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KIRKLAND **M&A UPDATE**

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Banker Beware

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In addressing disclosure claims relating to a potential conflict of interest affecting Zenith's financial adviser, the court noted with concern that, while the financial adviser's role advising Fairfax on an unrelated engagement soon before the Zenith deal was fully disclosed, the proxy statement omitted mention of the fact that the "day-to-day" banker, or "No. 2 fellow," that advised Zenith on the Fairfax transaction was the same person who had represented Fairfax on the earlier engagement. VC Laster, in what he termed a "close issue" in denying an injunction based on these disclosure claims, noted that the overlap in deal teams was "not ultimately material" in reliance on a number of factors including the absence of testimony about what this particular banker did on each deal, the unaffiliated nature and cash merger structure of the Zenith deal, and the relatively limited involvement of the bankers in negotiating the Zenith/Fairfax deal. Absent such factors, the court indicated that it would have been prepared to enjoin the shareholder vote because of the failure to fully disclose the extent of the potential conflict resulting from the overlap in personnel.

The decision holds important disclosure lessons for financial advisers and their clients by significantly expanding the extent of the court's expectations as to "full" disclosure of potential banker conflicts (an item that has been addressed more often in proxy statements as a result of NASD Rule 2290, which requires a provider of a fairness opinion to disclose any relationship with any parties to the transaction within the preceding two years). The court noted that "partial disclosure" of a potential conflict of interest may be misleading, noting that the existing disclosure about the prior Fairfax engagement would create the implication that the deal teams did not share a key banker (therefore requiring disclosure if this is not the case).

Equally important are the unstated potential implications of the decision beyond the disclosure realm, particularly in situations where there is heightened scrutiny of the "independence" of a target's advisers (e.g., an LBO, a minority squeeze-out or other affiliated transaction). Given the consolidation in the financial services industry and the move away from "exclusive" banker/client relationships, financial advisory firms often find themselves working opposite their own clients. These firms would be well-advised to pay close attention to the resulting potential conflicts of interest (far more often perceived than actual), including the composition of deal teams (especially the senior members) and the passage of time since the last opposing engagement. Clients also should be mindful of these issues as a transaction unfolds and should obtain any relevant relationship information from the advisory firm before the engagement begins, perhaps even addressing such matters in the engagement letter. VC Laster himself appeared to appreciate the more wide-ranging implications of his decision by noting that no one should cite his failure to grant the injunction as evidence that "Court of Chancery blesses same banker working for target side, having six months ago worked for bidder side."

It is clear that the Delaware courts will continue to critically appraise factors that may give rise to potential conflicts of interest for outside advisers. The list of such factors—which in recent years has focused on such items as the contingent nature of any fees and staple financing—appears to have further expanded to include the identity of individual bankers and the interval since the adviser's last engagement for the opposing party.

If you have any questions about the matters addressed in this *M&A Update*, please contact the following Kirkland authors or your regular Kirkland contact.

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