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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

IN RE NCS HEALTHCARE, INC., SHAREHOLDERS LITIGATION	Consolidated C.A. No.19786 **CONFIDENTIAL** **FILED UNDER SEAL**

ANSWERING BRIEF OF DEFENDANTS GENESIS HEALTH VENTURES, INC. AND GENEVA SUB, INC. IN OPPOSITION TO THE CLASS PLAINTIFFS' MOTION FOR PRELIMINARY INJUNCTION

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NATURE AND STAGE OF THE PROCEEDINGS

On October 29, 2002, the Court granted summary judgment against Count I of the plaintiffs' complaint, which alleged that voting agreements, by which NCS directors and major stockholders Jon Outcalt and Kevin Shaw agreed to vote their NCS shares in favor of the NCS/Genesis merger, violated the NCS certificate of incorporation.[1]

This is the answering brief of defendants Genesis Health Ventures, Inc. and Geneva Sub, Inc. in opposition to plaintiffs' preliminary injunction application, which is based on the fiduciary duty claims that had not been dismissed in the Court's summary judgment ruling.

STATEMENT OF FACTS

A. The parties.

Defendant Genesis Health Ventures, Inc. is a Pennsylvania corporation with its headquarters in Kennett Square, Pennsylvania. It is a leading provider of healthcare and support services to the elderly. Its two principal business segments are (i) pharmacy services and (ii) inpatient care in skilled nursing and assisted living centers.

Defendant Geneva Sub, Inc. is a Delaware corporation and a wholly owned subsidiary of Genesis formed for the merger with NCS.

Defendant NCS HealthCare, Inc. is a Delaware corporation headquartered in Beachwood, Ohio. It is a leading independent provider of pharmacy services to long-term care institutions including skilled nursing facilities, assisted living facilities and other institutional healthcare facilities.

[1] The same Order dismissed the identical claim in Count I of Omnicare's complaint. In a previous Order issued October 25, 2002, the Court dismissed Counts II through V of Omnicare's second amended complaint, holding that Omnicare lacked standing to assert breach of fiduciary duty claims because it had not become an NCS shareholder until after the announcement of the challenged merger. On Omnicare's appeal, the Supreme Court has set argument for December 3, 2002.

Defendant Jon Outcalt is Chairman of NCS's board of directors. As of July 28, 2002, he was the beneficial owner of 202,063 shares of NCS Class A and 3,476,086 shares of NCS Class B stock. Outcalt Voting Agreement (GX3).[2]

Defendant Kevin Shaw is President, Chief Executive Officer and a Director of NCS. As of July 28, 2002, he was the beneficial owner of 28,905 shares of NCS Class A and 1,141,134 shares of NCS Class B stock. Shaw Voting Agreement (GX2).

The plaintiffs own an unspecified number of shares of Class A common stock. They purport to represent a class consisting of all holders of Class A common stock. Consol. Am. Compl. ¶ 24.

B. NCS begins its two-year market canvass for potential transactions.

Beginning in 1999, NCS's board of directors and management became increasingly concerned about the company's financial condition and its future viability because of developing market conditions and significant changes in the healthcare industry. A contraction of reimbursement levels from government programs and health maintenance organizations, as well as general volatility in the industry, had led NCS's single largest customer and a number of other industry participants to seek protection under the federal bankruptcy laws. Outcalt 12-13 (GX57); Sells 58 (GX59). The impact of the reduction in reimbursement rates, coupled with deterioration in the quality and collectibility of NCS's accounts receivable and the general market perception of the healthcare sector, resulted in a precipitous decline in the NCS stock price. Gemunder 179-80 (GX50). These problems were exacerbated by the fact that NCS was highly leveraged. It had $206 million of senior debt, $102 million of subordinated debt, and substantial trade credit outstanding. Pollack 58 (GX58); NCS Schedule 14D-9 dated 8/20/02 ("14D-9") at 4 (GX4); Joint Proxy Statement/Prospectus dated 11/01/02 ("S-4") at 33 (GX5).

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2 References to "GX__" are to the exhibits submitted herewith. Plaintiffs' opening brief is cited as "OB__."

In February 2000, NCS retained UBS Warburg LLC as its financial advisor to identify possible strategic alternatives that would address these concerns. Outcalt 19-22 (GX57); Sells 58 (GX59). UBS Warburg targeted dozens of different entities – potential strategic buyers, financial acquirers and other potential investors (including Omnicare) – in an attempt to solicit their interest in a variety of transactions, including debt restructurings, acquisitions and other investments in NCS. Outcalt 19-21 (GX57); Shaw 19 (GX60); Pollack 61 (GX58). While this effort was ongoing, NCS defaulted on its line of credit. Pollack 54 (GX58); Outcalt 12 (GX57). As a result, in July 2000 a committee of holders of NCS's subordinated debentures (the "Noteholder Committee") was formed. Mencher 22 (GX55). To preserve its cash, NCS in late August 2000 stopped making payments to its principal supplier. Pollack 55 (GX58); 14D-9 at 4-5 (GX4); S-4 at 33 (GX5).

By October 2000, UBS Warburg's efforts had produced only one non-binding indication of interest, at an implied enterprise value of only $190 million – substantially less than the face value of NCS's senior debt. *See* 14D-9 at 5 (GX4). Under increasing pressure from its senior lenders and the Noteholder Committee, NCS began to consider a potential bankruptcy filing. At the same time, its relationship with Warburg deteriorated, Sells 59 (GX59); Outcalt 23 (GX57), and after careful consideration, including interviews, reference checks and a board presentation, NCS hired Brown, Gibbons, Lang & Company in December 2000 to replace UBS Warburg as its financial advisor. Shaw 21-23 (GX60); Brown Gibbons Retention Letter, dated 12/7/00 (GX6).

NCS's financial condition had not improved by February 2001. At that point, NCS's senior lenders required the company to pledge additional collateral security for the senior credit facility and prohibited NCS from making further interest payments on its outstanding debentures. *See* 14D-9 at 5 (GX4); S-4 at 34 (GX5). On April 6, 2001, as a result of NCS's failure to make the February interest payment due on the debentures (and because NCS indicated that it did not intend to make the August payment either), the indenture trustee gave NCS a notice of default and accelerated the entire principal on the debentures. *See* 14D-9 at 5 (GX4); S-4 at 34 (GX5); Pollack 54-55 (GX58). At about the same time, NCS began discussions with various investor groups regarding a restructuring in a "pre-packaged" bankruptcy, but NCS did not receive any proposal that it believed provided an acceptable recovery to its stakeholders. *See* 14D-9 at 5 (GX4); S-4 at 34 (GX5). By that point, the members of the Noteholder Committee believed that they had the ability to put NCS into involuntary bankruptcy proceedings should they so choose, and that they – rather than the stockholders – had the material economic interest in any transaction for NCS. Mencher 231, 237 (GX55).

C. NCS negotiates with Omnicare.

In the summer of 2001, NCS invited Omnicare to commence discussions with Brown Gibbons regarding a possible transaction. In a letter that Omnicare sent to a public fax machine at NCS, Omnicare proposed an acquisition of NCS's assets in a bankruptcy sale under § 363 of the Bankruptcy Code. Pollack 60-61 (GX58). The proposed price was $225 million, subject to the satisfactory completion of due diligence.[3] Letter from Gemunder to Shaw dated 7/20/01 (GX7). In late August 2001, Omnicare increased its price to $270 million, but still proposed to structure the transaction as an asset sale in bankruptcy. Letter from Gemunder to Shaw dated 8/29/01(GX8). Even at $270 million, Omnicare's proposal was substantially lower than the face value of NCS's outstanding debt. It would have provided little recovery to NCS's noteholders and no recovery at all to NCS's equity holders. Hodges 226-28 (GX53).

NCS asked Omnicare to execute a confidentiality agreement so that further discussions with Omnicare could be pursued. NCS and Brown Gibbons hoped to interest Omnicare in a transaction that would provide maximum value to all of NCS's stakeholders. E-mail from

[3] In bankruptcy transactions of the type repeatedly proposed by Omnicare, the purchase price represents the entire value available to satisfy debt holders, trade creditors, employee claims, transaction expenses (such as banker and legal fees) and equity holders. In a non-bankruptcy merger transactions of the types proposed by Genesis, the

(footnote continued)

Pollack to Outcalt dated 9/10/01 (GX9). But Omnicare refused to execute the form of agreement to which at least 36 other interested parties had agreed, objecting to customary restrictions on its ability: (i) to solicit NCS customers and employees; (ii) to use competitively sensitive non-public information for its own purposes, including to compete with NCS; and (iii) to acquire NCS debt securities. S-4 at 35 (GX5); Osborne 39-42, 96-97 (GX56). After protracted negotiations, Omnicare finally executed a limited confidentiality agreement in late September 2001. Gemunder 192 (GX50). That agreement allowed NCS to send Omnicare due diligence materials about the company. Confidentiality Agreement between NCS and Omnicare (GX10); *see also* 14D-9 at 5-6 (GX4); S-4 at 35-36 (GX5).

Beginning in October 2001, NCS made several direct attempts to persuade Omnicare to make a proposal that would provide some consideration to the stockholders of NCS. Pollack 63-64 (GX58). At a meeting with Omnicare's financial advisor, Merrill Lynch, Glenn Pollack of Brown Gibbons pointed out that the bankruptcy sale that Omnicare had proposed would not permit a reasonable recovery to the NCS noteholders and other unsecured creditors, and would provide no recovery to NCS's equity holders. Pollack asked Omnicare to reconsider its proposed transaction structure. Pollack 63-64, 67-68, 154 (GX58); Osborne 91 (GX56). In an effort to induce an offer for the company, Pollack told Merrill Lynch that Omnicare could derive substantial operating synergies from a merger with NCS, more than any other industry player would derive from such a transaction. Pollack 66-68, 73-83 (GX58). Later in October, Brown Gibbons provided additional due diligence material to Omnicare and offered to discuss at any time with Omnicare a possible transaction to acquire NCS. Pollack 63-64 (GX58); *see also* Omnicare Log of Due Diligence (GX11). But Omnicare advised Pollack it was not interested in pursuing a merger with NCS, rather

(footnote continued)

purchase price represents only the value to be paid to debt and equity holders; obligations to trade creditors, employees and advisors are satisfied in full after the merger.

than buying NCS's assets in a bankruptcy sale, and Omnicare never contacted NCS between early November 2001 and January 2002. Pollack 63-64, 95 (GX58); Sells 215-16, 218 (GX59). Instead, Omnicare commenced discussions with the Noteholder Committee. Hartman 70, 72 (GX52); Pollack 71 (GX58); *see also* GX12.

Nevertheless, NCS's efforts to interest Omnicare in a transaction continued into 2002. In January, Merrill Lynch requested updated financial information from NCS. In providing that additional due diligence material, Pollack stated in an e-mail to Merrill Lynch that NCS and its financial advisors were available to discuss a potential transaction at Omnicare's convenience. Pollack 63-64, 68-69, 71, 97-98 (GX58). Omnicare never responded to that invitation, nor did Omnicare's financial advisors even return Pollack's telephone calls. Pollack 64, 69, 95, 97-98 (GX58); Mencher 220-21 (GX55). Omnicare's silence in response to NCS's invitations to negotiate a transaction led NCS and its financial advisors to the only logical conclusion: that Omnicare did not have any interest in pursuing any transaction other than a purchase of assets in a bankruptcy transaction. Pollack 95 (GX58); *see also* Sells 216, 218 (GX59); Mencher 59, 75 (GX55); Osborne 39-42 (GX56).

Instead of responding to Brown Gibbons or NCS, Omnicare undertook to negotiate exclusively with the Noteholder Committee for a bankruptcy transaction. Hartman 145 (GX52); Mencher 39-40 (GX55); Pollack 97-98 (GX58). The last and best offer made by Omnicare in its negotiations with the Noteholder Committee was in March 2002, when it increased its proposal to \$313.7 million in a bankruptcy sale – which, in light of NCS's outstanding debt and obligations to unsecured trade creditors, would still provide *nothing* to the NCS stockholders and would not even satisfy NCS's debtholders in full. Hartman 118-19 (GX52); Hodges 227-28 (GX53). Omnicare purported to memorialize its proposal in a draft asset purchase agreement that it submitted to the Noteholder Committee in or about March 2002. Draft Asset Purchase Agreement (GX13). But in the view of the Committee's members, the draft agreement "did not represent the deal" that they had been discussing with Omnicare. Mencher 53-55, 58-59, 84-85, 122, 140 (GX55). Omnicare's draft asset purchase agreement also required that 20% of the purchase price be placed in escrow for an indefinite period, and it contained a $12.5 million break-up fee and expense reimbursement up to $1 million if NCS entered into an alternative transaction. Omnicare chose to include neither NCS nor its financial advisor, Brown Gibbons, in these negotiations. NCS did not even see a copy of the draft agreement until April 10, 2002. Pollack 65 (GX58); E-mail from Schwartz to Pollack dated 4/10/02 (GX14).

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Mencher 58-59 (GX55). In short, Omnicare tactically sought to acquire NCS in a bankruptcy sale, dealing solely with the Noteholder Committee, which it viewed as being in the driver's seat – as indeed the Noteholder Committee viewed itself in light of NCS's perilous final condition.

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NCS and Brown Gibbons communicated regularly with the Noteholder Committee, and kept informed of the progress of the negotiations between the Committee and Omnicare. Pollack 63-65, 68-72, 88-95 (GX58). In light of NCS's view that promising alternatives were developing that could capture value for all stakeholders, NCS indicated to the Noteholder Committee that it preferred not to pursue a bankruptcy sale. 14D-9 at 7 (GX4). Still, Pollack made clear that NCS was ready, willing and able to discuss other types of possible transactions with Omnicare. Pollack 63-65, 68-71, 88-95, 97-100 (GX58).

D. The NCS board creates an independent committee.

Beginning in the fall of 2000, NCS had implemented a variety of measures to improve cash flows from operations, including reductions in operating/overhead costs by accelerating the consolidation or closing of locations, continuing reductions in headcount, and more aggressive accounts receivable collection and inventory reductions. As a result of these and other initiatives, by early 2002, NCS began to forecast improved operating performance, although it remained in default on approximately $350 million of its debt and trade obligations. 14D-9 at 6 (GX4). The company was improving, although there was still a real risk of bankruptcy. Osborne 37-39 (GX56).

As NCS's performance improved, the NCS directors began to believe that it might be possible for NCS to enter into a transaction that (unlike Omnicare's proposals) would yield value for NCS stockholders. As a result, in March 2002 NCS determined that it would be prudent – though not required – to establish an independent committee of those board members who were neither NCS employees nor major NCS stockholders whose consideration of potential transactions might be "disproportionately affected" by their equity holdings, to the potential detriment of the holders of the company's debt. Shaw 48 (GX60); *see also* Osborne 26, 30-31 (GX56); Sells 29 (GX59). Directors Boake Sells and Professor Richard Osborne, two members of the board, who were neither employees nor significant stockholders of NCS, Pollack 51 (GX58), and who each had extensive knowledge of NCS and its industry, Shaw 50-51 (GX60), were appointed to the independent committee to consider and negotiate possible transactions for the company. Sells 44-45 (GX59) ("my role as the head of the special committee was to make sure that we were absolutely balanced in our approach to whether it was the senior debt, the noteholders, the vendors, the equity, that there was to be a very even handed approach to how we dealt with all those constituencies"); *see also* NCS board resolution creating independent committee (GX15). The entire NCS board, however, retained authority to approve any transaction.[4]

[4] Sells and Osborne had many conversations about selecting legal counsel for the independent committee and ultimately chose the same counsel as the NCS board because they knew that counsel to be competent and independent. Osborne 63-70 (GX56). The independent committee chose to retain Brown Gibbons for similar reasons. *Id.* at 79-84. The focus, of course, was to avoid possible conflict vis-à-vis the debtholders, not the stockholders.

E. NCS and Genesis discuss a possible deal.

While Omnicare was continuing to deal exclusively with NCS's debtholders, NCS continued to pursue other alternatives. Pollack 52-53 (GX58); Shaw 54-56 (GX60); Outcalt 34-37 (GX57); E-mail from Berlin to Pollack dated 3/11/02 (GX16); Presentation to Independent Committee dated 3/29/02 (GX17). Throughout the second half of 2001 and into 2002, NCS engaged in fairly detailed negotiations with a number of parties, entailing the exchange of proposed term sheets, letters of intent and the advancement by NCS of due diligence expenses incurred by interested parties. Shaw 54-59 (GX60). Yet NCS was unable to find a viable strategic alternative. During the winter of 2002, NCS began preliminary discussions with Genesis, which had first been contacted by the Noteholder Committee. E-mail from Berlin to Pollack dated 1/8/02 (GX18); Hager 29-30 (GX51). Unlike Omnicare, Genesis promptly executed NCS's standard form of confidentiality agreement and commenced its due diligence in early February 2002. Pollack 112-13 (GX58).

Genesis had recently been thwarted in an attempt to acquire another pharmaceutical company, an experience that crystallized for Genesis the conditions under which it would agree to pursue another such acquisition. In the fall of 2001, Genesis had signed a merger agreement with American Pharmacy Services. Because APS was in bankruptcy proceedings, the transaction was subject to an auction under the auspices of the bankruptcy court. Omnicare, which had theretofore shown little interest in APS, appeared at the bankruptcy court auction and topped Genesis' deal. Hager 20-21 (GX51). Genesis believed that Omnicare's bid for APS "was defensive in nature, to prevent [Genesis] from acquiring the asset. APS as a company did not fit Omnicare's historical acquisition strategies." *Id.* at 189-90. As a result of that experience, Genesis "was not interested in incurring a lot of expense and becoming a stalking horse in an acquisition opportunity." *Id.* at 22. As Genesis director Joseph LaNasa explained:

> We did not want to put the company through an experience like that again. It was an unproductive experience. Not a function of Omnicare outbidding Genesis. A function of loss of management time and attention and a process which gets employee morale up, with the potentiality of losing. We just did not want to be a stalking horse.

LaNasa 41 (GX54); *see also id.* at 121-22. And even though Omnicare, pursuant to the terms of Genesis' merger agreement with APS, paid Genesis a topping fee, the fee was "[n]ot even close" to adequately compensating Genesis for its lost time and effort and the unproductive distraction of its management. *Id.* at 122-23; *see also* Hager 190 (GX51).

Accordingly, when Genesis representatives had their first meeting concerning a possible transaction for NCS – on May 9, 2002 with members of the Noteholder Committee at the office of one of the NCS noteholders – Genesis "made it very clear . . . that if we were going to engage in any process, that we would not do so as a stalking horse." *Id.* at 24. "We didn't want to be someone who set forth a valuation for NCS which would only result in that valuation . . . being publicly disclosed, . . . and thereby creating an environment where Omnicare felt to maintain its competitive monopolistic position, that they had to match and exceed that level." LaNasa 37 (GX54).

On May 16, 2002, Scott Berlin of Brown Gibbons, Glenn Pollack, and Boake Sells of the NCS independent committee traveled to Philadelphia to meet with George Hager, CFO of Genesis, and Michael Walker, who was then the Genesis CEO. Pollack 113 (GX58); Hager 40-41 (GX51). At that meeting, Genesis impressed upon NCS its desire to structure a transaction that would offer Genesis some certainty of completion. Genesis was "not interested in spending time or expending effort in an environment where they would become what's commonly known as a stalking horse." Pollack 114 (GX58); *see also* Hager 40-42 (GX51); Sells 97-99 (GX59). Thus, Genesis "wanted a degree of certainty that to the extent [it] w[as] willing to pursue a negotiated merger agreement . . . , [it] would be able to consummate the transaction [it] negotiated and executed." Pollack 115 (GX58). Genesis was clear and consistent on the point: Hager informed the

NCS representatives that "we wanted to see . . . a significant majority of the bondholders supporting the transaction, and controlling voting interests of the equity supporting our transaction as well, if we were to pursue an acquisition of NCS." Hager 42 (GX51). NCS's financial advisors encouraged Genesis to complete additional due diligence, after which the parties would "take another opportunity to discuss value and structure." Pollack 113 (GX58).

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After conducting the additional due diligence, Genesis in June 2002 became the first party to propose a merger transaction that would provide any value to the NCS stockholders. Initially, Genesis proposed a merger transaction with no bankruptcy filing, full recovery by the senior debt holders, 70% recovery by holders of NCS notes, full assumption of trade credit obligations and a recovery of $7.5 million for NCS equity holders. 14D-9 at 7(GX4); S-4 at 38 (GX5). Then, on June 25, following a Genesis board meeting, George Hager communicated to Pollack proposed terms for a transaction that included repayment of the NCS senior credit facility in full, full assumption of trade credit obligations, an exchange offer or direct purchase of the NCS notes providing NCS noteholders with a combination of cash and Genesis common stock equal to the par value of the NCS notes (not including accrued interest), and $20 million in value for the NCS common stock. Hager 63 (GX51). Genesis repeated its insistence on certainty: Hager informed

Pollack that "the offer came with a requirement that we had a significant majority of the bondholders agreeing to the transaction, and the shareholders representing a majority of the voting interest would also agree to the transaction." *Id.* at 64. This Genesis proposal reflected total consideration to NCS's debt and equity holders of approximately $328 million[5] plus the assumption, by virtue of the merger structure of the transaction, of additional liabilities to trade and other unsecured creditors that brought the total value of the offer to close to $400 million – more than $80 million greater than Omnicare's last offer of $313.7 million in a bankruptcy transaction. *Id.* at 97-99. Pollack communicated this proposal to the members of the NCS independent committee. Osborne 116-17 (GX56).

F. Genesis and NCS sign an exclusivity agreement.

NCS's financial advisors and legal counsel met with Genesis and its legal counsel on June 26, 2002. Pollack negotiated with Hager an increase in the aggregate value to be received by NCS's stockholders to $24 million, or about $1 per NCS common share, from Genesis' previous offer of $20 million. Hager 67 (GX51). At that meeting, Hager also

> required of [NCS] . . . if they wished us to continue to try to move this process to a definitive agreement, that they would need to do it on an exclusive basis with us. We were going to, and already had incurred significant expense, but we would incur significant additional expenses . . . , both internal and external, to bring this transaction to a definitive signing. We wanted them to work with us on an exclusive basis for a short period of time to see if we could reach agreement.

Id. at 68; *see also id.* at 77, 164. On June 27, 2002, Genesis' legal counsel delivered a form of exclusivity agreement for review and consideration by NCS's legal counsel. S-4 at 39 (GX5).

At a meeting of the NCS independent committee on July 3, 2002, Pollack presented a summary of the terms of a possible Genesis merger. The NCS independent committee considered those improved terms, as well as Genesis' demand that negotiations going forward be conducted

5 $328 million represents $308 million outstanding principal under NCS's senior debt and subordinates

(footnote continued)

under an exclusivity arrangement for a limited period of time. Pollack 122-25 (GX58). Genesis had requested a 30-day exclusivity period, but NCS was not willing to be bound for that long. Accordingly, the agreement, which was dated as of July 1 but not executed until July 3, 2002, was set to expire on July 19 – barely more than two weeks later, including the long Fourth of July holiday weekend. Exclusivity Agreement (GX19); *see also* Hager 68, 185-86 (GX51); Sells 133-34 (GX59) ("This was a very limited time thing to see if we could get to a deal."); Osborne 110-11 (GX56). If the parties were still negotiating with one another at that point, the agreement would automatically extend through July 26. GX19 at 2; Osborne 111 (GX56); S-4 at 37 (GX5).

There is no basis for plaintiffs' contention that the exclusivity agreement "precluded NCS from even considering a superior offer." OB 16. While the agreement barred NCS from soliciting proposals from other parties during that limited period, nothing in the exclusivity agreement prevented NCS from receiving alternative proposals. And the exclusivity agreement expressly provided that it did not bind NCS to execute a transaction with Genesis. GX19. If NCS did receive a proposal from another party it considered worth pursuing, it was free to cease negotiations with Genesis, wait out the short remaining term of the exclusivity agreement, and then negotiate with the third party. Sells 128-34 (GX59). NCS had previous experiences with parties requesting agreements to negotiate with them exclusively for a limited period of time. At least one party had terminated negotiations with NCS after it had refused such an agreement. S-4 at 34 (GX5). Thus, the NCS directors had good reason to believe that they had to accede to Genesis' demand for a limited exclusivity period if "we wanted them to stay in the game" (Sells 128), but that doing so did not commit them to a transaction with Genesis, especially if they received what in their judgment was a superior proposal from another party before agreeing to a transaction with Genesis.

(footnote continued)

notes, plus $20 million for the NCS common stock.

G. NCS and Genesis continue their negotiations and extend the exclusivity agreement.

After NCS signed the exclusivity agreement on July 3, Genesis provided NCS with a draft merger agreement, together with a draft of the NCS noteholders' support agreement and draft voting agreements to be entered into by Messrs. Outcalt and Shaw, who together held a majority of the voting power of the NCS common stock. Hager 102 (GX51).

With respect to the voting agreements that Genesis required as a condition of any transaction, director Outcalt testified:

> My reaction was that it was very important to NCS that we keep Genesis in the process. I did not object to the idea of a voting agreement in principle, but I made no promises.
>
> Again, my willingness to sign a voting agreement was contingent upon our board approving a merger agreement with Genesis.

Outcalt 75 (GX57); *see also* Shaw 63-67 (GX60).

While Omnicare and Merrill Lynch continued to choose to stand mute, Genesis and NCS negotiated the terms of the merger agreement over the next three weeks. Over the course of those negotiations, the NCS independent committee and the Noteholder Committee persuaded Genesis to improve the terms of its offer. Osborne 118 (GX56); Mencher 164-66 (GX55). The parties were still negotiating productively on July 19, the initial expiration date of the exclusivity agreement, so the exclusivity period was automatically extended to July 26. By that date, NCS and Genesis were on the verge of executing a merger agreement and related voting agreements. E-mail from Fish to LaNasa, 7/24/02 (noting all parties had approved transaction) (GX20). Genesis proposed a further short extension of the exclusivity agreement so that it could finalize arrangements with the noteholders, whose commitment was required. The NCS independent committee met by telephone on the morning of July 26 to consider the Genesis request. Believing that NCS and Genesis were close to reaching agreement on the definitive merger documentation, and with no basis to suspect that Omnicare or anyone else was considering proposing an alternative transaction that would pay plaintiffs and other NCS stockholders anything, the independent committee authorized an extension of the exclusivity period through July 31. Letter Agreement Extending Exclusivity Agreement (GX21); Osborne 111-12 (GX56); Hager 127-28 (GX51).[6]

H. July 26: Omnicare breaks its silence.

When the exclusivity agreement was entered into on July 3 and extended on July 26, 2002, NCS had not received any proposal from any other party that was competitive with Genesis' offer. NCS had heard nothing from Omnicare for more than five months, except as relayed through the Noteholder Committee, and had heard of no Omnicare proposal since April. And during the entire span of Omnicare's year-long discussions with either NCS or the Noteholder Committee, Omnicare never expressed any interest in any transaction other than an asset sale in bankruptcy that would pay the NCS stockholders nothing. Thus, while the stockholder plaintiffs now treat Omnicare as their champion, Omnicare before July 26 was intent on ensuring that the NCS stockholders would go home empty-handed. Pollack 67 (GX58); Hodges 227-28 (GX53). On the afternoon of Friday, July 26, after the Genesis/NCS exclusivity agreement had been extended, Omnicare, admittedly aware since "the beginning of the week" (OB 18) that Genesis was close to a deal with NCS, faxed to NCS a conditional indication of interest in a transaction. Letter from Gemunder to Outcalt dated 7/26/02 (GX23); *see also* Pollack 185-86 (GX58).

That fax proposed a highly conditional offer in which Omnicare would retire NCS's debt at par plus accrued interest, and pay the NCS stockholders $3.00 cash for each of their shares. The proposal was expressly conditioned on satisfactory negotiation of a merger agreement and on

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6 During this time period, on July 26, 2002, the independent committee engaged Candlewood Partners to act as co-financial advisor and to render a fairness opinion in connection with the Genesis transaction. REDACTED REDACTED Outcalt 26-34 (GX57); Engagement Letter dated 7/26/02 (GX22).

Plaintiffs claim that the independent committee, specifically Sells, did not know of this issue, but the testimony that they cite, *see* OB 12, only establishes that Sells did not know why the engagement letter for Candlewood Partners was entered into on that particular date. Sells 57-58 (GX59). Moreover, the record is clear that Outcalt knew of the issue. Outcalt 28-29 (GX57). REDACTED

(footnote continued)

Omnicare's satisfactory completion of due diligence. That condition – *which plaintiffs never mention in their opening brief* – was crucial to Omnicare and one of the fundamental reasons why NCS did not accept the offer. Noteholder Committee advisor Judy Mencher warned Omnicare CEO Joel Gemunder that Omnicare "wouldn't get" NCS if it clung to its due diligence requirement.

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But Omnicare did not drop the due diligence condition. Hartman 131-32 (GX52).

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What we were trying to communicate to the board was we would need, in order to satisfy our obligations to our shareholders, . . . to do some

(footnote continued)

REDACTED The fact that Outcalt, a major shareholder, knew of the point but chose to go forward with the transaction indicates that the issue was not material.

meaningful due diligence. And all of you know why. And that we couldn't be expected in a nonhostile environment to undertake an acquisition or a merger without doing some due diligence.

Id.

The risks of proceeding without further due diligence, from Omnicare's perspective, were so significant to Gemunder that he believed that incurring that risk, by proceeding with the transaction with NCS without the due diligence, would have meant his job if the resulting transaction was unfavorable. Gemunder 240 (GX50). The risk was so great to Gemunder that he was prepared to lose the opportunity of a deal with NCS rather than proceed without more due diligence. *Id.* at 240-41. Gemunder explained the "exquisite discomfort" he felt over the July 26-28 weekend:

> I was at this time [the weekend of July 26-28] in a state of exquisite discomfort because I know what [NCS] wanted and I wanted to give it to them but I also knew that I couldn't because of my responsibility to my own stockholders.
>
> . . .

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Gemunder characterized the decision he faced as a "judgment" that he and his advisors had to make. *Id.* at 160.

Late on the afternoon of July 26, 2002, NCS representatives received voicemail messages from Omnicare representatives asking to discuss the letter. Minutes of 7/28/02 meeting at 2 (GX24); Gemunder 152 (GX50). The exclusivity agreement, as extended earlier that same day, barred NCS from returning that call. Osborne 127-28 (GX56). Still, the independent committee met by telephone on July 26 to consider its response. *Id.* at 123; S-4 at 41 (GX5). Committee member Richard Osborne testified that, even apart from the exclusivity agreement, he would not have considered it wise to risk a definitive deal with Genesis for the sake of pursuing Omnicare's "highly conditional expression of interest."[7] According to Professor Osborne,

> [The independent committee] knew that without Genesis, we believed without Genesis that it would be possible for Omnicare to change the deal. I mean, say, well, we saw something in some document, so we're not going to pay full value to the creditors, or we're going to reduce the $3.00 to a dollar or 50 cents, or something. We would have been extremely vulnerable.
>
> So there was a very careful discussion and a feeling that what I call, it's a generational thing, bird in hand, before your time, but a certainty of – what seemed to be the certainty of an imminent deal that would provide all the things that we talked about repeatedly to lenders and to shareholders.
>
> And if I may, just to finish, and we were mindful of the history of the relationship with Omnicare; the repeated proposals of bankruptcy, the difficulty in negotiating even the confidentiality agreement, absence of contact, coming in at this amazing last minute.
>
> So it was a very clear decision.

Osborne 128-29 (GX56); *see also id.* at 126-32; Sells 205-08 (GX59); Mencher 228-29 (GX55).

The NCS independent committee directed Glenn Pollack to forward a copy of the Omnicare July 26 fax to George Hager of Genesis and to use the Omnicare letter as leverage to extract a better deal. Osborne 132-34 (GX56). It worked. Genesis believed Omnicare's highly conditioned indication of interest was made only for defensive purposes to disrupt Genesis' negotiations with NCS. Hager 190 (GX51); LaNasa 86 (GX54); *see also* Sells 186-89 (GX59). Nevertheless, after Pollack spoke to Hager on July 26 and requested a better offer, Genesis increased its offer to NCS on July 27 with a proposal having a total consideration to debt and equityholders of approximately $340 million (not including the value of payments to trade and other unsecured NCS creditors that would be satisfied in full following the merger). Pollack 195-96 (GX58). Genesis offered to redeem the NCS notes in cash at their full principal amount, plus accrued and unpaid interest and a redemption premium – a $31 million increase in the cash payment from

[7] REDACTED

Genesis to NCS's noteholders. Pollack 195-96 (GX58). Genesis also offered an approximately 80% increase in the amount of Genesis stock to be delivered to NCS stockholders in the tax-free merger. Hager 138-39 (GX51). Finally, Genesis agreed to reduce the termination fee in the merger agreement from the $10 million it had originally proposed to $6 million. *Id.*; S-4 at 41 (GX5). While Genesis' financial advisor, Greenhill & Co., ultimately advised Genesis that it would give Genesis an opinion that its increased offer was fair to Genesis, the increased offer was "at the very high end of the valuation range from [Genesis'] fairness perspective." Hager 135 (GX51); *see also id.* at 153. Thus, the increased Genesis offer – including 0.1 share of Genesis common stock, or approximately $1.75[8] in value for each share of NCS stock – pushed the limits of what the Genesis board was willing to authorize Genesis negotiators to pay. As Joseph LaNasa, a Genesis director and executive committee member, testified:

> They may have had the ability to go up by hundredths of a fraction of a share, but nothing substantially more than that. Nothing materially more than that. . . . Even $1.75 was more than actually we wanted to do.

LaNasa 105 (GX54); *see also* Hager 186-87 (GX51).

Thus, the offer that Genesis' negotiators made to NCS on July 27 was at the outer bounds of what Genesis could and would pay for NCS, and represented for all intents and purposes the most favorable response to Omnicare's highly conditional indication of interest that NCS could have expected to receive from Genesis. As Genesis' lead negotiator, George Hager, explained:

> I didn't know if [the Genesis increased offer] was higher or not [than the Omnicare indication of interest]. I didn't know how to interpret that [Omnicare] letter. Due diligence, outs, etc. So it was very, very difficult to try to compare and contrast. Ours was a tax-free merger, theirs was obviously a taxable merger. Or a taxable acquisition. And so it was very, very difficult to compare on an exact basis. But I felt that was the appropriate response, and at the very highest level that I was comfortable paying for the business.

[8] For negotiating purposes, Pollack and Hager agreed to value Genesis common stock based on a ten to twenty day average of the closing price for Genesis stock. Pollack Aff., 11/7/02, ¶ 2 (GX25). The NCS board, the independent committee and Pollack were well aware that Genesis' closing stock price on 7/26/02 was $16.00 per share. *Id.*

Hager 136 (GX51).

And in proposing these improved terms on July 27, Genesis made clear that its new offer was a "take it or leave it" proposition. If the revised proposal was not accepted and the requisite agreements executed by the end of the day on July 28, Genesis would withdraw its offer and terminate negotiations. Hager 149-51, 192 (GX51); LaNasa 94-96 (GX54). Genesis thus remained adamant that it would not be used as a stalking horse. As George Hager again explained:

> It was Genesis' view that there was a two-year period that NCS had conducted a process to restructure itself, and had interest from many, many parties. It was our interest to enter into exclusive negotiations after July 3, to see if we could reach agreement that we believed was fair to the Genesis shareholder and fair to all of the NCS stakeholders. If that could occur then we would reach agreement. If it couldn't occur, they were more than free to conduct an auction process or engage in any process they chose to, without Genesis' involvement prospectively.

Hager 164 (GX51).

I. July 28: The NCS directors decide to sign the improved Genesis deal.

The judgment that the NCS independent committee and the other directors Outcalt and Shaw faced on July 28 was whether to lose a certain and definitive transaction with Genesis in order to commence due diligence and negotiations with Omnicare – which had been invited long ago by NCS to bid for the company, had had more than ample opportunity to do so, had eschewed negotiation with the NCS board in favor of dealing with the NCS debtholders, had long refused to make any proposal that provided anything to the NCS stockholders, and was even then conditioning its interest on yet additional (and undefined) due diligence (and other undetermined conditions) and negotiation of a merger agreement, with all the attendant pitfalls, traps and risks. NCS and its representatives had no reason to doubt George Hager's unequivocal warning that Genesis would walk away from the table if its deal was not signed by midnight on July 28. Pollack 189 (GX58); Sells 89-90 (GX59); Osborne 126-27 (GX56). And if that happened, there would be nothing to stop Omnicare from abandoning its July 26 indication of interest altogether, reducing its offer, returning to its insistence on a purchase of NCS assets in bankruptcy or taking any number of alternatives harmful or far less attractive to Genesis. Osborne 128-29 (GX56).

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I thought there was a huge amount of risk going back to Omnicare, because I was afraid it would chase Genesis away, and a bird in hand is always worth more than two in the bush." Mencher 194 (GX55); *see also id.* at 229 ("if you have two parties both willing to pay the bondholders in full and one has no contingencies and one has a contingency, the safer bet would always be to go forward with the one with no contingencies."); Pollack 235-37 (GX58).

In substance, the risk that Omnicare's due diligence condition imposed on NCS was the converse of the view, so strongly held on the Omnicare side, that Omnicare could not bear the risk of dropping the due diligence condition.

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That very risk that due diligence might cause Omnicare to withdraw its bid is the very same reason that NCS could not afford to lose the Genesis merger.

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The NCS directors faced a similar "exquisite discomfort" and similarly had to decide what in their judgment would be the most prudent choice under the circumstances. The "exquisite" risks for one were the same for the other.[9]

[9] Omnicare continued to demand due diligence even after it began its tender offer on August 8, 2002, *see* Amend. No. 1 to Omnicare 14D-1, Item 5 (Gemunder Letter of August 8, 2002) (GX26), and did not unequivocally abandon that demand until *August 27*, *see* Amend. No. 8 to Omnicare 14D-1, Item 5 (Gemunder Letter of August 27, 2002) (GX27).

The NCS independent committee met by telephone on July 28 to consider its response to the enhanced Genesis offer. Osborne 136-37 (GX56); Minutes of July 28, 2002 meeting (GX24). Glenn Pollack updated the independent committee on the terms of that offer and on the Genesis demand that definitive documentation be executed by midnight that night or it would walk away. S-4 at 41 (GX5). Outside legal counsel briefed the committee on the material terms of the merger agreement and the related documents, including the terms and effects of the stockholder voting agreements and provisions of the merger agreement preventing NCS from accepting superior proposals in the future. *Id.* at 41-42. In particular, legal counsel reminded the NCS independent committee that the merger agreement required NCS to submit the merger to a vote of the NCS stockholders, and because NCS stockholders representing in excess of 50% of the outstanding voting power would enter into commitments to vote their shares in favor of the merger agreement, stockholder approval of the merger would be assured even if the NCS board of directors were to withdraw or change its recommendation. *Id.* at 42. The board discussed the restrictions in light of § 203 of the Delaware General Corporation Law. Minutes of July 28, 2002 meeting at 3 (GX24). Legal counsel discussed the limited circumstances in which NCS could be required to pay a termination fee to Genesis, and noted that a significant reduction in the termination fee, from $10 million to $6 million, had been negotiated. S-4 at 42 (GX5). The independent committee was also informed of various individual benefits that Messrs. Shaw and Outcalt would derive from the Genesis merger, including the agreement under which Mr. Outcalt would enter a guaranteed four-year consulting relationship with Genesis following the closing of the merger. *Id.*; Shaw 117-18 (GX60).

At the same meeting on July 28, Candlewood Partners presented the NCS independent committee with a summary of its financial analyses of the merger and orally delivered its opinion (which was later confirmed in writing) that the proposed merger exchange ratio of 0.1 shares of Genesis common stock for each share of NCS Class A common stock and NCS Class B common stock was fair, from a financial point of view, to the holders of NCS common stock.[10] Pollack at 206, 209-17 (GX58); Osborne 139-40 (GX56); Candlewood Partners fairness opinion and presentation (GX28); 14D-9 at 10 (GX4).

Following further discussion and review, the NCS independent committee unanimously determined that the merger agreement and the transactions contemplated thereby were advisable, fair, and in the best interests of all of NCS's stakeholders (other than Messrs. Outcalt and Shaw) to whom the NCS board of directors owed a fiduciary duty, and recommended that the full NCS board of directors (and NCS stockholders) approve and adopt the merger agreement and the transactions contemplated thereby. Professor Osborne summarized the reasons why the committee recommended approval of the Genesis deal:

> Because there was a significant recovery for shareholders. Because the senior lenders would be paid in full and the noteholders were being paid in full, along with accrued interest. We were avoiding a bankruptcy with a company that was in this zone of insolvency.
>
> We had an opportunity to participate in the future of Genesis by way of the merger. As I recall – I don't have to tell you, it was a merger into Genesis, so in a way we're dealing with the shareholders of Genesis merged into and they would be the owners along with our shareholders as a result.
>
> We had reason to believe that the exchange of stock would be tax-free. It was highly certain. And we were surrounded otherwise by – at that point highly certain – by uncertainty and the realization that without Genesis, we were right back in the zone of insolvency, with all our major lenders – with the default on all of our major lenders.
>
> And we had Omnicare out there and the whole history of OmniCare that we've talked about, where they repeatedly try to put us in bankruptcy, or at least their proposals would have resulted in that. And the more recent proposal, which was highly conditional, came in at a time that was very suspect, did not assure that there would be full recovery for creditors, or that the amount that they were talking about for stakeholders – or for shareholders would have been realized, because of the due diligence and other conditions that they included in their what I would call sort of proposal to begin a negotiation.

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10 Plaintiffs claim that the NCS board did not seek a collar on the value of Genesis' stock. OB 29. In fact, there were discussions of a collar but no agreement was reached. Pollack Aff. dated 11/7/02, ¶ 3 (GX25).

> So for those reasons, it was very clear that we were doing the best thing – I felt very clear, I was doing the best thing for the – for our stakeholders, the creditors, as well as the shareholders. And so I voted for recommending it to the full board.

Osborne 143-45 (GX56). Boake Sells, the other member of the independent committee, concurred:

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REDACTED [11] *see also* 14D-9 at 8-10 (GX4).

At a telephonic meeting of the full NCS board of directors that same day, the board received the recommendations of the NCS independent committee on the proposed Genesis merger agreement; NCS's financial advisor and outside legal counsel made the same presentations they had made to the independent committee that morning, Pollack 217 (GX58); and the full board voted unanimously to approve the Genesis merger. The NCS board members discussed and fully understood the import of their actions. As director Boake Sells testified:

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REDACTED ; *see also* Outcalt 99-100 (GX57) (noting that he was fully aware of the merger agreement's restrictions); Shaw 72-75 (GX60) (same); Osborne 154 (GX56) (same).

[11] Plaintiffs chide Mr. Sells for failing to remember the exact words that Omnicare used to express the highly conditional nature of its July 26 indication of interest. OB 20. Mr. Sells testified on deposition that Omnicare's July 26 letter used the words "currently intends" as a means of qualifying its indication of interest in paying off NCS's debt. "Currently intends" *are* the words that Omnicare used in its tender offer documents on August 8. Omnicare tender offer dated 8/8/02 at 1 (GX29) ("We *currently intend* after the proposed merger with Omnicare to pay-off NCS HealthCare's line of credit.") (emphasis added). The July 26 indication of interest was conditioned differently, but no less expressly, and no less significantly. The fact that Omnicare conditioned its indication of interest on the satisfactory completion of due diligence and the negotiation of a merger agreement, rather than by using the "currently intends" construction, does not make that indication of interest any more certain, and does not render unreasonable the decision of the NCS independent committee and board of directors to favor the much more definitive Genesis merger.

Moreover, the approval of Messrs. Outcalt and Shaw establishes conclusively that the reason that the NCS directors voted unanimously in favor of the Genesis merger agreement was their considered judgment that it was in the best interests of NCS stockholders at the time it was approved. Outcalt and Shaw were the two largest NCS stockholders. If they thought there was any realistic prospect of signing a deal with Omnicare on the terms suggested in the July 26 proposal, Outcalt and Shaw together would have millions of dollars worth of motive to withhold their support for the Genesis merger, let the exclusivity period lapse, and pursue a transaction with Omnicare. As Shaw explained: "I became convinced that if the board thought that the merger was good for all our constituents and asked that I sign a voting agreement, that it would be a good thing for me to do. . . I signed this agreement as a shareholder, because I wanted to." Shaw 65, 67 (GX60).

In sum, after two years of canvassing the market and considering all manner of potential transactions, with cognizance of the highly uncertain nature of the Omnicare proposal, and in light of the real possibility of insolvency, the NCS board of directors had ample reason to support its judgment on July 28 that the very real risk of losing the Genesis transaction outweighed the potential benefit of pursing Omnicare's highly conditional indication of interest. Pollack 239-40 (GX58). As NCS director Sells testified: "[t]he biggest consequence [of pursuing the Omnicare indication of interest] would be losing that Genesis deal, which I couldn't stand the thought." Sells 219 (GX59).

J. NCS executes the merger agreement, and Messrs. Outcalt and Shaw sign the voting agreements.

Following the meetings of the NCS independent committee and the NCS board of directors, representatives of NCS and Genesis finalized and executed the merger agreement and the related documents on July 28. Merger Agreement (GX1); S-4 at 43 (GX5). The NCS directors were fully familiar with the material terms of the merger agreement at the time they signed it. Outcalt 91 (GX57). ("I had reviewed a number of drafts of the merger agreement over the course of the preceding weeks. What I did prior to signing that merger agreement was to be certain that I understood any changes that had been made since I had last reviewed it, which would have been a few days earlier.").[12]

That same evening, Messrs. Outcalt and Shaw executed the voting agreements by which they agreed to vote their NCS stock in favor of the merger and against any competing proposal. Outcalt, Shaw Voting Agreements (GX3, GX2); S-4 at 43 (GX5).

K. Subsequent events.

On July 29, 2002, hours after the NCS/Genesis transaction was executed, Omnicare faxed a letter to NCS restating its *conditional* indication of interest and attaching a draft merger agreement. Later that morning, Omnicare issued a press release publicly disclosing the indication of interest, in violation of the non-disclosure obligations contained in Omnicare's confidentiality agreement with NCS. GX30; 14D-9 at 10 (GX4); S-4 at 43-44 (GX5).

On August 8, 2002, Omnicare commenced a tender offer for the NCS shares at a price of $3.50 per share. GX29. By letter dated the same day, Omnicare expressed a desire to discuss the terms of the offer with NCS. GX26. Omnicare's letter continued to condition Omnicare's proposal on satisfactory completion of a due diligence investigation of NCS, a condition conspicuously absent from Omnicare's tender offer materials distributed to NCS stockholders. 14D-9 at 10 (GX4); S-4 at 45 (GX5). Omnicare also backslid, no longer willing to say that it "will" pay-off NCS's debt, but only that it "currently intends" to do so. GX29.

On August 8, 2002 and again on August 19, 2002, the NCS independent committee and full board of directors met separately to consider the Omnicare tender offer in light of the Genesis merger agreement. NCS's outside legal counsel and NCS's financial advisor attended both

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[12] Plaintiffs claim that neither of the independent committee members read the merger agreement before signing it. OB 23. But the deposition testimony cited by the plaintiffs only establishes that Sells and Osborne did not recall precisely when they first received copies of the merger agreement, not that they were unaware of the contents of the merger agreement before signing it. Sells 64, 65 (GX59); Osborne 146-47 (GX56).

meetings. As a result of those meetings and the discussions and analyses provided at each, the NCS board recommended that the NCS stockholders reject the Omnicare tender offer. 14D-9 at 10-12 (GX4); S-4 at 45-46 (GX5).

On September 10, 2002, NCS requested and received a waiver from Genesis allowing NCS to enter into discussion with Omnicare without first having to determine that Omnicare's proposal was a superior proposal under the Genesis merger agreement (§ 5.3(c)(iv)) and without having to require Omnicare to enter into a confidentiality agreement on terms no less restrictive than the Genesis/NCS confidentiality agreement. On September 13, NCS's legal and financial advisors met with Omnicare CEO Joel Gemunder, and thereafter on several occasions with Omnicare's advisors, to discuss Omnicare's tender offer and merger proposal. S-4 at 46-47 (GX5).

It was not until October 6, 2002 – more than two months after submitting its highly conditional indication of interest on July 26 – that Omnicare made an irrevocable offer to purchase all outstanding NCS common stock for $3.50 per share. Omnicare Merger Agreement (GX32 at ex. (a)(5)(A)). In response to that latest Omnicare offer, the NCS board voted to withdraw its recommendation that the NCS stockholders approve the Genesis merger. In announcing that recommendation, NCS explained that it does not have the right to terminate the Genesis merger agreement. S-4 at 50-51 (GX5).

SUMMARY OF ARGUMENT

Plaintiffs' fiduciary duty attack on the July 28, 2002 decision of the NCS board of directors and its independent committee fails to come to grips with the record, and while doctrinaire in its approach, is incompatible with settled Delaware doctrine.

For two years, NCS had searched desperately for a buyer to save it from a bankruptcy that would provide no return to the stockholders and losses to its debtholders. In July 2002, it finally found a savior in the form of Genesis. The Genesis offer provided the certainty of making whole all of NCS's debtholders and a very significant premium on a tax-free basis, with upside potential in the combined enterprise, to its stockholders. The NCS directors reasonably decided on July 28 that the certainty of recovery for all NCS stakeholders that would result from the Genesis merger outweighed the uncertainty and risks of pursuing the July 26, last minute, *conditional* indication of interest from Omnicare – a party that NCS had invited to bid a year before, that had steadfastly refused to offer anything for the stockholders, that had chosen to deal exclusively with the Noteholder Committee for a bankruptcy sale, that on July 26 appeared motivated primarily to disrupt the competitive threat of an archrival (Genesis), and that conditioned its July 26 proposal on yet additional due diligence so as to leave it with every option to reduce its offer, impose unacceptable terms, revert to a bankruptcy transaction yielding the stockholders nothing, or walk away entirely. *Plaintiffs' entire brief is written as if the NCS directors inexplicably chose a $1.60 stock deal over a $3.00 cash deal, and ignores the critical fact: that Omnicare's July 26 offer was subject to risky merger agreement negotiations and a due diligence condition – a condition that, by Omnicare's own account, it considered critical.* In short, the choice was not between $1.60 and $3.00, but between a certain, premium transaction and the mere hope of one.

There is simply no basis in law, equity or public policy for the Court to second guess the actual decision that the NCS directors faced and made – a decision made by *unconflicted* directors, on an *informed* basis and supported by director-stockholders (Outcalt and Shaw) representing the largest economic and voting interest in the matter. Plaintiffs have no basis to argue that the NCS directors were conflicted or had any reason to prefer Genesis over Omnicare. The NCS directors could not have been better informed. They had openly shopped the company for nearly *two* years. This is not a case where a target signs up a merger and then gets a better offer the next day. NCS was well aware of Omnicare's offer when it approved the Genesis transaction. The NCS directors properly considered the pros and cons of rejecting the certain Genesis offer in favor of attempting to negotiate with Omnicare, whose last-minute interest in paying something to the stockholders was insistently conditioned on satisfactory additional due diligence. The NCS directors reasonably determined that the risks in that course of action were too great. There is no basis for the Court to second-guess that decision.

A few important points are worth emphasizing here:

1. This is not a spurned bidder case. This is not an ignored bidder case. This is a case of a bidder who made a determination not to bid anything for the equity of NCS and refused to budge from that position for months and months – despite repeated entreaties from the NCS side that it do so. There is nothing to suggest that anyone on the NCS side had any reason to, or ever did, discriminate against Omnicare or any other of the more than 50 potential parties that NCS solicited in its two-year market canvass.

2. This is a highly unusual case in one respect. A company faced with the real prospect of bankruptcy has been able to achieve a transaction that (a) fully satisfies its obligations to approximately $367 million in senior debt, subordinated notes and general unsecured liabilities, and (b) provides a premium recovery for the equity that only weeks before had traded consistently at well under $0.20 per share.[13]

3. The NCS directors' decision to accept the Genesis merger proposal on July 28, 2002 must be viewed as of that date, *ex ante*. The choice that the directors then faced was straightforward. The Genesis proposal provided certainty of both satisfying in full all of NCS's debt and offering the stockholders a tax-free, premium stock merger that includes participation in the upside potential of the combined enterprise and a future control premium. On the other hand, the July 26 invitation from Omnicare to negotiate for a $3.00 per share cash merger was purposefully (and, by Omnicare's own account, importantly) conditioned on satisfactory results of yet more due

[13] NCS common stock traded in a $.10 - $.25 per share range in the year leading up to the July 28, 2002 merger agreement. The NCS stock price exceeded $.25 per share only in May 2002, and closed at $.74 per share on July 26, 2002 the last trading date before announcement of the agreement. *See* finance.yahoo.com (historical prices for ticker

(footnote continued)

diligence and merger agreement negotiations – leaving Omnicare a huge loophole to lower its price, walk away entirely, or revert back to a bankruptcy transaction, and still offering no commitment even to satisfy completely the NCS debtholders to whom the directors also owed a fiduciary duty under our law.[14] The fact that Omnicare, post-July 28, has now committed to an offer of $3.50 is irrelevant to the assessment of whether the NCS directors breached their duties on July 28 – and would be equally irrelevant if Omnicare goes to $4.00, $5.00, or $10.00. If anything, the fact that it took Omnicare over two months after July 28 to commit to an offer only gives additional credence to the NCS directors' decision not to trade the certainty of the Genesis offer for the uncertainty of Omnicare's July 26 proposal.

4. Importantly, the NCS directors on July 28 faced the certainty that Genesis would walk away if NCS chose not to bring the process to conclusion on that date. Genesis had made clear from the outset that it would not be a stalking horse for an auction. Genesis had been down that road before in another transaction, and was not willing to do so again. The NCS directors correctly understood that Genesis was not bluffing. The plaintiffs do not dispute that the directors' assessment that Genesis would walk was both reasonable and accurate. A further "auction" was not a possibility.

5. The July 28 decision of Outcalt and Shaw to support the Genesis merger, and to commit themselves to vote for it without any out to prefer a later-surfacing alternative, is compelling confirmation of the unassailability of the NCS directors' fiduciary decision. More than anyone else – and immensely more than any of the plaintiffs – Outcalt and Shaw had a personal

(footnote continued)

symbol "NCSS.OB" for 7/25/01 through 7/26/02) (GX33). The merger exchange ratio (.1 share), even in the short term based on the Genesis stock close of July 26 ($16.00 per share), represented $1.60 per NCS share.

[14] The NCS board (and the independent committee) properly considered the interests of both equityholders *and* debt holders. *See* Sells 44-45 (GX59); *Credit Lyonnais Bank Nederland, N.V. v. Pathe Communications Corp.*, C.A. No. 12150, 1991 Del. Ch. LEXIS 215, at *108, 108 n.55 (Del. Ch. Dec. 30, 1991) (holding that directors "managing the affairs of a solvent corporation in the vicinity of insolvency" owe duties to "the corporate enterprise," including creditors

(footnote continued)

financial interest in the July 28 decision. Omnicare's July 26 proposal at its nominal price held out the prospect to Outcalt and Shaw of some $5.1 and $1.6 million, respectively, over and above the level of Genesis' offer.[15] Indisputably, Outcalt and Shaw were perfectly free as stockholders to do as they pleased, to accept or reject Genesis' requirement of a voting agreement. They chose Genesis. There can be no better proof that the NCS board's decision to sign with Genesis ought not to be considered a breach of any fiduciary duty.

6. There is no basis in Delaware law for the essentially *per se* rule that plaintiffs advocate – *viz.*, that every merger contract must include a right to terminate if a higher bid comes along. The NCS/Genesis merger agreement – which does include a right (which NCS exercised) to engage in discussions with another suitor – appropriately required that the merger be put to a stockholder vote even if the NCS board withdrew or changed its recommendation. That provision is explicitly authorized by the 1998 amendment to 8 *Del. C.* § 251(c). Delaware law allows a contract to be a contract. A merger contract is not required to be an option.

In light of these important points, it should be clear that the NCS directors' July 28 fiduciary decision should not be overturned, regardless of the standard of review applied. As a matter of business judgment – which is the proper standard for the decision to enter into the merger agreement made by informed and unconflicted directors – the decision is unassailable. The *Revlon* duty to seek the highest value reasonably available is inapplicable here since the NCS/Genesis merger is not a "sale of control" within the meaning of *QVC*. But even that heightened standard was likewise clearly met: NCS had been shopped, and had been "in-play" for more than two years, and the directors had Omnicare's conditional $3.00 offer in hand when they made their decision to

(footnote continued)

and employees, as well as shareholders, and noting that "the right (both the efficient and the fair) course to follow for the corporation may diverge from the choice" that these separate constituencies would make for themselves alone).

15 Based on the difference between Omnicare's $3.00 per share July 26 proposal and the $1.60 per share value of the Genesis merger consideration (per the $16.00 closing price of Genesis common stock on that day).

approve the Genesis transaction; there can be no argument that the directors were not aware of the values and alternatives available to NCS. Furthermore, Delaware precedents confirm that directors reasonably may consider that an offer subject to satisfactory due diligence may be rejected in favor of a certain offer, even if lower-priced. Moreover, this is a <u>reverse</u>-*Revlon* case. Before the NCS/Genesis merger, absolute control of NCS resides with Outcalt and Shaw; after the merger, the NCS public stockholders will, for the first time, be stockholders in a company with no controlling stockholders, able to freely participate in the fluid marketplace, including for corporate control. *Unocal* review has never before been applied where, as here, everything claimed to be defensive – the commitment to put the merger to a stockholder vote and the Outcalt and Shaw voting agreements – is *stockholder-empowering*, not unilateral director action preclusive of anything. Even under *Unocal*, the choice of the Genesis merger was eminently reasonable in relation to the "threat" of loss of the Genesis transaction and any recovery for the equity (and no certainty of satisfaction of debtholders) if the company were left to the tender graces of Omnicare. REDACTED

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Similarly, the considered decision of the NCS board to enter into the merger agreement – with the § 251(c) provision – was no abdication of duty under 8 *Del. C.* § 141(a). It was an *exercise* of duty. It followed a lengthy, extensive and open canvass of the market for the best available deal. "[B]usiness decisions are not an abdication of directorial authority merely because they limit a board's freedom of future action" – even if that may "make it costly and difficult (indeed, sometimes impossible) to change course…."[16] With Omnicare's steadfast refusal (despite months of entreaty) to offer even a penny to the NCS stockholders, and then Omnicare's last-minute proposal to negotiate for a $3.00 per share merger conditioned on additional due diligence and

[16] *Grimes v. Donald*, 673 A.2d 1207, 1214-15 (Del. 1996).

agreement negotiations, the fully informed decision of the NCS directors to prefer the certainty of the Genesis merger was, supremely and ineluctably, an exercise of the directors' duties and prerogatives under 8 *Del. C.* § 141(a).

The real gist of this case can be summarized easily: NCS stockholders holding a majority of the voting power have committed contractually to vote for the NCS/Genesis merger, and the merger agreement, as permitted by 8 *Del. C.* § 251(c), obligates NCS to submit the merger to its stockholders for a vote. In the absence of those agreements, neither Omnicare nor the class plaintiffs would have filed, much less be pursuing, this litigation. The heart of this case does not involve director action preventing the stockholders from tendering their shares or voting on a merger proposal. To the precise contrary, the nub of plaintiffs' application is to prevent a stockholder vote. Plaintiffs' chief complaint with the NCS directors is that they are not in a position to prevent such a vote because of the § 251(c) provision in the merger agreement, so plaintiffs ask this Court to do so.

At bottom, plaintiffs ask this Court, by the stroke of a pen on a preliminary injunction application, to clear the way for the $3.50 bid that Omnicare submitted on October 6. That *ex post facto* appeal should be rejected. If accepted, plaintiffs' position would ill serve stockholder-value maximization, as no merger partner will have confidence that its contract will be honored in the event that a later bid at a higher short-term price comes along – even from a bidder (like Omnicare) who was solicited by the target but tactically refused for months and months to come forward with even one cent for the equity. Rational merger parties will not commit themselves to their highest offers if every merger contract is only an option subject to being trumped at any point. If that becomes the law, it is stockholder value that will suffer.

ARGUMENT

I. PLAINTIFFS HAVE NOT DEMONSTRATED A PROBABILITY OF SUCCESS ON THE MERITS OF ANY OF THEIR CLAIMS.

A. The terms of the merger agreement and voting agreements do not violate § 141(a) of the DGCL.

Plaintiffs contend that the merger agreement and voting agreements are void as violative of 8 *Del. C.* § 141(a). OB 62-64. According to plaintiffs, this invalidity arises from the fact that Outcalt and Shaw are obligated by the voting agreements to vote for the merger, and that the NCS board is obligated by the merger agreement's § 251(c) provision to submit the merger to a vote. Plaintiffs argue that the directors have abdicated their duties because they are not able to terminate the merger agreement even though they are no longer recommending it. OB 63-64. Plaintiffs' argument is factually and logically flawed, and not supported by the very distinguishable holdings in *Quickturn Design Sys., Inc. v. Shapiro*, 721 A.2d 1281 (Del. 1998) and *Carmody v. Toll Bros., Inc.*, 723 A.2d 1180 (Del. Ch. 1998).

The argument is factually flawed because it assumes that NCS did not (and could not) consider the Omnicare proposal before entering into the merger agreement. The clearly established facts do not support such a premise. On July 28, 2002, the NCS board had an a clear-cut decision to make: whether to execute the definitive agreement with Genesis that provided substantial value to both the debtholders and equityholders or, instead, recommence due diligence and negotiations with Omnicare (thereby losing the Genesis offer). The NCS directors did not abdicate that decision or delegate it to someone else; they *made* the decision.

The real essence of plaintiffs' argument is that the § 251(c) provision, when combined with the voting agreements, effectively precludes the NCS directors from terminating the merger agreement, once executed, in favor of a higher offer. It is true that the merger agreement requires NCS to submit the merger to a vote of the stockholders regardless of whether the board of directors continues to recommend the merger, and it is true that Outcalt and Shaw, who hold more than a majority of the voting power of NCS, are contractually obligated to vote for the merger. However, neither of these contractual obligations, either alone or in combination, constitute an improper abdication of the NCS board's responsibilities under § 141(a).

The board's obligation to submit the merger to a vote does not result in an improper abdication by the NCS directors for two reasons. First, this term of the merger agreement is expressly sanctioned by § 251(c), which provides that "[t]he terms of the [merger] agreement may require that the agreement be submitted to the stockholders whether or not the board of directors determines at any time subsequent to declaring its advisability that the agreement is no longer advisable and recommends that the stockholders reject it." 8 *Del. C.* § 251(c). This statutory subsection obviously envisions a situation in which the board of directors, after executing a merger agreement, determines that there is a better alternative to the merger previously recommended; and this statutory subsection specifically sanctions a provision in the merger agreement that obligates the board, despite that development, *not* to terminate the merger agreement but to submit it to the stockholders for a vote. It is absurd to suggest, as plaintiffs do here, that a provision specifically envisioned and permitted by § 251(c) nonetheless results in an impermissible abdication of directorial responsibilities under § 141(a).

Elementary principles of statutory construction dictate that sections of a statute should be construed "in connection with every other part or section so as to produce a harmonious whole." *Grimes v. Alteon, Inc.*, 804 A.2d 256, 265 n.35 (Del. 2002) (construing 8 *Del. C.* §§ 152 and 157, and quoting Norman J. Singer, 2A *Sutherland on Statutory Construction* § 46:05 (2000)); *see also Lewis v. Anderson*, 477 A.2d 1040, 1045-46 (Del. 1984). And it is equally fundamental that when different sections cannot be reconciled, "the specific statute must prevail over the general," and "the later enacted statute must prevail over the earlier." *Turnbull v. Fink,* 668 A.2d 1370, 1377 (Del. 1995) (citing 2B *Sutherland on Statutory Construction* § 51.04 (5th ed. 1992)); *see also Cede & Co. v. Technicolor, Inc.*, 758 A.2d 485, 494 (Del. 2000) ("[W]hen a specific statute is enacted that appears to conflict with an existing general statute, the subsequently enacted specific statute is controlling."). Moreover, in this case, § 141(a) specifically provides that the directors shall manage the corporation "except as may be otherwise provided *in this chapter* or in [the corporation's] certificate of incorporation" (emphasis added). Applied here, the more specific and later enacted authorization in § 251(c) must prevail over any purported prohibition, as an abdication of directorial responsibilities, in the more general and earlier enacted terms of § 141(a).

Second, even absent § 251(c)'s express sanction, a provision of this type would not constitute an impermissible abdication under § 141(a).[17] Every contract entered into by a corporation in some fashion limits the business alternatives available to the corporation after the contract is executed. Such limitations and contractual obligations do not constitute abdications of directors' responsibilities under § 141(a):

> [B]usiness decisions are not an abdication of directorial authority merely because they limit a board's freedom of future action. . . . In a world of scarcity, a decision to do one thing will commit a board to a certain course of action and make it costly and difficult (indeed, sometimes impossible) to change course and do another. This is an inevitable fact of life and is not an abdication of directorial duty.

Grimes v. Donald, 673 A.2d 1207, 1214-15 (Del. 1996); *see also Schoonejongen v. Curtiss-Wright Corp.*, 143 F.3d 120, 127 (3d Cir. 1998) (discussing *Grimes*). Indeed, the determination of whether to enter into such contracts, and the negotiation of the terms of such contracts, are an important part of the management oversight of a board.

Assuming that the execution of the contract itself is not the product of a breach of fiduciary duty, there is nothing in Delaware corporate law, statutory or fiduciary, that would require directors to insist that every material contract executed by the corporation contain a provision

[17] Prior to the amendment of § 251(c), § 251 had been interpreted as precluding a merger agreement from being submitted to a shareholder vote if the board of directors had withdrawn its recommendation of the merger. However, this preclusion was not because such a clause involved an abdication of director responsibility, but simply because § 251 was construed as requiring such a recommendation to be extant at the time of the vote. This interpretive gloss to § 251 was overturned by the amendment of § 251(c).

permitting its termination in the event that the directors determined that it was no longer in the interest of the corporation to comply with the contract. *Halifax Fund, L.P. v. Response USA, Inc.*, C.A. No. 15553, 1997 Del. Ch. LEXIS 76, at *5 (Del. Ch. May 13, 1997) ("the defendant's argument that they acted under a good-faith belief that they were acting in the best interests of the corporation is not relevant, because it does not constitute a valid legal defense to the present claim for breach of contract"). While the DGCL obviously requires that most merger agreements be conditioned on stockholder approval, merger agreements are not subject to some *per se* requirement, whether under § 141(a) or otherwise, that the agreement be terminable by the corporation being "acquired"[18] if its directors determine it is no longer in the best interests of the corporation to consummate the merger. No such requirement applies to other agreements the corporation may execute, and there are other agreements that the corporation may execute that are as or more important than merger agreements. This is particularly true where, as here, approval of a majority of the stockholder voting interest has been received.

Nor are the voting agreements an abdication of directorial responsibility or otherwise prohibited under § 141. Voting agreements are specifically permitted under § 218 of the DGCL, and the voting agreements in this case relate to conduct that has nothing to do with the powers or duties of directors. These agreements relate to the right and contractual obligations of stockholders to vote their shares. Stockholders have the right to vote their shares, or to agree to vote their shares, in whatever manner they see fit. *See, e.g., Malpiede v. Townson*, 780 A.2d 1075, 1100 (Del. 2001) (quoting *Bershad v. Curtiss-Wright Corp.*, 535 A.2d 840, 845 (Del. 1987): "Stockholders in Delaware corporations have a right to control and vote their shares in their own interest."); *Williams v. Geier*, 671 A.2d 1367, 1379 (Del. 1996); *Thorpe by Castlemen v. CERBCO*, 676 A.2d

[18] If such a requirement existed, every merger agreement should be required to contain a provision that *both* parties are permitted to terminate it whenever the directors of either party determine it to be in their respective best interest to do so. But that proposition is contrary to common sense and settled law. *Cf. In re IBP, Inc. S'holder Litig.*, 789 A.2d 14, 83 (Del. Ch. 2001).

436, 444 (Del. 1996); *Frankino v. Gleason*, C.A. No. 17399, 1999 Del. Ch. LEXIS 219, at *11 (Del. Ch. Nov. 5, 1999); *In re IXC Communications, Inc. S'holder Litig.*, C.A. No. 17324, 1999 Del. Ch. LEXIS 210, at *25-26 (Del. Ch. Oct. 27, 1999); *Emerson Radio Corp. v. International Jensen, Inc.*, C.A. Nos. 15130, 14992, 1996 Del. Ch. LEXIS 100, at *47-48 (Del. Ch. Aug. 20, 1996); *Jedwab v. MGM Grand Hotels, Inc.*, 509 A.2d 584, 598 (Del. Ch. 1986).

The voting agreements do not change the analysis of whether the § 251(c) term of the merger agreement constitutes an improper abdication of directorial responsibility. The authorization of such a provision by § 251(c) is not conditioned on the absence of a voting agreement or the absence of a block of shares being committed, whether contractually or simply as a matter of business preference, to vote for the merger. It would constitute judicial legislating to superimpose such conditions on the unfettered authorization of § 251(c). *Cf. McKesson Corp. v. Derdiger*, 793 A.2d 385, 395 (Del. Ch. 2002); *Rafferty v. Hartman Walsh Painting Co.*, 760 A.2d 157, 160 (Del. 2000).

Plaintiffs are, in essence, attempting to argue that stockholder approval that locks a corporation into a course of action amounts to an improper abdication by the directors. This is obviously absurd, and not the state of our law. If it were true, it would mean that *every* Delaware corporation would be in breach of § 141(a) during the period from the stockholder meeting to the merger closing date, a period that often stretches several months. The fact that here a commitment for stockholder approval was obtained concurrently with the merger agreement does not change the analysis.

Quickturn is consistent with the foregoing analysis and is readily distinguishable from the case here. In *Quickturn*, the Supreme Court invalidated the "deferred redemption provision" in a Rights Plan. That provision prevented "interested" directors from redeeming the Rights for six months following their election. The Court concluded that this provision was an impermissible abdication of directorial responsibility under § 141(a) for the following reason:

> While the Delayed Redemption Provision limits the board of directors' authority in only one respect, the suspension of the Rights Plan, it nonetheless restricts the board's power in an area of fundamental importance to the shareholders – *negotiating a possible sale of the corporation.*

721 A.2d at 1291-92 (emphasis added). Citing prior precedent that a defensive measure operating in breach of a board's fiduciary duties is invalid, the Court ruled "*[a] fortiori*, no defensive measure can be sustained which would require a new board of directors to breach its fiduciary duty." *Id.* at 1292.

Quickturn is thus distinguishable by reason of the nature of the constraint imposed on director action there.[19] and the manner in which the constraint was imposed. In *Quickturn*, the Delayed Redemption Provision imposed an absolute constraint on the directors' ability to negotiate any transaction with an "interested party." The constraint did not merely affect the directors' ability to terminate a previously existing contract, as is the case here. Instead, in *Quickturn*, the directors were precluded from *entering into* any agreement, even where the corporation was otherwise free to do so. The § 251(c) provision of the merger agreement here simply obligates the directors of NCS to submit the agreement to a stockholder vote. Indeed, it would seem inconceivable that a stockholder vote could be thought violative of *Quickturn*.

More generally, in *Quickturn*, the restraint could correctly be termed an "abdication" by the directors because the directors voluntarily and unilaterally imposed the restraint on themselves (and on their successors) when they adopted the Rights Plan. In the present case, the

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[19] *See* E. Norman Veasey, *The Traditional Interaction Between the Delaware Court of Chancery and the Supreme Court* (Tulane Corporate Law Institute, Mar. 4, 1999), at 21-22 (footnotes omitted):

> I am a reader of the Court's *Quickturn* opinion like lawyers and judges around the country. From my reading of the opinion, it appears that *Quickturn*, like *QVC*, focuses only on the issues before the Court. The holding in *Quickturn* is that it is not legally permissible for one board of directors to disable some persons who may be elected directors in the future from exercising their statutorily-mandated managerial prerogatives with regard to the exercising of their business judgment in deciding on pill-reduction. The *Quickturn* Court's citation of *QVC*, *Grimes v. Donald* and *Abercrombie v. Davies* should make this narrow holding clear.
>
> Nothing I read in the *Quickturn* opinion addressed, for example, a contract authorized by the board that binds the *corporation* to future performance. What action a future board may take in the exercise of

(footnote continued)

limitation, such as it is, is part of an arms-length contract (the merger agreement) negotiated in a commercial transaction demanded by Genesis in exchange for Genesis' willingness to engage in a valuable transaction. NCS directors did not "abdicate" their duty; they made the decision that confronted them on July 28, and negotiated under difficult conditions the best terms possible for a financially-distressed company and entered into a contract in which each side surrendered some future optionality to obtain certainty. That is the very nature of a contract.[20]

B. The NCS directors did not breach their fiduciary duties under any standard of review.

Plaintiffs' § 141(a) "abdication" claim based on the § 251(c) provision in the merger agreement was the lead fiduciary count in plaintiffs' complaint, but now is relegated to the back of their brief. Plaintiffs repackage that argument by contending that, where there are voting agreements covering a majority of the voting power, the NCS boards' approval of a merger agreement with a provision expressly authorized by 8 *Del. C.* § 251(c) requiring that the merger be put to a stockholder vote (i) violates the duty of care if the directors do so "without adequately exploring alternative transactions prior to that time," OB 38-39; (ii) violates *Revlon* obligations, OB 40-44; and (iii) violates *Unocal* as "preclusive," "coercive" and unreasonable, OB 46-62.

Plaintiffs are asking this Court to make a striking departure from the discretion accorded to directors making hard business decisions – a discretion accorded under the business judgment standard and the *Revlon* and *Unocal* standards of review. The decisions at issue here are far too fact specific and nuanced to be relegated to "judicial rules" that virtually dictate the substance

(footnote continued)

its business judgment with respect to the corporation's contract (to honor it, breach it or negotiate modifications) was not before the Court in *Quickturn*.

20 This Court's decision in *Carmody v. Toll Bros.* is distinguishable for the same reasons. The "dead hand" provision of the Rights Plan in that case was even broader than that in *Quickturn*, and it also was self-imposed. Moreover, *Carmody* also invalidated the "dead hand" provision because it created permanent distinctions in the powers of the different directors, which were not supported by any provisions in the certificate of incorporation. 723 A.2d at 1190-91.

of the business decision being made. Moreover, neither the law nor the facts – which plaintiffs' brief simply distorts – supports plaintiffs' arguments.

1. The decisions of the NCS directors are entitled to the presumptions of the business judgment rule.

In the context of mergers and acquisitions (no less than elsewhere), the business judgment rule operates as a procedural presumption that directors of a Delaware corporation act in good faith, with the requisite care and without any conflict of interest. *McMullin v. Beran*, 765 A.2d 910, 916-17 (Del. 2000). In seeking to enjoin this transaction, the burden rests with plaintiffs to demonstrate that a majority of the NCS directors were conflicted with respect to the transaction at issue, did not exercise the requisite due care, or acted in bad faith. Plaintiffs have failed to satisfy any of these requirements.

a. The NCS directors acted in good faith and were not conflicted.

The NCS board of directors consists of four directors, two of whom, Sells and Osborne, were named as an independent committee in March 2002, when it appeared that a transaction providing recovery to the equity holders was a real prospect – *i.e.*, in order to avoid any claim by *debtholders* of a conflict. Plaintiffs make no argument that either Sells or Osborne had any interest with respect to the merger agreement that conflicted with the interests of the NCS stockholders.

In the case of the other two directors, Outcalt and Shaw, their interests were strongly aligned with the interests of all stockholders. As the two largest stockholders of NCS, Outcalt and Shaw each had more to gain from a higher offer for NCS shares than any other stockholders. The Court may presume, in the absence of any evidence to the contrary, that directors who are stockholders will act in an economically rational manner:

> A director who is also a shareholder of his corporation is more likely to have interests that are aligned with the other shareholders of that corporation, as it is in his best interest, as a shareholder, to negotiate a transaction that will result in the largest return for all shareholders.

Orman v. Cullman, 794 A.2d 5, 27 n.56 (Del. Ch. 2002) (noting also that "the weight given that fact varies with the substantiality of the challenged director's holdings"); *see also Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361, 1380-81 (Del. 1995) ("[I]t cannot be presumed that the prestige and perquisites of holding a director's office or a motive to strengthen collective power prevails over a stockholder-director's economic interest. Stockholders are presumed to act in their own best economic interests when they vote in a proxy contest."); *In re Gaylord Container Corp. S'holder Litig.*, 753 A.2d 462, 484 (Del. Ch. 2000) (same); *McMillan v. Intercargo Corp.*, 768 A.2d 492, 504 (Del. Ch. 2000) ("The normal presumption is that the owner of a substantial block who decides to sell is interested in obtaining the highest price.").

For Outcalt, the difference between the consideration in the merger agreement and Omnicare's July 26 expression of interest was approximately $5.1 million; for Shaw, the difference was approximately $1.6 million. Plaintiffs previously contended that Outcalt and Shaw are entitled to receive certain payments on and after the consummation of the Genesis transaction, Consol. Am. Compl. ¶¶ 16-17, but these are payments pursuant to contractual obligations that pre-dated the Genesis deal and would be required under an acquisition by either Genesis or Omnicare. S-4 at 64 (GX5). The only exception is a consulting agreement between Genesis and Outcalt that provides for four annual payments of $175,000, *id.* at 55, an amount that pales in comparison to millions of dollars of additional consideration that Outcalt could have gained if the July 26 Omnicare proposal had eventuated.

Moreover, the history of negotiations between NCS and Omnicare negates any suggestion that Shaw and Outcalt were conflicted to favor Genesis.

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b. The NCS directors exercised the requisite care.

The duty of care relates to the process by which the board makes a decision. *Brehm v. Eisner,* 746 A.2d 244, 264 ("Due care in the decisionmaking context is process due care only"). And the applicable standard of conduct is "gross negligence." *Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985); *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984). Courts "do not measure, weigh or quantify directors' judgments," so the wisdom of a decision is not evaluated under the duty of care. *Brehm*, 746 A.2d at 264. Moreover, the determination of what information is necessary or material to the board decision is also a matter of directorial judgment. *Equity-Linked Investors, L.P. v. Adams*, 705 A.2d 1040, 1058 (Del. Ch. 1997) ("Where judgment is inescapably required, all that the law may sensibly ask of corporate directors is that they exercise independent, good faith and attentive judgment, both with respect to the quantum of information necessary or appropriate in the circumstances and with respect to the substantive decision to be made.").

On July 28, 2002, the NCS directors had a clear-cut decision to make. They had to choose between Genesis' definitive, but expiring offer, or Omnicare's higher but conditional proposal. In making that decision, the process employed by the NCS board was complete, diligent and certainly not grossly negligent. This board had spent two years attempting to find either an investor or a transaction that would rescue the equity of NCS. The company had navigated a course through multiple defaults on major debt; negotiated and engaged in due diligence with a number of interested parties, only to have many never make any proposal and none make a proposal that

21 Omnicare's Gemunder even surmised that Outcalt was embarrassed by the possibility that equity investors in NCS, which he founded, might lose their entire investment. Gemunder 285 (GX50). Thus, according to Gemunder, Outcalt was not only interested as a shareholder to obtain the best transaction possible for the NCS shareholders, but he also felt a special responsibility to the other NCS shareholders to rescue their investment in the company he created.

provided value to the stockholders; and avoided a bankruptcy filing, sought by Omnicare, that would have been fatal to the equityholders. NCS also had a history with Omnicare, and knew its tactics and strategy.

All of this information was evaluated by the NCS directors. The board was advised by experienced and eminently qualified financial and legal counselors. It had a merger partner with whom months of due diligence had been performed and a merger agreement that was the product of a month of negotiations. The board identified all the relevant factors to be considered in making the decision, and the board considered all of the information available to it on each of those factors. Finally, the board had the reaction and judgment of the two largest stockholders of NCS, who had more to gain or lose from the decision than anyone else. The NCS board performed as all boards should.

Plaintiffs make a number of factual arguments that distort the reality faced by the NCS directors, and even distort the very nature of the decision before them. For example:

(a) Plaintiffs contend that NCS "ignored Omnicare, both before and after they approved the merger agreement." OB 37. This assertion is manifestly false. The record is clear that NCS attempted to persuade Omnicare to offer something for the NCS shareholders. Pollack 63-65, 66-69, 71, 95-100 (GX58); Gemunder 93-94 (GX50). Omnicare refused. Gemunder and Hodges, two key Omnicare officers and directors, both testified that Omnicare would not have been willing to offer anything for the NCS shareholders absent the Genesis proposal. Gemunder 90-91, 120-28, 284 (GX50); Hodges 250-53 (GX53). Nor has NCS "ignored" Omnicare subsequent to the execution of the merger agreement. NCS and Omnicare have been involved in the discussions that produced Omnicare's belated "irrevocable" offer, which has prompted NCS to change its recommendation on the shareholder vote. Outcalt 111-15 (GX57).

(b) Plaintiffs complain that the NCS directors "caused NCS to enter into an exclusivity agreement. . . . denying themselves the opportunity to consider or even discuss any transaction other than the one with Genesis." OB 37. What plaintiffs ignore is that Genesis would not have negotiated without the exclusivity agreement, Hager 67-68 (GX51), and without the Genesis offer there would not have been any other proposals for NCS to consider, including the July 26 proposal by Omnicare. Gemunder 126-28 (GX50); Hodges 250-53 (GX53). Moreover, at the time the exclusivity agreement was signed, no one was excluded by it because no one else was interested, and the same was true when the exclusivity agreement was extended on July 26 (thanks to Omnicare's (non-)negotiating tactics).

(c) Plaintiffs observe that it was well-known that Omnicare was in a "position to offer the highest value for NCS." OB 39. What Omnicare was in a "position" to do, however, was irrelevant because Omnicare had made it well known that it would not make any offer that provided anything to the stockholders. Pollack 95 (GX58); Sells 216, 218 (GX59); Mencher 59, 75 (GX55); Osborne 39-42 (GX56); Gemunder 186 (GX50).

In addition, plaintiffs ignore that discussions with Omnicare on the weekend of July 26-28 would only have confirmed the wisdom of concluding a transaction with Genesis. REDACTED REDACTED NCS also would have learned not only that Omnicare's due diligence condition was a real condition, but that Omnicare had significant business concerns that it thought might not be favorably resolved after due diligence.

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Plaintiffs also ignore that Omnicare's July 26 proposal was subject to "the negotiation and execution of a mutually acceptable definitive merger agreement." Letter from

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Gemunder to Outcalt dated 7/26/02 (GX23). This was another major (and carefully constructed) reservation in Omnicare's indication of interest, and one that effectively rendered the $3.00 offer illusory. NCS had no assurance that Omnicare would not seek to impose unusual conditions or contingencies, impossible-to-satisfy representations and warranties, holdbacks or adjustments to the purchase price, or any number of other possible provisions that would have reduced the actual consideration to be delivered to NCS debt or equity holders, or reduced the likelihood of closing. Indeed, NCS had no assurance that Omnicare would find *any* terms "acceptable." Not only had NCS and Omnicare had difficulty agreeing on a confidentiality agreement, but Omnicare had been unable, after four months of negotiations, to reach an agreement with the Noteholder Committee on the terms of the asset purchase agreement, even though those parties had reached an agreement in principle on the economics of such a deal. Gemunder 62 (GX50); Mencher 58-59 (GX55).

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2. Plaintiffs' invocation of *Revlon* is unavailing; and *Revlon* precedents in any event fully support the NCS directors' decision here.

As part of their due care claim, plaintiffs also invoke *Revlon*[24] and its progeny in claiming that the NCS directors breached a *Revlon* duty to seek the best value reasonably available for the stockholders. OB 40-43. That claim is both factually unsupportable and legally incorrect.

In this part of their brief plaintiffs concede – indeed, they argue – that NCS and its financial advisor (Brown Gibbons), as well as the Noteholder Committee, had shopped NCS "actively through July 3, 2002"; that NCS tried to pursue a "structured auction"; and that the directors fully understood that their July 28 decision to enter into the merger agreement foreclosed their ability to obtain a higher price. OB 40-41. Plaintiffs engage in gross distortion of the facts,

24 *Revlon, Inc. v. MacAndrews & Forbes Holdings*, 506 A.2d 173 (Del. 1986).

however, in asserting as the linchpin of their argument that the directors "nonetheless agreed to accept the Genesis offer, which indisputably offered the NCS stockholders roughly *half* the consideration Omnicare was then offering." *Id.* at 41 (emphasis in original). Omnicare did not offer anything other than the possibility of $3.00, conditioned on satisfactory agreement negotiations and additional due diligence – facts that plaintiffs are at least consistent in ignoring. As the directors correctly understood, that condition left Omnicare with all the leeway in the world to reduce its proposal, withdraw entirely, or revert to a bankruptcy sale that would leave the stockholders with zero, which had been Omnicare's aim all along. *See, e.g.*, Osborne 126-32 (GX56); Sells 205-08 (GX59). The directors reasonably feared that Omnicare would have every incentive to do so once Genesis exited the scene after July 28, as it had made clear it would do. Plaintiffs do not dispute that the NCS directors reasonably believed that Genesis' "take it or leave it" was sincere.

Plaintiffs also are wrong as a matter of law in asserting that the *Revlon* standard attaches when directors seek to initiate an auction. What triggers *Revlon* is the sale of a company in a transaction that constitutes a change in control, *i.e.*, either an extinguishing of the stockholders' equity for cash or a transaction that results in creation of a control block. *See, e.g., Paramount Communications, Inc. v. QVC Network, Inc.*, 637 A.2d 34, 42-43 (Del. 1994). The *Revlon* inquiry is not triggered by seeking to conduct an auction that might end up with such a transaction.[25] Rather, the concern is with a transaction that represents the stockholders' one and only chance for a control premium.[26] And a stock-for-stock merger, as here, has consistently been held not to implicate *Revlon* duties. *E.g., Arnold v. Society for Savings Bancorp, Inc.,* 650 A.2d 1270, 1290 (Del. 1994)

[25] *See Wells Fargo & Co. v. First Interstate Bancorp*, C.A. No. 14696, 1996 Del. Ch. LEXIS 3, at *13 n.3 (Del. Ch. Jan. 18, 1996) (talking to a number of possible transaction partners, without actually undertaking a change of control transaction, did not invoke *Revlon* duties); *Arnold v. Society for Savings Bancorp.*, 650 A.2d 1270, 1290 (Del. 1994) (subjective intent of board did not trigger *Revlon).*

[26] *See* Vice Chancellor Leo E. Strine, Jr., *Categorical Confusion: Deal Protection Measures in Stock-for-Stock Merger Agreements*, 56 Bus. Law. 919, 927 n.25 (2001) (explaining why *Revlon* applies: "Because after such a transaction, the minority stockholders may only receive a control premium through the grace of the new controlling stockholder.").

(no change of control where control remains "in a large, fluid, changeable and changing market") (quoting *QVC*).

Indeed, this is the *reverse* of a Revlon case. As matters now stand – as has been true for every second of NCS's existence – NCS is controlled by the Class B ownership of Outcalt and Shaw. Following the NCS/Genesis merger, the NCS public stockholders will be stockholders in a company *without* a controlling stockholder, and thus, for the first time, stockholders in a company subject to an open and fluid market for control. *See QVC*, 637 A.2d at 45 (enhanced scrutiny in sale of control mandated by *diminishment* of current stockholders' voting power and control premium never being available again).

But even if *Revlon* scrutiny applied here, there would have been no breach. Under *Revlon*, the methodology employed to seek the best available value is itself a matter of judgment. There is "no single blueprint" required to be followed in the sale of every company, and the board's choices and decision-making processes – which may properly include consideration of the risk of non-consummation of a proffered alternative – are not subject to being second-guessed. *McMullin v. Beran*, 765 A.2d 910, 918 (Del. 2000); *see also QVC*, 637 A.2d at 44-45 ("'no single blueprint' that directors must follow"; court should not "second-guess" a board choice of "one of several reliable alternatives"); *Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1286-87 (Del. 1989); *Golden Cycle LLC v. Allan*, C.A. No. 16301, 1998 Del. Ch. LEXIS 237, at *48 (Del. Ch. Dec. 10, 1998) (court should not second-guess directors); *TW Servs. v. SWT Acquisition Corp.*, C.A. 10427, 1989 Del. Ch. LEXIS 19, at *24 (Del. Ch. Mar. 2, 1989) (*Revlon* duty is not "to proceed in any prescribed way; rather, it is the duty to exercise judgment (in good faith and prudently)").[27] There is no authority for

[27] Delaware courts have recognized that, even in a *Revlon* case, "deference . . . must be afforded directors in deciding how to sell a corporation," and that a board may even decide "to focus on negotiating a favorable price" with only one bidder. *In re Pennaco Energy, Inc.*, 787 A.2d 691, 693, 706 (Del. Ch. 2001). Whether "to take a public approach to selling a company versus a more discreet approach relying upon targeted marketing by an investment bank is the sort of business strategy question Delaware courts ordinarily do not answer." *McMillan v. Intercargo Corp.*, 768 A.2d 492, 505 (Del. Ch. 2000). *See also QVC*, 637 A.2d 45:

(footnote continued)

(or sense in) the proposition that, even where *Revlon* applies, a merger agreement signed after a thorough market canvass must also be subject to post-agreement market check. *See Barkan*, 567 A.2d at 1287-88 ("When . . . the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market."); *Golden Cycle*, 1998 Del. Ch. LEXIS 237, at *53 n.16 (recognizing inapplicability of post-agreement market check factor where company engaged in a "seven-month, 79 company exploration" prior to entry into merger agreement); *Braunschweiger v. American Home Shield Corp.*, C.A. No. 10755, 1989 Del. Ch. LEXIS 142, at *18-19 (Del. Ch. Oct. 26, 1989); *In re Envirodyne Indus.*, C.A. No. 10702, 1989 Del. Ch. LEXIS 42, at *9-10 (Del. Ch. Apr. 20, 1989) (finding that a thorough, pre-agreement market canvass constituted a "true market test"). No court has held, as plaintiffs implicitly contend, that a company must pursue both.

Here, the NCS directors strove over a long and difficult period to obtain the best offers available. The NCS directors may have preferred a "structured auction" with a "stalking horse" bidder, but no one – not Genesis and not Omnicare – was willing to play that role.[28] NCS then determined to agree to a short exclusivity period with Genesis – to see what could be achieved by negotiating with Genesis, with no commitment on NCS's part to agree to anything, and with NCS

(footnote continued)

> There are many business and financial considerations implicated in investigating and selecting the best value reasonably available. The board of directors is the corporate decision making body best equipped to make these judgments. Accordingly, a court applying enhanced judicial scrutiny should be deciding whether the directors made a reasonable decision, not a perfect decision. If a board selected one of several reasonable alternatives, a court should not second-guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the board's determination. Thus, courts will not substitute their business judgment for that of the directors, but will determine if the directors' decision was, on balance, within a range of reasonableness.

Quoted in *Golden Cycle*, 1998 Del. Ch. LEXIS 237, at *42.

[28] The absence of a "structured auction" is particularly irrelevant to the *Revlon* analysis where, as here, the company had very publicly been "in play" for a substantial amount of time, giving all potential bidders ample opportunity to make their interest known. *See Barkan*, 567 A.2d at 1287 (finding that "special circumstances" – namely that the filing of a Schedule 13D by a third party put Amsted "in play" for a 10 month period, with no other bidder emerging – supported a finding that Amsted's directors had satisfied their *Revlon* obligations in approving the challenged transaction).

retaining the option of allowing the exclusivity period to lapse if the directors determined that doing so would be beneficial.[29] There is no suggestion in the record – not even a hint – that NCS or its advisors skewed the process in one direction or another, in favor of one bidder over another, or had any reason to do so. And when Omnicare finally determined to offer the possibility of a transaction that would pay something to the equity (reversing its long-held refusal to do so only because it knew of Genesis' offer), Omnicare chose to burden that offer with the due diligence condition. As a result, the NCS directors reasonably decided not to lose the Genesis bid (as the record is unequivocal and uncontradicted it would have), *i.e.*, not to leave the company and its stockholders subject to Omnicare's good graces. That decision was entirely reasonable, and cannot rationally be thought to violate any fiduciary duty – under *Revlon* or otherwise.

It is well-settled that – even when *Revlon* applies – a board faced with alternative proposals may and should consider the proposals' relative risks of non-consummation. "[T]he likelihood that one of [two] alternatives may be less likely to close supplies a rational basis for preferring another proposal, even though it may be at a lower price." *Freedman v. Restaurant Assocs. Indus. Inc.*, C.A. No. 9212, 1987 Del. Ch. LEXIS 498, at *23 (Del. Ch. Oct. 16, 1987) (reasonable decision not to pursue competing proposal conditioned on due diligence). Bids conditioned on satisfactory results of due diligence or on securing financing have long been held justifiably rejected, even if nominally higher. *See id.*; *Golden Cycle,* 1998 Del. Ch. LEXIS 237, at *50 (board's rejection of bid that "remains conditioned on satisfactory results of due diligence" and other contingencies in favor of firm deal that was already in place was "defensible under *Revlon*");

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The directors certainly were entitled to choose to forego further efforts to engage with Omnicare, given Omnicare's history of refusing to engage with the company (preferring instead to pursue a bankruptcy sale with the Noteholder Committee) and its insistence on the due diligence condition that posed a substantial risk of non-consummation. *See Golden Cycle,* 1998 Del. Ch. LEXIS 237, at *48 (citing *In re J.P. Stevens & Co. S'holder Litig.*, 542 A.2d 770, 781 n.6 (Del. Ch. 1988)).

Matador Capital Mgmt. Corp. v. BRC Holdings, Inc., 729 A.2d 280, 292 (Del. Ch. 1998) (board justified in rejecting proposal that provided no evidence of any equity or debt financing). Even in the context of two all-cash bids, this Court has upheld the board's choice of a bid, like Genesis', that was "fully financed, fully investigated and able to close" promptly over a nominally higher yet more uncertain alternative offer. *Golden Cycle,* 1998 Del. Ch. LEXIS 237, at *49. Even in a *Revlon* case, directors properly are not obligated to delay, or worse to foreclose, a certain transaction merely to pursue the possibility that a conditional proposal from another party might eventuate into something more beneficial. *See Matador Capital*, 729 A.2d at 292 (emphasis added):

> It does not appear that the directors had a duty at that time to delay the proposed ACS transaction in order to pursue the possibility that ISL might succeed in promoting another bid, at least in the circumstances presented at that time. *See In re Anderson, Clayton Shareholders' Litig.*, Del. Ch., 519 A.2d 669, 676 (1986) *("Directors of a Delaware corporation have no duty to delay an otherwise appropriate transaction just because at the last minute a possible alternative arises that might, if it could be arranged, be more beneficial to the corporation or its shareholders than the transaction with which the company has been proceeding.")*.

See also In re RJR Nabisco, Inc., C.A. No. 10389, 1989 Del. Ch. LEXIS 9, at *52-*54, (Del. Ch. Jan. 31, 1989) (bidder had allowed 30 minutes for acceptance on pain of withdrawal; board could properly decide not to pursue another round of bids, as one of the costs of doing so might have been one of the bidders dropping out – even though "few thought the chances of such a withdrawal very high but no one, of course, was in a position to assure that it would not happen"; "no matter that my personal view might be that the risk was rather small").

As Chancellor Allen further observed in *RJR*, in terms apt here:

> [T]he act of asking another time for a highest and best bid might itself have costs. It is not inconceivable that KKR . . . could have walked away from the transaction. Thus, the risks (costs) associated with getting more information had to be weighed by the Committee against the likely benefits. . . . In my opinion this important decision is itself entitled to the deference courts give to business decisions made by disinterested directors with care in the honest pursuit of the corporation's interest.

> . . . It is the case that that decision was made under extreme time pressure. But where an arm's-length negotiating adversary imposes time limits, a board is forced to contend with that circumstance. If it exercises informed judgment in the circumstances, considers the risks posed by the deadline imposed, and concludes that it is prudent to act and acts with care, it has satisfied its duty.

Id. at *58-*59 (citations omitted); *see also id.* at *65-*66 (rejecting *post hoc* review of sale results under *Revlon*, and emphasizing that so long as the board's exercise of judgment is not "a sham or pretext to prefer one bidder for inappropriate reasons," the board satisfies its duties in exercising the power conferred by 8 *Del. C.* § 141(a)).

Indeed, Delaware courts and commentators have repeatedly observed that – even under *Revlon* and even apart from the 1998 adoption of 8 *Del. C.* § 251(c) – a board properly may enter into a no-outs merger agreement. *See* J.F. Johnston & F.H. Alexander, *Fiduciary Outs and Exclusive Merger Agreements*, Insights, Vol. 11, No. 2 (Feb. 1997), at 17:

> The answer to this objection [against a no-outs merger agreement] involves the recognition of a simple business reality. A fully informed board bent on value maximization may well decide that an exclusive merger agreement is the best route to value recognition. Chancellor Allen made this point at oral argument in *Renaissance Communications Corp. v. National Broadcasting Company Inc.*, [C.A. No. 14446 (Del. Ch. Aug. 3, 1995)]:
>
> > I think it is different if the board negotiates highly particular protections in order to get the highest price in the auction, because if the fiduciary duty always overrides an auction, you have just made auctions less valuable, because people obviously won't have the incentive to issue the best price. So it is self-defeating for the fiduciary law to say in all events a higher and later price gives rise to a fiduciary obligation to breach the contract.
>
> In other words, directors may conclude that the best way to maximize the value of a company is to induce a bidder to pay its highest price, which is only possible if that bidder is convinced that its bid will not be used to get other bids. . . .[30]

[30] Chancellor Allen there further observed:

> [U]nless you say that these fiduciary duties are afunctional – that is, they operate without regard to the impact they have – then there must be circumstances in which contracts can essentially – in this auction contest essentially remove from the board the later discretion. They

(footnote continued)

See also In re Mobile Communications Corp. of America, Inc., Consol. C.A. Nos. 10627, 10638, 10644, 10656 and 10697, 1991 Del. Ch. LEXIS 4, at *27 (Del. Ch. Jan. 7, 1991) (on approval of settlement; characterizing as "very weak" the *Revlon*-based claim against MCCA/BellSouth merger agreement's no-out provision post-stockholder approval); J.F. Johnston & F.H. Alexander, *supra*, (as to *Mobile*, "the distinction [between post- or pre-vote termination rights] should not be relevant to an analysis under *Revlon*. Indeed, in many situations, the necessity for regulatory approval may create a post-stockholder vote period that extends for a longer time than the period between the signing of the merger agreement and the stockholder vote.").

As the Court stated in *Malpiede v. Townson*, Del. Ch., C.A. Nos. 15943, 15944, 15946, Jacobs, V.C. (Tr. Sept. 29, 1997), in rejecting the argument that a board, which had effectively ended an auction process with no ability to accept a subsequent higher bid, was required to take steps to permit itself to deal with another bidder:

> [T]he rules of the game are not that the highest offer always wins no matter what the circumstances. This Court will intervene, but only if there is some showing measured by some appropriate evidentiary standard that the lower price [in the initial agreement] was the product of a breach of fiduciary duty.

Id. at 6.

3. Neither the provisions of the merger agreement nor the voting agreements are defensive responses subject to scrutiny under the *Unocal* doctrine because they constitute or facilitate stockholder action.

Plaintiffs argue that the voting agreements and the § 251(c) provision in the merger agreement constitute "defensive reactions" within the meaning of *Unocal Corp. v. Mesa Petroleum*

(footnote continued)

> can remove it from themselves if they do it in the right way. And they have to be able to do that. Otherwise, the auctions won't work.

Renaissance, 1995 WL 1798510, at *15 (Del. Ch. Aug. 1, 1995) (Argument on Plaintiffs' Motion for TRO). In *Renaissance*, the merger agreement provided for a "fiduciary" termination right. *See id.* at *3-4. Chancellor Allen's point was thus that the agreement could have provided for no out at all, for the policy reasons he identified – and this before 8 *Del. C.* § 251(c) and even in a *Revlon* cash sale context.

Co., 493 A.2d 946 (Del. 1985) and that these "defensive actions" were impermissibly "preclusive," "coercive" and unreasonable. OB 46-55. These propositions are wrong. As a threshold matter, the *Unocal* standard does not apply here because the voting agreements and the § 251(c) provision do not constitute unilateral board action designed to preclude or coerce stockholder choice. The voting agreements are stockholder action, not unilateral board action, and the § 251(c) provision facilitates, rather than precludes, stockholder action by requiring the NCS board to submit the merger to the stockholders for a vote. *Plaintiffs' real complaint is that they do not like the action taken by those stockholders with the power to approve the merger agreement.*[31]

The core of the *Unocal* doctrine is to subject "unilateral director action in the face of a claimed threat" to reasonableness scrutiny, *Williams v. Geier,* 671 A.2d at 1377, and to carefully scrutinize such unilateral conduct by directors when that conduct has the effect of either coercing involuntary stockholder action or precluding voluntary stockholder action. *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361, 1386-89 (Del. 1995). The fundamental point of the *Unocal* doctrine is to subject to reasonableness scrutiny unilateral board action that interferes with the ability of stockholders to tender their shares in a tender offer or otherwise act upon an acquisition proposal. Another policy that underlies *Unocal* is the tension between the stockholders' power to sell their shares and the directors' power to manage the affairs of the corporation. The reasonableness standard of *Unocal* is designed, at least in part, to address and reconcile that potential conflict. Thus, where a board action is not unilateral, and the action facilitates stockholder action, rather than precludes or coerces it, the policy concerns of *Unocal* are not implicated.[32]

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[31] One of plaintiffs' own authorities emphasizes that "the default rule under the Delaware General Corporation Law" is that "[t]he firm may be sold if stockholders agree to sell." Strine, *Categorical Confusion, supra,* at 924 (bolding and capitalization omitted). At bottom, that is what – and all that – plaintiffs are complaining about.

[32] *See also* Strine, *Categorical Confusion, supra,* at 934 n.44 ("closer reading of the cases suggests that the 'unilateral' question turns solely on whether the defensive measures were adopted without involvement by the stockholders," citing *Williams v. Geier*); *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 111 (Del. Ch. 1986) (*Unocal* review responds to the concern that "a board may be acting primarily in its own interests").

The core of plaintiffs' complaint is that stockholders holding a majority of the NCS stock made a determination to vote for the Genesis transaction, rather than pursue the Omnicare proposal, and that those stockholders, to obtain Genesis' commitment to a merger agreement, contractually obligated themselves to vote for the merger. While that voting commitment may block an offer by Omnicare, it is well-settled that *stockholder* action that may have the effect of making an acquisition of the company more difficult is *not* subject to *Unocal* scrutiny.

Thus, in *Williams v. Geier,* plaintiffs challenged a board decision to recommend a charter amendment that would recapitalize the corporation in a manner that had the practical effect of concentrating voting power in the hands of founding stockholders and adversely impacting the possibility of an acquisition not supported by those founding stockholders. The recapitalization, and the recommendation of it by the directors, was challenged as a "defensive action" subject to *Unocal* scrutiny. The Supreme Court concluded that neither the recapitalization nor the directors' decision to recommend it was subject to such scrutiny because the action was not *unilateral* board action; rather, it was action by the directors and stockholders. The Supreme Court explained that the policy underlying *Unocal* is the "omnipresent specter of the inherent conflict between the board's duty to the stockholders and the board's possible self-interest." 679 A.2d at 1377 n.18. The Court found that danger absent where the action at issue was not unilateral board action. *Id.*

A similar result was reached in *Stroud v. Grace,* 606 A.2d 75 (Del. 1992). That case also involved a charter amendment that had the alleged effect of concentrating control in the hands of certain stockholders and precluding changes in the control of the company. Nonetheless, the Supreme Court held that neither the charter provisions nor the director action recommending the charter provisions were subject to *Unocal* scrutiny:

> Inherent in all the foregoing principles [under *Unocal*] is a presumption that a board acted in the absence of an informed shareholder vote ratifying the challenged action. This significant distinction, in addition to the fact that Milliken faced no threat to corporate policy and effectiveness, or to the board's control, is fatal to plaintiffs' *Unocal* arguments.

606 A.2d at 83. *See also Emerson Radio Corp. v. International Jensen, Inc.*, C.A. Nos. 15130, 14992, 1996 Del. Ch. LEXIS 100, at *47-48 (Del. Ch. Aug. 20, 1996) (characterizing *Williams v. Geier* as holding that "an antitakeover defensive will not be reviewed under the enhanced scrutiny standard of [*Unocal*], when the defensive measure is approved by stockholders, as opposed to being adopted unilaterally by the directors").

The voting agreements and the § 251(c) provision do not constitute unilateral board action and they do not preclude or coerce stockholder action. The voting agreements are themselves the action of stockholders – not the unilateral action of directors. While the directors did approve the voting agreements, the essence of the agreement is stockholder action, not unilateral director action. It would turn *Unocal* literally upside down to hold that a voting agreement by stockholders to facilitate a merger is a "defensive action," either by the stockholders who execute the agreement or by the board of directors that approves it. The voting agreements are no more "defensive action" than the vote of stockholders at a meeting approving the merger or the execution of a written consent a day after the merger agreement is approved by the board. Nor does director approval of the voting agreements preclude or coerce stockholder action; it simply permits stockholders who have a majority of the voting interest to exercise their franchise.[33]

A comparable analysis applies to the § 251(c) provision. The 1998 amendment to § 251(c), allowing for the inclusion of such a term in a merger agreement, permits stockholder action where, under pre-existing case law, it might not have been permitted. Prior to that amendment, § 251(c) had been interpreted as precluding a stockholder vote if the board of directors, after approving the merger agreement but before the stockholder vote, had determined no longer to recommend it. *Smith v. Van Gorkom*, 488 A.2d 858, 887-88 (Del. 1985); 71 *Del. Laws* 339 (1998)

[33] If the directors of NCS had unilaterally acted to *preclude* the holders of a voting majority from exercising their voting power (or agreeing to exercise their voting power to facilitate a merger they supported), *that* board action would have been subject to the strictest scrutiny under *Unocal*. *Unitrin*, 651 A.2d at 1378-79.

(synopsis of amendment to § 251). With the amendment, the stockholders are permitted, if the merger agreement so provides, to vote on the merger regardless of whether the directors have changed or withdrawn their recommendation. This statutory amendment, and the merger agreement provision it permits, empower stockholder action, rather than preclude or coerce it.

Plaintiffs anticipate this defect in their *Unocal* claim and argue that the voting agreements (and, presumably, the § 251(c) provision in the merger agreement) are subject to *Unocal* because both involved director action, as well as stockholder action. OB 52. But the same was true in *Williams* and *Stroud*. The charter amendments at issue in those cases, no less than the voting agreements and merger agreement in this case, required both that the directors recommend the amendment and the stockholders approve it. Nonetheless, neither the charter amendments nor the directors' decisions to approve the charter amendments were subject to *Unocal* scrutiny. Board action is not defensive when it is neither unilateral nor interferes with the choice available to the stockholders. In this case, the gist of plaintiffs' complaint is that the directors did *not* preserve for themselves the ability to take defensive action, *i.e.*, withdraw their recommendation and preclude the stockholders from voting. *Unocal* does not apply to a board decision *not* to take "defensive action." *Day v. Quotron*, C.A. No. 8502, 1989 Del. Ch. LEXIS 164, at *14-15 (Del. Ch. Nov. 20, 1989); *cf. In re Pure Resources Inc. S'holder Litig.*, C.A. No. 19876, 2002 Del. Ch. LEXIS 112, at *69-70 (Del. Ch. Oct. 1, 2002).

In short, plaintiffs' invocation of *Unocal* fails on a fundamental level: the whole premise of *Unocal*'s enhanced scrutiny is the "omnipresent specter" of *director* conflict implicated by unilateral *directorial* defensive actions. What is claimed to be defensive here – the § 251(c) provision in the merger agreement and the voting agreements – are *stockholder empowering*.

4. The merger agreement and the voting agreements would be reasonable under the *Unocal* standard even if it applied here.

a. Pursuit of the Omnicare proposal risked injury to NCS and was a "threat."

It is a fundamental blind spot of plaintiffs' brief that they wholly ignore the risk, or "threat" in *Unocal* parlance, to NCS of pursuing the Omnicare proposal. First, Genesis was prepared to terminate negotiations with NCS if its definitive merger agreement were not signed on July 28. Plaintiffs do not dispute that reality, or the NCS directors' correct perception of it. Thus, pursuit of Omnicare's proposal, at a minimum, risked the loss of the Genesis transaction. Second, the loss of the Genesis transaction would have ended any leverage NCS had with Omnicare. It was very possible that Omnicare, after reviewing due diligence information, may have concluded, either in good faith or otherwise, that the assumed synergies that underlaid the July 26 proposal were not present or that, with Genesis gone, there would be no reason to maintain its $3.00 price. Omnicare purposefully and carefully maintained its total freedom to reduce its offer, walk away, or revert to the bankruptcy strategy that it had been following. Third, the NCS board of directors did not have the control of a normal board over the process of consummating a deal. The Noteholder Committee had the leverage to force NCS into bankruptcy and cause a sale of assets at a price that paid the debt in full and left nothing to the equity. Thus, if Omnicare had retreated from its offer, Omnicare had a potential seller, the Noteholder Committee, that could have forced a transaction on terms beneficial to the creditors and to Omnicare, but disastrous to the NCS stockholders. These are the real risks that NCS faced on July 28 – which plaintiffs' entire brief, and every argument in it, simply ignores.

b. The merger agreement and voting agreements are not preclusive.

Even if *Unocal* were to apply, the voting agreements and the § 251(c) provision in the merger agreement easily pass scrutiny under *Unocal*. As the Supreme Court explained in *Unitrin*, the reasonableness test under *Unocal* begins with a determination of whether the board action at issue is "preclusive" or "coercive." As explained, neither the voting agreements nor the § 251(c) provision in the merger agreement preclude or coerce stockholder action. The voting agreements *are* shareholder action. Stockholder action approving a merger cannot be deemed the type of "preclusion" or "coercion" that *Unocal* was intended to prevent.

Moreover, the consummation of the merger agreement with Genesis will not preclude the possibility of a transaction with Omnicare. The NCS stockholders are not being "cashed out" of their equity investment. They are receiving Genesis shares, which are publicly-traded, in exchange for their NCS shares.

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In *Paramount Communications, Inc. v. Time, Inc.*, 571 A.2d 1140, 1154-55 (Del. 1989) the Supreme Court held that the tender offer of Time for Warner Communications was not "draconian" under *Unocal* because "it did not preclude Paramount from making an offer for the combined Time-Warner company," *i.e.* was not preclusive.[34] *See also Unitrin*, 651 A.2d at 1387. The same is true here.

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[34] In his opinion denying Paramount's motion for a preliminary injunction, Chancellor Allen likewise noted that the revised deal did not preclude Paramount from making an offer for the combined Time-Warner entity. *See Paramount*, 1989 Del. Ch. LEXIS 77, at *65-66. This conclusion was based upon the testimony of the CEO of Paramount, who testified that Time's acquisition of Warner did not preclude Paramount from acquiring the combined entity, despite the size of the resulting company – precisely to the same effect as Gemunder's testimony here.

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c. **The NCS directors acted reasonably in approving the merger agreement.**

As the Supreme Court explained in *Unitrin*, a board's decision to take "defensive action" that is neither preclusive nor coercive is valid if it falls within a "range of reasonableness." *Unitrin*, 651 A.2d at 1387-88. When making a reasonableness inquiry, the Court does not substitute its judgment for that of the directors. Rather, even if the Court determines that a different course of action also would have been reasonable (or more reasonable), the action of the board is sustained so long as its action also is reasonable. *See also QVC*, 637 A.2d at 45 ("[A] court applying enhanced judicial scrutiny should be deciding whether the directors made a reasonable decision, not a perfect decision. If a board selected *one of several reasonable alternatives*, a court should not second-guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the board's determination.") (emphasis added); *Mentor Graphics Corp. v. Quickturn Design Sys.*, 728 A.2d 25, 40 (Del. Ch. 1998), *aff'd*, 721 A.2d 1281 (Del. 1998). Where the board is unconflicted, its judgment also will be accorded deference for that reason. *Unitrin*, 651 A.2d at 1375.

The unconflicted NCS board of directors faced a clear-cut decision on July 28. They could execute the Genesis merger agreement, which provided a great deal of value to NCS's equity and debt and which was the only definitive offer that NCS had received after a difficult two-year search or, instead, they could recommence negotiations and due diligence with Omnicare, a bidder

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(footnote continued)

that had been trying to force NCS into bankruptcy for the past nine months, and lose the Genesis deal. The NCS board fully understood that the Omnicare proposal suggested a value for the NCS shares in excess of the immediate market value of the Genesis stock to be received under the merger agreement, albeit that difference is considerably narrowed after taxes. As set forth in NCS's proxy statement, 14D-9 at 8-10 (GX4), and confirmed by the discovery record, the NCS board considered a host of factors in reaching its decision to approve the transaction with Genesis.

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Moreover, the NCS board was acting in an environment in which it could not trust Omnicare and in which NCS did not have control over its own fate. The distrust of Omnicare arose for many reasons, some known and others only reasonably suspected, but now confirmed by discovery:

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(b) Omnicare's July 26 claim that it had not had any "meaningful" due diligence to date was demonstrably false and, at best, suspicious. Omnicare had engaged in extensive due diligence with NCS the prior autumn. *See* Letter from Hartman to Pollack dated 8/16/01 (GX41); E-mails from Michael Faerm to Catherine Greany dated 10/23/01 and 10/30/01 (GX42-43). Within days of the execution of the confidentiality agreement, NCS had responded to Omnicare's requests. GX42; Omnicare Log of Due Diligence (GX11); Berlin 80-81 (GX48). At a subsequent due diligence meeting, Omnicare made an additional request for information and answers to questions raised by the information already received. GX43; Pollack 63-64 (GX58); Berlin 81-82 (GX48). That information was promptly provided except for certain categories of extremely sensitive, competitive information not covered by the confidentiality agreement. Berlin 113-14 (GX48). NCS later voluntarily provided further information. Berlin 97 (GX48); Pollack 64 (GX58). But rather than continuing discussions with NCS, Omnicare began negotiations with the Noteholder Committee.

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(e) Given Omnicare's determined efforts to avoid paying anything to the NCS equity, the NCS board had a legitimate concern that Omnicare's motivation to pay anything to the equity could be jeopardized if NCS lost the leverage of the Genesis proposal. Both Hodges, an Omnicare officer and director, and Gemunder testified that Omnicare would not have made the July 26 proposal to pay something for the equity except for the fact that Genesis had an interest in NCS. Gemunder 90-91, 120-28, 284 (GX50); Hodges 250-53 (GX53). If Genesis terminated its negotiations, the NCS board knew that Omnicare could find sufficient reason in the due diligence it was demanding to lower its price, revert to the bankruptcy transaction it had pursued all along, or walk away. Osborne 128-29 (GX56); Omnicare tender offer dated 8/8/02 at 18 (GX29) (Omnicare describes how it did not trust the financial information NCS provided to it in previous due diligence).

NCS's legitimate basis to distrust Omnicare was compounded by NCS's lack of control over its own affairs. If Genesis withdrew and Omnicare lowered its offer after due diligence, NCS lacked the ability to prevent Omnicare from completing an acquisition at the lower price. Gemunder knew that the Noteholder Committee had the ability to force NCS into bankruptcy and cause NCS to sell its assets to Omnicare without paying anything to the NCS equity. Gemunder 18 (GX50). And, if the Genesis transaction (which offered full payment to the debt) had been lost on July 28, the Noteholder Committee undoubtedly would have been motivated to close a deal with Omnicare so long as the debt was paid in full and regardless of whether the equity received anything. *Id.* at 219-20. The reality that the NCS directors faced was that Omnicare and the Noteholder Committee had the power to make that happen even if the NCS board opposed it.

The risk that NCS would lose Genesis was not just real, it was certain, and the NCS directors knew it. They also knew that acceptance of the Genesis proposal did not foreclose future opportunities for the NCS stockholders. REDACTED

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Considering all of the factors and the extraordinary situation and history of NCS, the decision of the NCS board of directors to enter into the Genesis merger agreement was well within the "range of reasonableness." Any other course presented unacceptable risks. While the plaintiffs make every effort to find fault with the outcome, the Genesis merger agreement is an extraordinarily positive result from a process that tottered on the edge of bankruptcy for over a year, and the process continues because the NCS stockholders, as future Genesis stockholders, will hold a continuing equity interest vastly superior to the one being exchanged.

5. The decisions in *ACE* and *Phelps Dodge* do not support plaintiffs' position.

The "no talk" decisions in *ACE*[36] and *Phelps Dodge*[37] provide no support for plaintiffs' doctrinaire position that the NCS directors should be deemed to have breached their duty of care or acted outside the "range of reasonableness" by agreeing to the NCS/Genesis merger agreement without "retain[ing] for themselves the ability to terminate the agreement in favor of a

36 *ACE Ltd. v. Capital Re Corp.*, 747 A.2d 95 (Del. 1999)

37 *Phelps Dodge Corp. v. Cyprus Amax Minerals Co.*, C.A. Nos. 17398, 17383, 17427, 1999 Del. Ch. LEXIS 202 (Del. Ch. Sept. 27, 1999) (Bench Ruling).

superior transaction or preserve for the stockholders the ability to decline to approve the initial merger." OB 38-39.

First, even plaintiffs necessarily limit the *per se* rule they sponsor to situations in which "a board approves a merger agreement without adequately exploring alternative transactions prior to that time." *Id.* at 38. Here, NCS fully explored alternatives for two years, openly shopping the company in an effort to avoid bankruptcy. As even plaintiffs must acknowledge, it is now accepted doctrine that no post-agreement market check is necessary as a fiduciary matter if there has been, as here, a pre-agreement market canvass. Second, the NCS/Genesis merger agreement did not contain a no-talk provision, but rather permitted NCS to have discussions with and provide confidential information to other parties – as it in fact did with Omnicare after the execution of the Genesis merger agreement.[38]

Third, and fundamentally, nothing in the analysis in *ACE* or *Phelps* supports plaintiffs' position. In *ACE*, the Capital Re board had an out under its merger agreement with ACE to terminate the agreement for a superior proposal (§ 8.3) – which right, the Court noted, the Capital Re board considered "crucial" to its ability "to protect its stockholders' rights." *ACE*, 747 A.2d at 98-99. The difficulty into which the Capital Re board had placed itself was that its merger agreement also contained a no-talk provision (§ 6.3) that prevented it from having discussions with or furnishing information to a third party unless its outside counsel opined in writing that doing so was required to prevent a breach of fiduciary duty. *Id.* As the *ACE* Court noted:

> Section 6.3 is therefore the logical gateway through which the Capital Re board must pass in order to position themselves to terminate the Merger Agreement under § 8.3.
>
> . . . That a third party would consummate a superior proposal under § 8.3 without negotiations with or material information from Capital Re strikes me as highly implausible.

[38] Merger Ag. § 5.3(c)(iv) (GX1); S-4 at 46-47 (GX5); Outcalt 112-15 (GX57).

Id. at 99 & n.8. On a TRO application by ACE seeking to prevent Capital Re from terminating the merger agreement, the *ACE* Court construed the no-talk provision as better read to leave the decision whether to talk to the board itself, *id.* at 103, and further reasoned that the contrary interpretation advocated by ACE (that an actual written opinion of counsel was required to permit discussions) would involve "an abdication by the board of its duty to determine what its own fiduciary obligations require" and render § 6.3 "no 'out' at all." *Id.* at 106, 107 ("*QVC*, Q.E.D."). Importantly, the ACE/Capital Re merger agreement did not contain an 8 *Del. C.* § 251(c) provision, *i.e.*, Capital Re had not agreed to put the merger to a vote regardless of its ultimate recommendation. *See id.* at 106 n.34. And *ACE* acknowledged – in words that bear directly on the present case – that a board could legitimately and prudently agree to a no-out merger agreement that would not allow for consideration of a subsequently emerging superior proposal:

> More fundamentally, one would think that there would be limited circumstances in which a board could prudently place itself in the position of not being able to entertain and consider a superior proposal to a transaction dependent on a stockholder vote. [FN 36].
>
> FN 36. *One legitimate circumstance may be where a board has actively canvassed the market, negotiated with various bidders in a competitive environment, and believes that the necessity to close a transaction requires that the sales contest end.*

Id. at 107 & n.36 (emphasis added).

The present case is precisely the case contemplated by the *ACE* language emphasized above. The Capital Re board had not made the judgment, plainly permitted by 8 *Del. C.* § 251(c), that its merger with ACE should be put to a stockholder vote regardless of what might come along. The issue before the Court in *ACE* was whether the merger agreement should be read to put the Capital Re board where it never thought it was, *i.e.*, in a no-out merger agreement. That is what *ACE* considered to implicate a duty of care breach – *not* affirmatively and knowingly agreeing to a no-out merger agreement:

> If the board mistakenly entered into a merger agreement believing erroneously that it had negotiated an effective out giving it the ability to consider more favorable offers, its mistake might well be found to be a breach of its duty of care.

Id. at 108-09. Here, in stark contrast, the NCS board did knowingly and carefully – after a two-year market canvas, and required to make a choice on July 28 – agree to a no-out merger agreement. Nothing in *ACE* precludes that option or requires that it be deemed an *ipso facto* breach of the duty of care or unreasonable, as plaintiffs contend.[39]

Likewise, *Phelps Dodge* decided nothing that supports plaintiffs here. The merger agreement in *Phelps Dodge* contained a "no talk" provision that was claimed to preclude either merger party from engaging in dialogue with Phelps concerning its proposal to combine with both of them. While accepting that Cyprus and Amax were "undoubtedly" under no duty to negotiate, the Court held that the decision not to negotiate "must be an informed one," and thus that no-talk provisions "are troubling precisely because they prevent a board from meeting its duty to make an informed judgment with respect to even considering whether to negotiate with a third party." *Phelps Dodge*, 1999 Del. Ch. LEXIS 202, at *4. Nothing of that sort is involved here. Here, NCS did negotiate with Omnicare. There was no lack of information; there was only a lack of a certain bid.

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[39] Noticeably restrained dicta in *ACE* suggests that a "*plausible* argument" might be constructed in that case under *Unocal,* 747 A.2d. at 108 (emphasis in original), *quoted* at OB 52. As demonstrated above, no meritorious argument under *Unocal* can be constructed here.

Indeed, the *ACE* opinion goes on to note that an acquiror has the ability to have its interest preferred, as against a fiduciary duty attack on a target's board, by "deal[ing] directly with the 'principals' – *i.e.*, the stockholders – rather than the 'agents' – *i.e.*, the board. If an acquiror wants to reduce the risk that the agent will exceed its authority, it has options for direct dealing (subject to reasonable defensive measures by the target board)." *Id.* at 109 n.52. That is precisely what the voting agreements in this case represent.

There is no pertinence at all here to plaintiffs' quotation of *ACE*'s dilation on *QVC,* OB 43-44. There is no dispute that *QVC* does not say that a board can "in all circumstances" agree to a merger agreement without an out, or that a board can enter into a merger agreement "without exercising due care." *ACE,* 747 A.2d at 107-08.

C. Plaintiffs cannot demonstrate that it is reasonably probable they will prevail on the merits of their claim that Genesis aided and abetted a breach of fiduciary duty.

The Delaware Supreme Court, in *Malpiede v. Townson*, 780 A.2d 1075 (Del. 2001), recently set forth the following four requirements for determining third-party liability for breach of a fiduciary duty: (1) existence of a fiduciary relationship; (2) breach of the fiduciary duty; (3) knowing participation in the breach by the defendants; and (4) damages proximately caused by the breach. *Id.* at 1096. Of these four requirements, plaintiffs do not have a reasonable probability of establishing any of the last three.

With regard to the second and fourth requirements, the Court explained in *Cantor Fitzgerald L.P. v. Cantor*, 724 A.2d 571 (Del. Ch. 1998), that "[a] common basis for disposing of accomplice liability theories is that [the p]laintiff has not proved the underlying claim for principal liability." *Id.* at 584. As set forth above, plaintiffs cannot prove the underlying breaches of fiduciary duty and therefore cannot possibly establish third-party liability under the *Malpiede* standard.

Moreover, plaintiffs will be unable to satisfy the third requirement. "Knowing participation" in a board's fiduciary breach requires that the third party act with the knowledge that the conduct advocated or assisted constitutes a breach. *See Malpiede*, 780 A.2d at 1097; *Associated Imports, Inc. v. ASG Indus., Inc.*, C.A. No. 5953, 1984 Del. Ch. LEXIS 483, at *33, (Del. Ch. June 20, 1984), *aff'd, Hubbard v. Associated Imports, Inc.*, 497 A.2d 787 (Del. 1985). And the Supreme Court and this Court have "consistently held that evidence of arm's-length negotiation . . . <u>negates</u> a claim of aiding and abetting, because such evidence precludes a showing that the defendants knowingly participated in the breach by the fiduciaries." *In re Frederick's of Hollywood, Inc. S'holder Litig.*, C.A. No 15944, 1998 Del. Ch. LEXIS 111, at *10 n.8 (Del. Ch. July 9, 1998) (emphasis added); *see also Greenfield v. Tele-Communications*, C.A. No. 9814, 1989 Del. Ch. LEXIS 49, at *6 (Del. Ch. May 10, 1989); *Repairman's Service Corp. v. National Intergroup, Inc.*, C.A. No. 7811, 1985 Del. Ch. LEXIS 405, at *26 (Del. Ch. Mar. 15, 1985) ("[T]here was intensive arm's-length bargaining between the parties with demands made and concessions granted on both sides."). There is more than ample evidence in the record establishing the existence of intensive arm's length negotiations between NCS and Genesis.[40]

Ignoring this authority, plaintiffs instead rely on *ACE*. OB 65-66. But nowhere in *ACE* does the Court consider third-party liability, much less a theory of aiding and abetting. Accordingly, there is no mention or application of the *Malpiede* factors. The *ACE* Court did discuss the tension between the rights of wronged stockholders and the contract rights of an acquiror after a fiduciary breach, noting that Delaware "case law does not do much to articulate an explicit rationale for [the] emphasis on the rights of the stockholders over the contract rights of the suitor." 747 A.2d at 105. In an apparent attempt to fill the void, the Court adopted three requirements for determining whether an acquiror's contract rights should yield, the first of which is: "whether the acquiror knew, or should have known, of the target board's breach of fiduciary duty." *Id.* at 105-06. Plaintiffs cannot satisfy that requirement here. The *ACE* Court explained that a contractual commitment that guarantees consummation regardless of the value of subsequent offers will usually raise suspicion (*see id.* at 106), but carved out an exception to that general observation for "circumstances . . . where a board has actively canvassed the market, negotiated with various bidders in a competitive environment, and believes that the necessity to close a transaction requires that the sales contest end." *Id.* at 107 n.36. That description depicts precisely the circumstance faced by the NCS directors here, and Genesis' perception of NCS's circumstance was precisely so.

Accordingly, in the absence of aiding and abetting, Genesis has an enforceable merger agreement with NCS, regardless of whether a breach of fiduciary duty occurred.

[40] In addition, the Delaware Courts have made clear that aiding and abetting liability arises when (1) the bidder attempts to create or exploit conflicts of interest in the board or (2) the bidder and the board conspire in or agree to the fiduciary breach. *See Malpiede*, 780 A.2d at 1097-98; *National Intergroup*, C.A. No. 7811, 1985 Del. Ch. LEXIS 405, at *26-27 (Del. Ch. Mar. 15, 1985). There is no evidence to support the existence of either set of circumstances in this case.

D. The termination fee in the merger agreement is well within the range of reasonableness.

This Court has repeatedly approved termination fees in merger agreements that do not exceed 5% of the value of the transaction. *See, e.g., Phelps Dodge*, 1999 Del. Ch. LEXIS 202, at *5 (stated in dictum that 6.3% fee stretches the "range of reasonableness"); *Kysor Indus. Corp. v. Margaux, Inc.*, 674 A.2d 889, 897 (Del. Super. Ct. 1996) ("Commentators have expressed the view that liquidated damage provisions in the one-to-five per cent range of the proposed acquisition price are within a reasonable range."); *Brazen v. Bell Atlantic Corp.*, 695 A.2d 43, 45 (Del. 1997); *Goodwin v. Live Entertainment, Inc.*, C.A. No. 15765, 1999 Del. Ch. LEXIS 5, at *69 (Del. Ch. Jan. 22, 1999) (3.125% "commonplace"); *Roberts v. General Instrument Corp.*, C.A. No. 11639, 1990 Del. Ch. LEXIS 138, at *27-28 (Del. Ch. Aug. 13, 1990) (2% "limited").

The merger agreement (§ 7.2(b)) provides a termination fee of $6 million. That fee is 1.67% of the overall $359 million transaction value at the time of the agreement, including both the debt and equity components, albeit it is 15.82% of the equity component alone.[41] Focusing on the latter percentage only, plaintiffs argue in passing that the fee is unreasonable. OB 53. It is very common to provide for a break-up fee in bankruptcy- or insolvency-related transactions where there is little or no equity value. Indeed, Omnicare paid a topping fee to Genesis on Omnicare's acquisition of APS, a transaction that provided no value for the equity. Gemunder 34-35 (GX50). While this Court recently noted that it is unresolved how the percentage computation of termination fees is made,[42] the logic for measuring those fees against the entirety of the consideration to be paid

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[41] The $359 million transaction value is calculated as the sum of (i) $37.9 million, the value of the approximately 23.7 million shares of NCS common stock outstanding on July 28 multiplied by the $1.60 per share value of the merger consideration based on the closing price of Genesis common stock on July 26, 2002, and (ii) $321 million, the approximate amount of principal, interest and change of control premium due to holders of NCS's senior debt and senior subordinated notes. It should be noted that the circumstances under which a termination fee is payable to Genesis are extremely limited and, with one exception that is within NCS's control, the fee would only be paid if NCS is actually acquired by another party. *See* Merger Ag. § 7.2(b) (GX1).

[42] This Court noted in *In re Pennaco* that while a termination fee was a "slightly smaller percentage of the combined equity and debt of Pennaco as measured by the transaction price . . . Delaware cases have tended to use equity value as the benchmark for measuring [termination fees]." *In re Pennaco Energy, Inc. S'holder Litig.*, 787 A.2d at 703

(footnote continued)

by the acquiror, not simply the equity component, is particularly compelling in this case where the requirement to pay-off NCS's existing debt was such an important element of the negotiations and ultimate agreement.

The logic is compelling for at least three additional reasons. First, the termination fee was not an unreasonable constraint on Omnicare's ability to make a higher bid. Omnicare's October 6 "irrevocable" offer is *not* conditioned on invalidation of the termination fee; it "provides for Omnicare's payment of the termination fee required by the Genesis merger agreement." S-4 at 47 (GX5).

Second, a permissible purpose of termination fees is to provide some compensation for the loss of the business opportunity to the initial bidder. In this case, the $6 million fee is far less than the loss that Genesis will suffer if it is deprived of the merger for which it negotiated and obtained a definitive agreement. It is far less, even, than Genesis' out-of-pocket expenses in pursuing the transaction.

Third, the termination fee is less than one-half the amount of the $12.5 million "topping fee" that Omnicare demanded in its proposed NCS asset purchase agreement, which provided no value to the equity. *See* Draft Asset Purchase Agreement (GX13). Indeed, if plaintiffs' position were correct, it would be impossible to have any break-up fees in bankruptcy transactions because, as in the bankruptcy offers made by Omnicare, there is most often nothing (or very little) for the equity holder in such transactions.

(footnote continued)

n.16. The Court went on to explain that "no case has squarely addressed which benchmark is appropriate. Each benchmark has analytical arguments in its favor." *Id.*

II. PLAINTIFFS HAVE NOT ESTABLISHED IRREPARABLE HARM, AND THE BALANCE OF THE EQUITIES FAVORS DENIAL OF A PRELIMINARY INJUNCTION.

A. Plaintiffs cannot establish irreparable injury.

Irreparable injury requires harm for which there is not an adequate remedy at law. *See Kohls v. Duthie*, 765 A.2d 1274, 1289 (Del. Ch. 2000). No such irreparable harm exists here. Contrary to plaintiffs' assertions (OB66-67), the bidding for NCS is completed. Omnicare has submitted an irrevocable, signed offer at a fixed price, with the consideration payable in cash (as opposed to stock);[43] Genesis has made it clear that it will not engage in a bidding war with Omnicare or any other potential purchaser of NCS; and no other party has approached NCS about making a bid for NCS, despite the significant publicity that has surrounded the announcement of the Genesis/NCS merger and the Omnicare tender offer. If plaintiffs believe the consideration they will receive in the NCS/Genesis merger is inadequate, they have an adequate remedy in appraisal rights. *See* Merger Agreement § 2.5(a) (GX1); 8 *Del. C.* § 262.

B. Genesis will be irreparably harmed by the grant of an injunction.

The only party that faces possible irreparable harm is Genesis. If the merger is enjoined, Genesis will lose the value of the combined Genesis/NCS entity, a loss that cannot be realistically calculated. *See ACE*, 747 A.2d at 101 ("[T]he opportunity to merge with or acquire another corporation is a sufficiently unique one, which, if wrongfully denied, gives rise to harm not easily quantifiable in monetary damages."); *True North,* 711 A.2d at 44-45 (describing the loss of a merger opportunity as damage that "cannot be easily quantified"). Thus, if the Court were to grant the injunction and subsequently conclude that the injunction was improvident, the potential loss to Genesis will be difficult, if not impossible, to determine. The reverse is not true

[43] *Cf. True North Communications, Inc. v. Publicis, S.A.*, 711 A.2d 34, 44-45 (Del. Ch. 1997) (finding irreparable harm where plaintiffs sought completion of a merger in which they would receive *stock* of the surviving corporation).

for plaintiffs, who have an adequate remedy at law if the motion for the preliminary injunction is not granted.

The harm that plaintiffs will suffer if the injunction is granted is therefore outweighed by the harm that NCS and Genesis will suffer if the injunction is granted. Accordingly, the balance of equities favors denial of the motion for preliminary injunction.

CONCLUSION

For the foregoing reasons, the motion for preliminary injunction should be denied.

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