

# The Delaware Quarterly

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Each calendar quarter, the Delaware Quarterly analyzes and summarizes key decisions of the Delaware courts on corporate and commercial issues, as Delaware's Supreme Court and Court of Chancery are generally regarded as the country's premier business courts, and their decisions carry significant influence over matters of corporate law across the nation.

## This Quarter's Highlights

It was a busy final quarter of 2014 for the Delaware Court of Chancery. Of particular note: (i) three decisions on aiding and abetting breach of fiduciary duty liability that will be of particular interest to financial advisors, lenders and those practitioners counseling them; and (ii) a suite of cases by four of the five Chancery Court judges addressing when and under what circumstances a stockholder with a minority equity stake in a corporation might nevertheless be deemed to be a controlling stockholder – not always with consistent results.

Garnering much attention on the aiding and abetting front was the post-trial damages opinion in *In re Rural/Metro Corp. Stockholders Litigation*, in which Vice Chancellor Laster apportioned liability against the financial advisor to the board of Rural/Metro Corporation in connection with its sale to Warburg Pincus for 83 percent of the \$91.3 million compensatory damages award due to Rural/Metro's stockholders. In doing so, the court substantially denied the financial advisor's claim for contribution against its settling co-defendants under the Delaware Uniform Contribution Among Tortfeasors Act, finding that certain of the settling defendants did not qualify as joint tortfeasors because they were entitled to exculpation from monetary damages under 8 *Del. C.* § 102(b)(7) – thereby rendering the financial advisor unable to reduce its damages liability by their settlement amounts. Vice Chancellor

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Laster followed that up with another aiding and abetting decision in *Pontiac General Employees Retirement System v. Ballantine, et al.*, where he declined to dismiss a claim against a lender for aiding and abetting a breach of fiduciary duty by the borrower's directors based on the parties' agreement to enter into a credit facility containing a "dead hand proxy put" provision, which essentially precluded turnover of the borrower's board as a result of a proxy solicitation. Given the lender's presumed familiarity with the court's prior precedent concerning the "entrenching," and thus "highly suspect," nature of such provisions, the court found that the pleadings established "knowing participation" on the part of the lender in the board's breach of fiduciary duty. Chancellor Bouchard, on the other hand, took a different tack in *Lee v. Pincus, et al.*, when he dismissed an aiding and abetting claim against underwriters who consented to the waiver of post-IPO lock-up restrictions for certain stockholders, finding that plaintiffs failed to plead facts creating a reasonable inference that the underwriters knew that their consent to waive lock-up restrictions would facilitate a breach of fiduciary duty by the issuer's board.

On the question of when and under what circumstances a minority equity stake in a corporation might be deemed controlling are a Chancery Court foursome – *In re KKR Financial Holdings LLC Shareholder Litigation*, *In re Zhongpin Inc. Stockholders Litigation*, *In re Crimson Exploration Inc. Stockholder Litigation*, and *In re Sanchez Energy Derivative Litigation*. While three of the four decisions found that specific allegations of board domination with respect to the challenged transaction are necessary to support an inference of control by a minority stockholder, one (*In re Zhongpin*) allowed a post-closing challenge to a going-private transaction to proceed past the motion to dismiss stage where the stockholder plaintiffs' allegations sufficiently raised an inference that the company's CEO and chairman could control the company – and, accordingly, that entire fairness rather than the business judgment review applied – notwithstanding the CEO's mere 17.3 percent ownership stake. Taking these decisions together, while it is clear that the Court of Chancery will perform a case-specific inquiry into the extent to which the alleged controller influenced the board's decision with respect to the transaction at issue, the extent to which the court may also properly consider the stockholder's influence over the day-to-day operations of the company in determining whether a stockholder with a minority interest may be deemed a controller at the pleadings stage remains something of an open question.

Each of these developments is discussed in greater detail below, followed by synopses of other recent decisions issued by the Delaware courts across a broad range of corporate governance topics, including: acquiescence; alternative entities; appraisal proceedings; arbitrations; attorney's fees; books and records actions; contract claims; derivative actions; discovery; experts; fiduciary duties; indemnification and insurance; injunctions; jurisdiction; justiciability; statutes of limitation; and various other issues of Delaware practice and procedure.

### ***In re Rural/Metro Corp. Stockholders Litigation*<sup>1</sup>**

On October 10, 2014, the Chancery Court issued its much-anticipated decision on damages in *In re Rural/Metro Corp. Stockholders Litigation* ("*Rural/Metro II*"). The court had earlier ruled, in a post-trial opinion, that financial advisor RBC Capital Markets, L.L.C. ("RBC") was liable for aiding and abetting breaches of fiduciary duty by the board of directors of Rural/Metro Corporation ("Rural Metro") in connection with Rural/Metro's 2011 sale to private equity firm Warburg Pincus ("Warburg"). Using the "quasi-appraisal" method of damages – i.e., the difference between the "fair" or "intrinsic" value of the Company's stock at the time of the merger and the actual sale consideration received – the court applied a discounted cash flow analysis to arrive at a total compensatory damages figure of approximately \$91.3 million.<sup>2</sup> The court concluded that figure would make whole the stockholders who suffered from the misconduct of six members of the Company's board of directors and its primary financial advisor, RBC. It also found that RBC, the sole remaining defendant after all other defendants had settled prior to trial, was jointly and severally liable for 100 percent of the damages incurred.<sup>3</sup>

Moreover, the court substantially denied RBC's claim for contribution against its settling co-defendants under the Delaware Uniform Contribution Among Tortfeasors Act ("DUCATA"), which generally permits contribution amongst joint tortfeasors and, in the context of partial settlements, entitles a non-settling defendant to a "settlement credit" reducing the amount of a money judgment for damages attributable to the conduct of settling defendants. While the court rejected plaintiffs' argument that DUCATA precludes any form of contribution by a defendant who commits an intentional tort, it nevertheless severely restricted RBC's ability to obtain such a credit (or any other form of contribution) on the facts of this case. In pertinent

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<sup>1</sup> C.A. No. 6350-VCL, 102 A.3d 205 (Del. Ch. 2014).

<sup>2</sup> *Id.* at 224-26.

<sup>3</sup> *Id.* at 215-16, 220-21.

part, the court concluded that RBC: (i) was precluded from seeking contribution for certain categories of claims under the equitable doctrine of unclean hands; (ii) was proportionately more culpable than other defendants for certain breaches of duty (e.g., claims related to RBC's potential conflicts of interest); and (iii) failed to establish that certain settling defendants were "joint tortfeasors" under DUCATA. On the last point, the court held as a matter of first impression that settling defendants *could not* qualify as joint tortfeasors under DUCATA (and thus could not be liable for contribution or even count for purposes of calculating a settlement credit) if they were entitled to exculpation from monetary damages under 8 Del. C. § 102(b)(7). Because RBC established that only two of the settling defendants would not have been exculpated had they remained in the case, the court conducted a "relative fault" analysis across only three parties: RBC and the two non-exculpated directors. For the reasons above and the court's view that RBC was comparatively more culpable, the court granted RBC only a 17 percent "settlement credit" based on damages attributable to the two directors, leaving RBC liable for the remaining 83 percent (\$75.8 million).

Beyond serving as yet another cautionary tale for financial advisors in the context of Delaware fiduciary duty law, the opinion has generated significant debate insofar as it treats Section 102(b)(7) of the Delaware General Corporation Law ("DGCL") as a liability-*shifting* mechanism rather than a liability-*reducing* mechanism, as traditionally construed.

### Background

#### *The Sale And Ensuing Litigation*

On March 28, 2011, Rural/Metro announced that it had entered into an agreement with Warburg by which Warburg would acquire all outstanding shares of Rural/Metro stock for \$437.8 million, or \$17.25 per share – a 37 percent premium over the pre-announcement market price.<sup>4</sup> Plaintiffs filed suit shortly thereafter, asserting claims for (i) breach of fiduciary duty against the six Rural/Metro directors who approved the transaction (including Rural/Metro's CEO and the Chairman of the special committee that the board of directors enacted in connection with the deal) (the "Director Defendants"), and (ii) aiding and abetting the Director Defendants' breaches of fiduciary duty against RBC and a secondary financial advisor retained by the Rural/Metro board, Moelis & Company L.L.C ("Moelis").<sup>5</sup>

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<sup>4</sup> *Id.* at 214.

<sup>5</sup> *Id.*

#### *The Partial Settlement*

Prior to trial, plaintiffs settled with the Director Defendants (for \$6.6 million) and Moelis (for \$5 million) in exchange for a release of claims.<sup>6</sup> The settlement agreements were guided in part by 10 Del. C. § 6304(b), which provides:

A release by the injured person of 1 joint tortfeasor does not relieve the 1 joint tortfeasor from liability to make contribution to another joint tortfeasor unless the release is given before the right of the other tortfeasor to secure a money judgment for contribution has accrued, and *provides for a reduction, to the extent of the pro rata share of the released tortfeasor, of the injured person's damages recoverable against all the other tortfeasors.*<sup>7</sup>

To preserve peace of mind and protect themselves from contribution claims brought by non-settling defendants, the settling defendants insisted on language along those lines, providing that the damages recoverable against those non-settling defendants would be reduced by the *pro rata* share (or proportional degree of fault), if any, of the settling defendants.<sup>8</sup> RBC, as the lone active defendant, amended its answer to include contribution claims against its co-defendants. Notably, it did not assert that its co-defendants committed wrongdoing; instead, it utilized a "united front" strategy wherein it contended that none of the directors breached their fiduciary duties.<sup>9</sup> The court approved the settlements, which barred RBC's contribution claims but preserved its right to argue for settlement credits based on the *pro rata* shares of the settling defendants.

#### *The Court's Post-Trial Liability Opinion*

At trial, RBC continued to pursue its united front theory, contending that there was no underlying breach of fiduciary duty and that, therefore, it could not be held liable for aiding and abetting. RBC made no effort to prove that the directors breached their fiduciary duties or that their fault was greater than its own for purposes of a reduction in damages.<sup>10</sup>

On March 7, 2014, the court issued its liability opinion, finding that the Director Defendants breached their fiduciary duties by greenlighting the initiation of a sale process without board authorization, by approving the

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<sup>6</sup> *Id.* at 215-16.

<sup>7</sup> 10 Del. C. § 6304(b) (emphasis added).

<sup>8</sup> The two settlement-agreement term sheets contained identical language: "Plaintiff and the Class agree, pursuant to 10 Del. C. § 6304(b), that the damages recoverable against all the other tortfeasors will be reduced to the extent of the *pro rata* share of [the other settling defendants]." *Rural/Metro II*, 102 A.3d at 215-16.

<sup>9</sup> *Id.* at 217.

<sup>10</sup> *Id.*

merger without a reasonable information basis for doing so, and by providing materially misleading information in the proxy statement regarding the merger.<sup>11</sup> As for RBC, the court found that it (i) failed to disclose actual and potential conflicts of interest relating to its efforts to obtain buy-side financing work from private equity firms that were simultaneously bidding to acquire the parent company of Rural/Metro's main competitor, Emergency Medical Services Corporation, and (ii) provided Rural/Metro's board with a flawed valuation analysis designed to ensure board approval of the Warburg transaction.<sup>12</sup> The court reserved decision on damages and the allocation of fault amongst RBC and the settling defendants.

After supplemental briefing and oral argument, the court issued its damages ruling on October 10, 2014.

### The Court's Analysis

#### Measure Of Damages

As an initial matter, the court determined that plaintiffs were entitled to a quasi-appraisal remedy, by which they would be compensated for the delta between the "intrinsic" value of their stock at the time of the transaction and the value they received in merger consideration. The court thus employed a discounted cash flow analysis using inputs identified in its earlier opinion based on trial evidence (e.g., approximate beta, perpetuity growth rate, and equity risk premium) and assessing the parties' supplemental submissions.<sup>13</sup> The court ultimately determined that the going-concern value of Rural/Metro stock at the time of the merger was \$21.42 per share – \$4.17 higher than the per-share merger consideration actually received.<sup>14</sup> Extrapolating that delta across the size of the class and the number of shares at issue, the court calculated total damages to the class of \$91.3 million.<sup>15</sup>

#### The Availability Of A "Settlement Credit" Under DUCATA

The court then considered whether the judgment against RBC should be reduced and analyzed the percentage of damages RBC would be required to pay under DUCATA, the statute governing allocation of fault among tortfeasors in Delaware.<sup>16</sup> DUCATA provides that, in certain circumstances, non-settling defendants can receive "settlement credit" for the "pro rata share" of damages

attributable to conduct of "joint tortfeasors."<sup>17</sup> RBC argued that, under DUCATA, it should be responsible for 12.5 percent of the total damages (1/8), since plaintiffs had settled with seven tortfeasors, each equally responsible for injuries to plaintiffs. In contrast, plaintiffs posited that RBC should be entitled to no settlement credit because it committed an intentional tort.

As a threshold issue, the court answered a question lingering within Delaware jurisprudence when it held that a defendant who commits an intentional tort may still be entitled to a settlement credit, subject to the court's discretion (e.g., a highly culpable, malicious act may persuade a judge to bar such reductions in damages). Rejecting plaintiffs' argument to the contrary, the court emphasized that, in the absence of guidance from the Delaware Supreme Court, "DUCATA does not establish a bright-line rule barring contribution for all intentional torts."<sup>18</sup>

At the same time, the court – citing the Delaware Supreme Court's decision in *Medical Center of Delaware, Inc. v. Mullins*<sup>19</sup> – also concluded that a defendant seeking a reduction in damages bears the burden of proving that settling co-defendants are, in fact, joint tortfeasors.<sup>20</sup> To meet that burden, a defendant must likewise prove that its settling co-defendants could not have prevailed on affirmative defenses had they litigated the case.

Here, the court found that the equitable doctrine of unclean hands prohibited RBC from obtaining a settlement credit for certain categories of claims stemming from false information RBC provided to the Director Defendants and its failure to disclose its potential and actual conflicts of interest.<sup>21</sup> The court reasoned that "[i]f RBC were permitted to seek contribution for these claims from the directors, then RBC would be taking advantage of the targets of its own misconduct."<sup>22</sup>

#### Qualification As Joint Tortfeasors Under DUCATA

Plaintiffs also challenged the settling defendants' qualification as "joint tortfeasors" in light of RBC's failure to offer evidence of wrongdoing against them at trial and continued "united front" defense. The court rejected plaintiffs' argument that, by failing to allege wrongdoing at trial, RBC waived its right to assert that settling defendants were joint tortfeasors for purposes of a contribution claim.<sup>23</sup>

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<sup>11</sup> *Id.* at 218-19.

<sup>12</sup> *Id.* at 219.

<sup>13</sup> *Id.* at 225-26.

<sup>14</sup> *Id.* at 226.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.* at 227, 236.

<sup>17</sup> See 10 Del. C. § 6304(b).

<sup>18</sup> 102 A.3d at 227.

<sup>19</sup> 637 A.2d 6, 8 (Del. 1994).

<sup>20</sup> 102 A.3d at 242-44.

<sup>21</sup> *Id.* at 237-39, 262.

<sup>22</sup> *Id.* at 239.

<sup>23</sup> *Id.* at 245.

It likewise rejected RBC's argument that, by the very act of executing settlement agreements, the co-defendants conceded that they were joint tortfeasors.<sup>24</sup>

Instead, the court framed its analysis in terms of Rural/Metro's exculpatory provision under Section 102(b)(7) of the DGCL. Critically, the court found as a matter of first impression that a settling defendant who would have been exculpated from monetary damages under a Section 102(b)(7) provision could not be considered a joint tortfeasor subject to DUCATA's contribution provisions.<sup>25</sup> After conducting a defendant-by-defendant analysis, the court held that three of the six Director Defendants were entitled to exculpation under Section 102(b)(7) – and thus that RBC could not receive settlement credits based on their conduct – insofar as the record evidence suggested that they “were disinterested and independent” and acted loyally and in good faith during the transaction.<sup>26</sup>

Conversely, the court found sufficient record evidence of personal interests on the part of the remaining three Director Defendants to raise a question as to their disinterestedness (and corresponding entitlement to exculpation). Of the three, two – the Company's CEO and the chair of the special committee – testified at trial. According to the court, their testimony adequately demonstrated that they were not disinterested in the merger and, thus, would not be exculpated under Rural/Metro's Section 102(b)(7) provision.<sup>27</sup> The court declined to reach a similar conclusion about the third “questionable” Director Defendant, who did not testify and about whom the court did not have sufficient evidence of interest or a lack of independence.<sup>28</sup>

### Allocation Of Fault Among Defendants

Having determined that the only “joint tortfeasors” under DUCATA were RBC and two Director Defendants, the court turned to allocating relative fault among the three. It rejected RBC's argument that it should apply equal fault among them, citing for support the Restatement (Third) of Torts, the U.S. Supreme Court, the Private Securities Litigation Reform Act, and legal commentators.<sup>29</sup> It found

that the two general violations – based on failure to disclose and the sales process itself – contributed equally to the harm, or 50 percent of the damages each.<sup>30</sup> It then subdivided the sale-process violation into two parts – the decision to initiate the process early and without board authorization, and the decision to approve the merger – and found that each contributed equally, or 25 percent of the total damages each.<sup>31</sup> The court then found that RBC was solely responsible for the disclosure violation because the directors completely relied on its misleading information in issuing the proxy statement.<sup>32</sup> The court also found that RBC alone was responsible for the decision to approve the merger, based on its misleading the board. As for the decision to initiate the sales process, the court allocated 17 percent of the fault to the two director defendants and 8 percent to RBC. In sum, RBC was responsible for 83 percent of the damages.<sup>33</sup>

### Quantifying The Settlement Credit

The court determined that RBC was thus entitled to a settlement credit under DUCATA in an amount representing the greater of: (i) the aggregate settlement amount paid by the settling co-defendants (\$11.6 million); or (ii) the damages attributable to the settling co-defendants RBC proved to be joint tortfeasors – the two directors not entitled to exculpation (17 percent of the damages or \$15.5 million).<sup>34</sup> The damages award was thus reduced by \$15.5 million (from \$91.3 million to \$75.8 million).

### Takeaways

*First, Rural/Metro II* heightens the stakes for defendants not entitled to Section 102(b)(7) protection, and, in particular, financial advisors found liable for aiding and abetting a breach of fiduciary duty, in the M&A litigation context. By precluding contribution claims against any exculpated defendant, the ruling has the potential to expose financial advisors – and other defendants who are not covered by the statutory protection – to significant monetary liability for exculpated breach-of-fiduciary-duty claims (*i.e.*, duty-of-care violations) without any recourse against the exculpated directors found to have committed the underlying breach. In other words, the decision makes clear that extending Section 102(b)(7) exculpation protections to certain defendants can magnify the monetary liability of other, non-exculpated defendants. In

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24 *Id.* at 245-47.

25 *Id.* at 249-52.

26 *Id.* at 259.

27 *Id.* at 255-59.

28 *Id.* at 258. The court also held that RBC failed to prove that Moelis was a joint tortfeasor because the record showed that the two “were not similarly situated” – “Moelis placed less emphasis on a sale of Rural . . . [and] noted that it would not seek to finance any of the bidders,” avoiding any conflict of interest. *Id.* at 260. The court thus held that RBC was only entitled to settlement credits based on the actions of two of the Director Defendants.

29 *Id.* at 261-62 (citing *McDermott, Inc. v. AmClyde*, 511 U.S. 202, 211-21 (1994); 15 U.S.C. § 78u-4f; Restatement (Third) of Torts: Apportionment of Liab. § 23 & Reporters' Note cmt. e (2000); Marc I. Steinberg & Christopher D. Olive, Contribution and Proportionate Liability Under the Federal Securities Laws in Multidefendant Securities Litigation After the Private Securities

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Litigation Reform Act of 1995, 50 SMU L. Rev. 337, 361-67 (1996)).

30 *Id.* at 262.

31 *Id.*

32 *Id.*

33 *Id.* at 262-63.

34 *Id.*



that sense, the decision permits Section 102(b)(7) to act as a liability-shifting mechanism as opposed to the liability-reducing mechanism seemingly envisioned by the statute's drafters. Coupled with the flexibility DUCATA provides in allocating fault, the court's exclusion of exculpated parties from joint-tortfeasor status could result in damages falling disproportionately on financial advisors and, by extension, officers, controlling stockholders, and others not entitled to protection under Section 102(b)(7).

*Second*, and by the same token, plaintiffs will be further incentivized to press aiding-and-abetting claims – and fiduciary-duty claims against non-exculpated corporate fiduciaries – at every turn, hoping to generate monetary liability where there once was none (i.e., breaches of the fiduciary duty of care). In that regard, the court's decision to allow plaintiffs to recover monetary damages from RBC for claims that are otherwise exculpated appears somewhat at odds with the underlying purpose of Section 102(b)(7) to insulate directors who commit certain types of breaches from monetary liability. On that logic, if a 102(b)(7) provision is viewed as an *ex ante* damages-claim waiver against qualifying directors, one can credibly argue that *reducing* the total damages award available to plaintiffs by the amount attributable to exculpated defendants, as opposed to saddling a non-exculpated defendant (and secondary violator) with that portion of the damages award, would be more consistent with the exculpatory principles embodied by Section 102(b)(7).

*Third*, the court's exclusion of exculpated defendants from contribution liability raises several considerations for practitioners. To begin with, defendants not protected by Section 102(b)(7) will have to think carefully about pursuing a "united front" theory at trial; should the argument not prevail on the merits, the court could ultimately exculpate certain defendants under 102(b)(7) and increase the share of monetary liability born by the non-exculpated defendants, who, in turn, will have sacrificed the opportunity to argue that any damages award should be reduced by amounts attributable to the conduct of the former. Relatedly, settling defendants may be forced to play a greater role in litigation going forward. Given the court's reluctance to find a non-testifying, settling director unworthy of exculpation under Section 102(b)(7) – and thus eligible as a "joint tortfeasor" for contribution purposes – non-settling defendants may well seek to compel the testimony of settling defendants in an effort to challenge their entitlement to exculpation. While the settling defendants would not incur damages, a judicial finding that they acted in bad faith or disloyally, and thus are not entitled to exculpation, nevertheless poses considerable reputational risk, to say nothing of the time

and costs of participating as a witness in a trial. All of which is counterintuitive to the concept of global resolution that settlement agreements are expected to provide.

*Finally*, while the exclusion of exculpated defendants from contribution is the key holding in the case, the court's exculpation analysis itself – and concomitant ruling that two Rural/Metro directors would not have been entitled to exculpation under Section 102(b)(7) – has raised eyebrows in the legal community for its seeming departure from the Delaware Supreme Court's landmark 2009 ruling in *Lyondell Chemical Co. v. Ryan*,<sup>35</sup> in which the Court held that the standard for a non-exculpated breach of fiduciary duties in the *Revlon* context is whether a director "utterly failed to attempt to obtain the best sale price" or demonstrated a "conscious disregard" of his or her duties. Here, for second time this year,<sup>36</sup> the court defined the standard somewhat differently: whether a fiduciary intentionally acts with a purpose other than the best interests of the corporation and its stockholders. Under that standard, the court found that one Director Defendant was "sufficiently motivated" by personal interests to sell the Company quickly because he was a managing director of a hedge fund that owned 22 percent of Rural/Metro's stock, wanted to exit its investment in three to five years, and desired to raise a new fund.<sup>37</sup> As for the second Director Defendant, the court found sufficient evidence of personal interest on the basis that he initially opposed a near-term sale, but performed an about-face after being pressured by a fellow director and realizing his ability to cash out equity awards more quickly upon a sale.<sup>38</sup> Suffice it to say, these facts appear to fall short of the egregious conduct envisioned by the Supreme Court in *Lyondell*.

### Healthways and Pincus

The Court of Chancery also issued two important decisions this quarter further defining the scope of third-party aiding and abetting liability based on alleged breaches of fiduciary duty by a board of directors. In *Pontiac General Employees Retirement System v. Ballantine, et al. ("Healthways")*,<sup>39</sup> a bench ruling issued on October 14, 2014, Vice Chancellor Laster held that a stockholder-plaintiff adequately stated a claim against a lender for aiding and abetting a breach of fiduciary duty by its borrower's directors based on the parties' agreement to enter into a credit facility that contained a so-called "dead hand proxy put" provision. The provision in

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<sup>35</sup> 970 A.2d 235, 243-44 (Del. 2009).

<sup>36</sup> See *Chen v. Howard-Anderson*, 87 A.3d 648 (Del. Ch. 2014).

<sup>37</sup> 102 A.3d at 255.

<sup>38</sup> *Id.* at 258-59.

<sup>39</sup> C.A. No. 9789-VCL, 2014 WL 6388645 (Del. Ch. Oct. 14, 2014).

question, allegedly added in response to a takeover threat, essentially precluded turnover of the borrower's board as a result of a proxy solicitation by allowing the lender, under such circumstances, to declare an event of default and accelerate the debt. Based on the facts alleged, and the lender's presumed familiarity with the court's prior precedent concerning the "entrenching," and thus "highly suspect," nature of such provisions, Vice Chancellor Laster concluded that plaintiff had adequately pleaded "knowing participation" on the part of the lender in the board's breach of fiduciary duty.

In *Lee v. Pincus, et al.*,<sup>40</sup> by contrast, a decision issued exactly one month later on November 14, 2014, Chancellor Bouchard dismissed an aiding and abetting claim against underwriters who consented to the waiver of post-IPO lock-up restrictions for certain stockholders, including half of the issuer's directors, that permitted them to sell some of their stock in a secondary offering. The court held that plaintiffs failed to plead facts creating a reasonable inference that the underwriters knew that their consent, which was necessary to waive the lock-up restrictions, would facilitate a breach of fiduciary duty by the issuer's board. With aiding and abetting allegations becoming increasingly commonplace, particularly in the wake of the court's decision in *In re Rural/Metro*, these two decisions merit close attention by those who counsel advisors to boards.

### ***Pontiac General Employees Retirement System v. Ballantine, et al.***<sup>41</sup>

#### **Background**

In 2010, Healthways, Inc. ("Healthways") entered into an amended and restated revolving credit and term loan agreement with one of the company's lenders. The agreement contained a "proxy put" provision that would be triggered if, at any time over a two-year period, a majority of Healthways' board of directors ceased to be comprised of "continuing directors," defined to include both directors then in office, as well as any directors subsequently elected with the board's approval.<sup>42</sup> The proxy put provision in the 2010 credit agreement did not contain a so-called "dead hand" feature, *i.e.*, one which would have excluded from the definition of "continuing directors" any directors elected pursuant to a dissident slate (even if ultimately approved by the then-current board).

Healthways' board subsequently came under pressure from the company's stockholders. In 2012, a major institutional stockholder submitted – and its fellow stockholders overwhelmingly approved (over the directors' objection) – a proposal to declassify the board.<sup>43</sup> Shortly thereafter, Healthways amended its credit agreement.<sup>44</sup> The amended agreement, which provided Healthways with a \$200 million revolving credit facility, now included a dead hand proxy put that defined "continuing directors" to exclude those nominated in connection with, or as a result of, a dissident proxy challenge (actual or threatened), even if the then-current directors ultimately approved their appointment.<sup>45</sup>

Pressure on the board continued. On December 2, 2013, another large institutional stockholder sent a public letter to the board expressing its concerns about the board's leadership and the company's performance.<sup>46</sup> In January 2014, that stockholder sent another letter stating its intent to wage a proxy fight. The company ultimately appeased that stockholder by providing it with representation on the Healthways board.<sup>47</sup> The stockholder's designated directors were not, however, considered "continuing directors" for purposes of the proxy put in the credit agreement.<sup>48</sup>

In March 2014, another stockholder – plaintiff in the case at hand – served the company with a Section 220 demand seeking to inspect documents and records relating to the negotiation of the dead hand proxy put in the 2012 credit agreement. According to the complaint, the company failed to produce documents showing that there was "substantive negotiation about the proxy put" or "that the company received 'extraordinarily valuable economic benefits' that might justify the proxy put."<sup>49</sup>

Plaintiff brought suit asserting claims for breach of fiduciary duty against the members of Healthways' board of directors, aiding and abetting against the company's lender, and for a declaratory judgment that the dead hand proxy put is unenforceable. Defendants moved to dismiss.

#### **The Court's Analysis**

Vice Chancellor Laster first held that plaintiff adequately stated a claim against Healthways' directors for breach of fiduciary duty. In so doing, the court rejected the

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<sup>40</sup> C.A. No. 8458-CB, 2014 WL 6066108 (Del. Ch. Nov. 14, 2014).

<sup>41</sup> C.A. No. 9789-VCL, bench opinion (Del. Ch. Oct. 14, 2014).

<sup>42</sup> *Id.* at 68-69.

<sup>43</sup> *Id.* at 69.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.* at 70.

<sup>46</sup> *Id.*

<sup>47</sup> *Id.*

<sup>48</sup> *Id.* at 70-71.

<sup>49</sup> *Id.* at 71 (citing *San Antonio Fire & Police Pension Fund v. Amylin Pharm., Inc.*, 983 A.2d 304, 315 (Del. Ch. 2009), *aff'd*, 981 A.2d 1173 (Del. 2009)).

directors' argument that the claim was not ripe insofar as the proxy put had not been triggered. The court held that "stockholders of the company are presently suffering a distinct injury in the form of a deterrent effect" on proxy challenges and other forms of stockholder opposition.<sup>50</sup> Further, without adopting a per se rule that entering into an agreement that contains a proxy put will always be a breach of fiduciary duty, the Vice Chancellor held that the allegations against Healthways' board – including the alleged lack of negotiation and informed consideration concerning the proxy put provision – were sufficient to withstand a motion to dismiss.

The court likewise declined to dismiss the aiding and abetting claim against the company's lender, whose principal argument was that it did not "knowingly participate" in any alleged breach of fiduciary duty by Healthways' directors and that it could not possibly be liable for aiding and abetting because the credit agreement was the product of arm's-length negotiation.

The court disagreed. Ruling from the bench, Vice Chancellor Laster explained that:

It is certainly true . . . that evidence of arm's-length negotiation negates claims of aiding and abetting. In other words, when you are an arm's-length contractual counterparty, you are permitted, and the law allows you, to negotiate for the best deal that you can get. What it doesn't allow you to do is to propose terms, insist on terms, demand terms, contemplate terms, incorporate terms that take advantage of a conflict of interest that the fiduciary counterparts on the other side of the negotiating table face.<sup>51</sup>

The latter, the court concluded, was what the company's lender was adequately alleged to have done. According to Vice Chancellor Laster, the lender was "on notice," from the Court of Chancery's prior precedent, that such dead hand proxy put provisions are "highly suspect and could potentially lead to a breach of duty on the part of" a borrower's directors.<sup>52</sup> Moreover, in light of the factual circumstances – most notably, the alleged lack of consideration that Healthways received in exchange for agreeing to the dead hand proxy put, coupled with the fact that the provision was added in the specter of a proxy fight – there was a question of fact as to whether the negotiation was truly arm's length.<sup>53</sup> For these reasons, the court denied the motion to dismiss.

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<sup>50</sup> *Id.* at 72-78.

<sup>51</sup> *Id.* at 79.

<sup>52</sup> *Id.* at 80.

<sup>53</sup> *Id.*

### *Lee v. Pincus, et al.*<sup>54</sup>

#### Background

Zynga Inc. ("Zynga"), the social gaming company and maker of FarmVille, completed its initial public offering in December 2011, selling 100 million shares at a price of \$10 per share.<sup>55</sup> Morgan Stanley & Co. LLC ("Morgan Stanley") and Goldman, Sachs & Co. ("Goldman") served as the lead underwriters for the IPO. Zynga's officers, directors and employees (along with most other pre-IPO investors) were subject to a 165-day lockup period that prevented them from selling their shares until May 2012.<sup>56</sup> The shares subject to the lockup restrictions totaled almost 700 million shares.<sup>57</sup>

In March 2012, Zynga's eight-member board of directors voted unanimously to modify the lockup restrictions in a number of respects. First, the board waived the lockup and blackout restrictions for approximately 49 million shares held by certain investors, including four of Zynga's eight directors, clearing the way for them to participate in a secondary offering in April 2012.<sup>58</sup> Second, the board simultaneously extended the original lockup period for the remainder of the approximately 200 million shares owned by these same investors.<sup>59</sup> Third, the board waived the lockup, but not the blackout, restrictions for approximately 114 million shares held by non-executive employees, meaning that, although those shares still could not be sold in the secondary offering, they could nevertheless now be sold prior to the expiration of the original lockup period.<sup>60</sup> There were approximately 325 million shares held by former employees and institutional investors whose lockup periods were not modified.<sup>61</sup> The modifications to the lockup restrictions were, as required, approved by the lead underwriters, Morgan Stanley and Goldman.<sup>62</sup>

The four board members now permitted to participate in the secondary offering did so, selling approximately 18 million shares at a price of \$12 per share.<sup>63</sup> After the secondary offering, Zynga's stock price began to slide precipitously. By the expiration of the original lockup

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<sup>54</sup> C.A. No. 8458-CB, memorandum opinion (Del. Ch. Nov. 14, 2014).

<sup>55</sup> *Id.* at 5.

<sup>56</sup> *Id.*

<sup>57</sup> *Id.*

<sup>58</sup> *Id.* at 7.

<sup>59</sup> *Id.* at 8.

<sup>60</sup> *Id.* at 7.

<sup>61</sup> *Id.*

<sup>62</sup> *Id.* at 6-7.

<sup>63</sup> *Id.* at 8.



period on May 29, 2012, the stock price had fallen to \$6.09.<sup>64</sup> By August 16, 2012, when all lockup restrictions expired, Zynga's stock was trading at \$3.00 per share.<sup>65</sup>

Plaintiff, an owner of stock that was at all times subject to the original lockup and blackout restrictions and thus unable to sell her shares until May 29, 2012, brought suit asserting claims for breach of fiduciary duty against Zynga's directors and aiding and abetting against Morgan Stanley and Goldman for their role in approving the modifications to the lockup restrictions. Defendants moved to dismiss.

### The Court's Analysis

The principal arguments advanced by Zynga's directors were that (i) the claims asserted by the stockholder-plaintiff were derivative, not direct, in nature, (ii) any claims that plaintiff may have were governed by contract law, not fiduciary principles, and (iii) in any event, the Zynga directors who were permitted to participate in the secondary offering as a result of the lockup modifications did not, when all was said and done, receive a net benefit. Chancellor Bouchard rejected each of these arguments.

First, he held that the claim was properly asserted as a direct one since the decision to modify the lockup restrictions did not affect all Zynga stockholders alike, but rather allegedly gave certain stockholders preferential treatment over others.<sup>66</sup> Second, he rejected the argument that any rights that stockholders had in this regard were merely contractual. On the contrary, the court described plaintiff's claim as "quintessentially a fiduciary duty claim," noting, *inter alia*, that no action "was taken under the terms of the contracts governing the putative class members' shares."<sup>67</sup> Third, the court rejected the directors' argument that they should not face liability because the four interested directors were not, net-net, advantaged by the lockup modifications, as they were permitted to sell only a minority of their shares in the secondary offering, and the extended lockup period that applied to the remainder of their shares as a result of the modifications left them in worse overall shape than other investors, as it turned out, given the decline in Zynga's stock price.<sup>68</sup> The Chancellor noted that the benefit conferred to directors for these purposes is to be viewed *ex ante*, not with the benefit of hindsight.<sup>69</sup> Concluding that at least half of the directors

approving the lockup modifications had had a financial interest in doing so, the court held that plaintiff had pleaded facts sufficient to rebut the business judgment rule and survive a motion to dismiss.<sup>70</sup>

The court, however, granted the underwriters' motion to dismiss the aiding and abetting claims asserted against them. Chancellor Bouchard focused his analysis on whether plaintiff had adequately alleged facts showing "knowing participation in the breach by the non-fiduciary defendants."<sup>71</sup> He concluded that she had not.

In his opinion, Chancellor Bouchard explained that knowing participation is a "stringent standard that turns on proof of scienter" on the part of the alleged aider and abettor.<sup>72</sup> Plaintiffs must provide factual allegations from which it is "reasonably conceivable" that the third-party acted "with the knowledge that the conduct advocated or assisted constituted a breach of fiduciary duty."<sup>73</sup> Examples of the types of factual allegations that might meet this stringent standard include, according to the Chancellor, situations involving: (i) facially "egregious" terms of a transaction; (ii) side deals of a "magnitude" that are "so excessive as to be inherently wrongful"; (iii) use of knowledge of the breach to gain advantage; or (iv) direct factual allegations that the aider and abettor "sought to induce the breach."<sup>74</sup>

The court concluded that no such allegations were present in *Pincus*. Plaintiff alleged that the underwriters profited from the secondary offering, and that this would not have been possible but for the board's action – with the underwriters express approval – in modifying the lockup restrictions. Plaintiff further alleged that the underwriters were "fully aware" that the board's actions in this regard constituted a breach of fiduciary duty.<sup>75</sup> Chancellor Bouchard rejected these allegations as "conclusory," stating that (i) "plaintiff has failed to plead any facts from which it is reasonably inferable that [the underwriters] knew when they provided their consent to modify the lockup restrictions that such action would facilitate a breach of fiduciary duty" by the directors, and (ii) "[t]he fact that [the underwriters'] consent was necessary for the Director Defendants to waive a lockup restriction,

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64 *Id.* at 9.

65 *Id.*

66 *Id.* at 13.

67 *Id.* at 21-22.

68 *Id.* at 24.

69 *Id.* at 27 (citing *In re Del Monte Foods Co. S'holders Litig.*, 25 A.3d 813, 830 (Del. Ch. 2011)).

70 *Id.* at 25.

71 *Id.* at 31 (citing *In re Rural Metro Corp. S'holders Litig.*, 88 A.3d 54, 80 (Del. Ch. 2014)).

72 *Id.* at 31 (internal quotation marks omitted).

73 *Id.* (internal alterations and quotation marks omitted).

74 *Id.* (quoting *In re Telecommunications Inc. Shareholders Litig.*, C.A. No. 16470-NC. 2003 WL 21543427 at \*2 (Del. Ch. July 7, 2003)).

75 *Id.* at 32.

without more, is insufficient” to support aiding and abetting liability.<sup>76</sup> Accordingly, the court granted the underwriters’ motion to dismiss.

### Takeaways

The *Healthways* and *Pincus* decisions reflect the increasing frequency with which financial advisors, lenders and other third-parties are accused of having aided and abetted a breach of fiduciary duty by a company’s board of directors. While determining the metes and bounds of what it takes to plead and prove “knowing participation” on the part of an advisor or other third-party in a given set of circumstances is an exercise that will continue to play out in the courts in the coming years, here is what we know from the court’s recent decisions in *Healthways* and *Pincus*:

*First*, as Chancellor Bouchard made clear in *Pincus*, “knowing participation” is and remains a “stringent” standard that requires well-pled allegations (and ultimately proof) demonstrating that a third-party acted with the knowledge that the board conduct in question constituted a breach of fiduciary duty. In other words, the third-party must have acted with scienter. A plaintiff can satisfy its pleading burden in this regard by, *inter alia*, providing direct factual allegations supporting the inference that the defendant sought to induce the alleged breach of fiduciary duty – such as by offering side payments or other incentives to the directors – or that it used its knowledge of the breach to gain some advantage. Knowing participation may also be inferred, the court has held, where the terms of a transaction are so “egregious” or “excessive” as to be “inherently wrongful.”

*Second*, when it comes to “knowing participation” in, and/or knowledge of, a fiduciary breach, Vice Chancellor Laster’s decision in *Healthways* suggests that the Court of Chancery presumes that third-party advisors and their counsel are aware of its prior precedent. Indeed, as noted above, the lender’s presumed knowledge of the court’s prior decisions calling into question the entrenching nature of dead hand proxy puts played a central role in Vice Chancellor Laster’s decision to deny the motion to dismiss the aiding and abetting claim in that case.

*Third*, although evidence of arm’s-length negotiations generally negates aiding and abetting liability for a counter-party to a transaction, liability will attach where a counter-party takes advantage of a conflict of interest on the part of a fiduciary on the other side, as plaintiffs alleged occurred in *Healthways*.

Finally, the *Healthways* decision suggests that directors and lenders alike may face liability for including “proxy put” provisions in credit agreements absent some compelling justification. Lenders and their advisors should proceed accordingly.

### Minority Control: *In re KKR Financial Holdings LLC Shareholder Litigation*;<sup>77</sup> *In re Zhongpin Inc. Stockholders Litigation*;<sup>78</sup> *In re Crimson Exploration Inc. Stockholder Litigation*;<sup>79</sup> and *In re Sanchez Energy Derivative Litigation*<sup>80</sup>

Finally, in a suite of cases decided this quarter, four different judges of the Court of Chancery had occasion to address the question of when and under what circumstances a stockholder with a minority equity stake in a corporation might nevertheless be deemed to be a controlling stockholder – not always with consistent results.

Thus, in *In re KKR*, Chancellor Bouchard granted defendants’ motion to dismiss, finding that the highly deferential business judgment rule – not the entire fairness standard of review – applied in a suit challenging the merger of KKR Financial Holdings LLC (“KFN”) and KKR & Co. L.P. (“KKR”). In so doing, the court rejected plaintiffs’ contention that, although KKR owned less than 1 percent of KFN stock, it was nevertheless a controlling stockholder because KKR’s affiliate allegedly exercised control over the day-to-day management of KFN. The Chancellor emphasized that the key question was whether the stockholder exercised control not over the company’s operations, but over *the decision to approve the merger*. Here, that decision remained vested in KFN’s board, a majority of which plaintiffs had failed to allege was beholden to KKR.<sup>81</sup>

In *In re Zhongpin*, by contrast, Vice Chancellor Noble denied defendants’ motion to dismiss a post-closing challenge to a going-private transaction for failure to state a claim, concluding that the stockholder plaintiffs’ allegations in that case sufficiently raised an inference that the company’s CEO and chairman could control the company – and, accordingly, that entire fairness rather than business judgment review applied – notwithstanding the CEO’s mere 17.3 percent ownership stake. Specifically, the court determined that such allegations suggested that the CEO possessed both “latent” control (via his

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<sup>77</sup> C.A. No. 9210-CB, 2014 WL 5139489 (Del. Ch. Oct. 14, 2014).

<sup>78</sup> C.A. No. 7393-VCN, 2014 WL 6735457 (Del. Ch. Nov. 26, 2014).

<sup>79</sup> C.A. No. 8541-VCP, 2014 WL 5449419 (Del. Ch. Oct. 24, 2014).

<sup>80</sup> C.A. No. 9132-VCG, 2014 WL 6673895 (Del. Ch. Nov. 25, 2014).

<sup>81</sup> The court further held that business judgment review would in any event apply because the merger was approved by a majority of disinterested stockholders in a fully-informed vote.

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<sup>76</sup> *Id.* at 33-34.

stock ownership) and “active” control (with respect to the day-to-day operations) of Zhongpin.<sup>82</sup> The court went on to conclude that entire fairness review applied notwithstanding the approval of a special committee and the fact that the deal (signed prior to the Delaware Supreme Court’s decision in *MFW*) was subject to (i) non-waivable majority-of-the-minority approval (which it obtained), (ii) a 60-day go-shop period (that was later extended) and (iii) a unilateral right on the part of the company to terminate the agreement for any reason during the go-shop period with no breakup fee, because the majority-of-the-minority condition had not been included in the CEO’s proposal at the outset.<sup>83</sup>

In *In re Crimson Exploration*, Vice Chancellor Parsons declined to apply entire fairness review to breach of fiduciary duty claims in a class action asserting inadequate price in a stock-for-stock merger, notwithstanding allegations that a hedge fund owning 33 percent of the stock was a controller. En route to dismissing the action under the business judgment rule, the court conducted an extensive survey of the Court of Chancery’s then-extant decisional law addressing “controller” status for minority stockholders, concluding that those cases “do not reveal any sort of linear, sliding-scale approach whereby a larger share percentage makes it substantially more likely that the court will find the stockholder was a controlling stockholder,” but show instead that “a large blockholder will not be considered a controlling stockholder *unless they actually control the board’s decision about the challenged transaction.*” (Emphasis added.)<sup>84</sup>

Finally, in *In re Sanchez Energy*, Vice Chancellor Glasscock dismissed a derivative suit, alleging claims of breach of fiduciary duty against the directors of Sanchez Energy in connection with an asset purchase, for failure to plead demand futility under Rule 23.1. Plaintiffs alleged that

demand should be excused because the transaction, in which Sanchez Energy purchased assets from an entity purportedly controlled by two of Sanchez Energy’s directors (members of the founding Sanchez family who were also minority stockholders), was tainted by those directors’ conflicts of interest and lack of independence. The court noted, among other things, that an effectively mandated audit committee of disinterested directors had approved the transaction and that plaintiffs’ complaint was, unsurprisingly, silent as to the committee’s evaluation process given plaintiffs’ failure to make a pre-suit books-and-records demand under 8 Del. C. § 220. While acknowledging that plaintiffs had highlighted various friendships and outside business relationships between the disinterested and allegedly conflicted directors, the court, citing both the Chancellor’s decision in *In re KKR* and Vice Chancellor Parson’s decision in *In re Crimson Exploration*, emphasized that, given their combined 21.5 percent (*i.e.*, less than 50 percent) stake in Sanchez Energy, in order to adequately allege that the two purportedly conflicted directors were controlling stockholders, plaintiffs must plead specific facts demonstrating actual control of the board *in connection with the transaction being challenged*, which the court described as the “defining and necessary feature of a controlling minority stockholder.” Allegations of day-to-day operational control were insufficient.

### Takeaways

While three of the four recent decisions in this area seem to agree that specific allegations of domination of the board with respect to the challenged transaction itself – rather than mere allegations of day-to-day managerial or operational control of the business – are necessary to support an inference of control by a minority stockholder, for the moment, at least, it is by no means safe to assume that a stockholder with a less than 35 percent stake in the company will be deemed not to be a controller. Rather, a case-specific inquiry into, among other things, the extent to which the stockholder in question influences the board or directs the day-to-day operations of the company may well result in a pleadings-stage determination that an inference of control by a stockholder holding a materially smaller block has been raised.

## Additional Developments In Delaware Business And Securities Law

Beyond those topics addressed above, the Delaware courts also issued noteworthy decisions in the following areas of law during the past quarter.

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<sup>82</sup> The court expressly acknowledged and distinguished prior Delaware precedent rejecting the notion at a 15-17 percent blockholder was a controller.

<sup>83</sup> On December 23, 2014, the court certified the Zhongpin Special Committee defendants’ interlocutory appeal from this decision based on their argument under the 102(b)(7) exculpation provision in the company’s charter. The court had rejected those arguments under *In re Cornerstone Therapeutics Inc. Stockholders Litigation*, C.A. No. 8922-VCG, 2014 WL 4418169 (Del. Ch. Sept. 10, 2014), in which defendants’ interlocutory appeal was certified by the Court of Chancery and accepted by the Delaware Supreme Court. *In re Zhongpin Inc. S’holders Lit.*, C.A. No. 7393-VCN (Del. Ch. Dec. 23, 2014).

<sup>84</sup> The court went on to determine that even if plaintiffs had sufficiently alleged that the hedge fund and certain other stockholders with which it was alleged to have acted in concert constituted a control group (and they had not), the handful of side benefits received by those stockholders (prepayment of a lien held by the fund and a registration rights agreement that allowed the fund to sell stock in a private placement) were insufficient to show that the fund either bargained for them in return for pricing its holdings or otherwise competed with common stockholders. The court further noted that there were no agreed upon additional benefits flowing to the alleged “controller” at the time the merger agreement was signed (the prepayment was not part of the merger agreement and the registration rights were of no value to the widely dispersed common stockholders). Accordingly, the court dismissed plaintiffs’ claims of inadequate price under the business judgment rule and in light of the company’s 102(b)(7) exculpatory charter provision.

### Acquiescence

In *Lehman Brothers Holdings Inc. v. Spanish Broadcasting System, Inc.*,<sup>85</sup> the Delaware Supreme Court affirmed the Court of Chancery's dismissal of plaintiffs' claims challenging defendant corporation's incurrence of debt. According to the Court, plaintiffs, who were preferred stockholders, had acquiesced to the incurrence of debt by failing to object to or invoke their purported right to limit the debt transactions at issue. The Court found that the corporation had relied on plaintiffs' silence in consummating the debt transactions.

### Alternative Entities

#### *Amendment to Partnership Agreement*

In *In re Kinder Morgan, Inc. Corporate Reorganization Litigation*,<sup>86</sup> Vice Chancellor Laster, in a memorandum opinion, denied plaintiffs' motion for preliminary injunction against the closing of a merger, finding that the merger did not require a heightened voting standard under the partnership agreement. Plaintiffs, holders of partnership units in the partnership, a subsidiary of Kinder Morgan, Inc., sought to block a transaction through which the parent company would emerge as the only publicly traded entity, alleging that the merger was subject to approval of a higher voting threshold of unit holders under the partnership agreement. While the partnership agreement only required approval by a majority of the outstanding units, plaintiffs argued that an exception applied, the "Amendment-By-Merger Exception," requiring a more arduous voting standard. The court found that this exception was only applicable if the partnership agreement were to be amended through the merger, which it was not. The court denied plaintiffs' motion, finding that plaintiffs do not have a reasonable probability of success on the merits because the partnership will be the surviving entity and because the merger will not otherwise amend the partnership agreement.

#### *Fiduciary Duties; Breach of Contract*

In *B&L Cellular, et al. v. USCOC of Greater Iowa, et al.*,<sup>87</sup> Vice Chancellor Laster, in a memorandum opinion, found that plaintiffs proved at trial that a sale of partnership assets and dissolution orchestrated by defendants was not entirely fair to plaintiffs, who held a minority of the partnership. Applying District of Columbia law as required by the partnership agreement, the court found that the

majority-controlling defendants had failed to ensure both the procedural and the substantive fairness of the sale of partnership assets to a related party, thus breaching their fiduciary duties to plaintiffs. The court oversaw valuation of the partnership assets and awarded plaintiffs their *pro rata* share of the difference between the valuation and original sale price, but denied plaintiffs' request for fees. Plaintiffs also proved improper release of confidential information to the appraisal advisor used in the transaction, but suffered only nominal damages from that violation.

### Appraisal Proceedings

In *Mehta, et al. v. Smurfit-Stone Container Corp., et al.*,<sup>88</sup> Vice Chancellor Laster, in a memorandum opinion, denied defendants' motion to dismiss plaintiff stockholders' claim for merger consideration where plaintiffs made a timely demand for appraisal, but subsequently withdrew their demand after the 120-day deadline to file an appraisal action lapsed. While defendants argued that plaintiffs could not withdraw their appraisal demand without the defendant corporation's consent, the court disagreed, holding that expiration of the deadline triggered defendants' obligation to pay plaintiffs the merger consideration.

### Arbitration

In *Roncone v. Phoenix Payment Systems, Inc., et al.*,<sup>89</sup> Vice Chancellor Noble, in a memorandum opinion, granted summary judgment in favor of plaintiff, confirming an arbitrator's award to plaintiff of unpaid commissions, liquidated damages, and attorney's fees in connection with an employment dispute. Plaintiff initiated an arbitration alleging that defendants violated the Delaware Wage Payment and Collection Act ("WPCA"). The court noted that as long as the arbitrator's determination was reasonable, the award would remain undisturbed. After reviewing the record, the court found that the arbitrator acted within the bounds of reason in limiting the scope of the arbitration and in relying on the original employment agreement. The court found that the arbitrator acted within the authority granted by the WPCA, which permits imposition of liability on employees in management positions who exercise authority over payment decisions. The court also held that WPCA claims may be heard in an arbitration and found that the arbitrator was within his authority in awarding liquidated damages and attorney's fees.

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<sup>85</sup> No. 174, 2014, 2014 WL 7010807 (Del. Dec. 11, 2014).

<sup>86</sup> C.A. No. 10093-VCL, 2014 WL 5667334 (Del. Ch. Nov. 5, 2014).

<sup>87</sup> C.A. No. 7628-VCL, 2014 WL 6882207 (Del. Ch. Dec. 8, 2014).

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<sup>88</sup> C.A. No. 6891-VCL, 2014 WL 5438534 (Del. Ch. Oct. 20, 2014).

<sup>89</sup> C.A. No. 8895-VCL, 2014 WL 6735210 (Del. Ch. Nov. 26, 2014).

### Attorney's Fees

#### Charging Lien

In *Zutrau v. Jansing, et al.*,<sup>90</sup> Vice Chancellor Parsons, in a letter opinion, granted plaintiff's former counsel's request for a charging lien but not in the amount counsel requested. The court considered, *inter alia*, whether an agreement between the parties precluded the entry of a charging lien and whether expert fees could be included in the calculation of the lien. The court found that the engagement letter between counsel and plaintiff did not preclude a lien. In connection with whether the lien could include the costs of experts called on behalf of plaintiff at trial – a question of first impression in Delaware – counsel argued that the expert fees should be included even though plaintiff was contractually obligated to pay the fees and not counsel, arguing that if plaintiff failed to pay, counsel's reputation and ability to retain experts in the future would be impaired. The court disagreed, noting that the rationale for a charging lien is to compensate the attorney for his or her efforts and that here there was no evidence that counsel would be liable for the expert fees. The court granted the lien in the amount of \$200,000 and ordered counsel to submit documentation of unpaid fees and expenses.

#### Fee Award

In *DiRienzo v. Lichtenstein, et al.*,<sup>91</sup> Vice Chancellor Parsons, in a bench ruling, approved a class settlement but reduced the fee award requested by plaintiff. The proposed settlement required that defendants pay \$1.3 million to the former minority stockholders of a corporation. Plaintiff's counsel sought \$390,000 in attorney's fees, an additional \$80,394.86 in expenses, and \$50,000 in lead plaintiff compensation. The court found that these amounts were unreasonably high. According to the court, based on the Delaware Supreme Court's recent ruling indicating that 33 percent of the settlement value represents "the very top range" of a reasonable fee award,<sup>92</sup> plaintiff's proposed 40 percent award was excessive. Accordingly, the court, acknowledging the complexity of the case, granted a \$400,000 all-in award, inclusive of up to \$10,000 in lead plaintiff compensation, representing 31 percent of the settlement value.

In *ReCor Medical, Inc. v. Warnking, et al.*,<sup>93</sup> Vice Chancellor Noble, in a letter opinion, determined the appropriate amount of attorney's fees to be awarded to plaintiff in accordance with a contractual fee-shifting provision. Plaintiff prevailed in a contractual dispute over intellectual property and sought attorney's fees under the parties' agreement, which provided that the prevailing party in any litigation arising under the agreement was entitled to attorney's fees and expenses. Defendants disputed the amount of fees, arguing, *inter alia*, that fees arising from pre-litigation negotiations and dismissed and abandoned claims should be excluded. Defendants also argued that they were entitled to a set-off for seeking injunctive relief to protect the intellectual property, which ultimately benefitted plaintiff. The court agreed with defendants' argument that protecting the patentability of the intellectual property was to plaintiff's benefit and found that while the fees sought by plaintiff fell within the range of reasonableness, the fees should be offset by plaintiff's costs in resisting the injunctive relief. The court credited defendant's fees in connection with the same.

In *In re TPC Group Inc. Shareholders Litigation*,<sup>94</sup> Vice Chancellor Noble, in a letter opinion, denied plaintiffs' application for an award of attorney's fees based on allegations that litigation brought by plaintiffs contributed to an increased merger price, finding that there was no connection between the lawsuit and the increase in the merger price. Plaintiffs, stockholders in TPC Group, had initiated suit after private equity firms announced a deal to acquire TPC at \$40 per share, claiming inadequate price, breaches of fiduciary duty through unfair process, and inadequate disclosures. These claims became moot after further disclosures and a raise in bid from \$40 to \$45. Plaintiffs claimed this increase was attributable to their litigation and that they should be awarded \$3,150,000 in attorney's fees and expenses. Noting that a key requirement of such an award is that the benefit to the corporation be causally related to the lawsuit – which normally takes the form of a rebuttable presumption with defendants, who are best situated to present alternate causes, given the burden of showing by a preponderance of the evidence the absence of causation between the litigation and price increase – the court found that defendants had met this burden by showing that the price increase was attributable to a rival bid, concerns over negative publicity, and fears of opposition from a leading proxy advisory firm. The court also noted that with

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90 C.A. No. 7475-VCP, 2014 WL 7013578 (Del. Ch. Dec 8, 2014).

91 C.A. No. 7094-VCP (Del. Ch. Oct. 10, 2014).

92 *Americas Mining Corp. v. Theriault*, 51 A.3d 1213, 1259 (Del. 2012).

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93 C.A. No. 7387-VCN, 2014 WL 5317768 (Del. Ch. Oct. 15, 2014).

94 C.A. No. 7865-VCN, 2014 WL 5500000 (Del. Ch. Oct. 29, 2014).



litigation challenges to mergers now seemingly inevitable, the likelihood of influencing an acquiror's pricing decision through litigation is diminished.

### Books and Records Actions

In *United Technologies Corp. v. Treppel*,<sup>95</sup> Chief Justice Strine, writing for the Delaware Supreme Court *en banc*, reversed the Court of Chancery in an inspection action under 8 Del. C. § 220. The Court of Chancery had rejected United Technologies' request to restrict the use of any information obtained by stockholder Treppel pursuant to a books and records inspection to legal action in a Delaware court, reasoning that such a limitation "is not the type of restriction that 220(c) seeks to impose." The Supreme Court disagreed, holding that because the "plain text of § 220 provides broad power to the Court of Chancery to condition a books and records inspection, the court erred in determining that it lacked authority under the statute to impose the requested restriction."

In *Oklahoma Firefighters Pension & Retirement System v. Citigroup Inc.*,<sup>96</sup> Master LeGrow, in a master's report, recommended that a plaintiff stockholder be allowed to inspect the records of a parent publicly traded company under 8 Del. C. § 220 based on alleged wrongdoing of its subsidiaries because plaintiff had stated a "credible basis" to infer possible mismanagement or wrongdoing by the management of the parent company. Plaintiff sought to inspect records relating to the discovery of fraud and possible money laundering at the subsidiaries, and defendant parent company argued that plaintiff had not stated a credible basis to infer mismanagement on the part of its board or senior management. While the court recognized that wrongdoing in a subsidiary alone is not a credible basis to infer mismanagement by the parent's senior management, plaintiffs had shown more. Master LeGrow found that evidence of the scope of the fraud at the subsidiaries, the effect of the fraud on the parent's profits, deficiencies in internal controls, and the oversight of the parent over the subsidiaries was sufficient to meet the very low burden of proof required by the "credible basis" standard under Section 220(b).

In *Prokupek v. Consumer Capital Partners LLC, et al.*,<sup>97</sup> Vice Chancellor Noble, in a letter opinion, granted defendant Smashburger Master LLC's motion to dismiss an inspection action filed by Smashburger's former CEO under Delaware's Limited Liability Company Act. The court found

that plaintiff lacked inspection rights under the LLC Act or the operative LLC agreement because he was no longer a member of the company when he demanded inspection. According to the court, Smashburger had redeemed all of plaintiff's units after Smashburger terminated plaintiff's employment. The court also rejected plaintiff's argument that he retained inspection rights as a former member of the company, concluding that no such rights exist under either the LLC agreement or the LLC Act, which, like its corporate analogue, 8 Del. C. § 220, the court noted is to be narrowly construed.

In *Wolst v. Monster Beverage Corporation*,<sup>98</sup> Vice Chancellor Noble, in a letter opinion, rejected plaintiff stockholder's books and records action under 8 Del. C. § 220, holding that plaintiff's "sole purpose" in bringing the action was to pursue a derivative action barred by laches. The court further held that the central holding in *American Pipe*,<sup>99</sup> *i.e.*, that the pendency of a class action tolls the limitations period for direct claims of putative class members, should not be extended to derivative claims.

### Contract Claims

#### *Breach of Contract*

In *Lockwood, et al. v. Capano*,<sup>100</sup> the Delaware Supreme Court reversed a Superior Court of Delaware order granting in part appellee's motion for summary judgment on its contract claim against appellants. The Court held that there existed a genuine issue of material fact as to whether having certain parties sign a contribution agreement in connection with a loan was a condition precedent to the agreement's formation and, accordingly, remanded the action for further proceedings.

In *NAMA Holdings, LLC v. Related WMC LLC, et al.*,<sup>101</sup> Vice Chancellor Laster, in a memorandum opinion constituting a virtual exegesis on the implied covenant of good faith and fair dealing, held that one holding company (Related WMC) breached such an implied covenant in connection with a custodial contract with a second holding company (NAMA) by failing to act neutrally as to funds in dispute between NAMA and two third-parties. The court, in a post-trial decision, found that Related WMC breached an implied term of the custodial contract by holding certain funds at issue in an arbitration between NAMA and the third-parties beyond the point when they could have been released to NAMA and arranging to release them into the third-parties'

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95 No. 127, 2014 (Del. Dec. 23, 2014).

96 C.A. No. 9587-ML, 2014 WL 5351345 (Del. Ch. Sept. 30, 2014).

97 C.A. No. 9918-VCN (Del. Ch. Dec. 30, 2014).

98 C.A. No. 9154-VCN, 2014 WL 4966139 (Del. Ch. Oct. 3, 2014).

99 *Am. Pipe & Constr. Co. v. Utah*, 414 U.S. 538 (1974).

100 No. 89, 2014, 2014 WL 7009737 (Del. Nov. 10, 2014).

101 C.A. No. 7934-VCL, 2014 WL 6436647 (Del. Ch. Nov. 17, 2014).

control, knowing that the third-parties intended to pocket some of the funds when they were not entitled to any of them. The court also held that Related WMC's parent company tortuously interfered with the custodial contract by directing Related WMC to release the entirety of the disputed amounts to the third-parties as part of a *quid pro quo* for the parent company's access to the third-parties' escrow accounts.

In *Great Hill Equity Partners IV, LP, et al. v. SIG Growth Equity Fund I, LLLP, et al.*,<sup>102</sup> Vice Chancellor Glasscock, in a memorandum opinion, denied, in significant part, defendants' motion to dismiss. Plaintiffs, representatives of the acquiring company, alleged that defendants, former stockholders and representatives of the target company, made fraudulent misrepresentations in connection with the acquisition, including by failing to disclose that a third-party was potentially going to terminate its payment-processing relationship with the target company. The court concluded that plaintiffs had sufficiently alleged claims for fraud and fraudulent inducement. The court did, however, dismiss plaintiffs' unjust enrichment claims against certain defendants on the ground that these defendants had received no merger consideration. The court also dismissed plaintiffs' declaratory judgment claim, finding that it was "duplicative" of plaintiffs' fraud claims.

### Interpretation

In *In the Matter of the Liquidation of Freestone Insurance Company*,<sup>103</sup> Vice Chancellor Laster, in a memorandum opinion, denied U.S. Bank, N.A.'s request to retain assets pursuant to a claimed security interest, finding that U.S. Bank was required to turn over the assets of Freestone Insurance Company, an entity currently in receivership under the administration of the Insurance Commissioner of the State of Delaware, to the Insurance Commissioner. Freestone had maintained \$175 million in cash and securities in an account with U.S. Bank, governed by a custody agreement under Minnesota law. Freestone became delinquent and the court issued a rehabilitation order causing title to Freestone's property to vest in the Commissioner as receiver. The Insurance Commissioner subsequently instructed U.S. Bank to return the assets, but U.S. Bank only agreed to release \$19 million of the account's assets – arguing that, *inter alia*, it was entitled to keep the remainder as security against indemnification claims under the custody agreement. The court found that under the Delaware Uniform Insurance Liquidation Act, the Insurance Commissioner held those rights previously

possessed by Freestone, including the return of the assets on demand subject to the provisions of the custody agreement. The court found that under the agreement, U.S. Bank could only withhold the fees and expenses it incurred in administering the account.

In *JD Holdings, LLC, et al. v. Jacqueline A. Dowdy as Trustee of the Revocable Trust of John Q. Hammons, et al.*,<sup>104</sup> Vice Chancellor Laster, in a memorandum opinion, held that the plain meaning of a right of first refusal agreement between an investor and hotel developer required the developer's trust to sell all hotel properties for cash within two years of the death of the developer or redeem all preferred equity units from the original limited partnership. The court rejected defendants' argument that the agreement constituted an unreasonable restraint on alienation, reasoning that the agreement permitted the trust to sell the property to anyone, subject only to the investor's right of first refusal. The court also rejected defendants' argument that the right of first refusal violated the rule against perpetuities.

In *Salamone, et al. v. Gorman*,<sup>105</sup> the Delaware Supreme Court affirmed in part and reversed in part the Court of Chancery's ruling interpreting a voting agreement in a dispute between two competing sets of stockholders regarding the composition of Westech Capital Corporation's board. One group of stockholders argued that the voting agreement provided that directors be designated pursuant to a per capita scheme while the other group asserted that the agreement mandated a per share scheme. The Supreme Court, largely adopting the Court of Chancery's rationale, found that Section 1.2(b) of the voting agreement, which governed the designation of an independent director by the majority of the holders of "Series A Preferred Stock," required application of a per share scheme. According to the Supreme Court, while there existed some evidence supporting a per capita interpretation of this "ambiguous" provision, such evidence failed to overcome Delaware's presumption "against disenfranchising the majority stockholder, absent a clear intent by the parties to a contract to do so." The Supreme Court also agreed with the Court of Chancery that, by its plain language, Section 1.2(c) of the voting agreement, which governed director designations by "Key Holders," required a per capita scheme. Finally, the Supreme Court reversed the Court of Chancery in part, holding that the

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<sup>102</sup> C.A. No. 7906-VCG, 2014 WL 6703980 (Del. Ch. Nov. 26, 2014).

<sup>103</sup> C.A. No. 9574-VCL (Del. Ch. Dec. 24, 2014).

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<sup>104</sup> C.A. No. 7480-VCL, 2014 WL 4980669 (Del. Ch. Oct. 1, 2014).

<sup>105</sup> No. 343, 2014, 2014 WL 7003889 (Del. Dec. 9, 2014).

director removal provisions pursuant to Section 1.4 of the agreement were intended to be “symmetrical” with the designation schemes set forth in Sections 1.2(b) and 1.2(c).

### *Letter of Intent*

In *ev3, Inc. v. Lesh, et al.*,<sup>106</sup> the Delaware Supreme Court reversed the Superior Court’s denial of a motion for a new trial because the lower court had erred in permitting plaintiffs to argue that non-binding Sections of a letter of intent later integrated into a merger agreement affected a funding provision in the underlying agreement, which defendant allegedly breached. The merger agreement between ev3, Inc. and Appriva Medical, Inc. made payments to Appriva stockholders contingent upon the company meeting milestones in the development of a medical device. Under Section 9.6 of the merger agreement, ev3 had “sole discretion, to be exercised in good faith” to fund the milestones. However, under an earlier non-binding provision of a letter of intent, ev3 was required to provide “sufficient capital” to meet the milestones. Defendant ev3 argued at trial that the non-binding letter of intent should not be used to interpret or contradict the clear terms of Section 9.6 of the merger agreement but the lower court disagreed and permitted Appriva’s stockholders to argue that ev3 not only failed to act in good faith under Section 9.6 but also breached a “promise” to honor the funding provision contained in the non-binding letter of intent. The Supreme Court found that the lower court erred in admitting the letter of intent to affect the meaning of the merger agreement, because by its own terms Section 9.6 of the merger agreement overrode any “provisions to the contrary” and made clear that it was within ev3’s discretion to provide funding for the achievement of the milestones. In addition, the merger agreement “did not convert the nonbinding funding provision into a binding contractual obligation.”

### *Merger Agreement; Estoppel*

In *Cooper Tire & Rubber Company v. Apollo (Mauritius) Holdings Pvt. Ltd., et al.*,<sup>107</sup> Vice Chancellor Glasscock declined to enforce a merger agreement in a memorandum opinion granting defendants’ motion for entry of a declaratory judgment on the grounds that the agreement’s closing conditions had not been met. Defendant Apollo’s attempt to purchase plaintiff Cooper had gone awry when (i) employees of Cooper’s Chinese subsidiary physically seized its Chinese facilities, halted production, and restricted access to financial documents

at the behest of a dissident minority partner in the affiliate and (ii) separate labor issues in the United States resulted in the failure of the parties to reach an agreement with labor under a collective bargaining agreement. Apollo sought declaratory relief to prevent Cooper from attempting to collect a \$112 million breakup fee, and the court found that, as a result of the disruptions in China and lack of progress in the labor negotiations, Cooper had failed to meet the merger agreement’s requirement that Cooper “cause each of its subsidiaries to conduct its business in the ordinary course of business.” The court also rejected Cooper’s contention that Apollo should be estopped from challenging Cooper’s failure to meet the closing conditions because it negotiated to buyout the Chinese dissident partner and objected to Cooper’s proposal to replace security personnel at the Chinese facility, finding that Apollo’s conduct did not rise to the level of participating or acquiescing in any breach of the terms of the merger agreement and, therefore, did not provide grounds for estoppel.

In *Cigna Health & Life Insurance Company v. Audax Health Solutions, Inc., et al.*,<sup>108</sup> Vice Chancellor Parsons, in a memorandum opinion, granted in part and denied in part plaintiff’s motion for judgment on the pleadings in a declaratory judgment action questioning the validity of certain provisions of a merger agreement that a buyer was seeking to enforce against the target company’s stockholders, finding invalid (i) a general release of claims provision in a letter of transmittal for lack of consideration and (ii) an indemnification obligation in the merger agreement as violative of 8 *Del. C.* § 251. Plaintiff argued that the general release obligation violated Section 251 because the letter was a contract entered into without consideration. The court agreed, finding that the release obligation was a new obligation that defendants sought to impose on plaintiff post-closing without any new consideration beyond the merger consideration to which plaintiff was entitled when the merger was consummated. In connection with the indemnification obligation, the court found that the provision violated Section 251(b)(5) because it prevented the target company’s stockholders from determining the value of the merger consideration. While the stockholders received their *pro rata* share of the merger consideration, the ultimate value of that consideration – consideration which may need to be returned to defendant for breaches of certain representations and warranties – was uncertain.

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<sup>106</sup> No. 515, 2013, 2014 WL 4914905 (Del. Sept. 30, 2014).

<sup>107</sup> C.A. No. 8980-VCG, 2014 WL 5654305 (Del. Ch. Oct. 31, 2014).

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<sup>108</sup> C.A. No. 9405-VCP, 2014 WL 6784491 (Del. Ch. Nov. 26, 2014).

### Derivative Actions

#### Creditor Derivative Claims

In *Quadrant Structured Products Co., Ltd., et al. v. Vertin, et al.*,<sup>109</sup> Vice Chancellor Laster, in an opinion dealing with creditor derivative claims, applied the business judgment rule in an action challenging a decision by the board of an insolvent corporation to adopt a high-risk business plan. Plaintiff creditors alleged, among other things, that all of the risk associated with the business plan would be borne by the corporation's creditors while the corporation's lone stockholder would benefit if the plan succeeded. According to the court, because the board's decision was intended to maximize the insolvent corporation's value, application of the business judgment rule was appropriate. The court did, however, conclude that the decision by certain directors not to defer interest on the notes held by the corporation's controller warranted entire fairness scrutiny. A month later, Vice Chancellor Laster, in a memorandum opinion, denied plaintiffs' motion for reargument with respect to their claim challenging the board's adoption of the high-risk business plan.<sup>110</sup>

#### Demand Futility

In *Higher Education Management Group, Inc., et al. v. Mathews, et al.*,<sup>111</sup> Vice Chancellor Parsons, in a memorandum opinion, granted defendants' motion to dismiss a derivative action for breach of the duty of loyalty, finding that plaintiffs failed to sufficiently plead that demand would have been futile under the *Aronson*<sup>112</sup> test. Plaintiffs, stockholders of Aspen Group, Inc., alleged that defendant directors and former CFO of the company knowingly misrepresented the existence of loans to the SEC. The court noted that in order to plead demand futility under *Aronson*, plaintiffs must show with particularized facts that: (i) the directors are not disinterested and independent; or (ii) the transaction was not the product of a valid exercise of business judgment. The court found that plaintiffs failed to meet the first prong of *Aronson* as plaintiffs failed to show that the majority of directors were aware of the fabricated loan or of the fact that it was not collectible. In addition, the court found that plaintiffs fell short of the high pleading threshold required to allege bad faith conduct under the second prong of *Aronson*. As such, the court dismissed plaintiffs' fiduciary duty claims for lack

of demand and plaintiffs' related aiding and abetting claim. The court also dismissed plaintiffs' waste and dilution claims.

### Discovery

#### Confidentiality Designations

In *Reid v. Siniscalchi, et al.*,<sup>113</sup> Vice Chancellor Noble, in a letter opinion, denied defendants' motion to maintain confidential treatment of documents filed in the action that were well over ten years old, finding that the need for confidential treatment was no longer apparent. Defendants failed to provide any persuasive reasons for continued confidential treatment and failed to explain why the need for confidential treatment outweighed the public interest in the proceedings. As such, the court deemed the documents public but stayed its order for sixty days to allow defendants to identify any particular documents that deserve continued confidential treatment.

#### Privilege Log

In *Mechel Bluestone, Inc., et al. v. James C. Justice Companies, Inc., et al.*,<sup>114</sup> Vice Chancellor Laster, in a memorandum opinion, partially granted defendants' motion to compel the production of documents identified on plaintiffs' privilege log, finding privilege waived as to the items where plaintiffs fell substantially short of the requirements supporting a claim of privilege. Plaintiffs' original privilege log designated over one-third of the production as privileged and included numerous omissions and inconsistencies. Defendants' complaints led to four revisions of the log, accompanied by late and problematic productions, illustrating broader and systemic problems with plaintiffs' counsel's discovery efforts. While the court declined defendants' request to require the production of all documents marked as privileged, the court did require production of the items suffering from several specific deficiencies that the court outlined in its opinion. In addition, the court ordered plaintiffs to prepare a corrected log and appointed a special discovery master, at plaintiffs' expense, to review any future challenges to the log and production.

#### Protective Orders

In *Theravectys SA v. Immune Design Corp.*,<sup>115</sup> Vice Chancellor Noble, in a letter opinion, granted in part and denied in part non-party Novasep US's motion for a protective order, finding that documents of a foreign

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<sup>109</sup> 102 A.3d 155 (Del. Ch. Oct. 1, 2014).

<sup>110</sup> C.A. No. 6990-VCL, 2014 WL 5465535 (Del. Ch. Oct. 28, 2014).

<sup>111</sup> C.A. No. 9110-VCP, 2014 WL 5573325 (Del. Ch. Nov. 3, 2014).

<sup>112</sup> *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984).

<sup>113</sup> C.A. No. 2874-VCN, 2014 WL 6486589 (Del. Ch. Nov. 20, 2014).

<sup>114</sup> C.A. No. 9218-VCL, 2014 WL 7011195 (Del. Ch. Dec. 12, 2014).

<sup>115</sup> C.A. No. 9950-VCN, 2014 WL 5500506 (Del. Ch. Oct. 31, 2014).

affiliate of Novasep were not within Novasep's possession, custody or control. The underlying dispute involved defendant Immune Design Corporation's ("IDC") alleged interference with the business relationship between plaintiff and the Belgian manufacturer Henogen SA, a Belgian corporate affiliate of Novasep. Applying Court of Chancery Rule 34(a), the court found that Novasep, whose primary function was only to facilitate agreements for affiliates like Henogen, lacked possession, custody or control of documents regarding Henogen's Belgian operations. The court did require, however, that Novasep produce any documents relating to (i) its own role in the negotiations between Henogen and IDC and (ii) its corporate structure and affiliate relationships, as those documents could aid in plaintiff's attempt to demonstrate Novasep's control over its foreign affiliate.

### *Sanctions; Role of Delaware Counsel*

In *James v. National Financial LLC*,<sup>116</sup> Vice Chancellor Laster, in a letter opinion, sanctioned defendant's discovery misconduct by establishing for purposes of trial that defendant's annual percentage rates for pay-day loans were higher than permitted under the Truth in Lending Act. After finding that defendants repeatedly failed to comply with discovery orders, provided inconsistent explanation for failures, and had a letter notarized without having the signor present, the court explained that technical incompetence was "not an excuse for discovery misconduct." The case is particularly noteworthy, however, for its confirmation that "the Court of Chancery does not recognize the role of purely 'local counsel,'" even when out-of-state counsel takes the lead role in the case, and held Delaware counsel responsible for the discovery failures despite their lack of involvement. Stressing in particular that Delaware counsel must be involved in discovery, the court explained that: "the court expects Delaware counsel to play an active role in the discovery process, including the collection, review and production of documents. If Delaware counsel does not directly participate in the collection, review and production of documents, then at a minimum Delaware counsel should discuss with co-counsel the court's expectations."<sup>117</sup>

## Experts

### *Valuation Expert*

In *AM General Holdings LLC v. The Renco Group, Inc.*,<sup>118</sup> Vice Chancellor Noble, in a letter opinion, appointed an appraiser to serve as a third valuation expert in a joint venture dispute over the value of an operating company in the global defense industry after the two joint venture investors sued each other over the operating company's financial and management operations. Both sides proposed two appraisal firms from which the court made its selection. The court emphasized the difficulty of the decision due to the sensitive nature of the operating company and the insurmountable task of finding an appraiser without any conflicts given the wide-ranging activities of the two investors and their affiliates. Relying on the guidelines established by the parties, including that the appraiser be a firm and not an individual, the court picked a smaller company – Valuation Research Corporation – that conducts valuations in the U.S. and abroad. The court also denied the motion of one of the parties to exclude or redact portions of the opposing party's alternate appraiser because that appraiser's comments, which appeared to contradict the moving party's appraiser, were not prejudicial.

## Fiduciary Duties

### *Aiding and Abetting*

In *Matthew v. Laudamiel, et al.*,<sup>119</sup> Vice Chancellor Noble, in a letter opinion, denied defendant Flakt Woods Group SA's motion for summary judgment on claims of aiding and abetting breach of fiduciary duty, tortious interference with contractual relations, and civil conspiracy, concluding that the claims were not foreclosed by parallel contract claims and that triable issues of fact remained. Normally, claims of breach of duty must have an independent basis from and not be duplicative of breach-of-contract claims for them to coexist. The court here determined that there was such an independent basis. It held that plaintiff adequately highlighted evidence that defendant may have conspired to oust him from his company, Aeosphere LLC, in order to facilitate defendant's acquisition of Aeosphere's clients after the corporation's dissolution and wind-up. But the court granted summary judgment on plaintiff's unjust enrichment claim, finding that plaintiff failed to point to any evidence that defendant was enriched by its actions in any way.

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<sup>116</sup> C.A. No. 8931-VCL (Del. Ch. Dec. 5, 2014).

<sup>117</sup> *Id.* at 27.

<sup>118</sup> C.A. No. 7639-VCN, 2014 WL 6734850 (Del. Ch. Nov. 28, 2014). The same opinion was also issued in a companion case, *The Renco Group, Inc. v. MacAndrews AMG Holdings LLC*, C.A. No. 7668-VCN, 2014 WL 6734850 (Del. Ch. Nov. 28, 2014).

<sup>119</sup> C.A. No. 5957-VCN, 2014 WL 5904716 (Del. Ch. Nov. 12, 2014).



### *Breach of Fiduciary Duty; Exclusivity Agreements; Termination Fees*

In *In re Comverge, Inc. Shareholders Litigation*,<sup>120</sup> Vice Chancellor Parsons, in a memorandum opinion, dismissed bad-faith claims against the Comverge board of directors for failing to sue the acquiring company for breach of an non-disclosure agreement, prematurely entering into an exclusivity agreement with the acquiring company, and conducting a flawed sales process. But the court allowed fiduciary duty claims against the board to go forward in the face of a 102(b)(7) exculpatory provision that were based on allegations of an unreasonable termination fee – a fee which, when considered in light of convertible notes issued pursuant to a bridge loan that the acquiring company funded immediately, was as high as 13 percent of the equity value of the transaction. The opinion provides guidance in negotiating acceptable deal protection measures where *Revlon* applies, essentially giving practitioners a road map to how the Chancery Court reviews challenges to third-party sales transactions. And in what is yet another recent decision refining the scope of third-party aiding-and-abetting liability, the court dismissed aiding-and-abetting claims against the acquiring company because the underlying, related fraud claims against the directors did not survive and, in any event, there were no allegations the company knowingly participated in a breach of fiduciary duty.

### *Duty of Loyalty*

In *Lake Treasure Holdings, Ltd., et al. v. Foundry Hill GP LLC, et al.*,<sup>121</sup> Vice Chancellor Laster, in a memorandum opinion, held that the developer of an electronic trading business breached his duty of loyalty to investors and engaged in a fraudulent transfer when he secretly transferred the trading software to a third-party for substantially less than he thought it was worth. Defendant Taylor was the sole general partner of a partnership with plaintiffs (including a family foundation), the purpose of which was to engage in electronic trading. When the venture was unsuccessful and plaintiffs eventually filed suit, Taylor, with the aid of personal friend Klee, then deceptively transferred certain trading algorithms to a succession of different entities under their control. The court found that: (i) Taylor violated his duty of loyalty, as evaluated by the entire fairness standard, when he stood on both sides of the transfer and no attempt at a fair process was made; and (ii) Klee was liable for aiding and abetting the breach because of his intimate knowledge of

and involvement in Taylor's maneuvers. The court awarded only nominal damages for these breaches, however, because plaintiffs failed to provide a reasonable estimate of damages – plaintiffs' estimates assumed large-scale investment and sustained profitability with little support. The court credited the trial testimony of defendants' expert that the algorithms, while believed by Taylor and Klee to be unique and valuable, were in fact easily reproducible from basic knowledge of trading and computers, and thus lacked any value as intellectual property. The court also held that Taylor and Klee had engaged in a fraudulent transfer under the Delaware Uniform Fraudulent Transfer Act because they had an actual intent to defraud and ordered them to return the algorithms to plaintiffs.

In *In re Novell, Inc. Shareholder Litigation*,<sup>122</sup> Vice Chancellor Noble, in a memorandum opinion, granted director defendants' motion for summary judgment on bad-faith claims asserted by plaintiffs, former stockholders of a corporation that had recently completed a merger. Plaintiffs alleged that defendants had improperly "treat[ed] bidders differently for reasons other than pursuit of the best interests of the corporation and its stockholders." The court concluded that plaintiffs lacked evidence sufficient to create a genuine issue of material fact that a majority of defendant directors were biased in favor of certain bidders. It noted that, although the evidence showed that the directors did not treat all bidders equally, there is no law prohibiting that practice. Instead, there must be material conflict of interest held by a majority of the members of the board, something that plaintiffs failed to even allege. The court emphasized that it is "not the Court's job to second-guess decisions made by a majority independent Board which show that its decision-making process and actions were reasonable, though perhaps imperfect."

## **Indemnification and Insurance**

### *Fee Advancement*

In *Holley v. Nipro Diagnostics, Inc.*,<sup>123</sup> Vice Chancellor Parsons, in a memorandum opinion, found that defendant company was required to advance plaintiff former executive's legal expenses in connection with several civil suits and an SEC action relating to various insider trading allegations and to plaintiff's rights to advancement and indemnification even though plaintiff had pled guilty to two counts of criminal insider trading in connection with tips he gave regarding the impending acquisition of Home Diagnostics, Inc. ("HDI") by defendant Nipro

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<sup>120</sup> C.A. No. 7368-VCP, 2014 WL 6686570 (Del. Ch. Nov. 25, 2014).

<sup>121</sup> C.A. No. 6546-VCL, 2014 WL 5192179 (Del. Ch. Oct. 10, 2014).

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<sup>122</sup> C.A. No. 6032-VCN, 2014 WL 6686785 (Del. Ch. Nov. 25, 2014).

<sup>123</sup> C.A. No. 9679-VCP, 2014 WL 7336411 (Del. Ch. Dec. 23, 2014).

Diagnostics, Inc. Defendant argued that plaintiff was not entitled to advancement because the indemnity agreement precluded indemnification for claims of insider trading. The court rejected this argument, noting that the right to advancement is not dependent on the right to indemnification. In addition, the court found that plaintiff's guilty plea was not conclusive on the question as to whether plaintiff may be entitled to indemnification in the SEC action, finding that there were many ways in which plaintiff could be "successful on the merits or otherwise" in that action. The court rejected defendant's argument that plaintiff was not entitled to advancement because plaintiff was not a party to the SEC action "by reason of the fact" that he was an officer of HDI, noting that the SEC complaint undeniably focused on plaintiff's position as chairman. The court also denied defendant's motion to dismiss or stay, finding that the summary nature of the proceedings and the balancing of the equities did not warrant a stay under *McWane*.<sup>124</sup> Finally, the court found that plaintiff was entitled to fees on fees – the fees incurred in bringing the instant action for advancement.

### Injunctions

#### *Permanent Injunctions*

In *North River Insurance Co. v. Mine Safety Appliances Co.*,<sup>125</sup> the Delaware Supreme Court affirmed the Court of Chancery's decision denying the appellant's request for an order enjoining the appellee from assigning to plaintiffs in an action pending in West Virginia the right to recover under the appellant's insurance policy. The Supreme Court held that because plaintiffs in the West Virginia action had the right, independent of any assignment, to bring a declaratory action against the appellant, the Court of Chancery "could not, via an injunction, completely remedy the harm sought to be avoided – namely, the risk of inconsistent judgments in the Delaware and West Virginia [a]ctions." The Supreme Court noted that the power to enjoin litigation in a foreign jurisdiction is discretionary and should be exercised cautiously.

#### *Preliminary Injunctions*

In *Mitchell Lane Publishers, Inc. v. Rasemas, et al.*,<sup>126</sup> Vice Chancellor Noble, in a memorandum opinion, denied plaintiff's motion for a preliminary injunction, finding that plaintiff failed to show a threat of irreparable injury as the potential injury identified was speculative and the

balance of the equities favored the defendants. Plaintiff Mitchell Lane Publishers, Inc. ("Mitchell Lane"), a publisher of children's books, brought the instant action against, among others, former employee Joseph Rasemas who started a competing publishing company, Purple Toad Publishing, Inc. Mitchell Lane claimed that Rasemas had used confidential and proprietary information gained during his employment at the company in breach of his fiduciary duties and sought interim injunctive relief, arguing that it would be irreparably harmed if Purple Toad continued to operate its business with Mitchell Lane's confidential information. While the court found that Mitchell Lane had a reasonable probability of success on its claim that Rasemas breached his fiduciary duty to safeguard confidential information, the court found that the confidential information at issue was stale and that its use posed no threat of irreparable injury. Moreover, the court found that defendants would suffer irreparable injury if an injunction was issued as this would likely end their business, and so the balance of the equities tilted in favor of the defendants.

In *Platinum Partners Value Arbitrage Fund L.P. v. Echo Therapeutics, Inc., et al.*,<sup>127</sup> Vice Chancellor Noble, in a letter opinion, denied a stockholder plaintiff's motion for a declaratory judgment and preliminary injunction. According to plaintiff, three of the defendant's five directors had improperly excluded the remaining two directors from participating in board-related activities. Plaintiff further alleged that these three directors ran the corporation for their own benefit. Because the corporation was, according to plaintiff, in "dire financial straits," plaintiff requested an order requiring that the corporation hold a stockholder meeting to vote on whether to remove the directors who had engaged in the alleged misconduct. Alternatively, plaintiff moved for expedited proceedings. The court noted that plaintiff did not "allege that it would be likely that a new board could obtain a reversal of fortune or suggest how a new board would be able to stem the downward decline." So the court rejected plaintiff's motions, finding that it had failed to identify any immediate and non-speculative harm.

In *In re TIBCO Software Inc. Stockholders Litigation*,<sup>128</sup> Chancellor Bouchard, in a memorandum opinion, refused to grant a preliminary injunction halting a stockholder vote on a proposed merger in the face of a basic math error inflating TIBCO's equity value by \$100 million where the target corporation board publically disclosed the mistake,

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<sup>124</sup> *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Engineering Co.*, 263 A.2d 281 (Del. 1970).

<sup>125</sup> No. 8, 2014, 2014 WL 5784588 (Del. Nov. 6, 2014).

<sup>126</sup> C.A. No. 9144-VCN, 2014 WL 4925150 (Del. Ch. Sept. 30, 2014).

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<sup>127</sup> C.A. No. 10303-VCN, 2014 WL 6606474 (Del. Ch. Nov. 14, 2014).

<sup>128</sup> C.A. No. 10319-CB, 2014 WL 6674444 (Del. Ch. Nov. 25, 2014).

but did not seek to renegotiate the per-share price with the acquirer. Plaintiff, a TIBCO stockholder, proffered two claims to support the PI motion: (i) contract reformation of the merger agreement to reflect the higher equity value; and (ii) breach of fiduciary duty against the target board for failing to make efforts to preserve the additional amount. The court found that there was no reasonable likelihood of success on the merits on the first claim because the parties to the merger, though both mistakenly believing that the equity value of the transaction was \$100 million greater than it in fact was, only included the specific per-share price (and not the aggregate equity value) in their merger agreement – which per-share price reflected the accurate aggregate amount. As to the second claim, the court found no irreparable harm because the claim concerned a definable sum of money (*i.e.*, \$100 million), and “a harm that can be remedied by money damages is not irreparable.” In light of the readily quantifiable nature of the alleged harm and plaintiff’s concession that he had no issue with the quality of the process resulting in the proposed merger, the court also found that the balance of equities weighed against enjoining the upcoming stockholder vote and that a delay would only harm TIBCO’s stockholders of timely receiving their \$24.00 per share if they decided to approve the merger.

### *Preliminary Injunctions; Revlon Duties*

In *C&J Energy Services, Inc., et al. v. City of Miami General Employees’ & Sanitation Employees’ Retirement Trust, et al.*,<sup>129</sup> Chief Justice Strine, writing for the Delaware Supreme Court *en banc*, provides directors and M&A practitioners with nuanced guidance on satisfying *Revlon* duties in the context of a sale of corporate control. The Court reversed the Court of Chancery’s bench ruling preliminarily enjoining a merger between C&J Energy Services, Inc. (“C&J”) and a division of Nabors Industries Ltd. (“Nabors”). The Court of Chancery, in issuing the injunction, had concluded that plaintiff stockholders demonstrated a reasonable likelihood of success on their claim that C&J’s board breached its fiduciary duties by failing to shop the company before or after execution of the merger agreement – even though the merger agreement contained a no-shop provision. The Supreme Court disagreed, unanimously holding that the Court of Chancery misapplied the *Revlon* doctrine by requiring the company to “shop itself to fulfill its duty to seek the highest immediate value.” According to the Supreme Court, “*Revlon* and its progeny do not set out a specific route that a board must follow when fulfilling its fiduciary

duties, and an independent board is entitled to use its business judgment to decide to enter into a . . . transaction that promises great benefit, even when it creates certain risks.” The Supreme Court rejected the notion that *Revlon* requires an “auction whenever [a] board approves a change of control transaction,” reasoning that such a transaction is “subject to an effective market check” as long as interested bidders have a fair opportunity to present a higher-value alternative and the board has the “flexibility to eschew the original transaction and accept the higher-value deal.”

In *In re Family Dollar Stores, Inc. Stockholder Litigation*,<sup>130</sup> Chancellor Bouchard, in a memorandum opinion, denied stockholder plaintiffs’ motion to enjoin the stockholder vote on a merger agreement pursuant to which Dollar Tree, Inc. would acquire Family Dollar Stores, Inc. for a combination of cash and Dollar Tree stock. Plaintiffs alleged that Family Dollar’s board breached its fiduciary duties by failing to engage in discussions with a new bidder, Dollar General, Inc., that had offered more cash per share than did Dollar Tree but whose proposal presented certain antitrust risks. The court, in rejecting plaintiffs’ motion, found that Family Dollar’s board was “motivated to maximize [the company’s] value and acted reasonably within the constraints of the fiduciary out provision in the merger agreement when it decided not to engage in negotiations with [Dollar General].” The court noted, for instance, that Family Dollar had been advised by its counsel that Dollar General’s offer had only a “40% chance of obtaining antitrust approval.” Relying on the Delaware Supreme Court’s recent decision in *C&J*,<sup>131</sup> the court thus determined that, in satisfaction of its *Revlon* duties, Family Dollar’s board “pursu[ed] the transaction it reasonably view[ed] as most valuable to stockholders.” Because interested bidders had a “full and fair opportunity to present a higher-value alternative” and the board had “the flexibility to eschew the original transaction,” the court held that plaintiffs failed to demonstrate a reasonable probability of success on the merits of their *Revlon* claims.

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<sup>130</sup> Consol. C.A. No. 9985-CB (Del. Ch. Dec. 19, 2014). On January 2, 2015, the court denied plaintiffs’ application for an interlocutory appeal of the decision, finding that plaintiffs did not satisfy the requirements of Supreme Court Rule 42(b) because the challenged opinion (i) did not decide an original question of law; (ii) did not conflict with the court’s decision in another case; and (iii) did not reverse or set aside a prior decision of the court. C.A. No. 9985-CB (Del. Ch. Jan. 2, 2015).

<sup>131</sup> *C&J Energy Servs., Inc. v. City of Miami Gen. Emps.’ & Sanitation Emps.’ Ret. Trust*, C.A. No. 9456-VCN, 2014 WL 7243153.

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<sup>129</sup> No. 655/657, 2014, 2014 WL 7243153 (Del. Dec. 19, 2014).

### *Temporary Restraining Order; Mandatory Injunction; Advance Notice Bylaws*

In *AB Value Partners, LP v. Kreisher Manufacturing Corporation, et al.*,<sup>132</sup> Vice Chancellor Parsons, in a memorandum opinion upholding advance-notice bylaws, denied a motion for a temporary restraining order that would have enjoined Kreisher Manufacturing's advance notice bylaw so that AB Value Partners, an activist hedge fund, could run a competing slate of directors at Kreisher's annual stockholder meeting. The court first found that the requested relief was more in the nature of a mandatory preliminary injunction because, if granted, it would provide AB Value Partners with all the remedy it sought; in contrast, the purpose of a typical status quo TRO is only to prevent imminent, irreparable harm pending a preliminary injunction or a final resolution on the merits. Moreover, while the emergency nature of a motion for a TRO typically results in a decision relying on little to no evidence, the court heard oral argument and was provided with a more complete factual record on which to base its decision. Thus, the court reasoned, AB Value Partners was obligated to satisfy at least the primary requirement for a preliminary injunction (*i.e.*, a reasonable probability of success on the merits) and not just the more lenient standard for a status quo TRO (*i.e.*, the existence of a colorable claim) – although the court concluded that AB Value Partners failed to satisfy even that lesser standard, as well. On the merits, the court found that advance-notice bylaws were commonly employed and would only be enjoined where inequitable circumstances were shown. The court held that AB Value Partners' showing on the merits was insufficient. The hedge fund did not proffer any compelling facts demonstrating that Kreisher's advance-notice bylaw was inequitable or that circumstances at the company had materially changed after the advance-notice deadline sufficient to forgive a late attempt to run a full, opposing slate of directors in elections held during the annual stockholder meeting. The court's decision stands as a good practitioner reference for its detailed review of prior Delaware decisions where advance-notice bylaws were both upheld and stricken.

### **Interim Custodian**

In *In re TransPerfect Global, Inc.*,<sup>133</sup> Chancellor Bouchard, in a letter opinion, denied plaintiff's motion for the appointment of a temporary custodian with authority to resolve deadlocks relating to the business and affairs of TransPerfect Global, Inc. ("TransPerfect") pending the

disposition of expedited proceedings for the appointment of a custodian under 8 *Del. C.* § 226(a)(2), finding that a temporary custodian was not urgently needed to protect TransPerfect in the short amount of time before trial. The court noted that plaintiff must demonstrate that a temporary custodian is "urgently needed for the immediate protection of the corporation."<sup>134</sup> The court determined that while plaintiff had identified a number of areas of fundamental disagreement that may well support a finding of deadlock and the appointment of a custodian after trial, plaintiff had not established that the appointment of a temporary custodian was urgently needed for the protection of TransPerfect between that time and trial. The disagreements did not pose an immediate threat because certain of the contested issues had been the subject of disagreement for months and the parties had made concessions that other issues would not pose a threat before trial, which was scheduled to be held in February 2015.

### **Jurisdiction**

#### *Forum Selection*

In *Scanbuy, Inc. v. NeoMedia Technologies, Inc.*,<sup>135</sup> Vice Chancellor Noble, in a letter opinion, granted defendant's motion to dismiss for improper venue plaintiff's declaratory-relief action arising out of a licensing agreement between the parties. The agreement contained a forum-selection clause providing that any dispute must "be brought in a Federal or state court seated in Atlanta, Georgia." Plaintiff argued that the forum-selection provision did not apply because the entire agreement had been terminated when defendant terminated plaintiff's license. The court rejected that argument and noted that, under Delaware law, interpretation of a termination provision in an agreement containing a forum-selection clause was an issue for the court identified in that clause. The court thus held that it could not decide whether the termination provision applied without "usurping the role of the Georgia courts."

#### *Personal Jurisdiction*

In *Reid v. Siniscalchi, et al.*,<sup>136</sup> Vice Chancellor Noble, in a memorandum opinion, denied defendant satellite-financing entities' motion to dismiss for lack of personal jurisdiction. According to the court, the complaint adequately alleged that defendants, based in Italy, were subject to Delaware's long-arm statute because at least one of them formed a Delaware parent company to which they transferred

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<sup>132</sup> C.A. No. 10434-VCP, 2014 WL 7150465 (Del. Ch. Dec. 16, 2014).

<sup>133</sup> C.A. No. 9700-CB, 2014 WL 6810761 (Del. Ch. Dec. 3, 2014).

<sup>134</sup> *Moore v. C.H.M. Enters., Inc.*, C.A. No. 7294 (1983), 1983 WL 102620, at \*2 (Del. Ch. Nov. 9, 1983).

<sup>135</sup> C.A. No. 9456-VCN, 2014 WL 5500245 (Del. Ch. Oct. 31, 2014).

<sup>136</sup> C.A. No. 2874-VCN, 2014 WL 6589342 (Del. Ch. Nov. 20, 2014).

membership interests as part of a conspiracy to breach a joint-venture agreement. Even if some of the defendants did not directly participate in the company's formation, they were nonetheless subject to the statute because they were agents of and coconspirators with the defendants who had sufficient minimum contacts in the state under the "conspiracy theory of personal jurisdiction." The court also rejected defendants' argument that plaintiff stockholder lacked standing to bring his derivative claims, reasoning his allegation that the "subsidiary and its controller parent wrongfully refuse[d] to enforce the subsidiary's claim directly" was sufficient to confer standing.

In *2009 Caiola Family Trust, et al. v. PWA, LLC, et al.*,<sup>137</sup> Vice Chancellor Parsons, in a memorandum opinion, denied individual defendant Ward Katz's motion to dismiss for lack of personal jurisdiction. The court concluded that it had personal jurisdiction over Katz, a Kansas resident, because he transacted business in Delaware by virtue of his control over Dunes Point West, a Delaware limited liability company central to the parties' dispute. The court also denied defendants' motion to dismiss on *forum non conveniens* grounds, reasoning that they had actively litigated this matter for three years before the Court of Chancery, thereby demonstrating that the Court of Chancery was a suitable venue. The court denied in significant part defendants' motion to dismiss under Rule 12(b)(6), finding that plaintiffs had sufficiently alleged breach-of-contract and breach-of-fiduciary-duty claims against defendants relating to Dunes Point West. The court did, however, grant defendants' motion to dismiss as to plaintiffs' waste claim, reasoning that plaintiffs' allegations that defendants failed to charge sufficient rent in connection with an apartment complex operated by Dunes Point West failed to meet the "onerous" pleading standard applicable to waste claims. Finally, the court denied plaintiffs' motion for partial summary judgment on their claims that defendants improperly commingled security deposits and that Katz abdicated his duties as managing member of a limited liability company that managed Dunes Point West's interests, finding that there existed disputed issues of material fact with respect to these claims.

### Subject Matter Jurisdiction

In *Vaccaro v. APS Healthcare Bethesda, Inc., et al.*,<sup>138</sup> Vice Chancellor Glasscock, in a letter opinion applying New York law, denied defendants' motion to dismiss for lack of subject matter jurisdiction. Defendants argued that plaintiff's claim seeking contract reformation, the sole basis

for the Court of Chancery's jurisdiction, failed as a matter of law. But the court found that reasonable ambiguity existed in the implicated contractual language, leaving the claim and jurisdiction intact.

### Justiciability

#### Ripeness

In *In re Allergan, Inc. Stockholder Litigation*,<sup>139</sup> Chancellor Bouchard, in a memorandum opinion, denied plaintiffs' motion for summary judgment seeking a declaration that a provision in the bylaws of Allergan, Inc. ("Allergan") did not prohibit the stockholders from removing the entire board and simultaneously electing a new slate of directors at a special meeting. The court concluded that the request was not ripe as plaintiffs, Allergan stockholders, had not yet pursued the tactic. They had been monitoring a proxy fight through which PS Fund 1, LLC ("PS Fund") sought to remove six of the nine members of the Allergan board at a special meeting. However, plaintiff stockholders advocated a different proxy strategy – one to remove and replace the entire board at the special meeting. That strategy implicated a provision in Allergan's bylaws, which the board had interpreted to permit stockholders to remove directors by written consent but not to elect their successors within one year of the request. But based on plaintiffs' failure to implement that strategy, the court determined that plaintiffs sought an improper advisory opinion. The court also found that the board's contrary interpretation of the provision was not a significant deterrent to the ability of the company's stockholders to exercise their franchise rights, as evidenced by PS Fund's current proxy fight for control of the board. So the dispute was not ripe for review.

### Practice and Procedure

#### Appeals

In *Pontone v. Milso Industries Corp., et al.*,<sup>140</sup> Vice Chancellor Parsons, in a letter opinion, granted plaintiff's and defendant's respective motions for certification of an interlocutory appeal challenging the court's ruling that fees and expenses for counterclaims are only advanceable if the counterclaims are compulsory. The court had, on this basis, ruled that two of plaintiff's counterclaims were not advanceable, while certain other counterclaims were. In granting the motions for certification, the court found that the first two requirements of Supreme Court Rule 42, which governs interlocutory appeals, were satisfied

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<sup>137</sup> C.A. No. 8028-VCP (Del. Ch. Dec. 18, 2014).

<sup>138</sup> C.A. No. 9637-VCG, 2014 WL 5206767 (Del. Ch. Oct. 15, 2014).

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<sup>139</sup> C.A. No. 9609-CB, 2014 WL 5791350 (Del. Ch. Nov. 7, 2014).

<sup>140</sup> C.A. No. 7615-VCP, 2014 WL 4967228 (Del. Ch. Oct. 6, 2014).



because the ruling at issue “determine[d] a substantial issue” and “establish[ed] a legal right.” The court further held that both sides cleared Rule 42’s final hurdle by identifying conflicting trial court precedent on whether a counterclaim must be compulsory to be advanceable. The court concluded that certifying the ruling at issue for interlocutory appeal would serve the interests of justice.

### Motions to Amend

In *Zutrau v. Jansing, et al.*,<sup>141</sup> Vice Chancellor Parsons, in a letter opinion, denied plaintiff’s motion to alter or amend the court’s earlier post-trial judgment, finding that plaintiff failed to show any manifest injustice or misapprehension of facts or law and failed to present any basis for the relief sought. The court had previously found that defendant, the president, sole director and majority stockholder of a private Delaware corporation, breached his fiduciary duties in connection with various self-serving business decisions and a reverse stock split through which he cashed out plaintiff’s shares in the company at an unfair price and ordered damages as the remedy. Plaintiff, unhappy with the court’s award of damages rather than rescission of the reverse stock split, terminated her counsel and filed a *pro se* motion contesting nearly every aspect of the judgment. The court reviewed the potentially applicable standards under which the motion might be decided – under Rule 59(e) to alter or amend judgment, Rule 59(a) to obtain a new trial, Rule 59(f) for reargument and Rule 15(b) to amend the pleadings – but found that plaintiff’s contentions were meritless regardless of the standard applied. Plaintiff’s motion largely disputed the court’s findings of facts and weighing of the evidence and failed to show any manifest injustice or misapprehension of the facts or law to entitle her to a new trial or reargument.

### Motions to Clarify

In *Indiana Electrical Workers Pension Trust Fund IBEW v. Wal-Mart Stores*,<sup>142</sup> Chancellor Bouchard, in a bench ruling, granted in part and denied in part Wal-Mart’s motion for clarification of the court’s October 13, 2013 Final Order and Judgment requiring Wal-Mart to produce certain categories of documents relating to an alleged cover-up of misconduct at the company’s Mexican subsidiary. Wal-Mart first appealed that decision to the Delaware Supreme Court, where it was affirmed on July 23, 2014. Afterward, Wal-Mart filed the instant motion seeking clarification of the original Final Order, claiming that the Supreme Court had given it leave to file the otherwise untimely motion.

The court rejected that claim, but exercised discretion to consider the merits under the court’s inherent authority to manage its docket largely because the underlying dispute would resurface when Wal-Mart produced the documents in line with its contested understanding of the Final Order. On the merits, the Court (i) agreed with Wal-Mart that a requirement of the Final Order directed at documents relating to the initial cover-up did not require production of materials from an internal investigation beginning in 2011, but (ii) rejected Wal-Mart’s request for exemption from preparing a privilege log for documents after 2011, as the court concluded that materials from this period could be responsive through other production categories in the Final Order.

### Motions to Dismiss

In *Matthew v. Laudamiel, et al.*,<sup>143</sup> Vice Chancellor Noble, in a letter opinion, granted plaintiff’s motion for summary judgment on an individual defendant’s counterclaim that plaintiff materially breached a limited liability company agreement (the “Agreement”). The court opined that while the issue of whether a breach is material is generally a question of fact that cannot be resolved under the summary judgment standard, that does not apply if the alleged breach was, as a matter of law, immaterial. According to the court, plaintiff’s alleged breaches of the Agreement had “no material effect” on the company. The court also noted that defendant failed to explain “why the board could not have overridden or circumvented” plaintiff’s alleged misconduct.

In *Baker, et al. v. Sadiq, et al.*,<sup>144</sup> Vice Chancellor Laster, in a bench ruling denying defendants’ motion to dismiss, applied a Rule 56 summary judgment standard (instead of the normal Rule 12(b)(6) standard) in ruling on the motion because defendants included a significant number of documents outside the pleadings as part of their briefing. The court noted that in limited circumstances, it may consider documents incorporated by reference implicitly or explicitly in a complaint while ruling on a motion to dismiss but those documents must be integral to the complaint – a standard that defendants’ documents failed to meet. In ruling on defendants’ earlier application regarding the documents, the court had warned defendants that it would consider converting the motion into a Rule 56 motion, but defendants still took the risk in introducing the documents. The court acknowledged that the motion would have

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<sup>141</sup> C.A. No. 7457-VCP, 2014 WL 6901461 (Del. Ch. Dec. 8, 2014).

<sup>142</sup> C.A. No. 7779-CB (Del. Ch. Oct. 15, 2014).

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<sup>143</sup> C.A. No. 5957-VCN, 2014 WL 5499989 (Del. Ch. Oct. 30, 2014).

<sup>144</sup> C.A. No. 9464-VCL (Del. Ch. Oct. 14, 2014).

been a “close case” under Rule 12(b)(6), but under Rule 56, plaintiffs had not been given a sufficient opportunity for discovery and the court denied the motion.

### *Motions to Expedite*

In *Smollar v. Potarazu, et al.*,<sup>145</sup> Vice Chancellor Noble, in a letter opinion, denied a stockholder plaintiff’s request to expedite proceedings to enjoin a buyout of VitalSpring Technologies, Inc. The court held that the harm posed by the buyout was too speculative and remote to support expedition. Plaintiff provided no details of the transaction he sought to enjoin and even appeared skeptical that the deal was or will ever be negotiated. Moreover, the buyout had not been publicly announced and there had been no indication of when it might close. The motion to expedite also had a procedural defect – although plaintiff requested a preliminary injunction, he failed to formally move for that remedy. Further, the court denied plaintiff’s request for a temporary receiver to ensure that the company’s annual meeting would take place because defendant provided evidence that the company will hold the meeting at a specified date.

### *Parallel Proceedings*

In *Willis, et al. v. PCA Pain Center of Virginia, Inc., et al.*,<sup>146</sup> Vice Chancellor Noble, in a letter opinion, held that while the court had subject matter jurisdiction to hear the case, it was proper to issue a stay until a parallel, ongoing case involving the same parties and same subject matter in Virginia had been decided. Plaintiffs brought suit seeking redress from defendants’ alleged failure to transfer their business to plaintiffs. The court found that it had subject matter jurisdiction because plaintiffs sought specific performance of a sale of unique assets, including an exclusive franchise right. The court then applied the *McWane*<sup>147</sup> factors and concluded that staying the case was appropriate because: (i) the Virginia case was filed before the Delaware case; (ii) the parties were substantially the same; and (iii) the core issues in the case did not involve Delaware corporate law or issues of internal corporate governance, and thus the Virginia court was capable of rendering prompt and complete justice.

### *Status Quo Orders*

In *2009 Caiola Family Trust v. PWA, LLC, et al.*,<sup>148</sup> Vice Chancellor Parsons, in a letter opinion, denied defendants’ motion to modify the court’s status quo order, which was

issued to preserve PWA, LLC’s (“PWA”) status as managing member of Dunes Point luxury condominiums in Kansas. The status quo order also prohibited PWA from taking certain actions absent unanimous written consent by the members of Dunes Point. PWA sought to extend the order to cover plaintiffs and certain Dunes Point owners, as plaintiffs had filed two notices of capital contributions in an attempt to remove PWA as managing member. The court found that plaintiffs’ actions already fell under the status quo order, which governed PWA’s status, and denied the motion to modify.

### *Statute of Limitations*

In *Knutkowski, et al. v. Cross*,<sup>149</sup> Vice Chancellor Glasscock, in a letter opinion, granted in part defendant’s motion for partial summary judgment regarding the effect of a promissory note. The court concluded that the statute of limitations barred recovery on certain installments under the note. According to the court, when a note calls for repayment of a loan in installments on discrete dates without an acceleration provision, only the portion of the note that falls within the applicable six-year statute of limitations under 6 Del. C. § 3-118(a) may be recovered. The court distinguished the promissory note at issue with agreements “on which the accrual date of a breach could not be readily determined or where damages were not ascertainable as of some intermediate date,” which muddy the severability issue and could require trial regarding the parties’ intent.

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<sup>145</sup> C.A. No. 10287-VCN, 2014 WL 6607074 (Del. Ch. Nov. 19, 2014).

<sup>146</sup> C.A. No. 9006-VCN, 2014 WL 5396164 (Del. Ch. Oct. 20, 2014).

<sup>147</sup> *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng’g Co.*, 263 A.2d 281 (Del. 1970).

<sup>148</sup> C.A. No. 8028-VCP (Del. Ch. Dec. 18, 2014).

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<sup>149</sup> C.A. No. 4889-VCG, 2014 WL 5106095 (Del. Ch. Oct. 13, 2014).

## Delaware Quarterly

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