger with Samsung Electronics America Inc.

According to Harman, the settlement ended a federal stockholder suit accusing the company of misleading investors about its $8 billion merger with Samsung's American branch.

Harman insurers Illinois National Insurance Co., Federal Insurance Co. and Berkley Insurance Co., however, argued that the settlement reflected a contractually prohibited hike in the ultimate deal price. As a result, the insurance companies invoked a director and officer coverage term barring price "bump ups" related to post-deal increases or settlement of inadequate price claims that boost the original terms.

In a 30-page decision, Delaware Superior Court Judge Paul R. Wallace ruled Friday that the federal stockholder action that insurers focused on as being disqualifying involved Exchange Act disclosure and securities fraud allegations against Harman in the U.S. District Court for the District of Connecticut, with no claim involving "inconsiderate" deal price as a remedy.

"Without a cognizable request to remedy inadequate deal price, it hardly seems possible that a settlement of the action could represent an effective increase in deal price," Judge Wallace wrote regarding the Connecticut case, Baum v. Harman International Industries Inc. "So, for the exclusion to

apply, inadequate deal price must be a viable remedy that was sought for at least one claim" in the stockholder litigation.

"On the record developed — which the insurers say is now adequate to resolve the issue — the court cannot find that any part" of the earlier settlement "represents an amount by which the transaction price or consideration is effectively increased," the judge wrote.

In a statement on Friday, Orrie A. Levy of , counsel to Harman, described the decision as "a big win for policyholders."

"In particular, the court recognized that damages representing an increase in deal consideration are not cognizable under Section 14(a)," of the Exchange Act, Levy said, "and that the terms of the settlement and other record evidence showed that the settlement represented the avoidance of the anticipated cost of defense, rather than an effective increase in deal consideration."

Judge Wallace observed that the parties didn't say what the stockholder settlement represented, but the insurers asserted that the 2017 suit sought "compensatory and/or rescissory damages," and pointed to that "as the basis to deny coverage under their bump-up exclusions."

Harman had estimated that its defense costs in the Baum action would have ranged from $25 million to $30 million, with the settlement coming in at $28 million — "right in the middle of the litigation cost estimate," Judge Wallace wrote. He said separately: "Avoiding the cost of further litigation is a valid reason to settle and the court has no reason to believe this reasoning was pretextual."

The decision could prove important to litigation over similar bump-up disputes elsewhere, given Delaware's status as an important center for corporate litigation.

Judge Wallace wrote that there had been no evidence on the true value of the shares that changed hands in the $112 per-share transaction.

"But if left to engage in such speculation, the [$28 million] settlement amount seems grossly inadequate as compensation for an inadequate deal price," the judge wrote. "There were 69,883,605 shares of

Harman common stock," with those who sued in federal court alleging that the true value was $116 per share.

"Taking this claim as true, the difference in the shares' actual value versus the deal value ($116 compared to $112) would be $279,534,420, which is significantly greater than the $28 million settlement," Judge Wallace noted.

The insurers who sued, Judge Wallace wrote, claimed that the court in the Baum action concluded that "inadequate consideration was sufficient to give rise to liability."

But the Baum court found that the loss alleged in the federal case resulted from alleged false statements or material omissions, the judge said, adding, "To insurers, this nuance seems of no moment. To the court though, it informs just why its conclusion here isn't at odds with the Baum court's pleading-stage ruling."

Earlier in the case, Judge Wallace wrote that, for the bump-up provision to exclude any settlement entirely, the transaction must involve a full acquisition, details regarding Baum must relate only to allegations of inadequate consideration and all of the Baum action settlement must represent an effective increase in consideration.

"Beyond debate, any bump-up provision like that here will exclude a settlement, or a specific portion of it, if the settlement clearly declares that its purpose is to remedy inadequate consideration given in an acquisition," the judge wrote.

Counsel for the insurers declined to comment on Friday.

Harman is represented by Jennifer C. Wasson and Carla M. Jones of Potter Anderson & Corroon LLP, and Robin L. Cohen, Orrie A. Levy and Maria Brinkman of .

Illinois National Insurance Co. is represented by Kurt M. Heyman and Aaron M. Nelson of Heyman Enerio Gattuso & Hirzel LLP, and Alexander S. Lorenzo and Kelsey Kingsberry of Alston & Bird LLP.

COHEN
ZIFFER
FRENCHMAN
& MCKENNA

Federal Insurance Co. is represented by Robert J. Katzenstein of Smith Katzenstein & Jenkins LLP and Daniel London of London Fischer LLP.

Berkley Insurance Co. is represented by Robert J. Katzenstein of Smith Katzenstein & Jenkins LLP and Cara T. Duffield of Wiley Rein LLP.

The case is Harman International Industries Inc. v. Illinois National Insurance Company, Federal Insurance Company and Berkley Insurance, case number N22C-05-098, in the Superior Court of the State of Delaware.

Click to read the full article.

Related People

Robin Cohen

Orrie A. Levy

Maria Brinkmann