EFiled: Sep 05 2014 03:40PM EDT
Filing ID 55987303
Case Number 343,2014

IN THE SUPREME COURT OF THE STATE OF DELAWARE

| | |
|---|---|
| GARY SALAMONE, MIKE DURA and ROBERT W. HALDER,<br><br>Defendants Below, Appellants,<br><br>v.<br><br>JOHN J. GORMAN, IV,<br><br>Plaintiff Below, Appellee. | No. 343, 2014<br><br>On Appeal from the Court of Chancery<br>Consol. C.A. No. 8845-VCN |

# APPELLANTS' REPLY BRIEF ON APPEAL AND CROSS-APPELLEES' ANSWERING BRIEF ON CROSS-APPEAL

GREENBERG TRAURIG, LLP
Michael J. Maimone (I.D. No. 3592)
Gregory E. Stuhlman (I.D. No. 4765)
E. Chaney Hall (I.D. No. 5491)
1007 North Orange Street, Suite 1200
Wilmington, Delaware 19801
(302) 661-7000

*Attorneys for Defendants Below, Appellants/Cross Appellees*

Dated: September 5, 2014

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

## SUMMARY OF ARGUMENT

4. Denied. Neither Defendants' interpretation of Section 1.2(b) of the Voting Agreement, nor the Trial Court's interpretation of Section 1.2(c) of the Voting Agreement, violates Section 212(a) of the DGCL.

## PRELIMINARY STATEMENT

Gorman's "Statement of Facts" in his Answering Brief is an example of revisionist history, unconstrained by reality and only marginally related to actual fact. During Gorman's years at Westech, Gorman did his best to operate the Company solely for his own benefit. Simply stated, Gorman stripped the Company of any chance at prosperity, siphoning off as much cash as he possibly could to support his lavish lifestyle (including raising wild African animals in his backyard, among other expensive hobbies), pay for escorts, and fly around the country in a private jet – all on Westech's dime. In addition, Gorman used Westech to support his highly-speculative investments that often were structured so that gains were realized by Gorman and losses were suffered by the Company. None of this is conjecture. Independent counsel retained by Westech prior to Gorman's resignation from the Board concluded as much following an investigation of the facts. *See* Monaco Dep., 23:7-9, 60:7-12 (A1015, A1052).

Despite the tale woven by Gorman, *see* An. Br. at 6, Gorman and Westech's search for cash that ended with the issuance of the Series A Stock and the Voting Agreement was not to "expand the sales base" of the Company's operating subsidiary. It was a bail out, necessitated because Gorman's greed and incompetent "leadership" left the Company in ruin. Monaco Dep., 13:20-21 (A1005); Fellus Dep., 39:2-25 (A688); Halder Dep., 32:22-24 (A829). Every

witness in this Action not named "Gorman" testified that immediately prior to the issuance of the Series A Stock, the Company was on the brink of collapse. Monaco Dep., 12:18-13:6 (A1004-05); Pallotta Dep., 40:7-15 (A990); Halder Dep., 33:15-17 (A830); Fellus Dep., 10:11-12 (A659).

The various other primary purchasers of Series A Stock knew Gorman well enough to know that they needed protection from him. As described more fully in the Opening Brief, *see* Op. Br. at 9-10, those investors purchased Series A Stock only because they believed that the Voting Agreement provided protection from Gorman. Indeed, Gorman's good friend Pallotta invested only when it was understood that Gorman could not gain control of the Board, even if Gorman purchased additional Series A Stock, common stock, or both. Monaco Dep. 56:11-57:11 (A1048-49). Curiously, in his Answering Brief, Gorman recognizes that Monaco handled the negotiations relating to the Voting Agreement on behalf of Pallotta, yet ignores Monaco's testimony that Pallotta would not have invested in the Series A Stock if it was possible – at any time – that Gorman could gain control of the Company's Board. *See* An. Br. at 7.

Gorman's campaign to "stack" the Board involved numerous wrongful actions and false statements. Gorman twisted, distorted, and disregarded the language, spirit, intent, and purpose of the Voting Agreement. Gorman denies the occurrence of important meetings with investors where topics were discussed and

agreed upon that directly are contrary to Gorman's position, yet, simultaneously, Gorman proffers stories of an agreement between Pallotta and himself in which they agreed to single-handedly control the Company, a story directly contradicted by Monaco and a story not supported by Pallotta. Gorman, increasingly desperate to regain control of his Westech "piggybank," even attempted to turn back time by backdating a proxy, and then *lied* to counsel to Defendants by stating that he had the proxy "in hand" weeks before the proxy had been drafted.

Gorman is not someone who allows truth to stand in the way of what he wants. The other primary Series A Stock holders, which includes the Company's key employees, knew that all too well, and that is the reason for the Voting Agreement. Unfortunately, as this Action has dragged on and the Opinion caused a deadlock, key employees became fearful that Gorman would find a way around the protection embodied in the Voting Agreement. Following Gorman's latest assault on Westech mere weeks ago[1] – the delivery to the Company of invalid written stockholder consents and the sending of letters to the Company's employees stating that he was in control of the Company – the revenue-generating employees finally grew tired of fighting Gorman, finally grew tired of living in

[1]In his Opening Brief, Gorman interjects "facts" relating to events that have taken place following the conclusion of the proceedings in the Trial Court. Such "facts" inappropriately were submitted by Gorman, as they were not a part of the record below. Defendants, however, felt compelled to respond to those alleged "facts," yet Defendants submit that none of the "facts" relating to events that took place after the conclusion of proceedings in the Trial Court properly are before this Court.

fear that they may have to live with Gorman's "leadership" again, and finally left the Company.

Following that exodus caused by Gorman's letters to the employees stating that he was now in charge, the Company became starved for revenue, fell below certain regulatory capital requirements, and ceased meaningful operations. In other words, Defendants did not "allow [Westech] to fall below regulatory capital requirements by distributing assets and allowing Halder to violate his restrictive covenants and abscond with employees" as Gorman contends.[2] An. Br. at 4. Rather, the Company's money-makers fled out of fear that Gorman would return.

The primary, non-Gorman parties to the Voting Agreement bargained for protection from Gorman's "leadership" and ability to control the Board, and those protections are embodied in the Voting Agreement. The language of the Voting Agreement does not support Gorman's position; Fellus' testimony, Pallotta's testimony, Monaco's testimony, and Halder's testimony do not support Gorman's position; and no document supports Gorman's position. The only "evidence" that supports Gorman's position is the testimony of Gorman. This Court should (a) reject Gorman's strained arguments based upon imagination and desperation rather than fact, and (b) adopt the interpretation of the Voting Agreement asserted by Defendants and fully supported by every witness not named "Gorman."

[2]Halder filed and action in Texas seeking a declaration that the restrictive covenants contained in his employment agreement no longer are in effect because the Company breached the employment agreement.

## ARGUMENT

### I. DEFENDANTS' INTERPRETATION OF THE VOTING AGREEMENT IS THE ONLY INTERPRETATION OF THE THREE INTERPRETATIONS OFFERED THAT IS CONSISTENT WITH THE LANGUAGE AND THE PURPOSE OF THE VOTING AGREEMENT

In this Appeal, this Court is presented with three competing interpretations of the Voting Agreement: Gorman's view, the Trial Court's view, and Defendants' view. Distilled to its essence, Gorman's view is that the Voting Agreement is a nullity because the Board is controlled by Gorman as the majority stockholder. The Trial Court's interpretation of the Voting Agreement misreads several provisions of the Voting Agreement, is contrary to Delaware law, and is internally inconsistent. Defendants' interpretation of the Voting Agreement, by contrast, gives meaning and effect to each provision of the Voting Agreement and fulfills the Voting Agreement's purpose of protecting minority stockholders. In short, the only interpretation of the Voting Agreement that is consistent with its language and purpose is the interpretation set forth by Defendants.

#### A. Gorman's Interpretation Eviscerates The Voting Agreement

Gorman's view reads out of effect the totality of the Voting Agreement. Once this Court analyzes Gorman's arguments, it becomes clear that the adoption of Gorman's view of the Voting Agreement would result in the empowerment of Gorman, as majority stockholder, to nominate and elect *every* director.

Following Pallotta's sale of Series A Stock, Gorman controls the Pallotta Director under Section 1.2(a) because Gorman holds a majority of the outstanding stock of the Company. This first of seven directorships is controlled by Gorman. Gorman argues that he controls the Series A Director under Section 1.2(b) because he holds a majority of shares of the Series A Stock. *See* An. Br. at 18-26. This is the second of seven directorships that Gorman purportedly controls. Gorman also argues that he controls the Key Holder Directors under Section 1.2(c) because he holds the majority of the stock held by the Key Holders. *See* An. Br. at 29-37. These are the third and fourth of seven directorships that Gorman purportedly controls. At this point, according to Gorman, he controls a majority of the Board.

The Pallotta Director (Section 1.2(a)), Series A Director (Section 1.2(b)), and the Key Holder Directors (Section 1.2(c)) select the two Industry Directors pursuant to Section 1.2(e). Not being satisfied with a majority of the Board, Gorman argues that, because he controls the four directorships under Section 1.2(a), Section 1.2(b), and Section 1.2(c), he controls the two Industry Directors under Section 1.2(e). These are the fifth and sixth of seven directorships that Gorman purportedly controls. The Board appoints the CEO of the Company pursuant to the Company's Bylaws, (B978), and the CEO automatically is nominated and required to be elected to the Board pursuant to Section 1.2(d). In light of the fact that (according to Gorman) the Board is comprised of six directors

controlled by him, the Gorman-controlled directors elect the CEO, who will become the CEO Director under Section 1.2(d). This is the seventh of seven directorships that Gorman purportedly controls. If Gorman's interpretation is correct (which it is not), then the Voting Agreement has no purpose.

Perhaps Gorman's proffered reading – that the majority stockholder controls the entirety of the Board – is not surprising because it is advanced by the majority stockholder. This reading, however, is without merit for at least four reasons. *First*, at the time the Voting Agreement was executed, Gorman controlled a majority of the outstanding common stock of the Company, and Gorman, Pallotta, and Fellus controlled a majority of the Series A Stock. If Gorman, Pallotta, and Fellus had the power to fill *all* directorships at the time the Voting Agreement was executed, then the Voting Agreement (as interpreted by Gorman) is meaningless, and the twenty-three other parties to the Voting Agreement were unnecessary and superfluous, including Halder, who was named a Key Holder. *Second*, the language of the Voting Agreement blatantly is inconsistent with Gorman's argument that only Pallotta and Gorman were to control the Board. *See* An. Br. at 8. *Third*, Gorman's interpretation runs contrary to the purpose of voting agreements in general, and the Voting Agreement in particular, which is to provide representation on a board of directors to minority stockholders and other constituencies that, absent such an agreement, would be unable to secure such

representation. *Fourth*, Gorman's actions leading up to the initiation of litigation plainly belie his position that the Voting Agreement empowered Pallotta and Gorman to control the Board. In other words, Gorman's now-proffered reading of the Voting Agreement is a post-litigation manifestation.

1. Gorman's Interpretation Necessitates A Finding That The Majority Stockholders At All Times Had The Power To Fill All Directorships, Which Renders The Voting Agreement Meaningless, And Renders Unnecessary And Superfluous The Twenty-Three Other Parties To The Voting Agreement

Immediately prior to the execution of the Voting Agreement, it is undisputed that Gorman controlled a majority of the outstanding stock of the Company, and, hence, controlled the Board. As outlined above, post-execution of the Voting Agreement, Gorman contends that, by virtue of his majority stockholder status, he controls the designation of each and every director of the Company pursuant to the terms of the Voting Agreement. In other words, Gorman advances the illogical argument that both before *and* after the execution of the Voting Agreement the majority stockholder of the Company possessed the right to designate each and every director of the Company. Such argument reads out of existence the totality of the Voting Agreement. Under Delaware law, all provisions of a contract must be given meaning. *Segovia v. Equities First Holdings, LLC*, 2008 WL 2251218, at *9 (Del. Super. Ct. May 30, 2008) ("[T]he Court must view the contracts as a whole and interpret them in a manner that gives 'a reasonable, lawful, and effective

meaning to all the terms.'"). Gorman's proffered reading does not read out of existence one (or even two) provisions of the Voting Agreement; rather, Gorman's proffered reading reads out of existence every single word of the Voting Agreement. For this reason alone, Gorman's arguments should be rejected.

In addition, immediately after the execution of the Voting Agreement, Gorman held or controlled through affiliates a majority of the Common Stock (approximately 2,447,934 shares) and 72 shares of Series A Stock (of a total then-339 outstanding shares of Series A Stock)[3] of the Company. Pallotta, Gorman's long-time friend, held 80 shares of Series A Stock. Fellus, Pallotta's business associate who was to become the CEO, held 40 shares of Series A Stock. On an as-converted basis, Gorman, Pallotta, and Fellus collectively controlled approximately 7,247,934 votes, constituting 58% of Westech's total voting power (12,481,722 votes).

The combined holdings of Gorman, Pallotta, and Fellus were more than sufficient to control the Board absent a Voting Agreement. If Gorman, Pallotta, and Fellus wanted to memorialize an agreement to vote their shares together, then they would have entered into such an agreement without including any other stockholders. They, however, did not enter into such an agreement. Instead,

[3]The Company repurchased one share of Series A Stock, and so currently there are 338 outstanding shares of Series A Stock.

Gorman, Pallotta, Fellus, and twenty-three[4] other stockholders negotiated and executed the Voting Agreement.

Under Gorman's interpretation of the Voting Agreement, the twenty-three other stockholders that are parties to the Voting Agreement have no meaningful input in the selection of the directors. These stockholders, therefore, received nothing in exchange for their agreement to vote their shares in favor of the directors selected by Gorman, Pallotta, and Fellus. Gorman fails to describe any other consideration that the minority received that would explain their willingness to become parties to a contract that does nothing to protect their interests. This begs the question: why would the minority have agreed to enter into the Voting Agreement? It strains the imagination to believe that twenty-three parties would have agreed to enter into a contract that offered them no benefit, and would be parties to a contract for no reason.

2. Gorman's Interpretation Is Inconsistent With The Language Of The Voting Agreement

The language of the Voting Agreement reflects that Gorman, Pallotta, and Fellus collectively do not control the Board. Section 1.2(b) provides that the Series A Designee is nominated by "the majority of the *holders*" of Series A Stock. The

[4]Schedule A of the Voting Agreement lists 48 holders. Pursuant to Section 7.17 of the Voting Agreement, "[a]ll Shares held or acquired by an Investor and/or its Affiliates shall be aggregated together for the purpose of determining the availability of any rights under this Agreement . . . ." After aggregating the holdings of the investors listed in Schedule A of the Voting Agreement, there are 26 holders.

"holders" of Series A Stock are listed on Schedule A to the Voting Agreement. The vast majority of these "holders" are employees who collectively invested $2 million in the Company. Just as Pallotta received a Pallotta Director in exchange for his $2 million investment, Section 1.2(b) provided the employees who comprised the vast majority of the Series A "holders" with a Series A Director.

Gorman argues that Section 1.2(b) does not mean what it says. He submits case law in which the term "the holders of a majority of shares" and the term "the majority of the holders" have been used interchangeably. The manner in which those terms have been used by Delaware courts and practitioners in cases unrelated to voting agreements, however, has no bearing on the manner in which the parties intended and understood those terms to be used in the Voting Agreement. The question before this Court is the intent of the parties. If the parties intended Section 1.2(b) to be a Gorman-Pallotta-Fellus Designee, then (a) they would have drafted it accordingly, and (b) the Voting Agreement would have twenty-three fewer parties. Section 1.2(b) was not drafted as, and was not intended to be, a Gorman-Pallotta-Fellus Designee.

Gorman's interpretation also fails to give effect to the language of Section 1.2(c), which governs the selection of Key Holder Designees.[5] Section 1.2(c)

[5]Interestingly, under Gorman's interpretation of Section 1.2(c), because he always has owned a majority of shares held by the Key Holders, Gorman contends that he always has been entitled to designate the two directors under Section 1.2(c). In addition to the other flaws in Gorman's proffered interpretation of Section 1.2 discussed herein, this makes little sense, as Pallotta,

provides that the Key Holder Designees are "two persons elected by the Key Holders." (A540). The Voting Agreement identifies the Key Holders as Gorman, Fellus, and Halder. (A619). The plain reading of Section 1.2(c) states that the Key Holders vote to select two Key Holder Designees. The candidates who receive two of the three votes of the Key Holders become Key Holder Designees.

Gorman argues that Section 1.2(c) does not mean what it says. He reads Section 1.2(c) to require the vote of a *majority of shares* held by the Key Holders, not the vote of the Key Holders. This reading transforms the Key Holder Designees into Gorman Designees because, at the time the Voting Agreement was executed, Gorman held a majority of shares held by the Key Holders. If the Key Holder Designees were intended to be Gorman Designees, then there was no reason to use the "key holder" language at all. The Voting Agreement would simply have identified Section 1.2(c) as a Gorman designee provision just as Section 1.2(a) was identified as a Pallotta designee provision.

3. Gorman's Interpretation Is Inconsistent With The Purpose Of The Voting Agreement

Voting agreements are often intended to protect minority stockholders by providing them with representation on a board of directors. *See, e.g.*, *Rohe v. Reliance Training Network, Inc.*, 2000 WL 1038190, at *16 (Del. Ch. July 21, 2000). Majority stockholders do not require this protection because they may

although he invested significantly more money than Gorman, only is entitled to designate one director under Section 1.2(a).

secure such representation by virtue of their status as majority stockholders. Gorman's interpretation nullifies the representation on the Board provided to the minority Series A holders under the terms of the Voting Agreement.

Gorman, Pallotta, and Fellus controlled sufficient stock to fill all directorships absent the agreement of any other stockholder. It would make sense, under Gorman's interpretation, for Gorman, Pallotta, and Fellus to enter a voting agreement to secure assurances from one another that each of their interests would be represented and protected. It does not make sense, however, that Gorman, Pallotta, and Fellus would have included the twenty-three employees in this arrangement, because the employees did not hold enough stock to present a threat.

The employees, as the minority stockholders, were the stockholders in need of the protections embodied in the Voting Agreement. Without the Voting Agreement, the employees would be unable to nominate any director to the Board. The interests of the employees would go completely unrepresented, notwithstanding the fact that the employees collectively invested approximately $2 million in the Company – as much as Pallotta, and more than Gorman. The employees were included in the Voting Agreement because they wanted representation on the Board in exchange for their investment, and Gorman knew at the time he entered the Voting Agreement that employee representation on the Board was a condition to the employees' investment in the Company. Gorman

should not now be heard to argue that these twenty-three parties should not receive the benefit of their bargain.

4. Gorman's Pre-Litigation Actions Belie His Belief That He Controls The Board

Gorman's actions belie his new found "belief" that the Voting Agreement was intended to vest control of the Company in Pallotta and Gorman. When Gorman had a conflict with the Board in June 2013, he resigned. (*See* A622). At that time, the Board consisted of Gorman and Halder as the Key Holder Directors, Monaco as the Pallotta Director, Salamone as the CEO Director, and Dura as an Industry Director. If Gorman truly believed that he had the authority to remove Halder, and to nominate and elect another Key Holder Designee, he would have removed Halder and nominated a Gorman crony to be a Key Holder Designee. Instead, Gorman "walked away" from the Company and then – apparently after experiencing a change of heart – initiated litigation. These are not the actions of a majority stockholder who believes that he controls the Board. Rather, Gorman's "belief" is a post-litigation contrivance, and his actions in June 2013 indicate quite clearly that (a) he did not believe that he had the ability to control the Board in light of the Voting Agreement, and (b) it was not the intent of the parties to the Voting Agreement that Gorman have the ability to control the Board.

B. The Trial Court's Interpretation Misreads The Voting Agreement

The Trial Court's interpretation of the Voting Agreement fails to give effect to the language and intent of the Voting Agreement. Notwithstanding an express statement by the Trial Court that "[a] plain reading [of Section 1.2(b)] by a reasonable third party that inquires no further would support Defendants' per capita theory," Opinion at *15 (A65), the Trial Court erred in reading the Series A Designee under Section 1.2(b) to be, in effect, a Gorman-Pallotta-Fellus designee. The Trial Court also misread Section 1.4(a) to permit the removal of the Key Holder Directors by Gorman. The Trial Court's reading of Section 1.4(a) does not give effect to the plain language of that provision, and is internally inconsistent with the Trial Court's interpretation of Section 1.2(e).

1. The Trial Court Incorrectly Decided That Section 1.2(b) Is A Majority Voting Provision

Gorman and Defendants presented to the Trial Court competing views of the meaning of Section 1.2(b). Gorman argued that the Series A Designee is nominated by a majority vote of the Series A Stock, while Defendants argued that the Series A Designee is nominated by a per capita vote among the holders of the Series A Stock. The Trial Court held that Section 1.2(b) was a majority voting provision despite explicitly stating that a plain reading of Section 1.2(b) supports Defendants' position. Opinion, at *15 (A65). Once the Trial Court determined that a plain reading of the Voting Agreement lead to the conclusion that the

contract was clear and mandated per capita voting, the inquiry should have been at an end.[6] Instead, in conflict with Delaware law, the Trial Court considered extrinsic evidence. That improperly-considered evidence led the Trial Court to conclude that, contrary to the plain reading of Section 1.2(b), that the Series A Designee is nominated by a majority vote of shares. Simply stated, the Trial Court placed extrinsic evidence above the unambiguous terms of Section 1.2(b) and found an interpretation at odds with a plain reading of the provision.

2. The Trial Court Incorrectly Concluded That Defendants' Reading Impermissibly Disenfranchises the Majority Stockholders

The Trial Court determined that Section 1.2(b) must be read as a majority vote provision in accordance with the law's presumption against disenfranchising the majority. That determination is incorrect for several reasons. *First*, the presumption against disenfranchisement is a contract construction tool to be applied to ambiguous contracts. This tool guides a court interpreting an ambiguous contract to choose a reading that does not disenfranchise the majority of stockholders. *Rohe*, 2000 WL 1038190, at *16 ("[O]ur courts rightly hesitate to construe a contract as disabling a majority of a corporate electorate from changing the board of directors unless that reading of the contract is certain and

[6]It is well-established Delaware law that a Court must not turn to extrinsic evidence to derive the intent of the parties if the language of a voting agreement is unambiguous. *See Chandler v. Ciccoricco*, 2003 WL 21040185, at *14 (Del. Ch. May 5, 2013); *see also Demetree v. Commonwealth Trust Co.*, 1996 WL 494910, at *4 (Del. Ch. Aug. 27, 1996) ("[I]f a contract is clear on its face, the Court should rely solely on the clear, literal meaning of the words.)."

unambiguous."); *Rainbow Navigation, Inc. v. Yonge*, 15 Del. J. Corp. L. 196, 204 (1989) ("A court ought not to resolve doubts in favor of disenfranchisement."). It is inapplicable where "[a] plain reading by a third party" supports one reading of the contract.

*Second*, Section 1.2(b) does not impermissibly disenfranchise the majority. As the Trial Court noted in the Opinion, "in the absence of the Voting Agreement, Gorman's majority ownership of the Company, even if no other shareholders supported him, would decide the outcome of a board election." Opinion, at *2 (A58). The intent of the Voting Agreement was to "disabl[e] a majority of a corporate electorate from changing the board of directors." *Rohe*, 2000 WL 1038190, at *16. The majority stockholders at the time the Voting Agreement was executed – Gorman, Pallotta, and Fellus – explicitly controlled three directorships if they voted together – the Pallotta Director and the Key Holder Directors. One directorship – the Series A Director – was reserved for the employees. The Series A Director (along with the Pallotta Director and the Key Holder Directors) would designate the three remaining directors – the Industry Directors and the CEO Director – but the employee director could not "veto" the designation of the CEO Director under Section 1.2(d).[7] Pallotta, Gorman, and Fellus, therefore, controlled four of the seven directorships. Allowing the employees, who collectively invested

[7]The employee director could "veto" the designation of the Industry Directors under Section 1.2(e).

$2 million in the Company, to select one out of seven directors hardly disenfranchises the majority stockholders.

3. The Trial Court's Reading of Section 1.4(a) Is Contrary To The Plain Language Of Section 1.4(a) And Is Internally Inconsistent With The Remainder Of The Opinion

The Trial Court read Section 1.4(a) to permit Gorman, as the holder of the majority of shares held by Key Holders, to remove Key Holder Directors. This interpretation is erroneous for four reasons. *First*, the Trial Court's interpretation of Section 1.4(a) is contrary to the plain language of the Voting Agreement. Section 1.4(a) contemplates that directors will be removed either by "Persons" entitled to nominate the directors or by "shares" entitled to nominate the directors. Simply stated, if the director is nominated by "Persons," then the director may be removed only by these "Persons"; if the director is nominated by "shares," then the director may be removed only by those "shares." Section 1.2(c) identifies the "Persons" entitled to nominate the Key Holder Designees (the Key Holders: Gorman, Fellus, and Halder) without reference to the shares held by Key Holders. Under the plain language of Section 1.4(a), the Key Holders, as the "Persons" entitled to nominate Key Holder Designees, are the only "Persons" entitled to remove Key Holder Directors. The Trial Court erroneously found that the Key Holder Directors may be removed by the vote of the majority of shares held by Key Holders, contrary to the plain language of Section 1.4(a).

*Second*, the Trial Court's application of Section 1.4(a) to Sections 1.2(c) and 1.2(e) is internally inconsistent. Similar to the Key Holder provision of Section 1.2(c), Section 1.2(e) identifies the "Persons" entitled to nominate the Industry Designees. Specifically, under Section 1.2(e), the Industry Designees are nominated by the Series A Director, the Pallotta Director, and the Key Holder Directors. In stark contrast to the Trial Court's conclusion with respect to removal of Key Holder Directors, the Trial Court (correctly) found that the Industry Directors only may be removed by the "Persons" entitled to nominate the Industry Designees. Section 1.4(a) should be applied consistently to Sections 1.2(c) and 1.2(e). Both Section 1.2(c) and Section 1.2(e) identify natural persons entitled to nominate directors. Further, neither Section 1.2(c) nor Section 1.2(e) requires those natural persons to be stockholders. Although the Key Holders currently are stockholders, their designation as Key Holders is independent of their status as stockholders. Similarly, the "Persons" entitled to nominate the Industry Designees (the Series A Director, the Pallotta Director, and the Key Holder Directors) need not be stockholders, and, in fact, the Pallotta Director (Monaco) was not a stockholder. The Trial Court inconsistently applied Section 1.4(a), and such inconsistency should be reversed.

*Third*, the Trial Court's interpretation ignores the important distinction between the word "Persons" and the term "a majority of shares," which is critical

to the Voting Agreement. Section 1.4(a), like Sections 1.2(b) and 1.2(c), reflects the Voting Agreement's distinction between a decision to be made by "Persons" and a decision to be made by "a majority of shares." Holding that the Key Holder Directors may be removed by a majority of shares held by the Key Holders (rather than by the Key Holders) disregards this critical distinction.

*Fourth*, the Trial Court's reading leads to an absurd result. If the Key Holders need not be stockholders, if the Key Holder Directors may be removed only by a majority of shares among the Key Holders, and if none of the Key Holders are stockholders, then the Key Holder Directors never may be removed. This simply is not supported by the language and intent of the Voting Agreement.

### C. Defendants' Reading Gives Effect To All Provisions Of The Voting Agreement

Defendants' reading of the Voting Agreement is the only reading that balances the competing interests of the parties to the Voting Agreement in a manner that comports with the language of the agreement, common sense, and Delaware law. Defendants argued that four primary groups invested in the Company, and, thus, those four groups negotiated and executed the Voting Agreement. The employees (lead by Halder) collectively invested approximately $2 million in consideration for a collective 81 shares of Series A Stock and the right to nominate the Series A Designee. Pallotta invested $2 million in consideration for 80 shares of Series A Stock and the right to nominate the Pallotta

Designee. Gorman invested $1.8 million in consideration for 72 shares of Series A Stock and the right to nominate (along with Halder and Fellus, as the Key Holders) the Key Holder Designees. Fellus invested $600,000 in cash and a $1 million note in consideration for 64 shares of Series A Stock and the right to nominate (along with Gorman and Halder, as the Key Holders) the Key Holder Designees.

Defendants also argued that the selection of the Key Holders under Section 1.2(c) reflects the parties' understanding that (a) the Westech Triumvirate – Halder, Gorman, and Fellus – would together manage and control the Company, and (b) the employees would have greater involvement in the management of the Company through their representative, Halder. In sum, the purpose of the Voting Agreement was to protect employees from Gorman, and the interpretation of the Voting Agreement offered by Defendants is the only interpretation of the Voting Agreement that acknowledges such purpose. Absent such interpretation by this Court, Gorman controls the Board, the employees have no representation on the Board, the employees have no involvement in the management of the Company, and the employees have no protection from Gorman.

## II. GORMAN'S INTERPRETATION OF SECTION 7.17 SHOULD BE REJECTED BECAUSE SUCH INTERPRETATION RENDERS THE SECTION UNNECESSARY AND MEANINGLESS

Section 7.17 is not a complicated contractual provision. Simply stated, it means what it says: "All Shares held or acquired by an Investor and/or its Affiliates shall be aggregated together for the purpose of determining the availability of any rights under this Agreement, and such Affiliated persons may apportion such rights as among themselves in any manner they deem appropriate." Voting Agreement at § 7.17 (A550).

Gorman's argument with respect to Section 7.17 intentionally is obtuse and disingenuous. Gorman argues that "[a]ffiliated shareholdings cannot simultaneously be aggregated yet separately apportioned for purposes of satisfying the independent holder requirement" advanced by Defendants. An. Br. at 43. This neither is the language of Section 7.17, nor is Defendants' argument. Rather, Section 7.17 provides that shares held by an investor and the investor's affiliates are aggregated for the purposes of determining rights available to the investor under the Voting Agreement, and the rights of that particular investor may be apportioned among the investor's affiliates as the investor deems appropriate. Voting Agreement at § 7.17 (A550). In other words, pursuant to Section 7.17, stockholdings of all affiliates are aggregated and resultant rights are apportioned among affiliates; it is not, as Gorman misapprehends, that stockholdings are

"simultaneously [] aggregated yet separately apportioned[.]" Despite Gorman's attempt to sweep Section 7.17 away, Section 7.17 is significant because it reveals the shortcomings in Gorman's interpretation of the term "holder" in Section 1.2(b).

As the Trial Court recognized during a hearing, under Gorman's incorrect reading of Section 1.2(b), "Mr. Gorman could create hundreds of companies that I assume would qualify as affiliates of his for transfer purposes and transfer one share each to his affiliates, and thus, each of them would be another holder and all of a sudden, he'd have a lot more holders." Trans. of Hr'g, 35:7-12 (A35). Section 7.17 prevents this kind of gamesmanship by aggregating the shares held by an investor and his affiliates. Accordingly, if Gorman transferred his shares to multiple Gorman-controlled entities (as Gorman suggests), then under Section 7.17 Gorman and his affiliates would count as only one "holder" for the purposes of Section 1.2(b).

Aggregation under Section 7.17 preserves the intent of Section 1.2(b). The investors intended Section 1.2(b) "to be one of the checks on Mr. Gorman's ability to stack the Board . . . ." Halder Dep., 56:9-11 (A853). "[E]ach person who holds Series A Stock . . . gets one vote for the purposes of designating the Series A Designee, regardless of how many shares of Series A Stock or common stock that person holds. The candidate who receives a majority of the votes from the Series A holders becomes the Series A designee." Zimmerman Aff., ¶ 12 (AR152); Clark

Aff., ¶ 10 (AR156-57); Halder Aff., ¶ 12 (AR162). Most of the Series A holders are key employees, and, thus, Section 1.2(b) was intended to provide the employees with the ability to nominate a director for election to the Board. By aggregating the shares held by each affiliated Series A holder, Section 7.17 ensures that each employee's vote would count equally with the larger investors, such as Gorman, with respect to nominating the Series A Designee.

Only two provisions of the Voting Agreement (Sections 1.2(b) and 4.4) mention "holders" rather than "shares" such that aggregation of shares under Section 7.17 may apply. Section 4.4 provides that "[n]o Investor shall be a party to any Stock Sale unless all holders of Series A Preferred Stock are allowed to participate in such transaction . . ." Voting Agreement at § 4.4 (A550). Unlike Section 1.2(b), Section 4.4 does not require a decision by the "holders," and so the aggregation of shares under Section 7.17 does not impact the holders' rights under Section 4.4. Section 1.2(b), therefore, is the only section of the Voting Agreement to which Section 7.17 applies, and Gorman's "reading" of the Voting Agreement would make Section 7.17 unnecessary and meaningless.

Gorman argues that Section 1.2(a), Section 4.2 and Section 7.8 of the Voting Agreement are impacted by Section 7.17, and, thus, Section 7.17 is not rendered unnecessary and meaningless by Gorman's proffered reading of this provision of the Voting Agreement. Gorman's argument fails for two reasons. *First*, Gorman

argues that Section 7.17 enables Pallotta, who is required to hold ten percent of the Series A Preferred in order to maintain his right to nominate a director pursuant to Section 1.2(a), to hold his shares through any number of affiliates and to aggregate those holdings in order to satisfy the ten percent threshold. Section 1.2(a) addresses this issue directly, however, as Section 1.2(a) *itself* includes as a part of the ten percent threshold that stock held by "Pallotta or his Affiliates." Voting Agreement at § 1.2(a) (A550). In other words, the aggregation effect already is contained within Section 1.2(a), without need to refer to Section 7.17. *Second*, Sections 4.2 and 7.8 are addressed to "shares" rather than "holders," and so Section 7.17 has no application to either Section 4.2 or Section 7.8.

Defendants' reading of Section 1.2(b) provides the only reasonable, lawful, and effective interpretation of Section 7.17 because it is the only reading that gives effect to Section 7.17. [8] In contrast, Gorman's reading of Section 1.2(b) renders Section 7.17 unnecessary and meaningless. Accordingly, reading Section 1.2(b) and Section 7.17 together demonstrates that the only reasonable interpretation of the word "holders" in Section 1.2(b) is that the Series A Designee is nominated by a per capita vote of the Series A holders.

[8]Under Delaware law, all provisions of a contract must be given meaning. *Segovia v. Equities First Holdings, LLC*, 2008 WL 2251218, at *9 (Del. Super. Ct. May 30, 2008) ("[T]he Court must view the contracts as a whole and interpret them in a manner that gives 'a reasonable, lawful, and effective meaning to all the terms.'").

## III. THE TRIAL COURT CORRECTLY HELD THAT THE VOTING AGREEMENT AS DRAFTED, AND AS INTERPRETED BY DEFENDANTS, IS CONSISTENT WITH SECTION 212 OF THE DGCL AND COMPORTS WITH SECTION 218 OF THE DGCL

### A. Question Presented

Did the Trial Court err in holding that neither Section 1.2(b) nor Section 1.2(c) violates Section 212 of the DGCL?

### B. Scope of Review

This Court reviews conclusions of law *de novo*. *Stegemeier v. Magness,* 728 A.2d 557, 561 (Del. 1999).

### C. Merits of Argument

Section 212(a) of the DGCL provides that "[u]nless otherwise provided in the certificate of incorporation . . . each stockholder shall be entitled to 1 vote for each share of capital stock held by such stockholder." 8 *Del. C.* § 212(a). Section 212(a) reflects the concern of Delaware law regarding transactions that create a misalignment between voting interest and economic interest. *See Kurz v. Holbrook*, 989 A.2d 140, 179 (Del. Ch.) ("[c]oncern about the underlying economic interests of stockholders can be seen in multiple strands of our law," which includes "the default rule of one share, one vote" codified in Section 212(a)), *aff'd in part, rev'd in part on other grounds, Crown Emak Partners, LLC v. Kurz*, 992 A.2d 377 (Del. 2010); *In re IXC Commc'ns, Inc. S'holders Litig.,* 1999 WL 1009174, at *8 (Del. Ch. Oct. 27, 1999) ("[g]enerally speaking, courts

closely scrutinize vote-buying because a shareholder who divorces property interest from voting interest[] fails to serve the 'community of interest' among all shareholders, since the 'bought' shareholder votes may not reflect rational, economic self-interest arguably common to all shareholders").

Although Section 212(a) codified the "one share/one vote" rule, Section 212(a) does not prohibit stockholders from agreeing upon the manner in which such shares will be voted. Indeed, Section 218(c) of the DGCL provides:

> An agreement between 2 or more stockholders, if in writing and signed by the parties thereto, may provide that in exercising any voting rights, the shares held by them *shall be voted* as provided by the agreement, or as the parties may agree, or as determined in accordance with a procedure agreed upon by them.

8 *Del. C.* § 218(c) (emphasis added); *see also Dweck v. Nassar*, 2005 WL 5756499, at *4 (Del. Ch. Nov. 23, 2005) ("Section 218(c) recognizes the validity of a voting agreement between any two or more stockholders").

Although each share of capital stock must have no more or no less than one vote per share (absent a provision in the certificate of incorporation that provides otherwise), the holders of such capital stock may enter into an agreement that obligates the stockholders to vote their stock in a manner that guarantees the election of particular individuals to a board of directors. As recognized by the Court of Chancery, stockholders may obligate themselves contractually to vote in favor of a particular individual to serve as a director, and such contractual

obligation will be respected except in extremely limited circumstances. *Rohe*, 2000 WL 1038190, at *16 n.50. Similarly, in *Carter v. Pearlman*, 1998 WL 326605 (Del. Ch. June 12, 1998), the Court of Chancery was presented with a voting agreement in which the stockholders agreed as follows:

> The Corporation's Board of Directors shall consist of six (6) individuals. Each Stockholder, for so long as he shall own at least 5% of the outstanding Common Stock, shall have the right to nominate himself to be a director. Each stockholder, for so long as he remains a stockholder of the Corporation, agrees to vote the shares of Common Stock owned by such Stockholder to elect the nominees of the other Stockholders.

*Id.* at *1. In that action, neither party challenged, and the Court of Chancery was not troubled by, the provisions of the voting agreement that permitted stockholders *to nominate* themselves and that obligated the stockholders that were parties to the voting agreement *to vote for (and, thus, to elect)* the nominated individuals to serve as directors. *See id.* at *2.

Contrary to the position asserted by Gorman, neither Defendants' interpretation of Section 1.2(b) of the Voting Agreement, nor the Trial Court's interpretation of Section 1.2(c) of the Voting Agreement, violates Section 212(a). It is unambiguous from the language of the Voting Agreement that the parties established a two-step process in connection with the nomination and the election of directors. The first step is the nomination process in which (a) "the majority of the holders of the Series A Preferred Stock" will designate one person to be a

nominee under Section 1.2(b), and (b) a majority of the "Key Holders" will elect two persons to be nominees under Section 1.2(c).[9] The second step is the election of the nominees by the stockholders to the Board. The nominees are designated – in the first step – under the provisions of the Voting Agreement, which is permitted under Section 218(c), and the nominees are elected – in the second step – in a manner consistent with the "one share/one vote" rule, which is consistent with Section 212(a).

Gorman argues that the nomination process and the election process are governed by the same set of rules; specifically, Gorman argues that although the election process mandated by the Voting Agreement comports with Section 212(a), the nomination process mandated by the Voting Agreement violates Section 212(a). If the Voting Agreement provided for "per capita" voting, *see Sagusa, Inc. v. Magellan Petro. Corp.*, 1993 WL 512487, at *2 (Del. Ch. Dec. 1, 1993), or "scaled voting," *see Providence & Worcester Co. v. Baker*, 378 A.2d 121, 124 (Del. 1977), in connection with the *election* of nominees to the Board without supporting provisions in the Company's Certificate of Incorporation ("Charter"), then Gorman's argument may have some merit. The Voting Agreement, however, does not provide for "per capita" voting or "scaled voting" in connection with the

[9]As stated above and in Defendants' Opening Brief, there are three "Key Holders" – Messrs. Halder, Fellus, and Gorman – and a majority of the "Key Holders" has the power and the authority to designate two persons to be nominees. *See* Halder Dep., 77:24-78:7 (A874); Fellus Dep., 29:12-15, 141:21-142:4 (A1023, 1032); Monaco Dep., 31:23-32:8, 40:24-41:3 (A678, 790).

elections of nominees to the Board; rather, the Voting Agreement provides (a) for per capita voting (a majority of holders of Series A Stock) for the designation of a *nominee* under Section 1.2(b), and (b) for per capita voting (the majority vote of the Key Holders) for the designation of two *nominees* under Section 1.2(c), and these nominees then are *elected* to the Board by a vote of the stockholders consistent with the "one share/one vote" rule and the Charter. To adopt Gorman's argument would require this Court to ignore the distinction between the nomination process and the election process established in the Voting Agreement.

The Voting Agreement does not misalign voting interest and economic interest (which is the primary concern of Section 212(a)), and the stockholders that are parties to the Voting Agreement (a) contractually agreed to a nomination process under Section 1.2(b) and Section 1.2(c) that permits per capita voting for the designation of nominees, and (b) contractually agreed to vote their stock for the nominees determined under Section 1.2(b) and Section 1.2(c) in a manner consistent with the "one share/one vote" rule and the Charter. There simply is no merit to the assertion that the Voting Agreement violated Section 212(a), and to hold that a violation does exist would invalidate the vast majority of stockholder agreements entered by stockholders of Delaware corporations in which the stockholders adopt a two-step process – a nomination process and an election process – similar to the process established in the Voting Agreement. Indeed, such

a holding would violate Delaware public policy, which permits stockholders under Section 218(c) to "'exercise wide liberality of judgment in the matter of voting.'" *Schreiber v. Carney*, 447 A.2d 17, 24 (Del. Ch. 1982) (quoting *Ringling Bros.-Barnum & Bailey Combined Shows, Inc. v. Ringling*, 53 A.2d 441, 447 (Del. 1947)).

To further highlight the flaws in Gorman's position, during a hearing before the Trial Court, Gorman's counsel did not have a clear response – and certainly did not have a good response – to a simple question asked by the Trial Court. Specifically, the Trial Court asked Gorman's counsel the following question, and the response of Gorman's counsel was confused and confusing:

> THE COURT: Wait. Before you go there, I had a question. It's for you. You have an investment club. A bunch of people get together, put their money together and they go out and buy ten shares of DuPont. They sit around the table and say, well, so and so is running for the board of directors, we're going to vote for him, we're not going to vote for him. And they vote ten to six in favor of Charlie.
>
> Is that prohibited by law because it's not in the DuPont charter because it is a per capita decision to vote the shares?
>
> * * *
>
> MR. BRAUERMAN: Well, for a number of reasons. The first is they're not an investment club. Second, in your example, the DuPont stockholder who has rights that would be subject to 212 is the investment club itself. So you're not looking at the DuPont level for the 212 issue. You have to – let's make them a corporation, not an LLC. So you have to look at it at the investment club level. The investment club level doesn't implicate 212 either so long as they're voting pursuant to their holdings. So if their ten members of the – or in Your Honor's example, 16 members – I work better with round

> numbers, so maybe I'll amend it. I know you're not supposed to amend hypotheticals, but 16 is really going to test my math skills.
>
> * * *
>
> MR. BRAUERMAN: We'll go with 16. But if there are 16 holders, 16 members or stockholders of the investment club, and they each hold the same amount of stock, and they each get the same number of voting, then there's nothing wrong. We haven't implicated 212. *If, at the investment club level, you give two of those stockholders who own 80 percent of the shares the same amount of voting power as the other 14 – I told you math was tough, the other 14 who own collectively 20 percent, and you give them each one vote, then you do have a 212 problem. But that's not a 212 problem at the DuPont level. That's a 212 problem at the investment club level.* And that's exactly what we have here. We have a situation where you have disparate holders getting the same voting power, and 212 prohibits that unless it's in the charter. That same problem would occur in the investment club but not at the DuPont level because the DuPont stockholder would be the investment club, and the investment club would be permitted to vote however the investment club, as a collective, was able to vote. DuPont wouldn't care how the investment club got there.

Trans. of Hr'g, 71:16-74:18 (AR71-74).

Counsel's strained answer misses the point. The issue is whether a stockholder vote is required, and if a stockholder vote is required, then the "one share/one vote" rule is applicable. The nomination of individuals to be elected directors by the stockholders does not involve a stockholder vote, and, thus, does not implicate Section 212, which is the point of the Trial Court's hypothetical. Indeed, absent an agreement that provides otherwise, directors typically *nominate* individuals to be elected directors by the stockholders, and such nomination process usually involves per capita voting by the directors. The election of individuals to serve as directors, however, does involve a stockholder vote, and,

thus, does implicate Section 212(a). Simply stated, and as highlighted by the Trial Court's hypothetical, the nomination process mandated by the Voting Agreement is not governed by (and, thus, does not violate) Section 212(a), and the election process mandated by the Voting Agreement is consistent with Section 212(a).

In sum, Gorman's assertion of a violation of Section 212 is an attempt to convince this Court to "rescue" him from an enforceable agreement that Gorman (and his counsel) negotiated over a long period of time, that Gorman executed and agreed to honor, but that Gorman no longer wants to honor. Gorman is inviting this Court, as a matter of judicial legislation, to invalidate the Voting Agreement under Section 212(a) because the Voting Agreement permits per capita voting in the nomination – but not the election – process. Section 212(a) simply does not create such a limitation in connection with the nomination process, and, thus, Gorman's invitation to invalidate the Voting Agreement should be declined by this Court. "Sophisticated market participants" should be forced to honor their agreements, and the General Assembly (rather than Delaware courts) should enact public policy limitations regarding voting agreements and the nomination process:

> I see no reason why this court should, as a matter of judicial legislation, promulgate public policy to rescue sophisticated market participants who make a knowing choice to enter such a contract. The General Assembly knows how to enact public policy limitations . . . when it so wishes. It has not chosen to do so in this area and I respect its judgment to leave these decisions to the contracting parties.

*Agranoff v. Miller*, 1999 WL 219650, at *17 (Del. Ch. Apr. 12, 1999) (citation

omitted).

## CONCLUSION

For the foregoing reasons, and the reasons set forth in the Opening Brief of Defendants, the Opinion and the Final Order of the Trial Court should be reversed with respect to the interpretation of Section 1.2(b), Section 1.2(c), the application of Section 1.4(a) to Section 1.2(c), and the interpretation of Section 7.17.

GREENBERG TRAURIG, LLP

*/s/ Michael J. Maimone*
Michael J. Maimone (#3592)
Gregory E. Stuhlman (#4765)
E. Chaney Hall (#5491)
1007 North Orange Street, Suite 1200
Wilmington, DE 19801
(302) 661-7000

Attorneys for Defendants Below,
Appellants/Cross Appellees

Dated: September 5, 2014

*DEL 86501931v5*

CERTIFICATE OF SERVICE

I hereby certify that on September 5, 2014 the foregoing APPELLANTS' REPLY BRIEF ON APPEAL AND CROSS-APPELLEES' ANSWERING BRIEF ON CROSS-APPEAL was caused to be electronically served upon the following counsel of record:

Neil B. Glassman, Esq.
Stephen B. Brauerman, Esq.
Vanessa R. Tiradentes, Esq.
Bayard, P.A.
222 Delaware Avenue, Suite 900
P.O. Box 25130
Wilmington, Delaware 19899

*/s/ Michael J. Maimone*
Michael J. Maimone (I.D. No. 3592)