Does *Trados* Matter?

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I. INTRODUCTION 102
II. *TRADOS* AND REACTIONS BY COMMENTATORS 104
A. The Court's Holding 104
B. The Court's Style 106
C. Reactions by Practitioners 108
D. Reactions by Legal Scholars 109
III. THE INTERVIEWEES 111
A. Location 111
B. Practice Focus & Exposure to Delaware Law 111
C. Number 115
IV. THE MODEST EFFECTS OF *TRADOS* 115
A. Familiarity with Trados 115
B. Ex Ante Contracts 116
1. Drag-Along Rights 117
2. NVCA Sale Right 119
C. Deal Process 120
1. Trados *Territory* 120
2. Independent Board or Shareholder Approval 122
3. Common-Continuation Value 123
4. Allocations to Common 124
5. The Beneficiary Question 125
V. IMPLICATIONS 128
A. What's Distinctive About Silicon Valley? 128
1. Muted Judicial Influence 128
2. Implications for Delaware Jurisprudence 131
B. Application to Trados 133
1. Tightening Trados *Triggers* 133
2. Fair Process Informed by Customary Process 135
a. Assessing Common-Continuation Value 135
b. Endorsing Allocations to Common? 137
VI. CONCLUSION 138

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I. INTRODUCTION

In 2013, the Delaware Chancery Court issued an opinion that reverberated loudly in Silicon Valley. In the case of *In re Trados Inc. Shareholder Litigation* ("*Trados*"),[1] the court scrutinized the action of a board of directors controlled by venture capital investors. Specifically, the court considered the board's decision to sell Trados Incorporated (the "company" or "Trados") for an amount that, in accordance with customary Silicon Valley stock terms, resulted in payouts to venture capital funds holding preferred stock but no payouts to common shareholders. After a lengthy trial, the court ultimately found that the transaction was fair to the common shareholders because of the company's limited prospects.[2] Yet the case was notable for the court's sharp critique of the board for failing to more vigilantly serve common shareholders.[3]

The case inspired a wave of law firm memos and client alerts speculating about effects on venture capital financing terms.[4] Leading law firms, acting through the National Venture Capital Association's legal forms group, developed an elaborate contractual "sale right" intended to contract around the case's holding.[5]

Legal scholars also took note of the case.[6] In particular, they focused on language in the opinion adopting a rule of "common maximization."[7] Under this approach to conflicts between common and preferred shareholders, a board has a paramount duty to pursue value for the common holders even when preferred holders have negotiated for control of the board.[8]

In this Article, I check back in on *Trados* by asking lawyers whether the case affects

1. There have been two opinions issued in the *Trados* litigation. The first related to a motion to dismiss. *See In re* Trados Inc. S'holder Litig., No. 1512-CC, 2009 WL 2225958 (Del. Ch. July 24, 2009). The other was a trial court opinion. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17 (Del. Ch. 2013). Unless specified otherwise, I use "*Trados*" to refer to the trial court opinion.

2. *See In re Trados*, 73 A.3d at 78 ("[T]he directors breached no duty to the common stock by agreeing to a Merger in which the common stock received nothing. The common stock had no economic value before the Merger, and the common stockholders received in the Merger the substantial equivalent in value of what they had before.").

3. *See id.* at 45 ("[P]laintiff proved at trial that six of the seven Trados directors were not disinterested and independent, making entire fairness the operative standard. This finding does not mean that the six directors necessarily breached their fiduciary duties, only that entire fairness is the lens through which the court evaluates their actions.").

4. *See infra* Part II (describing law firm memos discussing *Trados*).

5. *See* NAT'L VENTURE CAPITAL ASS'N, NVCA MODEL VOTING AGREEMENT n.53 (2018) [hereinafter, NVCA VOTING AGMT.] (referencing *Trados*).

6. *See* Robert P. Bartlett III, *Shareholder Wealth Maximization as Means to an End*, 38 SEATTLE U. L. REV. 255, 290–95 (2015) (criticizing the court's reasoning for failing to recognize the board as a venue for bargaining over the company's future); William W. Bratton & Michael L. Wachter, *A Theory of Preferred Stock*, 161 U. PA. L. REV. 1815, 1874–900 (2013) (discussing *Trados* in articulating an over-arching "theory of preferred stock"); Charles R. Korsmo, *Venture Capital and Preferred Stock*, 78 BROOK. L. REV. 1163, 1165, 1185–89 (2013) (discussing *Trados* as a basis for "reassess[ing] the law's treatment of preferred stock in the venture capital context"); Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. (forthcoming, 2019) at 30–32, 54–57 (discussing *Trados*); Simone M. Sepe, *Intruders in the Boardroom: The Case of Constituency Directors*, 91 WASH. U. L. REV. 309, 320 & n.12 (2013) (discussing *Trados* in an economic analysis of constituency directors); Leo E. Strine, Jr., *Poor, Pitiful, or Potently Powerful Preferred*, 161 U. PA. L. REV. 2025, 2039 (2013) (discussing *Trados* in a response to Bratton and Wachter).

7. *See infra* Part II.A (describing the rule of common maximization and its theoretical alternatives).

8. *See id.*

how they document venture capital financings or advise boards on exit transactions. This Article relies on original interviews with 20 lawyers, most of whom work for leading Silicon Valley firms.[9] These lawyers are predominantly "startup lawyers"—a distinct segment of the legal industry that guides high-risk startups through formation, financing, and eventual exit.[10]

I observe that *Trados* has a modest but noticeable effect on their advice to clients. Interviewees report that a mix of Silicon Valley norms and practical impediments thwart efforts to contract around *Trados* at the time a venture capital fund initially invests.[11] But interviewees report that *Trados* does affect the process of selling a startup. Most noticeably, boards are more systematic in assessing the value of continuing as a company.[12] At the margins, *Trados* may even result in special allocations to common shareholders (payments to common shareholders in excess of their base entitlement).[13] Though this customary practice appears relatively consistent across interviewees, the consensus does not necessarily extend to more conceptual matters. The interviewees do not agree on whether *Trados* announced a new rule, and they do not converge on a single articulation of the applicable fiduciary standard.[14]

Beyond capturing customary practice around *Trados,* the interviews provide a rare glimpse of the counseling moment when judicial pronouncements are transmitted to corporate managers. This presents an opportunity to examine the reach of Delaware courts as they seek to regulate the innovation economy from afar. After all, as Edward Rock stated in his influential depiction of Delaware jurisprudence, "what the business lawyer tells the client–rather than what the judge announces to the world–is the 'law.'"[15] Yet, there has been very little systematic study of how corporate lawyers actually translate judicial pronouncements into client advice.[16]

On this broader conceptual point, the interviewees describe a distinct business environment where Delaware law has muted effects. Due to a combination of resource restraints, litigation economics, and market realities, startups do not prioritize adherence to corporate caselaw.[17] In this environment, judicial broadcasts of corporate law principles might have less influence than they have with publicly traded companies.[18]

I argue that this weaker "signal strength" should influence the court's judicial form. Though ambiguity may serve a recognized function in Delaware jurisprudence, a fuzzy doctrine of judicial intervention has an especially high cost in a context where boards are

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9. *See infra* Part III (describing the practice environment of the interviewees).

10. For an overview of the tasks performed by startup lawyers, see generally Abraham J.B. Cable, *Startup Lawyers at the Outskirts*, 50 WILLAMETTE L. REV. 163 (2014). *See also* John F. Coyle & Joseph M. Green, *Startup Lawyering 2.0*, 95 N.C. L. REV. 1403 (2016-17). *See also infra* Part III (describing the practice focus of the interviewees).

11. *See infra* Part IV.B (considering whether *Trados* has affected drag-along rights or resulted in adoption of the NVCA sale right).

12. *See infra* Part IV.C.3.

13. *See infra* Part IV.C.4.

14. *See infra* Part IV.C.5.

15. Edward Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1096 (1997).

16. *See id.* at 1106 ("The mechanism by which Delaware opinions influence conduct is ultimately an empirical question, the full description of which awaits further research.").

17. *See infra* Part V.A.1.

18. *See id*.

unable or unlikely to engage in procedural cleansing through independent board committees or disinterested shareholder votes.[19] In this setting, I recommend that Delaware courts both clarify triggers for fairness review and strive to define right-sized standards of conduct informed by existing customary practice.

This Article proceeds in four parts. Part II provides an overview of *Trados* and reactions by practitioners and legal scholars. Part III describes the interviewees and their practice environment. Part IV describes the customary practice following *Trados,* including enhanced board process and additional payments to common holders attributable in part to the case. Part V identifies doctrinal and theoretical implications of the observations.

II. *TRADOS* AND REACTIONS BY COMMENTATORS

The *Trados* litigation has been in the spotlight since the court issued an initial opinion in connection with a motion to dismiss in 2009.[20] The litigation remained prominent as the case went all the way to trial, resulting in a voluminous second opinion in 2013 that elaborated on the court's earlier decision.[21] This Part summarizes key aspects of the 2013 opinion and reactions by practitioners and legal scholars.

A. The Court's Holding

In *Trados*, the court confronted at least three key questions: (1) does the *Trados* fact pattern amount to a cognizable conflict of interest for directors affiliated with preferred shareholders, (2) if so, what fiduciary standard applies to the conflicted directors, and (3) was the transaction at issue fair to the common shareholders?

First, the court held that board members affiliated with venture capital investors were conflicted when approving a merger resulting in payment of a liquidation preference to venture capital funds holding preferred stock.[22] Although the conflict may at first appear obvious based on the disparate payouts to common and preferred holders, the liquidation preference had been negotiated between the venture capital funds and an independent board. Once an insider strikes a fair bargain with an independent board, courts will not necessarily scrutinize the performance of that agreement.[23] Accordingly, the court's analysis of the conflict hinged on the *timing* of the sale.[24] Drawing an analogy to long-recognized conflicts between debt (creditors) and equity (shareholders),[25] the court noted that a liquidation preference creates incentives to act conservatively and to prematurely

19. *See infra* Part V.A.2 (explaining circumstances that frustrate procedural cleansing).

20. *See In re* Trados Inc. S'holder Litig., No. 1512-CC, 2009 WL 2225958 (Del. Ch. July 24, 2009) (denying the defendants' motion to dismiss).

21. *See supra* note 1 (describing the 2009 and 2013 opinions).

22. A liquidation preference is an attribute of preferred stock that entitles the holder to be repaid its investment in connection with a merger or other sale transaction. When a startup is sold, a preferred holder can elect to receive its liquidation preference or instead convert into common stock. When a company is sold for an amount below the liquidation preference, the preferred holders will elect to receive the preference and the common holders will not receive a payout. *See* Abraham J.B. Cable, *Opportunity-Cost Conflicts in Corporate Law*, 66 CASE W. RES. L. REV. 51, 63–64 (2015) (explaining the operation of a liquidation preference).

23. *See id.* at 67 (citing DEL. GEN. CORP. L. § 144 regarding conflict-of-interest transactions).

24. *See id.* at 68 (describing the plaintiffs' claims in *Trados*).

25. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17, 49 (Del. Ch. 2013) (describing the preferred stock as "debt-like").

accept acquisition proposals in circumstances where common shareholders might prefer a more risky strategy of continuing as a standalone company.[26] In these circumstances, common shareholders have nothing to lose and at least a remote chance of gaining by continuing. Preferred shareholders, in contrast, bear real risk in continuing because doing so jeopardizes their liquidation preference.[27]

Having determined that the venture capital designees were conflicted, the court then imputed that conflict to the board's facially independent directors based on the "web of interrelationships that characterizes the Silicon Valley startup community" and a resulting "owingness" to the venture capital investors.[28] The court also found that other directors holding management positions at Trados were conflicted based on a management incentive plan providing for cash bonuses in connection with the sale.[29]

After concluding its conflict analysis, the court then addressed the thorny question of to whom fiduciary duties are owed when the interests of common and preferred shareholders conflict. On this point (the "beneficiary question"), prior precedent and commentary proposed at least three competing theories.

- Under the rule of *common maximization*, a board owes its primary duty to common shareholders when the interests of preferred shareholders and common shareholders come into conflict.[30] The board's duty is to maximize the value to common shareholders as residual claimants—in other words, to pursue all plausible value of continuing as a standalone company rather than accepting a sale price at or around preferred stock liquidating preferences.
- Under the rule of *enterprise maximization*, a board's duty is to maximize the value of the entity, regardless of how proceeds will be distributed among shareholders pursuant to stock terms.[31]
- Under the *control-contingent* approach, the fact that common holders ceded board control to preferred holders should be taken into account in evaluating fiduciary duty claims. Under this approach, a preferred-controlled board could favor the interests of preferred holders.[32]

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26. *See id.* ("The different cash flow rights of preferred stockholders are particularly likely to affect the choice between (i) selling or dissolving the company and (ii) maintaining the company as an independent private business.").

27. For alternative (narrower) readings of the case, see *infra* Part IV.C.1.

28. *In re Trados*, 73 A.3d at 54–55.

29. *See id.* at 54. A management incentive plan (MIP) is a form of executive bonus plan with payouts conditioned on selling the company at or above a specified price. An MIP incentivizes an executive to seek a sale transaction that the executive would otherwise resist because it will result in the executive losing his or her job. *See id.* at 58 ("VC-backed portfolio companies commonly adopt plans similar to the MIP to incent management to favor exits.").

30. *See* Strine, *supra* note 6, at 2028 ("[T]he law suggests that when push comes to shove, the board has a duty to prefer the common's interests, as pure equity holders, over any desire of the preferred for better treatment based on some generalized expectancy that they will receive special treatment beyond their contractual rights.").

31. *See* Bratton & Wachter, *supra* note 6, at 1885–86 (describing enterprise maximization); Douglas G. Baird & M. Todd Henderson, *Other People's Money*, 60 STAN L. REV. 1309, 1323–28 (2008) (discussing enterprise maximization and relevant caselaw).

32. Jesse Fried and Mira Ganor have argued for the control-contingent approach. They describe it as follows:

> A common-controlled board is free to serve the interests of common shareholders at the expense of the preferred shareholders and aggregate shareholder value. In contrast, a preferred-controlled board can make business decisions that serve the preferred at the expense of common, as long as those

The *Trados* court specifically referred to each competing theory[33] and ultimately endorsed common maximization: "[G]enerally it will be the duty of the board, where discretionary judgment is to be exercised, to prefer the interests of the common stock—as the good faith judgment of the board sees them to be—to the interests created by the special rights, preferences, etc. . . . of preferred stock."[34]

Having determined that the board was conflicted and that it owed its primary duty to the common shareholders, the court then analyzed whether the transaction was "fair" to the common shareholders. In applying this fairness standard—Delaware fiduciary law's most stringent[35]—the court sharply rebuked the board's process and its failure to specifically consider the effects of a sale on common holders.[36] The court, however, was persuaded by the defendants' valuation expert that the company in fact had no substantial prospects for a turnaround, so zero was a fair price for the common stock.[37] In short, the court was critical of the board's conduct but ruled in favor of the board because of the company's poor prospects.

B. The Court's Style

In considering how lawyers translate *Trados* into client advice, it is helpful to go beyond *what* the court held and to consider *how* the court delivered the message.

One conspicuous feature of the opinion is its thick factual narrative. Tallying over 60 pages, the opinion includes a detailed description of the company's underlying business and key inflection points in its 20-year operating history, such as acquisitions of other companies,[38] management changes,[39] financing transactions,[40] product development milestones,[41] and the sale process at the center of the case.[42] It appears that eight years of litigation provided the court with a trove of background facts to set the stage for its analysis.

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decisions can be defended as in the best interests of the corporation.

Jesse M. Fried & Mira Ganor, *Agency Costs of Venture Capitalist Control in Startups*, 81 N.Y.U. L. REV. 967, 993 (2006). Note that Fried and Ganor's formulation of the control-contingent approach included an overriding obligation that all directors act "in the best interests of the corporation." When the *Trados* court summarized the control-contingent approach, it omitted this constraint on director conduct. *See In re Trados*, 73 A.3d at 38–40. The court's more aggressive formulation echoes the sentiments of commentators who have argued for elimination of fiduciary restraints in connection with preferred-common conflicts. *See* Baird & Henderson, *supra* note 31, at 1329–33 (describing a "contractarian solution" to preferred-common conflicts).

33. The court described the control-contingent approach as follows: "[A] board elected by the common stock owes duties to the common stock holders but not the preferred stock, but a board elected by the preferred stock can promote the interests of the preferred stock at the expense of common stock." *In re Trados*, 73 A.3d at 17 n.16 (citing Fried & Ganor, *supra* note 32). The court described enterprise maximization as follows: "[D]irectors should have a duty to maximize enterprise value, defined in the common-preferred context as the aggregate value of the returns to the common stock plus the preferred stock, taking into account the preferred stock's contractual rights." *In re Trados*, 73 A.3d at 17 n.16 (citing Bratton & Wachter, *supra* note 6; Baird & Henderson, *supra* note 31).

34. *In re Trados*, 73 A.3d at 40–41.

35. *See id.* at 55 (describing fairness review).

36. *See infra* text accompanying notes 51–53.

37. *See supra* text accompanying note 2.

38. *See In re Trados*, 73 A.3d at 23.

39. *See id.* at 25–27.

40. *See id.* at 21–25.

41. *See id.* at 24.

42. *See id.* at 28–34.

Equally notable is the court's attention to the distinctive context of Silicon Valley. Scholars from a range of disciplines have studied the region—as a specialized financial market,[43] an economic cluster,[44] a labor market,[45] and a social phenomenon.[46] Similarly, the *Trados* court drew heavily from academic literature. The court explained that venture capital investors are at odds with founders and other common holders because "[t]he cash flow rights of typical VC preferred stock cause the economic incentives of its holders to diverge from those of the common stockholders"[47] and "[t]he VC business model reinforces the economic incentives that the preferred stock's cash flow rights create."[48] The court looked to academic literature in concluding that facially independent directors are beholden to venture capital investors because of "the web of interrelationships that characterizes the Silicon Valley startup community."[49] Repeatedly, the court took judicial notice of Silicon Valley's exceptionalism, or at least signaled that fiduciary principles might operate differently in this context.[50]

Finally, the court's condemning tone makes an impression. The court was particularly critical of the process the Trados board followed in approving the sale. By failing to specifically consider the effects of the transaction on common stockholders, the board "did not understand . . . their job."[51] Worse yet, their experience and sophistication meant they "fully appreciated the diverging interests" of the common and preferred, yet they "refused to recognize the conflicts they faced."[52] Their testimony at trial was no more than a "vigorous and coordinated effort" to "recharacterize their actions retrospectively" and "show that they somehow blundered unconsciously into procedural fairness."[53] With all of this finger wagging, the court's ultimate holding in favor of the defendants feels like a surprise ending.[54]

Overall, *Trados* is an example of what Edward Rock identifies as the Delaware court's "normative/narrative" style. While there may be a temptation to reduce caselaw to

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43. *See, e.g.*, PAUL GOMPERS & JOSH LERNER, THE VENTURE CAPITAL CYCLE (2d ed. 2006) (providing economic analysis of venture capital).

44. *See, e.g.*, Michael E. Porter, *Clusters and the New Economics of Competition*, 76 HARV. BUS. REV. (Nov.–Dec. 1998) (identifying Silicon Valley as "one of the world's best-known clusters" of economic activity).

45. *See, e.g.*, Ronald J. Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants Not to Compete*, 74 N.Y.U. L. REV. 575, 587–92 (discussing the work of AnnaLee Saxenian).

46. *See, e.g.*, Mark C. Suchman & Mia L. Cahill, *The Hired Gun as Facilitator: Lawyers and the Suppression of Business Disputes in Silicon Valley*, 21 L. & SOC. INQ. 679 (1996) (discussing Silicon Valley from a sociological perspective).

47. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17, 49 (Del. Ch. 2013) (citing Bratton & Wachter, *supra* note 6, at 1832).

48. *See id.* at 50 (citing D. Gordon Smith, *The Exit Structure of Venture Capital*, 53 UCLA L. REV. 315, 316, 345 (2005)).

49. *See id.* at 54 (citing Fried & Ganor, *supra* note 32, at 988).

50. For other recent Delaware decisions acknowledging a distinctive business environment in Silicon Valley, see Frederick Hsu Living Tr. v. ODN Holding Corp., No. 12108-VCL, 2017 WL 1437308, at *5, *28 (Del. Ch. Apr. 14, 2017) (referring to the "highly networked Silicon Valley community" and discussing the incentives of venture capital investing); Sandys v. Pincus, 152 A.3d 124, *passim* (Del. 2016) (discussing relationships among venture capitalists and entrepreneurs in assessing a board member's independence).

51. *In re Trados*, 73 A.3d at 62.

52. *Id.* at 62.

53. *Id.* at 56.

54. *See supra* Part II.A (discussing the court's holding that the transaction was ultimately fair to the common holders because of the company's limited turnaround potential).

"algorithms"—rules that spit out concrete and consistent results—Delaware courts take a different approach.[55] They instead announce open-ended principles coupled with fact intensive analysis and sharp critiques of specific conduct.[56] The opinion has all of the hallmarks of the genre: announcement of broad principles,[57] thick factual description, and sharp rebukes for perceived procedural failures despite a holding in favor of the defendants.

C. Reactions by Practitioners

Starting with the court's 2009 opinion, *Trados* caught the attention of lawyers and law firms. A number of blog entries and law firm memos (together, the "practitioner materials") pondered the effects of the case.[58]

The practitioner materials generally described the case as a hollow victory for the defendants. They noted that the court's application of the rigorous fairness standard resulted in years of litigation and scrutiny, regardless of the outcome.[59]

The practitioner materials focused largely on ways to prevent litigation in the *Trados* fact pattern. Some of these commentaries focused on potential changes to customary venture capital financings—in other words, ex ante contracts. For example, practitioners considered whether the "drag-along rights" already included in most venture capital financings might be altered or adapted to give venture capital investors the ability to cause a sale of the company free from judicial scrutiny.[60] The practitioner materials also focused on how board deliberations and sale process could be enhanced to avoid, or stand up to,

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55. *See* Rock, *supra* note 15, at 1014 ("There is a persistent tendency to acknowledge that Delaware corporate law largely involves standards, but then to try to reduce it to a set of rules."). Rock describes the tendency to articulate rules as one that "naturally emerges from teaching Corporations and trying to help students synthesize cases into useful principles or algorithms." *Id.*

56. *See id.* at 1015–16 (describing the normative-narrative approach); *see also* William T. Allen, *Ambiguity in Corporate Law*, 22 DEL. J. CORP. L. 894, 900 (1997) (discussing his opinions as consisting of a "grand principle" combined with a "highly specific" application that is hard to generalize to a rule); Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061, 1075–81 (2000) (describing Delaware fiduciary law as consisting of "indeterminate" standards applied in "a fact and case specific manner").

57. In particular, the court described the applicable standard of conduct through the famously murky concept of "good faith." *See In re* Trados Inc. S'holders Litig., 73 A.3d 17, 40–41 (Del. Ch. 2013) ("[T]he standard of conduct for directors requires that they strive in good faith and on an informed basis to maximize the value of the corporation for the benefit of its residual claimants . . . .").

58. *See, e.g.*, *Venture Capital Investing: Can the Liquidation Preference of Preferred Stock Over the Common Stock Be Protected Where the Common Stock Receives Little or Nothing in an Exit?*, LATHAM & WATKINS: CLIENT ALERT (Oct. 21, 2010), https://www.lw.com/thoughtLeadership/protecting-the-liquidation-preference-in-venture-capital-investing (discussing the effects of the *Trados* case).

59. *See, e.g.*, David J. Berger, *Delaware Court of Chancery Upholds* Trados *Transaction as Entirely Fair*, HARV. L. SCH. F. ON CORP. GOVERNANCE AND FIN. REG. (Sept. 3, 2013), https://corpgov.law.harvard.edu/2013/09/03/delaware-court-of-chancery-upholds-trados-transaction-as-entirely-fair/ ("Although the Trados directors were ultimately found not liable, the transaction was the subject of years of litigation—a nearly inevitable result once a court finds that a majority of the board is conflicted and therefore applies the entire fairness standard.").

60. *See, e.g.*, Michael Kendall & C. Stephen Bigler, *The Illusory Preference*, THE DAILY DEAL (Feb. 22, 2010), https://www.goodwinlaw.com/~/media/Files/Publications/Attorney%20Articles/2010/Kendall_TheDaily Deal_2_22_2010.pdf ("Investors who can negotiate for the right to trigger the drag-along by themselves without the requirement of a board vote may avoid the fiduciary issues raised by the Trados case entirely."). Drag-along rights permit one group of shareholders to force another group of shareholders to cooperate with a sale of the company. I describe these rights, and proposed changes in response to *Trados*, in Part IV.B.1 below.

judicial review. Recommendations included increased use of valuation experts, independent board committees, and disinterested shareholder approval.[61]

Perhaps the clearest indication of practitioner interest in *Trados* was an alteration to the model legal forms produced by the National Venture Capital Association (NVCA). The NVCA is a trade group formed by venture capital funds.[62] One of the more prominent NVCA initiatives is the promulgation of model legal forms for venture capital financings. Leading Silicon Valley firms collaborate to provide these comprehensive, annotated legal documents at no charge on the NVCA website.[63] Although firms still maintain proprietary forms, the NVCA's model legal documents can be an important reference point for establishing what is customary or "market" within Silicon Valley.[64]

In explicit response to *Trados*, the NVCA legal forms group added a new variation to the forms—a "sale right."[65] Under the terms of this sale right, venture capital investors would have (1) a shareholder-level right to put the company up for sale and (2) a right to require the company to redeem the preferred stock at any resulting offer price.[66] The intended effect of the provision was to give investors a right to sell the company without the board leading the charge, thereby avoiding the board-level conflicts at issue in *Trados.* As discussed below, the sale right has not been widely adopted,[67] but its existence evidences the prominence of *Trados* in the Silicon Valley community.

D. Reactions by Legal Scholars

Legal scholars also showed a strong interest in *Trados*. In particular, they focused on the court's endorsement of common maximization. An insightful exchange between then-Chancellor Leo Strine, on one side, and Professors Bratton and Wachter, on the other side, is representative.

Bratton and Wachter criticized *Trados* for imposing on the board a dictate of common maximization. First, they noted the logical implications of the standard. Common shareholders in a failing company will *always* prefer to gamble on continuing, no matter how speculative and destructive of remaining company value, when the sale price falls below preferred stock liquidation preferences.[68] In that situation, common shareholders might be viewed as playing with house money (or more accurately, preferred holders' money). They argued that forcing the board to align with these incentives ignored the "broader transactional context" of an "ex ante bargain" by which the company "gave up

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61. *See, e.g.*, Douglas N. Cogan et al., *Corporate and Securities Alert: In re* Trados - *Important Lessons for Directors on Fiduciary Duties to Common Stockholders*, FENWICK & WEST (Sept. 18, 2013) (suggesting use of independent board committees, disinterest shareholder votes, or alternative entities such as LLCs).

62. *Who We Are*, NAT'L VENTURE CAP. ASS'N, https://nvca.org/about-us/ (last visited Feb. 1, 2019) (describing the NVCA as "[s]erving the venture community as the preeminent trade association").

63. *See* NVCA VOTING AGMT., *supra* note 5, at n.51.

64. *See infra* Part III.B (reporting that interviewees rely on NVCA forms as an important benchmark for negotiations).

65. *See supra* text accompanying note 5.

66. *See* Bratton & Wachter, *supra* note 6, at 1892 (describing the NVCA sale right).

67. *See infra* Part IV.B.2 (describing the NVCA sale right).

68. Bratton & Wachter, *supra* note 6, at 1889 ("Under a common stock-maximization norm, any result that wipes out the common is vulnerable to a 'might have waited' complaint."). *See also* Cable, *supra* note 22, at 89 (arguing that a strong version of common-maximization "requir[es] a preferred-controlled board to pursue extreme long-shot opportunities on behalf of the common").

the option to delay" in exchange for capital.[69] By imposing a standard at odds with these expectations, common shareholders could "disrupt the *ex ante* bargain in search of holdup value."[70]

Worse yet, according to Bratton and Wachter, doctrinal and practical impediments prevent venture capital investors from developing contractual workarounds.[71] For example, Bratton and Wachter considered the NVCA sale right, which they described as "convoluted and clever" but incapable of practically solving "the *Trados* problem."[72] Among other problems, they noted, Delaware caselaw may give a company significant leeway in delaying payment of a redemption right.[73]

Strine, in stark contrast, defended *Trados* and its endorsement of common maximization. First, Strine suggested, without elaboration, that the rule of common maximization had theoretical limits that curbed the extreme logical implications suggested by Bratton and Wachter. According to Strine, Bratton and Wachter presented a caricature of common maximization: "[T]hey cite no decisions in which any court has ever required preferred stockholders in control to engage in casino-like gambling and to pursue strategies without a bona fide potential for success that would leave creditors at unfair risk."[74]

Strine then took exception to Bratton and Wachter's reading of the implicit bargain underlying venture capital contracts and described a very different understanding of the parties:

> [Venture-capital investors] are not the only ones who take risks. Many early-stage companies have common stockholders who have made company-specific investments just as real as those made by the preferred, although not always in purely monetary ways. Employees work "on the come," and even some suppliers do. And some investors buy common stock. Many of these equity holders accept risk on the promise that the company is going to do what it says and try to take a risky technology or service idea and turn it into a viable profit generator.[75]

Besides reading the implicit bargain differently than Bratton and Wachter, Strine took a substantially different view of preferred stockholders' ability to contract around the case. He pointed to typical features of preferred stock, such as protective provisions and liquidation preferences, as an indication of preferred stockholders' bargaining capabilities.[76] He also suggested that investors could use entirely different instruments—such as high-yield debt coupled with warrants—to escape the shareholder paradigm in favor of a position as creditors.[77] In sum, he expressed "reasons to doubt that preferred

69. *Id.* at 1893–94.

70. *Id.*

71. Bratton and Wachter also discussed the shortcomings of drag-along rights, which may require common shareholders to cooperate with a sale favored by preferred shareholders. They noted that the typical drag-along provision still requires board support for any sale of the company because the Delaware statute compels board involvement in mergers. *Id.* at 1891. Those issues are discussed in detail below. *See infra* Part IV.B.1 (discussing proposed modifications of drag-along rights).

72. Bratton & Wachter, *supra* note 6, at 1893–94 (discussing Delaware caselaw that limits a board's authority to pay dividends even when the company is contractually committed to doing so).

73. *Id.*

74. Strine, *supra* note 6, at 2038.

75. *Id.* at 2037.

76. *Id.* at 2029, 2036–37.

77. *Id.* at 2036–37.

stockholders lack sufficient market clout to protect their interests at the negotiating table."[78]

III. The Interviewees

This Article considers *Trados* through semi-structured interviews with practicing lawyers.[79] This Part briefly describes the interviewees and their practice environment.

A. Location

With one exception, the interviewees practice in Silicon Valley or other Bay Area locations.[80] Despite the emergence of entrepreneurial hubs in other parts of the country, Silicon Valley remains the epicenter of venture capital activity.[81]

B. Practice Focus & Exposure to Delaware Law

In selecting interviewees,[82] I sought out "startup lawyers" who form emerging companies, negotiate and document venture capital investments, and advise boards in connection with exit transactions.[83] In describing their practice, the interviewees use terms such as "general corporate lawyer" or "general counsel."[84] It would be inaccurate, however, to describe these lawyers as generalists in any broad sense. Instead, they specialize in guiding startups through particular stages of development (generally before the company has an initial public offering of stock) in a particular business environment (the startup and venture capital "ecosystem").[85] In other words, these lawyers focus on

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78. *Id.* at 2029 (noting that preferred holders do bargain for liquidation preferences and protective provisions and stating that preferred could obtain a redemption right or invest in high-yield debt).

79. Interviews were conducted pursuant to an interview guide listing the following topics: method of keeping informed about legal developments, the frequency with which legal developments affect advice to clients, familiarity with *Trados*, the case's impact on venture capital financing terms, and the case's impact on advice to boards.

80. One interviewee practices outside of California, but within a firm that has a substantial Silicon Valley office.

81. NAT'L VENTURE CAPITAL ASS'N, NVCA YEARBOOK 2017 15, 23 [hereinafter, NVCA YEARBOOK], https://nvca.org/nvca-2017-yearbook-go-resource-venture-ecosystem/ (reporting that in 2016 over half of assets under management in the venture capital industry were attributable to California-headquartered funds and that over half of venture capital investments were made in California-headquartered startups).

82. I located initial interviewees through personal and professional contacts and then asked for referrals to other potential interviewees (i.e., a "snowball sampling" technique).

83. *See supra* note 10 (listing sources discussing the role of startup lawyers). Two of the interviewees self-identify as mergers and acquisitions lawyers, meaning they represent startups primarily in sale transactions and not in venture capital financings. *See* Interview with Lawyer #3, at 1; Interview with Lawyer #18, at 1.

84. *See* Interview with Lawyer #7, at 1 (referring to "traditional" and "general" corporate lawyers in contrast to specialists); Interview with Lawyer #11, at 1 (explaining that the interviewee acts as general counsel for early-stage companies); Interview with Lawyer #14, at 1 (describing his role as being a virtual general counsel); Interview with Lawyer #16, at 1 ("I'm a generalist."); Interview with Lawyer #17, at 1 (describing the interviewee's role as "outsourced general counsel").

85. *See* Interview with Lawyer #10, at 1 (describing the interviewee's typical client as "two people and an idea" with a "skill set that tapers off" when the company becomes publicly traded); Interview with Lawyer #11, at 1 (explaining that the interviewee represents companies from early stages to exit); Interview with Lawyer #17, at 1 (stating that the interviewee always represents startups). Some interviewees claimed further specialization within a particular industry focus. *See, e.g.*, Interview with Lawyer #1, at 1 (claiming expertise in the "life sciences industry vertical"). The interviewees are not unanimous in reporting that they focus on privately held companies.

matters commonly encountered by startups in Silicon Valley.

Startup lawyers are not the only kinds of lawyers who might have something to say about *Trados*. The interviewees interact with lawyers in their firms' mergers and acquisitions practice groups ("M&A lawyers")[86] and with lawyers practicing out of Delaware offices ("Delaware counsel").[87]

In fact, one of my more surprising observations was the extent to which the interviewees, despite being familiar with *Trados,* sometimes disclaim deep expertise in corporate caselaw. Though the interviewees mostly form and represent Delaware (as opposed to California) corporations,[88] they view their job as "issue spotting" and may leave finer points of Delaware caselaw to other specialists.[89] As one interviewee puts it, startup lawyers do not spend time "in front of the judiciary."[90]

According to interviewees with long practice experience, there is a trend in Silicon Valley towards increasing specialization. These interviewees report that "lifecycle representation" of a startup once extended to advising fully mature companies on a broad range of topics relating to corporate governance and federal securities laws. But increasingly startup lawyers have given way to an array of specialists in capital markets, federal securities law compliance, executive compensation, Delaware law, and mergers and acquisitions.[91] According to one interviewee, early models of startup lawyering

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See Interview with Lawyer #1, at 1 (indicating that the lawyer represents clients for "the full lifecycle of the client"); Interview with Lawyer #5, at 1 (describing his practice as being relationship based and spanning the life of the company); Interview with Lawyer #15, at 1 (indicating that the interviewee handles substantial public company governance); Interview with Lawyer #14, at 1 (describing typical clients as two people in a garage through the "entire lifecycle"); Interview with Lawyer #19, at 1 (describing representation of startups through the entire lifecycle, including as public companies). But several interviewees note a trend towards deferring to other specialists once a company achieves public company status. *See infra* text accompanying notes 91–92.

86. *See* Interview with Lawyer #7, at 1 (referencing M&A lawyers and Delaware counsel); Interview with Lawyer #11, at 1 (stating that the firm has a "pure M&A group" in addition to the emerging business group); Interview with Lawyer #14, at 1 (describing specialists in venture capital, corporate governance, and M&A); Interview with Lawyer #16, at 1 (discussing the firm's M&A and corporate governance specialists); Interview with Lawyer #18, at 1 (discussing the firm's M&A practice group).

87. *See infra* Part III.B (discussing the interviewees' interactions with Delaware counsel).

88. *See* Interview with Lawyer #1, at 2 (reporting that "most of our clients are Delaware incorporated"); Interview with Lawyer #10, at 1 (estimating that 99% of clients are Delaware corporations and 1% are Delaware LLCs or California corporations formed as such "by accident"); Interview with Lawyer #13, at 1 (reporting being familiar with Delaware corporate law more than California corporate law); Interview with Lawyer #16, at 1 (reporting that most clients are incorporated in Delaware); Interview with Lawyer #17, at 3 (describing the interviewee's expertise as California law and Delaware corporate law).

89. *See* Interview with Lawyer #7, at 1 (stating that M&A specialists follow Delaware cases, while startup lawyers "rely on summaries" and "issue spot"); Interview with Lawyer #9 (reporting that corporate lawyers are not as informed about Delaware caselaw as Delaware specialists); Interview with Lawyer #17, at 3 (suggesting that I should speak to an M&A specialist because they would be more familiar with *Trados*). *But see* Interview with Lawyer #14, at 1 ("I can handle 93% of Delaware questions.").

90. Interview with Lawyer #2, at 1.

91. *See* Interview with Lawyer #5, at 1 (describing a decline in "relationship based" representation of a company through all lifecycle stages); Interview with Lawyer #16, at 1 (reporting that when the interviewee graduated from law school "everyone wanted to be a generalist" but that the practice became more specialized); Interview with Lawyer #17, at 3 (explaining that the interviewee initially handled a larger variety of matters, including IPOs and public company work, but that legal reforms in the early 2000s made it more difficult to continue with public company work); Interview with Lawyer #19, at 1 (observing a push to specialize but "resist[ing]" the trend based on the belief that well-rounded lawyers provide better client service and a more fulfilling career).

envisioned lawyers working on a venture capital financing in the morning and a registration statement for a public offering in the afternoon, but increasing specialization at large firms means "that model is not followed anymore."[92]

This hyper-specialization raises the question of whether startup lawyers are the right lawyers to ask about *Trados*'s effects. If M&A lawyers and Delaware counsel are the true connoisseurs of Delaware case law, perhaps they are the best observers. For a number of reasons, I determined that startup lawyers were the most relevant practitioners for this study.

First, the interviewees explain that they maintain primary responsibility for most merger transactions.[93] Although M&A specialists or Delaware counsel might be available for particularly large or complex transactions, *Trados* is highly relevant to the type of modest or small exit that startup lawyers continue to primarily handle.

Second, startup lawyers guide a startup through key points in the startup lifecycle, starting with company formation, continuing through major financing transactions, and typically ending with an acquisition.[94] Accordingly, they have visibility to all of the key moments when *Trados* might affect advice to clients, including negotiation of venture capital financing terms, construction of corporate governance mechanisms (such as board composition), structuring of executive compensation, and board deliberations at the time of exit.

Third, interviewees describe a number of ways in which their work is indirectly influenced by Delaware law even if they do not consider themselves to be primary consumers of judicial opinions. According to many of the interviewees, firms feature significant "knowledge management" functions. Interviewees identified internal firm communications as a source of information about legal developments,[95] and they described

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92. *See* Interview with Lawyer #18, at 1–2. These observations are consistent with academic accounts of Silicon Valley law firms. The origin story of these firms centers on a group of charismatic firm founders who convinced clients to stay with them, rather than seeking out San Francisco corporate firms, through the company's full growth cycle and maturation. Lawrence M. Friedman et al., *Law, Lawyers, and Legal Practice in Silicon Valley: A Preliminary Report*, 64 IND. L.J. 555, 560 (1989). But Silicon Valley law firms have transformed into national law firms, and national law firms from other regions have set up shop in Silicon Valley. *See* Cable, *supra* note 10, at 189 (noting that prominent Silicon Valley firms are now listed among the Am Law 100 and that many Am Law 100 firms now feature Silicon Valley offices).

93. *See* Interview with Lawyer #7, at 1 ("[A]ll general corporate lawyers should be able to process a general M&A deal."); Interview with Lawyer #9, at 1 (reporting that the interviewee retains primary responsibility for mergers under $300 million); Interview with Lawyer #11, at 1 (reporting that the interviewee has handled an estimated 150 acquisitions even though the firm has an M&A group); Interview with Lawyer #18, at 1 (reporting "plenty of instances" when startup lawyers handle M&A transactions despite the firm having an M&A practice group).

94. *See* Interview with Lawyer #1, at 1 (indicating that the lawyer represents clients for "the full lifecycle of the client"); Interview with Lawyer #5, at 1 (describing his practice as being relationship based and spanning the life of the company, but also describing a trend towards specialization for company representation).

95. *See* Interview with Lawyer #1, at 2 (describing client alerts, handbooks, and email updates produced by the firm); Interview with Lawyer #3, at 1 (describing compilations of materials circulated within the firm); Interview with Lawyer #4, at 1 (describing the firm as "pretty good" at keeping the lawyers up to date); Interview with Lawyer #11, at 1 (reporting that the people follow Delaware law within the firm and that the "beauty of a big firm" is that it has "a lot of resources"); Interview with Lawyer #12, at 2 (describing practice group meetings as a primary source of information about legal developments); Interview with Lawyer #14, at 1 (discussing firm-generated alerts and memos on key developments); Interview with Lawyer #15, at 1 (discussing weekly email about legal developments). *But see* Interview with Lawyer #5, at 1 (claiming that there is no advantage to firm-generated updates versus externally produced materials).

systems for updating firm forms to reflect major developments.[96] In some cases, these systems extended beyond transactional documents and included fiduciary duty presentations to boards.[97] Some firms invest heavily in these efforts by hiring full-time knowledge management personnel.[98] If those systems are effective, startup lawyers act on a firm-wide assessment of Delaware law, whether or not they know it.

Of course, not all startup lawyers practice in firms with robust knowledge-management systems. Some interviewees practice in small firms or in large firms with relatively small Silicon Valley offices. Regardless of firm size, the level of formality in producing and maintaining firm forms differs.[99]

Interviewees indicate that industry-wide collaboration can substitute for, or supplement, intra-firm systems. Silicon Valley is perceived as a norms-laden environment with a strong sense of what is "market" and appropriate for a venture capital financing and exit transaction.[100] In particular, interviewees identify the NVCA forms project as a useful example of standardization across firms.[101]

Finally, interviewees report regular and systematic contact with the Delaware bar. Some interviewee firms have opened Delaware offices.[102] Most interviewee firms form relationships with existing Delaware firms, such as Richards, Layton & Finger or Morris, Nichols, Arsht & Tunnell LLP.[103] These Delaware firms are on call for consultation on

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96. *See* Interview with Lawyer #1, at 2–3 (describing knowledge management personnel and their role in updating firm forms); Interview with Lawyer #2, at 1 (describing the process for updating firm forms to reflect legal developments); Interview with Lawyer #4, at 1 (emphasizing the importance of firm forms and estimating approximately annual updates from legal developments); Interview with Lawyer #7, at 1 (discussing the process within the firm for updating forms to reflect legal developments).

97. *See* Interview with Lawyer #4, at 2 (describing standardized board presentations); Interview with Lawyer #12, at 2 (reporting that the firm has standardized board presentations regarding fiduciary duties).

98. *See* Interview with Lawyer #7, at 1 (discussing the internal updates by a knowledge management group within the firm); Interview with Lawyer #8, at 1 (discussing the role of knowledge management personnel in updating firm forms to reflect legal developments); Interview with Lawyer #11, at 1 (discussing full-time personnel who update firm forms); Interview with Lawyer #14, at 1 (discussing "reformed lawyers" who work for the firm as knowledge management personnel); Interview with Lawyer #15, at 1 (discussing the role of knowledge management lawyers in updating firm forms); Interview with Lawyer #19, at 1 (discussing the role of knowledge management and professional development personnel in updating firm forms and educating lawyers within the firm about legal developments).

99. *See* Interview with Lawyer #13, at 1 (explaining a former firm of the interviewee spent significant resources updating firms but that the interviewee's current firm was less systematic about updating forms); Interview with Lawyer #14, at 1 (reporting that it can be "a little murky" who "owns the form"); Interview with Lawyer #17, at 1 (describing a small firm with informal forms).

100. *See* Interview with Lawyer #10, at 1 (explaining that Silicon Valley is a "repeat player economy" with a small number of firms (the "five families") being a "center of gravity"); *see also* Brian J. Broughman & Jesse M. Fried, *Carrots & Sticks: How VCs Induce Entrepreneurial Teams to Sell Startups*, 98 CORNELL L. REV. 1319, 1341 (2013) ("Silicon Valley is a close-knit community with its own norms and ways of doing business.").

101. *See* Interview with Lawyer #12, at 3 (reporting a preference for NVCA forms); Interview with Lawyer #14, at 2 (reporting involvement in the NVCA drafting committee and describing the forms as informative); Interview with Lawyer #15, at 1 (discussing the possibility of using NVCA forms because they are "easily negotiated" and used "across the country"); Interview with Lawyer #17, at 1 (describing a preference for NVCA forms).

102. *See* Interview with Lawyer #1, at 2 (describing the firm's Delaware office); Interview with Lawyer #4 (describing the firm's Delaware office); Interview with Lawyer #8, at 1 (describing consultation with the firm's Delaware office on a "regular basis" and whenever a situation is "more than bread-and-butter" or "quasi-litigious"); Interview with Lawyer #9, at 1 (discussing regular presentations by the firm's Delaware office).

103. *See* Interview with Lawyer #13, at 1 (discussing frequent consultation with, and regular updates from,

particular client matters,[104] and they also provide regular corporate law updates through written materials and in person presentations.[105]

C. Number

I conducted a total of 20 interviews. I believe this number is sufficient to identify customary practice in response to *Trados*. A small number of firms handle the vast majority of venture capital financings in Silicon Valley. For example, six law firms handle over 75% of West Coast venture capital financings.[106] As discussed above, the interviewees report that their law firms are a primary source of information about legal developments and have systems in place to standardize work product within firms.[107]

Regarding the broader conceptual insights presented in Part V, this Article should be considered an exploratory study. As such, it seeks to make a primarily theoretical contribution to be tested by future confirmatory research.[108]

IV. THE MODEST EFFECTS OF *TRADOS*

This Part reports my primary observations regarding the effects of *Trados* on lawyers' customary advice to clients. In sum, the case has not had the effects on venture capital financing terms predicted by some commentators. It has had a modest but noticeable effect on sale process. In particular, lawyers now advise boards to more systematically consider continuation value and, in some cases, push consideration to common shareholders in excess of their baseline entitlements.

A. Familiarity with Trados

Nearly all of the interviewees are familiar with *Trados* at some level.[109] Some

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these firms); Interview with Lawyer #15, at 1 (discussing regular presentations by these firms); Interview with Lawyer #19, at 1 (discussing updates from these firms).

104. *See* Interview with Lawyer #7, at 1 (reporting that the firm consults Delaware counsel "all the time"); Interview with Lawyer #13, at 1 (stating that the interviewee consults Delaware counsel every few months).

105. *See* Interview with Lawyer #2, at 1 (describing periodic presentations by Delaware firms); Interview with Lawyer #10, at 1 (observing that it is in a Delaware firm's "business interest" to "maintain contact points" with Silicon Valley firms); Interview with Lawyer #11, at 1 (discussing updates from prominent Delaware firms); Interview with Lawyer #12, at 1 (stating that a prominent Delaware firm is "pretty proactive" about giving the firm regular updates); Interview with Lawyer #16, at 1 (reporting that the interviewee's firm works with and receives updates from Delaware firms); Interview with Lawyer #17, at 1 (describing regular updates from Delaware firms).

106. *See* PITCHBOOK, GLOBAL LEAGUE TABLES 29 (2017) (listing most active law firms by deal location).

107. *See supra* notes 95–98 and accompanying text (discussing knowledge management functions within firms).

108. *See* ROBERT A. STEBBINS, EXPLORATORY RESEARCH IN THE SOCIAL SCIENCES 1–9 (2001) (explaining the role of exploratory research in formulating grounded theory to guide future research).

109. *See* Interview with Lawyer #1, at 3 (reporting being "pretty familiar" with *Trados* and describing the basic fact pattern); Interview with Lawyer #3, at 2 ("I am familiar with [*Trados*], but not too in depth on that one."); Interview with Lawyer #4, at 1 (stating that the lawyer is "definitely aware" of *Trados*); Interview with Lawyer #5, at 1 (describing *Trados* as a rare case that matters in the startup context); Interview with Lawyer #7, at 1 (identifying *Trados* as a case discussed within the firm but reporting that "it's been a while" and "things have calmed down" in terms of the case's impact); Interview with Lawyer #8, at 1 (reporting that *Trados* "certainly came up"); Interview with Lawyer #9, at 1 (reporting some familiarity with the case); Interview with Lawyer #10, at 1 (stating that *Trados* is familiar and that the case is referenced when considering drag-along rights or when

interviewees know the case immediately by name and are able to give relatively detailed accounts of its facts and holdings. One interviewee describes it as "the most important [case] of my career."[110] Other interviewees recognize the case after some prompting. It is always possible that some interviewees claim familiarity with the case to avoid embarrassment. One interviewee humorously suggests that a corporate lawyer would "pretend" to know any case in order to look good.[111] But it was my strong sense, based on the full body of interviews, that *Trados* was, in fact, a familiar case, especially for those who practiced for a substantial period before the first opinion in 2009.

A number of interviewees comment that *Trados* is somewhat distinctive in its notoriety. They report that caselaw does not frequently affect their work representing private companies because most high-profile Delaware judicial opinions are tailored to public company deals.[112] For these lawyers, keeping up to date on contracting conventions (whether particular deal terms were "market") matter more than keeping up to date on Delaware corporate law.[113]

B. Ex Ante Contracts

The commentary following *Trados* contemplated two primary changes in venture capital financings: increased use of drag-along rights and adoption of the NVCA's new sale right. Interviewees have little familiarity with the NVCA sale right. While some interviewees report small changes in drag-along rights, the interviewees generally downplay the importance of these provisions.

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the common is getting nothing); Interview with Lawyer #12, at 1 (indicating that *Trados* was affecting a deal the interviewee was currently working on); Interview with Lawyer #13, at 1–2 (describing *Trados* as a case that the interviewee has read multiple times); Interview with Lawyer #14, at 1 (reporting that the interviewee is "extraordinarily" familiar with *Trados*); Interview with Lawyer #17, at 1 (reporting that the interviewee is "generally familiar" with *Trados*); Interview with Lawyer #19, at 1 (reporting that the interviewee is "of course" familiar with *Trados* and was "hit from every angle" by updates regarding the case); Interview with Lawyer #20, at 2 (reporting being familiar with *Trados*). I generally told interviewees that I wanted to interview them about how Delaware case law affects their practice. I did not generally mention *Trados* in advance of the interview. Four interviewees knew we would discuss *Trados* because they were familiar with my study or because a referring interviewee described the study in the course of arranging an introduction.

110. Interview with Lawyer #13, at 3.

111. *See* Interview with Lawyer #9, at 1.

112. *See* Interview with Lawyer #1, at 2 ("I'm mainly on the private company side of things . . . so there aren't a ton of court cases that end up changing the advice I'm giving."); Interview with Lawyer #3, at 1 (stating that influential judicial opinions are "actually pretty rare in Silicon Valley" because of the case law's focus on "public-public deals"); Interview with Lawyer #5, at 1 (stating that legal developments affect his work with startups "much less frequently" than his work with publicly traded companies); Interview with Lawyer #11, at 2 ("Cases are not in the nomenclature."); Interview with Lawyer #12, at 1 (reporting that Delaware case law "doesn't come up a lot"); Interview with Lawyer #12, at 2 ("We're too busy to have time to read cases and pontificate, as much as I'd like to do that."). *But see, e.g.*, Interview with Lawyer #15, at 1 (reporting that recent Delaware caselaw is increasingly focusing on private company governance); Interview with Lawyer #18, at 2 (observing that a number of Delaware cases regarding provisions of M&A agreements also affect private companies).

113. *See* Interview with Lawyer #2, at 1 (reporting that "course of dealing" affects the practice more than legal developments).

1. Drag-Along Rights

Drag-along rights are typical in venture capital financings.[114] The customary provision allows some collection of shareholders to require other shareholders to vote for a merger or tender their shares in a stock sale.[115] In its most traditional form, a drag-along right can only be triggered if the board approves the transaction. The reason is in part doctrinal—most typical forms of acquisition (asset sales and mergers) require board approval by statute.[116] This requirement of board approval means that a traditional form of drag-along provision cannot circumvent limits set by *Trados*—the board eventually has to weigh in on the transaction and at that point the *Trados* conflict emerges.[117]

By removing the reference to board approval in a drag-along right, however, the provision does create one narrow avenue for the preferred holders to sell the company without the board ever chiming in. Specifically, preferred shareholders could use such a drag-along right to force a stock sale—once the specified group of shareholders triggered the rights, all other parties to the agreement would be required to tender their shares and sign onto a customary stock purchase agreement.

Interviewees disagree on whether there has been a change in drag-along rights in response to *Trados*. Some interviewees suggest that it has been more common since *Trados* to draft drag-along rights without requiring board approval.[118] Other interviewees report that drag-along rights in general have become "more widespread."[119] Others, however, report seeing no meaningful change in drag-along rights,[120] or doubt that any such trend is

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114. According to a deal study by Cooley LLP, over 80% of financings handled by the firm from 2014 through 2018 included drag-along rights. *See Trends*, COOLEY GO, https://www.cooleygo.com/trends/ (last visited Feb. 11, 2019). *See also* Interview with Lawyer #4 (estimating that 90% of venture capital deals already included drag-along rights prior to Trados). *But see* Interview with Lawyer #10, at 1 (suggesting that only 60% of deals include drag-along rights).

115. *See* NVCA VOTING AGMT., *supra* note 5, at 6–12 (providing a form drag-along provision).

116. *See* DEL. GEN. CORP. L. § 251.

117. *See supra* note 71 (discussing doctrinal impediments to using drag-along rights to circumvent *Trados*). *See also* Interview with Lawyer #1, at 7 (stating that there is no way to "waive fiduciary duties" of the board to "consider the rights of all shareholders" when evaluating a merger). A recent Delaware case underscores the limitations of drag-along rights in the face of fiduciary duty problems. *See In re* Good Tech. Corp. S'holder Litig., C.A. No. 1150-VCL, 2017 WL 2537347 (Del. Ch. May 12, 2017).

118. *See* Interview with Lawyer #2, at 1 (stating that drag-along provisions omit the requirement of board approval more frequently in recent years); Interview with Lawyer #13, at 1 (reporting instances of removing the board approval from a drag-along provisions but also suggesting that clients have given some "push back" against that formulation). *But see* Interview with Lawyer #10, at 1 (suggesting that *Trados* has had the effect of advising against a drag-along right triggered by just the preferred and the board because of fiduciary duty concerns).

119. Interview with Lawyer #1, at 6. *See also* Interview with Lawyer #14, at 1 (suggesting a substantial increase in drag-along rights compared to 15 years ago).

120. *See* Interview with Lawyer #4, at 1 (stating that there is "no difference" in terms since *Trados* and that any uptick in drag-along rights would not be considered meaningful because they were already typical); Interview with Lawyer #6, at 1 (suggesting that any discussion of removing the board trigger from drag-along provisions was just "optics" and has not had any lasting effect); Interview with Lawyer #7, at 1 (reporting that *Trados* made no difference in "up front" contracting); Interview with Lawyer #8 (stating that *Trados* did not affect venture capital financings and the firm did not change its approach to drag-along rights); Interview with Lawyer #11, at 1 (stating that the case has not affected drag-along rights); Interview with Lawyer #12, at 1 (indicating that the interviewee's firm considered taking the board out as a trigger in the firm's form but decided "net-net it is better having it in" and observing no change to drag-long rights in general); Interview with Lawyer #17, at 2 (reporting "no difference" in drag-along rights); Interview with Lawyer #19, at 1 (reporting that *Trados* did not change the terms of venture capital financings).

related to *Trados*.[121]

Though interviewees are divided in assessing *Trados*'s effects, they are more unified in downplaying the significance of drag-along rights in general. As described further below, a combination of legal and practical barriers prevents preferred shareholders from using a drag-along right to sell a Silicon Valley startup:

- Acquirers have a strong preference for mergers or asset sales—both of which are negotiated with the target board and effected at the company level—rather than acquiring stock from individual shareholders.[122] Interviewees describe stock acquisitions using drag-along rights as idiosyncratic and unadvisable.[123]
- In Silicon Valley, acquisitions are often focused on acquiring talent rather than hard assets or specific technology—"the buyer wants the team."[124] Founders and employees, who hold key human capital, are typically the largest common shareholders.[125] Accordingly, it would be self-defeating to pursue a transaction without support from the bulk of common holders.[126]
- Enforcing a drag-along right may be prohibitively expensive.[127]
- Controlling shareholders also have fiduciary duties that may be implicated

121. *See* Interview with Lawyer #5, at 1 (stating that *Trados* has had a "pretty negligible impact on venture capital terms" and that any change in drag-along rights is "not framed in terms of *Trados*"); Interview with Lawyer #14, at 1 (noting an increase in drag-along rights but suggesting that "it's not strict causation"); Interview with Lawyer #20, at 2–3 (doubting that any changes in financing terms are attributable to *Trados*).

122. *See* PETER V. LETSOU, CASES AND MATERIALS ON CORPORATE MERGERS AND ACQUISITIONS 33–36, 136–39 (2006) (discussing the basic structure of mergers and asset sales); Interview with Lawyer #10, at 1 (stating that it is "bizarre" to write a drag-along provision without board approval in the trigger because board is required under the merger statute); Interview with Lawyer #13, at 1 (explaining that a merger is a preferable deal structure); Interview with Lawyer #15, at 3 (reporting that removing the board from the drag-along trigger does not work well because the board must approve a merger); Interview with Lawyer #17, at 2 ("I can't imagine using a stock sale [using a drag-along].").

123. *See* Interview with Lawyer #4, at 1 (asserting that it is "virtually impossible to sell a company without board approval" and having experience with only one acquirer who prefers stock sales and may use drag-along rights); Interview with Lawyer #5, at 1–2 (describing a rare "hostile takeover of a private company," which had "a tremendous number of downsides"); Interview with Lawyer #6, at 1 (stating that an acquirer negotiating directly with shareholders is "not happening"); Interview with Lawyer #14, at 2 (identifying one large acquirer who prefers stock purchases and might use a drag-along right). *See also* Interview with Lawyer #3, at 2 (discussing the difficulty of conducting a sale process when founders in management provisions are not cooperating).

124. Interview with Lawyer #7, at 2. *See also* Interview with Lawyer #3, at 3–4 ("The workforce generally has some value in addition to the IP, and you need to reward them somehow."); Interview with Lawyer #5, at 2 ("People are a big part of what you're acquiring.").

125. *See* Interview with Lawyer #14, at 3 (describing founders and employees as the primary common shareholders); Interview with Lawyer #17, at 1 (suggesting that the effects of *Trados* are limited by the fact that founders and employees are the most common shareholders and ordinarily receive compensation for future employment with the acquirer); Interview with Lawyer #17, at 2 (stating that it is "virtually impossible" to buy a company without the support of the founders).

126. For a description of how founders and employees can resist an undesirable transaction, see Broughman & Fried*, supra* note 100, at 1331–33.

127. *See* Interview with Lawyer #4, at 1 (stating that most lawyers are "nervous about enforcement" of drag-along rights because shareholders can make procedural objections); Interview with Lawyer #16, at 1 (discussing the enforceability of drag-along rights); *see also In re* Good Tech. Corp. Stockholder Litig., No. 11580-VCL, 2017 WL 2537347, at *4 (Del. Ch. May 12, 2017) (suggesting that a court might refuse to enforce a drag-along if a board violates its fiduciary duties in approving the applicable transaction).

by forcing a sale at the shareholder level.[128]

According to the interviewees, drag-along rights play a modest role of giving a majority of shareholders "leverage"[129] when dealing with smaller shareholders ("cats and dogs")[130] who would otherwise try to extract hold-up value or are nonresponsive.[131] But they are almost never exercised.[132]

In fact, a number of interviewees suggest that a heavy-handed drag-along right, even if more easily enforced, would defy customary understandings of how control should be allocated between founders and venture capital investors. According to one interviewee, the prevailing norm is "shared control" over exit decisions.[133] Several interviewees emphasize that the current deal climate is particularly founder friendly and that it would be far outside market norms for an investor to request sole discretion over exit decisions.[134]

2. NVCA Sale Right

The NVCA's model forms group proposed a sale right in response to *Trados*. As described above, this sale right aimed to take exit decisions out of the hands of the board by giving preferred shareholders (1) a contractual right to put the company up for sale and (2) a redemption right at any resulting offer price.[135]

Most interviewees are not familiar with the NVCA sale right or have not seen it included in venture capital financings.[136] A handful of interviewees have seen the sale right

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128. *See* Interview with Lawyer #2, at 1.

129. *See* Interview with Lawyer #4, at 1 (describing a drag-along rights as "leverage" and not a practical outcome).

130. *See* NVCA VOTING AGMT., *supra* note 5, at n.13 (suggesting that a "housekeeping" drag-along provision intended to "prevent dissent by minority 'cat and dog' stockholders" is in the interests of all shareholder constituencies).

131. *See* Interview with Lawyer #5, at 2 (reporting that drag-along rights are not usually triggered by just preferred stock shareholders and usually can be triggered only with common shareholder and board approval too); Interview with Lawyer #6, at 1 (describing drag-along rights as a tool for taking care of holdouts when both classes of stock "mostly agree" on a sale); Interview with Lawyer #13, at 1 (suggesting that 90% of drag-along rights are for "sweeping up" little shareholders rather than allocating sale control); Interview with Lawyer #16, at 1 (reporting that drag-along rights are intended for "administrative purposes").

132. *See* Interview with Lawyer #7, at 2 (reporting that the interviewee has never seen a drag-along right used); Interview with Lawyer #10, at 1 (reporting that the interviewee has never seen a drag-along right used); Interview with Lawyer #13, at 2 (reporting only one instance in which the interviewee has seen attempted use of a drag-along right); Interview with Lawyer #16, at 1 (reporting that the interviewee has never seen a drag-along right exercised); Interview with Lawyer #17, at 2 (reporting that drag-along rights and "90% of provisions" in a "standard VC deal" are never exercised).

133. *See* Interview with Lawyer #5, at 2 (reporting that very few drag-along provisions include just a preferred trigger, that venture capital investors usually "don't even ask," and that the usual arrangement is "shared control").

134. *See* Interview with Lawyer #4 (stating that a drag-along right without a board trigger is "a tougher up front deal"); Interview with Lawyer #8, at 1 (indicating that founders are unlikely to negotiate away control rights in the current market); Interview with Lawyer #14, at 2 ("Fundamentally, founders aren't going to agree to it.").

135. *See supra* text accompanying note 66 (discussing the mechanics of the sale right).

136. *See* Interview with Lawyer #1, at 7 (reporting that investor counsel has not asked for the sale right and that it would be considered "pretty aggressive"); Interview with Lawyer #3, at 7 ("I haven't seen it."); Interview with Lawyer #5, at 2 (reporting that the NVCA sale right is not being used); Interview with Lawyer #14, at 2 (indicating that the interviewee has not seen the NVCA sale right included in deals); Interview with Lawyer #16, at 1 (reporting that the interviewee never "had that appendix" in a deal).

included once or twice but view those transactions as idiosyncratic.[137]

When I described the sale right, the interviewees were skeptical about its efficacy. Some of their reasons for being skeptical echo their concerns about drag-along rights: it would be the rare acquirer who would step into a sale process initiated over substantial shareholder objection and without board leadership. As one interviewee states: "Fundamentally, deals happen when pretty much everyone wants the deal to happen. You don't drag people kicking and screaming."[138] They also note the difficulty of exercising redemption rights under current Delaware law.[139]

At times, the interviewees suggest a broader concern about any effort to craft a contractual response to *Trados*. One interviewee explains that there is "only so much contracting" you can do.[140] Another interviewee explains that controlling outcomes by contract is challenging because "it's very difficult early on to really understand where the company is headed."[141] In other words, parties to a venture capital financing face an incomplete contracting problem.

C. Deal Process

While the influence of *Trados* on ex ante contracts seems to be mild, interviewees indicate that *Trados* does have noticeable effects on board process in connection with exit transactions. Effects cited by interviewees include efforts to ratify transactions through independent committees and shareholder votes, more formal consideration of effects on common shareholders, and modest payments ("allocations") to common shareholders.

1. Trados *Territory*

Before considering how *Trados* affects customary board procedure, it is useful to consider *when* the interviewees consider the case. In other words, what is a "*Trados* case" to these interviewees?

Most basically, the interviewees associate the case with a disappointing result for common shareholders. They report thinking about the case whenever the common shareholders get little or no consideration in a sale transaction.[142]

137. *See* Interview with Lawyer #12, at 1 (reporting one instance of the sale right but with a foreign investor); Interview with Lawyer #13, at 1 (reporting that a counterparty once tried unsuccessfully to use the sale right); Interview with Lawyer #15, at 2 (stating that the interviewee has seen the right used once or twice but that it is likely ineffective because a redemption "ends up in a food fight"); Interview with Lawyer #17, at 2 (reporting one instance in which a non-Silicon Valley firm proposed the sale right); Interview with Lawyer #20, at 3 (reporting one instance in which an investor requested the sale right but describing it as atypical).

138. Interview with Lawyer #13, at 2.

139. *See* Interview with Lawyer #2 (noting the limits on an investor's ability to enforce a redemption right and the inevitability of some board involvement in any sale).

140. Interview with Lawyer #4, at 2.

141. Interview with Lawyer #1, at 6. *See also* Interview with Lawyer #7, at 1 (reporting that contracting for control over exit decisions is difficult because you are "so far from any understanding of what might happen").

142. *See* Interview with Lawyer #7, at 1 (suggesting that a *Trados* situation is where "the common don't get much"); Interview with Lawyer #8, at 2 (stating that *Trados* applies when the common gets "zilch" and a liquidation preference is paid); Interview with Lawyer #10, at 2 (suggesting that the interviewee begins thinking about *Trados* whenever the company is "going to have some unhappy shareholders"); Interview with Lawyer #14, at 2 (reporting that *Trados* is considered "when you may not clear the stack or by a wide margin"); Interview with Lawyer #17, at 1 (explaining that *Trados* applies when the company sells and all consideration goes to the preferred); Interview with Lawyer #18, at 3 ("The threshold is a deal where the common is getting nothing.");

Some interviewees, however, note problems with this broad interpretation. As one interviewee states, "that puts [nearly] every case into *Trados* in our industry."[143] A significant majority of startups fail in the sense of selling below or near the investors' liquidation preference.[144] But interviewees explain that company failure does not always, or even usually, result in real conflicts between common and preferred. One interviewee notes that even when venture capital investors recover a significant portion of their liquidation preference, that is a disappointing result by industry standards and not materially different than a total loss in terms of overall fund performance.[145] Moreover, the realistic alternative to selling is not usually continuation—it is winding down and liquidating with substantial losses for preferred and common.[146] Accordingly, some interviewees are less concerned about *Trados* in deals where the preferred takes substantial losses too.[147]

Ultimately, perceptions of litigation risk, as much as the severity of the conflict, seem to dictate the level of sensitivity to *Trados.* Risk is determined in part by the likelihood that the common stock does, in fact, have value as determined by the size of the "liquidation stack," the company's cash reserves, and the company's projections if it can raise additional funds.[148] But risk is also determined based on the composure of the common shareholder base. Interviewees cited "estranged founder[s]"[149] and "litigious angels"[150] with unusually large stakes as the biggest concern.[151] Finally, risk can result from more deal-specific circumstances such as whether common shareholders previously expended cash to exercise options.[152]

Interview with Lawyer #20, at 3 (reporting that the interviewee considers *Trados* when the common holders get little or no consideration).

143. Interview with Lawyer #19, at 3.

144. *See* Abraham J.B. Cable, *Incubator Cities: Tomorrow's Economy, Yesterday's Startups*, 2 MICH. J. PRIV. EQUITY & VENTURE CAP. L. 195, 202 (2013) (reviewing evidence that most venture-backed startups fail to return positive amounts to investors); Interview with Lawyer #18, at 3 (arguing that *Trados* is "not consistent with the VC-backed model" because nine out of ten startups fail).

145. *See* Interview with Lawyer #19, at 3.

146. *See also* Interview with Lawyer #6, at 2; Interview with Lawyer #10, at 2 (suggesting that by the time of sale, you might be about to send the company to Sherwood Partners, a prominent liquidator); Interview with Lawyer #20, at 3 (describing *Trados* as unique because the company had the resources to keep operating).

147. *See* Interview with Lawyer #4, at 2 (suggesting that the case applies in "narrow circumstances" and not when the company is running out of money); Interview with Lawyer #13, at 2 (suggesting that *Trados* is of less concern when it is "all up and to the right" and when "things are terrible"); Interview with Lawyer #14, at 3 (stating that the case is relevant when there is "more of a turnaround element" and not when there are "three months left of gas in the tank and the board isn't putting more money in"); Interview with Lawyer #15, at 2 (asserting that there is no conflict in selling the company if there is no viable path to funding the company's continued operation).

148. *See* Interview with Lawyer #5, at 3.

149. Interview with Lawyer #6, at 1. *See also* Interview with Lawyer #8, at 3 (identifying a "former disgruntled founder" as a source of litigation risk).

150. Interview with Lawyer #2, at 2. *See also* Interview with Lawyer #16, at 3 (identifying as a source of risk investors who were converted into common in a recapitalization).

151. *See* Interview with Lawyer #15, at 3 (stating that the shareholder base determines litigation risk, with particular emphasis on whether there are any common shareholders who invested large amounts or a "wingnut founder").

152. *See* Interview with Lawyer #3, at 10.

2. Independent Board or Shareholder Approval

Interviewees are understandably sensitive to judicial standards of review. One interviewee explains that litigation under the fairness standard is time consuming and "time is everything for these people."[153] Another interviewee reports that the "business judgment rule is everything."[154] Accordingly, the interviewees report that *Trados* motivates companies to form independent committees of directors or seek disinterested shareholder approval of transactions in order to cleanse the transaction and gain the benefit of the deferential business judgment rule.[155]

There are, however, significant practical impediments to forming an independent committee of directors in this context. Founders serving on the board often receive bonus payments in connection with a sale under a management incentive plan ("MIP") or receive other compensation arrangements with an acquirer.[156] *Trados* held that those kinds of payments disqualified the recipients from being considered independent.[157] *Trados* also found that facially independent directors were conflicted due to informal relationships with venture capital funds.[158]

These same considerations may also be impediments to obtaining disinterested shareholder approval. Founders, who may be conflicted due to an MIP, are often the largest holders of common shares. Other smaller holders—former employees, vendors, or early investors forced to convert in recapitalizations—may be understandably unmotivated to consent to a transaction paying them little or nothing.[159]

As one interviewee sums it up, "you're only as good as your options."[160] And companies sometimes "count noses and no one is independent."[161]

Finally, it is difficult to discern the extent to which *Trados* actually drives the shareholder approval process. For example, acquirers may require a high percentage of

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153. Interview with Lawyer #5, at 3.

154. Interview with Lawyer #6, at 2.

155. *See* Interview with Lawyer #1, at 3 (discussing independent board committees); Interview with Lawyer #1, at 4 ("[W]e put the deal in front of the common."); Interview with Lawyer #6, at 1 (discussing independent board committees and disinterested shareholder approval); Interview with Lawyer #7, at 2 (reporting that "optimally" a company seeks disinterested approval); Interview with Lawyer #8, at 2 (observing increased use of independent board committees but not disinterested shareholder approval); Interview with Lawyer #9, at 2 (suggesting that independent director or disinterested shareholder approval might be considered as a layer of protection against a *Trados* claim); Interview with Lawyer #12, at 2 (reporting that *Trados* "absolutely" pushes companies to get independent director approval); Interview with Lawyer #19, at 2 (stating that disinterested or independent approval is more common following *Trados*).

156. *See* Interview with Lawyer #12, at 2 (suggesting that the presence of a management incentive plan heightens concern about Trados). One interviewee noted this impediment to finding independent directors, but also suggested that management incentive plans could be structured in ways that mitigate the conflict. *See* Interview with Lawyer #5, at 2.

157. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17, 45 (Del. Ch. 2013).

158. *See id.* at 54 (noting a "close business relationship" between a purportedly independent director and venture capital investors).

159. *See* Interview with Lawyer #4, at 2 (discussing the difficulty of getting common shareholders to join merger agreements when the common stock is "out of the money"); Interview with Lawyer #6, at 1 (reporting that it is challenging to find disinterested common shareholders).

160. Interview with Lawyer #2, at 2.

161. *Id.*; *see also* Interview with Lawyer #10, at 3 (explaining that independent directors are "not in the network" for most companies); Interview with Lawyer #15, at 1 (stating that "you're lucky if you have a disinterested director" so "everything is an interested transaction").

shareholders (90-95%) to consent to a transaction or agree to liability provisions of a merger agreement.[162] Interviewees expressed the view that disinterested shareholder votes are "driven by the buy side" rather than fiduciary law.[163]

3. Common-Continuation Value

A number of interviewees report that preferred-controlled boards now more fully and formally consider the effects of a transaction on common holders—what I will call "common-continuation value."[164]

In part, interviewees describe increasing formality. As one interviewee puts it, the goal is to "force the board to say what it is feeling" by building a clear record of the analysis in board minutes.[165] Interviewees note that this cuts against the grain of historical practice in Silicon Valley, where management and governance have traditionally been lean.[166]

Beyond mere formality, interviewees describe meaningful exploration by boards of alternative transactions and prospects for continued operations. In the course of approving a sale, boards may investigate financing sources, the market for the company's product, employee retention, and layoffs and cost-cutting measures.[167] Given the cash-strapped

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162. *See* Interview with Lawyer #2, at 2 (reporting that buyers require a high percentage of target shareholders to approve a transaction); Interview with Lawyer #10, at 3 (stating that "the commercial baseline" encourages high vote thresholds and not *Trados*); Interview with Lawyer #14, at 2 (reporting that buyers require 90-95% buyer approval); Interview with Lawyer #16, at 2 (stating that acquirers will require near 100% shareholder approval). Disinterested shareholder approval may be required under Section 280G of the Internal Revenue Code to avoid additional tax on golden parachute payments. *See* Interview with Lawyer #3, at 6.

163. Interview with Lawyer #14, at 3.

164. *See* Interview with Lawyer #2, at 1 (reporting that because of *Trados* "a conversation about allocation of proceeds needs to happen"); Interview with Lawyer #8, at 1 (describing *Trados* as requiring a process that "considered common" holders); Interview with Lawyer #9, at 2 (suggesting that pre-*Trados* there was less analysis by the board of whether the company could continue); Interview with Lawyer #10, at 2 (reporting that *Trados* gave rise to "a notion" that the board has to "take into account what benefits the common shareholders"). *But see* Interview with Lawyer #18, at 4 (stating that it is "extremely rare" to have formal documentation of common-continuation value).

165. Interview with Lawyer #8, at 2. *See also* Interview with Lawyer #1, at 6 (reporting that *Trados* "certainly would affect the amount of documentation in the board minutes or the [board] process"); Interview with Lawyer #4, at 1 (reporting that boards are now "significantly more sensitive to process and documentation of alternatives"); Interview with Lawyer #5, at 4 (reporting that "[w]hat really happened is that people document formally" consideration of the common stock); Interview with Lawyer #7, at 2 (suggesting that you might "paper" the analysis in "board language"); Interview with Lawyer #13, at 2 (stating that *Trados* causes boards to be especially careful about documenting board process); Interview with Lawyer #16, at 2 (stating that lawyers now "document the discussion").

166. *See* Interview with Lawyer #10, at 2 (discussing the challenges of creating a formal record when management is not sophisticated and find themselves at a "fall back" outcome of a disappointing merger); Interview with Lawyer #18, at 4 (discussing an aversion to detailed minutes); Interview with Lawyer #19, at 2 (describing typical venture capital minutes as "Teflon").

167. Interview with Lawyer #6, at 1 (stating that *Trados* results in "focus on process" and "build[ing] a record" that the company "is running out of money" and "went out for deals"); Interview with Lawyer #8, at 1–2 (reporting that boards consider employee defections, the market for the company's products, and availability of additional financing); Interview with Lawyer #14, at 2 (stating that boards consider and document declining financial prospects, declining sales, competition, capital requirements, and lack of additional funding sources); Interview with Lawyer #15, at 2 (reporting that a board will go "up and down Sand Hill Road" looking for financing as part of the process); Interview with Lawyer #16, at 2 (describing a fact-intensive process that might consider, among other factors, how hard the company has been shopped and the company's business prospects).

nature of most startups,[168] this process focuses heavily on the availability of additional investment or other forms of financing such as debt.[169] This process is not so much a formal valuation of the common stock, but rather a qualitative analysis of viability.

The analysis can be thought of as serving multiple purposes. Sometimes the analysis confirms that there are no good alternatives to a proposed sale. Interviewees note that companies often lack reasonable financing options to continue operations, have failed to hit key development milestones, or are facing an exodus of employees.[170] In these circumstances, *Trados* might not be relevant practically or doctrinally.[171]

In addition, considering common-continuation value is relevant to the fairness review that a court will apply if it determines there is a *Trados* conflict. Fairness review includes scrutiny of both transaction outcomes and board process.[172] Formally considering common-continuation value directly responds to one of the *Trados* court's sharpest criticisms of that board's sale process.[173]

4. Allocations to Common

Some interviewees suggest that a *Trados*-inspired board discussion can affect transaction terms. Interviewees report that a board might hold out for a deal that clears liquidation preferences or request that preferred stock sacrifice some amount of its liquidation preference so that consideration flows to common stock.[174] Preferred holders might even convert to common stock so that preferred and common holders receive proportionate consideration.[175]

Payouts to common holders may not be frequent or large. One interviewee describes these allocations as a "nugget"[176] and another interviewee describes them as "a pittance to the common."[177] According to one interviewee, the "jaundiced view" of *Trados* is that it

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168. *See infra* text accompanying notes 206–207 (discussing financing challenges faced by startups and the practice of staging investments).

169. *See supra* note 167 (citing to interviewee statements referencing investigation of financing sources).

170. Interview with Lawyer #4, at 2 (recognizing that you cannot force investors to continue financing the company); Interview with Lawyer #8, at 2 (discussing "objective factors" that the company is failing).

171. As discussed above, some interviewees take the position that *Trados* does not apply in circumstances where preferred holders also take substantial losses. *See infra* Part IV.C.1.

172. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17, 55–65 (Del. Ch. 2013) (describing the substantive and procedural aspects of fairness).

173. *See generally supra* Part II.B (summarizing the court's sharp criticisms of the Trados board).

174. *See* Interview with Lawyer #1, at 4 (discussing situations where preferred shareholders or note holders are asked to sacrifice some consideration to common holders); Interview with Lawyer #2, at 1 (stating that "a conversation about allocation of proceeds needs to happen" and that the common might be allocated proceeds if the company has value); Interview with Lawyer #6, at 1 (reporting that a board might allocate consideration to common in a "pure *Trados* case"); Interview with Lawyer #7, at 2 (indicating that a company might seek to "adjust the economics" if there is litigation risk under *Trados*); Interview with Lawyer #10 (describing an example of a deal in which an investor considered waiving liquidation preference in part due to *Trados*); Interview with Lawyer #16, at 2 (discussing an example of preferred shareholder waiving their liquidation preference); Interview with Lawyer #19, at 3 (discussing the possibility of allocating some consideration to common as part of the board sale process). *But see* Interview with Lawyer #15, at 3 (stating that the interviewee has never seen an allocation to common as a result of *Trados*).

175. *See* Interview with Lawyer #12, at 2 (indicating that giving up the liquidation preference altogether is required to remove the *Trados* conflict).

176. *See* Interview with Lawyer #8, at 1.

177. Interview with Lawyer #2, at 1.

makes preferred shareholders "overpay for negligible [common stock] value."[178] But still, these possible substantive effects on transaction terms suggest that *Trados* has inspired more than window-dressing procedure.

Whether common holders are allocated consideration appears to turn largely on litigation risk.[179] One interviewee reports that boards "give the common a slice" as an "insurance policy."[180] Another states that the amount paid to common holders is "a function of risk and cost."[181]

As with other topics above, one can question the degree to which *Trados* in particular drives these allocations to common holders. Researchers have observed such payments in periods prior to the case.[182] In addition, several interviewees describe these allocations as compensation for consent to the transaction rather than a product of fiduciary analysis. As described above, Silicon Valley acquirers often require a high percentage of common holders to approve a transaction, unrelated to *Trados.*[183] Common holders may need some incentive to respond to requests for approval.[184] Accordingly, *Trados* is probably best understood as operating "at the margins."[185]

5. The Beneficiary Question

As described in Part II, the *Trados* court confronted a contested doctrinal question: to whom are the board's fiduciary duties owed? In answering this question, the court considered three competing theories: common maximization, the control-contingent approach, and enterprise maximization.[186] Despite the court's apparent endorsement of common maximization, the interviewees do not coalesce around any of these alternatives and strike a less definite tone when discussing what I will call "the beneficiary question."

As an initial matter, interviewees do not agree on whether *Trados* altered common understandings of fiduciary duties. Several interviewees state that *Trados* is not a substantial departure from preceding caselaw but rather a reminder or amplification of existing concepts.[187] But others suggest that the case defied their understanding of the

178. Interview with Lawyer #5, at 4.

179. *See* Interview with Lawyer #5, at 3 (reporting that the shareholders' capacity to sue might affect the decision to allocate consideration to common); Interview with Lawyer #7, at 2 (associating allocation to common with litigation risk).

180. Interview with Lawyer #6, at 1.

181. Interview with Lawyer #4, at 2.

182. *See* Broughman & Fried, *supra* note 100, at 1348 (observing allocations to common in sample transactions from early 2003 and 2004).

183. *See supra* note 162 (discussing buyer approval requirements).

184. *See* Interview with Lawyer #2, at 2 (describing how buyers' approval requirements affect allocations to common); Interview with Lawyer #9, at 2 (reporting that the interviewee might consider an allocation to common in order to obtain the requisite shareholder approval); Interview with Lawyer #10, at 3 (citing a combination of buyer approval requirements and *Trados* as motivating a waiver of liquidation preference); Interview with Lawyer #11, at 2 (suggesting that allocations to common are motivated by buyers' high consent requirements); Interview with Lawyer #12, at 2 (suggesting that a company might "push some consideration to common" in order to get disinterested shareholder approval); Interview with Lawyer #14, at 2 (discussing how a company might "buy the common vote" by "cutting the common into the deal"); Interview with Lawyer #19, at 3 (discussing allocations to common as part of "horse trading" over common shareholder approval).

185. *See* Interview with Lawyer #4, at 1.

186. *See In re* Trados Inc. S'holders Litig., No. 1512-CC, 2009 WL 222958, at *40–41 (Del. Ch. July 24, 2009) (discussing the court's references to the three competing theories).

187. *See* Interview with Lawyer #1, at 5 (stating that *Trados* "was reaffirming the way that the duty of loyalty

board's obligations regarding preferred-common conflicts.[188]

Similar ambiguity surfaces when interviewees try to summarize their views of current fiduciary law. In some instances, tones of enterprise maximization emerge. For example, an interviewee summarizes the applicable standard as an obligation in "tough cases" to "maximize value of the enterprise."[189] In contrast, other interviewees hint at common maximization. One interviewee summarizes *Trados* as "preferencing the right[s]" of the common holders.[190] Another interviewee states that the case requires paying something to the common because "you deprived future potential upside however small that might be."[191]

Several interviewees perhaps suggest a fourth option in stating that the board owes a duty "to all shareholders."[192] This ambiguous phrasing might signal that a fiduciary's role is to mediate or reconcile competing interests of beneficiaries. Rather than choosing sides (as common maximization and control-contingent suggest) or ignoring the conflict (as enterprise maximization suggests), the fiduciary facilitates a negotiation and compromise.[193]

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should have been working"); Interview with Lawyer #4, at 1 (explaining that the case was consistent with established understandings between what was permissible at the board versus shareholder level); Interview with Lawyer #5, at 3 ("We always worried about *Trados* as a theoretical claim."); Interview with Lawyer #6, at 1 (explaining that "conservative lawyers" has always recommended a carve-out to common in *Trados* situations).

188. *See* Interview with Lawyer #8, at 2 (stating that the interviewee heard the "common-only" reading of *Trados* and "didn't accept" it); Interview with Lawyer #12, at 2 (reporting that *Trados* surprised people "a little bit" but is ultimately "common-sensical"); Interview with Lawyer #18, at 3 (reporting that *Trados* was "surprising"); Interview with Lawyer #19, at 2 (reporting that *Trados* "surprised me"); Interview with Lawyer #20, at 4 (reporting that *Trados* surprised the interviewee "a little").

189. Interview with Lawyer #6, at 2. *See also* Interview with Lawyer #4, at 2 (describing "a duty to all shareholders to get best value for the company, including the value of continuing" rather than treating the company as "your toy"); Interview with Lawyer #7, at 2 (summarizing the board's duty as "mak[ing] sure you get the best transaction" and that "it's better than continuing"); Interview with Lawyer #8, at 2 (asserting that preserving enterprise value is the "higher priority"); Interview with Lawyer #13, at 2 (agreeing with the concept of enterprise maximization); Interview with Lawyer #17, at 2 ("Most people like me assume that as long as you maximize value it probably satisfies fiduciary duties."); Interview with Lawyer #18, at 3 (arguing that the "enterprise view" is conceptually correct but recognizing that *Trados* endorsed common maximization); Interview with Lawyer #19, at 2 (describing the interviewee as "in the camp" of enterprise maximization but recognizing that *Trados* endorsed common maximization).

190. Interview with Lawyer #1, at 3.

191. Interview with Lawyer #5, at 2. *See also* Interview with Lawyer #10, at 2 (stating that board members understand they need to "do right by the common" and that preferred holders are not "the favorites of the courts"); Interview with Lawyer #14, at 3 (stating that the board's "[p]rimary duty is to the common"); Interview with Lawyer #18, at 3 (explaining that "you have to look at the preferred as a contract and your primary duty is to the common").

192. *See* Interview with Lawyer #6, at 2 (describing a duty to "all shareholders"); Interview with Lawyer #4, at 2 (using the "all shareholders" language); Interview with Lawyer #9, at 2 (stating that the directors "have a duty to all shareholders inclusive of common and preferred" and "have to consider the shareholders in general"); Interview with Lawyer #13, at 3 ("Are preferred not shareholders? If you don't think of them as shareholders, then don't call them shareholders."); Interview with Lawyer #15, at 2 ("You represent all shareholders, and even more so the common shareholders."); Interview with Lawyer #17, at 2 (stating that the board owes its duties to "all of the shareholders as a whole" and not just the common); Interview with Lawyer #19, at 2 (reporting that pre-*Trados* the interviewee would advise board members they had a duty to "all shareholders").

193. The interviewees' customary practice illustrates how such a standard might operate. A board might formulate a compromise of preferred and common interests by going forward with the transaction (to protect the preferred holder's preference) conditioned on an allocation to the common (in recognition of the loss of continuation value). *See supra* Part IV.C.4.

Amid these varied characterizations of fiduciary law what perhaps stands out most is a reluctance to reduce the board's obligations to any tidy formula. Interviewees reject the very specific outcomes mandated by the purest readings of the competing theories. They balk at the suggestion that a board must pursue long-shot chances of succeeding as a stand-alone company.[194] They also reject the idea that a preferred-controlled board has special license to act in the interest of preferred holders.[195] Instead, some advanced an indeterminant formulation: the board owes its duties to *all* shareholders.

It is hard to know what to make of the interviewees' haziness around common maximization and its theoretical alternatives. The beneficiary question has been the focal point of most academic treatment of the case.[196] Moreover, the court engaged with this academic debate and squarely endorsed common maximization in its opinion.[197] Yet, the interviewees disagreed on the applicable standard and whether it was changed by *Trados*.

In fairness, the court's discussion of the beneficiary question was not necessarily as conspicuous in the opinion as it has been in academic accounts. The court did react to framing by academics and viewed common maximization as the most useful phrasing on the facts of *Trados*. But as explained above, the decision is mostly in the narrative/normative style with almost platitudinal statements of general principle and sharp rebukes of particular conduct—particularly the defendants' efforts to "recharacterize their actions retrospectively" as common-regarding.[198] Though the court did recite a rule of common maximization, it did so in couched terms ("generally") and relegated competing rules to a single footnote.[199] Subsequent extrajudicial dialogue suggests (as of yet undefined) limits on the concept.[200]

Equally important, the customary practice emerging in the wake of *Trados* is basically responsive to the opinion, regardless of any conceptual ambiguity. Reacting to the court's

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194. *See* Interview with Lawyer #6, at 2 (disagreeing that duties run "to common more so" and stating that "you don't have to go for it on any chance"); Interview with Lawyer #7, at 2 (stating that it is "not practical" to assess and pursue low continuation value); Interview with Lawyer #8, at 2 (objecting to the idea that fiduciary duties require the board to "always run the thing into the ground"); Interview with Lawyer #11, at 2 ("I don't necessarily believe that you have to follow a path that likely leads to zero."); Interview with Lawyer #13, at 3 (objecting to the idea that the board should turn down a transaction if the preferred can get 95% of their preference and the chance of the common getting anything is "much less likely"); Interview with Lawyer #14, at 3 (stating that the board's duty to common "should not be taken to extremes").

195. *See* Interview with Lawyer #7, at 2 (stating that in "no situation" would the preferred have special license to favor the interests of the preferred); Interview with Lawyer #10, at 2 (reporting that the control-contingent approach is not how the interviewee explains fiduciary duties to the board); Interview with Lawyer #12, at 2 (reporting that a rule permitting the preferred-elected directors to act in the interest of the preferred holders is "for sure" not correct); Interview with Lawyer #13, at 2 (voicing strong disagreement with the assertion that preferred-elected directors can favor preferred holders); Interview with Lawyer #15, at 2 (stating that control-contingent is "definitely not" the fiduciary standard"); Interview with Lawyer #17, at 2 (stating that "no lawyer" thinks a preferred control board has special license to favor the preferred). According to one interviewee, "any corporate lawyer" would tell you that a fiduciary "wears a different hat" in the boardroom and that there is a "meaningful difference" between exercising a shareholder-level right and making a board decision. In other words, it is common understanding that if a party to a financing wants to control a decision then that needs to be specified in a shareholder-level agreement. Interview with Lawyer #4, at 2.

196. *See supra* Part II.D (discussing reactions by legal scholars).

197. *See supra* notes 33–34 and corresponding text (summarizing the court's treatment of the three alternative theories).

198. *See supra* Part II.B (describing the style of the opinion).

199. *Id.*

200. *See supra* text accompanying note 74 (discussing commentary by then-Chancellor Strine).

sharp criticism of the Trados sale process,[201] boards now more systematically consider common-continuation value and alternatives to sale.[202] The fact that this process sometimes results in payouts to common holders suggests that the procedural enhancements are more than cosmetic.[203]

In sum, transmission from court to board is not completely static free—the interviewees lack consensus on key aspects of doctrine and vary in their familiarity with the case. But the emerging customary practice does seem to be essentially responsive to the case.

V. IMPLICATIONS

This final Part explores key implications for *Trados* doctrine and broader Delaware jurisprudence. It starts by identifying an important theme in the interviews: Silicon Valley startups do not optimize for fiduciary duty law to the same extent as public companies. Specifically, startup boards are unlikely to rely on elaborate procedural mechanisms (valuation experts, independent board committees, and disinterested shareholder votes) to insulate themselves from litigation based on ambiguous fiduciary law. Against this background, I argue that Delaware should strive to concretize and right-size fiduciary law. I apply these insights to two ambiguities that surface in the interviews: what precisely triggers fairness review in the *Trados* fact pattern and what constitutes fair process in those circumstances?

A. What's Distinctive About Silicon Valley?

This Subpart explores foundational questions for a judiciary charged with regulating Silicon Valley startups. First, how attentive are startup boards to Delaware law? Second, how should the answer to that question affect Delaware jurisprudence?

1. Muted Judicial Influence

Commentators describe Delaware courts as being in dialogue with corporate managers.[204] But this metaphor suggests a certain intimacy or closeness with the audience. In fact, Delaware law may be more like a broadcast.[205] Instead of speaking directly with most managers, Delaware jurists make pronouncements that are edited, amplified, and distributed by intermediaries, such as lawyers. When judges communicate in this way, they do not know if their message will come through clearly or even if the target audience will tune in at all. The interviewees report that in Silicon Valley, as compared to other settings, the court's signal is not always strong and the audience is not always fully engaged.

The interviewees report that resource constraints frustrate efforts to implement Delaware caselaw. By design, startups are usually almost out of money. Their financing

201. *See supra* notes 51–53.

202. *See supra* Part IV.C.3.

203. *See supra* notes 174–178.

204. *See, e.g.*, William Savitt, *The Genius of the Modern Chancery System*, 2012 COLUM. BUS. L. REV. 570, 594 (describing "dialogue" between the court and corporate actors).

205. Edward Rock uses a similar metaphor in likening corporate law cases to "sermons." *See* Rock, *supra* note 15, at 1016 (referring to Delaware's "corporate law sermons"). Even the sermon metaphor, however, suggests a devoted audience. As described below, it is not clear that startup boards show up on Sunday.

options are limited because they frequently lack bankable assets or substantial revenues.[206] When venture capital funds invest, they do so incrementally through installments ("stages") conditioned on meeting development milestones.[207]

Interviewees relate how corporate governance has a cost that most startups cannot afford.[208] Startups have limited ability to recruit and compensate independent directors and to fund special committees.[209] The size of most private company deals may not justify the teams of advisors that have become customary in public company acquisitions.[210] Under these conditions, even the most expert and enthusiastic advice can only go so far in influencing client conduct. As one interviewee explains, "you can give all the legal advice, but practicalities control."[211]

Small deal size affects compliance in another, more subtle, way: it reduces the probability of litigation in the average case. Litigation risk is a significant element of client advice. Using *Trados* as an example, assessments of litigation risk influence the decision whether to allocate any consideration to common in response to *Trados* and whether to consider the case at all.[212] If plaintiffs' lawyers are not motivated by the damages from startup litigation in most cases, the views of the Delaware judiciary may ultimately figure less prominently in board deliberations as a matter of habit.[213]

In addition to resource constraints, Silicon Valley's distinctive capital structure may diminish the stature of Delaware fiduciary law for startups. Corporate law theory sometimes conceptualizes common shareholders as vulnerable outsiders.[214] With limited ability to influence corporate decision making, these outsiders may deserve special

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206. *See* Bartlett, *supra* note 6, at 263 (discussing the financing challenges facing startups).

207. *See id.* at 263–64 (describing the structure of venture capital financing); Darian M. Ibrahim, *The (Not So) Puzzling Behavior of Angel Investors*, 61 VAND. L. REV. 1405, 1411–13 (2008) (describing the practice of staging investments in venture-capital financings).

208. *See* Interview with Lawyer #10, at 3 (describing a "disconnect" between the amount of process required for a Delaware corporation and the amount available to most startups); Interview with Lawyer #11, at 2 (explaining that a company at the "unicorn stage" might pay for a legal memo regarding caselaw but that a "run of the mill startup won't pay for that"); Interview with Lawyer #15, at 2 (explaining that companies have sometimes raised relatively little institutional money and therefore have limited corporate governance).

209. *See* Interview with Lawyer #14, at 2 (stating that many sale transactions are not large enough to justify "fund[ing]" a special committee). *See also supra* notes 160–161 (describing the difficulty of recruiting independent directors to startups); *see* Bratton & Wachter, *supra* note 6, at 1888 ("The independent board regime was designed with public companies in mind, not startups unable to reach the IPO stage."); Pollman, *supra* note 6, at 56 ("Most participants in the startup lack independence by design.").

210. *See* Interview with Lawyer #18, at 3 (stating that a company facing a *Trados* transaction is unlikely to involve a banker or valuation expert); RONALD J. GILSON & BERNARD S. BLACK, THE LAW AND FINANCE OF CORPORATE ACQUISITIONS 1056 (2d ed. 1995) (asserting that fairness opinions have become common place in public company acquisitions as a result of Delaware caselaw).

211. Interview with Lawyer #18, at 4.

212. *See supra* Part IV.C.4 (discussing how litigation risk results in allocations to common); Part IV.C.1 (discussing how litigation risk influences the degree of attention *Trados* receives); Interview with Lawyer #8, at 2 (stating that there may not be much money in suing under a *Trados* claim); Interview with Lawyer #16, at 3 (reporting that a board will sometimes go ahead with a sale to which *Trados* might apply because there is little litigation risk).

213. *See* Interview with Lawyer #16, at 2 (explaining that public companies have "better process" because it is a more litigious environment).

214. *See* Jeffrey Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549, 1556–64 (1989) (summarizing and critiquing an "investor protection" rationale for mandatory fiduciary duties to shareholder). For an informative application of the investor protection rationale to startups, see Korsmo, *supra* note 6, at 1208–11.

protection through fiduciary duties.[215] Common shareholders, therefore, are the natural plaintiffs in fiduciary litigation.

But in Silicon Valley the founders and employees who hold the bulk of common shares are also holders of essential human capital.[216] Startup boards and potential acquirers generally want "the team" and are sensitive to founder and employee incentives.[217] Even when the company is sold, continuing compensation arrangements are part of the deal for most common shareholders, and it is presumed that the vast majority of common shareholders will sign on to an exit.[218] This leaves the "cats and dogs"—estranged founders and former employees holding small stakes—as the potential plaintiffs.[219] Accordingly, a litigated common-preferred conflict is a "corner case."[220]

Even the structure of modern legal practice in Silicon Valley reflects, or perhaps contributes to, Delaware's diminished signal strength in the startup ecosystem. As described in Part III, the startup lawyers who design a company's governance apparatus and guide the board through most exits defer to other specialists for deep understanding of Delaware fiduciary law.[221] To be clear, these startup lawyers are familiar with *Trados* and do discuss fiduciary law with their clients.[222] But they also describe caselaw as somewhat peripheral to their practice and focus their attention on the financing conventions and other matters clients presumably value most.[223]

Putting it all together, we might place Silicon Valley in the middle of a continuum of judicial signal strength. At one end are highly responsive public companies, under constant threat of litigation and represented by specialists in Delaware jurisprudence.[224] At the opposite end, we might place small businesses or individuals who use Delaware entities only intermittently.[225] Silicon Valley might fall somewhere in between. Startup lawyers and their clients regularly engage with routine aspects of Delaware corporate law and also know and consider seminal cases like *Trados*. But a combination of resource constraints, litigation environment, and other considerations mean that startups are unlikely to optimize fully for fiduciary law.

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215. *See* Korsmo, *supra* note 6, at 1208–11.

216. *See* Pollman, *supra* note 6, at 34–37 (discussing the distinctive composition of the common shareholder base in startups).

217. *See supra* notes 124–126 and accompanying text.

218. *See id.*

219. *See supra* note 130 (explaining the term "cats and dogs" in reference to shareholders); *supra* notes 149–150 and accompanying text (describing the likely plaintiffs in a claim under *Trados*).

220. Interview with Lawyer #4, at 2.

221. *See supra* Part III.B (describing the practice focus of the interviewees).

222. *See supra* Part IV.A (reporting that the interviewees are familiar with *Trados*).

223. *See supra* Part III.B (discussing Delaware law and M&A specialists).

224. *See* Ronald J. Gilson, *The Fine Art of Judging: William T. Allen*, 22 DEL. J. CORP. L. 914, 915–18 (1997) (describing transactional lawyers and their clients as highly responsive to Delaware law in the context of public company mergers); Savitt, *supra* note 204, at 574 (discussing the high rate of litigation challenging public company mergers) (citing Matthew D. Cain & Steven M. Davidoff, Takeover Litigation in 2011, at 2 (Feb. 2, 2012) (unpublished manuscript), *available at* http:// ssrn.com/abstract=1998482).

225. Those parties might face resource constraints more severe than startups and might use lawyers who infrequently study entity law because their practice is less specialized or is specialized in areas where entity law is a minor aspect of the overall representation. For example, Delaware limited liability companies ("LLCs") are used in a wide variety of contexts. *See* Peter Molk, *Protecting LLC Owners While Preserving LLC Flexibility*, 51 U.C. DAVIS L. REV. 2129, 2141–46 (2018) (observing that LLC investors and their attorneys exhibit varying levels of sophistication).

2. Implications for Delaware Jurisprudence

If one accepts this account of moderate judicial influence, how should it affect Delaware jurisprudence? In this Subpart, I argue for (1) more clarity in defining the parameters of fairness review and (2) judicial guidance rooted in the practicalities of customary practice rather than comparison to public company standards.

To lay the groundwork for these recommendations, first consider some basic features of Delaware corporate law. Broadly, the court faces a tradeoff between preventing corporate mismanagement through judicial scrutiny and mitigating litigation abuse through judicial deference to boards.[226] Features of corporate litigation make it especially susceptible to litigation abuse,[227] so courts try to condition judicial intervention on strong indicia of managerial abuse, such as clear conflicts of interest.[228] Only claims that feature these hallmarks of managerial misconduct survive motion to dismiss and proceed to discovery. Other claims are subject to the business judgment rule and never see the light of day.[229]

Within this general framework, the court is forced to make other tradeoffs. For example, the court can announce bright-line rules that give corporate managers clear guidance on how to avoid or survive judicial scrutiny (and give plaintiff's lawyers clear guidance on which claims to not bother bringing). But such clear definition might also provide managers and their counsel a roadmap to evade regulation through contrived (but technically compliant) actions. Delaware courts might intentionally retain some ambiguity—good faith and the like—as an entry point for policing this kind of sham compliance.[230] Because of this delicate balance between specificity and vagueness, one prominent jurist describes judicial lawmaking as a primarily "artistic enterprise."[231]

In the context of these difficult tradeoffs, one can see why the court emphasizes procedural cleansing in its broader jurisprudence. In recent decades, Delaware courts have reiterated that approval of independent board committees or disinterested shareholders provides a "path back" to the business judgment rule.[232] A board's attempt at procedural cleansing does not remove all ambiguity from the court's analysis—it still must assess independence, disinterestedness, and other procedural issues. But courts are relatively comfortable with these squarely procedural questions,[233] allowing dismissal of many

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226. Cable, *supra* note 22, at 90–95 (discussing the function of the business judgment rule and fairness review).

227. *See id.* at 92–93.

228. *Id.* at 90–91.

229. *See id.* at 90–92 (describing how standards of review affect pre-trial motions).

230. *See* Allen, *supra* note 56, at 898 (asserting that bright-line rules carry a "risk that agents—such as corporate management—might deploy such well-defined rules cleverly (and technically correctly), but with the purpose in mind not to advance long-term interests of investors, but to pursue some different purpose"); Fisch, *supra* note 56, at 1081–85 (asserting that under-inclusive rules will be "easy to avoid through careful planning").

231. Allen, *supra* note 56, at 898.

232. D. Gordon Smith, *The Modern Business Judgment Rule*, *in* RESEARCH HANDBOOK ON MERGERS AND ACQUISITIONS 83, 84 (Claire A. Hill & Steven Davidoff Solomon eds., 2016); *see also* Robert B. Little & Joseph A. Orien, *Determining the Likely Standard of Review in Delaware M&A Transactions*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Apr. 28, 2017), https://corpgov.law.harvard.edu/2017/04/28/determining-the-likely-standard-of-review-in-delaware-ma-transactions-2 (describing the standards of review, and the steps necessary to obtain the benefit of the business judgement rule, in various transactional contexts).

233. *See* Allen, *supra* note 56, at 900–01 (reporting a relatively high degree of confidence in advising

claims before they accrue substantial hold-up value. Where corporate boards have capacity to take full advantage of this procedural self-help, the court can leave fiduciary principles more open-ended without leaving the door wide open for litigation abuse.

This Article suggests the need for a different balance point in Silicon Valley. Board composition, capital structure, economic reality, and resulting habit conspire against procedural cleansing.[234] Boards do confer with counsel and do what they can to spruce up process in the moment,[235] but they are often willing to roll the dice on fairness review.[236] The court, in essence, loses an ally in mitigating the cost of ambiguous fiduciary law.

In this circumstance, the court should be cautious about its customary vagueness. In particular, it should be as clear as possible regarding what precisely triggers fairness. The point of this move towards clarity is not necessarily to influence corporate managers—after all, they are not as responsive as they could be here. Instead, the primary purpose of increased clarity is to send a signal to the court's other target audience: *the plaintiff's bar*. Even the court's dictum could go a long way in identifying the claims not worth bringing in the first instance.[237]

That is not to say that the court should give up altogether on providing guidance to boards. After all, the court's sharpest criticisms in *Trados* got through to the Silicon Valley corporate community and incrementally improved board process.[238] But the court should be aware of its moderate influence and focus on identifying achievable hallmarks of fair process. If Delaware is going to influence startup boards, it will have to be through right-sized recommendations.[239] One way to develop achievable guidance is to root it in existing practices.

Of course, one might fairly ask why the responsiveness of Silicon Valley should be of particular concern to the Delaware judiciary. If startup boards do not prioritize Delaware caselaw and are willing to stomach the resulting litigation costs, why should Delaware courts bend over backwards for startup boards?

Most basically, Delaware courts have demonstrated that they *do* care. Their opinions reflect an interest in understanding how distinctive features of the Silicon Valley business environment affect application of Delaware law.[240] Phrased in more instrumental terms, Delaware courts have an interest in preserving their dominant position in the competition for corporate charter business. While Delaware entities now predominate in Silicon Valley,[241] it is hard to believe based on these interviews that entrepreneurs or venture

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corporate actors how a special committee should operate).

234. *See supra* Part V.A.1 (discussing the muted impact of judicial pronouncements in Silicon Valley and the infrequency of procedural cleansing).

235. *See supra* Part IV.C.3 (discussing how *Trados* affects board deliberations).

236. *See supra* notes 160–161 (reporting that procedural cleansing is often impractical).

237. *Cf.* Savitt, *supra* note 204, at 576–77 (discussing caselaw regarding attorney's fees and what it "signals" to the plaintiffs' bar); Matthew D. Cain et al., *The Shifting Tides of Merger Litigation*, 71 VAND. L. REV. 603, 619–30 (2018) (describing how litigation patterns were affected by recent Delaware case law and other legal reforms).

238. *See supra* Part IV.C (discussing the moderate impact of *Trados* on board process).

239. *See* Pollman, *supra* note 6, at 56 ("Traditional notions of 'fair process' and 'fair dealing' should adjust to calibrate expectations to the startup environment.").

240. *See supra* text accompanying notes 43–49 (describing the *Trados* court's attentiveness to features of Silicon Valley).

241. *See* Brian Broughman et al., *Delaware Law as Lingua Franca: Theory and Evidence*, 57 J.L. & ECON. 865, 872 (2014) (finding that most companies in a dataset of venture-capital backed startups were incorporated

capital funds view Delaware entities as indispensable. Nuisance suits are a cost that may justify switching costs at some level.

Finally, it is important to note that this is not a recommendation for a relaxation of substantive law. There may be reasons to subsidize the innovation economy, but lowering the standards for management integrity seems an ill-conceived approach. The point of this analysis is to highlight that ambiguity has a different cost in the distinctive milieu of Silicon Valley, which may justify paying additional attention to the boundaries of emerging caselaw.

B. Application to Trados

Having identified these guiding principles, what does it all mean for *Trados*? This Subpart addresses that question by sketching out what tightly prescribed fairness review and achievable board process would look like in a disappointing sale of a startup.

Importantly, these suggestions are grounded in the interviewees' customary practice. They respond to ambiguities that surfaced in the interviews, and they incorporate customary board procedure described by the interviewees. Existing practices, of course, will not always align with the court's expectations—sometimes the court plays a formative role in establishing norms. But existing practice can still be a useful *starting point* in the court's efforts to guide directors and their advisors. Practically, the court can know that such guidance is achievable. Normatively, guidance grounded in customary practice has majoritarian credentials.[242]

To better situate the discussion, consider a hypothetical startup (Startup A) that produces and sells a home electronics device. The company hires a talented team, completes product development and beta testing, and begins selling the product. The sales environment is challenging because Apple just launched a similar product. Along the way, two venture capital funds pitch in $20 million and receive a liquidation preference in that amount. The company's six-person board consists of two founders, a CEO recruited through the investors' professional networks, a representative of each of the venture capital funds, and a technology company veteran mutually selected by the venture capital funds and the founders. The common shareholder base includes the founders, a syndicate of early angel investors who received common shares, and a former employee who exercised a stock option grant.

1. Tightening Trados *Triggers*

As a practical matter, many interviewees adopt a broad reading of *Trados*—perceiving litigation risk whenever preferred shareholders receive disproportionate

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in Delaware).

242. The view that corporate law should and does consist of majoritarian defaults is sometimes referred to as a "contractarian" approach. For a comprehensive analysis of the contractarian approach and its various sub-species, see Henry N. Butler & Larry E. Ribstein, *Opting Out of Fiduciary Duties: A Response to the Anti-Contractarians*, 65 WASH. L. REV. 1 (1990). The contractarian approach was heavily debated in a symposium issue in the *Columbia Law Review* featuring a number of corporate law scholars. *See generally* Lucian Arye Bebchuck, *The Debate on Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395 (1989) (discussing symposium contributions by Frank Easterbrook & Daniel Fischel, Melvin Eisenberg, Jeffrey Gordon, John Coffee, Robert Clark, Lewis Kornhauser, Ralph Winter, Fred McChesney, Roberta Romano, Jonathan Macey, Anthony Kronman, and Oliver Hart).

consideration because of a liquidation preference.[243] Yet, several interviewees express concern that this approach is too quick to find conflict as an empirical and conceptual matter. They note that companies fail hard and frequently in Silicon Valley, and it is a bad day for all involved when preferred holders get pennies (or a few dimes) on the dollar. Like some commentators,[244] some interviewees perceive meaningful preferred-common conflict only in narrower circumstances where preferred holders receive most of their liquidation preference and, therefore, have more to lose by continuing.[245]

Returning to hypothetical Startup A, assume that Amazon offers to buy the company (in a play for its technology and talent) for $5 million, resulting in a $5 million payout of liquidation preference to preferred holders and no payout to common holders. The sale proceeds might be enough to motivate a disappointed angel investor or former employee to threaten litigation and make a grab for hold-up value. But is salvaging $5 million on a $20 million investment enough to motivate the VC-affiliated directors to forego meaningful prospects for a turnaround?[246] What if the offer is just $2.5 million?

The court should address the ambiguity surrounding what precisely triggers fairness review under *Trados*. Even if Delaware jurists strategically prefer "mushy" principles over algorithmic rules,[247] articulating some limits on the scope of *Trados* would be helpful. In other areas, Delaware courts have provided illustrative parameters without forfeiting the possibility of revisiting the issue based on the totality of circumstances.[248]

As a start, the court could demarcate some level of investor loss that puts the sale outside of *Trados*. The guidance could identify a presumptive threshold (for example: "ordinarily *Trados* will not apply where the preferred receives less than 25% of its liquidation preference")[249] and also provide examples of factors that can override the presumption (for example: "except where the company has sufficient operating capital to

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243. *See supra* Part IV.C.1 (reporting the interviewees' view of when *Trados* applies).

244. *See* Bratton & Wachter, *supra* note 6, at 1875–76 (associating common-preferred conflicts with the "moderate downside" and asserting that at the "extreme downside" things are "markedly easier" because "there are no allocational issues worth pressing"). In previous scholarship, I suggested an even narrower reading by emphasizing that *Trados* had some especially bad facts for the defendants in the form of testimony by one director admitting that he lost interest in the company and wanted to shut it down to turn his attention to more promising projects. Cable, *supra* note 22, at 73–77 (identifying a novel "opportunity-cost conflict" in the *Trados* fact pattern and the court's reasoning). I put that interpretation aside for purposes of this Article because it did not appear in the interviews.

245. *See supra* text accompanying notes 143–147.

246. The conventional wisdom has been that liquidation preferences are valuable to venture capital funds because of the incentives they create for entrepreneurs (discouraging underwhelming exits) and their role in mitigating information asymmetry. *See* Abraham J.B. Cable, *Fending for Themselves: Why Securities Regulations Should Encourage Angel Groups*, 13 U. PA. J. BUS. L. 107, 124–25 (2010) (discussing how liquidation preferences allow entrepreneurs to signal their confidence in achieving larger exits). Investment returns appear to be driven predominately by a small number of large exits, rather than the amount of liquidation preference from more modest exits. *See* Cable, *supra* note 144, at 228–33 (discussing why venture capital investors pursue "high-risk, high-reward exits").

247. *See supra* Part II.B (describing the Delaware judiciary's normative/narrative style).

248. For example, courts have provided guidance on what constitutes an acceptable break-up fee in a merger agreement by specifying a range (based on percentage of deal value) that will "generally" be acceptable. *See* McMillan v. Intercargo Corp., 768 A.2d 492, 505 (Del. Ch. 2000). Specifying this generally acceptable range, however, does not preclude the court from also interrogating other factors such as the structure of the fee. *See id.*

249. As a reference point, one interviewee suggests that *Trados* would be a significant concern if a merger results in recovery of 80% of the liquidation preference, but would not be a major topic of conversation with the board if the preferred received only 2% of the liquidation preference. *See* Interview with Lawyer #13, at 2.

execute an articulated plan for a turnaround").

Though this is a modest suggestion, it is an important one for striking the correct balance between policing managerial misconduct and preventing litigation abuse. The stakes are high when defining the parameters of fairness review because permitting such judicial scrutiny imbues even meritless claims with holdup value.[250]

2. Fair Process Informed by Customary Process

Having considered *when* fairness is triggered under *Trados*, the next question is *what* the case requires of a board. Can the customary practice described by the interviewees provide a roadmap for fair process?

Customary practice provides at least two insights. Most convincingly, qualitative assessment of the company's prospects, rather than formal valuation, should ordinarily be appropriate for startups. More tenuously, allocating consideration to common, rather than forgoing the merger, should be recognized as consistent with fair process in those hard cases where the prospects of a turnaround are nontrivial but still speculative.

a. Assessing Common-Continuation Value

Returning again to hypothetical Startup A, assume Amazon values the company's technology and workforce more highly and offers $18 million in a merger transaction (against the $20 million liquidation preference). At these numbers, we are more squarely in the moderate-downside fact pattern, where preferred holders are arguably incentivized to protect the liquidation preference and push for a sale. Assume further that company counsel is skeptical that the transaction can be cleansed by an independent board committee because there may not be even one independent director—the founders will likely receive compensation packages from Amazon and the CEO and industry expert are potentially beholden to the venture capital funds. Disinterested shareholder approval is likely a nonstarter based on these facts. Assuming the founders do not qualify because of their compensation packages, the angel investors and former employee have no motivation to be responsive. What should we expect of the board in these circumstances? How should the board evaluate whether zero dollars is a fair outcome for the common, chief beneficiaries of the board's fiduciary duties under a rule of common maximization?

At least one Delaware jurist asserts there will be instances where wringing out value for the common constitutes unnecessary "casino-like gambling."[251] Because the pure logic of common maximization does not reveal any obvious boundaries,[252] it is up to the court to explain how a board can legitimately determine that common-continuation value is so speculative that it may be disregarded in approving a merger.

One possibility, discussed by the *Trados* court, is for the board to obtain a fairness opinion that applies a variety of recognized valuation methods to show zero or near-zero value for the common stock.[253] Such valuations are ubiquitous in public company mergers.[254]

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250. *See* Cable, *supra* note 22, at 90–92 (discussing the effect of standards of review upon pretrial motions).

251. Strine, *supra* note 6, at 2038.

252. *See supra* note 68 (summarizing responses to common-maximization in legal scholarship).

253. *See In re* Trados Inc. S'holder Litig., 73 A.3d 17, 65 (Del. Ch. 2013) (considering the board's decision to forego a fairness opinion).

254. *See* Steven M. Davidoff, *Fairness Opinions*, 55 AM. U. L. REV. 1557, 1563–73 (2006) (discussing the

On the facts of *Trados*, there may have been valid reasons why the court criticized the Trados board for failing to obtain a fairness opinion. Trados was not your average startup. It was a "roll-up" (combination) of several established businesses.[255] It had a long operating history,[256] a stable business,[257] and cash in the bank.[258] It was selling for a proposed $60 million—a significant (though disappointing) amount for the early 2000s market.[259] In the court's view, Trados had plateaued rather than failed.[260] It was a circumstance where the company may have had the resources to invest in a respectable fairness opinion and sufficient operating history to provide useful inputs for a valuation. Apparently, even the acquirer subscribed to this view and pushed unsuccessfully for a fairness opinion.[261]

But in the ordinary case, boards are not faced with a choice between sale and pivot. Interviewees report that boards often choose between sale and dissolution.[262] In this more ordinary context, it is easier to understand why fairness opinions are the exception and not the rule. The cost may be disproportionate and the value questionable.[263]

In this environment, boards consider common-continuation value in a more qualitative way, rooted in the specifics of the startup business environment. They consider indicia of company failure: defecting employees, waning demand for the company's products, lack of alternative exit transactions, depleted cash, and a lack of additional financing sources.[264] Among these factors, one can imagine a lack of financing sources being a deciding factor in many cases. It takes cash to accomplish a turnaround, and current investors cannot be forced to continue funding.

The next time the court re-visits the *Trados* fact pattern, it should articulate what fair process might mean in the ordinary case. The interviewees' description of a qualitative

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prevalence of fairness opinions following the Delaware Supreme Court's decision in *Smith v. Van Gorkom*).

255. *See In re Trados*, 73 A.3d at 23 (describing Trados's history of acquisitions).

256. *See id.* at 21 ("At the time, Trados differed significantly from the stereotypical dot-com startup. Trados had been around for sixteen years and sold a successful desktop product.").

257. *See id.* (describing Trados's business strategy and results).

258. *See id.* at 32 ("Trados achieved an operating profit of $165,000, and its cash balance exceeded $5 million, beating budget.").

259. The average size of exit transaction for a venture-capital backed company has increased substantially in recent years. The median size of exit was $43.7 million in 2004 and reached $90 million by 2016. *See* NVCA YEARBOOK, *supra* note 81.

260. *See In re Trados*, 73 A.3d at 65, 67 ("Contrary to the defendants' exaggerated trial testimony, the Company was not headed for a cliff, and there was a realistic possibility that it could self-fund its business plan.").

261. *See id.* at 65.

262. *See supra* text accompanying note 146.

263. Commentators have questioned the reliability of fairness opinions and the weight they are given by Delaware courts in cases concerning public company acquisitions. *See* Davidoff, *supra* note 254, at 1573–78, 1606–11 (discussing the subjectivity of fairness opinions and summarizing critiques of fairness opinions by other commentators). There are reasons to be even more skeptical of the reliability of fairness opinions for acquisitions of startups. Fairness opinions are frequently based on discounted cash flow analysis based on future projections. *See id.* at 1574–76. Future projections are likely to be especially speculative for an emerging technology or product. Other frequently used valuation techniques, such as analysis of comparable companies and control premiums, are based on stock price information of the target company or comparable businesses. *See id.* This stock price information is not available for a startup and may not be available for its competitors.

264. *See supra* notes 167–171 (discussing factors that boards consider in evaluating common-continuation value). *See also* Interview with Lawyer #19, at 3 (stating that a board can sell a company under *Trados* if it has talked to diverse funding sources, pursued different strategic directions, and talked to strategic partners without success).

assessment, grounded in the world of startups, can serve as the starting point.

b. Endorsing Allocations to Common?

What the board should do when there *are* legitimate, though speculative, prospects for a turnaround is perhaps the most conceptually difficult question. Interviewees suggest one possibility—allocating consideration to common and completing the merger. Whether this element of customary practice should be considered fair dealing, in light of the court's endorsement of common maximization, is not such an easy question. Perhaps the most we can say is that the practice is weakly indicative of fair dealing.

Return one more time to hypothetical Startup A. Assume that the board undertakes a qualitative assessment of common-continuation value in accordance with Subpart V.B.2.a above. That assessment reveals that the company has enough cash to continue operating for six months; if it does not sell to Amazon, there is still a chance it can enter into a strategic partnership with Amazon to access better distribution channels; and Apple has botched its product launch. In short, there is a plausible but improbable path forward to creating value for common shareholders.

Commentary to date might imply that common maximization compels the board to decline the merger and attempt the turnaround. For example, commentators have described the board as facing a decision between accepting the merger or "continuing" the firm.[265]

But that does not appear to be customary practice. Instead, the interviewees report that boards more likely arrange allocations to common by negotiating with the preferred holders to concede some liquidation preference.[266] The merger happens, but at a cost to preferred holders. In the hypothetical above, for example, the board might approve the merger, but conditioned on the preferred shares waiving enough of their preference to allocate $500,000 to common shareholders.

If the merger is challenged by the disgruntled common shareholders, what should a court make of this allocation to common? Is it meaningful evidence of fair process?

In theory, common shareholders should be indifferent as to whether the company actually continues or just pays out the expected value of continuation. It may even be that the typical holder of common stock in a startup—a founder or employee with significant human capital wrapped up in a single company—would favor the immediate payout compared to the risk of continuing.[267] From this perspective, allocations to common are consistent with common maximization if they reasonably approximate common-continuation value.

But, practically speaking, allocating to common and continuing with the merger feels like a concession to the preferred holders. A case that reaches the court will likely not involve actual bargaining by the affected common holders themselves (a shareholder who directly negotiates a payment will presumably sign away his or her claims). Instead, a conflicted board calculates and negotiates the payout on behalf of the common stock. They

265. *E.g.*, Bartlett, *supra* note 6, at 295 (describing a "dilemma of whether to continue or liquidate a struggling firm"); Bratton & Wachter, *supra* note 6, at 1888 (describing the board's decision as a choice between immediate sale and "delay"); Cable, *supra* note 22, at 62–77 (comparing expected values of accepting a merger and attempting a turnaround).

266. *See supra* Part IV.C.4 (describing allocations to common).

267. Matthew Wansley, *Beach Money Exits*, 45 J. CORP. L. (forthcoming 2019) at 19–23 (identifying reasons why founders and employees might favor exits that venture-capital investors view as insufficient).

likely do so without benefit of an expert valuation or in circumstances where such valuations may be unreliable.[268] Common holders might rightfully be skeptical that the payout equals the expected value of a turnaround.

One might even argue that the customary practice is inconsistent with common maximization because it is no better than a compromise of common and preferred interests. The preferred holders do not get their full liquidation preference. The common holders do not get to see the project through. Instead, the board arguably eschews common maximization and tries to fulfill fiduciary duties to *all shareholders*—the favored phrasing of some interviewees when asked about the beneficiary question. Corporate law theorists have sometimes ascribed such a mediating role to corporate boards, but not without controversy.[269]

As long as the court is committed to common maximization, an allocation to common may be only weakly indicative of fair process. Without some concrete analysis that the value approximates common-continuation value (an analysis that will often be missing), such an allocation is only rough justice. But still, it is a concession by the preferred, in the form of foregone liquidation preference, and a benefit to common beyond their baseline entitlement. And it is a solution to a difficult circumstance—a high-risk business venture that is failing to meet initial lofty expectations—that appears to fall within Silicon Valley norms. Even in the context of rigorous fairness review, boards need some room to navigate this thorny end of a company's lifecycle.

VI. CONCLUSION

By incorporating in Delaware, Silicon Valley entrepreneurs subject themselves to a distant regulator. At some level, it is a surprising pairing of a famously maverick business

268. *See supra* notes 263–264 and accompanying text (describing fairness opinions as rare in startup exits).

269. *See generally* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999) (arguing that a board of directors serves as a "mediating hierarchy" to solve incentive problems associated with team production). *But see* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 601–05 (2003) (critiquing Blair and Stout's formulation due to the agency costs that might arise when purporting to serve a variety of constituencies); David Millon, *New Game Plan or Business as Usual? A Critique of the Team Production Model of Corporate Law*, 86 VA. L. REV. 1001 (2000) (critiquing Blair and Stout's formulation on descriptive and normative grounds). The practice also bears some resemblance to bargaining models of the board advanced by other corporate law scholars. According to these models, parties to venture capital financings overcome incomplete contracting problems by vesting control in a board that engages in intra-board renegotiations as more information emerges. *See generally* Bartlett, *supra* note 6; Brian J. Broughman, *The Role of Independent Directors in Startup Firms*, 2010 UTAH L. REV. 461 (2010). In these bargaining models, however, it is envisioned that the board members will, within limits, be permitted to advance the interests of a particular constituency that designated that director to the board (e.g., investors or founders). *See* Bartlett, *supra* note 6, at 260 (presenting a model in which "directors might bargain to maximize cash flows to a particular constituency (e.g., a preferred stockholder or common stockholders)" while owing "an ultimate duty to maximize the value of the firm"). In contrast, the customary practice described by the interviewees contemplates a uniform obligation for all directors and a facilitating role as opposed to actual intra-board bargaining.

community[270] with a court that traces its roots to ancient fiduciary principles.[271] Its success hinges on the lawyers who counsel entrepreneurs through key points in a startup's lifecycle. The challenge for courts and researchers studying the efficacy of caselaw is that this counseling moment takes place in private and leaves little record. This case study tries to shed light on this crucial moment of implementation. It shows how the court's message can get through loudly, if not entirely clearly, and it offers suggestions for improving signal strength in this distinctive environment.

270. *C.f.*, Elizabeth Pollman & Jordan M. Barry, *Regulating Entrepreneurship*, 90 SO. CAL. L. REV. 383, 398 (2017) (identifying startups that take advantage of legal grey areas and "beg forgiveness" rather than "ask[ing] for permission"); Abraham J.B. Cable, *Institutional Disruption: The Rise of the Reformer Startup*, 12 HASTINGS BUS. J. 1, 11 (2015) (discussing the startup ecosystem as "an institution that enables long-shot efforts to unseat incumbents"); Herment Taneja, *The Era of "Move Fast and Break Things" Is Over*, HARV. BUS. REV. (Jan. 22, 2019) ("Many of today's entrepreneurs live by Facebook founder Mark Zuckerberg's now-famous motto: 'Move fast and break things.'").

271. *See* William T. Quillen & Michael Hanrahan, *A Short History of the Delaware Court of Chancery—1792-1992*, 18 DEL. J. CORP. L. 819 (1993).