SUPERIOR COURT OF CALIFORNIA

COUNTY OF SANTA CLARA

STEPHEN BUSHANSKY, Individually and on behalf of all others similarly situated, Plaintiff, vs. ALLIANCE FIBER OPTICS PRODUCTS, INC., et al., Defendants.	Case No.: 16CV294245 **ORDER AFTER HEARING ON SEPTEMBER 29, 2017** **Preliminary Approval of Class Action Settlement**
RUDY LUCK, Individually and on behalf of all others similarly situated, Plaintiff, vs. ALLIANCE FIBER OPTICS PRODUCTS, INC., et al., Defendants.	Case No. 16CV294418

RICK DOERR, Individually and on behalf of all others similarly situated, Plaintiff, vs. PETER C. CHANG, et al., Defendants.	Case No. 16CV294681
BAHMAN KHAKI, Individually and on behalf of all others similarly situated, Plaintiff, vs. ALLIANCE FIBER OPTICS PRODUCTS, INC., et al., Defendants.	Case No. 16CV294833

The above-entitled matters came on regularly for hearing on Friday, September 29, 2017 at 9:00 a.m. in Department 1 (Complex Civil Litigation), the Honorable Brian C. Walsh presiding. The Court reviewed and considered the written submission of all parties and issued a tentative ruling on September 28, 2017. No party contested the tentative ruling and no party appeared; therefore, the Court orders that the tentative ruling be adopted and incorporated herein as the Order of the Court, as follows:

These related putative shareholder class actions arise from the sale of Alliance Fiber Optic Products, Inc. ("AFOP") to Corning Incorporated and its affiliates. Before the Court is plaintiffs' motion for preliminary approval of a settlement.

I. Factual and Procedural Background

Headquartered in Sunnyvale, California, AFOP is a Delaware corporation that produces fiber optic components and integrated modules for communications equipment. (First Amended Complaint in *Bushansky*, Case No. 16-CV-294245 ("FAC"), ¶¶ 2, 11.) On April 7, 2016, the company announced that it had entered into a merger agreement pursuant to which Corning would acquire all of the outstanding shares of its common stock for $18.50 per share, in a transaction valued at approximately $305 million. (*Id.* at ¶ 3.)

Plaintiffs allege that the transaction undervalued AFOP, with the sale price discounted nearly 14.9% from the company's 52-week high value of $22.35 per share on July 23, 2015. (FAC at ¶ 4.) They further allege that the individual defendants inappropriately agreed to "lock up" the transaction with deal protection devices, including a strict "no solicitation" provision, an "information rights" provision requiring the company to fully inform Corning of any competing offer within 48 hours, a "matching rights" provision allowing Corning four business days to match any alternative bid, a "no-waiver" provision restricting AFOP from modifying or waiving any material provision of any confidentiality or similar agreement to which it is a party, and a provision establishing a termination fee of $10.55 million. (*Id.* at ¶ 5.) Plaintiffs also allege that defendants failed to disclose material information to stockholders in the Schedule 14D-9 statement filed with the United States Securities and Exchange Commission on April 21, 2016. (*Id.* at ¶ 6.) Specifically, the statement omits and/or misrepresents material information concerning (1) the background of the proposed transaction, (2) the data and inputs underlying the financial valuation exercises supporting the fairness opinion provided by AFOP's financial advisor, Cowen and Company, LLC, and (3) the company's financial projections, relied on by Cowen. (*Ibid.*)

In April 2016, plaintiffs Stephen Bushansky and Rudy Luck filed suit against AFOP; individual defendants Peter C. Chang, Gwong-Yih Lee, James C. Yeh, Richard B. Black, and

Ray Sun; and Corning and its subsidiary, the Apricot Merger Company. In May 2016, plaintiff Bahman Khaki brought a complaint against the same defendants, and plaintiff Rick Doerr sued the individual defendants only. All four actions arise from the same general allegations described above and assert claims for breach of fiduciary duty and (with respect to Corning and Apricot) aiding and abetting breach of fiduciary duty.

The parties agreed to exchange expedited discovery and reached a non-monetary settlement on May 26, 2016, which included AFOP's agreement to provide supplemental disclosures in connection with the sale. The following day, AFOP filed these disclosures in Amendment No. 5 to its Schedule 14D-9. The shareholders voted to approve the sale on June 3, and on June 6, 2016, the merger was completed.

Plaintiffs now move for an order preliminarily approving the settlement, provisionally certifying the settlement class and appointing the class representatives, designating class counsel, approving the form and method for providing notice to the class, and scheduling a final fairness hearing.

I. Legal Standard for Approval of a Class Action Settlement

Generally, "questions whether a settlement was fair and reasonable, whether notice to the class was adequate, … and whether the attorney fee award was proper are matters addressed to the trial court's broad discretion." (*Wershba v. Apple Computer, Inc.* (2001) 91 Cal.App.4th 224, 234-235, citing *Dunk v. Ford Motor Co.* (1996) 48 Cal.App.4th 1794.)

> In determining whether a class settlement is fair, adequate and reasonable, the trial court should consider relevant factors, such as the strength of plaintiffs' case, the risk, expense, complexity and likely duration of further litigation, … the amount offered in settlement, the extent of discovery completed and the stage of the proceedings, the experience and views of counsel, the presence of a governmental participant, and the reaction of the class members to the proposed settlement.

(*Wershba v. Apple Computer, Inc., supra*, 91 Cal.App.4th at pp. 244-245, internal citations and quotations omitted.)

The list of factors is not exclusive and the court is free to engage in a balancing and weighing of factors depending on the circumstances of each case. (*Wershba v. Apple Computer, Inc., supra*, 91 Cal.App.4th at p. 245.) The court must examine the "proposed settlement agreement to the extent necessary to reach a reasoned judgment that the agreement is not the product of fraud or overreaching by, or collusion between, the negotiating parties, and that the settlement, taken as a whole, is fair, reasonable and adequate to all concerned." (*Ibid.*, quoting *Dunk v. Ford Motor Co., supra*, 48 Cal.App.4th at p. 1801, internal quotation marks omitted.)

> The burden is on the proponent of the settlement to show that it is fair and reasonable. However "a presumption of fairness exists where: (1) the settlement is reached through arm's-length bargaining; (2) investigation and discovery are sufficient to allow counsel and the court to act intelligently; (3) counsel is experienced in similar litigation; and (4) the percentage of objectors is small."

(*Wershba v. Apple Computer, Inc., supra*, 91 Cal.App.4th at p. 245, citing *Dunk v. Ford Motor Co., supra*, 48 Cal.App.4th at p. 1802.) The presumption does not permit the Court to "give rubber-stamp approval" to a settlement; in all cases, it must "independently and objectively analyze the evidence and circumstances before it in order to determine whether the settlement is in the best interests of those whose claims will be extinguished," based on a sufficiently developed factual record. (*Kullar v. Foot Locker Retail, Inc.* (2008) 168 Cal.App.4th 116, 130.)

II. The Settlement Process and the Parties' Agreement

Between May 4 and 25 of 2016, the individual defendants produced certain confidential documents in expedited discovery, including minutes of meetings of AFOP's board of directors, Cowen's engagement letters and presentations to the board, non-disclosure agreements with prospective bidders, and presentations and financial projections prepared by management. Plaintiffs' counsel retained a financial and valuation expert to evaluate these materials. On May 10, 2016, plaintiffs' counsel began settlement negotiations with a formal demand letter.

The parties reached an agreement-in-principle on May 26, 2016. The agreement provided for supplemental disclosures to the shareholders in advance of the shareholder vote on June 3, which are discussed further below. In addition, AFOP and Corning waived the standstill provision with "Party B" (identified in the Schedule 14D-9) to the extent that Party B was prohibited from making any confidential proposal to acquire AFOP. Plaintiffs do not indicate whether Party B made any proposal in the few days between the settlement and the shareholder vote, or realistically could have. The settlement contemplates that plaintiffs will petition the Court for an award of attorney fees and expenses not to exceed $2 million, and the parties are participating in a fee mediation on September 26 to attempt to reach agreement on a specific amount. The settlement includes a broad release of all claims "that arise out of any of the allegations, facts, practices, matters, [etc.] ... that are related, directly or indirectly, to the Actions, or the subject matter thereof...."

The settlement was subject to additional confirmatory discovery, including depositions of defendant and AFOP board member Richard B. Black and of the company's principal financial advisor at Cowen, Setch Subudhayangkul. These depositions were completed in February 2017 and December 2016, respectively. Plaintiffs' counsel has now concluded that the settlement is in the best interests of the putative class.

III. Analysis

While it appreciates counsel's recommendation, the Court lacks the information needed to "independently and objectively analyze" the settlement at issue. (*Kullar v. Foot Locker Retail, Inc., supra,* 168 Cal.App.4th at p. 130.) First, plaintiffs provide only a cursory, generic discussion of the merits of their claims and the risks of continued litigation, which does not address their findings based on the expedited and confirmatory discovery they conducted. Plaintiffs also provide little context to enable the evaluation of the standstill waiver they obtained

as part of the settlement, which took effect only a few days before the shareholders voted to approve the merger.

The major component of the settlement consists of supplemental disclosures, which also were made just a few days before the shareholder vote. As summarized in counsel's declaration, the supplemental disclosures pertain to: (1) the standstill waiver as to Party B; (2) specific line items related to generally accepted accounting principles ("GAAP") associated with the March and April 2016 financial projections discussed in the 14D-9; (3) an explanation that AFOP estimated $4 million in capital expenditures for 2016-2019 and $6 million for 2020, with an annual increase in working capital of roughly 0.7% of revenue; (4) an explanation of the factors considered in revising the April 2016 projections, including preliminary results from the first quarter of 2016 and management's perception of increased risk to the company's business; and (5) the provision of company by company multiples in the *Analysis of Selected Publicly Traded Companies* and *Analysis of Selected Transactions*. However, plaintiffs did not provide the Court with a comparison of the supplemental disclosures to the disclosures in the original Schedule 14D-9 and prior amendments thereto—in fact, these prior disclosures are nowhere to be found among the moving papers. The Court is unable to evaluate what the supplemental disclosures add to the "total mix" of information available to shareholders without reviewing these documents. (See *Zirn v. VLI Corp.* (Del. 1996) 681 A.2d 1050, 1056 [materiality of disclosures is evaluated based on whether there was a substantial likelihood that the disclosure would have significantly altered the "total mix" of information made available to shareholders].)

Also with regard to the disclosures, plaintiffs do not discuss a crucial opinion by the Delaware Court of Chancery on this subject, *In re Trulia, Inc. Stockholder Litigation* (Del. Ch. 2016) 129 A.3d 884. *Trulia* was filed in January 2016 and has been the subject of much commentary ever since. In the absence of briefing on the issue, the Court will discuss *Trulia* and its impact on this case in some detail.

IV. The Opinion in *Trulia*

Trulia announced the Chancery Court's repudiation of its past approach to disclosure settlements such as this one, the routine approval of which the court found to "have caused deal litigation to explode in the United States beyond the realm of reason." (*In re Trulia, Inc. Stockholder Litigation*, *supra*, 129 A.3d at p. 894.) The Court explained that disclosure settlements have "become the most common method for quickly resolving stockholder lawsuits that are filed routinely in response to the announcement of virtually every transaction involving the acquisition of a public corporation." (*Id.* at p. 887.) "[F]ar too often[,] such litigation serves no useful purpose for stockholders" and "serves only to generate fees for certain lawyers who are regular players in the enterprise...." (*Id.* at pp. 891-892.)

The court provided a detailed analysis of the worrisome dynamics at play in these cases:

> In such lawsuits, plaintiffs' leverage is the threat of an injunction to prevent a transaction from closing. Faced with that threat, defendants are incentivized to settle quickly in order to mitigate the considerable expense of litigation and the distraction it entails, to achieve closing certainty, and to obtain broad releases as a form of "deal insurance." These incentives are so potent that many defendants self-expedite the litigation by volunteering to produce "core documents" to plaintiffs' counsel....
>
> Once the litigation is on an expedited track and the prospect of an injunction hearing looms, the most common currency used to procure a settlement is the issuance of supplemental disclosures.... Given the Court's historical practice of approving disclosure settlements when the additional information is not material, and indeed may be of only minor value to the stockholders, providing supplemental disclosures is a particularly easy "give" for defendants to make in exchange for a release.
>
> Once an agreement-in-principle is struck to settle for supplemental disclosures, the litigation takes on an entirely different, non-adversarial character. ... Significantly, in advance of [settlement fairness] hearings, the Court receives briefs and affidavits from plaintiffs extolling the value of the supplemental disclosures and advocating for approval of the proposed settlement, but rarely receives any submissions expressing an opposing viewpoint.

(*Id.* at pp. 891-893.) This description perfectly encompasses the circumstances in this case. To address the potential for abuse arising in cases like these, the *Trulia* court indicated that

> practitioners should expect that disclosure settlements are likely to be met with continued disfavor in the future *unless the supplemental disclosures address a plainly material misrepresentation or omission*, and the subject matter of the proposed release is narrowly circumscribed to encompass nothing more than disclosure claims and fiduciary duty claims concerning the sale process, *if the record shows that such claims have been investigated sufficiently.*

(*Id.* at p. 898, italics added.)

Trulia was quickly endorsed by Judge Posner of the United States Court of Appeals for the Seventh Circuit in a published opinion, *In re Walgreen Co. Stockholder Litigation* (7th Cir. 2016) 832 F.3d 718. In adopting the *Trulia* standard for disclosure settlements, Judge Posner also cited "recent empirical work which shows that there is little reason to believe that disclosure-only settlements *ever* affect shareholder voting." (At p. 723, italics original.) While no published California opinion has yet addressed the impact of *Trulia*, the Court finds its reasoning and the reasoning of *Walgreen* to be compelling. Notably, deal practitioners should not be encouraged to file strike suits in California in order to avoid *Trulia*, a possibility which *Trulia* itself recognized. (See *In re Trulia, Inc. Stockholder Litigation*, *supra*, 129 A.3d at p. 899 ["[S]ome have expressed concern that enhanced judicial scrutiny of disclosure settlements could lead plaintiffs to sue fiduciaries of Delaware corporations in other jurisdictions in the hope of finding a forum more hospitable to signing off on settlements of no genuine value. … We hope and trust that our sister courts will reach the same conclusion [as ours] if confronted with the issue."].)

The Court will accordingly evaluate this settlement under the standard announced in *Trulia* and will provide plaintiffs with the opportunity to file supplemental briefing analyzing the proposed settlement under this standard.

V. Conclusion and Order

The hearing on the motion for preliminary approval is CONTINUED TO DECEMBER 8, 2017 at 9:00 a.m. to enable plaintiffs to address the issues raised herein.

By November 22, plaintiffs shall file and serve (1) a redline comparing the supplemental disclosures reflected in Amendment No. 5 to the 14D-9 to the prior disclosures reflected in the original 14D-9 or prior amendments thereto, along with complete copies of the 14D-9 and all amendments and (2) a supplemental memorandum, not to exceed 10 pages in length, addressing (A) the materiality of the supplemental disclosures and the scope of the release in light of *Trulia* and *Walgreen*, (B) the value of the standstill waiver considering the timing of the settlement and shareholder vote, and (C) the specific facts relevant to an evaluation of the merits of plaintiffs' claims and the risks of continued litigation.

IT IS SO ORDERED.

Dated: 9-29-17

Honorable Brian C. Walsh
Judge of the Superior Court