Unreported Cases

INTRODUCTION

UNREPORTED CASES is a continuing feature of the DELAWARE JOURNAL OF CORPORATE LAW. Select unreported cases of a corporate nature that have not been published by a reporter system are included. The court's opinions and memorandum opinions are printed in their entirety, exactly as received.

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IN RE DIAMOND FOODS, INC. DERIVATIVE LITIGATION

No. 7657-CS

In the Court of Chancery of the State of Delaware

February 28, 2013

Blake A. Bennett, Esquire, and Gregory F. Fischer, Esquire, of Cooch and Taylor P.A., Wilmington, Delaware; Mitchell M.Z. Twersky, Esquire, Lawrence D. Levit, Esquire, and Atara Hirsch, Esquire, of Abraham, of Fruchter & Twersky, LLP, New York, New York; and Francis A. Bottini, Jr., Esquire, and Albert Y. Chang, Esquire, of Bottini & Bottini, Inc., San Diego, California, Attorneys for Plaintiffs David A. Lucia and Board of Trustees of City of Hialeah Employees' Retirement System.

R. Judson Scaggs, Jr., Esquire, Susan W. Waesco, Esquire, Angela C. Whitesell, Esquire, and Frank R. Martin, Esquire, of Morris, Nichols, Arsht & Tunnell LLP, Wilmington, Delaware; and Dean Kristy, Esquire, Susan S. Muck, Esquire, and Jennifer C. Bretan, Esquire, of Fenwick & West LLP, San Francisco, California, Attorneys for Nominal Defendant Diamond Foods, Inc.

STRINE, *Chancellor.*

Two derivative plaintiffs, an individual and a pension fund, filed a derivative suit in this court against the directors and officers of Diamond Foods, Inc. ("Diamond"), a snack food manufacturer that is incorporated in Delaware and headquartered in California. The plaintiffs allege that, in a period between October 2010 and June 2012, two defendants, Diamond's former CEO and former CFO, breached their fiduciary duties by engaging in a manipulation of the company's financial statements.[1] The plaintiffs also allege that another nine defendants, who were directors of Diamond during the relevant period,[2] breached their fiduciary duty by failing to try in good

[1] These defendants, Michael Mendes and Steven Neil, were placed on administrative leave in February 2012, after Diamond's audit committee determined that the company's financial statements had been manipulated. *See* Def's. Op. Br. Ex. C (Diamond Foods, Inc., Form 8-K (Feb. 8, 2012)); *see also* V. Am. Compl. ¶¶ 25-26.

[2] These defendants are Laurence Baer, Edward Blechschmidt, John Gilbert, Glen Warren,

faith to ensure that the company operated in compliance with law.[3] The motive for this manipulation was to avoid revealing to a major strategic rival, Procter & Gamble—with whose Pringles division Diamond was planning to merge in December 2011—that Diamond was not as financially healthy as Procter & Gamble had believed.[4] This reality would have adversely affected the terms of the merger or even relieved Procter & Gamble of its obligation to close.[5] When the manipulation came to light, in November 2011, Diamond was forced to restate its financials, the Procter & Gamble merger cratered, the Diamond CEO and CFO were replaced, and several lawsuits were quickly brought.[6]

The first group of derivative suits was filed rapidly in the California state courts, alleging claims of the same essential nature as those brought in this case.[7] These three suits were consolidated, and the "California State Action" is ongoing, with both proceedings before the court and a settlement process before a mediator.[8] The derivative plaintiffs in this case brought the second set of suits, but not in this court. Rather, these derivative plaintiffs filed suit in the U.S. District Court for the Northern District of California, alleging state law claims of the kind outlined above and claims under § 14(a) of the Securities Exchange Act of 1934, on the grounds that Diamond's

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Richard Wolford, Robert Zollars, and Robert Lea, who were directors of Diamond at the time the plaintiffs filed their original complaint in June 2012. In addition, the plaintiffs name as defendants Dennis Mussell, a retired director, and the estate of Joseph Silveira, a director of Diamond who served on the company's audit committee, and who committed suicide after the manipulation of Diamond's financial statements came to light. V. Am. Compl. ¶¶ 27-35.

[3] *See, e.g.*, *Stone v. Ritter*, 911 A.2d 362 (Del. 2006) (affirming the standard for director oversight liability set out in *In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959 (Del. Ch. 1996)); *Guttman v. Huang*, 823 A.2d 492 (Del. Ch. 2003) (comparing the standards for pleading demand excusal in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), and *Rales v. Blasband*, 634 A.2d 927 (Del. 1993), and dismissing the plaintiffs' derivative claims based on allegations that the director defendants had engaged in insider trading and had failed to monitor the corporation's compliance with financial reporting standards).

[4] V. Am. Compl. ¶ 8.

[5] *Id.* ¶¶ 60, 146-47.

[6] *Id.* ¶¶ 99-104, 109-14.

[7] These suits were *Dean v. Baer*, Case No. 11-515895, filed on November 14, 2011; *Nguyen v. Baer*, Case No. 11-516073, filed on November 22, 2011; and *United Food & Commercial Workers Union v. Baer*, Case No. 11-516933, filed on December 29, 2011.

[8] In February 2012 the plaintiffs filed a consolidated complaint. Compl., *In re Diamond Foods, Inc. S'holder Deriv. Litig.*, Case No. 11-515895 (Cal. Super. Ct. Feb. 16, 2012) [hereinafter Cal. Compl.]. The consolidated plaintiffs entered mediation. After the mediation was unsuccessful, Diamond demurred from the complaint, and the California court sustained the demurrer. Kristy Aff. ¶ 3; Order, *In re Diamond Foods, Inc., S'holder Deriv. Litig.*, Case No. 11-515895 (Cal. Super. Ct. Nov. 13, 2012). Since that time, the plaintiffs have attended another mediation session. Kristy Reply Aff. ¶ 14.

proxy statements in 2010 and 2011 were materially misleading.[9] I refer to that suit as the California Federal Action. Because, as will be seen, the derivative plaintiffs here seek to subject Diamond and the defendants to suit in two forums simultaneously, I refer to them as the Dual Forum Plaintiffs.

Before me now is a motion by the defendants to dismiss or stay this derivative action brought by the Dual Forum Plaintiffs under the *McWane* doctrine.[10] In support of that motion, the defendants point out the following. First, the California Federal Action filed by the Dual Forum Plaintiffs was dismissed, with prejudice, by Judge Alsup of the U.S. District Court for the Northern District of California for lack of subject matter jurisdiction.[11] The court found that the Dual Forum Plaintiffs' § 14(a) claims, their sole grounds for federal jurisdiction, failed as a matter of law.[12] With the federal claims dismissed, the court found that it had no jurisdiction over the suit and did not consider any of the state law claims.[13]

One of the Dual Forum Plaintiffs has taken an appeal from that ruling.[14] But only a few weeks after noticing the appeal, the Dual Forum Plaintiffs filed a near-identical complaint in this court, without the federal securities law claims.[15] Thus, the Dual Forum Plaintiffs seek to have the dismissal of the California Federal Action overturned and to proceed in the U.S. District Court for the Northern District of California not only with their federal claims but with the *same* claims as those asserted in this action. The defendants argue that it is improper under *McWane* and basic principles of equity for the Dual Forum Plaintiffs to subject Diamond to the excess costs of litigating with the same plaintiffs over the same claims in two forums at once. The defendants are correct.[16]

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[9] 15 U.S.C. § 78n. These complaints were *Board of Trustees of City of Hialeah Employees' Retirement System v. Mendes*, Case No. 3:11-cv-05692-WHA (N.D. Cal. Nov. 28, 2011), and *Lucia v. Baer*, 3:11-cv-06417-JSC (N.D. Cal. Dec. 19, 2011). The two actions were consolidated, and a consolidated complaint was filed. Cons. Compl., *In re Diamond Foods, Inc. Deriv. Litig.*, Case No. 3:11-cv-05692-WHA (N.D. Cal. Mar. 1, 2012) [hereinafter Fed. Compl.].

[10] *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281 (Del. 1970).

[11] *In re Diamond Foods, Inc. Deriv. Litig.*, 2012 WL 1945814 (N.D. Cal. May 29, 2012).

[12] *Id.* at *5-7.

[13] *Id.* at *7.

[14] Notice of Appeal, *In re Diamond Foods, Inc. Deriv. Litig.*, Case No. 11-cv-5692-WHA (N.D. Cal. June 4, 2012).

[15] The Dual Forum Plaintiffs also dropped claims against Diamond's auditors, Deloitte & Touche. *See* Fed. Compl. ¶¶ 189-216.

[16] *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281, 283 (Del. 1970) (noting the "the wasteful duplication of time, effort, and expense that occurs when judges, lawyers, parties, and witnesses are simultaneously engaged in the adjudication of the same

Second, the defendants accurately point out that the Dual Forum Plaintiffs have failed to distinguish their claims from those being pressed in the California State Action. Those actions were filed *seven months* before the Dual Forum Plaintiffs filed their action in this court.[17] The Dual Forum Plaintiffs' belated Delaware complaint is not distinguishable in terms of quality from the consolidated complaint filed in the California State Action. Because the Dual Forum Plaintiffs' complaint comes so late in comparison to the California complaint, and is not materially different, there is no reason to disturb the orderly course of that litigation and mediation. Furthermore, the Dual Forum Plaintiffs have small stockholdings in Diamond, which makes it unlikely that they have a stronger economic motivation to prosecute their action more effectively on behalf of Diamond than the plaintiffs in the California State Action.[18]

Third, some derivative plaintiffs, who are not affiliated with either the Dual Forum Plaintiffs or the plaintiffs in the California State Action, did make a demand under 8 *Del. C.* § 220 and concluded that given the composition of the Diamond board, a demand to sue should be made.[19] In connection with that argument, the defendants note that Judge Kramer of the California Superior Court dismissed the original California State Action derivative complaint in that Action for failure to plead demand excusal, but gave leave to amend.[20] The Dual Forum Plaintiffs contend that they are better positioned to litigate demand excusal, but this is hardly the case. At the end of June 2012, when the Dual Forum Plaintiffs filed this action in

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cause of action in two courts").

[17] The original complaint in the Delaware action was filed on June 27, 2012. The Dual Forum Plaintiffs did not use the time between June 2012 and the disclosure of Diamond's financial irregularities in November 2011 to put together a complaint with a better chance of success, for example by filing a request for books and records under 8 *Del. C.* § 220. Oddly, it appears that Dual Forum Plaintiff Lucia made a demand for records on Diamond under *California*, not Delaware, law. Diamond refused that demand, and Lucia dropped it. Kristy Reply Aff. ¶ 18.

[18] The Dual Forum Plaintiffs have filed affidavits with the court attesting to their stock ownership. From 2011 on, plaintiff Lucia has held approximately 50 shares, and plaintiff Hialeah has held approximately 1,300 shares. Lucia Aff.; Voorhees Aff. Based on Diamond's closing share price of $15.25 on February 27, 2013, this gives the Dual Forum Plaintiffs a stockholding worth $21,000 in a corporation with a market capitalization of $340 million. *Diamond Foods, Inc.*, Yahoo! Finance, http://finance.yahoo.com/q?s=DMND (visited Feb. 27, 2013).

[19] *See* V. Compl., *Astor BK Realty Trust v. Diamond Foods, Inc.*, C.A. No. 7272-ML (Del. Ch. Feb. 22, 2012); Kristy Reply Aff. ¶ 4; *see also* Letter to the Court from Michael W. McDermott, Esq. (Dec. 20, 2012) (describing the efforts of Astor and its coplaintiff, Beaver County Retirement Fund, to obtain books and records under § 220).

[20] Order, *In re Diamond Foods, Inc., S'holder Deriv. Litig.*, Case No. 11-515895 (Cal. Super. Ct. Nov. 13, 2012). The California court did not grant leave to amend on one count, gross mismanagement, on the ground that that is not an independent cause of action.

Delaware, the Diamond board had twelve members.[21] Of these twelve members, the Dual Forum Plaintiffs have named seven as defendants. These members were on the Diamond board at the time of the financial manipulation. The Dual Forum Plaintiffs have not alleged that any of the five directors who joined the Diamond board after the events at issue are not independent and cannot consider a demand on the board. Therefore, if the California court was right that even *two* of the seven directors who are named as defendants were independent for purposes of demand excusal, then the Dual Forum Plaintiffs will not be excused from making demand on the ground that at least half the board is not independent.

The Dual Forum Plaintiffs point out that the California State Action Plaintiffs must file a new complaint in that Action, and observe that, since June last year, another three of the individual defendant directors have left the board.[22] As a result, the board now has nine members, a majority of whom joined the board after the events at issue, and whose independence neither the California State Action Plaintiffs nor the Dual Forum Plaintiffs have challenged. But, this does not give the Dual Forum Plaintiffs a significantly better chance of avoiding demand. The allegations as to the seven directors whose independence the Dual Forum Plaintiffs challenge are largely identical to the allegations made by the California State Action Plaintiffs, which were rejected by Judge Kramer.[23] Because of this, the Dual Forum Plaintiffs' contention that Diamond is attempting to settle with a weaker plaintiff in California is, in my view, meritless. In any event, it can be addressed by the Dual Forum Plaintiffs intervening in the California State Action, which is proceeding in the same state where they originally chose to sue.

Fourth, the defendants note that much of the relief sought in this action will depend on the outcome of securities litigation filed against Diamond relating to the accounting manipulation.[24] That is, because the

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[21] V. Compl. ¶ 123.

[22] The Dual Forum Plaintiffs cite a Diamond press release from January 14, 2013, which they supply in an exhibit. Pls.' Br. in Opp'n 18; *see* Bottini Aff. Ex. 5 (press release). The press release shows that four, not three, of the individual defendants have left the board. These four are Baer, Gilbert, Warren, and Wolford. One of these has been replaced, with the new director being William Tos. Therefore, if the Dual Forum Plaintiffs' argument had any traction (which it does not), the affidavit exhibit that they supply would be more helpful to their position than they in fact recognize.

[23] *Compare* Cal. Compl. ¶¶ 226, 230-33, 235-37, *with* V. Am. Compl. ¶¶ 128-40.

[24] This litigation is also before Judge Alsup in the federal district court. In November last year, the federal district court denied Diamond's and the individual defendants' motions to dismiss. *In re Diamond Foods, Inc. Secs. Litig.*, 2012 WL 6000923 (N.D. Cal. Nov. 30, 2012). The court

derivative actions seek to make the derivative defendants indemnify Diamond for any damages or costs it must pay as a result of the securities suits, the derivative actions should be stayed until the securities suits are concluded.[25] I agree.

Fifth, the defendants argue that the Dual Forum Plaintiffs' claim that a Delaware court must hear their derivative claims because they raise novel issues of Delaware law is belied by the actions of the Dual Forum Plaintiffs themselves. The Dual Forum Plaintiffs did not bring their Delaware law claims in this court in the first instance. Instead, they brought them in a federal court, and not even the U.S. District Court for the District of Delaware, which might have more opportunities to apply Delaware corporate law than the U.S. District Court for the Northern District of California. Even now, the Dual Forum Plaintiffs seek to prevail in their federal appeal and to prosecute all of their claims, federal and state, in the federal district court in California. Given the decisional law of this state's courts in cases like *Caremark*,[26] *Stone*,[27] *Guttman*,[28] *AIG*,[29] and *Citigroup*,[30] the defendants say that the legal principles to be applied are settled, and that the Dual Forum Plaintiffs have not identified any novel question to be litigated. Again, I agree.

Last, the defendants note that when the federal judge refused to exercise supplemental jurisdiction over the Dual Forum Plaintiffs' state claims, he expressly noted that the issues raised by those claims were already before his judicial colleague in the California State Action.[31] Instead of

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granted the motion to dismiss of the company's auditor, Deloitte & Touche. Since that time, Diamond has filed an answer to the consolidated complaint, and there has been further activity on the docket.

[25] Am. V. Compl. ¶¶ 168-70.

[26] *In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959 (Del. Ch. 1996).

[27] *Stone v. Ritter*, 911 A.2d 362 (Del. 2006).

[28] *Guttman v. Huang*, 823 A.2d 492 (Del. Ch. 2003).

[29] *In re Am. Int'l Group, Inc., Consol. Deriv. Litig.*, 965 A.2d 763, 798-99 (Del. Ch. 2009) (refusing to dismiss a *Caremark* claim against two director defendants under Court of Chancery Rule 12(b)(6), because the plaintiffs had pled facts supporting an inference that the defendants breached their fiduciary duty by being "directly . . . involved in," or "knowingly fail[ing] to stop," financial wrongdoing).

[30] *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 129-131 (Del. Ch. 2009) (dismissing plaintiffs' *Caremark* claim alleging that the directors failed to monitor the company's business risk, because the plaintiffs had not "alleg[ed] facts that could demonstrate bad faith on the part of the directors," and contrasting the allegations in that case with the allegations that survived a motion to dismiss in *AIG*, 965 A.2d 106).

[31] *See In re Diamond Foods, Inc. Deriv. Litig.*, 2012 WL 1945814, at *7 (N.D. Cal. May 29, 2012) ("The Court will not exercise supplemental jurisdiction over the remaining state law claims. In light of the fact that there are almost identical state suits pending before Judge Richard Kramer, it would be duplicative to reach these issues here in federal court.").

seeking to intervene in those actions and seek lead plaintiff status, the Dual Forum Plaintiffs opened up a third front in this court, subjecting Diamond and therefore its stockholders to excess costs.

In response to these arguments, which are measured and entirely supported by the record, the Dual Forum Plaintiffs simply respond that the wrongdoing alleged, although not of any novel type, is substantial and that a Delaware court should decide the case.[32] *They ignore the obvious reality that they filed the claims in a federal court in California first and continue to try to litigate those claims there.* The Dual Forum Plaintiffs then contend that they are somehow better positioned to plead demand excusal, despite having sought no books and records to enable them to do so, and despite having failed to demonstrate any superiority in pleading over their counterparts in the California State Action.[33] Although this court does not encourage races to the courthouse, the reality is that the Dual Forum Plaintiffs have not demonstrated that their later filings reflected more diligent research and investigation than the prior filed claims made in the California State Action. The complaint that was dismissed without prejudice in that Action was detailed, with 100 pages and 283 paragraphs.

Furthermore, the Dual Forum Plaintiffs belittle those derivative plaintiffs who sought books and records because those plaintiffs concluded that making a demand was the appropriate course of action.[34] But, given the structural independence of most public company boards and the difficulty of proving out a *Caremark* claim, that decision may have reflected sober and sensible legal judgment.[35] The Dual Forum Plaintiffs' blithe assertions that their complaint is superior are unaccompanied by any reasoned arguments in support of that position. Instead, the Dual Forum Plaintiffs make an array of extreme arguments about the good faith of Diamond and the defendants in conducting settlement discussions with the plaintiffs in the California State Action—discussions that occurred with the involvement of a former federal magistrate judge and with the knowledge of my California state colleague.[36]

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[32] Pls.' Br. in Opp'n 23-24.

[33] *Id.* at 18-19.

[34] *Id.* at 12 ("On April 3, 2012, the *Astor* Plaintiffs served a litigation demand on the Board, effectively conceding the Board's independence."); *id.* at 19 n.5 ("The *Dean* Plaintiffs' bargaining position is as weak as that of the *Astor* Plaintiffs, who have conceded the Board's independence by making a litigation demand in April 2012.").

[35] As Chancellor Allen wrote, "[t]he theory . . . advanced [in *Caremark*] is possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment." *In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996).

[36] Pls.' Br. in Opp'n 16-17; *see* Kristy Aff. ¶ 3; Kristy Reply Aff. ¶ 12.

The Dual Forum Plaintiffs allege that these discussions violated an order of Judge Alsup in the federal case, even though these discussions occurred in a case before the courts of another sovereign and after Judge Alsup had entered a final judgment of dismissal in his case.[37] The Dual Forum Plaintiffs' vinegar-laced arguments repeat ones they are simultaneously making about that issue to Judge Alsup and the U.S. Court of Appeals for the Ninth Circuit. The astringency of these arguments is more evident than their plausibility or merit, but the fact that the Dual Forum Plaintiffs seek to have me consider them at the same time as my federal colleague underscores why dismissal of this action is in order.

Given that (i) this action was brought well after these claims were already fairly in litigation in California state court; (ii) the Dual Forum Plaintiffs brought this action after bringing these same claims in a federal court in California and thus after conceding that a non-Delaware court could competently adjudicate the claim; (iii) the Dual Forum Plaintiffs continue to press an appeal that, if successful, will enable them to litigate their claims in federal district court; and (iv) the Dual Forum Plaintiffs have not demonstrated that they are better positioned to represent Diamond than the plaintiffs in the California State Action, the defendants' motion under *McWane* should be granted. The Dual Forum Plaintiffs are seeking a course of action that *McWane* exists to avoid, one in which the interests of justice are eroded by the excessive cost and burden of unnecessary litigation over the same issues in multiple forums.[38] And worst of all, it is *the Dual Forum Plaintiffs themselves* who seek to subject the same defendants to litigation with them in two forums. This is costly, inequitable, and unfair to Diamond and the very stockholders whose best interests the Dual Forum Plaintiffs are supposed to be advancing.

Given the evident inequity of their position, the Dual Forum Plaintiffs' claims in this court are dismissed with prejudice to their ability to proceed in this forum, but without prejudice to their ability to proceed in the California Federal Action if their appeal is successful and the federal court decides to

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[37] *See* Kristy Reply Aff. ¶¶ 2, 11. One of the Dual Forum Plaintiffs, Lucia, has filed a motion for an order to show cause why the defendants should not be sanctioned for violating the order barring negotiations. *Id.* ¶ 15. Lucia noticed a hearing for this motion for February 28. Therefore, I do not comment further on the Dual Forum Plaintiffs' contention, except to note that in the unopposed motion to consolidate that the Dual Forum Plaintiffs proposed in August last year, which I granted only because it was unopposed, counsel for the Dual Forum Plaintiffs expressly reserved the "authority to negotiate a settlement." Order of Cons. ¶ 6 (Aug. 7, 2012).

[38] *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281, 283 (Del. 1970).

exercise supplemental jurisdiction, or their ability to proceed in the California State Action if they seek intervention and *if* the California court grants them a role. But the Dual Forum Plaintiffs may not burden Diamond and its stockholders with litigation in a coastal state bordering the Atlantic, when they themselves chose to sue in the federal courts of a state bordering the Pacific.

For all these reasons, the defendants' motion to dismiss is GRANTED. The defendants shall submit an implementing order, upon approval as to form by the Dual Forum Plaintiffs, within five days.

GERALD KALLICK, ET AL v. SANDRIDGE ENERGY, INC., ET AL

No. 8182-CS

In the Court of Chancery of the State of Delaware

March 8, 2013

Stuart M. Grant, Esquire, Michael J. Barry, Esquire, and Bernard C. Devieux, Esquire, of Grant & Eisenhofer P.A., Wilmington, Delaware; and Mark Lebovitch, Esquire, and Jeremy Friedman, Esquire, of Bernstein Litowitz Berger & Grossman LLP, New York, New York, Attorneys for Plaintiff.

Donald J. Wolfe, Jr., Esquire, T. Brad Davey, Esquire, and Justin Morse, Esquire, of Potter Anderson & Corroon LLP, Wilmington, Delaware; and C. William Philips, Esquire, and Mark P. Gimbel, Esquire, of Covington & Burling LLP, New York, New York, Attorneys for Defendants.

STRINE, *Chancellor.*

The incumbent management and board of SandRidge Energy, an oil and natural gas business focusing on domestic exploration and production, face a serious proxy fight. A hedge fund, TPG-Axon ("TPG"), which holds a 7% stake in SandRidge, has launched a consent solicitation to destagger SandRidge's seven-member board by amending the company's bylaws,[1] remove all the directors, and install its own slate.[2] TPG claims that SandRidge's performance has been abysmal during the past six years, resulting in a performance that is extremely poor in comparison to other U.S. oil and gas companies.[3] TPG also alleges that, during the same period, SandRidge's incumbent board has lavished compensation on the

[1] The staggered board is implemented by bylaw, not by the certificate of incorporation, leaving it subject to direct stockholder reversal. This defensive planning flaw is rare, but not unprecedented. *See, e.g.*, *Chesapeake Corp. v. Shore*, 771 A.2d 293, 345-46 (Del. Ch. 2000) (finding, in a case addressing a consent solicitation, that stockholders have the right to declassify and replace the board when the classification provision is in the bylaw, not the charter).

[2] Pl's. Ex. B (Definitive Consent Solicitation Statement of TPG-Axon Partners, L.P. (Jan. 15, 2013)), at 1-2, 15-22 [hereinafter Definitive Consent Solicitation Statement].

[3] *Id.* at 11.

corporation's CEO, Tom Ward, paying him $150 million despite the company's subpar performance.[4]

By its consent solicitation, TPG wishes to seat a new SandRidge board majority that has committed to change the management of the company and explore strategic alternatives for the company, including an asset sale.[5] The incumbent board, whose members, along with SandRidge, are the defendants in this action, has resisted the consent solicitation and has energetically campaigned to convince SandRidge's stockholders not to give consents to TPG. Even further, it has tried to obtain revocations from stockholders who have given TPG consents.[6] The incumbent board contends that TPG's slate is less qualified to run SandRidge than it is because TPG's nominees lack expertise in "upstream" oil and gas exploration and have no specific experience with the company's principal asset, a 2.2 million acre oil and gas play in Kansas and Oklahoma (the "Mississippian Play").[7]

For present purposes, what is most relevant is that in originally opposing the consent solicitation, the incumbent board warned the stockholders that the election of TPG's proposed slate would constitute a "Change of Control" for the purposes of SandRidge's credit agreements simply because it involved the election of a new board majority not approved by the incumbent board, and that such a Change of Control would trigger the requirement in SandRidge's note indentures that SandRidge offer to repurchase its existing debt (the "Proxy Put").[8] That is, the incumbent board clearly told stockholders that if they chose to elect a new board majority, the Proxy Put would cause a material economic harm because SandRidge's

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[4] *Id.* at 12.

[5] *Id.* at 13.

[6] Pl's. Ex. P (SandRidge Energy, Inc., Definitive Consent Revocation Statement (Jan. 18, 2013)) [hereinafter Definitive Consent Revocation Statement].

[7] *Id.* at 5-6.

[8] Pl's. Ex. M (SandRidge Energy, Inc., Preliminary Consent Revocation Statement (Dec. 27, 2012)), at 7 [hereinafter Consent Revocation Statement]; Definitive Consent Revocation Statement at 8. The defendants object to the use of the term Proxy Put, claiming that it is "inappropriate" and "has all sorts of assumptions embedded in it." Pl's. Ex. H (Deposition of Daniel Jordan (Feb. 15, 2013)), at 20:25-21:4 (Mark Gimbel) [hereinafter Jordan Dep.]. But, the term is appropriate, because the Proxy Put gives the noteholders the right to put back their debt after a vote that seats a new board that has not been approved by the ousted incumbents. Like the appellation "poison pill" to describe a plan that gave stockholders "rights," the only value of which was to prevent them from accepting a tender offer because the "rights," if so triggered massively diluted the offeror, the term "Proxy Put" is not intrinsically pejorative. It is descriptive of the intended effect of the device, and the term Proxy Put is actually more closely descriptive. By use of the term, I imply no judgment about the device's utility. I just use language that tracks the device's operation.

lenders would have the right to put $4.3 billion worth of notes back to the company.

After taking that position, the incumbent board faced this litigation from the plaintiff, Gerald Kallick, a SandRidge stockholder who supports the TPG consent solicitation. Kallick argues that the incumbent board is breaching its fiduciary duties by failing to approve the TPG slate, which, under the indentures governing SandRidge's notes, would mean that the SandRidge stockholders could replace the incumbent board without triggering the Proxy Put. Because the incumbent board has been unable to identify any rational question about the integrity of the TPG slate, about their qualifications to serve as public company directors, or about the propriety of their motives, Kallick says there is no proper basis for the incumbent board to fail to approve them. At best, the incumbent board believes it is more qualified than the TPG slate, and believes that TPG's plans for SandRidge are not wise. Such mere differences in policy, says Kallick, are not a proper basis for failing to approve the TPG slate for purposes of the Proxy Put. Kallick therefore argues that the incumbent board should be enjoined from soliciting consent revocations until it approves the TPG slate, because otherwise it is able to inequitably exploit its incumbency to pressure voters to keep the directors in office simply to avoid the negative consequences of triggering the Proxy Put.

Since TPG first indicated that it would carry out a consent solicitation at the end of November last year, the incumbent board has wiggled and squirmed in order to avoid dealing with this litigation, or the discretion given it to approve the TPG slate for purposes of the Proxy Put. Facing Kallick's suit, the incumbent board assented to a schedule culminating in a preliminary injunction hearing. An order scheduling that argument was entered on February 7, 2013.[9] But, having warned its stockholders twice in its SEC filings that triggering the Proxy Put would be "extreme" and "risky," the incumbent board then reversed direction, and stated in an 8-K the very next day that there was *no* danger posed by the Proxy Put. That was because SandRidge's debt was trading at prices above the repurchase price set in the indentures, and thus debtholders were not likely to tender at a below-market price.[10] The record shows, however, that SandRidge's debt was trading well

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[9] *See* Stip. Sched. Order (Feb. 7, 2013).

[10] Pl's. Ex. R (SandRidge Energy, Inc., Form 8-K (Feb. 8, 2013)) [hereinafter February 8-K].

above par even when the incumbent board declared that triggering the Proxy Put would be "extreme" and "risky."[11]

The incumbent board then sought to cancel the preliminary injunction hearing to which they just had assented, claiming that there was no material likelihood of harm to the company in not approving the TPG slate.[12] But it failed to decide, one way or the other, whether it approved the TPG slate for purposes of the Proxy Put.[13] That remains true as of today. As a default matter, therefore, the incumbent board has left the TPG slate unapproved. Likewise, although the defendants admit that credit markets can move quickly and although the defendants' estimates of the costs of refinancing the debt keep shifting, the defendants claim that the doubt their own disclosures have created over the consequences of voting for the TPG slate is too insubstantial for the court to worry that the electoral playing field has been unfairly tilted.

In keeping with this state's public policy of stringent policing of the fairness of corporate elections, this court's decision in *San Antonio Fire & Police Pension Fund v. Amylin Pharmaceuticals* made clear that a board deciding whether to approve directors for the purposes of a Proxy Put could not act consistently with its fiduciary duties by simply failing to approve any director candidates who ran against the incumbent slate.[14] Rather, the incumbent board must respect its primary duty of loyalty to the corporation and its stockholders and may refuse to grant approval only if it determines that the director candidates running against them posed such a material threat of harm to the corporation that it would constitute a "breach of the directors' duty of loyalty to the corporation and its stockholders" to "pass[] control" to them.[15] In other words, unless the incumbent board determined, by way of example, that the rival candidates lacked ethical integrity, fell within the category of known looters, or made a specific determination that the rival candidates proposed a program that would have demonstrably material adverse effects for the corporation's ability to meet its legal obligations to its creditors, the incumbent board should approve the rival slate and allow the stockholders to choose the corporation's directors without fear of adverse financial consequences, and also eliminate the threat to the corporation of a

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[11] *See* Pl's. Ex. S (Morgan Stanley discussion materials (Feb. 6, 2013)), at 5 [hereinafter Morgan Stanley Presentation].

[12] Defs.' Mot. to Vacate the Scheduling Order (Feb. 11, 2013).

[13] *See* Definitive Consent Revocation Statement.

[14] 983 A.2d 304 (Del. Ch. 2009).

[15] *Id.* at 316 n.37.

forced refinancing. Notably, absent any determination by the incumbents that the rival slate has suspect integrity or specific plans that would endanger the corporation's ability to repay its creditors, there is no harm threatened to the creditors by the election of the slate. Rather, the only "harm" threatened is that the stockholders will choose to seat a new board of directors. The incumbents' expected view that they are better suited to run the company effectively is, without substantially more, not a sufficient fiduciary basis to deny approval to their opponents.

Given that the incumbent board has admitted it has no basis to doubt the integrity of the TPG slate or the basic qualifications of that slate to serve with competence as the directors of a public company, the incumbent board is merely basing its refusal to make a decision on its contention that the incumbents are the better choice at the ballot box.[16] Not only has the incumbent board failed to identify any threat the TPG slate poses to the company's creditors or ability to meet its legal obligations, its financial advisor, Morgan Stanley, has generously offered to pay off the existing debt holders and become the company's lender itself, if the TPG slate is elected.[17] That is, Morgan Stanley told the board that its own financial institution would risk $4.3 billion lent to SandRidge even if TPG's slate controlled the board. The incumbent board's further contention that the SandRidge stockholders will be too stupid not to be confused if the board approves the TPG slate for the sole purpose of alleviating the risk of the Proxy Put[18] is one premised on a view of stockholder cognition inconsistent with giving them a right to vote at all on important matters like elections and mergers.[19] That self-serving, paternalist explanation cannot justify the doubt that the Proxy

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[16] *See* Jordan Dep. 35:3-14, 36:3-37:3, 40:13-22.

[17] *See* Morgan Stanley Presentation at 5 ("Morgan Stanley would be willing to provide Change of Control backstop to SandRidge Energy . . . Commitment fee of 1.0% . . . Take-out fee of 2.0% payable on any bonds issued as a result of the Change of Control put[.]").

[18] Jordan Dep. 47:18-48:11 ("Q: [I]f the board could approve TPG-Axon's nominees solely for purposes of the change of control provision while simultaneously putting out public statement to its shareholders that it no way endorses TPG-Axon's nominees and does not support their election would there be any harm to SandRidge or its shareholders . . . ? A: I think if you confuse one shareholder sending mixed signals like that, you're doing harm. . . . . Q: *So you don't believe there would be any way to eliminate the confusion that would exist in that situation?* A: *Not totally. Not absolute, no.*") (emphasis added).

[19] *See, e.g.*, 8 *Del. C.* § 211(b) (stockholder right to vote to elect directors); *id.* § 242(b) (stockholder vote to right on charter amendment); *id.* § 251(c) (stockholder vote required for merger); *id.* § 271 (stockholder vote required for sale of "all or substantially all" of the assets of a company).

Put creates in an electoral contest in which each voting decision may turn out to matter immensely.[20]

Having failed to exercise its discretion in a reasonable manner, the incumbent board should be enjoined from soliciting consent revocations, voting any proxies it received from the consent revocations, and impeding TPG's consent solicitation in any way until the incumbent board has approved the TPG slate. The equities here weigh heavily in favor of the stockholders' right to make a free, uncoerced choice.

I. The Background To The Dispute

The factual analysis necessary to address the pending motion is framed by the reality that Kallick does not take much time attacking the SandRidge board's decision to agree to the Change of Control provision containing the Proxy Put in the first place. Kallick's focus instead is on whether the SandRidge board has properly used the contractual discretion left to it by the stockholders to approve the TPG slate for purposes of relieving the corporation of any duty to offer to repurchase SandRidge's debt if that slate is elected.

Kallick's narrow angle of attack is a pragmatic one, given that the note agreements were entered into over several years, starting in 2008, with lenders who provided valuable financing.[21] The record before the court surrounding whether the lenders pressed hard for the specific inclusion of a change of control provision dealing not simply with acquisitions of an actual control block or a merger, as opposed merely to the stockholders' election of a slate other than the management slate, is nonexistent. Given the obvious entrenching purposes of a Proxy Put provision, one would hope that any public company would bargain hard to exclude that toll on the stockholder franchise and only accede to the Proxy Put after hard negotiation and only for clear economic advantage.[22] In "frothy" credit financing markets, there is

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[20] *Mercier v. Inter-Tel (Del.), Inc.*, 929 A.2d 786, 811 (Del. Ch. 2007) ("The notion that directors know better than stockholders about who should be on the board is no justification at all."); *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 662 (Del. Ch. 1988) ("[W]hen viewed from a broad, institutional perspective, it can be seen that matters involving the integrity of the shareholder voting process involve consideration not present in any other context in which directors exercise delegated power.").

[21] Defs.' Ex. 1 ¶ 5 (Jordan Aff.); *see also* Pl's. Ex. E (SandRidge Energy, Form 10-Q (Nov. 9, 2012)), at 23.

[22] As Vice Chancellor Lamb put it in *Amylin*: "The court would want, at a minimum, to see evidence that the board believed in good faith that, in accepting [a Proxy Put], it was obtaining in return extraordinarily valuable economic benefits for the corporation that would not otherwise be

reason (such as SandRidge's financial advisor's own actions in this market) to suspect that the costs of such resistance would be insubstantial to non-existent. Most important, however, because of management's special interest in retaining office, the independent directors of the board should police aspects of agreements like this, to ensure that the company itself is not offering up these terms lightly precisely because of their entrenching utility, or accepting their proposal when there is no real need to do so.[23]

What scarce record exists here is not comforting in this regard. The long-standing independent director who testified on behalf of the defendants, Daniel Jordan, stated that he was ignorant of the existence of the Proxy Put in the indentures until TPG commenced its consent solicitation.[24] Jordan was on the board when the indentures were adopted and his testimony suggests that the independent board members were not engaged in any memorable way in reviewing any of the indentures, at least insofar as considering the implications of the put provisions that could affect proxy contests or other important events, such as an acquisition offer.[25] Given the importance of this litigation, one would have expected that if the independent directors had been consulted in advance and if there was a record of genuine negotiations to limit the impact of the provision on the viability of a proxy contest, the defendants would have refreshed Jordan's recollection of those fisticuffs with the credit providers. I thus assume that the Proxy Put provisions were accepted by management without resistance and without any input from the board. As it stands, the present motion focuses on the propriety of the defendants' failure to make a decision whether to approve the TPG slate for purposes of the consent solicitation, a failure that means that the electorate must assume that seating a majority of the TPG slate may trigger the Proxy Put.

A. SandRidge's Stockholders Run Out Of Patience With The Company's Woeful Performance

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available to it." *San Antonio Fire & Police Pension Fund v. Amylin Pharms., Inc.*, 983 A.2d 304, 315 (Del. Ch. 2009).

[23] *See id.* at 319 (urging boards, and their outside counsel, to be alert to Proxy Put provisions).

[24] Jordan Dep. 21:25-22:8 ("Q: [W]ere you aware of [the Proxy Put] at the time the company entered into its first note indenture? A: I don't remember. That was, gosh, five years ago. Q: Do you have any— A: *I don't know if it was in there. I mean, to answer your question, I do not know if it was in there or not.*") (emphasis added).

[25] *Id.* at 22:15-23:16.

SandRidge became a public company in 2007.[26] Its stock was offered at $26 a share, and rose to about $68 in July 2008.[27] It now trades at less than $6.[28] According to TPG, SandRidge has performed worse than any other company in the Russell 1000 Energy Index since its IPO.[29] Frustrated with SandRidge's performance and its weak corporate governance, TPG, one of the company's largest stockholders, wrote a public letter to SandRidge's board in November 2012.[30] TPG complained of a series of strategic missteps, including an erroneous focus on natural gas at the expense of oil; lax spending and financial discipline; and "appalling" corporate governance.[31] In the latter category, TPG noted that SandRidge's chairman and CEO, Tom Ward, has been paid more than $150 million over the last five years, and that he appeared to have engaged in self-dealing on behalf of himself and his family.[32] TPG demanded that SandRidge's bylaws be amended to declassify the board, that the board be reconfigured to include stockholder representatives, that Ward be replaced as CEO, and that the board look into strategic alternatives to maximize the value of its assets, including an asset sale.[33] A few days after TPG sent its letter, another large stockholder, Mount Kellett Capital Management, wrote a public letter to the incumbent board echoing TPG's demands.[34]

B. The Incumbent Board Adopts Defensive Measures, And Litigation Begins

The incumbent board responded by, among other things, adopting a poison pill, making it harder for the stockholders to take action by written consent, and requiring an affirmative vote of over 50% of stockholders to

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[26] Pl's. Ex. C. (SandRidge Energy, Inc., Form 10-K (Mar. 20, 2012), at 16.

[27] Definitive Consent Solicitation Statement, at 11; V. Am. Compl. ¶¶ 33-34.

[28] SandRidge Energy, Inc., *Google Finance*, https://www.google.com/finance?cid=704234 (visited Mar. 7, 2013).

[29] Definitive Consent Solicitation Statement, at 6.

[30] Pl's. Ex. 1 (SandRidge Energy, Inc., Schedule 13D (Nov. 13, 2012)), at Ex. 2 (letter to the Board of Directors (Nov. 8, 2012)) [hereinafter TPG November 8 Letter]. At the time of the letter, TPG-Axon had over 4.5% of SandRidge; it increased its stake later to 6.7%. *See id.*; Pl's. Ex. D (SandRidge Energy, Inc., Schedule 14A (Jan. 24, 2013)), at Ex. 3.

[31] TPG November 8 Letter, at 5.

[32] *Id.* at 5-7.

[33] *Id.* at 1-2.

[34] *Mount Kellett Sends Letter to the Board of SandRidge Energy*, PR Newswire (Nov. 15, 2012), http://www.prnewswire.com/news-releases/mount-kellett-sends-letter-to-the-board-of-sandridge-energy-179486931.html (last visited Mar. 7, 2013). At the time of sending the letter, Mount Kellett owned 4.5% of SandRidge's stock. *Id.*

amend any part of the bylaws concerning the election of directors.[35] TPG then wrote again to the incumbent board, informing them that it was going to seek a consent solicitation under 8 *Del. C.* § 228 to amend SandRidge's bylaws to destagger the board, and remove and replace the incumbent board.[36] Under § 228, TPG would have had 60 days to collect the required number of consents from the time of receiving its first consent.[37] The incumbent board announced that this 60 day period had begun on December 19, 2012, almost a month before TPG filed its definitive consent solicitation statement with the SEC, and before TPG filed its preliminary consent solicitation statement.[38] TPG filed suit on December 24, 2012, alleging that this challenge to the start date was inequitable and an attempt to manipulate the time period set out in § 228.[39]

On December 26, 2012, TPG filed its preliminary consent solicitation statement.[40] The incumbent board responded the following day by filing a preliminary consent revocation statement.[41] The incumbent board warned TPG's stockholders that, under the terms of the indentures governing SandRidge's senior notes, a replacement of the board would be deemed a change of control, and the company would be obliged to offer to repurchase $4.3 billion of debt at 101% of par.[42] The incumbent board warned that "*[t]he Company may not have sufficient liquidity to fund the purchase price for such senior notes as required under the Indentures,*" and that "*[a] mandatory refinancing of this magnitude would present an extreme, risky and unnecessary financial burden*" on the Company.[43]

On January 7, 2013, Kallick, who supports TPG's consent solicitation, initiated this action. In his complaint, Kallick pointed out that the incumbent

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[35] Pl's. Ex. J (SandRidge Energy, Inc., Form 8-K (Nov. 20, 2012)), §§ 1.01, 5.03.

[36] V. Compl., *TPG-Axon Partners, LP v. SandRidge Energy, Inc.*, C.A. No. 8147-CS (Del. Ch. Dec. 24, 2012), at Ex. B (letter from TPG to SandRidge (Nov. 30, 2012)).

[37] 8 Del. C. § 228(c) (providing that approval to take action by written consent must be obtained "within 60 days of the earliest dated consent delivered in the manner required by this section to the corporation").

[38] *See* Stip. & Order of Dismissal, *TPG-Axon Partners, LP v. SandRidge Energy, Inc.*, C.A. No. 8147-CS (Del. Ch. Jan. 17, 2013).

[39] V. Compl., *TPG-Axon Partners, LP v. SandRidge Energy, Inc.*, C.A. No. 8147-CS (Del. Ch. Dec. 24, 2013).

[40] *Id.* Ex. L (SandRidge Energy, Inc., Preliminary Consent Statement of TPG-Axon Partners, L.P. (Dec. 26, 2012)).

[41] *See* Consent Revocation Statement.

[42] *Id.* at 7. The $4.3 billion consists of six series of high-yield notes, with the first series maturing in 2016 and the last series maturing in 2023. *See* Pl's. Ex. E (SandRidge Energy, Form 10-Q (Nov. 9, 2012), at 23. The indentures governing the notes are identical in relevant part.

[43] Consent Revocation Statement, at 7 (emphasis added).

board could neutralize the effect of the Proxy Put by "approving" the TPG slate of directors, in accordance with the terms of the indentures.[44] The indentures provide, in relevant part, that a Change of Control occurs if,

> during any period of two consecutive years, individuals who at the beginning of such period constituted the Board of Directors of the Company or any Successor Parent (*together with any new directors whose election to such board or whose nomination for election by the stockholders of the Company or any Successor Parent, as the case may be, was approved by a vote of 66 2/3% of the directors then still in office who were either directors at the beginning of such period or whose election or nomination for election was previously so approved*), cease for any reason to constitute a majority of such Board of Directors then in office . . . .[45]

Kallick argued that, under this court's decision in *Amylin*, the mere fact that the incumbent board was opposing the slate proposed by a dissident stockholder did not mean that the board could not approve that slate for purposes of the Proxy Put.[46] In fact, Kallick pointed out that in *Amylin*, this court noted that in making that determination the "directors' duty of loyalty [is] to the corporation and its stockholders."[47] Because the incumbent board had no proper basis to deny approval to the TPG slate simply because it was proposing to unseat the incumbents, Kallick argued that the incumbent board was breaching its fiduciary duties by failing to approve the slate for the limited purpose of the Proxy Put.

TPG then filed its definitive consent solicitation statement with the SEC on January 15, 2013. The incumbent board then settled its dispute with TPG over the start date of the 60 day consent period, and agreed that it would be deemed to start on January 15.[48] The board filed its definitive consent revocation statement on January 18. The board reiterated that a change in control would be risky:

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[44] *E.g.*, V. Compl. ¶ 3.

[45] Pl's. Ex. F (SandRidge Energy, Inc., Indenture for 7.5% Senior Notes Due 2023)), at § 1.01 [hereinafter Indenture] (emphasis added).

[46] 983 A.2d 304, 314-15 (Del. Ch. 2009).

[47] *Id.* at 316 n. 37.

[48] Stip. & Order of Dismissal, *TPG-Axon Partners, LP v. SandRidge Energy, Inc.*, C.A. No. 8147-CS (Del. Ch. Jan. 7, 2013).

> The removal and replacement of a majority of the Board as a result of the TPG–Axon Consent Solicitation could constitute a "change of control" under certain of the Company's material agreements, requiring the Company, among other things, to offer to buy back over $4.3 billion of its senior notes, which could be materially harmful to the Company.[49]

But, the incumbent board also admitted that it could avoid triggering the change of control provision by approving TPG's slate:

> The removal and replacement of a majority of the members of your existing Board would constitute a "change of control" under the Company's senior secured revolving credit facility. . . . If the Company were required to offer to purchase all of such notes as described above, up to $4.3 billion of senior notes could become subject to repayment and refinancing by the Company. The amount ultimately subject to repayment and refinancing would depend upon the amount of outstanding senior notes for which the offer to purchase by the Company is accepted by holders. . . . *A refinancing of $4.3 billion would present an extreme, risky and unnecessary financial burden on your Company. The TPG–Axon Group's assertion that repayment of the Company's outstanding senior notes, if required, would not materially impact the Company reflects a fundamental misunderstanding of the Company's business, financial position and operations. However, if the Board takes actions to approve the TPG–Axon Group Nominees that are permitted by the Indentures, such refinancing would not be required.*[50]

The incumbent board then stated in the same disclosure that it had not yet decided whether it *would* approve the new slate.[51]

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[49] Definitive Consent Revocation Statement, at 5.

[50] *Id.* at 8 (emphasis added).

[51] *Id.* ("The Board has not made a determination with respect to the approval of any of the TPG–Axon Group nominees.").

C. The Incumbent Board Tries To Evade This Lawsuit By Changing The Position It Took In Its SEC Filings

In February, the incumbent board made an about-face. The defendants, after agreeing to a schedule leading to an injunction hearing on March 7, 2013, stated in an 8-K that if the Proxy Put was triggered, SandRidge's lenders would be "unlikely" to redeem their notes, because the notes were currently trading at a price greater than 101% of par.[52] Furthermore, the company would be able to obtain the "backup financing necessary" to repurchase any notes that were tendered.[53] Thus, the incumbent board no longer believed that electing an unapproved new slate would be "extreme" and "risky," as the incumbent board had described it in both its preliminary and definitive consent revocation statements. Instead, the incumbent board suggested that there might be *no* consequences at all to its failure to approve the insurgent slate.[54] Because of this lack of consequences, the defendants argued that expedited proceedings were unnecessary.

I did not grant the defendants' motion to vacate the scheduling order.[55] The defendants' motion was effectively an attempt to use a procedural mechanism to deny Kallick the relief he seeks in this lawsuit. If the motion had been granted, and the 60-day consent solicitation period had expired before the case was heard, Kallick's action would arguably have become moot. Furthermore, the incumbent board did not identify any reason why it had gone from informing its stockholders that the Proxy Put would represent an extreme risk to informing them that the Proxy Put represented *little* risk. Since September last year, SandRidge's bonds have been trading at well above 101% of par, just as they are now, a fact that the defendants acknowledge.[56] Thus, there is no reason, based on changing market conditions, why the board should have changed the information it gave to SandRidge's stockholders.

II. Kallick's Motion For Injunctive Relief

The incumbent board has refused to decide whether to approve TPG's slate for purposes of the Proxy Put, claiming that it would be confusing to

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[52] *See* February 8-K.
[53] *Id.*
[54] Defs.' Mot. to Vacate the Scheduling Order, at 2 (Feb. 11, 2013).
[55] *See* Tr. of Rulings of the Ct. (Feb. 15, 2013).
[56] *See* Morgan Stanley Presentation, at 4; *see also* Defs.' Ans. Br. 11.

the company's stockholders and detrimental to its position in the credit markets.[57] As a result of the incumbent board's non-decision, the electorate must consider the potential risks in electing a new slate of directors, an event that depending on which version of the incumbent board's own shifting view of reality one embraces, would either be of no consequence or be one that has an "extreme" deal of financial risk and cost. In his complaint, Kallick originally sought mandatory relief to require the board to approve the TPG slate.[58] In his brief, Kallick requested a narrower form of declaratory and injunctive relief to neutralize the incumbent board's non-decision. Kallick seeks (i) to enjoin the defendants from soliciting any consent revocations; (ii) to have any consent revocations obtained to date declared invalid; and (iii) to enjoin the defendants from taking any steps to hinder TPG's consent solicitation until they have complied with their fiduciary duties and have approved the TPG slate, or have explained in full why they will not approve it.[59]

The standard for a preliminary injunction in this court is well-known. To prevail on a motion for preliminary injunction, a plaintiff must prove that: (1) he is likely to succeed on the merits of his claims; (2) he will suffer imminent, irreparable harm if an injunction is not granted; and (3) the balance of equities weighs in favor of issuing the injunction.[60] Because the three prongs of this test are interconnected, I do not engage in a lengthy individual discussion of each one. Instead, I will discuss the facts in the record and the applicable law, and explain why the defendants are likely violating their fiduciary duty of loyalty to SandRidge and its stockholders. I then summarize, at the end, why Kallick prevails on all three prongs of the preliminary injunction test, and why I grant Kallick even more narrowly tailored injunctive relief than he seeks, but no mandatory or declaratory relief.

A. The Incumbent Board's Unconvincing Justification For Its

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[57] Defs.' Ans. Br. 2-3; Jordan Dep. 45:18-23 (explaining that the only harm of approving TPG's slate is that it would be "confusing to the shareholders").

[58] V. Am. Compl. 35-36.

[59] Pl's. Op. Br. 27.

[60] *Revlon, Inc. v. MacAndrews & Forbes Hldgs., Inc.*, 506 A.2d 173, 179 (Del. 1986) (citing *Gimbel v. Signal Cos.*, 316 A.2d 599, 602 (Del. Ch. 1974), *aff'd*, 316 A.2d 619 (Del. 1974)).

Refusal To Approve TPG's Slate

In defense of its non-decision as to whether to approve the TPG slate, the incumbent board makes a variety of cursory arguments. I now analyze them and make findings of fact as to them consistent with the appropriate procedural standard, which requires me to determine, from the record before me, what would likely be the state of reality found to exist after trial.[61] For reasons that may reflect the expedited nature of the case, but may also reflect the fact that the SandRidge board has engaged in inadequate deliberations concerning the Proxy Put, the record is decidedly spare. There are only two depositions in the record: one is of Daniel Jordan, a SandRidge director who is independent under New York Stock Exchange rules, and one is of Michael Johnson, a managing director at Morgan Stanley who is a financial advisor to SandRidge.

First, the defendants claim that the TPG slate does not consist of directors with sufficient energy industry experience.[62] The only available information about the nominees in the record, and the information the defendants also heavily rely on in reaching their conclusions about the nominees' qualifications, is the information available from the Definitive Consent Solicitation Statement, which is excerpted in brief:[63]

Name	Experience
Stephen Beasley	Mr. Beasley founded Eaton Group, an investment firm. He served as President of El Paso Corporation's Eastern Pipeline Group, which operates gas pipeline systems and distributes natural gas throughout the United States, for 4 years. While President of El Paso, he was also the Chairman and President of Tennessee Gas Pipeline Company and ANR Pipeline Company. He has served as a board of a director for several other companies in the energy industry.
Edward Moneypenny	Mr. Moneypenny was a senior Vice President and Chief Financial Officer of 7-Eleven, Inc. from 2002 to January 2006. In 2001, he was the President of and

[61] *E.I. du Pont de Nemours & Co. v. Bayer CropScience L.P.*, 958 A.2d 245, 251-52 (Del. Ch. 2008).

[62] Defs.' Ans. Br. 19.

[63] *See* Definitive Consent Solicitation Statement, at 17-21.

Name	Experience
	Chief Financial Officer of Covanta Energy Corporations which owns and operates infrastructure for the conversion of waste to energy. He was also the Chief Financial Officer of two other Fortune 500 energy companies, including Florida Progress Corporation (currently Duke Energy Corporation).
Fredric Reynolds	Mr. Reynolds served as Executive Vice President and Chief Financial Officer of CBS Corporation from January 2006 until August 2009. He also served as Chief Financial Officer of Westinghouse Electric Corporation from 1994 to 2000 when it was bought by CBS. Before Westinghouse, he served as Chief Financial Officer of Pepsi Company. He is currently a director of AOL, Inc., Mondelez International (formerly Kraft Foods, Inc.), and MGM Studios.
Peter Rothschild	Mr. Rothschild has 30 years of experience in investment and merchant banking. He is currently CEO of Daroth Capital Advisors. He was a managing director at Wasserstein Perella. Earlier in his career, at Drexel Burnham Lambert, he covered the energy industry for six years.
Dinakar Singh	Mr. Singh is a Co-Founder and CEO of TPG–Axon Capital. Before TPG, Mr. Singh was a partner at Goldman Sachs, where he worked for 14 years. He serves on the board of Columbia University Medical Center, the New York Public Library, the Rockfeller University, and Cold Spring Harbor Laboratories.
Alan Weber	Mr. Weber is currently CEO of Weber Group LLC, an investment management firm. He is also the former Chairman and CEO of U.S. Trust Co. He served as Aetna's Chief Financial Officer and worked at Citibank for 27 years.
Dan Westbrook	Mr. Westbrook has been a director of Enbridge Energy Company since 2007 and a member of its Audit, Finance, and Risk Committee. Before that role, he worked at BP China Gas Power, Upstream and at Amoco Corporation where he gained

Name	Experience
	experience developing energy and petroleum businesses.

Although the defendants admit that "five" of the directors in fact have "some" energy experience, they fault three of the five members for not having "upstream" oil and gas experience and the directors with upstream experience for not having experience with the Mississippian Play.[64] Despite these very particular arguments, the incumbent board has no reason to doubt the integrity of the TPG slate, as Jordan admitted in his deposition:

> Q: Did the board find out anything that would lead you to believe TPG-Axon's nominees are people of ill repute?
>
> A: No. I mean, that's—that's—no.
>
> Q: Did the board's internal investigation reveal that TPG-Axon's nominees were anything other than respected and well-accomplished business people?
>
> A: I'm sure they are in their own fields . . . .[65]

Taken as a whole, therefore, the record supports nothing more than the conclusion that the incumbent board, as expected, believes that it is managing the company in an optimal manner, that it has better qualifications than the TPG slate, that the TPG slate's plans for the company are not wise, and that the incumbents should therefore continue to run the company. In other words, the incumbent board has simply made the same determination that all incumbents who seek to continue in office make: we are better than the new guys and gals, so keep us in office. Such self-belief does not come close to a reasoned conclusion that the electoral rivals lack the integrity, character, and basic competence to serve in office. Nothing in this record

[64] Defs.' Ans. Br. 7-8.
[65] Jordan Dep. 40:2-10.

indicates that any incumbent board member or incumbent board advisor has any reasonable basis to dispute the basic qualifications of the TPG slate.

Second, the defendants used a leading question at a deposition to elicit the concern from Jordan that the company would be sued by noteholders if they approved of the nominees in bad faith:

> Q: Now, if the board were to approve the TPG-Axon slate even though it believed that the election of that slate would be harmful to SandRidge, would it be possible that bondholders could sue the company for making that approval decision in bad faith?
>
> A: Yeah. That's possible. Absolutely.[66]

But Jordan, while he was being examined by the opposing counsel, and before an hour-long break in the deposition, had already testified to a *diametrically opposite* conclusion:

> Q: Would approving TPG-Axon's director nominees for the limited purpose of the change of control provision violate any duties the company owes to its bondholders?
>
> A: *Violate any duties that we owe to our bondholders? Approving their slate? I don't think it does.*[67]

Relatedly, the incumbent board suggests that if it approves TPG's slate, this approval would compromise the company's ability to obtain financing because, presumably, such lenders would charge a higher price for credit, perceiving SandRidge as a company that "circumvents" change of control provisions.[68] The sum and substance of the record support for this proposition is this testimony by Johnson, the incumbent board's financial advisor:

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[66] *Id.* at 79:22-80:3.
[67] *Id.* at 75:18-24.
[68] Defs.' Ans. Br. 2-3.

Q: Would it be more difficult or expensive for a company like SandRidge to obtain financing without such a change of control provision?

A: Yes.

Q: If SandRidge were perceived as having approved the TPG-Axon slate simply in order to neutralize the change of control provisions in its debt instruments, could that have an effect on its ability to obtain financing in the future?

[Objection.]

A: It would—it would be highly likely in my opinion that it would have an impact on the price at which they could obtain financing. I'm not prepared to speculate on whether it would impact whether they could obtain financing or not.[69]

But, before he gave that answer, Johnson had testified as follows:

Q: Would a change in control at SandRidge affect market conditions for their bonds?

A: No.

Q: And why is that?

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[69] *Id.* Ex. 3, at 59:14-60:9 (Deposition of Michael Johnson (Feb. 22, 2013)) [hereinafter Johnson Dep.].

> A: The market conditions for the bonds are driven by factors that are separate from whether SandRidge has a change in control or not.[70]

At the same time as the incumbent board is arguing that creditors will exact a penalty for SandRidge's approval of a dissident slate, it also now argues to the court that, if the Proxy Put is triggered, there will be no harm even if the company does have to refinance, because the froth has returned to the debt markets, credit is easy to obtain, providers are competing to lend, and there will be insubstantial costs to refinance.[71] These arguments bring to mind one definition of genius, I suppose.[72] But viewed more realistically, these are fundamentally inconsistent propositions put forward to justify the incumbents' refusal to make an approval decision, one way or the other. In that regard, the lengths to which the incumbents' loyal financial advisor would go to aid their litigation aims were great but constrained: he refused to directly answer if it would be "harmful" to SandRidge to elect TPG's nominees.[73]

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[70] *Id.* at 30:6-14.

[71] The defendants have not quantified precisely the cost that failing to approve the TPG slate will impose on the company. They now suggest that the most likely cost of the Proxy Put is $17 million, which represents Morgan Stanley's 1% commitment fee of a $1.7 billion refinancing. The defendants assume that SandRidge will only need to refinance $1.7 billion because they subtract from the $4.3 billion principal of the notes outstanding $2.6 billion that the company has in cash through the recent sale of its Permian Basin assets. *See* Ans. Br. 27. This is a new position because the incumbent board earlier asserted that the full $4.3 billion would need to be refinanced, with higher refinancing costs. But, when SandRidge announced the sale of the Permian Basin assets, it stated that it would use the proceeds to "reduce debt, . . . fund capital expenditures and for general corporate purposes." Defs.' Ex. 4 (SandRidge press release (Feb. 26, 2013)). This indicates that not all of the $2.6 billion would be put towards paying off SandRidge's debt, and that SandRidge would need to obtain a commitment to refinance more than $1.7 billion. Furthermore, the defendants acknowledge that if noteholders did put back their debt, SandRidge would have to pay a take-out fee of 2% on the debt that SandRidge did reissue. Morgan Stanley Presentation, at 5. But at the same time, the defendants hold out the hope that financing could be obtained more cheaply from another bank. Defs.' Ans. Br. 28. The defendants have thus not provided any firm estimate of the cost that the Proxy Put will impose on the company. And perhaps most notably, the defendants' position that *if the TPG slate wins*, debt financing will be readily available to SandRidge belies any basis for asserting the TPG slate poses a rational threat to the company's ability to repay its debtholders.

[72] "The test of a first-rate intelligence is the ability to hold two opposed ideas in mind at the same time and still retain the ability to function." F. Scott Fitzgerald, *The Crack-Up* (1936).

[73] *See* Johnson Dep. 61:24-62:9 ("Q: Would—in your view, could it be harmful for the company to elect a slate that lacked that kind of exploration and production experience? A: I would say that because the company's growth is driven by the development of the Mississippian Play, as the company is currently configured, that *it would be more helpful to have board members who understand the mechanics of that position.*") (emphasis added).

Notably, the incumbent board and its financial advisors have failed to provide any reliable market evidence that lenders place a tangible value on a Proxy Put trigger—not a change in board composition accompanying a merger or acquisition or another type of event having consequences for the company's capital structure, but a mere change in the board majority. In fact, the evidence in the record indicates that credit providers would be happy to keep lending to the company if the board changed majority. Johnson's own employer, Morgan Stanley has offered to refinance SandRidge's debt for a 1% fee if the board majority turned over.[74] Thus, Johnson's suggestion that the incumbent board's approval of the TPG slate might have an effect on the price at which SandRidge could obtain financing is *inconsistent with his own presentation to the SandRidge board that Morgan Stanley would be happy to provide financing to SandRidge even if the TPG slate was in control.*

Kallick, for his part, stresses that Jordan could not recall any discussion about whether to include the Proxy Put in the company's notes and admitted that the company derives no benefit from them.[75] This testimony implies that the board gave little or no consideration to the adoption of the Proxy Put. But, boards have a duty to their stockholders to pay very close attention to provisions that affect the stockholder franchise, such as Proxy Puts. This court made this duty explicit in *Amylin.*[76]

Taken as a whole, the record, such as it is, reveals the following. The incumbent board has no reasonable basis to conclude that the TPG slate is unqualified to serve with basic competence and integrity as the directors of a public energy company. The incumbent board has identified no specific threat that the TPG slate's plans have on the ability of SandRidge to repay its creditors. To the contrary, its own current argument that the triggering of the Proxy Put is no longer an "extreme" financial risk, but a yawn, because lenders will be glad to cheaply refinance SandRidge's debt if the TPG slate wins, refutes any rational basis for the refusal to approve the TPG slate for purposes of relieving SandRidge of any harm from triggering the Proxy Put. Nonetheless, the board refuses to make a decision whether to approve the TPG slate for purposes of the Proxy Put, a protection that is supposedly for the benefit of the lenders, and thus leaves the corporation exposed to the potential for a mandatory refinancing of its $4.3 billion in long-term debt if the TPG slate is elected.

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[74] Morgan Stanley Presentation, at 5.

[75] Jordan Dep. Tr. 21:17-23:1, 23:21-24:2.

[76] *San Antonio Fire & Police Pension Fund v. Amylin Pharms. Inc.*, 983 A.2d 304, 319 (Del. Ch. 2009).

Regrettably, I am left with the impression that this condition of piquant ambiguity is one that the incumbent board, for tactical electoral reasons, finds of utility in its attempt to remain in power. That impression is reinforced by the shifts in position by the incumbents as this litigation has progressed, positions that seem more convenient than principled. In this context where the importance of the stockholders' right to choose is paramount, games-playing is not something our law takes lightly.[77]

With those basic facts in mind, I turn to resolving the application before me, which is neatly framed by the parties' starkly different views of what standard applies to determining whether the incumbent directors have likely breached their fiduciary duties by failing to approve the TPG slate for purposes of the Proxy Put.

B. The Standard Of Review

For their part, the incumbent board argues that the standard of review is the plain vanilla business judgment rule, which requires that their decision be approved if it can be attributed to any rational business purpose.[78] Thus, the incumbent board argues for something as close to non-review as our law contemplates.[79]

Not unexpectedly, Kallick comes playing the Sousa-inspired sounds of *Blasius*, arguing that the incumbents may only fail to approve the TPG slate if they can prove that there is a "compelling justification" for their decision.[80] Kallick argues that, because the effect of the Proxy Put is to place a toll on the voting decision of the electorate, the primary purpose of such a provision is disenfranchising within the meaning of the *Blasius* standard. As readers familiar with *Blasius* are well-aware, that standard of review is a potent one and its express trigger was stated in correspondingly stark terms. For the *Blasius* standard to be invoked, the challenged action had to be "taken for the sole or primary purpose of thwarting a shareholder vote."[81] If that predicate was laid, then the defendants could only justify their actions by showing a compelling justification, a very high standard drawing on the

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[77] *Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971) ("[I]nequitable action does not become permissible simply because it is legally possible.").

[78] *See Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

[79] *See generally* Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 Vand. L. Rev. 83 (2004) (arguing that, under the business judgment rule, courts refrain from reviewing directors' decisions).

[80] *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 661 (Del. Ch. 1988).

[81] *Id.* at 662.

closest scrutiny used in cases involving racial discrimination and restrictions on political speech.[82]

For reasons I have explained elsewhere, and will not repeat in detail, *Blasius*' importance rests more in its emphatic and enduring critical role in underscoring the serious scrutiny that Delaware law gives to director action that threatens to undermine the integrity of the electoral process, than in its articulation of a useful standard of review to decide actual cases.[83] Precisely because our law embraces a republican model giving directors substantial authority to use their own judgment while in office, it is vital that the stockholders have a genuinely fair opportunity to elect new directors.[84]

But the standard of review *Blasius* offers does little to address situations like this, where a contractual provision cannot be said to have the "sole or primary purpose" of impeding the stockholders' vote, because it might have a legitimate purpose of protecting creditors who in fact insisted on its inclusion for their own good-faith reasons, but does have the obvious potential to tilt the electoral playing field toward the incumbent board.

For reasons I have previously explained, our Supreme Court's invocation of a flexible, intermediate standard of review—*Unocal*—to address situations where boards of directors make decisions that have clear implications for their continued control was explicitly designed to give this court the ability to use its equitable tools to protect stockholders against unreasonable director action that has a defensive or entrenching effect.[85] By enabling the Court of Chancery to examine whether the directors taking actions have acted in a circumstantially reasonable way, the Supreme Court provided a responsible form of review that smokes out self-interest and pretext, by requiring boards that face the omnipresent specter of *Unocal* to justify their actions as reasonable in relationship to a threat faced by the corporation.[86] This Court has followed the Delaware Supreme Court and

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[82] *See, e.g.*, *United States v. Playboy Entm't Group*, 529 U.S. 803 (2000) ("If a statute regulates speech based on its content, it must be narrowly tailored to promote a compelling Government interest."); *Adarand Constructors, Inc. v. Pena*, 515 U.S. 200, 227 (1995) ("[G]overnment may treat people differently because of their race only for the most compelling reasons.").

[83] *See Chesapeake Corp. v. Shore*, 771 A.2d 293, 317-24 (Del. Ch. 2000); *Mercier v. Inter-Tel (Del.), Inc.*, 929 A.2d 786, 805-13 (Del. Ch. 2007). *See generally* Leo E. Strine, Jr., *The Story of* Blasius Industries, Inc. v. Atlas Corp., *in Corporate Law Stories* 244, 275 (J. Mark Ramseyer, ed., 2009).

[84] *Blasius*, 564 A.2d at 659 ("The shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests.").

[85] *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954-55 (Del. 1985).

[86] *E.g.*, *MM Cos., Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1129 (Del. 2003) ("Both

applied *Unocal* in these situations with a special sensitivity towards the stockholder franchise.[87]

By definition, a contract that imposes a penalty on the corporation, and therefore on potential acquirers, or in this case, simply stockholders seeking to elect a new board, has clear defensive value. Such contracts are dangerous because, as will be seen here, doubt can arise whether the change of control provision was in fact sought by the third party creditors or willingly inserted by the incumbent management as a latent takeover and proxy contest defense. *Unocal* is the proper standard of review to examine a board's decision to agree to a contract with such provisions and to review a board's exercise of discretion as to the change of control provisions under such a contract.[88]

Of course, the mere fact that the court uses a heightened reasonableness standard does not mean that the directors will fail to satisfy it. A reasonableness standard is just that. But it does mean that the directors must comply with their *Unocal* duties by identifying a circumstantially proper and non-pretextual basis for their actions, particularly when their actions have the effect of tilting the electoral playing field against an opposition slate. Relatedly, *Unocal* implements, and does not displace, *Schnell*'s generalized insistence that any director action be in fact taken for a proper purpose.[89] By smoking out the directors' reasons, *Unocal* surfaces the issues at stake, including the possibility of bad faith.[90] With these thoughts in mind, I now explain why the defendants' actions cannot pass the *Unocal* test.

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standards recognize the inherent conflicts of interest that arise when a board of directors acts to prevent shareholders from effectively exercising their right to vote either contrary to the will of the incumbent board members generally or to replace the incumbent board members in a contested election."); *Stroud v. Grace*, 606 A.2d 75, 92, n.3 (Del. 1992) (incorporating *Blasius* standard within *Unocal* review).

[87] *See Johnston v. Pedersen*, 28 A.3d 1079, 1089-90 (Del. Ch. 2011) (applying *Unocal* to preferred stock issuance designed to affect proxy contest); *Mercier*, 929 A.2d at 812-13 (applying *Unocal* to postponement of stockholder vote); *Chesapeake*, 771 A.2d at 330-334 (analyzing supermajority bylaw adopted to affect consent solicitation under *Unocal*).

[88] *See generally Moran v. Household Int'l, Inc.*, 500 A.2d 1346 (Del. 1985) (explaining that defensive measure must be evaluated not only at the time of adoption but also when later used in the face of an actual threat).

[89] *Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971).

[90] *See Unocal*, 493 A.2d at 955 (noting that the first prong of the *Unocal* test is "designed to ensure that a defensive measure to thwart or impede a takeover is indeed motivated by a good faith concern for the welfare of the corporation and its stockholders"); *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1375 (Del. 1995) (noting that a board that takes defensive measures in response to a hostile offer must show, under the first prong of the *Unocal* test, that "it determined in good faith [] that the [offer] presented a threat . . . that warranted a defensive response").

C. The Incumbent Board's Actions Are Likely A Violation Of Its Fiduciary Duty

Here, the directors have failed to demonstrate a reasonable justification for their refusal to consider whether to approve the TPG slate for purposes of the good faith standard of *Unocal*. In *Amylin*, this court made plain that the board's duty in exercising its discretion under such a contract was focused on the best interests of the corporation and its stockholders, and that its only duty to the creditors was to honor the implied covenant of good faith and fair dealing.[91] The crucial issue for the board's determination is the board's obligation to act in good faith: as Vice Chancellor Lamb held, the board could approve the new slate if "passing control would not constitute a breach of the directors' duty of loyalty to the corporation and its stockholders."[92] Because, as Vice Chancellor Lamb also noted, the failure to approve a new slate might "impinge on the free exercise of the stockholder franchise," and because a board that acts in good faith must seek to protect the stockholders' ability to make an uncoerced choice of directors, it follows that a board may only *fail* to approve a dissident slate if the board determines that passing control to the slate would constitute a breach of the duty of loyalty, in particular, because the proposed slate poses a danger that the company would not honor its legal duty to repay its creditors.[93]

Thus, this court in *Amylin* focused on the nature of the Proxy Put as a provision giving the creditors protection against a new board that would threaten their legitimate interests in getting paid.[94] Such situations could arise, for example, because the proposed new board consists of "known looters" or persons of suspect integrity. Or, the insurgent slate could have plans for the company posing a genuine and specific threat to the corporation and its ability to honor its obligations to its creditors that prevent the incumbent board from approving them in good conscience for purposes of

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[91] *San Antonio Fire & Police Pension Fund v. Amylin Pharms. Inc.*, 983 A.2d 304, 314-16 (Del. Ch. 2009).

[92] *Id.* at 316 n.37.

[93] *Id.* at 319.

[94] *Id.* at 307 ("[C]onstrued in accordance with generally applied standards, the provision is properly understood to permit the incumbent directors to approve as a continuing director any person, whether nominated by the board or a stockholder, as long as the directors take such action in conformity with the implied covenant of good faith and fair dealing and in accordance with their normal fiduciary duties.").

the Proxy Put.[95] By contrast, where an incumbent board cannot identify that there is a specific and substantial risk to the corporation or its creditors posed by the rival slate, and approval of that slate would therefore not be a breach of the contractual duty of good faith owed to noteholders with the rights to the Proxy Put, the incumbent board must approve the new directors as a matter of its obligations to the company and its stockholders, even if it believes itself to be better qualified and have better plans for the corporation than the rival slate. The stockholders, after all, have a fundamental interest in freely choosing for themselves who should constitute the board.[96]

In other words, the duty of loyalty requires the incumbent board to exercise their contractual discretion with the best interests of SandRidge and its stockholders firmly in mind, to the extent that it can do so without breaching the very limited obligations it owes to its noteholders. The parties do not dispute that, under *Amylin*, the incumbent board has the power to approve of TPG's nominees without endorsing the dissident's slate and maintaining its ability to run its own campaign.[97] Thus, it is undisputed that the incumbent board can neutralize any adverse consequences from the Proxy Put if TPG prevails in its proxy contest without signaling its support for the election of TPG's nominees. In this case, the corporation's best interest seems rather obvious, which is in letting its stockholders choose without fear of a compelled refinancing. From a purely financial standpoint, it is clear that SandRidge is not advantaged from being compelled to make an offer to redeem its long-term debt. There is only possible pain, and no possible gain, to SandRidge from triggering the Proxy Put.

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[95] Vice Chancellor Lamb wrote: "The key question is whether approval by the board, under the given circumstances, comports with the company's implied duty of good faith and fair dealing *which inheres in all contracts, including the Indenture*." *Amylin*, 983 A.2d. at 315 (emphasis added). Thus, the court recognized that the board should take into account the interests of its creditors in deciding whether to approve the slate. I read this statement as qualifying the court's later statement, in a footnote, that "the directors are under absolutely *no* obligation to consider the interests of the noteholders" in deciding whether to approve the new slate. *Id.* at 316 n.37. To be more precise, the directors are under no obligation to place any greater emphasis on the interests of the noteholders in making their decision as to the Proxy Put than as to any other decision that implicates the noteholders' contractual rights.

[96] *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988). ("The shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests. Generally, shareholders have only two protections against perceived inadequate business performance. They may sell their stock (which, if done in sufficient numbers, may so affect security prices as to create an incentive for altered managerial performance), or they may vote to replace incumbent board members.").

[97] *Amylin*, 983 A.2d at 313-14.

Regrettably, as I have discussed, the thin and shifting arguments of the incumbent board do not persuade me that any legitimate interest of SandRidge was served by the board's failure to make an approval decision. Rather, the incumbent board's behavior is redolent more of the pursuit of an incremental advantage in a close contest, where a small margin may determine the outcome, than of any good faith concern for the company, its creditors, or its stockholders. That self-interested, tactical reason for withholding approval implicates *Amylin*'s basic premise because an "eviscerating" threat to the shareholder franchise exists when the board retains the power to approve the dissident slate, but refuses to exercise that power to protect itself or give itself an advantage in a proxy context.[98] I therefore conclude that the board has likely acted with an absence of good faith and reasonableness inconsistent with their fiduciary duties.

D. The Incumbent Board Cannot Rely On The Hills Case

The defendants look to this court's decision in *Hills Stores Co. v. Bozic* as comfort for their conduct here.[99] That is an odd place for them to find repose. For starters, in *Hills*, the plaintiff was a hedge fund that had successfully taken control of the company in a proxy fight. The hedge fund's successful campaign for control followed years of pressure efforts that began within a year of the company's emergence from bankruptcy, when the hedge fund proposed having the company leverage up to repurchase $150 million of its shares.[100] During the course of the pressure campaign, severance agreements were entered into by the board with top managers that protected those managers by granting them severance if a change of control occurred that was not approved by the incumbent board, including by virtue of a proxy contest.[101] Litigation over these severance agreements and other matters occurred, which involved the hedge fund itself. That litigation was settled with the hedge fund as a party, the severance agreements were left in place, and the hedge fund got an agreement by the company to repurchase $75 million worth of its shares.[102]

Peace was fleeting and the hedge fund came back threatening the very next year, questioning the incumbent board's plans to make capital

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[98] *Id.* at 316.
[99] 769 A.2d 88 (Del. Ch. 2000).
[100] *Id.* at 91.
[101] *Id.* at 91-92.
[102] *Id.* at 93-94.

investments in the business and instead proposing to buy the company itself in a highly leveraged transaction. The hedge fund claimed it could finance up to half of the equity check necessary and had received a "highly confident" promise of debt financing to refinance all of the company's outstanding debt.[103] The incumbent board did not take defensive steps to stop the hedge fund, but refused to approve the change in control for purposes of the severance agreements or the company's credit agreements, which had a similar provision to the Proxy Put in this case.[104] After the hedge fund had installed its own slate as directors, it had the new board sue the outgoing directors for breach of fiduciary duty, alleging that the directors' failure to approve the change of control had cost the company $20 million. This court granted summary judgment to the defendant ex-directors under the *Unocal* standard.

The distinctions between *Hills* and this case are several. To begin with, the primary focus of the litigation was on severance agreements. These involve considerations that are distinct from credit agreements. As I have observed, a lender wants to get paid. An employee wants to get paid too, but has concerns about the identity of her boss that are far more extensive, and legitimately so. A lender, such as the noteholders in this case, can protect itself by financial covenants, such as coverage and leverage ratios.[105] The reality is that the debt, in this context, issued by the company is impersonal. Once the debt is underwritten, it trades like a security. An employee cannot protect herself against a fundamental shift in managerial approach, and has an obvious interest in knowing who her boss is. The record in *Hills* made clear that the board viewed itself as having made a specific, enforceable promise to pay severance to the executives if the incumbent board did not approve a change of control of the board itself.[106] Indeed, the severance agreements were forged specifically because of the managers' fear that the hedge fund itself would take control.[107] Thus, the contractual context and record involve, in my view, distinctive considerations that the defendants here slight.

Lumping together all contracts that have change of control provisions may have some simplistic analytical appeal. The costs, however, of ignoring that different types of contracts address different concerns strike me as large,

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[103] *Id.* at 95.
[104] *Id.* at 100-01.
[105] Indenture artt. 4-5.
[106] *Hills*, 769 A.2d at 100-01.
[107] *Id.* at 91-92.

and the contractual obligation that the corporation owes to its contractual partner in exercising discretion to approve a change in control is of course influenced by the contractual expectations of that partner. And even as to credit agreements, not all changes of control are the same. Critical for lenders are changes in control that directly affect capital structures in a way that could impair the lenders' ability to get repaid, such as mergers or leveraged equity acquisitions. These concerns were paramount in *Hills*, where the board feared, rightly, that an acquirer would leverage up the company.[108] By contrast, in this case, TPG has said that it does not want to leverage SandRidge, but wishes to explore the possibility of selling off assets, in part to reduce SandRidge's cost of capital.[109] And the incumbent board's own financial advisor has offered to finance the company if the insurgent slate prevails, negating any suggestion that the insurgent slate poses a substantial threat to creditors.

As important, the board in *Hills* identified specific threats to the fundamental ability of the company to honor its legal obligations that were posed by the hedge fund and its specific plans for the company. Unlike SandRidge, which the defendants admit is not facing a solvency problem, Hills Stores was in a weak financial state. The company had only recently emerged from bankruptcy and was in the tumultuous retail industry. Furthermore, the hedge fund was proposing to have the company take on enormous leverage having already pressured it to leverage up to repurchase shares the year before, while boasting that it was able to write a full 50% of the equity check, on a deal in which equity was to comprise less than a quarter of the acquisition price.[110] Thus, in contrast to the record here, the board in *Hills* identified specific concerns that turning over control to the hedge fund would be a breach of duty of loyalty because the hedge fund's plans would "be seriously adverse to the interests of the company and its stockholders."[111]

After touting its ability to refinance the company's debt and finance an LBO, the hedge fund in fact won control. It promptly made good on the board's concerns by being unable to live up to its boasting, confirming the reasonableness of the board's basis for failing to approve the change in control.[112]

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[108] *Id.* at 91.
[109] *E.g.*, Definitive Consent Solicitation Statement, at 12.
[110] *See Hills*, 769 A.2d at 95-96.
[111] *Id.* at 101.
[112] *Id.*

The sketchy testimony of Jordan that he regards the incumbent slate on which he serves as better qualified than the TPG slate, and that the TPG slate lacks enough experience and does not have a clear plan to replace Ward as CEO, does not approach the specific basis that the board in *Hills* identified as the basis for failing to approve a change in control.[113] Therefore, *Hills* cuts against, rather than supports, SandRidge's position.

E. Kallick Is Entitled To A Preliminary Injunction

Kallick has shown that he is entitled to a preliminary injunction. It appears, on this record, that the SandRidge directors are violating their fiduciary duty. Thus, for the reasons I have explained, he has a strong likelihood of success on the merits. On the second prong of the test, because "it constitutes a fundamental offense to the dignity of [the] corporate office for a director to use corporate power to seek to coerce shareholders in the exercise of the vote," there is immediate, irreparable harm when the directors of a corporation leverage a Proxy Put to enhance the incumbent's board chances of procuring stockholder votes in a closely contested election, which could be decided by a few percentage points.[114] Irreparable harm also exists because damages would be difficult to calculate.[115] And, on the third prong, I find that the balance of equities favor Kallick over the incumbent board. This is particularly true because Kallick is seeking narrowly tailored relief that is proportionate to the conduct of the incumbent board. Therefore, the conditions for a preliminary injunction are satisfied.

In his complaint, Kallick moved for mandatory and declaratory relief requiring the incumbent board to approve the TPG slate and to have all consent revocations the board has received so far declared invalid.[116] In his briefing, Kallick requests a narrower form of relief, seeking (i) to enjoin the defendants from soliciting any consent revocations; (ii) to have any consent

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[113] Jordan Dep. 35:25-36:20 ("Q: At the December 27th meeting, what was discussed with respect to the qualifications of TPG-Axon's nominees? A: *I really don't recall*, but it's the pounding theme from day one is that *they are not only unqualified, they are—they would totally destroy and erode all value away from the company*. Q: Did Mr. Ward express an opinion on TPG-Axon's nominees at the December 27th meeting? A: I don't recall what he said. Q: Has Mr. Ward ever expressed an opinion regarding TPG-Axon's director nominees? A: I'm sure he has, but I don't—I don't recall the exact verbiage or what he said. He knows they're not qualified. Q: Okay. Has he provided any additional color beyond his opinion that they're unqualified? A: No, he hasn't.") (emphasis added).

[114] *Sutton Hldg. Corp. v. DeSoto, Inc.*, 1991 WL 80223, at * 1 (Del. Ch. May 14, 1991).

[115] *See Sealy Mattress Co. v. Sealy, Inc.*, 532 A.2d 1324, 1341 (Del. Ch. 1987).

[116] V. Am. Compl. 35-36.

revocations obtained to date declared invalid; and (iii) to enjoin the defendants from taking any steps to hinder TPG's consent solicitation until they have complied with their fiduciary duties, and have approved the TPG slate or explained in full why they will not approve it.[117] Because this is a motion for a preliminary injunction, I grant the negative injunctive relief only, and do not grant the mandatory or declaratory relief.[118] Therefore, I enjoin the incumbent board from: (i) soliciting any further consent revocations; (ii) relying upon or otherwise giving effect to any consent revocations they have received to date; and (iii) impeding TPG's consent solicitation process in any way, unless and until the board approves the TPG slate for the limited purposes of the Proxy Put. Given the cloud the incumbent board has intentionally flown over the voting decisions and the absence of any rational, good faith justification for its non-decision as to approval, I believe this limited injunctive relief is proportionate and equitable. The incumbent board is not without options. It can solicit consent revocations again if it decides to approve the TPG slate for purposes of the Proxy Put. And SandRidge stockholders, of course, remain free to revoke any consent given to TPG. SandRidge may disclose this decision publicly in an SEC filing and that will make that option clear.

IV. Conclusion

I grant Kallick injunctive relief as set forth in this opinion. The plaintiff is to submit an implementing order, after notice as to form to the defendants, by the end of the day.

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[117] Pl's. Op. Br. 27.

[118] *See, e.g.*, Williamson v. McMonagle, 83 A. 139, 140 (Del. Ch. 1912) ("Preliminary injunctions should not generally be mandatory . . . .").

MESO SCALE DIAGNOSTICS, LLC, ET AL v. ROCHE DIAGNOSTICS GMBH., ET AL

No. 5589-VCP

In the Court of Chancery of the State of Delaware

February 22, 2013
Revised: March 8, 2013

Collins J. Seitz, Jr., Esquire, and David E. Ross, Esquire, Seitz Ross Aronstam & Moritz LLP, Wilmington, Delaware; and Mark C. Hansen, Esquire, Michael J. Guzman, Esquire, Gregory G. Rapawy, Esquire, Joseph S. Hall, Esquire, and Christopher C. Funk, Esquire, of Kellogg, Huber, Hansen, Todd, Evans & Figel, P.L.L.C., Washington, D.C.; Attorneys for Plaintiffs.

Andre G. Bouchard, Esquire, and Jamie L. Brown, Esq., Bouchard Margules & Friedlander P.A., Wilmington, Delaware; and Nancy J. Sennett, Esquire, Paul Bargren, Esquire, Brett H. Ludwig, Esquire, and Eric L. Maassen, Esquire, of Foley & Lardner LLP, Milwaukee, Wisconsin; Attorneys for Defendants.

PARSONS, *Vice Chancellor.*

This action is before me on a motion for summary judgment relating to, among other things, license rights to sophisticated diagnostic and assay technology. In 2003, a foreign pharmaceutical and diagnostic holding company lost or was in danger of losing its exclusive license to that technology. The holding company sought to acquire a new license from the then-patent holder. In 2003, the holding company entered into a series of contemporaneously executed agreements that granted it a new non-exclusive license from the patent holder. The plaintiffs, two Delaware limited liability companies with disputed springing rights to the same patented technology, consented to the second non-exclusive license. As part of that transaction, the holding company acquired the patent holder, but not before the intellectual property assets were transferred to a separate company. In 2007, the holding company acquired that separate company through a reverse triangular merger.

In 2010, the plaintiffs filed the complaint in this action asserting that the foreign holding company and a number of their affiliates breached two

agreements related to the 2003 transaction. In the first count, the plaintiffs claim that the 2007 reverse triangular merger was an assignment by operation of law that required their consent. The plaintiffs' second count asserts that the defendants breached the new 2003 license by selling products and services based on the technology outside the licensed field of use.

The defendants have moved for summary judgment on multiple grounds. As a preliminary matter, the defendants contend that the first count is time-barred by the doctrine of laches. The defendants also seek summary judgment on the first count on the grounds that: (1) the anti-assignment clause in a global consent signed by the plaintiffs was intended to govern only the assignment of rights contained in that global consent and (2) a reverse triangular merger cannot be an assignment by operation of law. In seeking summary judgment on the second count, the defendants contend that the plaintiffs were not parties to the license agreement with the right to enforce the provisions of that agreement. In that regard, the defendants argue that the contract in question is unambiguous and that there is no triable issue of material fact relating to its meaning.

Having considered the parties' extensive briefing and arguments and the voluminous record before me at this stage, I grant summary judgment on the first count on the basis that the reverse triangular merger was not an assignment by operation of law or otherwise, such that it would have required the plaintiffs' consent. I deny, however, the defendants' motion for summary judgment on the second count because the license agreement is ambiguous, the defendants failed to prove that New York law conclusively bars the plaintiffs' claim, and the plaintiffs have raised triable issues of material fact.

I. BACKGROUND

A. The Parties

Plaintiffs Meso Scale Diagnostics, LLC ("MSD") and Meso Scale Technologies, LLC ("MST" and, collectively, "Plaintiffs" or "Meso") are Delaware limited liability companies. MST was founded by Jacob Wohlstadter to commercialize his invention of a new application of electrochemiluminescent ("ECL") technology. In 1995, MST and IGEN International, Inc. ("IGEN") formed MSD as a joint venture.[1] The joint venture was created to research and develop the use of various technologies

[1] *See* Transmittal Aff. of Jamie L. Brown ("Brown Aff.") Ex. 5.

in diagnostic procedures, including procedures utilizing ECL technology.[2] Jacob Wohlstadter is the President and Chief Executive Officer ("CEO") of MSD and MST.

The defendants in this case are all affiliates or subsidiaries of the F. Hoffmann-La Roche, Ltd. family of pharmaceutical and diagnostics companies. Roche Holding Ltd. ("Roche Holding") is a publicly traded joint stock company organized under the laws of Switzerland.[3] Roche Diagnostics GmbH is a limited liability company organized under the laws of Germany and a wholly owned subsidiary of Roche Holding.[4] Defendant Roche Diagnostics Corp., which is incorporated in Indiana, is also a wholly owned subsidiary of Roche Holding.[5] IGEN is a Delaware corporation that was acquired by Roche Holding in 2003 and remains a wholly owned subsidiary of Roche Holding.[6] IGEN LS, LLC ("IGEN LS") is a Delaware limited liability company and wholly owned subsidiary of IGEN.[7] BioVeris Corp. ("BioVeris") is a Delaware corporation and wholly owned subsidiary of Roche Holding.[8] BioVeris owns and licenses a portfolio of patents based on and related to ECL technology.[9] Lili Acquisition Corp. ("Lili Acquisition") was subsidiary of Roche Holding that was merged into BioVeris on June 26, 2007 and no longer exists.[10] The following diagram depicts the relationships of the defendants (collectively "Defendants" or "Roche"):

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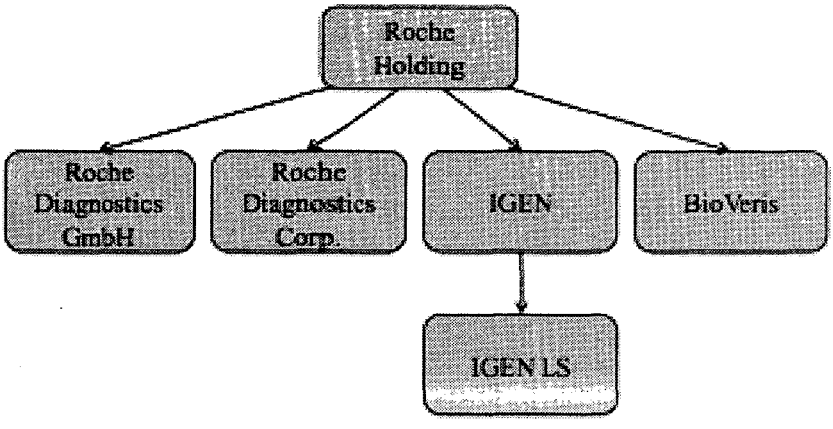
[2] *See id.* at 00036568.
[3] Decl. of Claus-Joerg Ruetsch in Supp. of Defs.' Mot. for Summ. J. ("Ruetsch Decl.") ¶ 2.
[4] *Id.* ¶ 3.
[5] *Id.* ¶ 4.
[6] *Id.* ¶ 5.
[7] *Id.* ¶ 6.
[8] *Id.* ¶ 7.
[9] Ruetsch Decl. ¶ 8.
[10] *Id.* ¶ 9.



B. Facts[11]

1. The 1992 License

In 1992, IGEN granted Boehring Mannheim GmbH ("BMG"), a company acquired by Roche in 1998, a license (the "1992 License") to use its patented ECL technology.[12] The 1992 License was narrow in scope and only allowed BMG to use the licensed technology in hospitals, blood banks, and clinical reference laboratories.[13] The license explicitly excluded use of the technology in the proximity of a patient, such as home, patient bedside, ambulance, and physician office uses.[14]

2. The MSD License

MSD was formed in 1995 as a joint venture between IGEN and MST, and was intended to be the exclusive vehicle for developing and commercializing the use of various technologies in diagnostic procedures, including procedures utilizing ECL technology.[15] IGEN also "granted to MSD an exclusive, worldwide, royalty-free license [*i.e.*, the "MSD License"]

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[11] Unless otherwise noted, the facts set forth in this Opinion are undisputed and taken from the verified pleadings, admissions, affidavits, depositions, and other evidence submitted to the Court.

[12] Brown Aff. Ex. 9.

[13] *Id.* §§ 1.4, 4.1–4.2.

[14] *Id.* § 1.4.

[15] Brown Aff. Ex. 5 at 00036568, § 4.1.

to practice the IGEN Technology to make, use and sell products or processes (A) developed in the course of the Research Program, or (B) utilizing or related to the Research Technologies."[16] Those technologies included "selection and screening methods," "electrodes," and "multi-array diagnostic[s]."[17] The MSD License has a perpetual term and provides that it will survive a termination of the MSD joint venture for any reason.[18] The MSD License also contains a now-disputed springing right under which, if an exclusive license previously granted to a third party, such as the exclusive rights granted to Roche under the 1992 License, was terminated or IGEN was no longer restricted by such a license from licensing to MSD, the technology automatically would be licensed to MSD.[19] Finally, IGEN agreed, as part of the MSD joint venture agreement (the "Joint Venture Agreement") and for the term of that agreement, that it would not use or allow its technology to be used to compete with MSD with respect to the Research Program.[20]

3. The Fourth Circuit litigation

In 1997, IGEN brought suit against Roche for breach of contract for, among other things, failing to pay royalties, failing to share ECL improvements with IGEN, and selling ECL-based products outside the contractually limited field.[21] While the suit was ongoing, Roche allegedly sought to settle with IGEN by acquiring ownership or access to the ECL rights.[22] In 2001, Roche made a public tender offer to acquire IGEN for $1.5 billion.[23] After conducting due diligence, however, Roche became concerned that acquiring IGEN "would *not* achieve the stated objectives of unencumbered ownership, avoidance of future litigation and discontinuation

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[16] Transmittal Aff. of David E. Ross in Supp. of Pls.' Opp'n to Defs.' Mot. for Summ. J. ("Ross Aff.") Ex. 3 § 2.1.

[17] Brown Aff. Ex. 5 § 1.11.

[18] *Id.* § 6.1.

[19] Ross Aff. Ex. 3 § 2.1 ("In the event any such exclusive license terminates, or IGEN is otherwise no longer restricted by such license from licensing such technology to MSD, such technology shall be, and hereby is, licensed to MSD pursuant hereto."). The scope and exclusive nature of MSD's rights under Section 2.1 of the MSD License is disputed by Roche. Because the record was not fully developed on this question, I assume for purposes of Roche's summary judgment motion that any license granted pursuant to Section 2.1 is exclusive.

[20] Brown Aff. Ex. 5 § 4.1.

[21] *See IGEN Int'l, Inc. v Roche Diagnostics GmbH*, 335 F.3d 303, 308 (4th Cir. 2003).

[22] Ross Aff. Ex. 9 at 771 (Keller), 961 (Ruetsch).

[23] *Id.* Ex. 11 at 0036626.

of business relationships with business entities controlled by the Wohlstadter family."[24] Roche ultimately informed IGEN that it could not pursue an acquisition at that time.[25] During later settlement negotiations in 2002, Roche sought to have MSD and MST "consent to and join in the license granted to Roche as necessary to [e]nsure Roche's non-exclusive use of the ECL Technology in Roche's Field."[26]

While negotiations were still ongoing, the jury returned a special verdict in IGEN's favor finding that Roche had materially breached the 1992 Agreement and awarding compensatory and punitive damages against it.[27] As a result, the United States District Court for the District of Maryland then allowed IGEN to terminate the 1992 License; the United States Court of Appeals for the Fourth Circuit affirmed that decision on July 9, 2003.[28] That same day, IGEN sent Roche a notice purporting to terminate the 1992 License.[29] As a result of the termination of the 1992 License and MSD's springing rights in the MSD License, those rights, according to MSD, were automatically and exclusively licensed to MSD.[30] In other words, Plaintiffs appear to contend that the ECL rights IGEN previously had licensed to Roche were now exclusively licensed to MSD.[31]

4. The 2003 Transaction

Roche had expressed concern over the possible termination of the 1992 License in its 10-K for the fiscal year ended March 31, 2003, stating that in the event the 1992 License was terminated, its business would be materially adversely affected.[32] Not surprisingly, therefore, just two weeks after the appellate ruling, Roche sought to reacquire ECL licensing rights so as to preserve its immunoassay business, which relied on ECL technology. Ultimately, Roche agreed to purchase IGEN for $1.25 billion and, along with IGEN, MSD, and MST, entered into a transaction (the "2003

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[24] *Id.*

[25] *Id.*

[26] Ross Aff. Ex. 16.

[27] *IGEN Int'l, Inc. v. Roche Diagnostics GmbH*, 335 F.3d at 308.

[28] *Id.* at 315.

[29] Ross Aff. Ex. 40 at 007352324, Ex. 41.

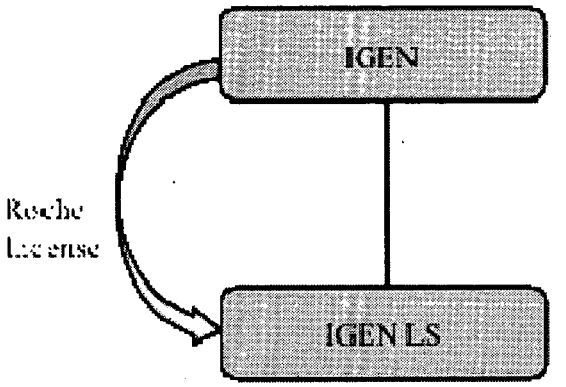
[30] *See id.* Ex. 3 § 2.1 ("In the event any such exclusive license terminates . . . such technology shall be, and hereby is, licensed to MSD pursuant hereto.").

[31] *Id.* Ex. 21 at 281.

[32] Brown Aff. Ex. 12 at 0019211-12.

Transaction"), which was memorialized in a number of contemporaneous agreements (the "Transaction Agreements.").[33]

As part of the 2003 Transaction, IGEN provided a license (the "Roche License" or "License") to IGEN LS, a newly formed and wholly owned subsidiary of IGEN.[34]



Under the Restructuring Agreement, IGEN's operating business and intellectual property rights (including IGEN's ECL intellectual property) were spun off to IGEN Integrated Healthcare, LLC, *i.e.* "Newco," which eventually became BioVeris.[35] IGEN LS retained its rights as a licensee under the Roche License.

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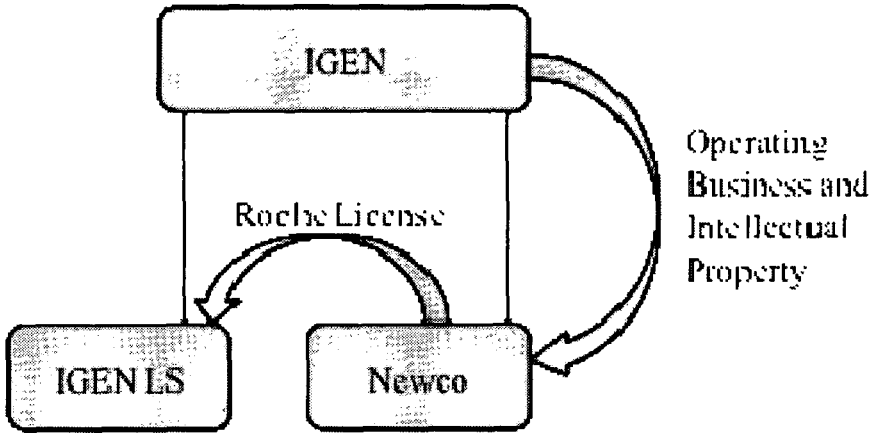
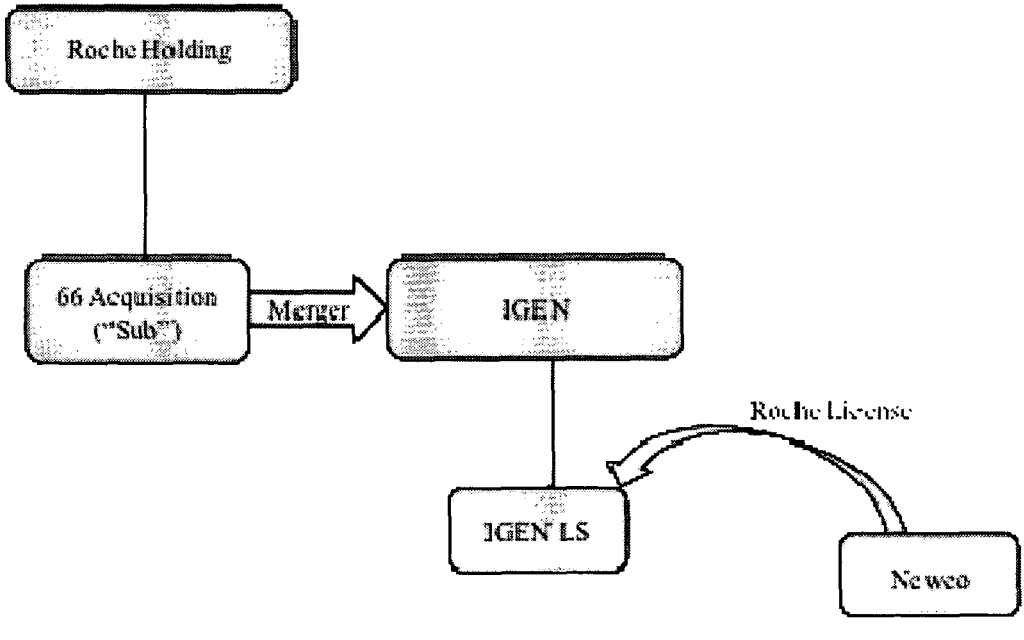
[33] *See* Ross Aff. Ex. 28. The "Transaction Agreements" are comprised of: (1) the Global Consent; (2) the Merger Agreement; (3) the Restructuring Agreement; (4) the Post-Closing Covenants Agreement; (5) the Tax Allocation Agreement; (6) the Ongoing Litigation Agreement; (7) the Release Agreement; (8) the License Agreement; (9) the Improvements License Agreement; (10) the Covenants Not to Sue; (11) the PCR [Polymerase Chain Reaction] License Agreement; and (12) the PCR Services Agreement.

[34] *See id.* Ex. 29.

[35] Brown Aff. Ex. 14.

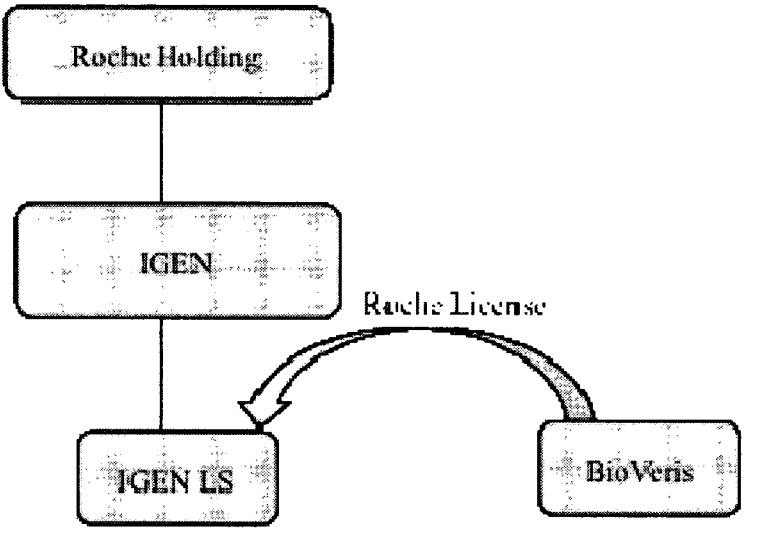


Under the Merger Agreement, 66 Acquisition Corporation II ("Sub"), a wholly owned subsidiary of Roche Holding, then was merged with and into IGEN.[36]



[36] *Id.* Ex. 13.

Finally, Newco changed its name to BioVeris Corporation and became a publicly held and publicly traded company.[37] As a result of the 2003 Transaction, which was signed on July 24, 2003, BioVeris obtained IGEN's intellectual property rights and Roche obtained a limited-field license indirectly through IGEN LS.



The details of the relevant Transaction Agreements are summarized below.

a. The Roche License

Under the Roche License, IGEN granted IGEN LS "only for use in the Field, an irrevocable, perpetual, Non-Exclusive, worldwide, fully-paid, royalty-free right and license under the Licensed ECL Technology, to develop, . . . use, . . . sell, . . . and otherwise commercially exploit Products."[38] "Products" is defined as "ECL instruments, service for ECL instruments and spare parts; and ECL Assays."[39] The Roche License defines "Field" as "the analyzing of specimens taken from a human body, including without limitation, blood, bodily fluid or tissue, for the purpose of testing, with respect to that human being, for a physiological or pathological state, a

[37] *Id.* Ex. 14 § 2.01.
[38] Ross Aff. Ex. 29 § 2.1.
[39] *Id.* § 1.13.

congenital abnormality, safety and compatibility of a treatment or to monitor therapeutic measures."[40] The Field explicitly excluded

> analyzing for (A) life science research and/or development, including at any pharmaceutical company or biotechnology company, (B) patient self testing use; (C) drug discovery and/or drug development . . . including clinical research or determinations in or for clinical trials or in the regulatory approval process for a drug or therapy, or (D) veterinary, food, water, or environmental testing or use.[41]

The Roche License was "non-exclusive" and ultimately permitted BioVeris to "exercise the licensed rights itself in the licensee's field or grant non-exclusive licenses in the licensee's field to a third party, or retain for itself any non-exclusive license rights."[42]

Section 2.5 of the Roche License provided an enforcement mechanism to ensure that Roche did not conduct out-of-field sales. Section 2.5(a) contemplated the appointment of a neutral third party to monitor Roche's compliance by examining such records as necessary. Section 2.5(b) also provided that if out-of-field sales occurred, Roche could continue to sell until BioVeris notified Roche it was prohibited, and BioVeris's exclusive remedy would be that Roche would have to pay to it 65% of all revenues earned from out-of-field sales. The Roche License also stated that if the parties to the agreement were unable to resolve a dispute through good faith negotiation, any dispute arising out of or relating to the agreement would be resolved solely by arbitration.[43]

The Roche License designates IGEN and IGEN LS as the "Parties" to the agreement.[44] BioVeris later succeeded to IGEN's rights and obligations. Moreover, the agreement expressly provided that, except for limited circumstances, "nothing [in the Roche License] is intended to confer upon any person other than the Parties hereto and their respective successors and permitted assigns, any benefit, right or remedy under or by reason of [the Roche License]."[45]

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[40] *Id.* § 1.7(a).
[41] *Id.* § 1.7(b).
[42] *Id.* § 1.10.
[43] Ross Aff. Ex. 29 §§ 6.1–6.2.
[44] *Id.* at 1.
[45] *Id.* § 14.11.

The signature pages of the Roche License, however, were followed by a document entitled "CONSENT BY MESO SCALE DIAGNOSTICS, LLC AND MESO SCALE TECHNOLOGIES, LLC" (the "Meso Consent").[46] The Meso Consent states that MSD and MST

> consent to the [Roche License] . . . and . . . consent to and *join in the licenses granted* to [Roche] in the [Roche License] . . . . Furthermore, MSD and MST . . . represent and warrant to [Roche] that each of them . . . waive any right that either of them may have to in any way restrict or limit [Roche's] exercise of the licenses granted in the [Roche License] during the Term thereof.[47]

The Meso Consent was signed by MSD and MST.[48]

b. The Global Consent

Jacob Wohlstadter participated in the negotiations between IGEN and Roche regarding the 2003 Transaction, although the parties dispute his role.[49] Defendants contend that Wohlstadter extracted $37.5 million for MSD's consent to the transfer of IGEN's interest in MSD to BioVeris.[50] On the other hand, Plaintiffs contend that "Roche made clear that it would not pay for a license or make a $1.4 billion payment unless Meso agreed to both consent to and join in" the Roche License.[51]

In addition to the Meso Consent, MSD and MST also signed the Global Consent. The latter document contained an important provision preventing the assignment of rights of Newco (ultimately, BioVeris) without the prior written consent of the other parties.[52] Specifically, Section 5.08 stated:

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[46] *Id.* at 0055887.

[47] *Id.* (emphasis added).

[48] *Id.*

[49] *See* Brown Aff. Ex. 10 at 44–49.

[50] Defs.' Br. in Supp. of Their Mot. for Summ. J. ("Defs.' Opening Br.") 7.

[51] Pls.' Opp'n to Defs.' Mot. for Summ. J. ("Pls.' Answering Br.") 13 (citing Ross Aff. Ex. 10 at 123; Ex. 14 at 204–05, 233–34). Jacob Wohlstadter had an interest in IGEN for which he received approximately $10 million as a result of the 2003 Transaction. Brown Aff. Ex. 64 at 237 (Jacob Wohlstadter).

[52] Ross Aff. Ex. 28 § 5.08.

> Neither this Agreement nor any of the rights, interests or obligations under this Agreement shall be assigned, in whole or in part, *by operation of law or otherwise by any of the parties without the prior written consent of the other parties*; provided, however, that the parties acknowledge and agree that the conversion of Newco in accordance with Section 2.01 of the Restructuring Agreement and the continuation of Newco as a result thereof shall be deemed not to be an assignment and shall not require any consent of any party. Any purported assignment without such consent shall be void. Subject to the preceding sentences, this Agreement will be binding upon, inure to the benefit of, and be enforceable by, the parties and their respective successors and assigns.[53]

Importantly, the Global Consent stated that the Agreement was among Roche Holding, IGEN, IGEN Integrated Healthcare, LLC, MSD, MST, Jacob Wohlstadter, and JW Consulting Services, L.L.C. In another section of the Global Consent, MSD, MST, Jacob Wohlstadter, and JW Consulting Services, L.L.C. acknowledged receipt of the twelve Transaction Agreements, consented to the consummation of the transactions, and granted all waivers and consents necessary to permit the consummation of the transactions and the performance by the parties of their obligations under the Transaction Agreements.[54]

In Section 3.02 of the Global Consent, MSD and MST acknowledged and consented to the MSD Transfer, whereby "all of [IGEN]'s rights under and in respect of the MSD Agreements shall be assigned to, and all of the Company's liabilities under and in respect of the MSD Agreements will be assumed by[] Newco."[55] Notably, the MSD Agreements included both the Joint Venture Agreement and the MSD License. Meso also consented to and accepted "the assumption by Newco of all rights, obligations, duties and Liabilities (express and implied) of [IGEN] under the MSD Agreements."[56] Finally, MSD and MST acknowledged and consented that, as a result of the transfer, Newco would own "all right, title and interest in and to any and all intellectual property and other proprietary and confidential information or

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[53] *Id.* (emphasis added).
[54] *Id.* § 3.01.
[55] *Id.* § 3.02(a), (b).
[56] *Id.* § 3.02(b).

materials owned by [IGEN] . . . to which MSD [or] MST . . . has any direct or indirect rights or benefits . . . pursuant to the MSD Agreements."[57]

c. The Post-Closing Covenants Agreement

One of the Transaction Agreements, the Post-Closing Covenants Agreement, contained a provision that prevented Roche for four years from making a proposal to acquire or from acquiring any securities or assets of Newco (*i.e.*, BioVeris), although Newco independently could waive or amend that restriction.[58]

5. Roche's acquisition of BioVeris

After the 2003 Transaction was completed, BioVeris alleged that Roche was selling ECL-based products outside of the Field. Roche asserted that the out-of-field sales were minimal and estimated that it owed a $1.5 million fee to BioVeris under the 65% royalty provided for in Section 2.5(b) of the Roche License.[59] BioVeris, however, estimated that the fee due from Roche for out-of-field sales could exceed $30 million annually.[60] The parties therefore engaged Ernst & Young LLP ("Ernst & Young") as a neutral "field monitor" to calculate out-of-field sales.[61]

According to Roche, Samuel Wohlstadter, the CEO of BioVeris, "repeatedly" proposed to Roche that it buy BioVeris to resolve the dispute over out-of-field sales.[62] Consistent with that suggestion, on July 20, 2006, Samuel Wohlstadter waived the four-year restriction in the Post-Closing Covenants Agreement and permitted Roche to discuss a consensual transaction with BioVeris.[63]

As an independent business, BioVeris was not very profitable. For example, in 2006, BioVeris had only $20.6 million in revenues and incurred a net loss of $27.9 million.[64] Nevertheless, in March 2007, Roche offered to

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[57] *Id.* § 3.02(e).
[58] Brown Aff. Ex. 21 § 3.10.
[59] Ross Aff. Ex. 47 at 17.
[60] *Id.*
[61] *Id.*
[62] Brown Aff. Ex. 70 at 56–57.
[63] *Id.* Ex. 30.
[64] Ross Aff. Ex. 52 at 42–43.

pay approximately $600 million in cash for BioVeris, a 58% premium over its pre-announcement market capitalization of approximately $370 million.[65]

The record shows that Roche's sole objective was to acquire BioVeris's intellectual property rights.[66] Roche internally had valued those intellectual property rights at 1.695 billion Swiss francs, or approximately $1.4 billion.[67] Roche also touted the fact that "[b]y acquiring BioVeris, Roche [would] own the complete patent estate of the [ECL] technology deployed in [Roche's] Elecsys product line which gives Roche Diagnostics the opportunity to fully exploit the entire immunochemistry market."[68]

The acquisition of BioVeris (the "BioVeris Merger") was structured as a reverse triangular merger.[69] Lili Acquisition was formed as an "acquisition subsidiary" of Roche and merged into BioVeris on June 26, 2007, with BioVeris as the surviving corporation.[70] As a result of the merger, "all the properties, right, privileges, powers and franchises of [BioVeris] and [Lili Acquisition] [vested] in [BioVeris], and all claims, obligations, debts, liabilities and duties of [BioVeris] and [Lili Acquisition] [became] the claims, obligations, debts, liabilities and duties of [BioVeris]."[71]

In September 2007, BioVeris notified its customers that it was discontinuing certain product lines and that they would need to develop a plan to transition to another supplier or alternate technology.[72] In September and October 2007, Roche closed down BioVeris's research and development plant and delivered exit dates to each employee of BioVeris.[73] At all times after the BioVeris Merger, however, BioVeris continued to hold the intellectual property relevant to this dispute.[74]

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[65] *Id.* Ex. 41 at 3, 4, 14 (27,247,902 outstanding shares; $13.60 pre-announcement share price; $21.50 per share merger consideration).

[66] *See, e.g.*, *id.* Ex. 44 at 44 (Humer) ("Q: Okay. Just again to my question, was BioVeris'[s] condition as an operating company irrelevant to your decision to buy BioVeris? A: BioVeris held certain patent rights and intellectual property which we wanted to acquire. Q: Did it matter to you what BioVeris'[s] operating business did as a matter of its financials? A: That was not relevant.").

[67] *See id.* Ex. 55 at 0071130; X-Rates, Historical Rates, http://www.x-rates.com/historical/?from=USD&amount=1.00&date=2007-04-16.

[68] *Id.* Ex. 59 at 0041325.

[69] *Id.*

[70] Brown Aff. Ex. 4 §§ 1.1, 1.4.

[71] *Id.* § 1.4.

[72] Ross Aff. Ex. 67.

[73] *Id.* Ex. 68.

[74] Tr. 71.

briefing. It is not necessary for me to consider this affidavit or these arguments, because the determinations of the previous action have preclusive effect. Genger himself acknowledges that if the rulings of the previous action are given preclusive effect, the Trump Group is entitled to summary judgment.[117] But, in the interest of completeness, I consider Genger's arguments anyway, and explain why they do not defeat summary judgment.

A. The Trump Group Has The Right To Buy The Genger Shares

1. The Doctrine Of Issue Preclusion Prevents Genger From Challenging The Findings Of The Previous Action[118]

The doctrine of issue preclusion provides that "[w]hen an issue of fact or law is actually litigated and determined by a valid and final judgment, and the determination is essential to the judgment, the determination is conclusive in a subsequent action between the parties, whether on the same or a different claim."[119] The Supreme Court has adopted a four-prong test for issue preclusion. Issue preclusion applies if "(1) the issue sought to be precluded [is] the same as that involved in the prior action; (2) that issue [was] actually litigated; (3) [the issue was] determined by a final and valid judgment; and (4) the determination [was] essential to the prior judgment."[120]

The three essential findings that underpin the Trump Group's motion—that the 2004 transfers were invalid, that the Trans-Resources

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[117] Genger Br. in Opp'n 25 ("The Trumps Are Not Entitled To Summary Judgment Absent Preclusion").

[118] The Trump Group has also suggested that it should also be able to prevail under the related doctrine of claim preclusion. The doctrine of claim preclusion provides that "a judgment, once rendered, [is] the full measure of relief to be accorded between the same parties on the same 'claim' or 'cause of action.'" Charles Alan Wright et al., 18 *Federal Practice and Procedure* § 4402 (2d ed., updated 2012) (citation omitted).

Here, the doctrine of claim preclusion is not applicable. Because two indispensable parties were missing from the previous action—TPR and the Orly Trust—our Supreme Court held that its decision was not the "full measure of relief" between the Trump Group and Genger as to the block in question in this case, the Genger Shares. Supr. Ct. Op. 202-03. Instead, the Supreme Court suggested the Trump Group obtain relief in a court that had jurisdiction over all the relevant parties to determine the beneficial ownership of the shares. *Id.* at 203 n.98. Thus, the Supreme Court held that the prior action did not have the effect of barring a future action to determine the beneficial ownership of the Genger Shares and the Orly Trust Shares. The Revised Final Judgment Order, although it stated that it was a "final judgment," left open the question of the beneficial ownership of the Genger and Orly Trust shares. Rev. Final J. Order ¶¶ 15-16.

[119] Restatement (Second) of Judgments § 27 (1982).

[120] *Acierno v. New Castle Cnty.*, 679 A.2d 455, 459 (Del. 1996) (quoting *Graham v. IRS*, 973 F.2d 1089, 1097 (3d Cir. 1992)); *see also Technicorp Int'l II, Inc. v. Johnston*, 1997 WL 538671, at *4 (Del. Ch. Aug. 25, 1997) (applying the same test to determine if issue preclusive effect was to be given to determinations made in a § 225 action).