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IN THE SUPREME COURT OF THE STATE OF DELAWARE

PATRICK DAUGHERTY, Plaintiff Below/Appellant, v. JAMES DONDERO, HUNTON ANDREWS KURTH LLP, MARC KATZ, MICHAEL HURST, SCOTT ELLINGTON, and ISAAC LEVENTON, Defendants Below/Appellees.	No. 60, 2023 (Appeal from Court of Chancery C.A. No. 2019-0956-MTZ)

OPENING BRIEF OF APPELLANT PATRICK DAUGHERTY

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NATURE OF PROCEEDINGS

This case arises from a decade-long dispute between appellant Patrick Daugherty, a former partner and senior executive of Highland Capital Management L.P. ("Highland"), and appellee James Dondero, Highland's founder and former CEO. At the direction and based on the advice of his attorneys, including appellees Hunton Andrews Kurth LLP ("Andrews Kurth"), Marc Katz, Michael Hurst, Scott Ellington, and Isaac Leventon, Dondero carried out a multi-step scheme to defraud Daugherty of his Highland compensation and a Texas jury award.

In 2012, Highland sued Daugherty in Texas, and Daugherty asserted counterclaims against Highland and third-party claims against Highland's then-affiliate Highland Employee Retention Assets LLC ("HERA"). During those proceedings, defendants created a sham escrow account, they claimed to hold Daugherty's membership interest in HERA until a final verdict was reached. Ultimately, the Texas jury awarded Daugherty $2.6 million plus interest against HERA, and the verdict was affirmed on appeal. In furtherance of their scheme to defraud Daugherty of his HERA interest and jury award, defendants orchestrated several transactions that transferred all of HERA's assets, and Daugherty's HERA interest, to Highland. HERA was left with no assets, and Daugherty was unable to collect his judgment.

In 2017, Daugherty sued Highland, HERA, Highland ERA Management LLC ("HERA Management"), and Dondero in the Court of Chancery, in a case captioned *Daugherty v. Highland Capital Management, L.P.*, C.A. No. 2017-0488-MTZ (the "Delaware Related Action"), regarding the sham escrow and transfer of HERA's assets to Highland. Dondero was dismissed at the pleading stage, but the case proceeded to trial on October 14, 2019, against Highland, HERA, and HERA Management. On the second day of trial, Dondero revealed for the first time that they challenged wrongs were done at the direction and based on the advice of counsel. The next morning, on the third and final day of trial, Highland filed for bankruptcy, automatically staying the Delaware Related Action. The Delaware Related Action remains stayed.

After Dondero implicated his attorneys in the wrongdoing, Daugherty, who was unable to amend his complaint in the Delaware Related Action due to the bankruptcy stay, initiated this action on December 1, 2019, to preserve his claims before they were time barred. In this action, Daugherty seeks to recover against Dondero and the attorney defendants for their acts related to the sham escrow.

Defendants moved to dismiss this action, and the Court of Chancery stayed the action pending resolution of Highland's bankruptcy. Then, in a

May 5, 2022 status conference, the Court of Chancery requested supplemental briefing on, among other things, the claim-splitting doctrine. The parties filed supplemental briefs and the Court of Chancery heard oral argument on October 6, 2022. In a letter decision dated January 27, 2023, the Court of Chancery granted defendants' motions to dismiss based on claim splitting and denied Daugherty's request to consolidate this action and the Delaware Related Action.

SUMMARY OF ARGUMENT

1. The Court of Chancery reversibly erred in granting defendants' motions to dismiss based on the claim-splitting doctrine and declining to consolidate this action and the Delaware Related Action. Consolidation, an appropriate procedure to join split claims, is warranted under Court of Chancery Rule 42 because there are common questions of law and fact in the actions. And, although claims were split, they were not split impermissibly, as the Court of Chancery held. The claims were not split for tactical advantage but because of procedural necessity. Defendants withheld key evidence until trial in the Delaware Related Action, and Daugherty was prevented from amending his complaint in that action before the limited period expired due to the automatic bankruptcy stay imposed during trial. Declining consolidation in these circumstances does not further the claim-splitting doctrine, which is to "prevent exposure to duplic[ative] litigation and/or double recoveries." *J.L. v. Barnes*, 33 A.3d 902, 921 (Del. Super. 2011). Only Dondero was an overlapping defendant, and he was dismissed from the Delaware Related Action at the pleading stage. There is also no risk of double recovery. The Court of Chancery's decision should be reversed.

STATEMENT OF FACTS

I. Daugherty's HERA Interest

Daugherty was a partner and senior executive of Highland from 1998 to 2011. A0608 ¶ 8. Highland was co-founded and used to be controlled by Dondero and Mark Okada, their affiliates, and various trusts for their benefit. A0608 ¶ 9. After performing poorly during the 2008 financial crisis, Highland created HERA to curb employee resignations by offering employees a replacement of their previously received deferred compensation. A0610 ¶¶ 19-20. Daugherty became a member of HERA in 2009, and initially was awarded 1,571.86 Series A Preferred units, making him the largest holder in HERA. A0611 ¶¶ 22-23.

Daugherty resigned from Highland on September 28, 2011, but remained a director of HERA. A0612 ¶ 25. On February 16, 2012, the HERA directors, except Daugherty, removed Daugherty as a director. A0612 ¶ 26. Immediately thereafter, the new board executed a Second Amended and Restated Agreement (the "2012 Amendment"), which included a dispute-resolution provision. A0612-A0613 ¶¶ 26-28. Specifically, Section 12.1 stated that if a member of HERA "commences litigation" or "otherwise initiates any dispute or makes any claim … related to HERA," "then with the consent of 75% of the Board, all pending and future distributions to" that

litigating member "shall be immediately suspended and held in escrow by HERA until the final, non-appealable resolution of the Dispute." A0612-A0613 ¶ 27.

II. Highland Initiates the Texas Litigation

Just seven weeks after the 2012 Amendment, Highland commenced an action against Daugherty, captioned *Highland Capital Management, L.P. v. Daugherty*, 12-04005, District Court of Dallas County, Texas 68th Judicial District (Dallas) (the "Texas Action"). A0605, A0613 ¶¶ 1, 29. Daugherty responded to the Texas Action with counterclaims against Highland for breach of contract and defamation and third-party claims against HERA. A0614 ¶ 30.

A. Defendants Transfer HERA's Assets to Highland

During the Texas Action, Dondero purported to buy the HERA units held by all HERA members except Daugherty. His intent was to isolate Daugherty as a member of HERA. A0614-A0615 ¶¶ 31-32, 34. Then, Dondero moved the management powers of HERA to a new entity, Highland ERA Management, LLC, controlled by Dondero. Through a series of transactions, defendants emptied HERA of all its assets and transferred those assets to Highland. A0616-A0617 ¶¶ 35-36, 38.

Also during the Texas Action, Dondero purported to execute the Third Amended and Restated Agreement of HERA, which stripped virtually all the rights of HERA unit holders (i.e., Daugherty). A0617-A0618 ¶ 39. Dondero also purported to execute an Expense Allocation Agreement on behalf of Highland and HERA, drafted by Leventon, under which 93.4 percent of Highland's legal expenses related to the Texas Action were reallocated to HERA. A0620-A0621 ¶¶ 44-45. Dondero also purported to execute an Assignment Agreement on behalf of Highland and HERA, declaring that Highland held the sole economic interest in HERA and transferring HERA's assets to Highland. A0622 ¶¶ 47-48.

B. Defendants Create a Sham Escrow

In connection with the Texas Action, Dondero and his attorneys formed an escrow for Daugherty's HERA assets (the "Escrow") so that they could represent to the Texas jury, falsely, that the assets had not been stolen. A0622-A0623 ¶ 51. Daugherty's HERA interest, valued at approximately $3.1 million, was put in the Escrow with Abrams & Bayliss LLP ("Abrams & Bayliss") as escrow agent. A0623 ¶ 52. The Escrow Agreement provided that if Daugherty prevailed in the Texas Action, the escrowed assets shall be transferred to HERA. A0623-A0624 ¶ 54. Although some of Daugherty's

assets were placed in the Escrow, defendants never intended to return his assets, even if he won in the Texas Action. A0623-A0625 ¶¶ 52-58.

C. Daugherty Prevails in the Texas Action

The Texas jury found that HERA breached the implied covenant of good faith and fair dealing by adopting certain provisions of the 2012 Amendment, and awarded Daugherty $2.6 million plus interest. A0628 ¶ 66. The Texas Court of Appeals affirmed the verdict, making the judgment collectable as of December 1, 2016. A0632 ¶ 74.

On December 3, 2016, encouraged by Highland, Abrams & Bayliss resigned as escrow agent and the escrow assets were transferred to Highland instead of to HERA. A0633-A0634 ¶¶ 77-78. After Highland seized the Escrow assets, Daugherty was unable to collect the judgment awarded to him in the Texas Action. A0634 ¶ 79. These Escrow-related antics would later result in a rare application of the crime-fraud exception in the Delaware Related Action. *See* A0149-A0249; A0250-A0262.

III. In the Delaware Related Action, Dondero Blames His Attorneys

After defendants deprived Daugherty of his Texas judgment and HERA interest, Daugherty initiated the Delaware Related Action on July 6, 2017. A0604-A0605. Daugherty asserted claims against Highland, Dondero, HERA, and Highland ERA Management concerning, among other things,

the Escrow and his right to indemnification from Highland relating to the Texas Action. A0642-A0651. On July 11, 2018, Dondero was dismissed from the case, leaving Highland, HERA, and HERA Management as the defendants. Ex. A at 5. Trial was scheduled for October 14-16, 2019. A0607 ¶ 7 n.1.

On the second day of trial, Dondero—for the first time—revealed that his misconduct toward Daugherty was done at the direction and based on the advice of his outside and in-house counsel, i.e., the other defendants in this action. A1646 at 1; Ex. A at 15-17. He testified, for example:

> Q. Did Highland have outside counsel advising with respect to the purchase of the units?
>
> A. Yes. I believe the whole situation was the most lawyered thing we've ever done. I mean, there was counsel for each of the board members, there was counsel for Highland, there was counsel for HERA, there was Delaware counsel. Everything was orchestrated, dictated by counsel.
>
> Q. Did Highland have -- did that counsel that Highland used also advise counsel on the documents, the transaction documents, relating to those purchases?
>
> A. Yes. All the functional documents and major moves at various turning points were all at the request -- or decided by counsel.
>
> …
>
> Q. Did you have any communication -- are you familiar with Abrams & Bayliss, with what Abrams & Bayliss is?
>
> A. I know they're a Delaware law firm. But beyond that, no.

Q. Did you ever have any communications with Abrams & Bayliss about them resigning as escrow agent?

A. No. Highland and myself, I know, were purposely kept separate from this whole thing. And it was driven by -- it was driven by counsel.

. . .

Q. My question is a little bit more specific because it relates to the escrow assets and Mr. Daugherty. If you had been told by counsel that Mr. Daugherty was entitled to the escrow assets, you would have given him the escrow assets; right?

A. Yes. We would have done whatever counsel told us. We tried very hard to compartmentalize this mess. We have a business to run. And this is -- a half dozen lawsuits, haranguing everybody in public, it was all intended to disrupt our business as much as possible. So we tried to delegate it and compartmentalize it to the lawyers as much as possible.

. . .

Q. Let's talk about which lawyers you're referring to. So I'll start with the in-house lawyers again. Which in-house lawyers of Highland are you relying on with respect to the transfer of the escrow assets?

A. It would have been the same three internal lawyers working with external counsel.

Q. Mr. Ellington, Mr. Leventon, and Mr. Surgent; is that right?

A. I believe so. I believe they were the ones at that time and place.

Q. Which outside counsel are you relying on?

> A. I don't know if Andrews and Kurth had merged with Piper. I don't know who else was involved besides the Abrams guys. But it would have been, more likely than not, those two counsels with whatever other counsel was representing some of the people who were sued individually.

A0325-A0326; A0329; A0334; A0339-A0341; A0349-A0354; A0365-A0368; A0383. Dondero implicated his attorneys (his co-defendants here) as the originators of the wrongful acts, blaming them for key acts that harmed Daugherty and putting their advice at issue on a broad range of topics covering all the critical acts. A1646 at 1. Simply put, "the whole situation was the most lawyered thing we've ever done" and "[w]e would have done whatever counsel told us." A0325; A0366.

IV. Highland's Bankruptcy

Highland declared bankruptcy the next morning, October 16, 2019, which was supposed to be the final day of trial. A0607 ¶ 7 n.1. As a result, the Delaware Related Action was stayed and remains stayed. *Id.* When Highland's bankruptcy was sprung on Daugherty and the Court, Daugherty's counsel stated:

> I haven't seen the bankruptcy petition. I don't know which entities are affected by the bankruptcy petition. And I know even less about bankruptcy law. So I'm not going to tell you what I think should happen as a matter of bankruptcy law today.

> We're certainly not going to oppose putting this proceeding on ice as a practical matter. The issues we're going to look into are pursuing the at-issue waiver exception that was raised. And given all these developments, I expect you'll see from us, either in the form of a motion to amend the complaint or a new complaint, a coordinated action claim against some of the individuals or parties you've either seen this week or heard from this week who are not subject to bankruptcy protection.
>
> So we would ask that, in any event, as a practical matter, the trial record be left open so we can pursue all those potential alternatives.

A0598-A0599. The trial paused when Dondero had opened new fronts in the litigation and pinned blame on his lawyers as the real culpable actors.

During the bankruptcy proceedings, Dondero's employment was terminated and even more facts were revealed about how Dondero and his enablers defrauded Daugherty. Some of those facts are recited in Highland's pending claims against Dondero, Ellington, and Leventon. A1159-A1557. Ellington and Leventon were terminated for cause in January 2021. A1647 at 2. In 2022, Highland finally acknowledged, "Dondero, through HCMLP, engaged in an asset-stripping campaign designed to render HERA judgment-proof, further exposing HCMLP to liability and unnecessary legal costs." A1194 ¶ 79. Highland's new CEO, James Seery, testified:

> It actually looks like, frankly, the escrow was never really an escrow and it was a -- it was a fraud from the beginning. And that one's a pretty disturbing one.

A1357.

The bankruptcy also revealed discovery misconduct during the Delaware Related Action. For example, the bankruptcy revealed that Highland and its counsel had a secret server that Dondero and his internal counsel routinely used, which was concealed during discovery in the Delaware Related Action. A1648 at 3. Additionally, the bankruptcy court twice found Dondero in contempt for violating a TRO. A1650 at 5. During testimony at the first show cause hearing, it was revealed that Dondero and Ellington destroyed their cell phones that were provided by Highland. A1650 at 5. Yet, in the Delaware Related Action, Leventon testified at his custodian of records deposition that Highland did not "have access to people's phones" and that Highland did not own any cell phones for the custodians. A1650 at 5.

V. Daugherty Files This Action to Preserve Claims

Faced with an automatic stay of the Delaware Related Action and a soon-expiring limitations period, Daugherty filed this nominally new action against defendants, i.e., Dondero and those he implicated as the root bad actors, to preserve his claims. Daugherty initiated this action on December 1, 2019, and filed an Amended Complaint on May 15, 2020. A0604. He asserts claims for fraudulent transfer, conspiracy to commit fraud, breach of

fiduciary duties, and aiding and abetting breach of fiduciary duties. A0642-A0651.[1] Essentially, this action states claims that conform to the evidence presented at trial and arise out of evidence revealed at trial in the Delaware Related Action. *Id.*

Daugherty proposed that this action be consolidated with the Delaware Related Action. A0956. Defendants moved to dismiss this action, (A0707-A0711; A0712-A0716; A0942-A0945), and Dondero, Ellington, and Leventon also moved in the alternative to stay this action. A0712-A0716. The Court of Chancery stayed the action pending resolution of the bankruptcy action. A1015-A1080.

VI. Daugherty and Highland Settle in Bankruptcy

On December 8, 2021, Highland filed in the bankruptcy court a Motion for Entry of an Order Approving Settlement with Patrick Hagaman Daugherty (Claim No. 205) and Authorizing Actions Consistent Therewith (the "Settlement Motion"). A1089-A1135. The settlement included the following terms:

- Daugherty will receive an allowed general unsecured, non-priority Class 8 claim in the amount of $8.25 million;

[1] Daugherty's answering brief in response to the motions to dismiss catalogs the allegations against each defendant. A0958-A0965.

- Daugherty will receive an allowed subordinated general unsecured, non-priority Class 9 claim in the amount of $3.75 million;
- Daugherty will receive a one-time payment of $750,000;
- Daugherty and Highland and certain affiliates (including Thomas Surgent) exchanged releases;
- Ownership of HERA and Highland ERA Management was transferred to Daugherty and related parties; and
- Litigation between Daugherty and Highland was dismissed.

A1082-A1083.

The bankruptcy court approved the settlement on March 8, 2022, over the objection of Ellington. A1419-A1422. Daugherty's potential recovery from the settlement is $12,750,000.[2] The bulk of that recovery relates to unique claims Daugherty had against Highland and not against defendants, such as his claims for contractual indemnification. Roughly one-fourth of Daugherty's $40.7 million bankruptcy claim was based on liability unique to Highland that had nothing to do with defendants. A1423-A1557. In the Delaware Related Action, Daugherty sought damages of $8,573,934.69 apart from his indemnification-related claims against Highland. A0291-A0292 ¶¶ 100-101.

[2] As of the hearing on defendants' motions to dismiss, Daugherty had received $7,850,000 from the settlement. A1834-A1835.

VII. The Court of Chancery's Decision Below

After Daugherty and Highland's settlement was approved and this action and the Delaware Related Action remained stayed, "Daugherty respectfully propose[d] that these actions be consolidated, as this would have been a single action but for the bankruptcy stay, and if they are consolidated, that he have an opportunity to file a consolidated amended complaint." A1298-A1299.

The Court of Chancery requested supplemental briefing on claim splitting. A1558. After supplemental briefing (A1559-A1575; A1576-A1592; A1593-A1641; A1642-A1724; A1725-A1739; A1740-A1754; A1755-A1767), the Court heard oral argument on October 6, 2022 (A1768-A1851) and issued its decision on January 27, 2023. Ex. A.

The Court of Chancery granted defendants' motions to dismiss based on the claim-splitting doctrine and dismissed Daugherty's claims without prejudice. *Id.* at 19. The Court of Chancery declined to apply an exception to the claim-splitting doctrine based on the new evidence that Dondero revealed during the trial of the Delaware Related Action. *Id.* at 16-19. The Court of Chancery also declined to consolidate this action and the Delaware Related Action. *Id.* at 20.

ARGUMENT

I. The Court of Chancery Erred in Dismissing This Action Based on the Claim-Splitting Doctrine

A. Question Presented

Whether the Court of Chancery reversibly erred in dismissing this action based on the claim-splitting doctrine where Daugherty was faced with newly revealed evidence of wrongdoing, a bankruptcy stay, and an expiring limitations period. Preserved at A0981-A0985; A1652-A1655.

B. Scope of Review

This court reviews a trial court's grant of a motion to dismiss de novo. *Account v. Hilton Hotels Corp.*, 780 A.2d 245, 248 (Del. 2001); *Bagwell v. Prince*, 1996 WL 470723, at *2 (Del. 1998).

C. Merits of the Argument

The Court of Chancery reversibly erred by granting defendants' motions to dismiss. The claim-splitting doctrine should not preclude Daugherty from pursuing joint and several liability against defendants. Daugherty could not have asserted the claims in this action against defendants in the Delaware Related Action because defendants improperly withheld evidence implicating them during the Delaware Related Action and, the day after the evidence was revealed, the Delaware Related Action was stayed because of Highland's bankruptcy. Where a plaintiff such as

Daugherty is forced to split claims because defendants withhold evidence and then effect a bankruptcy stay after the evidence is revealed, the law does not punish the plaintiff. The rule against claim splitting does not apply "where the defendant has committed fraud on the plaintiff by concealing evidence 'of a part or phase of claim that the plaintiff failed to include in the earlier action'" or where "the information on which the second action is based was not reasonably discoverable during the pendency of the first action." *Havercombe v. Dep't of Educ. of P.R.*, 250 F.3d 1, 8 n.9 (1st Cir. 2001) (quoting Restatement (Second) of Judgments § 26, cmt. c and citing *Marrapese v. R.I.*, 749 F.2d 934, 944 (1st Cir. 1984)). Moreover, because consolidation is an appropriate procedure to resolve split claims and the standard under Court of Chancery Rule 42 is met here, this action should be consolidated with the Delaware Related Action.

1. Dismissal Does Not Further the Purposes of the Claim-Splitting Doctrine

The claim-splitting doctrine is meant to "prevent exposure to duplic[ative] litigation and/or double recoveries." *J.L. v. Barnes*, 33 A.3d 902, 921 (Del. Super. 2011); *Winner Acceptance Corp. v. Return on Capital Corp.*, 2008 WL 5352063, at *18 (Del. Ch. Dec. 23, 2008) (rule against "[c]laim splitting 'reflects the policy that it is preferable to require a plaintiff to present all of his theories of recovery (and supporting evidence) in a

single action, than to allow him to prosecute overlapping or repetitive actions in different courts or at different times'") (quoting *Balin v. Amerimar Realty Co.*, 1995 WL 170421, at *4 (Del. Ch. Apr. 10, 1995), and discussing *Maldonado v. Flynn*, 417 A.2d 378, 381 (Del. Ch. 1980)); Ex. A at 9-10 ("Two principles drive the claim splitting doctrine: (1) 'that no person should be unnecessarily harassed with a multiplicity of suits'; and (2) a litigant should be prohibited 'from getting 'two bites at the apple.'").

The Court of Chancery stated, "[t]hese simultaneously pending, overlapping cases undoubtedly risk subjecting Defendants to multiple judgments and potentially risk giving Daugherty two chances at prevailing on claims arising from the same series of transactions …." Ex. A at 10. This is incorrect for three reasons. First, Dondero is the only overlapping defendant, and he was dismissed from the Delaware Related Action at the pleading stage. A0038. Second, because there is no overlap between the current defendants in either litigation, there is no risk of duplicative litigation or multiple judgments. And, third, Daugherty is not seeking double recovery against defendants in addition to what he has collected or may collect from Highland. Any recovery Daugherty receives from the bankruptcy settlement that is ruled to be attributable to claims for which the current defendants bear joint and several liability would reduce any damages

against the current defendants. In any event, offsetting damages is not an issue that can be resolved at the pleading stage. *Lebanon County Employees' Ret. Fund v. Collis*, 287 A.3d 1160, 1208 (Del. Ch. 2022)("A court does not typically parse the scope of damages at the pleading stage.").

2. An Exception to Claim Splitting Applies

The rule against claim splitting does not apply "where the defendant has committed fraud on the plaintiff by concealing evidence 'of a part or phase of claim that the plaintiff failed to include in the earlier action'" or where "the information on which the second action is based was not reasonably discoverable during the pendency of the first action." *Havercombe*, 250 F.3d at 8 n.9 (quoting Restatement (Second) of Judgments § 26, cmt. c and citing *Marrapese*, 749 F.2d at 944); *see also Salvati v. Fireman's Fund Ins. Co.*, 368 F. Supp. 3d 85, 92 (D. Mass. 2019); Restatement (Second) of Judgments § 26, cmt. j ("A defendant cannot justly object to being sued on a part or phase of a claim that the plaintiff failed to include in an earlier action because of the defendant's own fraud. … The result is the same when the defendant was not fraudulent, but by an innocent misrepresentation prevented the plaintiff from including the entire claim in the original action.").

The Court of Chancery did not apply this exception. According to the Court of Chancery, "Daugherty has failed to persuade me that the defendants in the [Related] Delaware Action concealed either the attorney defendants' involvement in the underlying events or the principals' intention to rely on advice of counsel to defeat the claims against them." Ex. A at 12. The Court of Chancery also stated, "it appears Daugherty did not pursue documents or testimony under the at-issue exception until his objection to Dondero's trial testimony." *Id.*

But the record shows the opposite. Before Dondero's trial testimony blaming his attorneys for the Escrow-related misdeeds in 2016 (A0325-A0326, A0329, A0334, A0339-A0341, A0349-A0354, A0366-A0368, and A0383), one of Highland's affirmative defenses had been that "Defendants did not act with the necessary knowledge, intent, or scienter, and instead acted in good faith." A0247 ¶ 8. In discovery, Daugherty asked for the full basis of the defense. A0050 ¶ 64. Defendants never disclosed an advice-of-counsel defense or indicated that the challenged acts were directed by counsel. Throughout the litigation, Highland's counsel withheld this evidence that was required to be produced. This is what made Dondero's trial testimony so momentous. It wasn't until trial that Dondero, for the first

time, sold out his lawyers and blamed them for the Escrow-related misconduct.

The Court of Chancery noted that "Daugherty did not move to compel a more expansive [discovery] response." Ex. A at 13. But Daugherty pursued all areas of discovery with vigor and the withholding of evidence cannot be attributed to his negligence in exploring the claims and defenses in the Delaware Related Action. Daugherty even served a document subpoena on Andrews Kurth and sought the deposition of Katz (*id.*), but his motion to compel was denied. A0052. In suggesting that Daugherty should have "renewed" that defeated motion or brought more motions, the Court of Chancery misplaced blame for defendants' discovery deficiencies. Defendants should have been forthcoming with their discovery responses and Daugherty should not be penalized for their discovery tactics, which required the appointment of a special master.[3] A0263.

As for whether an advice-of-counsel defense was fairly raised, even at trial Katz argued that the defendants still had not offered an advice-of-

[3] The Court of Chancery also stated, "in a May 24, 2019 motion to compel, Daugherty expressed concerns with the defendants' April 2019 privilege log, but he did not seek relief on any entry on the basis of the at issue exception." Ex. A at 13. But Daugherty had no basis at that time to pursue an at-issue exception because Dondero did not put the blame on his lawyers until trial.

counsel defense. Dondero responded to the question "You testified that you relied on the advice of counsel for that process?" with a "Yes." A0334. Katz then claimed that the testimony "*absolutely does not put the advice at issue*." A0335 (emphasis added). Katz was wrong on the merits; Dondero's testimony did raise an advice-of-counsel defense and put that advice at issue. But the important point for present purposes is that defendants still deny that they raised an advice-of-counsel defense. It is thus unfair to hold that Daugherty should have filed more discovery motions based on the at-issue exception to ferret out a litigation position that defendants still deny taking.

If this case is dismissed based on claim splitting, it would reward Dondero and his enablers for implicating new culpable actors on the second day of trial, withholding communications with those actors, and then handcuffing Daugherty the next day through the bankruptcy stay. The Court of Chancery was concerned that if the actions were to be consolidated, the doctrine of claim splitting would never bar a second action. Ex. A at 19. But his would not be so where evidence is not concealed and sprung on the plaintiff at trial immediately before a bankruptcy stay is imposed.

3. Consolidation Is the Proper Result

Consolidation is an appropriate procedure to address split claims. *See, e.g.*, *Walton v. Eaton Corp.*, 563 F.2d 66, 71 (3d Cir. 1977) ("The district

court's decision to consolidate Mrs. Walton's two actions was obviously unobjectionable. When a court learns that two possibly duplicative actions are pending on its docket, consolidation may well be the most administratively efficient procedure. If the second complaint proves to contain some new matters, consolidation unlike dismissal of the second complaint without prejudice or staying the second action will avoid two trials on closely related matters."); *Miller v. U.S. Postal Service*, 729 F.2d 1033, 1036 (5th Cir. 1984) (finding that the district court erred in dismissing an action because "[t]he proper solution to the problems created by the existence of two or more cases involving the same parties and issues, simultaneously pending in the same court would be to consolidate them"); *Devlin v. Transp. Commc'n Int'l Union*, 175 F.3d 121, 130 (2d Cir. 1999) (remanding for consideration of consolidation).

Indeed, even *Dondero* proposed consolidation below: "Pursuant to Court of Chancery Rule 42, this Court can consolidate this action and the Delaware Related Action because both actions arise from the same issues of law and fact." A0773.

Court of Chancery Rule 42(a) states:

> When actions involving a common question of law or fact are pending before the Court, it may order a joint hearing or trial of any or all the matters in issue in the actions; it may order all the actions

> consolidated; and it may make such orders concerning proceedings therein as may tend to avoid unnecessary costs or delays.

Ct. Ch. R. 42(a). "The prerequisite for consolidating multiple actions is a finding of common issues of law, common issues of fact, or both." *Mirarchi v. Picard*, 2002 WL 749164, at *1 (Del. Ch. Apr. 22, 2002). "In determining whether to consolidate actions the Court must employ its discretion to weigh the possible saving of time and effort that consolidation would bring against any inconvenience, delay, or expense which it could occasion." *Joseph v. Shell Oil Co.*, 498 A.2d 1117, 1123 (Del. Ch. 1985). Further, "[t]he inquiry is whether justice can be administered between the parties without a multiplicity of suits." *Mirarchi*, 2022 WL 749164, at *1.

In denying Daugherty's consolidation request, the Court of Chancery stated:

> After more than two years of hard-fought litigation involving extensive motion practice, Daugherty is effectively requesting that I permit him to amend his complaint on the third day of trial to add, among other things, five new defendants to the case, based on a legal theory and discovery position he was on notice of during discovery. To allow consolidation here would only make an already procedurally complicated situation even more complicated just as it is approaching its resolution.

Ex. A at 20.

The Court of Chancery improperly applied the standard under Rule 42. There is no question that the actions involve a common nucleus of fact. Ex. A at 6-7. Absent Highland's bankruptcy, the claims in this action would have been presented in a proposed amended complaint in the Delaware Related Action, both to conform to the evidence presented at trial and to incorporate the evidence withheld until trial.[4] Any inconvenience, delay, or expense caused by consolidation would be due to the prior withholding of evidence and the automatic stay caused by Dondero's decision to file for bankruptcy. Contrary to the Court of Chancery's holding, consolidation would uncomplicate and streamline the remaining claims against the remaining parties. The Court of Chancery also erred in observing that this situation "is approaching its resolution." Far from it, the dispute between Daugherty and defendants is unresolved, and will remain so unless he is permitted to pursue his claims in a consolidated action.

[4] Daugherty could not have moved to amend his complaint in the Delaware Related Action without risk of violating the bankruptcy stay. *Creighton v. Fleetwood Enters., Inc.*, 2009 WL 1210881, at *2 (E.D. La. May 4, 2009)(denying motion for leave to file amended complaint against debtor as a violation of the automatic stay); *Sosbee v. Steadfast Ins. Co.*, 702 F.3d 1012, 1025 (5th Cir. 2012)("When a debtor files for bankruptcy under Chapter 11, an automatic stay goes into effect under 11 U.S.C. § 362 and suspends the nonbankruptcy court's authority to continue judicial proceedings then pending against the debtor . . ."); *GATX Aircraft Corp. v. M/V Courtney Leigh*, 768 F.2d 711, 716 (5th Cir. 1985) (same).

CONCLUSION

The Court of Chancery's decision granting defendants' motion to dismiss should be reversed and this action should be remanded and consolidated with the Delaware Related Action.

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