otherwise disinterested Board members decided to abdicate their duties and favor Rosenschein. Fourth, Plaintiffs never direct the Court to specific evidence of an occasion when the Board acquiesced in Rosenschein's desires or Rosenschein attempted to impose his will upon it. Finally, the Board's decision to sell the Company is supported by other reasons cognizable under the business judgment rule, including the Board's apprehension that Google would soon compete directly against the Company and its recognition that, although the Company had benefited from a recent uptick in revenues, future results were uncertain.

The evidence Defendants provide, such as the Board meeting minutes, demonstrates a Board appropriately balancing business risks and attempting to comply with its fiduciary duties. Because Plaintiffs' arguments suffer from the problems identified above, no genuine issue of material fact is present and Defendants are entitled to summary judgment on the claim that Rosenchein somehow dominated these four directors.[140]

D. *Did Beasley and Dyal Control the Board?*

Similarly, the Court does not need to determine whether Beasley and Dyal were conflicted because of the scant evidence offered by Plaintiffs regarding the Redpoint directors' ability to dominate the Board. Defendants' evidence indicates that Rosenschein and UBS served as the primary negotiators leading the Company through discussions with AFCV. The Board meeting minutes in December and February also portray a Board that deliberated without any undue interference. Plaintiffs contend a triable issue of fact exists because the Redpoint representatives held two meetings with Summit or AFCV without other Company representatives and because Beasley unsuccessfully attempted to increase the merger consideration. However, Plaintiffs do not demonstrate any specific acts of control. Moreover, there is no showing of any harm that could have resulted from these meetings.

Plaintiffs next argue that triable issues of fact exist because a series of emails include certain directors, but not others. These emails are not evidence of domination. Most of the cited emails are among Shelffo, Rosenschein, Beasley, Dyal, and Segall.[141] The emails provide updates

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[140] A corollary of Plaintiffs' failure to explain the nature of Rosenschein's domination of the Board is that they never argue he controlled, manipulated, or otherwise failed to provide information which the Board needed. None of the evidence Plaintiffs provide causes the Court to question whether disputed issues of fact exist in this regard as well.

[141] Zeldin Aff., Exs. 26, 40, 43, 44. Plaintiffs also direct the Court to an email from

about the AFCV negotiations or are side comments about those updates to a smaller group of recipients. That some directors were included in these emails simply reflects the reality that certain directors may have been more involved in the minutia of the transaction and others may have reviewed it at a higher level.

Plaintiffs also point to two emails in a side conversation between Redpoint representatives and Summit.[142] In the second email, a Summit representative explained why the deal price should be lowered based on Summit's additional diligence findings and then questioned if the "price you negotiated with us" would be honored.[143] The representative's use of "you," when read in the context of the email, refers to Beasley and Dyal as representatives of the Company and does not support a reasonable inference that Dyal or Beasley had a pre-cooked deal with Summit. However, even if these two had made a deal with Summit, there is no evidence that Dyal or Beasley had any ability to, or attempted to, force such a deal on the Board. On the contrary, the record demonstrates otherwise and ample evidence is present that the Company's representatives led the negotiation process, used reasonable efforts to attempt to increase the sale price, and that there was no pressure applied by Dyal or Beasley during the Board's well-documented deliberations.

Defendants' evidence establishes that the Board did not act in bad faith in complying with its fiduciary duties and that Rosenschein, Beasley, and Dyal did not dominate the Board. The evidence that Plaintiffs have forwarded to rebut Defendants' showing does not demonstrate a genuine issue of material fact upon which Plaintiffs could state a claim. Thus, the Director Defendants' motion for summary judgment is granted.

E. *Did the Buyout Group Aid and Abet a Breach of Fiduciary Duty?*

An aiding and abetting a breach of fiduciary duty claim requires a plaintiff to prove: (1) the existence of a fiduciary relationship, (2) a breach of the fiduciary's duty, (3) knowing participation in that breach by

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Segall to Shelffo and Beasley and another email from Segall to Beasley and Dyal. Zeldin Aff., Exs. 24, 22.

[142] Zeldin Aff., Exs. 52, 53. In the first email, Dyal explicitly disclaimed the need for Dyal and Beasley to participate in a call in which AFCV would explain why it would not raise its offer price.

[143] Zeldin Aff., Ex. 53.

the defendants, and (4) damages proximately caused by the breach.[144] Plaintiffs argue that genuine issues of material fact are present regarding whether the Buyout Group aided and abetted the Director Defendants' breach of fiduciary duty by knowingly participating in the breach and whether the Buyout Group received confidential information from the Board.

Plaintiffs argue the Buyout Group knowingly participated in the breach because the Shelffo Emails state that "time is not a friend to this deal" and that a Summit representative sought to speak with Redpoint. This evidence cannot reasonably be interpreted as evidence of knowing participation. The Redpoint directors informed the Summit representative that they had no need to speak directly about the issues the representative raised and that other Company representatives could follow up on Summit's concerns. Shelffo, in her emails, states that the Board may call off the deal because of concerns about AFCV's ability to finance the deal. Neither of these communications can reasonably be interpreted as evidence of a plan to breach or to induce a breach.

Next, Plaintiffs argue that the Buyout Group received confidential information from the Board because Shelffo indicated that the Buyout Group "pushed" for the market check to be completed in two weeks, because AFCV added $0.25 to the share price to expedite the deal, and because Beasley contacted Summit in January to try to raise the price. Plaintiffs argue that all of these circumstances indicate that the Buyout Group received confidential information in order to engineer a deal to buy the Company at the cheapest price possible.

Plaintiffs essentially invite the Court to interpret certain negotiations as evidence that confidential communication was elsewhere being exchanged. The Court declines to do so. The evidence Plaintiffs cite demonstrates that even arm's length negotiators need to email one another to complete a deal and that sometimes they offer suggestions on how to expedite the deal, which the opposing party may accept or reject. Plaintiffs provide no evidence indicating that confidential information was exchanged and are thus left only with their assertions that a conspiracy must have existed between the Buyout Group and the Board. Such assertions cannot create a genuine issue of material fact.

Because Defendants present evidence of arm's length negotiations between the parties and Plaintiffs provide no evidence which can

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[144] *Malpiede v. Townson*, 780 A.2d 1075, 1096 (Del. 2001).

reasonably be interpreted to demonstrate knowing participation in a breach or the exchange of confidential communication and because no underlying breach of fiduciary duty is present, the Court grants the Buyout Group's motion for summary judgment.

V. CONCLUSION

For the reasons stated above, no genuine issue of material fact exists that the Director Defendants did not act in bad faith and that Rosenschein, Beasley, and Dyal did not control the Board. The transaction was approved by an independent and disinterested majority of the Board which did not act in bad faith. The Director Defendants' motion for summary judgment is therefore granted. Because there is no dispute of material fact as to whether the Buyout Group aided and abetted any breach of fiduciary duty, its motion for summary judgment is also granted.

An implementing order will be entered.

LEHMAN BROTHERS HOLDINGS INC. AND T. ROWE PRICE HIGH YIELD FUND, INC., ET AL V. SPANISH BROADCASTING SYSTEM, INC.

No. 8321-VCG

In the Court of Chancery of the State of Delaware

February 25, 2014

Garrett B. Moritz and S. Michael Sirkin, of Seitz Ross Aronstam & Moritz LLP, Wilmington, Delaware; OF COUNSEL: Robert J. Stark, Sigmund S. Wissner-Gross, May Orenstein and Marek Krzyzowski, of Brown Rudnick LLP, New York, New York, Attorneys for Plaintiff Lehman Brothers Holdings Inc.

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Robert S. Saunders, Nicole A. DiSalvo, Ronald N. Brown, III and Matthew P. Majarian, of Skadden, Arps, Slate, Meagher & Flom LLP, Wilmington, Delaware, Attorneys for Defendant Spanish Broadcasting System, Inc.

GLASSCOCK, *Vice Chancellor*.

In this case, the Plaintiffs, equity holders in the Defendant company, invested in preferred stock that accrued dividends daily, which dividends were payable quarterly as and if declared by the company's board of directors. If the dividend was not paid for four consecutive quarters, the Certificate of Designation in connection with the stock provided that a "Voting Rights Triggering Event" (a "VRTE") had occurred, conferring upon the Plaintiffs certain rights, including a right to fill seats on the company board, and to constrain the company from acquiring certain additional debt during the period the dividend arrearage continued. In 2009, the company began to fail to make dividend payments, and—under the Plaintiffs' reading of the Certificate of Designation—a VRTE occurred no later than July 2010. Nonetheless, the Plaintiffs did not assert their rights under the Certificate of Designation at that time. Moreover, when the company's board

determined that it needed additional capital and acquired debt in separate, publically-announced transactions in May 2011 and January 2012, the Plaintiffs stood mute. Finally, on February 14, 2013, one of the Plaintiffs filed this suit, contending that a VRTE had occurred in 2010, and therefore the debt transactions of 2011 and 2012 were in breach of its contract rights under the Certificate of Designation. The Plaintiffs seek damages as a result of the breach.

The Defendant contends that the Plaintiffs misread the Certificate of Designation, and that no VRTE occurred in 2010. I need not reach that issue, however, because I find that, assuming that a VRTE did occur, the Plaintiffs, with at least imputed knowledge of both that fact and that the board nonetheless intended to incur additional debt, made no objection to that action, and instead stood by and allowed the breach to occur. Under the particular facts set out below, I find that the Plaintiffs acquiesced to the actions of the company during the time of any VRTE resulting from the failure of the company to pay dividends through July 2010, and the Plaintiffs are therefore not entitled to the relief they seek.

I. FACTS

A. *The Preferred Stock Offerings*

Defendant Spanish Broadcasting System, Inc. ("SBS," or the "Company") is a Delaware corporation that owns and operates Spanish-language radio and television stations in the United States, generating most of its revenue from the sale of advertising airtime on its twenty-one radio stations and through its television group.[1] Though SBS "is well-positioned to benefit from favorable market demographics," the Company experienced net losses in 2008 and 2009, and generated only "modest" net income of $15 million in 2010 and $23.7 million in 2011.[2]

SBS currently has two classes of common stock and two classes of preferred stock. SBS initiated a public offering of its first class of preferred stock—Series A Preferred Stock ("Series A")—in 2003, as a way of financing its acquisition of radio station KXOL-FM without incurring additional debt.[3] At that time, SBS, represented by legal counsel Kaye Scholer LLP and financial advisor Sterling Advisors LLC, worked with underwriters Merrill Lynch and Lehman Brothers Inc.

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[1] Lehman Compl. ¶ 9.
[2] *Id.* at ¶¶ 9, 11.
[3] Lehman's Mem. of Law in Support of its Mot. for Summ. J. at 5.

("LBI"), a former affiliate of Plaintiff Lehman Brothers Holdings Inc. ("Lehman"), to organize the Series A offering. The offering was structured such that Series A preferred stock would initially be placed with qualified institutional buyers, and then pursuant to a Registration Rights Agreement, Series A shares would eventually be exchanged for shares of Series B Preferred Stock ("Series B") in a registered offering, with Series B trading in the secondary market. Though an equity offering, SBS and its underwriters approached the offering as a debt alternative, "described in debt-like terms," marketed to SBS's existing bondholders and providing what essentially functioned as a maturation date on which date the preferred stockholders could require SBS to repurchase the preferred shares.[4]

The terms of the Series A offering were initially set out in drafts of the offering memorandum, created by LBI and modified by SBS's legal counsel, and ultimately delineated in the Series A Certificate of Designation. The SBS board approved the filing of the Series A and Series B Certificates of Designation on October 15, 2003, and those Certificates were authorized by resolution via a unanimous written consent dated October 28, 2003.[5] On October 30, 2003, LBI, Merrill Lynch, and Deutsche Bank, acting as underwriters, acquired 75,000 shares of Series A to place with qualified institutional buyers, including with Plaintiff T. Rowe Price. The underwriters did not retain any of the Series A shares.

In February 2004, SBS filed a registration statement with the Securities and Exchange Commission in connection with its plan to permit investors to exchange shares of Series A for freely-transferable shares of Series B. The T. Rowe Price funds that had acquired Series A shares fully participated in the conversion to Series B shares, and between 2004 and 2008, T. Rowe Price acquired additional shares of Series B on the secondary market totaling 13,200 shares, or roughly 14% of shares outstanding.[6] In addition, LBI acquired over 35,000 shares of Series B on the secondary market; as of September 2012, that stake represented roughly 38% of the 92,349 total shares of Series B outstanding.[7] In September 2008, LBI entered bankruptcy, and its shares of Series B were held by JP Morgan Chase as security for clearing and settlement services. In March 2010, Plaintiff Lehman became

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[4] *Id.* at 7.
[5] *Id.* at 10-11.
[6] T. Rowe Compl. ¶¶ 22-23.
[7] Lehman Compl. ¶ 16.

subrogated to JP Morgan's rights in the Series B shares, and in March 2012, Lehman emerged from bankruptcy.[8]

B. *The Series B Certificate of Designation*

According to the Certificate of Designation, Series B stockholders receive dividends "when, as and if declared by the Board of Directors," accruing at an annual rate of 10.75%.[9] These dividends accrue on a daily basis and are "payable quarterly in arrears on October 15, January 15, April 15, and July 15 of each year."[10]

This action involves a disagreement about the interpretation of a provision included in the Series B Certificate of Designation (the "Certificate"), which defines a Voting Rights Triggering Event: the VRTE. That provision states:

> If . . . at any time, dividends on the outstanding Series B Preferred Stock are in arrears and unpaid (and in the case of dividends payable after October 15, 2008, are not paid in cash) for four (4) consecutive quarterly dividend periods . . . the number of directors constituting the Board of Directors of the Company will be adjusted to permit the holders of the majority of the then outstanding Series A Preferred Stock and Series B Preferred Stock, voting together as one class, to elect two directors.[11]

Where a VRTE has occurred such that the preferred stockholders' voting rights have vested, "a proper officer of the Company shall, upon the written request of holders of record of 10% or more of the then-outstanding Series A Preferred Stock and Series B Preferred Stock . . . call a special meeting of holders" in order to fill the two board seats due to the preferred stockholders upon the occurrence of a VRTE.[12] If, after 30 days of receipt of the written request, the Company fails to hold a special election, then preferred stockholders owning 10% or more

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[8] Lehman's Mem. of Law in Support of its Mot. for Summ. J. at 12-13.

[9] Series B Cert. of Designation § 4(a).

[10] *Id.*

[11] *Id.* § 9(b); *see also id.* § 4(a) ("If at any time dividends on the Series B Preferred Stock are in arrears and unpaid for four consecutive quarterly dividend periods, holders of Series B Preferred Stock will be entitled to the voting rights specified in Section 9 of this Certificate of Designations.").

[12] *Id* § 9(d).

of the outstanding shares may themselves "call such meeting at the expense of the Company."[13]

In addition, where a VRTE has occurred, SBS is prohibited from incurring certain additional debt, and if SBS wishes to incur new debt, it must either pay its arrearages or obtain a waiver. Specifically, the Certificate provides:

> The Company shall not, and shall not permit any of its Restricted Subsidiaries to, directly or indirectly, create, incur, issue, assume, guarantee or otherwise become directly or indirectly liable, contingently or otherwise, with respect to (collectively, "incur") any Indebtedness (including Acquired Debt) . . . [if] the Company's Debt to Cash Flow Ratio at the time of incurrence of such Indebtedness . . . would have been no greater than 7.0 to 1.0.
>
> So long as no Voting Rights Triggering Event shall have occurred and be continuing or should be caused thereby, the provisions of the first paragraph of this Section 11(b) will not apply to the incurrence of any [Permitted Debt].[14]

While the Certificate does not expressly provide a mechanism whereby the Preferred Stockholders may waive the Company's limitations on incurring debt while a VRTE is in effect,[15] the Certificate states that "[w]ithout the consent of each Holder affected, an amendment or waiver of . . . this Certificate of Designations may not (with respect to any shares of Series B Preferred Stock held by a non-consenting Holder): . . . (iv) waive the consequences of any failure to pay dividends on the Series B Preferred Stock . . . ."[16]

The parties dispute the circumstances under which a VRTE comes into effect under the language of Section 9(b) cited above; that is, what constitutes dividends "in arrears and unpaid . . . for four (4) consecutive quarterly dividend periods." Specifically, the Plaintiffs argue that a

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[13] *Id.*

[14] *Id* § 11(b); *see also id.* § 2 ("'Voting Rights Triggering Event' has the meaning set forth in Section 9(b)."); *id.* § 9(b)(v) ("[E]ach of the events described in clauses (i), (ii), (iii), (iv) and (v) being referred to herein as a 'Voting Rights Triggering Event'").

[15] *But see id.* § 9(f) (permitting the Company to enter into a merger transaction or sell substantially all of its assets with the consent of a majority of the preferred stockholders).

[16] *Id.* § 9(h).

VRTE occurs when an arrearage persists through four consecutive quarters, while SBS contends that a VRTE occurs only if the Company fails to make four consecutive quarterly dividend payments.

Section 9(b) also provides SBS with an option to "pay in kind" ("PIK"); accordingly, until October 15, 2008, SBS retained an option to pay dividends in cash or in additional preferred stock.[17] The PIK option thus provided SBS with the flexibility to pay dividends in additional stock if the Company faced liquidity problems, although such preferred stock issued in PIK payments would later accrue dividends themselves. In addition, the Certificate provides that after October 15, 2008, the Series B shares are redeemable at SBS's option for a premium,[18] and that after October 15, 2013, holders of Series B shares may require SBS to repurchase their shares for $1000 per share in addition to all accumulated and unpaid dividends.[19] The latter right is limited by SBS's liquidity, and although on October 15, 2013, the Plaintiffs exercised the right to the maximum extent they could, of the $140 million worth of preferred shares outstanding, SBS redeemed only $2.5 million; as a result, both Plaintiffs still hold a position in the Company.[20]

C. *SBS Suffers a Liquidity Crisis and Stops Paying Dividends*

From the issuance of Series B in 2004 through April 2009, SBS paid the Series B stockholders quarterly dividends. SBS explains that during that period, "SBS chose to pay 12 dividends in cash as a result of the company's healthy financial position and the general state of the economy, and did not need to consider deferring any dividends at all."[21] In light of the financial crisis in 2008, however, SBS "embarked on a cash preservation program in response to declining financial conditions which, if allowed to continue, may have left [SBS] out of cash by the end of the year."[22] By the spring of 2009, SBS "had exhausted almost all available means of cash conservation, but was still not on track to maintain healthy cash flows in the future."[23] As a result, on May 15, 2009, SBS publically announced:

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[17] *Id.* § 4(a).
[18] *Id.* § 6. That right expired without being exercised. Oral Arg. Tr. 19:17.
[19] Series B Cert. of Designation § 7.
[20] Oral Arg. Tr. 20:3-16.
[21] Def.'s Op. Br. in Support of its Mot. for Summ. J. at 10.
[22] *Id.* at 12.
[23] *Id.* at 14.

> On May 12, 2009, our Board of Directors under management's recommendation determined that, based on, among other things, the current economic environment and future cash requirements, it would not be prudent to declare or pay the July 15, 2009 cash dividend of approximately $2.5 million.[24]

SBS made the decision to defer cash dividends despite its contention that "declaring and paying a cash dividend is in most circumstances better for the company than deferring the dividend, as the reputational damage to SBS resulting from deferral hurts its standing in the market and can both depress the price of its stock and make it harder for the company to secure financing."[25] Subsequently, SBS declared one dividend per year, payable on April 15 each year, and declined to pay dividends for the three quarters in between. Under SBS's reading of the Certificate, such a dividend payment practice does not trigger a VRTE. The Plaintiffs disagree. They now allege that in April or July 2010,[26] a VRTE occurred, since at that point dividends had been in arrears for four consecutive quarters; however, despite public announcements of SBS's intent to defer dividend payments, the Plaintiffs never voiced an objection, exercised rights available to them upon the happening of a VRTE, or even informed SBS that they believed a VRTE had occurred, until they filed this lawsuit, almost three years later.[27] Notably, each Plaintiff held more than 10% of the outstanding preferred stock at the time the VRTE allegedly occurred; each, therefore, independently had the right to demand election of board members on behalf of the preferred stockholders. Nevertheless, neither made the demand to exercise that right as contemplated by the Certificate.

The Plaintiffs argue that four continuous quarters of dividend arrearages trigger a VRTE under Section 9(b), and that this was SBS's understanding as well, at least until SBS sought to escape its obligations under that Section in 2009. Specifically, the Plaintiffs point to the way

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[24] Lehman's Mem. of L. in Support of its Mot. for Summ. J. at 8.

[25] Def.'s Op. Br. in Support of its Mot. for Summ. J. at 15.

[26] T. Rowe Price alleges that a VRTE occurred on April 15, 2010. T. Rowe Compl. ¶ 4. Lehman believes a VRTE occurred in July 2010. Lehman Compl. ¶ 1.

[27] Def.'s Op. Br. in Support of its Mot. for Summ. J. at 17. SBS did receive a letter from Goodwin Procter on behalf of "holders of the 10-3/4% Series B Preferred Stock," *after* both debt incurrences, on February 14, 2012, stating an intent to "investigate and pursue their claims against the Company . . . for breaches of [the board's] fiduciary duties . . . ." Def.'s Op. Br. in Support of its Mot. for Summ. J. Ex. 54.

in which SBS has altered its description of a VRTE in various disclosures: prior to March 2009, SBS "closely paraphrased" the language of Section 9(b), but in its March 31, 2009 Form 10-Q stated that "[u]nder the Series B preferred stock certificate of designations, failure to make four consecutive quarterly cash dividend payments will result in the right of the holders of the Series B preferred stock to elect two directors to the board."[28] Then, in 2012, in a prospectus for the issuance of new notes, SBS stated that a VRTE would occur if SBS "fail[ed] to pay at least one of every four consecutive quarterly dividends on the Series B preferred stock in cash."[29] The Plaintiffs suggest that this change in describing a VRTE tracks how SBS has changed its own interpretation of Section 9(b).

On the other hand, SBS contends that it is the Plaintiffs who have recently manufactured their interpretation of Section 9(b). SBS points to communications between Lehman's investment banks, Torque Point Advisors and BlackRock, Inc., which indicate that Lehman was looking for "leverage" and "opportunities" that might arise if Lehman was "successful in arguing that there [had] been [a VRTE]."[30]

D. *SBS Incurs Additional Debt*

SBS contends that, "[s]ecure in the knowledge that no VRTE had occurred,"—having received from holders of Series B stock no request for a special meeting to fill director seats—"SBS conducted its business as usual after 2010."[31] Accordingly, on May 6, 2011, SBS publically announced that it planned to purchase a Houston, Texas television station by issuing an $8 million promissory note. Despite the purported existence of a VRTE under what the Plaintiffs contend is the clear, unambiguous language of Section 9(b), the Plaintiffs did not voice objections to the incurrence of debt at that time, and the transaction closed nearly three months later, on August 1, 2011. The Plaintiffs now contend, under their reading of the Certificate, that the 2011 debt incurrence constituted a breach of contract.

On January 27, 2012, SBS publically announced that it planned to issue senior secured notes, paying 12.5% on $275 million, in order to

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[28] Lehman's Mem. of L. in Support of its Mot. for Summ. J. Ex. 15 at 22.
[29] *Id.* Ex. 22 at 15.
[30] Def.'s Op. Br. in Support of its Mot. for Summ. J. Ex. 55.
[31] Def.'s Op. Br. in Support of its Mot. for Summ. J. at 17.

refinance existing debt that was coming due.[32] SBS contends that, had it failed to refinance, the Company would have become insolvent. The indenture agreement governing those notes contained a covenant "prohibiting [SBS] from making more than one out of every four quarterly dividend payments to holders of Series B Preferred Stock, unless certain debt leverage ratios are satisfied, in which case [SBS] can only make two out of every four quarterly dividends."[33] The notes offering closed on February 7, 2012, again without objection from the Plaintiffs, who now claim that this debt incurrence also breached the terms of the Certificate.

E. *The Plaintiffs Determine a VRTE has Occurred*

The Plaintiffs contend that a VRTE occurred in April or July 2010, the fourth quarter in which a dividend arrearage persisted. T. Rowe Price avers, however, that it "understood for the first time that a VRTE might have occurred" more than two years later, in November 2012.[34]

Lehman contends it was also unaware of any VRTE until late 2012. Lehman became subrogated to the rights of JP Morgan in LBI's Series B shares in March 2010.[35] A few months later those shares were returned to Lehman. Throughout 2012, "internally at [Lehman], it was believed that SBS had been continuing to exercise PIK rights,"[36] although the source of that misapprehension, if any, is not disclosed in the record. It was therefore not until November of that year that Lehman began investigating "SBS, its history, and its financial condition," and eventually concluded that a VRTE had been in effect since July 2010.

Since this lawsuit was initiated, all parties agree that a subsequent event has caused a VRTE to go into effect. Accordingly, this action will not determine the Plaintiffs' current rights with respect to their position as preferred stockholders, other than their entitlement to damages in connection with the debt incurred in August 2011 and February 2012.

F. *Procedural History*

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[32] In addition to the public announcement, representatives at Lehman had actual knowledge of the notes offering "a few weeks" before the announcement. *Id.* Ex. 4 at 199-201.

[33] Def.'s Op. Br. in Support of its Mot. for Summ. J. at 10.

[34] Mot. for Summ. J. of T. Rowe Price at 16.

[35] Lehman's Mem. of L. in Support of its Mot. for Summ. J. at 22.

[36] *Id.* at 23.

On February 14, 2013, Lehman filed its Verified Complaint in this Court seeking a declaratory judgment that a VRTE had occurred and damages for breach of contract. SBS subsequently moved to dismiss that action, and Lehman moved for partial summary judgment. I heard oral argument on those motions on May 20, 2013, and found that Section 9(b) was ambiguous on its face. Accordingly, I permitted SBS to convert its Motion to Dismiss into a Motion for Summary Judgment, and deferred the cross Motions for Summary Judgment pending further supplementation of the record.

Plaintiff T. Rowe Price then filed its Verified Complaint on June 17, 2013, seeking a declaration that a VRTE had occurred, and damages for breach of contract and breach of the implied covenant of good faith and fair dealing. I granted the Plaintiffs' Motion to Consolidate on July 3, 2013. Lehman filed an Amended Complaint on October 9, 2013, including an additional claim for breach of the implied covenant of good faith and fair dealing. At this juncture, Lehman,

T. Rowe Price and SBS have all moved for summary judgment. SBS has also moved for judgment on the pleadings as to the Plaintiffs' claims for breach of the implied covenant of good faith and fair dealing.

II. STANDARD OF REVIEW

The parties have filed cross Motions for Summary Judgment.[37] A motion for summary judgment will be granted where there exist no genuine issues of material fact and the moving party has demonstrated entitlement to judgment as a matter of law; thus, "[t]he moving party bears the initial burden and the Court must view the evidence in the light most favorable to the nonmoving party."[38] However, where the parties have cross moved and have not represented that an issue of material fact is in dispute, "the Court shall deem the motions to be the equivalent of a stipulation for decision on the merits based on the record submitted with the motions."[39]

III. ANALYSIS

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[37] Defendant SBS has also separately moved for judgment on the pleadings as to Plaintiff T. Rowe Price's claim for breach of the implied covenant of good faith and fair dealing. Because that claim is subject to the same analysis under which I dismiss the Plaintiffs' other claims, I need not address that Motion for Judgment on the Pleadings separately.

[38] *Graven v. Lucero*, 2013 WL 6797566, at *2 (Del. Ch. Dec. 20, 2013).

[39] Ct. Ch. R. 56(h).

Together, the Plaintiffs in this action have requested the following relief: a declaratory judgment determining that a VRTE was in effect in April or July 2010 and that the incurrence of debt on two separate occasions after that date breached the Certificate; contract damages arising from those breaches; and damages for breaching the implied covenant of good faith and fair dealing. SBS, in addition to disputing the Plaintiffs' interpretation of the Certificate provision at issue, argues that the Plaintiffs' claims are barred by the doctrines of laches, acquiescence, ratification, and unclean hands.

Below, I address SBS's affirmative defenses of laches and acquiescence. Because I find that the Plaintiffs' claims for relief are barred by the doctrine of acquiescence, I need not address the substantive arguments the parties have raised regarding the interpretation of the contractual provision in dispute, which I previously found to be ambiguous. Accordingly, the Defendant's Motion for Summary Judgment is granted, and the Plaintiffs' Motions for Summary Judgment are denied.

A. *Laches*

Laches, in our Court, has two applications; one by analogy to the legal statute of limitations, and one purely equitable. As a court of equity, this Court is not bound by the statute of limitations, which applies to actions at law; "[a] statute of limitations period at law does not automatically bar an action in equity because actions in equity are time-barred only by the equitable doctrine of laches."[40] Under most circumstances, however, a limitations period analogous to the statute of limitations will presumptively bar equitable relief,[41] and conclusively bar legal relief. Here, the analogous three-year limitations period for contract actions has not yet run.[42]

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[40] *Whittington v. Dragon Grp., L.L.C.*, 991 A.2d 1, 9 (Del. 2009) (internal citations omitted).

[41] *See U.S. Cellular Inv. Co. of Allentown v. Bell Atl. Mobile Sys., Inc.*, 677 A.2d 497, 502 (Del. 1996) ("Absent some unusual circumstances, a court of equity will deny a plaintiff relief when suit is brought after the analogous statutory period.").

[42] I note that, with respect to T. Rowe Price's claim for a declaratory judgment that a VRTE has occurred, three years have passed; however, the breach of contract action arising out of the incurrence of debt while a VRTE was in effect is not barred. In addition, SBS argues that Lehman's claim for breach of the implied covenant of good faith and fair dealing is barred by the analogous statute of limitations, since the Amended Complaint in which that count was raised was filed more than three years after SBS implemented its alleged plan to avoid a VRTE. Because these claims are barred under the reasoning articulated in Section

Though the analogous statute of limitations effectively applies presumptively, in this Court, "he who seeks equity must do equity": in accordance with that maxim, a court of equity will not permit one who sits on his rights to then receive equitable relief.[43] Thus, equity encompasses the doctrine that if a plaintiff seeking equitable relief unreasonably delays in bringing her claim, and that delay unfairly prejudices the defendant, laches will bar the equitable relief the plaintiff seeks.[44] By contrast, as the maxim "he who seeks equity must do equity" does not apply to a plaintiff seeking *legal* relief, a plaintiff who unreasonably delays will not be barred from seeking legal relief if the action is brought within the analogous limitations period.[45] Such a result is intuitive, as it would make little sense for a plaintiff in the Court of Chancery, under the clean-up doctrine, or, as here, by statute,[46] to be placed in a worse position than if she had filed in a Delaware court of law where laches would not bar suit.[47]

The parties dispute whether the relief that the Plaintiffs seek here is equitable or legal in nature, and consequently, whether laches may bar their claims. As noted above, the Plaintiffs seek a declaratory judgment that a VRTE and breach have occurred, and contract damages. Because

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III.B of this Memorandum Opinion, I need not address those arguments.

[43] *See* 2 Pomeroy's Equity Jurisprudence § 418 (5th ed. 1941) (explaining that the maxim "equity aids the vigilant, not those who slumber on their rights"—the equitable basis for the doctrine of laches—"may properly be regarded as a special form of the yet more general principle, He who seeks equity must do equity").

[44] *Whittington*, 991 A.2d at 8.

[45] *See, e.g.*, *Laventhol, Krekstein, Horwath & Horwath v. Tuckman*, 372 A.2d 168, 169-70 (Del. 1976) ("Generally speaking, an action in the Court of Chancery for damages or other relief which is legal in nature is subject to the statute of limitations rather than the equitable doctrine of laches."); *CertainTeed Corp. v. Celotex Corp.*, 2005 WL 217032 (Del. Ch. Jan. 24, 2005) (analyzing claims for contract damages and specific performance under the doctrines of laches by analogy to the statute of limitations and equitable laches, respectively, though the claims arose under the same set of facts); 2 Pomeroy's Equity Jurisprudence § 419e (5th ed. 1941) ("It is frequently held that where a legal right is involved, and, upon ground of equity jurisdiction, the courts have been called upon to sustain the legal right, the mere laches of a party, unaccompanied by circumstances amounting to an estoppel, constitutes no defense. As has been expressed, 'if a legal right gets into equity, the statute [of limitations] governs. '") (internal citations omitted); 3 Pomeroy's Equity Jurisprudence § 817 (5th ed. 1941) ("[Laches] does not cut off the party's title, nor his remedy at law; it simply bars his right to equitable relief, and leaves him to his legal actions alone.").

[46] *See* 8 *Del. C.* § 111 (vesting the Court of Chancery with jurisdiction to interpret, apply, enforce or determine the validity of corporate instruments).

[47] Similarly, the "unclean hands" doctrine bars equitable, but not legal, relief. *See, e.g.*, *USH Ventures v. Global Telesystems Grp., Inc.*, 796 A.2d 7, 20 n.16 (Del. Super. 2000) ("The defense of 'unclean hands' is generally inappropriate for legal remedies."); *In re Estate of Tinley*, 2007 WL 2304831, at *1 (Del. Ch. July 19, 2007) (explaining that "a litigant seeking equitable relief who appears with unclean hands will find that relief barred to her," but that the doctrine will not bar legal relief).

the issues involved in considering the Plaintiffs' request for a declaratory judgment must necessarily be addressed in determining whether the Plaintiffs are entitled to contract damages, the declaratory judgment claims must be subject to the same analysis as the claims for contract damages.[48] Because I find, for the reasons that follow, that the relief requested by the Plaintiffs is legal in nature, the doctrine of laches is not applicable.

The Plaintiffs contend that because they seek legal relief in the form of contract damages, such relief is not subject to a laches analysis. SBS, on the other hand, suggests that the measure of contract damages the Plaintiffs have put forward—namely, compelling the dividend payments SBS would have been required to pay before it could incur debt;[49] estimating the results of a hypothetical consent fee; or determining the liquidation value of the preferred shares, assuming their refusal to consent to the refinancing would have forced the Company into insolvency—are in reality forms of equitable, and not legal, relief.

The Chancellor's recent decision in *Fletcher International, Ltd. v. ION Geophysical Corp.*,[50] at least with respect to the second measure supported by the Plaintiffs, suggests that the Defendant's position is incorrect. In that case, the preferred stockholder-plaintiff sought a preliminary injunction preventing the defendant-corporation from issuing a $40 million bridge loan in violation of the preferred stockholders' contractual right to consent to the issuance; the Court denied the application on the partial basis that the threat of injury was not irreparable, but was compensable with damages.[51] After trial, Chancellor Strine then addressed the appropriate measure of damages to which the plaintiff was entitled: expectation damages, as determined based on a hypothetical negotiation between the parties over the consent.[52]

As *Fletcher* demonstrates, at least one measure of damages supported by the Plaintiffs—a hypothetical consent fee—is a proper measure of contract, rather than equitable, damages. So too are the other

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[48] *See, e.g.*, *Certainteed Corp.*, 2005 WL 217032, at *16 ("CertainTeed has pled counts for declaratory judgment that track the [claims for contract damages]. The parties shall also include in the implementing order language that dismisses those counts to the extent that the related counts for damages have not survived . . . . ").

[49] The Defendant disputes the Plaintiffs' methods of computing damages. Because I grant the Defendant's Motion on other grounds, I need not reach those arguments.

[50] 2013 WL 6327997 (Del. Ch. Dec. 4, 2013).

[51] *Fletcher Int'l, Ltd. v. ION Geophysical Corp.*, 2010 WL 1223782, at *4 (Del. Ch. Mar. 24, 2010).

[52] *Fletcher Int'l, Ltd. v. ION Geophysical Corp.*, 2013 WL 6327997, at *1 (Del. Ch. Dec. 4, 2013).

measures of damages suggested by the Plaintiffs. They are simply a method to express the loss suffered by the Plaintiffs in monetary terms, then award that amount as damages to make the Plaintiffs whole. Such a request for damages is *not* equitable relief, as would be, for instance, specific performance. That this Court has the discretion to determine what measure of damages is appropriate for breach of contract[53] does not convert such legal relief into equitable relief. Since such damages, if I were to calculate them, would be legal, rather than equitable, recovery is not precluded under a laches analysis.

B. *Acquiescence*

Unlike the doctrine of laches—comprehensibly explained in our case law— the doctrine of acquiescence has been inconsistently applied and has rarely been addressed in a thorough, doctrinally-satisfying manner. I will not attempt to so address it here.[54] It should suffice for

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[53] *See Cobalt Operating, LLC v. James Crystal Enterprises, LLC*, 2007 WL 2142926, at *29 (Del. Ch. July 20, 2007) ("In Delaware, the traditional method of computing damages for a breach of contract claim is to determine the reasonable expectations of the parties. Expectation damages are calculated as the amount of money that would put the non-breaching party in the same position that the party would have been in had the breach never occurred. Moreover, when a contract or agreement is silent as to the remedy for a breach, *the Court of Chancery has the discretion to award any form of legal* or equitable *relief* . . . .") (emphasis added).

[54] "Acquiescence" as a doctrine has been applied in at least three separate iterations. First, our case law explains that stockholders who informedly accept the benefit of a merger transaction by accepting the merger consideration acquiesce in the transaction and cannot then challenge it. *See, e.g.*, *Bershad v. Curtiss-Wright Corp.*, 535 A.2d 840, 848 (Del. 1987) ("Since Bershad tendered his shares and accepted the merger consideration, he acquiesced in the transaction and cannot now attack it."); *Wechsler v. Abramowitz*, 1984 WL 8244, at *2 (1984) ("Acquiescence, also an equitable defense, is based upon the rule that equity will not permit a complainant to stultify himself by complaining against acts in which he participated or in which he has demonstrated his approval by sharing in the benefits—even though the suit might otherwise be meritorious. The doctrine has been applied in various situations but in corporate suits it is generally held that a stockholder who, with knowledge of all the pertinent facts, has concurred in acts of the directors or majority stockholders cannot afterwards attack such acts."). Second, the doctrine of acquiescence is, at times, used nearly synonymously with the doctrine of laches; in other words, where a plaintiff delays unreasonably in silence and thereby unfairly prejudices the defendant, she is said to have acquiesced in his conduct. 3 Pomeroy's Equity Jurisprudence § 817 (5th ed. 1941). In those circumstances, acquiescence works a "quasi estoppel"—the plaintiff is estopped from seeking equitable, but not legal, relief. *See id.* ("This effect of delay is subject to the important limitation that it is properly confined to claims for purely equitable remedies to which the party has no strict legal right. Where an injunction is asked in support of a strict legal right, the party is entitled to it if his legal right is established; mere delay and acquiescence will not, therefore, defeat the remedy, unless it has continued so long as to defeat the right itself."). Third, the doctrine of acquiescence has been

purposes of this Memorandum Opinion to note that inaction or silence on the part of a plaintiff, in certain circumstances, can bar a plaintiff from relief both equitable and legal.[55] The doctrine of acquiescence effectively works an estoppel: where a plaintiff has remained silent with knowledge of her rights, and the defendant has knowledge of the plaintiff's silence and relies on that silence to the defendant's detriment, the plaintiff will be estopped from seeking protection of those rights.[56] As described above, the equitable doctrine of laches focuses on *the plaintiff's* unreasonable delay, and why it would be inequitable to award *the plaintiff* the relief she seeks. Acquiescence, on the other hand, like estoppel, focuses on *the defendant's* knowledge of and reliance on the plaintiff's behavior (or lack thereof), and why the plaintiff must be adjudged complicit in the very breach for which she seeks damages. Although laches will not prevent a plaintiff from receiving legal relief, where the defendant has relied on the plaintiff's silence, acquiescence may.[57]

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used in the sense applied here, as a species of estoppel, estoppel by silence.

[55] *See, e.g.*, *Mizel v. Xenonics, Inc*., 2007 WL 4662113, at *7 (Del. Super. Oct. 25, 2007) (denying a motion for summary judgment on the partial basis that acquiescence as a defense to a breach of contract claim created a triable issue of fact); *USH Ventures v. Global Telesystems Grp., Inc*., 796 A.2d 7, 19 (Del. Super. 2000) ("Other equitable defenses are commonly recognized at law in contract as well as tort. Ripeness and mootness, which were originally equitable in nature, are commonly applied by this Court. Waiver has been, for some time, used at law as a valid defense to contract suits. Likewise, the equitable doctrine of acquiescence has been applied by this Court."); *In re PNC Delaware v. Berg*, 1997 WL 720705, at *4 (Del. Super. Oct. 22, 1997) ("[H]owever one characterizes the behavior of the Bank, whether it be in terms of waiver, acquiescence, estoppel, abandonment, or novation, the evidence is overwhelming that the Bank forewent its claim on the contract rights connected with the files that went to the Tighe firm."); *Mead v. Collins Realty Co*., 75 A.2d 705, 707 (Del. Super. 1950) ("Strictly speaking, then, it would appear that when a party to a contract breaches it in some minor respect and upon the tender by him of performance the other party, knowing of the defect, deliberately acquiesces, then the purported waiver of the right so accrued is not binding in the absence of consideration. . . . However, the thought of one party to a contract with full knowledge of the facts deliberately excusing some minor breach in performance and thereafter bringing an action for damages is repugnant. The Restatement bars a right of action in such case and, more importantly, the decisions of this State are in accord.").

[56] Another way this doctrine of acquiescence has been characterized is as estoppel by silence or estoppel by inaction. *See, e.g.*, 28 Romualdo P. Eclavea & Eric C. Surette, Am. Jur. Estoppel and Waiver § 57 (2d. 2013) ("The courts are especially disposed to uphold a claim of estoppel by silence or inaction where one party with full knowledge of the facts has stood by without asserting his or her rights or raising any objection while the other party, acting on the faith of such apparent acquiescence, incurred large expenditures that will be wholly or partially lost if such rights or objections are subsequently given effect."). Acquiescence in this sense is therefore not a doctrine separate from estoppel; rather, it is a subset of estoppel in which the defendant relies to her detriment on the plaintiff's silence rather than affirmative actions.

[57] *See* 3 Pomeroy's Equity Jurisprudence § 818 (Acquiescence as an Estoppel to Rights of Property or of Contract) (5th ed. 1941) (explaining that the doctrine of acquiescence may act as a bar at law to the vindication of property rights and contract rights).

SBS argues that the Plaintiffs acquiesced in the incurrence of additional debt at a time when a purported VRTE was in effect; that the Plaintiffs had knowledge of the VRTE and notice of the debt transactions; that the Plaintiffs remained silent despite that knowledge; and that SBS relied on that silence by incurring the additional debt. I agree, for the reasons explained below, that—assuming that the debt was incurred during a VRTE—such conduct on the Plaintiffs' part amounts to acquiescence, and must bar them from seeking contract damages in this action.

In order to prevail on a defense of acquiescence (as I use the term here), a defendant must show that (1) the plaintiff remained silent (2) with knowledge of her rights (3) and with the knowledge or expectation that the defendant would likely rely on her silence, (4) the defendant knew of the plaintiff's silence, and (5) the defendant in fact relied to her detriment on the plaintiff's silence.[58] The Plaintiffs here claim that they did not have actual knowledge of their rights prior to SBS's incurrence of debt. Our case law is inconsistent as to the quality of knowledge required for a finding of acquiescence.[59] However, I find that here, where all information necessary for the Plaintiffs' assessment of their rights was contained in publically-available documents and disclosures, and where the crucial fact in relation to a VRTE—the payment (or nonpayment) of dividends—is uniquely within the interest of the Plaintiffs as preferred stockholders with large ownership interests in the instrument, the Plaintiffs' knowledge of the circumstances affecting their rights as preferred stockholders must be imputed to them. Such a rule is not inconsistent with this Court's approach to other applications of estoppel.[60]

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[58] *Id.* § 805 (Equitable Estoppel—Elements and Requisites; Generally); *id.* § 818 ("Acquiescence consisting of mere silence may also operate as a true estoppel in equity to preclude a party from asserting legal title and rights of property, real or personal, or rights of contract. The requisites of such estoppel have been described.").

[59] *See Frank v. Wilson & Co.*, 32 A.2d 277, 283 (Del. 1943) ("Knowledge, *actual or imputed*, of all material facts is . . . essential . . . .") (emphasis added); *but see, e.g.*, *Julin v. Julin*, 787 A.2d 82, 84 (Del. 2001) ("Application of the standards underlying the defense of acquiescence is fact intensive, often depending, as here, on an evaluation of the knowledge, intention and motivation of the acquiescing party."); *In re Celera Corp. S'holder Litig.*, 2012 WL 1020471, at *9 (Del. Ch. Mar. 23, 2012), *rev'd in part on other grounds*, 59 A.3d 418 (Del. 2012) ("In general, to be susceptible to an acquiescence defense, the plaintiff must: (1) have 'full knowledge of his [or her] rights and all material facts;' (2) possess a 'meaningful choice' in determining how to act; and (3) act voluntarily in a manner 'show[ing] unequivocal approval' of the challenged conduct.") (internal citations omitted).

[60] *See, e.g.*, *Cornerstone Brands, Inc. v. O'Steen*, 2006 WL 2788414, at *3 n.12 (Del. Ch. Sept. 20, 2006) ("In order to prevail on an equitable estoppel theory, plaintiff must show (1) conduct by the party to be estopped that amounts to a false representation, concealment of

Here, the Plaintiffs had, at a minimum, imputed knowledge that a VRTE was in existence: the Certificate, which defined a VRTE, is a publically available document that controlled by its terms the nature and value of the significant investment in SBS held by the Plaintiffs. I note that the Plaintiffs themselves contend that the pertinent language in the Certificate was clear. Further, from SBS's public statements,[61] the Plaintiffs would have known, if they had been acting as prudent investors, that SBS had deferred dividends such that, under the Plaintiffs' understanding of the Certificate, a VRTE came into existence.[62] This is particularly so since the preferred stock was created as an alternative to a debt instrument, paying investors a quarterly fixed rate of return: when SBS stopped paying that return, any prudent investor with a large stake in the instrument should immediately have realized that the benefit of her bargain was being thwarted, or, at least, deferred.[63] The Certificate itself anticipates that holders of large interests in the preferred stock will monitor their investment, and accordingly places the responsibility to

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material facts, or that is calculated to convey an impression different from, and inconsistent with, that which the party subsequently attempts to assert, (2) knowledge, actual *or constructive*, of the real facts and the other party's lack of knowledge and the means of discovering the truth, (3) the intention o[r] expectation that the conduct shall be acted upon by, or influence, the other party and good faith reliance by the other, and (4) action or forbearance by the other party amounting to a change of status to his detriment.") (emphasis added); *Brown v. Fenimore*, 1977 WL 2566 (Del. Ch. Jan. 11, 1977) ("[Plaintiff] was a party to the agreement to distribute the shares of B&F as reported in the minutes of the January 28 meeting, and with knowledge, actual *or imputed* of the actual contribution of the [defendants], acquiesced in the consummation of the transaction, and acquiescence and participation in an issue of stock without consideration or for an insufficient consideration will bar the right of the assenting stockholder to complain against its issuance.") (emphasis added).

[61] Def.'s Op. Br. in Support of its Mot. for Summ. J. Ex. 38. Plaintiff T. Rowe Price's contention that SBS affirmatively concealed facts that would have put the Plaintiffs on notice of their claims, by removing language regarding a VRTE in its Form 10-K, is without merit. Answering Br. in Opp'n to Def.'s Mot. for Summ. J. by T. Rowe Price at 16. The Certificate, which defines a VRTE, is a public document, and the Plaintiffs should have known that, under the "clear language" reading it supports, a VRTE was in effect.

[62] The Plaintiffs contend that they initially believed that when the Company deferred dividends, it was actually paying its dividends as a PIK. This argument is unavailing, however, because the Company announced publically that it was deferring dividends, and because the Plaintiffs were on inquiry notice of the Certificate, which permitted dividends to be paid in kind only until October 15, 2008.

[63] I acknowledge that Plaintiff Lehman became subrogated to J.P. Morgan's rights in the Series B stock in March 2010, and the shares were returned to Lehman shortly thereafter. Although in bankruptcy until March 2012, Lehman acknowledges in briefing that as of March 24, 2010, it gained "possession and control of the shares of Series B Stock." Lehman's Mem. of Law in Support of its Mot. for Summ. J. at 13. It therefore should have been aware of the terms of its investment from that time forward; notably, according to Lehman, a VRTE did not come into effect until July 2010, several months after Lehman gained possession and control of its interest in the preferred stock.

request a special meeting to fill director seats created upon the occurrence of a VRTE on preferred stockholders owning a 10% or greater interest in the security. Here, Plaintiffs Lehman and T. Rowe Price owned a respective 38% and 14% interest in the Series B stock, so that each independently had the right to trigger an election; nevertheless, neither pursued their resulting right to seats on the Company board or otherwise acknowledged the VRTE.

The Plaintiffs also had notice that SBS intended to take on additional debt prior to the incurrence, as the Company publically announced its intent to consummate the first debt offering on May 6, 2011, *three months* prior to the actual offering on August 1 of that year. The Plaintiffs, with notice that the VRTE was in effect and of the Company's intent to take on additional debt, did nothing. Then, on January 27, 2012, the Plaintiffs again had notice,[64] via public announcement, of SBS's intent to restructure its debt with a note offering ending on February 7, 2012, and again, did nothing. To ensure that SBS did not rely on its silence, the Plaintiffs needed only to *notify* SBS that, under what it insists is the *clear* language of the Certificate, a VRTE was in effect, and therefore a debt incurrence would constitute a breach. Instead, the Plaintiffs made no such objection; SBS was aware that all relevant information regarding a VRTE and the debt transactions was available to the preferred stockholders; was aware that, despite access to that information, no preferred stockholder requested to fill seats on the board, or objected to the incurrence of debt; and relied on the lack of objection in consummating the debt transactions. That reliance is evidenced by SBS's credible assertion that, had it known of any preferred stockholders' objections prior to the incurrence of debt, it would have acted to avoid committing the alleged breach, either by eschewing additional debt; seeking a consent from the preferred stockholders, though, admittedly, such a unanimous consent might have been difficult to obtain; or petitioning this Court for a declaratory judgment *before* incurring the additional debt.[65] The Plaintiffs themselves, in seeking a

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[64] As noted above, the evidence indicates that at least one of the Plaintiffs, Lehman, had actual knowledge of the offering prior to the public announcement on January 27, 2012. *See supra* note 32.

[65] *See, e.g.*, Def.'s Op. Br. in Support of its Mot. for Summ. J. at 49 (arguing that the Plaintiffs had a duty to mitigate damages by notifying the Company of their objections before the debt—and thus, the damage—was incurred, and noting that "[i]f Plaintiffs had notified SBS that they believed a VRTE was in effect, the parties' present dispute may have been resolved in advance of SBS's debt incurrences, thus avoiding the current lawsuit."); Oral Arg. Tr. 160:23-161:9 ("Instead, whether willfully or by ignorance—the record supports simply by

consent fee as a measure of damages, must recognize that had they voiced an objection prior to the incurrence of debt, the Company would have sought to avoid a breach. Because, as I have previously found, the language employed by the parties to define a VRTE is facially ambiguous (permitting the Company a reasonable inference that no VRTE had in fact occurred), and because preferred stockholders with a significant economic interest in the Series B shares, including the Plaintiffs, did not request that the Company hold a special meeting to fill board seats created by the happening of a VRTE, such reliance was reasonable, and thus should have been foreseeable to the Plaintiffs. Further, reliance on the Plaintiffs' silence was *detrimental* to SBS because, had SBS known of the Plaintiffs' objections to the incurrence of additional debt, it could have, at a time prior to incurring any damages, chosen its own course: it could have estimated the cost of obtaining a consent from the preferred stockholders, taking into account any possible leverage generated by the VRTE provision's facial ambiguity; taken on additional debt to pay the accrued arrearages; become insolvent and restructured; eschewed the incurrence of additional debt; or litigated a declaratory judgment action, potentially avoiding any damages at all. SBS could have thus acted to minimize or avoid any damages by choosing what it believed to be its lowest cost option for responding to the preferred stockholders' objections, had it only known of them.

Now, almost three years after the alleged VRTE went into effect, and one year after the latest debt incurrence, the Plaintiffs argue that they are entitled to damages for a breach they might have prevented by exercising their rights to fill board seats, or by objecting to the purported breach. Moreover, the breaches of which they complain, the incurrence of additional debt, arose from actions taken by the board for the benefit of the corporation of which the Plaintiffs are among the equity holders, and from which actions the Plaintiffs therefore received a benefit.[66]

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ignorance—[the Plaintiffs] sat on their rights and didn't do anything about it. When, if they had acted differently, if they had said, "Wait a minute. We think a VRTE has occurred," we would have had an opportunity to come to the Court and have that question resolved. If they had said, "Wait a minute. We don't think you can incur this debt," we would have had an opportunity to come to court and get that question resolved and avoid any breach.") (emphasis added); *id.* 87:22-88:1, 88:16-17 (Plaintiffs' counsel acknowledging SBS's assertion that "they would have negotiated some sort of a deal had someone raised the issue with them," but declining to rebut that fact, instead contending that "[SBS] would have tried to negotiate some consent, but that's not prejudice"). I note that this action is before me on a stipulated record, which contains no indication that SBS did not in fact rely on the Plaintiffs' silence in incurring debt while the alleged VRTE was in effect.

[66] Notably, acceptance of a benefit is not a required element of this particular application of the doctrine of acquiescence, estoppel by silence. However, the fact that the

To be clear, the following factors form the basis for my decision that the Plaintiffs acquiesced in the debt transactions: (1) the Plaintiffs, in purchasing the Series B preferred stock, were investing in equity akin to debt instruments, the salient feature of which was the payment of quarterly dividends; (2) the Certificate's language, at least in the Plaintiffs' view, required the Company to refrain from incurring four consecutive quarters of arrearages, or trigger a VRTE, which would provide the Plaintiffs a right to place directors on the board as well as prevent the additional incurrence of debt; (3) the Plaintiffs should have known both that dividends were payable quarterly and that they had not received all quarterly dividend payments, commencing May 9, 2009; (4) thereafter, the Plaintiffs should have known (under their reading of the Certificate) that a VRTE was in effect as of April or July 2010; (5) the Plaintiffs had imputed, and in Lehman's case, actual, knowledge of SBS's intent to enter into the debt transactions in August 2011 and February 2012; (6) despite notice of all of these facts, the Plaintiffs did nothing, leading SBS to believe that the Plaintiffs acquiesced in the debt transactions; (7) that belief was reasonable, and thus foreseeable to the Plaintiffs, particularly in light of (a) the mechanism to fill board seats implemented in the Certificate whereby SBS would expect preferred stockholders with a large position in SBS (such as the Plaintiffs) to request the Company hold a special meeting upon the occurrence of a VRTE, (b) the facially ambiguous language of the VRTE provision, and (c) the fact that those debt transactions the Plaintiffs now challenge did at the time they were incurred confer on the Plaintiffs, as equity holders in the Company, a benefit which at that time they were apparently content to accept; (8) SBS entered into the debt transactions in reliance on the Plaintiffs' acquiescence; and (9) should the Plaintiffs be permitted to pursue damages here, such reliance will prove detrimental to SBS since, had the Plaintiffs notified SBS of their objections prior to the debt incurrence, SBS could have chosen for itself its lowest cost alternative for resolving the dispute. To hold otherwise would be to encourage substantial investors to stand by, witness a breach, and permit the accrual of damages that could have been prevented, or at least mitigated, but for their silence. Obviously, in a case not involving the particular considerations above—for example, if an investor held only a small equity interest in a company such that it would not be expected to closely

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Plaintiffs benefitted from the Company's incurrence of debt—setting aside whether such benefit would have outweighed the benefit preferred stockholders might have received in liquidation, or negotiated as a consent fee—lends additional credence to my finding that SBS reasonably understood the Plaintiffs' silence to indicate an acceptance of the transactions.

monitor that investment, or lacked the ability to protect its rights through procedural protections contained in a Certificate of Designation such that a Company could not reasonably expect that investor to notify it of objections to actions taken in potential violation of the Certificate—an analysis under the doctrine of acquiescence might produce a different result.

It is appropriate, for all the reasons above, that Plaintiffs be estopped from receiving the relief they seek here, under the doctrine of acquiescence.

IV. CONCLUSION

For the foregoing reasons, the Plaintiffs' Motions for Summary Judgment are denied, and SBS's Motion for Summary Judgment is granted. The parties should provide me with an appropriate Order.

ORACLE PARTNERS, L.P. V. BIOLASE, INC.

C.A. No. 9438-VCN

In the Court of Chancery of the State of Delaware

Date Submitted: April 25, 2014
Date Decided: May 21, 2014

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NOBLE, *Vice Chancellor*

Telephonic board meetings are undoubtedly routine for Delaware corporations. They allow dispersed directors to confer quickly over important issues regarding the corporation's business affairs. Despite their prevalence and utility, however, telephonic meetings have certain disadvantages—foremost among them being the lack of non-verbal communication, such as shaking another's hand or nodding one's head in agreement. The comparative strengths and weaknesses of telephonic and in-person board meetings generally may not matter that much. But, as this action demonstrates, when what was communicated on the phone is in dispute—and thereby becomes the subject of a fundamental corporate governance dispute among a corporation's directors, officers, and stockholders—the Court cannot help but wonder whether there would have even been a dispute had the directors simply met in person.

At issue in this action is what was said, and the legal effect of those statements, during a telephonic meeting on Friday, February 28, 2014, (the "Meeting") of the board of Defendant and Counterclaim-Plaintiff Biolase, Inc. ("Biolase"). Before the Meeting, Biolase had six directors: Federico Pignatelli ("Pignatelli"), Frederick Moll, M.D. ("Moll"), Norman Nemoy, M.D. ("Nemoy"), James Talevich

("Talevich"), Alexander Arrow, M.D. ("Arrow"), and Samuel Low, D.D.S. ("Low").[1]

On March 3, the Monday following the Meeting, Biolase issued a press release announcing that Arrow and Low had resigned from the board and that two individuals—Paul Clark ("Clark") and Jeffrey Nugent ("Nugent")—had been appointed to the board, which still had six members.[2] But, three days later, the company filed a Form 8-K with the Securities and Exchange Commission ("SEC") disclosing that Clark and Nugent had been appointed to the board, which purportedly had increased to eight members. The March 6 Form 8-K included the March 3 press release as an exhibit.[3]

Within a week, Plaintiff and Counterclaim Defendant Oracle Partners, L.P. ("Oracle"), a Biolase stockholder,[4] initiated this action pursuant to 8 *Del. C.* § 225 to determine the proper composition of the board. The directorships of Pignatelli, Moll, Nemoy, and Talevich (collectively, the "Undisputed Directors") are not at issue.[5] Oracle seeks a declaration that the current board consists of the Undisputed Directors, Clark, and Nugent.[6] In opposition, Biolase seeks a declaration that only the Undisputed Directors are current members of the board. Biolase has also asserted counterclaims against Oracle for fraud and negligent misrepresentation.[7]

This post-trial memorandum opinion sets forth the Court's findings of fact and conclusions of law.[8] For the reasons set forth below, the Court concludes: (i) the current directors of Biolase are the Undisputed Directors and Clark, who was appointed during the Meeting to the vacancy that had been created when Arrow verbally and effectively resigned; (ii) the Biolase board has one vacancy that was created when Low resigned by email after the Meeting; and (iii) Oracle is not liable to Biolase for fraud or negligent misrepresentation.

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[1] Joint Pretrial Stip. and Order ("Pre-Trial Stip.") § II, ¶ 4.

[2] *Id.* § II, ¶ 6.

[3] *Id.* § II, ¶ 8.

[4] *Id.* § II, ¶¶ 1, 12.

[5] On March 20, 2014, the Court entered a Status Quo Order providing that the Undisputed Directors would constitute the Board during the pendency of this litigation. By the terms of the Status Quo Order, the Board may only act by supermajority vote (i.e., three of four directors).

[6] *Id.* § IV.A; Verified Compl. ¶¶ 24-27.

[7] Pre-Trial Stip. § IV.B; Answer and Verified Countercl. of Def. Biolase, Inc. ¶¶ 28-51.

[8] The Court held a one-day trial in this matter on April 24, 2014, approximately six weeks after Biolase filed its Verified Complaint.

I. BACKGROUND

A. *The Parties*

Oracle, a Delaware limited partnership based in Greenwich, Connecticut, is a "strategic investment firm solely within the health care industry."[9] Larry Feinberg ("Feinberg") is the managing member of Oracle's general partner.[10] Oracle has never been involved in a proxy contest, a going-private transaction, or, prior to this action, any litigation.[11] Presently, it beneficially owns 16.4% of Biolase's common stock.[12]

Biolase, a publicly traded Delaware corporation with its headquarters in Irvine, California, is a medical device manufacturer focused on the dental industry. Its main products are laser-based devices.[13] Pignatelli is Biolase's chairman and Chief Executive Officer ("CEO").[14] Arrow is the company's President and Chief Operating Officer ("COO").[15] Frederick Furry ("Furry") is the company's Chief Financial Officer ("CFO") and was offered as its witness pursuant to Court of Chancery Rule 30(b)(6).[16]

For several years, Biolase has had a stockholder Rights Agreement (*i.e.*, a poison pill) under which rights certificates would be distributed when a stockholder acquired 15% of the company's common stock.[17] The Biolase board raised the pill threshold to 20% on February 4, 2014,[18] in anticipation of the private placement by which Oracle became a 16.4% stockholder later that month.

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[9] Trial Tr. ("Tr.") 5 (Feinberg).
[10] Feinberg Dep. 9.
[11] Tr. 6 (Feinberg).
[12] Pre-Trial Stip. § II, ¶ 1.
[13] Joint Exhibit ("JX") 220.
[14] Tr. 266 (Pignatelli).
[15] *Id.* 106-07 (Arrow).
[16] *Id.* 229 (Furry).
[17] *Id.* 274 (Pignatelli).
[18] JX 73.

B. *Key Individuals*

1. The Undisputed Directors: Pignatelli, Moll, Nemoy, and Talevich

Pignatelli first became involved with Biolase in 1991, when he financed the company with approximately $1 million. He has been a director since 1991 and the chairman of the board since 2010. Pignatelli asserts that he spends "110 percent" of his time as chairman and CEO of Biolase, but he conceded that he has engagements with several other businesses.[19] Perhaps because of these other commitments, Pignatelli regularly works remotely.[20]

Nemoy has been a director of Biolase since 2010,[21] and Moll and Talevich have been directors since 2013.[22] Nemoy is the chair of the board's nominating and corporate governance committee.[23]

2. Arrow and Low

Arrow joined the board in July 2010 and became President and COO in 2013. From Arrow's perspective, Pignatelli has run both the business and the board of Biolase with a "dictatorial management style."[24]

Low joined the board in mid-December 2013. Pignatelli and Arrow recruited him to become a director after they had met at an industry conference.[25]

3. Clark and Nugent

Clark has significant experience in the pharmaceutical industry, both at the officer and board levels. As of March 2014, he was serving as a director on three other boards, including of a private company of which Moll was also a director.[26] Nugent likewise has considerable executive and director experience with medical device and related

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[19] Tr. 264, 266-67 (Pignatelli); JX 6.
[20] Tr. 167 (Arrow).
[21] JX 6.
[22] Moll Dep. 25-26; Pre-Trial Stip. § II, ¶ 3.
[23] Moll Dep. 43.
[24] Tr. 106-07, 109 (Arrow).
[25] *Id.* 322-23 (Low).
[26] JX 161; Moll Dep. 43.

companies, most recently with an aesthetic dermatology business that used laser technology similar to that of Biolase.[27]

C. *Oracle Becomes Interested in Investing in Biolase*

Based on a suggestion from one of his analysts, Feinberg first looked into investing in Biolase during the summer of 2013. His interest was piqued when Moll, an acquaintance and a medical device "innovator," joined the board. The more Feinberg looked into Biolase, the more he viewed it as an "exciting company" with "great technology."[28]

Feinberg eventually met Pignatelli, and the two discussed a potential "large investment" by Oracle in Biolase.[29] Two of Feinberg's initial concerns were that the company had "very poor corporate governance" and, in particular, that it "need[ed] a real CEO to run the company."[30] He was not discussing a co-CEO arrangement. Pignatelli seemed generally receptive to these ideas, although he was hesitant about a current investment because he believed the company's stock was undervalued.[31]

On September 4, Feinberg emailed Pignatelli and Arrow a proposed term sheet for an investment of $6 million for stock and warrants. The proposal also contemplated that the Biolase board would expand by two members, with the new directors nominated by Oracle and reasonably acceptable to the company.[32] At Pignatelli's direction,[33] Arrow responded with an $11 million investment proposal under which Oracle would purchase $6 million of Biolase stock then and commit to buy $5 million more by the end of the year.[34] Feinberg found this proposal "ridiculous."[35]

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[27] JX 161.

[28] Tr. 6-7, 9 (Feinberg).

[29] *Id.* 9 (Feinberg), 269 (Pignatelli).

[30] *Id.* 9 (Feinberg).

[31] *Id.* 9, 103-04 (Feinberg). Pignatelli claimed that he only discussed stepping aside as CEO in "general terms," *id.* 271 (Pignatelli), but Feinberg's contemporaneous notes support the Court's conclusion that Pignatelli and Feinberg discussed this issue from the beginning of their relationship. JX 239 ("Federico would be thrilled to be just chairman, doesn't want to be CEO. He wants to get pushed upstairs.").

[32] JX 16, 17.

[33] Tr. 112 (Arrow).

[34] JX 17.

[35] Tr. 102 (Feinberg).

In a series of emails, the parties debated whether Oracle's proposal would be dilutive to other Biolase stockholders or "long-term accretive."[36] During the exchange, Feinberg repeated his views on the company's corporate governance and management needs to both Pignatelli and Arrow:

> We believe Biolase needs to both supplement its current Board of Directors with more experienced operational personnel, as well as bring in a full-time CEO with medical device experience to help fix the operational issues and implement the strategic vision of Federico.[37]

This subject was not new to Arrow; he had frequently discussed the possibility of hiring a new CEO with Pignatelli, who regularly agreed that it would be "appropriate for him to step aside when the right person could be brought in."[38]

Frustrated by the company's response, Feinberg and one of his analysts considered other options. At one point, it was suggested that Oracle might want to "add on weakness and go hostile anytime."[39] Feinberg's understanding of the term "hostile" in this context was that Oracle would "actively attempt to influence management . . . to improve the board of directors and improve management."[40] In other words, Oracle was not seeking to "control" Biolase—Feinberg wanted strong, independent directors to manage the company.

Another possibility they considered was that Pignatelli might eventually be replaced as CEO. At no point did Feinberg suggest that he wanted to be the CEO of Biolase or that some specific person should have that position. Feinberg testified that this was not so much a plan, or even a goal, but rather a discussion of "what might transpire with this investment over time."[41] At least in part, it appeared to be a reaction to the lack of commitment and business sophistication that Feinberg

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[36] *Id.* 13 (Feinberg).

[37] JX 17; Tr. 14-15 (Feinberg). At trial, Pignatelli denied ever receiving this email, suggesting that the document may have been altered or forged. *Id.* 273, 299 (Pignatelli). The Court cannot accept Pignatelli's speculation in light of the weight of conflicting testimony.

[38] Tr. 112-13 (Arrow). Arrow testified that Pignatelli told him explicitly, on more than one occasion, that he would like to step aside as CEO; this sentiment even was part of Pignatelli's pitch to persuade him to join the company. *Id.* 110-11.

[39] JX 20.

[40] Tr. 44-45 (Feinberg). Feinberg further explained that he wanted "to have enough influence on the company that they will listen to their largest shareholders." *Id.*

[41] *Id.* 61-62, 66-67 (Feinberg).

perceived in Pignatelli during their negotiations. Oracle did not directly invest in Biolase at that time.

D. *Oracle Buys Biolase Stock on the Open Market*

Throughout the fall of 2013, Oracle bought Biolase stock in the public markets. Some of these purchases were made before Biolase announced its 2013 third quarter results, which revealed that the company was running out of cash.[42] Feinberg had exchanged at least one email with Moll about this problem.[43]

Oracle continued to accumulate Biolase stock. In November 2013, it filed a Schedule 13D with the SEC disclosing that it beneficially owned 9.89% of the company's stock.[44] The "Purpose of the Transaction" section of the Schedule 13D stated, in part:

> To the extent permitted by law, the Reporting Persons [i.e., Oracle and its affiliates] may take such actions with respect to their investment in the Issuer [i.e., Biolase] as they deem appropriate in order to protect their investment and maximize shareholder value. Such actions may include, without limitation, discussions with other stockholders and/or with management and the Board of Directors of the Issuer concerning the business, operations or future business and strategic plans of the Issuer and composition of the Board of Directors, as well as purchasing additional Shares, selling Shares, engaging in hedging or similar transactions with respect to the Common Stock or taking any other action with respect to the Issuer or any of its securities in any manner permitted by law . . . .[45]

Feinberg understood this language to reflect that Oracle was "considering all possible options" with a goal of "improv[ing] shareholder value."[46]

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[42] JX 27.

[43] JX 23.

[44] Pre-Trial Stip. § II, ¶ 1.

[45] JX 28. Oracle's lawyers at Kane Kessler, P.C. ("Kane Kessler") prepared the initial Schedule 13D and the subsequent amendments. Tr. 54 (Feinberg).

[46] Tr. 17 (Feinberg). An email he sent to Clark about the Schedule 13D reflected that understanding. JX 34. Separately, after this filing, Feinberg shared his view with at least Clark and a third party that Biolase would likely benefit from different management. Tr. 68 (Feinberg).

This section was not modified when Oracle later filed several amendments to its Schedule 13D.

E. *Feinberg's Thoughts on Biolase's Need for Management*

Around this time, Feinberg expressed his view privately to Clark, a casual friend with whom he occasionally invested,[47] that he felt Biolase needed "new management, two boards seats, and to recapitalize."[48] Earlier, Feinberg had suggested to Clark that "[t]he board will easily swing in our direction" on these points.[49] He based this expectation on conversations he had had with several Biolase directors—namely, Erin Enright ("Enright") and Gregory Lichtwardt ("Lichtwardt")[50]—who wanted Oracle "to get involved to help recapitalize the company and to bring in and effect better corporate governance."[51] Enright and Lichtwardt were in the midst of a significant disagreement with other Biolasedirectors, led primarily by Pignatelli, over the financial direction of the company. They wanted to form a special committee to raise approximately $20 million to pay accounts payable, to reduce a line of credit, and to create working capital. Pignatelli strongly opposed this effort.[52] Unable to resolve this fundamental disagreement, Enright and Lichtwardt resigned from the Biolase board on December 4, 2013.[53]

Internally at Oracle, Feinberg explained that he thought Enright was quitting the board because "she thinks we're not being aggressive enough." Specifically, he understood Enright as wanting Oracle "to do a proxy fight."[54] Perhaps reacting to the news that two directors sympathetic toward improving the company's corporate governance had

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[47] Tr. 34-35 (Feinberg).

[48] JX 32; *see also* JX 34.

[49] JX 32. At his deposition Feinberg described this particular email as referring to the board's likelihood of agreeing to "bringing good senior management in to supplement Mr. Pignatelli." Feinberg Dep. 88.

[50] Tr. 22-24 (Feinberg).

During an impromptu meeting in December among Arrow, Pignatelli, Enright, and an Oracle analyst at a dental show in New York, the CEO position was a subject of conversation. The theme seemed to be that Pignatelli would be willing to step aside as CEO, and the Oracle analyst endorsed this sentiment. *Id.* 115 (Arrow); JX 37.

[51] Tr. 20 (Feinberg).

[52] *See* JX 30, 31; Tr. 116-17 (Arrow).

[53] Pre-Trial Stip. § II, ¶ 2; Tr. 22-24 (Feinberg), 117 (Arrow).

[54] JX 37. Feinberg also wrote, "So I think we should," but nothing came of that comment at the time. *Id.*

just resigned, Feinberg suggested to a third party that Oracle might "get active and perhaps nasty" regarding its Biolase investment.[55]

F. *Oracle Continues to Buy Biolase Stock*

Almost in passing, Pignatelli suggested in December 2013 that Oracle might want to take Biolase private "in the $5 range."[56] Feinberg never seriously considered that option. Going private was not part of his investment thesis, and he was concerned that if Oracle attempted a takeover, then "a corporate buyer would step in and take the company" at a higher price.[57]

Near the end of 2013, Oracle bought additional Biolase stock on the public markets. It also purchased approximately $612,000 worth of stock from the company in a private placement.[58] Altogether, Oracle's beneficial ownership had increased to 11.4%. Biolase notes that Oracle's amended Schedule 13D did not include any of the sentiments that Feinberg may have shared with others in the interim.[59]

Feinberg grew more eager to effect corporate governance changes at Biolase as the new year began. In January, Feinberg emailed Clark to let him know that Oracle was "considering launching a proxy contest for 2 board seats in a few weeks," and he apparently wanted to gauge Clark's interest in participating. Feinberg thought they both could get elected, and he expected they would likely "have enough support to force the hiring of a new CEO and a refinancing."[60] Clark said he would "be happy to join [Feinberg] on the board."[61] It does not appear that Oracle took any further steps toward initiating a proxy contest at the time.

Coincidentally, the company's need for financing appeared again in 2014. The company filed a shelf registration statement for $12.5 million, the maximum to which Pignatelli would agree,[62] in January. But, as of the date of trial in this action, Biolase had not yet sold any stock pursuant to this registration statement—perhaps because it already had a willing investor: Oracle.

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[55] JX 38; Tr. 71 (Feinberg).
[56] JX 40.
[57] Tr. 25-27 (Feinberg).
[58] *Id.* 24-25 (Feinberg); JX 43
[59] Tr. 74-76 (Feinberg); JX 44.
[60] JX 56; Tr. 77-79 (Feinberg).
[61] JX 56.
[62] Tr. 117-18 (Arrow).

Pignatelli asked Feinberg if Oracle would be interested in making a $5 million investment in Biolase in February 2014. As the parties negotiated an investment in that range, it became clear that an additional purchase by Oracle of that much stock, at current prices, would have taken its ownership over the company's 15% poison pill threshold. After he discussed the merits of amending the pill with Feinberg, Pigantelli recommended to the board that it raise the threshold from 15% to 20%.[63] The board quickly did so.[64] Oracle then invested approximately $5 million in Biolase through another private placement on February 10,[65] which, with other small market purchases, brought it to its current 16.4% ownership.[66]

G. *Possible New Directors for Biolase*

The next day, Feinberg again requested to talk with Pignatelli about his corporate governance and management concerns.[67] Feinberg mentioned that he had several director nominees in mind.[68] Pignatelli noted that two current directors—Arrow and Low—would not be up for reelection at the 2014 annual meeting and that he was considering inviting Nugent, who had been the CEO of several companies, to be on the board.[69] Pignatelli also wrote, "I agree on Board,"[70] which Feinberg interpreted as Pignatelli's agreeing that Biolase needed more experienced directors.[71]

Feinberg suggested two candidates: Clark and Mark Gainor ("Gainor").[72] Pignatelli found the resumes of both candidates to be "excellent," but he noted that he "already [had] sort of a commitment for a Board membership with Jeff Nugent."[73] At this time, however,

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[63] *Id.* 273-76 (Pignatelli); JX 53. Pignatelli later suggested that had he known that Oracle wanted to control the board, he would not have recommended that the Board approve Oracle's additional investment or raise the poison pill threshold. Tr. 278 (Pignatelli). Whether Oracle ever sought to control the board is a separate issue.

[64] JX 73.

[65] JX 71.

[66] JX 78.

[67] JX 76.

[68] JX 84.

[69] Tr. 279-80 (Pignatelli); JX 84.

[70] JX 84.

[71] Tr. 30-31 (Feinberg).

[72] JX 98; Tr. 278 (Pignatelli).

[73] JX 98.

Pignatelli had not offered any board position to, let alone come to an agreement with, Nugent.

1. Clark

Feinberg disclosed to Pignatelli that he had been involved with Clark in several past investments.[74] Other than one common investment, Feinberg and Clark have no current business relationships. Clark is also not an investor in Oracle.[75]

There is no evidence that Feinberg and Clark had any agreement, implicit or otherwise, regarding what Clark would do if he became a Biolase director.[76]

Feinberg did testify, however, that he had an expectation that Clark, as an independent director with considerable experience, likely "would bring in a new management team, particularly [a] chief executive officer."[77]

2. Gainor

Gainor, like Clark, has extensive management experience in the healthcare and pharmaceutical industries.[78] He and Feinberg have been friends for over a decade.[79]

3. Nugent

Nugent grew interested in Biolase because of the possibilities of its laser technology. After talking to Arrow at an industry conference, however, Nugent arranged to meet with Pignatelli.[80] Before he had even met Pignatelli, Nugent already believed that Biolase was "poorly managed, . . . and as a result, . . . undervalued."[81]

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[74] JX 108.

[75] Tr. 34-35 (Feinberg).

[76] This is not to say, however, that Feinberg had not shared his views about Biolase with Clark in the past. In particular, Feinberg had expressed his belief that "Pignatelli would not make it in the long run as CEO" and that "a new CEO would be a likely outcome." *Id.* 36 (Feinberg).

[77] *Id.* 36-37 (Feinberg).

[78] JX 98.

[79] Tr. 105 (Feinberg). The parties did not provide additional information about Gainor.

[80] *Id.* 176-77 (Nugent).

[81] JX 82.

Feinberg was at first annoyed that Pignatelli had suggested Nugent—not because Feinberg knew Nugent, but because he did not. Feinberg and Nugent had met only once, and briefly, about an investment opportunity in 2010. They have no business relationship or common investments, and Nugent is not an investor in Oracle.[82] Feinberg was initially concerned that Nugent might not be a truly independent director but might instead be "teaming up" with Pignatelli.[83]

These feelings soon changed. As part of what he considered his "due diligence to find out if this was something [he] really wanted to do," Nugent met with Feinberg, the representative of the company's largest stockholder. The two met briefly in mid-February to discuss Biolase, including its corporate governance and leadership.[84]

Based on their conversation, Feinberg came to expect that Nugent, as an experienced, independent director like Clark, would "effect change in the CEO position."[85] There is no evidence that they had any agreement, in general or specific terms, as to what Nugent would do as a Biolase director. Any understanding that the two shared was, according to Nugent, "to put stronger, independent directors on the board in order for those individuals to make the right decisions to be able to improve the value of that company."[86] After this meeting, Oracle came to view Nugent's involvement as a strength, not a weakness.[87]

Feinberg later told Pignatelli that, although he did not "really know" Nugent, he nonetheless thought that adding Nugent to the board could be a "very good idea" for Biolase.[88] Feinberg did not disclose their

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[82] Tr. 31-33, 39-40 (Feinberg), 176 (Nugent).

[83] *Id.* 32 (Feinberg); JX 90. The whole point of adding two new directors, in Feinberg's opinion, was to get individuals who were independent, not those who might be Pignatelli's "friends . . . that would do what he wanted." Tr. 33 (Feinberg).

[84] Tr. 189-91 (Nugent). Feinberg recalled that Nugent suggested he might be interested in the CEO position, but he had several other opportunities to consider. *Id.* 38-39 (Feinberg). Nugent would later express a similar sentiment to Clark after the Meeting, but he was cautious that any senior position with Biolase would require relocating his family, which he did not take lightly. *Id.* 190-91 (Nugent); JX 151.

[85] Tr. 39 (Feinberg).

[86] *Id.* 189 (Nugent).

[87] Although the exact chronology is unclear, sometime around this meeting an Oracle analyst expressed the view that the firm might get "control" of the board with Moll, Oracle's two nominees (Clark and Gainor), and Nugent. JX 83. Feinberg explained at trial that his understanding of the term "control" in this context did not mean having directors beholden to him but rather having a "majority of directors who would be independent, logical, normal thinking directors." Tr. 82-84 (Feinberg).

In other words, Feinberg sought to have Biolase under the "control" of independent directors, and thus not beholden to him—or, more importantly, Pignatelli.

[88] JX 108.

recent meeting. When asked why, Feinberg testified that he "didn't want to potentially lose whom [he] believed would be a huge improvement as a director on the board of Biolase," because he feared that "if Mr. Pignatelli thought Mr. Nugent had [a] dialogue with [him], then [Pignatelli] would no longer consider Mr. Nugent."[89] For the same reason, Feinberg also encouraged others not to disclose that he may have known Nugent.[90] It appears that Feinberg wanted Nugent as a Biolase director not because Oracle could control him, but rather because Feinberg thought Nugent was exactly the type of independent director that the company desperately needed.

H. *Pignatelli Informally Interviews the Director Candidates*

1. Pignatelli Discusses the CEO Position with Nugent

Nugent and Pignatelli first met on February 20, 2014.[91] At their dinner meeting, they discussed two main subjects: first, the company and its technology; and second, the opportunity for Nugent to join the board and have a "CEO/chairman position." Pignatelli told Nugent—as he had said several times in the past to Arrow and Feinberg—that he was ready to step down as CEO if he was able to find someone who could do a better job,[92] implying that Nugent might be that person. Pignatelli sent Nugent a text message to that effect the next day.[93]

2. Pignatelli Chooses Clark over Gainor

Feinberg's two director candidates, Clark and Gainor, met with various Biolase executives at the company's California offices on Tuesday, February 25. Pignatelli and Arrow made presentations, and Furry participated in these meetings for several hours. Furry could not

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[89] Tr. 40-41, 91-92 (Feinberg).

[90] *Id.* 95-96 (Feinberg). JX 125.

[91] Tr. 309 (Pignatelli). Nugent and Feinberg exchanged emails about what to expect during the meeting, but they did not discuss anything substantive or otherwise material. *See, e.g.*, JX 95, 96, 102; Tr. 92-94 (Feinberg).

[92] Tr. 178-79, 186 (Nugent).

[93] JX 210; Tr. 179-80 (Nugent). Although Pignatelli denied that he ever mentioned to Nugent that he was ready to step down as CEO, *id.* 309 (Pignatelli), the weight of the evidence demonstrates that the opposite more likely occurred.

recall any discussion of Oracle. Of the two candidates, Pignatelli ultimately preferred Clark.[94]

3. Nugent Tours the Biolase Offices

Two days later, on February 27, Nugent toured Biolase's offices. He likewise met with several people, including Pignatelli, Arrow, Furry, and Talevich.[95] But, even before these meetings, based on his diligence with investors and dental surgeons whom he knew personally, Nugent believed there was a "serious question as to Mr. Pignatelli's competence as chairman and CEO and his ability to dramatically change the performance of that company." During his day in California, Nugent's view of Pignatelli changed "dramatically," and for the worse. [96]

One scene in particular demonstrated the weaknesses of Biolase's corporate governance practices. Nugent was in the room when Pignatelli called Nemoy, the head of the board's nominating and corporate governance committee, and "told" Nemoy what he wanted to happen during the Meeting: for Arrow and Low to resign, and for Clark and Nugent to be appointed. Within an hour, Nemoy sent an email to the board reflecting what Pignatelli had requested.[97] Nugent viewed this dynamic—a chairman and CEO unilaterally dictating what the board would do—as very problematic.[98] Throughout the day, Nugent was also becoming very troubled by Pignatelli's management style of "striking fear" into employees.[99]

At some point, Feinberg and Pignatelli came to an agreement on the two persons to add to the Biolase board: Clark and Nugent.[100] Each nominee was likely informed that the other would also be nominated as a director. Clark told Pignatelli that he did not know Nugent, but he did

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[94] Tr. 231-33 (Furry).

[95] *Id.* 180 (Nugent). Again, while Furry was in the room, Oracle did not come up in the meetings with Nugent. *Id.* 234-35 (Furry).

[96] *Id.* 180-83 (Nugent). For example, Nugent was very concerned about the "preposterous" and unrealistically positive guidance that Pignatelli planned on giving analysts during the company's upcoming earnings release. Nugent was very vocal about this issue with Pignatelli and others. *Id.* As he did with similar testimony critical of his management, Pignatelli denied having such a conversation with Nugent before the Meeting. *Id.* 280-81 (Pignatelli).

[97] JX 118.

[98] Tr. 184-85 (Nugent).

[99] *Id.* 183 (Nugent).

[100] *Id.* 33 (Feinberg).

find Nugent's background "impressive."[101] Separately, Feinberg would later inform Gainor that he would not be a director of Biolase.[102]

I. *Pignatelli Tells Arrow and Low that They are Going to Resign from the Board*

Part of the agenda for the Meeting was to nominate a slate of directors for Biolase's 2014 annual stockholder meeting. By February 21, Pignatelli had decided that Arrow and Low would not be re-nominated and that Clark and Nugent would be nominated in their stead.[103] That plan continued to change, however. Talevich proposed a few other options,[104] but Pignatelli ultimately decided, no later than February 27, that Arrow and Low would resign during the Meeting and be replaced immediately by Clark and Nugent.[105] Expanding the board from six directors to seven or eight was never considered before the Meeting, according to Furry, because of these "planned" vacancies.[106]

1. Arrow

Pignatelli first told Arrow that he did not want him on the board long-term in December 2013. The possibility that Arrow might resign did not come up in earnest, however, until around February 27. That day, when Pignatelli requested that Arrow resign from the board during the Meeting, Arrow was "surprised and unhappy." The two debated for some time over whether Arrow should resign or serve out the rest of his term.[107]

That night, Arrow had dinner with Pignatelli and Nugent. On the drive there, Arrow discussed the resignation with Nugent, who encouraged Arrow to "not get too exercised on it right now."[108] Primarily

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[101] JX 116.

[102] Although the exact timing is unclear, sometime on February 27 or 28, Feinberg also wrote that Clark and Nugent "will immediately call a board meeting to review the CEO position and eliminate Federico from that job." JX 148. The point of sending the message was to "placate" Gainor, his friend, and let know him what was happening. Tr. 105 (Feinberg). Regardless of whatever Feinberg may have expected, Nugent flatly rejected that they had any agreement to terminate Pignatelli as CEO. *Id.* 211-12 (Nugent).

[103] JX 103.

[104] JX 135.

[105] JX 118, 119.

[106] Tr. 250 (Furry).

[107] *Id.* 119-21 (Arrow).

[108] *Id.* 187 (Nugent).

two topics were discussed at dinner: Arrow's resignation from the board, and Nugent's opportunity to become the CEO of Biolase. At some point, Arrow likely said that he wanted a few days to think about resigning because he felt that he had been given short notice about it.[109]

But, by the end of the meal, Arrow agreed to "resign the next morning" during the Meeting. He and Pignatelli even shook hands to memorialize their agreement.[110]

2. Low

After he became a director in December 2013, Low grew concerned that his membership on the board might jeopardize his consulting agreement with the company. By the middle of February 2014, Low informed Arrow and Furry that, if he needed to pick one position, he preferred to be a consultant instead of a director.[111] Likely the day before the Meeting, Pignatelli called Low and asked him to resign. Low testified that he told Pignatelli that he would consider resigning "if it was in the best interests of the company." Based on this conversation and the emails circulated by Pignatelli and Nemoy, Low understood that he and Arrow would be resigning from the board and that Clark and Nugent would be appointed as their replacements.[112]

J. *February 28, 2014*

1. The Meeting

The board convened the Meeting at 10:00 a.m. PST. Furry and Michael Carroll ("Carroll"), Biolase's Secretary and General Counsel, had prepared the agenda.[113] Carroll began the meeting by bringing up the resignations of Arrow and Low.[114]

Arrow quickly interrupted Carroll to discuss whether the expiration date on his director stock options could be extended. He also likely suggested that the board could be expanded to seven. Pignatelli reacted negatively to Arrow's comments, demanding that Arrow follow

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[109] *Id.* 121, 149-50 (Arrow).

[110] *Id.* 122 (Arrow). During dinner, Pignatelli intimated that he would keep Arrow as President and COO for as long as he was CEO. *Id.*

[111] *Id.* 326-27 (Low).

[112] *Id.* 328-29 (Low).

[113] *Id.* 236 (Furry); JX 126.

[114] Tr. 122. (Arrow).

through on that "hand shake deal" to resign. The two probably argued for between fifteen and thirty minutes. Arrow eventually asked Moll about what he should do, and Moll encouraged him to follow Pignatelli's lead on this point.[115] Arrow testified that, at the end of the debate, he said, "Okay, I agree, I go along with that."[116] With those words, Arrow believed that he had verbally resigned from the board.[117]

Low recalled that the agenda provided that he would be resigning from the board, but he testified that he never spoke during the Meeting.[118] In fact, no one could recall that Low said anything during the Meeting.[119] Despite Pignatelli's statements to the contrary,[120] Low's resignation was not conditioned on his accepting any consulting agreement.[121] Low further testified that he intended his resignation to become effective "[w]ith the completion of a written resignation." That is, he "assumed that [he] would not be a board member after [he] had tendered a written resignation," which he planned to do, presumably after the Meeting.[122]

After the discussion of the resignations, the board unanimously voted to appoint Clark and Nugent as directors.[123] Furry was fairly confident that Arrow affirmatively participated in this vote, but he could not recall if Low said anything.[124] Arrow believed that he voted on the appointments. He did so not to suggest that he was still a director, but rather to avoid "mak[ing] it seem like [he] was spiteful that [he] had just been forced to resign."[125]

Carroll prepared a draft of the board minutes of the Meeting.[126] The draft reflects that the resignation discussion occurred before the

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[115] *Id.* 123-24, 154-55 (Arrow).

[116] *Id.* 124 (Arrow).

[117] *Id.* 124-125 (Arrow). The deposition and trial testimony of other witnesses supports Arrow's understanding that he had resigned. *Id.* 237 (Furry); Low Dep. 33; Moll Dep. 59; Talevich Dep. 45. Only Pignatelli claimed that Arrow did not agree to resign. Tr. 315 (Pignatelli).

[118] Tr. 324 (Low).

[119] *Id.* 161 (Arrow), 238 (Furry), 283 (Pignatelli); Moll Dep. 57; Talevich Dep. 45-46.

[120] Tr. 313 (Pignatelli).

[121] *Id.* 329-30 (Low).

[122] *Id.* 325, 330-31 (Low).

[123] *Id.* 127 (Arrow), 239 (Furry); Moll Dep. 123; Talevich Dep. 46-47.

Only Pignatelli testified that the Board voted for the appointments of Clark and Nugent before the discussion of the resignations. Tr. 282 (Pignatelli). Even when challenged at trial that his testimony on the chronology differed from that of everyone else, he maintained that he had "a very clear recollection of that meeting." *Id.* 314-15 (Pignatelli). Given the weight of evidence to the contrary, the Court cannot adopt Pignatelli's testimony on this issue.

[124] Tr. 239 (Furry).

[125] *Id.* 156 (Arrow).

[126] *Id.* 240 (Furry).

appointments and that the Meeting concluded at 11:12 a.m. PST.[127] Because of this proceeding, the board has not yet adopted the minutes.[128]

2. Arrow's Conversation with Pignatelli

After the Meeting, Arrow again asked Pignatelli why it could not have been another director—namely, Nemoy—who resigned. Arrow argued that, as an officer, he received no director compensation, but Biolase paid $42,000 to Nemoy to serve as a board member. He also still wanted to be a part of the new slate of directors for the 2014 annual meeting.[129] Pignatelli was not persuaded, and this conversation did not change anything for either of them.

3. The Resignation Emails

Shortly after the Meeting, Carroll provided Arrow and Low with a template resignation email for them to send to Pignatelli. The template stated, in part:

> Dear Federico:
>
> This letter is notice to Biolase, Inc. (the "Company") that I am resigning as a member of the Board of Directors of the Company, effective as of 12:00 p.m. Pacific Time today.
>
> Yours very truly,[130]

Arrow copied the template into a new email, added additional comments about his time on the board, and then sent it to Pignatelli and Carroll.[131] Unlike Low, Arrow did not think that he needed to tender a written resignation to resign; rather, he sent the email because he was "instructed to do so by [Biolase's] general counsel." Because it was "obvious" that he had resigned during the Meeting, it "did not occur" to Arrow to

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[127] JX 227.

[128] There was testimony at trial suggesting that this draft may have been edited on March 21. Furry acknowledged that if the metadata on the draft minutes reflect edits on March 21, then that would have been during the course of this litigation. Tr. 252 (Furry).

[129] *Id.* 161-62 (Arrow).

[130] JX 128.

[131] Tr. 125-26 (Arrow); JX 137.

change the effective time or to note that he was "confirming" his prior resignation.[132]

Low sent his resignation email, with no modifications, to Pignatelli and Carroll within an hour of the Meeting.[133]

K. *Clark and Nugent's Conduct as Purported Directors of Biolase*

Even though Clark and Nugent had never talked substantively before the Meeting,[134] that did not stop them from immediately getting to work as directors to understand the business and affairs of Biolase. Late on February 28, they jointly requested certain information from the other directors, including the financial results for the fourth quarter and year-end of 2013.[135] Furry then circulated a draft of Biolase's 2013 Form 10-K filing to the board.[136]

Feinberg had limited conversations with Clark and Nugent after the Meeting. But, based on what the three of them did discuss, Feinberg understood that Clark and Nugent believed that "the situation was much worse than they thought," especially regarding potential guidance that Biolase would soon issue to investors about its expected growth for 2014.[137] There is no evidence suggesting that Feinberg directed or controlled Clark's or Nugent's actions or decisionmaking process after the Meeting.

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[132] Tr. 126, 166, 171 (Arrow).

[133] *Id.* 324 (Low); JX 136.

[134] JX 121.

[135] JX 139. Nugent would later forward this request, which he did not view as confidential information, to Oracle. JX 144; Tr. 213-15 (Nugent).

The day before the Meeting, Nugent signed a confidentiality agreement with Biolase not to disclose any material, non-public information. JX 130. Nugent conceded at trial that he likely provided confidential information to Oracle regarding certain board activities, but he believed that the unusual circumstances warranted doing so. Tr. 204-07 (Nugent). *Compare* JX 160, *with* JX 157; *see also* JX 171, 186.

At first, Feinberg testified that he did not believe that Clark or Nugent had ever provided material, non-public financial information about Biolase to Oracle. Tr. 45, 52 (Feinberg). He subsequently noted that he may have learned certain non-public, financial information during a phone call from Clark or Nugent in which they expressed their pessimism about Biolase meeting its numbers in the upcoming Form 10-K that was soon to be released. *Id.* 96-98.

After the purchases in February, Oracle did not trade in, and has no current plans to trade in, Biolase stock. *Id.* 42.

[136] JX 138; Tr. 286 (Pignatelli).

[137] Tr. 47-48 (Feinberg).

Over the weekend, Clark and Nugent "shared [their] observations" about Biolase. Both thought that the company was in "a very dangerous situation" with Pignatelli as chairman and CEO. Nugent described the feeling as "all red lights[,] . . . no yellow lights." They both agreed it was necessary and appropriate to seek to make a change in the CEO position—and sooner rather than later.[138]

L. *The Dispute Arises*

1. The March 3 Press Release

Biolase announced the purported changes to its board in a press release it issued on March 3. The press release stated, in part:

> [T]he Board of Directors (the "Board") has appointed Paul Clark and Jeffrey Nugent to the Board. Dr. Alexander K. Arrow and Dr. Sam Low tendered their resignations from the Board on February 28, 201[4]. As a result of these appointments and resignations, BIOLASE's Board currently consists of six directors, five of whom are independent directors.[139]

Pignatelli is quoted as being "thrilled" by these new appointments.[140] Furry, who helped draft the press release, believed it was accurate.[141]

2. Clark and Nugent Ask Pignatelli to Resign

That same day, Clark and Nugent called Pignatelli and tried to convince him, "as nicely as [they] could," that it was "an opportune time for him to step down."[142] Pignatelli was "furious" that he was asked to quit as CEO and chairman, and as a director.[143] He told Clark and Nugent that he would raise this issue with the board and then quickly hung up the phone. Pignatelli claims that when he reached other

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[138] *Id*. 193 (Nugent).
[139] JX 161.
[140] *Id.*
[141] Tr. 241 (Furry).
[142] *Id.* 193-94 (Nugent).
[143] *Id.* 286-87, 317 (Pignatelli).

directors that day—Moll, Nemoy, and Talevich—they were all "shocked" by what Clark and Nugent had requested.[144]

After speaking with Pignatelli, Nugent called Feinberg and relayed much of what had just happened.[145] Feinberg would subsequently talk to Pignatelli and express his own "shock[]" at the situation.[146] The evidence does not show that Feinberg directed Clark or Nugent to ask Pignatelli to resign.[147]

3. Pignatelli Solicits Arrow and Low to Rescind their Resignations

Pignatelli then spoke with Carroll and Furry, and they considered their options. One of the ideas they discussed was expanding the board from six members to eight members to try to prevent a majority of directors who might vote to remove Pignatelli as CEO. To that end, they considered whether Arrow and Low could be asked to rescind their resignations.[148] Pignatelli ultimately solicited Arrow and Low to do so.[149] Each of Arrow and Low purported to rescind his resignation on March 3.[150]

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[144] *Id.* 287-88 (Pignatelli).

[145] *Id*. 219 (Nugent).

[146] *Id.* 289 (Pignatelli).

[147] Although he had made his feelings about Biolase's management known generally, Feinberg never talked with Clark or Nugent about asking Pignatelli to resign from the board. He testified at trial that their doing so was a bad idea. His view was that Pignatelli, who had been an "ambassador" for the company for years, "should remain involved until the board could rule as to what his role should be going forward." *Id.* 49 (Feinberg).

Around this time, Feinberg and Moll exchanged several text messages about recent developments at Biolase. Feinberg suggested that he had asked for Clark and Nugent to remove Pignatelli as CEO, but at the same time he expressed his frustration about the way in which Clark and Nugent acted on March 3. JX 228. The Court cannot infer control or an agreement from these messages, particularly when other evidence strongly implies that Feinberg, Clark, and Nugent had each independently, and for different reasons, come to the same conclusion: Biolase management needed to change.

[148] *Id.* 256-57 (Furry).

[149] *Id.* 129 (Arrow), 260 (Furry), 317 (Pignatelli), 332 (Low).

Pignatelli wanted Arrow back on the board if he was willing to go along with a proposal for the board to form a special committee of all Biolase directors except Clark and Nugent. This special committee would have all the powers of the full board, including the ability to nominate a slate of directors for the company's upcoming stockholder meeting. *Id.* 129 (Arrow). Arrow agreed to go along with it. *Id.* 130-31 (Arrow).

[150] JX 162, 163. Despite doing so, Low understood was that it would take a board action for him to return to the board. Tr. 333 (Low).

4. The Board Asks for Information from Clark and Nugent

Several Biolase directors sought to learn the full extent of Clark's and Nugent's possible motivations for asking Pignatelli to resign. The board's nominating and corporate governance committee, chaired by Nemoy, requested information from them on March 5 about their possible relationships and communications with Oracle since the Meeting.[151] In response, Clark and Nugent each claimed to have no material relationship with Oracle or Feinberg.[152]

M. *The Events of March 6-7*

1. Biolase Files a Form 8-K Regarding the Meeting

Pignatelli instructed someone at Biolase to file a Form 8-K with the SEC on March 6.[153] The Form 8-K stated, in part:

> On February 28, 2014, the Board of Directors (the "Board") of Biolase, Inc. (the "Company") appointed Paul Clark and Jeffrey Nugent to the Board. . . . As a result of these appointments, BIOLASE's Board currently consists of eight directors, six of whom are independent directors.[154]

The Form 8-K made no mention of the resignations of Arrow or Low, but it did include the March 3 press release as an exhibit. Despite the obvious contradiction between the Form 8-K and the attached press release, Furry believed that the March 6 Form 8-K was accurate when it was filed.[155]

2. A Biolase Board Meeting with Eight Purported Directors

Pignatelli scheduled a telephonic board meeting for March 7 with eight director invitees—the Undisputed Directors, Clark, Nugent, Arrow, and Low.[156] Kane Kessler, Oracle's counsel, drafted or reviewed a letter

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[151] JX 169, 177.
[152] JX 182, 190.
[153] Tr. 260-61 (Furry).
[154] JX 145.
[155] Tr. 242 (Furry).
[156] JX 171.

that Clark and Nugent submitted to the board regarding the Form 8-K and the upcoming meeting.[157] Biolase points to the possible relationship between Kane Kessler and Clark and Nugent as proof of Oracle's influence over, and control of, these individuals. The evidence does not support Biolase's contention. Nugent testified that one of the key reasons why he contacted Kane Kessler was that he wanted prompt legal advice on certain issues, but he was not able to retain independent counsel until approximately March 11, when he, Clark, and several others retained Ropes & Gray LLP ("Ropes").[158]

It is likely that all eight individuals dialed in to this telephonic meeting.[159] When the meeting began, Pignatelli proposed a motion—likely one that would create a special committee comprised of everyone except Clark and Nugent and invested with all the powers of the board—but he was soon cut off by Talevich, who stated that another motion was pending. Nugent then moved to remove Pignatelli as chairman and CEO.[160] Nugent's motion was seconded, but Pignatelli quickly declared that the motion was out of order and thus would not be up for a vote. At that time, Biolase's counsel, Jones Day, suggested to continue the meeting until the following week.[161] It is likely that Clark and Nugent talked with Feinberg after this telephonic board meeting.[162]

3. Oracle Notifies Biolase of its Intent to Run a Proxy Contest

In light of the uncertainty (and possibly serious dispute) regarding the composition of Biolase's board, Oracle filed the materials necessary to nominate directors at the upcoming annual meeting with the SEC on March 7.[163] Feinberg felt that, with what had happened during the past week as only more evidence of the company's poor corporate governance and weak management, he "needed to take action and get serious

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[157] JX 179, 183; Tr. 55 (Feinberg).

Feinberg also likely reviewed this letter. *Id.* 56-57 (Feinberg). Nugent could not recall who drafted which parts of it. *Id.* 197-99 (Nugent).

[158] Tr. 225-26 (Nugent).

[159] *See, e.g.*, *id.* 131-32 (Arrow); Low Dep. 45.

[160] Tr. 131-32 (Arrow). The next day, Nugent circulated a draft of this motion. JX 195.

[161] Tr. 132 (Arrow). Arrow thought Nugent's motion would have passed. *Id.* 133.

The adjourned meeting was rescheduled for March 10, and then March 12, before it was ultimately cancelled. Pre-Trial Stip. § II, ¶¶ 10-11, 13.

[162] Tr. 223-24 (Nugent); JX 193. The substance of any phone call remains unclear.

[163] JX 184.

representation on the board of directors."[164] Oracle nominated four directors: Moll, Clark, Nugent, and Eric Varma, an Oracle analyst.[165]

Feinberg's testimony as a whole reveals that he is not interested in controlling Biolase; he wants independent directors to be in control. To that end, he acknowledged that he might not agree with the decisions made by independent directors. But, Feinberg understood it to be the role of the board, not Oracle as a stockholder, to direct the company's business affairs, which would include choosing management.[166]

N. *The Effect of this Dispute on Biolase's Business*

As the company's CFO, Furry believes that the dispute over the composition of the board has had a negative effect on Biolase. Specifically, he testified about its consequences on the company's ability to raise capital, employee morale, and line of credit with its primary lender.[167] Pignatelli echoed these comments, claiming that this litigation has had a "dramatic" effect on Biolase.[168]

II. CONTENTIONS

A. *Oracle's Claim Regarding the Composition of the Board*

Oracle contends that a preponderance of the evidence confirms that the parties intended for Arrow and Low to resign from the board, and for Clark and Nugent to be appointed to these vacancies, during the Meeting.[169] It argues that Biolase's bylaws, which include language similar to 8 *Del. C.* § 141(b), permitted Arrow and Low to resign verbally, which it claims they did.[170] Oracle submits that all of the

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[164] Tr. 49-50 (Feinberg).

[165] *Id.* 86 (Feinberg).

The notice of intent paperwork purportedly reflected that, unbeknownst to Feinberg, Clark had purchased Biolase stock sometime after Feinberg informed him in November 2013 that it was going to file a Schedule 13D. *Id*. 86-87 (Feinberg).

[166] *Id.* 45-46 (Feinberg).

[167] *Id.* 242-47 (Furry).

[168] *Id.* 290-92 (Pignatelli).

Separately, the Court notes that Arrow testified that Pignatelli had repeatedly tried to influence his testimony. The evidence ranged from an employment agreement offered as a "bribe," *id.* 135-37 (Arrow); JX 202, to a demand for Arrow's personal cell phone records, Tr. 141 (Arrow); JX 233, to even a threat "to crucify" Arrow over the situation, Tr. 142 (Arrow); JX 235.

[169] Pl.'s Pre-Trial Br. ("Oracle Br.") 38-39.

[170] *Id.* 35-38.

evidence, other than Pignatelli's testimony, establishes that these resignations occurred, and were thereby effective, before the appointments.[171] Alternatively, to the extent that one or both of the resignations may not have been effective before the appointments, Oracle argues that Clark and Nugent were duly appointed under 8 *Del. C.* § 223(d) as of the effective date of the resignations.[172]

Biolase rejects Oracle's presentation of the facts and interpretation of the relevant case law. Foremost, Biolase argues that only a written or electronic resignation by a director is permitted under the company's bylaws, if not also the relevant statute, 8 *Del. C.* § 141(b).[173] Were the Court to conclude that its bylaws permit verbal resignations, Biolase submits that the preponderance of the evidence demonstrates that neither Arrow nor Low resigned before or during the Meeting, meaning that there were no vacancies to which Clark and Nugent could have been appointed.[174] It further contends that the facts here are outside the scope of 8 *Del. C.* § 223(d) and that, in any event, the Court should deny Oracle the relief it seeks under the unclean hands doctrine.[175]

B. *Biolase's Counterclaims for Fraud and Negligent Misrepresentation*

Biolase contends that Oracle is liable for fraud, or at least negligent misrepresentation, for two alleged "deceptions": (i) concealing that it wanted board representation to oust Pignatelli as CEO; and (ii) failing to disclose its purported "agreements" with Clark and Nugent to fire Pignatelli once they became directors. It argues that Oracle's Schedule 13D in particular was false because it did not disclose Oracle's intent to change management or to start a proxy contest.[176]

In opposition, Oracle argues that Biolase has not carried its burden on either of the counterclaims for several reasons. First, Oracle contends that it was not, despite Biolase's suggestions otherwise, seeking to obtain control over the company.[177] Second, it argues that the evidence does not show that it had any arrangement or understanding, especially regarding Pignatelli's position as CEO, with either Clark or Nugent before or after

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[171] *Id.* 38-39.
[172] *Id.* 41-43.
[173] Biolase, Inc.'s Pretrial Br. ("Biolase Br.") 30-33.
[174] *Id.* 33-36.
[175] *Id.* 37-43.
[176] *Id.* 44-51.
[177] Oracle Br. 45-48.