



CORPORATE UPDATE - When to Consider Using Special Committees in the Current Crisis

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In the current environment, many companies are considering transactions with related parties (including significant shareholders, management and their affiliated entities) that might benefit from the use of a special committee to ensure a robust process and increased protection from later scrutiny.

General considerations on when to form a special committee under Delaware law:

- A majority of the Board has an interest in the decision or transaction that differs from the stockholders in general
- There is concern that the Board will be viewed as controlled or dominated by an interested director
- Transaction at issue is one where the directors or a controlling stockholder “stands on both sides” of a transaction
- Controlling stockholder receives different consideration from that received by the other stockholders

Typical transactions that suggest special committee involvement:

- Going private or “freeze out” transactions with a significant stockholder
- Leveraged buyouts where management will have an interest in the surviving company
- Purchases or sales of securities or assets to or from significant stockholders or management
- Stockholder derivative litigation

Less common transactions prevalent in the current environment that may suggest special committee involvement:

- Dividend/distribution decisions (e.g., to end, reduce, continue or commence) where a controlling stockholder has a view that is at odds with the unaffiliated directors
- Financial restructurings where management will have an interest in the surviving company but public equity holders and subordinated debtholders will not
- Recapitalizations or debt exchanges where related parties or management receive different treatment
- Bridge financing or backstop arrangements provided by related parties
- Renegotiation or creation of commercial arrangements where an actual or potential conflict might exist
- Other transactions involving significant stockholders, management or their affiliated entities

However, in the absence of a conflicted transaction, we caution that special committee involvement may:

- Interfere with a company’s ability to transact quickly
- Be unnecessary where director recusal, independent director oversight or other more limited measures are sufficient
- Imply a conflict exists even where one does not, which may encourage additional scrutiny and litigation
- Threaten relationships and communication within the Board and with management
- Incur significant additional costs of separate financial and legal advisors

Whether the formation of a special committee is necessary or advisable is highly dependent on the facts and circumstances of the proposed transaction and parties.

Where special committee involvement is warranted and desired, Boards should consider empowering the committee early (e.g., before valuation discussions occur) including, if appropriate, authorizing them to hire independent counsel and an independent financial advisor, to avoid a tainted process and the loss of potentially valuable legal protections.

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