

IN THE SUPREME COURT OF THE STATE OF DELAWARE

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

---

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. )

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APPELLEE'S OPENING BRIEF

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Team E  
Counsel for Defendants Below-  
Appellees

February 11, 2011

**TABLE OF CONTENTS**

TABLE OF CITATIONS..... iv

NATURE OF PROCEEDINGS..... 1

SUMMARY OF ARGUMENT..... 3

STATEMENT OF FACTS..... 4

ARGUMENT..... 6

**I. THE DELAWARE CHANCERY COURT PROPERLY UPHELD THE EXCLUSIVE FORUM BYLAW PROVISION BECAUSE SUCH PROVISIONS ARE PRESUMPTIVELY VALID AND CLEAR DELAWARE STATUTORY AUTHORITY PERMITS THE CREATION OF THE PROVISION, IN ADDITION THE CONTRACT WAS FAIRLY CREATED AND PLACES NO SUBSTANTIVE LIMITATIONS ON THE RIGHTS OF PINPOINT STOCKHOLDERS. .... 6**

**A. Question Presented ..... 6**

**B. Scope of Review ..... 6**

**C. Merits of the Argument ..... 6**

**1. Delaware corporate law..... 6**

*a. The authority of the Pinpoint Directors to create and adopt the exclusive forum bylaw is permitted by corporate law statute. .... 6*

*b. The exclusive forum bylaw provision is a creation of Delaware courts and is presumptively valid. .... 7*

*c. The Pinpoint Bylaw is procedural, placing no substantive restrictions on stockholders’ substantive rights. .... 9*

*d. Exclusive forum provisions have been upheld for LLCs and because of close similarities in corporate governance, should also be upheld for C Corporations. .... 10*

**2. Contract law doctrine reinforces the enforceability of the Pinpoint Bylaw based on freedom of contract. .... 10**

*a. The corporate charter was subject to equal bargaining power and standard business practices and realities sustain the validity of the charter. .... 11*

*b. The actions of the board were fundamentally fair because there was no evidence of bad motive and because there is a substantial relation between Pinpoint and its exclusive forum. .... 13*

*c. Galaviz v. Berg was a matter of federal common law, in which that court failed to consider Delaware statutory law, and should not control these proceedings. .... 14*

**II. EQUITABLE CONSIDERATIONS CONCERNING THE BOARD’S ADOPTION OF THE EXCLUSIVE FORUM PROVISION DO NO MERIT A DEPARTURE FROM A DEFAULT BUSINESS JUDGMENT RULE ANALYSIS ..... 16**

**A. Question Presented ..... 16**

B. Scope of Review ..... 16

C. Merits of the Argument ..... 17

    1. Judicial review for "entire fairness" is not appropriate because the terms and effect of the Pinpoint Bylaw do not operate to the exclusive benefit of the Pinpoint Directors or abridge substantive rights held by the stockholders. .... 18

    2. Heightened scrutiny under *Unocal's* reasonableness and proportionality test is not appropriate because the Pinpoint Bylaw is not a defensive measure. .... 21

    3. The Pinpoint Bylaw is supported by rational business purposes of efficiency and predictability, and therefore valid under the business judgment rule. .... 23

    4. The Pinpoint Bylaw constitutes a valid contractual agreement between Pinpoint and its stockholders and cannot be displaced by the *McWane* principle, which is a default rule effective only in the absence of an express agreement between parties. .... 24

CONCLUSION..... 25

## TABLE OF CITATIONS

CASES**UNITED STATES SUPREME COURT**

<i>American Dredging Co. v. Miller</i> ,	
510 U.S. 443 (1994).....	9
<i>Bremen v. Zapata Off-Shore Co.</i> ,	
407 U.S. 1 (1972).....	8, 9, 12
<i>Carnival Cruise Lines, Inc. v. Shute</i> ,	
499 U.S. 585 (1991).....	12, 13, 14, 20

**UNITED STATES COURT OF APPEALS**

<i>Argueta v. Banco Mexicano, S.A.</i> ,	
87 F.3d 320 (9th Cir. 1996).....	14

**UNITED STATES DISTRICT COURT**

<i>Bbdova, LLC v. Automotive Technologies, Inc.</i> ,	
358 F.Supp.2d 387 (D. Del. 2005).....	9
<i>Galaviz v. Berg</i> ,	
2011 WL 135215 (N.D. Cal. Jan. 3, 2011).....	14
<i>Process &amp; Storage Vessels, Inc. v. Tank Service, Inc.</i> ,	
541 F.Supp. 725 (D. Del. 1982).....	8

**SUPREME COURT OF DELAWARE**

<i>Aronson v. Lewis</i> ,	
473 A.2d 805 (Del. 1984).....	24
<i>Beam v. Stewart</i> ,	
845 A.2d 1040 (Del. 2004).....	19
<i>Broz v. Cellular Info. Sys.</i> ,	
673 A.2d 148 (Del. 1996).....	19
<i>Cede &amp; Co. v. Technicolor, Inc.</i> ,	
634 A.2d 345 (Del. 1993).....	16, 17, 18, 19, 24
<i>Centaur Partners, IV v. National Integroup, Inc.</i> ,	
582 A.2d 923 (Del. 1990).....	6
<i>Citron v. Fairchild Camera &amp; Instrument Corp.</i> ,	
569 A.3d 52 Del. 1989).....	16
<i>Elf Atochem North America, Inc. v. Jaffari</i> ,	
727 A.2d 286 (Del. 1999).....	10
<i>Emerald Partners v. Berlin</i> ,	
787 A.2d 85 (Del. 2001).....	17
<i>Frantz Mfg. Co. v. EAC Indus.</i> ,	
501 A.2d 401 (Del. 1985).....	6
<i>Gantler v. Stephens</i> ,	
965 A.2d 695 (Del. 2009).....	20, 21
<i>Graham v. State Farm Mut. Auto. Ins. Co.</i> ,	
565 A.2d 908 (Del. 1989).....	12
<i>Grobow v. Perot</i> ,	
539 A.2d 180 (Del. 1988).....	17
<i>Ingres Corp. v. CA, Inc.</i> ,	
8 A.3d 1143 (Del. 2010).....	8, 25

*Kahn v. Household Acquisition Corp.*,  
 591 A.2d 166 (Del. 1991).....16

*Levitt v. Bouvier*,  
 287 A.2d 671 (Del. 1972).....16

*McDermott Inc. v. Lewis*,  
 531 A.2d 206 (Del. 1987).....9

*McWane Cast Iron Pipe Corp. v. McDowell-Wellman Engineering Co.*,  
 263 A.2d 281 (Del. 1970).....3,18,24,25

*Mills Acquisition Co. v. MacMillan, Inc.*,  
 559 A.2d 1261 (Del. 1989).....21,23

*M.P.M. Enters., Inc. v. Gilbert*,  
 731 A.2d 790 (Del. 1999).....6

*Sinclair Oil Corp. v. Levien*,  
 280 A.2d 717 (Del. 1971).....17

*State v. Tabasso Homes*,  
 42 Del. 110 (Del. 1942).....10,11

*Tulowitzki v. Atlantic Richfield Co.*,  
 396 A.2d 956 (Del. 1978).....12

*Unitrin, Inc. v. American General Corp.*,  
 651 A.2d 1361 (Del. 1995).....17,21,23

*Unocal Corp. v. Mesa Petroleum Co.*,  
 493 A.2d 946 (Del. 1985).....3,16,17,21,23

*Waggoner v. Laster*,  
 581 A.2d 1127 (Del. 1990).....16

**COURT OF CHANCERY OF DELAWARE**

*Abry Partners V, L.P. v. F & W Acquisition LLC*,  
 891 A.2d 1032 (Del. Ch. 2006).....11,13,14

*In re Revlon, Inc. Shareholders Litig.*,  
 990 A.2d 940 (Del. Ch. 2010).....4,7

*In re Topps Co. S'holders Litig.*,  
 924 A.2d 951 (Del. Ch. 2007).....25

**STATUTES**

**FEDERAL**

False Claims Act,  
 31 U.S.C. § 3729 (2009).....5

**DELAWARE**

Del. Code Ann. tit. 8, § 102(b)(1) (2010).....8

Del. Code Ann. tit. 8, § 109 (2010).....4,7

Del. Code Ann. tit. 8, § 109 (a) (2010).....7,15

Del. Code Ann. tit. 8, § 109 (b) (2010).....7

Del. Code Ann. tit. 8, § 141(a) (2010).....7,17

Del. Code Ann. tit. 6, § 18-201(b) (2010).....10

Del. Code Ann. tit. 8, § 106 (2010).....10

**SECONDARY AUTHORITY**

**LAW REVIEWS AND JOURNALS**

Sara Lewis, *Transforming the "Anywhere but Chancery" Problem Into the "Nowhere but Chancery" Solution*,  
14 Stan. J.L. Bus. & Fin. 199, 206 (2008).....8

**INTERNET SOURCES**

Berkshire Hathaway Bylaws, amended Nov. 5, 2010, available at  
<http://www.sec.gov/Archives/edgar/data/1067983/000119312510254196/dex31.htm>.....12

## **NATURE OF PROCEEDINGS**

This is an appeal filed by the plaintiff-below/appellant, Edward Miller ("Miller") from a procedural interlocutory order of the Court of Chancery of the State of Delaware in and for New Castle County (the "Court of Chancery") ruling in favor of defendants-below/appellees the Board of Directors of Pinpoint Bearings, Inc. (the "Pinpoint Directors") and Pinpoint Bearings, Inc. ("Pinpoint").

Miller filed a lawsuit in federal court in Houston, Texas on December 1, 2010, asserting both a derivative claim for breach of fiduciary duty on behalf of Pinpoint against the Pinpoint Directors and a claim for breach of the federal securities laws (the "Miller Federal Action"). (Mem. Op. 7.) Plaintiffs Eileen Webb, Richard Patrick, and Harold Kohn, shareholders of Pinpoint, filed a lawsuit in the Court of Chancery asserting derivative claims for breach of fiduciary duty on behalf of Pinpoint against the Pinpoint Directors on December 2, 2010 (the "Original Delaware Actions"). (Mem. Op. 7-8.) The Court of Chancery entered an Order of Consolidation at the request of counsel for the plaintiffs in the Original Delaware Action on December 8, 2010. (Mem. Op. 8.) On December 13, 2010, Pinpoint and the Pinpoint Directors filed a motion in the federal court in Houston to stay the Miller Federal Action in favor of the consolidated Original Delaware Actions. (Mem. Op. 8.) At present, the motion to stay remains pending in federal court. (Mem. Op. 8.)

In addition to his existing Federal Action, Miller filed a lawsuit in the Court of Chancery asserting a derivative claim for breach of fiduciary duty against the Directors on December 15, 2010

(the "Miller Delaware Action"). (Mem. Op. 8.) The Miller Delaware Action includes identical breach of fiduciary duty claims as the earlier filed Miller Federal Action and the Original Delaware Actions. (Mem. Op. 8-9.) Simultaneously to his Delaware filing, Miller filed two motions with the Court of Chancery, first asking to modify the Order of Consolidation to include the Miller Delaware Action; and second moving to stay the now consolidated Delaware Actions in favor of allowing the Miller Federal Action to proceed. (Mem. Op. 9.)

On January 12, 2011, Chancellor McCloskey of the Court of Chancery granted Miller's Motion to modify the Order of Consolidation, denied Miller's Motion to stay the Delaware Action, and granted a Motion of the Pinpoint Directors to enjoin Miller from prosecuting his derivative fiduciary claims in the Miller Federal Action in Texas or any other forum. (Mem. Op. 20-21.)

Miller petitioned and the Court of Chancery certified an appeal from Chancellor McCloskey's interlocutory Opinion and Order and this Court accepted the interlocutory appeal on January 18, 2011. (Del. Sup. Ct. Appeal Order 1-2.) This is the Appellees' opening brief in opposition to Appellant's appeal.

**SUMMARY OF ARGUMENT**

**I.** The Order by the Court of Chancery enforcing Pinpoint's exclusive forum bylaw provision should be affirmed by this Court. The Pinpoint Directors initiated the change on the authority of a recent Court of Chancery opinion. The Delaware General Corporation Law provides statutory authority for the Directors to manage the affairs of the corporation and also defers to the provisions of Pinpoint's charter on matters of bylaw amendments. The appellant, Miller, cannot challenge the fact that the Pinpoint charter expressly confers the power of unilateral bylaw amendment on the Directors.

Consistent with Delaware case law, the provisions of Pinpoint's charter should be given full contractual force under the principles of freedom of contract. The Pinpoint Directors' actions were fundamentally fair and motivated by proper purposes of efficiency and predictability. This Court need only look to Delaware state corporate governance law and decline to adopt persuasive precedents.

**II.** This Court should refuse to apply a *Unocal* standard of "entire fairness" to the Pinpoint Directors' adoption of the Pinpoint Bylaw, as Miller has failed to allege facts to upset the presumption of the business judgment rule. The Pinpoint Bylaw was the product of an informed and disinterested process by the Pinpoint Directors and is supported by rational business purposes. Because the Pinpoint Bylaw is part of a contractual agreement between Pinpoint and its stockholders, the common law analysis of *McWane* is displaced and inapplicable. Under these equitable considerations, the Pinpoint Bylaw should be upheld by this Court.

**STATEMENT OF FACTS**

Pinpoint is a Delaware public corporation with headquarters and manufacturing operations in Houston, Texas. (Mem. Op. 4.) Pinpoint specializes in precision roller and ball bearings for aerospace applications. (Mem. Op. 4.) Pinpoint's seven member Board of Directors consists of three directors who also serve as executive officers of the Company and four directors with no other affiliation. (Mem. Op. 5.) Outstanding shares of Pinpoint are traded on the New York Stock Exchange and held by over 28,000 shareholders scattered among all fifty states. (Mem. Op. 4, 13.)

On June 10, 2010, after the Court of Chancery opinion, *in re Revlon, Inc. Shareholders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010), condoning the adoption of exclusive forum provisions in corporate charters, the Pinpoint Directors amended their bylaws and adopted such a bylaw. (Mem. Op. 2.) Pinpoint's Exclusive Forum Bylaw ("Pinpoint's Bylaw") provides:

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

(Mem. Op. 2-3). Consistent with Delaware General Corporation Law (the "DGCL") section 109 and Pinpoint's charter, the Pinpoint Directors voted to adopt the above bylaw to achieve efficiency

and predictability in the application of Delaware corporate governance law. (Mem. Op. 14.)

The underlying events giving rise to the present legal action began when Pinpoint settled an investigation and claim by the Office of the Inspector General of the United States (the "OIG") on November 30, 2010. (Mem. Op. 6.) The OIG investigation arose after a Pinpoint employee informed the government of the omission of required testing by Pinpoint managers for products that were part of government contracts for the United States military in violation of the False Claims Act, 31 U.S.C. § 3729 (2009). (Mem. Op. 5.)

Pinpoint responded to the OIG investigation by convening a meeting of the Directors, at which meeting a special investigation committee comprised of two independent Pinpoint Directors was appointed. (Mem. Op. 6). The special committee relied on independent legal counsel to aid the investigation and upon review deemed the claims to be valid. (Mem. Op. 6). In the interest of remaining an eligible government contractor and avoiding further criminal indictment, the entire Pinpoint Board approved a settlement between the OIG and Pinpoint. (Mem. Op. 6-7). Pinpoint issued a press release concerning the OIG investigation and the terms of the settlement on the same date the settlement agreement was finalized. (Mem. Op. 7).

After Pinpoint's announcement of the investigation and settlement, Miller commenced his federal action in district court in Houston, Texas on December 1, 2010. (Mem. Op. 7.)

## ARGUMENT

I. THE DELAWARE CHANCERY COURT PROPERLY UPHELD THE EXCLUSIVE FORUM BYLAW PROVISION BECAUSE SUCH PROVISIONS ARE PRESUMPTIVELY VALID AND CLEAR DELAWARE STATUTORY AUTHORITY PERMITS THE CREATION OF THE PROVISION, IN ADDITION THE CONTRACT WAS FAIRLY CREATED AND PLACES NO SUBSTANTIVE LIMITATIONS ON THE RIGHTS OF PINPOINT STOCKHOLDERS.

### A. Question Presented

Whether a corporation's exclusive forum bylaw provision that was validly adopted by the Board of Directors, should control the bringing of derivative actions for breach of fiduciary duty in both federal and Delaware state courts?

### B. Scope of Review

Questions on the validity of a corporation's bylaw amendments are a mixture of law and fact. *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985). This Court applies a *de novo* standard of review to conclusions of law. *M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 795 (Del. 1999). Interpretation of corporate bylaw provisions are reviewed *de novo*. *Centaur Partners, IV v. National Integroup, Inc.*, 582 A.2d 923, 926 (Del. 1990).

### C. Merits of the Argument

The question presented requires consideration of both Delaware corporate law, under which the nominal defendant incorporated, and contract law, which governs the enforceability of the provision.

#### 1. Delaware corporate law

a. *The authority of the Pinpoint Directors to create and adopt the exclusive forum bylaw is permitted by corporate law statute.*

In amending their bylaws, the Pinpoint Directors acted with express statutory authority, as well as implied authority based on the board's power to manage the business affairs of the corporation. See

Del. Code Ann. tit. 8, §§ 109, 141(a) (2010). Delaware statutory law expressly permits that a corporate charter may confer on the directors the power to amend the bylaws. tit. 8, § 109(a) ("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."). Section 109(b) of the DGCL authorizes bylaws to contain "any provision . . . relating to . . . the rights and powers of [the] stockholders." tit. 8, § 109(b). The Pinpoint Bylaw addresses the authority of stockholders to bring derivative fiduciary claims. As such, the Pinpoint Bylaw necessarily "relates" to the powers of stockholders and therefore, the adoption of the Pinpoint Bylaw must be valid.

Additionally, DGCL Section 141(a) grants to the board of directors the exclusive authority to manage the affairs of the business, except as provided in the corporate charter and elsewhere in the DGCL. Del. Code Ann. tit. 8, § 141(a) (2010). This is important for two reasons. First, section 141(a) creates a presumption that all affairs of the corporation should be within the purview of the Directors. Second, the portion of DGCL Section 141(a) that provides an exception for the corporate charter clearly anticipates the amendment of the charter, as in the case of Pinpoint.

*b. The exclusive forum bylaw provision is a creation of Delaware courts and is presumptively valid.*

A Delaware Court of Chancery judge acknowledged the permissibility of exclusive forum provisions in the *Revlon* opinion. *In re Revlon, Inc. Shareholders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010) (stating that "corporations are free to respond with charter

provisions selecting an exclusive forum for intra-entity disputes"). The *Revlon* Court premised the statement referencing exclusive forum bylaws on Del. Code Ann. tit. 8, § 102(b)(1), which permits the corporate certificate to contain any provisions necessary for the management of the corporation, so long as the provision is not in violation of applicable law. Delaware judicial decisions on corporate governance matters affirm the presumption in favor of the Pinpoint Directors and place the burden on Miller to rebut the presumption of the validity of Pinpoint's exclusive forum bylaw provision. *Ingres Corp. v. CA, Inc.*, 8 A.3d 1143, 1146 (Del. 2010) quoting *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 15 (1972); Sara Lewis, *Transforming the "Anywhere but Chancery" Problem Into the "Nowhere but Chancery" Solution*, 14 Stan. J.L. Bus. & Fin. 199, 206 (2008). Both Delaware and federal law indicate that private parties may contract to pursue all litigation in a given forum. *Process & Storage Vessels, Inc. v. Tank Service, Inc.*, 541 F.Supp. 725, 733 (D. Del. 1982). In *Bremen v. Zapata*, the U.S. Supreme Court held that forum provisions should not be set aside "absent a strong showing that enforcement would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching." 407 U.S. 1, 12-15 (1972). The *Revlon* court specifically anticipated the creation of exclusive forum provisions and federal cases uphold their general validity, lending judicial authority to the creation of the Pinpoint Bylaw.

*c. The Pinpoint Bylaw is procedural, placing no substantive restrictions on stockholders' substantive rights.*

The Pinpoint Bylaw is entirely procedural and places no substantive limitation on stockholders' rights to bring a breach of fiduciary duty claim. The United States Supreme Court has held that forum issues raise questions of procedure rather than substance. *American Dredging Co. v. Miller*, 510 U.S. 443, 453 (1994). As every remedy for fiduciary duty remains available in Delaware courts, there is no substantive impact on stockholder rights and the bylaw is valid. (Mem. Op. 12.) Furthermore, under conflict of law principles, Delaware substantive law would control regardless of where the case is heard, so there can be no substantive difference in applicable law. *McDermott Inc. v. Lewis*, 531 A.2d 206, 215 (Del. 1987).

The Pinpoint Bylaw provides only procedural limitations and should be deemed reasonable. A substantive limitation on stockholder rights could rise to the level of unreasonableness, however, the Pinpoint Bylaw only impacts forum selection and in no way implicates stockholders' ability to bring a derivative suit. Absent the implication of substantive rights, Miller must show that the forum is so inconvenient that he will be deprived of his day in court. *Bbdova, LLC v. Automotive Technologies, Inc.*, 358 F.Supp.2d 387, 390 (D. Del. 2005) (citing *Bremen v. Zapata*, 407 U.S. 1, 18 (1972)). There is no evidence in the record that Delaware would prove to be a particular difficult forum for Miller as he has already engaged in legal maneuverings in Delaware that indicate the accessibility of Delaware state courts.

d. *Exclusive forum provisions have been upheld for LLCs and because of close similarities in corporate governance, should also be upheld for C Corporations.*

The Delaware Supreme Court has not directly addressed the validity of exclusive forum provisions in corporation bylaws, but this Court has enforced a similar provision for limited liability company ("LLC") agreements. *Elf Atochem North America, Inc. v. Jaffari*, 727 A.2d 286, 290 (Del. 1999). This Court should note the similarities between LLCs and C corporations, and by analogy, enforce Pinpoint's exclusive forum bylaw provision. Both LLCs and corporations are governed by agreements and bylaws and an LLC agreement functions like corporate bylaws in that neither are filed with the Delaware Secretary of State. See Del. Code Ann. tit. 6, § 18-201(b); Del. Code Ann. tit. 8, § 106. Additionally, LLCs provide the liability shielding function of corporations. *Elf Atochem*, 727 A.2d at 290. The legal relationship between LLCs and corporations bolsters the argument that if similar forum provisions in LLC agreements have been enforced, then identical provisions in corporate bylaws also should be enforced.

**2. Contract law doctrine reinforces the enforceability of the Pinpoint Bylaw based on freedom of contract.**

Not only does Delaware corporate law support the validity of the Pinpoint Bylaw, but contract law doctrine does so as well. Having established that Delaware corporate law gives the power to directors to amend the bylaws, the unilateral adoption of the Pinpoint Bylaw by Pinpoint Directors must be proper under contract law. One of the basic tenets of American jurisprudence is freedom of contract. *State v. Tabasso Homes*, 42 Del. 110, 116 (Del. 1942) (stating the general rule that "the right to contract is one of the great, inalienable

rights accorded to every free citizen" and recognizing that "freedom of contract is the rule and restraints on this freedom the exception"). The present case is nothing more than two parties (the corporation and its stockholders) entering into a specific contract to meet their mutual needs. As such, the full force of contract law principles uphold the validity of the Pinpoint Bylaw.

*a. The corporate charter was subject to equal bargaining power and standard business practices and realities sustain the validity of the charter.*

Miller raises concerns about the relative bargaining power of the stockholders and the Directors. (Mem. Op. 13.) The argument proceeds that since 28,000 people own shares of Pinpoint and because those people are scattered across all fifty states, then they could not possibly have bargained on equal terms with the Pinpoint Directors and Pinpoint. (Mem. Op. 13.) Miller's argument fails for two reasons—there was equal bargaining power and standard business realities dictate the necessity of this type of agreement.

First, the nature of the corporate governance contract is different than typical contracts of adhesion. *See Abry Partners V, L.P. v. F & W Acquisition LLC*, 891 A.2d 1032, 1059-60 (Del. Ch. 2006) (providing a discussion of bargaining power and the sophistication of parties). The present case involves investors who are more sophisticated than average consumers subjected to contracts of adhesion. Specifically, Miller, at the time of filing of this suit, owned 5,000 shares of Pinpoint common stock, which he purchased over the course of 20 years of employment with the Pinpoint. The total value of Miller's stock is approximately \$230,000. This was not a one

time, simple transaction, but a series of purchases over the course of two decades. The relative sophistication of the parties makes this case more similar to *Zapata*, in which the United States Supreme Court held that forum provisions are presumed valid. *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 12 (1972).

However, should this Court find that the contract is adhesive, the contract is not automatically rendered unenforceable. *Graham v. State Farm Mut. Auto. Ins. Co.*, 565 A.2d 908, 912 (Del. 1989). Instead, to invalidate a contract based on unequal bargaining power, the terms must be "so one-sided as to be oppressive." *Id.* (citing *Tulowitzki v. Atlantic Richfield Co.*, 396 A.2d 956, 960 (Del. 1978)). The Delaware Supreme Court adopted a "mores and business practices" test to determine whether the terms are oppressive and in that case This Court found persuasive the fact that all but one individual accepted the terms of the deal. *Tulowitzki v. Atlantic Richfield Co.*, 396 A.2d 956, 960 (Del. 1978). The Pinpoint Bylaw was changed in June 2010, and presumably announced pursuant to an 8-K filing and no objections were noted in the record. Further, this type of provision is not unique, indicating that this is an accepted practice within the business community. See, e.g., Berkshire Hathaway Bylaws, amended Nov. 5, 2010, available at <http://www.sec.gov/Archives/edgar/data/1067983/000119312510254196/dex31.htm>.

Second, even if the court finds unequal bargaining power, the analysis of *Carnival Cruise Lines, Inc. v. Shute* should control. In that case, the Court enforced an exclusive forum provision in form contract tickets for a cruise. 499 U.S. 585 (1991). The Court

rejected a pure *Zapata* analysis in favor of an approach that considered the “realities of form passage contracts.” *Id.* at 593. This analogy applies to the realities of modern investing. Pursuant to the securities law, Pinpoint would have given notice of the change to the bylaws to all its 28,000 stockholders, soon after the adoption in June, and Pinpoint would be unduly burdened if required to provide additional notice. Consistent with the restrictions of securities law, and the principles of caveat emptor, the Pinpoint Bylaw must be valid to reinforce the efficiency of Delaware commercial law. *Abry Partners V, L.P. v. F & W Acquisition LLC*, 891 A.2d 1032, 1059-60 (2006). For this Court to hold otherwise, risks grinding the wheels of commerce and investment to a halt.

*b. The actions of the board were fundamentally fair because there was no evidence of bad motive and because there is a substantial relation between Pinpoint and its exclusive forum.*

The *Carnival* Court held that a signed contract is valid with regards to all terms, no matter whether they were read. *See generally Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (2001). This was, however, subject to a fundamental fairness test. *Id.* at 595. Applying a fundamental fairness test to the actions of the Pinpoint Directors requires an inquiry as to whether there was a bad faith motive in selecting the forum for suit in a place in order to discourage potential plaintiffs from making legitimate claims. *Id.* at 595. In *Carnival*, the Court found it persuasive that the cruise line company operated out of Florida, where it had its principal place of business. *Id.* at 595. Similarly, Pinpoint is a Delaware corporation, hence governed by Delaware law and giving rise to a reasonable

relationship between the corporation and the state of the exclusive forum provision. Delaware law holds that the chosen law of contracting parties should be upheld when there is a material relationship to the transactions. *Abry Partners V, L.P. v. F & W Acquisition LLC*, 891 A.2d 1032, 1046 (Del. Ch. 2006). In the *Abry* case, the court recognized that it made sense for parties from different states and operating in interstate commerce to select a reliable body of law from the state of incorporation. *Id.* at 1047. Further, the *Carnival* Court held that fundamental fairness cannot exist when there is evidence of fraud or overreaching on the part of the company. *Carnival*, 499 U.S. at 595. There is no evidence in the Court of Chancery opinion or elsewhere in the record of fraud or overreaching in the representations made by the Pinpoint Directors.

Finally, the Ninth Circuit has held that fundamental fairness will be violated when a party will not have a meaningful day in court. *Argueta v. Banco Mexicano, S.A.*, 87 F.3d 320, 324 (9th Cir. 1996). Nothing about the Delaware state court system would prevent stockholders from having a meaningful day in court in that state. With a full range of remedies available to plaintiffs, no evidence of bad motive, and a clear relationship between the corporation and the forum state, the Pinpoint Bylaw is fundamentally fair.

*c. Galaviz v. Berg was a matter of federal common law, in which that court failed to consider Delaware statutory law, and should not control these proceedings.*

A federal judge in California recently addressed the enforceability of an exclusive forum bylaw provision. *Galaviz v. Berg*, 2011 WL 135215 (N.D. Cal. Jan. 3, 2011). That case purported to

rely on general contract principles to nullify the forum provision. *Id.* at \*3. Specifically, that court rested the decision to deny the motion to dismiss on the lack of mutual consent. *Id.* Plaintiffs in *Galaviz* did not allege fraud or undue influence in the creation of the forum provision and plaintiffs did not challenge that they would still have a meaningful day in court in Delaware. *See id.* The decision, however, fails to consider two key points. First, in *Galaviz* and in the case at bar, stockholders were free to sell their shares and exit if they found the forum provision offensive and there is no evidence that sale would have been difficult as Pinpoint shares are traded on the New York Stock Exchange. Second, Delaware statutory law specifically grants this authority to the Directors, putting stockholders on notice that this type of change might occur. Del. Code Ann. tit. 8, § 109(a) (2010). Furthermore, federal common law determined the ruling in *Galaviz*, thus the case has no precedential effect for a court sitting in Delaware and applying Delaware state law. For these reasons, the *Galaviz* decision should not control the result in the case at bar.

**II. EQUITABLE CONSIDERATIONS CONCERNING THE BOARD'S ADOPTION OF THE EXCLUSIVE FORUM PROVISION DO NO MERIT A DEPARTURE FROM A DEFAULT BUSINESS JUDGMENT RULE ANALYSIS.**

**A. Question Presented**

Whether enhanced judicial scrutiny should be applied to a board of director's adoption of an exclusive forum bylaw when the board's action does not usurp any rights reserved to the stockholders or implicate any breach of the board's fiduciary duties?

**B. Scope of Review**

The Court of Chancery correctly found that the Pinpoint Director's adoption of an exclusive forum bylaw did not impose any substantive limitation on stockholders and failed to raise any specter of a disqualifying self-interest or loyalty on behalf of the Pinpoint Directors. The formulation and ultimate rejection of the duty of loyalty and the reasonableness and proportionality standards under *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985), involves questions of law which are subject to *de novo* review by this Court. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993); *Kahn v. Household Acquisition Corp.*, 591 A.2d 166, 175-76 (Del. 1991); *Waggoner v. Laster*, 581 A.2d 1127, 1132 (Del. 1990).

Assuming a correct formulation of the rules' elements, the Court of Chancery's findings upon application of the business judgment rule are, on appeal, entitled to substantial deference unless clearly erroneous or not the product of a logical and deductive reasoning process. *Cede & Co.*, 634 A.2d at 360; *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.3d 52, 64 (Del. 1989); *Levitt v. Bouvier*, 287 A.2d 671, 673 (Del. 1972).

### C. Merits of the Argument

A fundamental principle of Delaware law is that the business and affairs of a corporation are managed by its board of directors. Del. Code Ann. tit. 8, § 141(a) (2010); see *Cede & Co.*, 634 A.2d at 360. The business judgment rule “operates to preclude a court from imposing itself unreasonably on the business and affairs of a corporation” so long as the board is fulfilling its fiduciary duties to “protect the interests of the corporation and to act in the best interests of its shareholders.” *Cede & Co.*, 634 A.2d at 360. The directors of a Delaware corporation hold three primary fiduciary duties: due care, loyalty, and good faith. *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001). Absent a violation of any one of these three duties, a court will uphold a director-approved transaction within a board’s authority if the action can be “attributed to any rational business purpose.” *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971); see also *Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988).

In an attempt to upset the presumption of the business judgment rule, Miller has argued that the Pinpoint Director’s decision to adopt the Pinpoint Bylaw was motivated by self-interest and therefore in violation of the duty of loyalty owed to Pinpoint’s stockholders. Relying on strained analogies to board action while under the threat of takeover and merger, Miller urges this Court to analyze the Pinpoint Directors’ decision under the tests espoused in *Unocal* and *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361 (Del. 1995). Both arguments, however, are without merit given the purely procedural nature of the Pinpoint Bylaw and the complete absence of any

disqualifying Pinpoint Director interest furthered by adopting the Pinpoint Bylaw. The Pinpoint Bylaw, when understood in its true context, was a valid business decision within the Pinpoint Director's express authority under its charter. Accordingly, this Court should uphold the Pinpoint Bylaw and defer to the presumption of the business judgment rule.

- 1. Judicial review for "entire fairness" is not appropriate because the terms and effect of the Pinpoint Bylaw do not operate to the exclusive benefit of the Pinpoint Directors or abridge substantive rights held by the stockholders.**

A review of the process surrounding the adoption of the Pinpoint Bylaw and its impact on substantive stockholder rights proves that the Pinpoint Directors did not shirk from their fiduciary duties when acting to consolidate future litigation, premised on statutory authority of Delaware, in the Court of Chancery. The Pinpoint Director's action simply manifests a recognition of sustained approval of similar bylaw provisions by the Delaware state courts and the decision to increase efficiency and minimize litigation costs to the benefit of Pinpoint and Pinpoint stockholders. Consequently, the Pinpoint Bylaw cannot be the basis of a violation of fiduciary duty by the Pinpoint Directors.

Under the duty of loyalty test expressed by this Court, Miller is unable to identify any aspect of the record that would support a finding that the Pinpoint Director's acted in their own self-interest when adopting the Pinpoint Bylaw. In *Cede & Co.*, this Court distilled the duty of loyalty from its traditional and consistent formulations. 634 A.2d at 345. The Court said, "[e]ssentially, the duty of loyalty

mandates that the best interest of the corporation and its stockholders takes precedence over any interest possessed by a director . . . and not shared by the stockholders generally.” *Id.* This Court continued, “[t]he primary basis upon which a director's independence must be measured is whether the director's decision is based on the corporate merits of the subject before the board, rather than extraneous considerations or influences.” *Beam v. Stewart*, 845 A.2d 1040, 1049 (Del. 2004). In undertaking this analysis, this Court must find facts sufficient to undermine the integrity of the corporate decision-making process. *See Broz v. Cellular Info. Sys.*, 673 A.2d 148, 154 (Del. 1996) (characterizing a trial court's findings in regard to an alleged duty of loyalty violation as “being fact-dominated”).

In the case at bar, the record fails to reveal a locus of facts surrounding the Pinpoint Director's action to suggest that the Pinpoint Bylaw was anything other than a business decision implemented to the benefit of all Pinpoint directors, officers, and stockholders. First, the Pinpoint Director's adopted the Pinpoint Bylaw on June 10, 2010. (Mem. Op. 17, n. 39 and accompanying text.) The Pinpoint Director's action was the product of informed advice by outside counsel, and the Court of Chancery concluded that Pinpoint Directors were motivated solely by corporate considerations of “convenience, efficiency, and relative predictability.” (Mem. Op. 17.) The record does not disclose any threat perceived by the Pinpoint Directors that would allow Miller to characterize the Pinpoint Director's action as self-interested, and it undisputed that the events which precipitated

these proceedings did not occur until months after the Pinpoint Bylaw's adoption. (Mem. Op. 5.)

Moving beyond the circumstances surrounding the Pinpoint Director's action, the very terms and effect of the Pinpoint Bylaw do not purport to serve any director's interest to the exclusion of the stockholders generally, nor does the Pinpoint Bylaw restrict rights normally reserved for the stockholders of a corporation. In instances of meritorious allegations of self-interest before this Court, directors are typically standing on both sides of a transaction where the director's personal interest, such as financial gain or incumbency, does not align with the corporation's welfare. See e.g., *Gantler v. Stephens*, 965 A.2d 695, 707-08 (Del. 2009). Here, the Pinpoint Bylaw did not present a benefit that was to the exclusion of the stockholders. As stated *supra*, the Court of Chancery found that the Pinpoint Bylaw functioned only as a procedural limitation on the forum available for litigating derivative, state law claims. (Mem. Op. 18.) The Pinpoint Bylaw's corporate objectives—"convenience, efficiency, and relative predictability"—work to the benefit of Pinpoint and its stockholders alike. (Mem. Op. 17.) The result is especially beneficial for stockholders, whose share values would likely decrease if the corporation was forced to defend derivative suits in any forum where jurisdiction may be found. See *Carnival Cruise Lines v. Shute*, 499 U.S. 585, 594 (1991) (suggesting that forum selection clauses may lower litigation costs borne by a corporation).

**2. Heightened scrutiny under *Unocal*'s reasonableness and proportionality test is not appropriate because the Pinpoint Bylaw is not a defensive measure.**

Miller's alternative test, heightened scrutiny for reasonableness and proportionately as expressed in *Unocal*, is unwarranted under the present facts. To trigger *Unocal* scrutiny, there must be some initial determination that the Pinpoint Directors acted "primarily in [their] own interests, rather than those of the corporation and its shareholders." *Unocal*, 493 A.2d at 954. This Court has stated:

We have held that when a court reviews a board action, challenged as a breach of duty, it should decline to evaluate the wisdom and merits of a business decision unless sufficient facts are alleged with particularity, or the record otherwise demonstrates, that the decision was not the product of an informed, disinterested, and independent board.

*Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1279 (Del. 1989).

*Unocal* and *Unitrin* involved defensive actions taken in the midst of a hostile takeover bid. Enhanced judicial scrutiny was proper because the Court found that a takeover, by definition, threatens the sitting director's control of the corporation. See *Unocal*, 493 A.2d at 954 (finding takeovers involve "the omnipresent specter that a board may be acting primarily in its own interests"). Over time, this Court has continued to reiterate that reasonableness and proportionality are limited to decisions involving threats to control. See *Gantler v. Stephens*, 965 A.2d 695, 705 (Del. 2009) (stating that *Unocal* scrutiny applies to defensive measures in response to *threats to control*).

Any attempt at showing that the Pinpoint Bylaw is a defensive measure against a threat to Pinpoint Directors' control of the corporation is unsupported by the operation of the Pinpoint Bylaw, as well as by Miller's actions in filing the lawsuit in Delaware. Under the Pinpoint Bylaw, a stockholder bringing a derivative action may still seek any legally available means of redress and any possible remedy in vindicating his rights. (Mem. Op. 17.) The Pinpoint Bylaw only dictates that the Court of Chancery, well-versed in the corporate governance law of Delaware, settle disputes that arise under Delaware law. The benefit of expertise and predictability provided by such an arrangement accrues equally to both appellants and appellees.

Given these benefits, Pinpoint's state of incorporation, Delaware, is certainly not an arbitrary location nor can it be objectively viewed as a material obstacle to filing a derivative claim. Regardless, Pinpoint is a publicly traded company and any stockholder offended by the Pinpoint Bylaw could simply exit by selling his or her shares on the market. Most importantly, the facts of the present matter prove that the Pinpoint Bylaw does not impede derivative suits against Pinpoint Directors. Miller himself acknowledged the Pinpoint Bylaw and voluntarily submitted himself to the jurisdiction of the Court of Chancery. In sum, Miller's ability to submit before the jurisdiction of the Court of Chancery and file a motion to consolidate his claim with the other parties should weigh heavily against the suggestion that the Pinpoint Bylaw dissuades derivative actions to the exclusive benefit of Pinpoint Directors.

Further, even a generous interpretation of the record cannot support an inference that Pinpoint Directors acted in order to preserve their control of the corporation. At the time the Pinpoint Bylaw was adopted, there was no indication of a threat to the corporation. The only potential threat addressed by the Pinpoint Bylaw is a derivative action against the directors, and a derivative action does not present the same exigencies to directors' continued control of the corporation that are unquestionably implicit in a takeover situation. A board that is attempting to "stare down" a takeover bidder fully understands that it will be promptly replaced if the takeover is successful. The court is right to recognize that "a board may be primarily acting in its own interests" in this situation. *Unocal*, 493 A.2d at 954. A derivative action against one or more Pinpoint Directors, however, does not necessitate removal if the action succeeds. Accordingly, this Court's oft-repeated language in *Unocal* and *Mills Acquisition Co.* forbids heightened judicial scrutiny in favor of the business judgment rule. See *Unitrin*, 651 A.2d at 1373 (noting that heightened scrutiny does not apply when plaintiff fails to rebut the presumption of the business judgment rule).

**3. The Pinpoint Bylaw is supported by rational business purposes of efficiency and predictability, and therefore valid under the business judgment rule.**

The Pinpoint Bylaw does not present a question of any Pinpoint Director's loyalty, nor reasonableness and proportionality under a threat to control, and therefore this Court must uphold the Pinpoint Director's decision under the business judgment rule. The business judgment rule is a deferential judicial review, premised on the

"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 was taken was in the best interests of the company." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

The Court of Chancery found that the Pinpoint Bylaw was supported by rational business purposes of efficiency, convenience, and predictability. (Mem. Op. 18.) Their analysis is fully supported by the record and entitled to substantial deference by this Court. See *Cede & Co.*, 634 A.2d at 360. Accordingly, this Court should sustain the Court of Chancery's ruling and uphold the Pinpoint Bylaw.

**4. The Pinpoint Bylaw constitutes a valid contractual agreement between Pinpoint and its stockholders and cannot be displaced by the *McWane* principle, which is a default rule effective only in the absence of an express agreement between parties.**

Having shown that the Pinpoint Bylaw is a valid contractual agreement between Pinpoint and its stockholders pursuant to Delaware law and unaffected by equitable considerations, Miller's motion to stay proceedings in Delaware should not be granted by way of reliance on the first-filed rule outlined in *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Engineering Co.*, 263 A.2d 281 (Del. 1970). In *McWane*, this Court suggested that discretion to stay a Delaware action in favor a prior action pending in another jurisdiction "should be exercised freely in favor of the stay when there is a prior action pending elsewhere, in a court capable of doing prompt and complete justice, involving the same parties and the same issues." *Id.* at 283.

An examination of these factors, however, is not warranted given this Court's recent holding in *Ingres Corp. v. CA, Inc.*, A.3d 1143,

1160 (Del. 2010).<sup>1</sup> In *Ingres*, this Court held that the *McWane* principle is a default rule of common law, freely displaced by a valid contract. Further, *Ingres* concluded that "selection clauses are 'presumptively valid' and should be 'specifically enforced'" absent clear evidence that "enforcement would be unreasonable or unjust." *Id.* at 1146. Application of the Pinpoint Bylaw is certainly not unreasonable in the present matter. Miller voluntarily submitted to the Court of Chancery's jurisdiction in consolidating his action in Delaware. Pursuant to the analysis in Issue I, *supra*, and the Opinion and Order below, the Pinpoint Bylaw must control in Miller's derivative suit as a valid contractual agreement between the parties. Under *Ingres*, the *McWane* principle is displaced, and Miller is not entitled to a stay of the Delaware proceedings.

#### CONCLUSION

Because the exclusive forum bylaw was validly adopted under both Delaware corporate law and contract law and not subject to attack on equitable grounds, this Court should refuse to upset the Order of the Court of Chancery below.

Respectfully Submitted,

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Team E

February 11, 2011

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<sup>1</sup> Even if this Court were to engage in a *McWane* analysis, it is certainly not required to defer to the prior action. Delaware courts have declined, under *McWane*, to stay a Delaware action on that basis that a chartering state "has a powerful interest in ensuring the uniform interpretation and enforcement of its corporation law." *In re Topps Co. S'holders Litig.*, 924 A.2d 951, 953 (Del. Ch. 2007).