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Case Number 180,2020

IN THE SUPREME COURT OF THE STATE OF DELAWARE

TEMPERATSURE HOLDINGS, LLC, a Delaware limited liability company,	)	
Defendant/Counterclaim Plaintiff/Third Party Plaintiff-Below/Appellant,	)	No. 180, 2020
v.	)	
	)	CASE BELOW:
B&C HOLDINGS, INC., a Colorado corporation,	)	Superior Court of the State of Delaware
Plaintiff/Counterclaim Defendant Below/ Appellee,	)	C.A. No. N19C-02-105 AML CCLD
and	)	
CHRISTOPHER SMITH,	)	
Third Party Defendant-Below/Appellee.	)	

ANSWERING BRIEF OF APPELLEES B&C HOLDINGS, INC. AND CHRISTOPHER SMITH

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Dated: October 9, 2020

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NATURE OF PROCEEDINGS

This appeal is about an unambiguous contract. The contract is the promissory note ("Note") that Appellant Temperatsure Holdings, LLC ("Temperatsure") made in favor of Appellee B&C Holdings, Inc. ("B&C") when Temperatsure bought B&C's company in 2016 (the "Transaction"). The Note's principal ("Principal") represents the Transaction's earnout component.

The Note required Temperatsure, after calculating the earnout, to send B&C a "Principal Statement." A Principal Statement, according to the Note, is just a "statement setting forth [Temperatsure's] calculation of the Principal," *i.e.*, the earnout. If B&C did not dispute Temperatsure's statement within 15 days, the Principal would be "final and binding."

In July 2017, Temperatsure's CFO, Robert Kahle, sent B&C's co-owner, Appellee Christopher "C.P." Smith, an email (the "CFO's Email") confirming what Kahle previously had told Smith orally: that Temperatsure had calculated the Principal to be the Note's $6,000,000 maximum. B&C did not dispute that Principal. For nearly a year, the parties performed based on the $6,000,000 Principal. Temperatsure twice paid B&C interest based on that Principal. Board-meeting packages reported the $6,000,000 Principal. With board-member knowledge, Temperatsure reaffirmed to its auditors the $6,000,000 Principal. When it was struggling to comply with the covenants in its senior debt agreement, Temperatsure

even asked B&C to help it by converting its $6,000,000 debt into 6,000,000 equity units. Only when B&C refused Temperatsure's request to convert its debt (after Temperatsure refused to cover any resulting tax liability) did Temperatsure repudiate its statements that the Principal is $6,000,000, contend that it never sent B&C a Principal Statement, and send B&C a new statement asserting a lower Principal.

The Superior Court (the "Court") correctly held that the CFO's Email is Temperatsure's Principal Statement under that term's plain-English definition. It correctly rejected Temperatsure's attempts to graft onto the definition other requirements contrary to the Note's text and overall scheme. Because B&C did not dispute the Principal Statement, the $6,000,000 Principal is final and binding.

This appeal also includes Temperatsure's attempt, which the Court also properly rejected, to use a fiduciary duty claim to blame Smith for what Temperatsure now says was its error in calculating the Principal. Because of his conflict of interest, being both B&C's Transaction representative and Temperatsure's post-closing president, Smith rightly took no part in Temperatsure's calculation and, accordingly, had no reason to think Kahle erred. Temperatsure cites no authority finding a duty of candor violation in similar circumstances.

SUMMARY OF ARGUMENT

1. Denied. The Court did not err by holding that the CFO's Email is Temperatsure's Principal Statement. The Note defines Principal Statement as "a statement setting forth [Temperatsure's] calculation of the Principal." This simple definition is consistent with the Note's overall scheme, which directed Temperatsure to detail its underlying calculations in "LTM Gross Profit Statements," not the Principal Statement. The CFO's Email is a statement setting forth Temperatsure's Principal calculation. It is thus Temperatsure's Principal Statement.

Temperatsure's scattershot arguments to the contrary all miss the mark. For example, although Kahle did not write the number "$6,000,000," his email states its mathematical equivalent. Temperatsure invokes various contract provisions that it violated, but neither the Note nor Delaware law permits Temperatsure to use its own breaches to escape its promise that if it delivered a statement setting forth its Principal calculation and B&C did not dispute that statement, Temperatsure's stated Principal would be final and binding.

2. Denied. The Court did not err by rejecting Temperatsure's failure-of-a-condition-precedent defense. Temperatsure abandoned that defense when B&C argued on summary judgment that the defense is meritless and Temperatsure did not respond. In addition, the Note shows that Temperatsure's performing a GAAP LTM Gross Profit calculation was, in any event, not a condition of its being bound by its

own Principal Statement. Because the Court correctly held that a GAAP calculation was not a condition precedent, its conclusion that even if such a condition existed, Temperatsure waived it, is not a ground for reversal.

3. Denied. The Court correctly held that Temperatsure's interpretation of the Note is unreasonable. Temperatsure criticizes the Court for citing *Greenstar IH Rep, LLC v. Tutor Perini Corp.* but *Greenstar* is on point.

4. Denied. The Court did not err by rejecting Temperatsure's fiduciary duty claim. Temperatsure insinuates that Smith concealed from the board that Kahle miscalculated the Principal or so seriously failed to follow the Note's Principal-calculation procedures that Smith must have known the $6,000,000 Principal was wrong. The record shows, however, that the only "procedure" Smith knew Kahle had not performed was delivering LTM Gross Profit Statements to B&C. Though not delivering those statements was a contract breach, it was a harmless one because once Temperatsure informed B&C that the earnout was the maximum, B&C had nothing to dispute and so did not need the undelivered information. Importantly, because of his conflict of interest, Smith refrained from discussing the substance of the earnout determination with Kahle and thus had no reason to think Kahle erred. By respecting his conflict of interest, Smith acted loyally to Temperatsure, not disloyally.

STATEMENT OF FACTS

A. The Parties

Smith founded the predecessor to Temperatsure LLC ("OpCo") in 2004. JA1758, 138:9-21. Smith and his wife formed B&C to hold their OpCo equity. JA282, ¶ 2. The private equity firm Endeavour Capital formed Temperatsure to buy OpCo from B&C. JA2721, 9:21-23. Temperatsure is now OpCo's sole owner. *Id.* 9:19-20. Three Endeavour funds own a majority of Temperatsure's equity. JA2721, 10:3-5. B&C is a minority owner of Temperatsure. *Id.* 10:6-8.

The board's four members other than Smith comprise Temperatsure's Special Litigation Committee ("SLC"). JA638, ¶ 78. Smith was Temperatsure's CEO from the Transaction until 2018. JA2721, 10:14-23; JA283, ¶ 4.

B. The Note

Part of B&C's consideration for selling OpCo in 2016 was an earnout embodied in the Note. JA2721, 9:8-11. The earnout was to be determined based on Temperatsure's and OpCo's consolidated gross profits during the last twelve months ("LTM Gross Profit"), measured at the end of each month from January through July 2017. JA771, §§ 1(ii)-(iii). If any month's LTM Gross Profit reached $19,000,000, the Principal would be $6,000,000. *Id.* § 1(iii). If LTM Gross Profit never exceeded $18,000,000, the Note would terminate. *Id.* If the highest LTM Gross Profit fell

between $18,000,000 and $19,000,000, the Principal would be between $0 and $6,000,000, determined on a straight-line basis using that LTM Gross Profit. *Id.*

Within 15 days after each measurement period, Temperatsure was supposed to deliver to B&C a statement setting forth that month's LTM Gross Profit. *Id.* § 2(a). Each "LTM Gross Profit Statement," as the Note called it, was to include "reasonable supporting documentation for the estimates and calculations contained therein (together with any information reasonably requested by [B&C])." *Id.* By August 15, 2017, 15 days after the last measurement period, Temperatsure had to deliver to B&C "a statement setting forth its calculation of the Principal." JA772, §§ 2(c). The Note calls this statement the "Principal Statement." *Id.*

What would happen next depended on whether B&C wanted to dispute the Principal Statement. If so, B&C had to send Temperatsure a "Dispute Notice" within 15 days. *Id.* The Note calls such a dispute a "Dispute." *Id.* If B&C initiated a Dispute, Temperatsure had 15 days to respond. *Id.* If Temperatsure responded and the parties could not resolve their Dispute, an Arbitrating Accountant would. *Id.*

If, on the other hand, B&C did not want to dispute the Principal Statement, it needed only to refrain from sending a Dispute Notice:

> If [B&C] does not deliver to [Temperatsure] within [15 days] a [Dispute Notice], then (i) the Principal Statement and the calculation of the Principal will be deemed to have been accepted and agreed to by [B&C] and will be final and binding upon the parties; and (ii) the Principal set forth in the Principal Statement will be the Principal for all purposes of this Note.

Id. Interest under the Note is due quarterly. JA773, § 3. The initial annual interest rate was 5%. *Id*. The rate increases to 10%, however, if Temperatsure defaults. *Id.*

C. Temperatsure Informs B&C that the Principal Is $6,000,000.

As its CFO, Kahle performed Temperatsure's LTM Gross Profit calculations. JA1866, 52:17-21. In February 2017, Kahle informed Smith orally that the $19,000,000 threshold was surpassed in the January 2017 measurement period, so the Principal would be $6,000,000. JA1750-51, 108:24-110:5; JA1864, 45:20-25. Kahle confirmed the Principal in a July 7, 2017 email when he wrote:

> The interest payment is being wired today. You should receive $125,000 which is 5 months interest on the note.

JA1458-60. At the Note's 5% rate, annual interest on $6,000,000 is $300,000 or $25,000 per month. By stating that the interest was $25,000 per month ($125,000 for five months), the email reaffirmed that Temperatsure had calculated a $6,000,000 Principal.

After Kahle informed B&C that the Principal would be the maximum, Kahle did not send B&C LTM Gross Profit Statements and B&C did not insist that Temperatsure do so. JA36, ¶¶ 41, 43. On July 7, 2017, Temperatsure paid B&C the $125,000 in interest. JA283, ¶¶ 7, 8. On July 22, 2017, Kahle reported to the board that the payment had been made. JA1422, JA1434 ("CP Note Interest Paid"). B&C did not dispute Temperatsure's $6,000,000 calculation. JA284, ¶ 12.

D. Temperatsure Affirms the $6,000,000 Principal and Proposes that B&C Convert Its $6,000,000 Note into Equity.

In November 2017, Temperatsure paid B&C another quarter's interest at $25,000 per month. JA628, ¶ 51. Over the next eight months, the monthly board packets reported the $6,000,000 Principal, SLC members reviewed the LTM Gross Profit figures, and no member indicated to Smith that the $6,000,000 Principal was wrong. JA285, ¶ 19; JA497-528; JA1289-99. In April 2018, SLC member Dietz Fry and an Endeavour colleague re-examined the earnout in light of the same accounting errors Temperatsure asserts here and the colleague, copying Fry, informed Temperatsure's auditors that the $6,000,000 earnout was indeed earned. Fry did not correct his associate's report. *See* JA837-41; JA1647, 62:17-64:16.

By June 2018, however, Temperatsure faced a problem: it was approaching the debt-to-EBITDA limit in its bank covenants. JA2749, 122:11-14. To reduce debt, Temperatsure proposed that B&C convert its debt into equity. *Id.* 123:3-7. On June 27, 2018, Temperatsure sent B&C a proposed conversion agreement stating:

> The original principal amount and total accrued interest owed to [B&C] pursuant to the Note is $6,075,000.

JA1307. Temperatsure proposed that B&C exchange the Note for 6,075,000 super-preferred LLC units in Temperatsure. *Id.* Fry testified that in making this proposal, Temperatsure was stating to B&C that the Note was "a 6-million-dollar debt."

JA1665, 136:6-13. B&C declined the proposal when it learned that the conversion might trigger a large tax liability. JA1679, 190:17-191:12.

E. Temperatsure Recalculates the Principal.

About two weeks after B&C declined to convert its Note, SLC member Derek Johnson emailed that "while previously we as a board were under the opinion that the earnout was fully achieved we now have a spreadsheet from the company that appears to show the earnout was not fully achieved[.]" JA323. Outside of Smith's presence, Fry and new CFO Thomas Bell described Temperatsure's new calculation as just that: a *revision* to its first Principal calculation. JA1455 (referring to "yesterday's earnout *recalculation*"); JA1519 (attaching "first pass at the *revised* calculation"); JA1524 (discussing how to tell bank earnout was being "*reassessed*"); JA1531 (referring to "*restated* seller note").[1] Smith responded to Johnson's email by reminding the board that the $6,000,000 Principal became final in 2017. JA40, ¶ 72.

Nevertheless, on August 6, 2018, President Tony Aleide emailed B&C what he called "LTM gross profit statements for the Months of January 2017 to July 2017," supporting documentation, and a "Principal statement." JA2327-426. The "LTM gross profit statements" were a one-page spreadsheet showing "LTM Gross

[1] Throughout this brief, emphasis has been added and internal citations and quotations omitted unless otherwise noted.

Profit" in seven columns. JA2330. Immediately following the spreadsheet was Aleide's "Principal Statement" asserting a Principal of $946,671. JA2331.[2]

B&C responded by letter that "[t]he Company's attempt to change the Principal long after it was established is of no effect." JA255-58. B&C added that it also disagreed with Temperatsure's new accounting on the merits. JA258-61. When Temperatsure rejected B&C's demand that Temperatsure pay all past-due interest, B&C sent Temperatsure a default notice. JA264-68. B&C then filed this action seeking (1) a declaration that the Principal is $6,000,000 and that Temperatsure owes interest based on that amount and (2) damages for breach of contract. JA44-46, ¶¶ 88-99. Temperatsure commenced an accounting arbitration but said it would hold it in abeyance pending a judicial determination of arbitrability or that arbitrability should be decided by an Arbitrating Accountant. JA217.

F. The Court's Opinion

Following discovery, the Court granted B&C's and Smith's motions for summary judgment and denied Temperatsure's cross-motion. Opening Brief

[2] Although not labeled "Principal Statement," the information at JA2331, which immediately followed Aleide's "LTM Gross Profit Statements" (JA2330), is the only possibility for what Aleide was referring to when he wrote to B&C that he had attached both "LTM gross profit statements for the Months of January 2017 to July 2017" and "the Principal statement pursuant to section 2(c)." *See* JA2326-31. B&C made this point at oral argument and Temperatsure did not dispute it. *Compare* JA2867-72 *with* JA2878-96 & JA2902-JA2904.

("OB"), Ex. B (the "Opinion"). At bottom, the motions posed three questions: (1) whether the parties' disagreement over the Principal constitutes a "Dispute" that must be resolved through accounting arbitration; (2) whether the $6,000,000 Principal is "final and binding"; and (3) whether Temperatsure's fiduciary duty claims and related defenses have merit. Questions (1) and (2), however, turn on the same underlying question: what is Temperatsure's Principal Statement? Because B&C did not dispute the company's statements that the Principal is $6,000,000, if the CFO's Email (or another statement that the Principal is $6,000,000) is the Principal Statement, then, under section 2(c) of the Note, (1) no "Dispute" exists, resolving arbitrability, *and* (2) the $6,000,000 Principal is "final and binding." JA772. If, on the other hand, Aleide's August 2018 statement is the Principal Statement, a Dispute would exist (because B&C did dispute that statement) and the Principal disagreement would be arbitrable. The Court first decided which document is Temperatsure's Principal Statement. It then addressed Smith's fiduciary duties.

1. Principal Statement Ruling

The Note's definition of Principal Statement, the Court observed, does "not require the statement to have any degree of formality or contain any minimum quantum of data, apart from the figure Temperatsure determined was the Note's Principal." *Id*. at 18. And though the CFO's Email is written in terms of the interest B&C would receive, it "sets forth what Temperatsure calculated the Principal to be"

because "[t]here is no dispute that $125,000 for five months' interest at the Note's 5% annual rate equals a $6,000,000 Principal." *Id*. at 19. Thus, the CFO's Email is Temperatsure's Principal Statement. *Id*. at 18-22.

Temperatsure's contrary position, the Court held, is unreasonable. *Id*. at 22-36. That Temperatsure breached some of its obligations under the Note does not unbind it from its own Principal calculation. *Id*. at 24. The Note's GAAP-calculation provision does not impose a condition precedent to enforcement of the Note's "final and binding" clause. *Id*. at 24-26. Even if it did, the parties effectively waived such a condition by performing the Note for nearly a year based on the $6,000,000 Principal. *Id*. at 26-27. The Court concluded:

> Temperatsure's argument would require the Court to conclude: (1) Temperatsure's previous calculation of Principal, on which both sides relied from a period of 13 months, was meaningless because Temperatsure did not comply with its own obligations … and (2) B&C was required to demand Temperatsure perform its obligations and B&C's failure to do so imperils its earn-out, even though B&C had no reason to insist upon strict compliance once the full earn-out was achieved. The Court simply is not persuaded that sophisticated parties are required to behave irrationally.

Id. at 35.

2. Fiduciary Duty Ruling

Key to the fiduciary duty issue, the Court held, is that no evidence shows that Smith knew Kahle had not followed GAAP. *Id*. at 38-39. As a result, no plausible argument exists that Smith acted disloyally or with incomplete candor by failing to

alert the board that Temperatsure technically breached the Note by not sending B&C LTM Gross Profit Statements. *Id*. at 39.

G. The Court's Judgment

After the Court issued its Opinion, the parties stipulated to the form of judgment. *See* OB, Ex. C. That judgment declares that the Principal is $6,000,000 and awards B&C damages for past-due interest according to formulas and in amounts to which the parties agreed. *Id*. at 3-4.

ARGUMENT

I. THE CFO'S EMAIL IS TEMPERATSURE'S PRINCIPAL STATEMENT

A. Question Presented

Did the Court correctly hold that the CFO's Email is Temperatsure's Principal Statement?[3]

Preservation: Temperatsure preserved this issue. JA2634-68; JA2825-56; JA2858-905.

B. Scope of Review

B&C agrees that this Court reviews summary judgment rulings *de novo*.

C. Merits of Argument

1. Basic Contract Interpretation Principles Establish that the CFO's Email is the Principal Statement.

"When [a] contract is clear and unambiguous, [courts] will give effect to the plain-meaning of the contract's terms and provisions." *Sunline Commercial Carriers, Inc. v. CITGO Petro. Corp.*, 206 A.3d 836, 846 (Del. 2019). "Delaware adheres to the 'objective' theory of contracts, i.e., a contract's construction should be that which would be understood by an objective, reasonable third party." *Id*. "The

[3] This question subsumes, and the following merits discussion covers, both Arguments I and III of the Opening Brief. Temperatsure's Argument III challenges the Court's citation to the *Greenstar* case. *See* OB36-38. That argument and case, however, concern which document constitutes the Principal Statement. Thus, it is proper to address them in this Argument I.

contract must also be read as a whole, giving meaning to each term and avoiding an interpretation that renders any term mere surplusage," *id.*, or that conflicts with the contract's "overall scheme or plan," *Riverbend Cmty., LLC v. Green Stone Eng'g, LLC*, 55 A.3d 330, 334-35 (Del. 2012). Courts interpret clear terms "according to their ordinary meaning." *Id*.

Interpreted in accordance with these rules, the Note unambiguously provides that a Principal Statement is any statement, formal or not, that Temperatsure delivers to B&C and that sets forth what Temperatsure calculated the Principal to be. As mentioned, the Note defines Principal Statement in simple words: "a statement setting forth [Temperatsure's] calculation of the Principal." JA772, § 2(c). The ordinary meaning of "statement" is "something stated" or "the act or process of stating." Webster's Online Dict., www.merriam-webster.com/dictionary/statement. In the Note and other Transaction documents, the parties defined dozens of capitalized terms to give words special meaning but did not do so for "statement." *See* JA770-71; JA849-62. When the parties wanted a statement to include additional information, they said so. For example, the Note required each LTM Gross Profit Statement to include "reasonable supporting documentation for the estimates and calculations contained therein (together with any additional information reasonably requested by [B&C])." JA771, § 2(a). The Note requires nothing for a Principal Statement beyond Temperatsure's Principal calculation. *See* JA770-80.

This plain-English interpretation is consistent with the Note's overall scheme. That scheme sets forth a comprehensive process for determining the Principal promptly and with finality. Pursuant to that scheme Temperatsure was to disclose the details and backup B&C might need to dispute Temperatsure's earnout calculation in the LTM Gross Profit Statements, not the Principal Statement. *See* JA771, § 2(a). The main consequence under the Note of delivering a Principal Statement was to initiate section 2(c)'s special process for finally determining the Principal. *See id*. § 2(c). Under that process, each side's last-stated Principal is deemed final and binding if the other side does not dispute it by a specified deadline. *Id*. Nothing more than a simple statement of what Temperatsure calculated the Principal to be is necessary to perform this process-triggering function.[4]

The CFO's Email is a statement Temperatsure delivered to B&C that sets forth what Temperatsure calculated the Principal to be. It says: "The interest payment is being wired today. You should receive $125,000 which is 5 months interest on the note." JA1458-60. One-hundred-twenty-five-thousand dollars for five months' interest at the Note's 5% annual rate equals a $6,000,000 Principal. The email could have said "You should receive 5 months' interest based on a $6,000,000 Principal"

[4] As discussed in Part I-C-2-e, the Principal Statement may serve an additional purpose and contain additional elements beyond the final Principal amount when the highest calculated LTM Gross Profit falls between $18,000,000 and $19,000,000. Here, however, Temperatsure's CFO determined that an LTM Gross Profit exceeded $19,000,000.

and the email's substance would have been the same. The email, therefore, was a statement by Temperatsure setting forth its $6,000,000 Principal calculation. It thus was Temperatsure's Principal Statement.

2. Temperatsure's Counterarguments Fail.

Conceding that the $6,000,000 Principal is final and binding if the CEO's Email is its Principal Statement, OB8, Temperatsure offers a smorgasbord of arguments hoping something will persuade this Court that the email is not its Principal Statement. Temperatsure's arguments all miss the mark.

a. Temperatsure Did Not Have to Write "$6,000,000" for Its CFO's Email to Be Its Principal Statement.

Temperatsure argues that its CFO's Email cannot be its Principal Statement because the email does not contain a Principal "figure" but merely identifies an amount of interest and a time period from which one can "extrapolate" the Principal. OB5, 19-20. In other words, Kahle did not write: "$6,000,000."

That $125,000 for five months' interest at an annual rate of 5% equals a $6,000,000 Principal is not "extrapolation." It is math. To extrapolate is to "project, extend, or expand (known data or experience) into an area not known or experienced so as to arrive at a usually conjectural knowledge of the unknown area." Webster's Online Dict., www.merriam-webster.com/dictionary/extrapolate. The $6,000,000 Principal is not a conjecture, inference, or expansion from the CFO's Email into an unknown area. It is the arithmetic equivalent of $125,000 for

five months' interest at a 5% interest rate. Nothing in the Note suggests that only a single number suffices when setting forth Temperatsure's Principal calculation, as opposed to any description that communicates the calculated Principal.

Even if Temperatsure had to recite "$6,000,000," it did so before it changed its asserted Principal in August 2018, most clearly in its proposal that B&C convert the $6,000,000 debt into 6,000,000 equity units. JA1302. As SLC member Fry testified, Temperatsure's June 2018 proposed conversion agreement proposed to B&C that B&C convert "what the Company was at that time stating to be a six-million-dollar debt." JA1665, 136:6-13. If reciting "$6,000,000" were necessary, therefore, the company's June 2018 statement did just that.

b. Temperatsure Did Not Have to Deliver LTM Gross Profit Statements to B&C for Its CFO's Email to Be Its Principal Statement.

Citing sections 2(a) and (b) of the Note, Temperatsure argues that the CFO's Email is not a Principal Statement because Temperatsure did not also send B&C LTM Gross Profit Statements. OB5-6, 21-22, 27. Neither section has any bearing on the definition of Principal Statement or whether the email meets that definition.

As explained, section 2(a) did direct Temperatsure to send B&C LTM Gross Profit Statements. *See* JA771, § 2(A). In so doing, however, the section does not mention the Principal Statement. *See id*. Nor does the Principal Statement definition mention section 2(a). *See* JA772, § 2(c). Though each was a part of section 2's

overall process, sections 2(a) and (c) were distinct steps within that process. Section 2(a) provided the step in which Temperatsure, each month, was supposed to disclose to B&C its detailed LTM Gross Profit calculations. Section 2(c) provided the step in which Temperatsure was supposed to state to B&C its Principal calculation. Temperatsure indisputably breached section 2(a) seven times (for all seven earnout measurement periods) by not sending B&C any LTM Gross Profit Statements. But one can fail to perform some parts of a contractual process while performing others. No language in the Note indicates that if Temperatsure failed to send B&C LTM Gross Profit Statements, it could not send a statement setting forth what it nevertheless calculated the Principal to be, or that it would not be bound by that statement if B&C did not dispute it. Temperatsure's section 2(a) breaches turned out to be harmless because, having been told that the Principal is the maximum, B&C did not need the information to which section 2(a) entitled it.

The analysis is similar as to section 2(b), which directed Temperatsure to determine the Principal "based on the greatest LTM Gross Profit set forth on any LTM Gross Profit Statement delivered [to B&C]." JA772, § 2(b). Temperatsure contends that, because of this provision, if it did not deliver an LTM Gross Profit Statement to B&C, then even if it delivered a statement setting forth what it calculated the Principal to be, that statement is not its Principal Statement. *See* OB21-23. Temperatsure's conclusion does not follow from its premise.

For one thing, the Principal Statement definition does not require a statement to set forth a *correctly determined* Principal to be a Principal Statement. However Temperatsure determined the Principal, when it informed B&C what it calculated the Principal to be, it was delivering to B&C, as a matter of plain, ordinary English, a "statement setting forth its calculation of the Principal." JA772, § 2(c).

Second, like section 2(a), section 2(b) neither references nor is referenced in the Principal Statement definition. When the parties wrote in section 2(b) that Temperatsure should determine the Principal based on the greatest LTM Gross Profit "set forth on any LTM Gross Profit Statement delivered [to B&C]," they obviously presumed that Temperatsure would comply with section 2(a) and deliver LTM Gross Profit Statements. Nothing in the Note suggests, however, nor would an objective, reasonable third party think, that the parties intended to *benefit* Temperatsure by absolving it from a statement setting forth its Principal calculation, thereby depriving B&C of the protection of section 2(c)'s "final and binding" clause, if Temperatsure *violated* sections 2(a) and (b) by computing LTM Gross Profit and Principal without first sending B&C LTM Gross Profit Statements.

Nothing about this analysis renders sections 2(a) and (b) "superfluous." *Cf.* OB5, 22-23, 26. Those sections required what they required. What Temperatsure characterizes as rendering the sections "superfluous" is merely the Court's having recognized that neither the Note nor the law permits Temperatsure to use its own

breaches of the sections to escape its promise in the "final and binding" clause. *See Tang Capital Partners LP v. Norton*, 2012 WL 3072347, at *8 & n.41 (Del. Ch. July 27, 2012) ("A provision that allows either party by his own breach to excuse his own performance is a commercial absurdity.").

c. Sending it Early Did Not Convert the CFO's Email into a Non-Principal Statement.

Temperatsure next argues that the CFO's Email cannot be a Principal Statement because Kahle sent the email earlier than the Note contemplated. OB6, 22-23, 25-26. Section 2(b) says Temperatsure was supposed to determine the Principal "as soon as practicable after the LTM Gross Profit Statement for the month ended July 31, 2017 is prepared, but in no event later than fifteen (15) days following" that date. JA772, § 2(b). From this Temperatsure argues that a July 7, 2017 email cannot have been a Principal Statement.

This is yet another attempt to graft onto the Principal Statement definition terms that do not exist. As explained, the definition does not say that a statement setting forth Temperatsure's Principal calculation is a Principal Statement only if the company performed the calculation in accordance with section 2(b). *See id.* § 2(c); *supra* pp.20-21. Nor does the sentence on which Temperatsure relies say merely that Temperatsure should determine the Principal after July 31, 2017—it also says Temperatsure should determine the Principal "in no event later than fifteen (15) days following" July 31, 2017 (language that, using ellipses, Temperatsure omits from

page 26 of its brief). If this sentence were deemed to modify the definition of Principal Statement, Temperatsure would have had to deliver its statement, not only after July 31, 2017, but by August 15, 2017. If that were the case, however, Aleide's August 2018 statement could not be Temperatsure's Principal Statement either. The nonsensical result would be that if Temperatsure failed to deliver a Principal Statement during the first 15 days of August 2017—as Temperatsure contends happened—the company never could deliver a Principal Statement and section 2(c)'s dispute resolution process, which is triggered by delivery of the Principal Statement, would become a nullity. This interpretation is not reasonable.

Construing the Note as a whole, the only reasonable conclusion is that section 2(b)'s direction that Temperatsure should calculate the Principal "as soon as practicable after the LTM Gross Profit Statement for the month ended July 31, 2017 is prepared, but in no event later than [August 15, 2017]" was a deadline to ensure prompt calculation, disclosure, and determination of the Principal in the event that the final Principal determination depended on the last (July 2017) measurement period. Because here Temperatsure determined that the maximum Principal was achieved based on the first (January 2017) measurement period, there was no reason to delay informing B&C because, at that point, the last measurement period was irrelevant.

As the next section discusses, the Note does say that interest should accrue only after Principal is determined under section 2. It is reasonable, therefore, to construe an early-delivered Principal Statement not to be effective until August 1, 2017, so as not to accelerate accrual. But Temperatsure's position that the Court should deem a pre-August 1, 2017 statement that otherwise fits the definition of a Principal Statement *not a Principal Statement*—but should accept its post-August 15, 2017 statement as a Principal Statement—has no basis in the Note's language or structure and would contravene its scheme of finalizing the Principal promptly.[5]

d. Paying Interest Early Does Not Convert the CFO's Email into a Non-Principal Statement.

Temperatsure is correct that the earliest interest could accrue under the Note was 15 days after it delivered its Principal Statement, yet Temperatsure wired B&C the first interest payment the same day its CFO emailed B&C. OB3, 6, 22-23. All this shows, however, is that Temperatsure accrued and paid interest early, not that the CFO's Email is not a Principal Statement, for the simple reason that Temperatsure's interest payments do not affect whether Temperatsure sent B&C a statement setting forth its Principal calculation.[6]

[5] In any event, as shown above, Temperatsure sent B&C statements reaffirming the $6,000,000 Principal after August 1, 2017 and before Aleide's August 2018 statement. *See supra* p.18.

[6] Notably, Kahle's early accrual and payment of interest was based on an instruction from SLC member Fry, not Smith. *See* JA1406-08; JA1885-86, 129:6-131:13.

A basic hypothetical illustrates the point. Say that on August 1, 2017 Temperatsure sent B&C a document titled "PRINCIPAL STATEMENT" reporting its Principal calculation. According to Temperatsure, if it simultaneously wired B&C an interest payment, even this "PRINCIPAL STATEMENT" would not be a Principal Statement because the company would have paid interest less than 15 days after it delivered the statement. By Temperatsure's logic, if it paid interest early, it never could issue a Principal Statement, because no statement the could precede Temperatsure's interest payment by at least 15 days—Aleide's August 2018 statement included.

This makes no sense. The correct due date of course is necessary to calculate how much interest Temperatsure owes B&C. After the Court issued its Opinion, however, the parties stipulated to B&C's damages, taking the correct date into account. OB, Ex. C. None of this changes the fact that the CFO's Email confirmed to B&C that Temperatsure calculated a $6,000,000 Principal, and thus is Temperatsure's Principal Statement.

e. B&C's Interpretation Does Not Render the Terms "Elements" and "Amounts" Superfluous.

Temperatsure's next argument goes like this: section 2(c) defines "Dispute" as a dispute by B&C to "any elements of or amounts reflected on the Principal Statement that affect the calculation of the Principal." Because the plural words "elements" and "amounts" must have meaning, "a Principal Statement must include

more than simply the Principal amount." OB24-25. Absent from Temperatsure's brief is what additional information a Principal Statement must contain. *See id*. That is because the Note requires no additional information, at least when, as here, Temperatsure determines that the Principal is the $6,000,000 maximum.

Section 2(c)'s reference to "elements" and "amounts" certainly indicates that a Principal Statement *might* contain more than one "element" or "amount" that B&C will want to dispute. Nothing in the Note, however, requires the Principal Statement to contain multiple elements and amounts in all situations. Elements and amounts beyond the Principal amount would become relevant if the highest LTM Gross Profit Temperatsure computed fell between $18,000,000 and $19,000,000, because in that situation Temperatsure would have to convert the LTM Gross Profit into a Principal between $0 and $6,000,000, and that conversion would involve math—elements and amounts—that would not already appear on the LTM Gross Profit Statements. No such elements or amounts come into play, however, when LTM Gross Profit reaches $19,000,000, because in that situation the Note simply declares that the Principal is $6,000,000. *See* JA771, § 1(iii)(A).

Ironically, Aleide's purported August 2018 Principal Statement proves this point. Here is Aleide's purported "Principal Statement":

Max LTM Gross Profit	$18,157,778
Amount above Floor	$157,778
% Earned	15.8%
Max Earnout	$6,000,000
Earnout Achieved	$946,671

JA2331; *supra* p.10 & n.2. While B&C obviously disagrees that Aleide's statement *is* the Principal Statement, the statement shows how little information even Temperatsure realizes a Principal Statement need contain.

Of the five rows that comprise Aleide's purported Principal Statement, at least the middle three, if not the first four, are necessary only because of Temperatsure's August 2018 contention that the highest LTM Gross Profit fell between $18,000,000 and $19,000,000. These rows show how Temperatsure got to a Principal of $946,671 from a supposed greatest LTM Gross Profit of $18,157,778. These rows are not required, however, when, as Temperatsure's CFO determined was the case in 2017, the greatest LTM Gross Profit exceeds $19,000,000, because in that circumstance the Note automatically deems the Principal to be $6,000,000. *See* JA771, § 1(iii)(A). When the Principal is the maximum, Aleide's spreadsheet shows, all that is left for Temperatsure to show is that the $6,000,000 maximum was achieved. Which is exactly what the CFO's Email showed.

f. Temperatsure's Hypothetical Does Not Establish Reversible Error.

Citing no authority, Temperatsure posits that if the CFO's Email had stated a Principal less than $6,000,000, B&C had not disputed it, and Temperatsure had argued that the email was its Principal Statement, Temperatsure's argument would be "roundly rejected." OB29. Temperatsure's premise seems to be that Kahle's email was so vague about the Principal, this Court never would consider it a "statement" to which B&C should be held. Just as the CFO's actual email did not confuse B&C, however, there is no reason to believe that Temperatsure's hypothetical email would have confused B&C, in which case there would be no reason not to deem it a Principal Statement. The real problem for Temperatsure in the hypothetical situation would be that its failure to send B&C LTM Gross Profit Statements no longer would be harmless because B&C now would need Temperatsure's LTM Gross Profit calculations and supporting documentation to assess the company's sub-maximal Principal. B&C would not be bound by the "final and binding" clause, not because it had not received a Principal Statement, but because Temperatsure would have committed a prior *material* breach of section 2(a).

Even if one agreed that an unclear communication by Temperatsure should not be deemed a "statement setting forth [its] calculation of the Principal" binding on B&C, moreover, it does not follow that Temperatsure may attack its *own*

communication as unclear when, as here, the communication was not unclear to B&C. Temperatsure's hypothetical does not show that the Court erred.

g. Temperatsure's Stated Principal Need Not Be Correct for Its Statement to Be a Principal Statement.

Finally, Temperatsure implies that its CFO's Email is not a Principal Statement because it did not calculate the LTM Gross Profit underlying the $6,000,000 Principal in accordance with GAAP. *See* OB27 (arguing that the Court disregarded the Note's purported purpose of compensating B&C based on performance measured according to GAAP). The Note refutes this theory too.

As explained, the Note does not say that a statement is a Principal Statement only if the calculation it sets forth is correct. It says a Principal Statement is any statement "setting forth [Temperatsure's] calculation of the Principal," whatever the calculation is. JA772, § 2(c). This plain meaning is confirmed by the rest of section 2(c). By permitting B&C to "dispute" Temperatsure's Principal Statement and directing an arbitrator to "revis[e]" an erroneous Principal Statement (if a "Dispute" gets that far), *see* JA772-73, section 2(c) shows that a statement need not contain a correct Principal to be a Principal Statement in the first place. Whether Temperatsure's stated Principal is final and binding, moreover, hinges not on its being correct but on its being undisputed. JA772, § 2(c). If B&C does not dispute the Principal Statement within 15 days, the statement's Principal is final and binding, correct or not. *Id.* If B&C does timely dispute Temperatsure's Principal, sets forth a

different Principal, and Temperatsure does not dispute that number within 15 days, B&C's number is final and binding, correct or not. *Id.* The Note strikes a balance between correctness and prompt resolution. Section 2(c)'s streamlined process for resolving disagreements about the Principal would be pointless if either party could take the position any time it wants that the stated Principal is erroneous, so no Principal Statement was delivered and the "final and binding" clause never triggered.

Greenstar IH Rep, LLC v. Tutor Perini Corp. is on point. 2017 WL 5035567 (Del. Ch. Oct. 31, 2017). *Cf.* OB36-38. As here, a contract required buyer to calculate the profit on which an earnout was to be based and send its report to seller. *Id*. at *3. If seller did not object within a specified time, the reported figure would be "binding." *Id*. After reporting profits to seller and paying two years' earnouts, buyer changed its position and stopped paying, claiming that its prior calculations were based on inaccurate information that did not accord with GAAP. *Id*. at *4, 6. Seller sued for the payments buyer should have made based on the never-disputed reports. *Id*. The court granted seller judgment on the pleadings. The contract, the court explained, "spell[ed] out unambiguously how the Earn-Out Payments … [were] to be calculated," namely through the streamlined process to which the parties agreed. *Id*. at *6. Buyer's argument that it did not owe earnout payments if it could demonstrate that the calculations were non-GAAP-compliant "fail[ed] at the threshold" because nothing in the contract's references to GAAP negated or

qualified the mandate that if seller did not object to buyer's reports, the reports were binding. *Id*. at *7. To accept buyer's interpretation "would be to render the language 'shall be binding' superfluous—a result, under our law, that must be 'avoided.'" *Id*. at *6. This Court affirmed for the reasons the Court of Chancery stated. *Tutor Perini Corp. v. Greenstar IH Rep, LLC*, 2018 WL 2186582, at *1 (Del. May 11, 2018).

Temperatsure is correct that *Greenstar* does not address the meaning of the Note's Principal Statement definition. *See* OB36-38. But neither do Temperatsure's arguments about its not sending B&C LTM Gross Profit Statements, not calculating LTM Gross Profit in accordance with GAAP, sending the Principal Statement early, and paying interest early—because none of the Note provisions to which those matters refer are part of, or even mention, the Principal Statement definition. At the end of the day, though, Temperatsure *is* trying to do what *Greenstar* says it may not: use non-compliance with other contract provisions to escape its unambiguous promise that if B&C did not dispute its stated Principal, that Principal would be "final and binding." As in *Greenstar*, to accept Temperatsure's interpretation would be to render the language "final and binding" superfluous.

For all these reasons, the Court correctly held that the CFO's Email is Temperatsure's Principal Statement.

II. TEMPERATSURE'S FAILURE-OF-A-CONDITION-PRECEDENT DEFENSE FAILS

A. Question Presented

Did the Court correctly reject Temperatsure's defense of failure of a condition precedent?

Non-Preservation: Temperatsure did not preserve this issue. Considering the issue now would disserve the interests of justice because, as shown below, Temperatsure deprived B&C of the opportunity to develop a complete record.

In its summary judgment opening brief, B&C argued that Temperatsure's condition-precedent defense lacks merit as a matter of law. JA745. Temperatsure's answering brief contained no response. *See* JA2237-91. B&C noted Temperatsure's abandonment of the defense in B&C's reply brief. JA2656. Temperatsure's cross-motion reply brief still did not address the defense. JA2825-56. Though Temperatsure stated at oral argument that the allegedly failed condition was a "failure of the company to calculate principal in accordance with GAAP," JA2896:9-20, it offered no argument in support of the defense's merits. JA2858-905.

Temperatsure's citations for where it preserved the issue consist of B&C's entire summary judgment reply brief (JA2634-68), which, as noted, showed that Temperatsure's answering brief did *not* address the defense; Temperatsure's entire cross-motion reply brief (JA2825-56), which did not mention the defense; and the entire summary judgment argument transcript (JA2858-905), in which, again,

Temperatsure did not argue the defense's merits. *See* OB30. Temperatsure provides no "clear and exact reference to the pages of the appendix where [it] preserved" its alleged defense, as Rule 14(b)(vi)(A)(1) requires, because none exists.

B. Scope of Review

B&C agrees that this Court reviews summary judgment rulings *de novo*.

C. Merits of Argument

In the midst of its contract analysis as to which document constitutes the Principal Statement, the Court added that Temperatsure's "affirmative defense similarly posit[s] that the 'GAAP-compliant LTM Gross Profit statements and delivery of a Principal Statement based on those delivered GAAP-compliant LTM Gross Profit statements was a condition precedent to enforcement of the Note.'" Opinion at 23-24 (quoting Answer ¶ 22 (JA619)). But, the Court held, the Note does not condition enforcement of the Note's "final and binding" clause on Temperatsure's having delivered LTM Gross Profit Statements or performed a GAAP calculation. *Id.* at 24-26. "Even if the GAAP compliance requirement could be construed as a condition precedent …, both parties effectively waived this condition through their performance under the Note." *Id*. at 26-27. Temperatsure contends that the Court's waiver statement constitutes reversible error. OB30-35. Temperatsure is wrong, for at least two reasons.

1. Temperatsure Did Not Argue the Alleged Defense Below.

As explained, Temperatsure did not assert its condition-precedent defense in response to B&C's summary judgment motion, much less establish the defense's merits or that it presents a triable issue. As a result, the defense is not a basis for reversing summary judgment. *See, e.g.*, *Williams Natural Gas. Co. v. Amoco Prod. Co.*, 1991 WL 101369, at *2 (Del. Ch. June 10, 1991) (summary judgment granted for plaintiff when defendant failed to meet its burden of supporting its affirmative defense). B&C agrees with Temperatsure that it would be error to reject Temperatsure's condition-precedent defense based on a waiver argument B&C did not raise—*if* Temperatsure had invoked the defense in response to B&C's motion and *if* Temperatsure had shown that a GAAP calculation is a condition to enforcing the Note's "final and binding" clause. Likewise, the Court's having happened to discuss a defense that Temperatsure did not raise does not entitle it to resurrect that defense. *See Jenkins v. Delaware State Univ.*, 2014 WL 4179958, at *6 n. 69 (Del. Ch. Aug. 22, 2014) (deeming unbriefed affirmative defenses "abandoned"); *Naughty Monkey LLC v. MarineMax Ne. LLC*, 2010 WL 5545409, at *3 n. 35 (Del. Ch. Dec. 23, 2010) (same); *Oakwood Acceptance Corp. v. Penn*, 1994 WL 150864, at *6 (Del. Super. Mar. 4, 1994) (same). Had Temperatsure asserted the defense in response to B&C's motion, B&C might have responded that Temperatsure waived the alleged condition for the reasons the Court discussed. *See* Opinion at 26-27. Temperatsure

created the situation on which it now seeks reversal—that the parties did not argue waiver—by not asserting at summary judgment that any condition precedent existed to waive.[7]

2. A GAAP Calculation Is Not a Condition Precedent to Enforcing the Note's "Final and Binding" Clause.

Beyond Temperatsure's abandoning its condition-precedent defense, the defense is meritless as a matter of law. As the Court explained, whether one provision's performance is a condition of another provision's enforcement is a matter of contractual intent and interpretation. *Id.* at 24-25. For the reasons in Part I-C-2-g above, the Note is clear that Temperatsure did not have to calculate LTM Gross Profit according to GAAP for a statement setting forth its Principal calculation to be a Principal Statement and, if undisputed by B&C, to be final and binding.

Temperatsure suggests that a GAAP calculation should be deemed a condition precedent because the Note called for a GAAP calculation to protect both parties, not just B&C. *See* OB31-32. Who the provision was to protect is irrelevant, however, because, again, the Note does not make a GAAP calculation a prerequisite to a final Principal determination. Importantly, moreover, Temperatsure had the power to protect itself from an erroneous (*e.g.*, non-GAAP) calculation because *it controlled*

[7] As the Opinion shows, the Court discussed the defense, not because Temperatsure asserted it in response to B&C's motion, but because Temperatsure mentioned it in its answer. *See* Opinion at 23-24 & n.94.

the calculation. *See* Restatement (Second) of Contracts § 227(1) (1981) (cited in, *e.g.*, *Kansas City Southern v. Grupo TMM, S.A.*, 2003 WL 22659332, at *4 n.28 (Del. Ch. Nov. 4, 2003)) (doubt as to whether provision is a condition should be resolved against party if power to fulfill the alleged condition lay in that party's control). Once again, Temperatsure is trying to use its own non-compliance to escape the "final and binding" clause.

The Opening Brief identifies Temperatsure's delivery of LTM Gross Profit Statements as another failed condition precedent. *See* OB32. In addition to the reasons above, which apply equally to this alleged failed condition, this argument fails because Temperatsure told the Court at oral argument that the only supposedly failed condition was "a failure of the company to calculate principal in accordance with GAAP." JA2896:9-20.

Temperatsure spends most of its argument attacking the Court's conclusion that Temperatsure's performance of the Note amounted to a waiver. *See* OB30-35. But the Court's waiver conclusion was mere dictum, secondary to its ruling that no condition precedent exists. *See* Opinion at 23-28. Because that ruling was correct, whether Temperatsure's performance of the Note amounted to a waiver is irrelevant. The Court did not err by rejecting Temperatsure's abandoned alleged defense of failure of a condition precedent.

III. SMITH DID NOT VIOLATE HIS DUTY OF CANDOR

A. Question Presented

Did the Court correctly reject Temperatsure's duty of candor claim?

Non-Preservation: Temperatsure's preservation statement is only partially correct. Temperatsure claims to have preserved the issues of whether Smith concealed from Temperatsure's board that Kahle had not complied with "the Note's procedures to (1) deliver GAAP-compliant LTM Gross Profit Statements to the noteholder [*i.e.*, Temperatsure's obligations under sections 1(ii) and 2(a) of the Note]; and (2) calculate the Principal of the Note based on the greatest LTM Gross Profit amount reflected in those delivered LTM Gross Profit Statements [*i.e.*, Temperatsure's obligations under section 2(b)]." OB39. Temperatsure did not preserve item (2). *See* JA2280-86, 2850-55. As shown below, the only "procedure" whose non-performance by the company Temperatsure contended that Smith concealed concerned the (non)delivery to B&C of LTM Gross Profit Statements, not the calculation of the Principal. No interests of justice require allowing Temperatsure to raise this issue now.

B. Scope of Review

B&C agrees that this Court reviews summary judgment rulings *de novo*.

C. Merits of Argument

To try to portray Smith as disloyal, Temperatsure insinuates that he hid from the board that Kahle had calculated LTM Gross Profit and the Principal improperly. Temperatsure says, for example, that Smith "knew that the CFO had not delivered a GAAP-compliant LTM Gross Profit Statement to B&C," implying that Smith knew the calculations were not GAAP-compliant. OB40. It repeatedly says that Smith knew the Note's "procedures" were not being followed, suggesting that Smith hid systematic errors from which Temperatsure faced harm. *Id*. at 9, 14-16, 39-43.

Temperatsure's statements are highly misleading. The only "procedure" Smith knew Temperatsure had not performed was sending B&C LTM Gross Profit Statements. Not alerting the board that the company had not sent B&C this information was not a duty of candor violation because no evidence indicates that not delivering LTM Gross Profit Statements to B&C posed harm to *Temperatsure*. As explained, Temperatsure's section 2(a) breaches were not ones B&C would or could assert against Temperatsure because once Temperatsure informed B&C that the maximum earnout had been earned, B&C did not need the undelivered information. Critically, Temperatsure cites no evidence—because none exists—that Smith knew or had any reason to believe *that Kahle had made an accounting error*, *i.e.*, that the $6,000,000 Principal was wrong. *See* OB39-43. Though it literally is true that Smith "knew that the CFO had not delivered a GAAP-compliant LTM

Gross Profit Statement to B&C," that is because Temperasture did not deliver *any* LTM Gross Profit Statement to B&C. It is equally true that Smith knew the CFO had not delivered a purple LTM Gross Profit Statement to B&C. One could substitute any adjective for "GAAP-compliant" and the statement would hold.

Temperatsure's counsel confirmed all this at oral argument:

> MR. INGEBRETSEN: … [Smith] knew that the CFO was not following the procedures in the note. These gross profit statements were, according to the note, to be calculated in accordance with GAAP. He knew that B&C had not received these.
>
> THE COURT: Well, but that's sort of an important distinction. Because he knows B&C hadn't received them, does that necessarily mean he knows they are not making the calculations?
>
> MR. INGEBRETSEN: Not necessarily. But he knew that the procedures weren't being followed.…
>
> THE COURT: But again, you're saying [Smith] knew the procedures weren't following [sic]. *What you mean is knew they weren't sending the last 12-month gross profit statement?*
>
> MR. INGEBRETSEN: *Correct.*
>
> THE COURT: *You're not alleging that [Smith] was aware that any other procedures were not being followed?*
>
> MR INGEBRETSEN: *Correct.*

JA2893:17-2895:20.

The unrebutted evidence is that Kahle reported only the earnout *result* to Smith, not his underlying computations. JA1750-51, 108:24-110:5. Smith refrained from discussing the substance of the earnout determination with Kahle because of

the conflict of interest Smith had being both B&C's representative for the Transaction and Temperatsure's president. JA1733, 38:19-39:4; JA283, ¶ 9. Because Smith was unaware of the underlying computations, no basis exists to find that Smith "hid" anything from the board, much less information a reasonable person would think presented material harm or risk to Temperatsure.

The fiduciary duties of loyalty and care undoubtedly include a duty of candor, which requires officers to make certain disclosures to their boards. But Temperatsure cites no authority finding a duty of candor violation in remotely similar circumstances. In *Mills Acquisition Co. v. Macmillan, Inc.*, the one case it does cite (without explanation), the CEO concealed at a critical board meeting that a bidder vying to buy the company had received an improper tip of its rival's bid, advantaging the tippee whose proposed leveraged buyout would have benefited the CEO. 559 A.2d 1261, 1272, 1275-77, 1282-83 (Del. 1989). *Mills* and other cases show that an officer violates his or her duty of candor if he or she fails to disclose known information and, by doing so, exposes the company to serious harm. *See, e.g.*, *Hampshire Group, Ltd. v. Kuttner,* 2010 WL 2739995, at *34 (Del. Ch. July 12, 2010) ("[W]hen a corporate officer is aware of financial misreporting that involves high-level management and that has evaded the corporation's auditors, and nonetheless certifies that he is not aware of any material weakness in the company's internal controls, he is making a false statement and failing to bring material

information to the board, in breach of his duty of loyalty."); *Ryan v. Gifford*, 935 A.2d 258, 271-72 (Del. Ch. 2007) (officer concealed knowledge of illegal stock options backdating to escape detection); *Hoover Indus., Inc. v. Chase*, 1988 WL 73758, at *2 (Del. Ch. July 13, 1988) (director failed to disclose "a defalcation or scheme to defraud the corporation of which he ha[d] learned").

Smith's alleged conduct does not approach such malfeasance. No reasonable trier-of-fact could find that by not calling to the board's attention to Temperatsure's harmless breach of section 2(a), while being unaware of any accounting error by Kahle, Smith was "us[ing] superior information or knowledge to mislead" the board or otherwise hiding information that, if revealed, would have helped Temperatsure avoid harm to Smith's detriment. *Mills*, 559 A.2d at 1283. Temperatsure does not explain how merely failing to send B&C LTM Gross Profit Statements could have exposed Temperatsure to harm. *See* OB39-43. The closest it comes is to declare that "the procedures in the Note for determining the Principal amount were for the benefit of both B&C and Temperatsure." OB41. But it does not specify the supposed benefit *to Temperatsure* of the Note's requiring it to provide its LTM Gross Profit calculations and supporting documentation *to B&C*. *See* OB39-43. Indeed, the only evidence Temperatsure even cites for its position that section 2(a) was partially for its benefit is one deposition answer each by Fry and Smith. *See* OB26 (citing JA1686, 220:17-25 & JA1740, 66:25-67:4). The Fry Q&A was:

> Q. Are you saying you do not believe that Mr. Smith had a conflict of interest in working on the earnout on behalf of the Company even though he had a personal interest in B&C and was the designated representative of B&C under the Note?
>
> A. Correct. I think the procedures were provided for. And the procedures are clear and simple and served as a protection for the Company.

JA1686, 220:17-25. This testimony does not identify the "procedures" to which Fry was referring, much less explain how they "served as a protection for the Company." The Smith Q&A was:

> Q. You would agree with me that the requirement that the gross profit be determined in accordance with GAAP was a protection for the Company as well.
>
> A. Sure.

JA1740, 66:25-67:4. This exchange does not address at all the delivery of LTM Gross Profit Statements—the "procedure" as to which the company says Smith should have notified the board. As the Court correctly observed, Temperatsure controlled OpCo, had the necessary information to calculate the Principal, and did not need to send LTM Gross Profit Statements to B&C to perform its own calculations correctly. Opinion at 25. None of this shows that Smith "concealed" information of potential harm to Temperatsure.

Implicit in Temperatsure's argument is the notion that if it only sent B&C LTM Gross Profit Statements, the Principal would have been determined differently. At best, this is rank speculation. If anything, the record suggests the opposite.

Even after Kahle left the company Temperatsure's controller *reaffirmed* that the highest LTM Gross Profit exceeded $19,000,000. JA809-12. Despite the controller's figures being provided to SLC members Johnson, Fry, and Mark Dorman and their having had financial results for all earnout measurement periods for more than half a year, no SLC member questioned the conclusion that the Principal is $6,000,000. JA720-25; JA809-10.

Later, Temperatsure's auditors asked Fry whether the $6,000,000 earnout had been earned. JA783-85. After conceding to the auditors that "[w]e initially thought that the earnout was achieved," Fry and an Endeavour colleague re-examined the matter "with an understanding of the accounting errors made throughout the period." *Id*. The colleague, copying Fry, then reconfirmed to the auditors that "Yes," the "LTM figure during some months throughout the measurement period were [sic] above" $19,000,000. JA839. Fry did not correct his associate's answer. JA1647, 62:17-64:16. Instead, over the next two-and-a-half months Fry treated the Principal as $6,000,000, even serving as the board's point person on communicating with Smith about a possible B&C conversion of its $6,000,000 debt into equity. JA1283-99; JA1664, 131:13-18. As late as June 27, 2018, the day Temperatsure formally proposed to B&C that it convert its $6,000,000 Note, new CFO Thomas Bell informed the auditors: "[B]ased on our best available current information, we believe the earn-out threshold was achieved." JA1514. When Temperatsure did change its

position a few weeks later, Bell still reported to Fry: "As part of the audit process I advised [the auditors] that we believed the earnout was earned and that we had no reason to believe it was not earned (which was an accurate statement at the time)." JA1520-22.

In sum, with all the knowledge the SLC members and new CFO had nearly a year after the CFO's Email, they still took the position that the Principal was $6,000,000—until B&C declined Temperatsure's request to help Temperatsure with its debt covenant problems by converting the $6,000,000 debt into equity. In these circumstances, no reasonable factfinder could find that the Principal would have been different had only Smith told the board in 2017 that Kahle had not sent him the LTM Gross Profit Statements that B&C did not need.

Smith acted properly—loyally—by recognizing his conflict of interest and staying out of Temperatsure's LTM Gross Profit calculation. It was reasonable for him to expect the board to communicate with its CFO to ensure that the company was protecting itself. As the Court cogently summarized: "Without any facts suggesting that Smith knew Kahle was not following GAAP or otherwise was miscalculating the Principal amount, there is no plausible argument that Smith acted disloyally or with incomplete candor by failing to alert Temperatsure's board to [a] technical violation of the Note." Opinion at 39.

CONCLUSION

The judgment should be affirmed.

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CERTIFICATE OF SERVICE

I, Philip Trainer, Jr., do hereby certify on this 9th day of October, 2020, that I caused a copy of Appellees' Answering Brief to be served by efiling via File and Serve*Xpress* upon counsel for the parties as follows:

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