THE M&A JOURNAL

THE INDEPENDENT REPORT ON DEALS AND DEALMAKERS

VOLUME 20 NUMBER 8

CONTENTS

AUGUST-SEPTEMBER, 2020

*The M&A Journal is published approximately every six weeks, with ten issues per volume. The sequence of issues is therefore tracked by volume and issue number, rather than by month.

Before the Supreme Court:

Delaware's Judicial Regime for Balancing Political Parties

THE SUPREME COURT HEARD the first oral argument of its new term on October 5 in a case that could transform the rules under which Delaware's governor appoints judges to the most powerful courts in American corporate law. The state has a unique regime designed to maintain a political balance on the bench between members of the Democratic and Republican parties.

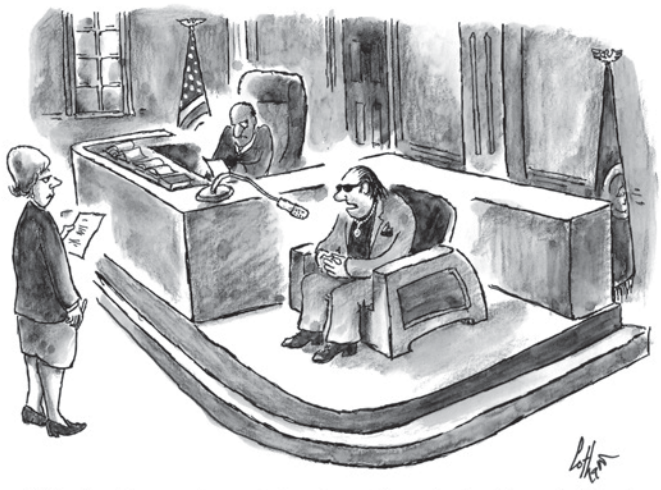
That system effectively bars anyone who is not affiliated with either party---an independent or a member of the Green Party, for example—from a seat on the Delaware Superior Court, its Court of Chancery, and the state Supreme Court. The Third Circuit found that this structure runs afoul of the First Amendment's guarantee of freedom of association. That issue is what is now before the Supreme Court.

Entitled *John C. Carney, Governor of Delaware (Petitioner) v. James R. Adams (Respondent)*, the case came on for oral argument with the high court in precisely the sort of political equipoise that Delaware has sought to maintain. The court will likely end up issuing its decision in precisely the state of imbalance that Delaware has sought to avoid for its own judiciary with six justices nominated by Republican presidents and three by Democratic administrations. At the time the oral argument was heard, Delaware Justice Ruth Bader Ginsburg's seat was draped in mourning black with eight sitting justices, five put in place by the Republicans and three by Democrats.

The Delaware mathematical system for judiciary nominees, which dates back to 1897 and has been modified repeatedly over the years, has two aspects, known in the current litigation as the "bare majority" provision and the "major political party" provision. For certain courts and for the three courts as a whole, if there is an even number of judges, no more than half can be from one of the two major political parties. If the courts have an odd number of seats, only a bare majority (half plus one) can from the same political party. Those are "bare majority provisions.

The creation of the 1897 constitution did not include the establishment of a supreme court. Typically, appeals from lower court decisions were handled by ad hoc panels made up of the chancellor and two judges from the Superior Court. In 1951, to win over opponents of the proposed state supreme court, the legislature decided that not only would the court be subject to a bare majority provision but also a new requirement that the other seat must go to a

Delaware ➔



"He should never have spoken to me in such a partisan fashion."

Delaware

continued

member of the other major political party. Under the current configuration, three of the five justices of the new supreme court must be members of one of the major political parties, and two must be from the other. The Delaware Supreme Court, the Court of Chancery, and the Superior Court are now covered by "bare majority" and "major political party" provisions. For all other state courts, only the bare majority provision applies.

This judicial structure went undisturbed until 2016, when Joel Friedlander, a star Delaware lawyer, wrote an article for the Arizona Law Review, questioning the constitutionality of that portion of Article IV, Section 3 of the Delaware constitution that sets up the major party provision, for which Mr. Friedlander uses the more accurate term The Political Balance Requirement, reaffirmed by constitutional amendments not only in 1951, but also in 1961, 1963, and 1994.

First, he cites several prominent Delaware officials who have praised the state system for nominating judges. Former Chief Justice E. Norman Veasey, for example, once described the policy as follows: "The constitutional requirement of a bipartisan judiciary is unique to Delaware. It mandates that in each court individual and in all Delaware constitutional courts collectively there may not be more than a bare majority of one major political party. This system has served well to provide Delaware with an independent and depoliticized judiciary and has led, in my opinion, to Delaware's international attractiveness as the incorporation domicile of choice."

In his article, Mr. Friedlander refers collectivity to the two prongs of the system as the Political Balance Requirement. He recalls his first encounter with this system and then poses the questions that came before the Third Circuit in 2019 and then before the Supreme Court itself. "I first heard this same sentiment at the pre-admission conference for lawyers who had just passed the bar exam, when a member of the Delaware Supreme Court expressed pride in the Delaware judiciary and the Political Balance Requirement. I wondered at the time if the provision was unconstitutional. Over the years, I continued to wonder but never researched the issue. Does the First Amendment permit a State to disqualify from appointment to a state judgeship any lawyer who is neither a Democrat nor a Republican? Put differently, can the elected representatives of two major political parties strike a legally binding bargain that sets aside one half of a State's judiciary for members of one party and the other half for members of the other party? Can a State Constitution limit the number of State judges belonging to a single political party?" He concludes that the major party provision, or, as he labels it, the Two-Party Feature, is unconstitutional but reaches no conclusion about the constitutionality of the bare majority provision.

After reading Mr. Friedlander's article, James Adams, a Delaware state employee, government employee, and law school graduate, decided to try get those questions answered. He had left the Democratic Party in 2016 and considered himself a progressive and supported Bernie Sanders. He decided to try to become a judge but found himself confronted with the requirement of party membership for the top three courts and the bare-majority rule that blocked any move to join the Family Court.

Represented by David Finger of Wilmington's Finger & Slanina, Mr. Adams filed suit In February of 2016 seeking a federal injunction against the provision in the state constitution that requires a political balance on the courts. He won an injunction from the district court, which agreed that the provision was a violation of the First Amendment's guarantee of freedom of association. The ruling was upheld by a three-judge panel of the Third Circuit. Delaware, represented by Michael McConnell, a former federal judge and Stanford First Amendment professor, petitioned the Supreme Court for review.

What follows is the official transcript of the oral argument in *Carney v. Adams*.

PROCEEDINGS

(10:04 a.m.)

Chief Justice Roberts: Our first case today is Number 19-309, John Carney, Governor of Delaware, versus James Adams. Mr. McConnell.

ORAL ARGUMENT OF MICHAEL W. McCONNELL ON BEHALF OF THE PETITIONER

Mr. McConnell: Mr. Chief Justice, and may it please the Court: A fundamental feature of our system of federalism, recognized most clearly in *Gregory versus Ashcroft*, is that states have broad leeway in setting qualifications for their high-ranking officials, including their judges. Delaware has used that freedom to create a system unique among the states of constitutionally mandated political balance for its judiciary, with the result that Delaware's courts are widely

regarded as the least partisan and most professional in the nation. The Third Circuit has upended that system based on an implausible reading of this Court's political patronage cases. *Elrod* and *Branti* expressly permit using political affiliation for appointments to high-level discretionary positions. But even if we're wrong about that, the Delaware provisions serve a compelling interest in creating a uniquely balanced and nonpartisan judiciary.

Now, to make matters worse, the Third Circuit invalidated the bare majority provision based solely on severability, despite having found that Mr. Adams has no standing to challenge that requirement. That analysis directly conflicts with both federal and state severability doctrines. There is no doubt whatsoever that the bare majority requirement can stand on its own. It stood on its own for more than 50 years, from 1897 to 1951. It stands on its own with respect to two of Delaware's five constitutional courts even today.

There is not the slightest reason to believe that Delaware's constitutional drafters would eliminate the bare majority requirement if they knew the major party provision would be struck down. That said, both provisions of the Delaware constitution pass muster under the First Amendment. And Mr. Adams, who passed up the chance to apply for a host of judgeships both before and after changing party affiliation, lacks standing to challenge either one. I look forward to your questions.

Chief Justice Roberts: Well, Mr. McConnell, I'd like to begin with the standing issue. Our cases, like *Gratts* and *Northeastern Florida*, require that a plaintiff injured by being excluded from competing for a position need only establish that he's ready and able to apply for it. Don't you think he's ready and able?

Mr. McConnell: He -- he shows by his actions that he is neither -- he may be able, but he isn't ready in that there were numerous judgeships for which he was constitutionally eligible and didn't apply.

It would be as if in the -- in the contractor case, a -- a -- a -- a suit was brought by somebody who had been offered a contract and just chose not to take it.

Chief Justice Roberts: Well, I don't think that's applicable. The contractor wants to enter into any contract he can to sell his goods. But just because Adams passed up some judgeships doesn't mean he's not interested in one that will become available or was available when the others were.

Mr. McConnell: Well, Mr. Chief Justice, he -- he testified in his deposition under oath that he was interested in all five courts. He was specifically asked, all five of the courts? And his answer was yes.

Chief Justice Roberts: Well, he also said that he would consider and apply for the next available judicial position. He said that under oath at the summary judgment stage. What -- what more does he have to do?

Mr. McConnell: Well, he did not, in fact, apply for the next available position, even when he was eligible for it.

Chief Justice Roberts: Is there anything else he has to do? He -- he satisfies all of the qualifications. He seems adamant about wanting a position.

Mr. McConnell: His -- actually, even his allegations have been -- have fallen very short of the concrete plans that this Court requires in -- in *Lujan*. His allegations are vague in the extreme. He said he has desired and still desires a judgeship. That's from his amended complaint. He says that he would seriously consider and apply for a -- a judgeship. That's from his answers to interrogatories. He never out and out says that if --that he will apply for a -- a judgeship if the -- if -- if he becomes eligible. And I don't know how he could allege that anyway given that there have been numerous judgeships for which he is eligible and he has never -- and he -- and -- and -- and he has passed up most of those. If -- if Mr. Adams is held to have standing here, then I think anyone would have standing to challenge provisions of constitutions that they have academic disagreements with simply by saying that they might want to -- to take -- take advantage of them at some point, but, in *Lujan* --

Chief Justice Roberts: Thank -- thank you, counsel. Thank you, counsel. Justice Thomas?

Justice Thomas: Thank you, Chief Justice. Mr. McConnell, I'd like to just move to the merits briefly. How -- I'd like to know how far you'd go with your argument. Could Delaware, for example, pass a law requiring all judges to be members of one or the other of the major parties?

Mr. McConnell: I don't think so, Your Honor. The—the test in both *Gregory versus Ashcroft* and in *Branti* and *Elrod*, which—which fit together very nicely, is the—the qualifications have to be reasonably appropriate. I can't see under any circumstances that that requirement would be reasonably appropriate.

Justice Thomas: Changing a little here, what if you—how would your argument be different or this case be different if, for example—if the—your judges were elected and an Independent was prevented from being on the ballot?

Mr. McConnell: Well, Justice Thomas, this

Delaware ➔

Delaware

continued

Court has a whole separate line of jurisprudence under the Equal Protection Clause having to do with elections, and those cases would apply. And I think an out-and-out exclusion of an Independent from being able to be put on the ballot violates not only that person's rights but the voters' rights. But, when a state does not subject a position to elections but, rather, to appointment, those cases do not apply.

Justice Thomas: Well, what -- what, for -- would this be -- would your case be better or worse if this were not a matter of constitutional provision but, rather, a matter of a tradition or practice that had a long standing?

Mr. McConnell: Under this Court's precedents, I think it's the same, because the -- the -- the cases that the Third Circuit relied on, *Elrod* and *Branti* and *O'Hare* and *Rutan*, all involve the exercise of appointment discretion by the appointing officer. And so, if Mr. Adams is right here about the state constitution, it would seem to follow from those cases that he would have a right even as to the executive. Now he forswears that, he says that isn't his position, which I can understand because it would be -- it would fly in the face of -- of -- you know, of longstanding and universal practice. So, of course, he doesn't want to admit that that's the logical implication of his position, but it is.

Justice Thomas: And, briefly, you've studied this area. Is it -- do you find any historical support for impose -- preventing states from imposing political qualifications?

Mr. McConnell: None at all.

Justice Thomas: Thank you.

Chief Justice Roberts: Justice Breyer?

Justice Breyer: All right. Thank you. I -- I'd like to return to Justice Thomas's first question. As I understand it, the Constitution says, in respect to the Supreme Court, the Superior Court, and a number of other courts -- not all -- that you have offices --you have some offices that are for the same major political party, but they can't be more than a bare majority. And then it says the remaining members shall be of the other major political party. So why isn't that just the problem that you said was the problem? If -- if a bare-- if a majority or an even number are Democrats, the rest must be Republicans, and the Green Party need not apply. It can't.

Mr. McConnell: Well, Justice Breyer, the -- the reason for this is -- is not to exclude Independents or the Green Party but, rather, as a necessary backstop to the bare majority requirement because, without it, it would be just too easy for the governor to name a political ally, you know, from an allied party. I mean, take Mr. Adams as a great example of this because he professes to be --after having been a life-long Democrat, he professes to be a Bernie Sanders Independent. So, if there were already a Democratic majority on the Court and the governor were able to name Mr. Adams, it would just fly in the face and frustrate the purposes of the political balance provision.

Justice Breyer: Well, I agree there might be a reason for it, but how do you get around the fact that the way that it's written and applied is you have to be a Republican or a Democrat? And there are other parties. Period.

Mr. McConnell: Well --

Justice Breyer: And so why is that constitutional?

Mr. McConnell: Well, it's constitutional because it's -- it advances the states' compelling governmental interest in political balance on the courts, and there --and there is no other provision that would achieve that purpose in a less restrictive way, or at least no one has identified it.

Justice Breyer: I see your argument. And the other question I have is it is the case that the -- the Plaintiff in this case did apply or did say he would apply to become a judge in any court were it not for these requirements. Now why isn't that good enough to give him standing? I -- I mean, he's -- if he -- assume -- should we have a hearing to decide if he's sincere? Do you think he's insincere in that or what?

Mr. McConnell: Actually, I think -- I think that a -- first of all, this decided in his favor on motion for summary judgment. So the question is whether the trier of fact could, on this record, conclude that Mr. Adams does not have a serious interest in serving on the courts. And the fact that he could have applied for any number of positions, both before and after he changed his political affiliation, casts serious doubt on his sincerity.

Chief Justice Roberts: Thank you, counsel. Justice Alito?

Justice Alito: Mr. McConnell, what do you think is the minimum that Mr. Adams would have to allege in order to have standing? Suppose he looked up when the next vacancy would occur on any of the covered courts and said, I plan to apply for that position. Would that be sufficient?

Mr. McConnell: I -- Justice Alito, I -- I think so. His big problem is that his actions do not line up with his words. Now it is true that even his words are vague and, I think, insufficient under this Court's precedent in *Lujan*, which requires concrete plans, but what you describe probably

would satisfy *Lujan*. The problem is I don't think he could swear to it given that there have been so many judgeships for which he's entirely eligible that go by.

Justice Alito: Well, couldn't he say, in the past, I was equivocal about this, but now I've made up my mind, I want to be a judge, and a position will open up on this particular court on this particular date, and I plan to apply for that? Wouldn't that be enough?

Mr. McConnell: Well, not without taking back his sworn statement that he would be interested in serving on any of the five courts, because, among those five courts, two of them are perfectly open to him. In fact, he has a better shot on -- I mean, legally speaking, on those two courts because, as an Independent, he could never violate the bare majority requirement. But he -- despite the fact that those case -- those openings have been numerous he still brings the lawsuit. It seems evident that he's -- he's really interested here in pursuing a theory that he read about in a law review, not really getting a judgeship.

Justice Alito: On the merits, your answer to Justice Thomas about a hypothetical constitutional provision requiring that all of the judges on a particular court be members of a particular party was that that would not be reasonably appropriate, whereas the -- the breakdown in the provision at issue here is reasonably appropriate. So, if we hypothesize a court with nine members, at what point would the breakdown specified in the constitution be inappropriate? If it -- nine to nothing, presumably, would not be, according to your prior answer, but what about eight to one, seven to two, six to three, five to four? At what point would something become not reasonably appropriate?

Mr. McConnell: I understood Justice Thomas's hypothetical to be that the Court be entirely members of one party. I do not see --I can't conceive what the legitimate governmental interest would be for that. But, here, the State is doing something that's actually quite commonsensical, makes a great deal of sense, if you believe in a bipartisan judiciary. And that's what -- that's the difference here. It isn't numbers. It's whether the use of partisan affiliation is reasonably appropriate for --

Chief Justice Roberts: All right. Thank you.

Mr. McConnell: -- his decision.

Chief Justice Roberts: Thank you counsel. Justice Sotomayor?

Justice Sotomayor: Counsel, I'm -- I -- I just want to make sure I understand things. You used the word "bipartisan," but, in your briefs, you said that this provision, the majority party provision, promotes partisan balancing and the public's perception of an independent judiciary. I just don't understand why the majority party rule promotes either of those two interests and does it in a better way than the bare majority provision at issue in your section -- in your Number 2 of Article III? There, all that is required of the bare majority is that it be no more than a bare majority. It doesn't have to be. But could you explain to me why it has to be two parties only who can be judges?

Mr. McConnell: Well, Justice Sotomayor --

Justice Sotomayor: And to promote those particular interests, because that's the State's interest.

Mr. McConnell: So the State's interest is in -- is in balance. And what the major party provision does is it prevents the governor from appointing somebody from an allied party, a party that's very closely associated with one of the two major parties, or an Independent who may have been a member of the other major party, as, of course, Mr. Adams was for his entire career. So this is really a backstop provision to make sure that the bare majority provision works.

Justice Sotomayor: Well, but --

Mr. McConnell: And as the --

Justice Sotomayor: -- if you'll—if you'll excuse me a moment with that, those two examples. It seems to me that no rightly thinking governor is going to appoint someone from the other party who is completely misaligned with his or her views. They could pick the most—I—I—I I don't know if there's such a word -- the softest Republican, the one most closely aligned with Democratic values or—or something of that nature. It just doesn't seem to me that the --that the mere membership in a party connotes an acceptance by a governor.

Mr. McConnell: Well, Justice Sotomayor, this is really a question of -- of experience and reality. And political party in this country is -- it's universally used by political science and scientists as the proxy for a philosophy and ideology, and it's especially true now in the last -- in the last 20 or 30 years, when -- when the two parties have been through, you know, what they call partisan sorting, so that today the most liberal Republican is -- is at least similar to but, you know, probably more conservative than the most conservative Democrat.

Chief Justice Roberts: Thank you, counsel. Justice Kagan?

Justice Kagan: Good morning, Mr. McConnell. If I could go back to the standing questions that you've been answering. As I understood your

Delaware ➔

Delaware

continued

answers, you said two things. One was that Mr. Adams never out and out said he was going to apply, and the second was that, in fact, he didn't apply on numerous occasions. So, as to the first -- I mean, this is his deposition testimony. I think the -- the Chief Justice referred to this. He said: I would apply for any judicial position that I thought I was qualified for, and I believe I'm qualified for any position that would come up. So isn't he -- you know, he out and out says he wants a judicial position, doesn't he?

Mr. McConnell: He's -- that certainly fall shorts of a concrete plan, as required by *Lujan*, but I think his big problem is that --

Justice Kagan: If I could --

Mr. McConnell: -- as to the --

Justice Kagan: -- just stop you there. Why -- why does it fall short of a concrete plan? He's basically saying, I'm -- I want -- I would apply for any judicial position that would come up. That's what -- that's what he says. That's a concrete plan: I would apply for any judicial position that would come up.

Mr. McConnell: Of course, he hasn't followed through on that on -- on many occasions, which I think is --

Justice Kagan: Okay. So --

Mr. McConnell: -- the problem.

Justice Kagan: -- that's your second argument, Mr. McConnell, but, as to that, I mean, isn't the answer that it would be completely futile to apply? I mean, as long as this constitutional provision is in effect, and he's an Independent, he's not going to get a position --

Mr. McConnell: Oh, no, that's --

Justice Kagan: -- so why would we insist that he have to file an application?

Mr. McConnell: Justice Kagan, that's just not so. Of the five constitutional courts, two of them do not have a major party provision, and he's eligible for every single vacancy on those courts.

Justice Kagan: Well, if he had said, what I'm -- what I'm interested in is the three that have both the provisions, the -- the major party as well, would he have to apply?

Mr. McConnell: Well, probably not, but that isn't what he said. And we have to judge this case according to the case that he has brought to us.

Justice Kagan: I -- I -- I guess it seems a lot to me like the cases where we've said, you know, when somebody challenges an admissions policy, you know, in *Gratts*, in -- in *Bakke*, things like that, we're not going to make you file the application. We're certainly not going to judge what the likelihood of somebody thinking that the application is meritorious is. As long as this policy remains in effect, you can just challenge the policy.

Mr. McConnell: Yeah, but the problem here is that he could apply and he would be eligible. And he has stated that he -- that he's interested in any of the five courts. He doesn't apparently care which one.

So it would be -- it would be as if somebody said, I want to go to any public university in Texas, but I can't -- but I haven't applied to any of them, and one of them, I think, there's a -- there's an obstacle.

Chief Justice Roberts: Thank you, counsel. Justice Gorsuch.

Justice Gorsuch: Thank you. Mr. McConnell, I'd like to return to the question of the historical pedigree of these requirements. I understand your argument that there are a great many bare majority requirements across country and across time. How -- how about with respect to the major party requirement? What analogues do you have for that?

Mr. McConnell: Justice Gorsuch, as far as I know, the -- the Delaware Constitutional Convention of 1896 was an innovator. I think it was the first state constitutional provision or even analogue even. There was a -- there was a -- there were a couple of small statutes having to do with elections prior to that, but I think it was, in fact, an analogue. But there's certainly no examples in the -- in history of -- of provisions of this sort being regarded as unconstitutional. In fact, for most under the jurisprudence –

Justice Gorsuch: But let me -- let me -- let me -- let me interrupt you there, and I'm sorry for doing so, but with our limited time. That -- that -- that's what I thought the answer would be, and -- and -- and that raises for me the following question. That's the reason for the first question. The major party provision prohibits Independents from service, serving as -- as judges. That -- that's quite a -- quite a sweeping rule. And I -- as I understand you, you've -- you've indicated that you'd agree that that violates the Equal Protection Clause as applied to elect -- elect -- elected positions. But you indicate that it's somehow very different with respect to appointed positions. And I guess I'm not clear why, given the absence of any historically rooted tradition along these lines with respect to the major party requirement. I understand your argument that it serves as a backstop for the bare majority rule, which does have historical antecedents, plenty of them, but, near as I can tell, none of those has ever included this backstop

before. This is a novel thing. And it does -- does prohibit a great percentage of the population from participating in the process.

Mr. McConnell: Just, Justice Gorsuch, may I make two points about this? First, although I can't point to a specific use of this particular matter, this Court has approved any number of limitations on First Amendment rights as a condition to public service. The Hatch Act cases, for example, are a much more severe limitation on free speech rights, applying to lots more people for lots more positions, and the Court has -- has consistently upheld them. But, secondly, as to the uniqueness here, this actually, I think, points in Delaware's favor. It is true that Delaware is the only state that does this. But it is also the only state that has created a judiciary of a particular sort that -- that is fair. It's like --

Justice Gorsuch: Thank you, counsel.

Mr. McConnell: -- the Delaware judiciary is a jewel.

Chief Justice Roberts: Justice Kavanaugh?

Justice Kavanaugh: Thank you, Mr. Chief Justice. And good morning, Mr. McConnell. To pick up on standing from the comments and questions of the Chief Justice and Justice Kagan, you keep saying he hasn't applied. Of course, he hasn't applied. He's not eligible. And that's the point. He says, once I'm eligible, I will apply. And I took your answer to Justice Kagan then to be, well, he's applying to too many courts. And I -- I guess I don't understand why, if he says, I'm interested in any of three or four different courts, that defeats his intent to apply for standing purposes.

Mr. McConnell: Well, Justice Kavanaugh, when he says he's interested in any of the five courts, and there are positions for which he is eligible, constitutionally eligible on some of those courts, it indicates that --that his actions at least do not conform to his words.

Justice Kavanaugh: Well, he's not eligible because he's not a Republican or Democrat.

Mr. McConnell: He is eligible for two of the five courts, including the one for which his qualifications would seem to be the -- the best match, namely, the family court.

Justice Kavanaugh: On the merits question, could a state exclude Republicans and Democrats from being judges and allow only Independents to be judges?

Mr. McConnell: Justice Kavanaugh, I thought about that, and I think it's a difficult question. I don't -- I can't answer that a definite no. I think it is not impossible that --not a -- that a state has the constitutional authority under *Gregory versus Ashcroft* and other cases to say that judges simply may not be registered members of any party.

Justice Kavanaugh: Why can't -- to pick up on Justice Sotomayor's question, why can't Independents even better serve the goal of a balanced judiciary nonpartisan/bipartisan judiciary?

Mr. McConnell: This provision is not really about whether Independents can do a good job as judges. It's about governors and -- and whom they can apply. And the limitation applies to the governor. It's a separation of powers type provision. If a -- if a governor simply used his discretion to balance the courts, nobody would even bat an eyelash. Obviously constitutional. It -- it's very odd to say that the constitution cannot direct the governor in his exercise of discretion. But it's the governor who might very well name a-- a supposed independent who is, in fact, an ally of his party.

Justice Kavanaugh: Well, I guess there's a mismatch, arguably, between the state's interest in excluding Independents altogether from being judges, because Independents could certainly -- wouldn't you agree that Independents could serve the purpose of achieving a balanced nonpartisan or bipartisan judiciary?

Mr. McConnell: Absolutely. But giving governors the discretion to name Independents or allied parties would frustrate the purpose of the provision. It doesn't make it impossible. I don't -- I don't -- I'm not saying it's an -- an essential backstop, just that it is a valuable backstop.

Justice Kavanaugh: Thank -- thank you, Mr. McConnell.

Chief Justice Roberts: Mr. McConnell, why don't you take a minute to wrap up.

Mr. McConnell: Thank you. The -- the framers of the Delaware constitution had lived through domination of the courts by one party and then by the other. On the basis of that experience, they resolved that a bipartisan bench would bring about, and I quote, "a fuller and freer discussion of the matters that come before them and lead to fair and impartial decisions." In other words, they wanted the judiciary to remain stable, balanced, and nonpartisan, even when elections go all for one party for a period of time.

Now their decision has survived the test of fire. For the last 27 years, one party has held both the governorship and the Senate in Delaware, but the courts have remained balanced and nonpartisan. That is a remarkable achievement. We may not be able to prove with scientific precision that Article IV, Section 3 is the cause, but we don't want to risk it. States all over the country use partisan affiliation as part of judicial selection with partisan elections and partisan appoint-

Delaware ➔

Delaware

continued

ments. Delaware should be able to use partisan affiliation to bring political balance. Thank you.

Chief Justice Roberts: Thank you counsel. Mr. Finger.

ORAL ARGUMENT OF DAVID L. FINGER ON BEHALF OF THE RESPONDENT

Mr. Finger: Mr. Chief Justice, and may it please the Court: Delaware's constitution denies Mr. Adams the opportunity to apply for a judgeship because he does not belong to a major political party. The language "political party" excludes unaffiliated voters. The Delaware code provides that unaffiliated and independent voters are voters without a political party. And if one severs the phrase "political party" from the provisions, then the text becomes incoherent and does not achieve its desired goal.

Petitioner is really asking this Court to rewrite the provisions under the guise of severance, and that should be left to the Delaware legislature. This phrase of "political party" affects all the issues before the Court. A party who suffers unequal treatment has standing to challenge a discriminatory exception that favors others. As long as judicial seats are allocated exclusively to political parties, unaffiliated lawyers are categorically excluded. The Petitioner's arguments, at least in their brief, are based on the assumption that a judge's political affiliation is determinative of how that judge will vote in a case. And this Court can look to its own history as a refutation of that premise. If this Court accepts the premise, it's the end of the idea of an independent judiciary. And if this Court rejects the premise, then, irrespective of the standard of review, the challenged provisions must fall. Judicial engineering to avoid extremism in judging is not an interest that overcomes the First Amendment, and there's no evidence that political discrimination has had any beneficial effect on the quality of justice in Delaware. Merely repeating that it has doesn't make it so. For these reasons, this Court should affirm the decision of the Third Circuit. Thank you.

Chief Justice Roberts: Counsel, your client said that he would apply -- was interested in serving as a judge on -- on any court, and yet there were several opportunities for him to apply to judgeships for which he was qualified and he didn't do it. So why shouldn't we not take his standing assertions as serious?

Mr. Finger: Well, again, his -- his statements are judged to have been made in good faith. He -- he didn't want to apply and he didn't feel that he could not at the time. He may have been in error as to these two minor courts. But we shouldn't ghetto-ise it and say he -- he has to apply only to these lower courts when there's these other courts that he wants to be on as well.

Chief Justice Roberts: Well, but he did say --

Mr. Finger: And under --

Chief Justice Roberts: -- he did say that he wanted to be -- he would be interested in a judgeship on any of the courts.

Mr. Finger: He did say that, Justice -- Chief Justice, but he also -- there are a number of factors which are outside the record that I can't tell you I know them which affected the decision at one time. He does want to. There may have been intervening factors that prevented him from doing that. But, nonetheless, the -- the law -- or -- or the jurisprudence of this Court has been that there's not a concrete step point that --that flows from *Lujan* but the fact that it's unlawful conduct that impedes the ability to undertake the action that determines the standing.

Chief Justice Roberts: Well, the strongest statement he has is that he would consider and apply for the job. Now, if -- if I got an application for a clerkship from someone who said she would consider and apply for the job, I really wouldn't know what to make of that.

Mr. Finger: Well, it -- it might be in the context where there -- there's no restriction on -- on your decision-making in terms of whether to accept or decline or to follow up with an interview. He can't -- for at least three of the five courts, he can't even apply, or he can apply, but what's the point?

Chief Justice Roberts: Counsel, in their opening brief, Mr. McConnell emphasized our decision in Williams-Yulee, and in his reply brief as well. You don't cite that case at all in your brief, if I'm remembering correctly, and I wondered what your response was to their reliance on it?

Mr. Finger: The Williams case --again, the Court in that case did apply the -- the heightened standard of judicial review. Again, this is not -- the problem with that case and the Hatch Act-type cases is those are cases involving conduct, not merely thought, restrictions on the ability of -- of -- of a judge to do something or a political employee to do something which reflects a political judgment. In this case, it is a question of political thought. No one expects a judge, no matter what their political persuasion, to come out and advocate for -- in the role of a judge for a particular political party. So those cases are distinguished from -- from this case.

Chief Justice Roberts: Thank you, counsel. Justice Thomas?

Justice Thomas: Thank you, Mr. Chief Justice. Mr. Finger, in *Lujan*, we said that a petitioner's "someday" intentions really were not sufficiently concrete to amount to an injury. This looks -- and his intentions of someday doing something did not amount to an injury. This looks much like that. And would you tell me how this differs from the problem that we had in Lujan?

Mr. Finger: Certainly, Justice Thomas. The -- I -- I point to the *Friends of the Earth versus Laidlaw* decision of this Court in 2000, in which it distinguished the *Lujan* case, saying that a statement that someone would take action but for unlawful conduct goes beyond mere someday intention. And that--

Justice Thomas: So how does --

Mr. Finger: -- and that statement --

Justice Thomas: -- unlawful -- I mean, I thought that in *Laidlaw* there was at least some sanctions involved. What would be the sanction against Petitioner -- Respondent here?

Mr. Finger: The sanction would be the denial of the opportunity.

Justice Thomas: And what was it in *Laidlaw*?

Mr. Finger: In *Laidlaw*? I don't recall that off the top of my head, Your Honor -- Justice Thomas.

Justice Thomas: Normally, I think, when we think of a sanction, it's a penalty of some sort or a criminal sanction. The -- let me ask you this: If you don't need anything more concrete than his indication that he would have applied, how formal would this have -- would that have to be, that his intention -- the announcement of his intention? Could he just say to a couple of friends at a cocktail party, oh, I think I'm --I would have applied for this job but for the fact that I'm not a Republican or a Democrat? Or does it have to be in writing? What does it have to be?

Mr. Finger: That's a good -- a very good question. The question then becomes --going back to the Lujan case, the Court uses the phrase "concrete plan," but there's no interpretation of what constitutes a concrete plan. A statement under oath, as it is in this case, that that was what -- what was on his mind, absent some evidence that he is deliberately misleading or lying, should be accepted.

Justice Thomas: What if he has a long history of saying, I'm going to do this and I'm going to do that, and never really gets around to doing it?

Mr. Finger: Well, again -- again, it would depend on the circumstances. As I said, there may be things that come up in one's life that interfere with a given opportunity. Nonetheless, if -- if someone has a constant record of saying, I'm going to do this, and doesn't, then that is some evidence cutting against that person.

Justice Thomas: Thank you.

Chief Justice Roberts: Justice Breyer?

Justice Breyer: As I understand it, and correct me if I'm wrong, two of the five courts, he's perfectly eligible and always has been to apply for, because you can be an Independent. That's the family court and the Court of Common Pleas. So we're only thinking about the other three. Now, as to the other three --

Mr. Finger: That's correct.

Justice Breyer: Is that right?

Mr. Finger: That's correct.

Justice Breyer: Okay. So, as to the other three, what should we do? He -- in --there was a summary judgment motion. He said he wanted to apply to any court. Before he changed his party registration, he could have, since he was a Democrat -- my clerk counted 16 openings that were on the other three courts he could have applied to. So -- so here's a person who says any court, he could have applied before to any, he can apply now to two. Should we have a hearing on that as to whether -- or should we what?

Mr. Finger: Just, Your Honor, let me respond first by saying --

Justice Breyer: Yeah.

Mr. Finger: -- one has to look at the timing of those openings. Mr. -- Mr. Adams testified that while he was working at the Department of Justice, while he was interested in a someday, at that point, he was very happy working with the attorney general, Beau Biden, and wasn't seeking actively a judgeship. It was only after he went into temporary retirement to rethink his position and when he came back a year later in 2017 that he decided that a judgeship was his -- his -- his leading goal. And of those 16, most of them happened -- predated that point in time.

Justice Breyer: Good. I knew you would have an answer to my argument, and that's why I was asking, should we have a hearing on it.

Mr. Finger: Again --

Justice Breyer: Should we send it back for a hearing so that the judges can listen and decide whether he was serious about this or not?

Mr. Finger: I think --

Justice Breyer: Or just write it in a law review article?

Mr. Finger: I -- I think not, Your Honor, for this reason. Both the district court and the Third Circuit did not find a reason to infer that he was not sincere. Now that goes to the question of whether it's a question of fact or question of law. Whether the testimony and the evidence give

Delaware ➔

Delaware

continued

rise to any inference is a question of law. And lower courts have found that --that the -- the evidence presented -- and both parties moved for summary judgment, so the -- so the state seemed to feel it was prepared, but the evidence submitted, they found, did not rise to the -- to the level of creating an inference of insincerity.

Justice Breyer: No, I know that, but sincerity is not the same thing as having a chance. And he could have had any chance he wanted to, and then there's the argument about the other three. That's -- that's one of the things I'm not certain about, but -- whether sincerity is the answer to this. What do you think?

Mr. Finger: Well, if it's not sincerity, then -- then there -- very often in a case where someone says, I want to do something, but I can't, I --

Justice Breyer: Doesn't mean, sorry, if I sincerely want to go to the North Pole, nonetheless, I can't go?

Mr. Finger: Yes. If -- if -- if -- if there is a -- if there is a government-imposed impediment to that, and there's nothing that really rises to the level of a -- a challenging the legitimacy of his intentions, then there's not -- then you -- we have -- we have achieved the -- the standing requirement.

Chief Justice Roberts: Thank you, counsel. Justice Alito?

Justice Alito: Because this issue of standing was decided at summary judgment, we are required to look at the record in the light most favorable to your adversary, isn't that so?

Mr. Finger: That's correct.

Justice Alito: And as was previously mentioned, Mr. Adams' best statement about his plans appears to have been the statement that he would "consider and apply for a future vacancy." Isn't that right?

Mr. Finger: That's correct, Justice Alito.

Justice Alito: And if we view that in the light most favorable to the other side, can we say that means that he would actually apply? He said he would "consider and apply."

Mr. Finger: Yes. If -- if -- if the word "apply" was not there, it would be pure consideration of -- "consider and apply" indicates a positive, affirmative action.

Justice Alito: Well, if you're going to apply, you're done considering. And if you're going to consider, you haven't made up your mind whether you're going to apply. Isn't that right?

Mr. Finger: That certainly would be true -- is true even in -- in isolation, but, when someone says, I will consider and apply, one can reasonably decide -- see that the person does have a goal in mind.

Justice Alito: If we say that the record does not support summary judgment on this, is there any reason for us to go on to the merits of the case? Wouldn't that be deciding a hypothetical case at that point?

Mr. Finger: That was -- well, that would require the Court to make a determination that he was not -- that his testimony was not --was not sincere, not truthful, in which case you would have to go --

Justice Alito: You applied for -- let me turn to another matter -- you applied for an injunction, and there was no ruling on that, was there?

Mr. Finger: That's correct. I'm not sure that we looked -- yeah, we may have included a request for an injunction in the complaint, but we were basically seeking declaratory judgment, which we received.

Justice Alito: Well, had you withdrawn the -- the -- the request for an injunction?

Mr. Finger: We've taken no action on the injunction issue.

Justice Alito: Well, is it still pending?

Mr. Finger: No, it is not because the declaratory judgment action essential -- has the essential effect of an injunction in that it creates a rule of law that the -- that the state has to abide by.

Justice Alito: Well, why is that so? If the governor refuses to comply with the Third Circuit's decision, can he be held in contempt?

Mr. Finger: I believe so.

Justice Alito: Contempt of the declaratory --

Mr. Finger: It is -- it is a -- I'm sorry.

Justice Alito: Contempt of the declaratory judgment?

Mr. Finger: Yes and point to the Court's order instructing what must be done. It is not --

Justice Alito: All right. On the merits, in just -- in just the couple seconds that are left, suppose the governor -- suppose there's no provision like this one, but a governor says, under no circumstances will I ever appoint to any judgeship a member -- a person registered as a member of the other party. From the standpoint of somebody who wants to apply for a judgeship, is there any difference between that situation and the situation here?

Mr. Finger: No, because it becomes an effective unconstitutional policy of the governor.

Justice Alito: Thank you.

Chief Justice Roberts: Justice Sotomayor? Justice Sotomayor?

Justice Sotomayor: Counsel, your last answer

troubles me because there are three rights at issue here that I see, at least three. It's your right, your client's right as an Independent to seek judicial appointment, and that right is being limited by this majority party rule. Then there's the governor's right under *Elrod* and *Branti* to decide who he wants to appoint to a certain position, and he could --maybe not this governor, but another governor might want an Independent or another third-party applicant, but the constitution stops him from doing that. And that's where I think *Elrod* and *Branti* would have quite a -- a lot to say about whether or not your political affiliations have much to do with your decision-making. And -- and that, I think, would be what we would have to face given Justice Alito's question, a governor who says, I won't appoint somebody from another party under any circumstance. But that's not the case here. The case here involves the state, and it's the state's choice for its own interests balancing partisanship and promoting an independent judiciary who says, I want to prohibit both your client and the state and the governor from acting in a particular way, i.e. from selecting you merely because you're an Independent. And it seems to me that the bare majority rule, that, or proposition in this case, is more than adequate to take care of those two interests, but the majority party rule doesn't -- isn't. But you're arguing against both. Can you tell me why you're saying we can't have severance?

Mr. Finger: Certainly. As I indicated in my opening, Justice Sotomayor, the language of – of the -- of the provisions cannot be -- you can't point to a phrase or term that'll take out and -- and remain coherent. And I'll just give the first example regarding the Delaware Supreme Court. The language says: Three of the five Justices of the Supreme Court in office at the same time shall be --

Justice Sotomayor: Counsel, I don't mean -- I don't mean to stop you because I'm mostly interested in the second one. Take a look. All you have to do is take out the last proposition, "the remaining members of such office shall be of the other major political party."

Mr. Finger: Yes.

Justice Sotomayor: And take out the word "major." That's just excising a portion.

Mr. Finger: But it still relegates Independents and minor parties to -- to the --to the minority. It precludes -- it neuters the influence of unaffiliated judges by diminishing the importance of their vote by -- numerically.

Chief Justice Roberts: Thank you, counsel. Justice Kagan?

Justice Kagan: Good morning, Mr. Finger. I just want to make sure I understood your answer to Justice Alito. He said a governor comes in and he says, you know, I'm a Democrat and I'm committed to appointing only Democrats to the bench. They share my judicial philosophy. That's what I'm doing. You think that that would be unconstitutional?

Mr. Finger: I think that would be -- certainly, governors have the right to include political affiliation amongst the factors they consider. But, if they are making a determination based on a classification without regard to individual merit and a classification that is -- is protected by the constitution –

Justice Kagan: Well, I'm sure that they're making decisions with regards to merit. There are lots of meritorious Democrats. But they're -- they're just saying, I'm not going to consider Republicans, I'm only going to consider Democrats. Or, alternatively, let's take another hypothetical. Suppose a -- a -- a governor comes in and says, I'm going to do -- I -- I like this Delaware scheme. We don't have one in my state. But I'm going to do exactly this. I'm going to make sure that there's only a bare majority and make sure that it's evenly divided between Democrats and Republicans. A governor couldn't do that either. There's no constitutional provision. There's no law. This is just a governor's view of good judicial appointment-making.

Mr. Finger: Again, these go back to the communist cases and the question of communists need not apply, which we find --which is not acceptable under the First Amendment. It is -- it is simply a form it's taking -- as opposed to a written law, it is a -- a decision of a government authority. And in those cases, if you're doing it just because you like it or just because you don't like someone of another political party, that is no different than -- than having a law that says you can -- you cannot apply.

Justice Kagan: So you -- you don't think that there's any difference between the two, having a -- a law from somebody else, whether it's the constitution or the legislature passes it, on the one hand, and just it being a decision of the appointing authority?

Mr. Finger: No, I believe that unwritten policies, which violate constitutional language, are just as subject to -- to judicial attack as written ones.

Justice Kagan: Okay. Let's assume that we do what you ask us to do and -- and apply strict scrutiny or some form of heightened scrutiny. Why does this fail? I understood your principal argument to be that this was not the least restric-

Delaware

continued

tive alternative. So I guess my question is, what --what would be a less restrictive alternative?

Mr. Finger: The less restrictive alternative is already -- exists. It is in the Delaware Code of Judicial Conduct, which says that judges shall not consider political concerns in making their decisions. Of course, Mr. --

Justice Kagan: Well, I -- I -- doesn't that go to something very different? I mean, sure, that code of conduct is very important and it makes sure that judges are ethical, but it doesn't do what this law tries to do, which is to say we want to create balanced courts, we want to do that both for the appearance of justice, that those courts won't look political, and we also want to do it because we think that those courts will make better decisions. They won't go to the extremes. They'll move to the center. There won't be polarization. There'll be compromise.

Mr. Finger: Yes, so -- and I -- I -- I believe, for the second point, political --the question whether -- whether it is partisan, bipartisan, that is challengeable from the perspective of the public, who could also say that by creating this -- this political compromise, you -- we are agreeing that judges are making political decisions.

Chief Justice Roberts: Thank you, counsel. Justice Gorsuch?

Justice Gorsuch: Counsel, we've already discussed standing an awful lot, but I just wanted to clear up one small thing that we didn't discuss, and that concerns the bare majority requirement. The Third Circuit held that your client had no standing to contest that because, as an Independent, it doesn't preclude him from taking office in any judicial capacity. I did not see a cross-petition from you on that. I did see one or two stray sentences in your brief suggesting you contest that. I -- I -- I'd just like clarity now. Are you expecting us to -- to rule on that, or do you concede that that issue is not before us?

Mr. Finger: I believe that issue is not before the Court. The Third Circuit did not pass on it but merely relied on -- on severable -- severance or the lack of severability. And that's what I meant.

Justice Gorsuch: Counsel -- counsel, thank you. If you agree it's not before us, that's great. That's all I needed to hear. With respect to the merits, on *Elrod* and *Branti*, I want you to react to this, the notion that they might be an odd fit here. They've been applied to protect the affiliation rights of what the Court has called low-level employees in the executive branch. And, here, we have -- and -- and they've also been there to ensure that patronage doesn't go too far. Here, we have a requirement that doesn't concern the rights of affiliation necessarily and actually mitigates the problem of patronage by ensuring as it has for the last, I guess, 27 years that a -- a governor has to pick a candidate from the opposite party. So the -- first of all, they seem kind of an odd fit. And then -- then there's the overlay of the Tenth Amendment, which grants states considerable power to organize their own governments, so long as they're republican forms of government, and this Court has repeatedly emphasized the importance of that right in *Gregory versus Ashcroft*. So can you just react to -- to those thoughts?

Mr. Finger: Yes, Justice Gorsuch. *Branti* is relevant at least in that it -- it creates a limited exception to what I'm calling the communist rule, that is, the absolute bar on the -- using political affiliation. And the -- although I don't believe that those -- those cases refer to it as limiting it to low-level employees, that's a characterization that was put in -- in -- in my opponent's brief. As for the Tenth Amendment, this Court has also recognized that states' rights are still bounded by the -- the -- the Constitution of the United States.

Justice Gorsuch: Thank you, counsel.

Chief Justice Roberts: Justice Kavanaugh?

Justice Kavanaugh: Thank you, Mr. Chief Justice. Good morning, Mr. Finger. Picking up on a question earlier from Justice Gorsuch, there is a long tradition of governors considering political affiliation when selecting judges. Delaware seems to just make explicit what has been implicit in many states that leave it to the governor. Why, then -- given that traditional practice matters in First Amendment analysis, why is that different in kind than governors considering political affiliation?

Mr. Finger: Because, Justice Kavanaugh, it's not an exclusive fact. Taking the federal bench for -- just, for example, since President Roosevelt, there has been approximately 5 to 10 percent of appointees coming from the other party. And I take this from a law review article that appeared in the amicus brief of the former justices of the Delaware Supreme Court. That same law review article also shows that, since President Carter, there's been an increase too of about 5 percent of -- of candidates -- of appointments.

Justice Kavanaugh: So --

Mr. Finger: But roughly --

Justice Kavanaugh: -- I'm sorry to interrupt. So the problem is the categorical nature of Delaware's rule. I think I understand that. Mr. McConnell also identifies, I guess, what I

would describe as the "leave well enough alone" principle, that the results in Delaware have been superb with judges, you know, Collins Seitz and Bill Allen and Leo Strine and Norm Veasey, and leading lights of the judiciary. What's your response to that argument, that it's produced an excellent, widely respected judiciary?

Mr. Finger: Again, there's no evidence that this highly respected and -- and properly recognized judiciary actually results from this provision. That's a -- that's a case of a sort of illusory truth effect where a statement is made over and over and people tend to believe it more. But there's nothing concrete to -- to -- to support that. It's not really even intuitive.

Justice Kavanaugh: Okay. Next question is, if you were to win here, what would happen to partisan balance requirements for federal independent agencies, state redistricting commissions, state judicial nominating commissions, and the like?

Mr. Finger: Well, nothing should directly follow from that. These -- these various agencies and commissions, they all have different interests involved. So a decision by this Court will not *per se* do away with those requirements.

Justice Kavanaugh: Thank you, Mr. Finger.

Mr. Finger: Thank you.

Chief Justice Roberts: Mr. Finger, why don't you take a minute to wrap up.

Mr. Finger: Thank you, Your Honor. I thank the Court for the opportunity. In conclusion, I just want to say the state's interest in the stability of its judicial system should -- should not permit it to insulate the judiciary from Independents or unaffiliateds or members of minor -- major political parties. The goals are not met by the provisions, and the assumptions underlying them, as set forth in the brief, indicate that they are not achieving that goal solely on that basis. There are other factors in Delaware which create an excellent judiciary and will continue to do so without these limitations on the rights of people other than Democrats and Republicans. I thank the Court.

Chief Justice Roberts: Thank you, counsel. Mr. McConnell, three minutes for rebuttal.

REBUTTAL ARGUMENT OF MICHAEL W. McCONNELL ON BEHALF OF THE PETITIONER

Mr. McConnell: Thank you very much, Mr. Chief Justice. The -- I want to address a couple of small points and then -- and then the major one. In Justice Breyer's discussions, both with me and with Mr. Finger, we talked about sincerity. But -- and I even used the word "sincerity," but I want to emphasize that the ultimate test here isn't whether Mr. Adams was sincere. The question is whether applying would be futile. And that's a question of fact. It's not a question of -- of sincerity. And then, ultimately, the question is whether a trier of fact, reasonable trier of fact, could have -- have found on this record against Mr. Finger -- Mr. Adams on the summary judgment motion.

Now the second small point that --that I would like to emphasize here is that severability is a -- which we didn't discuss a great deal today -- is of enormous practical importance because, even if the major party provision were struck down, there is no justification for striking down the bare majority provision. It -- it's especially clear because Mr. Adams does not even have standing to challenge that. And it does -- we know that it could stand on its own because it does -- it has for so many years, and it's of -- you know, of grave importance to the state that even if we were to lose on the major party provision, that the -- that the bare majority provision still stand.

But, finally, I want to turn to the merits, which is really what matters here. And the -- the -- we believe that under *Gregory versus Ashcroft*, as well as *Branti* and -- and *Elrod*, that strict scrutiny is not appropriate, that the language used by the courts in -- in the patronage cases all involve reasonableness. Is there a reasonable relation between the requirement? And this is because it's basically an unconstitutional conditions case.

What Mr. Adams is alleging is that he's being denied an available public benefit because of his exercise of a constitutional right. But that kind of an argument doesn't work if the restriction is germane to the purpose for which the benefit was -- was created. So strict scrutiny should not apply. But, even if it did apply, the question is whether the challenged provision confers a compelling governmental interest in the least restrictive way. And, here, no one doubts that the state has a compelling interest in promoting public confidence in the judiciary. Now the bare majority requirement may be sufficient to achieve that interest under normal circumstances, where political parties seesaw back and forth, but the major party provision makes the bare majority provision more effective, especially under the actual circumstances here of long --

Chief Justice Roberts: Thank you, counsel.

Mr. McConnell: -- party domination. Thank you.

Chief Justice Roberts: Thank you counsel. The case is submitted.

(Whereupon, at 11:05 a.m., the case was submitted.)

~~MA~~

Earn-outs as Consideration

The Implied Duty of Good Faith and Fair Dealing & The Obligation of Commercially Reasonable Efforts

by Rebecca Seidl, Ana Estrada, Nicole Cors and Paul Crimmins

Rebecca Seidl is counsel in Mayer Brown's Houston office and a member of the Corporate & Securities practice group and Global Oil & Gas and Infrastructure Investment groups. Rebecca has a broad transactional practice, specialized in M&A and strategic investments across the energy industry.

Ana Estrada is a Corporate & Securities associate in Mayer Brown's Houston office. She represents publicly held and privately owned companies on a variety of domestic and cross-border transactional matters, with an emphasis on Latin America.

Nicole Cors is an associate in Mayer Brown's Chicago office and a member of the Corporate & Securities practice. Prior to attending law school, she worked as a financial analyst at an international technology company.

Paul Crimmins concentrates his practice on mergers and acquisitions, joint ventures, and general corporate representation. He advises some of Mayer Brown's largest corporate clients, and serves as the co-lead of Mayer Brown's Chicago Corporate & Securities practice.

Introduction

One of the more popular mechanisms to bridge valuation differences is the use of an earn-out. An earn-out is a mechanism whereby a portion of the purchase price is contingent and calculated based on the performance of the acquired business over a specified time period following closing. Earn-outs are intended to bridge a valuation gap between an optimistic seller and a skeptical, or cash-strapped, buyer.

An earn-out can also serve as a form of incentive-based compensation to sellers who continue on as management, and thereby allow buyers to retain and motivate management with aligned interests of maximizing profit. An earn-out used for these purposes can help facilitate a smooth transition of the acquired business to the buyer even though the seller's management may no longer have traditional equity in the acquired business.

Although no standard earn-out model exists, there are several principal considerations that should be addressed in the negotiation and drafting of an earn-out provision: (1) the definition and the scope of the acquired business, the performance of which will determine whether the earn-out is achieved; (2) the selection of the performance metric; (3) the selection of an appropriate accounting measurement standard; (4) the establishment of the earn-out period and determination of the payout structure; (5) the allocation of control of the acquired business between the buyer and the seller during the earn-out period; and (6) the level of support (if any) that the buyer will commit to give the acquired business in attempting to achieve its earn-out objectives. This briefing memo addresses recent case law developments in three areas: the implied duty of good faith and fair dealing (often asserted in cases of alleged misconduct or failure to properly support the acquired business), the interpretation of clauses requiring use of "reasonable efforts" toward the achievement of the earn-out (items 5 and 6 of the list in the previous sentence), and the challenges of proving damages (causation) notwithstanding a breach. Examination of these cases provides useful guidance in crafting and documenting earn out provisions.

Recent Developments in Case Law

1. The Implied Covenant of Good Faith and

Fair Dealing

One theory that sellers will commonly invoke in disputes over earn-out provisions is that the buyer breached the implied covenant of good faith and fair dealing causing the seller to miss the earn-out. The argument is that the buyer breached the implied covenant of good faith and fair dealing by operating the acquired business in a manner that frustrated the achievement of the earn-out (i.e., didn't act fairly), notwithstanding that the cited actions were not expressly restricted in the acquisition agreement. In general, the implied duty of good faith and fair dealing prohibits either party to a contract from doing anything that will destroy or injure the right of the other party to receive the benefit of the contract.

An example of the practical application of this theory, albeit with a focus on the post-closing conduct of the sellers, was presented in *Vista Outdoor, Inc. v. Reeves Family Trust*.[1] In this case, the Court evaluated whether former executives and co-founders of the seller breached the implied covenant of good faith and fair dealing through self-dealing transactions devised to inflate profits that would trigger the earn-out payment. Here, Vista Outdoor, Inc. acquired Jimmy Styks in a purchase agreement that provided for a $40M earn-out payment if certain targets were met. The buyer hired the former co-owners and executives of the seller to run the acquired business after an unsuccessful first year following the closing. The executives planned to meet the earn-out by introducing a new high-margin product that was previously given to customers for free and personally purchasing the entire inventory in order to inflate revenues and trigger an earn-out payment. The Court found that the executives did not use appropriate means to satisfy the earn-out, thereby breaching the implied covenant of good faith and fair dealing. In reaching this conclusion, the Court reasoned that through the transaction, the executives knowingly acted to artificially increase profits during a critical period, thereby overstating the value of the acquired business. Further, the transaction was outside of the ordinary course of business, inconsistent with past practice, and was intended to manipulate the earn-out, running afoul of the implied covenant of good faith and fair dealing.

Collab9, LLC v. En Pointe Technologies Sales, LLC[2] provides another example of the practical application of this theory, focusing on the actions of the buyers. In this case, the seller sold substantially all of its assets to the buyer. The parties agreed that the buyer would be responsible for business operations post-closing and additional earn-out payments would be made if the buyer met certain revenue and profit targets. The seller alleged that the buyer took actions to prevent the achievement of earn-out payments, including transferring contracts to a sham entity, transferring salespersons and accounts, and providing knowingly false earn-out certifications and statements. The buyer made a motion to dismiss. The court granted the buyer's motion to dismiss, finding that the implied covenant argument was duplicative of claims of breach of contract. The Court found that the asset purchase agreement was comprehensive and explicitly granted the buyer discretion to operate the business and that the agreement explicitly stated that the seller did not have express or implied obligations to maximize the earn-out. The Court reasoned that the implied covenant of good faith and fair dealing is a gap-filler for matters that the parties had not anticipated and that applying the implied covenant of good faith and fair dealing would give the seller rights beyond those bargained for in the contract.

However, oftentimes a Court will require an explicit contractual provision of good faith and fair dealing, as was the case in *Lazard Technology Partners, LLC v. Qinetiq North America Operations*.[3] Here, the parties negotiated a merger agreement that included a $40M closing payment and a $40M earn-out dependent on the revenue streams. The earn-out provision in the merger agreement prohibited the buyer from diverting or deferring revenue in order to reduce or limit the earn-out payment. During the earn-out period, the revenues did not reach the required level and the seller brought suit. Under the merger agreement, the buyer was not permitted to take any actions, carried out with the intention of avoiding the earn-out. The seller contended that the buyer had breached the requirements of the earn-out provision and, further, the covenant of good faith and fair dealing. In this case, the Court upheld the plain meaning of the merger agreement and the Court concluded that the seller was not permitted to rely on the covenant of good faith and fair dealing in order to limit the buyer's conduct under the merger agreement. In reaching this determination, the Court noted two important points: one, that the merger agreement only required the buyer to run the business in a manner that did not interfere with the earn-out payment (as opposed to affirmatively helping the business) and two, that the seller had attempted to include additional post-closing obligations in the agreement that were eventu-

Earn-outs ➔

Rebecca Seidl
Mayer Brown

Ana Estrada
Mayer Brown

Nicole Cors
Mayer Brown

Paul Crimmins
Mayer Brown

Earn-outs

continued

ally left out. Ultimately, the Court reasoned that the implied covenant of good faith and fair dealing should be explicitly included in a merger agreement, in order for any party to benefit from such an obligation.

Similarly in *American Capital Acquisition Partners, LLC v. LPL Holdings, Inc.*[4] the parties entered into a stock purchase agreement in which LPL acquired 100% of the outstanding equity interests in a subsidiary of American Capital Acquisition Partners, LLC, Concord Capital Partners, Inc. Under the agreement, the parties established a contingent purchase price provision of up to $15M, which depended upon the amount of gross margin above the set thresholds. In this case, the seller argued that the buyer breached the implied covenant of good faith and fair dealing in two ways: one, the buyer failed to meet its affirmative obligation to make sufficient technological adaptations and two, the buyer took actions to shift employees and customers in order to avoid the earn-out payment. On the first point (failure to affirmatively support), the Court did not apply the implied covenant of good faith and fair dealing, reasoning that the implied covenant could only be invoked to fill a gap when it was clear that the parties would have agreed to the provision. Here, the parties did not negotiate for any provision at this point and thus, the Court refused to find the implied covenant of good faith and fair dealing. On the second point, the Court reasoned that if the buyer had not interfered and shifted the sales, the earn-out target would have been reached and the earn-out payment triggered. For this reason, the Court ultimately found that the buyer had breached the implied covenant of good faith and fair dealing by shifting sales to avoid the earn-out payment.

Courts have also refused to apply the implied duty of good faith and fair dealing if express efforts provisions, or even general "reasonable efforts," are included. In *Fortis Advisors LLC v. Dialog Semiconductor PLC*,[5] the buyer acquired a semiconductor business for $310M, with an earn-out payment of up to $35M, dependent on post-merger revenues during two periods. The parties negotiated the terms of the earn-out payment, including an express requirement to use commercially reasonable best efforts to achieve the revenues required for the earn-out payments. The provision further included specific obligations and prohibitions regarding the operation of the acquired business. At the end of the earn-out period, the buyer failed to achieve sufficient revenues to trigger the earn-out payment and the seller sued, arguing that the buyer breached its contractual obligations and also breached the implied duty of good faith and fair dealing. The Court dismissed the case, ultimately determining that the seller had failed to state a claim from which relief could be granted. In reaching this conclusion, the Court reasoned that the duty of good faith and fair dealing only applies to agreements that are missing specific language needed to give effect to otherwise negotiated for provisions. Here, the seller was not able to demonstrate a gap or ambiguity in the earn-out provision or the merger agreement with regards to the requirements of the business operations. Rather, the Court determined that the earn-out provision included the express language (use of commercially reasonable efforts and specific prohibitions) to properly evaluate the earn-out provision and therefore decided to dismiss the seller's claim.

These cases demonstrate that the implied covenant of good faith and fair dealing will not impose new, not negotiated for obligations (and certainly won't impose an obligation that was rejected in the deal negotiations). Sellers need to bear in mind that this is a "gap filling" mechanism, assisting in the reasonable implementation of negotiated provisions or preventing misconduct. The trending case law does not seem to support use of this implied covenant to provide affirmative support toward achieving the earn out targets.

2. Commercially Reasonable Efforts

Historically, the implied covenant of good faith and fair dealing has been the primary theory invoked by a party where there has been no breach of an express covenant in an acquisition agreement. However, the acquisition agreement will often include a general "commercially reasonable efforts" obligation. The commercially reasonable efforts obligation has been asserted to impose on buyers an obligation to take additional affirmative steps to promote and develop the products of the acquired business.

The application of such a clause is demonstrated in *Merrit Quarum v. Mitchell International, Inc.*[6] In this case, the buyer entered into a stock purchase agreement to acquire several individual sellers' shares in a medical industry software company. The parties executed a stock purchase agreement with an earn-out provision and an employment agreement in which one of the sellers would remain employed with the company. The earn-out agreement included express cov-

enants which regulated the operations and provided additional compensation to the sellers based on sales benchmarks two years following closing. When the benchmarks were not met, the sellers alleged breach of the earn-out provision. The seller claimed that the buyer did not act in good faith or use commercially reasonable efforts to improve sales. In reaching a decision, the Court evaluated a negative covenant in the earn-out agreement in which the buyer agreed to act in good faith and a commercially reasonable manner to avoid actions that would decrease the earn-out payment. The Court ultimately determined that the language of the expressly negotiated provision required the buyer to refrain from taking an affirmative action to frustrate the earn-out. Note the negotiated language basically prevented the buyer from interfering, but it did not require the buyer to affirmatively support the business. Therefore, the Court determined that there was no breach of the obligation to use commercially reasonable efforts.

In the case of *Himawan v Cephalon*,[7] the Court refused to dismiss the seller's claims that the buyer had breached its obligations under the merger agreement. As part of the merger agreement, an earn-out provision required the buyer to use commercially reasonable efforts to market two developmental disease treatments. The buyer successfully marketed the first treatment and subsequently made corresponding earn-out payments. However, the buyer abandoned the development of the second treatment and made no further earn-out payments to the seller. In refusing to dismiss the seller's claims, the Court specifically considered the definition of commercially reasonable efforts within the merger agreement. The Court determined that the earn-out provision was clear and unambiguous in outlining the expected obligations to be fulfilled by the buyer. The Court also considered the seller's contention that other companies, similarly situated to that of the buyer, had pursued similar disease treatments to that of the one abandoned by the buyer. For this reason, the Court determined that the dispute ultimately created issues of fact with regard to whether the buyer's actions were "commercially reasonable," and the claim withstood a motion to dismiss.

In agreeing to "commercially reasonable" provisions, sellers need to be sensitive to the actions that the standard qualifies - i.e., is it to use efforts merely not to interfere, or conversely to affirmatively support the acquired business. The latter (affirmative efforts) would seem to subsume the non-interference covenant. Finally, sellers need to be aware that a commercially reasonable efforts clause does permit a weighing of the buyer's considerations, and may not constitute an unconditional obligation.

3. Damages

Even where a seller is successful in proving a breach of an acquisition agreement in relation to an earn-out, the seller will not receive damages unless it can prove that it would have met its earn-out targets but for the buyer's breach. For example in *Holland Loader Company LLC v. FLSmidth AS*,[8] the Court found that, despite the buyer's breach by failure to use commercially reasonable efforts to market and sell products, the seller could not prove damages. In its decision the Court reasoned that the damages calculation was too speculative to be considered because it was based on projections to secure internal research and development funding instead of sales projections and historical data.

In *Bergheim v. Sirona Dental Systems Inc.*,[9] the buyer purchased a computer-aided design start-up, negotiating an earn-out provision based upon revenues and sales targets for a new technology. The seller was awarded the earn-out payment following arbitration. The buyer then sued, arguing that damages could not be calculated on a new product. However, the Court upheld the arbitration decision granting damages. It reasoned that the damages were established with reasonable certainty by using historical and expert information about sales data, seemingly a fact based question that could have gone either way.

Due to the challenges associated with proving earn-out damages, sellers may wish to consider including some type of liquidated damages provision.

Conclusion

Earn-outs may be a useful method for parties to M&A transactions to bridge valuation differences. However, earn-outs are complicated and parties to an M&A transaction may find that earn-outs simply delay disputes rather than resolve them. To minimize the risk of disputes, it is essential that the earn-out provisions be carefully negotiated and documented. Optimally the parties will attempt to mitigate the risk of the most common sources of earn-out-related litigation by considering whether to clearly and comprehensively specify the degree of control the buyer and seller will have over the acquired business during the earn-out period and the level of support that the buyer will be obligated to provide to the acquired business. Lacking that,

Earn-outs ➔

Earn-outs

continued

sellers might rely on a more general "reasonable efforts" provision, or actual implied duty of good faith and fair dealing, but, as discussed above, courts will in some cases limit the application of such remedies.

Footnotes

1 234 F. Supp. 3d. 558 (S.D.N.Y. 2017).
2 2019 WL 4454412 (Sup. Ct. Del.)
3 No. 464 (S.C. Del. 2014).
4 014 WL 354496 (Del. Ct. Chancery).
5 2015 WL 401371 (Del. Ct. Chancery).
6 2020 WL 351291 (S.C. Del.).
7 2018 WL 6822708 (Del. Ch. Dec. 28, 2018).
8 796 Fed. App'x 40 (2d. Cir. 2019).
9 2017 WL 354182 (S.D.N.Y).

~~MA~~

Part II
Covid v. Bar Exam
A case of students ensnared

In our last issue, (Volume 20, Number 7), we wrote about the plight of two young lawyers whose identities were protected by the pseudonyms "Mary" and "Susan," both bedeviled by the mayhem inflicted on them during the pandemic as they try to begin their careers in Big Law. This is Part II of their saga.

On the morning of October 5, the day that Washington, D.C. was to administer its bar exam along with eighteen other jurisdictions, Mary noticed a construction crew arriving at the building to begin drywall repairs on a neighboring apartment that had also suffered damage in the same storm that collapsed Mary's and Susan's own ceiling. "Of course, it's 2020. Of course there is a construction crew about to start hammering away on the day of the first at-home, on-line bar exam in the country's history," Mary remembers thinking to herself. The obliging neighbor agreed to postpone the repairs until the exam was over.

It would be a long two days. Already, over the previous week the D.C. bar examiners were forced to admit that a breach in the system had released to the world all the character-and-fitness applications of all its bar applicants. "You could not find a document with more personal information about all of us," says Mary. "I've never put so many facts about myself in one file, from details of my last eleven years of life, to my social security number, to my grandmother's maiden name. All suddenly without a firewall."

On the day of the test, perhaps the most egregious and cringe-making of all the many stumbles came when the facial recognition software consistently failed to verify people of color. "Could there be a more apt metaphor for the legal profession's general attitude toward desperate law graduates during the pandemic?" Mary asks. "And as for young people of color, could there be a more stinging manifestation of systemic racism than to be shut out of a profession because you cannot be recognized or even seen?"

Many of the actual questions on the bar exam perplexed a number of students. "I paid for a program that shows you the last 6,000 questions on the bar exam so I could practice for my test," Mary says. "The questions on the D.C. bar often bore no resemblance to those of the past. They seemed oddly out of context and often nonsensical." There were also computer crashes aplenty, as well as the danger of a computer shutdown. "I spent the last set of multiple-choice questions watching the battery life on my computer steadily decrease," Mary says. "My last fifty questions were spent anxiously watching it tick ever lower—38 percent left, then 37 percent, 36, 35—I was racing against the clock."

Mary had spent the night before taking the required mock exam and practicing compliance with the myriad rules apparently designed to prevent cheating, surely the most peculiar set of regulations ever imposed on students taking a standardized test. "For example," she says, "I tend to twirl my hair when I read. That's one of

the things that was impermissible. While forcing myself to stop doing it, I found myself mouthing the words of what I was reading to help process the questions. That's another thing that's not allowed. So I'm sitting there trying not to move, trying not to break any rules, trying not to do the wrong things and trying to focus on answering the practice questions."

Test takers were not allowed to let their eyes leave the screen. No one was allowed to touch his or her face or hair. Leaving one's seat was not allowed, not even to answer the calls of nature. No menstrual products were on the list of permitted items. One test taker recalls how she had to leave the room to deal with her menstruation and, by doing so, failed the exam. A woman at the Washington, D.C. bar exam took her laptop into the bathroom with her, maintaining the required eye contact with her computer the entire time, and peed in full view of the camera. A male student simply peed in place and finished the last thirty minutes of the exam sitting in his own urine.

One bar exam even had its own newborn baby as the proverbial silver lining to the tumultuous clouds. A May graduate of the Loyola University Chicago School of Law, Brianna Hill's exam was scheduled for July 28 so it seemed there would be no conflict between her pregnancy and the exam. After all, she was not due until October 19. But when the test was not given in July and eventually scheduled for early October, Ms. Hill knew she would then be 38 weeks pregnant. She emailed the Illinois bar examiners, explained her situation, and asked for more bathroom breaks. Her request was denied.

She began taking the exam in her home office and toward the end of the first section she felt her water break, she told The New York Times. She knew that if she left her seat, she would be disqualified. She finished the first section 45 minutes after her labor had started and then, during the half hour break before the second section was to begin, she phoned her midwife at the hospital, who assured her they didn't need to see her immediately. So she finished the second section and only then did her husband rush her to the hospital. Three hours later, she gave birth to her son, Cassius Phillip Hill Andrew.

There was still the second test day to get through. The next morning, after a long night, she finished the final two sections of the bar exam from her hospital bed, with her husband in charge of their new-born. She nursed her son during the break between the two sections, completing the bar exam without breaking any of the rules. "The whole time, my husband and I were talking about how I wanted to finish the test and my midwife and nurses were on board," she was quoted as saying. "There just wasn't another option in mind."

There were once many options for lawyers trying to enter the profession in the U.S. In the colonial era, for example, it was the local courts that handled this task, typically after aspiring attorneys had studied the law on their own and completed some form of apprenticeship that met with court approval. These training periods could last as long as a decade or more. In some colonies, one had to apply to each court for permission to come before it. In others, a stamp of approval from the highest court would open the doors of all that colony's courts to successful applicants. Those who had been admitted to the profession by England's Inns of Court, in contrast, were considered entitled to practice in any of the thirteen colonies. After the revolution, most states set up their own requirements for bar admission, which varied extensively. There were virtually no law schools at the time. They would not become commonplace until after the Civil War and the onset of the more complex economy of the industrial revolution.

During the 1820s and 1830s and into the Civil War, admission standards became "erratic and whimsical," and steadily all but disappeared, according to a 1995 note in the Case Western Reserve University School of Law, entitled "Do We Need the Bar Examination?, by Daniel R. Hansen. This was largely due to a growing sense that to set up rigid professional requirements would be to encourage an elitism that would be contrary to democratic ideals, according to Mr. Hansen in his law review article. After all, only the rich would be able to meet the standards. Only the well-connected could set up apprenticeships with established practitioners. Instead, public sentiment of the day favored getting rid of all admissions requirements so that virtually any White male could call himself a lawyer. Exams still existed, Mr. Hansen explains, but they were flawed affairs because the courts had no expertise in administering standardized tests or forming the necessary series of questions.

Often the exams that did exist were peculiar affairs. Mr. Hanen cites an anecdote about Abraham Lincoln, a member of the Illinois board of examiners, who once quizzed an applicant from the bathtub. "He asked me in a desultory way the definition of a contract," the applicant would later write, "and two or three fundamental questions, all of which I answered readily, and I thought, correctly. Beyond these meager

Covid v. Bar Exam ➔

Covid v. Bar Exam

continued

inquiries . . . he asked nothing more. As he continued his toilet, he entertained me with recollections—many of them characteristically vivid and racy—of his early practice and the various incidents and adventures that attended his start in the profession. The whole proceeding was so unusual and queer, if not grotesque, that I was at a loss to determine whether I was really being examined at all."

From 1870 on, law schools began to proliferate around the country, but apprenticeships were still the most popular method of becoming a lawyer. Diploma privilege, joining the bar simply by graduating from a law school, developed partly as a marketing tool to entice students to attend the new academies. Professing to be alarmed at the lack of uniform standards among the law schools, the ABA delivered a mortal blow to diploma privilege in 1921. The organization proclaimed that it was "of the opinion that graduation from a law school should not confer the right of admission to the bar, and that every candidate should be subject to an examination by public authority to determine his fitness." Thus did the bar exam come into its own.

There is range of justifications for the exam that has changed little since the second decade of the twentieth century. It is said that it cuts off incompetent applicants, that it motivates students to work hard in law school, that it ensures that law schools maintain high standards and that applicants get a comprehensive understanding of the law. In the modern era, these arguments in favor of the efficacy and purpose of the exam still abound and have for decades.

In his Case Western article, back in 1955 for example, Mr. Hansen marches through the history and the justifications for the bar exam and dismisses the history as chilling and the justifications as specious. Among other flaws, he finds the exam nothing more than a test of memorization. "Rather than testing for competency (or incompetency)," he writes, "the bar exam is essentially an achievement test and does not test for what lawyers actually do. In fact, there is strong evidence to suggest that the bar exam merely verifies what has already taken place in the law school."

The chaos and cruelty of this year's test has renewed cries to eliminate the bar exam altogether. It is being witheringly criticized as merely a clumsy way to sustain the law guild as just that—an association that preserves its power and wealth by granting admission to the few, the same argument of the 1820s against elitism. There has never been any evidence that the exam helps to make sure that only the qualified can practice, nor that it serves any goal of excellence or motivation not already achieved by less problematic means.

Like so much else in American history, including such institutions as the electoral college, the exam can be seen to have arisen from a desire to exclude the unwanted from the profession. That zeal was on glaring display a few years before the bar exam was born. In 1911, three Black lawyers—William H. Lewis and Butler R. Wilson, both of Massachusetts, and William R. Morris of Minnesota—gained admission to the American Bar Association. These were men of high accomplishment and social standing. Their application process did not reveal their ethnicity, however, and when this was discovered, the horrified ABA rescinded their admission in 1912, proclaiming that "the settled practice of the Association has been to elect only White men to membership." There is an argument to be made that the more subtle means of law school accreditation and the bar exam can be deployed in furtherance of the same end.

~~MA~~

Website: www.themandajournal.com

E-mail: info@themandajournal.com

Editorial Office: 215-309-5724

Orders & Subscriptions: For individual subscriptions, discounted multi-copy institutional subscription rates, or additional copies, please call 215-309-5724 or fax 215-309-5724.

THE M&A JOURNAL
the independent report on deals and dealmakers

Editor/Publisher	**John Close**
Design and Production	**John Boudreau**
Senior Writers	**Gay Jervey, R. L. Weiner**
Writing/Research	**Frank Coffee, Jeff Gurner, Terry Lefton**
Circulation	**Dan Matisa**
Web Production	**John Boudreau**

The M&A Journal, 1008 Spruce Street, Suite 2R, Philadelphia, PA 19107