

Memorandum

Fourth Circuit: Proxy Statement Need Not Have Included Cash-Flow Projections Given the Array of Other Metrics

June 16, 2023

On June 1, 2023, the Fourth Circuit affirmed a district court’s grant of summary judgment in favor of the defendant bank holding company, which was alleged to have violated Section 14(a) of the Exchange Act by misleading shareholders about the true value of their shares ahead of a stock-for-stock merger. [*Karp v. First Conn. Bancorp*, 2023 U.S. App. LEXIS 13528 \(4th Cir. 2023\) \(Diaz, J.\)](#). Affirming the district court’s ruling, the Fourth Circuit held that no reasonable jury could find the omission from the proxy statement of certain cash-flow projections prepared by the defendant’s financial advisor was material. The Fourth Circuit also held that the district court properly granted summary judgment on loss causation grounds because plaintiff had failed to show that the omitted cash-flow projections caused the alleged damages.

Background

In 2018, defendant and another bank holding company proposed a merger in which defendant’s shareholders would receive 1.725 shares of the acquirer’s stock for each share of defendant company stock they held, reflecting an implied cash value of approximately \$32.33 per share. This represented a 24.3% premium over the stock’s closing price on the day the merger was announced. Defendant’s proxy statement summarized its financial advisor’s analyses and disclosed “a bevy of information, including projections of total assets, net assets, returns on average assets and tangible common equities, and earnings per common share.” Plaintiff alleged the proxy statement was materially misleading because it did not disclose the specific cash-flow figures used in the financial advisor’s discounted cash flow analysis. Plaintiff also alleged that the proxy statement was deficient because it did not disclose that in 2017, defendant’s financial advisor presented another set of “more optimistic” cash-flow projections to defendant’s board in connection with a different potential merger. Defendant’s shareholders voted to approve the 2018 merger. Plaintiff commenced a putative class action claiming that defendant’s failure to disclose the cash-flow projections—and in particular the more optimistic 2017 projections—led shareholders to undervalue their shares and approve the merger. Both parties moved for summary judgment, the district court denied plaintiff’s motion and granted the defendant’s.

No Reasonable Jury Could Find the Omission of the Cash-Flow Projections Material

On appeal, the Fourth Circuit agreed with the district court that there was no genuine dispute of material fact regarding any of the elements of plaintiff’s Section 14(a) claim. The court explained that “[t]o prevail in a private

cause of action asserting a violation of Section 14(a) . . . a plaintiff must show that (1) the proxy statement contained a material misrepresentation or omission (2) that caused the plaintiff injury and that (3) the proxy solicitation was an essential link in the accomplishment of the transaction.”

As to materiality, plaintiff argued that a reasonable investor would have found the omitted cash flow projections would have been material to a reasonable investor because they would have showed that the merger consideration was inadequate and that the financial advisor’s valuation was skewed. Rejecting this, the Fourth Circuit held that no reasonable jury could find the omission of the cash-flow projections material. The Fourth Circuit agreed with defendant that it was “not enough to speculate that shareholders might have found the projections helpful to the deliberations, so long as the merger proxy ‘provided a thorough and accurate summary’ of the financial advisor’s work.” The Fourth Circuit noted that, “as other courts have held, shareholders aren’t entitled to double-check every aspect of the advisor’s math so long as the proxy statement contains an adequate and fair statement of their work.”

Citing *Kuebler v. Vectren Corp.*, 13 F.4th 631 (7th Cir. 2021) (holding that cash-flow projections were immaterial as a matter of law given all the other information provided), the Fourth Circuit concluded that based on “the array of metrics in the proxy statement,” it was unlikely that the more optimistic cash-flow projections “would have significantly altered the total mix of information.” The court further pointed out that plaintiff did not testify that the cash-flow projections would have actually affected his vote, and did not remember whether or how he had voted on the merger, or what information he would have relied on.

No Genuine Issue of Material Fact Relevant to Loss Causation

The Fourth Circuit explained that in a private Section 14(a) action, a plaintiff must “prove that the defendant’s misrepresentation (or other fraudulent conduct) proximately caused the plaintiff’s economic loss.” *Dura Pharms. v. Broudo*, 544 U.S. 336 (2005); see 15 U.S.C. § 78u-4(b)(4). Defendant argued that plaintiff “must tie the misleading proxy statements directly to the economic harm by showing that omission of the projections prevented [the] shareholders from receiving \$35.51 per share for their stock.” The court agreed with defendant that plaintiff “failed to show that disclosure of the projections would have either (1) caused another buyer to pay more than \$32.33 per share, or (2) caused shareholders to reject the merger, and (in that case) that the share price on the day of the merger would have been \$35.51.”

The Fourth Circuit concluded that plaintiff’s evidence did not establish that he or any other shareholder suffered an economic loss because the proxy statement did not contain the cash-flow projections. The Fourth Circuit noted that defendant’s stock was trading at \$26 per share the day before the merger was announced, which was “well below the merger consideration of \$32.33.” Further, plaintiff did not suggest that the shareholders missed out on “a viable superior offer” by approving the merger, because there was only one offer and the acquirer was willing to walk away if defendant rejected its \$32.33 offer.

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