

IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE PINPOINT BEARINGS, INC. ) Consol. Civil Action No. 4952-VCM  
SHAREHOLDERS LITIGATION )

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EDWARD MILLER, )  
)  
Petitioner Below, )  
Appellant, )  
)  
v. ) Civil Action No. 4958-VCM  
)  
)  
MICHAEL SANCHEZ, CLAIRE ) On Appeal from the Court of  
MITCHELL, BRENDAN ELLSWORTH ) Chancery of the State of  
TIMOTHY FLETCHER, MARSHA ) Delaware in and for New Castle  
FRANKLIN, DAPHNE KEYES, AND ) County  
ERIC LAM, )  
)  
Respondents Below, )  
Appellees, )  
)  
and )  
)  
PINPOINT BEARINGS, INC., )  
)  
Respondents Below, )  
Nominal Appellee. )

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APPELLEES' ANSWERING BRIEF

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Team V  
Counsel for the Director Appellees  
February 11, 2011

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## NATURE OF PROCEEDINGS

This appeal follows the New Castle Court of Chancery's ("Chancery Court") denial of Plaintiff Edward Miller's ("Plaintiff Miller") motion to stay proceedings in Delaware and grant of the Board of Directors' ("Directors") motion to enjoin Plaintiff Miller from prosecuting derivative or fiduciary claims outside of Delaware. *In re Pinpoint Bearings, Inc. S'holders Litig.*, No. 4952-VCM, slip op. at 19-20 (Del. Ch. Jan. 12, 2011). The Chancery Court reached its decision after ruling that Pinpoint Bearings, Incorporated's ("Pinpoint") exclusive forum bylaw was valid and enforceable. *Id.*

On December 1, 2010, Plaintiff Miller filed a derivative lawsuit in the United States District Court for the Southern District of Texas ("Texas Action") alleging that the Directors breached their fiduciary duty of directorial oversight and violated Section 10(b) of the Securities Exchange Act. *Id.* at 4, 7. The next day, Plaintiffs Eileen Webb, Richard Patrick, and Harold Kohn ("Delaware Plaintiffs") filed three separate derivative suits ("Original Delaware Action"), which were later consolidated, with the Chancery Court alleging the same breaches of fiduciary duty as Plaintiff Miller. *Id.* at 3, 7, 8.

On December 13, 2010, the Directors filed a motion to stay proceedings in the Texas Action; however, that motion remains pending. *Id.* at 8. Two days later, Plaintiff Miller filed a derivative suit in Chancery Court alleging the same breach of fiduciary duty as his Texas Action, a motion to join the Delaware Plaintiffs' consolidated action, and a motion to stay proceedings in Delaware. *Id.* at 8-9. In response, the Directors filed a motion to enjoin Plaintiff Miller from

prosecuting derivative or fiduciary claims outside of Delaware with the court. *Id.* at 10. The Delaware Plaintiffs also oppose Plaintiff Miller's motion to stay. *Id.* at 1. After the Chancery Court ruled in favor of the Directors, Plaintiff Miller filed an interlocutory appeal with the Supreme Court of Delaware concerning the validity and enforceability of Pinpoint's exclusive forum bylaw, which this Court granted. (Order Granting Interlocutory Appeal 2, Jan. 14, 2011.)

### SUMMARY OF ARGUMENT

1. The exclusive forum bylaw is valid and enforceable because the Directors adopted it in accordance with Delaware law and Pinpoint's charter, and the bylaw does not have an unreasonable or inequitable effect. A corporation's charter and bylaws are a contract between the corporation and its shareholders. Bylaws are presumed valid unless contrary to law or inequitable in application. The bylaw is consistent with Delaware law and is not inequitable because it does not entrench the Directors or restrict the shareholders' substantive rights. Therefore, the Court should uphold the validity and enforceability of the bylaw.

2. The Directors should be protected by the business judgment rule because their adoption of the exclusive forum bylaw did not breach their fiduciary duties. Plaintiff Miller solely alleges breach of the duty of loyalty, but the bylaw does not entrench the Directors, financially benefit the Directors, or restrict the shareholders substantive right to bring suit against the Directors. Since no proof of directorial self-interest exists, the Court should apply the business judgment rule. The exclusive forum bylaw serves a rational business purpose because it provides greater efficiency, convenience, and predictability to Pinpoint and its shareholders in derivative litigation. Thus, the Court should affirm the lower court's rulings.

**STATEMENT OF FACTS**

Pinpoint, a manufacturer of parts used in the aerospace industry, is incorporated in Delaware with its corporate headquarters and manufacturing operations located in Houston, Texas. *In re Pinpoint*, No. 4952-VCM, slip op. at 4. Pinpoint is a publicly-traded company that employs approximately 8,000 individuals. *Id.* Pinpoint's primary purchaser, the United States military, has accounted for more than sixty percent of Pinpoint's revenues for the last five years. *Id.* at 5. Pinpoint's Directors consist of three inside directors and four outside directors. *Id.* On June 10, 2010, the Directors adopted a bylaw designating Delaware courts as the exclusive forum for any derivative action or fiduciary claim brought on behalf of the corporation after considering the added efficiency, convenience, and predictability such a bylaw would produce. *Id.* at 2, 19.

In September 2010, a Pinpoint engineer informed the Office of Inspector General ("OIG") that he discovered three mid-level Pinpoint managers had routinely misrepresented the performance of some required testing to the government since early 2009. *Id.* at 5. The OIG began investigating and formally notified Pinpoint. *Id.* at 6. The Directors appointed two outside Directors to a special investigation committee ("Special Committee"), which found the allegations to be true. *Id.* at 6. On November 30, 2010, the Directors approved a settlement with the OIG that imposed \$500 million of fines on Pinpoint to avoid criminal liability and ineligibility as a military contractor. *Id.* at 6-7. That same day, Pinpoint issued a press release disclosing the investigation and terms of the settlement. *Id.* at 7. This litigation followed. *Id.*

## ARGUMENT

### **I. THE EXCLUSIVE FORUM BYLAW IS VALID AND ENFORCEABLE BECAUSE IT WAS ADOPTED IN ACCORDANCE WITH DELAWARE LAW AND IS NOT UNREASONABLE OR INEQUITABLE IN ITS APPLICATION**

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

Whether an exclusive forum bylaw adopted by a corporation's board of directors, as allowed by its charter and Delaware law, is valid and enforceable against its shareholders in derivative and breach of fiduciary duty actions.

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

The validity of the exclusive forum bylaw is a mixed question of law and fact. *See Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985). The Court reviews for clear error and should reverse "only if the findings below are clearly wrong and the doing of justice requires their overturn." *Id.*

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

The Directors validly adopted an enforceable exclusive forum bylaw because the Directors acted within the confines of Delaware law and Pinpoint's charter, and the bylaw is not unreasonable or inequitable in its application. *See Frantz*, 501 A.2d at 407; *Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971); *In re Pinpoint*, No. 4952-VCM, slip op. at 12 (stating Pinpoint's charter expressly grants the Directors power to adopt bylaws). A corporation's charter and bylaws are a contract between the corporation and its shareholders. *Kidsco Inc. v. Dinsmore*, 674 A.2d 483, 492 (Del. Ch. 1995). A corporation's charter may grant both the shareholders and the board the power to adopt, amend, or repeal bylaws and "[t]he bylaws

may contain any provision . . . relating to the business of the corporation, the conduct of its affairs, and its rights and powers or the rights and powers of its stockholders, directors, officers, or employees.” DEL. CODE ANN. tit. 8, § 109 (2010). If adopted by shareholders or an empowered board, a bylaw is presumptively valid if not inconsistent with statutory law, common law, or the corporation’s charter and not unreasonable or inequitable in its application.

*Frantz*, 501 A.2d at 407. In accordance with Pinpoint’s charter, the Directors used their power to adopt the exclusive forum bylaw at issue, which relates to the powers and rights of the shareholders. *In re Pinpoint*, No. 4952-VCM, slip op. at 2. Accordingly, the Directors validly adopted the bylaw. *See Frantz*, 501 A.2d at 407. Furthermore, the bylaw is not unreasonable or inequitable in its application because it does not entrench the Directors or restrict the shareholders’ substantive rights. *See Schnell*, 285 A.2d at 439; *Openwave Sys. Inc. v. Harbinger Capital Partners Masterfund I, Ltd.*, 924 A.2d at 228, 239 (Del. Ch. 2007) (noting that Delaware courts often uphold advance notice bylaws, a procedural restriction on shareholders). Since the Directors acted within Delaware law and the exclusive forum bylaw is not unreasonable or inequitable, the Court should uphold the validity and enforceability of the bylaw and affirm the lower court’s holding as it was not clearly erroneous.

**1. Exclusive forum clauses are valid and enforceable under contract law absent unreasonableness or fraud**

The exclusive forum bylaw, a contract between Pinpoint and its shareholders, is valid and enforceable under contract law because it is not unreasonable, unjust, or procured through fraud. *See Ingres*

*Corp. v. CA, Inc.*, 8 A.3d 1143, 1146 (Del. 2010); *Kidsco*, 674 A.2d at 492 (“[B]ylaws are a contract between the corporation and its shareholders.”). Forum selection provisions in a contract are presumptively valid and enforceable “unless the resisting party clearly shows that enforcement would be unreasonable and unjust, or that the clause is invalid for such reasons as fraud and overreaching.” *Ingres*, 8 A.3d at 1146. Inconvenience or additional cost does not satisfy the test of unreasonableness; rather, the plaintiff must demonstrate the agreement seriously impairs his ability to pursue the claim. *Id.* at 1146 n.9.

Plaintiff Miller cannot overcome the exclusive forum bylaw’s presumption of validity because enforcement of the bylaw is not unreasonable, unjust, or fraudulent. *See id.* at 1146. The bylaw does not satisfy the test of unreasonableness because it does not substantially impair Plaintiff Miller’s ability to pursue this action, as he has demonstrated by filing this suit in Delaware. *See Ingres*, 8 A.3d at 1146 n.9; *In re Pinpoint*, No. 4952-VCM, slip op. at 8. Any claim that the bylaw is unjust lacks merit because the actual plaintiff in this derivative suit, *Pinpoint*, is incorporated in Delaware, the substantive rights of the shareholders have not changed, and *Pinpoint*’s charter empowers the Directors to adopt bylaws. *See In re Pinpoint*, No. 4952-VCM, slip op. at 4, 12. Lastly, the bylaw is not fraudulent because the Directors adopted it in accordance with Delaware law and to further *Pinpoint*’s interests. *See tit. 8, § 109; In re Pinpoint*, No. 4952-VCM, slip op. at 19. Thus, under principles

of contract law, the Court should uphold the validity and enforceability of Pinpoint's exclusive forum bylaw.

**a. A nexus exists between contract law and corporate law**

Pinpoint's charter and bylaws are a contract between the corporation, which acts through its Directors, and its shareholders. See *Kidsco*, 674 A.2d at 492 (citing *Centaur Partners, IV v. Nat'l Intergroup, Inc.*, 582 A.2d 923, 926 (Del. 1990); see also Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts*, 88 IOWA L. REV. 1, 16 (2002) ("Corporate constituents contract not with each other, but with the corporation."). Delaware courts have recognized that a corporation's charter and bylaws are a contract between the corporation and its shareholders. *Kidsco*, 674 A.2d at 492. The shareholders and the board of directors, if allowed by the corporation's charter, may independently adopt bylaws; thus, both parties can unilaterally adopt enforceable bylaws if consistent with the law and the corporation's charter. tit. 8, § 109; *CA, Inc. v. AFSCME Emps. Pension Plan*, 953 A.2d 227, 232 (Del. 2008). By agreeing to Pinpoint's charter, the Directors and shareholders have consented to be bound by the terms of the charter, including the unilateral adoption of bylaws. See *CA, Inc.*, 953 A.2d at 232. Further, the Directors and shareholders provide mutual consideration because both parties must adhere to any legally-enforceable bylaw adopted by either party. See *id.*; but see *Underbrink v. Warrior Energy Servs. Corp.*, 2008 WL 2262316, at \*9 (Del. Ch. 2008) (finding no precedent of invalidating a board-approved bylaw for lack of consideration). Therefore, a nexus exists between contract law and corporate law, and

the determination of whether the exclusive forum bylaw is valid and enforceable must incorporate aspects of both.

**2. The Directors adopted the exclusive forum bylaw pursuant to Delaware corporate law and Pinpoint's charter thereby binding the shareholders**

**a. The exclusive forum bylaw is valid and enforceable under statutory law**

Under Delaware statutory law, the exclusive forum bylaw is valid and enforceable because Pinpoint's charter granted the Directors the power to adopt bylaws, and the bylaw relates to the powers and rights of the shareholders. See tit. 8, § 109; *In re Pinpoint*, No. 4952-VCM, slip op. at 12. A corporation's charter may grant both the shareholders and the board the power to adopt, amend, or repeal bylaws and "the bylaws may contain any provision . . . relating to the business of the corporation, the conduct of its affairs, and its rights and powers or the rights and powers of its stockholders, directors, officers, or employees." tit. 8, § 109. Bylaws are presumptively valid unless inconsistent with Delaware corporate statutes or the corporation's charter. *Frantz*, 501 A.2d at 407. Here, Pinpoint's charter grants the Directors the power to adopt bylaws, and the bylaw relates to the powers and rights of the shareholders because it identifies the forum where suits involving the internal affairs of the corporation must be brought. *In re Pinpoint*, No. 4952-VCM, slip op. at 12. Thus, the presumption of the bylaw's validity remains.

**b. The exclusive forum bylaw is valid and enforceable under common law**

The exclusive forum bylaw is valid and enforceable under Delaware common law because the bylaw does not have an inequitable effect. See

*Schnell*, 285 A.2d at 439; *Openwave*, 924 A.2d at 239. If a bylaw is consistent with statutory law, the presumption of validity persists unless it violates a common law precept. *CA, Inc.*, 953 A.2d at 238. Delaware courts have struck down legally adopted bylaws only if the bylaw is inequitable in application. *Schnell*, 285 A.2d at 439; *Hollinger Int'l, Inc. v. Black*, 844 A.2d 1022, 1080 (Del. Ch. 2004). Pinpoint's exclusive forum bylaw is not inequitable because it does not entrench the Directors or restrict the substantive rights of the shareholders. See *Schnell*, 285 A.2d at 439; *Openwave*, 924 A.2d at 239. Plaintiff Miller cannot overcome the bylaw's presumption of validity. *CA, Inc.*, 953 A.2d at 238. Because the lower court did not clearly err when upholding the validity of the bylaw, the Court should affirm.

**c. The exclusive forum bylaw is valid and enforceable because it furthers the policy goal of vesting management power with a corporation's board of directors**

The Court should uphold the validity and enforceability of the exclusive forum bylaw because it furthers the Delaware corporate policy of separating ownership and management while also promoting the precept that the board of directors should have the ultimate authority in managing a corporation's business affairs. See *CA, Inc.*, 953 A.2d at 239; *MM Cos. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1126 (Del. 2003). The fundamental principle of corporate law is the separation of control and ownership of the corporation, which is accomplished by allowing the shareholders to elect the board of directors and granting broad managerial power to the board. *MM Cos.*, 813 A.2d at 1126. In an analogous case, the Court upheld an exclusive forum selection provision and arbitration provision in a LLC operating agreement

because it furthered the statute's policy goal of maximizing freedom of contract principles. *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 295 (Del. 1999).

Similarly, in order to further the policy goals of corporate law, a board of directors must be allowed to make lawful managerial decisions that further its corporation's interests. *See id.*; *see also* DEL. CODE ANN. tit. 8, § 141(a) (2010); *MM Cos.*, 813 A.2d at 1126 (identifying policy goals of corporate law). Here, the Directors lawfully adopted an exclusive forum bylaw in order to provide greater efficiency and predictability to derivative and fiduciary claims brought against the corporation. *See Frantz*, 501 A.2d at 407; *In re Pinpoint*, No. 4952-VCM, slip op. at 19. Since the Directors adopted the bylaw legally and to further Pinpoint and its shareholders' interests, the Court should uphold the validity and enforceability of the bylaw to advance well-founded policies of Delaware corporate law.

**d. A *McWane* analysis is inapplicable due to the validity and enforceability of the exclusive forum bylaw**

Since the exclusive forum bylaw is valid and enforceable under Delaware law, the *McWane* principles that would generally apply have been displaced. *See Ingres*, 8 A.3d at 1145; *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281, 282-83 (Del. 1970). *McWane* stands for the legal proposition that Delaware courts should favor granting a party's motion to stay if a prior action involving the same parties and issues is pending in another court that is "capable of doing prompt and complete justice." *Ingres*, 8 A.3d at 1145. However, when parties agree on a lawful forum selection

provision, the court should honor the provision even if a *McWane* analysis would otherwise compel a different result. *Id.* Here, Pinpoint's exclusive forum bylaw displaces *McWane* because it was validly adopted under Delaware law. *See id.*; *Frantz*, 501 A.2d at 407. Thus, the *McWane* principles do not alter the analysis and the Court should uphold the lower court's decision.

**e. Galaviz v. Berg does not bind the Court and does not persuasively apply Delaware law**

The recent decision in the Federal District Court of Northern California addressing the validity of exclusive forum bylaws is unconvincing because the decision does not bind Delaware courts and did not apply accepted principles of Delaware corporate law. *Galaviz v. Berg*, 2011 WL 135215, at \*4 (N.D. Cal. 2011). Delaware courts have acknowledged that bylaws are a contract between the corporation and its shareholders. *Kidsco*, 674 A.2d at 492. Although the *Galaviz* court did not refute that bylaws are contracts between the corporation and its shareholders, it incorrectly applied the strict contract principle of mutual consent. *See* 2011 WL 135215, at \*4. Further, the court did not address the shareholders' independent and concurrent power to unilaterally bind the Directors through bylaws. *Id.* Since the *Galaviz* court did not decide the case under accepted principles of Delaware law, its decision should be unheeded by this Court.

*Galaviz* also raised concerns about the validity of the exclusive forum bylaw's retroactive application and Delaware's stance on exclusive forum provisions outside of the corporation's charter; however, the *Galaviz* court's arguments are unpersuasive under Delaware law. 2011 WL 135215, at \*4; *See Kidsco*, 674 A.2d at 492-93; *In re*

*Revlon, Inc. S'holders Litig.*, 990 A.2d 940, 960 (Del. Ch. 2010).

First, no issue with retroactivity of the exclusive forum bylaw exists because Pinpoint's charter explicitly puts its shareholders on notice that its bylaws may be adopted, amended, or repealed by either its Directors or its shareholders at any time. See *Kidsco*, 674 A.2d at 492; *In re Pinpoint*, No. 4952-VCM, slip op. at 12. Shareholders, such as Plaintiff Miller, who held shares of Pinpoint before the bylaw was adopted, do not have a vested right to challenge a bylaw adopted pursuant to a valid charter provision. See *Kidsco*, 674 A.2d at 492-93.

Second, the *Galaviz* court, citing *In re Revlon*, favored enforceability of a forum selection provision only when found in the charter. 2011 WL 135215, at \*4. It seems the *Galaviz* court mistakenly used dicta from *In re Revlon* to support its argument that the bylaw was unenforceable on contractual grounds of lack of mutual consent. *Id.* As argued above, this issue does not arise here because the shareholders consented to the charter provision that allowed the adoption of the bylaw by the Directors. *In re Pinpoint*, No. 4952-VCM, slip op. at 12. Further, analogizing the bylaw to a contractual provision granting one party the unilateral power to amend the contract is unavailing because shareholders also retain that right. See tit. 8, § 109(a); *Galaviz*, 2011 WL 135215, at \*4. The *Galaviz* court was mistaken in its application of Delaware law, and thus, the Court should uphold the validity and enforceability of Pinpoint's exclusive forum bylaw by affirming the lower court's decision.

**II. THE DIRECTORS DID NOT BREACH THEIR FIDUCIARY DUTIES TO THE CORPORATION OR ITS SHAREHOLDERS BY ADOPTING THE EXCLUSIVE FORUM BYLAW AND ARE ENTITLED TO THE PROTECTIONS OF THE BUSINESS JUDGMENT RULE BECAUSE THE BYLAW DOES NOT ADVANCE THE DIRECTORS' SELF-INTERESTS OR PRESENT A CONFLICT OF INTEREST**

**A. Question Presented**

Whether the Directors properly discharged their fiduciary duties when adopting a valid and enforceable exclusive forum bylaw and, thus, are entitled to the protection of the business judgment rule.

**B. Standard of Review**

"When shareholders challenge actions by a board of directors, generally one of three standards of judicial review is applied: the traditional business judgment rule, an intermediate standard of enhanced judicial scrutiny [*Unocal*], or the entire fairness analysis." *Emerald Partners v. Berlin*, 787 A.2d 85, 89 (Del. 2001). The Chancery Court ruled that the business judgment rule applied to the adoption of the bylaw because the Directors did not breach their fiduciary duties or adopt defensive measures. *In re Pinpoint*, No. 4952-VCM, slip op. at 17-18. Whether the Directors acted equitably in the adoption of the exclusive forum bylaw is a mixed question of law and fact; thus, the proper standard of review requires this Court reverse the lower court's findings only if the Court finds clear error and justice so requires its overturn. *Frantz*, 501 A.2d at 407, 408.

**C. Merits of the Argument**

**1. The Directors' adoption of the exclusive forum bylaw should be examined under the business judgment rule because no breach of fiduciary duty occurred**

Pinpoint's Directors properly discharged their fiduciary duties and are entitled to the protection of the business judgment rule

because the bylaw does not entrench the Directors, provide a pecuniary interest, or restrict the substantive rights of the shareholders. See *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993); *Frantz*, 501 A.2d at 408; *Openwave*, 924 A.2d at 239; *In re Pinpoint*, No. 4952-VCM, slip op. at 17. Directors of corporations must discharge their duty of loyalty, due care, and good faith at all times to be protected by the business judgment rule. *Emerald Partners*, 787 A.2d at 90. The business judgment rule is a presumption that "the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation and its shareholders" when making a business decision. *Id.* To rebut this presumption, the initial burden is on the plaintiff to prove that the board of directors violated at least one of its fiduciary duties in making a decision; otherwise, the business judgment rule attaches to protect directorial decisions. *Id.* at 91.

Here, Plaintiff Miller solely alleges a breach of the duty of loyalty by the Directors in adopting the exclusive forum bylaw. *In re Pinpoint*, No. 4952-VCM, slip op. at 16. Specifically, Plaintiff Miller argues that the Directors' engaged in self-dealing and acted self-interestedly by restricting the available forum for shareholder litigation, or alternatively, the Director's response to a perceived threat was not reasonable and proportional under *Unocal*. *Id.* However, the bylaw does not perpetuate the Directors' position on the Directors, provide the Directors a pecuniary benefit, or limit the substantive rights of the shareholders; thus, no breach of duty of loyalty is present and *Unocal* does not apply. See *Cede*, 634 A.2d at

361; *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985); *Frantz*, 501 A.2d at 408; *Openwave*, 924 A.2d at 239. Therefore, Plaintiff Miller cannot rebut the presumption of the business judgment rule and the Court should affirm the lower court's decision as it is not clearly erroneous. See *Emerald Partners*, 787 A.2d at 91; *Frantz*, 501 A.2d at 407.

**a. The exclusive forum bylaw does not perpetuate the Directors' control of Pinpoint or present any cognizable conflict of interest**

The exclusive forum bylaw does not advance the Directors' self-interests because it does not entrench or promote the entrenchment of the Directors. See *Frantz*, 501 A.2d at 408. Corporate bylaws are presumed valid; however, if a board of directors acts for the sole or primary purpose of perpetuating its own control, the business judgment rule does not shelter the directors. *Id.* at 407-08. Here, the exclusive forum bylaw does not perpetuate the Directors' control of Pinpoint because it does not increase their time on the board or shelter them from removal. See *Schnell*, 285 A.2d at 439 (holding a bylaw adopted to advance an election date gave an inequitable advantage to incumbent directors). In *Frantz*, where the board decided to dilute the voting stock when facing a hostile takeover, the Court held the board's actions were inequitable because the primary purpose of the dilution was to perpetuate the board's control of the corporation. 501 A.2d at 402, 408. Unlike *Frantz*, the Pinpoint Directors passed the exclusive forum bylaw primarily to promote efficiency, convenience, and predictability for the corporation and its shareholders. See *id.*; *In re Pinpoint*, No. 4952-VCM, slip op. at

19. Since there is no indication that the bylaw was adopted for the primary purpose of perpetuating the incumbent Directors' control of Pinpoint, the Court should apply the business judgment rule.

Furthermore, the lower court was not persuaded that the exclusive forum bylaw even "raises any cognizable interest for loyalty analysis purposes." *In re Pinpoint*, No. 4952-VCM, slip op. at 17. There was no conflict of interest present in the adoption of this bylaw because the Directors were not in a defensive position as there was no threat to their control of Pinpoint. See *Unocal*, 493 A.2d at 955. Since the exclusive forum bylaw in no way entrenched the Directors' control of Pinpoint and no conflict of interest existed at the time the bylaw was adopted, the Court should apply the business judgment rule.

**b. The bylaw does not provide a pecuniary benefit to the Directors**

The Directors did not act in their own self-interest when adopting the exclusive forum bylaw because the bylaw does not provide a personal benefit to any one of the Directors. See *Cede*, 634 A.2d at 361. When a board of directors acts in a manner that provides an individual director or the directors as a whole with a personal financial benefit, the duty of loyalty has been breached or at least called into question and the business judgment rule will not apply. *Id.* at 362. The bylaw does not provide a financial benefit to the Directors and does not insulate them from claims for monetary relief if a fiduciary duty were breached. *In re Pinpoint*, No. 4952-VCM, slip op. at 17. Thus, the exclusive forum bylaw does not implicate directorial self-interest or a breach of the duty of loyalty.

**c. The bylaw does not restrict the substantive rights of the shareholders in court actions**

The Directors do not benefit from the exclusive forum bylaw because it does not limit the types of actions shareholders can take against the Directors. See *Openwave*, 924 A.2d at 239 (noting that Delaware courts often uphold advance notice bylaws, a procedural restriction on shareholders); see also *CA, Inc.*, 953 A.2d at 235 (upholding bylaws that procedurally restrict the board). A procedural bylaw is typically upheld unless it restricts the shareholder franchise or is inequitable. *Openwave*, 924 A.2d at 239; see also *Quickturn Design Sys., Inc. v. Shapiro*, 721 A.2d 1281, 1288-89 (Del. 1998) (upholding bylaw requiring three months delay after special shareholder meeting was called). Here, Pinpoint shareholders' right to bring derivative and fiduciary claims against Directors is unchanged, only the choice of forum is restricted. *In re Pinpoint*, No. 4952-VCM, slip op. at 17-18. Further, the bylaw does not limit the forum for direct actions that shareholders may bring and it increases predictability, maximizes corporate resources, and was adopted in the best interest of the corporation. *Id.* For these reasons, the bylaw does not implicate directorial self-interest, there is no breach of fiduciary duty, and the business judgment rule is the correct standard of review.

**d. The Court should uphold the Directors' adoption of the bylaw under the business judgment rule**

The Directors satisfy the requirements of the business judgment rule because they properly discharged their fiduciary duties and the adoption of the exclusive forum bylaw serves a rational business

purpose. See *Unocal*, 493 A.2d at 954. Once the business judgment rule attaches, it protects decisions made by directors as long as the decision “can be attributed to any rational business purpose.” *Id.* A rational business purpose for the bylaw exists because the bylaw was enacted to promote:

[E]fficiency and convenience of having all fiduciary litigation confined to the Court of Chancery, the avoidance of related litigation in multiple venues and the benefit of what the Board determined would be greater predictability in the application of Delaware corporate governance standards, both existing and newly developing.

*In re Pinpoint*, No. 4952-VCM, slip op. at 16.

Plaintiff Miller cannot convincingly argue a breach of fiduciary duty occurred because there was no entrenchment by the Directors, no financial self-interest or self-dealing, and the substantive rights of shareholders have not been limited in any way. See *Cede*, 634 A.2d at 361; *Frantz*, 501 A.2d at 408; *Openwave*, 924 A.2d at 239. Therefore, the business judgment rule applies. *Emerald Partners*, 787 A.2d at 91. Since the Directors were acting for a rational business purpose, as shown here and held in the lower court, the adoption of the bylaw is valid and should be protected by the business judgment rule. See *id.*

## **2. An entire fairness review is not warranted**

Since Plaintiff Miller cannot rebut the presumption of the business judgment rule and the Directors did not act self-interestedly, an entire fairness analysis is not warranted. See *id.* at 90. A plaintiff “must allege sufficient facts from which the court could reasonably infer” that a breach of fiduciary duty occurred before the entire fairness standard may apply. *Underbrink*, 2008 WL 2262316, at \*11. Here, the factual circumstances do not support this

standard of analysis because Delaware courts have historically applied entire fairness to mergers involving conflicts of interest where the duty of loyalty has been breached. See *Emerald Partners*, 787 A.2d at 90; *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. Supr. 1995) (applying the entire fairness analysis to an appraisal performed as a defensive measure to thwart a third party merger); *Cede*, 634 A.2d at 361 (applying entire fairness to a merger plan approved by defendant directors). Because Plaintiff Miller has not alleged sufficient facts for a reasonable inference of breach of fiduciary duty, this situation does not involve a merger, and there is no conflict of interest, the entire fairness standard of review is unwarranted.

**a. The Directors' actions would pass muster if subjected to the entire fairness standard**

Alternatively, if the Court nonetheless subjects the Directors' actions to an entire fairness review, the adoption of the bylaw is both procedurally and substantively fair (*i.e.* fair dealing) and should be upheld. See *Cinerama*, 663 A.2d at 1163; *Nixon v. Blackwell*, 626 A.2d 1366, 1376 (Del. 1993) (applying only the fair dealing test to the adoption of an employee stock ownership plan under entire fairness); *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983) (ruling that entire fairness constitutes fair dealing and fair price). *Weinberger* establishes the proposition that fair dealing concerns "when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained." *Cinerama*, 663 A.2d at 1163 (citing *Weinberger*, 457 A.2d at 711). Further, "[a]ll aspects of

the issue must be examined as a whole since the question is one of entire fairness." *Weinberger*, 457 A.2d at 711.

**i. The bylaw's adoption was procedurally fair**

The adoption of the exclusive forum bylaw was procedurally fair because the Directors acted within the confines of Delaware law and Pinpoint's charter. See tit. 8, § 109; *Frantz*, 501 A.2d at 407; *In re Pinpoint*, No. 4952-VCM, slip op. at 12. The bylaw was initiated and structured by the Directors pursuant to Pinpoint's charter. *In re Pinpoint*, No. 4952-VCM, slip op. at 2, 12. The record does not show any issues with the disclosure of this bylaw, and the approval of the Directors validly followed the procedure set out in Pinpoint's articles of incorporation. *Id.* Similarly, the timing of this bylaw did not violate Pinpoint's charter or bylaws. *Id.* For these reasons this court should find that procedurally this bylaw passes the entire fairness standard.

**ii. The bylaw's adoption was substantively fair**

The adoption of the exclusive forum bylaw is substantively fair because it does not serve an inequitable purpose or directorial self-interest; rather, it was adopted to advance the interests of Pinpoint and its shareholders. See *Schnell*, 285 A.2d at 439; *In re Pinpoint*, No. 4952-VCM, slip op. at 19. A fair price analysis is unnecessary because no financial transaction occurred. *Nixon*, 626 A.2d at 1376. The Court in *Nixon* did not further examine the aspect of fair price because no formalized transaction was connected to the adoption of an employee stock ownership plan. *Id.* Similarly, the Directors' adoption of the bylaw did not relate to a specific financial transaction, and

thus, no fair price analysis is required. See *id.*; *In re Pinpoint*, No. 4952-VCM, slip op. at 2. Nevertheless, the bylaw is substantively fair because there is no inequitable effect or directorial self-interest present. See *Schnell*, 285 A.2d at 439. The bylaw does not substantively limit the rights of potential litigants in bringing both injunctive and monetary claims against Pinpoint and its Directors or entrench the Directors on the board. See *id.* Therefore, the adoption of this bylaw is entirely fair and withstands all challenges Plaintiff Miller has brought forth on duty of loyalty grounds.

### **3. A *Unocal* analysis is unwarranted**

The *Unocal* enhanced scrutiny standard is inapplicable because the exclusive forum bylaw does not represent a defensive measure taken against the threat of a takeover. See *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1372 (Del. 1995). The bylaw further does not raise a “specter” of potential self-interest on the part of the Directors because the bylaw does not entrench the Directors or provide a financial benefit to the Directors. *Unocal*, 493 A.2d at 954. The lower court also found that “[t]he Director Defendants’ only ‘interest’ in having such claims exclusively litigated in Delaware is one of convenience, efficiency and relative predictability,” expressly refusing to acknowledge any cognizable challenge to a duty of loyalty. *In re Pinpoint*, No. 4952-VCM, slip op. at 17. Since the *Unocal* standard of review is inapplicable, the Court should apply the business judgment rule and uphold the lower court’s decision.

**a. Even if *Unocal* applied, the Directors' adoption of the exclusive forum bylaw should be upheld**

Even if an attenuated *Unocal* analysis applied by claiming the Directors' acted self-interestedly by constraining derivative litigation to Delaware courts, their actions would be reasonable and proportionate to the perceived threat of future excessive litigation costs that could drain Pinpoint's resources. See *Unocal*, 493 A.2d at 954. The *Unocal* standard requires that the board of directors prove they had reasonable grounds for believing a danger to corporate policy and effectiveness existed and their actions were proportionate to the perceived threat. *Unitrin*, 651 A.2d at 1373.

The Directors' adoption of the exclusive forum bylaw was reasonable and proportionate to the perceived threat of future excessive litigation costs. See *id.* at 1384-86. The *Unitrin* Court held that an action is not reasonable and proportionate if it is draconian, meaning having a preclusive or coercive effect. *Id.* at 1384, 1387. Here, the adoption of the bylaw was done in accordance with the Directors' legal authority and according to the charter, so it cannot be said to be coercive. See *id.* at 1387; *In re Pinpoint*, No. 4952-VCM, slip op. at 12. Further, if a majority of Pinpoint's shareholders are dissatisfied with the exclusive forum bylaw, they can elect new directors or amend the bylaw themselves; thus, the bylaw is not preclusive. See tit. 8, § 109(a); *MM Cos.*, 813 A.2d at 1127; *Unitrin*, 651 A.2d at 1387. Even if the *Unocal* standard of review applied, the Directors' actions were reasonable and proportional to the threat posed and should be upheld by the Court.

**b. Even if a *Blasius* review applied, it would not be ripe for adjudication**

The *Blasius* standard of review is inapplicable to the Directors' actions because the primary purpose of the exclusive forum bylaw was not to impede the exercise of shareholder voting power and the claim is not ripe for adjudication. See *Blasius Indus. Corp. v. Atlas Corp.*, 564 A.2d 651, 661 (Del. Ch. 1988); *State v. Adkins*, 2009 WL 996370, at \*2 (Del. 2009) (holding that an issue is not ripe if it requires some future occurrence). *Blasius* held that when a board acts "for the primary purpose of impeding the exercise of stockholder voting power," it must then provide a compelling justification for its actions for those actions to be upheld. 564 A.2d at 661. Arguably, the effect of the Director-adopted exclusive forum bylaw in connection with *CA, Inc.*, which holds that board-adopted bylaws will be upheld over shareholder-adopted bylaws if the two are inconsistent, is the diminished voting power of Pinpoint's shareholders when seeking to adopt a bylaw. See 953 A.2d at 232. However, that was not the primary purpose of the bylaw. *In re Pinpoint*, No. 4952-VCM, slip op. at 19. Further, until the shareholders adopt a bylaw contrary to or that repeals the exclusive forum bylaw, the claim is not ripe for adjudication because it is not clear whether the majority of the shareholders support or oppose the bylaw. See *Adkins*, 2009 WL 996370, at \*2. Neither *Blasius* nor any other standard of review other than the business judgment rule is applicable; thus, the Court should affirm the lower court's ruling.

### CONCLUSION

For these reasons, the Directors humbly request that this Court uphold Pinpoint's exclusive forum bylaw, affirm the lower court's decision to deny Plaintiff Miller's motion to stay proceedings in Delaware, and grant the Directors' motion to enjoin Plaintiff Miller from prosecuting derivative or fiduciary claims outside of Delaware.