EFiled: Feb 10 2021 02:08PM EST
Filing ID 66325781
Case Number 354,2020


**IN THE SUPREME COURT OF THE STATE OF DELAWARE**

| | | |
|---|---|---|
| **MANTI HOLDINGS, LLC, MALONE MITCHELL, WINN INTERESTS, LTD., EQUINOX I. A TX, GREG PIPKIN, CRAIG JOHNSTONE, TRI-C AUTHENTIX, LTD., DAVID MOXAM, LAL PEARCE,** and **JIM RITTENBURG,** | : | |
| Petitioners-Below/ Appellants/Cross-Appellees, | : | |
| v. | : | No. 354, 2020 |
| **AUTHENTIX ACQUISITION COMPANY, INC.,** | : | Court Below: Court of Chancery of the State of Delaware |
| Respondent-Below/ Appellee/Cross-Appellant. | : | C.A. No. 2017-0887-SG |

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

John L. Reed (I.D. No. 3023)
Peter H. Kyle (I.D. No. 5918)
Kelly L. Freund (I.D. No. 6280)
**DLA PIPER LLP (US)**
1201 North Market Street, Suite 2100
Wilmington, DE 19801
(302) 468-5700
john.reed@dlapiper.com
peter.kyle@dlapiper.com
kelly.freund@dlapiper.com

*Attorneys for Petitioners-Below/ Appellants/Cross-Appellees*

DATED: February 10, 2021

## TABLE OF CONTENTS

**PAGE**


PRELIMINARY STATEMENT ..... 1

SUMMARY OF ARGUMENT ON CROSS-APPEAL ..... 5

ARGUMENT ON APPEAL ..... 7

I. PETITIONERS COMPLIED WITH THEIR CONTRACTUAL OBLIGATIONS AND THE BUYER IS THE PARTY THAT REFUSES TO ADHERE TO THE PLAIN LANGUAGE OF THE STOCKHOLDERS AGREEMENT ..... 7

A. The Buyer is Not a Beneficiary With Independent Rights ..... 8

B. The Potential Obligations in the Stockholders Agreement Were Never Triggered ..... 11

C. The Stockholders Agreement is, at Best, Ambiguous and it Was Misconstrued by the Trial Court ..... 14

D. The Buyer's Argument on the "Same Price" Condition Fails to Explain the Operative Language in the Stockholders Agreement ..... 17

II. THE COMPANY'S ENFORCEMENT OF THE STOCKHOLDERS AGREEMENT VIOLATES SEVERAL SECTIONS OF THE DELAWARE GENERAL CORPORATION LAW ..... 19

A. Enforcement by the Company Violates Section 151(a) ..... 19

B. Enforcement by the Company Violates Section 262 ..... 21

1. The Buyer Misreads the Statutory Language ..... 21

2. The Buyer Confuses the Case Law and Corporate Power ..... 24

C. Enforcement by the Company Violates Section 218 ..... 31

ARGUMENT ON CROSS-APPEAL.....36

I. THE TRIAL COURT CORRECTLY DECIDED THE INTEREST ISSUES.....36

A. Questions Presented.....36

B. Standard and Scope of Review.....36

C. Merits of Argument.....36

1. Petitioners Are Entitled to Interest on the Merger Consideration Held by the Buyer.....36

2. Authentix is Not Entitled to Pre-Judgment Interest on its Attorneys' Fees Award.....40

CONCLUSION.....44

## TABLE OF AUTHORITIES

**CASES** **PAGE(S)**

*Abercrombie v. Davis*,
130 A.2d 338 (Del. 1957).....31, 32

*Alta Berkeley VI C.V. v. Omneon, Inc.*,
41 A.3d 381 (Del. 2012).....15

*Arnold v. State*,
49 A.3d 1180 (Del. 2012).....22

*Baio v. Commercial Union Ins. Co.*,
410 A.2d 502 (Del. 1979).....25

*Belle Isle Corp. v. Corcoran*,
49 A.2d 1 (Del. 1946).....31, 32

*Bonanno v. VTB Holdings, Inc.*,
2016 WL 614412 (Del. Ch. Feb. 8, 2016).....34

*Branin v. Stein Roe Inv. Counsel, LLC*,
2015 WL 4710321 (Del. Ch. July 31, 2015).....40, 41

*C&J Energy Services, Inc. v. City of Miami General Employees' and Sanitation Employees' Retirement Trust*,
107 A.3d 1049 (Del. 2014).....16

*Cede & Co. v. Technicolor, Inc.*,
542 A.2d 1182 (Del. 1988).....27

*Chrysler Corp. (Del.) v. Chaplake Holdings, Ltd.*,
822 A.2d 1024 (Del. 2003).....36

*Citadel Holding Corp. v. Roven*,
603 A.2d 818 (Del. 1992).....5, 38, 42

*Citrin v. Int'l Airport Centers LLC*,
922 A.2d 1164 (Del. Ch. 2006).....41

*Delmar News, Inc. v. Jacob Oil Co.*,
584 A.2d 531 (Del. Super. 1990) .....9

*Dweck, et al., v. Nassar, et al.*,
2005 WL 5756499 (Del. Ch. Nov. 23, 2005).....32

*Felder v. Anderson, Clayton & Co.*,
159 A.2d 278 (Del. Ch. 1960) .....22

*Finkelstein v. Liberty Digital, Inc*.,
2005 WL 1074364 (Del. Ch. Apr. 25, 2005).....23

*Gleason v. Norwest Mortg., Inc.*,
2008 WL 2945989 (D.N.J. July 30, 2008) .....43

*Graham v. State Farm*,
565 A.2d 908 (Del. 1989).....24

*GRT, Inc. v. Marathon GTF Tech., Ltd*.,
2012 WL 2356489 (Del. Ch. June 21, 2012) .....16

*Halpin v. Riverstone Nat'l, Inc.*,
2015 WL 854724 (Del. Ch. Feb. 26, 2015).....13, 17

*Harbor Fin. Partners Ltd. v. Butler*,
1998 WL 294011 (Del. Ch. June 3, 1998),
*rev'd sub nom. on other grounds Elliott Assocs., L.P. v. Avatex Corp.*,
715 A.2d 843 (Del. 1998).....17

*Hercules, Inc. v. AIU Ins. Co.*,
784 A.2d 481 (Del. 2001).....42

*In re Appraisal of Dell Inc*.,
2015 WL 4313206 (Del. Ch. July 13, 2015) .....27, 38

*In re Appraisal of Dell, Inc.*,
2016 WL 3077828 (Del. Ch. May 31, 2016) (Order) .....38

*In re Appraisal of Metromedia*,
971 A.2d 893 (Del. Ch. 2009) .....20

*In re Coffee Assocs., Inc.*,
1993 WL 512505 (Del. Ch. Dec. 3, 1993) .....10

*In re Native Am. Energy Grp., Inc.*,
2011 WL 1900142 (Del. Ch. May 19, 2011) .....32

*In re Shorenstein Hays-Nederlander Theatres LLC Appeals*,
213 A.3d 39 (Del. 2019).....12

*In re VAALCO Energy, Inc. S'holder Litig.*,
C.A. No. 11775-VCL (Del. Ch. Dec. 21, 2015).....28

*Jones Apparel Group, Inc. v. Maxwell Shoe Co., Inc.*,
883 A.2d 837 (Del. Ch. 2004) .....21, 22

*Kaye v. Pantone, Inc.*,
395 A.2d 369 (Del. Ch. 1978) .....22

*Klaassen v. Allegro Development Corp.*,
2013 WL 5739680 (Del. Ch. Oct. 11, 2013).....26

*Kortum v. Webasto Sunroofs Inc.*,
769 A.2d 113 (Del. Ch. 2000) .....24

*Lehrman v. Cohen*,
222 A.2d 800 (Del. 1966).....32

*Libeau v. Fox*,
880 A.2d 1049 (Del. Ch. 2005) .....24

*Matter of Appraisal of Ford Holdings, Inc. Preferred Stock*,
698 A.2d 973 (Del. Ch. 1997) .....*passim*

*Mehta v. Smurfit-Stone Container Corp*,
2014 WL 5438534 (Del. Ch. Oct. 20, 2014).....5, 39

*MTA Can. Royalty Corp. v. Compania Minera Pangea, S.A. De C.V.*,
2020 WL 5554161 (Del. Super. Sep. 16, 2020) .....16

*NAMA Hldgs., LLC v. Related World Mkt. Ctr, LLC*,
922 A.2d 417 (Del. Ch. 2007) .....9

*Neal v. Alabama By-Prod. Corp.*,
1988 WL 105754 (Del. Ch. Oct. 11, 1988) .....36, 37

*Nemec v. Shrader*,
991 A.2d 1120 (Del. 2010).....16

*O'Brien v. IAC/InterActive Corp.*,
2010 WL 3385798 (Del. Ch. Aug. 27, 2010),
*aff'd sub nom. IAC/InterActive Corp. v. O'Brien*,
26 A.3d 175 (Del. 2011).....41

*Oceanic Exploration Co. v. Grynberg*,
428 A.2d 1 (Del. 1981).....31

*Personnel Decisions, Inc. v. Bus. Planning Sys., Inc.*,
2008 WL 1932404 (Del. Ch. May 5, 2008) .....24

*Quadrant Structured Prod. Co. Ltd. v. Vertin*,
2014 WL 5465535 (Del. Ch. Oct. 28, 2014).....29

*Rainbow Nav., Inc. v. Pan Ocean Nav., Inc.*,
535 A.2d 1357 (Del. 1987).....23

*Red Clay Educ. Ass'n v. Bd. of Educ. of Red Clay Consol. Sch. Dist.*,
1992 WL 14965 (Del. Ch. Jan. 16, 1992) .....24, 25

*Rohe v. Reliance Training Network, Inc.*,
2000 WL 1038190 (Del. Ch. July 21, 2000).....26

*Salzberg v. Sciabacucchi*,
227 A.3d 102 (Del. 2020).....22

*Sciabbacucchi v. Salzberg, et al.*,
2018 WL 6719718 (Del. Ch. Dec. 19, 2018),
*rev'd on other grounds*, 227 A.3d 102 (Del. 2020).....20, 29

*Shared Commc'ns Servs. of ESR, Inc. v. WHTR Real Estate Ltd. P'ship*,
2017 WL 1372777 (Pa. Super. Apr. 13, 2017).....43

*Shields v. Shields*,
498 A.2d 161 (Del. Ch. 1985).....12

*Sterling v. Mayflower Hotel Corp.*,
93 A.2d 107 (Del. 1952).....21, 22

*Tang Capital P'rs, LP v. Norton*,
2012 WL 3072347 (Del. Ch. July 27, 2012).....25

*Trans World Airlines Inc. v. Summa Corp.*,
1987 WL 5778 (Del. Ch. Jan. 21, 1987),
*aff'd*, 540 A.2d 403 (Del. 1988).....42

*Underbrink v. Warrior Energy Servs. Corp.*,
2008 WL 2262316 (Del. Ch. May 30, 2008).....40

*UniSuper Ltd. v. News Corp.*,
898 A.2d 344 (Del. Ch. 2006).....30

**STATUTES**

8 *Del. C.* § 102(f).....30, 33

8 *Del. C.* § 109(b).....30, 33

8 *Del. C.* §§ 121.....27, 33

8 *Del. C.* § 122.....27, 33

8 *Del. C.* § 141(k).....26, 28

8 *Del. C.* § 151(a).....19, 20

8 *Del. C.* § 202(b).....35

8 *Del. C.* § 218.....*passim*

8 *Del. C.* § 225 ..... 32

8 *Del. C.* § 228 ..... 7, 13, 14, 15

*8 Del. C.* § 242 ..... 19

8 *Del. C.* § 259 ..... 10

8 *Del. C.* § 262 ..... *passim*

8 *Del. C.* § 291 ..... 25

14 *Del. C.* § 4007(a)(5) ..... 24, 25

**OTHER AUTHORITIES**

Cornerstone Research, *Appraisal Litigation in Delaware: Trends in Petitioners and Opinions 2006–2018* (2019), *available at* https://www.cornerstone.com/publications/reports ..... 23

Fisch, Jill E., *Private Ordering and the Role of Shareholder Agreements* (2020), *https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3201&context=faculty_scholarship* ..... 35

Original Synopsis, Senate Bill 75, 148th General Assembly (2015-2016) ..... 33

Schoenfeld, Matthew, *The High Cost of Fewer Appraisal Claims in 2017: Premia Down, Agency Costs Up*, HARVARD BUS. L. REV. (Jan. 2, 2018) ..... 23

## PRELIMINARY STATEMENT[1]

The buyer's Answering Brief (cited as "AB") distorts the plain meaning and natural operation of the words chosen by the parties to the SA. On the critical corporate law issues, the buyer blurs the important distinctions between (i) mandatory versus permissive sections of the DGCL, (ii) charters/bylaws versus separate agreements, (iii) knowing waivers versus *ex ante* waivers, and (iv) enforcement of agreements between stockholders versus enforcement by corporations against stockholders.

This Court should not lose sight of the circumstances here: the buyer is using the terminated SA, under which it was *never* an intended beneficiary, to (i) deprive Authentix's former stockholders of their "mandatory" right to an independent judicial appraisal, (ii) avoid its obligation to pay "fair value," and (iii) force Petitioners to pay $1.4 million in attorneys' fees for asserting their "absolute" statutory right. The buyer also wants to deny Petitioners interest on the Merger consideration it held for more than two years.

The actual beneficiaries of the SA—the Carlyle Stockholders—*never* exercised their Bring-Along Right or enforced any provision of the SA before it terminated upon consummation of the Merger. They and the Board never deemed it "necessary or desirable" that Petitioners do anything "in connection with the

[1] Abbreviated terms have the same meaning as in Petitioners' Opening Brief.

consummation of" the Merger, and therefore, never gave them notice, obtained their written consents, or required them to take any of the actions enumerated in Section 3(e), as they could have done before the SA terminated. The buyer can disagree with those decisions by the Carlyle Stockholders and the Board, but the SA contains *no* survival provisions and it cannot be revived and enforced by the buyer.

Authentix only identifies *potential* obligations in the SA that were never invoked. When quoting Section 3(e), Authentix's Answering Brief uses ellipses to create the impression that the "consent to and raise no objections" language is immediately followed by the "refrain from the exercise of appraisal rights" language. It is not. Those two phrases are separated by 296 words, and in between, Section 3(e) states that Petitioners "shall take all actions that the Board and/or the applicable Carlyle Stockholders *reasonably deem necessary or desirable in connection with the consummation* of such transaction." (Emphasis added.) Some of the actions the buyer wishes the Carlyle Stockholders and/or the Board had deemed "necessary," and required Petitioners to take, includes voting their shares in favor of the Merger, executing written consents in favor of the Merger, executing necessary documents (*e.g.*, the Merger Agreement), and refraining from the exercise of appraisal rights, etc. Instead, the Carlyle Stockholders and the Board closed the Merger (after a rushed process so Carlyle could receive a prompt payout) and terminated the SA without enforcing it.

Putting aside that the *intended* beneficiaries never enforced the SA while it remained viable, and that it terminated the instant the buyer took control of the Company, the plain language in Section 12 (the "Termination" provision of the SA) is not the only thing the buyer disregards. Authentix declares that "[t]he SA clearly and unambiguously waives appraisal rights" (AB at 46 (quoting Ex. B at 10)), but simply saying it does not make it so. The words "refrain" and "waive" have distinct meanings, and the SA deliberately uses the words "refrain" and "waive" in different places. Despite this, the buyer argues that the word "refrain" in Section 3(e) should be interpreted as "waive." But obviously, if the SA's words have to be interpreted contrary to their plain meaning, and if the obligation to "refrain" has to be applied as surviving termination despite the lack of survival provisions, the SA does not satisfy the requirement under Delaware law that waivers of rights be "clear and unambiguous."

Moreover, the trial court's strained reading was not necessary to give meaning to the SA because the Carlyle Stockholders could have exercised their Bring-Along Right or other rights but did not. Thus, the trial court failed to adhere to the requirement under Delaware law that special rights and restraints on rights be "strictly construed."

Finally, Authentix's response to the foundational statutory rights issues is that (i) freedom of contract is Delaware's preeminent public policy and it trumps the General Assembly's chosen words, and (ii) market forces determine what provisions of the DGCL are really mandatory, not the General Assembly. According to Authentix, investors and Delaware corporations can agree to anything, rendering the relationship between stockholders and Delaware corporations no different from the relationship between members and LLCs. That is wrong. To reiterate, we are talking about *advance* general waivers of mandatory rights, not *knowing* waivers in connection with actual transactions. If this Court countenances the use of ancillary agreements by Delaware corporations to alter mandatory stockholder rights on an *ex ante* basis, it will pave the way for destruction of the "corporateness" Delaware has strived to preserve with *inviolate* mandatory terms in the DGCL.

## SUMMARY OF ARGUMENT ON CROSS-APPEAL

I. DENIED. Petitioners are entitled to interest on the Merger consideration the buyer held for more than two years.

First, this action was filed pursuant to 8 *Del. C*. § 262. The trial court followed *Matter of Appraisal of Ford Holdings, Inc. Preferred Stock*, 698 A.2d 973 (Del. Ch. 1997), which held that preferred stockholders can agree in advance that fixed consideration constitutes the "fair value" contemplated by Section 262, thereby mooting the need for a judicial appraisal. This dispute is about whether Petitioners so agreed in the SA. The trial court's ruling that the SA comports with *Ford Holdings* did not change the nature of the proceeding. This remains a dispute about what amount constitutes "fair value." If this Court affirms the ruling that the SA fixed the "fair value" for Petitioners, the judgment for that "fair value" should include interest pursuant to Section 262(h), just like any other appraisal proceeding where the Court of Chancery determines the amount that represents "fair value."

Second, even if the trial court went beyond *Ford Holdings* and held that Section 262 does not apply or was expressly "waived" nine years in advance, Petitioners are entitled to pre-judgment interest as a matter of right and/or to prevent unjust enrichment. *See Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826 (Del. 1992) ("In Delaware, prejudgment interest is awarded as a matter of right …. [and] is to be computed from the date payment is due"); *Mehta v. Smurfit-Stone Container*

*Corp*, 2014 WL 5438534, at *5 (Del. Ch. Oct. 20, 2014) (holding that where a corporation retains merger consideration of stockholders past the time it is owed to dissenting stockholders, the elements of an unjust enrichment are satisfied). Although the amount of consideration due is in dispute, Petitioners were at all times entitled to consideration from the Merger, just like all the other stockholders, and the buyer held that consideration for more than two years.

II. DENIED. The buyer is not entitled to interest on its attorneys' fee award dating back to the date the fees were first incurred.

Unlike the advancement context, where fees are owed as they become due, this situation is akin to indemnification. In the indemnification context, payment obligations do not arise until a decision is rendered on the merits. There is little relevant case law, but the few courts that have directly addressed the point in time at which prejudgment interest begins to accrue on a fee award have held that it is *not until* the obligation arises. To wit, the payment obligation does not arise until after a decision on the merits that determines who prevailed and after a determination of the amount of reasonable fees owed to the prevailing party. That rationale is sound and, respectfully, it should be followed here.

## ARGUMENT ON APPEAL

### I. PETITIONERS COMPLIED WITH THEIR CONTRACTUAL OBLIGATIONS AND THE BUYER IS THE PARTY THAT REFUSES TO ADHERE TO THE PLAIN LANGUAGE OF THE STOCKHOLDERS AGREEMENT

The buyer's arguments: (i) distort the plain language in the provision of the SA that is, at best, ambiguous (*i.e.*, Section 3(e)); and (ii) disregard the language and operation of the provision of the SA that is indisputably clear (*i.e.*, Section 12).

Before termination of the SA and its "respective rights and obligations," Petitioners did exactly what the SA obligated them to do (or "refrain" from doing). During the period of the SA's enforceability, Petitioners:

- did not use their voting power to oppose or object to the Merger in compliance with Section 3(e)(ii)(i);
- could have been asked, but were never asked, to execute the Merger Agreement pursuant to Section 3(e)(ii)(ii);
- could have been asked, but were never asked, to vote their shares in favor of the Merger pursuant to Section 3(e)(ii)(iii);
- could have been asked, but were never asked, to deliver formal written consents to the Merger under 8 *Del. C*. § 228 pursuant to Section 3(e)(ii)(iii); and
- refrained from exercising appraisal rights, even though they were never asked pursuant to Section 3(e)(ii)(iv) to do so *before* the SA terminated because the Merger closed before they were provided with notice and *before* the window to exercise their appraisal rights was triggered.

### A. The Buyer is Not a Beneficiary With Independent Rights

*Pre*-Merger Authentix and *post*-Merger Authentix are treated differently under the SA. Authentix does not effectively grapple with Section 12, which unambiguously provides:

> This Agreement, *and the respective rights and obligations of the Parties*, *shall terminate* upon the earlier of the (a) consummation of a Company Sale and (b) execution of a written agreement of each Party … to terminate this Agreement; provided, however, that Section 2, 3, 4, 6, 7, 8 and 9 hereof shall terminate upon the closing of an IPO.

(JA0066 (emphasis added).)

The question is not whether the SA can be enforced post-termination. It cannot. Emphasizing that Authentix is a signatory and that the buyer maintains Authentix as the surviving corporation (AB at 28) misses the point. The "respective rights and obligations of the Parties," which includes Authentix, terminated upon consummation of the Merger, *without exception*, and Authentix—*no matter who controls it*—cannot enforce rights the Company once might have been able to exercise but chose not to during the duration of its term. Contracts are about expectations and no buyer could reasonably argue that they had an expectation of independent and live rights in the face of Section 12.

The buyer fails to cite a single case for the proposition that it has independent, live and enforceable rights in the face of Section 12. Even the trial court did not hold that the buyer was an intended beneficiary with enforceable rights. The trial court held that Petitioners' obligation to "refrain" vested *and* survived closing. The real question is whether that conclusion is correct (discussed *infra*). The effect of the trial court's ruling is that the buyer benefitted (incidentally) from Petitioners' obligation to "refrain" that allegedly accrued *prior to* termination of the SA. This was a temporal observation by the trial court, not an express finding grounded in contract language or law that the buyer is an "intended" beneficiary.

Authentix ignores the case law holding that only *intended* beneficiaries may enforce an agreement, *NAMA Hldgs., LLC v. Related World Mkt. Ctr, LLC*, 922 A.2d 417, 434 (Del. Ch. 2007), and that an entity that *may have* benefitted only incidentally from a contract—like the buyer here—still "has no rights under the contract" unless they are an *intended* beneficiary. *Delmar News, Inc. v. Jacob Oil Co.*, 584 A.2d 531, 534 (Del. Super. 1990). "[T]he contracting parties must *intend* to confer a benefit." *Id.* (emphasis added).[2]

[2] *Delmar News* dealt with third-party beneficiaries, but the analogy is apt: "If, however, the parties to the contract did not intend to benefit the third-party *but the third-party happens to benefit from the performance of the contract* either indirectly or coincidentally, *such third person has no rights under the contract*." 584 A.2d at 534 (emphasis added).

To reiterate, Petitioners did not enter into the SA with *the buyer*, nor did they agree *nine years in advance* to (i) "waive" appraisal rights after-the-fact for some then-unknown buyer in the event the Carlyle Stockholders refused to enforce the SA, or (ii) pay the attorneys' fees of some then-unknown buyer in the event of a dispute over whether a buyer can enforce the SA *post*-termination.

The termination of the rights and obligations in the SA is also consistent with 8 *Del. C.* § 218. Stockholder agreements, like the SA, "govern[] the relationship between the Company's *current* shareholders." *In re Coffee Assocs., Inc.*, 1993 WL 512505, at *2 (Del. Ch. Dec. 3, 1993) (emphasis added). Once the stockholders are cashed out, as here, there is no longer any relationship to govern.

It is true that forum selection and fee-shifting provisions survive for disputes legitimately arising under an agreement (AB at 30-31), but they survive *only* for parties who were actual beneficiaries of those provisions while the agreement was live. None of the cases cited by Authentix holds otherwise. Here, post-change-of-control-Authentix was *never* a beneficiary, pre-or post-termination, period.

Finally, there was no pre-termination breach of the SA that accrued for which the buyer could sue as the successor-in-interest per 8 *Del. C.* § 259. Indeed, Petitioners did nothing prior to termination of the SA because they were never made aware of the Merger before the SA terminated. Again, *pre*-Merger Authentix and *post*-Merger Authentix are treated differently under the SA. The present dispute

with the buyer about whether the SA is enforceable by the buyer is not a dispute between Petitioners and *pre*-Merger Authentix. The events giving rise to the buyer's defense and its effort to enforce the "loser pays" provision—*i.e.*, the mailing *by the buyer* of the misleading Information Statement and demand that Petitioners execute written consents—*all* occurred *after* the Merger closed and *after* the SA terminated. A buyer that under no reading of the SA was ever intended to inherit a live SA and have independent rights cannot enforce it as a party or intended beneficiary.

### B. The Potential Obligations in the Stockholders Agreement Were Never Triggered

The real focus should be on whether any obligations vested pre-termination, and if so, whether they survived termination. The answer to both questions is "no."

Even assuming the obligation to "consent to and raise no objections" was triggered upon mere approval of the Merger by the Board, Petitioners fully complied with their obligation by not even attempting to use their voting power to oppose or object to the Merger.

The buyer suggests that not only was the obligation to "consent to and raise no objections" triggered when the Board voted to approve the Merger, but that the vote triggered, encompassed and vested everything Petitioners could have been asked to do, but were not. (AB at 24, 27-30.) That is not a fair reading of Section 3(e). The commercial rationale for the "consent to and raise no objections" language is to ensure a transaction can be approved and closed promptly and with certainty.

It is one thing to agree not to use your vote to prevent the accomplishment of a transaction, but to suggest that such language also evinces a clear and unambiguous intent to irrevocably waive a "mandatory" right is something entirely different. Notably, however, even this portion of Section 3(e) was not invoked because it was not necessary. The Merger was approved and closed without any risk of objection or delay because Petitioners had no prior notice.

With regard to the other *potential* obligations enumerated in Section 3(e) that Petitioners could have been asked to perform, it is undisputed that neither the Carlyle Stockholders nor the Board "reasonably deem[ed]" them "necessary or desirable in connection with consummation of the Merger." Motivated to provide a prompt payout to Carlyle, they ran a rushed sales process, quickly consummated the Merger, and terminated the SA. Thus, the other potential obligations in Section 3(e) were never exercised/triggered and therefore never vested. As observed in *Shields v. Shields*, "[t]he fact that a merger may have the effect of eliminating a class of corporate securities and thus legally mooting an *unexercised* power with respect to such securities is neither shocking nor novel." 498 A.2d 161, 168 (Del. Ch. 1985).

Furthermore, the buyer's argument on the operation of Section 3(e) improperly ignores the "reasonably deem" and "necessary or desirable" language and renders it surplusage. *See In re Shorenstein Hays-Nederlander Theatres LLC Appeals*, 213 A.3d 39, 56-57 (Del. 2019) (courts should avoid interpreting contracts

in a way that renders meaningless the words chosen by the parties). The buyer may wish the Carlyle Stockholders and the Board had enforced the SA while it remained viable, but they did not. Nor did the buyer demand that it be enforced *as written* before it terminated. This situation is like *Halpin v. Riverstone Nat'l, Inc.*, 2015 WL 854724 (Del. Ch. Feb. 26, 2015), where the right to demand written consents was not exercised as written.

Separately, *the buyer*'s after-the-fact request that Petitioners execute written consents was not a request from "*the Board* and/or *the applicable Carlyle Stockholders*" during the term of the SA. Moreover, a request that Petitioners execute written consents after the Merger occurred cannot "reasonably" be construed as an action taken in connection with, let alone "necessary" for "consummation" of the Merger that had *already* been consummated. Once the Merger closed, the SA terminated and nothing further was required to make it effective.

Finally, the obligation to "refrain from the exercise of appraisal rights" could not have vested pre-termination. When a merger is simultaneously approved and closed by written consent pursuant to 8 *Del. C.* § 228—like the Merger here—appraisal rights are not triggered until *after* closing. *See* 8 *Del. C.* § 262(d)(2) (*i.e.*, notice to stockholders within 10 days of closing and service of the demand letter within 20 days of notice). Pre-termination/closing, Petitioners had nothing to exercise, or "refrain from exercising." Relatedly, to be cut off from appraisal rights,

the "consent" must be "pursuant to § 228," *see id.*, § 262(a), and prior to termination of the SA, Petitioners were never asked to execute written consents, nor did they. The trial court misunderstood both of these dispositive points and Authentix's Answering Brief fails to effectively address them.

### C. The Stockholders Agreement is, at Best, Ambiguous and it Was Misconstrued by the Trial Court

Even assuming the "refrain" obligation was triggered before the SA terminated, it did not survive termination. On this, the trial court erred in multiple ways in its construction and application of Section 3(e).

First, by holding that appraisal rights can *only* be "exercised" post-closing and that the "refrain" obligation must survive termination to avoid being a "nullity," the trial court ignored (i) the case law discussing the delivery of the appraisal demand letter as an "exercise" of appraisal rights and (ii) the real-world fact that some deals are structured such that they can be terminated (obviously *pre*-closing) if too many stockholders "exercise" appraisal rights. Authentix's Answering Brief fails to refute or even address this point.

Second, the trial court erred in holding that "[t]he SA clearly and unambiguously *waives* appraisal rights." (Ex. B at 10 (emphasis added).) If the SA represents a clear relinquishment of a right, Authentix and the trial court would not have to interpret the word "refrain" to mean "waive." This is not a "semantic quibble." (AB at 25.) The word "waive" is not even used in Section 3, though it

could have been if that was the intent. The plain meaning of "refrain" represents a narrower obligation rather than a relinquishment, forever, of rights. Nothing in the SA indicates that Petitioners assumed an "irrevocable" obligation. The trial court violated the most basic precept of contract construction: that words be given their "plain, ordinary meaning." *Alta Berkeley VI C.V. v. Omneon, Inc.*, 41 A.3d 381, 385 (Del. 2012).

Third, the trial court ignored the plain language and operation of Section 12. The trial court's conclusion that the "refrain" obligation must survive is contrary to the express and unambiguous language in Section 12. The SA does not contain *any* language *even hinting* that Section 3 might not be governed by Section 12, although it could have. Nor did the "refrain" obligation have to be interpreted as surviving to avoid being a "nullity" because the SA could have been enforced as written. Authentix's Answering Brief does not overcome any of these points.

The buyer's actions upon consummation of the Merger demonstrate that even the buyer understood that the SA is ambiguous, at best, and that the Carlyle Stockholders and the Board never enforced the rights/obligations in the SA. That is why, *after* the closing and termination of the SA, the buyer sent out a notice of appraisal rights per the requirement of Section 262(d)(2) and asked Petitioners to execute written consents per 8 *Del. C.* § 228 "to *waive* any appraisal rights that you may have under Section 262." (JA0459 (emphasis added).) The buyer would have

seen no need to make such a request if Petitioners had already "clearly and unambiguously *waive[d]* appraisal rights," as the buyer argues today. (AB at 46 (quoting Ex. B at 10) (emphasis added).)

In sum, the buyer's construction of the SA does not work with respect to a merger effectuated by written consent with no prior notice to stockholders, like the Merger here. Even so, there was no basis under Delaware law for the trial court to "blue-pencil" Section 12 and re-write the SA through creative interpretation of the word "refrain" to try to accommodate a scenario which the contracting parties themselves did not contemplate. *See C&J Energy Services, Inc. v. City of Miami General Employees' and Sanitation Employees' Retirement Trust*, 107 A.3d 1049, 1072 (Del. 2014); *Nemec v. Shrader*, 991 A.2d 1120, 1125 (Del. 2010) ("Parties have a right to enter into good and bad contracts, the law enforces both."). "[A] party may not come to court to enforce a contractual right that it did not obtain for itself at the negotiating table," *GRT, Inc. v. Marathon GTF Tech., Ltd*., 2012 WL 2356489, at *7 (Del. Ch. June 21, 2012), because "it is not this Court's function to save sophisticated contracting parties from an unfair or unanticipated result of their own corporate transactions." *MTA Can. Royalty Corp. v. Compania Minera Pangea, S.A. De C.V.*, 2020 WL 5554161, at *14 (Del. Super. Sep. 16, 2020).

The aforementioned rules apply to a straightforward contract analysis, but what the trial court did here is even more problematic because contracts that purport to waive rights—like the SA—must be "clear and unambiguous" and must be "strictly and narrowly" construed. *See Halpin*, 2015 WL 854724 at *8; *Harbor Fin. Partners Ltd. v. Butler*, 1998 WL 294011, at *6 (Del. Ch. June 3, 1998), *rev'd sub nom. on other grounds Elliott Assocs., L.P. v. Avatex Corp.*, 715 A.2d 843 (Del. 1998). Respectfully, the trial court's rulings and the buyer's arguments violate both of these rules of law.

### D. The Buyer's Argument on the "Same Price" Condition Fails to Explain the Operative Language in the Stockholders Agreement

The trial court never ruled on whether the "same price" condition was satisfied, only that it does not apply to the Merger. For that reason, Petitioners only addressed the latter. Although Authentix addressed the former (AB at 35), it is not properly before the Court.

Nothing Authentix says in its Answering Brief detracts from the explanation in Petitioners' Opening Brief as to why the "same price" condition applies to mergers and direct stock sales but not to asset sales. Petitioners' argument is not circular. (AB at 32-33.) Not all sales of securities are mergers, but all mergers are sales of equity securities. Notably, Authentix does not effectively explain how, if the Merger is not a "sale of Equity Securities" under Section 3(e), Petitioners could have been required (*if* they had been asked) to execute a "merger agreement" for a transaction

involving documents "executed by each Carlyle Stockholder *selling Equity Securities*." (JA0074 (emphasis added).)

Finally, the trial court's "waiver" finding is based on *Ford Holdings*. If the "same price" condition does not apply to the Merger, then there is nothing in the SA *purporting* to substitute for "fair value," which is the requirement under *Ford Holdings* to moot a judicial appraisal.

## II. THE COMPANY'S ENFORCEMENT OF THE STOCKHOLDERS AGREEMENT VIOLATES SEVERAL SECTIONS OF THE DELAWARE GENERAL CORPORATION LAW

### A. Enforcement by the Company Violates Section 151(a)

The trial court's ruling and Authentix's argument that 8 *Del. C.* § 151(a) does not apply are both based on a false premise: that "the SA is not the equivalent of imposing limitations on a class of stock." (AB at 36 (quoting Ex. A at 11).) That is exactly what the SA does.

It is undisputed that the SA was binding on *all* of the Company's outstanding stock at the time of execution in 2008 and Section 13(b) states that it "shall be binding upon … assigns and any other transferee and shall also apply to any securities acquired by a Holder after the date hereof." (JA0089.) The SA is targeted at the stock itself, which is why it applies to subsequent transferees and subsequent purchases. Indeed, not a single share of Authentix stock was exempt from the SA.

By claiming authority to define the rights of its stock through a separate contract, Authentix urges a violation of the DGCL. *See* 8 *Del. C.* § 151(a) (providing that corporations "may issue 1 or more classes of stock … [with] such designations, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions thereof, *as shall be stated and expressed in the certificate of incorporation or of any amendment thereto*") (emphasis added); *see also id.,* § 242 (permitting amendment to rights or preferences of certain series

or classes of stock *only* by charter amendment); *In re Appraisal of Metromedia*, 971 A.2d 893, 899 (Del. Ch. 2009) ("A preferred shareholder's rights are defined in either the corporation's certificate of incorporation or in the certificate of designation, which acts as an amendment to the certificate of incorporation.") (citing *Elliot Assocs., L.P. v. Avatex Corp.*, 715 A.2d 843, 852 (Del. 1998)).

Authentix's citation to 8 *Del. C.* § 218 (AB at 37) is unavailing. Whether or not Section 218 limits the number of *stockholder*-parties to an agreement (it does not) is irrelevant. The relevant inquiry is who is purporting to enforce the agreement. This Court does not have to decide the limits of what stockholders can do to each other by separate agreement, but any "substantive limitation [on stockholder rights] must appear in the charter" to be enforced by a corporation. *Sciabbacucchi v. Salzberg, et al*., 2018 WL 6719718, at *18 n.49 (Del. Ch. Dec. 19, 2018), *rev'd on other grounds*, 227 A.3d 102 (Del. 2020). Given the breadth of Section 13(i), it cannot operate independently of Section 151(a) of the DGCL.

Application of Section 151(a) in this circumstance is not just mandated by the statutory language, it preserves the hierarchical corporate contract and ensures that *corporations* do not impermissibly alter "mandatory" rights attached to stock in ways that would be illegal if placed in the charter.

## B. Enforcement by the Company Violates Section 262

### 1. The Buyer Misreads the Statutory Language

Authentix never explains away the binding and well-reasoned precedent holding that mandatory provisions of the DGCL cannot be overridden by the corporation. *See Sterling v. Mayflower Hotel Corp.*, 93 A.2d 107, 118 (Del. 1952); *Jones Apparel Group, Inc. v. Maxwell Shoe Co., Inc.*, 883 A.2d 837, 843 (Del. Ch. 2004) (following *Sterling*).

Petitioners' Opening Brief explained that *Ford Holdings* and its progeny have already held that (i) Section 262 is a "mandatory" provision and (ii) "mandatory provisions may not be varied by the terms of the certificate of incorporation *or otherwise*." 698 A.2d at 976 (emphasis added). Contrary to Authentix's contention (AB at 44), *Ford Holding* did *not* rule that stockholders can "waive" appraisal rights. The Court held that for contractually-based preferred stock, the need for a judicial appraisal can be mooted where the certificate of designation creating the security contains a "fixed consideration" substituting for "fair value." *Id.* at 977-978. The SA does not provide the requisite fixed amount. Nor does Authentix provide a rationale for extending *Ford Holdings* to common stock. Indeed, to do so would run contrary to the rationale in *Ford Holdings*, which is based on the contractual nature of preferred stock.

Authentix's argument that appraisal rights can be waived because Section 262 "does not explicitly prohibit contractual modification or waiver" (AB at 38 (quoting Ex. B at 10)) should be rejected. First, Authentix invites the Court to cast aside the General Assembly's chosen word "shall" and the ruling in *Ford Holdings* based on that word. *See also Kaye v. Pantone, Inc.*, 395 A.2d 369, 374-375 (Del. Ch. 1978) (holding stockholders have an "absolute right" to appraisal); *Felder v. Anderson, Clayton & Co.*, 159 A.2d 278, 286 (Del. Ch. 1960) (same).

Second, no provision of the DGCL uses the words "mandatory" or "shall not be waived," so, according to the buyer, any stockholder right is waivable. This is contrary to this Court's recent ruling in *Salzberg v. Sciabacucchi* that the DGCL contains "statutory parameters" that must be "honored." 227 A.3d 102, 116 (Del. 2020); *see also Sterling*, 93 A.2d at 118 (a corporation cannot "transgress a statutory enactment or a public policy settled by the common law or implicit in the [DGCL] itself"). Lack of a prefatory clause—*e.g.*, "unless otherwise provided in the certificate of incorporation"—is not always determinative of what is modifiable, *see Jones Apparel*, 883 A.2d at 847-848, but the General Assembly's use of the <u>*mandatory*</u> word "shall" <u>*without*</u> a prefatory clause is determinative. *See Arnold v. State*, 49 A.3d 1180, 1183 (Del. 2012) ("The mandatory 'shall' … normally creates an obligation impervious to judicial discretion").

Third, the buyer's proposed reading of the DGCL conflicts with this Court's construction and protection of other stockholder rights. For example, in *Rainbow Nav., Inc. v. Pan Ocean Nav., Inc.*, this Court held that Section 220 creates mandatory inspection rights that "can only be taken away by statutory enactment." 535 A.2d 1357, 1359 (Del. 1987).

Finally, Section 262 is "freighted" with public policy, *Finkelstein v. Liberty Digital, Inc.*, 2005 WL 1074364, *13 (Del. Ch. Apr. 25, 2005), and any modification of Section 262 by a corporation contravenes that public policy. *See Ford Holdings*, 698 A.2d at 977 (acknowledging "the public policy reflected in Section 262").[3] The public policy behind inviolate appraisal rights has even greater significance for stockholders of private companies—like Petitioners—who lack a robust market for their shares. *See* Cornerstone Research, *Appraisal Litigation in Delaware: Trends in Petitioners and Opinions 2006–2018*, p. 9 (2019), *available at* https://www.cornerstone.com/publications/reports (finding that appraisal petitioners of "public targets receiv[ed] on average only an 8 percent award to deal price, as opposed to 47 percent for private firms.").

[3] Putting aside the General Assembly's use of the indefeasible word "shall" and the public policy behind Section 262, there are also economic and market efficiency reasons for preventing the blanket elimination of appraisal rights. *See, e.g.*, Schoenfeld, Matthew, *The High Cost of Fewer Appraisal Claims in 2017: Premia Down, Agency Costs Up*, HARVARD BUS. L. REV. (Jan. 2, 2018) (observing a decline in merger premia corresponding with a decline in appraisal filings).

### 2. The Buyer Confuses the Case Law and Corporate Power

The buyer's contention that Delaware courts routinely enforce contractual waivers of statutory rights (AB at 39-43) is based on a series of inapposite cases that either involve *permissive* statutory provisions or *knowing* waivers in connection with specific transactions. Petitioners' Opening Brief already distinguished *Libeau v. Fox*, 880 A.2d 1049 (Del. Ch. 2005), *Kortum v. Webasto Sunroofs Inc.*, 769 A.2d 113 (Del. Ch. 2000), and *Graham v. State Farm*, 565 A.2d 908 (Del. 1989). Authentix's other cases fare no better.

*Personnel Decisions, Inc. v. Bus. Planning Sys., Inc.*, is unavailing because the Court merely concluded that Delaware public policy would not be offended by an agreement that provided for arbitration outside Delaware. 2008 WL 1932404, at *6 (Del. Ch. May 5, 2008). Again, arbitration is a substitute for a trial, not a waiver of a claim/remedy.

In *Red Clay Educ. Ass'n v. Bd. of Educ. of Red Clay Consol. Sch. Dist*., the school district revised school start times without the consent of the teachers' union. 1992 WL 14965, at *6 (Del. Ch. Jan. 16, 1992). The Court considered an alleged violation of the Public School Employment Relations Act ("PSERA"), which provides that "[i]t is an unfair labor practice for a public school employer or its designated representative to … (5) Refuse to bargain collectively in good faith with an employee representative." 14 *Del. C.* § 4007(a)(5). That provision is not

structured as a mandatory right with the word "shall." Rather, Section 4007(a)(5) enumerates a series of unfair labor practices. The Court did not construe the situation as an *ex ante* waiver, and instead, held that the PSERA requirement was modified by the parties' collective bargaining agreement, which the Court read to provide that "neither party will be required to negotiate *with respect to any matter covered in the contract*." *Id.* at *4 (emphasis added). Properly read, the collective bargaining agreement satisfied the requirement of Section 4007(a)(5).

Likewise, in *Tang Capital P'rs, LP v. Norton*, the Court did not consider a mandatory provision of the DGCL, but rather, the permissive authority of the Court of Chancery to appoint a receiver per 8 *Del. C.* § 291 upon application of a noteholder. 2012 WL 3072347, at *7 (Del. Ch. July 27, 2012). Putting aside that *Tang* involved a noteholder, not a stockholder, the plain language of Section 291 does not permit analogy to Section 262. *See* 8 *Del. C.* § 291 ("… the Court of Chancery … *may*, at any time, appoint 1 or more persons to be receivers of and for the corporation ….") (emphasis added).[4]

[4] Authentix's citation to *Baio v. Commercial Union Ins. Co.* is odd because the Court dealt with a specific situation rather than an *ex ante* waiver of a statutory right. 410 A.2d 502, 508 (Del. 1979) (finding equity required modification of the statutory right of subrogation). *Baio* has no application here.

Authentix's final case ignores the distinction between enforcement by a fellow stockholder versus the corporation itself. In *Klaassen v. Allegro Development Corp.*, the Court considered a bylaw that modified Section 141(k), which provides that "[a]ny director or the entire board of directors *may* be removed" by holders of the majority of stock, subject to certain exceptions. 2013 WL 5739680, at **24–26 (Del. Ch. Oct. 11, 2013) (describing 8 *Del. C.* § 141(k)) (emphasis added). The modification of "voting" power was in a stockholders agreement, which the bylaw referenced. *Id.* at *22. The limitation was being enforced by the designee of a stockholder-party thereto. The Court acknowledged that the bylaw was otherwise unlawful and that the modification of Section 141(k) could only be enforced between the stockholder-parties to the agreement. *Id.* at **24–25. Here, the Company is enforcing the SA.

The buyer claims the SA was not "imposed on Petitioners by the corporation" (AB at 39), but the Carlyle Stockholders did not enforce it and the buyer is trying to do so as "the corporation" on the basis that Authentix is a *signatory*. (*Id.* at 28.) The buyer seeks a blanket ruling that *corporations* may enforce contracts with provisions that would be illegal if placed in the charter. Such a ruling would misconstrue *Klaassen* and violate Delaware law and public policy. *See Rohe v. Reliance Training Network, Inc.*, 2000 WL 1038190, at *16, n. 49 (Del. Ch. July 21, 2000) ("[S]tockholders can bind themselves contractually in a stockholders agreement in a

manner that cannot be permissibly accomplished through a certificate of incorporation.").

The buyer contends that because stockholders can "inadvertently lose" their right of appraisal, the right is not "fundamental." (AB at 43.) That makes no sense. *Any* claim, even a serious personal injury claim, can be lost in multiple ways (*e.g.*, statutes of limitations, etc.), but that does not diminish the claim. Likewise, the availability of a fiduciary duty claim is irrelevant because the defendants and the elements of the claims are entirely distinct. *See*, *e.g.*, *Cede & Co. v. Technicolor, Inc.*, 542 A.2d 1182, 1189 (Del. 1988) ("A determination of fair value does not involve an inquiry into claims of wrongdoing in the merger"). As a matter of Delaware law and public policy, stockholders are *entitled* to faithful fiduciaries *and* a "fair value" proceeding when their stock is taken without their consent in a merger.

With regard to general contracting authority (AB at 47), a Delaware corporation "may exercise all of the powers and privileges granted by [the DGCL]" in furtherance of its lawful business activities, 8 *Del. C.* § 121(a), and that includes the power to "make contracts." *Id.*, § 122(13). However, Section 122 does not authorize corporations to "make" or enforce *any* "contracts" they want, particularly if they violate public policy and mandatory stockholder rights. A corporation's freedom of contract yields to the the public policy embedded in the mandatory provisions of the DGCL. *See In re Appraisal of Dell Inc.*, 2015 WL 4313206, at *13

n.11 (Del. Ch. July 13, 2015) (citing *Jones Apparel* and rejecting notion that the DGCL permits maximum or unrestrained freedom of contract). The DGCL is not the LLC Act.

Here, the General Assembly crafted Section 262 as a mandatory provision. It can only be modified in advance with respect to contractually-based preferred stock that provides *fixed* consideration for "fair value." There is, of course, no impediment to stockholders waiving appraisal rights for a transaction after they *know* what value is to be exchanged. Otherwise, the Section 262 right cannot be taken away by the corporation *ex ante*.

The General Assembly's chosen words determine the public policy of Delaware's corporation law, not private equity and venture capitalists. (AB at 37, 45.) Courts strike down any so-called "market" provisions that violate the DGCL. In *In re VAALCO Energy, Inc. S'holder Litig.*, the Court struck down a "for-cause" removal bylaw because it violated Section 141(k):

> To the extent that this upsets expectations at some give-or-take 175 public companies . . . , that is just a consequence of people not reading the statute . . . . Just as 'all the other kids are doing it' wasn't a good argument for your mother, . . . the idea that 175 other companies might have wacky provisions isn't a good argument for validating your provision.

C.A. No. 11775-VCL, at 59–60 (Del. Ch. Dec. 21, 2015) (TRANSCRIPT).

Parties can choose to structure their affairs under Delaware law, but if a corporation is their chosen form, they must operate within Delaware's hierarchal corporate contract: (i) DGCL; (ii) charter; (iii) bylaws; and (iv) other agreements to which the corporation is a party. *See Quadrant Structured Prod. Co. Ltd. v. Vertin*, 2014 WL 5465535, *3 (Del. Ch. Oct. 28, 2014). "The contract that gives rise to the artificial entity is not an ordinary private contract among private actors." *Sciabbacucchi*, 2018 WL 6719718, at *18.

> When accepted by the Delaware Secretary of State, the filing of a certificate of incorporation effectuates the sovereign act of creating a "body corporate"—a legally separate entity. The State of Delaware is an ever-present party to the resulting corporate contract, and the terms of the corporate contract incorporate the provisions of the DGCL. Various sections of the DGCL specify what the contract must contain, may contain, and cannot contain. *The DGCL also constrains how the contract can be amended*.

*Id.* at *2; *see also id.* at *19–20.

Delaware public policy, as evidenced by the General Assembly's use of the mandatory word "shall," does not permit a roundabout amendment by a corporation of state-granted mandatory rights within the hierarchal corporate contract. Delaware has carefully preserved "corporateness" with inviolate mandatory terms for the very purpose of distinguishing corporations from alternative entities. The notion that a Delaware corporation has a legitimate interest in relieving a *future* buyer of the statutory obligation to pay "fair value" to its stockholders turns the hierarchy on its

head. Permitting an *ex ante* waiver is also inconsistent with "[t]he rule in Delaware [] that a release cannot apply to future conduct." *UniSuper Ltd. v. News Corp.*, 898 A.2d 344, 348 (Del. Ch. 2006).

It was wrong for the trial court to impose its view that the "ability to avoid appraisal would make the [corporation] more attractive to potential buyers." (Ex. A, p. 10.) That was a policy determination, which improperly eradicated the contrary policy determination already made by the General Assembly when it crafted Section 262 as a mandatory stockholder right. A corporation with stockholders—all bound by an ancillary agreement—who have no rights under Sections 115, 211, 220, 225, 262, etc., no right to bring direct or derivative fiduciary claims, and no protection from "loser pays" provisions per Sections 102(f) and 109(b), would undoubtedly be attractive to an investor seeking to acquire control, but that does not make the elimination of such rights permissible, even if all of that is unambiguously set forth in a separate agreement between the corporation and its stockholders.[5]

[5] The trial court's view on appraisal overlooks the purpose of appraisal rights, which is to protect stockholders being cashed out against their will by ensuring they receive "fair value" from a buyer. The trial court seems to suggest that the "attractive[ness]" of a target whose stockholders have no appraisal rights is that the buyer can save post-closing litigation expense and therefore pay more upfront, but it is equally true that the "attractive[ness]" is that it can pay less with no fear of an independent judicial appraisal. Here, the alleged waiver of appraisal rights was not part of the Merger negotiations, so it was not given up in exchange for an increase in the offer.

Condoning the use of ancillary agreements by corporations to alter mandatory rights *ex ante* would destroy the multiple policy considerations imbedded in the DGCL, and with it, the Delaware franchise.

### C. Enforcement by the Company Violates Section 218

Authentix argues that Section 218 applies only to voting trusts and *not* to stockholder agreements (AB at 49-50), but Section 218 is titled "Voting trusts and other voting *agreements*." (Emphasis added.) Authentix's position is at odds with the case law. In *Abercrombie v. Davis*, this Court used the words "stockholders' agreement" when referring to the 1925 enactment of the first statute, observing that prior to statutory authorization, any "*stockholders' agreement* provid[ing] for joint or concerted voting" was likely illegal at common law. 130 A.2d 338, 344 (Del. 1957) (emphasis added).

This Court has pointed out that the statute (now Section 218) "fully occupie[s]" the "field." *Id.* (emphasis in original) (citations omitted); *see also Oceanic Exploration Co. v. Grynberg*, 428 A.2d 1, 5 (Del. 1981) ("[Section] 218 of the Delaware General Corporation Law provides the *exclusive method* for creating voting trusts of stock of a Delaware corporation") (emphasis added). The trusts *and* agreements covered by Section 218 "derive their validity from *limited* statutory authorization." *Belle Isle Corp. v. Corcoran*, 49 A.2d 1, 4 (Del. 1946) (emphasis added).

Authentix makes no effort to show that the SA falls outside the ambit of Section 218 because it separates voting rights from ownership for the principal purpose of exercising voting control in certain circumstances. *See Lehrman v. Cohen*, 222 A.2d 800, 805 (Del. 1966) (citing *Abercrombie*). The SA was intended to provide a *potential* tool to control Petitioners' vote in the event of a merger, and if utilized, restrain their appraisal rights under certain circumstances and deter their right to sue by shifting fees. An agreement between stockholders that "interfere[s] with stock ownership rights" falls within the scope of Section 218. *Dweck, et al., v. Nassar, et al.*, 2005 WL 5756499, at *4-5 (Del. Ch. Nov. 23, 2005).

The caselaw regarding Section 225 of the DGCL is on point. Prior to 2008, corporations had no authorization to proceed under Section 225. *See In re Native Am. Energy Grp., Inc.*, 2011 WL 1900142, at *5 (Del. Ch. May 19, 2011). Section 218 is no different than Section 225 when it comes to the need for corporations to have statutory authorization. In 2008, the General Assembly granted it to corporations with regard to Section 225(b) but has never done so with respect to Section 218. The validity of stockholder agreements is derived solely from "statutory authorization." *Belle Isle*, 49 A.2d at 4; *Abercrombie*, 130 A.2d at 344. There is no authority for a Delaware corporation to enter into and enforce a stockholder agreement that alters the rights of *all* of its own stockholders for *the corporation's own benefit*.

Here too, 8 *Del. C.* §§ 121 and 122 (AB at 47) do not help Authentix's cause. General contracting authority does not overcome the lack of statutory authorization for corporations under Section 218, nor does it authorize corporations to "make" or enforce *any* "contracts" they want, particularly if they violate public policy and mandatory stockholder rights. Again, a Delaware corporation must operate within Delaware's well-recognized hierarchical corporate contract. The general authority under Section 122(13) to enter into contracts is not a license for Delaware corporations to upend Delaware's hierarchical corporate contract at will.

Authentix is correct that the Synopsis to 8 *Del. C.* §§ 102(f) and 109(b) states that the ban on "loser pays" provisions was "not intended, however, to prevent the application of such provisions pursuant to a stockholders agreement *or other writing* signed by the stockholder against whom the provision is to be enforced," Original Synopsis, Senate Bill 75, 148th General Assembly (2015-2016) (emphasis added), but this is not new statutory authorization for corporations. Indeed, the Synopsis does not address *who* can enforce the "stockholders agreement." The Synopsis provides no meaningful insight. One understanding of the Synopsis is that it emphasizes that Sections 102(f) and 109(b) should not to be construed to prevent (as a matter of public policy): (i) "two or more *stockholders*," per the statutory language and authority of Section 218, from entering into and enforcing a *stockholders* agreement with a fee-shifting provision; and (ii) a corporation from entering into

"other writing[s]," such as settlement agreements with stockholders, that contain fee-shifting provisions in the event of a breach. Nothing in the Synopsis suggests that it expanded the then-existing authority of corporations under the DGCL, definitively recognized corporate authorization in Section 218, or condoned the *ex ante* alteration of mandatory stockholder rights in some "other writing."

Authentix also makes an argument by analogy and cites *Bonanno v. VTB Holdings, Inc*., 2016 WL 614412 (Del. Ch. Feb. 8, 2016), as an instance where courts found that forum selection clauses in stockholders agreements were enforceable. *Bonanno* is distinguishable in several respects, and the Court there certainly did not grapple with the myriad issues Petitioners have raised here.

In *Bonanno*, the plaintiff brought an action in Delaware for redemption of his series B preferred stock, a *contract* right arising from a stock purchase transaction (not the DGCL), and the defendant parent corporation successfully enforced a New York forum selection provision contained in several contracts relating to that stock purchase transaction. 2016 WL 614412, at *1-3. The defendant corporation in *Bonanno* did not seek to eliminate through contract the right to bring a claim, nor did it seek to eliminate the right of *all* stockholders to bring claims in Delaware. If anything, *Bonanno* stands for the proposition that a forum selection clause in a separate agreement with a select group of stockholders may be enforceable for disputes arising under the agreement to enforce rights *created* by the agreement

itself. The rights in *Bonanno* were entirely *independent* of the rights attached to the stock under the DGCL. The latter (*i.e.*, all mandatory rights available to stockholders under the DGCL) are independently available and inviolate once a stockholder becomes a stockholder.

In sum, there is no authority in the DGCL for corporations to enter into stockholder agreements to alter mandatory stockholder rights outside the charter. Upon review of the trial court's ruling below, one scholar said it best:

> The problem with this analysis is that these shareholder agreements address corporate governance rather than merely an individual shareholder's rights …. An agreement to forsake appraisal rights affects the terms of future transactions…. Moreover, if all shareholders must agree to the terms of the shareholder agreement as a condition of acquiring stock, it is misleading to characterize the agreement as purely personal. If the agreement requires them to waive their statutory rights, then no shareholder is capable of exercising those rights and, as a practical matter then, the corporation has eliminated them.

*See* Fisch, Jill E., *Private Ordering and the Role of Shareholder Agreements*, at 28-29 (2020), *available at:* *https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3201&context=faculty_scholarship*.

## ARGUMENT ON CROSS-APPEAL

## I. THE TRIAL COURT CORRECTLY DECIDED THE INTEREST ISSUES

### A. Questions Presented

Whether Petitioners are entitled to interest on the Merger consideration and whether Authentix is entitled to interest on its attorneys' fees award? (Preserved at JA1678-JA1683; JA1891-JA196; and JA2583-JA2588.)

### B. Standard and Scope of Review

This Court reviews questions of law *de novo*, including questions of entitlement to interest. *Chrysler Corp. (Del.) v. Chaplake Holdings, Ltd.*, 822 A.2d 1024, 1031 (Del. 2003).

### C. Merits of Argument

#### 1. Petitioners Are Entitled to Interest on the Merger Consideration Held by the Buyer

The buyer wants an interest-free windfall from its retention of Petitioners' funds since the closing of the Merger. That position is inconsistent with 8 *Del. C.* § 262(h), case law and equity.

Courts have held that stockholders may not be entitled to interest where they fail to properly perfect their appraisal rights, *see Neal v. Alabama By-Prod. Corp.*, 1988 WL 105754, at *5 (Del. Ch. Oct. 11, 1988), but that is not this case. Petitioners complied with the statutory prerequisites of Section 262. Instead, this dispute is

about whether Petitioners agreed in advance to a fixed consideration substituting for "fair value," thereby eliminating the need for a judicial appraisal.

Even assuming the rulings below were correct, the trial court followed *Ford Holdings* and held that stockholders can agree in advance that specified merger consideration constitutes "fair value." (Ex. B at 8-9 ("My finding is informed by Delaware precedent, including the *Ford Holdings* case" in which the preferred stockholders and the corporation "fixed 'fair value' at a set price"); *id.* at 7 (observing that "*Ford Holdings* … upheld a contract that fixed the appraisal price of preferred stock," mooting the need for judicial appraisal). This is an appraisal action filed pursuant to 8 *Del. C.* § 262. The trial court's ruling that the SA falls within *Ford Holdings* did not change the nature of the petition or the proceeding. This is still a dispute about what amount constitutes "fair value." If this Court affirms that the SA fixed the "fair value" for Petitioners, judgment should be entered for payment of that "fair value," with interest pursuant to Section 262(h).

Contrary to Authentix's position (AB at 53), an actual "claim" for the Merger consideration was never necessary because this dispute is over the amount of the consideration, not whether Petitioners are entitled to consideration. In fact, Authentix expressly asked the trial court to "direct Petitioners to … *accept the Merger consideration for Petitioner's shares*…." (JA0154), so a claim for the Merger consideration would not have presented a live controversy. Authentix's

position is the equivalent of arguing that in any appraisal petition, dissenting stockholders must also assert a claim (presumably in the alternative) for the merger consideration to cover for the possibility that their position on "fair value" may be rejected. That makes no sense.

Authentix's entire approach ignores the trial court's adherence to *Ford Holdings*, and Authentix's reliance on *In re Appraisal of Dell, Inc.*, 2016 WL 3077828 (Del. Ch. May 31, 2016) (Order), is unavailing because *Dell* was a failure-to-perfect case (*see id*. ¶ 4 ("The petitioners did not properly perfect their appraisal rights ….")), and this is not. In *Dell*, the petitioners voted in favor of the merger and transferred their shares to a new stockholder of record that had not timely demanded appraisal. (*Id.* ¶ 5.) There were no such procedural missteps here.

Authentix's reliance on Section 3.8 of the Merger Agreement is similarly misplaced. Authentix argues that Petitioners' share certificates must be surrendered with a Letter of Transmittal, but that is a mechanism for confirming that the stockholder both owns the shares and is declining to seek appraisal. Here, Authentix filed a Section 262(f) list that leaves no doubt that Petitioners are stockholders entitled to the Merger consideration (if not a judicial appraisal).

Even if the Court went beyond *Ford Holdings* and held that Section 262 simply does not apply, Petitioners are entitled to pre-judgment interest as a matter of right, *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826 (Del. 1992) ("In

Delaware, prejudgment interest is awarded as a matter of right …. [and] is to be computed from the date payment is due"), or to prevent unjust enrichment. *See Mehta v. Smurfit-Stone Container Corp*, 2014 WL 5438534, at *5 (Del. Ch. Oct. 20, 2014) (holding that where a corporation retains merger consideration of stockholders past the time it is determined to be owed to dissenting stockholders, the elements of an unjust enrichment are satisfied).

There is little authority here, but *Smurfit-Stone* is instructive. There, the Court found that the rights of stockholders who demanded appraisal lapsed 120 days after the close of the merger because no petition was filed. 2014 WL 5438534, at *5 (Del. Ch. Oct. 20, 2014). The Court determined that the remedy was "relatively straightforward: damages equal to the amount of the cash portion plus an award of pre- and post-judgment interest running from … the day after the 120–day filing period ran, until the date of payment." *Id.* at *6. The Court awarded interest running from the date the former stockholders were *entitled to receive* the merger consideration, not the date they began to make efforts to forego appraisal and be paid the merger consideration. *Id.* Here, Petitioners were entitled to merger consideration *as of the Merger*, with interest running from that time.[6]

[6] The buyer's decision not to hold the Merger consideration in an interest-bearing account should not impact the analysis. That was the buyer's decision. Likewise, it was the buyer's decision not to pre-pay the Merger consideration per Section 262(h).

### 2. Authentix is Not Entitled to Pre-Judgment Interest on its Attorneys' Fees Award

Authentix relies on inapposite cases. For example, *Underbrink v. Warrior Energy Servs. Corp.*, 2008 WL 2262316 (Del. Ch. May 30, 2008), is an advancement case. Fees in advancement cases are owed when they are incurred and submitted; not so here. The indemnification context is analogous to the present situation. Losing party obligations, like indemnification payment obligations, do not arise until a decision is rendered on the merits.[7]

Courts that have addressed the point in time at which prejudgment interest begins to accrue on a fee award hold that it is *after* the obligation arises, which is after a decision on the merits that determines who prevailed and after a determination of the amount of fees owed to the prevailing party.

In *Branin v. Stein Roe Inv. Counsel, LLC*, the plaintiff sought prejudgment interest on fees awarded under a contractual indemnification right, "suggest[ing] that interest should run from when he expended funds in the New York Action…." 2015 WL 4710321, at *7 (Del. Ch. July 31, 2015). The Court rejected this position,

[7] Even in the advancement context, "[a] party seeking advancement is [only] entitled to interest from the date on which the party 'specified amount of reimbursement demanded *and* produced his written promise to repay.'" *Underbrink*, 2008 WL 2262316 at *19 (quoting *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826, n.10 (Del. 1992)). Further, for "those expenses subject to advancement, but incurred before the date of Plaintiffs' undertakings, *pre-judgment interest shall run from the date of their respective undertakings*…." *Id.* (emphasis added).

explaining that a request for indemnification "is properly made once the underlying litigation is resolved or when the threshold standard [of entitlement] can be practicably addressed." *Id.* at *8. "Lacking a right to advancement, Branin was responsible for fronting the costs of his defense" and "Defendants breached no obligation to indemnify him while the New York Action was pending because, for instance, determination of his good faith [and entitlement to indemnification] would not have been a reasonable effort until the outcome of (and reasons for the outcome of) the New York Action was known." *Id.*; *see also Citrin v. Int'l Airport Centers LLC*, 922 A.2d 1164, 1167 (Del. Ch. 2006) ("In the contractual setting, pre-judgment interest should…not accrue until the point at which the defendant has, without justification, refused to live up to its obligation to make payment.") (citing *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826 (Del. 1992)).[8]

So too here. Petitioners could not have breached any obligation to pay fees until the merits of the case were decided. In other words, as in *Branin*, no demand could be made, and no obligation to cover fees could accrue, until the trial court ruled on the merits and determined Authentix to be the prevailing party.

[8] *See also O'Brien v. IAC/InterActive Corp.*, 2010 WL 3385798, at *16 (Del. Ch. Aug. 27, 2010), *aff'd sub nom. IAC/InterActive Corp. v. O'Brien*, 26 A.3d 175 (Del. 2011) ("[P]rejudgment interest generally is awarded from the date of a demand for indemnification….").

*Trans World Airlines Inc. v. Summa Corp*., 1987 WL 5778 (Del. Ch. Jan. 21, 1987), *aff'd*, 540 A.2d 403 (Del. 1988), is inapposite. *Trans World* was a post-trial decision awarding damages caused by a breach of fiduciary duty, where the parties disputed the applicable rate of interest but *not* the issue of entitlement to prejudgment interest. Nevertheless, in dicta, the Court correctly observed that "awards of monetary damages by Delaware courts bear interest *from the date of the onset of liability* '*as a matter of right*.'" *Id.*, at *1 (quoting *Metropolitan Mut. Fire Ins. Co. v. Carmen Hldg. Co.*, 220 A.2d 778, 781 (Del. 1966)). Authentix had no right to, and Petitioners had no "liability" for, attorneys' fees until the trial court determined Authentix to be the prevailing party and determined the amount of fees to which it was entitled.

Likewise, *Hercules, Inc. v. AIU Ins. Co.*, 784 A.2d 481 (Del. 2001), does not help Authentix's cause. *Hercules* was an insurance coverage dispute where this Court analogized to an advancement case (*Citadel Hldg. Corp. v. Roven*, 603 A.2d 818, 822 (Del. 1992)), and held that notice of potential liability was not sufficient to trigger accrual of pre-judgment interest. *Id.* at 508 ("no payment was due until Hercules made an unequivocal request for payment.").

Other courts have considered the precise question presented here and have reached the same conclusion. *See, e.g.*, *Shared Commc'ns Servs. of ESR, Inc. v. WHTR Real Estate Ltd. P'ship*, 2017 WL 1372777, at *8 (Pa. Super. Apr. 13, 2017) (holding that "prejudgment interest *cannot* accrue on an award of attorneys' fees and costs pursuant to a contractual fee-shifting provision because the obligation to pay these fees does not arise until the trial court enters a final judgment") (citing *PPG Indus., Inc. v. Zurawin*, 52 F. App'x 570, 581 (3d Cir. 2002)) (emphasis original); *Gleason v. Norwest Mortg., Inc.*, 2008 WL 2945989, at *5 (D.N.J. July 30, 2008) (addressing contractual fee-shifting award and holding that "[b]ecause New Jersey law prohibits interest on attorney's fees absent a specific agreement to such effect, Gleason is not entitled to prejudgment interest for attorneys' fees ….").[9]

Authentix's request for prejudgment interest reaching back to the date of attorney invoices is inappropriate and inconsistent with the relevant case law.

[9] There is no provision for prejudgment interest under Section 13(i) of the SA.

## CONCLUSION

Respectfully, the trial court's interpretation and application of the SA should be reversed and its rulings on interest should be affirmed.

DATED: February 10, 2021

**DLA PIPER LLP (US)**

*/s/ John L. Reed*

John L. Reed (I.D. No. 3023)
Peter H. Kyle (I.D. No. 5918)
Kelly L. Freund (I.D. No. 6280)
1201 North Market Street, Suite 2100
Wilmington, DE 19801
(302) 468-5700
(302) 394-2341 (Fax)
john.reed@dlapiper.com
peter.kyle@dlapiper.com
kelly.freund@dlapiper.com

*Attorneys for Petitioners-Below/ Appellants/Cross-Appellees*

*Manti Holdings, LLC, Malone Mitchell, Winn Interests, Ltd., Equinox I. A Tx, Greg Pipkin, Craig Johnstone, Tri-C Authentix, Ltd., David Moxam, Lal Pearce, and Jim Rittenburg*