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IN THE

Supreme Court of the State of Delaware

CHICAGO BRIDGE & IRON COMPANY N.V., Plaintiff Below-Appellant, v. WESTINGHOUSE ELECTRIC COMPANY LLC and WSW ACQUISITION CO., LLC, Defendants Below-Appellees.	**No. 573, 2016** CASE BELOW: COURT OF CHANCERY OF THE STATE OF DELAWARE, C.A. No. 12585-VCL

APPELLANT'S OPENING BRIEF

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NATURE OF PROCEEDINGS

Plaintiff-Appellant Chicago Bridge & Iron Company N.V. ("CB&I") is a global construction contractor serving the energy industry. On October 27, 2015, it agreed to sell its nuclear power plant construction Business to Westinghouse Electric Co. ("Westinghouse"), a designer of nuclear power plants. The transaction closed on December 31, 2015. CB&I received zero upfront consideration for the sale, with the possibility for certain earnout amounts upon completion of the projects. Rather, the parties intended the transaction to end disputes between them concerning responsibility for cost overruns on two nuclear power plant projects that they had been building together as consortium partners. Westinghouse's own CEO called the transaction a "quitclaim."

Under the Purchase Agreement (the "Agreement"), after Closing the parties were to attempt to agree on the amount of Net Working Capital in the Business sold to Westinghouse as compared to a Target Net Working Capital figure. The Agreement provided a process (at §1.4) for an Independent Auditor to resolve disputes concerning the calculation of that amount following a set of Agreed Principles that required the application of "GAAP, consistently applied" by CB&I. Depending on the final Net Working Capital amount, an amount would either be paid to Westinghouse as buyer (if lower) or added to the potential earn-out amount for CB&I as seller (if higher).

The Agreement included extensive provisions eliminating any further liability of CB&I to Westinghouse once the transaction closed. Among those provisions was an extremely rare one for private company transactions (at §10.1) by which CB&I's liability for breaches of its financial representations and warranties — which included that the Financial Statements of the Business conformed with GAAP and that there were no undisclosed material liabilities — was extinguished at Closing. Westinghouse could have chosen not to close. But if it chose to close, it was not entitled to any recovery post-Closing even if CB&I had breached such financial representations and warranties.

Following extensive due diligence by Westinghouse before and after signing the Agreement, Westinghouse chose to close. After closing Westinghouse asserted a Net Working Capital amount that was approximately *$2 billion less* than the Target Net Working Capital figure of $1.174 billion.

On July 21, 2016, CB&I filed suit in the Court of Chancery alleging that Westinghouse's claim was an attempt to use the Net Working Capital true-up process set out in §1.4 to recover on claims that it had given up, including by way of §10.1. CB&I sought an order declaring that Westinghouse's claims had been extinguished and further declaring that Westinghouse could not seek to circumvent the Agreement's eliminations of liability by way of the Independent Auditor process.

Westinghouse moved for judgment on the pleadings. In a Memorandum Opinion issued December 5, 2016, the Court of Chancery granted Westinghouse's motion. It held that the Independent Auditor is empowered to resolve all disputes between CB&I and Westinghouse over the Net Working Capital true-up, including those concerning GAAP compliance of CB&I's Financial Statements even though such claims amount to an allegation that CB&I breached its representations and warranties. *See* Memorandum Opinion, Exhibit A hereto ("Op."); *see also* Order, Exhibit B hereto. This is CB&I's appeal.

SUMMARY OF ARGUMENT

I. The Court of Chancery erred by dismissing Count I of the Complaint, which sought to bar Westinghouse from seeking recovery before the Independent Auditor predicated on allegations that CB&I breached representations and warranties in the Agreement as such claims were extinguished at Closing. The dismissal was based on a finding that the "controlling precedent" (Op. 15) was *Alliant Techsystems, Inc.* v. *MidOcean Bushnell Holdings, L.P.*, 2015 WL 1897659 (Del. Ch. Apr. 24, 2015). *Alliant* construed the agreement at issue there to relegate matters of GAAP compliance — even if they amounted to an allegation that a seller breached its representation and warranties — to an Independent Auditor in connection with a working capital true-up process. The Court of Chancery here incorrectly distinguished an earlier decision by then-Vice Chancellor Strine, *OSI Systems, Inc.* v. *Instrumentarium Corp.*, 892 A.2d 1086 (Del. Ch. 2006). *OSI* ruled that claims for breaches of representations and warranties may *not* be pursued before an Independent Auditor under the guise of a working capital adjustment. As *OSI* made clear: "[Purchaser] cannot bypass the contractual Indemnification process . . . and then seek a gigantic Closing Adjustment by attempting to convince the Independent Accounting Firm that [Seller's financial statement] was materially inaccurate and infected by improper accounting." *Id.* at 1095.

In finding *Alliant* controlling and declining to follow *OSI*, the Court of Chancery failed to address the key distinction between the relevant contract terms. In *Alliant*, the contract directed that working capital was to be based on "GAAP" — full stop. In *OSI*, by contrast, and in the instant case, the contract standard is GAAP as "consistently applied" by Seller. As the *OSI* decision held, a GAAP "consistently applied" standard empowers the Independent Auditor only to follow the seller's historical accounting practices, the purchaser having failed to challenge them as not GAAP-compliant before Closing — *not* to conduct post-Closing what is in essence a *de novo* evaluation of the seller's accounting for consistency with any identifiable theory of GAAP. The Court of Chancery did not address this difference, one well recognized as material by practitioners.

Courts in other jurisdictions have likewise found dispositive the distinction between the "GAAP" and "GAAP consistently applied" standards. *See, e.g.*, *Westmoreland Coal Co.* v. *Entech, Inc.*, 794 N.E.2d 667, 670 (N.Y. 2003) (buyer's objections "unambiguously [fell] within the Agreement's indemnification provisions, not its purchase price adjustment provisions" because the contract "stress[ed] consistency" with the seller's past accounting practices) and *HBC Solutions, Inc.* v. *Harris Corp.*, 2014 WL 6982921, *7 (S.D.N.Y. Dec. 10, 2014) (buyer's objections concerning seller's GAAP compliance subject to purchase price dispute resolution process because contract did "not stress (or even demand)

consistency with the accounting principles used in preparation of other financial statements"). This Court should make clear that Delaware courts also enforce this distinction.

The Court of Chancery's failure to follow the critical "consistently applied" doctrine of *OSI* led it to fail to give effect to the plain language of the liability extinguishment provision of §10.1 of the Agreement. Westinghouse's position essentially renders nugatory the agreement in §10.1 eliminating Westinghouse's ability to recover for breaches of representations and warranties. If, as Westinghouse contends, it is free to recover through the Independent Auditor process for claims predicated on the prior Financial Statements having been improper under GAAP, then there essentially would have been no purpose for the "consistently applied" language of §1.4 and the Agreed Principles or for the carefully crafted release language of §10.1.

Finally, the Court of Chancery's ruling effectively treats the Independent Auditor as a plenary law arbitrator, rendering meaningless the Agreement's contractual stipulation in §1.4(c) that the Independent Auditor is to act as an "expert not as an arbitrator."

II. The Court of Chancery erred in dismissing Count II of the Complaint, which alleged that Westinghouse breached the covenant of good faith and fair dealing by presenting claims to the Independent Auditor that effectively seek to

revisit the very dispute over cost overruns on the nuclear projects that the parties intended to resolve by this "quitclaim" transaction. In so ruling, the Court of Chancery failed to address Westinghouse's plain waiver of any contention that Count II does not state a claim. Compounding that error, by dismissing this Count with prejudice on grounds waived by Westinghouse, the Court reached the merits of, and left no forum for relief on, the dispute in Count II, even as it held that all disputes between the parties over Net Working Capital are for the Independent Auditor.

* * *

Post-closing accounting true-up exercises before Independent Auditors have become an increasingly common part of business transactions. They also have spawned extensive litigation raising the point that, like here, purchasers are abusing these processes in an effort to circumvent clear contractual limits on their rights and revisit the intent and economics of the underlying deal. This appeal presents this Court with its first opportunity to address the increasingly important issue of when an Independent Auditor is empowered to engage in effectively a *de novo* GAAP review as part of a net working capital process — even if doing so swallows other bargained-for promises in the agreement that eliminate a buyer's rights.

STATEMENT OF FACTS

A. The parties and their prior relationship

The Agreement at issue stems from the parties' prior relationship as consortium partners for the construction of two nuclear power plants, the first in the United States in over three decades. (A10-11).

Plaintiff's former subsidiary, CB&I Stone & Webster, Inc. ("S&W"), agreed to be the construction contractor for two plants designed by Westinghouse, and received from Westinghouse safeguards (including rights to reimbursement) against the risk of cost overruns inherent in the untested, first-of-their-kind projects. (A19-20).

Friction arose between the parties involved in the projects as a result of cost overruns and delays caused by Westinghouse's design changes. (A10-11, A20, A22-23). Westinghouse eventually saw the value in involving both CB&I and the project owners in a "global" resolution to the long-standing dispute concerning cost overruns. (A22-24, A189). Accordingly, CB&I and Westinghouse, as well as Toshiba Corp. of Japan (Westinghouse's parent), began discussing a potential resolution. (A23-24).

B. Negotiation of the Agreement

From the beginning, the transaction was intended and structured to provide CB&I with a clean break from all liabilities on the projects. (A23-24). As per the

parties' term sheet: "CB&I shall receive a full release from Westinghouse and each of the project owners for any and all liabilities related to the AP1000 [nuclear power plant] projects (past, present, and future) arising from or in any manner associated with the nuclear business being acquired by Westinghouse." (A11, A29). As Westinghouse's CEO put it, the transaction was a "quitclaim." (A11).

Near the start of negotiations in July 2015, CB&I provided Westinghouse with financial information, including S&W's balance sheet position on the projects as of June 30, 2015, based upon which CB&I and Westinghouse agreed on a $1.174 billion "peg" of the estimated net working capital to exist in the Business[1] at the time of its transfer to Westinghouse. (A25-27). Starting with their first term sheets, the parties recognized that CB&I, through S&W, had recorded a $1.16 billion "claim cost" — the asset representing CB&I's right to recover costs incurred and paid by S&W from either the project owners or Westinghouse. (A26-28). Consistent with the purpose of the transaction, CB&I and Westinghouse reached a compromise to finally resolve the issue of CB&I's claim cost. As eventually set forth in §1.3 of the Agreement, CB&I was entitled to receive a combination of deferred payments due upon completion of the projects and a share

[1] The scope of the transaction eventually included S&W's other AP1000 projects in China and CB&I's Nuclear Integrated Services business (collectively with the U.S. projects, the "Business"). Capitalized terms not defined herein are used as defined in the Agreement.

of future Westinghouse profits, if any, but with its total potential recovery capped at an amount well below its $1.16 billion claim cost. (A25-26, A32-33).

During negotiations, Westinghouse conducted due diligence on S&W's actual costs incurred and estimates to complete the projects — estimates which were based on a consistent GAAP methodology audited by CB&I's external auditor and which had been shared with Westinghouse on a regular basis as consortium partner — so that Westinghouse could assess the status of the projects and what liabilities Westinghouse would assume. (A30-31, A46-47). Westinghouse also conducted due diligence on the components of the net working capital peg, including the $1.16 billion claim cost. (A30-31).

C. The Agreement

CB&I, S&W, and Westinghouse (along with acquisition-vehicle WSW Acquisition Co., LLC) signed the Agreement on October 27, 2015 pursuant to which Westinghouse would acquire CB&I's nuclear Business for no upfront cash consideration. (A32). As noted, the contract granted CB&I a mixture of deferred payments and a limited share of future Westinghouse profit, if any, totaling well less than it was owed, in exchange for a *total* release from future liability.

1. Release of claims

The Agreement contained a series of releases allowing CB&I to walk away from the nuclear projects free and clear. In §12.18(a), Westinghouse released "any

and all rights, defenses, claims or causes of action (including rights of contributions) known and unknown, foreseen and unforeseen, arising prior to or on the Closing that each of [WSW] and [S&W] and/or its Subsidiaries have or may in the future have against [CB&I] . . . arising out of, resulting from or relating to the Projects, the Business, the Project Agreements, the Consortium Agreements and any Liability or Loss relating thereto." (§12.18(a)). In turn, CB&I agreed to a separate release of Westinghouse. (§12.18(b)).

In addition to the releases between CB&I and Westinghouse, as specifically contemplated by the Agreement (§8.3(c)), CB&I entered into releases with the owners of the two US nuclear projects, whereby CB&I and the owners released any claims against one another. (A35). With CB&I out of the picture, Westinghouse was then able to achieve a global resolution to disputes over the projects by negotiating its own private settlements with the owners. (A39). The effectiveness of these settlements was also set forth as a condition precedent in the Agreement (and in fact occurred pre-Closing). (§8.1(e), A39).

2. Representations and warranties

In the Agreement, CB&I made several key representations as to the financial condition of the Business and the accuracy of its Financial Statements, including the balance sheet of the Business as of June 30, 2015 (§2.6(a)); the lack of Liabilities not disclosed on the repped-to balance sheet (§2.6(e)); and the absence

of any Material Adverse Effects since the date of the repped-to balance sheet, June 30, 2015 (§2.19).

Under the terms of the Agreement, Westinghouse's only recourse in the event it took issue with the accuracy of these representations and warranties was to not close. (§8.1; A34). The Agreement required (and permitted, via the access clause at §5.4) Westinghouse to satisfy itself, before Closing, of their accuracy. Once Westinghouse closed, §10.1 of the Agreement was express that there were would be "no liability for monetary damages" for a breach of any of the representations absent a finding of "actual fraud." (A34). In that deliberately negotiated provision rarely found in private company transactions (A447), the Agreement provided that "none" of these representations (and any other representations not specified as "Fundamental Representations") "shall survive the Closing." (§10.1; A29-30, A34).[2] Once Westinghouse closed, CB&I's exposure on its Financial Statements was over.

3. Indemnification

During negotiations, Westinghouse had attempted to get CB&I to indemnify Westinghouse for breaches of CB&I representations, including the core financial representations — an attempt that was unequivocally rejected. (A29-30). As

[2] None of the limited exceptions to this lack of ongoing CB&I liability is relevant here. (A447).

CB&I's general counsel explained by email to Westinghouse, because CB&I "receive[d] no cash at Closing (and potentially none for a significant time, if at all) and view[ed] the fundamental transaction benefit as stepping away from liability, indemnities threaten[ed] to undercut the logic of the transaction and its basic purpose for [CB&I]." (A29-30). The ultimate bargain struck between the parties embodied this rationale.

Not only is there no obligation that CB&I indemnify Westinghouse for any alleged breach of CB&I's financial representations and warranties, the post-Closing indemnification provision the parties did agree upon imposed an expansive indemnification obligation *on Westinghouse*. Section 10.4 required Westinghouse to indemnify CB&I for "all claims or demands against or Liabilities of [S&W] . . . or otherwise related to the Business or the" Projects. (§§10.4, 11.1). The extraordinary protection of this indemnification obligation extended "regardless of where or when or against whom such claims, demands or other Liabilities are asserted or determined or whether asserted or determined prior to, on or after" signing or Closing. (*Id.*). That provision underscored the whole point of the Agreement — that after Closing, CB&I would walk away with no risk of future liability from any quarter.

4. Working capital

The Agreement also provided for a standard working capital adjustment mechanism. This mechanism was included to account for changes in working capital between June 30, 2015, when the working capital peg was set, and Closing.[3] (A26-28). If the working capital of the Business when transferred had fallen below the peg, CB&I would owe Westinghouse the net difference, and vice-versa. (A26-28).

Consistent with the limited purpose of the true-up mechanism, the parties set out Agreed Principles narrowly circumscribing the scope of the working capital calculation to ensure that it would not deviate from the methodologies and practices employed by CB&I and S&W that had been the basis of the negotiations with Westinghouse — the same methodologies and practices that were the basis of the financial information used to generate the Target Net Working Capital figure and the Financial Statements to which CB&I had provided its representations and warranties. Per the Agreed Principles, working capital was to "be determined in a manner consistent with GAAP, *consistently applied by [CB&I]* in preparation of the financial statements of the Business, as in effect on the Closing Date." (Sch.

[3] As is standard, the final purchase price was made up of several elements, including the working capital adjustment. Only the working capital adjustment is at issue between the parties.

11.1(a); A164-65) (emphasis added). The Agreed Principles further confirmed that net working capital would be calculated:

> based on the past practices and accounting principles, methodologies and policies applied by the Company [S&W] and its Subsidiaries and the Business (a) in the Ordinary Course of Business and (b) in the preparation of: (i) the balance sheet of the Company and its Subsidiaries for the year ended December 31, 2014 (adjusted to reflect the [nuclear construction] Business); and (ii) the Sample Calculation set forth on Schedule 1.4(f).

(*Id.*).[4] The GAAP-compliance of the December 31, 2014 balance sheet was explicitly included as one of CB&I's representations, and the Sample Calculation was based on the balance sheet as of June 30, 2015 — also included as a Financial Statement that CB&I represented was prepared in accordance with GAAP. (Schs.1.4(f), 2.6(a)).

The basic idea was simple. Both sides — CB&I and Westinghouse — knew how the net working capital had been calculated at this point, and the Agreement provided that any true-up to account for subsequent changes up through Closing would be based on the same methodologies — "consistently applied." The point was to prevent any deviation from past practice, by either side.

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[4] The Agreement similarly required that Westinghouse's Closing Statement be "prepared and determined from the books and records of the Company [S&W] and its Subsidiaries and in accordance with United States generally accepted accounting principles ('GAAP') applied on a consistent basis throughout the periods indicated." (§1.4(f)).

Pursuant to §1.4(c), disputes about net working capital were to be submitted to an Independent Auditor "functioning solely as an expert and not as an arbitrator." (A38). The Independent Auditor was precluded from engaging in independent review and was limited to considering matters raised in the written submissions of the parties that were "in accordance with the applicable guidelines and procedures" set forth in the Agreement (§1.4(c)) — in other words, that followed the mandate of the Agreed Principles to use "GAAP, consistently applied by [CB&I]." (Sch. 11.1(a)).

D. The current dispute

Initially, the true-up worked as intended to enable the Business to operate pre-closing. CB&I invested approximately $1 billion of its cash in the Projects during the second half of 2015 (including post-signing) and, accordingly, CB&I expected to recoup the appropriate portion of that additional funding after the transaction closed. (A27-28, A40). CB&I ultimately calculated that the Net Working Capital Amount at Closing was $1,601,805,000 (approximately $428 million above the peg) based on the same principles and methodologies that it had previously used in preparing the Financial Statements of the Business, in calculating the prior working capital estimates presented to Westinghouse, and in generating the books and records that Westinghouse had thoroughly diligenced. (A41).

After receiving a 30-day extension, Westinghouse presented a bare-bones Closing Statement on April 28, 2016 in which it asserted that CB&I suddenly owed it more than $2 billion. (A13-14, A40, A42). In the months that followed, Westinghouse dribbled out further details of its "calculation," after repeated prodding by CB&I to explain this seemingly absurd working capital number. (A41). The limited information that Westinghouse has provided nonetheless made it clear that to reach this dramatically different result, Westinghouse had applied entirely new accounting methodologies without any apparent effort to meet the contractual requirement of consistency. (A14-15, A43).

CB&I filed its Complaint on July 21, 2016. As alleged in the Complaint, Westinghouse's Closing Statement contains disguised claims for breaches of representations and warranties in the Agreement for which Westinghouse has no surviving claim or indemnity right as against CB&I (the "Non-Surviving Claims"). The Complaint provides significant detail on the three largest disputed items:

- ***Revenue Reserves for Claim Cost:*** A significant portion of "claim costs" are the portion of cost-overrun amounts that CB&I had estimated it would recover from either Westinghouse or the project owners. Westinghouse asserted (falsely) that CB&I's "claim cost" in the Net Working Capital Amount "estimated 100 percent collectability on impact-based scope work" and was thus "not in accordance with GAAP."

Westinghouse claimed that CB&I should have taken an *additional* 30% discount on these costs and, due to other accounting knock-ons, asserted a $903.9 million reduction in the Net Working Capital Amount. Effectively, in claiming that 30% discount, Westinghouse is asserting that CB&I should have assumed that Westinghouse would not honor its obligations under the consortium agreements and would successfully avoid liability for 30% of those claims. It was these very claims that led the parties to negotiate the resolution culminating in the Agreement, and which were specifically resolved in §1.3. (A43-47).

- ***ETC/EAC Liability Change:*** Estimate to Complete ("ETC") and Estimate at Completion ("EAC") are, respectively, the amounts that CB&I expected to expend on the projects in order to complete them and the total amount that would be spent on the projects once completed. Such estimates are a standard part of construction accounting and require forecasting of project costs. (A21-22, A25). Despite conducting thorough due diligence on the EAC and ETC for the projects, Westinghouse asserted that the projects will cost approximately $3.2 billion more to complete — a figure radically inconsistent with CB&I's prior Financial Statements — and that as of Closing CB&I should have recorded an additional liability of $956.6 million in

anticipation of these additional costs, reflecting again its improper additional 30% haircut on CB&I's anticipated recovery for cost overruns. (A21-22, A30-31, A45-47).

- ***Margin Fair Value Liability Claim:*** Margin fair value liability is a non-cash valuation account established by a purchaser at the date of an acquisition to reflect a reduction of the net purchase price that was obtained due to the buyer's assumption of an unfavorable contract. Westinghouse contends that CB&I wrongly excluded from the Financial Statements the remaining margin fair value liability of $432 million that CB&I had recorded in connection with its acquisition of the Shaw Group, S&W's prior parent, in 2013. Westinghouse advances this claim even though the financial statements provided by CB&I had consistently excluded this margin fair value liability when reflecting the Business to be transferred (as this non-cash liability did not involve a future cash outflow for CB&I or Westinghouse and thus had no relevance from Westinghouse's perspective) and the liability was never included in the net working capital peg diligenced by Westinghouse. (A48-49).

The Complaint explains that each and every one of Westinghouse's assertions concerning the Non-Surviving Claims, though packaged as a working capital dispute, is actually a claim for breach of representations and warranties that

was extinguished at Closing. (A43-49). Accordingly, CB&I's Complaint sought the Court of Chancery's intervention by requesting a declaration that the Agreement barred Westinghouse from smuggling the Non-Surviving Claims into the working capital true-up process, and asked for judicial enforcement of the parties' agreement that Westinghouse has no remedy for such claims.

Westinghouse filed its Answer on August 9, 2016. On September 2, 2016, Westinghouse filed a Motion for Judgment on the Pleadings. The Court of Chancery granted that motion in its entirety on December 2, 2016, and this appeal followed.

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN GRANTING WESTINGHOUSE'S MOTION FOR JUDGMENT ON THE PLEADINGS AS TO COUNT I.

A. Question Presented

Does the Agreement extinguish Westinghouse claims for breaches of CB&I's representations and warranties such that they may not be brought before the Independent Auditor as part of the Net Working Capital true-up procedure? This question was raised below (A460-82) and considered by the Court of Chancery (Op. 10-15).

B. Scope of Review

The Supreme Court reviews *de novo* a trial court's grant of a motion for judgment on the pleadings. *Desert Equities, Inc.* v. *Morgan Stanley Leveraged Equity Fund, II, L.P.*, 624 A.2d 1199, 1204-05 (Del. 1993).

C. Merits of Argument

The dispute here arises out of a common provision in private company purchase agreements: a post-closing, net working capital adjustment. These provisions, designed to take advantage of an accelerated proceeding in front of an accountant to put to rest quickly and finally disputes regarding changes in the condition of the sold business between signing and closing, have become increasingly ripe for dispute. Jorge L. Freeland & Nicholas D. Burnett,

Reevaluating Purchase Price Adjustments from A Seller's Perspective, The M&A Lawyer, July/Aug. 2009. This Court has not yet had an opportunity to speak on the important issues raised on this appeal. But the Court of Chancery and practitioners have set guideposts that prohibit Westinghouse's tactic here: funneling excessive working capital claims that upend the fundamental economic bargain of a deal into this accelerated, narrow, expert determination process in the hopes of recovering at least some additional amount. The Agreement contained two of the main provisions that have been identified in precedent cases to avoid the result reached below: a requirement that the working capital calculations be prepared on a basis "consistent" with past practices, and the mandate that the Independent Auditor would act "solely as an expert and not as an arbitrator." The Court of Chancery's opinion did not meaningfully address either.

1. *OSI*, not *Alliant*, is the guiding precedent.

The Court of Chancery erred in holding that *Alliant*, not *OSI*, is the "controlling precedent." Op. 15. *First*, the court erred when it held that the Agreement here and the agreement in *Alliant* both contain provisions "requir[ing] that the Closing Payment Statement and the Closing Statement comply with GAAP" — full stop. Op. 15. The presence of the term "GAAP" is not unique to *Alliant*: the contract in *OSI* also required that the working capital statements be prepared in accordance with "Transaction Accounting Principles" that included

GAAP in their definition. Compl. Ex. A, Ex. A ("Definitions"), *OSI Sys., Inc.* v. *Instrumentarium Corp.*, 892 A.2d 1086 (Del. Ch. 2006) (C.A. No. 1374-N) ("OSI Agreement"). But as in *OSI*, and by contrast with *Alliant*, the Agreement here does *not* require GAAP-compliance first, above all else. Instead, it requires that the Closing Statement be prepared in accordance with GAAP "*applied on a consistent basis* throughout the periods indicated and with the Agreed Principles." (§1.4(f) (emphasis added)). The Agreed Principles further require working capital to be calculated using GAAP "consistently applied" by CB&I in the preparation of the Financial Statements of the Business (Sch. 11.1(a)) — reinforcing that the point was to avoid GAAP disputes by accepting the methodology consistently used by CB&I.

This language matches the contract in *OSI*, not *Alliant.* The *OSI* contract provided:

> The Initial Modified Working Capital Statement shall be prepared in *accordance with the Transaction Accounting Principles applied consistently* with their application in connection with the preparation of the Reference Statement of Working Capital and the Statement of Estimated Closing Modified Working Capital. . .
>
> . . .
> "Transaction Accounting Principles" means U.S. GAAP; <u>provided</u>, <u>however</u>, that . . . with respect to any matter as to which there is more than one principle of U.S. GAAP, *Transaction Accounting Principles means the principles of U.S. GAAP applied in the preparation of the Financial Statements* . . . .

OSI Agreement § 2.09(a), Ex. A ("Definitions") (italic emphasis added). Thus, though GAAP was to play a role in *OSI* in the preparation of both the working capital calculations and the underlying financial statements (to which the company made representations and warranties), the working capital statements had to be prepared on a basis consistent with GAAP *as previously applied by the seller* — just as here.

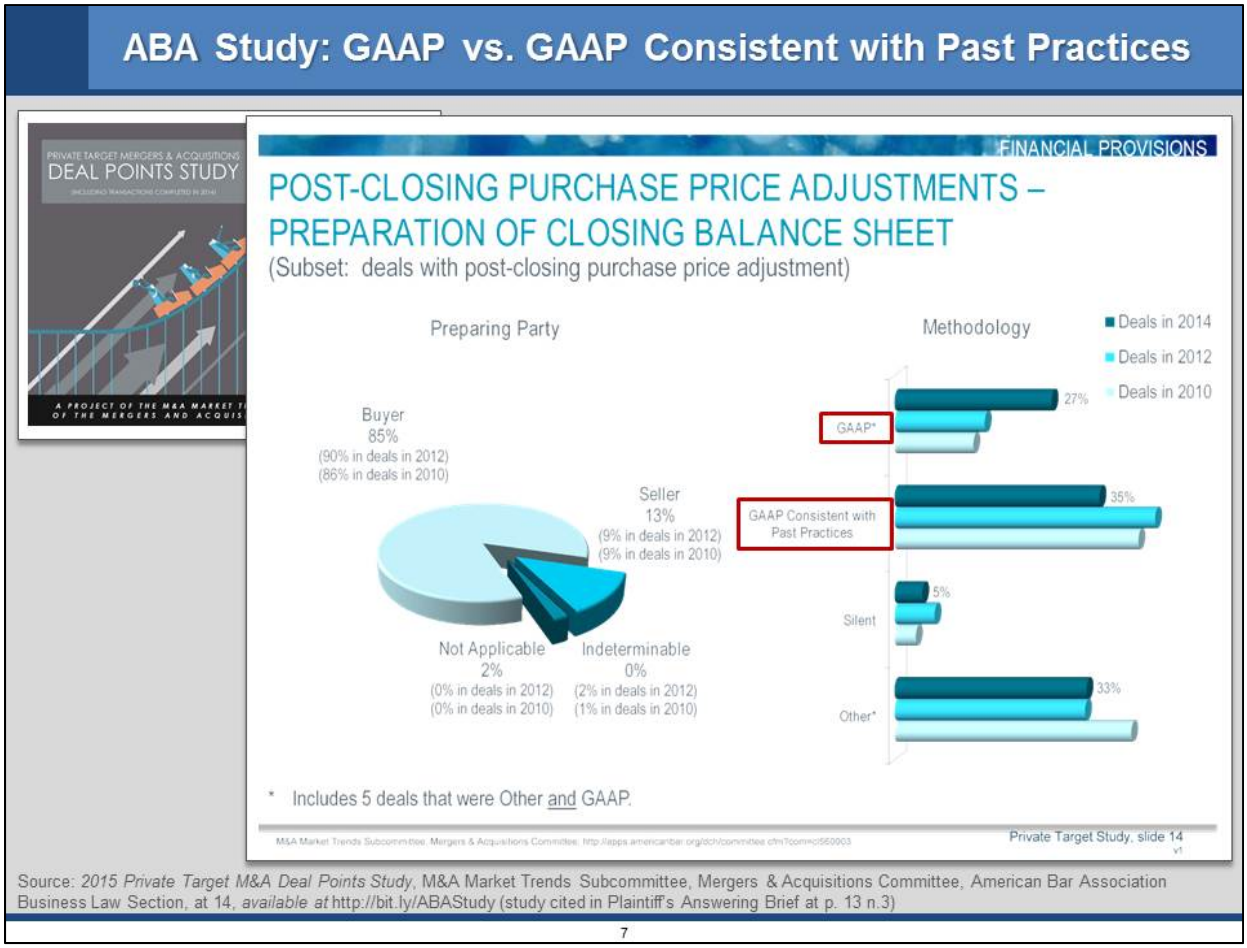
By contrast, the contract in *Alliant* provided:

> "Net Working Capital" means the sum of all current assets . . . of the Group Companies less the sum of all current liabilities . . . calculated *in accordance with GAAP and otherwise* in a manner consistent with the practices and methodologies used in the preparation of the Financial Statements referenced in Section 3.4(a)(i) . . . .

Compl. Ex. A § 1.1, *Alliant Techsystems, Inc.* v. *MidOcean Bushnell Holdings, L.P.*, 2015 WL 1897659 (Del. Ch. Apr. 27, 2015) (C.A. No. 9813–CB) (italic emphasis added). There, "GAAP and otherwise" explicitly contemplated that GAAP compliance — full stop — was the first and overriding objective. Consistency was secondary, only applicable to the extent not addressed by GAAP. The "GAAP and otherwise" language was not present in *OSI*, nor is it present here. Much as Chancellor Bouchard distinguished *Alliant* from *OSI*'s requirement of the *consistent* application of GAAP, *Alliant*, 2015 WL 1897659, at *11, the Court of Chancery should have done the same here.

Courts outside Delaware have similarly found this distinction determinative. In *Westmoreland*, New York's highest court held there was no question that provisions requiring working capital to be calculated "in accordance with GAAP *applied on a consistent basis with [the seller's] past practices*" meant that the buyer's objections alleging GAAP non-compliance had to be brought as an action at law for breach of representation. 794 N.E.2d at 668-70. And in another case, based on the same exact distinction, the Southern District of New York found that the seller's GAAP challenge *could* be brought before the accountant because the contract first and foremost required that "Closing Working Capital" be prepared "in accordance with U.S. GAAP" and only secondarily called for consistency. *HBC Solutions, Inc.*, 2014 WL 6982921, at *2.

Practitioners also recognize the difference between a post-closing true-up procedure seeking "GAAP" compliance and those seeking compliance with "GAAP consistent with past practice." The American Bar Association Business Law Section's *2015 Private Target M&A Deal Points Study* highlighted this exact distinction in categorizing different types of provisions in net working capital clauses:



M&A Market Trends Subcommittee, Mergers & Acquisitions Committee, American Bar Association Business Law Section, at 14, *available at* http://bit.ly/ABAStudy; A594, A642 (presenting slide during oral argument).

In sum, the "consistently applied" requirement is the critical distinction between the contracts in *Alliant* and in this matter. Yet the Court of Chancery's opinion does not mention it. The "consistently applied" language makes clear that the parties intended the working capital process to be a comparison of the working capital at the beginning and ending periods using the same GAAP methodologies — CB&I's methodologies — in each period. *See Westmoreland*, 794 N.E.2d at

671 ("What is most important is that, when preparing financial statements intended to be used for comparative purposes, the methodology be consistently applied . . . ."). Indeed, in a prior transcript ruling the Vice Chancellor below recognized that exact distinction. *See* Tr. of Oral Argument, *Gen. Dynamics Corp*. v. *Orbital Sciences Corp.*, C.A. No. 5759-VCL, at 70-71 (Del. Ch. Nov. 10, 2010) ("*Gen. Dyn.* Tr."). But the ruling below fails to deal with the "consistency" language and thereby undermines a significant contractual protection for CB&I on the scope of the Net Working Capital true-up before the Independent Auditor.

Second, the Court of Chancery erred in distinguishing *OSI* on the basis that "[a]s in *Alliant* and unlike in *OSI*, the Seller's representation [here] regarding the Company's financial statements being GAAP compliant did not encompass the Closing Payment Statement." Op. 15.

In the first place, the Court of Chancery was incorrect about the facts of *OSI*. Though the court found that the seller had provided representations and warranties as to the "Reference Statement," which is the equivalent of the Target Net Working Capital figure here, *OSI*, 892 A.2d at 1087, 1092-93, the representations and warranties in *OSI* did *not* extend to the equivalent of CB&I's Closing Payment Statement, there called the "Statement of Estimated Closing Modified Working Capital." *Id.* at 1088. Regardless, this is a distinction without meaning where a seller's statement of working capital "flow[s] from the financial statements

that were the subject of [its] contractual representation[s]." *Severstal U.S. Holdings, LLC* v. *RG Steel, LLC*, 865 F. Supp. 2d 430, 441 (S.D.N.Y. 2012); *see also Gen. Dyn.* Tr. 70 (finding it irrelevant that the target net working capital number was a "negotiated amount" because it was still "based on financial statements" for which representations were made). This follows as a matter of both the Complaint's allegations and logic: the working capital adjustment here is based on and derived from past financial statements (A26-27) — it is, unsurprisingly, *not* made "out of whole cloth." *Gen. Dyn.* Tr. 68.

Numerous courts have recognized that a challenge to a working capital adjustment based on GAAP compliance is necessarily a back-door challenge to previous financial statements that used that same GAAP methodology. The *Westmoreland* court applied this precise principle: to the extent the buyer's objections "related to accounting conventions, estimates, assumptions or asset values *common to both* the interim financial statements [for which representations and warranties were made] and the closing date certificate," they "unambiguously" formed breach of representation claims that could not be addressed through the contract's purchase price adjustment procedure. 794 N.E.2d at 670. Furthermore, "insofar as [the buyer] objected to asset values carried over from the interim financial statements to the closing date certificate for failure to comply with

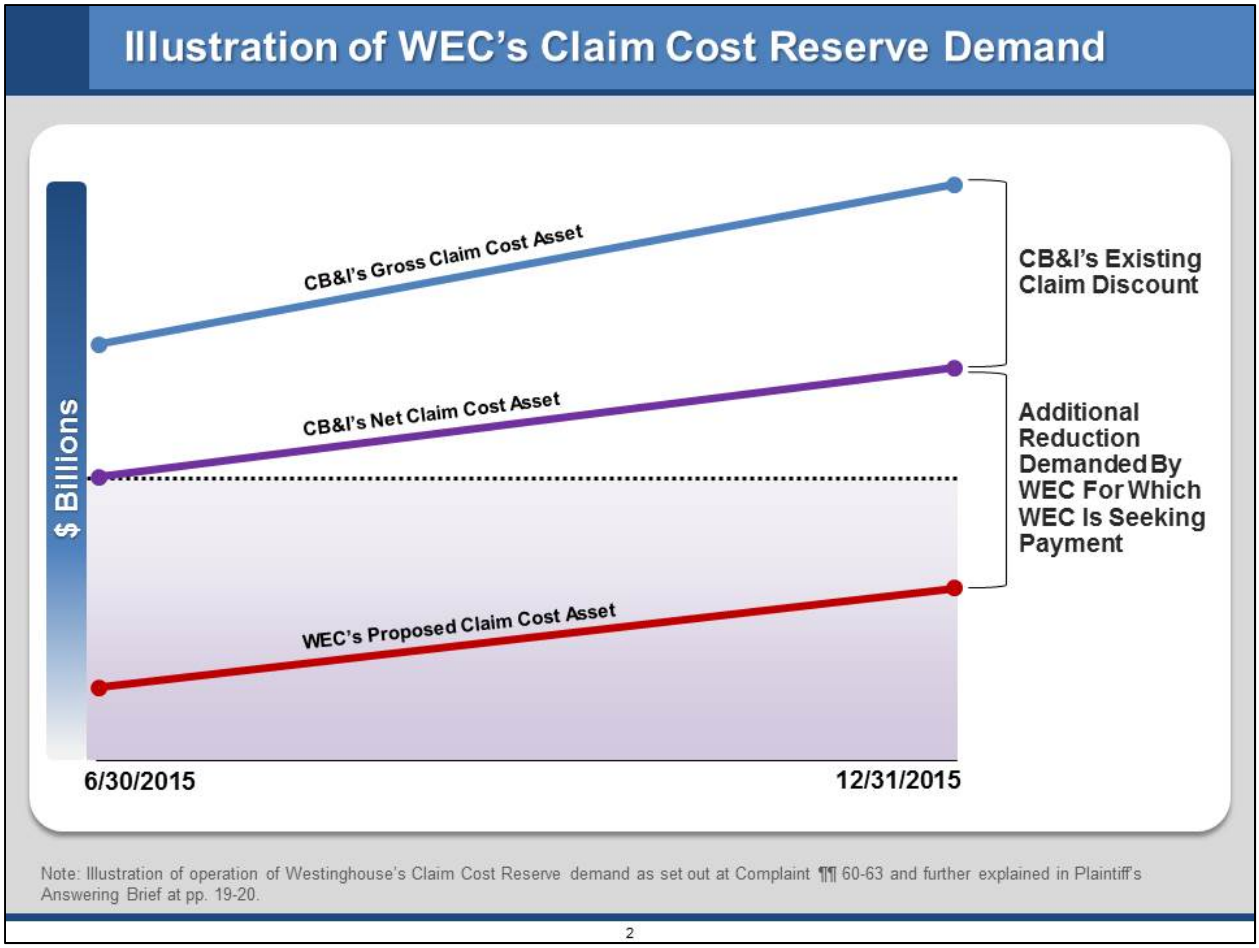
GAAP, consistently applied," the buyer's only remedy was to bring a claim for breach of representation in court. *Id.* at 669; *see also OSI*, 892 A.2d at 1095.

This contractual connection between the Net Working Capital amount and CB&I's prior financial statements is particularly significant here. The accounting judgments at issue require assessing estimates of planned costs through completion of the projects several years into the future that, as a matter of accounting for construction projects, are carried forward period to period and used to calculate current period net working capital. (A25, A46-47). Changes to those estimates in one period, such as those propounded by Westinghouse as of Closing, necessarily implicate CB&I's Financial Statements in the earlier period for which it provided representations and warranties. Westinghouse is thus not solely attacking the GAAP compliance of the working capital calculations as of December 31, 2015, but is *necessarily* contesting CB&I's Financial Statements from which the Target Net Working Capital Amount was derived — a challenge precluded by §10.1 of the Agreement. (A42-49).

For example, Westinghouse, in its assessment of the value of working capital as of December 31, 2015, takes an extra 30% haircut from the "claim cost" asset (and made other accounting adjustments that further reduced this asset). In asserting that position, Westinghouse is wiping off of the balance sheet a large portion of an asset virtually all of which existed on June 30, 2015. In other words,

Westinghouse can only be saying one of two things: (i) that CB&I did not fairly present its Financial Statements, in breach of either §2.6(a) or §2.6(e); or (ii) assuming the GAAP-compliance of the Financial Statements as of June 30, 2015, that between June 30 and December 30 there was a change so monumental that it wiped out more than $900 million in working capital, which can only amount to an allegation that CB&I breached its representation in §2.19 regarding the absence of any Material Adverse Effects since June 30, 2015. In any case, Westinghouse is taking a position that is precluded by its clear agreement not to contest CB&I's Financial Statements once it closed. That core agreement drove the essence of the bargain: that post-Closing CB&I would be relieved of any further liability for the Financial Statements (or otherwise).

The high-level graphic below, shown to the Court of Chancery at oral argument (A577-78), illustrates that Westinghouse's adjustment applies to prior periods. And, even if one were to look simply at Westinghouse's December figure, Westinghouse's proposed reduction brings the value of the asset well below where it was in June (as indicated by the purple shading showing the value of the asset as reflected on the June balance sheet). (A637).



The Agreement prohibits Westinghouse from seeking, through the guise of a working capital dispute, recovery for claims that necessarily implicate CB&I's prior Financial Statements and amount to a contention that those Financial Statements were "infected" with accounting error. *OSI*, 892 A.2d at 1095. Or to put it another way, if Westinghouse prevails on its claim, it will be paid monies for amounts that should have been on the balance sheet as of June 30, even at the same time that it gave up any right (at §10.1) to assert such claim post-Closing. As then-Vice Chancellor Strine made clear in *OSI*, such an "end-run [of] the contractual Indemnification process" cannot be sanctioned. *Id.*

Third, the Court of Chancery erred in relying on the notion that, as in *Alliant*, the parties' Agreement contains a "carve-out" clause at §10.3. Op. 15. It is true that §10.3 and its parallel in *Alliant* both state that no indemnification remedy shall "operate to interfere with or impede the operation of the [net working capital adjustment] provisions." The *Alliant* court — in short order, and after having already determined that a challenge to GAAP compliance *could* be part of the purchase price adjustment because the contract there lacked the "consistency" requirement — called this language a "trumping provision," *Alliant*, 2015 WL 1897659, at *9, because it was triggered when "a dispute could be brought *either* as part of the purchase price adjustment procedure *or* as an indemnification claim." *Id.* at *2 (emphasis added).

Here, however, absent actual fraud, the Agreement barred Westinghouse from bringing a breach of representation claim *at all* after Closing. The Court of Chancery's ruling that due to §10.3 all of CB&I's claims, including any argument about the impact of §10.1, are for the Independent Auditor misses the fundamental point: the parties bargained for a narrow working capital adjustment provision like the one in *OSI* where the Agreed Principles limit the scope of disputes before the Independent Auditor to those applying Seller's (CB&I's) GAAP methodology, "consistently applied." By advocating for GAAP methodologies that deviate from those accounting practices used by CB&I in generating the Financial Statements,

Westinghouse is asserting a position that necessarily may not be considered as part of the working capital process. It is a claim that Westinghouse agreed to extinguish. There is therefore no overlap that needs to be "carve[d]-out."

2. The Court of Chancery's decision undermines the overall purpose and structure of the Agreement.

It is a "cardinal rule . . . that, where possible, a court should give effect to *all* contract provisions." *Martin Marietta Materials, Inc.* v. *Vulcan Materials Co.*, 68 A.3d 1208, 1221 (Del. 2012) (quotation omitted) (italics in original). "The meaning inferred from a particular provision cannot control the meaning of the entire agreement if such an inference conflicts with the agreement's overall scheme or plan." *GMG Capital Investments, LLC* v. *Athenian Venture Partners I, L.P.*, 36 A.3d 776, 779 (Del. 2012). Thus, complex commercial contracts such as the Agreement "are best interpreted not by focusing on a single clause, but by considering the parties' language in the context of their entire agreement." *First Olefins L.P.* v. *Am. Olefins, Inc.*, 1996 WL 209719, at *7 (Del. Ch. Mar. 1, 1996). The Court of Chancery's Opinion ignores this cardinal principle, effectively allowing the Net Working Capital process set forth in §1.4 to swallow the entire Agreement and negate the critical contractual provision designed to allow CB&I to exit the scene with no liability based on any attack on its prior accounting practices.

First, the Agreement is clear that CB&I is to have no liability for breaches of representation and warranty after Closing. In *OSI*, the court recognized that the buyer's position in the net working capital true-up process was an attempt to "end-run the contractual Indemnification process" which provided for a *cap* to its recovery. 892 A.2d at 1095. That concern is even stronger here. Rather than attempting to avoid a cap on recovery, Westinghouse is seeking to avoid an entire elimination of recovery under § 10.1: "there shall be **no liability** for monetary damages after the Closing in respect thereof."[5]

As detailed in the Complaint, the transaction was to operate as a "quitclaim" in which CB&I was to walk away from the projects free and clear. This intent is confirmed throughout the Agreement. (*See* pp. 8-13, *supra*). The express terms of §10.1 — cutting off liability after Closing for a breach of CB&I's core financial representations — unambiguously capture this fundamental goal. Then-Chancellor Strine recognized the clear contractual intent of non-survival provisions in *GRT, Inc.* v. *Marathon GTF Technology, Ltd.*, observing that:

> where the contract expressly provides that the representations and warranties terminate upon closing . . . the parties have made clear their intent that they can provide no basis for a post-closing suit seeking a remedy for an alleged misrepresentation. That is, when the

[5] Section 10.1 does preserve CB&I's liability to Westinghouse "in respect of actual fraud." But the Agreement precludes Westinghouse from making the same claims before the Independent Auditor freed from the heavy burden of proof for such "actual fraud" claims that the parties bargained for, and the procedural protections that would be afforded in any such "actual fraud" action.

> representations and warranties terminate, so does any right to sue on them.

2011 WL 2682898, at *13 (Del. Ch. July 11, 2011).

Here, the Court of Chancery offered no explanation as to how there could be both a clear bar to any remedy for breach of representation and warranty (§10.1) and yet, at the same time, permit recovery by Westinghouse for such matters through the working capital process in §1.4(c), effectively reading §10.1 out of the Agreement altogether.[6] The notion that in essentially the same breath, the parties freed (at §10.1) CB&I from any such liability but gave Westinghouse the right to pursue such a claim by way of §10.3 makes no sense. Section 10.3 only preserved the right for Westinghouse to pursue proper claims before the Independent Auditor, but a claim that CB&I breached GAAP is not proper as it is inconsistent with the GAAP "consistently applied" standard. Any other reading renders §10.1 a dead letter.

Second, the Court of Chancery also seemed to accept Westinghouse's argument (A257; A515) that somehow the GAAP-compliance of the Financial

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[6] Westinghouse's counsel all but conceded this at oral argument before the Court of Chancery. In an effort to preserve §10.1 as meaningful, counsel offered that under Westinghouse's reading of the contract perhaps §10.1 could do work to protect CB&I from "third-party claims that reflect certain of the representations and warranties or that implicate certain of those representations and warranties," but not (critically) from claims for such breaches by Westinghouse. (A548). Of course this is not what CB&I bargained for in entering into a "quitclaim" agreement *with Westinghouse*. Nor does it make sense for CB&I to be freed of liability from claims originating with "third-parties" *but not Westinghouse*.

Statements, the accuracy of which was represented to in Article II, was divorced from any GAAP-compliance mandated by Article I in determining the Net Working Capital amount. *See* Op. 13, 15. It is illogical, and contrary to the clear rules of Delaware law that complex business contracts be read as a whole, that the parties would have agreed to use one GAAP standard to measure the Business being sold pre-Closing and an entirely separate standard to measure the post-Closing true-up of Net Working Capital for purposes of the determination of the purchase price. But even more, the plain language of §1.4(f) requires Westinghouse's Closing Statement to be prepared in accordance with GAAP "applied on a consistent basis throughout the periods indicated and with the Agreed Principles." (§1.4(f)). The Agreed Principles require working capital to be calculated using GAAP "consistently applied" by CB&I in the preparation of the financial statements of the Business. (Sch. 11.1(a)). Neither the Court of Chancery nor Westinghouse have provided an explanation for how the so-called "Article I calculations" can be completely severed from the Financial Statements represented and warranted in Article II.

By contrast, CB&I has set out a consistent reading of the Agreement that allows both the §1.4 process and the §10.1 bargain to be respected. Had CB&I operated the Business between June 30, 2015 and December 31, 2015, in a manner that caused the net working capital to fall below the peg, Westinghouse would

have been entitled to recover the difference. That was the deal. Conceivably, in the absence of §10.3, CB&I could have sought indemnification from Westinghouse for such a "Loss" relating to the Projects pursuant to §10.4. This of course would have been improper. This is the work that §10.3 does in the Agreement: It prevents CB&I from starving the business, as a working capital true-up is meant to do, and allows Westinghouse to recover, dollar for dollar, had CB&I failed to maintain the business between signing and closing. It does not allow Westinghouse to negate the essence of the entire deal by, with a nothing-to-lose mentality, making massive claims in the Independent Auditor process that would entirely vitiate the agreed-to relinquishment of any claims as to the GAAP-compliance of CB&I's Financial Statements, in the hope that a non-law trained accountant will "split the baby" or otherwise award them at least some of this outlandish claim.

3. The Court of Chancery's holding improperly expands the authority of the Independent Auditor.

Finally, the Court of Chancery erred in ruling that the language of §1.4, providing that "any and all matters that remain in dispute with respect to the Objections Statement, the Closing Statement and the calculations set forth therein," somehow brings breach of representation claims (subject to an "actual fraud" standard) within the Independent Auditor's authority. Op. 15.

First, the phrase "any and all matters" cannot be read in a vacuum. This is typical language found in many working capital provisions, including those meant to be read narrowly. For example, the contract in *OSI* outlined a process for resolving disputes over working capital that was nearly identical to the one in the Agreement. Like here, the parties were to exchange specific objections to the working capital calculations, negotiate for a set period of time, and then, "all matters that remain in dispute" were to be submitted to the Independent Auditors. The following chart demonstrates that the Agreement here mirrors the *OSI* agreement.

***OSI* Agreement**	**CB&I/WEC Agreement**
§2.10(a): "Instrumentarium shall notify the Acquiror in writing (the 'Notice of Disagreement') prior to the expiration of the Review Period if Instrumentarium disagrees with the Initial Modified Working Capital Statement. The Notice of Disagreement shall set forth in reasonable detail the basis for such dispute, the amounts involved and Instrumentarium's determination of the amount of Working Capital and Modified Working Capital as of the Closing Date."	§1.4(b): "If Seller Parent has any objections to the Closing Statement and/or any calculations set forth therein, Seller Parent shall deliver to Purchaser a statement setting forth its objections thereto and, in reasonable detail, the reasons therefor, a specific dollar amount related to each objection and Seller Parent's alternative calculations with respect to each disputed item (the 'Objections Statement')."

***OSI* Agreement**	**CB&I/WEC Agreement**
§2.10(c): "If at the end of the Consultation Period Instrumentarium and the Acquiror have been unable to resolve any differences that they may have with respect to the matters specified in the Notice of Disagreement, Instrumentarium and the Acquiror shall submit all matters that remain in dispute with respect to the Notice of Disagreement (along with a copy of the Initial Modified Working Capital Statement marked to indicate those line items that are not in dispute) to" the Independent Auditor. (emphasis added)	§1.4(c): "At the end of such 30-day period, Seller Parent and/or Purchaser may submit to the Independent Auditor for review and resolution in accordance with the terms and provisions hereof, any and all matters that remain in dispute with respect to the Objections Statement, the Closing Statement and the calculations set forth therein." (emphasis added)

This "any and all" language cannot and should not be read to make the net working capital true-up process so broad as to swallow the rest of the contract. The only proper reading of the contract's emphasis on GAAP "consistently applied," as in the contract in *OSI*, is that the Net Working Capital calculation — contractually set to occur only after the extinguishment of Westinghouse's ability to challenge CB&I's representations regarding its Financial Statements — was "designed to handle disputes about the extent of change in" the Company's working capital between the negotiation and closing. *OSI*, 892 A.2d at 1095. There is no basis upon which to find that the provision in *OSI* was meant to be narrow, but the one in the Agreement here was meant to be broad.

Second, as a result of the improper emphasis placed on the single phrase "any and all," the Court of Chancery's ruling expands the authority of the

Independent Auditor beyond anything the parties could have reasonably conceived, effectively reading out of the contract the language "acting as an expert, not an arbitrator." The Court of Chancery concluded that the language of §1.4 was "sufficiently broad to encompass determinations about GAAP compliance" — which as just discussed was itself incorrect — but then issued an order providing that *all* of CB&I's claims could be properly presented before the auditor. Those claims include legal issues of contract interpretation and potentially the application of an "actual fraud" standard, both of which are "not generally viewed as the kind of disputes that would be resolved by the person charged with 'truing up' the books." *Matria Healthcare, Inc.* v. *Coral SR LLC,* 2007 WL 763303, at *6 (Del. Ch. Mar. 1, 2007). This type of intricate legal exercise could not be further from "examining the corporate books and applying normal accounting principles." Op. 14 (citing *Alliant*, 2015 WL 1897659, at *10).

Indeed, though the Court of Chancery here indicated that "Chancellor Bouchard . . . observed [in *Alliant*] that courts in Delaware and elsewhere had already interpreted the scope of similar provisions to encompass assessments of accounting methodology," the court oversimplified the holdings of the cases "collect[ed]" in the *Alliant* opinion. Op. 14. The court in *Alliant*, in an attempt to give meaning to the word "expert," cited *Matria*, *HBC Solutions*, and *Severstal* for the proposition that other courts, under their unique facts, had held that accountants

are generally competent to consider "assessments of accounting methodology" rather than just do "math." *Alliant*, 2015 WL 1897659, at *10. But none of those opinions dealt with the language at issue here requiring that the Independent Auditor "function[] solely as an expert and *not as an arbitrator*." Courts that have specifically considered the effect of that language have made clear that it has meaning. This includes the *Alliant* court: a sentence of the *Alliant* opinion partially quoted by the Court of Chancery contrasts the process of resolving disputes "as accountants do" with "entertaining arguments from lawyers and listening to testimony," *id.* (quoting *Omni Tech Corp.* v. *MPC Solutions Sales, LLC*, 432 F.3d 797, 799 (7th Cir.2005)), which is exactly what the Order erroneously now contemplates will happen before the Independent Auditor if CB&I's §10.1 contention is to be properly considered. *See also Westmoreland*, 794 N.E.2d at 671-72 (The buyer's "objections related to noncompliance with GAAP are, in fact, claims for breach of a representation or warranty. ***These claims may only be pursued in a court of law, with its attendant protections of discovery, rules of evidence, burden of proof, and full appellate review***." (emphasis added)).

Finally, in conflating the contract's narrow working capital adjustment provision with a traditional all-encompassing arbitration clause, the ruling below upends the settled expectations of the parties and undermines Delaware's strongly contractarian principles. As the Court of Chancery recognized, both CB&I and

Westinghouse are sophisticated parties — and they chose the words of their contract deliberately. The specification that the Independent Auditor is to function "solely as an expert and not as an arbitrator" has to be given meaning — and the Court of Chancery's interpretation gives it none. This Court, which has not previously ruled on the precise import of this commonly used language, should clarify the boundaries between (a) the limited expert determination provision the parties chose here, and (b) a sweeping arbitration clause whereby the parties intend to delegate to a non-judicial decision maker with the authority to decide all legal and factual issues necessary to resolve a dispute. *See* Purchase Price Adjustment Clauses and Expert Determinations: Legal Issues, Practical Problems and Suggested Improvements 16-20 (June 2013) (including "acting as an expert, not an arbitrator" language in sample purchase agreement to ensure narrow treatment of working capital process); *AQSR India Private, Ltd.* v. *Bureau Veritas Holdings, Inc.*, 2009 WL 1707910, at *2 (Del. Ch. June 16, 2009) (finding a provision similar to §1.4(c) to be "a narrow dispute resolution mechanism that is designed to take advantage of the technical expertise, rather than the arbitration skills, of the Referee"). As things stand in light of the decision below, this distinction has been eviscerated.

II. THE COURT OF CHANCERY ERRED IN GRANTING JUDGMENT ON THE PLEADINGS AS TO COUNT II.

A. Question Presented

Did CB&I plead sufficient allegations to survive a motion for judgment on the pleadings as to Count II, in particular given that Westinghouse made no argument on Count II in its opening brief in support of its motion? CB&I presented the argument that Westinghouse had waived any argument as to Count II (A482-85, A606-14) but the Court of Chancery's opinion did not address it.

B. Scope of Review

The Supreme Court reviews *de novo* a trial court's grant of a motion for judgment on the pleadings. *W. Coast Opportunity Fund, LLC* v. *Credit Suisse Sec. (USA), LLC*, 12 A.3d 1128, 1131 (Del. 2010).

C. Merits of Argument

1. Westinghouse waived any argument as to Count II by failing to address the merits of CB&I's claims in its opening brief.

Westinghouse waived any argument it had with respect to Count II by ignoring it altogether in its brief in support of its motion for judgment on the pleadings. Its waiver could not have been starker: Westinghouse's opening brief contained not a single argument in support of judgment on Count II. But even if Westinghouse had not yet waived any argument that Count II fails to state a viable claim, in its Reply Brief Westinghouse unambiguously *admitted* that it was seeking

dismissal of Count II "*not* for failure to state the elements of a claim" but rather "because the parties' dispute does not belong before this Court." (A520 (emphasis added)).

Under the circumstances, the Court of Chancery committed reversible error in granting judgment on the pleadings of Count II. The decision, which did not address CB&I's argument of Westinghouse's waiver, did not follow authority establishing that a party's failure to address a legal argument in its opening brief constitutes waiver. *Emerald Partners* v. *Berlin*, 726 A.2d 1215, 1224 (Del. 1999) ("Issues not briefed are deemed waived."); *see also Murphy* v. *State*, 632 A.2d 1150, 1152 (Del. 1993); *Haney* v. *Blackhawk Network Holdings, Inc.*, 2016 WL 769595, at *7 (Del. Ch. Feb. 26, 2016). Westinghouse's waiver should have been fatal as to Count II.

On these grounds alone, this Court should reverse the Court of Chancery's judgment on the pleadings of Count II. Even as the Court of Chancery dismissed Count I in favor of permitting the Independent Auditor to resolve CB&I's Count I claims, it dismissed the dispute in Count II not in favor of the Independent Auditor but instead on the merits of a position indisputably waived by Westinghouse.

2. Regardless of waiver, CB&I stated a claim sufficient to survive judgment on the pleadings as to Count II.

CB&I stated a claim in Count II that Westinghouse has breached the implied covenant of good faith and fair dealing by attempting to upend the finality of the

parties' painstaking resolution of their dispute over responsibility for cost overruns. Despite CB&I's well-pleaded allegations, as summarized below, the Court of Chancery summarily dismissed Count II, holding: "Because the Purchase Agreement addresses the matter, there is no gap for the implied covenant to fill." Op. 16. Yet the Court of Chancery identified no provision at all in the Agreement that purportedly addresses the terms that CB&I pleaded must inhere in the contract. This constitutes reversible error.

In fact, the Complaint details how the terms, structure, and entire purpose of the Agreement make clear that the parties entered into the transaction to put an end to their long-standing dispute over Westinghouse's financial responsibility for cost overruns. (A12, A25-29, A35-36, A43-45, A52-53). The parties thus designed a specific mechanism to resolve how CB&I would recover on its $1.16 billion claim cost. (*See, e.g.*, A14, A25, A28, A35-36, A44-47, A52-53). Section 1.3 and its related schedules in the Agreement spell out the parties' compromise solution: the contract granted CB&I a mixture of deferred payments and a share of future Westinghouse profit, if any, with CB&I's potential recovery limited to $544 million of the $1.16 billion claim cost asset recorded in the target net working capital peg in exchange for a *total* release from future liability. The parties' intent with respect to this provision resolving their global dispute is clear — all that is missing is an explicit statement reflecting their understanding that these payments

were negotiated specifically to compensate CB&I on its cost overrun claims as part of a "quitclaim" transaction in which the dispute over recoverability on these cost overruns could not be subsequently revisited through any other provision in the Agreement.

It is settled Delaware law that where the parties had "understandings or expectations that were so fundamental that they did not need to negotiate about those expectations," the implied covenant serves as a gap-filling measure to preserve these fundamental expectations. *NAMA Holdings, LLC* v. *The Related Cos., L.P.*, 2014 WL 6436647, at *16 (Del. Ch. Nov. 17, 2014). "To supply an implicit term, the court looks to the past and asks what the parties would have agreed to themselves had they considered the issue in their original bargaining positions at the time of contracting." *Allen* v. *El Paso Pipeline GP Co.*, 113 A.3d 167, 184 (Del. Ch. 2014) (internal citation omitted).

The implied terms that CB&I asked the Court of Chancery to supply directly reflect, and are fully consistent with, the parties' fundamental expectations in negotiating the Agreement. It is clear that, had the issue been raised *ex ante*, CB&I and Westinghouse would have proscribed Westinghouse from launching a renewed challenge to CB&I's claim cost recoverability by casting aside the carefully crafted resolution reached in §1.3 through the guise of another provision in the very same Agreement. It is inconceivable that the parties would have ever agreed that

Westinghouse could upend the finality of the resolution the parties painstakingly reached in §1.3, and further diminish the value of CB&I's claim cost asset through a further 30% haircut. But that is exactly what Westinghouse has done in its two largest claims before the Independent Auditor in the true-up process. (A21, A30-31, A43-47). This ought not be permitted, in particular in this case where Westinghouse has nowhere disputed that CB&I's well-pleaded allegations state a viable claim for breach of the implied covenant.

CONCLUSION

For the foregoing reasons, this Court should reverse the Court of Chancery's grant of judgment on the pleadings in favor of Westinghouse, and remand for further proceedings in the Court of Chancery.

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