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IN THE SUPREME COURT OF THE STATE OF DELAWARE

KATHERINE D. CROTHALL, *et al.* Defendants Below/Appellants, - and - ADHEZION BIOMEDICAL, LLC, a Delaware limited liability company, Nominal Defendant/Appellant, v. ROBERT ZIMMERMAN, Plaintiff Below/Appellee, - and - THE WILLIFORD FIRM, LLC and EVAN O. WILLIFORD, Intervenors Below/Appellees	)	No. 608, 2013

JOINT REPLY BRIEF ON APPEAL AND ANSWERING BRIEF ON CROSS-APPEAL OF DEFENDANTS BELOW/APPELLANTS, KATHERINE D. CROTHALL, MICHAEL GAUSLING, PETER MOLINARO, ROBERT TONI, STEVE BRYANT, ORIGINATE ADHEZION A FUND, INC., ORIGINATE ADHEZION Q FUND, INC., ORIGINATE VENTURES, LLC, LIBERTY VENTURES II, L.P., LIBERTY ADVISORS, INC., AND THOMAS R. MORSE AND NOMINAL DEFENDANT/APPELLANT ADHEZION BIOMEDICAL, LLC

Appeal from the Decision of the Court of Chancery, C.A. No. 6001-VCP

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SUMMARY OF ARGUMENT IN ANSWER TO CROSS-APPEAL

1. Denied.[1] The Chancery Court's erroneous interpretation of the Operating Agreement is reviewable in this appeal. The Chancery Court's interpretation is not "moot" because there plainly is an "actual controversy" between parties with "real and adverse" interests, namely, defendants and Williford. The Chancery Court expressly made its interpretation of the Operating Agreement the basis of its award of fees. Defendants contend that Williford is not entitled to a fee award in part because the Chancery Court erred in interpreting the Operating Agreement. Williford contends the trial Court's interpretation is correct and that he is entitled to the fee awarded. Nor is there any merit to Williford's argument that the Chancery Court's interpretation is not reviewable because it was not included in a final order. There is no dispute that the Chancery Court's fee award is a final appealable order, and that defendants timely appealed that order. Thus, any prior non-final ruling affecting the fee award, including the Chancery Court's interpretation of the Operating Agreement, is properly before this Court.

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[1] This paragraph corresponds to the fourth paragraph in Williford's "summary of argument," which presents a new issue on cross-appeal.

2. Denied.[2] Williford does not have standing to argue merits issues that his former client abandoned. In any event, the Chancery Court correctly applied the law in determining that the independence of director defendant Steven Bryant was not negated by Bryant's prior working relationship with Adhezion's CEO. Under the case cited by Williford, *Beam v. Stewart*, 845 A.2d 1040 (Del. 2004), the evidence presented to the Chancery Court at trial overwhelmingly supported the Court's finding that Bryant was independent. The Chancery Court also correctly applied the law in determining that the VC investors did not control Adhezion through a "blood pact" or voting block. The standard stated by Williford is not materially different from the one applied by the Chancery Court, and even if it were, the result is the same as the one reached by the Chancery Court.

[2] This paragraph corresponds to the fifth paragraph in Williford's "summary of argument," which presents a new issue on cross-appeal.

ARGUMENT

I. ARGUMENT IN REPLY: WILLIFORD DID NOT CREATE A CORPORATE BENEFIT BECAUSE THE CHANCERY COURT'S INTERPRETATION OF THE OPERATING AGREEMENT IS WRONG AS A MATTER OF LAW

A. The Chancery Court's Erroneous Interpretation of the Operating Agreement is not "Moot"

Williford wrongly argues that because *his* former client was dismissed for lack of standing after he sold all of his ownership units in Adhezion, the Chancery Court's interpretation of Adhezion's Operating Agreement is now "moot" and cannot be reviewed by this Court. There is nothing moot about it.

As Williford himself acknowledges, the Chancery Court expressly predicated its fee award on its underlying interpretation of the Operating Agreement: "[T]his Court's Post-Trial Opinion serves as the basis for my decision in this Memorandum Opinion to award attorneys' fees to [Williford]." Oct. 14, 2013 Op. at 26. There plainly is an "actual controversy" between defendants and Williford regarding the Chancery Court's interpretation of the Operating Agreement, and their interests with respect to this issue are "real and adverse." *Tyson Foods, Inc. v. Aetos Corp.*, 809 A.2d 575, 582 (Del. 2002) (internal quotation marks omitted). Defendants assert that because the Chancery Court's interpretation of the Operating Agreement in the Post-Trial Opinion is wrong, there is in fact no basis to support the award of fees. Williford, by contrast, asserts that

his is entitled to fees because the Chancery Court's interpretation is correct. That is the opposite of mootness.

Moreover, the Chancery Court itself opined that its interpretation of the Operating Agreement "might have issue preclusive effect in a future case." Oct. 14, 2013 Op. at 26. It is well-settled that a party is "aggrieved," and may appeal, any decision that "includes a collateral adverse ruling that can serve as a basis for the bars of *res judicata*, collateral estoppel, or law of the case in the same or other litigation." *Hercules Inc. v. AIU Ins. Co.*, 783 A.2d 1275, 1277 (Del. 2000).

There is equally no merit to Williford's contention that the Chancery Court's interpretation of the Operating Agreement is not reviewable because it "was not put in any final judgment." Ans. Brf. at 12. There is no dispute that the Chancery Court's October 16, 2013, Order awarding Williford $300,000.00 in fees is a final appealable order. That final Order "brings up for review all interlocutory or intermediate orders involving the merits and necessarily affecting the final judgment which were made prior it its entry." *Robinson v. Meding*, 163 A.2d 272, 275 (Del. 1960); *see SIGA Techs., Inc. v. Pharmathene, Inc.*, 67 A.3d 330, 342 n.33 (Del. 2013). The Chancery Court's interpretation of the Operating Agreement in its Post-Trial Opinion necessarily "affect[ed] the final judgment" because the Chancery Court expressly made it "the basis for [its] decision . . . to award

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attorneys' fees to" Williford. Oct. 14, 2013 Op. at 26. Thus, there is no finality obstacle to this Court's review of the Chancery Court's interpretation of the Operating Agreement.

Contrary to Williford's assertions, nothing in *Tyson Foods* alters these conclusions. In that case, the trial Court's post-trial decision was not the basis for any award of fees. Instead, the parties *settled* the case after the trial Court entered its post-trial opinion. *Tyson Foods,* 809 A.2d at 578. One party then tried to appeal the trial Court's findings, months after they had been entered, because certain other parties in separate litigation were attempting to use those findings against it. *Id.* at 579. This Court refused to hear that appeal because the party seeking review had voluntarily "elected not to exercise its right to appeal" and had instead chosen to settle. *Id.* at 582. The appeal was therefore both untimely and moot. *Id.* at 577, 582-83.

By contrast, this appeal is neither untimely nor moot. Defendants could not appeal the Chancery Court's Post-Trial Opinion when it was entered because, unlike in *Tyson Foods*, the "contemplation of additional proceedings on the issue of attorneys' fees render[ed]" that Opinion "interlocutory" at that time. *Nama Holdings, LLC v. World Market Center Venture, LLC*, 2 A.3d 74, 74 (Del. 2010). However, once the Chancery Court's final fee award was entered on October 16, 2013, defendants filed a timely notice of appeal. As just noted, that notice of

appeal also brings up for review the Chancery Court's interpretation of Adhezion's Operating Agreement in its Post-Trial Opinion. *Robinson*, 163 A.2d at 275. Thus, there can be no question that defendants' appeal is timely.

Nor did defendants voluntarily forego their appeal rights by entering into any settlement that could moot their challenge to the Chancery Court's interpretation of the Operating Agreement. To the contrary, there still is a live controversy between defendants and Williford regarding the propriety of the Chancery Court's fee award, which, by definition, includes the express basis for that award, namely, the Chancery Court's underlying interpretation of the Operating Agreement.

In short, this Court can review the Chancery Court's interpretation of Adhezion's Operating Agreement that is the basis for the Chancery Court's fee award.

B. The Chancery Court's Interpretation of Adhezion's Operating Agreement is Wrong as a Matter of Law

Williford's efforts to defend the Chancery Court's interpretation of Adhezion's Operating Agreement on the merits fail.

First, most of Williford's arguments focus on establishing something that is not in dispute: the Operating Agreement requires that new ownership units in Adhezion must be "authorized" before they can be "issued," and new units are

"authorized" by an amendment to the Operating Agreement. Ans. Brf. at 14-15.[3] Everyone agrees that this is the case. The issue is whether an amendment to the Operating Agreement to authorize new units is governed by the body of Section 15.11 of the Operating Agreement, which provides that amendments must be approved by a majority of common unitholders and two-thirds of the preferred unitholders, or is instead governed by Section 15.11's exception for "the issuance of additional Units" under Section 3.8. Both the plain language of the Operating Agreement, and the evidence at trial, demonstrate that the exception controls.

The plain meaning of the Operating Agreement, which was corroborated by Miller's unrebutted testimony, established that the purpose of Section 15.11's exception was to ensure that Adhezion's capital raising efforts would not be subject to approval of the common unitholders. A. 408.[4] The original common unitholders, including Zimmerman, deliberately bargained away any right to approve future capital raising efforts when they entered into the Operating Agreement with the preferred unitholders. *Id.* If, as Williford argues, an

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[3] Contrary to Williford's assertions, Appellants never argued at trial or in their post-trial brief that the Board had "the right" to issue new units "without amending the Operating Agreement." Ans. Brf. at 16.

[4] All references to the Opening Brief's appendix are designated by "A__;" all references to the Answering Brief/Opening Brief on Cross-Appeal's appendix are designated by "B__," and all references to this Reply Brief/Answering Brief on Cross-Appeal's appendix are designated by "AR__."

amendment to authorize additional units were subject to the approval requirements in the body of Section 15.11, and not the exception, then the common unitholders would have the ability to block future capital raising efforts by withholding approval of such an authorizing amendment, the very right they chose to relinquish.

Williford speculates that common unitholders would "reasonably expect" that their approval would be required to increase the number of authorized units. Ans. Brf. at 18. But no *evidence* at trial established that any common unitholder had such an expectation. Williford elicited no testimony from his former client, Zimmerman, remotely suggesting that he had that expectation, and in fact the unrebutted testimony at trial established that "the exception regarding the issuance of additional units was specifically negotiated in this transaction so that the company could issue additional units without having to get the consent of the common holders," and that Zimmerman himself *did not want* common unitholders (of which he was one) to have a right to approve additional capital investments in Adhezion. *See* A. 405.

Second, Williford wrongly argues that an amendment to authorize new units must require common unitholder approval under Section 15.11, because there is no "provision giving anyone else [such as Adhezion's Board] *unilateral* authority to authorize any additional shares." Ans. Brf. at 16 (emphasis added). Defendants

have never argued that Adhezion's Board could "unilaterally" amend the Operating Agreement to authorize new units. To the contrary, Section 3.2 of the Operating Agreement expressly states that such an amendment must be approved by two-thirds of the preferred unitholders. A. 229-230. But the right of the *preferred* unitholders to approve an amendment authorizing new units cannot give the *common* unitholders an approval right they bargained away. Like the Chancery Court, Williford erroneously reasons that because the Board's power to create and issue new units under Section 3.8 is "subject to" to the provision in Section 3.2 requiring that the consent of two-thirds of the preferred unitholders must be obtained to "create, authorize or reserve" units, the Board's powers under Section 3.8 must somehow *not* include the power to "authorize" new units. Ans. Brf. at 17. Williford then asserts that because the Board's powers under Section 3.8 supposedly do not include the "authorization" of new units, an amendment to authorize new units must be subject to the approval requirements in the body of, and not the exception to, Section 15.11, including the requirement of approval by a majority of common unitholders. *Id.* This reasoning ignores that the consent rights in Section 3.2 are protections that the preferred unitholders specifically negotiated for *themselves* so that they, and they alone, would have veto power with respect to certain actions by the Board, including future capital raising efforts.

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A. 263, 406-407. To turn the preferred unitholders' specifically negotiated consent rights into a veto power possessed by the *common* unitholders is contrary to the plain purpose of Section 3.2, and devoid of any support in the trial record.

Moreover, Section 15.11 already requires that amendments to the Operating Agreement not subject to its exception must be approved by two-thirds of the preferred unitholders, in addition to a majority of common unitholders. If an amendment to authorize new units were subject to the approval requirements in the body of, and not the exception to, Section 15.11, then such an amendment would already require the approval of two-thirds of the preferred unitholders, and the preferred unitholders' specifically negotiated right to approve the authorization of new units under Section 3.2 would be pointless.

Thus, the clear effect of the language in Section 3.8 that the Board's capital raising powers are "subject to the provisions of Section 3.2" is *not* to carve out from those powers the power to "authorize" new units. Instead, the clear effect of Sections 3.8 and 3.2 together is that the Board *does* have the power to amend the agreement to authorize new units, but this power simply is subject to the consent of the preferred (not the common) unitholders.

The Chancery Court therefore erred in concluding that the approval of common unitholders was necessary to authorize new units under the Operating Agreement, and there is thus no basis to support any award of fees to Williford.

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II. ARGUMENT IN REPLY: THE CHANCERY COURT'S AWARD OF ATTORNEYS' FEES SHOULD BE REVERSED BECAUSE WILLIFORD'S EFFORTS CONFERRED NO COMPENSABLE CORPORATE BENEFIT ON ADHEZION OR ITS UNITHOLDERS

The sole "benefit" that Williford says the Chancery Court's ruling conferred on Adhezion is that the ruling may be "valuable" "in any future dispute" because it constitutes "*stare decisis* as to the common unitholders' voting rights in the Court of Chancery in the State of Delaware in which Adhezion is domiciled." Ans. Brf. at 25. This is precisely the kind of speculative "benefit" that cannot support an award of fees under Delaware law. *Richman v. De Val Aerodynamics, Inc.*, 185 A.2d 884, 885 (Del. Ch. 1962) (explaining that the benefit must be "substantial" and not "speculative in character"). There is no evidence that any "dispute" with any common unitholder is ever likely to arise. The only Adhezion common unitholder that ever had any "dispute" with defendants is Zimmerman. He failed after long and expensive litigation in the Chancery Court to establish that he had ever been treated unfairly, and then sold all of his units (suggesting that he in fact did not value the results achieved in the litigation at all). Williford cites no evidence that any other common unitholder puts any value on the results of Williford's efforts. To the contrary, the far more reasonable conclusion is that Adhezion's common unitholders would have preferred to avoid the waste of resources that Williford and his former client caused.

In any event, the arguable *stare decisis* effect of the Chancery Court's ruling, if any, is "not a substantial, identifiable economic benefit upon which to base an award of attorneys' fees." *Thorpe v. CERBCO, Inc.*, 1997 Del. Ch. LEXIS 18, *14 (Del. Ch. Feb. 6, 1997), attached as Ex. A. Williford, like the Chancery Court, attempts to distinguish *Thorpe* by arguing that the Chancery Court's ruling interpreting the Operating Agreement is "narrow" and "specific." Ans. Brf. at 23. But that fact, if anything, simply further *limits* its value. Unlike the "therapeutic benefit" cases on which Williford relies, Ans. Brf. at 21-22, the Chancery Court's ruling did not require any change in how Adhezion was managed or governed, and did not alter any of the transactions that Williford and his former client challenged. To the contrary, the Chancery Court correctly held that altering the transactions, "[r]ather than rectify wrongdoing and avoid unjust enrichment," "would create a windfall for Zimmerman." Jan. 31, 2013 Op. at 66.

Nevertheless, Williford argues that the Chancery Court's interpretation of the Operating Agreement confers a benefit because it may ensure that the purported "wrong" will not "recur." Ans. Brf. at 24. But that cannot be a benefit to Adhezion, because the trial record is compelling that there was not — and would not have been in the future — any risk of harm to Adhezion or its unitholders. Although the Chancery Court found that the common unitholders should have been permitted to vote to approve (or disapprove) previous capital raises, it also found

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that despite that the capital was desperately needed (obviously giving the providers of capital great negotiating power), no common unitholder was harmed by any of the challenged transactions because each of those transactions provided Adhezion with "crucial capital on fair terms." Jan. 31, 2013 Op. at 67. There is nothing in the record to support speculation that, absent the Chancery Court's interpretation, the Board would have departed from its longstanding and uniform practice of approving capital raises only on terms that are fair to Adhezion and to its unitholders. No Delaware case supports a fee award for achieving such a speculative "benefit."

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III. ARGUMENT IN REPLY: THE AMOUNT OF ATTORNEYS' FEES AWARDED BEARS NO RELATIONSHIP TO THE MINIMAL TIME AND EFFORT WILLIFORD SPENT ON THE SOLE ISSUE ON WHICH HE WAS SUCCESSFUL.

The Chancery Court itself acknowledged that in determining an award of fees, the Court should "consider the work the attorneys performed to achieve the benefit and the amount and value of the attorney time *required* for that purpose." Oct. 14, 2013 Op. at 30. Yet the Chancery Court engaged in no such analysis, and instead awarded Williford nearly the entirety of his lodestar, despite that almost none of his work in this case was devoted to achieving the "benefit" he supposedly achieved.

Williford does not dispute that very little of his time was devoted to litigating the interpretation of Adhezion's Operating Agreement. Rather, he argues only that "counsel cannot know beyond estimating risk what claims will be successful after a trial, and so must spend appropriate time litigating each without the benefit of hindsight." Ans. Brf. at 29. He then admits that the "fiduciary duty claims that ultimately did not prevail . . . were much more fact intensive than the common unitholder approval claim" and "took more effort." *Id.* at 29-30. But that is not a reason to compensate Williford for his unsuccessful efforts. If the unsuccessful claims required more work than the sole successful claim, that is a risk that any lawyer taking a case on a contingent-fee arrangement must accept. Williford is in essence asking for a risk-free contingent fee arrangement. On his

argument, a lawyer bringing contingent-fee shareholder litigation in Chancery Court would have no incentive to evaluate the relative strengths and weaknesses of the potential claims in the case because, so long as he succeeds on some tiny part of the case, the company will be forced to pay for his work on all issues.

Moreover, contrary to Williford's assertions, no Delaware case holds that all of an attorney's time is recoverable even when, as here, almost all of the arguments the attorney presented were rejected. The cases cited by Williford do not say otherwise. In *Citrix Systems,* the Court noted that the claim on which it allowed an interim award of fees was "closely related" to another claim that was yet to be resolved. *La. State Emps. Ret. Sys. v. Citrix Sys., Inc.,* 2001 Del. Ch. LEXIS 115, *36 (Sep. 17, 2001), attached as Ex. B. In *First Interstate,* the Court allowed the attorneys to recover some time spent on earlier pleadings because that work "contributed to the final pleading" that was successful. *In re First Interstate Bancorp Consol. S'holder Litig.,* 756 A.2d 353, 364 (Del. Ch. 1999). Similarly, in *Bradbury,* the Court concluded that it would "not wholly disregard" time spent on unsuccessful claims because that time "contributed, to some extent, to the benefits achieved." *San Antonio Fire & Police Pension Fund v. Bradbury,* 2010 Del. Ch. LEXIS 218, *47-*48 (Oct. 28, 2010), attached as Ex. C. Lastly, in *Golden State,* all of the claims were settled. When the parties submitted the settlement agreement to the Court for approval, the defendants *agreed* to pay the plaintiffs'

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attorneys' fees, but the Court awarded approximately one third of the amount requested because the attorneys' efforts produced only a "modest benefit." *In re Golden State Bancorp Inc. S'holders Litig.*, 2000 Del. Ch. LEXIS 8, *1, *15 (Jan. 7, 2000), attached as Ex. D.

In contrast to all of these cases, Williford and his former client were unsuccessful except for a single issue asserted in a discrete count at the tail end of their amended complaint. None of the evidence Williford pursued in discovery was relevant to this discrete claim, and he declined to cross-examine the sole witness who testified to it at trial. Instead, virtually all of Williford's effort was spent in a misguided attempt to show that the challenged transactions undervalued Adhezion and unfairly diluted Zimmerman's interest in the company. Those efforts not only failed completely, they contributed nothing to the sole issue on which he was successful. The Chancery Court's fee award should be reversed because it fails to take this basic fact into account.

IV. ARGUMENT IN ANSWER TO CROSS-APPEAL: THE ISSUE OF BRYANT'S INDEPENDENCE IS NOT PROPERLY ON APPEAL, AND IN THE ALTERNATIVE, THE COURT DID NOT ERR

A. Questions Presented

1. Whether Williford has standing to challenge the Chancery Court's findings on merits issues that have nothing to do with the fee petition on appeal.

2. Whether the Court of Chancery erred in holding that a director was independent where he shared a prior professional and social friendship with Adhezion's CEO, and where he himself was not interested in the transactions.

B. Standard and Scope of Review

The question of whether Williford has standing to challenge the Chancery Court's findings on merits issues that have nothing to do with the fee petition on appeal is a question of law that this Court considers for the first time on appeal. If the Court considers Williford's arguments on the merits, the question of whether the Chancery Court applied the correct legal standard is a legal question that this Court reviews de novo. *Alaska Elec. Pension Fund v. Brown*, 988 A.2d 412, 417 (Del. 2010). To the extent that the Chancery Court's conclusions turned on factual findings, they are subject to an abuse of discretion standard and are given "significant deference." *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214, 217 (Del. 2010).

C. Merits of Argument

1. Zimmerman Does Not Have Standing to Challenge Bryant's Independence

An attorney challenging a Court's decision on a fee petition does not have standing to challenge merits issues in the Court's underlying opinion, where, as here, his client has chosen to abandon the case. *Lindh v. Randolph*, 525 A.2d 1013, 1987 Del. LEXIS 1108, *9 (May. 4, 1987) ("[W]here a judgment has been entered which affects the interest of a client, but the client does not wish to appeal, an attorney has no standing to appeal in his own right to a higher Court."). Accordingly, Williford cannot now use the appeal and cross-appeal of the fee award to relitigate the merits of all of his former client's claims in the case.[5]

2. Bryant was Independent

In any event, Bryant was independent. Williford attempts to challenge Bryant's independence on the basis of the Chancery Court's so-called "admission" that "Molinaro and Bryant worked closely together and served on the same boards of directors periodically since the 1980s." Ans. Brf. at 33 (quoting Jan. 31, 2013

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[5] By contrast, *defendants* have standing to challenge the Chancery Court's interpretation of the Operating Agreement because that interpretation was the express basis for the fee award, and because the Chancery Court wrongly held that defendants themselves breached the Operating Agreement by not seeking common unitholder approval of the challenged transactions. Williford has no such personal interest in the merits rulings his former client declined to appeal.

Op. at 55). Williford exaggerates evidence that the two men had attended the same large university, had worked together for the same employers for portions of their careers and occasionally socialized at hunting and fishing events, and that Molinaro described Bryant as a "friend;" he then argues that these facts alone demonstrate that Bryant was not "independent" because he and Molinaro shared a "particularly close or intimate personal or business affinity" as set forth in *Beam.* Ans. Brf. at 31-33 (citing *Beam,* 845 A.2d at 1050). This is wrong. None of the evidence demonstrated a "particularly close or intimate personal or business affinity" between Bryant and Molinaro that casts "reasonabl[e] . . . doubt[]" on Bryant's independence as an Adhezion director under *Beam. Beam*, 845 A.2d at 1051.

Williford seizes on the "particularly close or intimate personal or business affinity" language of *Beam*, and argues that the Chancery Court failed to apply this standard to the case. This language does not help Willford, however, because the facts and posture in *Beam* made clear that the type of relationship shared by Molinaro and Bryant was not one that threatened Bryant's independence.

Beam was decided at the motion to dismiss stage, where all inferences had to be drawn in the plaintiff's favor and no evidence had yet been presented to the

Court.[6] *Id.* at 1044. In *Beam*, this Court noted that for a stockholder-plaintiff to allege that a director was not independent, "the complaint … must create a reasonable doubt that a director is not so *beholden* to an interested director . . .that his or her discretion would be sterilized." *Id.* at 1050 (internal quotation marks omitted). The Court explained that "[a]llegations of mere personal friendship or mere outside business relationship, standing alone, are insufficient to raise a reasonable doubt about a director's independence." *Id.*

The Court in *Beam* acknowledged that "[*s*]*ome* professional or personal friendships, which *may* border on or even exceed familial loyalty and closeness, *may* raise a reasonable doubt" as to whether a director is independent, but noted that "[n]ot all friendships, or even most of them, rise to this level." *Id.* (emphasis added). The Court flatly rejected any suggestion that the "structural bias" of board membership, or the close professional and social relationships that often precede it, alone impede the independence of a director. *Id.* In particular, the Court stated that one director's independence was not threatened by merely "mov[ing] in the same social circles," "develop[ing] business relationships," or attending the same

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[6] Notably, Williford criticizes the Chancery Court for citing *Benerofe v. Cha*, 1996 WL 535405, at *7 (Del. Ch. Sept. 12, 1996), a case decided on a motion to dismiss. But the main case that Williford himself relies on, *Beam*, was decided on the same procedural posture.

events as another, interested director, and his independence was not threatened simply because the two men "call[ed] eachother friends." *Id.* at 1051. Rather, for a director's independence to be threatened, his "friendship [with an interested director] must be accompanied by *substantially more* in the nature of *serious* allegations that would lead to a reasonable doubt as to [the] director's independence." *Id.* at 1052.

Here, unlike in *Beam,* there has been a full trial on the merits and Williford is not entitled to have all inferences drawn in his favor. Williford failed to present any "serious" evidence at trial to demonstrate that Bryant was at all "beholden" to Molinaro, and Bryant's prior friendship and socialization with Molinaro are exactly the sorts of things that the *Beam* Court found insufficient to negate a director's independence. Here, as in *Beam,* Bryant himself was not interested in the transaction, and Williford did not show that Bryant's social and professional ties with Molinaro threatened his independence. Molinaro describing Bryant as a "friend" plainly is insufficient, and Zimmerman's self-serving "recollection" that Molinaro called Bryant his "very best personal friend" is of dubious value and beside the point. There was nothing presented at trial to demonstrate that, "because of the nature of [Bryant's and Molinaro's relationship," Bryant "would be more willing to risk his . . .reputation than risk the relationship with

[Molinaro]." *Id.* at 1052. For these reasons, the Chancery Court here satisfied the standard set forth in *Beam.*

The other case relied on by Williford, *In re Oracle Corp. Derivative Litig.*, 824 A.2d 917 (Del. Ch. 2003), similarly does not help him. In *Oracle*, the Court held that members of a special litigation committee ("SLC") had failed to show an absence of material fact regarding their independence, where there were substantial ties between the SLC members who were employed by Stanford University, on the one hand, and their fellow faculty members or Stanford benefactors who were accused of insider trading, on the other. *Id.* The Court in *Oracle* emphasized the unique loyalty found among faculty and donors on prestigious academic campuses, and recognized the difficulty that Stanford professors might have in accusing prominent members of their "community of scholars" of insider trading. *Id.* at 942.[7]

Like *Beam*, *Oracle*'s relevance to this case is limited because of the vastly different procedural posture and standard applied by the Court. In *Oracle*,

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[7] The Court stated, "[i]t is no easy task to decide whether to accuse a fellow director of insider trading. For Oracle to compound that difficulty by requiring SLC members to consider accusing a fellow professor and two large benefactors of their university of conduct that is rightly considered a violation of criminal law was unnecessary and inconsistent with the concept of independence recognized by our law." *Id.* at 921.

plaintiffs only had to show that if all inferences were drawn in their favor, the SLC members' ties to their faculty colleagues and heavy donors might threaten their independence. This is vastly different from the case here, where in the context of trial, Williford failed to show that the connections between Molinaro and Bryant actually threatened Bryant's independence.

In addition, the facts of *Oracle* are vastly different from those here, such that the SLC members' independence in *Oracle* was much more likely to be threatened. First, the personal relationships at issue in *Oracle* were different from those here. The Court's decision in *Oracle* was limited to the special bonds between the faculty and benefactor members of Stanford's prestigious "community of scholars." Here, meanwhile, the ties between Bryant and Molinaro were nothing more than the ordinary social and professional ties that often arise between business associates.

Second, the types of decisions facing the SLC members in *Oracle* were different. In *Oracle,* the SLC was required to investigate and draw conclusions about insider trading accusations. Such accusations obviously are more serious than those at issue here – inasmuch as they may result in *criminal* penalties in addition to civil ones – and therefore there is a higher likelihood that the independence of the SLC members would be compromised by their relationships to

the accused.[8] Accordingly, the procedural posture and facts of *Oracle* make it of limited use here.

More instructive is *Benihana of Tokyo, Inc. v. Benihana, Inc.*, 891 A.2d 150 (Del. Ch. 2005), which was issued *after* trial where the Court had "the benefit of a full record" – just like the decision under review here. *Id.* at 176. In *Benihana*, one director had been close friends with the CEO director for over 40 years – longer than the friendship between Molinaro and Bryant – and had met with the CEO director every 10 to 14 days. *Id.* at 177-79. The Court held that in the context of all the evidence presented, this close friendship did not destroy the director's independence, especially because the director himself was not interested in the transaction at issue. *Id.* at 179; *see also In re Western Nat'l Corp. Shareholders Litig.*, 2000 Del. Ch. LEXIS 82, at *41-*42 (Del. Ch. May 22, 2000), attached as Ex. E, (finding that "close social and professional ties… do not warrant the inference" that a director is not independent). Notably, the Court was not persuaded by pretrial decisions cited by plaintiffs, emphasizing the higher burden of proof applicable at trial. *Benihana*, 891 A.2d at 178. Under *Benihana*, in light

[8] Given the heavy penalties and stigma that accompanies criminal acts, the independence of an individual's judgment would be more vulnerable to compromise if he were asked to accuse his colleagues of acts carrying *criminal* penalties, than of mere participation in an interested financial transaction that only carries *civil* consequences.

of all the evidence presented at trial, the Chancery Court correctly found that Bryant's friendship with Molinaro did not undermine his independence.

V. ARGUMENT IN ANSWER TO CROSS-APPEAL: THE ISSUE OF THE VC INVESTORS' CONTROL IS NOT PROPERLY ON APPEAL, AND IN THE ALTERNATIVE, THE COURT DID NOT ERR

A. Questions Presented

1. Whether Williford has standing to challenge the Chancery Court's findings on merits issues that have nothing to do with the fee petition on appeal.

2. Whether the Court of Chancery erred in holding that unitholders were not controlling for purposes of imposing fiduciary duties, where the unitholders were not part of a voting block, had no formal or informal agreement to act in concert, shared no economic bonds or legally significant connections, did not act together, and did not join hands to impose their will and exert actual control upon Adhezion.

B. Standard and Scope of Review

The question of whether Williford has standing to challenge the Chancery Court's findings on merits issues that have nothing to do with the fee petition on appeal is a question of law that this Court considers for the first time on appeal. If the Court considers Williford's arguments on the merits, the question of whether the Chancery Court applied the correct legal standard is a legal question that this Court reviews de novo. *Alaska Elec. Pension Fund*, 988 A.2d at 417. To the

extent that the Chancery Court's conclusions turned on factual findings, they are subject to an abuse of discretion standard and are given "significant deference." *Golden Telecom, Inc.*, 11 A.3d at 217.

C. Merits of Argument

1. Zimmerman Does Not Have Standing to Challenge Whether the VC Investors Together Controlled Adhezion

As explained above, Williford cannot now use the appeal and cross-appeal of the fee award to relitigate the merits of all of Zimmerman's claims. Williford spends several pages of his brief arguing that the Chancery Court erred in holding that Originate and Liberty did not together control Adhezion. This issue has nothing to do with the Chancery Court's basis for awarding of fees and Williford makes no effort in his brief to argue otherwise. Accordingly, the issue is outside of this appeal.

2. The VC Investors Did Not Together Control Adhezion

Neither Originate nor Liberty owned a majority interest in Adhezion, Jan. 31, 2013 Op. at 40, and thus Williford was required to show at trial that Originate and Liberty acted together to exercise "actual control" over Adhezion despite their individual lack of majority ownership. *Kahn v. Lynch Communication Systems, Inc.*, 638 A.2d 1110, 1114 (Del. 1994); *see also In re PNB Holding Co. Shareholders Litigation*, 2006 Del. Ch. LEXIS 158 at *30-*31

(Aug. 18, 2006), attached as Ex. F, (applying *Lynch*); *In re MAXXAM,, Inc.*, 659 A.2d 760, 770-71 (Del. Ch. 1995) (same). Williford failed to do so.

Williford relies on a handful of communications that the Court concluded in its summary judgment opinion *might* support an inference that Originate and Liberty acted in concert to exercise control over Adhezion, when all inferences were construed in Zimmerman's favor. *See* Ans. Brf. at 35-36. These communications, while perhaps sufficient to pass the lenient summary judgment standard of review, were insufficient to support Zimmerman's position when put in context at trial and thus are insufficient to support Willford's position on appeal.[9]

First, Willford cites an e-mail from September 2009, written by Molinaro while preparing for an investor conference. Ans. Brf. at 35. That email stated,

[redacted] *See* AR.1

[9] Contrary to Willford's suggestion, the Court's denial of summary judgment on this issue is not itself an affirmative factual finding that Originate or Liberty in fact exercised such alleged control. *Cf., e.g., In re John Q Hammons Hotels Inc. Shareholder Litigation,* 2011 Del. Ch. LEXIS 1 (Del. Ch. Jan. 14, 2011), attached as Ex. G, (entering judgment for defendants after trial on issues involving the fairness of a merger, following a pretrial denial of summary judgment to defendants on those same issues); *In re The Walt Disney Company Derivative Litigation,* 907 A.2d 693 (Del. Ch. 2005) (entering judgment for a defendant after trial on the issue of duty of loyalty, following a pretrial denial of summary judgment to that defendant on that same issue).

[redacted]

Zimmerman's counsel asked Molinaro to read this e-mail out loud at trial but asked him nothing else about it. AR.6-7. This email does not reflect any coordination between Liberty and Originate, and suggests only that the entities may have had similar views on a fundraising issue. Further, if this unexplained e-mail is supposed to show that Liberty and Originate were resistant to investments in Adhezion as large as [redacted], that suggestion is directly refuted by Gausling's own efforts to secure a [redacted] investment in Adhezion by [redacted] only one month after Molinaro's e-mail was sent. AR.17-18. Gausling testified that he would have been "happy" to see a new investor put this much money into Adhezion notwithstanding that it would have significantly exceeded Originate's own investment. AR.15-16.

Second, Willford cites the September 2009 board meeting minutes in which Morse and Gausling reassured Molinaro that their firms "would continue to *temporarily* satisfy Adhezion's cash requirements" while Adhezion attempted to negotiate a deal with Medline. Ans. Brf. at 35-36; B. 3. (emphasis added). The trial record precludes any inference of agreement or control from this statement. Morse explained that "it looked to me like, at the end of September, that the company had no chance of raising outside money and they should focus on getting distribution partners. And this comment was giving the company runway enough in cash in order to try and do that." AR.11-12. Molinaro testified that this was a

[redacted]

"reaffirmation to go ahead and continue to focus [his] efforts on trying to find a strategic partner," not a permanent order to abandon all efforts at outside fundraising. AR.4. Indeed, Molinaro approached [redacted] about making a [redacted] nvestment in Adhezion approximately one month after the September 29 board meeting. AR.19-25, AR.5.

Third, Willford cites deposition testimony in which Bryant supposedly stated that Originate and Liberty did not "want [Molinaro] to continue trying to raise venture capital funding" because they "want[ed] [Molinaro] to focus on running the business." Ans. Brf. at 36; *see also* Ans. Brf. at 39-40. Bryant clarified at trial that he was referring to the September 2009 board meeting. AR.9-10. He explained that he joined in the recommendation to Molinaro to temporarily cease fund-raising because "the business needed focus from its executive team" following the collapse of the 3M negotiations. AR.8. In any case, this recommendation does not demonstrate agreement or control. It is simply sound business advice, which was reasonably endorsed by both Originate and Liberty, as well as an outside director whom the Court already had held was disinterested and independent. Examining the evidence in the context of trial, Originate and Liberty were not, together, a controlling unitholder, and owed no fiduciary duties to Adhezion. *See In re PNB Holdings*, 2006 Del. Ch. LEXIS 158 at *34; *see also Emerson Radio Corp. v. Int'l Jensen Inc.*, 1996 Del. Ch. LEXIS 100 at *53-54

[redacted]

(Aug. 20, 1996), attached as Ex. H, ("[T]he record does not establish that those two shareholders are connected together in any legally significant way (e.g., by common ownership or contract."), *appeal denied*, 1996 Del. LEXIS 311 (Aug. 23, 1996)), attached as Ex. I.

Recognizing that he could not prevail if his arguments on appeal were limited to weighing the evidence, Williford attempts to muddy the waters regarding the appropriate legal standards – but this attempt is unsuccessful. Williford argues that the Chancery Court misstated the standard when it quoted from *In re PNB Hldg. Co. Shareholders Litigation* and argues that the proper test is "whether a controlling part of the 'voting power in the corporation join hands in imposing its policy upon all' or where a controlling group of unitholders 'speak for and determine the policy of the corporation.'" Ans. Brf. at 36-37 (quoting *Allied Chemical & Dye Corp. v. Steel & Tube Co.*, 14 Del. Ch. 1, 12 (Del. Ch. 1923) (mistakenly cited by Williford as quoting *Weinberger v. UOP, Inc.*, 409 A.2d 1262, 1265 (Del. Ch., 1979)). Williford's standard is no different in substance than the one used by Chancery Court, and even if it were, its application to the facts presented at trial do not suggest a different result.

To determine whether Originate and Liberty together exerted actual control over Adhezion, the Chancery Court looked to whether the VC Investors were involved in a "blood pact" or otherwise "bound together by voting agreements *or*

[redacted]

other material, economic bonds to justify treating them as a unified group," whether they "*acted together*," and whether they were "*connected in some legally significant way*." Jan. 31, 2013 Op. at 40-41. This standard is more expansive than the one attributed to the Chancery Court by Williford, and it correctly accounts for ways in which unitholders may be connected to justify treating them as a majority unitholder. Further, the standard is materially equivalent to the standard stated in the 1923 case of *Allied Chemical & Dye Corp.*, which required a "join[ing] of hands" to show that the majority "imposed" their "policy" on Adhezion. The record does not suggest that Originate and Liberty "joined hands" to "impose" any particular policy on Adhezion, so even under Williford's own phrasing of the applicable standard, his argument fails.

At most, the evidence presented at trial showed that Originate and Liberty shared some parallel interests or conduct, but Zimmerman fails to cite any caselaw suggesting that parallel interests or conduct is sufficient to treat Originate and Liberty as a controlling unitholder that imposed its will on Adhezion. This is not surprising. If mere parallel interests or conduct were sufficient to impose fiduciary duties, then such duties would have to be imposed on virtually *every* unitholder in a corporation – because at some point, every unitholder likely would share in the interests of the majority or engage in conduct similar to the majority. In any case, Originate and Liberty did not act in unison here. For instance, Originate

individually approached [redacted] about investing [redacted] in Adhezion, without Liberty. AR.17-18. And, Originate participated in the January 2011 transaction, whereas Liberty did not participate in this transaction at all. AR.43-44.

Moreover, both the October 2008 Operating Agreement and the February 2010 Operating Agreement were carefully structured to *prevent* Originate or Liberty from exercising actual control. *See, e.g.*, A. 165 at § 3.2(b); A. 229 at § 3.2(b); A. 406-A. 407, A. 410 (Miller). Originate and Liberty were each limited to designating only one board member, giving them less than a majority. Material transactions, including the issuance of units, could be authorized only by vote of holders of two-thirds of the preferred units. *Id.* Neither Originate nor Liberty ever held two-thirds of Adhezion's preferred units; thus, neither of them could effect a material transaction. Further, the provisions of the Operating Agreement governing board composition and the two-thirds vote requirement could not be altered or amended without the agreement of holders of a majority of the Class A Common Units. *See, e.g.*, A. 199 at § 15.11; A. 263 at § 15.11; A. 407-A.408 (Miller). On balance, the facts cited by Williford were sufficient to defeat summary judgment when all inferences were construed in the plaintiff's favor. But, once the entire record was presented at trial, it became clear that Originate and Liberty never held enough power to control Adhezion. *Cf. Ivanhoe Partners v.*

[redacted]

Newmont Mining Corp., 535 A.2d 1334, 1345 (Del. 1987) (stating that largest shareholder was not controlling where it was limited by contractual restrictions to only 40% representation on the board of directors).

Zimmerman grasps at a smattering of other evidence in an effort to demonstrate concerted behavior and control by Originate and Liberty, but none of it calls the Chancery Court's conclusions into question. *See* Ans. Brf. at 38-41. The fact that Pepper Hamilton did a small amount of business for Originate and Liberty does not raise a conflict or show that the entities acted together to exercise control over Adhezion. The evidence that Originate and Liberty were "on both sides" of the challenged transactions means little here because Williford does not argue on appeal that the transactions were unfair or allowed Originate and Liberty to exert their will over Adhezion.

[redacted]

CONCLUSION

For all these reasons, defendants respectfully request that this Court reverse the Chancery Court's award of attorneys' fees to Williford, or in the alternative, remand the case to the Chancery Court for a reassessment of the fee award.

Respectfully submitted,

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