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Re: *Gaines v. Narachi, et al.*
C.A. No. 6784-VCN
Date Submitted: October 5, 2011

Dear Counsel:

The Plaintiff, a stockholder of AMAG Pharmaceuticals, Inc. ("AMAG"), has moved pursuant to Court of Chancery Rule 59(f) for reconsideration (or reargument) of a portion of this Court's September 30, 2011, letter opinion and

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order.¹ At issue is my conclusion that the Plaintiff failed to plead a colorable claim that the Joint Proxy/Prospectus (the “Proxy”)² suffered from a material omission related to its disclosure of the data underlying Morgan Stanley’s discounted cash flow (“DCF”) analysis. For the reasons set forth below, the Plaintiff’s motion for reargument is granted.

In connection with its assessment of the exchange ratio, AMAG’s directors engaged Morgan Stanley to provide a fairness opinion. As part of the basis of its fairness opinion, Morgan Stanley performed a DCF analysis to calculate the estimated equity values of AMAG and Allos Therapeutics, Inc. (“Allos”). As is normally the case, the DCF analysis was performed by discounting each company’s unlevered free cash flows, and “free cash flows” took on, essentially, the standard definition.³ The Proxy explains that “[f]or the purposes of the [DCF] analysis, Morgan Stanley used certain financial projections prepared by AMAG

¹ *Gaines v. Narachi*, C.A. No. 6784-VCN (Del. Ch. Sept. 30, 2011). A party moving for reargument must show that the “Court has overlooked a decision or principle of law that would have controlling effect or the Court has misapprehended the law or the facts so that the outcome of the decision would be affected.” *Miles, Inc. v. Cookson Am., Inc.*, 677 A.2d 505, 506 (Del. Ch. 1995).

² Letter to the Court from Stephen C. Norman, Esquire, dated Sept. 26, 2011, Ex. A (Proxy).

³ See Proxy at 74.

management, as well as certain adjustments thereto and extrapolations therefrom prepared with the guidance of AMAG management and which were approved for Morgan Stanley’s use by AMAG management.”⁴ Later, the Proxy discloses AMAG’s projected future revenue and earnings before income taxes (“EBIT”) under two scenarios, which, it explains, were “included” among the “projections provided to Morgan Stanley.”⁵ The forecasted free cash flows utilized by Morgan Stanley are not disclosed.

In advancing its argument that free cash flows must be disclosed, the Plaintiff relies primarily on three cases: *Maric Capital Master Fund, Ltd. v. Plato Learning, Inc.*,⁶ *David P. Simonetti Rollover IRA v. Margolis*,⁷ and *In re Netsmart Techs., Inc. S’holders Litig.*⁸ But these cases do not state a blanket rule that free cash flow estimates used in a DCF analysis must always be disclosed. In *Simonetti*, this Court found that the proxy in question met the standard of disclosing the substance of the investment banker’s work with regard to a DCF

⁴ *Id.*

⁵ *Id.* at 88.

⁶ 11 A.3d 1175 (Del. Ch. 2010).

⁷ 2008 WL 5048692 (Del. Ch. June 27, 2008).

⁸ 924 A.2d 171 (Del. Ch. 2007).

analysis⁹ when only revenue and EBITDA forecasts were disclosed.¹⁰

Additionally, in *Netsmart*, where the disclosures concerning the DCF analysis were found to be deficient,¹¹ the resulting Order of March 19, 2007, called for disclosure of revenue and earnings projections, but did not specifically require the disclosure of free cash flow numbers.

Furthermore, the rationale for requiring such robust disclosure of the detailed information used in performing a DCF analysis is muted in the instant case. All three of the cited cases emphasized the fact that the shareholder plaintiffs would be cashed out in the proposed mergers.¹² This is an important consideration in determining the level of disclosure required surrounding future cash flows because those shareholders were being asked to decide whether to take a sum certain at that time in exchange for their right to those future cash flows. Here, the

⁹ *Simonetti*, 2008 WL 5048692, at *10.

¹⁰ See *David P. Simonetti Rollover IRA v. Margolis*, C.A. No. 3694-VCN (Del. Ch.), Transmittal Aff. of Brian D. Long, Esquire, Ex. 1-a (Trizetto Group, Inc. Proxy Statement) 29.

¹¹ See *In re Netsmart Techs.*, 924 A.2d at 202-05.

¹² See *Maric*, 11 A.3d at 1178; *Simonetti*, 2008 WL 5048692, at *9; *In re Netsmart Techs.*, 924 A.2d at 203.

Plaintiff is not being cashed out and will remain entitled to a portion of AMAG's future cash flows.¹³

Nevertheless, the standard for expedition requires only that the "plaintiff has articulated a sufficiently colorable claim and shown a sufficient possibility of a threatened irreparable injury" to justify the additional costs of an expedited proceeding.¹⁴ Although the Proxy disclosed the EBIT projections—essentially a precursor to free cash flow—used by Morgan Stanley in its DCF analysis, the Proxy did not disclose the related free cash flow estimates. This Court has stated that shareholders who are being advised to cash out are entitled to the best estimate of the company's future cash flows.¹⁵ While application of this standard has not always resulted in a finding that free cash flows, specifically, must be disclosed, there is a colorable argument that, in this case, free cash flows should be disclosed to meet this standard. Indeed, in *Maric* this Court enjoined the proposed merger

¹³ AMAG's forecasted future cash flows may still be of interest to AMAG shareholders voting on the merger, though, since their stake in these cash flows will be diluted by the issuance of shares to acquire Allos. The question, of course, is whether in this context the additional information sought is merely helpful or actually material.

¹⁴ *Giammargo v. Snapple Beverage Corp.*, 1994 WL 672698, at *2 (Del. Ch. Nov. 15, 1994).

¹⁵ See *Maric*, 11 A.3d at 1178; *Simonetti*, 2008 WL 5048692, at *10; *In re Netsmart Techs.*, 924 A.2d at 203. While the AMAG shareholders are not being cashed out, there is a colorable argument that this standard should be applied in the instant case.

until free cash flow projections were disclosed,¹⁶ despite the fact that the proxy already disclosed projected revenues, EBIT, and a variation of EBITDA.¹⁷ Finally, it should be noted that from the record it is unclear whether AMAG management provided Morgan Stanley with free cash flow projections or if Morgan Stanley derived its free cash flow estimates from the disclosed EBIT projections.¹⁸ While the Plaintiff's argument might be stronger if management provided Morgan Stanley with free cash flow projections but then "excised" these numbers from the Proxy,¹⁹ this Court has previously contemplated requiring the disclosure of cash flow projections made by the investment bank advising the board,²⁰ and any rule stating that cash flow projections not provided by management never need to be disclosed could be abused in circumstances where such disclosure would be

¹⁶ *Maric*, 11 A.3d at 1178-79.

¹⁷ See *Maric Capital Master Fund, Ltd. v. Plato Learning, Inc.*, C.A. No. 5402-VCS (Del. Ch.), Transmittal Aff. of P. Bradford deLeeuw, Esquire, Tab 2 (PLATO Learning, Inc. Proxy Statement) 27.

¹⁸ Indeed, this question is a matter of a material dispute of fact between the Plaintiff and the Defendants. See Defs.' Opp'n to Pl.'s Mot. for Recons. ¶ 9. While the Plaintiff and Defendants are divided on this question, review of the documents provided to the Court to date suggests that the Defendants are correct, and AMAG management did not provide Morgan Stanley with free flow projections. See Defs.' Opp'n to Pl.'s Mot. for Recons., Ex. H. (Farmer Aff.) 1-2. Nonetheless, at the current stage of the proceedings, the Court is not engaged in fact finding, and must consider this a material dispute of fact.

¹⁹ See *Maric*, 11 A.3d at 1178.

²⁰ See *In re Netsmart Techs.*, 924 A.2d at 203.

necessary in order to provide adequate information to shareholders. In conclusion, the Plaintiff has pled a colorable claim that the Proxy's omission of the free cash flow projections utilized by Morgan Stanley is a material omission that raises a threat of irreparable injury.²¹

* * *

This conclusion requires the Court to consider the Defendants' argument that the Plaintiff's application for interim injunctive relief is barred by laches. Given the nature of the claim that the Plaintiff is asserting and the work that already has been done on this claim in the context of the motion to expedite, it is difficult to conclude that any prejudice will be suffered by the Defendants.²²

* * *

Accordingly, for the foregoing reasons, the Plaintiff's Rule 59(f) motion is granted.

²¹ See, e.g., *Simonetti*, 2008 WL 5048692, at *13 ("a breach in the disclosure duty actually results in irreparable harm to the stockholders").

²² The doctrine of laches generally requires the establishment of three elements, one of which is "prejudice to the defendant." *Reed v. Spazio*, 970 A.2d 176, 182-83 (Del. 2009).

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Counsel are requested to confer on a means to supplement the current record as may be necessary and to set a schedule for the filing of memoranda on this limited issue. Argument on this disclosure claim will be heard at the same time as argument in the related *In re Allos Therapeutics, Inc. Shareholders Litigation*, Consolidated C.A. No. 6714-VCN, scheduled for October 17, 2011, at 10:00 a.m., in Dover.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-K