

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

IN RE PINPOINT BEARINGS, INC. : No. 17, 2011  
SHAREHOLDERS LITIGATION :

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EDWARD MILLER, :  
 :  
 Plaintiff Below- :  
 Appellant, :  
 :  
 v. :  
 :  
 MICHAEL SANCHEZ, CLARE MITCHELL, :  
 BRENDAN ELLSWORTH, TIMOTHY :  
 FLETCHER, MARSHA FRANKLIN, :  
 DAPHNE KEYES AND ERIC LAM, : Court Below:  
 : Court of Chancery of the  
 Defendants Below- : State of Delaware in and  
 Appellees, : for New Castle County  
 : Civil Action No. 4958-VCM  
 and :  
 :  
 PINPOINT BEARINGS, INC., :  
 :  
 Nominal Defendant Below- :  
 Appellee. :

**APPELLEE'S ANSWERING BRIEF**

Team P  
Counsel for Appellee:  
Pinpoint Bearings, Inc. Board of  
Directors  
Date Filed: February 11, 2011

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## NATURE OF PROCEEDINGS

This is an interlocutory appeal from an Opinion and Order of the Court of Chancery in and for New Castle County dated January 12, 2011, denying Plaintiff Edward Miller's ("Plaintiff") motion to stay proceedings (the "Delaware Motion to Stay") in favor of an action filed one day earlier in the United States District Court for the Southern District of Texas (the "Federal Action"), and granting Defendants', the Board of Directors (the "Directors" or the "Board") of Pinpoint Bearings, Inc. ("Pinpoint"), motion to enjoin Plaintiff (the "Injunction Motion") from prosecuting any derivative or fiduciary claims in the Federal Action or any other forum.

Plaintiff filed a complaint in the Court of Chancery on December 15, 2010, alleging the Directors breached their fiduciary duty of oversight. Concurrently, Plaintiff filed the Delaware Motion to Stay and an unopposed motion to consolidate his action with an already existing derivative lawsuit, which was granted. The Directors then filed the Injunction Motion based on a Pinpoint bylaw (the "Forum Bylaw") requiring derivative lawsuits and fiduciary claims be brought solely in the Delaware Court of Chancery. The Court of Chancery ruled on January 12, 2011, that the Forum Bylaw was both enforceable under Delaware law and valid on equitable grounds.

Plaintiff applied to the Court of Chancery for certification of an interlocutory appeal, which it granted on January 14, 2011. This Court then accepted Plaintiff's appeal on January 18, 2011.

## SUMMARY OF ARGUMENT

The Court of Chancery properly held Pinpoint's Forum Bylaw valid and enforceable under Delaware law, and therefore correctly granted the Directors' Injunction Motion and correctly denied Plaintiff's Delaware Motion to Stay. Under 8 Del. C. § 109(b), the Forum Bylaw was appropriate subject matter for a bylaw because it relates to the rights of the shareholders as a procedural, process-oriented rule, but does not substantively limit those rights. Furthermore, the Forum Bylaw is also enforceable under traditional standards applied to contractual forum selection clauses. The Forum Bylaw was freely negotiated by shareholders, who also had the ability to amend Pinpoint bylaws. Moreover, this Court's precedent enforcing LLC forum selection clauses also indicates that the Forum Bylaw should be enforced. Finally, *McWane* does not apply because the Forum Bylaw is valid; however, even if it were not valid, this Court should maintain jurisdiction.

Furthermore, the Forum Bylaw was adopted on equitable grounds because the Directors did not breach any fiduciary duty owed to the shareholders by amending the bylaws to include a forum selection provision. Therefore, the business judgment rule is the proper standard of review. Additionally, if the Forum Bylaw is classified a defensive measure, the action taken was made in good faith, upon reasonable investigation, and was proportionate to the general threat of defending derivative and fiduciary lawsuits filed in an improper jurisdiction. Thus, the business judgment rule presumption remains.

## STATEMENT OF FACTS

Pinpoint is a publicly traded corporation with 88 million outstanding shares of stock and over 28,000 shareholders from all 50 states. *In re Pinpoint Bearings, Inc. S'holders Litig.*, Del. Ch. Nos. 4958-VCM, 4952-VCM, 2010, at 4 n.2, McCloskey, C. (Jan. 12, 2011). It is incorporated in Delaware and its corporate headquarters are located in Houston, Texas. *Id.* at 4. On June 10, 2010, Pinpoint adopted the Forum Bylaw, which states that the Delaware Court of Chancery is the exclusive forum for any derivative actions or actions asserting breach of fiduciary duty claims. *Id.* at 2.; see App. at B6.

Approximately three months after the Forum Bylaw was adopted, in September of 2010, Pinpoint was investigated by the Office of Inspector General of the United States ("OIG") in connection with some alleged misconduct by mid-level managers, which had supposedly been going on since 2009. *Id.* at 5-6. To avoid criminal charges and maintain relations with the United States military, a customer who accounts for over 60% of Pinpoint's annual revenues, *id.* at 5, Pinpoint carefully settled with the OIG on November 30, 2010 after a thorough investigation by a special committee and independent counsel. *Id.* at 6. Several derivative lawsuits were subsequently filed. *Id.* at 7-8.

On December 1, 2010, Plaintiff<sup>1</sup> filed a derivative lawsuit against the Directors<sup>2</sup> in the United States District Court for the Southern

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<sup>1</sup> Plaintiff is currently the appellant in this case.

District of Texas, located in Houston. *Id.* at 4. Plaintiff is a resident of Houston and a Pinpoint shareholder. *Id.* at 3-4. In the Federal Action, Plaintiff asserts a claim against the Directors under federal securities law and a derivative claim for breach of their fiduciary duty of oversight under Delaware law. *Id.* at 7.

The next day, on December 2, 2010, three more shareholders filed separate derivative actions in the Delaware Court of Chancery, alleging the same breach of fiduciary duty claim as Plaintiff. *Id.* at 7-8. These three actions were consolidated on December 8, 2010 (the "Original Consolidated Action"). *Id.* at 8. The Directors then filed a motion in the Federal Action for a partial stay in favor of the Original Consolidated Action, relying on the Forum Bylaw. *Id.* The Texas court has yet to rule on the Directors' motion.

Subsequently, on December 15, 2010, Plaintiff filed a new complaint and two motions in the Delaware Court of Chancery, alleging the same fiduciary claim. *Id.* at 8-9. The directors then filed the Injunction Motion. The Court of Chancery denied Plaintiff's Motion to Stay and granted Defendants' Injunction Motion, *id.* at 20, and this Court should affirm.

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<sup>2</sup> There are seven directors of Pinpoint, three of whom are inside directors employed by the corporation in another capacity. The three inside directors are Michael Sanchez (CEO), Clare Mitchell (President), Brendan Ellsworth (CFO). The four outside directors are Timothy Fletcher, Marsha Franklin, Daphne Keyes, and Eric Lam. *In re Pinpoint*, No., 4958-VCM at 5.

## ARGUMENT

### **I. THE COURT OF CHANCERY PROPERLY MAINTAINED JURISDICTION OVER THIS LAWSUIT BECAUSE THE FORUM BYLAW IS LEGALLY VALID AS A MATTER OF DELAWARE LAW.**

#### **A. Question Presented**

Is the Forum Bylaw adopted by the Pinpoint board of directors legally valid and enforceable where a forum selection provision is proper procedural subject matter for a bylaw under 8 Del. C. § 109(b) and where the Forum Bylaw easily satisfies the standards traditionally applied to forum selection clauses?

#### **B. Scope of Review**

The grant or denial of a preliminary injunction is reviewed for abuse of discretion. *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 395 (Del. 1996). However, this Court reviews questions of law, including statutory construction and interpretation, *de novo*. *Bay City, Inc. v. Williams*, 2 A.3d 1060, 1061 (Del. 2010).

#### **C. Merits of Argument**

This Court should affirm the Court of Chancery's Order granting the Directors' Injunction Motion and denying Plaintiff's Delaware Motion to Stay. The Forum Bylaw adopted by the Pinpoint Board is legally valid and enforceable under Delaware law for two main reasons. First, under 8 Del. C. § 109(b), the Forum Bylaw is proper subject matter for a bylaw because it is a process-oriented rule which relates to the rights of the shareholders. See *CA, Inc. v. AFSCME Emp. Pension Plan*, 953 A.2d 227, 235 (Del. 2008). Second, the Forum Bylaw easily satisfies the factors and underlying policies applied to forum

selection clauses. See *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991); *Ingres Corp. v. CA, Inc.*, 8 A.3d 1143 (Del. 2010). As the Court of Chancery properly noted, Plaintiff has the burden to show that the Forum Bylaw is invalid, and he is unable to meet that burden. *In re Pinpoint, No.*, 4958-VCM, at 11. Corporation bylaws are presumed valid, and courts should construe them in a manner consistent with the law. *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985).

**1. The Forum Bylaw Is Legally Valid as a Matter of Delaware Law Because It Is a Procedural Rule Which Properly Relates to the Rights of Pinpoint's Stockholders Under 8 Del. C. § 109(b).**

**a. The Forum Bylaw is a procedural rule.**

The Forum Bylaw is legally valid under Delaware law because it satisfies the requirements of 8 Del. C. § 109(b), which allows bylaws to contain any provision relating to the business of the corporation or the rights of its stockholders, so long as it is not inconsistent with law or the corporate charter. See App. at B3. This section has been interpreted to mean that bylaws are procedural rules used to define the process by which substantive business decisions are made. *AFSCME*, 953 A.2d at 234-35. Moreover, they "set down rules and procedures that bind a corporation's board and its shareholders." *Id.* at 234 (emphasis added). Furthermore, 8 Del. C. § 109(a) states that stockholders have the ability to adopt, amend, and repeal bylaws and allows a corporate charter to confer these same powers upon a board. See App. at B3. Boards have broad authority to manage corporate business and affairs under 8 Del. C. § 141. See *Quickturn Design Sys., Inc. v. Shapiro*, 721 A.2d 1281, 1291-92 (Del. 1998); App. at B4.

Here, it is undisputed that Pinpoint's charter expressly confers the power to amend bylaws to the Board. *In re Pinpoint*, No., 4958-VCM, at 12. This authority is also reflected in Article 14 of Pinpoint's bylaws. See App. at B7. By adopting the Forum Bylaw, the Board was merely streamlining the process through which lawsuits would take place. Because lawsuits are to be expected, this is an essential part of managing a public corporation's business and affairs.

Many permissible bylaws also set forth processes which govern shareholder rights. See *AFSCME*, 953 A.2d at 235. For example, bylaws may impose restrictions on the transfer of shares, designate the place for stockholder meetings, and set the manner for setting the time of stockholder meetings. See Brett H. McDonnell, *Sticky Defaults and Altering Rules in Corporate Law*, 60 SMU L. Rev. 383, 437 (2007) (listing which provisions may be included in corporate bylaws). Furthermore, matters relating to lawsuits, such as indemnification policies, are permissible in bylaws. See 8 Del. C. § 145(f); App. at B5. Accordingly, it follows that a forum selection provision, which would govern certain procedures a shareholder must follow during a lawsuit, is fully appropriate for corporate bylaws.

**b. The Forum Bylaw is valid because it relates to the rights of the shareholders without limiting those rights.**

While the Forum Bylaw properly "relates" to the procedural rights of shareholders under § 109(b), it is not in any sense a substantive limitation on shareholder rights. See 8 Del C. § 102(b)(1) (allowing limitations on stockholder rights in the charter); App. at B2. Under

the internal affairs doctrine, a principle recognizing that the state of incorporation should govern a corporation's internal affairs, Delaware law already applies to out of state derivative lawsuits. See *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982). Because Delaware law applies regardless, it is no limitation to mandate that Delaware courts apply their own law. See Joseph Grundfest, *Choice of Forum Provisions in Intra-Corporate Litigation: Mandatory and Elective Approaches (The 2010 Pileggi Lecture)* (Rock Center for Corporate Governance at Stanford University, Working Paper No. 91, 2010), at 19, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1690561](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1690561). And as the court below correctly noted, all remedies remain fully available in Delaware courts. *In re Pinpoint*, No., 4958-VCM, at 12; see also *In re The Topps Co. S'holders Litig.*, 924 A.2d 951, 962 n.39 (Del. Ch. 2007) (listing a "sampling of cases" granting relief). Even if one were to surmise that a forum selection bylaw limits rights because remedies vary depending on the law, this rationale is not applicable in the context of a corporate derivative suit, as in this case. On the contrary, it is in fact an advantage to shareholders when states apply their own laws. See *VantagePoint Venture Partners v. Examen, Inc.*, 871 A.2d 1108, 1112-13 (Del. 2005).

Finally, Delaware case law indicates that forum selection bylaws are well within a board's authority. See, e.g., *In re Revlon, Inc. S'holders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010); *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 296 (Del. 1999). Most notably,

recently in *In re Revlon Shareholders Litigation*, the Court of Chancery stated that "corporations are free to [adopt] charter provisions selecting an exclusive forum." 990 A.2d at 960. Though this statement could be construed as limiting forum selection provisions to corporate charters, the court made an explicit reference to a corporation with a forum selection bylaw and expressed no concerns. See *id.* at 960 n.8. It further acknowledged that "issues implicated by an exclusive forum selection provision must await resolution." *Id.* Certainly, by no means did the court explore all the possibilities for a forum selection provision, nor did it state that such a provision *could not* be adopted into the bylaws. Therefore, it is clear that under Delaware law, a forum selection provision properly belongs in corporation bylaws, and it should be upheld by this Court.

**2. The Forum Bylaw Is Legally Valid and Enforceable as a Matter of Delaware Law Because It Clearly Satisfies the Standards Applied to Forum Selection Clauses and the Policies Expressed by the United States Supreme Court and this Court's Precedent.**

From a contractual perspective, the Forum Bylaw is legally valid as a matter of both Delaware law and federal law. The United States Supreme Court has adopted a policy by which forum selection clauses are "prima facie valid." *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 10 (1972). Delaware courts also employ this presumption. See *Ingres*, 8 A.3d at 1145. Corporations are created by the State, which grants powers and defines the rights acquired by purchasing shares. *VantagePoint*, 871 A.2d at 1112 (citing *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 91 (1987)). As creatures of the State, corporations

are governed by corporate law; however, contract law is still implicated because "charters and by-laws are contracts among the shareholders of a corporation." *Centaur Partners, IV v. Nat'l Intergroup, Inc.*, 582 A.2d 923, 928 (Del. 1990). Therefore, the Forum Bylaw can be appropriately analyzed under standards generally applied to contractual forum selection clauses. See *Carnival Cruise Lines*, 499 U.S. at 593-97; *Zapata*, 407 U.S. at 10-19.

**a. The Forum Bylaw is enforceable under *Carnival Cruise Lines* and *Zapata* standards.**

The Forum Bylaw is enforceable because as a freely negotiated agreement "unaffected by fraud, undue influence, or overweening bargaining power," it should be given full effect. *Zapata*, 407 U.S. at 12-13. *M/S Bremen v. Zapata Off-Shore Co.* addressed a forum selection clause designating England as the forum of choice. *Id.* at 12. The United States Supreme Court enforced the clause, emphasizing that it was specifically bargained for by sophisticated parties, and English courts were more than capable of resolving the dispute. *Id.*

Building upon this presumption of enforceability, in *Carnival Cruise Lines, Inc. v. Shute*, the United States Supreme Court held that a forum selection clause in a form contract was enforceable against an injured ship passenger. 499 U.S. at 595. Applying *Zapata* factors, the Court found that the clause was not unreasonable. *Id.* at 593-94. The passenger had conceded notice, there was no fraud or overreaching because the ship was headquartered in the chosen forum, which "belied" a "bad-faith motive," and there was also no evidence of fraud in obtaining consent. *Id.* at 595. The Court rejected the argument that

the clause should not be enforced because it was not the subject of bargaining, listing three policy reasons as to why it should be valid: (1) the cruise line had a "special interest in limiting the fora" where it could be subject to suit, (2) establishing a forum ex ante would dispel confusion, saving time and expense, and (3) money saved would benefit passengers through reduced fares. *Id.* at 593-95.

*Carnival Cruise Lines* sets a high bar for showing that a forum selection clause is unenforceable. See Sara Lewis, Note, *Transforming the "Anywhere but Chancery" Problem into the "Nowhere but Chancery" Solution*, 14 Stanford J.L. Bus. & Fin. 199, 211 (2008). In assessing whether the Forum Bylaw here is unreasonable, we must therefore look to whether there was fraud or overreaching, whether the forum selected is gravely inconvenient, whether it was freely negotiated, and whether there are strong policy concerns against it. See *id.*, *supra*, at 209-17. Here, there was clearly no fraud or overreaching by the Board. Just as in *Carnival Cruise Lines*, there is no "bad-faith motive" in attempting to limit potential lawsuits to the state of incorporation. See 499 U.S. at 595. By deciding to incorporate in Delaware, corporations have already chosen Delaware law to govern their affairs and lawsuits by way of the internal affairs doctrine. See *Topps*, 924 A.2d at 958. Furthermore, if England was not considered gravely inconvenient in *Zapata*, then Delaware, the corporation's "residence", is far from meeting that standard. See Lewis, *supra*, at 215-16 (noting it is never inconvenient to litigate in one's state of residence).

Moreover, even with the Directors' ability to unilaterally amend the bylaws, the Forum Bylaw was absolutely freely negotiated. First, shareholders bought with notice of the Board's ability to amend bylaws in the corporate charter. See *In re Pinpoint*, No., 4958-VCM, at 12. Therefore, they clearly had no vested interest in the right to bring a lawsuit elsewhere, because "where a corporation's by-laws put all on notice that [they] may be amended at any time, no vested rights can arise." *Kidsco Inc. v. Dinsmore*, 674 A.2d 483, 492 (Del. Ch. 1995). Furthermore, the SEC's EDGAR website mandates relevant provisions be listed, and this constitutes public notice under federal securities law. See *Grundfest*, *supra*, at 20. But perhaps most crucially, shareholders at all times maintained absolute control over the decision because they, too, have the power to unilaterally amend the bylaws. See *In re Pinpoint*, No., 4958-VCM, at 14 n.31; App. at B7.

Finally, policy concerns weigh in favor of enforcement. The only factor in Plaintiff's favor is that the federal claims would remain in Texas. See *In re Pinpoint*, No., 4958-VCM, at 9. This concern is insignificant because these claims would not also be heard in Delaware, thereby avoiding duplicative litigation. Nor would it be inconvenient to Plaintiff, because he is acting in a representative capacity and will have little personal involvement in the cases. See *Topps*, 924 A.2d at 961. Conversely, there are policy concerns similar to those in *Carnival Cruise Lines* which fall heavily in favor of enforcement. *Pinpoint* has a special interest in limiting the fora because, as a corporation with shareholders in every state, it could

be subjected to lawsuits anywhere. See *In re Pinpoint*, No., 4958-VCM, at 4 n.6. In addition, establishing a forum ex ante saves parties time and expense, and savings can be reflected in stock prices, which makes the Forum Bylaw within the shareholders' interests. See Lewis, *supra*, at 210.

**b. The *Galaviz v. Berg* decision was wrongly decided.**

As the Court of Chancery briefly noted, in *Galaviz v. Berg* the United States District Court for the Northern District of California denied the defendant corporation's motions to dismiss derivative suits on the basis of a forum selection provision in its bylaws. *Galaviz v. Berg*, Nos. C 10-3392 RS, C 10-42332011, 2011 WL 135215, at \*2 (N.D. Cal. Jan. 3, 2011). The *Galaviz* court held that under the principles of contract law, a forum selection bylaw would not be enforceable where one party was purportedly able to unilaterally amend the contract. *Id.* at \*4. The court declined to decide whether the bylaw was enforceable under Delaware corporate law, claiming it was a matter of federal common law. *Id.*

Simply put, the *Galaviz* court got the analysis wrong. As a primary matter, the decision was based upon federal common law and not Delaware law, which should have been applied pursuant to the internal affairs doctrine. See *Rogers v. Guaranty Trust Co.*, 288 U.S. 123, 130 (1933) (noting the doctrine applies to both state and federal courts). Furthermore, if the court's reasoning were followed, all corporate bylaws would be ineffective from a contractual perspective. However, it is long settled that the contract rights of shareholders are

"subject to alteration under the amendatory provisions of the General Law." *Hartford Accident & Indem. Co. v. W.S. Dickey Clay Mfg. Co.*, 24 A.2d 315, 426 (Del. 1942). Perhaps, purely as a matter of contract law, a unilaterally amended contract will not suffice. However, corporate law clearly allows for unilateral amendments to bylaws. See *id.*; App. at B3. The Pinpoint shareholders already knew Delaware law would apply and were aware that both they and the Board could amend the bylaws at any time--"their contractual expectations deserve respect." *Topps*, 924 A.2d at 958.

**c. The Forum Bylaw is enforceable according to this Court's jurisprudence and Delaware case law.**

The Forum Bylaw is enforceable under Delaware precedent and is in line with policies routinely advocated by this Court. In *Elf Atochem v. Jaffari*, this Court emphasized giving maximum effect to freedom of contract and enforceability of agreements. *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999). Parties formed an LLC and entered into a separate agreement, which set forth details for the LLC's governance and also contained an arbitration and forum selection clause. *Id.* at 287-88. The LLC itself was not a signatory to the agreement. *Id.* This Court enforced the clause, noting that parties are free to contract around default rules of law. *Id.* at 295. Lower courts have since followed suit by enforcing similar provisions. See *Douzinis v. Am. Bureau of Shipping, Inc.*, 888 A.2d 1146.

After *Elf Atochem*, it's clear that this Court is willing to enforce forum selection provisions located in corporate governance

documents. See 727 A.2d at 296. As the lower court here aptly noted, LLC agreements are similar to corporate bylaws because neither is filed with the State when forming an entity, yet each has contractual force in defining governance expectations. *In re Pinpoint*, No., 4958-VCM, at 11 n.21. In addition, the agreement in *Elf Atochem* was not signed by the LLC itself, yet it still bound the company. See 727 A.2d at 288. It can be analogized to this case, where shareholder approval is not required to amend bylaws, yet they are still contractually bound. See *Hartford Accident*, 24 A.2d at 426. Furthermore, while there is a strong public policy in favor of arbitration, it relinquishes certain fundamental rights, such as the right to have a jury trial. See *Elf Atochem*, 727 A.2d at 295. Conversely, *no rights* are given up or limited by forum selection bylaws--merely the option to file a lawsuit in an alternate forum, which would apply *the same law*. If this Court is willing to enforce an LLC's agreement which limits fundamental rights based on the parties' contractual expectations, then it should be willing to enforce the Forum Bylaw under the same rationale.

**d. *McWane* does not apply when there is an enforceable forum selection clause, nor would it apply in this case, even absent the controlling Forum Bylaw.**

In *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Engineering Co.*, this Court held that courts should exercise discretion in favor of a stay where a prior action, involving the same parties and issues, is pending in another court capable of doing prompt and complete justice. 263 A.2d 281, 283 (Del. 1970). However, subsequent cases

have limited *McWane*, noting that it usually applies when an individual plaintiff sues in a convenient forum, and the defendant files a responsive suit in an alternate forum. *Topps*, 924 A.2d at 956. But in a representative lawsuit, "*McWane* has far less bite." *Id.* Furthermore, where there is a legally enforceable forum selection clause, it should be honored and *McWane* does not apply. *Ingres*, 8 A.3d at 1145.

*McWane* is combated by the fact that "a state has a compelling interest in ensuring the consistent interpretation and enforcement of its corporation law." *Topps*, 924 A.2d at 958. In *In re Topps Shareholders Litigation*, a merger was announced and the next day a lawsuit was filed in New York; one day after that, several more were filed in Delaware, the state of incorporation. *Id.* at 954-55. Noting that it had treated complaints as simultaneously filed when there were "trivial time differences," *id.* at 957, the Court of Chancery maintained jurisdiction over the case, denying the motion to stay. *Id.* at 964. It set forth abundant policy reasons for the decision: New York had no legitimate interest in adjudicating the case, the plaintiff was a representative and had no legitimate interest in obtaining a ruling from a non-Delaware court, random results are bad for investors, Delaware courts are more efficient, and most importantly, Delaware should speak first on new issues of law to provide certainty. *Id.* at 960-64. The court gave little weight to the fact that there might be a simultaneous lawsuit, stating that it was "sympathetic," but it would not stay the case. *Id.* at 953.

Here, because the Forum Bylaw is enforceable, *McWane* will not apply. See *Ingres*, 8 A.3d at 1145. However, even absent the Forum Bylaw, this Court should maintain jurisdiction. *Topps* indicates that even if this Court were to hold the Forum Bylaw invalid, it would still be in Delaware's best interest to keep the lawsuit in its own courts. See 924 A.2d at 961-64. Just as in *Topps*, the lawsuits here were filed only one day apart, which are "trivial time differences"--a view that this Court has agreed with. *Id.* at 957; see also *King v. Verifone Holdings, Inc.*, No. 330, 2011 WL 284966, at \*8 (Del. Supr. Jan. 28, 2011). In addition, given that the failure to monitor claim addresses issues of Delaware law this Court needs to resolve, it has a compelling interest in maintaining jurisdiction. See Andrew D. Appleby & Matthew D. Montaigne, *Three's Company: Stone v. Ritter and the Improper Characterization of Good Faith in the Fiduciary Duty "Triad,"* 62 Ark. L. Rev. 431, 431 (2009). Finally, the *Topps* opinion notes that even if a plaintiff were from the state of the first-filed action, as in this case, as a representative plaintiff, he would have "no cognizable interest" in having another state adjudicate a claim under Delaware law. *Id.* at 961. In light of *Topps*, the ultimate policies behind enforcing the Forum Bylaw and maintaining jurisdiction are abundantly clear, and this Court should affirm.

**II. THE COURT OF CHANCERY PROPERLY RULED THAT THE FORUM BYLAW WAS ADOPTED ON EQUITABLE GROUNDS BECAUSE THE DEFENDANT DIRECTORS DID NOT BREACH THEIR FIDUCIARY DUTY.**

**A. Question Presented**

Did the Directors breach any fiduciary duty owed to their shareholders by amending Pinpoints bylaws to include a forum selection provision where the proper jurisdiction for filing derivative and fiduciary lawsuits was named?

**B. Scope of Review**

Questions of law are reviewed *de novo*. *Nixon v. Blackwell*, 626 A.2d 1366, 1375 (Del. 1993).

**C. Merits of Argument**

This Court should affirm the Court of Chancery's ruling declaring the Forum Bylaw valid upon equitable grounds because the Directors did not breach any fiduciary duty, and instead enacted the Forum Bylaw in the best interest of Pinpoint. Furthermore, if the action taken is classified as a defensive measure, it was adopted upon good faith investigation and was proportionate to the threat of defending derivative or fiduciary lawsuits filed in an improper jurisdiction.

**1. The Directors' Decision to Adopt the Forum Bylaw is Subject to Review Under the Business Judgment Rule.**

The decision made by the Directors to adopt the Forum Bylaw was in the best interest of Pinpoint and thus is subject to review under the business judgment rule. The purpose of the business judgment rule is to promote and protect the free exercise of managerial power afforded to directors under 8 Del. C. § 141(a). *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985); see App. at B4. While exercising their power,

the business judgment rule is a presumption "that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interest of the company." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

The Directors' reason for adopting the Forum Bylaw was to ensure that all derivative and fiduciary litigation be confined to Delaware courts for the purpose of convenience, efficiency, and relative predictability in the application of the incorporating state's laws. See *In re Pinpoint*, No., 4958-VCM, at 17 n.39. Thus, the Directors' motivation was to reduce the associated costs of defending derivative and fiduciary lawsuits, while at the same time ensuring proper application of Delaware law, both of which are in the best interest of Pinpoint. Furthermore, because the Directors received advice from legal counsel before acting, it is clear they made the decision in good faith and on an informed basis. *Id.* at 18 n.44.

By enacting the Forum Bylaw, the Directors formally adopted the internal affairs doctrine as an official measure of their corporate policy, and thus made a further effort to reduce the cost of defending derivative and fiduciary lawsuits. The internal affairs doctrine provides that "a court - state or federal - sitting in one state will as a general rule, decline to interfere with . . . [a] corporation organized under the laws of another state but will leave controversies as to such matters to the courts of the state of the domicile." *Topps*, 924 A.2d at 959 (citing *Rogers v. Guaranty Trust Co.*, 288 U.S.

123, 130 (1933)). Judge Learned Hand stated "when a trial involve[s] the internal affairs of a corporation, the rule is that the courts of a foreign forum will not assume jurisdiction over it." *Id.* (citing *Weiss v. Routh*, 149 F.2d 193, 195 (2d Cir. 1945)). This is true because the state of incorporation has a particular interest in seeing its laws applied correctly, *id.* at 958, especially in Delaware where over 50% of publicly traded companies are incorporated. *About Agency*, Delaware Division of Corporations (Feb. 1, 2011, 8:21 AM), <http://www.corp.delaware.gov/aboutagency.shtml>. In adopting the Forum Bylaw, the Directors made a valid business judgment to ensure all fiduciary and derivative litigation be brought before the Delaware Court of Chancery. This decision was made to head off defending lawsuits filed in an improper jurisdiction in order to minimize unnecessary litigation expenses. Therefore, the Directors' decision was again made in good faith and in the best interests of Pinpoint.

**2. The Entire Fairness Standard Does Not Apply Because the Directors Did Not Breach Any Fiduciary Duty Owed to the Shareholders.**

The entire fairness test does not apply because Plaintiff likely did not meet the evidentiary burden to rebut the business judgment rule presumption. In order for the entire fairness standard to arise, the initial burden lies with the plaintiff to allege sufficient facts that will call into question the directors' action as breaching one of their fiduciary duties--duty of loyalty, good faith, or due care. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993). However, 8 Del. C. § 102(b)(7) provides exculpation for duty of care

claims; therefore, the entire fairness standard is generally applied only to breach of loyalty claims based on self-interested transactions. *Emerald Partners v. Berlin*, 787 A.2d 85, 92-93 (Del. 2001). Traditionally, a self-interested transaction arises when a director is found standing on both sides of the transaction or when a director receives a benefit to the exclusion of the shareholders. *Cede*, 634 A.2d at 362. If the plaintiff has provided adequate evidence to rebut the business judgment rule, the burden then shifts to the directors to prove the "entire fairness" of their action. *Id.* at 361.

Plaintiff has asserted that the Directors acted self-interestedly by unilaterally adopting the Forum Bylaw because in doing so they have usurped control over all shareholder litigation. *In re Pinpoint*, No., 4958-VCM, at 16. In light of the internal affairs doctrine, the Forum Bylaw was adopted to minimize the cost of defending derivative and fiduciary lawsuits brought in an improper jurisdiction. This is a benefit received by *all* stakeholders of Pinpoint. Therefore, when there is no indication of self-interested behavior, merely stating the Directors breached their duty of loyalty will not serve to rebut the business judgment rule.

Furthermore, even if there were facts to invoke the entire fairness standard, the Directors' action would still prove to be entirely fair to the shareholders. The entire fairness standard is concerned with procedural and substantive rights of a corporation's shareholders:

The concept of fairness has two basic aspects: fair dealing and fair price. The former embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained. The latter aspect of fairness relates to the economic and financial considerations of the proposed [action], including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock . . . All aspects of the issue must be examined as a whole since the question is one of entire fairness.

*Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1162-63 (Del. 1995). The challenged action in the present case involves only an analysis of fair dealing.

The procedural process by which the Directors adopted the Forum Bylaw was well within the powers afforded to them under Pinpoint's bylaws, and thus was not an abuse of discretion or a matter of broad overreaching. See App. at B7. This is especially true considering that the shareholders still retain the power to amend the bylaws and repeal the forum selection provision. See *id.* In addition, the bylaws are also an appropriate corporate document for including a forum selection provision, since a corporation's bylaws refer strictly to procedural matters, as noted earlier. See App. at B3. Therefore, the Directors did not overreach or abuse their discretion.

Moreover, the timing in which the Forum Bylaw was adopted further strengthens the process of fair dealing. The Directors enacted the Forum Bylaw on June 10, 2010, about three months before the fraudulent actions were reported, and about four and a half months before the lawsuit was filed. *In re Pinpoint*, No., 4958-VCM, at 5-7. Although the activity was purportedly going on since early 2009, there is no

evidence the Directors knew of its occurrence. Consequently, despite concerns expressed by the California court in *Galaviz v. Berg*, there is no indication the Directors had fraudulent motives for adopting the Forum Bylaw; it was clearly enacted in the best interest of Pinpoint. See 2011 WL 135215, at \*2.

In addition to being procedurally fair, the Forum Bylaw is also substantively fair because the Directors have not usurped any shareholder power. If the directors act to entrench themselves in office, such a motive will over ride the business judgment rule and will subject their behavior to heightened scrutiny. See *Kidsco*, 674 A.2d at 493-94; *Frantz*, 501 A.2d at 408. The shareholders still have the ability to bring fiduciary and derivative lawsuits against Pinpoint and its Directors, thus no power has been taken away. However, they now are simply required to file such claims in the Delaware Court of Chancery. See App. at B6. As noted, this is an added benefit to the shareholders since the internal affairs doctrine requires derivative and fiduciary lawsuits be litigated within the incorporating state's jurisdiction. See *Topps*, 924 A.2d at 953. Therefore, the Forum Bylaw does not prevent shareholders from bringing claims with merit; rather, it saves them money by preventing claims from being filed in an improper forum. See *Lewis*, *supra*, at 210.

**3. If Enhanced Judicial Scrutiny Under *Unocal* were to Apply, the Directors' Decision to Adopt the Forum Bylaw was Reasonable and Proportionate to the Threat Posed, and Therefore is Subject to the Business Judgment Rule.**

The Directors' decision to adopt the Forum Bylaw was made in good faith, upon reasonable investigation, and was proportionate to the general threat of defending derivative litigation filed in an improper jurisdiction. For a defensive action to fall within the ambit of the business judgment rule, the initial burden lies on the directors to show by good faith investigation that they had reasonable grounds for believing a threat to corporate policy existed. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985). However, there is no requirement that a defensive measure be adopted in response to an imminent threat; general threats also qualify. See *Moran v. Household Intern., Inc.*, 490 A.2d 1059 (Del. 1985). Once the defensive measure has been adopted, in order to fully pass the enhanced scrutiny of *Unocal Corp. v. Mesa Petroleum Co.*, the action taken must be proportionate to the threat posed. 493 A.2d at 955. Moreover, proof of good faith investigation is substantially enhanced when the action taken was approved by a majority of outside directors. *Id.*; *Aronson*, 473 A.2d at 812.

The Directors adopted the Forum Bylaw in good faith and with reasonable investigation by first consulting legal counsel regarding the matter. See *In re Pinpoint*, No., 4958-VCM, at 18 n.44. Additionally, the decision was made by a majority of disinterested directors, given that the board was comprised of four outside directors and three officers of Pinpoint. See *id.* at 5. Therefore, proof of good faith and reasonable investigation has been materially enhanced.

Furthermore, the Forum Bylaw was proportionate to the threat posed. The purpose of the Forum Bylaw is to ensure that fiduciary and derivative claims will be heard in a Delaware court. See *id* at 2 n.4; App. at B6. As previously noted, the Delaware Court of Chancery is the appropriate jurisdiction for derivative and fiduciary claims of a Delaware corporation, given that the internal affairs doctrine already applies. Therefore, the Directors did not adopt an overly broad measure, but instead made the governing default rule a part of their corporate policy.

Because the action taken was clearly made in good faith, by reasonable investigation, and was proportionate to the threat posed, Plaintiff must now provide sufficient evidence to rebut the business judgment rule. *Unocal*, 493 A.2d at 955. For the reasons stated above, Plaintiff is unable to show that the Directors breached any one of their fiduciary duties in adopting the Forum Bylaw, and therefore, the presumption of the business judgment rule remains intact.

#### **CONCLUSION**

The Forum Bylaw is valid under Delaware law because it is a procedural rule which properly belongs in corporate bylaws and it satisfies the standards for contractual forum selection clauses. Furthermore, under the business judgment rule, the Directors did not breach any fiduciary duties in adopting the Forum Bylaw, and it is therefore enforceable on equitable grounds. Accordingly, this Court should affirm the Court of Chancery's Order granting Defendants' Injunction Motion and denying Plaintiff's Delaware Motion to Stay.



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**8 Del C. § 102. Contents of certificate of incorporation.**

(b) In addition to the matters required to be set forth in the certificate of incorporation by subsection (a) of this section, the certificate of incorporation may also contain any or all of the following matters:

(1) Any provision for the management of the business and for the conduct of the affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the stockholders, or any class of the stockholders, or the governing body, members, or any class or group of members of a nonstock corporation; if such provisions are not contrary to the laws of this State. Any provision which is required or permitted by any section of this chapter to be stated in the bylaws may instead be stated in the certificate of incorporation;

(7) A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under § 174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit. No such provision shall eliminate or limit the liability of a director for any act or omission occurring prior to the date when such provision becomes effective. All references in this paragraph to a director shall also be deemed to refer to such other person or persons, if any, who, pursuant to a provision of the certificate of incorporation in accordance with § 141(a) of this title, exercise or perform any of the powers or duties otherwise conferred or imposed upon the board of directors by this title.

**8 Del C. § 109. Bylaws.**

(a) The original or other bylaws of a corporation may be adopted, amended or repealed by the incorporators, by the initial directors of a corporation other than a nonstock corporation or initial members of the governing body of a nonstock corporation if they were named in the certificate of incorporation, or, before a corporation other than a nonstock corporation has received any payment for any of its stock, by its board of directors. After a corporation other than a nonstock corporation has received any payment for any of its stock, the power to adopt, amend or repeal bylaws shall be in the stockholders entitled to vote. In the case of a nonstock corporation, the power to adopt, amend or repeal bylaws shall be in its members entitled to vote. Notwithstanding the foregoing, any corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws upon the directors or, in the case of a nonstock corporation, upon its governing body. The fact that such power has been so conferred upon the directors or governing body, as the case may be, shall not divest the stockholders or members of the power, nor limit their power to adopt, amend or repeal bylaws.

(b) The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees.

**8 Del C. § 141. Board of directors; powers; number, qualifications, terms and quorum; committees; classes of directors; nonstock corporations; reliance upon books; action without meeting; removal.**

(a) The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation. If any such provision is made in the certificate of incorporation, the powers and duties conferred or imposed upon the board of directors by this chapter shall be exercised or performed to such extent and by such person or persons as shall be provided in the certificate of incorporation.

**8 Del C. § 145. Indemnification of officers, directors, employees and agents; insurance.**

(f) The indemnification and advancement of expenses provided by, or granted pursuant to, the other subsections of this section shall not be deemed exclusive of any other rights to which those seeking indemnification or advancement of expenses may be entitled under any bylaw, agreement, vote of stockholders or disinterested directors or otherwise, both as to action in such person's official capacity and as to action in another capacity while holding such office. A right to indemnification or to advancement of expenses arising under a provision of the certificate of incorporation or a bylaw shall not be eliminated or impaired by an amendment to such provision after the occurrence of the act or omission that is the subject of the civil, criminal, administrative or investigative action, suit or proceeding for which indemnification or advancement of expenses is sought, unless the provision in effect at the time of such act or omission explicitly authorizes such elimination or impairment after such action or omission has occurred.

**Article 12. Forum.** The Court of Chancery of the State of Delaware shall be the sole and exclusive forum for (i) any derivative action or proceeding brought on behalf of the corporation, (ii) any action asserting a claim of breach of a fiduciary duty owed by any director, officer or other employee of the corporation to the corporation or the corporation's stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law or the corporation's certificate of incorporation or bylaws, or (iv) any other action asserting a claim governed by the internal affairs doctrine.

**Article 14. Amendments.** These bylaws may be made, altered, amended or repealed by vote of a majority of the directors in office or by vote of a majority of the stock outstanding and entitled to vote. Any bylaw, whether made, altered, amended or repealed by the stockholders or directors, may be altered, amended or reinstated, as the case may be, by either the stockholders or by the directors as hereinbefore provided.