#### IN THE

## Supreme Court of the State of Delaware

BTRTA FOREST PRODUCTS, INC., a Delaware corporation, MATTHEW SUNSTEIN, VIKRAM SARABHAI, MICHAEL F. ALLEN, MILES D. LIU, KATHLEEN L. TODMAN, HERBERT McCUSKER, PAULA ABAZIAN, JANICE L. STERN, WILLIAM D. HEMPHILL, RAVERT WARD L.P., and BTR ACQUISITION CORP.,

Defendants Below, Appellants,

v.

CONSOLIDATED FOREST INDUSTRIES CO., a Delaware corporation,

Plaintiff Below, Appellee.

No. 142, 2012

Court Below:
Court Of Chancery of the State
of Delaware
C.A. No. 6943-CJ
"CD-ROM Version To Be Filed"

APPELLEE'S REPLY BRIEF

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CONSOLIDATED FOREST INDUSTRIES

Dated: February 9, 2012

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### NATURE OF PROCEEDINGS

This interlocutory appeal arises out of Defendant BTRta Forest Products, Inc.'s ("BTRta") termination of a merger agreement with Plaintiff Consolidated Forest Industries Co. ("CFI") in favor of a less financially beneficial merger with Defendant Ravert Ward L.P. Plaintiff commenced this litigation on December 16, 2011. The Chancery Court of Delaware held that BTRta violated its duties of care and loyalty contrary to Revlon and Section 102(b)(7) of the Delaware General Corporation Law; particularly, it held that BTRta cannot use Article II of its certificate of incorporation to circumvent its duties. Moreover, it held that the deal-protection devices employed by the BTRta board in the Ravert Ward agreement would likely be impermissible under Omnicare. Thus, the Chancery Court of Delaware granted Plaintiff's motion for a preliminary injunction on January 31, 2011, preventing the consummation of the BTRta-Ravert Ward merger. Defendants filed this interlocutory appeal on February 2, 2012, and this Court granted certification on February 10, 2012.

<sup>&</sup>lt;sup>1</sup> CFI met its burden for a preliminary injunction by demonstrating: "(1) a reasonable probability of success on the merits at a final hearing; (2) an imminent threat of irreparable injury; and (3) a balancing of the equities [that] tips in its favor." Mem. Op. 13; Zrii, LLC v. Wellness Acquisition Group, Inc., 2009 Del. Ch. LEXIS 167, \*24 n. 93 (Del. Ch. Sept. 21, 2009), citing Argyle Solutions, Inc. v. Prof'l Sys. Corp., 2009 Del. Ch. LEXIS 63, 2009 WL 1204351, at \*2 (Del. Ch. May 4, 2009) (citing Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1341 (Del. 1987)).

#### SUMMARY OF ARGUMENT

- 1. Delaware law protects shareholders from unreasonable decisions made by corporate directors, such as the ones made by the directors in this case, by requiring enhanced scrutiny pursuant to <a href="Revlon">Revlon</a> and <a href="Unocal">Unocal</a> rather than blindly deferring to directors' judgment. Under <a href="Revlon">Revlon</a>, the BTRta board had a duty to act in good faith and obtain maximum shareholder value in any change of control transaction. Instead, the directors attempted to redefine their duties under Article II of BTRta's certificate of incorporation and circumvent the CFI agreement in favor of the Ravert Ward agreement at a \$1.50 per share loss based solely upon the unsubstantiated conclusion that CFI would not uphold its assurances. These actions violated the directors' duty of loyalty and duty of care because they made their decision in an uninformed manner, based on the improper influence of Article II, and failed to obtain maximum value for stockholders.
- 2. The BTRta board's choice to terminate the CFI agreement in favor of the Ravert Ward agreement does not withstand judicial scrutiny under <u>Unocal</u> or <u>Omnicare</u> because they employed draconian deal-protection devices which locked up the Ravert Ward merger. The directors did not reasonably perceive an actual danger to corporate policy in the CFI merger agreement to justify their use of deal-protection devices in the Ravert Ward agreement because they received several assurances from CFI to uphold their corporate policies and then executed a merger agreement with CFI.

In fact, the devices they enacted were coercive because the directors agreed to vote their 50.4% of outstanding equity in favor of the Ravert Ward merger, making the stockholders' decision a foregone conclusion, regardless of whether the merger remained in the best interest of the corporation. Moreover, the devices were preclusive because the stockholders could not vote on any superior proposal, including that of CFI, and it was mathematically impossible for any other proposal to succeed based upon the directors' voting power. Further, the concerns expressed by the dissent in Omnicare are inapplicable here because the directors locked up the Ravert Ward transaction despite a superior offer and without looming financial pressures.

### STATEMENT OF FACTS<sup>2</sup>

Plaintiff CFI is a Delaware corporation based in Boise, Idaho that produces paper and wood products throughout the world. Mem. Op. 3. In September 2011, CFI expressed interest to enter into a merger agreement to acquire Defendant's Maine-based company, BTRta. Mem. Op. 4, 8. Two of the BTRta directors, Sunstein and Sarabhai, were initially hesitant to accept CFI's offer of \$16.50 per share, but during a meeting with CFI on October 7, 2011, they were assured their environmental goals would be fulfilled. Mem. Op. 8-9. Through their service as consultants to the Environmental Committee of CFI's board of directors, Sunstein and Sarabhai would be involved in any significant changes to CFI's environmental practices pertinent to the operations acquired from BTRta. Id. In addition to these good-faith assurances, CFI increased its offer to \$17 per share. Id.

Accordingly, CFI and BTRta executed a merger agreement on October 17, 2011. Id. Under the CFI agreement, BTRta was required to present the agreement to its stockholders for a vote, but it could terminate the agreement in favor of a superior proposal within a 60-day period after the board approved the CFI agreement. Mem. Op. 10. A superior proposal is one which the BTRta board deemed in good faith would better serve the best interests of the company as defined by Article II of BTRta's certificate of incorporation. Id. Specifically, Article II purported to permit a director to circumvent his fiduciary duties provided that he "consider the long-term prospects and interests of the Company and its stockholders, and the social, economic, legal, or

The facts are uncontested. Mem. Op. 3, n. 4.

other effects of any action . . . [including the effect upon] the environment and the economy of those communities and the larger world." Mem. Op. 6. However, if BTRta terminated the agreement, CFI would receive a termination fee valued at 3.2% of the total transaction, or \$15 million. Mem. Op. 10.

Despite CFI's generous offer and good-faith assurances that it would continue to enforce BTRta's company goals, Sunstein and Sarabhai sought out other offers through their financial advisor, Eberhard Jefferson LP ("Eberhard"). Mem. Op. 9-10. Eberhard arranged for Sunstein and Sarabhai to meet with an acquisitions firm, Ravert Ward, in late October 2011. Mem. Op. 10. Ravert Ward initially offered a mere \$13 per share and insisted it could not offer more. Mem. Op. 11. As the 60-day grace period was nearing a close, Eberhard reached out to Ravert Ward again in late November 2011. Id. Following several meetings in early December, BTRta and Ravert Ward negotiated terms whereby Ravert Ward agreed to offer \$15.50 per share and, like CFI, agreed to manage the operation in accordance with Sunstein and Sarabhai's environmental goals. Id.

The terms for BTRta, however, were much more restrictive in the Ravert Ward agreement than in the CFI agreement. Mem. Op. 11-12. Under the Ravert Ward agreement, Sunstein and Sarabhai would be required to vote all of their shares of Class B stock in favor of the merger, which essentially finalized the sale because Sunstein and Sarabhai, along with their family members, hold 50.4% of the company's stockholder voting power. Mem. Op. 5-6, 12. Further, BTRta's board would need to present the agreement for a vote to the stockholders by

April 1, 2012, even if the board no longer desired the Ravert Ward merger, BTRta could not solicit any further merger proposals, and in the event of termination, BTRta would be required to pay \$15 million. Mem. Op. 12.

After hastily concluding that CFI would not uphold its environmental assurances, the BTRta board determined it would declare the Ravert Ward agreement a "superior proposal" to the CFI agreement and accept Ravert Ward's agreement on December 13, 2011. Id. Although the board scheduled a stockholder vote on the Ravert Ward merger for March 23, 2012, Sunstein and Sarabhai's requisite voting agreements with Ravert Ward already determined the fate of the vote. Mem. Op. 13. Thus, after BTRta informed CFI of BTRta's plans to terminate the CFI contract, CFI's counsel contacted BTRta's counsel on December 14, 2011 to inform BTRta that CFI would seek injunctive relief based upon BTRta's breach of its fiduciary duties. Id. On December 16, 2011, CFI commenced this action and moved for a preliminary injunction against the Ravert Ward merger. Id.

#### ARGUMENT

I. THE BTRTA BOARD OF DIRECTORS CANNOT CONTRACT AROUND ITS FIDUCIARY DUTIES TO MINORITY STOCKHOLDERS, AND FAILURE TO EXERCISE THOSE DUTIES IN CONCERT WITH REVLON WAS A BREACH OF THE BOARD'S DUTIES OF LOYALTY AND DUE CARE.

#### A. Question Presented

Whether the BTRta board of directors breached its fiduciary duties of loyalty and due care when it approved the Ravert Ward merger at a price significantly below CFI's offer despite the board's duty under Revlon to seek the highest value available for all stockholders.

#### B. Scope of Review

This Court generally reviews the grant or denial of a preliminary injunction for abuse of discretion on factual issues. <u>Kaiser Aluminum</u>

<u>Corp. v. Matheson</u>, 681 A.2d 392, 394 (Del. 1996). This Court will not, however, defer to the trial court's embedded legal conclusions. Id.

#### C. Merits of the Argument

As stockholder representatives, directors have "unremitting" fiduciary duties to protect the corporation and its stockholders.

Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 938 (Del. 2003).

Ordinarily, in corporate transactions implicating fiduciary duties, courts give deference to the decisions of directors, under the business judgment rule. Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34, 42 (Del. 1994). However, directors cannot abdicate their duty to protect the interests of all stockholders. Id. Rather, in concert with the need to protect minority stockholders, enhanced scrutiny under Revlon and Unocal are threshold inquiries that apply

before the business judgment rule. <u>Id.</u> at 45. Under enhanced scrutiny, the reviewing court must consider the "adequacy of the [directors'] decision making process" and carefully examine "the reasonableness of the directors' action in light of the circumstances then existing." Id.

Revlon sought to prevent conflicts of interest in mergers by "demanding that directors act with scrupulous concern for fairness to shareholders." Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1286 (Del. 1989) (emphasis added). Thus, Revlon stands for one overriding objective: protecting the interests of stockholders from director misconduct. Paramount v. QVC, 637 A.2d at 42-43. Directors are subject to Revlon standards when a corporation "embarks on a transaction-on its own initiative or in response to an unsolicited offer-that will result in a change of control." Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 242 (Del. 2009). After change of control becomes inevitable, the directors' role changes "from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company." Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986). Thus, once Revlon applies, a board can no longer protect the interests of various constituencies at the expense of stockholders. Id.

The Court of Chancery correctly found that the BTRta board cannot contract around its fiduciary duties under Revlon and breached its duties of loyalty and due care by failing to obtain the highest share price available. The board's approval of an all-equity sale of BTRta automatically triggered enhanced Revlon duties because the sale

constituted a change of control transaction as defined by BTRta's certificate of incorporation. Once Revlon duties applied, the BTRta board's powers were limited to one specific duty: obtain maximum stockholder value. The board cannot contract around this duty, and when the board failed to secure the highest possible price, it breached the duties of loyalty and due care.

 The BTRta board cannot contract around its duty of loyalty, and advancing the interests promoted by Article II at the expense of the minority stockholders is a violation of the directors' duty of loyalty under Revlon.

A certificate of incorporation "shall not eliminate or limit the liability of a director . . . [f]or any breach of the director's duty of loyalty to the corporation or its stockholders . . . ." 8 Del. C. § 102(b)(7) (emphasis added). Further, Section 102(b)(7) precludes limitation of liability for directors' failure to act in good faith, a subset of duty of loyalty. Id.; Stone ex rel. AmSouth Bancorporation v. Ritter, 911 A.2d 362, 369 (Del. 2006). Thus, directors cannot contractually alter their duty of loyalty because that would necessarily limit their liability and contradict Section 102(b)(7).

A corporation breaches its duty of loyalty when it fails to act in good faith. Lyondell, 970 A.2d at 239-40. Although there are no "legally prescribed steps" directors must follow, specific actions implicate bad faith. Id. at 243. For instance, directors act in bad faith by putting their conflicting self-interests ahead of the interests of minority stockholders. Strassburger v. Earley, 752 A.2d 557, 581 (Del. Ch. 2000). In Strassburger, the Court of Chancery held two directors liable for subordinating the interests of minority

stockholders to those of one majority stockholder in a stock repurchase plan. <u>Id.</u> Thus, directors cannot favor majority stockholders at the expense of minority stockholders. <u>Id.</u>

Additionally, when a fiduciary acts in conscious disregard of a "known duty to act," he violates his duty of loyalty. Stone, 911 A.2d at 369 (quoting In re Walt Disney Co. Derivative Litig., 906 A.2d 27, 67 (Del. 2006)). Under Revlon, directors' have one duty: maximizing share value. Revlon, 506 A.2d at 182. Subject to this duty, directors must not allow "improper influence" to inhibit their evaluation of whether a transaction satisfies stockholders' interests. McMullin v. Beran, 765 A.2d 910, 923 (Del. 2000). Rather, the board has an "uncompromising duty of loyalty" to act on behalf of all stockholders in maximizing share value. Id. (quoting Weinberger v. UOP, Inc., 457 A.2d 701, 710 (Del. 1983)) (internal quotation marks omitted).

Section 102(b)(7) statutorily prohibits the BTRta board from shirking its duty of loyalty to stockholders. Specifically, under 102(b)(7), Article II cannot eliminate the directors' liability for breaches of the duty of loyalty. While 102(b)(1) of the Delaware General Corporation Law allows directors to include a provision in the certificate of incorporation defining the power of directors, it does not permit directors to contract around their fiduciary duties. 8 Del. C. § 102(b)(1). Thus, the BTRta board was subject to duty of loyalty considerations throughout negotiations with CFI and Ravert Ward.

In conscious disregard of its obligations to minority stockholders, the BTRta board instead promoted the specific interests of Sunstein and Sarabhai and thus breached its duty of loyalty.

Similar to <u>Strassburger</u>, where directors acted in bad faith by subordinating the interests of minority stockholders to those of a single majority stockholder, here, the BTRta board acted in bad faith by approving the Ravert Ward merger at the minority stockholders' expense. Despite a premium CFI offer and several assurances that CFI would honor BTRta's environmental commitments, Sunstein and Sarabhai sought a buyer that more closely suited their specific environmental interests. Mem. Op. 11. Under Sunstein and Sarabhai's influence, the board terminated the financially superior CFI merger and hastily approved the Ravert Ward merger at a price per share well below CFI's offer. Thus, the BTRta board consciously disregarded its <u>Revlon</u> duty to maximize share value at the expense of the minority stockholders.

Furthermore, Article II was an "improper influence" on the board's decision to contract with Ravert Ward because the board used Article II to override its duty of loyalty. Once Revlon duties applied, as they did here, the board's sole responsibility was to maximize share value. Contrary to Revlon, the BTRta board terminated the financially superior CFI agreement and approved the Ravert Ward merger based on Article II and perceived differences in CFI and Ravert Ward's corporate social responsibility. Mem. Op. 12. However, once Revlon applied to the transaction, Article II should have had no bearing on the board's decision. Rather, consistent with this Court's declaration in McMullin, the board had a duty to maximize value on behalf of all stockholders. Thus, the board breached its duty of loyalty to the BTRta stockholders when it relied on Article II to approve the Ravert Ward merger at a loss of \$1.50 per share.

 Throughout the CFI and Ravert Ward agreements, the BTRta board remained subject to a duty of care under <u>Revlon</u>, and it breached that duty by failing to secure the highest share price available.

Section 102(b)(7) does not eliminate directors' duty of care to minority stockholders. Arnold v. Society for Sav. Bancorp, Inc., 678 A.2d 533, 542 (Del. 1996). Rather, 102(b)(7) leaves the directors' overarching duty of care intact by affording stockholders equitable relief in the event of a breach. 8 Del. C. § 102(b)(7); Arnold, 678 A.2d at 542. Further, contractual provisions, "whether or not they are presumptively valid in the abstract, cannot define or limit the fiduciary duties of directors charged with protecting stockholder interests." Paramount v. QVC, 637 A.2d at 48. Paramount involved a contract provision that precluded negotiation with competing suitors in a merger transaction. Id. The defendants argued these provisions prevented them from shopping for a superior offer, eliminating their duty to seek the best available stock price. Id. However, the Court determined that the directors' decision to sell control triggered Revlon duties regardless of a contractual provision limiting competition. Id.

In an active auction, directors must allow market forces to "operate freely," to ensure all stockholders receive the most value per share. Revlon, 506 A.2d at 184. Further, where bidders make substantially similar offers, directors cannot satisfy their fiduciary duties by "playing favorites with the contending factions." Id. At a minimum, the directors must act with fairness to all stockholders in scrutinizing transactions under Revlon. Mills Acquisition Co. v. MacMillan, Inc., 559 A.2d 1261, 1285 (Del. 1989). Thus, in

transactions subject to  $\underline{\text{Revlon}}$  review, fairness to all stockholders is paramount. Id.

When scrutinizing transactions, a board's failure to inform itself demonstrates a lack of due care and subjects the board's actions to enhanced judicial scrutiny. McMullin, 765 A.2d at 922. The duty of care requires directors to act in an "informed and deliberate manner" before submitting a merger proposition to stockholders. Id. at 920. For example, in McMullin, faced with time constraints, the board met only once and accepted a proposition promulgated by the majority shareholder. Id. Further, because the transaction in McMullin was a "final-stage transaction," the directors faced an enhanced duty to protect minority stockholders. Id. at 917. These facts were sufficient to state a claim against the directors for failure to determine the proper value of the target corporation. Id. at 922.

The BTRta board cannot use Article II to elude their duty of care to minority stockholders. Section 102(b)(7) does not permit an outright circumvention of the board's duty of care. Rather, consistent with this Court's holding in Arnold, CFI is entitled to seek equitable relief for the board's failure to satisfy its duty of care.

Furthermore, consistent with this Court's reasoning in Paramount, the board cannot contract around its fundamental duties. The CFI agreement gave the board sixty days to seek a "superior proposal" as defined in Article II. Mem. Op. 10. However, under Paramount, BTRta could only incorporate Article II into the CFI agreement to the extent it is consistent with a board's fiduciary duties to stockholders. Therefore,

despite the provision in Article II, the board remained subject to its duty of care as defined in Revlon.

Additionally, the board failed to act in an informed and deliberate manner because it approved the Ravert Ward merger without considering the substantially similar social policies offered in the CFI agreement. Contrary to Revlon, where this Court stipulated that directors cannot play favorites with potential suitors, here, the board chose the Ravert Ward agreement despite assurances from CFI that it would provide similar protection for BTRta's environmental goals. In fact, CFI offered Sunstein and Sarabhai consulting roles in all significant decisions involving environmental practices relating to the BTRta operations, precisely the roles they would assume under the Ravert Ward agreement. Mem. Op. 9, 11.

Furthermore, similar to <a href="McMullin">McMullin</a>, where the board breached its duty of care by rushing into an agreement, here, faced with the expiration of CFI's 60-day allowance to seek a superior proposal, the board approved the Ravert Ward agreement after one meeting. Despite its <a href="Revlon">Revlon</a> duties, the board approved this agreement for \$1.50 less per share than the CFI agreement. Ultimately, rather than scrutinizing the Ravert Ward agreement, the board hastily approved an inferior final-stage transaction on a baseless assumption that CFI would not meet BTRta's environmental goals. Thus, the board violated its fiduciary duties by failing to consider the impact the Ravert Ward merger would have on BTRta's minority stockholders.

II. BTRTA'S BOARD OF DIRECTORS VIOLATED ITS FIDUCIARY DUTIES TO THE STOCKHOLDERS WHEN IT EMPLOYED DRACONIAN DEAL-PROTECTION MEASURES TO LOCK UP THE RAVERT WARD MERGER AGREEMENT EVEN THOUGH THE BOARD HAD ALREADY APPROVED THE FINANCIALLY SUPERIOR CFI OFFER.

#### A. Question Presented

Whether the Ravert Ward Merger Agreement is unenforceable because the BTRta board of directors, contrary to its fiduciary duties to the stockholders, used draconian deal-protection devices to make the merger transaction a fait accompli.

#### B. Scope of Review

This Court generally reviews the grant or denial of a preliminary injunction for abuse of discretion on factual issues.

<u>Kaiser</u>, 681 A.2d at 394. This Court will not, however, defer to the trial court's embedded legal conclusions. Id.

#### C. Merits of the Argument

Merger transactions are a "shared enterprise and ownership decision." Omnicare, 818 A.2d at 930. Delaware corporation law expressly creates a balance of power between the board of directors and the stockholders to enforce that premise. Id.

Accordingly, while the board has authority to approve an initial merger agreement, it must submit the agreement to a stockholder vote before the transaction can become final. 8 Del. C. § 251(c). Thus, when a board adopts deal-protection devices to effectively "lock up" a merger agreement, the board may oppress the

stockholders' rights to vote contrary to the board's recommendation.

Omnicare, 818 A.2d at 930.

The deal-protection devices in the Ravert Ward Merger Agreement are unenforceable because they are repugnant to the directors' fiduciary duties to the stockholders. Specifically, the BTRta board failed to yield to its supervening fiduciary duties when it approved draconian deal-protection devices to lock up the merger, effectively robbing the stockholders of their right to a meaningful vote.

# 1. The "lock-up" provisions in the Ravert Merger Agreement must withstand enhanced scrutiny under Unocal.

Deal-protection devices that lock up a merger transaction create a conflict of interest between the board's interest in protecting the merger agreement it has approved, the stockholders' statutory right to make the final decision on the merger, and the board's duty to perform its fiduciary duties. Omnicare, 818 A.2d at 930. The "omnipresent specter" of that conflict requires a threshold determination that the deal-protection devices in the merger agreement do not exceed the board's statutory authority and are consistent with directors' fiduciary duties. Id. at 930-31 (quoting Unocal Corp. v. Mesa

Petroleum Co., 493 A.2d 946, 954 (Del. 1985)). Therefore, when a board adopts deal-protection devices to protect a merger it has approved, those devices "must withstand enhanced judicial scrutiny under the Unocal standard of review" to determine whether they are repugnant to the directors' continuing fiduciary duties. Id. (citing Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140, 1151-55 (Del. 1989)).

The Ravert Ward Merger Agreement must withstand enhanced judicial scrutiny under <u>Unocal</u> because the BTRta board adopted deal-protection devices to effectively lock up the transaction. First, the board agreed to present the Ravert merger to a stockholder vote, regardless of whether the board continues to view the merger as the best option for BTRta and its stockholders. Mem. Op. 12. Second, the board guaranteed that BTRta would not solicit superior offers prior to a stockholder vote on the merger. <u>Id.</u> Finally, directors Sunstein and Sarabhai pledged to vote all of their Class B shares, which represent 50.4% of stockholder voting power when combined with their family members, in favor of the merger. Mem. Op. 5-6, 12.

Essentially, the board adopted deal-protection devices to ensure that the Ravert merger was a foregone conclusion and to relegate the stockholders' § 251(c) rights to mere formality. Therefore, under <a href="Omnicare">Omnicare</a>, enhanced judicial scrutiny is proper to determine whether the directors locked up the Ravert Merger Agreement contrary to their ongoing fiduciary duties to the stockholders.

2. The deal-protection devices in the Ravert Ward Merger agreement are unenforceable because they are draconian "lock-up" provisions that make the transaction a fait accompli contrary to the board's fiduciary duties.

Deal-protection devices are a valid means to protect a merger agreement only if the board proves it reasonably believed that "a danger to corporate policy and effectiveness existed" and the devices are "reasonable in relation to the threat posed." Omnicare, 818 A.2d at 935 (quoting Unocal, 493 A.2d at 955). This two-pronged approach, the Unocal test, is prudent for two reasons. First, it allows the

board "latitude in discharging its fiduciary duties. . . ." <u>Id.</u> at 931 (quoting <u>Unitrin</u>, <u>Inc. v. Am. Gen. Corp.</u>, 651 A.2d 1361, 1388 (Del. 1995)). Second, the board does not have absolute statutory power to approve a merger agreement and thus does not have "unbridled discretion" to protect a merger with "any draconian means available." <u>Id.</u> at 932. Therefore, when a board uses deal-protection devices to lock up a merger agreement in response to a threat to the corporation's interests, this Court will only defer to the board's judgment if the devices are not draconian and are reasonable in relation to the threat posed. Id. at 931.

## a. Allowing the BTRta stockholders to vote on the CFI merger posed no reasonable threat to BTRta.

The <u>Unocal</u> test requires the board prove it adopted the deal-protection devices because it reasonably perceived a danger to the corporation's interests. <u>Omnicare</u>, 818 A.2d at 935. Further, the board must show it adopted the devices to protect the merger out of a good-faith concern for the corporation and stockholders' welfare. <u>Unocal</u>, 493 A.2d at 955. In <u>Unocal</u>, the Unocal board adopted deal-protection devices in response to a hostile tender offer from Mesa Petroleum to protect stockholders because the board deemed the Mesa offer price too low. <u>Id</u>. at 958. Similarly, in <u>Omnicare</u>, the board of NCS, an insolvent corporation, adopted deal-protection devices because it feared that it would lose a valuable offer from Genesis with no comparable alternative. <u>Omnicare</u>, 818 A.2d at 918, 935. The NCS board's primary concern was that Genesis would withdraw its offer rather than face a potential bidding war with Omnicare. Id. at 924.

<u>Unocal</u> and <u>Omnicare</u> illustrate a key point in merger transactions: a board adopts deal-protection devices in a merger agreement to give that agreement an advantage, or disadvantage, over any other potential transactions that materialize before the stockholders vote. <u>Id.</u> at 932. Logically then, a board must demonstrate that it reasonably perceived a specific danger to the corporation's interests before it can employ deal-protection devices in a merger agreement. Id. at 935.

The BTRta board's conclusion that the risk of losing the Ravert Ward transaction was a threat to BTRta was not reasonable. The board erroneously relies on Article II of BTRta's certificate of incorporation, which permits directors to consider broader societal interests in their decision making, to justify their sweeping action. Specifically, after the board approved the CFI merger agreement, directors Sunstein and Sarabhai had "misgivings" about whether they could continue to promote "larger societal interests" if under CFI's control. Mem. Op. 10. While the concern for larger societal interests is consistent with Article II, the board cannot avoid the fact that it voted for the CFI merger after Sunstein and Sarabhai met with CFI's representatives who allayed the directors' concerns. Mem. Op. 9. Presumably, the board would never have approved the CFI merger if it posed any legitimate threat to BTRta's corporate policies.

### b. The deal-protection devices in the Ravert Ward Merger Agreement are unenforceable because they are draconian.

Deal-protection devices in a merger agreement are unenforceable unless they are "reasonable in relation to the threat posed."

Omnicare, 818 A.2d at 935 (quoting Unocal, 493 A.2d at 955). Each

device must withstand <u>Unocal</u> scrutiny, and when a board's dealprotection devices are "inextricably related", the board's actions
must survive scrutiny "collectively as a unitary response" to the
threat. <u>Id.</u> at 932 (quoting <u>Unitrin</u>, 651 A.2d at 1387). Moreover,
deal-protection devices need not be part of the merger agreement
itself to be subject to <u>Unocal</u> analysis. <u>Id.</u> at 934. In <u>Omnicare</u>, two
NCS directors holding a majority of the voting power pledged their
votes in favor of the Genesis merger. <u>Id.</u> This Court ruled that the
separate voting agreements acted in concert with the merger
agreement's mandatory stockholder vote provision as a structural
defense for the merger. <u>Id.</u> Thus, the Genesis merger was a foregone
conclusion at the expense of any subsequent superior transaction. Id.

Although directors need not make perfect business decisions to survive enhanced scrutiny, a board does not have "unbridled discretion" to protect a merger with "any draconian means available."

Id. at 931-32. This Court has consistently held that coercive or preclusive deal-protection devices fall within the common law definition of draconian. Id. at 932 (citing Unitrin, 651 A.2d at 1387). Accordingly, when a board adopts deal-protection devices that are coercive or preclusive in a merger agreement, those devices are per se unreasonable. Id. at 935.

Coercive deal-protection devices are measures a board employs to force a management-sponsored alternative upon the stockholders. Id. (citing <u>Unitrin</u>, 651 A.2d 1387). Further, coercive measures include those where the board or another party effectively forces the stockholders to vote on a merger for a reason other than its merits.

Id. at 935 (citing Williams v. Geier, 671 A.2d 1368, 1382-83 (Del. 1996)). In Omnicare, the mandatory stockholder vote provision, the noshop provision, and the voting agreements predetermined the Genesis merger's outcome without regard for its merits at the time of the stockholder vote. Id. at 936. Considering the Genesis merger agreement lacked a fiduciary out clause, this Court held that the structural deal-protection devices were impermissibly coercive because they robbed the stockholder vote of its effectiveness. Id. at 935-36.

Whether a board coercively robs stockholders of an effective vote depends on the particular facts of the case. Brazen v. Bell Atl.

Corp., 695 A.2d 43, 50 (Del. 1997) (citing Williams, 671 A.2d at 1383). In Brazen, this Court held that a mere termination fee provision in a merger agreement was not, on its own, coercive. Id. In stark contrast, in Omnicare, the NCS board adopted multiple deal-protection devices that were collectively coercive. Omnicare, 818 A.2d at 936. Accordingly, the Omnicare Court ruled that the NCS directors failed to "yield to the supervening responsibility . . . to discharge their fiduciary duties on a continuing basis." Id. at 939.

Preclusive deal-protection devices are draconian measures that deprive stockholders of the right to receive all offers or preclude other bidders from making a superior offer. Id. at 935 (citing Unitrin, 651 A.2d 1387). In Omnicare, the NCS board precluded stockholders from approving Omnicare's superior offer by adopting deal-protection devices that predetermined the outcome of the Genesis merger. Id. at 936. Although the board did not obligate the minority stockholders to vote in favor of the transaction, the board used

draconian, preclusive deal-protection devices to make the Genesis merger a "fait accompli", rendering minority stockholder votes meaningless. Id. In fact, after locking up the Genesis merger, the NCS board later withdrew its support for the merger and officially recommended the stockholders vote against the Genesis transaction. Id. Unfortunately for stockholders, the NCS board had already made it "mathematically impossible . . . for the Omnicare transaction or any other proposal to succeed, no matter how superior the proposal." Id. (emphasis added) (internal quotation marks omitted).

Notwithstanding the lack of any threat to the corporation, the deal-protection devices that the BTRta board adopted to lock up the Ravert Ward transaction are draconian and thus unenforceable. Specifically, the board conceded to Ravert Ward's demand for three "inextricably related" deal-protection measures that ensure the transaction is a fait accompli. First, the board prohibited itself from soliciting any alternative to the Ravert Ward merger. Mem. Op. 12. Second, the board quaranteed that it would submit the merger to a stockholder vote, regardless of whether the board still considered the merger to be in the corporation's best interests. Id. Finally, the board arranged for directors Sunstein and Sarabhai to sign voting agreements pledging to vote all of their Class B shares in favor of the merger - Sunstein, Sarabhai, and their family members own all Class B shares, a combined 50.4% of the voting power of the corporation's outstanding stock. Mem. Op. 5-6, 12. These three measures, in concert, make the Ravert Ward merger a foregone conclusion, and any subsequent stockholder vote is mere formality.

The deal-protection devices noted above are coercive because they force the stockholders to accept the management-sponsored alternative. Moreover, the deal-protection devices are coercive because any future stockholder vote is certain to only reflect the merits of the transaction at the time the board adopted the agreement rather than at the time the actual vote is held. Immediately after the board approved the merger agreement, directors Sunstein and Sarabhai signed voting agreements to predetermine the outcome of the guaranteed stockholder vote. Mem. Op. 12. Thus, when the BTRta board adopted the deal-protection measures in the Ravert Ward Merger Agreement, it robbed the stockholders of an effective vote on the transaction contrary to the board's continuing fiduciary duties. These are precisely the coercive measures that this Court forbade in Omnicare.

The deal-protection measures in the Ravert Ward Merger Agreement are also preclusive. The BTRta board made it mathematically impossible for any proposal other than the Ravert Ward transaction to succeed, no matter how superior the proposal. Although it did not obligate the minority stockholders to vote for the Ravert Ward merger, the board precluded all stockholders from voting for the CFI merger. Because of the agreement with Ravert Ward, the stockholders had no opportunity to vote on the CFI proposal of \$17.00 per share, the stockholders must accept the Ravert Ward proposal of \$15.50 per share, and the board cannot pursue any superior offers. Mem. Op. 9, 11-12.

The BTRta board used draconian deal-protection measures to lock up the Ravert Ward Merger Agreement even though BTRta did not face any

reasonable threat to the corporation's interests. Therefore, the Ravert Ward Merger Agreement is unenforceable.

# 3. The <a href="Omnicare">Omnicare</a> Dissent's primary criticism does not apply to the BTRta board's lock-up of the Ravert Ward merger.

Omnicare held that the lock-up provisions in the Genesis merger agreement and the directors' voting agreements, in concert, were contrary to the board's continuing fiduciary duties to the stockholders, and thus the merger agreement was unenforceable. Omnicare, 818 A.2d at 939. The Omnicare Dissent, however, argues that the Majority erred because it weighted ex post results too heavily in its analysis and did not rely solely upon the circumstances at the time the board approved the agreement. Id. at 940 (Veasey, C.J., dissenting). Indeed, "dissenting opinions 'illustrate that principled differences of opinion about the law [are] ... never compromised for the sake of unanimity.'" Id. at 939 n.90 (quoting Randy J. Holland & David A. Skeel, Jr., Deciding Cases Without Controversy, 5 Del. L. Rev. 115, 118 (2002)). Accordingly, while Omnicare established precedent that serves both corporate and stockholder interests, the Dissent deserves consideration. The Omnicare Dissent's primary concerns, however, do not materialize in the facts of this case.

Despite the Omnicare Majority's prudential concern that a board of directors cannot "abdicate its fiduciary duties to the minority [stockholders]", the Dissent notes that it would have allowed the board more leeway because NCS was "on the brink of bankruptcy" when it entered the Genesis merger agreement. Id. at 937, 940. Further, the

Dissent notes that Omnicare's second bid was hostile and arrived after both the NCS board approved the Genesis merger and directors Outcalt and Shaw signed the voting agreements. <u>Id</u>. Thus, at the time the NCS board locked up the Genesis agreement, the Genesis proposal was the only bid that offered stockholder value. Id. at 941.

This Court, however, need not consider any ex post results to rule that the BTRta board' acted contrary to its fiduciary duties when it locked up the Ravert Ward merger. The BTRta board faced none of the pressures that affected the NCS board in Omnicare. First, the record shows no indication that BTRta was in financial peril. Second, the Ravert Ward merger was not the only viable option available to BTRta. Indeed, the BTRta board had already approved the CFI merger when it locked up the Ravert Ward transaction. Mem. Op. 9, 12. Moreover, the CFI merger was not only available to BTRta at that time, the CFI merger offered superior value to BTRta stockholders. The BTRta board cast aside CFI's offer of \$17.00 per share only to hastily lock up Ravert Ward's offer of a mere \$15.50 per share. Mem. Op. 9, 11. Thus, the Omnicare Dissent's chief criticism does not apply to this case.

Therefore, the Ravert Ward Merger Agreement is unenforceable because the BTRta board employed draconian defensive devices to lock up the merger contrary to its fiduciary duties to the stockholders. Furthermore, BTRta's board cannot contract around its fiduciary duties to minority shareholders. Additionally, by failing to maximize value for all shareholders, the directors breached their duty of care and loyalty under Revlon. Thus, this Court should refuse to upset the order of the Chancery Court.