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OF THE
STATE OF DELAWARE

COURT OF CHANCERY COURTHOUSE
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Master's Final Report

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Re: *In re ISN Software Corp. Appraisal Litigation*,
Civil Action No. 8388-VCG

Dear Counsel:

This is an appraisal action brought by Petitioners Ad-Venture Capital Partners, Polaris Venture Partners, VI, L.P., and Polaris Venture Partners Founders' Fund VI, L.P. to determine the fair value of their shares in ISN Software Corp. ("ISN"). On January 9, 2013, the ISN board of directors approved a freeze-out transaction through which, upon written consent of ISN's majority stockholders, certain minority stockholders of ISN were cashed out of their interest

in ISN for $38,317 per share;[1] the Petitioners filed their Verified Petition for Appraisal in this action on March 7, 2013. On October 30, 2013, Vice Chancellor Glasscock issued a bench ruling on the Petitioners' First Motion to Compel,[2] in which he rejected the Respondent's argument that discovery from the files of certain managers and directors of ISN would not uncover information relating to the ISN board's decision in setting the merger price, and instead determined that the Petitioners' request for documents from those files was reasonably calculated to lead to the discovery of evidence both admissible and relevant in an appraisal proceeding.[3] On April 7, 2014, I heard oral argument and issued a partial bench Draft Report on the Petitioners' Second Motion to Compel; I hereby adopt my April 7 bench ruling as a Final Report, and address the remaining issues below.

I. *Analysis*

Petitioners contend in their Second Motion to Compel that (1) the Respondent has improperly claimed attorney-client privilege over certain draft documents created by management but sent to attorneys "for review," and (2) the

[1] The transaction was structured such that ISN formed a subsidiary, 2013 Sub Inc., with which ISN merged, ISN remaining the surviving entity; the Polaris entities and a third party, Gallagher, received cash in the merger while Ad-Venture Capital Partners received stock in the surviving entity. Pet'rs' Op. Br. Ex. E at 2, 6.

[2] *In re ISN Software Corp. Appraisal Litig.*, C.A. No. 8388-VCG (Del. Ch. Oct. 30, 2013) (TRANSCRIPT).

[3] *See id.* at 26:22-27:7 ("The scope of discovery under Rule 26 is broad. It's clear to me that the discovery that is being sought from the custodians from whom it is being sought is within the scope of that rule. That is, that it is designed to lead to the discovery of evidence that will be useful at this appraisal trial. The fact that only the two custodians who have already had documents produced are the ones who had knowledge of the merger is not conclusive to me in any way because this is not a breach of duty action.").

Respondent has waived the attorney-client privilege with respect to otherwise privileged communications pertaining to the ISN board's decision to set the merger price, as the Respondent has placed the merger price "at issue." I address those contentions in turn.

1. Draft Documents

The attorney-client privilege prevents discovery of communications between lawyers and clients where a lawyer's advice is sought in "a professional legal capacity;" the privilege is intended to "foster the confidence of the client and enable [her] to communicate without fear in order to seek legal advice."[4] The Petitioners here challenge the Respondent's claim of privilege over certain draft documents, including draft board minutes, created by ISN's management but "forwarded to counsel for legal review."[5] The Petitioners contend that the Respondent may not "claim privilege over a document merely because it was forwarded to counsel,"[6] as "ISN has never made a claim of work-product with respect to draft minutes," and "the drafts Petitioners' [sic] seek are of minutes in which (1) no attorney attended, (2) no attorney authored and (3) the final minutes

[4] *Lee v. Engle*, 1995 WL 761222, at *1 (Del. Ch. Dec. 15, 1995).
[5] Pet'rs' Op. Br. at 9.
[6] *Id.* at 10.

do not reflect a single conversation with counsel."[7] According to the Petitioners, "ISN is attempting to shield relevant non-privileged documents from discovery by funneling those documents through its counsel," but the facts contained in the draft documents at issue "do not become privileged merely by transmitting those facts to an attorney."[8]

On the other hand, the Respondent contends that draft board minutes are *per se* not discoverable, and that "documents sent to legal counsel for the purpose of facilitating the rendition of professional legal services are privileged,"[9] understanding this Court's decisions in *In re Quest Software Inc. Shareholders Litigation*[10] and *Jedwab v. MGM Grand Hotels, Inc.*[11] to foreclose the Petitioners' discovery requests for draft documents. Specifically, the Respondent suggests that a comparison of draft documents sent for legal review and their final counterparts may reveal the underlying legal advice that caused the Company to make certain edits to those documents.

In *Jedwab*, this Court denied a plaintiff's motion to compel the production of draft SEC disclosure documents, explaining that:

> Since plaintiff has available to it the publicly-filed [SEC disclosure] documents, it is apparent that the only information available from prior drafts relates to matters appearing in prior drafts that were

[7] Pet'rs' Reply Br. at 5.
[8] *Id.* at 7.
[9] Resp't's Opp'n Br. at 8-9.
[10] 2013 WL 3356034 (Del. Ch. Sept. 7, 2010).
[11] 1986 WL 3426 (Del. Ch. Mar. 20, 1986).

> deleted, augmented or otherwise modified in the final product. Even a superficial understanding of the process by which SEC filings are prepared by lawyers and other advisors of a client permits one to understand that such modifications are made as a result of communications between a client or its representatives and its lawyers.[12]

The Court found that the documents sought by plaintiffs were therefore privileged, noting:

> It might be argued that the inference of a privileged communication, as opposed to the communication itself, ought not to be enough to successfully invoke the privilege, and it is doubtlessly true that the simple fact that from a document one may infer a communication from a client to a lawyer *would not alone establish a basis to protect such a document from discovery*. However, at least where, as here, *the document itself is prepared by a lawyer in a setting in which it is intended to remain confidential* until a final version is deemed appropriate for public disclosure and where the only pertinence of the document to the discovery process is the inferential disclosure of the communication from a client to its lawyer, it strikes me that the underlying policies of the lawyer-client privilege are properly implicated and that discovery of such a document would inappropriately permit access by third parties to privileged communications.[13]

Though the Respondent contends that *Jedwab* is controlling here, I disagree. As made clear by the italicized language above, the Court in *Jedwab* was primarily focused on attorney participation in drafting the documents in dispute; where attorneys endeavored to make legal conclusions as to the appropriate inclusion or omission of certain facts, *their own work product* created in undertaking that task

[12] *Id.* at *3.
[13] *Id.* (emphasis added).

was protected by the attorney-client privilege. The Court acknowledged that in circumstances where, as here, drafts were not "prepared *by a lawyer* in a setting in which [they were] intended to remain confidential," the ability to infer an attorney-client communication "would not alone establish a basis to protect such a document from discovery."[14] I therefore find unpersuasive the Respondent's contention that, though the documents in dispute were not drafted by an attorney, management's decision to send those documents to legal counsel "for review" caused them to become privileged.

The Respondent also cites this Court's decision in *Quest* for the broad proposition that draft documents are not discoverable.[15] In *Quest*, plaintiffs sought production of draft minutes of special committee meetings "because the produced [final] minutes were unsigned, not final, and prepared in large tranches."[16] The Court denied the request based on *Lee v. Engle*'s application of the work-product doctrine,[17] which doctrine applies only "to materials an attorney assembled and brought into being in anticipation of litigation"[18] in protection of "the privacy of lawyers in their work . . . ."[19] Here, where attorneys did not draft the minutes or other documents requested by the Petitioners, nor did they gather the information

[14] *Id.* (emphasis added).
[15] Resp't's Opp'n Br. at 8.
[16] *In re Quest Software Inc. S'holders Litig.*, 2013 WL 3356034, at *5.
[17] *Id.*; *see also Lee*, 1995 WL 761222, at *6 (applying *Jedwab*, as "[t]here, the draft documents consist[ed] of both factual and opinion *work product*") (emphasis added).
[18] *Lee*, 1995 WL 761222, at *4.
[19] *Id.*

contained therein, the work-product doctrine does not shield such documents from production, and the Court's holding with respect to draft documents in *Quest* is inapposite.

Ultimately, as the Respondent has presented no persuasive basis to find that the draft documents, including draft minutes, sought by the Petitioners are privileged, I recommend the Court find that that they are not, and accordingly compel their production.

2. "At-Issue" Exception

The Petitioners also seek to compel the production of documents reflecting otherwise-privileged communications evidencing how the ISN board arrived at the merger price. Because the Respondent has indicated that its valuation expert may place some weight on the merger price in his expert report—in other words, that the Respondent may take the position at trial that the merger price is indicative of the fair value of ISN—the Petitioners contend that the Respondent has placed the merger price "at issue" such that the "at-issue" exception to a claim of privilege applies.

As this Court explained in *Quest*,

> The "at issue" exception to the attorney-client privilege exists where either "(1) a party injects the privileged communications themselves into the litigation, or (2) a party injects an issue into the litigation, the truthful resolution of which requires an examination of confidential communications." The exception "rests upon a fairness rationale" and recognizes that a party cannot use the attorney-client privilege as both

> a "shield" from discovery and a "sword" in litigation. A defendant may not refuse to produce privileged attorney-client communications only to rely subsequently on the substance of those communications to prove its case.[20]

The issue the Petitioners contend the Respondent has injected into this litigation is whether the merger price is indicative of the fair value of ISN; the documents requested are communications reflecting how the ISN board arrived at that merger price, as the Petitioners contend that access to the board's "contemporaneous communications" is necessary to fairly test the assertion that the merger price accurately reflects the fair value of ISN. I disagree, however, that confidential communications are necessary to fairly test that assertion. For one, both parties bear the burden at trial to establish the fair value of ISN,[21] and in meeting that burden, the Respondent's expert will be unable to rely on any information not produced to the Petitioners;[22] the "fairness rationale" noted above is therefore not implicated. Perhaps more importantly, the Petitioners have ready access to information sources necessary to test the assertion that the merger price is

[20] *In re Quest Software Inc. S'holders Litig*., 2013 WL 3356034, at *2 (citations omitted).
[21] *See Highfields Capital, Ltd. v. AXA Fin., Inc*., 939 A.2d 34, 42 (Del. Ch. 2007) ("Both parties 'have the burden of proving their respective valuation positions by a preponderance of the evidence.'") (citations omitted).
[22] *See, e.g.*, *Grunstein v. Silva*, 2012 WL 5868896, at *1 (Del. Ch. Nov. 20, 2012) ("'Delaware decisions involving the 'sword and shield' concept have precluded a party from shielding evidence from an opposing party and then relying on the evidence at trial to meet its burden of proof on an issue central to the resolution of the parties' dispute.'") (quoting *Air Prods. & Chems., Inc.*, 2011 WL 284989, at *3 (Del. Ch. Jan. 20, 2011)); *id.* ("Because Defendants' knowledge and understanding of these issues are based on the advice of counsel, the Court will not allow Defendants to use this evidence when Plaintiffs have been shielded from it.").

indicative of the fair value of ISN: namely, they may ask the ISN managers and directors at deposition what actions were taken to arrive at the merger price, and on that basis demonstrate that the merger was not the result of a market canvass and arm's length negotiation.[23] That possibility is not the Petitioners' *sole* source of information, but *supplements* the Respondent's production of non-privileged documents describing the steps taken by the ISN board in setting the merger price, including the January 9, 2013 board meeting minutes at which meeting the board approved the merger agreement;[24] the 2011 valuation opinion upon which the board based the merger price;[25] and an email circulated among management reflecting certain adjustments made to that valuation.[26] Because to "truthfully resolve" whether the merger price is indicative of fair value does not require the disclosure of confidential communications, I recommend the Court decline to compel production of the privileged documents Petitioners seek.

II. *Conclusion*

[23] *See Huff Fund Inv. P'ship v. CKx, Inc.*, 2013 WL 5878807, at *11 (Del. Ch. Nov. 1, 2013) ("I rely on the merger price as the best and most reliable indication of CKx's value. This Court has previously recognized that 'an arms-length merger price resulting from an effective market check is entitled to great weight in an appraisal.' Indeed, when this Court has evaluated claims that transactions between a corporation and its fiduciaries were not entirely fair, we have identified the paradigm of an *arms-length negotiation or public auction* as the standard against which an interested transaction should be compared.") (citations omitted) (emphasis added).
[24] Pet'rs' Op. Br. Ex. E.
[25] *Id.* Ex. G.
[26] *Id.* Ex. I. ISN has also produced handwritten notes summarizing adjustments made to the 2011 valuation. *See id.* Ex. H.

For the foregoing reasons, I recommend the Petitioners' Second Motion to Compel be granted in part and denied in part. I refer the parties to Court of Chancery Rule 144 for the process of taking exceptions to a Master's Final Report.

Sincerely,

/s/ Kim E. Ayvazian

Kim E. Ayvazian

Master in Chancery