1. The agency theory and alter ego theories of personal jurisdiction

   a. Standards

   The agency and alter ego theories of indirect personal jurisdiction are similar in effect but different in scope. The theories have at least three factors in common. The first common factor is the attribution of the agent's or subsidiary's jurisdictional activities to its principal or parent. "The principles of agency allow a court to establish jurisdiction over the parent based upon its jurisdiction over a subsidiary." This theory "involves a straightforward examination of whether the out-of-state defendant conducted business satisfying § 3104 through an agent." Similarly, although not identically, "[u]nder the alter ego theory of personal jurisdiction, 'the contacts of an entity with a particular forum can be attributed to another person or entity if the entity having the forum contacts is the mere alter ego

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83 The Delaware Supreme Court explained the different scope of the agency theory of personal jurisdiction and the alter ego theory:

These two methods for establishing jurisdiction involve showing either that the absent parent instigated the subsidiary's local activities or that the absent parent and the subsidiary are in fact a single legal entity. . . . They are obviously similar in that both involve disregarding separate entity status and shifting responsibility for the subsidiary's actions onto the parent. The difference between [the agency] and [alter ego theories] lies in the extent of this shifting of responsibility. Under the [agency] theory, only the precise conduct shown to be instigated by the parent is attributed to the parent; the rest of the subsidiary's actions still pertain only to the subsidiary. The two corporations remain distinct entities. If [alter ego] is shown, however, all of the activities of the subsidiary are by definition activities of the parent. [The alter ego theory] requires a greater showing of interconnectedness than attribution, but once shown, its scope is broader. Under both theories, the parent is declared responsible for in-state activities of the subsidiary, but [under the agency theory] the responsibility results from causing a separate legal entity to act while [under the alter ego theory] there is no separate legal entity at all.

Sternberg v. O'Neil, 550 A.2d at 1125-26 n.45 (quoting Lea Brilmayer & Kathleen Paisley, Personal Jurisdiction and Substantive Legal Relations: Corporations, Conspiracies and Agency, 74 CAL. L. REV. 1, 12 (1986)).

84 Telcordia Techs., Inc. v. Alcatel S.A., 2005 WL 1268061, at *2 (D. Del. May 27, 2005); see also WOLFE & PITTENGER § 3.05[c][2], at 3-93 to 3-94 ("[T]he doctrine may provide a basis for attributing the jurisdictional contacts of a subsidiary corporation (the agent) to a nonresident parent corporation (the principal)"); Outokumpu Eng'g Enters. v. Kvaerner Enviropower, 685 A.2d 724, 729 (Del. Super. 1996).

The Delaware long-arm statute itself explicitly recognizes that the forum contacts of an agent may provide a basis for jurisdiction over the principal. The statute states that it provides jurisdiction "over any nonresident, or his personal representative, who in person or through an agent," commits one of the enumerated acts that might support such jurisdiction. 10 Del. C. § 3104(c) (emphasis added).

of such other person or entity."86 Unlike the agency theory, courts will ignore the corporate boundaries between parent and subsidiary on an alter ego theory only if fraud or inequity is shown.87

The second common factor is that a successful showing of alter ego or agency does not necessarily mean that the principal or parent is subject to jurisdiction. As theories of indirect jurisdiction, the underlying question on both theories is whether the subsidiary's actions satisfy § 3104 of the long-arm statute.88 The third common factor is that both theories require a fact intensive inquiry.89

For the agency theory, the factual inquiry includes whether: "(1) the agent ha[s] the power to act on behalf of the principal with respect to third parties; (2) the agent do[es] something at the behest of the principal and for his benefit; and (3) the principal ha[s] the right to control the conduct of the agent."90 Thus, in the parent-subsidiary context, the critical question is "whether the parent corporation dominates the activities of the subsidiary."91

87Applied Biosys., Inc. v. Cruachem Ltd., 772 F. Supp. 1458, 1465-66 (D. Del. 1991) ("The agency theory, by contrast, examines the degree of control which the parent exercises over the subsidiary.").
88For an analysis of the relationship between the agency theory and § 3104, see Ace & Co. v. Balfour Beatty PLC, 148 F. Supp. 2d 418, 425 (D. Del. 2001) ("The agency theory requires not only that the precise conduct shown to be instigated by the parent be attributable to the parent . . . but also that such conduct satisfy § 3104(c)(1); i.e., that the jurisdictional conduct take place in Delaware."); HMG/Courtland Props., Inc. v. Gray, 729 A.2d 300, 307 (Del. Ch. 1999) ("In circumstances where [the agency] test is satisfied as to a corporate parent and its subsidiary, the court does not ignore the separate existence of the companies, but only 'will consider the parent corporation responsible for the specific jurisdictional acts of the subsidiary.'") (citing Applied Biosys., 772 F. Supp. at 1463).
89For an analysis of the alter ego theory and § 3104, see Gray, 729 A.2d at 307-08 (extensive citations omitted); see also Medi-Tec of Egypt Corp. v. Bausch & Lomb Surgical, 2004 WL 415251, at *3 (Del. Ch. Mar. 4, 2004). The court in Gray noted the following relationship between asserting jurisdiction under the alter ego theory and the requirements of § 3104: [T]he use of an alter ego test in these circumstances is also consistent with the express language of § 3104 because it is a way of examining whether an out-of-state resident has deployed "an agent" to conduct forum-directed activity. If the entity which has engaged in the direct activity in Delaware satisfying § 3104 is no more than the alter ego of an out-of-state defendant, it is fair to conclude that the alter ego acted as the out-of-state defendant's agent in conducting those activities, thus meeting the statutory criteria permitting service.
729 A.2d at 308
"Among the specific factors relevant to this determination are the extent of overlap of officers and directors, methods of financing, the division of responsibility for day-to-day management, and the process by which each corporation obtains its business. No one factor is either necessary or determinative; rather it is the specific combination of elements which is significant."92 Thus, a subsidiary is not an agent of its parent merely because the parent: holds a majority of the subsidiary's shares, shares officers and directors with the subsidiary, or finances the operations of the subsidiary.93 "Under the agency theory of personal jurisdiction, only acts of the agent that are directed by the principal may serve as a basis to assert jurisdiction over the principal."94

For the alter ego theory, Delaware courts have "looked to the law of the entity in determining whether the entity's separate existence is to be disregarded."95 While VG 109 is a Dutch limited liability company, neither side has discussed the relevant provisions of Dutch law, other than as they relate to the minimum capitalization requirements. Thus, the record does not reflect whether Dutch business law includes a concept similar to the alter ego theory. To the extent Dutch law may not recognize such a theory, NIBC has waived that defense. Nevertheless, in the limited instances where the parties have cited Dutch law, I have considered it; otherwise, I have applied Delaware law to the facts of this case.

In applying the alter ego theory of personal jurisdiction, Delaware courts typically focus on two critical elements:

1) that the out-of-state defendant over whom jurisdiction is sought has no real separate identity from a defendant over

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91Ashland Oil, 456 F. Supp. at 841. "[T]he control must be actual, participatory, and total." Id. (citing Krivo Indus. Supply Co. v. Nat'l Distilling & Chem. Corp., 483 F.2d 1098, 1105 (5th Cir. 1973)).
93"See Ashland Oil, 456 F. Supp. at 841 (extensive citations omitted).
whom jurisdiction is clear based on actual domicile or satisfaction of Delaware's long-arm statute; and 2) the existence of acts in Delaware which can be fairly imputed to the out-of-state defendant and which satisfy the long-arm statute and/or federal due process requirements.\textsuperscript{96}

In that regard, Delaware courts apply "the alter ego theory rather strictly, using an analysis similar to those used in determining whether to pierce the corporate veil."\textsuperscript{97} Courts generally only disregard the corporate entity in the interest of justice, when such matters as fraud, contravention of law or contract, public wrong, or equitable considerations among members of the corporation are involved.\textsuperscript{98}

Some specific facts a court may consider when being asked to disregard the corporate form include: "(1) whether the company was adequately capitalized for the undertaking; (2) whether the company was solvent; (3) whether corporate formalities were observed; (4) whether the dominant shareholder siphoned company funds; and (5) whether, in general, the company simply functioned as a facade for the dominant shareholder."\textsuperscript{99} A decision to disregard the corporate entity generally results not from a single factor, but rather some combination of them, and "an overall element of injustice or unfairness must always be present, as well."\textsuperscript{100}

b. Analysis

As for the agency theory, EBG contends VG 109 is an agent of NIBC because they share normal operating activities, management, and an office, and because, as VG 109's managing member, NIBC controlled its business

\textsuperscript{96}Gray, 729 A.2d at 307-08 (extensive citations omitted); see also Medi-Tec of Egypt Corp. v. Bausch & Lomb Surgical, 2004 WL 415251, at *3 (Del. Ch. Mar. 4, 2004).

\textsuperscript{97}Gray, 729 A.2d at 307; see also Ruggiero v. FuturaGene, plc, 948 A.2d 1124, 1135 (Del. Ch. 2008); Sears I, 744 F. Supp. 1297, 1305 (D. Del. 1990) ("It is only the exceptional case where a court will disregard the corporate form . . . .").

\textsuperscript{98}Pauley Petroleum, Inc. v. Cont'l Oil Co., 239 A.2d 629, 633 (Del. 1968).

\textsuperscript{99}Id. (citation omitted).

activities and funding. NIBC has not denied that VG 109 was its agent. Thus, drawing all inferences in favor of EBG, I find, for purposes of determining NIBC's amenability to suit in Delaware, that VG 109 did act as NIBC's agent.

Turning to the alter ego theory, EBG makes several arguments in favor of ignoring the corporate form and treating VG 109 as NIBC's alter ego. Determining whether NIBC would be subject to personal jurisdiction under the alter ego theory involves two separate questions: (1) does VG 109 have a separate identity from NIBC, or is it merely its alter ego, and (2) whether there are Delaware acts of VG 109 that satisfy § 3104(c)(1) which could be imputed on alter ego grounds to NIBC. For the reasons discussed infra, I answer the second question in the negative; consequently, I need not decide the first question. Nonetheless, I note that, even drawing all inferences in EBG's favor, I doubt that EBG has met its burden of demonstrating that VG 109 is NIBC's alter ego for purposes of defeating NIBC's motion to dismiss.

EBG makes the following arguments in favor of ignoring the corporate form: (1) "NIBC knowingly used VG109 as an instrument and means to attempt to shield itself from liability for tax obligations"; (2) "VG109 had insufficient capital to meet its tax obligations"; (3) VG 109 is NIBC's wholly owned subsidiary; (4) NIBC shares its principal Netherlands office with VG 109; (5) NIBC and VG 109 share management; (6) NIBC is VG 109's managing director; and (7) VG 109 allegedly transferred its interest in EBG for no consideration.

With respect to NIBC's use of VG 109, EBG, however, has not made a sufficient showing of fraud or other inequity to justify a departure from the usual rule recognizing the corporate form. Even drawing all inferences in favor of EBG, it has not shown that NIBC's use of the corporate form for its VG 109 subsidiary constituted "a sham and exist[s] for no other purpose than as a vehicle for fraud." To the contrary, NIBC has presented uncontroverted evidence that VG 109 pre-dated the formation of EBG and serves as a broader investment vehicle, which has held other assets besides

101 See PAB at 21.
102 See DRB at 16-17; Tr. at 11-12.
103 PAB at 18-19. Because EBG has cited nothing in any affidavit or pleading to support its seventh factual allegation, regarding the absence of consideration for VG 109's transfer of its interest in EBG, I have disregarded that allegation as merely conclusory and unsupported by any specific facts. In that regard, EBG has failed to meet its burden of pleading the fraud element of alter ego jurisdiction with particularity. See Ct. Ch. R. 9(b) (requiring that circumstances constituting fraud be pled with particularity).
104 Wallace, 752 A.2d at 1184.
the membership interests in EBG. In fact, VG 109 was formed as a special purpose entity in July 2001, several years before the creation of EBG.\textsuperscript{105} In addition, VG 109 has observed a number of corporate formalities. It has, for example, filed separate U.S. tax returns and maintains separate books and records.\textsuperscript{106} Moreover, although VG 109 and NIBC's alleged breach of contract may be unjust or wrongful, the requisite element of fraud under the alter ego theory must come from an inequitable use of the corporate form itself as a sham, and not from the underlying claim.\textsuperscript{107}

EBG's contention that NIBC's use of the corporate form to obtain limited liability itself supports asserting alter ego jurisdiction is also unconvincing. EBG relies on one paragraph in its complaint, "NIBC knowingly used VG109 as an instrument and means to attempt to shield itself from liability for tax obligations related to its ownership interest in EBG."\textsuperscript{108} As previously discussed as to NIBC's direct amenability to jurisdiction, I find that statement wholly conclusory and otherwise unsupported by any specific facts in the Complaint. Without more, EBG has failed to plead facts sufficient to support a reasonable inference that NIBC's use of VG 109's limited liability status was fraudulent or inequitable.\textsuperscript{109}

EBG also has not shown that VG 109's capitalization was so minimal as to prove that it was a sham entity. There is no evidence, for example, that capitalizations of similar firms exceeded that of VG 109.\textsuperscript{110} Insolvency, in and of itself, does not justify piercing the corporate veil.\textsuperscript{111} Additionally, the fact that VG 109 met and slightly exceeded the minimum capitalization required for such entities under Dutch law further undermines EBG's position.

\textsuperscript{105}See id. ¶ 11.

\textsuperscript{106}See Van der Have Aff. ¶¶ 17, 19.

\textsuperscript{107}Any breach of contract . . . is, in some sense, an injustice. Obviously this type of 'injustice' is not what is contemplated by the common law rule that piercing the corporate veil is appropriate only upon a showing of fraud or something like fraud. The underlying cause of action does not supply the necessary fraud or injustice. To hold otherwise would render the fraud or injustice element meaningless, and would sanction bootstrapping." \textit{Mobil Oil Corp. v. Linear Films, Inc.}, 718 F. Supp. 260, 268 (D. Del. 1989); see also Sears I, 744 F. Supp. 1297, 1305 (D. Del. 1990).

\textsuperscript{108}Compl. ¶ 26.

\textsuperscript{109}See Anderson v. Abbott, 321 U.S. 349, 361 (1944) ("Normally the corporation is an insulator from liability on claims of creditors. The fact that incorporation was desired in order to obtain limited liability does not defeat that purpose.").

\textsuperscript{110}See Mason v. Network of Wilmington, 2005 WL 1653954, at *4 (Del. Ch. July 1, 2005) (merely stating that firm was insolvent did not show firm was under-capitalized; pertinent facts could have included a comparison of similar firms in the industry).

\textsuperscript{111}See Mason, 2005 WL 1653954, at *3.
The other facts cited by EBG in favor of disregarding VG 109's corporate form all relate to the close interrelationship between VG 109 and NIBC: they share offices, officers, and letterhead, and VG 109 is a wholly-owned subsidiary of NIBC, which is managed by NIBC. In the absence of fraud and inequity, however, these facts do not warrant disregarding the corporate form.

Nor would EBG's potential inability to sue NIBC in Delaware for the taxes due from VG 109 create the requisite inequity. Documents contemporaneous with the formation of EBG show it was well known that the lenders, such as NIBC, might take an ownership interest in EBG indirectly through a subsidiary. The parties to the EBG operating agreement could have required a guaranty by any lender that elected to participate through a subsidiary, but they did not. Similarly, assuming EBG will be making future distributions, EBG could "be repaid by reducing the amount of the current or next succeeding distribution or distributions . . . ." The record suggests this would be true even if VG 109 has transferred its economic interest to a third party. Alternatively, EBG presumably could seek relief from NIBC and VG 109 in the Netherlands.

112 Amended LLC Agreement § 11.4. The record does not indicate whether or not there have been or are likely to be any succeeding distributions.

113 See id. § 4.4 ("[EBG] shall be entitled to treat the record holder of Units as shown on its books as the owner of such Units for all purposes, including the payment of distributions and the Voting rights . . . regardless of any Transfer of such Units . . . ."). The parties dispute the validity of the alleged transfer by VG 109. Assuming the transfer to a third party was valid, EBG has not shown why the transferee would not be liable for the alleged tax withholding, if the membership transfer was reflected on the books of EBG. If VG 109's alleged March 2006 transfer was valid, EBG does not address why the transferee would not be subject to the consent to jurisdiction provision in the Amended LLC Agreement, or even in the absence of the consent provision, why the alleged transferee would not be subject to personal jurisdiction as a "New York banking institution organized and existing under the laws of the state of Delaware." See Pinckney Aff. Ex. 1 at 1. On the other hand, assuming instead that the transfer was invalid, EBG omits any discussion of whether it could obtain a judgment against VG 109 and seek satisfaction, not only out of the 20,000 euros left in EBG, but also by pursuing the EBG units that remain assets of VG 109.

114 With regard to any implied drafting chicanery on the part of NIBC with the intent to avoid jurisdiction anywhere, EBG offers no reason to question the competency or jurisdiction of the judicial system in the Netherlands, where both NIBC and VG 109 are domiciled, and where there exists a well-known history of commercial acumen, including securities markets that predate even London's. See John C. Coffee, The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control, 111 Y.L.J. 1, 9 (2001). Accordingly, to the extent EBG could be making an argument based on something akin to NIBC contriving "no other [available] forum," as suggested in Shaffer v. Heiner, 433 U.S. 186, 211 n.37 (1977), the implication is unavailing.
2. Did VG 109 commit jurisdictional acts in Delaware that can be imputed to NIBC?

Although I have found that VG 109 was an agent of NIBC for purposes of NIBC's 12(b)(2) motion to dismiss, the issue remains whether VG 109 committed any acts in relation to the formation of EBG that could be imputed to NIBC and support the exercise of personal jurisdiction over NIBC in Delaware under §3104. EBG contends "NIBC caused VG109 to enter into the [Amended LLC Agreement] in which VG109 not only consented to this Court's jurisdiction, but obligated itself to repay to EBG any tax advances made on its behalf."\(^{115}\) NIBC responds that VG 109 committed no jurisdictional act in Delaware that could be imputed to NIBC to satisfy the requirements of § 3104(c), because VG 109 executed the Amended LLC Agreement in the Netherlands, and not in Delaware.\(^{116}\)

To the extent EBG contends this Court should use the agency theory of jurisdiction to impute VG 109's contractual consent to personal jurisdiction over it in Delaware to NIBC, that argument is untenable. EBG has not cited any case that supports imputing a specific contractual obligation of an agent to a principal for purposes of establishing personal jurisdiction over the principal. In this case, VG 109 admittedly is subject to this Court's jurisdiction by virtue of its consent reflected in the Amended LLC Agreement. To allow EBG to impute that contractual consent by VG 109 to NIBC would sanction bootstrapping and defeat the careful drafting of the consent provision of the Agreement, which only applies to the parties to the Agreement.\(^{117}\) Because sophisticated parties negotiated the Original and Amended LLC Agreements, and included a consent to jurisdiction by the parties, but not their affiliates, I reject EBG's attempt to circumvent the parties' intention under the guise of an agency argument.

I next address whether VG 109 transacted any business in Delaware from which EBG's claims arose that would satisfy the requirements for personal jurisdiction under § 3104(c)(1) of the long-arm statute. Stated differently, if VG 109 had not consented to jurisdiction in Delaware for any alleged breach of the Amended LLC Agreement, would it still have been subject to jurisdiction in Delaware under § 3104. In analyzing this issue, I note that: EBG is a Delaware LLC; VG 109 is a Dutch entity; VG 109 signed the operative agreements in the Netherlands; VG 109 owns less than

\(^{115}\) PAB at 21.
\(^{116}\) See DRB at 16-17.
\(^{117}\) See discussion supra Part II.B.2.a-b.
3% of the interests in EBG;\textsuperscript{118} VG 109 is not alleged to have exercised control over EBG or misused EBG in any way in terms of dealings with third parties; and the underlying dispute here concerns whether, under the terms of the Amended LLC Agreement, EBG properly paid taxes due on behalf of VG 109, and whether VG 109 is obligated to reimburse EBG for those payments. Thus, the question reduces to whether a minority, passive investor in a Delaware LLC who allegedly breaches the LLC agreement in a manner that affects the rights of the LLC and its members \textit{inter se} is subject to jurisdiction under Delaware's long-arm statute for the alleged breach. Without a showing that the investor in the LLC took some additional action from which the asserted cause of action arose to consciously take advantage of the laws of Delaware, I conclude the answer to that question is no. Therefore, even if all of the actions of VG 109 in this case related to the EBG Amended LLC Agreement were imputed to NIBC, those actions still would not provide a sufficient basis for subjecting NIBC to the jurisdiction of this Court.

The fact that VG 109 executed the Agreement in the Netherlands, not Delaware, is not dispositive. It is not necessary for the execution of an agreement actually to have taken place in Delaware for it to constitute the transaction of business.\textsuperscript{119} VG 109's execution of the Amended LLC Agreement, as a fundamental governance document, conceivably could supply a basis for personal jurisdiction in this Court. Executing and then allegedly breaching an LLC agreement also presents interesting jurisdictional questions, because the LLC agreement is itself a conceptual hybrid. On the one hand, an LLC agreement is similar to a certificate of incorporation, because it is a foundational document that controls the governance of the entity. In that sense, the LLC agreement relates to the very nature of the entity, and manipulation of its governance provisions could qualify as a jurisdictional act.\textsuperscript{120} On the other hand, the Delaware Limited Liability Company Act and Delaware courts have emphasized the importance of freedom of contract when dealing with LLC agreements.\textsuperscript{121}

\textsuperscript{118}As of May 24, 2004, EBG is listed as having approximately 4.5% of the membership interest. Original LLC Agreement at Schedule II. As of October 11, 2005, VG 109 is listed as having approximately 2.5% of the membership interest. Am. LLC Agreement at Schedule A-1.

\textsuperscript{119}AeroGlobal Capital Mgmt., LLC v. Cirrus Indus., Inc., 871 A.2d 428, 440 (Del. 2005) ("While evidence of physical presence may be helpful in determining a party's intent to transact business and to show the actual transaction of business in this State, ... such evidence is not the sine qua non for jurisdiction under Delaware's Long Arm Statute.").

\textsuperscript{120}See discussion \textit{supra} Part II.B.1.a-b (discussing how both the Cairns and Papendick opinions involved elements of control not present here).

\textsuperscript{121}See discussion \textit{supra} Part II.B.2.a (discussing how freedom of contract predominates over statutory requirements when considering LLC agreement interpretation).
Not surprisingly, therefore, LLC agreements also may contain provisions that do not implicate the fundamental attributes and workings of a Delaware entity. Some provisions relate more to the respective rights and obligations of members of a particular LLC, and the alleged breach of those provisions by a minority member of an LLC may not satisfy § 3104(c)(1).

Here, the obligation to reimburse EBG for tax withholdings is a collateral provision that does not significantly affect the operation of EBG under Delaware law. Thus, the mere act of promising to reimburse EBG for tax withholdings in the Amended LLC Agreement, and then allegedly failing to perform on that promise in relation to a payment made by the LLC more than two years after the nonresident defendant joined the LLC would not provide an adequate basis for subjecting a party to personal jurisdiction, absent its consent.

*Papendick* and its progeny stand for the proposition that a foreign corporation's ownership of a Delaware subsidiary may constitute the transaction of business under Delaware's long-arm statute where the underlying cause of action arises from the creation and operation of the Delaware subsidiary, because in that instance the foreign corporation availed itself of the benefits and protections of the laws of the State of Delaware. EBG, however, has made no showing that it was a subsidiary of either VG 109 or NIBC, as that term is commonly understood, as opposed to being merely a company in which VG 109 was a minority investor.122

Therefore, EBG has not shown how a foreign business entity's execution of a governance document like the Amended LLC Agreement would fall within the *Papendick* line of cases where the foreign entity holds less than 5% of the total membership interest. Moreover, there is nothing in the record to suggest VG 109 had any kind of controlling influence, operational or otherwise, over EBG. Because VG 109 committed no jurisdictional acts in Delaware, there are no contacts to impute to NIBC sufficient to subject it to jurisdiction in Delaware under either the agency or alter ego theory of jurisdiction.

III. CONCLUSION

For the reasons stated, I grant NIBC's motion to dismiss EBG's claims against NIBC for lack of personal jurisdiction.

IT IS SO ORDERED.

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122*Cf. Gibralt Capital Corp. v. Smith*, 2001 WL 647837, at *5 (Del. Ch. May 8, 2001) ("As a general rule, ownership of stock in a Delaware corporation, without more, will not suffice to establish general in personam jurisdiction.").
IN RE LORAL SPACE & COMMUNICATIONS INC.
CONSOLIDATED LITIGATION

Court of Chancery of the State of Delaware, New Castle

No. 2808-VCS

September 19, 2008

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David J. Teklits, Esquire, and Thomas W. Briggs, Jr., Esquire, of Morris,


STRINE, Vice Chancellor

I. Introduction

A satellite company, Loral Space and Communications Inc., emerged from bankruptcy with a large stockholder, defendant MHR Fund Management LLC, whose business model involved taking control of distressed companies and positioning itself to reap the benefits of control for itself and its investors. MHR soon used its influence at Loral to place one of its advisors, defendant Michael B. Targoff, as Loral's CEO. Targoff went into the job of CEO with the goal — conceived in connection with MHR's creator, defendant Mark H. Rachesky — of having MHR make a substantial equity investment into Loral that would permit Loral to pursue acquisitions and invest in growing its existing business lines.

Almost as soon as Targoff assumed the managerial reins at Loral, he proposed that MHR make an investment of $300 million into Loral, an investment equal to over half of Loral's existing stock market capitalization.
Targoff and others affiliated with MHR argued that Loral had to raise no less than $300 million and that it had to be in equity, despite the fact that there was no magic to the $300 million figure and that the company's own financial advisor suggested viable options for raising capital that involved both debt and equity.

Even though the $300 million constituted a huge percentage of the company's existing capitalization, the Loral board eschewed any consideration of a sale of the company as a whole, a sale that would have threatened MHR's effective control position. Instead, a "Special Committee" was formed with a narrow mandate to raise $300 million in equity capital fast through a deal with MHR. The Special Committee's chair was a close friend of Rachesky, served on three boards at the instance of MHR, and was touted by MHR as one of its investment advisors.

The Special Committee never made a market check to see whether capital was available on better terms than MHR was offering. Instead, the Special Committee, which hired an outgunned financial advisor with far less experience than MHR's advisor, Deutsche Bank, did nothing substantial to test the market, and blew off an expression of interest by Goldman Sachs to invest in Loral because Goldman would only provide up to $100 million of the desired $300 million in capital.

Having decided to move fast, the Special Committee struck the basic economic terms of its deal with MHR after less than two weeks of work and after conducting no market check. It then granted MHR convertible preferred stock with a high dividend rate and low conversion rate compared to the market comparables identified by its advisor. Then, despite the supposed need for urgency, months went by while Loral management took the lead in haggling with MHR over other terms of the convertible preferred, with the Special Committee staying involved but in a less forward way than Loral management. Eventually, the other terms were struck, which gave MHR extraordinary class voting rights over any action of the Loral board that could "adversely affect" the holders of the preferred or the common stock into which it was converted, the right to put the convertible preferred to Loral in a Change of Control for a value of at least $450 million, and the potential to acquire a total of 63% of Loral's equity. Although the terms of the "MHR Financing" capped MHR's common stock voting power at 39.99%, the class voting rights it acquired gave MHR a unilateral veto over any strategic initiative Loral undertook.

Despite the fact that the process dragged on, the Special Committee never used that breathing space to subject the MHR Financing to a real market check. Similarly, even though the MHR Financing gave MHR a veto over the company's future, the Special Committee never considered whether Loral should be exposed to a hot market for corporate control, in which
private equity buyers were using the availability of easy credit to make good buys. Instead, the Special Committee simply dealt with MHR, which drove a bargain that left itself with terms that were better than market.

Although MHR justifies that result by arguing that it took on extraordinary risk, MHR's own behavior is much more consistent with aggressive, profit-seeking behavior. The defendants admit that if MHR was willing to backstop an offering of securities, then Loral had the chance to raise substantial capital in the public markets. But MHR refused to consider any deal in which it received anything other than all of the securities Loral was offering. That is, MHR wanted all of the opportunity for itself, a posture suggestive of its view that Loral had positive profit opportunities. Indeed, throughout this process, Loral was involved in considering a strategic acquisition of another satellite corporation, Telesat, a transaction that MHR was very interested in seeing Loral consummate. Before the MHR Financing documents were signed, Loral — which had been encouraged by Telesat's CEO to consider a purchase of Telesat — was invited to bid in an auction for Telesat. The day after the MHR Financing documents were signed, Loral put in that bid and within two months had landed a deal with Telesat.

The public announcement of the MHR Financing sparked outrage among Loral investors. In reaction, Loral announced that it was considering alternatives that would allow other investors to participate. But rather than explore alternatives, the Loral Special Committee eventually decided to simply close the deal with MHR.

This suit was brought by plaintiffs owning a substantial number of Loral shares, alleging that the MHR Financing was a conflicted, unfair deal approved by an inept and outwitted Special Committee. The defendants, who include MHR and the directors of Loral, contend that the MHR Financing was fair to Loral and necessary to enable Loral to raise required capital.

In this decision, I conclude that the MHR Financing was unfair to Loral. Using its effective control, MHR set in motion a process in which the only option that the Special Committee considered was a deal with MHR itself. Rather than acting as an effective agent for the public stockholders by aggressively demanding a market check or seeking out better-than-market terms from MHR in exchange for no market check, the Special Committee gave MHR terms that were highly favorable to MHR, in comparison to the convertible preferred transactions its own advisor deemed comparable. These terms gave MHR a chokehold on Loral's future and 63% of its equity. Regrettably, the negotiation process was also marred by the conduct of its chairman and financial advisor, who undercut Loral's own negotiation
position. Even more egregiously, during the special committee process, its chairman was seeking to have MHR invest in his own business.

The lack of a market check and the unusual nature of the MHR Financing make it a challenging task to determine the correct remedy. But the behavior of MHR itself suggests that Loral had positive growth prospects that MHR wanted to capture solely for itself; growth prospects that MHR was uniquely positioned to know about and that were not known by the public markets. Given MHR's burden to demonstrate fairness, its own positive view of Loral's prospects, and the unduly favorable terms it extracted from an ineffective Special Committee, I enter a remedy reforming the MHR Financing to convert MHR's convertible preferred into non-voting common stock. I use a price that takes into account MHR's access to inside information, its insulation of itself from market pressures, and its attainment of a $6.75 million fee for placing securities with itself, but that also gives substantial weight to Loral's actual stock trading price. This remedy also addresses the unfair control benefits attained by MHR.

Finally, this decision addresses a related lawsuit. Certain noteholders of a Loral subsidiary, Skynet, have sued Loral and Skynet. The noteholders argue that Skynet breached the implied covenant of good faith and fair dealing in the note indenture by redeeming their notes for 110% of par value and accrued interest. The reason is that Skynet's right to redeem was subject to the requirement that not more than two-thirds of the noteholders object. MHR held over 45% and agreed not to object. Its agreement not to object resulted from the negotiations over the MHR Financing. In a section of a key agreement, MHR agreed not to object to early redemption of the notes if Loral entered a strategic transaction exceeding $600 million in value. The noteholders contend that their rights were violated because MHR received consideration for its decision not to object, in the form of the favorable terms of the MHR Financing, that were not offered to other noteholders.

I reject that argument. The terms of the notes contain no restriction on payments for consents. Unlike most note issuances, here, one holder, MHR, owned a large position and was singularly able to deliver a non-objection that would enable early redemption. During the negotiations over the indenture governing the notes, the creditors' committee tried to get a provision inserted prohibiting any payments in connection with consents. That provision was rejected, as was a contrary provision, and the eventual indenture was silent on the question. But noteholders were clearly told that MHR had a sufficient number of notes to unilaterally consent to early redemption.

The implied covenant in a bond indenture is not a license for judges to invent market terms that should act as a default rule simply because plaintiffs or the judge think that would be a good thing. Bond indentures are carefully
negotiated instruments filled with many restrictions. Therefore, courts should be chary in assuming that there are gaps to be filled, particularly when parties actually considered the question and the agreement ultimately reached incorporated no restriction on the rights of the issuer to bargain with a large holder for its consent. And that is particularly the case when it is clear that many indentures expressly prohibit such payments, that such an express restriction was sought, and did not make it into the indenture. What the noteholders got here is precisely the fruits of the bargain they struck, which was a full 110% of principal value plus accrued interest, in a situation when fewer than two-thirds of the noteholders did not object. Indeed, what happened was highly foreseeable, as the other noteholders should have foreseen that MHR, which was Loral's largest stockholder, might have reasons to not object to early redemption in connection with a strategic transaction good for Loral's equity holders that would not be identical with respect to noteholders who did not have a similar equity stake. No reasonable expectancy was upset here; the other noteholders got the compensation provided by the notes themselves.

II. Factual Background

A. The Key Players

1. Loral And Its Largest Stockholder, MHR

Loral Space and Communications Inc. ("Loral" or the "Company") is a satellite communications company. Loral was formed to succeed to the business conducted by its predecessor company, which went into bankruptcy in 2003. Loral emerged from bankruptcy on November 21, 2005. At that time, and through much of the relevant time period, Loral had two primary businesses that were approximately equal in size — satellite manufacturing and satellite-based communications services. Loral's satellite manufacturing business is conducted by its subsidiary, Space Systems/Loral, Inc. ("SS/L"). SS/L manufactures only commercial satellites, such as those used for satellite television (e.g., DirecTV) and satellite radio (e.g., Sirius), because it has been unsuccessful in its attempts to enter the market for government satellites.¹ Loral's satellite-based communications services business, also known as Fixed Satellite Services ("FSS"), was operated by its subsidiary Loral Skynet Corporation ("Skynet") until October 31, 2007, when it was

¹Tr. at 679 (Townsend).
transferred to a joint venture commonly referred to as Telesat. More on that joint venture later. Skynet owns satellites and then leases the capacity of those satellites to other organizations.

Loral, like many companies emerging from bankruptcy, had a large institutional stockholder base comprised of former creditors. The largest Loral stockholder was MHR Fund Management LLC (together with its affiliates, "MHR"), "a New-York based investment firm that takes a private equity approach to investing in distressed and undervalued middle-market companies." MHR is the eponymous creation of defendant Mark H. Rachesky, who is MHR's President. Before the transaction that is the subject of this action, MHR owned 35.9% of Loral's common stock, which it acquired as part of Loral's emergence from bankruptcy. MHR publicly maintained that it had "control of Loral's board," and that sentiment was echoed in Loral's 10-Ks stating that "MHR is our controlling shareholder."

MHR's control position at Loral was an easy fit with its investment strategy. As MHR explained in its marketing materials, one of MHR's investment strategies focused on extracting control premiums from inefficiently traded, middle-market companies:

MHR believes that the markets for distressed and undervalued middle-market companies are inefficient at all levels of the capital structure . . . . Within this context, MHR is unusually well-positioned to extract significant control premiums through accumulating blocking positions in debt investments, negotiating bond indenture modifications through majority ownership positions, accumulating large equity stakes and exercising influence through close relationships with management, taking board positions, and otherwise bringing to bear the Managing Principals' wealth of knowledge and experience in effectuating control and influence.

Consistent with MHR's investment strategy, MHR owned large positions in several debt instruments issued by Loral and its subsidiaries in addition to its large block of Loral common stock. In particular, MHR

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2 JX 1222 at 1.
3 Pre-Trial Stip. at 1.
4 JX 1222 at 29 ("MHR's significant equity ownership and control of Loral's board enables it to play a dominant role in creating and implementing Loral's post-reorganization strategy."); JX 103 at 19 (2005 10-K stating "MHR is our controlling shareholder and may have conflicts of interest with us in the future."); JX 1005 at 25 (2006 10-K stating the same).
6 JX 1222 at 3.
owned approximately 45% of the "Skynet Notes," which were 14% secured notes with a total face value of $126 million and were issued in a rights offering made in connection with Loral's emergence from bankruptcy. MHR owned a higher percentage of the Skynet Notes as compared to the common stock, 45% versus 36%, because MHR backstopped the Skynet Notes rights offering and bought any notes other eligible creditors were offered but failed to purchase. The Skynet Notes had a high coupon rate that made them "very expensive" to Loral. The Skynet Notes were not due until 2015, but they could be redeemed by Loral in 2009 without the consent of the holders of the Skynet Notes (the "Noteholders") at 110% of principal plus accrued interest. In addition, the Skynet Notes could be redeemed before 2009 at 110% plus accrued interest unless Noteholders representing more than two-thirds of the outstanding principal value objected. Thus, given MHR's 45% stake in the Skynet Notes, it had the ability to unilaterally consent to the early redemption of the Skynet Notes. That control over the Skynet Notes' consent only added to the influence MHR had over Loral.

2. The Loral Directors

Loral had eight directors on its board at the time the "Securities Purchase Agreement" that documented the MHR Financing was signed. The Chairman of Loral's Board of Directors was defendant Rachesky, who was Carl Icahn's chief investment advisor before he co-founded MHR with defendant Hal Goldstein, now a Managing Director at MHR. Goldstein joined Rachesky on Loral's board, as did MHR's other Managing Director, defendant Sal Devabhaktuni.

In addition, two other Loral directors, CEO and Vice-Chairman Michael B. Targoff and Special Committee Chairman John D. Harkey, Jr., were affiliated with MHR. MHR listed Targoff and Harkey as two of its five "Selected Investment Advisors" in its marketing materials. MHR boasted about its majority representation on Loral's board in a December 2005 letter to its investors explaining:

Post the bankruptcy [in which Rachesky was the chair of Loral's unsecured creditor's committee], MHR has maintained its position of influence and control in Loral in order to maximize value to its investors. MHR is the largest holder of

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7Tr. at 866 (Targoff).
8JX 1222 at 21.
Loral's common stock, preferred stock and notes. In addition, Mark Rachesky, Hal Goldstein, and Sai Devabhaktuni, the three MHR managing principals, and John D. Harkey, Jr., and Michael B. Targoff, both MHR advisors, constitute 5 of the 9 members of Loral's new board of directors.9

Targoff, who had previously been a partner at a large New York law firm, joined Loral's predecessor in 1982 and served in various executive positions until 1998, when he left to pursue his own business as a telecommunications investor and entrepreneur. Targoff assisted MHR in making its first investment in Loral's predecessor in 2001. After that, Targoff and his assistant were allowed to set up shop in MHR's midtown Manhattan offices rent-free. In exchange for free rent in one of America's most expensive office locations, Targoff provided advice to MHR on potential transactions and business opportunities.

Targoff became directly involved again with Loral during the bankruptcy process. MHR had been appointed as the head of the unsecured creditors committee, and relations between the creditors committee and Loral's management were "dysfunctional." 10 Targoff stepped in and served as an intermediary between the creditors' committee, primarily its Chairman Rachesky, and Loral's management, primarily Loral's then-CEO Bernard Schwartz. Targoff continued that intermediary role post-bankruptcy when he was named as the Vice-Chairman of Loral's board of directors. Within a few months after Loral emerged from bankruptcy, Schwartz resigned his role as Loral's Chairman and CEO. Schwartz's resignation was the result of the dysfunctional relationship he had with the MHR directors. Indeed, it came at a time when Rachesky and Targoff had started to hire a headhunter to replace Schwartz. Rachesky and Targoff then agreed that Targoff would become CEO at the beginning of March 2006. Thus, Targoff was named Loral's new CEO and retained his role as Vice-Chairman. Rachesky replaced Schwartz as Chairman.

Harkey, who was named chairman of the Special Committee, is the Chairman and CEO of Consolidated Restaurant Companies, Inc., a Dallas-based restaurant company with approximately 130 restaurants. Harkey and Rachesky were business school classmates at Stanford, have maintained a "long-time friendship," and serve as business resources and references for each other. Based on Rachesky's recommendation, Harkey serves as a

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9JX 45 at 1-2.
10Tr. at 760 (Targoff).
11Tr. at 286 (Simon).
director on three boards — Loral, Leap Wireless International, Inc., and Emisphere Technologies, Inc.\textsuperscript{12} Unsurprisingly, MHR holds large blocks of stock in each of those companies.\textsuperscript{13}

The other member of the two-person Special Committee was defendant Arthur L. Simon. Simon was a partner at Coopers & Lybrand L.L.P., Certified Public Accountants, before he retired in 1994. Since that time, Simon's only substantial involvement in the business world has been his service on Loral's board and the board of a publicly traded defense contractor that was once part of Loral.\textsuperscript{14}

Loral's other directors at the time the MHR Financing was approved were defendants John P. Stenbit and Dean Olmstead. The plaintiffs have spent little effort describing the roles of Olmstead and Stenbit in the events relevant to this lawsuit.\textsuperscript{15}

B. Loral's Post-Bankruptcy Business Challenges

Loral faced business challenges as it emerged from bankruptcy. At a high level, Loral's problem was that it desired growth, but its business plan and capital structure exiting bankruptcy were geared toward a no-growth plan. Chief among the challenges faced by Loral were Skynet's small scale and the capital needs at both Skynet and SS/L.

Skynet's scale problem was, in part, a result of the bankruptcy process. Skynet sold five of its satellites during bankruptcy and the four remaining satellites left it as a "subscale business."\textsuperscript{16} As Near Earth LLC, an industry analyst hired by plaintiff Highland Capital to value Loral, put it, "Skynet is the smallest of the global [FSS] operators, and as such ... it has scale economy and marketing disadvantages compared to its larger competitors."\textsuperscript{17}

Both business units — SS/L and Skynet — had capital needs. SS/L needed capital to help address cash flow difficulties and fund spending priorities necessary for future growth. The capital requirements of Skynet were more considerable. The most mundane called for cash to replace an existing satellite, T-11N, that was running out of fuel. The most substantial

\textsuperscript{12}Tr. at 114 (Harkey).
\textsuperscript{13}In fact, Harkey, Targoff, and Rachesky are all directors of Leap.
\textsuperscript{14}Tr. at 275 (Simon).
\textsuperscript{15}Given this dearth of evidence about Olmstead and Stenbit, I say almost nothing more about them. As the plaintiffs have failed to provide any basis for me to infer subjective bad faith on their part, and therefore failed to provide any basis for me to hold them liable given the presence of an exculpatory provision in the Loral charter, I must dismiss the claims against these directors.
\textsuperscript{16}Tr. at 677 (Townsend); see also Tr. at 765 (Targoff).
\textsuperscript{17}JX 706 at HCOP0005449.
need was for capital that would enable Skynet to pursue an acquisition that might contribute to its scale. This last need is what emerged most prominently from the trial record as requiring a large capital infusion for its attainment.


Loral had an opportunity to gain scale in its FSS business in late 2005 because New Skies Satellites Holdings Ltd. was up for auction. New Skies was another player in the global FSS industry with five satellites. Loral began pursuing an acquisition of New Skies just before Loral exited bankruptcy and continued that pursuit after it emerged from bankruptcy. But, Loral's attempt to acquire New Skies was compromised by questions about Loral's financial strength and stability.

During the discussions over New Skies, Targoff was still only Loral’s Vice-Chairman and working out of MHR's offices. At that time, Targoff and MHR considered an equity investment by MHR to shore up Loral's financial condition and enable Loral to ease New Skies' concerns. Targoff and MHR discussed that $200 million would resolve New Skies' apprehension about Loral's bid, but Targoff suggested that "$300 [million would] make[] this baby hum."18 In Targoff's view, the additional $100 million was necessary for Loral's growth, including building the new T-11N satellite. MHR decided not to make any investment at that time, and Loral, although it was the highest bidder, lost the New Skies auction because of concerns over its financial wherewithal.

After the failed New Skies bid, Targoff "came to think . . . even more strongly" that Loral needed a large cash equity infusion.19 Targoff also believed that "the most practical and feasible way" to get the sizeable equity infusion that he believed Loral needed was to get it from MHR.20 Notably, when Targoff was first advocating an equity investment by MHR in Loral,

18 JX 42 (December 21, 2005 email from Targoff to MHR’s principals and outside counsel).
19 Tr. at 776 (Targoff).
20 Tr. at 777 (Targoff). Part of the reason for Targoff’s belief that an equity investment by MHR was the most feasible method for obtaining additional equity financing was that, as part of the Registration Rights Agreement between MHR and Loral that was signed as Loral exited bankruptcy, Loral agreed not to initiate an underwritten offering of its securities for its own account for nine months after Loral filed a registration statement at MHR’s request. JX 32 § 3.2(c); Tr. at 778 (Targoff). Although MHR never requested that Loral file such a registration statement, Loral and MHR agreed to start the nine-month period on June 1, 2006. Thus, this restriction was one of several reasons Loral narrowed its capital raising focus to MHR.
he did so on behalf of MHR, referring to the possible investment as "our $200mm (I think it should be $300) commitment" in a December 2005 to MHR's principals.\(^21\)

**D. Targoff Becomes CEO And The Special Committee Is Appointed To Seek Financing From MHR**

When Targoff became Loral's CEO at Rachesky's impetus, Targoff therefore made getting board approval for a large additional investment by MHR into Loral his first management priority. Very quickly, Rachesky and Targoff engaged MHR's counsel to help them implement this goal, which was already in place when Targoff assumed the top managerial reins at Loral. MHR's counsel emailed Targoff and copied Rachesky and Goldstein a copy of an article entitled "Sale of Control Transaction: Pre-Agreement Auction or Post-Agreement Market Check" and stated that it "covers some of the fundamental principles of Delaware law in this area that would be relevant to the type of transaction we discussed."\(^22\) A few days later, on March 6, 2006, Loral's outside counsel emailed Targoff and Loral's inside counsel suggesting that the entire fairness standard would apply to a transaction with MHR and that Loral should use an independent special committee.\(^23\) No special committee was appointed at that time. Instead, ten days later, on March 16, 2006, Targoff emailed Rachesky requesting that MHR consider making an equity infusion.\(^24\) Targoff explained that Loral might find itself in an inadequate position to take advantage of surfacing strategic initiatives and stated that he did not want to be "forced to go to equity markets at a time when [Loral's] needs reflect weakness."\(^25\) Of course, Targoff already knew that his suggestion would be received warmly. And it was. Rachesky responded quickly by sending a letter indicating that "MHR is prepared to invest a total of up to $250 million in Loral" and that MHR "fully expect[s] to negotiate and close a transaction in very short order."\(^26\)

Shortly after the exchange between Targoff and Rachesky, Loral held a telephonic board meeting on March 23, 2006. Targoff updated the board about a possible transaction with Telesat, the satellite communications

\(^{21}\)JX 42 (emphasis added).

\(^{22}\)JX 72 (Doron Lipshitz email dated March 1, 2006).

\(^{23}\)JX 75 (Bruce Kraus email with excerpts of Kahn v. Tremont, 694 A.2d 422 (Del. 1997), and the statement "even if you have an independent committee, you're not home free, but you can imagine the result if you didn't use one at all").

\(^{24}\)24 JX 1244.

\(^{25}\)Id.

\(^{26}\)JX 1246 (letter dated March 20, 2006).
services subsidiary of BCE, Inc., commonly known as Bell Canada Enterprises. Telesat had announced in February that it was pursuing an IPO, and Targoff received a call from the CEO of Telesat giving him a heads-up that Telesat was trying to convince its parent company to do a private sale instead. Loral soon retained Morgan Stanley to help it in an on-going basis in pursuing a strategic deal of some sort with Telesat. Not coincidentally to his interest in a deal with Telesat, Targoff also told the board that Loral would need to "plan for its long term capital requirements in order to take advantage of various opportunities" and that "[i]f MHR is involved in providing financing, the approval of a special committee of independent directors would be required."27

The next Loral board meeting, held April 7, 2006, opened with Targoff again mentioning to the board that Loral was exploring a deal with Telesat.28 Later in the meeting, Targoff presented his case that Loral should raise $300 million in equity in the form of an investment by MHR.29 Targoff outlined a "wish list"30 of the items Loral could use $300 million for over a five-year horizon.31 These items were not trivial ones, they were real business objectives, but nor were they objectives that required funding of $300 million imminently or on any firm timetable.32

Without considering the possibility of other forms or sources of financing,33 the Loral board appointed the Special Committee to "evaluate and negotiate" the proposed equity financing from MHR.34 Oddly, the board chose to comprise the Special Committee of only two members and to make Harkey — an advisor of MHR35 — its Chair, with Simon as the only other member. In their brief, the Special Committee argues that in "a perfect world" the composition of the Committee might have been different, "[b]ut,

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27 JX 97 at 3.
28 JX 119.
29 Targoff had been in discussion with MHR about the equity investment for weeks, as evidenced by the following March 22, 2006 internal MHR email:
   '[With respect] to the equity investment, [Targoff] plans to brief the board about his desire to add equity and show them our letter exchange. He plans on having [his] case for the investment fully built and ready for the April 7 [b]oard meeting and to create the special board committee and proceed from there.
JX 93 (email from Goldstein to Rachesky and Devabhaktuni).
30 Tr. at 700 (Townsend).
31 JX 121 (April 7, 2006 presentation to the board).
32 See Tr. at 791 (Targoff acknowledging there was "no deadline" for the propose capital raise).
33 Tr. at 148 (Harkey).
34 JX 119 at 4.
35 JX 45 at 1-2; JX 1222 at 21.
as [is] often the case, perfection was not available." In other words, Loral was effectively controlled by MHR and lacked a complement of several independent directors, from whom a larger special committee free from conflicting ties to MHR could be selected. Indeed, it appears from the rapidity of action that Targoff and Rachesky had settled on the composition of the Special Committee beforehand. In Targoff's words, the Special Committee's "mandate was to negotiate a transaction with MHR that they could tell the company, they believed, if they could get there, was reasonable and best available to the company." 37

From its creation, the Special Committee's effectiveness was hampered. Several factors contributed to this. First, the Committee was comprised of two members, neither of whom had any particular expertise or experience in the satellite industry. One of them, Harkey, was also, as shall be discussed more, someone with a close personal relationship with Rachesky and who maintained important business ties to MHR. The other, Simon, had been retired for many years, was not experienced in serving on a special negotiating committee, and did not bring energy to his duties.

More importantly, the Special Committee immediately allowed itself to go down the most dangerous path for anyone dealing with a controlling stockholder - that of believing that its only option was to do a deal with the controller. From the get-go, the Special Committee was pushed by Targoff and the MHR to move very rapidly to acquire $300 million in equity capital, leading the Special Committee to believe that time was of the essence. Although the Special Committee's literal mandate varied over time, substantively the Special Committee was only empowered to consider an equity investment from MHR. The original resolution establishing the Special Committee indicated that the Special Committee's mandate was to negotiate and execute a $300 million equity financing. 38 It did not mandate that the Special Committee determine the best available source of financing for Loral. 39 Later, at a May 26, 2006 board meeting, the Special Committee mandate was expanded to include such a determination to "satisf[y] the lawyers' definition of what the special committee should do." 40 But even so, both Special Committee members understood the Special Committee's mandate to require that it (1) "raise $300 million, not less," (2) in "equity,

37 Tr. at 822 (emphasis added).
38 JX 129.
39 Id.
40 Targoff Dep. at 573; JX 119.
not debt," and (3) get the financing "quickly."\textsuperscript{41} According to Simon, the Special Committee declined to pursue alternatives that were not "large enough and fast enough."\textsuperscript{42} In other words, the Special Committee's mandate, even after it was expanded, was framed and understood in such a way that the Special Committee believed its only option was to pursue a transaction with MHR.

The Special Committee's narrow mandate of obtaining $300 million in equity financing and the resulting focus on the MHR Financing persisted despite an April 18, 2006 presentation from Morgan Stanley, Loral's longtime investment banker, recommending a different approach.\textsuperscript{43} Morgan Stanley noted Loral had two primary needs for capital: positioning Skynet for a strategic merger and providing liquidity to fund Loral's business plans at Skynet and SS/L. Morgan Stanley considered a multitude of debt and equity financing alternatives and recommended that the company pursue a bifurcated approach to the financing needs: 1) a $150 to $200 million public common stock offering with a commitment from MHR to invest $50 to $100 million at the market clearing price to equitize Skynet for a potential merger; and 2) revolving credit facilities at Skynet and SS/L to provide liquidity to execute their business plans. Morgan Stanley's rationale for the common stock offering was that it was simple, could be executed relatively fast, and it would increase Loral's float and broaden its stockholder base. But the Special Committee rejected that alternative because it "would not achieve [its] objective."\textsuperscript{44}

Perhaps more important, MHR resisted any notion that it backstop a public offering or take only a major portion but not all of a private offering. MHR would, it said, do all $300 million or none at all.

E. The Special Committee Undertakes Its Task And Quickly Agrees With MHR On The Primary Financial Terms

Despite being told they needed to move fast, the Special Committee instead moved slowly, depriving itself of time that might have been devoted to expanding its exploration of options. After it was appointed on April 7, 2006, the Special Committee did not hold its first meeting until May 15, 2006. At that meeting, the Special Committee selected King & Spalding as its legal advisor. The following day MHR sent the Special Committee a

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\textsuperscript{41} Tr. at 150 (Harkey); see also Tr. at 339-40 (Simon).
\textsuperscript{42} Tr. at 339 (Simon).
\textsuperscript{43} JX 136.
\textsuperscript{44} Tr. at 41 (Harkey).
letter of intent with proposed terms for a $300 million convertible preferred stock investment by MHR.

The Special Committee then undertook the search for a financial advisor to evaluate the proposed transaction and match wits with MHR's financial advisor, Deutsche Bank. The Special Committee did preliminary diligence with respect to numerous investment banks, including many in the bulge bracket, but ultimately settled on North Point Advisors LLC, a small investment bank with whom Harkey had worked in the past. The Special Committee selected North Point despite the concerns expressed by Loral's general counsel that "[he] was not familiar with North Point and . . . that [Loral] would likely prefer that the Committee select a financial advisor with more 'street name recognition.'" North Point was headed by David Jacquin, a former Cravath M & A attorney who had no graduate training in business or economics but had previously worked in fairly rapid succession at several large investment banks. Jacquin and North Point had no experience in the satellite industry. Jacquin had little, if any, experience with the type of convertible preferred equity financing MHR was proposing, but he told the Special Committee that North Point works with Brad England, Jacquin's former colleague, "on any convertible [sic] or equity linked products" and that "Brad will work closely with us on this project." In fact, Jacquin had not spoken to England in over a year, had not talked to him about Loral, and ultimately never sought out his help with Loral. Despite the experiential and stature gap between North Point and Deutsche Bank, North Point was brought on board on May 23.

Then it became hurry up time again, as a target was set for the Special Committee to make a recommendation at the June 14 Loral board meeting, less than three weeks later and with Memorial Day weekend and the beginning of beach season intervening. To that end, North Point, put together a presentation for the Special Committee on Sunday, June 4, 2006.

45JX 193 (May 23, 2006 Special Committee minutes). Oddly, the Special Committee eliminated Lehman Brothers from consideration because Harkey went to business school with a Managing Director at Lehman and Simon also had a long-standing relationship with that same director. The Special Committee concluded that those relationships "could affect Lehman's ability to provide independent advice to the Committee." JX 193. Of course, Harkey was Rachesky's business school classmate, long-time friend, and professional "advisor."

46JX 186 (May 19, 2006 Special Committee minutes).

47JX 195 (May 24, 2006 email from Jacquin to the Special Committee's counsel in response to Simon's request that Jacquin "forward . . . Brad England's name for the record").

48This task strained both North Point's experience and capacity. See JX 238 (June 2, 2006 internal North Point email to Jacquin stating that "[f]rankly, none of us have had a ton of experience
North Point told the Special Committee that "the sale of convertible preferred to MHR is the best alternative to the Company to raise the capital needed" and that "the Company should pay a dividend between 5% and 7.5% and that the conversion premium should be 12% to 15%." Based on that advice, "the Committee decided that the Committee would proceed with negotiations with MHR for the sale of convertible preferred stock to MHR as the best available source of equity capital to the Company." The Special Committee's determination that MHR was the best available source of financing was, in part, based on the erroneous belief that North Point had conducted a market check before the June 4 presentation.

But North Point did not contact any third parties about the Loral financing before its June 4 presentation. NONE.

Having determined without any market check or reasoned exploration of other alternatives that its only real option was a deal with MHR, the Special Committee met with MHR at MHR's offices on June 7, 2006 to hammer out the terms of the financing. In attendance were the Special Committee's advisors, North Point and King & Spalding, and MHR's advisors, Deutsche Bank and Stroock & Stroock & Lavan. The meeting lasted a full day and resulted in agreement that the convertible preferred stock (the "Preferred Stock") would accrue interest at a 7.5% coupon rate and that MHR would have to pay a 12% premium to convert the preferred into common stock. That is, the Special Committee gave MHR the most favorable terms outlined in North Point's prior advice, terms better for MHR than the typical terms in the comparables North Point had identified.

The meeting also touched upon the "Revlon issue," which was the Special Committee's concern that the financing not result in a change of control. This was a very real issue because an equity infusion of $300 million was nearly 54% of Loral's existing market capitalization of $560 million as of June 1. Given that MHR already controlled 35.9% of Loral's equity, a further investment of $300 million by Loral would involve it holding over 58% of the company's total equity. But, consistent with its overall behavior, the Special Committee approached this reality in a blinkered way. Rather than checking whether, in a then-frothy M & A

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on evaluating this type of deal and its [sic] pretty complex so there [sic] I can feel the group is a bit overwhelmed").

49 JX 250 at 3 (June 4, 2006 Special Committee minutes); see also JX 249 (June 4, 2006 North Point presentation).

50 JX 250 at 3.

market, a sale of all of Loral might be advantageous, the Special Committee simply managed the "Revlon issue" to avoid triggering the duty to seek the highest value by capping MHR's voting power at some level that did not give it affirmative clear majority control but still left MHR with so substantial a negative control over Loral that the market would rightly perceive it to be a controlled company totally insulated from the market for corporate control. Put bluntly, Targoff's and Rachesky's support for raising no less than $300 million gave the Special Committee, if it had been advised to aggressively pursue the best interests of Loral's non-MHR stockholders, leverage to push for a broader search for alternatives. If, as Targoff and Rachesky were suggesting, Loral had positive growth prospects, there was a story to be told to a marketplace then filled with avid buyers. Instead of exploiting this opportunity, however, the Special Committee and its advisors simply maneuvered to avoid a technical invocation of Revlon duties.

Thus, on June 7 — less than two full weeks after North Point was engaged and without any market check — the Special Committee struck its basic economic deal with MHR. As Special Committee Chairman Harkey put it himself, the June 7 meeting resolved "90 percent of the primary terms" of the financing.\(^5\)

F. The Terms Of The Convertible Preferred Stock\(^3\)

Once the Special Committee had committed itself to doing a deal with MHR, the process again slowed down. Between the June 7 meeting, when the core monetary terms were agreed to, and October 17, 2006, when the Securities Purchase Agreement effectuating the MHR Financing was ultimately signed, the complex terms of that Agreement were negotiated.\(^4\) Those terms are very complicated, and fortunately many of the complicating factors are not material to this opinion. As such, I only describe the terms necessary to understand the basics of the Convertible Preferred Stock and simplify the mechanics of the Preferred Stock where appropriate. The

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\(^5\)Tr. at 63.

\(^3\)The terms discussed throughout this section are taken from the October 17, 2006 Securities Purchase Agreement, JX 562, and the February 27, 2007 Securities Purchase Agreement and Certificates of Designation, JX 994.

\(^4\)See JX 563 (email from Loral's assistant general counsel to King & Spalding after the Securities Purchase Agreement was signed, stating that "I do think it is safe to say that between us and MHR we have now come up with the most complicated thing known to man!"); JX 372 (email from Loral's outside counsel to Loral's assistant general counsel stating that he "was working through [the financing] documents . . . and found them pretty rough going just from the point of view of following the syntax!").
primary financial terms remained the same as agreed to at the June 7 meeting — $300 million in Convertible Preferred Stock would be issued to MHR with a 7.5% coupon and a 12% conversion premium. Loral was required to pay the 7.5% dividends in "paid in kind" ("PIK") securities for the first 17 quarters. After that time, Loral has the option to pay the dividends in cash if it meets certain financial requirements. The conversion price was set at $30.1504 per share of common stock based on a 12% premium over Loral's stock price of $26.92 on October 16, 2006. Loral paid MHR a $6.75 million placement fee for bringing itself to Loral to buy the Preferred Stock.

The Preferred Stock was broken up into two series because, as noted, the parties wanted to cap MHR's voting power at 39.999% to avoid having the MHR Financing subject the board to Revlon. MHR acquired 136,526 shares of Series A Preferred for $301.504 per share. Each Series A Preferred is convertible into 10 shares of common stock. If all the Series A Preferred shares are converted into common stock, MHR would increase its voting power from 35.9% to 39.999%. MHR also acquired 854,486 shares of Series B Preferred for $301.504 per share. The Series B Preferred is convertible into non-voting common stock. The Preferred Stock contains a threshold provision such that the non-voting stock automatically converts to voting stock whenever the percentage of Loral's voting stock held by MHR dips below 39.999%. In addition, upon certain events, some of which will be described below, all the non-voting stock converts to voting stock.

Important "Change of Control Provisions" were also negotiated to address how MHR's Preferred Stock would be treated in a merger or other change of control. The Change of Control Provisions apply during the "Make Whole Period," which is the first 66 months (5 and a half years) following closing of the MHR Financing. The upside Change of Control Provision, or conversion right, gives MHR the right to convert its Preferred Stock into the number of shares of common stock that MHR would have otherwise received if the Preferred Stock were converted at the end of the Make Whole Period. Combined with MHR's ownership predating the financing, MHR could own 63% of Loral's equity upon a Change of Control. The downside Change of Control Provision, or "Put Right," gives MHR the right to redeem its Preferred Stock, including the unpaid dividends, for the remainder of the Make Whole Period, for cash at the

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55Keller Report at 10. This amount presumes that Loral was required to pay PIK for the entire Make Whole Period. If the Change of Control took place after the mandatory PIK period and Loral qualified to pay dividends in cash at that time, the equity amount would be reduced because Loral could elect to pay the value for the dividends that would otherwise be paid over the Make Whole Period in cash rather than common stock.
conversion price. The approximate amount of the redemption payment is $450 million. The future dividends portion of the cash put payment contains no discount to present value to reflect that if not for the Change of Control, those dividends would be paid at a future time.

The Change of Control Provision is triggered by events such as an entity acquiring more than 50% of Loral's voting power, the transfer of control to another entity through a business combination, and a sale of substantially all of Loral's assets. The Change of Control Provision does not exempt a self-trigger by MHR. Instead, the Provision prevents MHR from receiving the additional benefits of the Make Whole if MHR triggers the Change of Control unless the Change of Control is approved by Loral's board or MHR triggers the Change of Control by acquiring more than 90% of Loral's voting power.

The Preferred Stock also has extensive class voting and consent rights that give MHR the power to veto Loral's ability to engage in a wide variety of transactions. Those voting and consent rights are complex and are backed by the requirement that any change to the Preferred Stock itself requires the affirmative vote or consent of each affected holder of the Preferred Stock. The most pertinent and "off-market" voting right is the requirement that Loral obtains majority approval from the Preferred Stockholders before it can:

authorize, or take any action, directly or indirectly, to alter, repeal, change or amend any provision of the Certificate of Incorporation or this Certificate of Designation, whether by or in connection with any merger, consolidation, reclassification, business combination, exchange, recapitalization, joint venture, partnership, sale, transfer, conveyance, lease, other disposition of all or substantially all of its property or assets, any similar transaction or otherwise, if such authorization or action would reasonably be expected to adversely affect the rights, preferences, privileges or powers of the [Preferred Stock or the

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56 The parties specified that the sale of any one of Skynet or SS/L would not trigger the sale of substantially all of the assets Change of Control provision. This clarification was likely put in place in anticipation of the potential sale of Skynet as part of the Telesat transaction.

57 Certificates of Designation § VI(F).

58 JX 383 (Loral's own outside legal counsel commenting on the class voting rights).
common stock] into which the [Preferred Stock is] convertible, or any of the holders thereof.]59

In other words, the Preferred Stock gets a class vote and has blocking power over a proposed transaction if it requires a certificate change and would reasonably be expected to adversely affect not only the Preferred Stock but also more broadly to "adversely affect" the holders of either the Preferred Stock or the common stock into which the Preferred is converted. The voting rights were so onerous and broad that Loral's outside counsel commented that because of those voting rights, he was "not sure [he could] ever give a legal opinion that any action is duly authorized."60

The Securities Purchase Agreement also provided that Loral's board would be expanded by one member and that MHR would have the right to nominate the director for that new vacancy.61

One final relevant section of the Securities Purchase Agreement, Section 5.01, provided that MHR would not object to the redemption of the Skynet Notes, the "very expensive" notes issued when Loral emerged from bankruptcy,62 if Loral engaged in a strategic transaction in excess of $600 million. As described above, the terms of the Skynet Notes provided that Skynet could redeem the Notes before 2009 so long as no more than two-thirds of the Noteholders objected. MHR owned enough of the Notes itself to enable it to unilaterally consent to an early redemption of the Notes.

G. The Four-Plus Months From Agreement On The Primary Terms To Signing The Securities Purchase Agreement — The Negotiation Of The Non-Financial Terms And The Supposed Market Check

The complex terms outlined were forged during negotiations after June 7 involving the Special Committee, primarily acting through King & Spalding and Targoff, who haggled on behalf of Loral with MHR over the non-financial terms of the MHR Financing. Having for all practical purposes committed to a transaction with MHR that would result in MHR controlling over 60% of Loral's equity, the Special Committee and Targoff worked industriously to avoid triggering Revlon and nibbled around the edges of how much control MHR would have over Loral.

59Certificates of Designation § VI(E)(iii).
60JX 383.
61§ 5.11.
62Tr. at 866 (Targoff).
It is important to view the delay in closing the transaction in context. MHR, not Loral, wanted the MHR Financing to take the form of preferred stock. And MHR set the baseline for both the terms and the scrivening of the Securities Purchase Agreement. The "[n]egotiations began by focusing on MHR’s term sheet and then moved to the negotiation of definitive documentation, drafted by Stroock, MHR's counsel." That complexities arose in such a transaction was unsurprising, given the size of the MHR Financing and the control issues involved.

But those complexities and resulting delay might, one would think, have inspired the Special Committee and its advisors to reconsider their monocular focus on obtaining financing from MHR. One of, if not the, primary reasons for choosing MHR was speed. Despite it becoming clear that the MHR Financing was not going to be closed within the "one week for the MHR convertible preferred stock [compared] to eleven weeks for the rights offering" that formed part of the basis for selecting the Financing from among the alternatives, the Special Committee never performed a serious market check of the financing alternatives. Instead, it was content to let King & Spalding, North Point, and Targoff haggle with MHR for more than four months.

Having obtained an additional four months to consider whether the MHR Financing really was the best source of available financing for Loral, the Special Committee and its advisors did nothing substantial to test their original rushed conclusion that hinged on the now questionable assumption that the MHR Financing could be closed much more quickly than any other alternative. The closest attempt at a market check was Jacquin making calls to two private investment funds. But North Point did not view that as important enough, or if one believes Jacquin, it was important but forgettable, to include in North Point’s "Market Check of Alternatives" portion of its final presentation to the Special Committee.

Making two calls to two funds is not a real market check. North Point did nothing of a professionally competent nature to assess the market’s interest.

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63JX 242 (email from Targoff to Art Simon stating that "[a]ny provision that limits [Loral’s] ability to take an action that [it] could have taken if [the Financing] had been common should be considered fair [bait] for negotiation" because the Financing "is preferred at [MHR’s] request, not for pricing benefit to the company").
64JX 549 at 11 (October 17, 2006 Special Committee Presentation recommending Financing to Loral's board).
65JX 250 (June 4, 2006 Special Committee minutes).
66See Tr. at 434-38 (Jacquin).
67See Tr. at 481-82 (Jacquin); JX 557 at 44.
Seeking to excuse this lack of a market check, the defendants have suggested that the Special Committee relied on Deutsche Bank's and Morgan Stanley's "indications" to North Point that the MHR Financing was the best option and that a public capital raise that would meet Loral's needs was unlikely. As to Deutsche Bank, this is a remarkable assertion as Deutsche Bank was MHR's financial advisor for the MHR Financing! Its objective, as its lead banker on the matter indicated, was to get the best deal for its client, MHR. Deutsche was hardly going to suggest subjecting its client's bid to a market check.

Moreover, the defendants distort both what Morgan Stanley told the Loral board and what it was authorized to do. Morgan Stanley never opined that the MHR Financing was the best option for Loral or that it was fair to Loral. Nor was Morgan Stanley ever empowered to actually explore whether there were preferable alternatives for Loral. All that Morgan Stanley told the Special Committee was that if Loral wanted, as Targoff said it did, $300 million in equity financing quickly, then a deal with MHR was the most "efficient" way to do that, in the sense that it was the fastest. Morgan Stanley expressly avoided giving any fairness opinion. In fact, as noted, early in the process, Morgan Stanley recommended a common stock offering combined with revolving lines of credit. But that was never pursued. And, in August 2006, when the primary terms of the MHR Financing were in place, Morgan Stanley proposed a $100 to $150 million public convertible preferred offering with primary financial terms that were better than the MHR Financing — a 5.25% to 5.75% coupon compared to 7.5% and a 20% to 25% conversion premium compared to 12%. But that proposal, like every other alternative, was rejected because it did not meet Loral's objectives as defined by Targoff and Rachesky.

Thus, the reality was that the Special Committee and its advisors never conducted a professional market check, and Loral never authorized Morgan Stanley to perform one.

Indeed, beyond not pursuing any serious market check, the Special Committee rebuffed an unsolicited inquiry from a Goldman Sachs'
Proprietary Investing Group. In September 2006, Goldman Sachs approached Loral "with the view towards a potential equity investment." Loral's management forwarded the information about Goldman Sachs' interest to North Point's Jacquin. Jacquin followed up with Goldman Sachs, but dismissed Goldman Sachs as a potential source of financing when he discovered that the particular Goldman Sachs group had a $100 million cap on individual investments.\(^{72}\)

That is, rather than perceiving the interest by Goldman Sachs in a potential $100 million equity investment as a sign that a real market check might result in the potential to raise capital on better terms and without deepening MHR's control, North Point and the Special Committee simply continued on their inertial path.

In particular, even after Goldman Sachs' inquiry and even after Morgan Stanley had suggested it could raise $100-150 million in the public equity markets, North Point and the Special Committee never actively considered another alternative that might have addressed the concerns about the ability of any individual investor (other than MHR) to fund the entire $300 million — assembling a group of Loral's institutional holders to either provide the financing themselves or backstop a public offering.\(^{73}\) That alternative would have taken advantage of one of Loral's unique features as a company that had recently emerged from bankruptcy — a relatively concentrated stockholder base of large institutions. It also would have leveraged Goldman Sachs' interest in making a substantial equity investment.

But that option was never considered. Likewise, North Point and the Special Committee never pressed MHR hard to backstop a public offering on its own or to do so in concert with a few well-known investment banks, say Morgan Stanley and Goldman Sachs. Rather, the Special Committee simply assented without protestation to MHR's contention that it would buy all or none, a stark position suggestive that MHR wanted a large opportunity all for itself. Without pitching even a fuss about this, North Point and the Special Committee simply locked into getting the financing from that conflicted source, Loral's controlling stockholder, MHR.

Although the defendants now say that a public offering would have been injurious to the Company as it would have signaled weakness, they admit that the Special Committee never sought to use the interest of Goldman Sachs, the presence of a stockholder base comprised heavily of institutional investors, and the ideas of Morgan Stanley to propose a public

\(^{71}\) JX 410.
\(^{72}\) Tr. at 431 (Jacquin).
\(^{73}\) Tr. at 417-18 (Jacquin).
offering that would have been a sign of strength — to wit, a public offering that gave all Loral stockholders a chance to participate, with the knowledge that a combination of MHR, Goldman Sachs, and potentially others would buy whatever shares were not purchased by Loral holders.

Admittedly, there can be no certainty that the pursuit of options of this kind (which could have come in various permutations) would have borne fruit. But, what is certain is that the Special Committee undertook no serious look at these or other market options from the time of its constitution on April 7 until it approved the Securities Purchase Agreement on October 17.

Even where there was activity, the Special Committee played a less than forceful role. The process of closing on the MHR Financing began to take shape in late September. By September 28, the Special Committee and North Point were prepared to recommend the MHR Financing. But Targoff wanted one final shot at improving some of the terms and the Special Committee gave him that opportunity. As it turns out, Targoff and not the Special Committee negotiated most of the terms of the MHR Financing, including the Change of Control Provision, the Make Whole, and the cash v. PIK feature of the dividend payments. This was in accord with the Special Committee's own sense that its most important tasks were already done by June. As the Special Committee itself saw it, the Special Committee's "key" meetings with MHR and its advisors were over, as they occurred on May 31 (introduction), June 7 (agreement on primary financial terms), and June 23 (discussion of Revlon issues). That is not to suggest that the Special Committee was not updated during the remainder of the process by staying informed about the negotiations, but the Special Committee members were largely passive after those first few meetings — meetings at which they, without a market check, quickly tunneled into consummating a deal with MHR and forewent any serious consideration of other alternatives.

As the terms of the MHR Financing were finalized, Targoff and Rachesky were the key negotiators. Internal King & Spalding correspondence the day before the terms of the MHR Financing were finalized discussed Targoff and Rachesky agreeing to various terms and stating that "[Targoff] is a lot closer than we are to the psychology of the negotiation."

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74JX 549 at 14 (October 17, 2006 Special Committee presentation recommending the Financing to Loral's board).

75In fact, it appears that the Special Committee's counsel was specifically excluded from certain negotiations, at the impetus of defendant Goldstein, until "the Company and MHR ha[d] resolved all open issues." JX 536 (October 13 email from Loral's Vice President to Loral's outside counsel).

76JX 542.
To the extent that the Special Committee was active in the negotiations, Harkey was the member involved.\textsuperscript{77} That is not to suggest that Simon did not participate in the Special Committee process by attending Special Committee calls, but he otherwise deferred entirely to Harkey and the Committee's advisors. That is evident in Simon's emails early in the negotiation process asking "What is happening???"\textsuperscript{78} and "I am wondering where we are headed."\textsuperscript{79} Later in the process, Simon went camping on a remote lake with no electricity for a one-month period beginning in late August. Simon took a six-mile boat trip for "a couple telephone meetings" during that time, but his involvement was clearly limited.\textsuperscript{80} Simon's emails and his role while he was camping at the lake are consistent with the impression that Simon gave at trial — someone who realized that he had responsibilities as a Special Committee member but who was content to simply show up by telephone at meetings when the Special Committee's advisors called for one. As a result, Simon was often unaware of or perplexed by the state of the negotiations.

Not only that, Harkey's relationship with MHR appears to have undercut the Special Committee's negotiation position. For example, in August 2006, as the negotiation process zeroed in on a final few key issues, Harkey forwarded MHR Managing Director and Loral board member Goldstein a copy of an email from King & Spalding to the Special Committee and North Point identifying the remaining open issues and summarizing the Committee's discussion of those issues, including its "fallback" position.\textsuperscript{81} Harkey told Goldstein to "give [the issues] some thought

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\textsuperscript{77}Tr. at 279 (Simon testifying that "on occasion I felt it more appropriate for [Harkey] to directly contact Hal Goldstein or Mark Rachesky, than myself, because he had dealt with these people over a period of time, knew them better."). The Special Committee minutes support the conclusion that, in general, Harkey was the only Special Committee member who ever engaged MHR himself. See, e.g., JX 290 (June 21, 2006 minutes stating that "Harkey provided an update on his discussions with Mark Rachesky and Hal Goldstein of MHR"); JX 309 (July 5, 2006 minutes stating that "Harkey reported that he and Mr. Targoff had spoken with representatives of [MHR] about the open financial terms relating to the proposed offering"); JX 340 (August 3, 2006 minutes stating that Harkey said that he, Goldstein, King & Spalding, and Stroock "had several discussions with a view to resolving the outstanding issues").

\textsuperscript{78}JX 214 (May 27, 2006 email, during the critical less-than-two-week period after North Point was hired and before the Special Committee formally decided that MHR was the best source for the financing, stating that Simon had "no knowledge of what is planned next").

\textsuperscript{79}JX 286 (June 15, 2006 email from Simon that further stated "[i]s the negotiation now between S&K [sic] and Strook [sic]? When (or should?) [Harkey] and/or I get involved in order to finalize this transaction . . . ?").

\textsuperscript{80}Tr. at 307 (Simon).

\textsuperscript{81}JX 353 (August 14, 2006 email from Harkey to Goldstein).
\end{flushleft}
and let's talk." Although Harkey maintained at trial that this was a cunning negotiation strategy and that the Special Committee was actually very happy with its fall-back position, there is no indication that Simon or the Special Committee's advisors were aware of Harkey's ruse. Likewise, at around that same time, Harkey joined Goldstein and Stroock, MHR's legal advisor, in a telephonic meeting that was a "strategy session for how to approach [King & Spalding]."

Harkey's close relationship with MHR was evidenced by the fact that he was personally soliciting investments from MHR late in the negotiation process. In early September 2006, Harkey emailed an MHR analyst proposing that MHR invest $30 million for a 40% stake in Joe's Crab Shack, a potential investment that Harkey's company, Consolidated Restaurants, was pursuing. Harkey told MHR that "[i]f we can slide into this one, it is exciting." Approximately a month later and only weeks before the Securities Purchase Agreement was signed, Harkey sought a $40 million investment by MHR in his own company. The discussion, modeling, and due diligence over MHR's potential investment in Harkey's company spanned a time within which the Securities Purchase Agreement was signed and involved a trip to the offices of Harkey's company in Dallas by an MHR analyst. Consistent with the reality that Rachesky, Targoff, and Harkey were all enmeshed in financially and personally advantageous relations with each other, Targoff also solicited an investment, albeit a much smaller one, from both Rachesky and Harkey as the terms of the MHR Financing were being finalized. In mid-September, Targoff emailed Rachesky and Harkey to

82 Id.
83 See Tr. at 95-98. Harkey first denied this at trial and then equivocated by saying that although he was presenting the investment opportunity to MHR, his company was not contemplating an investment in Joe's Crab Shack. The record suggests otherwise, including testimony by Jacquin that Harkey's company was interested in buying Joe's Crab Shack and that Harkey told him that he had discussed the deal with four or five groups, including MHR. Tr. at 520-21.
84 JX 409 (emphasis added).
85 See, e.g., JX 501 (October 4, 2006 email from Harkey to an MHR analyst with a "Buyout Model" for his company); JX 515 (October 10, 2006 email from the CFO of Harkey's company to an MHR analyst discussing a due diligence list); JX 602 (October 23, 2006 financial model of Harkey's company that was updated by an MHR analyst and included a line item for "MHR Financing").
86 Like the Joe's Crab Shack solicitation, Harkey also denied this at trial and stated that he was only seeking advice from MHR on how to structure the financing. Tr. at 129. But again, the overwhelming weight of evidence suggests otherwise. See, e.g., Capers Dep. at 29-30 (King & Spalding attorney stating that after the closing of the MHR Financing Harkey told him that he had solicited MHR to invest in his company).
consider joining him and "a couple of friends" in a promising investment opportunity. All very chummy.

By the middle of October, Targoff and Rachesky had finalized the terms of the Financing. On October 17, 2006, the Special Committee recommended the MHR Financing to Loral's board and North Point finalized its opinion that the MHR Financing was fair. Just a few weeks before, Loral received an invitation to bid in an auction for Telesat, and immediately began putting its bid package together. The day after the Securities Purchase Agreement was signed, Loral put in its first bid for Telesat.

H. The Securities Purchase Agreement Is Met With Outrage From Loral Stockholders

Loral announced the signing of the Securities Purchase Agreement on October 17, 2006 and trumpeted the financing as facilitating "both internal and external growth opportunities." Within a matter of days, plaintiffs Highland Capital and Murray Capital wrote letters questioning the fairness of the MHR Financing. Highland Capital informed the Special Committee that it proposed to offer the same $300 million investment "under improved economic terms."

Eventually, the Special Committee responded by suspending its recommendation of the MHR Financing. Loral issued a press release announcing that determination, a press release that suggested that the Special Committee would be considering alternatives to the MHR Financing, including requesting that MHR consider proposing an alternative that would allow all interested stockholders to participate. In response, MHR did propose a rights offering, but MHR refused to backstop the rights offering and demanded a fee for the termination of the original MHR Financing. And MHR soon pulled the rights offering from the table after Loral's stock price materially increased in December. The Special Committee never authorized North Point or Morgan Stanley to contact Highland Capital or to otherwise perform a market check.

The reason for the sharp spike in Loral's stock price was that on December 18, 2006, Loral announced that it entered a transaction to acquire
Telesat, the Canadian FSS provider, from BCE. As noted, from the time the Special Committee was formed, Loral had been exploring a potential deal involving Telesat. Although Telesat was not committed to a sale as of Spring 2006, its CEO had tipped Targoff to his support for a deal with Loral and Morgan Stanley was retained to help Loral land a deal with them. By late-September, before the MHR Financing was finalized, Telesat had decided to conduct an auction. And, as noted, Loral entered its first bid in the auction for Telesat on October 18, 2006, only a day after the Securities Purchase Agreement was signed. After several rounds of bidding, Loral prevailed in the auction process. The Telesat transaction was designed to comply with Canadian communications law requiring that a Canadian satellite company must be controlled by a Canadian investor, and therefore involved a joint venture between Loral and its Canadian partner, the Public Sector Pension Investment Board (PSP). PSP was a critical part of the Telesat transaction and was brought into the transaction by MHR, with whom PSP had a pre-existing investment relationship. The joint venture retained the Telesat name and consisted of the former Telesat assets and Loral Skynet. Loral acquired a 64% equity interest in the joint venture, but only a 33.3% voting interest. According to BCE, Telesat's former owner, the MHR Financing was "very important" to the success of Loral's bid for Telesat because it made Loral's bid credible.93

Shortly after the Telesat deal was announced, and still facing a suspended Special Committee recommendation, MHR proposed an amendment to the Securities Purchase Agreement slightly lowering the coupon rate and increasing the conversion premium.94 But MHR soon withdrew that proposal because of complications it would create with the NASD. As a firm with stock listed on the NASDAQ, Loral needed stockholder approval to issue securities convertible into 20% or more of the common stock if those securities were issued at or below the greater of the market price or the book value. In essence, Loral and MHR could not agree to a similar financing with slightly improved terms because that new financing would be tested against the then-current Loral stock price and trigger the stockholder approval requirement. Loral and MHR knew that the stockholders would not approve a new proposal with only slightly improved terms,95 and as a result, MHR withdrew that proposal.

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93Tr. at 395 (Smith).
94Tr. at 88 (Harkey).
95Tr. at 849 (Targoff); Tr. at 1329 (Rachesky). Loral's stockholders would not approve a similar financing with only slightly improved terms because closing the MHR Financing without materially changing the conversion premium to reflect Loral's increased stock price would result in a
Moreover, the NASD concluded that the same stockholder approval requirement was triggered by the terms of the original MHR Financing because of the manner in which the Make Whole provision functioned. But, the NASD took the position that if the parties amended the original MHR Financing to pay the Make Whole upon a Change of Control in non-voting common stock rather than common stock, they could avoid the stockholder vote requirement. Thus, the Special Committee and Loral had the option of agreeing to modify the Make Whole and proceeding with the MHR Financing or refusing to modify the Make Whole and thus effectively terminating the Securities Purchase Agreement.

The Special Committee and Loral were concerned about the possibility of being sued by MHR — Loral's controlling stockholder — if they refused to modify the Make Whole and close on the MHR Financing. The Securities Purchase Agreement provided that a condition precedent to the obligation to close was either NASD confirmation that stockholder approval was not required or stockholder approval. The Securities Purchase Agreement did require Loral to use "reasonable best efforts" to secure NASD approval, but the best efforts section of the Agreement also made clear that the parties were not required to consummate the transaction on "materially different" terms. Most important, the Securities Purchase Agreement made clear that nothing in the best efforts section of the Agreement required any party to amend the Agreement. But there was uncertainty in the minds of the Special Committee's advisors about whether Loral could be required to amend the terms of the Securities Purchase Agreement in a way that was either immaterial or not adverse to Loral. Ultimately, despite some internal firm correspondence suggesting a different outcome, King & Spalding advised the Special Committee that if Loral refused to modify the contract and MHR sued, a court would "most likely" require Loral to accept the amendment to the Make Whole required by the NASD if the MHR Financing were to be consummated without stockholder

huge immediate profit for MHR. Between January 1, 2007 and February 27, 2007, Loral's stock traded in the ballpark range of $10 to $20 over the original conversion price. Targoff estimated that at that time MHR already had a $200 million profit on the $300 million MHR Financing. Tr. at 848.

96Securities Purchase Agreement § 4.01(h).
97Id. § 5.13(b).
98Id. § 5.13(d) ("Notwithstanding anything to the contrary herein, nothing in this Section 5.13 shall require any party to amend this Agreement or to waive or forbear from exercising any of its rights or remedies hereunder.").
99JX 1400.
Loral's outside counsel concurred with King & Spalding's advice.\textsuperscript{101}

The Special Committee thus conceded and agreed to amend the Securities Purchase Agreement to obviate a stockholder vote and to go forward with the MHR Financing on the original terms. On February 27, 2007, the Special Committee, North Point, and the Board of Directors all affirmed that the amendment to the Securities Purchase Agreement did not change their conclusions that the MHR Financing was fair \textit{as of} October 17, 2007.\textsuperscript{102} The result was that Loral completed the MHR Financing on February 27 and announced that it had done so.\textsuperscript{103}

That was a surprising development to Loral's non-MHR stockholders and other interested parties, who had been led to believe by Loral that the Special Committee had been seriously considering alternatives to the MHR Financing that would allow interested stockholders to participate. But that was not really the case because MHR abandoned any consideration of allowing others to participate after the Telesat transaction became public, if not sooner, and the Special Committee yielded rather easily to that demand.

\section*{III. Legal Analysis}

The plaintiffs argue that the MHR Financing was grossly unfair to Loral, and resulted from fiduciary misconduct by the Loral directors. The plaintiffs contend that the Special Committee bent to the will of MHR, allowing it the chance to increase its ownership stake to 63\textsuperscript{%}\textsuperscript{104} and to obtain an iron grip over the Company's future, on terms that were unfavorable to Loral. Because MHR had effective control of the Loral board, the plaintiffs argue that MHR has the burden of showing that the MHR Financing was fair to Loral.

For their part, the defendants argue that the MHR Financing was a fair method of providing Loral with sorely needed capital. They contend that the record proves that there was no other source of capital that would have provided Loral with what it needed on better terms or in the time frame it required. Not only that, the defendants argue that Loral's and MHR's prior admissions in SEC filings that MHR was Loral's controlling stockholder

\textsuperscript{100}JX 968 (February 26, 2007 Special Committee minutes).
\textsuperscript{101}Tr. at 847 (Targoff).
\textsuperscript{102}JX 978 (February 27, 2007 board minutes); JX 984 (February 27, 2007 Special Committee minutes).
\textsuperscript{103}JX 994 (Loral February 27, 2007 8-K).
\textsuperscript{104}This figure includes the PIK dividends that Loral is obligated to pay MHR for the first 17 quarters of the deal. On the day the MHR Financing closed, MHR had a 57\textsuperscript{%} equity stake.
were imprecise, non-binding statements. Because MHR only had 35.9% of the vote, the defendants contend that the entire fairness standard is not the right metric.

In the remainder of this opinion, I address these competing positions, beginning with the question of what standard of review applies.

A. The Entire Fairness Standard Applies

The defendants' contention that the entire fairness standard does not apply is made in a half-hearted way, and for good reason. Although much of the parties' back-and-forth about the applicability of that standard focuses on whether MHR was a controlling stockholder, a more mundane reality should not be overlooked. As pointed out earlier, MHR itself told the world that a majority of the Loral board was affiliated with MHR. MHR directly controlled three of Loral's eight directors, defendants Rachesky, Goldstein, and Devabhaktuni. Furthermore, two additional Loral directors, the two directors most responsible for negotiating the MHR Financing, Special Committee Chairman Harkey and CEO Targoff cannot be deemed to be independent of MHR. Targoff was made CEO largely at MHR's instance, going straight from MHR's rent-free tenant and "advisor" to Loral's CEO, and brought with him a plan to have MHR substantially deepen its investment in Loral. Given MHR's "control" position and "dominant role" at Loral, Targoff knew that his continuance as CEO depended in large measure on keeping in MHR's good graces. Not only that, Targoff and Rachesky were so close that Targoff felt free to seek having Rachesky (and Harkey) invest with him and other "friends" in an opportunity that arose during the Special Committee process.

Likewise, Harkey cannot be considered as independent of MHR. His business and personal ties to MHR and Rachesky are too material, as is evidenced by Harkey's status alongside Targoff as one of MHR's "Selected Investment Advisors." Harkey and Rachesky were business school classmates and remain close friends. Harkey was on the boards of three public companies precisely because of his relationship with MHR and Rachesky. Like Targoff, Harkey solicited investments in both his own company and another potential transaction from MHR during the Special Committee process. Beyond just the close personal and professional relationships with MHR and Rachesky, Harkey and Targoff were aware that

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105 JX 45 at 1-2.
106 JX 1222 at 29.
107 Id. at 21.
MHR knew how to use its clout to get its way. After all, they were both advisors to MHR, a firm that, as noted, boasted that it "is unusually well-positioned to extract significant control premiums through [among other things] bringing to bear the Managing Principals' wealth of knowledge and experience in effectuating control and influence."  

Thus, regardless of whether MHR was a controlling stockholder of Loral, the MHR Financing was an interested transaction, and a majority of the Loral board – five of the eight members at the time the Securities Purchase Agreement was signed – was affiliated with MHR. Given that reality, the entire fairness standard presumptively applies. 

Moreover, MHR's belated protestations that it was not a controlling stockholder after all are not convincing. In determining whether a blockholder who has less than absolute voting control over the company is a controlling stockholder such that the entire fairness standard is invoked, the question is whether the blockholder, "as a practical matter, possesses a combination of stock voting power and managerial authority that enables him to control the corporation, if he so wishes." MHR possessed such practical power over Loral, and that power shaped the process for considering and approving the MHR Financing.

Outside of this litigation, MHR and Loral have consistently and publicly maintained that MHR controls Loral. Moreover, even at trial, Targoff admitted that he "would use [the] term" controlling stockholder to describe MHR and that MHR "control[s] de facto in some respects." These admissions comport with the facts regarding MHR's practical power over Loral.

MHR seated a majority of Loral directors affiliated with itself, and touted that fact publicly. Rachesky assumed the Chairmanship himself and was also a member of the two-person Compensation Committee. He installed his MHR advisor Targoff as CEO. With 36% of the votes, MHR hardly feared a proxy fight, and although it did not have the power to

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108 Id. at 3.
109 The entire fairness standard applies where a majority of the board is interested or lacks independence from the interested party. See, e.g., Rales v. Blasband, 634 A.2d 927, 936 (Del. 1993); Aronson v. Lewis, 473 A.2d 805, 815 (Del. 1984); Orman v. Cullman, 794 A.2d 5, 22-23 (Del. Ch. 2003); see also R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS §4.16[A] (2008).
110 See, e.g., Kahn v. Lynch Commc'n Sys., Inc., 638 A.2d 1110, 1116-17 (Del. 1994); Kahn v. Tremont Corp., 694 A.2d 422, 428-29 (Del. 1997).
111 In re Cysive S'holders Litig., 836 A.2d 531, 553 (Del. Ch. 2003).
112 Loral's financial advisor, Morgan Stanley, put it well, considering MHR to have "effective control" over MHR. Brail Dep. at 126.
113 Tr. at 901.
unilaterally vote in charter changes or effect a merger, it had substantial blocking power.¹⁴ Not only that, MHR had blocking power over Loral's ability to redeem the Skynet Notes and had at least some power to control Loral's ability to conduct an underwritten offering for its own benefit. Both factors played a role in shaping the negotiation of the MHR Financing.

And at the level of basic strategy, it is evident that MHR controlled Loral's decision to pursue the growth strategy that necessitated additional capital financing and the time table for obtaining that capital.

Indeed, early on in the process, when Rachesky and Targoff were causing Loral to embark on the process of considering a large equity investment in MHR, the Loral board recognized that the interested nature of the transaction and MHR's clout would likely subject any resulting transaction to entire fairness review.¹¹⁵ To address that, the Special Committee was formed with the hope that that device would, at the very least, shift the burden of persuasion as to the issue of fairness.

Given MHR's practical control over Loral and the presence of an MHR-affiliated board majority, I therefore have little difficulty in concluding that the entire fairness standard applies in the first instance to the MHR Financing. Furthermore, given the performance of the Special Committee, there is no need to consider some of the more intricate, interstitial standard of review issues that might have arisen had the Special Committee process been less desultory.¹¹⁶

Rather, I turn directly to the question of whether MHR Financing was fair to Loral.

B. The Defendants Have Not Met Their Burden To Prove That The MHR Financing Was Fair

The familiar entire fairness standard requires the court to consider two factors: fair dealing and fair price.¹¹⁷ But the test for an entire fairness is not "bifurcated . . . between fair dealing and price. All aspects of the issue must

¹¹⁴Defs.' Pre-Trial Op. Br. at 15 ("It was unrealistic to believe that Loral could obtain shareholder approval for a rights offering without MHR's consent.").
¹¹⁵See JX 75; JX 97 at 3.
be examined as a whole since the question is one of entire fairness."\textsuperscript{118} Although the relationship between process and price in coming to the ultimate fairness determination is fraught with some imprecision, this case is a good illustration of the relationship between the process used to effect a transaction and the defendants' ability to meet their burden to demonstrate financial fairness. When the process used involves no market check and the resulting transaction is a highly unusual one impossible to compare with confidence to other arms-length transactions, the court is left with no reasoned basis to conclude that the outcome was fair.

1. Fair Dealing

The fair dealing inquiry is fact intensive and "embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."\textsuperscript{119} The critical issue here is whether the Special Committee functioned as an effective proxy for arms-length bargaining, such that a fair outcome equivalent to a market-tested deal resulted.\textsuperscript{120} An effective special committee "must function in a manner which indicates that the controlling shareholder did not dictate the terms of the transaction and that the committee exercised real bargaining power 'at an arms-length.'\textsuperscript{121}

That did not happen here. I reach this conclusion for several reasons. For starters, the composition of the Special Committee was flawed. Harkey was poorly situated to be a Special Committee Chairman, a position that, if done well, forced him to push back hard against his close friend, Rachesky, and Rachesky's firm, MHR, but which Harkey in fact never did. Even if I could put aside Harkey's less than straightforward trial testimony regarding his knowledge that he was publicly listed as one of MHR's Selected

\textsuperscript{118}Id.
\textsuperscript{119}Id.
\textsuperscript{120}See, e.g., Lynch, 638 A.2d at 1120-21 ("Particular consideration must be given to evidence of whether the special committee was truly independent, fully informed, and had the freedom to negotiate at arm's length."); In re Trans World Airlines, Inc. S'holders Litig., 1988 WL 111271, at *7 (Del. Ch. Oct. 21, 1988) ("[A] special committee [should act as a] surrogate for the energetic, informed and aggressive negotiation that one would reasonably expect from an arm's-length adversary.").
\textsuperscript{121}Kahn v. Tremont, 694 A.2d 422, 429 (Del. 1997); see also Perlegos v. Atmel Corp., 2007 WL 475455, at *16 n.119 (Del. Ch. Feb. 8, 2007) ("[S]pecial committees have not been viewed as 'independent' where, for example, they lacked any negotiating power, where members' independence was materially affected because they stood to benefit in some form, or where they were so dominated or manipulated by self-interested fiduciaries that their independence was mere fiction.").
Advisors when he accepted the role of Special Committee Chairman\(^\text{122}\) and his efforts to get MHR to invest in Joe's Crab Shack as well as his own company, Consolidated Restaurants, during the process,\(^\text{123}\) his relationships with Rachesky and MHR were too substantial to make him a fit member of the Special Committee, much less Chairman. Likewise, Harkey never informed his fellow Committee member, Simon, or its advisors that he was forwarding its internal communications to MHR, including its fallback position on a key negotiating point.

And Harkey's fellow member, Simon, brought the scientific concept of inertia to the Special Committee by generally remaining at rest until set into motion by the Committee's advisors. As the Delaware Supreme Court has explained, in the context of a special negotiating committee, "courts evaluate not only whether the relationships among members of the committee and interested parties placed them in a position objectively to consider a proposed transaction, but also whether the committee members in fact functioned independently."\(^\text{124}\) Simon was undoubtedly in a difficult position as the second member of a Special Committee led by a conflicted Chairman negotiating with a controlling stockholder.\(^\text{125}\) But Simon's generally passive approach did not help. The record reveals that Simon was confused about the status of key issues at several points throughout the process. Although Simon lacked any conflicting ties to MHR, he demonstrated neither the knowledge nor the inclination to prod Harkey and the Special Committee's advisors toward an effective and aggressive strategy to ensure Loral got a fair deal.

\(^{122}\) See Tr. at 98-113.

\(^{123}\) As this court has stated, "independence is the sin[e] qua non of the entire negotiation process." Gesoff v. IIC Industries, Inc., 902 A.2d 1130, 1146 (Del. Ch. 2006). The Special Committee members were put on notice of this bedrock principle in a memo from the Special Committee's legal advisors explaining that "[t]he effectiveness of the Committee's work is utterly dependent on its members' complete independence and good faith." JX 182 (May 17, 2006 memo from King & Spalding to the Special Committee). That memo also asked the directors to disclose any relationships with Rachesky or MHR. At that nascent stage of the Special Committee, Harkey informed the Special Committee that he had a relationship with Rachesky, but did not disclose the full extent of that relationship, including that he had agreed to be an MHR advisor. Tr. at 113 (Harkey). Harkey also never disclosed to Simon or the Special Committee's advisors that he was soliciting investments from MHR as the terms of the MHR Financing were being finalized. A Special Committee is supposed to inspire judicial confidence about the integrity of decisionmaking in a conflict setting, not undermine it.


\(^{125}\) Cf. Gesoff, 902 A.2d at 1146 ("[I]n those rare circumstances when a special committee is comprised of only one director, Delaware courts have required the sole member, 'like Caesar's wife, to be above reproach.'") (quoting Lewis v. Fuqua, 502 A.2d 962, 967 (Del. Ch. 1985)).
Second, the Special Committee's financial advisor was outgunned and outwitted. As this court has observed on numerous occasions, the "effectiveness of a Special Committee often lies in the quality of the advice its members receive from their legal and financial advisors." Here, the Special Committee chose a financial advisor that was not qualified to swim in the deep end. That was evident from the start, where the Special Committee questioned North Point's expertise in convertible securities and North Point promised that it would work with an expert (which it never did) and Loral's general counsel suggested that the Special Committee hire a more prominent investment bank. The work performed by North Point bore out those concerns.

North Point did no market check before advising the Special Committee to agree to the basic economic terms of the MHR Financing on June 7, a mere eleven days after being hired. After that, North Point remained inactive, claiming to make two phone calls to gauge interest, but never undertaking or seeking the mandate to undertake the kind of market search that an effective investment bank would have. Indeed, North Point seemed to lean on MHR's bank, Deustche Bank, as providing a reasonable basis for being so passive and not seeking to engender market competition.

As or even more troubling was that North Point seemed intent on making the MHR Financing appear more fair rather than providing an objective opinion to the Special Committee and helping the Special Committee use any leverage it had to strike a better deal for Loral and its non-MHR stockholders. For example, Jacquin told a North Point associate to exclude revenue multiples, which increased Loral's enterprise value, from the financial analysis in North Point's presentation to the Special Committee because "[w]e need to make this appear to be more fair." North Point's discounted cash flow valuation of Loral also included a subjective 5%
company specific risk premium, which was made by Jacquin without any basis in academic theory or market returns, and which had the effect of inflating Loral's weighted average cost of capital, thereby decreasing North Point's DCF valuation and making the MHR Financing appear to be a better deal. Likewise, Jacquin undermined Targoff during the negotiations by telling Deutsche Bank that he would not refuse to give a fairness opinion because of a particular issue when Targoff was using that possibility as leverage to get a better deal from MHR. This behavior echoed Harkey's behavior in undermining Loral's leverage by giving MHR negotiators information about Loral's side of the table that MHR should not have had.

Regrettably, the ineffectiveness of North Point was not overcome by the presence of transactional lawyers with a large strategic view of their role as counsel. The Special Committee had technically effective counsel from a well-respected firm, but that counsel did not help overcome the lack of any strategic thinking by either North Point or the Special Committee itself. In fact, counsel's role leads to the next factor that undermined the effectiveness of the Special Committee.

That factor was the Special Committee's cramped view of its mandate. From inception, the Special Committee was told, without any substantial basis, that it had to get $300 million in equity financing and get it quick. As noted previously, this goal set by Targoff and Rachesky actually suggested that the Special Committee consider a very broad mandate, which was the possibility of a sale of the entire company. After all, if Loral needed that much equity capital, an amount well over half of its market capitalization, and had positive uses for it that presented the potential for increased profits, why not explore a hot market?

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129Tr. at 541 (Jacquin); JX 557 at 77 (October 17, 2006 North Point presentation); see Gessoff, 902 A.2d at 1158 ("This court has also explained that we have 'understandably . . . suspicious of expert valuations offered at trial that incorporate subjective measures of company-specific risk premia, as subjective measures may easily be employed as a means to smuggle improper risk assumptions into the discount rate so as to affect dramatically the expert's ultimate opinion on value."") (quoting Solar Cells, Inc. v. True N. Partners, 2002 WL 749163, at *6 (Del. Ch. Apr. 25, 2002)).

130The point in question dealt with Targoff's attempt to gain more flexibility for Loral in deciding whether to pay MHR dividends in cash or in PIK. Jacquin told Deutsche Bank that North Point's fairness opinion would not "hinge on pik vs cash" but that he would "prefer to have better optics if possible (e.g. cash option if certain conditions are met, but those conditions can be almost impossible to meet)." JX 1394 (July 12, 2006 email from Deutsche Bank to Rachesky and Goldstein). Jacquin asked Deutsche Bank not to tell Loral about the conversation because Targoff was unhappy about the mandatory PIK feature of the MHR Financing and was attempting to use the fact that North Point would not give a fairness opinion if the mandatory PIK feature was part of the MHR Financing as leverage to improve that term. Tr. at 1081 (Sung of Deutsche Bank).
This sort of thinking should have come to mind for an obvious reason: MHR was anxious to put in a large amount of capital. MHR is not a charity. It wanted to invest to make money. But the Special Committee never seemed to grasp this, at any time in the process, and never sought to engender any sort of market competition, choosing only to manage as a legal matter, the "Revlon" implications of such a large sale of equity, rather than to respond to the realities as an aggressive negotiator seeking advantage would have.

Likewise, the Special Committee hewed very literally to what it was told by MHR and Targoff. The Special Committee had to get $300 million fast because that is what it was told. Thus, instead of doing any market check, it quickly cut a deal with MHR on key economic terms. Then, when the process dragged on, it never used that delay as a chance to actually explore the market. And even when the market came to it with credible options (e.g., Goldman Sachs), it brushed them aside as not literally meeting the $300 million target, without any thought given to how $100 million, for example, might be a useful start to an alternative package that would put pressure on MHR to come up with better terms.

Even as to the $300 million, the record is devoid of any convincing evidence as to the magic or business logic of that number. The record reveals that Loral needed capital, but its own very experienced banker, Morgan Stanley, outlined ways to meet its most important capital needs that did not require that a single buyer acquire $300 million in equity. From this record, the only magic of the $300 million in equity that emerges is that it had the intended effect of narrowing the Special Committee's focus to a deal with MHR only and causing the Special Committee to eschew any consideration of raising capital of a lesser amount, raising that amount by a different means, or even being more assertive and seeking a buyer for the whole company. Hence, the result. A Special Committee that was formed in early April and did not hire a financial advisor until May 23, used a month and a half to do nothing. Then it cut the key economic terms of a deal eleven days later with no market check. Then, when things dragged on another three months, it never used the time to widen its perspective and market test its assumptions.

The Special Committee's tunnel vision undoubtedly played into the last factor I consider, which is the less-than-intrepid manner in which it approached its assignment. Whenever the Special Committee or its advisors had an opportunity use leverage it had or create additional leverage, they
found a way to avoid doing so. The Special Committee and its advisors largely explain this by saying that any different course of conduct was inconsistent with the need, set by Targoff and Rachesky, to get $300 million in equity financing and fast. But, as noted, the exacting specificity of that need to meet a five-year "wish list" of various items put together by Targoff was unsubstantiated and went unchallenged by the Special Committee, even when the time frame stretched out. Instead, the Special Committee simply continued to reject any exploration of alternative options at all, not even bothering to see where they might lead, even when getting $300 million quickly had turned into getting $300 million rather deliberately.

This timidity is not behavior that provides assurance that MHR was confronted with the sort of pressures it would have faced in a market-tested deal negotiated at arms-length. Had the Special Committee and its financial advisor acted with a truly independent mindset — the mindset necessary to serve as an effective proxy for arms-length bargaining and an effective special committee process — it might have questioned a mandate that foreclosed any alternative other than the MHR Financing. This should be especially true here, where Loral's experienced and long-time investment bank, Morgan Stanley, recommended alternatives that differed from the Special Committee's narrow mandate. And had the Special Committee bothered to inquire into the oddly precise nature of Loral's capital needs, it might have discovered that, as Targoff explained at trial, "[he] needed equity, not for operations" but rather for "growth" and "the sooner the better, as far as [he] was concerned, but there was no deadline." In other words,

131 Cf. Paramount Communications, Inc. v. QVC Network, Inc., 637 A.2d 34, 51 (Del. 1994) ("QVC's unsolicited bid presented the opportunity for significantly greater value for the stockholders and enhanced negotiating leverage for the directors. Rather than seizing those opportunities, the Paramount directors chose to wall themselves off from material information which was reasonably available and to hide behind the defensive measures as a rationalization for refusing to negotiate with QVC or seeking other alternatives.").
132Tr. at 700 (Townsend).
133 See, e.g., Tr. at 40-41 (Harkey stating that the Special Committee rejected Morgan Stanley's April recommendation of a public common stock offering because "[i]t wasn't for $300 million); Tr. at 170 (Harkey stating that the Special Committee rejected Morgan Stanley's August recommendation of a smaller public convertible preferred stock offering because it "did not meet the objectives"). Moreover, Jacquin used the $300 million size to rebuff Goldman Sachs' inquiry about a smaller investment by telling Goldman: "That's interesting. We're actually pursuing equity that's in excess of that. It's actually in excess of hundreds of millions of dollars." Tr. at 431. Jacquin used the same "in excess of hundreds of millions of dollars" refrain when he pitched the Loral investment to two private investment funds using nothing other than his oral statements that Loral had a "great trajectory." Tr. at 436.
134Tr. at 487 (Jacquin acknowledging that "[a]s the negotiations [with MHR] became complicated, that did not change [his] view that perhaps [he] should try to talk to other groups").
135Tr. at 791-92.
this was not a situation where Loral needed the financing to escape an impending bankruptcy or some other type of emergency that might justify paying a "high price" and not fully exploring all the available options.\textsuperscript{136}

The Special Committee also explains its torpor by reference to its concern that MHR would walk away if the Committee complicated the process by generating different alternatives to a deal solely with MHR.\textsuperscript{137} But where was MHR going? The idea of a large infusion of capital was generated at MHR itself, when Targoff was still there, and largely inspired by MHR's belief that Loral had positive investment opportunities. Admittedly, MHR had declined to make an investment to fund the New Skies transaction, but that was at a time when it was at odds with Loral's former CEO. But, by 2006, MHR had installed Targoff, its advisor and the individual responsible for its original investment in Loral, as CEO, with a strategy going in that involved an infusion of capital into Loral to fuel growth. Would MHR, as owner of 35.9\% of Loral's equity, ultimately decide not to finance the growth opportunities that supposedly required $300 million in equity simply because the Special Committee insisted on searching the market to make sure it was getting the best terms? We will, of course, never know because the Loral Special Committee and its advisors never had the gumption to give it even the weakest of tries.

Sadly, by the end of the negotiation process, it appears that Loral's CEO, Targoff, was a more aggressive negotiator than the Special Committee itself or the Committee's financial advisor, North Point. By that stage, Harkey, Simon, and North Point seemed willing to sign off on terms that were more advantageous to MHR than Targoff himself wanted to accept. This was exemplified by the unedifying behavior of Harkey and North Point in sharing information with MHR negotiators that undercut others, including Targoff and King & Spalding, who were negotiating for Loral.

After the Securities Purchase Agreement was signed on October 17, the Special Committee was confronted with final and unexpected opportunities to use leverage against MHR to obtain better terms for the MHR Financing. Again, it squandered those opportunities. Although the Special Committee suspended its positive recommendation of the MHR Financing after Highland Capital and Murray Capital objected to the MHR Financing and publicly said it would explore alternatives that would allow interested stockholders to participate in the financing, it never seriously did so. The Special Committee never even followed up on Highland Capital's offer of

\textsuperscript{136}Zahler Dep. at 99 (Loral President and COO Eric Zahler explaining that his view on the final conversion price and coupon was that "we paid a high price").

\textsuperscript{137}Tr. at 363 (Simon).
the same financing with improved economic terms by, for example, requesting a term sheet from Highland Capital. Nor did it engage North Point or a better equipped bank to seek out alternatives.

And, when the NASD stockholder approval requirement triggered the need to amend the Securities Purchase Agreement at a time when MHR had an approximate $200 million gain on the Financing, the Special Committee shied away from using the uncertainty about whether it was required to amend those terms as leverage against MHR.\textsuperscript{138} The Special Committee was concerned that Loral might lose a lawsuit against it by MHR if it refused to amend the Securities Purchase Agreement. But why the great fear? MHR would have had to seriously consider the unedifying spectacle of a company's controlling stockholder suing its Special Committee because the Special Committee refused to amend a contract and thereby deprive the stockholders of a vote on the deal. Moreover, the likely relief sought by MHR would have been specific performance. In that scenario, MHR and not the Special Committee seems to have had the most to lose.

In saying this, I am fully cognizant that it is easy to focus on a discrete aspect of any Special Committee process and find a reason to be critical. I do not point to specific examples of this process because any one of them, in isolation, is dispositive. But it is the sheer accumulation of examples of timorousness and inactivity that contributes to my conclusion that this Special Committee did not fulfill its intended function. When, over the course of nearly a year, there appears to be no instance in which the Special Committee took any of the numerous opportunities available to it to explore the marketplace and determine whether it could obtain better terms than were available from the controlling stockholder, MHR, it is impossible for me to conclude that the Special Committee acted as an effective guarantor of fairness.

2. Fair Price

MHR, with support from its fellow defendants, attempts to meet its burden to prove fairness principally by arguing that it, MHR, was the only source of capital in town, was taking a very high risk, and therefore deserved compensation for that risk. For their part, the plaintiffs have rested their

\textsuperscript{138}Cf. \textit{QVC}, 637 A.2d at 50 ("The Paramount directors had the opportunity in the October 23-24 time frame, when the Original Merger Agreement was renegotiated, to take appropriate action to . . . improve the economic terms of the Paramount-Viacom transaction. . . . Nevertheless, the Paramount Board made no effort to eliminate or modify these counterproductive devices, and instead continued to cling to its vision of a strategic alliance with Viacom.").