DELAWARE SUPREME COURT UPHOLDS VALIDITY OF NOL RIGHTS PLAN

October 5, 2010

To Our Clients and Friends:

The Delaware Supreme Court yesterday upheld the Delaware Court of Chancery's decision approving the adoption by Selectica, Inc. of a shareholder rights plan with a 4.99% trigger.[1] Unlike the more typical poison pill, which is geared towards defending against unsolicited takeovers, Selectica's pill was aimed at protecting one of the company's most valuable corporate assets, its net operating loss carry-forwards for tax purposes ("NOLs"). Selectica adopted the NOL pill in response to a perceived threat that its longtime competitor, Versata Enterprises, would acquire a position in the company big enough to impair the value of the NOLs. For a fuller description of the facts and the Court of Chancery's decision, please see our memo of March 2, 2010: *Poison Pill Update: Delaware Chancery Court Upholds NOL Rights Plan With 4.99% Trigger.*

In its appeal, Versata argued that the lower court misapplied the *Unocal* analysis in two respects. First, Versata claimed that the Selectica board did not conduct a reasonable investigation sufficient to conclude that the NOLs were an asset worth protecting and that there was a threat to the corporate enterprise. The Delaware Supreme Court, pointing to, among other things, the care taken by the board in its investigation, the board's reasonable reliance on expert opinion, and the contentious history of the relationship between Selectica and Versata, concluded that the Court of Chancery did not err in deciding that Selectica's board had reasonable grounds to believe that "a danger to corporate policy and effectiveness" existed.

Second, Versata argued that the NOL pill, either alone or together with Selectica's staggered board and the "reloaded" NOL pill that Selectica adopted after Versata triggered the initial pill, had a preclusive effect on the Selectica shareholders' ability to pursue a successful proxy contest for control of the board. The Supreme Court again agreed with the Court of Chancery, holding that there was no evidence that a 4.99% ownership limit would render success in a proxy contest "realistically unattainable." The Court also rejected Versata's argument that even if it could prevail in a proxy contest, the staggered board effectively prevented a bid conditioned on redemption of the NOL poison pill, since the bidder would

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1 *Versata Enterprises, Inc. v. Selectica, Inc., No. 193, 2010, C.A. No. 4241 (October 4, 2010)(en banc).*

need to win two proxy contests to gain control of the board. According to the Court, that the two defensive measures may make it more difficult or time-consuming to gain control of the board did not mean that they were preclusive.

The Court emphasized that *Unocal* analysis is highly contextual in nature. "The fact that the NOL Poison Pill was reasonable under the specific facts and circumstances of this case," it cautioned, "should not be construed as generally approving the reasonableness of a 4.99% trigger in the Rights Plan of a corporation with or without NOLs." Each poison pill must be scrutinized in light of all relevant facts and circumstances, both when it is adopted and when a board decides whether to disarm it.

Please feel free to contact us with any questions.

Paul S. Bird	Andrew L. Bab	William D. Regner	Vadim Mahmoudov
+1 212 909 6435	+1 212 909 6323	+1 212 909 6698	+1 212 909 7207
psbird@debevoise.com	albab@debevoise.com	wdregner@debevoise.com	vmahmoudov@debevoise.com