#### IN THE SUPREME COURT OF THE STATE OF DELAWARE

EDWARD MILLER,	)	
EDWIND FILEBOX,	)	
Plaintiff Below-	)	
Appellant,	)	
	)	
V •	)	No. 17, 2011
	)	
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
	)	
and	)	Civil Action No. 4958-VCM
	)	
PINPOINT BEARINGS, INC.,	)	
	)	
Nominal Defendant Below-	)	
Appellee.	)	

### Appellees' Opening Brief

Filed By: Team Q Counsel for Appellee February 11, 2011

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#### NATURE OF PROCEEDINGS

In this interlocutory appeal plaintiff Edward Miller ("Miller") challenges the Court of Chancery's January 12, 2011 Opinion and Order. Miller's litigation against Pinpoint Bearings, Inc. ("Pinpoint") began on December 1, 2010, when Miller filed a derivative action against the Board in U. S. District Court for the Southern District of Texas (the "Federal Action"). The next day, Plaintiffs Webb, Patrick and Kohn filed complaints in Delaware state court mirroring Miller's claims. On December 8, 2010, the Court of Chancery consolidated the Delaware actions.

On December 15, 2010, Miller filed a complaint and two motions in Delaware court. The complaint alleged the same claims as in the Federal Action. One motion was a Motion to Consolidate with the other Delaware actions, while the second motion asked the court to stay all fiduciary litigation in Delaware in favor of the Federal Action. Both the Board as defendants and Pinpoint as a nominal defendant opposed Miller's Motion to Stay, and in response, moved for an injunction barring Miller from prosecuting any derivative or other fiduciary claims in any forum other than Delaware.

In its January 12, 2011 Opinion, the Court of Chancery granted Miller's Motion to Consolidate, but also granted the defendants' Motion to Enjoin Miller's Federal Action. After the ruling Miller began the process for an interlocutory appeal. The Court of Chancery granted Miller's application for certification for interlocutory appeal in an Order dated January 14, 2011. This Court accepted Miller's interlocutory appeal in an Order dated January 18, 2011.

#### SUMMARY OF THE ARGUMENT

- 1. Delaware law affords great deference to a board's ability to effectively manage corporate resources. This case seeks to undermine that ability -- where a stockholder refuses to recognize a valid forum selection clause (the "Bylaw") that benefits the corporation and stockholders alike.
- 2. Bylaws and forum selection provisions carry a heavy presumption of validity. To prove the Bylaw is invalid Miller must overcome this heavy burden. Miller's claim fails because the forum Bylaw is valid and enforceable; the Bylaw is also enforceable on equitable grounds.
- 3. First, the Bylaw is valid because the Board had the legal authority to adopt it. Additionally, forum selection clauses are appropriate in bylaws because they relate to stockholders' rights to file lawsuits. Additionally, because no stockholders had initiated suit prior to the Bylaw's adoption, no stockholders held a vested right to rely on the pre-amended bylaw language. Second, the Bylaw is enforceable because the forum clause is reasonable. The clause does not seriously prohibit Miller from his day in court, the main consideration in evaluating the reasonableness of bylaws.

  Additionally, the provision does not contravene Delaware public policy. In fact, Delaware public policy strongly supports having its courts deal with Delaware-chartered corporate disputes.
- 4. Turning to the equitable considerations, courts typically apply one of three judicial standards of review: the traditional business rule, the <u>Unocal</u> standard, or the entire fairness test. Courts employ the business judgment rule unless a plaintiff can rebut its heavy

presumption of validity. Because Miller fails to successfully rebut that presumption, this Court should apply the business judgment rule.

- 5. Under the business judgment rule, this Court should uphold and enforce the Bylaw because the Board adopted it for a rational purpose. Primarily, the Board sought to increase Pinpoint's efficiency, convenience and the relative predictability of litigation involving the corporation.
- 6. Even under the <u>Unocal</u> standard or the entire fairness test,
  Miller's claim fails. It fails under <u>Unocal</u> because the Board
  reasonably believed Pinpoint's policy and effectiveness were
  threatened and the Board's adoption of the Bylaw was reasonable in
  relation to the perceived threat. Under the entire fairness test
  Miller's claim fails because the Bylaw was entirely fair. The Bylaw
  was entirely fair because it provided benefits to all stockholders, by
  increasing the corporation's economic and financial benefits.
- 7. Delaware has worked hard to build a solid corporate law foundation. Allowing a stockholder to fracture that foundation simply because he seeks a more convenient forum is a step in the wrong direction. Thus, this Court must affirm because corporate boards need the authority to manage business resources effectively.

#### STATEMENT OF FACTS

On June 10, 2010, defendants, directors (the "Board") of nominal defendant Pinpoint, adopted an exclusive forum bylaw making Delaware the exclusive forum for any derivative action or other claim for breach of fiduciary duty. R. 2. Pinpoint is a Delaware corporation that manufactures highly engineered precision roller and ball bearings for aerospace application. R. 4. Its principal customers are the U.S. military and commercial aircraft manufacturers. R. 4.

Several months after the Bylaw adoption, in early September 2010, a Pinpoint engineer contacted the U.S. Inspector General's office (the "OIG") on concerns that three mid-level managers might be improperly omitting product testing required by Pinpoint's U.S. military contracts. R. 5. A week later, on September 8, 2010, the OIG notified Pinpoint of its intent to investigate the allegations. R. 6.

Immediately, the Board launched its own independent investigation into the claims. R. 6. The Board discovered a pattern of improper and undisclosed cost-cutting steps that mid-level managers took on a number of government contracts. R. 6. Recognizing the validity of the complaint and the importance of the military contracts, the Board negotiated a settlement between the company and OIG. R. 6. The settlement, finalized on November 30, 2010, allowed Pinpoint to keep its important military contracts. R. 6. That same day Pinpoint issued a press release disclosing the terms of the settlement. R. 6-7. Immediately following the press release, Miller filed his derivative action in Texas Federal Court. R. 6-7.

#### ARGUMENT

#### QUESTIONS PRESENTED

- I. Under Delaware corporate law, is Pinpoint's forum selection clause valid and enforceable, (1) when the Board adopted it pursuant to its legal authority without abridging stockholders' vested rights; and (2) when the forum selection clause neither seriously impairs Miller's ability to pursue his cause of action nor contravenes Delaware public policy?
- II. Under Delaware law, should the Court uphold and enforce the Bylaw, when the Board adopted it in the best interest of Pinpoint's stockholders?

#### SCOPE OF REVIEW

This Court analyzes Court of Chancery decisions involving questions of law de novo. Kahn v. Lynch Commc'n Sys., 669 A.2d 79, 84 (Del. 1995). This Court has also held that interpretation of bylaws is a question of law. Centaur Partners, IV v. Nat'l Intergroup, Inc., 582 A.2d 923, 926 (Del. 1990). Accordingly, this Court should analyze the Court of Chancery's interpretation of Pinpoint's Bylaw under the de novo standard of review.

#### MERIT OF ARGUMENT

I. Pinpoint Bearing Inc.'s forum selection clause is valid and enforceable because the Board had the authority to adopt it and because the provision is both reasonable and consistent with Delaware public policy.

Corporate bylaws carry a strong presumption of validity. Frantz Mfg. Co. v. EAC Indus., 501 A.2d 401, 407 (Del. 1985). Pinpoint's forum selection Bylaw is valid because Pinpoint's charter expressly empowered the Board to make changes to its Bylaws without stockholder approval. The Board acted within both the authority of Delaware law and Pinpoint's Charter. Thus, the forum provision is valid.

Forum selection clauses also carry a presumption of validity.

M/S Bremen v. Zapata Off-Shore Co., 407 U.S. 1, 9-10 (1972). Parties seeking to overturn a forum selection clause face a "heavy burden of proof." Carnival Cruise Lines, Inc. v. Shute, 499 U.S. 585, 595 (1991). Pinpoint's forum provision is enforceable because it is reasonable and does not deny stockholders the ability to pursue their causes of action. Furthermore, the Bylaw supports Delaware public policy. Thus, the Bylaw is enforceable.

### A. Pinpoint's forum selection clause is valid because the Board had the authority to adopt it.

Bylaws are valid when a board adopts them: (1) under the proper authority; (2) in the proper internal document and; (3) while preserving stockholders' vested rights. 8 Del. C. § 109(a)-(b); CA, Inc. v. AFSCME Emps. Pension Plan, 953 A.2d 227, 235 (Del. 2008); Schoon v. Troy Corp., 948 A.2d 1157, 1165 (Del. Ch. 2007). The Bylaw is valid because the Board adopted it under the proper authority of Pinpoint's Bylaws and Delaware law; the exclusive forum provision is appropriate as a bylaw; and it preserves stockholders' vested rights.

### 1. The Bylaw is valid because the Board adopted it under the proper authority of Pinpoint's Bylaws and Delaware law.

A corporation can adopt any bylaw that relates to a board's rights and authority. 8 Del. C. § 109(a)-(b). Bylaws can confer boards with the authority to change the bylaws unilaterally. Id. at § 109(a). If a board has the authority to adopt a bylaw unilaterally, the board can adopt any bylaw "relating to ... the rights or powers of its [stockholders]." Id. at § 109(b).

Here, the Board adopted the Bylaw under the proper authority of the Pinpoint's Bylaws and Delaware law. Pinpoint can adopt any bylaw that relates to the Board's rights and authority. ARTICLE 14 of Pinpoint's Bylaws relates to the Board's power by conferring the Board with the authority to change the Bylaws unilaterally. Having the authority to adopt a bylaw unilaterally, the Board properly adopted the Bylaw because it relates to the rights of Pinpoint's stockholders regarding litigation involving the corporation. Therefore, the Board adopted the Bylaw under the proper authority of Pinpoint's Bylaws and Delaware law.

## 2. The Bylaw is valid because the exclusive forum provision is appropriate as a bylaw.

Bylaws are procedural; therefore, a provision should be procedural to be appropriate as a bylaw. CA, Inc. v. AFSCME Emps.

Pension Plan, 953 A.2d 227, 235 (Del. 2008). In CA, Inc., a board challenged a provision that would require the corporation to reimburse stockholders for certain board election expenses. Id. at 230. The board argued the provision was substantive because it mandated corporate spending and removed the decision from the board. Id. at 235-36. However, the Court disagreed, and held that even though the provision removed the board's decision, the provision was procedural because it only affected the procedure relating to elections and not the election results. Id. at 237. Because the provision was procedural, the provision was appropriate as a bylaw. Id. at 235.

Here, the exclusive forum provision is appropriate as a bylaw because it is procedural. Similar to the  $\underline{CA}$  provision that mandated corporate spending and removed the decision from the board, the

exclusive forum provision mandates all litigation occur in Delaware courts and removes that decision from stockholders. However, the exclusive forum provision is procedural because it only affects the procedure relating to litigation and not the substantive merits of that litigation, like the <u>CA</u> provision was procedural because it only affected the procedure relating to elections and not the election results. Because the exclusive forum provision is procedural, the provision is appropriate as a bylaw; therefore, the Bylaw is valid.

### 3. The Bylaw is valid because it preserves stockholders' vested rights.

Corporations can generally change stockholders' rights by amending its bylaws, but they cannot change a stockholders' vested rights. Schoon v. Troy Corp., 948 A.2d 1157, 1165 (Del. Ch. 2007). Stockholders only have vested rights if they detrimentally rely on a bylaw. Kidsco, Inc. v. Dinsmore, 674 A.2d 483, 492 (Del. Ch. 1995).

To detrimentally rely on a bylaw, stockholders must perfect their rights by benefitting from that bylaw. Salaman v. Nat'l Media, Corp., 1992 WL 808095 (Del. Supr. Oct. 8, 1992), at 2. National Media, Corp.'s bylaws mandated that it reimburse directors for litigation related to their jobs as directors. Id. In 1990, stockholders sued Salaman, a director, in federal court, alleging breach of oversight.

Id. at 2. Pursuant to the bylaws, National Media, Corp. regularly reimbursed him for his expenses, however, during the course of the suit, National Media Corp. amended its bylaws, eliminating the mandatory provision for director reimbursement, and ceased the reimbursements. Id. at 4. Because Salaman had perfected his rights by receiving reimbursements, he detrimentally relied on the pre-amended

bylaw. Because Salaman had detrimentally relied on the pre-amended bylaw, he had vested rights that National Media Corp. could not change by amending its bylaws.

v. Berg, 2011 U.S. Dist. LEXIS 1626 (N.D. Cal. Jan. 3, 2011), at 1.

In <u>Galaviz</u>, a company unilaterally adopted an exclusive forum bylaw before stockholders filed a derivative claim in a foreign jurisdiction. <u>Id.</u> at 1-2. The California court expressed concern about a board's ability to unilaterally change bylaws. <u>Id.</u> at 4. The court held that contract law did not allow unilateral changes to a contract under these circumstances. <u>Id.</u> at 4. However, the court failed to acknowledge that the stockholders did not rely on the preamendment provision; they did not file suit before the board passed the bylaw. That court went against the settled Delaware principal that it takes more than stock ownership to created a vested right.

The Board did not interfere with stockholders' vested rights.

The Salaman court reasoned that Salaman's right to reimbursement vested as soon as stockholders brought suit because he then relied on the pre-amended provision throughout the litigation. If stockholders had brought suit before Pinpoint's Board amended the Bylaw, this Court would likely hold that the stockholders had a right to rely on pre-amended bylaw language.

However, not only did no stockholder file suit against the Board under the pre-amended bylaw, but also the government had not even begun its investigation into the allegations. The <u>Salaman</u> decision is noteworthy because of when it determined the right vested; it vested

at the time of suit and not at the time of wrong doing. Pinpoint stockholders need something more than ownership of stock before the Board amended the Bylaw.

The recent <u>Galaviz</u> decision further supports Delaware public policy supporting Delaware courts hearing Delaware corporation disputes. <u>Infra</u> Part II.B. The facts in <u>Galaviz</u> are similar to the facts at issue before this Court; both boards adopted forum selection clauses before stockholders relied on pre-amendment bylaw provisions. Subsequently, stockholders of both corporations filed suits in forums other than Delaware. However, whereas Delaware corporate law is well settled on the issue of when rights vest, the California court ignored the vested rights issue and inexplicably ruled in favor of the stockholders. The California court misses the point -- Because stockholders did not rely on the pre-amendment bylaw, no rights vested. Thus, neither Oracle's nor Pinpoint's forum selection clause affects stockholders' vested rights.

B. Pinpoint's forum selection clause is enforceable because it allows for efficient and predictable justice, is strongly supported by Delaware public policy, and preserves stockholders' substantive rights.

Only claimants who can demonstrate a "strong showing" against forum selection clauses can effectively rebut the presumption of validity of forum selection clauses. M/S Bremen v. Zapata Off-Shore

Co., 407 U.S. 1, 9-10 (1972). In order to rebut the presumption,

claimants must satisfy the test set forth in Ingres Corp. v. CA, Inc.,

8 A.3d 1143, 1146 (Del. 2010). Claimants must prove that enforcement

would be: (1) unreasonable and unjust; (2) strongly against the public

policy of the state where the action commenced; (3) or that the clause is invalid for such reasons as fraud or overreaching." Id.

The Board reasonably adopted the forum selection clause in the name of efficient and predictable justice, which benefits both the corporation and stockholders alike. Plaintiffs cannot show the clause seriously impairs their ability to bring a cause of action.

Additionally, Delaware public policy supports forum selection clauses, thus adopting one would not contravene Delaware public policy.

Fraud or overreaching occurs when a party uses a position of trust to pursue a private interest. <u>Guth v. Loft, Inc.</u>, 5 A.2d 503, 510 (Del. 1939). Because the Board acted within the authority granted by Pinpoint's Charter, the Board in no way abused its position of interest. <u>Supra Part I.A.1</u>. Additionally, Section II of this brief vividly demonstrates that the board did not breach any fiduciary duties when it adopted the bylaw. <u>Infra Part II.B.</u> Thus, Pinpoint's forum selection clause is enforceable.

### 1. The forum selection clause was not unreasonable because it does not deprive plaintiffs of their day in court.

Forum selection clauses are unreasonable and unjust only when enforcement would "seriously impair the plaintiff's ability to pursue his cause of action." <u>Ingres</u>, 8 A.3d at 1146. Mere inconvenience or added expense does not equate to unreasonableness. <u>Carnival Cruise</u>
Lines, Inc. v. Shute, 499 U.S. 585, 595 (1991).

The party attempting to prove inconvenience faces a "heavy burden of proof." Id. at 589. Carnival Cruise Lines included a forum selection clause on passenger tickets, directing all litigation to Florida courts. Id. at 587. Carnival included the clause among three

paragraphs of small print on the back of each passenger ticket. <u>Id.</u> at 587. Shute, a passenger, filed suit in Washington after injuring herself during a cruise and Carnival moved to enforce the forum selection clause. <u>Id.</u> at 588. In gauging the reasonableness of the clause, the U.S. Supreme Court noted that Shute claimed both physical and financial hardships in traveling to Florida to bring her claims. <u>Id.</u> at 595. These hardships were not enough to meet the high burden of proof required by the reasonableness standard; the hardships did not seriously impair Shute's ability to pursue her claim. Id.

Furthermore, Carnival had several legitimate reasons to include a forum clause. <u>Id.</u> at 593. Carnival had a special interest in limiting the fora because cruise ships carry people from all over the country. <u>Id.</u> The clause saved resources of the judiciary and the litigants, which could mean reduced ticket prices for passengers. <u>Id.</u> at 593-94. These justifications outweighed the hardship alleged by the plaintiff; thus, Carnival's forum clause was reasonable. <u>Id.</u> at 595.

Here, Pinpoint's forum selection clause is reasonable because it does not seriously impair stockholders ability to bring causes of action. The Court in <u>Carnival</u> held that both physical and financial hardships were not enough to overcome the high burden of proving inconvenience. Here, plaintiffs are bringing a derivative suit, which imposes almost no inconvenience. None of the plaintiffs currently work for Pinpoint and none of the plaintiffs were witness to the alleged safety issues. Thus, plaintiffs are in not seriously impaired from bringing their cause of action.

Furthermore, Pinpoint has several legitimate reasons to enact its forum selection clause. Just as Carnival had an interest in limiting the fora, Pinpoint has the same interest. Carnival has tens of thousands of customers all over the United States; Pinpoint has tens of thousands of stockholders all over the United States. Naturally, limiting the fora avoids corporations to travel to jurisdictions across the country and defend itself against lawsuits. Additionally, Delaware courts mean efficient and predictable decisions, a benefit for both the corporation and its stockholders. Mandating Delaware as the forum of choice helps cut down on forum shopping; it also reduces the possibility of subjecting complex cases to foreign judges with limited knowledge of Delaware law. Infra Part I.B.2. Thus, like Carnival, Pinpoint proffers many valid, reasonable justifications for its forum selection clause. These justifications, plus the fact that the Bylaw does not deprive Miller of his day in court supports one conclusion; the Bylaw is reasonable.

2. Delaware public policy supports the idea that a corporation's chartering state courts should handle the corporation's disputes.

Forum provisions are unenforceable "when they contravene a strong public policy in the forum where the suit is brought." M/S Bremen v.

Zapata Off-Shore Co., 407 U.S. 1, 15 (1972). However, less than a year ago, in Baker v. Impact Holdings, Inc., a Delaware Court of Chancery held that forum selection clauses in stockholder agreements did not violate Delaware public policy. No. 4960-VCP, (New Castle Co., Del. Ch. May 13, 2010). Vice Chancellor Parsons concluded that "there is no statute or other clear indication of a legislative intent to limit

the scope of forum selection clauses with respect to corporations..."

Id. at 5.

Just three days later, Vice Chancellor Laster echoed similar sentiments in In re Revlon, Inc. S'holders Litig., 990 A.2d 940, 960 (Del. Ch. 2010). There, in responding to the idea that corporate boards could be exposed to lawsuits in multiple jurisdictions, Vice Chancellor Laster said, "if boards of directors and stockholders believe that a particular forum would provide an efficient and value-promoting locus for dispute resolution, then corporations are free to respond with charter provisions selecting an exclusive forum for intra-entity disputes." Id.

Additionally, Delaware public policy strongly supports that its state courts interpret Delaware corporate disputes. In re Topps Co. S'olders Litig., 924 A.2d 951, 959 (Del. Ch. 2007). In In re Topps, the New Castle Court of Chancery entertained a motion to dismiss or stay a derivative action designed to enjoin a merger. Id. at 592. The moving party sought to dismiss the action filed in Delaware, the chartering company's home state, in favor of trying the case in New York. Id. In denying the motion to stay the Delaware proceedings, the court detailed a multitude of reasons why Delaware courts should hear Delaware corporations' disputes. See Generally Id.

The court stated, "the chartering state [has] a powerful interest in ensuring the uniform interpretation and enforcement of its corporation law, so as to facilitate growth and efficiency." <a href="Id.">Id.</a> Also, Delaware courts are far more efficient than other jurisdictions because of their vast experience handling Delaware corporation law.

Id. at 953. The court added that new issues were of special concern to the state of incorporation. Id. In fact, Delaware courts have special mechanisms for handling new issues; litigants proffering new issues can request expedited and direct interlocutory appeal directly to the Delaware Supreme Court. Id. at 954. Not only does Delaware support forum selection clauses, it enthusiastically supports hearing Delaware corporation disputes.

Pinpoint's forum clause is in line with Delaware public policy.

Not only does Delaware avoid limiting the applicability of forum selection clauses, but Delaware also highly favors having its courts deal with issues related to Delaware-chartered corporations.

Additionally, the issue before this Court is a case of first impression in Delaware. In fact, this case is before this Court as a direct result of proprietary Delaware judicial rules expediting cases of first impression. It is imperative that this Court hear the issue in an efficient and predictable manner. Thus, Pinpoint's forum selection clause does not contravene Delaware public policy.

### II. This Court should uphold and enforce the Bylaw because the Board adopted it equitably.

To determine the equity of a Board's decision, courts typically apply one of three judicial standards of review: the traditional business judgment rule, the <u>Unocal</u> standard, or the entire fairness test. <u>Emerald Partners v. Berlin</u>, 787 A.2d 85, 89 (Del. 2001).

Courts apply the business judgment rule to protect corporations from unreasonable interference. <u>Cede & Co. v. Technicolor</u>, 634 A.2d 345, 360-61 (Del. 1994). In rare circumstances, courts will apply an

enhanced judicial review, known as the <u>Unocal</u> standard, before applying the protective business judgment rule. <u>Paramount Commc'ns</u>, <u>Inc. v. QVC Network</u>, <u>Inc.</u>, 637 A.2d 34, 42 (Del. 1994). Finally, courts only scrutinize a board's decision under the entire fairness test if a plaintiff rebuts the business judgment rule's strong presumption. Cede & Co., 634 A.2d at 361.

A. This Court should apply the business judgment rule because the Bylaw was not a defensive measure that involved a perceived threat to corporate control and Miller cannot rebut the business judgment rule's strong presumption.

Courts apply the business judgment rule to protect corporations from second-guessing the merits and wisdom of a board's decision and unreasonably interfering with the corporation's affairs. Cede & Co., 634 A.2d at 360-61. The business judgment rule is a strong presumption that a board "acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interest of the company." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984). Procedurally, the rule places a heavy burden on plaintiffs to rebut its strong presumption before a court will scrutinize a board's decision. Emerald Partners, 787 A.2d at 90-91.

In rare circumstances, courts will apply an enhanced judicial review before applying the protective business judgment rule. QVC

Network, Inc., 637 A.2d at 42. Enhanced judicial review, known as the Unocal standard, only applies to cases where a board unilaterally adopts a defensive measure against a perceived threat to corporate control. Williams v. Geier, 671 A.2d 1368, 1377 (Del. 1996). This Court created the Unocal standard during the hostile takeover era of the 1980's because it recognized that boards could act in its own

self-interest and violate fiduciary duties during contests for corporate control. Id. at 1377; Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985). Courts apply the Unocal standard to defensive measures relating to corporate control to ensure that boards do not unreasonably dilute or obstruct stockholders' voting rights under the guise of a defensive measure. QVC Network, Inc., 637 A.2d at 42.

Courts only scrutinize a board's decision under the entire fairness test if a plaintiff rebuts the business judgment rule's strong presumption. Cede & Co., 634 A.2d at 361. To rebut the rule's presumption, a plaintiff must provide sufficient evidence that a board, in making the challenged decision, breached a fiduciary duty.

Id. A board has a fiduciary duty of loyalty and breaches that duty by making a decision in its own self-interest. Id. A board acts in its own self-interest if the challenged decision exclusively benefits the board and the benefit is materially significant. Id. at 362-63; Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. (1989).

A benefit is materially significant if it is likely to influence a board to disregard its fiduciary duties to pursue that benefit. <u>In re Gen. Motors Class H S'holders Litig.</u>, 734 A.2d 611, 617 (Del. Ch. 1999). In <u>Grover v. Simmons</u>, 642 A.2d 792, 798 (Del. Ch. 1993), a board negotiated and received full indemnification as part of a merger agreement. The court held that even if indemnification was considered to exclusively benefit the board, it was not likely influence the board to disregard its fiduciary duties because it was commonplace in corporate affairs and the board retained substantive liability for all

duty of loyalty claims under Delaware law; therefore, the benefit was not materially significant. <u>Id.</u> at 804-05. Because the board did not receive a benefit that was materially significant, the board did not act in its own self-interest. <u>Id.</u> Therefore, the board did not breach its fiduciary duty of loyalty and the court did not apply the entire fairness test. Id.

Here, the Court should apply the protective business judgment rule to avoid second-guessing the merits and wisdom of the Board's adoption of the Bylaw and unreasonably interfering with Pinpoint's affairs. The rule should protect the Board because in adopting the Bylaw, the Court presumes the Board "acted on an informed basis, in good faith and in the best interest of the company." Aronson, 473 A.2d at 812. Procedurally, the rule places a heavy burden on Miller to rebut this presumption before the Court will scrutinize the Board's decision.

The Court should not apply the <u>Unocal</u> standard before applying the protective business judgment rule because even though the Bylaw was adopted unilaterally, it is not a defensive measure and did not involve a perceived threat to corporate control. The Bylaw is not a defensive measure because it preserved all the substantive rights of litigants. The only threats the Board perceived were inefficiency, inconvenience, and relative unpredictability; not the loss of the Board's corporate control. Furthermore, the Bylaw in no way diluted or obstructed stockholders' voting rights. Therefore, the Court should not apply the <u>Unocal</u> standard before applying the protective business judgment rule.

The Court should not scrutinize the Board's decision to adopt the Bylaw under the entire fairness test because Miller cannot rebut the business judgment rule's presumption. Miller provides no evidence that the Board, by adopting the Bylaw, breached a fiduciary duty. The Board did not breach the fiduciary duty of loyalty because the Board did not act in its own self-interest. The Board did not act in its own self-interest because the adoption of the Bylaw did not exclusively benefit the Board. The Bylaw benefited the entire corporation equally by providing efficiency, convenience, and relative predictability in litigation involving the corporation. The reduced cost associated with these benefits would increase the corporation's overall profit, which would in turn be shared equally by the stockholders. Because the Bylaw's benefits would be shared equally by the stockholders, the Bylaw did not exclusively benefit the Board.

Alternatively, the Board did not act in its own self interest because the benefit is not materially significant. The benefit is not materially significant because it is not likely to influence the Board to disregard its fiduciary duties. Similar to the indemnification in Grover, exclusive forum bylaws are commonplace in corporate affairs. Following the Revlon decision, several corporations, including Pinpoint, adopted exclusive forum bylaws. Furthermore, like the board in Grover, the Board here retained all substantive liability. Delaware courts will certainly adjudicate all claims of substantive liability against the Board justly, without providing the Board increased leniency. Because exclusive forum bylaws are commonplace in corporate affairs, and the Board retained all substantive liability,

the benefit is not likely to influence the Board to disregard its fiduciary duties; therefore, the benefit is not materially significant.

Because the Bylaw did not exclusively benefit the Board, or alternatively, the benefit was not materially significant, the Board did not act in its own self-interest; therefore, the Board did not breach the fiduciary duty of loyalty. Because the Board did not breach a fiduciary duty, Miller cannot rebut the business judgment rule's strong presumption; therefore, the court should not scrutinize the Board's decision to adopt the bylaw under the entire fairness test. Because neither the <u>Unocal</u> standard nor the entire fairness test apply, the Court should apply the protective business judgment rule to avoid second-guessing the merits and wisdom of the Board's adoption of the Bylaw and unreasonably interfering with Pinpoint's

# B. While the Court should apply the business judgment rule, the Court should uphold and enforce the Bylaw regardless of which test the Court applies.

The determination of which test to apply is often outcomedeterminative because the presumption of the business judgment rule is so strong whereas the scrutiny of the entire fairness test is so exacting. Nixon v. Blackwell, 626 A.2d 1366, 1376 (Del. 1993).

However, in this case, the Court should uphold the Bylaw regardless of which test the Court applies: the business judgment rule because the Board adopted the bylaw for a rational purpose; the Unocal standard because the Board reasonably believed Pinpoint's policy and effectiveness was threatened and the Board's adoption of the Bylaw was

reasonable in relation to the perceived threat; and the entire fairness test because it was entirely fair to Pinpoint's stockholders.

1. Under the business judgment rule, the Court should uphold and enforce the Bylaw because the Board adopted the bylaw for a rational purpose.

The business judgment rule is a strong presumption that a board "acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interest of the company."

Aronson, 473 A.2d at 812. Substantively, the business judgment rule protects corporations from courts second-guessing the merits and wisdom of a board's decision and unreasonably interfering with the corporation's affairs. Cede & Co., 634 A.2d at 360-61. Courts do not interfere with or disturb a board's decision if a board acts for any rational purpose. Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971).

Here, the Court presumes that the Board adopted the Bylaw on an informed basis, in good faith, and in the honest belief that the Bylaw was in the best interest of Pinpoint. The Court should not second guess the Board's decision and unreasonably interfere with Pinpoint's affairs because the Board adopted the Bylaw for a rational purpose. The Bylaw's rational purpose was to increase efficiency, convenience, and relative predictability in litigation involving the corporation. Therefore, under the business judgment rule, the Court should uphold and enforce the Bylaw.

2. Under the Unocal standard, the Court should uphold and enforce the Bylaw because the Board reasonably believed Pinpoint's policy and effectiveness was threatened and the Board's adoption of the Bylaw was reasonable in relation to the perceived threat.

Courts do not review the wisdom of a board's decision under the Unocal standard; courts review whether a board properly exercised its business judgment when making a challenged decision. Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140, 1151 (Del. 1990). To determine if a board properly exercised its business judgment, courts ask two preliminary questions. Id. at 1151-52. First, did the board reasonably believe that corporate policy and effectiveness were threatened? Id. at 1152. The board can establish the reasonableness of its belief by showing it acted in good faith and reasonably investigated the issue. Id. Second, did the board make a reasonable decision in relation to the perceived threat? Id. The board's decision does not have to be perfect, but must simply be one of several reasonable alternatives. QVC Network, Inc., 637 A.2d at 45. After answering both questions satisfactorily, courts apply the protective business judgment rule. Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1373 (Del. 1995).

Here, the Board properly exercised its business judgment when adopting the Bylaw. First, the Board reasonably believed that Pinpoint's policy and effectiveness was threatened by the inefficiency, inconvenience, and relative unpredictability associated with litigation involving the corporation. The Board established the reasonableness of its belief because the Board acted in good faith and reasonably investigated the issue by considering several factors and

receiving the advice of outside counsel. Therefore, the Board reasonably believed that Pinpoint's policy and effectiveness was threatened.

Second, the Board's adoption of the Bylaw was reasonable in relation to the perceived threat. Even if the Bylaw was not perfect, it was one of several reasonable alternatives. The Bylaw is reasonable because it preserves all the stockholders' substantive rights, while increasing the benefits of efficiency, convenience, and relative predictability that all stockholders equally share.

Therefore, the Board's adoption of the Bylaw was reasonable in relation to the perceived threat.

Because the Board reasonably believed that Pinpoint's policy and effectiveness was threatened and the Board's adoption of the Bylaw was reasonable in relation to that perceived threat, the Board properly exercised its business judgment. Therefore, under the <u>Unocal</u> standard, the Court should apply the protective business judgment rule and enforce and uphold the bylaw.

3. Under the entire fairness test, the Court should uphold and enforce the Bylaw because it was entirely fair to Pinpoint's stockholders.

If a plaintiff rebuts the business judgment rule's strong presumption, courts scrutinize a decision to examine its entire fairness. Cede & Co., 634 A.2d at 361. To be entirely fair, a decision must be the product of fair dealing and fair value.

Weinberger v. UOP, Inc., 457 A.2d 701, 711 (Del. 1983). An examination of fair dealing involves how a decision was initiated, its timing, how it gained approval, and whether it involved proper

disclosures. Id. A fair value examination deals with the economic and financial considerations, including "any... elements that affect the intrinsic or inherent value of a stock." Id.

Here, the Board's adoption of the Bylaw was entirely fair because it was the product of fair dealing. The Board's adoption of the Bylaw was initiated with the Court of Chancery writing that boards "are free to [adopt]... charter provisions selecting an exclusive forum for intraentity disputes." In re Revlon, Inc. S'holders Litig. 990 A.2d 940, 960 (Del. Ch. 2010). Following this decision on March 5, 2010, the number of corporations adopting exclusive forum bylaws increased dramatically. Professor Joseph A. Grundfest, Stanford Law Sch., Choice of Forum Provisions in Intra-Corporate Litigation: Mandatory and Elective Approaches (Oct. 6, 2010), available at http://papers.ssrn.com/sol3/papers.cfm?abstract id=1690561. Barely three months later, on June 10, 2010, the Board became one of these many corporations and unilaterally adopted the Bylaw. The Board never withheld information from stockholders and Miller provides no evidence the Board acted in bad faith. Therefore, the Bylaw was the product of fair dealing.

Furthermore, the Board's adoption of the Bylaw was entirely fair because it produced a fair value. The Bylaw is a fair value for the corporation because it increased the corporation's economic and financial benefits by reducing the costs associated with litigation involving the corporation. Litigation in several states simultaneously would unnecessarily drain corporate funds and unfairly impacts the remaining stockholders. For example, Miller is only one

of 28,000 stockholders living in all fifty states and he filed a claim in Texas. Three other stockholders filed nearly identical claims in Delaware. Without the Bylaw, the remaining 27,976 stockholders would unfairly bear the costs associated with litigating two identical claims simultaneously in separate jurisdictions across the country. Thus, the Bylaw produced a fair value.

Because the Bylaw was the product of fair dealing and fair value, the Board's decision was entirely fair. Therefore, under the entire fairness test, the Court should uphold and enforce the Bylaw.

#### CONCLUSION

This Court should affirm the Court of Chancery's holding that Pinpoint's forum selection bylaw provision is valid and enforceable. The Board had the authority to adopt the Bylaw and the Bylaw is both reasonable and consistent with Delaware public policy. Additionally, the Bylaw is enforceable under equitable considerations. The business judgment rule is the proper standard to evaluate the Board's decision and under that rule, the Bylaw is enforceable because it was adopted for a rational purpose.

Respectfully Submitted,

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Team  $Q_{,}$ 

Attorneys for Appellees