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STATEMENT OF THE CASE

A. Nature of the Case

This Court must decide whether the unilaterally adopted Exclusive Forum Bylaw ("Forum Bylaw") is legally and equitably valid and is enforceable upon Pinpoint's shareholders. This Court must also decide whether the state law derivative action and the federal action should be adjudicated in the Texas federal court.

Mr. Miller's first-filed action in the Texas federal court includes claims under the Exchange Act and fiduciary claims against Defendant Directors ("Directors"). Directors assert that the Forum Bylaw requires that the derivative suit be litigated in Delaware. The Bylaw adoption demonstrates Directors' motives of self-interest and plans to usurp control over litigation.

Directors have asked for a partial stay in regards to Mr. Miller's derivative suit and an injunction precluding litigation of the derivative suit in the Texas federal court. The Chancery Court granted the stay and allowed Mr. Miller's Exchange Act claim to proceed in Texas; however, the Texas federal court has not ruled on the partial stay of the Federal Action. Therefore, to ensure judicial efficiency, convenience, and consistency, Mr. Miller respectfully requests that this Court deny the stay and dismiss the injunction.

B. Course of Proceedings and Disposition in the Court Below

On December 1, 2010, in the Southern District of Texas, Petitioner-Plaintiff Mr. Edward Miller brought suit against Respondent-Defendants Pinpoint Bearings, Inc. ("Pinpoint") and Pinpoint's Board of Directors, alleging a breach of the Directors'

fiduciary duty of oversight and a violation of federal securities law. (Op. 1, 7.) Miller, as a longtime shareholder, adequately represents the putative class of shareholders, who acquired their shares during the period of the fiduciary breach. (Op. 4.)

The following day, three separate shareholders each filed essentially identical derivative oversight complaints in the Delaware Court of Chancery. (Op. 7.) Pursuant to a proposed Order of Consolidation, all three complaints were consolidated to *In re Pinpoint Bearings, Inc. Shareholders Litigation*. (Op. 8.)

On December 13, Directors and Pinpoint filed a motion to partially stay the pending derivative action in the Southern District of Texas in favor of the consolidated shareholders' action in Delaware. (Op. 8.) Directors relied on the unilaterally adopted Forum Bylaw to support their motion. (Op. 8.) Because the federal court has exclusive jurisdiction over the federal claim, Directors sought concurrent litigation, hoping to litigate the federal claim in Texas and the consolidated derivative claim in Delaware. (Op. 9.)

Two days later in Delaware, Mr. Miller simultaneously filed an identical derivative fiduciary oversight claim to his prior Texas claim and modified the order of consolidation to include his action with the other shareholders. (Op. 9.) He then filed a second motion moving for a stay of the consolidated action in favor of the federal action. (Op. 9.) In vigorous opposition to Mr. Miller's motion to stay, the Directors moved for an injunction barring Mr. Miller from bringing fiduciary claims in any other court. (Op. 10.)

The lower court issued an interlocutory opinion and order granting Mr. Miller's motion to modify the Order of Consolidation and include Mr. Miller's Delaware derivative claims. (Op. 20.) The lower court denied Mr. Miller's motion to stay the Delaware action and granted the Directors' injunction. (Op. 21.)

Subsequently, Mr. Miller applied to the Court of Chancery, pursuant to Supreme Court Rule 42, for Certification of an Interlocutory Appeal. (Del. Ch. Order 2.) Since enforcing the Bylaw presented a substantial issue, established a legal right, and presented a first-instance question of law in Delaware, the court certifies the question of law. (Del. Ch. Order 2.) Based in the certified question of law, Mr. Miller petitioned, and this Court accepted, an appeal from the Court of Chancery's Interlocutory Order. (Del. Order 2.)

C. Statement of Facts

Pinpoint manufactures aerospace precision roller and ball bearings, which are used in the aircraft construction. (Op. 4.) It conducts the majority of its business with the United States military, earning over 60% of its yearly revenue from its military contracts. (Op. 4-5.) It is publicly traded on the New York Stock Exchange, with a market capitalization of nearly \$4 billion and 88 million shares of outstanding stock. (Op. 4.) Collectively, Pinpoint has shareholders in all fifty States. (Op. 4.) Although Pinpoint is a Delaware corporation, its headquarters, 8,000 employees, and all of its business is conducted in Houston, Texas. (Op. 4.)

Edward Miller, a lifelong resident of Houston, Texas, was a valuable employee of Pinpoint for over twenty years until his retirement in 2004. (Op. 3-4.) He became a shareholder of Pinpoint during his employment and currently owns 5,000 shares of common stock, valued near \$230,000. (Op. 3.) Between 2009 and 2010, Mr. Miller purchased an additional 200 shares from Pinpoint. (Op. 4.)

In 2009, unbeknownst to Mr. Miller, Pinpoint began "regularly omitting . . . required testing" on its military aircraft components, "falsely representing to the military in its billing and invoice submissions." (Op. 5-6.) On June 10, 2010, just months before disclosure of Pinpoint's violations, the Board amended its Bylaws by unilaterally adopting a forum selection bylaw. (Op. 2.) The Forum Bylaw named Delaware as the sole forum for all derivative suits resulting from fiduciary breaches. (Op. 2.)

In September 2010, a Pinpoint engineer, Roland Thompson, informed the U.S. Office of Inspector General (OIG) of Pinpoint's testing failures. (Op. 5.) Mr. Thompson, who "regularly participates in such testing," explained to the OIG that the testing failures were "a pattern of improper cost-cutting measures" in Pinpoint's military contracts. (Op. 5.) Shortly thereafter on September 8, 2010, the United States government informed Pinpoint that it was being officially investigated, and Pinpoint sought the help of outside counsel from the Houston law firm of Venner and Lee, LLP. (Op. 6.)

Counsel found that Mr. Thompson's complaint was meritorious, and the Board granted Venner and Lee the authority to enter into settlement negotiations with the OIG, which was finalized on November

30, 2010. (Op. 6.) In the settlement, Pinpoint admitted to five violations of the False Claims Act. (Op. 6.) Pinpoint agreed to pay \$500 million in fines and penalties and was ordered to terminate the managers involved in the testing failures, thus "avoid[ing] debarment or suspension of its status as an eligible contractor with the U.S. military" and "any criminal indictment." (Op. 6-7.)

Later that day, but after the close of the stock market, Pinpoint disclosed the OIG investigation and subsequent settlement to the public in a press release. (Op. 7.) Upon the opening of the stock market the following day, Pinpoint's stock price decreased \$5 a share, which resulted in a \$440 million loss in market capitalization. (Op. 7.) Numerous suits precipitated from the substantial economic penalties that resulted from Directors' fraudulent billing and failure to oversee the operations of Pinpoint. (Op. 7.)

SUMMARY OF THE ARGUMENT

I. This Court should find Pinpoint's Forum Bylaw legally invalid as a matter of law. Although directors are authorized to unilaterally adopt bylaws under Delaware General Corporate Law, the Bylaw was adopted at a time when Directors were breaching their fiduciary duties. Under common contract law, the shareholders were non-signatories, they contest the Bylaw, and it was procured by fraud. Thus, this Bylaw must be found invalid.

II. Even if the Forum Bylaw is found to be legally valid, this Court should find that it is inequitable as a matter of law. The business-judgment rule does not protect the Directors because of the adoption's fraudulent undertones. When viewed under either enhanced judicial

scrutiny or strict scrutiny, the Forum Bylaw does not pass equitable muster and is invalid as a matter of law.

III. Finally, this Court should find that the Southern District of Texas is the appropriate forum to hear both the federal and the derivative claims under both the *McWane* doctrine and traditional forum non conveniens.

STANDARD OF REVIEW

In reviewing the “validity and fairness” of the Forum Bylaw, this Court faces a “mixed question of law and fact.” *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985). This Court must reverse the lower court’s findings if they “are clearly wrong and the doing of justice requires their overturn.” *Id.* Because justice requires that the proper forum for both claims is Texas, this Court should find Pinpoint’s Forum Bylaw invalid.

ARGUMENT

I. THE FORUM BYLAW IS NOT LEGALLY VALID UNDER EITHER DELAWARE GENERAL CORPORATE LAW OR COMMON LAW.

Question Presented

Even though Directors are authorized to unilaterally adopt bylaws, did the Court of Chancery err in finding the Exclusive Forum Bylaw valid when it was adopted during a fiduciary breach, improperly binding non-signatories?

Merits of Argument

The lower court’s contractual analysis upholding the Bylaw’s legal validity was erroneous due to the fiduciary implications of the director-shareholder relationship. Under Delaware General Corporate Law, directors are permitted to unilaterally adopt bylaws if

authorized by its certificate of incorporation. 8 Del. C. §109(a) (2010). Contract interpretation's general rules apply because bylaws are contracts between a corporation and its shareholders. *Centaur Partners, IV v. Nat'l Intergroup, Inc.*, 582 A.2d 923, 928 (Del. 1990).

A. Directors' unilateral adoption of the Bylaw impaired shareholders' contractual rights.

Shareholders' contractual rights are subject to a board's unilateral power to adopt bylaws; however, any adopted bylaw must be legal and permissible. 8 Del. C. §109(b); see *Kidsco, Inc. v. Dinsmore*, 674 A.2d 483, 492 (Del. Ch. 1995). Moreover, statutory power to adopt bylaws cannot give directors authority to destroy or impair contractual rights. *Salaman v. Nat'l Media Corp.*, 1992 Del. Super. LEXIS 564, at *17 (Del. Super. Ct. Oct. 8, 1992). Infringing upon a shareholder's "right to pursue effective enforcement of the fiduciary duties owed to them" is highly questionable. Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 Del. J. Corp. L. 57, 133 (2009).

This Court has not specifically addressed whether it is permissible for a board to unilaterally adopt an exclusive forum selection bylaw. Yet, this Court has held that directors cannot use their positions of trust as a mechanism to further their own interests. *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939). Shareholders consent to unilateral governance within the confines of a fiduciary relationship, understanding that a director will act in a corporation's best interest. *Stroud v. Grace*, 606 A.2d 75, 84 n. 1 (Del. Super. Ct. 1992); see 8 Del. C. §109(b). If seeking shareholder action, directors have a fiduciary obligation to fully and fairly

disclose any material information. *Stroud*, 606 A.2d at 84. Although disclosure is typically associated with shareholder voting and proxy solicitation, *Stroud* acknowledged that disclosure could be applicable outside of its statutory mandates. *Id.*

The lower court relied separately on both Delaware General Corporate Law and common contract law in its decision to uphold the adopted Bylaw. (Op. 14, 15.) The court reasoned that directors are permitted to adopt bylaws and forum selection clauses are prima facie valid; therefore, the Bylaw bound the shareholders. (Op. 14, 15.) However, this fusion of principles is impermissible in the instant case because the Bylaw adoption resulted from a fiduciary breach.

B. The Forum Bylaw is legally invalid and does not bind the non-signatory shareholders.

Under Delaware common law, a contractual forum clause is “presumptively valid” and will control. *Simm Assocs. v. PNC Nat’l Bank*, 1998 Del. Super. LEXIS 444, at *8 (Del. Super. Ct. Oct. 8, 1998) (citing *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972)). Forum selection clauses will only bind non-signatories if the forum selection clause is valid, the non-signatories and the contract are closely related, and the claim arises from and relates to the agreement. *Baker v. Impact Holding, Inc.*, 2010 Del. Ch. LEXIS 111, at *11 (Del. Ch. Jan. 28, 2010). These prerequisites must be satisfied for the bylaw to bind the shareholders. *Id.*

1. In this case, two of the three prerequisites are unsatisfied; thus, the Bylaw does not bind the shareholders.

Although “presumptively valid” and “regularly enforced,” a forum selection clause is unenforceable if proved that it resulted from

fraud. *Id.* Fraud occurs when a party overtly misrepresents facts, deliberately conceals material information, or remains silent "in the face of a duty to speak." *Nicolet, Inc. v. Nutt*, 525 A.2d 146, 149 (Del. 1987). The duty of disclosure "is a derivative of the duties of care and loyalty." *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1166 (Del. 1995).

In this matter, Mr. Miller's federal securities claim stems from Directors' failure to timely disclose the violations and investigation. (Op. 7.) Failing to disclose material information financially harmed Pinpoint and its shareholders. (Op. 7.) Additionally, the Bylaw was adopted in June 2010, concurrent to the breach of Directors' duty of oversight. (Op. 2.) Directors' failure to timely release material information "in the face of a duty to speak" demonstrates their lack of discretion and unfaithfulness to the shareholders. *Nicolet, Inc.*, 525 A.2d at 149. This silence indicates that the Forum Bylaw was adopted under fraudulent conditions and is invalid.

Additionally, Mr. Miller's claims do not stem from the Bylaws. While the Bylaws govern the fiduciary relationship between Pinpoint's Directors and shareholders, the derivative suit is based on Directors' fiduciary breach of oversight and not a provision of the Bylaws. (Op. 7.) Generally, Mr. Miller is a shareholder and is bound by Pinpoint's Bylaws; yet, this is insufficient to bind him to the legally invalid Forum Bylaw. *Weygandt v. Weco, LLC*, 2009 Del. Ch. LEXIS 87, at *14 (Del. Ch. May 14, 2009). Pinpoint's Forum Bylaw was procured by reason of fraud, and the derivative cause of action does not extend

from the Bylaw. The Forum Bylaw is legally invalid as a matter of law; thus, neither Miller, nor any other non-signatories, should be bound.

2. Corporate law restrictions bind the Directors.

Although the Court of Chancery recently suggested in dicta that corporations are free to adopt exclusive forums for dispute resolution, it was suggested in the context of charter provisions. *In re Revlon S'holders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010). Directors assert that this Court has bound a non-signatory to a contested forum selection clause in an LLC agreement, but Pinpoint is not an LLC. *Elf Atochem N. Am. v. Jaffari*, 727 A.2d 286 (Del. 1999). An LLC is flexible and allows members to govern their relationships through substantial contractual freedom. *Id.* at 290. Delaware's policy behind LLC agreements "is to give the maximum effect to the principle of freedom of contract." *Id.* at 295. Conversely, "corporate law limits contractual freedom by imposing certain mandatory rules." Sara Lewis, *Transforming the "Anywhere by Chancery" Problem into the "Nowhere by Chancery" Solution*, 14 Stan. J.L. Bus. & Fin. 199, 208 (2008). The relationship between a corporation's directors and shareholders is fiduciary, not strictly contractual. *Id.* Concealing the fiduciary breach of oversight and adopting a forum clause adverse to the shareholders' interests was fraudulent under this Court's precedent. *See Nicolet, Inc.*, 525 A.2d at 149. Therefore, the Forum Bylaw is not legally valid.

II. EVEN IF THIS COURT FINDS THAT THE ADOPTED BYLAW IS LEGALLY VALID, THE BYLAW IS INVALID AS A MATTER OF EQUITY; THUS, PINPOINT CANNOT ENFORCE THE FORUM CLAUSE UPON ITS SHAREHOLDERS.

Question Presented

If the Forum Bylaw is legally valid, did the Court of Chancery err in refusing to review the Forum Bylaw's equitable considerations under enhanced judicial scrutiny or strict scrutiny?

Merits of Argument

The Directors are fiduciaries, and, as such, owe its shareholders, including Mr. Miller, a duty of care and a duty of loyalty. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 367 (Del. 1993). A director's fiduciary duties to "protect the interests of the corporation and to act in the best interests of its shareholders" are "unyielding." *Id.* at 360. A plaintiff alleging that a director breached his fiduciary duties bears the burden of proof and must overcome the business-judgment rule. *Cinerama, Inc.*, 663 A.2d at 1162. The business-judgment rule essentially shields the Directors' decisions from the court's scrutiny and presents a high, but attainable, burden for the plaintiff. *Id.* Yet, the business-judgment rule may be defeated by "providing evidence that the board of directors . . . breached any one of its triad of fiduciary duties: good faith, loyalty, or due care." *Id.* at 1164.

This Court has recognized the duty of loyalty as a "mandate," in which "the best interest of the corporation and its shareholders takes precedent over any interest possessed by a director . . . not shared by the shareholders generally." *Cede & Co.*, 634 A.2d at 361. Evidence that a director acted self-interestedly, coupled with

evidence of a director's disloyalty, sufficiently establishes a breach of his duty of loyalty. *Id.* at 363. Moreover, a director's decision demonstrating self-dealing will be precluded from seeking business-judgment rule protections and must be subject to strict scrutiny under the entire fairness test or enhanced judicial scrutiny.

A. The unilateral adoption of the Bylaw was within Directors' specter of self-interest; thus, it must be reviewed with enhanced judicial scrutiny.

Adopting the Forum Bylaw is subject to enhanced judicial scrutiny because it was a defensive device adopted for the purpose of entrenching the directors in office. *In re Gaylord Container Corp. S'holders Litig.*, 1996 Del. Ch. LEXIS 149, at *6 (Del. Ch. Dec. 19, 1996). A court must review a director's self-interested action with enhanced judicial scrutiny before applying the business-judgment rule. *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1373 (Del. 1995); see *Unocal, Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 957 (Del. 1985).

If demonstrated with factual support that a director breached his fiduciary duty, the business-judgment rule will not protect the director. *Williams v. Geier*, 671 A.2d 1368, 1378 (Del. 1996). If a director's action is defensive, unilateral, and the shareholder challenges the action and seeks to restrain enforcement, it will be subject to enhanced judicial scrutiny. See *Stroud*, 606 A.2d at 82; *Williams*, 671 A.2d at 1377; *Unitrin, Inc.*, 651 A.2d at 1374.

1. Directors' adoption of the Forum Bylaw evidences a defensive measure to combat a breach of their duty of oversight.

"Corporate Directors have a fiduciary duty to act in the best interest of the corporation's stockholders." *Unocol, Corp.*, 493 A.2d at 955. When corporate directors' control is threatened, any response

implicates an inevitable conflict of interest. *In re Gaylord*, 1996 Del. Ch. LEXIS 149, at *7. If the circumstances surrounding a director's action raise an inference of a fiduciary breach, and the shareholders' complaint challenges the decision, the court must review it with enhanced judicial scrutiny. *Id.* at *8.

Whether a device is defensive is fact-specific, dependent upon the timing and circumstances surrounding the adoption. *Unitrin, Inc.*, 651 A.2d at 1372; see *Stroud*, 606 A.2d at 75. While stockholders cannot simply rely on conclusive contentions and their allegations must have some factual support, *Williams*, 671 A.2d at 1328, allegations will be sufficient if they fairly support an "inference of improper purpose." *In re Gaylord*, 1996 Del. Ch. LEXIS 149, at *10. A showing of bad faith is essential to establish director oversight liability. *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).

A director fails to act in good faith if he consciously disregards his duties and "intentionally fails to act in the face of a known duty to act." *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 67 (Del. 2006). If directors and senior officers have no reason to suspect deceptive practices, they cannot be liable for merely trusting their employee's integrity. *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996). In order to satisfy their responsibilities, a corporation's reporting system must timely alert the board with operational information. *Id.* at 970. In cases where corporate liability results from employee misconduct, directors will be liable if they lacked good faith in monitoring operations and continually failed to exercise oversight. *Id.* at 971.

The facts surrounding the Bylaw's adoption support a fair inference that it was adopted for an improper purpose. *Stone*, 911 A.2d at 370. Pinpoint's CEO, CFO, and President all served as Directors and were responsible for monitoring and overseeing day-to-day operations. (Op. 5.) Beginning in early 2009, Pinpoint improperly cut costs and defrauded the government in its omission of requisite tests. (Op. 5.) In the midst of this fraudulent activity, Directors adopted the Forum Bylaw, effectively limiting derivative suits to Delaware. (Op. 2.) This adoption was defensive because Directors were breaching their fiduciary duty to the shareholders, aware of a possible looming derivative suit. (Op. 5.) A proper assumption is that in limiting the forum to Delaware, Directors relied on business-judgment rule protection. The Forum Bylaw served to entrench Directors in their respective positions.

Directors will assert that they were unaware of the fraudulent billing; however, the three inside Directors failed to monitor Pinpoint's system for nearly two years. (Op. 5.) This failure to monitor operations indicates a lack of good faith. *In re Walt Disney Co.*, 906 A.2d at 67. Furthermore, the Bylaw adoption in the midst of a breach supports an inference of improper purpose. *Nicolet, Inc.*, 525 A.2d at 149. This Court must review the Bylaw with enhanced judicial scrutiny because it was most likely adopted for defensive purposes, and the shareholders contest it.

2. The Forum Bylaw is not equitable when viewed under enhanced judicial scrutiny.

When reviewed under enhanced judicial scrutiny, the unilateral adoption of the Forum Bylaw was neither reasonable nor proportional.

Unitrin, Inc., 651 A.2d at 1373. The adoption is unreasonable because Directors did not have "reasonable grounds for believing that a danger to corporate policy and effectiveness existed." *Unocol, Corp.*, 493 A.2d at 954. Reasonable grounds garnering protection of the business-judgment rule require good faith and reasonable investigation. *Id.*

Directors did not have reasonable grounds in adopting the Bylaw because no corporate threat existed. *Unocol, Corp.*, 493 A.2d at 955. When looking to the facts, Directors chose to restrict derivative actions to Delaware knowing that a derivative suit was looming. Yet, reasonable perception of a derivative lawsuit is not a threat to corporate policy. Directors unreasonably attempted to remedy the pending litigation with the Forum Bylaw. This Court should infer that the Directors' perceived threat was personal, and the remedy was self-serving.

Additionally, "a majority of outside independent directors" evidences reasonableness and good faith but is not conclusive. *Unitrin, Inc.*, 651 A.2d at 1375. This Court has found that a presence of ten or more outside directors was sufficient to satisfy the reasonable and good faith burden. See *Paramount Commc'ns, Inc. v. Time, Inc.*, 571 A.2d 1140 (Del. 1989) (12 of 16 directors were independent.); *Polk v. Good*, 507 A.2d 531 (Del. 1986) ("the presence of 10 outside directors . . . constitute[d] prima facie evidence of good faith and reasonable investigation"). In this case, four of Pinpoint's seven Directors were independent; however, the three interested Directors were serving Pinpoint in the highest positions available - CEO, CFO, and President. (Op. 5.) Adopting the Bylaw was

in response to a perceived a threat to their corporate positions and not on behalf of the shareholders. Because they acted self-interestedly and unreasonably, the adoption of the Forum Bylaw is inequitable when viewed under enhanced judicial scrutiny.

B. Under the entire fairness test of strict scrutiny, Directors cannot prove the objective fairness of the Bylaw adoption.

Pinpoint's adoption of the Bylaw fails enhanced judicial scrutiny; consequently, it cannot effectively survive strict scrutiny under the entire fairness test. Under this test, once the plaintiff successfully overcomes the presumption of the business-judgment rule, "the burden shifts to the defendant . . . to prove to the trier of fact the 'entire fairness' of the transaction to the shareholder plaintiff." *Cinerama, Inc.*, 663 A.2d at 1162. Directors must prove the objective fairness of the transaction; their subjective beliefs are irrelevant. *Gesoff v. IIC Indus.*, 902 A.2d 1130, 1144 (Del. Ch. 2006).

In applying the entire fairness test, courts look to several factors, including the transaction's timing, its initiation, negotiations surrounding the transaction, disclosure, and approval. *Venhill Ltd. P'ship v. Hillman*, 2008 Del. Ch. LEXIS 67, *76 (Del. Ch. June 3, 2008). The entire fairness test is "designed to assess whether a self-dealing transaction should be respected or set aside in equity." *Id.* at *66. Thus, it guards shareholders from directors' inequitable conduct "where the law's normal range of protections are insufficient." *Gesoff*, 902 A.2d at 1144.

In *Gesoff*, the Court of Chancery found the application of the business-judgment rule improper as to the directors' unilateral

imposition of the merger price on minority shareholders. *Id.* “[T]he process [was] entirely suffused with [the directors’] coercive power,” thus, applying the business-judgment rule would have further promoted the directors’ self-interest over shareholders’ protests. *Id.*

Additionally, directors that orchestrated and negotiated a recapitalization transaction were enjoined from doing so after a court found that the directors’ conduct evidenced a fiduciary breach. *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103 (Del. Ch. 1986). The court employed the entire fairness test because the transaction was “designed and effective to deprive shareholders of effective choice [and] to entrench the existing Board.” *Id.* at 105.

In the instant case, Directors’ conduct must be subjected to the heightened scrutiny of the entire fairness test. The unilateral adoption of the Forum Bylaw demonstrates a breach of their duty of loyalty. First, the Bylaw mandates shareholders to litigate derivative claims in Delaware, virtually extinguishing shareholders’ rights to choice of forum. Directors have usurped all control over litigation, precluding Pinpoint shareholders from exercising their rights in Pinpoint’s best interest. Directors have used their power to coerce the shareholders into the Delaware forum. Even though Pinpoint’s Board consisted of three inside Directors and four outside Directors, entrenchment can exist even where “a transaction creates a species of director interest even on the part of outside directors.” *Id.* at 115.

Despite the location of its headquarters, 8,000 employees, and business transactions in Houston, Texas, Directors have chosen the

inconvenience of the Delaware forum. The Bylaw adoption occurred simultaneously to Pinpoint's violations in its contracts with the military. With the threat of potential litigation arising, Directors made an apparent attempt to protect their positions on the Board by forcing all fiduciary claims to the Delaware forum in hopes of continued tenure.

Therefore, Directors' adoption of the Forum Bylaw should not be entitled to the business-judgment rule but must be subjected to the heightened scrutiny of the entire fairness test. Directors cannot show the Bylaw's objective fairness to Pinpoint shareholders because its adoption and enforcement demonstrates self-dealing, coercion, possible entrenchment, and a breach of the duty of loyalty.

III. BECAUSE THE FIRST COMPLAINT WAS FILED IN TEXAS, THIS COURT SHOULD GRANT THE STAY ACCORDING TO THE MCWANE DOCTRINE, AS ESTABLISHED AND IMPLEMENTED BY THE DELAWARE SUPREME COURT.

Question Presented

Under the *McWane* principle, did the Court of Chancery err in refusing to apply the first filed rule, enjoining Mr. Miller from litigating in the Southern District of Texas?

Merits of Argument

Delaware courts frequently utilize the *McWane* doctrine, also known as the first-filed rule, when a plaintiff filed a prior action in another court involving both the same parties and issues. *In re the Bear Stearns Cos., Inc. S'holder Litig.*, 2008 Del. Ch. LEXIS 46, at *15 (Del. Ch. Apr. 9, 2008). This Court in *McWane* held that "as a general rule, litigation should be confined to the forum in which it is first commenced." *McWane Cast Iron Pipe Corp. v. McDowell-Wellman*

Eng'g Co., 263 A.2d 281, 283 (Del. 1970). “[T]he first-filing plaintiff is rightly given primacy, assuming that her chosen forum is a convenient one.” *In re the Topps Co. S’holders Litig.*, 924 A.2d 951, 956 (Del. Ch. 2007). Accordingly, courts applying the *McWane* doctrine routinely grant a stay, which promotes judicial efficiency, consistent judgments, and comity between states’ courts. *In re the Bear Stearns Cos., Inc.*, 2008 Del. Ch. LEXIS 46, at *15.

Applying the *McWane* doctrine to the instant case conclusively establishes that this Court must grant the stay. The first derivative suit stemming from Directors’ fiduciary breaches was filed by Mr. Miller in the United States District Court for the Southern District of Texas, on December 1, 2010. (Op. 4.) Three other shareholders filed subsequent complaints in the Chancery Court of Delaware the next day; however, “their three complaints allege virtually the same derivative oversight claim that [Mr.] Miller asserted in the Federal Action.” (Op. 7.) Additionally, Mr. Miller is a lifelong resident of Houston, Texas. (Op. 4.) Likewise, Pinpoint’s headquarters is located in Houston, where it conducts all of its business and supervises its 8,000 employees. (Op. 4.) Texas is a convenient forum for Mr. Miller and Directors; it is not an unexpected forum for the other shareholders. Therefore, this Court should afford Mr. Miller’s Federal Action with the right of primacy according to the *McWane* doctrine.

A. This Court should refuse Directors’ argument that the *McWane* doctrine is inapplicable.

As an attempt to rebut the first-filed rule and deny Mr. Miller’s motion to stay, Directors will likely assert the court’s holding in

Topps, but *Topps* is distinguishable from the instant case. *In re the Topps Co.*, 924 A.2d at 951. The Chancery Court in *Topps* denied the Ohio plaintiff's motion to stay the litigation in Delaware in favor of New York; however, it is important to note that the court based its reasoning on the fact that the plaintiff was "not even a resident of the state in which he [sought] to litigate" - actually none of the plaintiffs involved were New York residents. *Id.* at 953. What is more, the court gave great deference to the fact that "stockholders invested on the understanding that Delaware law would govern their relations with the firm." *Id.* at 962. In its decision, the court explicitly stated, "in the end . . . the New York court has, to date, not stayed its hand in deference to this court, and the possibility for an unseemly and inefficient duplication of effort and for the production of inconsistent results therefore looms." *Id.* at 964.

Conversely to the plaintiffs in *Topps*, Mr. Miller is a domiciliary of Texas, the forum in which he first filed. Likewise, Directors, Pinpoint's headquarters, and employees are located in Texas. (Op. 4.) Furthermore, Mr. Miller was a Pinpoint employee for twenty years and currently owns 5,000 shares of Pinpoint stock, whereas each of the other shareholders in this derivative suit owns no more than 200 shares. (Op. 3.) Yet, similar to *Topps*, the court in the Federal Action has yet to rule on a partial stay in deference to this Court. (Op. 8.) Consequently, in applying the court's reasoning in *Topps* to the instant case, there is a "possibility for an unseemly and inefficient duplication of effort" and "inconsistent results." *In*

re the *Topps Co.*, 924 A.2d at 964. Therefore, this Court should grant the stay in deference to Mr. Miller's first filed action in Texas.

1. The McWane doctrine is applicable despite Directors' unilateral adoption of the Forum Bylaw.

Directors are mistaken in arguing that the forum clause overrides any *McWane* application. In determining forum, Delaware courts have asserted that the *McWane* doctrine is a common law default rule that may be discounted for cases in which "'both parties have agreed in advance to a forum.'" *Aveta, Inc. v. Delgado*, 942 A.2d 603, 607 (Del. Ch. 2008). Additionally, the first-filed rule is given less deference "when parties freely agreed that litigation should be conducted in another forum." *Healthtrio, Inc. v. Margules*, 2007 Del. Super. LEXIS 34, at *13 (Del. Super. Ct. Jan. 16, 2007).

Moreover, this Court in *Schnell* held that an "inequitable action does not become permissible simply because it is legally possible." *Schnell v. Chris-Craft Industries Inc.*, 285 A.2d 437, 439 (Del. 1971). In that case, the directors amended their bylaws and changed the date of the corporation's annual meeting in order to prevent dissident shareholders from seeking proxies, which would threaten the directors' tenure. *Id.* Although the directors had the legal authority to amend their bylaws, the court stated that the "management ha[d] attempted to utilize the corporate machinery and the Delaware Law for the purposes of perpetuating itself in office." *Id.* at 439.

Nevertheless, the foundation of Mr. Miller's argument is the unilateral adoption of the Bylaw. (Op. 10.) Mr. Miller and Directors never agreed to a forum prior to this derivative suit. Directors never provided Mr. Miller with the opportunity to freely agree to the

forum. The Bylaw was an attempt by the Directors to protect their position at Pinpoint, but it is inequitable to its shareholders. Thus, this Court should not uphold the inequitable Bylaw and dismiss the *McWane* doctrine as simply a common law default rule.

2. The internal affairs doctrine is irrelevant in determining choice of forum.

Directors assert that the stay should be denied based upon the internal affairs doctrine applicable to Delaware Corporate Law. In *Topps*, the court referred to the doctrine as a "principle which recognizes that only one state should have the authority to regulate a corporation's internal affairs." *In re the Topps Co.*, 924 A.2d at 958. Yet, the court confused the issue of choice of law and choice of forum, incorrectly treating both principles as identical.

The internal affairs doctrine is a "choice of law regime" and "does not provide anything like a blanket basis for Delaware keeping forum over Delaware corporate law claims." 34 Del. J. Corp. L. at 63. The United States Supreme Court expressed that although "the trial will involve issues which relate to the internal affairs," "there is no rule of law which requires dismissal of a suitor from a forum." *Koster v. (Am.) Lumbermens Mut. Cas. Co.*, 330 U.S. 518, 527 (1947). Simply stated, "choice of Delaware law does not mandate choice of Delaware forum" - the internal affairs doctrine is "neither dispositive of, nor even particularly meaningful to the resolution of forum disputes." 34 Del. J. Corp. L. at 63.

Directors' assertion that the internal affairs doctrine nullifies the *McWane* doctrine is incorrect, as the first-filed rule pertains to choice of forum and not choice of law. Therefore, the *McWane* doctrine

still applies to the present case, and this Court should grant the stay in favor of the Texas forum.

B. Even if this Court refuses to apply the *McWane* doctrine, it must grant the stay because Texas is the best choice of forum.

Delaware courts have referred to similar suits filed just days apart as contemporaneously filed and have used their discretion in not applying the first-filed rule. See *In re the Bear Stearns Cos.*, 2008 Del. Ch. LEXIS 46. Yet, even if this Court determines that Mr. Miller's action was contemporaneously filed with the Delaware suits, Mr. Miller's motion to stay must be granted.

"Where a Delaware and foreign state actions are essentially contemporaneously filed, the court . . . conducts a balancing of relevant considerations akin to the forum non conveniens analysis to determine whether the Delaware action should be stayed." *County of York Employees Retirement Plan v. Merrill Lynch & Co.*, 2008 Del. Ch. LEXIS 162, * 2 (Del. Ch. Oct. 28, 2008). According to traditional forum non conveniens, whether a Delaware court will grant a motion to stay depends on several factors such as the applicability of Delaware law, access to proof, availability of witnesses, similar pending actions in another jurisdiction, a need to view the premises, and considerations that promote an expeditious and inexpensive trial. *Id.* at *16. Additionally, "[d]uplicative proceedings are disfavored because they waste judicial and financial resources, and because the competing proceedings create . . . a potential for inconsistent rulings." *Id.* at *24.

In the present case, Texas encompasses Mr. Miller, Directors, Pinpoint headquarters, 8,000 employees, and all of Pinpoint's business

activity. Pinpoint's contracts, records, and files are located in Texas as well as potential witnesses. Additionally, Texas is the location where the Directors breached their fiduciary duties, failed in their duty of oversight, violated the terms of the military contracts, and defrauded the U.S. military. Directors "envision concurrent litigation" of Mr. Miller's claims in the state and federal courts. (Op. 8.) This dream presents an enormous conflict for judicial efficiency and contradicts the notion of expeditious and inexpensive litigation. The Federal Action involves the same parties and issues, and the court is capable of concurrently adjudicating the state and federal claims. In granting the stay, this Court would prevent inconsistent rulings, promote justice, and encourage comity between the courts.

In determining the forum in which justice would best be served, the United States Supreme Court explained, "the ultimate inquiry is where trial will best serve the convenience of the parties and the ends of justice." *Koster*, 330 U.S. at 527. The Court scrutinized businesses that choose to incorporate in a state "while every other activity is conducted far from [that] state" and held that the "domicile of a corporation whose activities are conducted elsewhere than in the chartering state may be entitled to little consideration." *Id.* at 528. The Court established that "judicial abstention in deference to the incorporating state is no longer the rule." 34 Del. J. Corp. L. at 80. Therefore, the United States Supreme Court does not support the belief that only Delaware courts can decide cases involving Delaware corporations. *Id.*

Although Pinpoint is incorporated in Delaware, the Delaware courts do not have automatic precedence over other forums. If this Court, in its discretion, refuses to apply the *McWane* doctrine, it must establish Texas as the appropriate forum in regards to the litigants based on a balance of justice and convenience.

CONCLUSION

The Chancery Court erred in concluding that the Forum Bylaw is valid and enforceable against Pinpoint shareholders. Because Directors usurped control over litigation, precluding shareholders' choice of forum, the Forum Bylaw is legally and equitable invalid.

Furthermore, the Chancery Court erred in denying the stay and granting the injunction. This Court should give Mr. Miller's first-filed Federal Action primacy, in consideration of efficiency, convenience, and consistent outcomes. Therefore, this Court should grant the stay and dismiss the injunction.

Respectfully Submitted

/s/ J

Counsel for Appellant