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IN THE SUPREME COURT OF THE STATE OF DELAWARE

LAZARD TECHNOLOGY PARTNERS LLC, a representative of the former equityholders of Cyveillance, Inc.,

Plaintiffs Below-Appellants,

v.

QINETIQ NORTH AMERICA OPERATIONS LLC,

Defendant Below-Appellee.

No. 464, 2014

COURT BELOW:

COURT OF CHANCERY OF THE STATE OF DELAWARE, C.A. NO. 6815-VCL

CORRECTED ANSWERING BRIEF OF DEFENDANT BELOW-APPELLEE

OF COUNSEL:

Allen M. Gardner
Jessica E. Phillips
LATHAM & WATKINS LLP
555 Eleventh Street, NW
Suite 1000
Washington, DC 20004
(202) 637-1200

Srinivas M. Raju (#3313)
Robert L. Burns (#5314)
RICHARDS, LAYTON & FINGER, P.A.
One Rodney Square
920 North King Street
Wilmington, Delaware 19801
(302) 651-7700

Attorneys for Defendant Below-Appellee QinetiQ North America Operations LLC

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NATURE OF THE PROCEEDINGS

This appeal arises from the Court of Chancery's decision, after four days of trial, that Plaintiff Lazard Technology Partners ("Lazard") had failed to prove either its breach of contract claim or its breach of the implied covenant of good faith and fair dealing claim against Defendant QinetiQ North America ("QNA"). Lazard had alleged that, after QNA's acquisition of Cyveillance, Inc. under a July 2009 Merger Agreement, QNA had purposely mismanaged the surviving corporation with the intent of preventing Cyveillance's stockholders from realizing a contingent earn-out payment that would have been payable had certain enumerated revenue goals been met. The Court of Chancery held that "the evidence does not support a finding that QNA representatives acted with the necessary degree of intent to reduce or limit the earnout payment ...." Ex. A to Br. at 63:12-15. The Court also held that the implied covenant only operates to fill unanticipated gaps and that the evidence demonstrated that the parties had negotiated extensively over the post-closing obligations.

The Court first held that QNA did not breach the Merger Agreement. Section 5.4 of the Merger Agreement prohibited QNA from taking "any action to divert or defer contracts or business opportunities that would result in Company Revenue with the intent of reducing or limiting the Earn-out Payment." A0801. The Court held that "[g]iven the language of 5.4, to succeed on its contract claim[,]

Lazard had to prove at trial that QNA had the intent to reduce or limit the earnout payment. Absent this bad intent, actions that diverted or deferred opportunities would not violate Section 5.4." Ex. A to Br. at 71:1-6. In interpreting the intent provision of Section 5.4, the Court specifically noted that Lazard's shareholder representative, "Mr. [Kevin] Burns of Lazard agreed with this interpretation." *Id.* at 71:6-8. The Court then applied that standard to the facts and found that extensive evidence established that rather than trying to limit the Earn-out, QNA took steps to expand Cyveillance's sales and develop new products and services. In summary, the Court held that "having heard the witnesses testify and reviewed what is an extensive factual record, I cannot conclude that QNA acted with an intent to reduce or limit the earnout payments." *Id.* at 77:12-15.

After determining that Lazard had failed to prove its breach of contract claim, the Court of Chancery held that the implied covenant of good faith and fair dealing was inapplicable to the case given the extensive negotiation history over QNA's post-closing obligations. The Court held in the alternative that if it were to imply a provision at all it would parallel the intent language from Section 5.4 because that was the only standard to which the parties would have agreed.

The Court of Chancery's decision is well-reasoned, fully supported by the evidence adduced at trial, and follows well-settled Delaware law. It should be affirmed.

SUMMARY OF ARGUMENT

I. Denied. The Court of Chancery properly and correctly interpreted and applied Section 5.4 of the Merger Agreement to require Lazard to prove that QNA took actions to divert or defer Company Revenue with the intent of reducing any Earn-out payment.

II. Denied. The Court of Chancery correctly determined, based on all of the evidence produced at trial, that the implied covenant of good faith and fair dealing did not apply in this case in accord with well-settled Delaware law.

COUNTER-STATEMENT OF FACTS

A. The Parties

1. Qinetiq North America, Inc. And Its UK Parent Qinetiq, Ltd.

QinetiQ North America, Inc. ("QNA") "is a defense and security technology company that provides technology-based products and services to government and commercial customers."[1] Ex. A to Br. at 64:4-7. During the relevant time period, QNA was a wholly-owned subsidiary of QinetiQ, Ltd. ("QUK"), a United Kingdom technology, security, and aerospace company. *Id.* 64:9-11. Due to national security restrictions, QUK, QNA, and the U.S. Department of Defense entered into a Proxy Agreement to insulate QNA's business from interference from QUK. The Proxy Agreement establishes a proxy board comprised of U.S. citizens who must pre-approve every communication made between QUK and QNA. *See* B0001-31. As the Court of Chancery found, "[b]ecause the U.S. government has restrictions on contracting with foreign firms or foreign-owned firms, there are restrictions on the ability of QNA to interact with its own UK parent." Ex. A to Br. at 64:13-16. As such, QNA operated autonomously, and QNA and QUK had

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[1] Duane Andrews was the Chief Executive Officer of QNA during the relevant time period. B1006 at 708:20-24. Dr. Steve Cambone joined QNA in 2007 and became President of MSG in 2009. B1089-92 at 791:1-792:11. MSG had $487 million in revenue and 3,000 employees in 2009. *Id.*; B0061.

an arms-length relationship, as opposed to a typical parent-subsidiary relationship. B0515 at 217:11-24; B0534 at 236:12-17.

2. Cyveillance, Inc. And Its Shareholder Representative Lazard Technology Partners LLC

Cyveillance was a venture capital-backed cyber technology company that provided Software as a Service ("SaaS") tools to monitor the internet for threats. B0312 at 14:12-18. Cyveillance focused its business on the commercial market. Its key customers were in the financial, insurance, and pharmaceutical industries. B0615 at 317:3-14.

Plaintiff Lazard Technology Partners LLC ("Lazard") was a preferred stockholder in Cyveillance. At the time of the acquisition, Lazard and the other investors in Cyveillance had together invested almost $80 million in Cyveillance. B0430 at 132:12-15. Lazard's investment represented approximately 25 percent of that total. B0308 at 10:14-17; *see also* B0307-08 at 9:22-10:13. Kevin Burns was one of two founders and managing principals of Lazard during the relevant time period. B0305-06 at 7:10-8:12. Mr. Burns served as Lazard's board designee at Cyveillance from May 1998 until the sale in mid-2009. B0308 at 10:18-23.

From its inception, Cyveillance never made a profit. B0328 at 30:6-8; *see also* B0819 at 521:15-19 ("Cyveillance was losing [money] since the day it [was] created."). In March 2009, as merger agreement negotiations with QNA were proceeding, Cyveillance's auditors noted that Cyveillance had an accumulated

deficit of almost $77 million, and that these factors raised "substantial doubts about the [C]ompany's ability to continue as a going concern." B0427 at 129:2-9; B0042.

B. Merger Negotiations

In early 2008, a mutual friend of Cyveillance CEO Mr. Panaghiotis Anastassiadis and Mr. Andrews put them in touch. B0617 at 319:17-23. QNA was interested in acquiring Cyveillance with the hope of providing Cyveillance's services to the federal government. B1018-19 at 720:21-721:15.

C. The Parties' Fully Integrated Merger Agreement

QNA ultimately acquired Cyveillance in May 2009, under a Merger Agreement governed by Delaware law which became effective July 1, 2009.[2] *See generally* A0753. QNA agreed to pay the stockholders of Cyveillance an up-front cash payment of $40 million, as well as an Earn-out Payment of up to an additional $40 million if certain "Company Revenue" targets were realized during the two-year Earn-out Period covering the calendar years 2009 and 2010. A0771-72 § 1.11; A0817.

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[2] Section 13.8 of the Merger Agreement states that "This Agreement (together with the disclosure schedules to this Agreement) constitute the entire agreement among the parties and supersede any other agreements, whether written or oral, that may have been made or entered into by or among any of the parties hereto or any of their respective Affiliates relating to the transactions contemplated hereby." A0829 § 13.8.

1. Company Revenue

The Merger Agreement defines "Company Revenue" as "worldwide revenue of the Company ... during the Earn-out Period arising out of the licenses or services, ... related directly to and data derived from the use of [Cyveillance's] core technology ...." A0816.[3]

2. The Earn-Out Period And Earn-Out Payment

Although the Merger Agreement did not close until July 2009, the Earn-out Period was defined as "the period commencing on January 1, 2009 and ending on December 31, 2010." A0817. Under the Merger Agreement, if Company Revenue from the sale of Cyveillance products reached at least $30 million during the Earn-out Period, Cyveillance's stockholders would receive an Earn-out Payment pursuant to the formula set forth in Sections 1.11(c) and (d) of the Merger Agreement. *See* A0772 § 1.11(c), (d). If Company Revenue did not reach the $30 million threshold, the Merger Agreement provided for no Earn-out Payment. *See id.* § 1.11(e).

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[3] If Cyveillance earned "revenue ... for the combined organization postmerger that [was] derived solely because" QNA had acquired Cyveillance and was attributed to Cyveillance's technology, then "we wanted to ensure that ... was counted." B1009 at 711:12-16. However, if revenue was "incidental to [Cyveillance's] being part of the organization," such as one of Cyveillance's customers that QNA was able to sell non-cyber products or services to, then QNA did not want to "pay for [that] as ... part of the merger" and as such it would not count toward Company Revenue. *Id.* at 711:16-21.

3. Management Of The Surviving Corporation

Section 5.4 of the Merger Agreement exclusively governs QNA's conduct with respect to managing Cyveillance post-merger. *See* B0806 at 508:9-18 (Mr. Anastassiadis conceding that "do not defer or divert business contracts with the intent of preventing the earn-out … was the only restriction on how [QNA] agreed to operate Cyveillance after the merger."). Under Section 5.4, during the Earn-out Period, QNA "shall not … take any action to divert or defer contracts or business opportunities that would result in Company Revenue with the intent of reducing or limiting the Earn-out Payment." A0801 § 5.4.

Notably, Section 5.4 contains only negative covenants. During the merger negotiations, Lazard proposed numerous broad affirmative covenants that would have required QNA to: (1) operate Cyveillance in a manner reasonably consistent with past practices; (2) operate Cyveillance in good faith to maintain existing or greater levels of business, to preserve relationships of customers and employees; (3) cause Cyveillance to have adequate amounts of capital required to achieve the Earn-out Payment; (4) make reasonable efforts to recruit and employ sufficient employees to achieve the Earn-out Payment; and (5) market and bid for new contracts consistent with past practices. B0379-80 at 81:12-82:16; B0813-14 at 515:5-516:4; B0382 at 84:3-24. As Mr. Anastassiadis and Mr. Burns both conceded, QNA flatly rejected each of these affirmative covenants. A0074 § 5.6;

A0178-79 § 5.5; B0802-06 at 504:8-508:8; B0379-80 at 81:3-82:16; B0382-83 at 84:3-85:15.

D. QNA's Efforts To Sell Cyveillance Products And Services During The Earn-Out Period

Upon closing of the merger, Cyveillance was integrated into Mission Solutions Group ("MSG") run by Dr. Steve Cambone. B1090 at 792:6-11. As the Court of Chancery found, QNA made substantial and numerous efforts to sell Cyveillance products and services to new and existing federal government customers throughout the Earn-out Period. *See* Ex. A to Br. at 71:11-16 ("There is extensive contemporaneous evidence establishing that rather than trying to limit the earnout, QNA in fact took steps to expand Cyveillance's sales and develop new products and services.").

Such contemporaneous evidence includes the following examples reflecting QNA management and employees' efforts to generate contracts and business opportunities for Cyveillance:

- Within days of the Cyveillance acquisition, QNA held meetings with potential customers to market Cyveillance and coordinated a U.S. visit by QUK executives to understand Cyveillance's capabilities to market it to UK customers. B0881-82 at 583:19-584:9; B0056; B0875-79 at 577:22-581:11; B0055.
- Dr. Cambone reached out to personal contacts at the Office of the Director of National Intelligence ("ODNI") and the CIA to try to sell Cyveillance products, within two weeks of the Cyveillance acquisition. Dr. Cambone directed all of his managers to seek task orders that could be used on existing government contracts to sell Cyveillance products. *See* B0920 at 622:12-16; B0195-97; B0885-86 at 587:6-588:14; B0113. QNA was

ultimately successful in winning the ODNI pilot for Cyveillance in March 2010. B0211.

- QNA marketed Cyveillance's anti-fraud services to the DoD in the wake of the Fort Hood tragedy in the fall of 2009. B0907-08 at 609:3-610:21; B0166-68.
- QNA marketed Cyveillance to multiple elements of the U.S. Air Force in 2009 and early 2010, using both its own employees and hired consultants. B0914-15 at 616:18-617:20; B0174-76; B0919-20 at 621:22-622:11; B0187-94; B0203.
- QNA sponsored a Cyber Safety 101 offering of Cyveillance's goods and services to the federal government and school districts, as well as QNA's commercial customers, during the Earn-out Period. B0399-400 at 101:17-102:3; B0892-93 at 594:11-595:17; B0130, B0153-57; B0177-78.
- QNA made efforts to generate contracts and business opportunities for Cyveillance goods and services with QinetiQ Australia clients during the Earn-out Period. B0396 at 98:4-15; B0198-202; B0245-57.
- QNA went "all over the government" pitching Cyveillance during the Earn-out Period, including several approaches to national security agencies, as well as to the U.S. Air Force and the National Guard. B1034-35 at 736:15-737:9; *see also* A0902; B0225.
- Dr. Cambone had multiple direct conversations with the commander of the 24th Air Force—the element responsible for all Air Force cyberspace combat and support forces—in which he attempted to sell Cyveillance to the Air Force. B1101-03 at 803:18-805:11. He also hosted multiple 24th Air Force generals at QNA headquarters in a further attempt to market Cyveillance. *Id.*
- Dr. Cambone personally approached the Deputy Director of National Intelligence for Collection, a former Deputy Director of National Intelligence for Collection, a former Principal Deputy Director of National Intelligence and Director of the National Reconnaissance Office, and the Director of the National Counterterrorism Center in an effort to market Cyveillance to the U.S. intelligence community. B1105-09 at 805:14-811:9; B0204; B1112 at 814:4-22; B0195-97; B1116-17 at 818:12-819:1; B0206; B0208-10.
- In June 2009—prior to the close of the acquisition—Dr. Cambone "had the entire senior staff of MSG around the table on Prosperity Avenue in the

MSG headquarters, and asked them to be certain to begin to include the Cyveillance offerings in their interactions with their customers." B1135-36 at 837:22-838:12. QNA went on to provide training sessions to this senior staff to ensure that they understood Cyveillance's capabilities. *Id.*

- In the spring of 2010, Dave Papas, director of cyber-security strategy for QNA, reached out to his contacts at the Food and Drug Administration ("FDA") to market Cyveillance as a solution to FDA concerns about pharmaceuticals being sold over the Internet. B1172-73 at 874:11-875:1; B0214-15.
- In the summer of 2010, QNA successfully marketed Cyveillance data feeds as an element of the Cadenza solution to the Air National Guard. B0232-37.
- In the summer of 2010, QNA engaged in efforts on the DIA Cyber Defense special vulnerability assessment project as well as marketed similar Cyveillance capabilities to the U.S. Strategic Command ("STRATCOM") in response to STRATCOM's need to conduct analysis of foreign media. B0238.
- In the summer of 2010, several QNA employees, along with a Cyveillance employee, attended meetings with U.S. Army personnel in Fort Huachuca, Arizona, and Fort Monmouth, New Jersey to market Cyveillance and the Knowledge Discovery Appliance ("KDA") to entities at these facilities. B1173-75 at 875:14-877:7.
- In the summer of 2010, QNA employees presented Cyveillance capabilities to the Federal Emergency Management Agency ("FEMA") and the Department of Homeland Security ("DHS") as a means to address FEMA and DHS's open source intelligence collection and social media communication requirements. B1182-83 at 884:4-885:19; B0239-41.
- In the summer of 2010, QNA employees met multiple times with the director of the U.S. Navy's open source intelligence and analysis program office to propose Cyveillance capabilities as a solution to the Navy's open source intelligence requirements. B1183-85 at 885:20-887:11.
- QNA marketed Cyveillance to DARPA during the Earn-out Period by responding to several requests for information ("RFIs"), a process by which DARPA solicits new technology which may be of use to the DoD. B1189 at 891:7-19. In the spring of 2010, QNA partnered Cyveillance with teams from Invincea, a cyber-security software company headed by a former DARPA program manager, and George Mason University, to successfully market Cyveillance as a solution to DARPA's "Cyber Genome" RFI.

B1189-92 at 891:20-894:7; B0216-24. In the fall of 2010, QNA also drafted and submitted a white paper to DARPA marketing Cyveillance as a solution to DARPA's "CINDER" RFI. B1192-93 at 894:12-895:21; B0248-49.

- QNA, with assistance from Cyveillance employees, used an existing QNA contractual relationship with the U.S. Secret Service to market Cyveillance to the Secret Service. In September 2010, these efforts resulted in the Secret Service signing a three-year, multimillion dollar agreement for Cyveillance goods and services that was effected through a QNA contract vehicle. B1193-96 at 895:22-898:24.
- In September 2010, QNA submitted a bid to the NYPD in response to an RFI. B0239-44.
- QNA employees met with operations staff of the U.S. Cyber Command during the Earn-out Period to market Cyveillance and KDA to U.S. Cyber Command. B1188-89 at 890:5-891:1.
- QNA also sought to team Cyveillance with other industry service providers to create "high revenue-generating partnership[s]" for Cyveillance during the Earn-out Period. *See* B1201-02 at 903:19-904:7.

E. Cyveillance's Performance During The Earn-Out Period

Despite all of QNA's efforts, revenue from Cyveillance products and services fell short of the $30 million Earn-out threshold. As the Court of Chancery concluded, a variety of product and market factors led to the disappointing results. First, "[b]ecause the U.S. government has restrictions on contracting with foreign firms or foreign-owned firms, there are restrictions on the ability of QNA to interact with its own UK parent. Those restrictions contributed in a material way to some of the problems that led to the failure to achieve the earnout." Ex. A to Br. at 64:13-18. The "second major factor that affected the ability of Cyveillance to meet its earnout" was that "because of delays in closing the merger agreement the

[earnout] period ultimately only covered 18 months." *Id.* at 67:10-15. The Court noted that this was "particularly problematic when ... dealing with government contracts, because the government contracting timeline turned out to be much longer than the parties anticipated, and the ability of the parties to interest the government in quick-hitting transactions that would be achieved during the 18-month period proved to be virtually nonexistent." *Id.* at 67:16-23. Third, the Court found that "the federal government had budgetary problems and restrictions during the earnout period that, if nothing else, affected people's willingness to engage in purchases." *Id.* at 67:24-68:4. Finally, Cyveillance itself only made approximately $27 million of commercial revenue—$7 million short of what it initially represented to QNA that it could achieve on its own, and $3 million short of its final projection during the merger negotiations. B0032; B0423 at 125:14-20.

F. Cyveillance's Post-Earn-Out Performance

After the Earn-out Period ended, Cyveillance continued to struggle to sell its products to the federal government and still never made a profit. B0415 at 117:10-12. Cyveillance's revenue for Fiscal Year 2012, the twelve-month period ending March 31, 2012, was somewhere in the range of $15 to $17 million. B0743 at 445:20-22.

G. Procedural History

On August 29, 2011, Lazard filed a two-count complaint, alleging breaches of Sections 5.3 and 5.4 of the Merger Agreement and the implied covenant of good faith and fair dealing. *See* B0296-97. A four-day trial commenced in the Court of Chancery on March 3, 2014, during which ten witnesses testified in person and an additional fourteen witnesses testified via deposition testimony and expert reports. *See* A1574-76.

After post-trial briefing and oral argument, the Court of Chancery ruled in favor of QNA on both counts.[4] Ex. A to Br. at 62:4-81:1. With regard to the breach of Section 5.4, the Court held that "[g]iven the language of 5.4, to succeed on its contract claim[,] Lazard had to prove at trial that QNA had the intent to reduce or limit the earnout payment. ***Absent this bad intent, actions that diverted or deferred opportunities would not violate Section 5.4.***" *Id.* at 71:1-6.[5] The Court then noted that "[i]n an example of the candor that all witnesses showed during trial, ***Mr. Burns of Lazard agreed with this interpretation.***" *Id.* at 71:6-8. The Court held that "[t]here is extensive contemporaneous evidence establishing

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[4] Lazard has not appealed the Court's decision granting QNA judgment on Lazard's breach of Section 5.3 claim.

[5] All emphases added, unless otherwise specified.

that rather than trying to limit the earnout, QNA in fact took steps to expand Cyveillance's sales and develop new products and services." *Id.* at 71:11-15.

The Court then turned to the evidence from which Lazard argued an inference of intent to limit the Earn-out could be drawn "notwithstanding that extensive evidence of efforts to increase sales and support sales." *Id.* at 71:17-20. The Court discussed an opportunity to sell Cyveillance products and offerings to the GCHQ, a British intelligence agency. *Id.* at 71:24-76:10. The Court found that QNA delayed the opportunity, but found that they were not stalling to defeat the Earn-out, but rather because of concern about "its ability to sell to the U.S. intelligence community." *Id.* The Court also discussed the execution of a reseller agreement with QUK. *Id.* at 76:11-77:11. The Court noted that the execution of the reseller agreement took "[a] bizarrely long time" but then found "this was the function of a high bureaucratic internal approval structure that was driven largely because of the government restrictions involving the proxy agreement between QNA and QUK and concern about what, if anything, QNA could do in terms of the reseller agreement." *Id.* In summary the Court held that "having heard the witnesses testify and reviewed what is an extensive factual record, I cannot conclude that QNA acted with an intent to reduce or limit the earnout payments." *Id.* at 77:12-15.

With regard to the implied covenant of good faith and fair dealing, the Court of Chancery held that "having reviewed both the agreement in question as well as the evidence that's been provided about the negotiating history, I do not believe that this is a gap that should be filled with specificities that would cover the types of actions that QNA supposedly failed to take in this case." *Id.* at 78:16-21. Cyveillance had attempted to negotiate for a range of additional affirmative post-closing obligations but QNA rejected all of them. Thus, the Court held the implied covenant did not apply in this case given the facts found at trial. The Court went on to say that even "if I were to imply any provision at all, it would parallel the language of Section 5.4" because "the evidence from the specific provision upon which the parties agreed—namely, an intent based standard—leads [the Court] to conclude that the only substitute provision upon which the parties would have agreed to would have again been an intent-based standard." *Id.* at 79:12-19.

Following the post-trial bench ruling, the Court of Chancery issued a Final Order and Judgment in favor of QNA on all counts of the verified complaint, and ordered Lazard to pay QNA costs pursuant to Court of Chancery Rule 54. Ex. B to Br.

Lazard filed a timely notice of appeal of the final order and judgment to this Court on August 27, 2014, and filed its opening brief on appeal on October 27, 2014. *See* A00A1. This is QNA's Answering Brief on Appeal.

ARGUMENT

I. THE COURT OF CHANCERY PROPERLY INTERPRETED SECTION 5.4 TO REQUIRE LAZARD TO PROVE THAT QNA ACTED WITH THE INTENT TO REDUCE OR LIMIT THE EARN-OUT PAYMENT

A. Question Presented

Whether the Court of Chancery correctly interpreted and applied Section 5.4 of the Merger Agreement to require Lazard to prove that QNA took actions to divert or defer contracts or business opportunities that would result in Company Revenue with the intent of reducing or limiting the Earn-out payment.

B. Standard And Scope Of Review

This Court reviews the Court of Chancery's interpretation of written agreements de novo. *Gotham P'rs v. Hallwood Realty P'rs*, 817 A.2d 160, 170 (Del. 2002). After a trial on the merits, this Court "accords considerable deference to the trial judge's factual findings unless they are clearly erroneous." *Hudak v. Procek*, 806 A.2d 140, 144 (Del. 2002).

C. Merits Of Argument

Section 5.4 provides that QNA "shall not ... take any action to divert or defer contracts or business opportunities that would result in Company Revenue with ***the intent*** *of reducing or limiting the Earn-out Payment.*" A0801. Lazard contends that the Court below erred in interpreting this provision because all

Section 5.4 required it to prove at trial was that QNA "took deliberate action" "knowing that it would negatively impact the Earn-out." Br. at 15.

Lazard's post-trial interpretation of Section 5.4 is unequivocally wrong. First, Lazard's interpretation of Section 5.4's intent standard is flatly contradicted by the admission of Lazard's *own* founder and Cyveillance board member, Mr. Kevin Burns. Second, Lazard's argument is entirely untethered to the plain language of Section 5.4, and flies in the face of standard canons of contract interpretation. Third, Lazard's reliance on the common law from intentional tort cases is entirely misplaced because the parties contracted for the specific intent provision in Section 5.4. Fourth, the Chancery Court properly found that neither QNA's opposition to the GCHQ "opportunity" nor the length of time it took to enter into the Reseller Agreement with QUK had anything to do with the Earn-out. Finally, the Court of Chancery's decision should be affirmed for the separate reason that Lazard utterly failed to prove that either the GCHQ "opportunity" or the Reseller Agreement "would have resulted in Company Revenue."

1. Lazard's Argument Is Flatly Contradicted By The Evidence Adduced At Trial, Including Its Own Shareholder Representative's Testimony

The Court of Chancery properly held that given the language of Section 5.4, to succeed on its breach of contract claim, "Lazard had to prove at trial that QNA had the intent to reduce or limit the earnout payment. Absent this bad intent,

actions that diverted or deferred opportunities would not violate Section 5.4." Ex. A to Br. at 71:1-6. In support of this interpretation of Section 5.4, the Court of Chancery specifically noted that "[i]n an example of the candor that all witnesses showed during trial, ***Mr. Burns of Lazard agreed with this interpretation***." *Id.* at 71:6-8. Mr. Kevin Burns, Lazard's founder and chief negotiator of the Merger Agreement, unequivocally testified that "under the final agreement, QinetiQ North America could divert or defer business opportunities ***as long as it wasn't with the intent of preventing the earnout***." B0379 at 81:1-15.

Tellingly, Lazard ignores entirely Mr. Burns' testimony as well as the Court of Chancery's reliance on that testimony in determining the meaning of Section 5.4. Moreover, Lazard cites absolutely nothing from any witness in support of its argument that the intent of the parties in entering into Section 5.4 was to prevent QNA from taking any deliberate actions that had a foreseeable impact on the Earn-out. For good reason. That was not the intent of the parties, as Mr. Burns conceded and as the Court of Chancery found, following an orderly and deductive process.

Further, Lazard also conveniently ignores the evidence adduced at trial regarding the negotiation history of Section 5.4. As explained above, Lazard proposed numerous broad affirmative covenants that would have required QNA to take a number of affirmative actions related to Cyveillance during the Earn-out

Period. B0379-80 at 81:12-82:16; B0813-14 at 515:5-516:4; B0382 at 84:3-24. Yet QNA rejected each of these affirmative covenants. A0074 § 5.6; A0130 § 5.5; B0802-06 at 504:8-508:8; B0379-80 at 81:3-82:16; B0382-83 84:3-85:15. Lazard's post-trial interpretation of Section 5.4's intent standard would have imposed upon QNA far more of a burden than the affirmative covenants that it explicitly rejected. Under Lazard's theory, any action that QNA took that could have impacted the time frame of a sale and thus the Earn-out would be a breach of Section 5.4 regardless of QNA's reason for taking the action. That is simply not what the parties agreed to.

2. Lazard's Proposed Interpretation Of Section 5.4 Contradicts The Plain Language Of That Provision And Flies In The Face Of Standard Canons Of Contract Interpretation

Lazard contends that the Court of Chancery erred when it required Lazard to prove that QNA acted with the "the sole, specific, and express intent to reduce or limit the Earn-out Payment." Br. at 15. Lazard contends that Section 5.4 required no such thing. But Lazard's argument is contradicted by the plain language of Section 5.4, which requires Lazard to prove that QNA acted with the specific intent to reduce or limit the Earn-out Payment. Moreover, Lazard's interpretation ignores several standard canons of contract interpretation.

Under the plain language of Section 5.4, QNA agreed not to divert or defer contracts or business opportunities that would result in Company Revenue "with

the intent of reducing or limiting the Earn-out Payment." A0801 § 5.4. The parties chose to use the definite article "the" to provide distinct limits to the noun—intent—that precedes the definite article. *See ION Geophysical Corp. v. Fletcher Int'l, Ltd.*, 2010 WL 4378400, at *7 (Del. Ch. Nov. 5, 2010) ("The definite article 'the' is generally used 'as a function word to indicate that a following noun or noun equivalent is definite ....'" By contrast, "[t]he word 'a' is an indefinite article used as a function word before singular nouns when the referent is unspecified." (citations omitted)); *see also Stephan v. Pa. Gen. Ins. Co.*, 621 A.2d 258, 261 (Conn. 1993) (same); *Allstate Ins. Co. v. Foster*, 693 F. Supp. 886, 889 (D. Nev. 1988) (same). Lazard contends that the Court of Chancery "introduced a new term into the contract that the parties themselves did not employ," Br. at 15-16, but it is Lazard's new interpretation of Section 5.4 that would re-write the parties' bargain. Lazard would have the Court ignore the definite article "the" that modifies "intent" in contravention of the plain language of the Merger Agreement. But in Delaware, "courts will not rewrite contractual language ... just because one party failed to extract as complete a range of protections as it, after the fact, claims to have desired during the negotiation process." *Allied Capital Corp. v. GC-Sun Hldgs., L.P.*, 910 A.2d 1020, 1033 (Del. Ch. 2006). As the Court of Chancery correctly found, absent proof of this

specifically identified intent, QNA's actions to divert of defer contracts or business opportunities do not run afoul of Section 5.4.

Lazard also contends that all Section 5.4 required it to prove was that QNA "took deliberate action" "knowing that it would negatively impact the Earn-out." Br. at 15. But this interpretation would have this Court remove the phrase "the intent" and replace it with "knowing." The parties did not agree to a knowing standard; they agreed to a specific intent standard, as Mr. Burns conceded.

3. Lazard's Reliance On The Common Law Meaning Of Intent Is Misplaced

In search of a theory for appeal, Lazard relies on the common law meaning of intent. But Lazard's citations to the common law are irrelevant. It is well-settled that parties to a contract may contract around the common law. *See, e.g., Interim Healthcare, Inc. v. Spherion Corp.*, 884 A.2d 513, 552 (Del. Super. Ct. 2005) (express language of highly negotiated contract overrides common law platitudes). That is precisely what the parties did here, as Mr. Burns himself testified.

Moreover, the one contract case cited by Lazard is entirely inapposite.[6] In *Hexion Specialty Chems., Inc. v. Huntsman Corp.*, 965 A.2d 715 (Del. Ch. 2008),

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[6] Lazard cites a number of intentional tort cases (Br. at 17 n.21) that are inapplicable here, where Lazard's own witness testified plainly about the meaning of Section 5.4 and the Court of Chancery relied upon that evidence to interpret the parties' agreement.

Hexion entered into a merger agreement to buy the defendant seller corporation, Huntsman. No longer wishing to go through with the deal due to a change in Huntsman's financial situation, Hexion sought (without consulting Huntsman) a valuation opinion that the combined entity would be insolvent. Hexion argued that such an insolvency opinion allowed it to terminate the merger under the agreement's no "financing out" provision, which provided that if the buyer's financing was not available at closing, then the buyer was excused from performing under the agreement. *Id.* at 721. The financing commitment letter required as a condition precedent to the banks' obligation to fund the transaction that the banks receive a solvency certificate or opinion indicating that the combined entity would be solvent. *Id.* at 724. As they had received an insolvency letter, no bank would provide financing. *Id.* at 730.

Hexion argued that it did not knowingly and intentionally breach the agreement because the failure to consummate the merger was caused by the banks' refusal to finance the deal—not Hexion's actions. The Court rejected that argument and found that Hexion followed a "carefully designed plan to obtain an insolvency opinion" knowing that it would make closing impossible. *Id.* at 725–26. For that reason, their "'knowing and intentional'" breach was "a breach that [was] a direct consequence of a deliberate act." *Id.* at 748. Lazard argues that "[i]f a 'knowing and intentional' breach requires only a deliberate act with a direct

consequence, simple common law 'intent' cannot require more." Br. at 17. But unlike the "knowing and intentional" breach provision in *Hexion*, Section 5.4 specifies the precise intent that QNA was prohibited from acting with.

4. The Court Of Chancery Properly Found That QNA's Actions Related To The Replication Of Cyveillance In The United Kingdom And The Reseller Agreement Had Nothing To Do With The Earn-Out

Lazard contends that it proved at trial that QNA took deliberate action to stall two revenue opportunities. The first opportunity Lazard points to was an alleged opportunity to sell its products and services to GCHQ. But GCHQ made absolutely clear in July 2010—less than five months before the end of the Earn-out Period—that it "***d[id] not wish to buy*** [Cyveillance's] service provided from a US-based SOC [Security Operation Center], and insist[ed] that service & account management is UK based." B0227-28. In other words, a full replication of Cyveillance in the UK was the only potential option for selling to GCHQ and QNA opposed that option.[7] As the Court of Chancery found, QNA did not want to create a full replication of Cyveillance in the UK because it was concerned about

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[7] In addition, QNA had a number of other sound business justifications for opposing the replication of Cyveillance in the UK: 1) Cyveillance itself had estimated the cost of doing so at $10 million plus the costs of diverting people and resources; 2) GCHQ never offered any amount of money to Cyveillance either for its services or to establish a replication of Cyveillance in the UK; and 3) QNA had practical concerns about whether the technology was even capable of being replicated in the UK. B0231; B0997 at 699:10-14; B0998 at 700:18-701:1; B1213-14 at 915:1-916:23.

jeopardizing "its ability to sell to the U.S. intelligence community." Ex. A to Br. at 75:13-16. Dr. Cambone testified that he was concerned that providing Cyveillance to a UK government customer could impact QNA's relationship with the U.S. intelligence community, and stated that establishing a full-blown Cyveillance capability in the UK was a "terrible idea" because he thought it would "do considerable harm to our USG prospects." B1147-50 at 849:22-852:4; B0212; B0251. The Court found Dr. Cambone's testimony that "he was concerned about the effect on QNA's relationship with the U.S. intelligence community" to be credible and a "sincerely held" belief. Ex. A to Br. at 75:11-76:3. Moreover, both Rick Rose, Cyveillance's former CFO, and Mr. Anastassiadis conceded at trial that QNA's decision not to replicate Cyveillance in the UK "***had nothing to do with the [E]arnout.***" B0503 at 205:2-6; B0689 at 391:1-12; B0863-64 at 565:17-567:7; B0253-54. The Court of Chancery followed an orderly process by properly applying the intent standard from Section 5.4 to hold that QNA did not oppose replication of Cyveillance in the UK "to defeat the earnout." Ex. A to Br. at 74:7-8.

The second alleged "opportunity" was the International Reseller Agreement between QNA and QUK to sell Cyveillance products and services in the United Kingdom. The Court of Chancery noted that the execution of the reseller agreement took "[a] bizarrely long time" but found after "wad[ing] through the

series of e-mails and fits and starts with which this reseller agreement was negotiated and reviewed and reviewed," that "this was the function of a high bureaucratic internal approval structure that was driven largely because of the government restrictions involving the proxy agreement between QNA and QUK and concern about what, if anything, QNA could do in terms of the reseller agreement." *Id.* at 76:11-77:4. Indeed, Lazard's own witness conceded that QNA "hustled" and "bird-dogged" QUK to get the Reseller Agreement finished and in place. B0539-40 at 241:13-242:15. Lazard argues that its experts observed that a typical parent/subsidiary reseller agreement is a routine matter but, as the Court of Chancery found, the corporate relationship between QNA and QUK was atypical precisely because it was governed by a proxy agreement. Ex. A to Br. at 76:20-77:11. The Court of Chancery correctly found that the delay in putting the Reseller Agreement in place was because of the proxy agreement and did not have anything to do with an intent to limit the Earn-out. *Id.* Again, contrary to Lazard's contentions, the Court below followed an orderly and deductive process.

5. The Court Of Chancery's Decision Can Also Be Affirmed Because Lazard Failed To Prove That The Opportunities Lazard Alleges Were Diverted Or Deferred "Would Result In Company Revenue"

The Court of Chancery's decision can be affirmed for the separate reason that Lazard failed to prove at trial that either of the two "opportunities" that Lazard

claims on appeal that QNA diverted or deferred "***would [have] result[ed] in Company Revenue***" as required by Section 5.4.[8] *See* A0801 § 5.4.

a. GCHQ

Lazard claims that the opportunity with GCHQ "by itself would have resulted in a substantial Earn-out Payment." Br. at 18. This argument is belied by the only evidence adduced at trial. As of July 23, 2010, GCHQ had made it clear that it d[id] not wish to buy the [Cyveillance] service provided from a US-based SOC, and insist[ed] that service & account management [be] UK based." B0277-28. Moreover, "Cyveillance has been adamant that it will not allow the implementation of a UK node unless there is a substantial up front payment" from GCHQ. *Id.* But GHCQ never offered any amount of money to Cyveillance either for its services or to establish a replication of Cyveillance in the UK. Indeed, Lazard does not contend that it did. Instead, Lazard merely cites the $23 million that Mr. Anastassiadis *asked* GCHQ to pay. *Id.* But GCHQ never offered a single dollar to Cyveillance or QNA for the replication of Cyveillance's capabilities in the UK either during the Earn-out Period or after. Thus, Lazard failed to prove that

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[8] Lazard inexplicably alleges that "QNA presented no damages case." Br. at 2. But Lazard bore the burden of proving its damages, which it failed to do. *See LaPoint v. AmerisourceBergen Corp.*, 2007 WL 2565709, at *9 (Del. Ch. Sept. 4, 2007), *aff'd* 956 A.2d 642 (Del. 2008) (TABLE) ("To be entitled to compensatory damages, *plaintiffs* must show that the injuries suffered are not speculative or uncertain ....").

this alleged opportunity "***would [have]*** result[ed] in Company Revenue." *See* A0801 § 5.4.

b. International Reseller Agreement

Similarly, not a single sales opportunity was lost as a result of the length of time it took for the parties to negotiate the Reseller Agreement. Cyveillance CFO Mr. Rose acknowledged that QUK was trying to sell Cyveillance products in the UK in 2009, months prior to the execution of the Reseller Agreement, and conceded that the lack of a reseller agreement "didn't stop sales efforts." B0540-42 at 242:19-244:5; B0169-73. Moreover, Cyveillance itself was marketing and pitching its products and services in the UK prior to the execution of the Reseller Agreement and throughout the Earn-out Period. B0846-47 at 548:14-549:7; B0227-28; B0207. Indeed, in its post-trial briefs, Lazard did not even argue—let alone prove—that signing the International Reseller Agreement earlier somehow "would have resulted in Company Revenue."

II. THE COURT OF CHANCERY PROPERLY CONCLUDED THAT THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING DID NOT APPLY BECAUSE THERE WAS NO CONTRACTUAL GAP TO FILL

A. Question Presented

Whether the Court of Chancery correctly determined that there was no contractual gap to be filled in this case by the implied covenant of good faith and fair dealing, because the parties engaged in extensive arms-length negotiations in which Cyveillance proposed numerous specific affirmative covenants, which were not ultimately agreed upon by the parties and were intentionally omitted from the final agreement. *See* Ex. A to Br. at 70:16-24, 77:16-80:3.

B. Scope Of Review

This Court reviews de novo the application of the implied covenant of good faith and fair dealing but "[d]eterminations of fact and application of those facts to the correct legal standards ... are reviewed for an abuse of discretion." *Schock v. Nash*, 732 A.2d 217, 232 (Del. 1999) (citing *Hogg v. Walker*, 622 A.2d 648, 654 (Del. 1993)).

C. Merits Of Argument

Lazard contends that the Court of Chancery erred by holding that the intent standard from Section 5.4 displaced the implied covenant of good faith and fair dealing. Br. at 28. This argument fundamentally misconstrues the Court of Chancery's decision, which held Lazard may not invoke the implied covenant of

good faith and fair dealing because "there is no gap that should be filled in this case." Ex. A to Br. at 79:9-24. It did not hold that Section 5.4 displaced the implied covenant; rather it held that Section 5.4 speaks directly to "the types of actions that QNA supposedly failed to take in this case." *Id.* at 78:18-21. The Court of Chancery's ruling is completely consistent with this Court's rulings on the application of the implied covenant in an earn-out context and entirely supported by all of the evidence presented at trial. The Court of Chancery's ruling should be affirmed.

1. The Court Of Chancery Properly Determined That The Implied Covenant Did Not Apply To The Merger Agreement Because There Was No Unanticipated Gap To Fill

Lazard contends that the Court of Chancery erred by "applying the 'intent' standard of Section 5.4 to QNA's discretionary decision-making under the Merger Agreement rather than the standards required by the implied covenant of good faith and fair dealing. Br. at 27-28. This is an obvious misreading of the Court of Chancery's decision. *See id.* at 30.

This Court has held that the implied covenant "cannot properly be applied to give the plaintiffs contractual protections that 'they failed to secure for themselves at the bargaining table.'" *Winshall v. Viacom Int'l Inc.*, 76 A.3d 808, 816 (Del. 2013) (citation omitted). The implied covenant only operates to "infer[] contractual terms to handle developments or contractual gaps that ... *neither party*

anticipated." *Nemec v. Shrader*, 991 A.2d 1120, 1125 (Del. 2010) (emphasis added). Thus, the doctrine only applies "when the contract is truly silent with respect to the matter at hand," *Allied Capital Corp.*, 910 A.2d at 1032 (Del. Ch. 2006), and it is "clear from the [contract] that [the parties] would have agreed to" the omitted terms. *Winshall*, 76 A.3d at 816.

Applying these well-settled and fundamental principles of law, the Court of Chancery properly held that "there is no gap that should be filled in this case." Ex. A to Br. at 79:24. The Court of Chancery found that "Cyveillance attempted to negotiate for a range of affirmative post-closing obligations, but QNA rejected all of them" in favor of the only post-closing obligation placed on QNA, which was Section 5.4.[9] *Id.* at 78:22-79:8. Because QNA's post-merger obligations regarding its management of Cyveillance are "expressly covered by the contract ... the implied duty to perform in good faith does not come into play." *Dave Greytak Enters., Inc., v. Mazda Motors of Am. Inc.*, 622 A.2d 14, 23 (Del. Ch. 1992). Rather, Section 5.4's negative covenant articulates the extent of QNA's duties, and

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[9] The Court of Chancery's decision that there was no unanticipated gap to fill is supported by the evidence presented at trial. Multiple witnesses, including Mr. Anastassiadis, confirmed that Section 5.4 was the ***only*** restriction on QNA's post-closing obligations with respect to the management of Cyveillance after the merger. B0806 at 508:9-18 (Mr. Anastassiadis conceded that Section 5.4 "was the ***only*** restriction on how [QNA] agreed to operate Cyveillance after the merger."); A0801 § 5.4.

conversely Cyveillance shareholders' rights, with regard to the management of the surviving corporation after the merger. A0801 § 5.4.

Lazard argues that Section 5.4 applied only to "defined circumstances," namely when specific contracts or business opportunities involving Cyveillance capabilities arose but that the parties post-merger relationship involved more than just QNA's actions with respect to specific contracts or business opportunities that arose for Cyveillance. Br. at 30-31. Lazard argues that the merger agreement was silent as to how QNA would exercise its discretion other than in these "defined circumstances." *Id.* at 31. But the implied covenant only operates to "infer[] contractual terms to handle developments or contractual gaps that ... *neither party anticipated*." *Nemec*, 991 A.2d at 1125 (emphasis added). The Court of Chancery found that not only did both sides fully anticipate post-closing obligations such as introducing Cyveillance offerings to QNA's own government client base, but that Lazard tried to negotiate for the precise terms they now argue should have been implied into the contract by the Court of Chancery. Ex. A to Br. at 78:22-79:8. The Court of Chancery properly refused to use the implied covenant "to give the plaintiffs contractual protections that 'they failed to secure for themselves at the bargaining table.'" *Winshall*, 76 A.2d at 816.

2. The Court Of Chancery Correctly Ruled, In The Alternative, That If The Merger Agreement Had A Gap To Fill It Would Be Filled With An Intent-Based Standard

After determining that the Merger Agreement contained no gap to be filled by the implied covenant, the Court of Chancery ruled in the alternative that ***even if*** there were a gap to be filled in the Merger Agreement, it could not be filled with the objective standard pressed by Lazard because the evidence at trial overwhelmingly proved that the parties had explicitly considered such objective standards and that QNA had expressly rejected them at the bargaining table. Ex. A to Br. at 79:9-80:3.

Lazard contends that "there is no evidence [that the parties] ever agreed that an intent-based standard would govern all of QNA's discretionary decisions relative to [Cyveillance]." Br. at 32 (emphasis added). This argument misses the point as a matter of law and is wrong as a factual matter. The implied covenant only applies when it is "clear from the [contract] that [the parties] would have agreed to" the omitted terms. *Winshall*, 76 A.3d at 816. It is clear from the negotiating history and the contract that the parties *would not* have agreed to the "specificities that would cover the types of actions QNA supposedly failed to take," and in fact affirmatively *did not* agree to those specificities. Ex. A to Br. at 78:15-21; *Winshall*, 76 A.3d at 816. Rather, the evidence at trial conclusively showed that the parties considered the precise types of post-closing affirmative

covenants Lazard argues should have governed QNA's actions, yet rejected them in the bargaining process. The only standard that the parties did agree to with regard to *any* post-closing obligation placed on QNA was the intent standard.[10]

3. The Court Of Chancery Correctly Found As A Factual Matter That QNA Took Steps To Expand Cyveillance Sales And Develop New Products And Services

Finally, Lazard contends that "the evidence at trial readily established that QNA, contrary to its prior representations that it could and would sell Cyvelliance's offerings in volume to its government customers, ... precluded opportunities from the arising in the first place." Br. at 34 (emphasis omitted) (internal citations omitted). The Court of Chancery's factual finding that "[t]here is ***extensive*** contemporaneous evidence establishing that rather than trying to limit

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[10] Lazard contends that the negotiating history shows that the parties considered and rejected the idea that an intent standard would govern all of QNA's discretionary decisions relative to Cyveillance. Br. at 32 n.50. Lazard cites A0583 in support of this, which was a draft of the Merger Agreement with language proposed by Lazard's *own* lawyers. The language proposed in this draft by Lazard (QNA shall not "take any action intended to result in a reduction of the Earn-out Payment below that which would have been achieved if such action had not been taken, including without limitation diverting or deferring contracts or business opportunities that would result in Company Revenue to products, businesses or periods that would not result in Company Revenue") was rejected by QNA and replaced with the more precise language that became Section 5.4 (QNA shall not "take any action to divert or defer contracts or business opportunities that would result in Company Revenue with the intent of reducing or limiting the Earn-out Payment."). Both versions supply a specific intent-based standard governing QNA's post-merger obligations with respect to the conduct of the surviving corporation, with the final agreed-upon version containing narrower and more precise language governing QNA's conduct. Moreover, there is no evidence supporting Lazard's argument about the meaning of this proposed (but rejected) language.

the earnout, QNA in fact took steps to expand Cyveillance's sales and develop new products and services" belies this argument.

Lazard contends that its experts—who did not testify at trial—observed that QNA's efforts were "marginal," Br. at 34 n.52, but this was unequivocally refuted at trial. Indeed, both Mr. Anastassiadis and Mr. Burns conceded again and again that QNA had taken steps to generate contracts and business opportunities for Cyveillance and that such efforts were inconsistent with an intent to limit the Earn-out Payment. *See* B0881-82 at 583:19-584:9; B0056; B0875-79 at 577:22-581:11; B0055; B0920 at 622:12-16; B0195-97; B0885-86 at 587:6-588:14; B0113; B0907-08 at 609:3-610:21; B0166-68; B0399-400 at 101:17-102:18. Lazard's arguments directly contradicting its own fact witnesses must be rejected.

CONCLUSION

For the foregoing reasons, the Court of Chancery's decision granting Defendants Below-Appellees' judgment on all counts should be affirmed in full.

OF COUNSEL:

Allen M. Gardner
Jessica E. Phillips
LATHAM & WATKINS LLP
555 Eleventh Street, NW, Suite 1100
Washington, DC 20004
(202) 637-2200

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/s/ Srinivas M. Raju
Srinivas M. Raju (#3313)
Robert L. Burns (#5314)
RICHARDS, LAYTON & FINGER, P.A.
One Rodney Square, 920 N. King Street
Wilmington, Delaware 19801
(302) 651-7700

Attorneys for Defendant Below-Appellee QinetiQ North America Operations LLC