

# Delaware Court Identifies Numerous Issues Regarding Medley Capital Corporation Board

*Excerpts from the Delaware Chancery Court's March 11 Memorandum Opinion on how the MCC directors—including those now up for reelection—"violated their fiduciary duties" to MCC stockholders*

## Executive Summary

At its Annual Meeting on June 4, 2019, the MCC board is asking stockholders to re-elect members of the board of directors that was found in March to have violated its fiduciary duties to you, MCC's stockholders.

The below excerpts from the [Delaware Chancery Court's Memorandum Opinion](#) highlight the board's troubling behavior.

NexPoint believes MCC stockholders should review this account when evaluating Seth Taube and Arthur Ainsberg, and we urge you to consider how the incumbent directors failed to protect stockholders' interests as you vote at the Annual Meeting on June 4, 2019.

NexPoint urges MCC stockholders to:

- **Reject the incumbent directors and vote FOR NexPoint's truly independent nominees.**
- **Vote using your BLUE proxy card to elect Stephen A. Mongillo and Mark T Goglia to the board.**

Learn more about the alternative director candidates, NexPoint's truly independent nominees, at [www.MedleyCapitalVote.com/nominees](http://www.MedleyCapitalVote.com/nominees).

## Opinion Overview

“...the Court holds that Medley Capital’s directors violated their fiduciary duties in entering into the Proposed Transactions.”

- “[T]he majority of the members of the special committee failed to act independently when negotiating the Proposed Transactions.” – Page 5

At no point in time is this protection more critical than in the context of a conflicted transaction. In this case, FrontFour has demonstrated that the Taube brothers are controllers not because of flaws inherent in the structure of BDCs, but rather, **because those tasked with standing independent from the Taube brothers willfully deferred to their authority.**” – Page 65

- “[T]he timing, structure, initiation, and negotiation of the Proposed Transactions were conceived for the purpose of—and did—advance the Taubes’ interest at the expense of Medley Capital’s other stockholders.” – Page 66

- “Defendants violated their duties of disclosure to inform stockholders of the process that led to the Proposed Transactions and the expressions of interest from third parties.”- Page 75

- “To recap, FrontFour has proven that: **Conflicted insiders tainted the process** that led to the Proposed Transactions. **The Special Committee negotiated with willful blinders**, not knowing: the value that third-parties had placed on Medley Management; that Medley Management felt “enormous pressure” to enter into a transaction; that standstill agreements prevented third parties from coming forward; and that Medley Management—not Medley Capital—was shopped in the 2017 sale process on which they relied when determining not to conduct a pre-signing market check.

Compounding these problems, **the Special Committee agreed to deal protections preventing an effective post-signing market check**”. – Pages 84-86

- “For the foregoing reasons, the Court holds that Medley Capital’s directors violated their fiduciary duties in entering into the Proposed Transactions.” – Page 87

## The Board’s Process for Evaluating the Transactions

“a deeply flawed process [that] obscure[d] the fair value of Medley Capital”

- “The proxy creates the **misleading impression** that the special committee replicated arm’s-length negotiations amid the conflicts tainting the Proposed Transactions. To vote on an informed basis, the stockholders must know the reality—that **the majority of the**

members of the special committee failed to act independently when negotiating the Proposed Transactions.” – Page 5

- “Critically, **none of the committee members knew** that approximately thirty confidentiality agreements contractually foreclosed potential third parties from proposing a transaction with Medley Capital.” – Page 38
- “The **Special Committee did not probe meaningfully** into the value of Medley Management.” – Page 39
- “Also, the **Special Committee did not know** about two expressions of interest from third parties concerning a transaction with Medley Capital.” – Page 39
- “Ultimately, **this is a case in which a deeply flawed process obscures the fair value of Medley Capital**. The record reveals that Taube brothers obstructed any pre-signing price competition from ‘interlopers.’” – Page 68

## The Taube Brothers’ Influence

“In the end, the Special Committee allowed Medley Management to extract a huge [approximately 100%] premium while Medley Capital stockholders received none.

- “In reality, when the Taube brothers proposed the transactions in June 2018, **Medley Management was facing enormous financial pressure**. Medley Management had engaged in two sales processes in 2017, both of which failed, which left merging with affiliates as Medley Management’s only solution.” – Page 3
- “Brook Taube had conceived of this transaction in March 2018 as a fallback to the Party X deal”. – Page 24
- “Then, throughout the negotiations, Brook Taube **pressured the Special Committee** to stick to the aggressive timeline.” – Page 33
- “[Brook Taube] instructed Tonkel: ‘Thursday board meetings are the time to **push these guys hard** in person.’” – Page 34
- “On February 1, 2019, NexPoint made both its proposals public. On February 6, 2019, Medley Capital and Sierra issued a press release indicating that their respective special committees had unanimously determined not to pursue the second NexPoint Proposal. The press release purported to identify the reasoning behind the determinations by the Special Committees. **But Medley Management had drafted the press release before the Special Committee had even made its determination.**” – Page 49-50
- “The Special Committee also sat supine in negotiations concerning the Proposed Transactions, **allowing the Taube brothers to dominate the process**...In the end, the

**Special Committee allowed Medley Management to extract a huge [approximately 100%] premium while Medley Capital stockholders received none.” – Page 63-64**

- **“In this case, the timing, structure, initiation, and negotiation of the Proposed Transactions were conceived for the purpose of—and did—advance the Taubes’ interest at the expense of Medley Capital’s other stockholders. In the events leading up to the Proposed Transactions, the Taube brothers created an informational vacuum, which they then exploited. The Special Committee was not truly independent and did not negotiate at arm’s length.” – Page 66**

## The Special Committee’s “Ignorance”

**“special committee members determined not to run any pre-signing market check or consider alternative transactions”**

- **“In reality, during the negotiation process, the Special Committee was disabled by its ignorance of: the details of the bids made for Medley Management during Project Elevate; the ‘enormous pressure’ facing Medley Management and the Taubes; and the standstill agreements that forbade potential transaction partners from presenting proposals directly to Medley Capital...” – Page 76**
- **“The Medley Capital special committees did not know any of this information before this litigation. They were not told. They did not ask.” – Page 4**
- **“In the midst of this informational vacuum, Medley Capital’s special committee members determined not to run any pre-signing market check or consider alternative transactions... They capitulated to the aggressive timeline, although Medley Capital had no business reasons for rushing toward a deal.” – Page 4**
- **“Before this litigation, the Special Committee was unaware of the pressures Medley Management faced during this time period. In a candid moment during trial, Ainsberg admitted that he wished he had known.” – Page 23**
- **“The Special Committee did not analyze the value of Medley Management, or understand what Medley Management would obtain in the Proposed Transactions, although in effect Medley Capital and Medley Management were competing for consideration.” – Page 35**
- **“The Special Committee did not consider alternative transactions, although disgruntled stockholders were publicly advocating for a sale process as of April 2018.” – Page 35**
- **“The Special Committee did not conduct a pre-signing market check. When asked why, Hirtler-Garvey said she was happy with the transaction at hand. She wanted a deal with Medley Management.” – Page 36**
- **“Nor has anyone acting on behalf of the Special Committee contacted NexPoint or Origami, despite their expressed willingness to improve their proposals.” – Page 51**

## The Independent Directors' "Deference" to the Taube Brothers

**"the Taube brothers dominated and controlled the board"**

- "FrontFour proved that **half of the Medley Capital special committee was beholden to the Taube brothers**, and thus the **Taube brothers dominated and controlled the board** with respect to the Proposed Transactions." – Page 4
- "Out of the gate, the **Special Committee failed to assert control over the timing of the process**. At the June 2018 Medley Capital Board meeting, Medley Management presented an aggressive timeline, which contemplated that the parties would execute definitive transaction agreements and announce a transaction by July 31, 2018. This made sense for Medley Management, which had shopped itself for more than a year prior to that point. By contrast, Medley Capital had not undertaken any strategic process before the June meeting." – Page 32
- "The **Special Committee deferred to the Taube brothers** although the committee had ample negotiating leverage—the ability to terminate the Management Agreement or simply reject the deal, either of which would have had devastating consequences for Medley Management." – Page 64

## Insider Compensation and Poor Alignment of Interests

**"None of Medley Capital's fiduciaries (officers and directors) have interests aligned with the interests of Medley Capital's common stockholders."**

- "Another salient fact: **None of Medley Capital's fiduciaries (officers and directors) have interests aligned with the interests of Medley Capital's common stockholders**. As to the inside directors and management, their financial interests lie in Medley Management." – Page 12
- "**Ainsberg, Hirtler-Garvey, and Mack have each been paid over \$1 million for serving on the Board and its committees**. For the company's fiscal year ending September 30, 2018, Ainsberg earned \$299,000 as a Medley Capital director, **representing roughly half of his 2018 income**. By contrast, at the deal price, the value of ALL of the outside directors' combined common stock is under \$40,000." – Page 12
- "In the Proposed Transactions, **two of Medley Capital's four outside directors will serve on the Board of the combined company**; all four outside directors interviewed for the position after the Merger Agreement was signed." – Page 12

- “In a July 11, 2018, email to the Medley Management Board, Brook Taube emphasized that ‘[t]ime is not in our favor given performance, inquiries, letters, etc.’ He went on to underscore the fact that **the transaction represented a ‘100% premium and a great deal’ for Medley Management.**” – Page 34
- “Employment contracts connected to the merger provide for **lucrative positions for Medley Management’s senior management.** The cost of these employment contracts exceeds the estimated synergies arising from the Proposed Transactions.” – Page 44

## Medley Management’s Performance

### “Medley Capital’s ‘NAV has dropped for a remarkable fifteen quarters”

- “Since its January 20, 2011 IPO, by every industry measure, **Medley Capital has been in a steady financial decline.** This decline occurred during a period of sustained stock market and sector share price increases. Medley Capital’s performance is poor compared to its peers. Due to Medley Capital’s poor financial performance, Medley Management faced financial pressures.” – Page 14
- “By May 2018, Brook Taube felt that Medley Management was “under enormous pressure” financially. **Wells Fargo noted that Medley Capital’s ‘NAV has dropped for a remarkable fifteen quarters,’ and observed Medley Capital’s ‘severe underperformance.’** In Mack’s words, by May 2018, Medley Capital’s credit portfolio was ‘bottoming out.’ The management team faced fee waivers at Medley Capital and NAV issues ‘across the board,’ which would have a ‘meaningful impact on [Medley Management].’” – Page 21
- “Terminating the Management Agreement would trigger Fortress’s rights under the joint venture. Rejecting the deal would foreclose Medley Management’s only viable solution to the enormous financial pressure they labored under.” – Page 65

*FrontFour Capital Group LLC, et al. v. Brook Taube, et al., Case No. 2019-0100*

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**IMPORTANT INFORMATION:** On May 13, 2019, NexPoint Advisors, L.P. (“NexPoint”), together with the other participants named below, filed a proxy statement and accompanying BLUE proxy card with the SEC to solicit stockholder votes for the election of its slate of highly-qualified director nominees in connection with the Annual Meeting of Stockholders (the “Annual Meeting”) of the Company expected to take place on June 4, 2019.

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