

### IX. “Can You Buy Me Now?”: The Erratic Closing of the Verizon-Yahoo Merger

On July 25, 2016, telecommunications front-runner Verizon Telecommunications, Inc. (Verizon) announced its merger with search engine company, Yahoo! Inc. (Yahoo).<sup>948</sup> Verizon agreed to purchase most of Yahoo’s assets for \$4.83 billion.<sup>949</sup> In September 2016, after both parties signed a Stock Purchase Agreement solidifying the terms of the deal, Yahoo disclosed it had been the victim of a data breach in 2014 that compromised 500 million accounts.<sup>950</sup> Months later, in December 2016, Yahoo announced it had been the victim of a second data breach in 2013.<sup>951</sup> The 2013 breach compromised over one billion of its users’ accounts, making it “the largest known security breac[h] of one company’s computer network.”<sup>952</sup> After Yahoo disclosed the second data breach, a Verizon executive stated the company was uncertain about the future of the deal.<sup>953</sup>

On January 23, 2017, amidst speculation about the deal’s viability, the Securities and Exchange Commission (SEC) announced an investigation into “whether Yahoo Inc.’s two massive data breaches should have been reported sooner to investors . . . .”<sup>954</sup> Had Verizon wanted to exit the deal upon learning of the cybersecurity breaches,

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<sup>948</sup> Cristina Alesci et al., *Verizon is Buying Yahoo for \$4.8 Billion*, CNN MONEY (July 25, 2016), <http://money.cnn.com/2016/07/25/technology/yahoo-verizon-deal-sale/> [<https://perma.cc/GVD6-WH25>].

<sup>949</sup> *See id.*

<sup>950</sup> Ryan Knutson, *Verizon Executive Says Company Is Unsure About Yahoo Deal*, WALL ST. J. (Jan. 5, 2017), <http://www.wsj.com/articles/verizon-executive-says-company-is-unsure-about-yahoo-deal-1483636506> [<https://perma.cc/F8E8-5XJN>]. The agreement between the companies was dated July 23, 2016. YAHOO! INC. & VERIZON COMM’NS INC., STOCK PURCHASE AGREEMENT 1 (2016), <https://www.sec.gov/Archives/edgar/data/1011006/000119312516656036/d178500dex21.htm> [<https://perma.cc/3CEL-6ZSK>] [hereinafter STOCK PURCHASE AGREEMENT].

<sup>951</sup> Vindu Goel & Nicole Perlroth, *Yahoo Says 1 Billion User Accounts Were Hacked*, N.Y. TIMES (Dec. 14, 2016), <https://www.nytimes.com/2016/12/14/technology/yahoo-hack.html> [<https://perma.cc/PQA4-BKNV>].

<sup>952</sup> *Id.*

<sup>953</sup> Knutson, *supra* note 3.

<sup>954</sup> Aruna Viswanatha & Robert McMillan, *Yahoo Faces SEC Probe Over Data Breaches*, WALL ST. J. (Jan. 23, 2017), <http://www.wsj.com/articles/yahoo-faces-sec-probe-over-data-breaches-1485133124> [<https://perma.cc/BVF5-ZXVL>].

the material adverse effect (MAE) provisions woven throughout the Stock Purchase Agreement would have been Verizon's best defense to renegotiate or exit the deal.<sup>955</sup> Using an MAE provision to exit the deal, however, would have proven difficult for Verizon. Both companies are incorporated in Delaware and the Delaware Court of Chancery has yet to find in favor of a company invoking an MAE provision attempting to escape a merger agreement.<sup>956</sup>

Nevertheless, as announced on February 21, 2017, Verizon was able to renegotiate the deal to reduce the purchase price by \$350 million.<sup>957</sup> The terms of the amended Stock Purchase Agreement suggest the MAE clause had been used as leverage during negotiations to reduce the price, as "[u]nder the amended terms, the data breaches or losses will not be taken into account in determining whether a 'business material adverse effect' has occurred or whether certain closing conditions have been satisfied."<sup>958</sup>

On March 1, 2017, Yahoo, in its 10-K filing with the SEC, reported the findings of an independent board committee regarding Yahoo's knowledge and response to both hackings.<sup>959</sup> The findings concluded senior executives and legal staff learned of the existence of an undisclosed number of compromised accounts by late 2014, but

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<sup>955</sup> STOCK PURCHASE AGREEMENT, *supra* note 3, at 63 (outlining the conditions that must be met in order for Verizon to be bound by its obligations under the Stock Purchase Agreement). One representation and warranty made within the Stock Purchase Agreement was "[s]ince December 31, 2015, there has not occurred a Business Material Adverse Effect." *Id.* at 23. It follows that if Verizon were able to prove the data breaches constituted a "Business Material Adverse Effect," Verizon would not be obligated to close the deal with Yahoo.

<sup>956</sup> Steven Davidoff Solomon, *Why Verizon Can't Quit Yahoo*, N.Y. TIMES: DEALBOOK (Dec. 20, 2016), [https://www.nytimes.com/2016/12/20/business/dealbook/why-verizon-cant-quit-yahoo.html?\\_r=0](https://www.nytimes.com/2016/12/20/business/dealbook/why-verizon-cant-quit-yahoo.html?_r=0) [<https://perma.cc/8M4D-32QL>]; STOCK PURCHASE AGREEMENT, *supra* note 3 at 7, 27 (representing both companies are legally incorporated in the state of Delaware).

<sup>957</sup> Scott Moritz, *Verizon Reaches Deal for Lowered Yahoo Price After Hacks*, BLOOMBERG (Feb. 21, 2017), <https://www.bloomberg.com/news/articles/2017-02-21/verizon-said-to-reach-deal-for-lowered-yahoo-price-after-hacks> [<https://perma.cc/7HQH-7N6F>].

<sup>958</sup> Solomon, *supra* note 9. such findings ese findings,t remains to be seen if the SEC will take action against Yahoo that will further delay the closing of

<sup>959</sup> Yahoo! Inc., Annual Report (Form 10-K) 46 (Mar. 1, 2017) [hereinafter Yahoo Annual Report].

failed to properly investigate or inquire as to the knowledge of the company's security team.<sup>960</sup> The independent committee also ordered remedial actions after its findings.<sup>961</sup> Yahoo's CEO will not receive her 2016 cash bonus and the board accepted her offer to forfeit her 2017 annual equity award,<sup>962</sup> and the committee directed Yahoo to enhance its cybersecurity measures.<sup>963</sup>

This article discusses the delayed closing of the Yahoo-Verizon merger due to the disclosures of the cyber attacks Yahoo suffered in 2013 and 2014. Section A explains the terms of the Stock Purchase Agreement and Verizon's reasons for acquiring Yahoo. Next, Section B summarizes the two Yahoo cyber attacks and Verizon's reactions to each disclosure. Then, Section C describes how MAE clauses are used in merger agreements and discusses the likelihood that Verizon could have succeeded on an MAE claim. Section D discusses the SEC's investigation of whether Yahoo disclosed the 2013 and 2014 hackings in a timely manner, and Section E concludes.

### A. The Deal

The Verizon-Yahoo merger was expected to close in the first quarter of 2017.<sup>964</sup> According to the Stock Purchase Agreement signed

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<sup>960</sup> *See id.* at 47 (“[I]t appears certain senior executives did not properly comprehend or investigate, and therefore failed to act sufficiently upon, the full extent of knowledge known internally by the Company’s information security team.”).

<sup>961</sup> *Id.*

<sup>962</sup> *Id.*

<sup>963</sup> *See id.* at 47–48 (“[T]he Board has directed the Company to implement or enhance a number of corrective actions, including revision of its technical and legal information security incident response protocols to help ensure: escalation of cybersecurity incidents to senior executives and the Board of Directors; rigorous investigation of cybersecurity incidents and engagement of forensic experts as appropriate; rigorous assessment of and documenting any legal reporting obligations and engagement of outside counsel as appropriate; comprehensive risk assessments with respect to cybersecurity events; effective cross-functional communication regarding cybersecurity events; appropriate and timely disclosure of material cybersecurity incidents; and enhanced training and oversight to help ensure processes are followed.”).

<sup>964</sup> Alesci, *supra* note 1; Deepa Seetharaman & Ryan Knutson, *Yahoo Sees Verizon Deal Taking Longer Than Expected*, WALL ST. J. (Jan. 23, 2017), <https://www.wsj.com/articles/yahoo-sees-verizon-deal-taking-longer-than-expected-1485206759> [<https://perma.cc/M9XB-PBLL>].

by both parties, Verizon was supposed to purchase Yahoo's shares for \$4,825,800,000.<sup>965</sup> Excluded from the transaction were Yahoo's holdings in Yahoo Japan and Alibaba.<sup>966</sup> The sale will end Yahoo's twenty-one-year run as an independent company, during which it had rejected other lucrative offers.<sup>967</sup> The merger marks yet another effort by Verizon to garner a larger audience for its online platforms in order to generate revenue through advertising.<sup>968</sup> The deal is a natural progression of Verizon's increasing investment efforts in digital content and advertising following Verizon's purchase of AOL.<sup>969</sup> Yahoo's impressive number of monthly active users (MAUs),<sup>970</sup> at over one billion, is a high selling point for Verizon.<sup>971</sup> While "others in the space" have active users in the billions, Verizon's post-AOL MAUs are currently in the 200–300 million range.<sup>972</sup>

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<sup>965</sup> STOCK PURCHASE AGREEMENT, *supra* note 3, at 1.

<sup>966</sup> Alesci, *supra* note 1. Currently, Yahoo holds a "15% stake in Chinese e-commerce giant Alibaba and [a] 35.5% stake in Yahoo Japan, a joint venture with Japan's Softbank." Yue Wang, *What Can Yahoo Do With Its Alibaba Stake?*, FORBES (July 27, 2016), <https://www.forbes.com/sites/ywang/2016/07/27/what-can-yahoo-do-with-its-alibaba-stake/#1a0f80ce1cd0> [<https://perma.cc/4Q45-ACXQ>].

<sup>967</sup> *Id.* ("In 2008, for example, Microsoft was willing to pay more than \$45 billion for Yahoo, an offer that rebuffed by cofounder Jerry Yang.")

<sup>968</sup> See Jason Anders, *Why Verizon Wants Yahoo*, WALL STREET J. (Oct. 30, 2016), <https://www.wsj.com/articles/why-verizon-wants-yahoo-1477879861> [<https://perma.cc/KN6T-F9QR>]. See udesgition of the Business . . . rticle.e on the merger).t a st that will be sub against Yahoo for its delayed disclosure.re

<sup>969</sup> See *id.* (explaining Verizon's need for more "eyeballs" in order to "monetize their platform through advertising"). Verizon closed its acquisition of AOL in June of 2015. See Tom DiChristopher, *Verizon Closes AOL Acquisition*, CNBC (June 23, 2015), <http://www.cnbc.com/2015/06/23/verizon-closes-aol-acquisition.html> [<https://perma.cc/277A-V9BA>].

<sup>970</sup> As an example of how MAUs are determined, Facebook defines a "monthly active user as a registered Facebook user who logged in and visited Facebook through our website or a mobile device, or used our Messenger app (and is also registered Facebook user), in the last 30 days as of the date of measurement." David Cohen, *Facebook Changes Definition of Monthly Active Users*, ADWEEK (Nov. 6, 2015), <http://www.adweek.com/digital/monthly-active-users-definition-revised/> [<https://perma.cc/M8UZ-S7S4>].

<sup>971</sup> See Knutson, *supra* note 3 (explaining the value of Yahoo's MAUs); Solomon, *supra* note 7 (comparing the valuations of Snap to Yahoo).

<sup>972</sup> See Anders, *supra* note 21.

Also included in the terms of the deal are various MAE clauses, which are used in merger agreements to “insulate the target from undergoing any change that would substantially impact its utility for the acquiring firm.”<sup>973</sup> “Business Material Adverse Effect” has a complex definition within the Stock Purchase Agreement: “Any circumstance, event, development, effect, change or occurrence that, individually or in the aggregate . . . has had, or would or would reasonably be expected to have, a material adverse effect on the business, assets, properties, results of operation or financial condition of the Business.”<sup>974</sup> The definition includes many exceptions to what may be considered when determining whether an event is materially adverse.<sup>975</sup> MAE terms are included in the seller’s representations and warranties,<sup>976</sup> covenants and agreements,<sup>977</sup> and closing conditions<sup>978</sup> of the Stock Purchase Agreement.

## **B. Subsequent Developments: Yahoo Cyber Data Breaches**

On September 23, 2016, Yahoo disclosed it had been the victim of a cyber attack in 2014, which compromised roughly 500

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<sup>973</sup> Alana A. Zerbe, Note, *The Material Effect Provision: Multiple Interpretations & Surprising Remedies*, 22 J.L. COM. 17, 18 (2003). See generally, STOCK PURCHASE AGREEMENT, *supra* note 3.

<sup>974</sup> STOCK PURCHASE AGREEMENT, *supra* note 3, at 70.

<sup>975</sup> See *id.*

<sup>976</sup> *Id.* at 7–27.

<sup>977</sup> *Id.* at 51 (“Seller shall promptly advise Purchaser of any fact, change, event or circumstance that has had or would reasonably be expected to have a Business Material Adverse Effect, and each party shall promptly advise the other of any fact, change, event or circumstance that is reasonably likely to cause the failure of any condition to Closing set forth in Section 5.02 or Section 5.03, as applicable; provided, that any failure to give notice in accordance with the foregoing with respect to any breach shall not in and of itself be deemed to constitute the failure of any condition set forth in Section 5.02 or Section 5.03 to be satisfied.”) (emphasis in original).

<sup>978</sup> *Id.* at 63 (“[E]ach other representation and warranty of Seller contained in this Agreement, without giving effect to any materiality, “Business Material Adverse Effect” or similar qualifications therein, shall be true and correct both at and as of the date of this Agreement and as of the Closing Date as if made on and as of the Closing Date . . . except for such failures to be true and correct as would not, individually or in the aggregate, reasonably be expected to have a Business Material Adverse Effect.”).

million user accounts.<sup>979</sup> Yahoo stated the stolen account information “may have included names, email addresses, telephone numbers, dates of birth, hashed passwords . . . and, in some cases, encrypted or unencrypted security questions and answers.”<sup>980</sup> Following this disclosure, Yahoo executives remained highly optimistic about the \$4.83 billion deal and Yahoo’s potential value to Verizon.<sup>981</sup> Marni Walden, President of Product Innovation and New Business at Verizon, did note, however, that “[w]hat we have to be careful about is what we don’t know. I’ve got an obligation to make sure that we protect our shareholders and our investors, so we’re not going to jump off a cliff blindly.”<sup>982</sup> Verizon’s General Counsel, on the other hand, indicated that the breach may be considered a material event under the Stock Purchase Agreement, potentially allowing Yahoo to change the terms of the agreement.<sup>983</sup>

Then, on December 15, 2016, Yahoo announced a separate data breach had occurred in 2013 and compromised the same type of private information as the 2014 breach, but with more than one billion user accounts affected.<sup>984</sup> On January 5, 2017, Marni Walden appeared less confident about the future of the deal, stating she was unsure whether the deal would proceed<sup>985</sup> and that it would take time before the decision to move forward would be made, as Verizon was

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<sup>979</sup> Seth Fiegerman, *Yahoo Says 500 Million Accounts Stolen*, CNN MONEY (Sept. 23, 2016), <http://money.cnn.com/2016/09/22/technology/yahoo-data-breach/> [<https://perma.cc/86MP-WYRB>].

<sup>980</sup> *Id.*

<sup>981</sup> See Anders, *supra* note 21 (quoting Verizon executive Marni Walden stating that “[t]he first question is, does this deal strategically make sense to us. And the answer to that is it absolutely does.”).

<sup>982</sup> *Id.*

<sup>983</sup> See Thomas Gryta & Deepa Seetharaman, *Verizon Puts Yahoo on Notice After Data Breach*, WALL ST. J. (Oct. 13, 2016), <https://www.wsj.com/articles/verizon-sees-yahoo-data-breach-as-material-to-takeover-1476386718> [<https://perma.cc/K3Y7-XYG9>].

<sup>984</sup> Robert McMillan et al., *Yahoo Discloses New Breach of 1 Billion User Accounts*, WALL ST. J. (Dec. 15, 2016), <https://www.wsj.com/articles/yahoo-discloses-new-breach-of-1-billion-user-accounts-1481753131> [<https://perma.cc/QW27-AZ8M>].

<sup>985</sup> See Knutson, *supra* note 3 (“When asked at an investor conference in Las Vegas whether the telecom giant would proceed with the deal, Ms. Walden said: ‘Unfortunately, I can’t sit here today and say with confidence one way or the other because we still don’t know.’”).

still missing facts necessary to make an informed decision.<sup>986</sup> Yahoo remained optimistic, claiming it was still “confident in Yahoo’s value and [that it] continue[d] to work towards integration with Verizon.”<sup>987</sup> Verizon ultimately decided to move forward with the deal perhaps due, in part, to the difficulty Verizon would have faced in proving that the data breaches constituted an MAE.<sup>988</sup>

### C. Material Adverse Effect Clauses

MAE clauses give parties to merger or acquisition agreements the opportunity to allocate risks of changes, events, or discoveries that may occur between the signing and closing of a merger agreement.<sup>989</sup> An MAE clause allows a purchaser or target company to escape its obligation to close a deal if either company experiences a material adverse change anytime between the date the contract is signed and its closing date.<sup>990</sup> In October 2016, statements made by Verizon’s General Counsel suggested the company might be looking to escape or renegotiate the deal based on its MAE terms.<sup>991</sup> However, invoking an MAE clause is not an easy task, as the Delaware Court of Chancery has never found an MAE to exist with respect to such a heavily negotiated acquisition deal.<sup>992</sup>

In order to find the existence of a MAE, the party invoking the clause must prove “there has been an adverse change in the target’s business that is consequential to the company’s long-term earnings power over a commercially reasonable period, which one would expect to be measured in years rather than months.”<sup>993</sup> The court has

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<sup>986</sup> *See id.*

<sup>987</sup> *Id.*

<sup>988</sup> Moritz, *supra* note 10; *see* Solomon, *supra* note 9.

<sup>989</sup> Zerbe, *supra* note 26, at 18.

<sup>990</sup> *Id.*

<sup>991</sup> *See* Reuters, *Why Verizon Now Thinks Yahoo’s Data Breach Could Halt the Merger*, FORTUNE (Oct. 13, 2016), <http://fortune.com/2016/10/13/verizon-yahoo-merger/> [<https://perma.cc/CG3V-TULL>] (“Verizon’s general counsel Craig Silliman told reporters at a roundtable in Washington the data breach could trigger a clause in the deal that would allow the U.S. wireless company not to complete it.”).

<sup>992</sup> *See* Solomon, *supra* note 9; STOCK PURCHASE AGREEMENT, *supra* note 3, at 7, 27 (representing both companies are incorporated in Delaware).

<sup>993</sup> *Hexion Specialty Chems., Inc. v. Huntsman Corp.*, 965 A.2d 715, 738 (Del. Ch. 2008).

noted it is “not a coincidence” that “Delaware courts have never found a material adverse effect to have occurred in the context of a merger agreement,”<sup>994</sup> reasoning that MAE clauses provide a “backstop protecting the acquirer from the occurrence of unknown events that substantially threaten the overall earnings potential of the target in a durationally-significant manner. A short-term hiccup in earnings should not suffice; rather [an adverse change] should be material when viewed from the longer-term perspective of a reasonable acquirer.”<sup>995</sup> This “heavy” burden of proof falls on the buyer.<sup>996</sup>

The odds that Verizon would have been able to meet this burden are questionable. After the announcement of the 2014 hacking in September 2016, Yahoo actually reported in its third-quarter earnings release that traffic on its site was “slightly up.”<sup>997</sup> In addition, Yahoo’s EBITDA<sup>998</sup> was \$229 million in the third quarter and its revenue was \$858 million, both of which were “within the midrange of Yahoo’s estimates for 2016.”<sup>999</sup> Further, while Yahoo’s “Mavens”<sup>1000</sup> revenue had dropped 4 percent from its Mavens revenue in 2015, the drop was “largely because of declines in video with three other segments growing modestly.”<sup>1001</sup> The substantial size of Yahoo’s MAUs may also make it difficult for Verizon to successfully invoke the Stock Purchase Agreement’s MAE provision. Snap, which went public March 2, 2017 with a \$34 billion valuation, brings in 150 million MAU.<sup>1002</sup> Twitter

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<sup>994</sup> *Id.* at 738.

<sup>995</sup> *In re* IBP, Inc. S’holders Litig., 789 A.2d 14, 68 (Del. Ch. 2001).

<sup>996</sup> *See* Hexion Specialty Chems., 965 A.2d at 738.

<sup>997</sup> Solomon, *supra* note 9.

<sup>998</sup> EBITDA is an indicator of a company’s financial health and stands for “earnings before interest, taxes, depreciation, and amortization.” *See* Katherine Arline, *What is EBITDA?*, BUS. NEWS DAILY (Feb. 25, 2015), <http://www.businessnewsdaily.com/4461-ebitda-formula-definition.html> [<https://perma.cc/32L3-WFL5>].

<sup>999</sup> Solomon, *supra* note 9.

<sup>1000</sup> *See* Trefis Team, *How “Mavens” Can Drive Yahoo’s Revenues?*, FORBES (Dec. 3, 2015), <https://www.forbes.com/sites/greatspeculations/2015/12/03/how-mavens-can-drive-yahoos-revenues/#5ffd10a018c5> [<https://perma.cc/4MD8-WPTU>]. Mavens Revenue is revenue generated by advertising sales on mobile, video, native and social platforms. *Id.*

<sup>1001</sup> *Id.*

<sup>1002</sup> *See* Maureen Farrell et al., *Snapchat Shares Jump 44% in Market Debut*, WALL ST. J. (Mar. 2, 2017), <https://www.wsj.com/articles/snapchat-parent-snap-opens-higher-in-market-debut-1488471695> [<https://perma.cc/>



brings in 317 million MAU and had a market capitalization of \$12.43 billion in October 2016, and Vice Media, who “has nowhere near the same audience” as Yahoo, may be interested in putting itself up for sale with a valuation of \$5 billion.<sup>1003</sup> Yahoo, in contrast, brings in one billion MAU and its previous purchase price of \$4.83 billion is only six times its current revenue.<sup>1004</sup> Thus, the surprisingly low price Verizon was able to negotiate would make it difficult for it to prove the breaches had such a MAE on Yahoo to rise to the level required by the Chancery Court. Yahoo’s earning potential to Verizon, according Marni Walden, derives from its MAUs. Given that Yahoo’s MAUs have not been impacted by disclosure of the breaches, and taking into consideration the relatively low purchase price, it is hard to say the earnings potential of Yahoo was “substantially threaten[ed] . . . in a durationally-significant manner.”<sup>1005</sup>

Despite its historical failures in the Court of Chancery, the MAE still appears to give a party with a possibility of invoking the clause significant leverage in renegotiating merger agreements.<sup>1006</sup> On February 21, 2017, Yahoo and Verizon announced they had entered a new agreement that reduced the purchase price by \$350 million, dropping the price of the deal to roughly \$4.48 billion.<sup>1007</sup> This new deal also provides that (1) the data breaches “will be disregarded for purposes of determining whether certain closing conditions have been satisfied and in determining whether a ‘Business Material Adverse Effect’ has occurred” and (2) Yahoo and Verizon will be equally responsible for “post-closing cash liabilities related to certain data security incidents and other data breaches incurred by [Yahoo].”<sup>1008</sup>

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<sup>1003</sup> Michelle Castillo, *Why Verizon probably won't back out of the yahoo deal*, CNBC (Jan. 6, 2017), <http://www.cnbc.com/2017/01/06/why-verizon-probably-wont-back-out-of-the-yahoo-deal.html> [<https://perma.cc/6BW9-L4SR>].

<sup>1004</sup> Solomon, *supra* note 9.

<sup>1005</sup> *In re IBP, Inc. S'holders Litig.*, 789 A.2d 14, 68 (Del. Ch. 2001); Vinu Goel, *Yahoo Says Traffic Rose Despite Hacking That Could Alter Verizon Deal*, N.Y. TIMES (Oct. 18, 2016), <https://www.nytimes.com/2016/10/19/technology/yahoo-says-traffic-rose-despite-hacking-that-could-alter-verizon-deal.html> [<https://perma.cc/PA9T-VRFF>].

<sup>1006</sup> *See id.* (“Of course, this doesn’t mean that Verizon isn’t pursuing the possibility of using the material adverse effect clause to alter the deal terms.”).

<sup>1007</sup> Yahoo! Inc., Current Report (Form 8-K) (Feb. 20, 2017) [hereinafter Yahoo Current Report].

<sup>1008</sup> Yahoo Annual Report, *supra* note 12, at 131.

Because the SEC is required to approve proxy statements calling for a shareholder vote to approve a merger or acquisition, many believe the deal would be delayed beyond the parties' April-closing timeline.<sup>1009</sup> Yahoo ultimately filed their proxy statement on April 24, 2017 and the SEC approved the statement that same day.<sup>1010</sup> Shareholders will vote whether to approve or reject the merger on June 8, 2017 and the deal is expected to close by the end of the month, although it has not been reported whether the two-month delay in closing is a result of the SEC's investigation.<sup>1011</sup>

#### D. SEC Investigation of Yahoo's Seemingly Delayed Disclosure

The SEC is currently investigating Yahoo to determine whether the data breaches should have been reported to investors earlier.<sup>1012</sup> In 2011, the Division of Corporation Finance (DCF), a branch of the SEC, released a guidance statement on its "views regarding disclosure obligations relating to cybersecurity risks and cyber incidents."<sup>1013</sup> In its guidance, the DCF explained that while "no existing disclosure requirement explicitly refer[red] to cybersecurity risks and cyber incidents," many of the SEC's current regulations "may impose an obligation on registrants to disclose such risks and

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<sup>1009</sup> See Ryan Knutson, *Why Verizon Decided to Stick With Yahoo Deal After Big Data Breaches*, WALL ST. J. (Feb. 21, 2017), <https://www.wsj.com/articles/why-verizon-decided-to-still-buy-yahoo-after-big-data-breaches-1487679768> [<https://perma.cc/TQP2-UFAV>] ("An investigation under way at the Securities and Exchange Commission—about what Yahoo knew about the data breaches and when, and whether it properly informed investors—could slow that timeline.").

<sup>1010</sup> See Yahoo! Inc., Definitive Proxy Statement (Form DEFM14A) (Apr. 24, 2017) [hereinafter Yahoo Proxy Statement]; *Filing Detail*, U.S. SEC. & EXCH. COMM'N, <https://www.sec.gov/Archives/edgar/data/1011006/000119312517133449/0001193125-17-133449-index.htm> [<https://perma.cc/E2NF-LQE3>].

<sup>1011</sup> See Yahoo Proxy Statement, *supra* note 63; Deepa Seetharaman, *Yahoo's Marissa Mayer to Reap \$187 Million After Verizon Deal*, WALL ST. J. (Apr. 25, 2017), <https://www.wsj.com/articles/yahoos-marissa-mayer-to-make-186-million-from-verizon-deal-1493103650> [<https://perma.cc/2ZK5-ZFAJ>].

<sup>1012</sup> Viswanatha & McMillan, *supra* note 7.

<sup>1013</sup> DIV. OF CORP. FIN., SEC. & EXCH. COMM'N, CF DISCLOSURE GUIDANCE: TOPIC NO. 2 (2011), <https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm> [<https://perma.cc/TWV7-XAJN>].

incidents.”<sup>1014</sup> Specifically, the DCF noted, “material information regarding cybersecurity risks and cyber incidents is required to be disclosed when necessary in order to make other required disclosures, in light of the circumstances under which they are made, not misleading.”<sup>1015</sup> Information will be “considered material” by the SEC “if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision or if the information would significantly alter the total mix of information made available.”<sup>1016</sup> Further, the DCF stated that the purpose of the federal securities laws is “to elicit disclosure of timely, comprehensive, and accurate information about risks and events that a reasonable investor would consider important to an investment decision.”<sup>1017</sup>

While no current regulations specifically address cyber incident disclosures, the SEC may use Yahoo’s historic breaches as a tool to clarify its future expectations regarding these types of cybersecurity breaches.<sup>1018</sup> In Yahoo’s annual report filed on March 1, 2017, an independent committee of Yahoo’s board of directors concluded its investigation of the incidents finding that:

the Company’s information security team had contemporaneous knowledge of the 2014 compromise of user accounts . . . [and] in late 2014, senior executives and relevant legal staff were aware that a state-sponsored actor had accessed certain user accounts . . . [but] certain senior executives did not properly comprehend or investigate, and therefore failed to act sufficiently upon, the full extent of knowledge known internally by the Company’s information security team.<sup>1019</sup>

The findings of the independent committee seem to suggest there was a significant delay between senior executives gaining knowledge of hackings—admittedly, the full scope of which was not

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<sup>1014</sup> *Id.*

<sup>1015</sup> *Id.* (citing 17 C.F.R. §§ 240.12b-20, 230.408, 240.14a-9 (2010)).

<sup>1016</sup> *Id.* at n.3 (citing *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988)).

<sup>1017</sup> *Id.*

<sup>1018</sup> See Viswanatha, *supra* note 7 (“Legal experts say the SEC has been looking for a case to clarify what type of conduct would run afoul of guidance the agency issued in 2011.”).

<sup>1019</sup> Yahoo Annual Report, *supra* note 12, at 47.

yet known—and its subsequent disclosure in 2016 to investors.<sup>1020</sup> It has yet to be reported whether or not the SEC will in fact be taking action against Yahoo.<sup>1021</sup>

### **E. Conclusion**

After months of uncertainty, Yahoo and Verizon ultimately decided to move forward with the deal at a lower price.<sup>1022</sup> Barring any other disclosures or events not related to the 2013 and 2014 data breaches that could give either party the right to walk away from the deal occurring, the deal should close as long as Yahoo receives shareholder approval of the newly amended deal in June.<sup>1023</sup>

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<sup>1020</sup> See *id.*; Fiegerman, *supra* note 32.

<sup>1021</sup> See Seetharaman, *supra* note 64.

<sup>1022</sup> See Moritz, *supra* note 10.

<sup>1023</sup> See Yahoo Current Report, *supra* note 60; Seetharaman, *supra* note 64.

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