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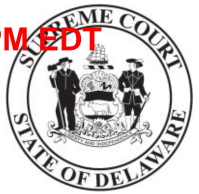

IN THE SUPREME COURT OF THE STATE OF DELAWARE

SANDRA MANNO and MANNO ENTERPRISES LLC, Defendants-Counterclaim Plaintiffs below, Appellants, v. CANCAN DEVELOPMENT, LLC, ROBERT A. GRANIERI, ROBERT J. GRANIERI and GEORGE TOTH, Plaintiffs-Counterclaim Defendants below, Appellees.	)	No. 378, 2015D On Appeal from C.A. No. 6429-VCL in the Court of Chancery of the State of Delaware

APPELLEES' ANSWERING BRIEF

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NATURE OF PROCEEDINGS[1]

Sandra Manno and Manno Enterprises, LLC have separately appealed from the Court of Chancery's post-trial opinion and judgment in this case. The Court of Chancery issued that opinion after hearing three-and-a-half days of revealing testimony, and after wading through many hundreds of documents. As can be seen from the opinion, the Court of Chancery based its decision on the (often colorful) facts and its judgments on credibility, and found largely for the Plaintiffs-Counterclaim Defendants below.

Defendants-Counterclaim Plaintiffs below appealed, but the arguments they make here demonstrate the burden they face. Defendants object to the Court of Chancery's liability conclusions—conclusions that by their nature rely on both law and fact—and endeavor to transform them into claimed mistakes of law. This attempt at legal alchemy fails, though, because the Vice Chancellor's conclusions were not based upon any misunderstanding of the law. Rather, the Court of Chancery took normal principles of equity and applied them to the particular facts of this case. There is nothing extraordinary or out of place about any of the Court's legal holdings, while its findings of fact were supported both by the overwhelming evidence before it and its specific findings on the relative credibility

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[1] Unless otherwise noted, the definitions used by the Court of Chancery in its opinion are used herein. In addition, Manno Enterprises' Opening Brief is cited as "EOB," and Manno's Opening Brief is cited as "MOB."

of the witnesses.

Manno Enterprises LLC, which was wholly owned by Sandra Manno until just before this case was filed in 2011, and apparently came under new management (with separate counsel) after the opinion was issued, misunderstands the burden it faces in its appeal. For example, when presenting its second argument it insists that "entire fairness review" is the applicable scope of review here on appeal, thus confusing the legal standard below and the scope of review on appeal.

Moreover, and at least as significantly, Manno Enterprises fails to grapple sufficiently with the Court of Chancery's factual findings and the factual record before that Court. The soundbite version of its argument is that RG Junior diverted a corporate opportunity from CanCan Development, LLC because he was "paranoid" and greedy, and that the Court of Chancery inexplicably failed to apply the corporate opportunity doctrine or the entire fairness standard against him. In making that argument, however, Manno Enterprises fails to mention, much less discuss, the most important of the surrounding facts.

Specifically, Manno Enterprises overlooks that immediately after Manno was fired by CanCan in March 2011, she and Manno Enterprises took the position that she personally owned most of CanCan's important property, leaving it with little of value. In a complaint filed in New Jersey, and then in counterclaims filed

in this action and maintained at least up to trial, Manno and Manno Enterprises claimed that she personally owned all of CanCan's intellectual property and CanCan's subsidiaries. Those subsidiaries in turn held the options to buy the key parcels of property for the project, including the "Church Property."

Those claims to ownership were utter nonsense. CanCan, using RG Junior's money, had paid for everything and Manno had specifically approved the filing of paperwork showing that both the subsidiaries and the intellectual property were owned by CanCan Development and not by her. Yet, Manno and Manno Enterprises refused to withdraw those claims until trial, and her new business partner, David Flaum, who now directs Manno Enterprises, bought his interest with the direct knowledge that she claimed to own those assets.

Manno Enterprises mentions none of that in its brief, but it is those assertions of ownership that caused RG Junior to take the actions he did. Like any sensible person, he was not going to put millions into CanCan to exercise the options and buy the Church Property when Manno and Manno Enterprises were seeking a judgment that Manno and not CanCan owned the options.

RG Junior thus bought the land through a new entity. Then, in keeping with his fiduciary duty, he offered to let CanCan buy the land at his cost if Manno (and her partner, Flaum) put up their own share of the money to finish the project. As the Vice Chancellor found, RG Junior made the offer on the assumption that if

Manno and Flaum actually put in some money of their own (Flaum, a very successful real-estate developer, could easily have done so), they would have had a powerful incentive to stop making false claims that placed a cloud on CanCan's title. They rejected that course of conduct, though, and instead argued that: (1) RG Junior had a fiduciary duty to invest millions in CanCan in order to buy the Church Property; but (2) CanCan did not own the subsidiaries that held the options to buy the Church Property. Neither Manno nor Manno Enterprises has ever been able to justify how they could take such flatly contradictory positions.

None of that is mentioned in Manno Enterprises' brief, but it provides the factual background for the Vice Chancellor's decision. Perhaps Manno Enterprises omitted those facts because it intends to save any discussion of them for its reply, but that would be impermissible under Supreme Court Rule 14(c). Whatever the reason for the omission, it is critical because—as this Court has stressed so often in the past—equity is deeply contextual and is dependent on an in-depth understanding of the facts. Ignoring them does not make them disappear.

Nor does Manno's brief fare any better. Her main argument is that the Court of Chancery should have concluded that her business partner, Joe Py, was independent, and since Py approved Manno's spending it should have been upheld under the business judgment rule. That argument has factual holes. There was no showing, for example, that Py was aware that Manno was personally pocketing

CanCan cash. Nor was there any proof that Py knew that she was spending large sums of CanCan's money on her other business ventures.

Moreover, the Court of Chancery's conclusion that Py was not independent but was complicit with Manno was supported by the evidence. Py and Manno were long-time partners whose business dealings went back years. Manno insists that Py was a family friend of the Granieris. That is correct—that is how he was able to convince them to invest in the Project. But after hearing the evidence, the Vice Chancellor concluded that "Py and Manno's relationship was sufficiently close that Py cannot be regarded as independent." May 27, 2015 Memorandum Opinion ("Op.") 37. That conclusion was amply supported by the record.

In the end, both appeals purport to challenge the trial Court's legal conclusions, but in fact attack its factual findings, and those findings are fully supported by the record. The judgment below should be affirmed.

SUMMARY OF ARGUMENT

A. Manno Enterprises' Arguments

1. Denied. The Court of Chancery correctly held as a matter of fact that CanCan was financially incapable of purchasing the Church Property given that CanCan lacked its own resources (which Manno Enterprises admits) and could not raise from third parties the funds needed to pursue the opportunity.

2. Denied. The Court of Chancery correctly found that RG Junior carried the "heavy burden" to show that the dissolution of CanCan was entirely fair to Manno Enterprises. The Court of Chancery found that Plaintiffs-Counterclaim Defendants proved that Manno Enterprises' interest in CanCan had no value at the time CanCan was dissolved because CanCan's value did not exceed the Granieris' liquidation preference. In addition, it specifically found that the price paid for CanCan's assets "was at least fair and likely excessive." Op. 60.

3. Denied. Plaintiffs-Counterclaim Defendants proved to the Court of Chancery's satisfaction that the capital calls that diluted Manno Enterprises' interest in CanCan were entirely fair. The capital calls "were necessary for CanCan to avoid immediate failure, made at a time when financing on comparable terms was not available from the market, priced comparably to similar transactions to which Manno [Enterprises] had agreed, and valued CanCan well in excess of what it was actually worth." Op. 57. Moreover, Manno Enterprises was given the

opportunity to participate on equal terms in the calls in order to preserve its membership stake (or increase its stake even if the calls were not fully subscribed), yet chose not to do so. Under all of the circumstances considered by the Court of Chancery, the capital calls were entirely fair.

B. Manno's Argument

1. Denied. The Court of Chancery correctly held that Manno breached her fiduciary duty of loyalty by extracting undeserved compensation from CanCan and through other forms of disloyal and wasteful spending. Py's check-signing authority does not serve to insulate Manno's actions because the Court of Chancery found that Py did not exercise any business judgment in signing checks and was not independent of Manno in any event given their previous business dealings. In addition, Py was not under the control of Plaintiffs-Counterclaim Defendants such that there is any adverse inference to be garnered from his failure to testify. Plaintiffs-Counterclaim Defendants attempted to take testimony from Py, but were informed by his attorney that he was elderly and unwell due to recent brain surgery. The Court of Chancery's findings are all supported by the record and Manno was properly found liable to CanCan for $970,123 for her breaches.

STATEMENT OF FACTS

The following is a concise summary of the detailed factual statement set forth in the Court of Chancery's opinion.

A. The Granieris Invest and Manno Starts Spending.

Sandra Manno and Joseph Py were co-managers of CanCan until their mismanagement and wrongdoing were discovered by the Granieris and they were fired. Py and Manno are longtime business partners having tried (and failed) to develop several other projects together. Op. 5. Py brought the Granieris into the Project with RG Junior providing $2 million for a 32% interest in CanCan and his father providing $30,000 for a 10% interest. *Id.* at 6-7.

Once those funds were in place, Manno started spending. First, Manno began taking a salary and covering all of her expenses except for items that were obviously personal. *Id.* at 9. RG Junior understood she was taking $10,000 a month, but it later turned out that Manno was taking far greater amounts. Second, Manno was worried about her financial security (she wrote to Py that she wanted "to arrange for some cash . . . [to] put away in a lock box here to feel secure"), so she started using the Company's debit card to make cash withdraws from ATMs, withdrawing $97,999.50 between September 2009 and March 2011.[2] *Id.* at 14-16.

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[2] During this same period, Manno made frequent cash withdrawals from her personal accounts too taking out over $132,000 from her Manno Enterprises account (from money deposited by CanCan) and $62,000 from her bank account. Manno withdrew over $285,000 in cash while

Next, Manno hired her brother, Joey Manno, at $30,000 per month as President of the Casino Sub, and hired her sister, Patty Manno, at $5,000 per month.[3] *Id.* at 8, 12. Manno made some other colorful hires, including her longtime friend Lisa Marie Ponzio (who had been working as a part-time hairdresser), and Frank Barbera, aka "Frankie the Fish," a New Jersey "real-estate consultant" who had been convicted two years earlier for paying cash bribes to the president of the Atlantic City Council. *Id.* at 13-14.

Manno also began spending freely on meals and entertainment, with CanCan racking up $142,411.69 in expenses from September 2009 through April 2011. For example, Manno spent $401.85 on a brunch with Patty while taking her to the airport. *Id.* at 16-17. CanCan paid $60,449 for flights with no business purpose (*e.g.*, first-class flights for Ponzio to fly down from Philadelphia) and spent $18,180 on limousines. *Id.* at 17. CanCan also incurred $41,448 in hotel charges without any documented business purpose. The expenses often came from people working on, or associated with, Manno's non-CanCan projects. *Id.* at 18.

B. Toth Arrives to Find the Project a Mess.

In July 2010, Manno fired her brother Joey as President. *Id.* She replaced

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managing the Project. Op. 15.

[3] While Patty initially was paid by check, in November 2010, Manno routed Patty's pay to her own personal bank account once CanCan implemented a direct deposit payroll system. Shortly thereafter, Manno gave "Patty" a raise to $7,500 per month. She also made large cash withdrawals shortly after each deposit hit her account. *Id.* at 13.

him in September with George Toth, who the Court found to be "a competent operator, and a credible witness." *Id.* at 18. At the time Toth joined, RG Junior had invested $6.5 million in CanCan yet there was nothing to show for it. In addition, the Project was a mess. *Id.* There were no financial statements, no budgets, no business plans, and no clear reporting structure. Toth instituted weekly operational meetings and began preparing a budget. *Id.* at 18-19.

In the fall of 2010, Toth traveled to New York to meet with potential investors and to speak with investment banks. *Id.* at 19. RG Junior attended these meetings, and it was after speaking with Toth that he became concerned about his investment and started to conduct more due diligence. *Id.* at 20. RG Junior asked for more detailed financial information about the Project, which is when he discovered that Manno was getting paid over twice what he had been told and that CanCan's other expenses were also much higher. *Id.* at 19.

RG Junior commissioned a background check on Manno and the results of that report caused him great concern, particularly the description of Flaum's lawsuit against Manno, which mirrored what RG Junior was experiencing. RG Junior also hired consultants to evaluate the Project, and they started raising red flags. *Id.* at 20.

All during this time, Manno kept insisting that RG Junior provide more financing to keep the Project alive. *Id.* Finally, RG Junior insisted on finishing the

long-discussed operating agreement before he put in more money. *Id.* at 21. On December 20, 2010, the parties executed the Operating Agreement, which contains two key provisions pertinent to this dispute: (1) members were not required to contribute any additional capital; and (2) all capital would be returned before any distribution of profits. A80 §7.3; A81-83. Manno reviewed several drafts of the Operating Agreement with her counsel (who she had CanCan pay) and understood that the draft agreement did not guarantee her any income or returns. Op. 21-22.

C. RG Junior Attempts an Amicable Resolution.

In early 2011, RG Junior decided he needed to either sell his interest in CanCan or terminate Manno. He wanted an amicable resolution, though, given his concern that Manno might use her relationships with the city officials to sabotage the Project if she were unhappy. *Id.* at 24.

His ideal solution was to sell his and his father's interest in CanCan for $10 million. *Id.* While exiting at $10 million would have given them a positive return, RG Junior recognized that finding a buyer was highly unlikely. *Id.* at 25. The next-best alternative was to buy Manno Enterprises out and have Toth take over managing the Project. *Id.* Before broaching that subject, however, RG Junior wanted to obtain supermajority control, which would soon happen given CanCan's cash burn and constant need for funds. *Id.* Once RG Junior held a supermajority, he convened a meeting of members on February 23, 2011, and asked Manno and

Py to resign. RG Junior also offered to sell his interest in CanCan for $10 million. Manno and Py said they would only leave if they were fired. *Id.*

A week later, RG Junior and Manno met in New York and negotiated a settlement. Manno would relinquish her interest in CanCan in exchange for an immediate $30,000, an additional $20,000 upon her resignation as manager, and another $150,000 if she renegotiated the option on the Church Property. RG Junior paid Manno $30,000 as agreed and sent her a settlement agreement. Manno never signed the agreement and never returned the $30,000. *Id.* at 26.

Instead, on March 8, 2010, RG Junior received a letter from a law firm on behalf of Manno claiming that Manno retained ownership of the Project's intellectual property and alleging that RG Junior had breached his fiduciary duties to Manno Enterprises when obtaining a supermajority interest. *Id.* Manno thereafter continued to assert that she owned the IP and also began claiming to own Casino Sub personally, including the option it held on the Church Property.

On March 10, 2011, the Granieris formally removed Manno and Py as managers. After he was fired, Py had his counsel contact RG Junior to say that Py wanted to surrender his entire interest in CanCan to RG Junior for $10 due to Py's feelings of guilt. *Id.*; B386.

D. RG Junior and Toth Try to Move the Project Forward.

Once Toth was installed, he worked to reduce the Company's G&A

expenses to focus cash on the architect, engineers and lawyers needed to move the project forward. B451-53; B460-61. CanCan continued to need monthly infusions of capital in order to operate. RG Junior was not required to contribute additional capital to CanCan, but without any funding, the Company would cease to exist. A80 §7.3; B387-88; B464-65. RG Junior determined, with the help of counsel, to issue capital calls to all members. Op. 27-28; B388-96.

There was an established pattern of RG Junior contributing $200,000 in exchange for 1 point, but in those transactions only Manno Enterprises' and Py's interests had declined in a linear fashion, which seemed unfair to RG Junior given that all members were not diluted. B388-90. Using the Company's short-term cash requirements as compiled by Toth, RG Junior determined how many membership interests should be issued so that any reduction to Manno Enterprises' interest (to the extent Manno Enterprises did not contribute to the call) was a little less than it had been previously dollar for dollar. Op. 28; B390.

On March 16, 2011, RG Junior caused CanCan to make a capital call on its members for $500,000. Manno Enterprises did not supply any capital, RG Senior supplied $50,000, and RG Junior funded the balance. RG Junior followed the same procedure for capital calls of $500,000 on April 28, $1,000,000 on May 26, and $1,000,000 on June 30, 2011. Those times, RG Junior contributed the entire amount when the other members failed to contribute their share. Op. 28.

In addition to funding CanCan's short-term needs, Toth and RG Junior sought permanent financing for CanCan. Op. 30; B401-06. Toth had spent much of his time in New York meeting with various banks and investment bankers during Manno's tenure and continued after she left. B446-48. During those meetings, Toth and RG Junior learned that CanCan lacked important financial budgets, business plans and key management needed to approach investors. Op. 30. But Toth worked to put them in place and then CanCan entered into an agreement with Cantor Fitzgerald & Co. to raise $400 to $450 million through the issuance of debt and equity in order to finance development of the Project. Cantor failed to raise any money. *Id.* Even with a new management team and the assistance of an investment bank, the Project could not be financed.

E. RG Junior Preserves CanCan's Opportunity.

From her removal until two weeks before trial, Manno and Manno Enterprises maintained that Manno owned CanCan's subsidiaries, the Project's intellectual property, and the options to purchase the land for development. *See* B106; B109; B1120; B130; B170-73; B274; B337-42; B315; B317-B322. Those claims made it impossible for CanCan to exercise the option to purchase the Church Property or other needed parcels without risking a cloud on the title that would make financing impossible. The option to acquire the Church Property was set to expire on July 31, 2011, and in order to preserve CanCan's ability to

purchase it, RG Junior structured a transaction, again with the assistance of counsel, that would secure the Church Property, permit him to fund the purchase through a separate entity, and preserve CanCan's opportunity to purchase the Church Property if it could obtain the necessary funding. B410-15.

After Casino Sub's option expired, RG Junior's newly formed entity, Land Holdings I, LLC ("LHI"), bought the Church Property for $5 million—$1 million less than the price Manno negotiated. Op. 29. Immediately after closing, LHI granted CanCan an option to purchase the Church Property at any time before December 31, 2011 for the same $5 million price. *Id.* The five-month option cost CanCan $50,000—less than half what Manno agreed to pay for the original 90-day option on the Church Property. LHI also purchased the other properties surrounding the Church Property for $9.4 million, subject to CanCan's options. *Id.*

F. Manno Enterprises Obtains a Financial Backer.

David Flaum is a prominent Rochester real-estate investor who was previously involved with Manno in the proposed development of various gaming projects until he filed suit against her for breach of fiduciary duty and taking his money. *See* B1-32. They eventually settled that dispute with Manno agreeing to give Flaum 50% of any future gaming endeavor. Op. 31. After Manno was fired from CanCan, she reached out to Flaum about the Project—which she had been hiding from him until then—and he became a 50% owner of Manno Enterprises

with a 20-year option to purchase Manno's remaining interest in Manno Enterprises for $1. *Id.* That option cost Flaum $40,500, thus implying a value of $81,000 for Manno's interest in CanCan and a value of $1.2 million for all of CanCan's equity. *Id.* RG Junior was unaware of Flaum's involvement until he received an email from Flaum "out of the blue" on September 6, 2011 offering to assist in building the Project for no compensation except to retain an 11.5% interest with no right of dilution or cash call. *Id.* at 30-31.

With the knowledge that Manno now had a financial backer for Manno Enterprises in place, and with CanCan out of third-party financing options, RG Junior put together one final opportunity for CanCan to move forward—a $25 million capital call through which RG Junior would contribute his entire interest in LHI to CanCan, including all of the real estate purchased, the rights to the architect's agreement, and any cash held by LHI. *See* A235-53; B415-18. All that was needed to complete the call was for Manno/Flaum to put up Manno Enterprises' *pro rata* share of the offering, which would have cost Flaum only $1,650,015. If Manno/Flaum failed to put up their share, the call would fail and CanCan would be dissolved. *See id.*

G. After the Call Failed, CanCan Was Dissolved.

After Manno/Flaum failed to subscribe to the $25 million offering, RG Junior worked to dissolve CanCan and wind up its affairs by selling assets to LHI

at book value. Op. 33. LHI paid a "generous" price of $1,919,722.81 for office furniture, market research, and engineering studies. *Id.* Given that the Operating Agreement provides for the return of capital before any other distributions to members are made (A82 § 8(i)), any amounts remaining after creditors were paid went to the Granieris given their $11.4 million in capital contributions. Op. 33.

H. The Scarlet Pearl.

After CanCan was dissolved, RG Junior moved forward with LHI to develop a scaled-down project, the Scarlet Pearl casino. The project has a different brand and design, there is no retail shopping center and the number of hotel rooms was reduced from 500 to 300 rooms. Op. 33-34. LHI also obtained all of the necessary government approvals on behalf of the Scarlet Pearl and did not use any approvals gained by CanCan given RG Junior's concerns about Manno's interactions with government officials. Op. 34; B426-27.

LHI started discussing the possibility of financing in January 2012. It engaged Cantor and Jefferies to seek financing, both without success. Op. 34. LHI then negotiated for over a year with Carl Icahn to no avail. *Id.* LHI at last turned to UBS in 2014, which was successful in obtaining $140 million in debt financing at 14%, and still required a total $121 million equity investment by RG Junior plus a $15 million personal completion guarantee. *Id.*; B428-34; B447-48. The Scarlet Pearl is scheduled to open before year-end 2015.

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY FOUND THAT CANCAN WAS FINANCIALLY UNABLE TO UNDERTAKE THE CORPORATE OPPORTUNITY.

A. Question Presented

Whether the Court of Chancery's determination that CanCan was financially unable to purchase the Church Property is clearly erroneous.

B. Standard of Review

Although Manno Enterprises frames its attack on the Court of Chancery's conclusion that there was no usurpation of a corporate opportunity as a legal question, Manno Enterprises really is challenging the Court's factual findings. *See* EOB 14-21. Factual finding are reviewed "with a high level of deference[,]" and "will not be set aside on appeal unless they are clearly wrong and the doing of justice requires their overturn." *Montgomery Cellular Holding Co. v. Dobler*, 880 A.2d 206, 219 (Del. 2005) (footnotes omitted).

C. Merits of the Argument

1. Manno Enterprises Ignores the Full Record Below, Which Supports the Court of Chancery's Finding that No Corporate Opportunity Was Usurped.

"[A] claim that a corporate opportunity has been wrongfully taken is wholly dependent upon the facts presented." *Schreiber v. Bryan*, 396 A.2d 512, 519 (Del. Ch. 1978). Given the nature of the corporate opportunity doctrine it could not be

otherwise. Yet, Manno Enterprises fails to grapple with the full record supporting the Court of Chancery's decision. Instead, Manno Enterprises takes quotes from RG Junior out of context in an attempt to paint him as a "paranoid" and faithless fiduciary who purportedly only purchased the Church Property through LHI in order to thwart CanCan's opportunity. *See* EOB 15-16. The record, however, proves the contrary. As the Court of Chancery specifically found, "[r]ather than harming CanCan," LHI's purchase of the Church Property "left the company in a better position after the transaction." Op. 58.

Manno Enterprises never mentions that, from the time of Manno's removal until (at least) two weeks before trial, Manno and Manno Enterprises maintained under oath that Manno personally owned CanCan's subsidiaries, the intellectual property for the project, and the options to purchase the land for development. *See* B106; B109; B1120; B130; B170-73; B274; B337-42; B315; B317-B322. Despite repeated requests to drop those claims, Manno and Manno Enterprises refused.

Manno's claims to own the subsidiaries put a cloud on CanCan's ability to exercise the options to purchase the land needed for the project such that it would have been impossible to find financing if CanCan did go forward with the purchase. As RG Junior testified:

> Well, my plain concern, and also a concern of my advisors, was that we could have a big problem trying to purchase the land given this allegation was out there. If we had done so -- I don't know how long this litigation would have gone on. Financing probably would have --

> certainly would have been impossible while the question existed as to who owned the land or whether we had purchased it inappropriately. And this was quite devastating.

B409.

RG Junior was also concerned that if he did not buy the property immediately, Flaum would help Manno purchase the Church Property herself, which would prevent CanCan from moving forward. *See* B410-12. It is in this context that RG Junior created a new entity (LHI) to purchase the Church Property; and then gave CanCan an option to purchase it at the same price LHI paid. That then preserved CanCan's ability to move forward. *See id.*

Manno Enterprises takes RG Junior's testimony out of context to claim that he took these actions to preserve his opportunity to purchase the Church Property, but RG Junior credibly testified that he took these steps to preserve CanCan's ability to move forward. *See* B411 ("to preserve CanCan's opportunity"); B414 ("I was very concerned that -- and, again, it may seem paranoid -- that Mr. Flaum might buy a small key piece of those properties, which would prevent CanCan from being able to move forward."); B415 ("we were trying to preserve CanCan's opportunity to go forward with this deal at the same time that we were trying to make sure that we didn't lose control of the land")). The contemporaneous documents support RG Junior's statements and the Court of Chancery's findings.

LHI purchased the Church Property only after CanCan's option expired

(options on other pieces of land continued) and at a $1 million discount to the price negotiated by Manno. B143-68; B411; B468-69. LHI then immediately entered into an option agreement with CanCan permitting it to purchase the Church property from LHI until December 31, 2011 for the same price LHI paid (and at a lower option fee than it previously held), thus potentially saving CanCan $1 million. B133-42; B411-12. This was the first time CanCan had the clear ability to purchase the land since Manno claimed to own the subsidiaries. B468.

Finally, Counterclaim Defendants put together a $25 million capital call through which RG Junior would contribute his interest in LHI to CanCan, including the real estate purchased, the rights to the architect's agreement, and any cash held by LHI. *See* A235-53; B415-18. All that was needed to complete the call was for Manno/Flaum to put up Manno Enterprises' *pro rata* share of the offering, which would have cost Flaum only $1,650,015, a small sum to him. B415-16; B423; A237. If they did not put up their share, the call would fail and CanCan would be dissolved.

Flaum claimed that the offering was a "sham," but the sham was Manno and Manno Enterprises' insistence that Manno owned the options. *See* B345-47. The Court of Chancery found that the offer was real and made in good faith. Op. 59-60. Thus, the Court of Chancery correctly found that RG Junior acted faithfully to preserve CanCan's corporate opportunity.

2. The Court of Chancery Correctly Applied the Law to the Facts.

In order for a corporate opportunity claim to prevail, the company must be "financially able to undertake" the opportunity. *Guth v. Loft, Inc.*, 5 A.2d 503, 511 (Del. 1939); *Odyssey Partners, L.P. v. Fleming Cos., Inc.*, 735 A.2d 386, 412 n.24 (Del. Ch. 1999) (no corporate opportunity if the company lacks financial capacity to undertake it). Whether a company has that financial capacity "is largely a question of fact to be determined from the objective facts and surrounding circumstances existing at the time the opportunity arises." *Borden v. Sinskey*, 530 F.2d 478, 490 (3d Cir. 1976). Here, the Court of Chancery found, based on the facts and circumstances, that: "CanCan lacked the resources to purchase the Church Property. CanCan did not have the money and could not raise it from third parties. RG Junior had no obligation to provide the financing." Op. 57.

That finding is fully supported by the record. It is undisputed that CanCan did not possess the $6 million it needed to purchase the Church Property, and even Manno Enterprises acknowledges, "CanCan <u>always</u> needed additional investments to keep the business going – it at no point generated any revenue of its own." EOB 34 (emphasis in original). Manno Enterprises argues, however, that "a company may depend on financing, loans, or other transactions to take advantage of corporate opportunities…." EOB 17-18. That is true but irrelevant because the Court of Chancery found as a matter of fact that CanCan <u>could not</u> raise funding

from third parties. *Cf. Schreiber*, 396 A.2d at 520 (denying summary judgment because "[i]t is unclear from the present record. . .whether POGO was in fact financially unable to take advantage of the opportunity for expansion"); *Norman v. Elkin*, 617 F. Supp. 2d 303, 313 (D. Del. 2009) (denying summary judgment given genuine issue of fact as to whether the company could raise needed funds).

Here, the Court of Chancery heard how RG Junior asked on multiple occasions to be bought out of CanCan for $10 million. Manno tried to find investors to provide the funds, but never could. B373-74; B447. Next, both Toth and RG Junior sought financing for CanCan from the fall of 2010 onward. *See* B401-06. Toth had spent much of his time in New York meeting with various banks and investment bankers during Manno's tenure and continued after she left. B446-48. During those meetings, Toth and RG Junior learned that CanCan needed audited historical financials, budgets, a business plan, a marketing plan, 85% documented construction drawings, and a guaranteed maximum price from a contractor before funding could be contemplated. Op. 30; B403-05; B446. The banks also wanted a full management team in place, including an owner's representative with construction experience and a CFO. Op. 30; B405; B455-59.

To that end, Toth hired appropriate management and created the necessary financial plans and projections for potential investors. B454-63. With those items checked off, in June 2011, CanCan entered into an agreement with Cantor

Fitzgerald for Cantor to raise $400 to $450 million through the issuance of debt and equity to finance development of the Project. B406-07; B441-42. Cantor went to market, but could not raise the funds. B467-68.

Manno Enterprises finally argues that "[t]he Court's error is obvious – CanCan's financial 'ability' was and is the same as LHI's…." EOB 19. That argument wrongly assumes, however, that RG Junior was obligated to provide financing to CanCan. He was not. A80 §7.3; B362. Nor was there any fiduciary obligation that he put his funds into CanCan instead of LHI. Manno Enterprises' reliance on *Thorpe v. CERBCO, Inc.*, 676 A.2d 436 (Del. 1996), to support this argument is misplaced. In *Thorpe*, there was no corporate opportunity for the company to undertake given the controlling stockholders' right to veto any sale of substantially all of the company's assets. 676 A.2d at 443. The Court found, however, that the controlling stockholders failed to exercise that power within their duty of loyalty because they misrepresented the transaction to the board. *Id.* at 442. By contrast, the Court of Chancery found here that RG Junior acted in a manner that was at all times fair to CanCan, and that put CanCan in a better position than it had been prior to LHI's purchase of the Church Property.

While RG Junior faced a tough burden at trial to establish that CanCan was financially unable to take advantage of the corporate opportunity, the facts overcame that burden, and the Court of Chancery's conclusion should be affirmed.

II. THE DISSOLUTION OF CANCAN AND SALE OF ASSETS WAS ENTIRELY FAIR TO MANNO ENTERPRISES.

A. Question Presented

Whether the Court of Chancery's finding that RG Junior proved the entire fairness of his conduct is clearly erroneous.

B. Standard of Review

In its brief, Manno Enterprises confuses the standard of review on appeal with the standard applicable to the Court of Chancery's review of CanCan's dissolution and sale of its assets. EOB 22. The Court of Chancery's "findings upon application of the duty of loyalty. . ., being 'fact dominated,' are, on appeal, entitled to substantial deference unless clearly erroneous or not the product of a logical and deductive reasoning process." *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993) (citation omitted). Moreover, "[w]hen factual findings are based on determinations regarding the credibility of witnesses. . .the deference already required by the clearly erroneous standard of appellate review is enhanced." *Cede & Co. v. Technicolor, Inc.*, 758 A.2d 485, 491 (Del. 2000).

C. Merits of the Argument

Manno Enterprises argues that the Court of Chancery's determination that the dissolution of CanCan and sale of its assets was entirely fair "erred in its application of the entire fairness standard and reached a fundamentally flawed conclusion." EOB 22. As with its challenge to the Court of Chancery's corporate

opportunity conclusion, Manno Enterprises fails to address the full factual record surrounding the Vice Chancellor's determination. For example, Manno Enterprises asserts that "it is uncontested that RG Junior was motivated by animosity towards Ms. Manno and 'paranoia' about Mr. David Flaum[.]" EOB 23. That assertion, though, is flatly contradicted by the record and fails to address the disabling effect of Manno and Manno Enterprises' claims that Manno personally owned CanCan's subsidiaries and options. *See* Section I(C)(1), *supra*. Far from being "uncontested that RG Junior was motivated by animosity towards Ms. Manno," he testified credibly that he understood that he owed fiduciary duties to Manno Enterprises even though he was frustrated with Manno personally.[4] B386-87. The Court of Chancery found that RG Junior upheld his fiduciary duties and met his burden to prove that the dissolution and sale of assets was entirely fair, and that determination is not clearly erroneous.

1. CanCan Had No Future and There Was No Better Alternative.

In evaluating the fairness of a transaction, the Court makes a unitary fairness conclusion based upon the totality of the circumstances. *See Emerald Partners v.*

[4] Manno Enterprises quotes only part of a statement from Counterclaim Defendants' post-trial brief below in its brief. *See* EOB 30. The full statement follows: "Is it true that by March 2011 Rob was thoroughly fed up with Manno's antics? Yes, but he also understood that he nevertheless owed fiduciary duties to Manno Enterprises even after Manno treated her own fiduciary duties with contempt." B534.

Berlin, 2003 WL 21003437, at **22, 38 (Del. Ch. April 28, 2003), *aff'd*, 840 A.2d 641 (Del. 2003) (Table). "A fiduciary can satisfy the entire fairness standard in a transaction where an interest holder receives nothing if the fiduciary proves that 'there was no future for the business and no better alternative for the [interest] holders.'" Op. 58 quoting *Blackmore Partners, L.P. v. Link Energy LLC*, 864 A.2d 80, 86 (Del. Ch. 2004). *See also In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 76 (Del. Ch. 2013) (finding common stockholders' receipt of nothing in a merger as fair when common stock had no economic value before the merger).

Manno Enterprises contends that *Blackmore Partners* "weighs strongly in Enterprises' favor" because there it was "reasonable to infer" that a properly motivated fiduciary would not have agreed to a transaction that wiped out the common stock's value. EOB 24-25. A trial court could draw such an inference, of course, but how can a matter of inference survive the "clearly erroneous" standard? Moreover, *Blackmore Partners* involved a motion to dismiss and thus the plaintiff was given every reasonable inference. 864 A.2d at 85-86. After finding such an inference, the Court of Chancery went on to note: "Of course, it is also possible to infer (<u>and the record at a later stage may well show</u>) that the Director Defendants made a good faith judgment, after reasonable investigation, that there was no future for the business and no better alternative for the unit holders." *Id.* at 86 (emphasis added). This is a post-trial appeal and the trial record did indeed show

that Counterclaim Defendants made a good faith judgment that CanCan had no future and there was no better alternative than to dissolve and sell its assets.

Manno Enterprises also attacks the Court of Chancery's conclusion that the asset sale was fair by claiming that CanCan "had great value" shortly before the dissolution because: (1) RG Junior offered to be bought out in February 2011 for $10 million, which implied a value for CanCan of $15.3 million; (2) Toth contracted with Cantor to raise $450 million in financing; and (3) there was a $21.2 million appraisal of the property for the project in 2010. EOB 25, 27-29.

None of that undermines the Court of Chancery's conclusion. First, no one ever offered to pay RG Junior anything, much less his asking price. Manno had tried to find an investor to replace RG Junior, but failed. Op. 59; B447. And if it were true that CanCan was really worth $15 million or more as Manno Enterprises now contends, why did Manno and Flaum never take RG Junior up on his offer or participate in the capital call to support the project?

Second, the Cantor financing failed. Cantor could find no investor interested in providing the equity portion of the deal. Op. 30, 59. Even LHI went through several failed attempts to find financing, and years later was only able to place the debt for a much smaller project when RG Junior put in $121 million in equity with a $15 million personal guarantee. As the Court of Chancery stated, "[a] real-world market check is overridingly important evidence of value." *Union Ill. 1995 Inv.*

Ltd. P'ship v. Union Fin. Gp., Ltd., 847 A.2d 340, 350 (Del. Ch. 2004).

Manno Enterprises confusingly cites to *Ross Holding and Management Co. v. Advance Realty Group, LLC*, 2014 WL 4374261 (Del. Ch. Sept. 4, 2014), as sufficient authority to find the Vice Chancellor's determination clearly erroneous. EOB 28. In *Ross Holding*, however, the Court of Chancery found, as a factual matter, that it was undisputed that the common stock had value at the time of the challenged transaction. 2014 WL 4374261 at *20 n.175. What the *Ross Holding* Court would not permit was the defendants' use of a hypothetical model showing negative value years after the challenged transaction to prove that the challenged transaction created value for the common. *Id.* That is not what Counterclaim Defendants did here. They pointed to the inability of Cantor Fitzgerald to obtain any financing for CanCan at the same time as the dissolution as evidence that CanCan's equity had no value.

Finally, the ROI Consultants Appraisal does not undermine the Court of Chancery's findings because, although CanCan held an option from LHI to purchase the Church Property, it had no funding to actually exercise that option given Flaum's and Manno's refusal to participate in the financing. Even Manno Enterprises acknowledges that a fair price includes "'all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock.'" EOB 26 quoting *Weinberger v.*

UOP, Inc., 457 A.2d 701, 711 (Del. 1983) (emphasis added). And one thing that had harmed CanCan's inherent value here was Manno and Manno Enterprises' claims that Manno owned CanCan's subsidiaries, options and intellectual property.

In the end, LHI purchased CanCan's assets for an aggregate price of $1,919,722.81, which was the <u>book value</u> for work previously done on CanCan's behalf, including the cost of professional fees and market research, much of which could no longer be used. A281-82; B470-75. LHI also paid CanCan $954,000 for the escrow money it paid on options that were now worthless and LHI could not exercise. B473. What that meant was CanCan was getting repaid sums it had spent on a project it could not complete on property Manno said it did not own. As the Court of Chancery said, it was "at least fair and likely excessive." Op. 60.

Manno Enterprises says it received no value from this sale, but fails to acknowledge that CanCan itself was paid fully. *See* EOB 27. Manno Enterprises received no value because of the liquidation preference in the Operating Agreement, which required the Granieris' $11.4 million in capital to be repaid first. Manno was aware of this structure and how it could potentially disfavor Manno Enterprises (B57; B60; B75), yet she signed the Operating Agreement, telling her counsel that "I full well know I am taking a risk." B73, emphasis added.

2. Manno Enterprises' Challenge to the Process Fails.

Manno Enterprises attacks the process involved in the dissolution and sale of

assets, but ignores the reality that there was no independent party to oversee the dissolution and sale. Op. 27. Although Counterclaim Defendants were interested, the Court of Chancery found that they acted at all times in a manner befitting their fiduciary duty of loyalty. Op. 54, 58-60. Given this finding, the precedent cited by Manno Enterprises (EOB 29) fails to undermine the Court of Chancery's holding that the dissolution here was entirely fair. *See William Penn P'ship v. Saliba*, 13 A.3d 749, 757 (Del. 2011) (it was only "impossible to demonstrate that the sale was entirely fair, no matter what the price" because the defendants "manipulated the sales process through misrepresentations and repeated material omissions"); *HMG/Courtland Props., Inc. v. Gray*, 749 A.2d 94, 117 (Del. Ch. 1999) (given undisclosed, material facts, the defendants failed to "convince[the Court] that their misconduct did not taint the price to HMG's disadvantage"); *Bomarko, Inc. v. Int'l Telecharge, Inc.*, 794 A.2d 1161, 1180 (Del. Ch. 1999) (unfair dealing existed when the interested fiduciary failed to disclose all material information and used his position to mislead other fiduciaries).

Finally, Manno Enterprises claims there was no urgency to dissolve CanCan. EOB 24. But, as the Court of Chancery stated, the timing did not favor RG Junior or prevent Manno Enterprises from obtaining alternative financing. Op. 59. Manno and Flaum had had their opportunity and rejected it.

III. MANNO ENTERPRISES WAS NOT UNFAIRLY DILUTED.

A. Question Presented

Whether the Court of Chancery's finding that Manno Enterprises was not unfairly diluted is clearly erroneous.

B. Standard of Review

While RG Junior does not dispute that his issuance of the capital calls was subject to entire fairness review below, the Court of Chancery's decision, "being 'fact dominated,'" will be given "substantial deference" by this Court unless that determination is "clearly erroneous or not the product of a logical and deductive reasoning process." *Cede*, 634 A.2d at 360.

C. Merits of the Argument

1. The Court of Chancery's Finding that the Capital Calls Were Entirely Fair Was Not Clearly Erroneous and Is Supported by the Record.

Manno Enterprises argued to the Court of Chancery that it was unfairly diluted from 29% to 6.6001%. On appeal, Manno Enterprises focuses only on the dilution of its interest from 11.5% to 6.6001% (EOB 31 n.10), which was caused by four capital calls issued by RG Junior after Manno and Py were terminated. RG Junior needed to establish "'to the *court's* satisfaction that the transaction was the product of both fair dealing *and* fair price." Op. 52 quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1163 (Del. 1995). RG Junior met his burden

and proved to the Court of Chancery's satisfaction that the capital calls were entirely fair. Op. 54. Indeed, the calls "were necessary for CanCan to avoid immediate failure, made at a time when financing on comparable terms was not available from the market, priced comparably to similar transactions to which Manno [Enterprises] had agreed, and valued CanCan well in excess of what it was actually worth." Op. 57. The Court of Chancery's finding is supported by the record and should be affirmed.

After Manno's removal, CanCan still needed cash to operate. B387-88. Manno Enterprises acknowledges that "CanCan always needed additional investments to keep the business going…." EOB 34 (emphasis in original). RG Junior issued capital calls in which Manno Enterprises could participate on equal terms and preserve its membership stake. RG Junior had Toth assemble schedules of CanCan's cash requirements (B395; B465-66), and RG Junior then determined the amount of interests that should be issued based on the dilution to which Manno Enterprises had previously agreed (*see* B388-96).

By taking this approach, the first capital call priced CanCan higher than the most recently approved transaction. Op. 55. In the Court of Chancery's view, RG Junior "could have demanded more onerous terms" because CanCan was "a highly speculative business," and Manno's wrongdoing meant that CanCan was "significantly less valuable." Op. 55. RG Junior thought he was pricing the

subsequent three capital calls at the same price as the first by using the same price on a percentage basis, but that approach failed to take into account the additional units that had been issued in the previous calls, which meant the per implied unit price declined to $27,311 by the last call. Op. 55. Had RG Junior used a constant per price unit, Manno Enterprises would have held a 7.19% instead of a 6.6001% interest.

But that did not render the capital calls unfair because CanCan was worthless and "RG Junior dramatically overpaid when making these investments." Op. 56. RG Junior was motivated to "throw good money after bad" in order to avoid litigation, protect what little value remained and protect his large liquidation preference. Op. 56-57.

Manno Enterprises accuses the Court of Chancery of using faulty logic to justify its finding of fairness by relying on CanCan's value at the time of dissolution to find no harm resulting from the change from 7.19% to 6.6001%. EOB 34. As set forth above in Section II(C)(1), however, CanCan's value never exceeded RG Junior's liquidation preference, and the Court of Chancery was thus correct that changing the price per implied unit would not have made any difference to Manno Enterprises, which still would have received nothing.

IV. THE COURT OF CHANCERY'S DECISION FINDING MANNO LIABLE FOR BREACH OF HER FIDUCIARY DUTY OF LOYALTY IS SUPPORTED BY THE RECORD AND THE LAW.

A. Question Presented

Whether the Court of Chancery's decision finding Manno liable for breach of her fiduciary duty of loyalty is clearly erroneous.

B. Standard of Review

While this Court reviews legal findings *de novo*, the Court of Chancery's factual findings are given a high level of deference unless they are clearly erroneous or not the product of an orderly and logical deductive process. *See* Section II(B), *supra*. Damage awards are reviewed for an abuse of discretion, and this Court will not substitute its "own notions of what is right for those of the trial judge if that judgment was based upon conscience and reason, as opposed to capriciousness or arbitrariness." *Gatz Props., LLC v. Auriga Capital Corp.*, 59 A.3d 1206, 1212 (Del. 2012).

C. Merits of the Argument

1. Manno's Self-Interested Compensation Was a Breach of Her Fiduciary Duty of Loyalty.

Manno claims on appeal that the Court of Chancery failed to consider record evidence supporting her entitlement to the compensation she took and erroneously concluded that there was no independent protection provided by Py's approval of her compensation. MOB 11-19. While compensation decisions are typically the

purview of business judgment, the Court of Chancery correctly held that is not the case when the compensation decisions are self-interested and made without independent protections, as was the case here. *See* Op. 35-37.

a. The Record Does Not Support Manno's Claim to $432,000 in Compensation.

Manno argues that it was contrary to the record evidence for the Court of Chancery to conclude that she was only entitled to the $207,000 in compensation that Plaintiffs conceded was appropriate because the undisputed evidence shows that Manno was entitled to at least $432,000 in salary and reimbursement of expenses. MOB 11. That evidence might be undisputed, but it does not favor Manno. What it shows is that Manno's testimony on this point continued changing, with it varying from $5,000 to $10,000, or perhaps $15,000 a month, which was then increased to $30,000 in September 2010. B331; B333-35. The documents are similarly confused. B40 (demanding $5,000 and half of her $3,000 rent); B44 (demanding $10,000); B289; B291; B297-300; B305-306; B311-313. Nor was Manno able to distinguish, as required, between which portion of her payments was to reimburse her for expenses and which was for her fee. *See* Op. 9-10; B301-309. Though Manno claims that she was entitled to reimbursement of her full $3,000 in rent, the contemporaneous evidence showed that Manno only expected to be paid half of that. *See* B40 (requesting half of her $3,000 rent); B77 ("we started with cancacn [sic] giving me 150 towards my 3000 rent and then it

stopped and i paid it..i want to go abck [sic] and count that 150o [sic] monthly against my receipts"); B296; B299-300.

Plaintiffs accepted that the $10,000 per month RG Junior had been told she was receiving was at least arguably reasonable, but Manno failed to prove her entitlement to any amounts above that. RG Junior did not discover those increased amounts until the fall of 2010. B356-60. He held a telephonic meeting with Manno and Py letting them know he did not approve their salaries. B356-57; B370-71. Manno admitted that RG Junior sent her an email complaining about overspending (B294-95), and he further questioned employee/consultant salaries in a desire to get the monthly "burn rate" down to $200,000 to $250,000 per month B97. On February 16, 2011, Manno sent RG Junior a list of CanCan employees and their monthly payments. It did <u>not</u> include Manno or Py, which suggested that they had ceased their unauthorized payments. *See* B99-100. They had not, but RG Junior did not discover that until later.

b. The Court of Chancery's Finding that Py Failed to Exercise Business Judgment and Lacked Independence Is Supported by the Record.

i. Py Exercised No Meaningful Review or Oversight.

The Court of Chancery correctly denied Manno's argument that Py's approval of her compensation and CanCan's other payments rendered those decisions protected business judgments. The Court held that "Py did not make a

business judgment; he simply rubber stamped the larger checks." Op. 37. That conclusion is supported by the record, which shows that Manno would send urgent demands to Py that he transfer various amounts into her Manno Enterprises account, and Py would typically comply that same day. *Compare* B41 (demanding $3,000); B46 (demanding $5,000); B49 (demanding $5,000) *and* B52 (demanding $7,500) *with* B197). After Traci Havelin was hired as an accountant for the Company, Manno would give bills to Havelin or tell her what bills needed paid; Havelin would create a list of all the bills for payment, which Manno would then approve. B481-83. The list plus the originals of the invoices (to the extent they existed) would be sent to Py who would sign the checks as requested. *Id.* Thus, although Manno might not have had check signing authority, Py acted essentially as a pass-through without exercising any oversight.

Manno also claims that "Py ratified Manno's withdrawals" of $98,000 in ATM cash from the Company's bank accounts because he received the bank statements and never registered any objection. MOB 13-14. In fact, as the Court below found, Manno was largely pocketing the money and there is no proof that Py knew that. But, Py's failure to ask any questions about the $98,000 in withdrawals only serves to further underscore that he exercised no meaningful review over Manno's spending. Manno began making maximum cash withdraws from the Company's accounts in October 2009. B190. Nearly one year later, the

Company's auditors alerted Py to the issue of the cash withdrawals (B483), which raises the question of whether the elderly Py had applied any oversight. Once alerted to the issue, Py pro forma instructed Manno to stop using the debit card to withdraw cash. B324-25. Manno's withdrawals then slowed down for a while, but then picked back up and Py never checked her again. *See* B486-87; B192-93.

ii. Py Lacked Independence from Manno

The Court of Chancery also correctly found that "Py and Manno's relationship was sufficiently close that Py cannot be regarded as independent." Op. 37. Because Py was not independent of Manno, his "involvement did not insulate Manno's unilateral decision from entire fairness review." *Id.* There is ample support in the record to support that conclusion.

Py was a family friend of the Granieris, but Manno also had a "friendly, trusting relationship with Joe Py…." B353. Indeed, Manno testified that Py was the first person she called to become involved in the CanCan Project. B292.

Manno and Py had previously worked together to develop a casino in Oklahoma with the Keetoowah Economic Development Authority, but that project ended in litigation. Op. 5; B281-87; B1-32. Manno set out again to partner with Py and the Keetoowah in the fall of 2010—while she was getting paid to work on the CanCan Project—to obtain land in Oklahoma, provide technical assistance and raise capital for a casino project. B53; B64-72. The agreements with the

Keetoowah were between Rockledge Holding Company and/or Rockledge Development, LLC (collectively, "Rockledge"). At trial, Manno insisted Py had formed Rockledge, but that she had no "relationship" with it even though she was listed as an "authorized representative" and used her same Manno Enterprises' P.O. Box as the address for Rockledge. B65; B350-55. After some probing questions by the Vice Chancellor, Manno finally admitted that she had an unwritten affiliation in which Py agreed to give Manno "a piece of Rockledge" if any deal went through. B352-53. Not surprisingly, Manno used CanCan funds and personnel to support the venture.

Finally, at trial Manno asserted that she was entitled to a marketing agreement with CanCan (though she has dropped that failed claim on appeal). In support of her claim, Manno offered a draft agreement between CanCan Casino Resort & Spa LLC and J&S Marketing, LLC, which uses Py's home address. *See* B88; B94. Manno acknowledged that "J&S" stands for "Joe and Sandra Marketing." B336. It was one more joint venture to be paid for by CanCan.

Given all of the evidence of Manno and Py's business dealings, it was not an error for the Court to find that Py lacked independence from Manno.

iii. No Adverse Inference Was Warranted from Py's Failure to Testify.

Manno also argues that an adverse inference should be taken from the failure to obtain any testimony from Py. MOB 14. Plaintiffs attempted to take Py's

deposition, however. *See* D.I. 97. Py's attorney entered an appearance in the Pennsylvania Court of Common Pleas and refused to produce Py for his deposition. After much discussion, Py's attorney stated that Py had just undergone brain surgery and would not be capable of sitting for his deposition. Because of that, the deposition did not go forward.

In addition, the authority relied upon by Manno for an adverse inference is inapposite. *See* MOB 14. Plaintiffs have no control over Py and it would not have been "natural" for Plaintiffs to bring him to trial. Although Py had been a long-time family friend prior to their investment, the Granieris discovered that their trust in Py was misplaced and they sought to remove Py along with Manno from the outset. *See* B103-04 (asking both Py and Manno to resign). The Granieris ultimately fired Py on March 10, 2011 at the same time they fired Manno. *See* B385-86. After he was fired, Py had his counsel contact RG Junior to say that Py wanted to surrender his entire interest in CanCan to RG Junior due to Py's feelings of guilt. B386. RG Junior has never spoken with Py since his removal. B400.

By contrast, Manno would have benefitted from having brought Py to trial (if he were fit to testify) to prove that Py was aware of her expenditures. She did not consider him to be a part of the conspiracy among the Granieris and Toth, and says she had had contact with him as late as July 2, 2014. *See* B288 (Py not part of conspiracy); B290 (testifying about the status of Py's current gaming venture)).

c. CanCan's Audit and IRS Filings Do Not Insulate Manno from Liability.

Manno also argues that the Court of Chancery failed to consider the effect of the Company's audit of its financials and CanCan's other filings with the IRS as insulating her from any claim of wrongdoing. MOB 16. An audit, however, can only be as good as the information upon which it relies, and an auditor must rely on management's representations in determining whether fees and expenses are for proper business purposes. *See* B501-02; B506-07. For example, one document relied upon by the auditor to issue its opinion is a written statement by Manno that her monthly consulting fee was approximately $30,000 in 2009, and that she had no expenses reimbursed in 2009. *See* B53a. Manno testified at trial, however, that she was only receiving $5,000 to $10,000 per month in 2009—not $30,000—and that the majority of that money was for her expenses. *See* B333-34. There is little an audit can do to deal with such deception.

CanCan's filings with the IRS prove little as well. The form 1099s issued to Manno merely reflect that various amounts were paid from CanCan or its subsidiaries to Manno (through Manno Enterprises). The 1099s make no judgment whether that compensation or the unauthorized cash withdrawals that the auditor required be put on Manno's 1099 were proper or authorized.

d. Manno Failed to Prove Her Compensation Was Entirely Fair.

Manno argues that the Court of Chancery clearly erred in finding that she failed to prove her compensation is fair. MOB 19-21. Given that Manno unilaterally set her own compensation, however, she had an "exceptionally difficult" burden to persuade the Court of Chancery that it was fair unless it was "justified by reference to reliable markets or by comparison to substantial and dependable precedent transactions…." *Valeant Pharms. Int'l v. Jerney*, 921 A.2d 732, 748 (Del. Ch. 2007). Manno made no attempt to justify her compensation by reference to reliable markets. Instead, Manno's sole justification for the compensation she took is the salaries she had CanCan pay others.

The Court of Chancery found those comparisons inapt, however, because (i) Manno set that compensation and "she consistently overpaid," (ii) Manno lacked the experience and expertise of other hires, (iii) Manno owned equity in CanCan when the other consultants did not, and (iv) the hiring of other employees to take over her duties should have decreased her salary, not increased it. Op. 37.

The Court's findings are supported by the record. Manno was the one who offered to pay Toth $35,000 per month plus expenses for 25 hours of work a month. B436; A47-54. As Toth testified, "in my career that never happened" before, and he did not try to negotiate for more because he thought $35,000 a month for a "nonexisting project" was a "pretty good salary." B436; B450-51.

Manno also claims that Toth's expenses further justify the unauthorized amounts she took. *See* MOB 20. But Toth was constantly on the road, spending long times in New York meeting with investment bankers and other professionals. *Compare* A155 *with* B489-91. Manno, by contrast, stayed in Mississippi with occasional trips to New Orleans or Jackson. *See* B489-90. Most of her expenses had little or nothing to do with business.

Joey Manno's $30,000 per month salary also does not support the fairness of Manno's fees. RG Junior's knowledge that Joey was receiving $30,000 does nothing to confirm that such monthly salary is the objective industry standard for executives in the casino industry. There is no evidence that RG Junior had any familiarity with the casino industry other than his investment in CanCan.

Manno also looks to amounts that were paid to certain consultants who were hired after she was fired as a benchmark for the fairness of her compensation. This reliance is also misplaced. It was Manno herself who suggested Albo Antenucci's compensation of $25,000 per month. *See* B101. CanCan only paid the Fine Point Group total fees of $33,600 plus reimbursement of travel expenses over a several month period and not $35,000 per month indefinitely. B488-89. And Steve Overly was hired in a dual general counsel/CFO role at $25,000 per month. B476. Moreover, none of the individuals whose salaries Manno attempts to use as a benchmark for what she "should" have received had any equity in the Company.

Thus, Manno's compensation should never have been at the level of other consultants given the equity stake she had in the Project.

Finally, Manno claims that CanCan's increased operating expenses after her termination justifies the compensation she received. MOB 21. As explained at trial, those expenses increased because the Project had to hire the real professionals who the banks required to be in place before financing could be discussed. *See* Section I(C)(2), *supra*. Meanwhile, Manno's extraordinary expenses, such as the Super Box and private planes, were eliminated. B460-61. The Court of Chancery's decision on this point was correct.

e. There Was No "Mutually Acceptable" Consulting Agreement.

Manno claims for the first time on appeal that there was no requirement that the consulting agreement contemplated by the Operating Agreement be in writing, and that an oral agreement would suffice so long as it was on mutually acceptable terms. MOB 10. While Manno argued below that it was a breach of the Operating Agreement for RG Junior to fail to enter into a consulting agreement with her, she never raised the claim that there was an oral contract that was "mutually acceptable" to RG Junior as supermajority member. *See* B611 at n. 3. As Manno never raised this argument to the Court of Chancery, she may not raise it for the first time on appeal. *See* Del. Supr. Ct. R. 8.

It is also wrong. The Operating Agreement "plainly states that any

consulting agreement would have to be in writing" (Op. 50), and Manno's compensation was never on "terms mutually acceptable" to RG Junior since he objected to Manno's compensation once he discovered what she was getting paid in the fall of 2010. *See* Section IV(C)(1)(a), *supra*. In addition, Manno's argument that RG Junior implicitly approved Manno's compensation because he could have removed her at any time after June 8, 2010 both miscalculates the Granieris' holdings (*see* Op. 24) and fails to recognize that the Operating Agreement was not executed until December 20, 2010. Moreover, Rob had to proceed cautiously with removing Manno given the practical problems of how to move the project forward without Manno's involvement while she claimed enormous influence with city officials.

2. Manno Failed to Meet Her Burden to Prove the Propriety of Other Challenged Corporate Expenditures.

a. Manno Failed to Meet Her Burden.

Manno challenges the Court's finding that she is liable for $456,123 in corporate expenditures (MOB 22-28), which includes, among other things, the salaries of her siblings, "Frankie the Fish" and Ponzio, and other charges for hotels, meals and airfare that lacked a documented business purpose. Manno argues that she should be insulated from liability for all of these corporate expenditures because Py approved and paid them. MOB 22. As previously discussed, though, the trial Court found that Py "rubber stamped" whatever checks

Manno requested to be sent. *See* Section IV(C)(1)(b)(i), *supra*. And while, "[o]rdinarily, these expenses would be subject to the business judgment rule," in this case "many of the expenses related to … interested transactions...." Op. 43.

When a plaintiff shows "definite instances where [fiduciaries] did not properly allocate expenses" between companies controlled by the fiduciary, then the burden is on the fiduciaries to account for those funds by establishing the "purpose, amount and propriety of the disbursements." *Carlson v. Hallinan*, 925 A.2d 506, 537 (Del. Ch. 2006); *Technicorp Int'l II v. Johnston*, 2000 WL 713750, at *16 (Del. Ch. May 31, 2000). The Court of Chancery agreed that Plaintiffs showed definite instances where Manno improperly used CanCan funds to benefit herself and the various projects that she was pursuing personally. Op. 17, 39-44. As such, Manno bore the burden at trial to establish the purpose, amount and propriety of the challenged expenses, and she failed to meet that burden.

Manno claims that Plaintiffs' use of Havelin's testimony undermines any finding by the Court of Chancery that the challenged expenses were improper because Havelin failed to withhold the correct amount of taxes from her paychecks when she worked at LHI. MOB 22-23, 26. Each challenged expense, however, is backed up by the testimony of CanCan's expert, Richard Rowland, who took all of CanCan's Quickbook statements and reviewed all of CanCan's invoices on file to determine which expenses had inadequate documentation to back them up as

legitimate CanCan expenses. *See* B176-79; B210-71; B494-500. It was only then that Havelin was used to identify expenses that she knew were legitimate (for example, airfare for Toth). Plaintiffs would have been within their right to make Manno prove the propriety of *all* corporate expenditures that lacked a documented business purpose. Thus the use of Havelin was a <u>benefit</u> to Manno. It <u>cut</u> the amount challenged. Finally, while Havelin's failure to withhold taxes could go to her credibility, the Court of Chancery was made aware of her activity prior to rendering its decision, and thus factored that into its credibility assessment.

b. The Court of Chancery's Findings Are Supported by the Record.

Manno argues that there is no support in the record for the Court of Chancery's factual finding that Manno is responsible for $92,778 in salary paid to her brother, Joey Manno. MOB 24. Manno, however, <u>admitted</u> on April 10, 2010 that Joey was useless and performing no work for CanCan, and she stood by that assessment during her deposition. *See* Op. 38; B34 ("my brother who is the biggest mistake of my life making him president[,] he has no focus, drinks heavily…. But my investor likes Joey so I tolerate him and give him only baby stuff to do so he doesnt **** up and I assign his duties to others and he isnt even aware of it."); B293. Plaintiffs thus argued that any compensation paid to Joey after April 10, 2010 should be chargeable to Manno since it was waste to pay Joey for performing no work in the absence of a contract. Manno failed to respond to

Plaintiffs' argument or otherwise show that Joey's salary was entirely fair. Op. 39.

Manno continues to profess confusion as to the $92,778 amount challenged by Plaintiffs and awarded as damages by the Court of Chancery, but Exhibit C to Rowland's report identifies each payment that was made to Joey after Manno's admission on April 10, 2010, and those amounts total $92,778.38: 5/3/2010 payment of $30,000; 5/3/2010 payment of $2,778.38; 6/1/2010 payment of $10,000; 6/2/2010 payment of $20,000; and 6/30/2010 payment of $30,000. *See* B207. Thus, the Court of Chancery's factual finding is supported by the record.

Manno also argues that there is no support in the record to charge her for her sister Patty's salary of $66,392. MOB 25-26. The Court of Chancery found, however, that Manno failed to prove that paying Patty was entirely fair. Not only was there a familial conflict of interest, but starting in November 2010, Manno was diverting Patty's salary to herself. Op. 39.

Manno claims Patty provided valuable services for CanCan and that there is insufficient evidence rebutting Patty's testimony about what she did for the Company. MOB 26. That, however, is incorrect. CanCan paid actual professionals to conduct most of the work Patty claims to have done (*see* B37; B327-29), and both Toth and Havelin testified that they had no idea what Patty did for the Company. *See* B439; B477-80. That Toth had no idea what Patty's role was in a Company with less than 10 employees is particularly noteworthy given his

position as President of CanCan. Finally, if there were any doubt whether Patty was providing valuable services to the Company, the fact that Patty permitted her entire paycheck to be deposited into Manno's personal bank account for many months undermines any argument that Patty was actually doing work for CanCan. *See* Op. 13, 39.

Manno does not seriously challenge the Court of Chancery's factual findings on any of the other expenditures other than to say that the expenditures provided value to CanCan. MOB 26. That hollow statement, however, is not enough on appeal to overturn the Court of Chancery's factual findings that Manno failed meet her burden of proof or committed waste.

CONCLUSION

For the foregoing reasons, Plaintiffs-Counterclaim Defendants respectfully request that this Court deny the appeals and affirm the Court of Chancery's ruling.

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CERTIFICATE OF SERVICE

I hereby certify that on October 5, 2015, a copy of Appellees' Answering Brief and Appendix thereto was caused to be served upon the following counsel of record by File & ServeXpress.

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