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Quinn Emanuel Private Equity Litigation Practice Alert

Settlement of First Delaware PE Busted Deal Case on Eve of Trial

In July 2020, Quinn Emanuel achieved a favorable settlement for its client Advent International in the first scheduled "Busted Deal" trial of the COVID-19 era. The week before trial, the parties reached a settlement in which Advent agreed to purchase Forescout, a leader in network access control, for $1.43 billion, a substantial reduction from the original deal size of $1.9 billion it had agreed to just five months earlier.

On February 6, 2020, Advent and Forescout finalized an agreement pursuant to which Advent would acquire all outstanding shares of Forescout common stock in an all-cash transaction valued at $1.9 billion. However, soon thereafter, Forescout announced that in the first quarter of 2020, it experienced an almost 25 percent decrease in year-over-year revenue growth and it missed street consensus earnings projections by more than 70 percent. It identified COVID-19 as the primary cause for its drastic underperformance.

Advent was shocked; it had reasonably expected that Forescout's business model could weather the shift to the work-from-home environment that became predominant as a result of the COVID-19 crisis, especially since many of Forescout's competitors in the cybersecurity industry thrived in the first quarter. As a result of Forescout's underperformance in the first quarter, Advent believed that the closing conditions for the deal had not been satisfied.

Three days before the scheduled May 18, 2020 closing of the merger of Advent's affiliate with and into Forescout, Advent announced that it would not consummate the deal. On May 19, Forescout sued for specific performance of the $1.9 billion transaction.

Advent had three reasons for backing out of the deal, each of which presented challenges:

The first reason was that Forescout's poor first-quarter performance constituted an MAE (Material Adverse Effect) under the parties' Merger Agreement. Establishing an MAE can be a difficult task and in fact there has been only one case in the history of Delaware Chancery Court declaring an MAE. More challenging still, the Agreement specifically excluded any downturns in performance caused by "pandemics" from constituting a Material Adverse Effect, unless the company was *disproportionately* impacted by the pandemic. Advent therefore had to show Forescout's dramatic downturn was *unique* among its peers.

The second reason was that Forescout had failed to operate the company as it would in the ordinary course, which it was obligated to do by the parties' Agreement. This presented novel interpretation challenges in light of the pandemic: what does it mean to operate in the "ordinary course" in light of a global pandemic, with shut-down orders and other government prohibitions? Courts are grappling with whether such a requirement should be evaluated in the context of a global pandemic, or in the context of the pre-pandemic world, a question that may turn on the specific wording of the ordinary course provision. And even if the measuring stick is how a company should operate in a global pandemic, courts are struggling with *how* to measure what a company should do during a pandemic, given COVID-19's unprecedented impact on the world.

The third reason Advent argued was that specific performance could not be awarded under the contract unless the debt financing contemplated by the Agreement was available, and that such financing was not available because Advent could not, in good faith, deliver a solvency certificate to the lenders. Advent had a good faith basis to believe that Advent could not shoulder the $400 million debt load necessary to consummate the transaction as written and therefore it refused to sign the solvency certificate. Forescout argued, however, that the deal was not contingent on financing and, in any event, Advent had an obligation to seek alternative financing for the transaction and if it refused to do so, Forescout should be permitted to line up alternative financing itself.

Compounding the complexity was an extremely expedited trial schedule for this $2-billion case. Two days after Advent was sued, and before it even filed an opposition, Delaware Vice Chancellor Glasscock set trial for the first week of June, giving Advent an unprecedented ***one week*** to take document, fact, and expert discovery, and prepare for trial. Through a stipulation of the parties, the trial setting was ultimately moved six weeks out to July 20th, 2020, a date chosen by the Chancery Court to permit it to render a decision before the August 6 debt financing "drop dead" date. Although that drop-dead date was arguably rendered moot as a result of a notice by the lenders that they would no longer be funding the debt, the Court declined to reschedule the trial, instead ordering the first ever full Zoom trial in Delaware Chancery Court history.

In the seven weeks leading up to the settlement, Quinn Emanuel took twenty-five depositions via Zoom, filed seven expert reports, filed two motions to compel, and, in partnership with co-counsel and local counsel, reviewed over 200,000 documents, all while simultaneously learning the case and preparing for trial.

On the eve of trial, Forescout agreed to a significantly reduced purchase price. Advent can now look forward to owning a company that develops and sells world-class cybersecurity products at a price more reflective of the actual state of the business and with a dramatically reduced debt load.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to reach out to:

Harvey Wolkoff
Email: harveywolkoff@quinnemanuel.com
Phone: +1 617-712-7108

Andrew Rossman
Email: andrewrossman@quinnemanuel.com
Phone: +1 212-849-7282

David Mader
Email: davidmader@quinnemanuel.com
Phone: +1 212-849-7148

Diane Cafferata
Email: dianecafferata@quinnemanuel.com
Phone: +1 213-443-3666