

IN THE

SUPREME COURT OF THE STATE OF DELAWARE

CALLISON INC., TIMOTHY MICHAELS :
 CLARE LIEBERMAN, RHANEY PATRICKS, :
 JULIO LUIS-ROJAS, PATRICK AUSTIN :
 MARSHA FRANKLIN, ARI SINGH and :
 ALLEN ENTERPRISES INCORPORATED, : No. 162, 2013

Defendants Below,
Appellants,

v.

GALENA CAPITAL PARTNERS, LLC.,

Plaintiff Below,
Appellee.

GALENA CAPITAL PARTNERS, LLC.,

Plaintiff,

v.

CALLISON INC., TIMOTHY MICHAELS
 CLARE LIEBERMAN, RHANEY PATRICKS,
 JULIO LUIS-ROJAS, PATRICK AUSTIN
 MARSHA FRANKLIN, ARI SINGH and
 ALLEN ENTERPRISES INCORPORATED,

Defendants.

:
 : Court Below:
 : Court of Chancery
 : of the state of Delaware
 : Civil Action No. 7918-CN

APPELLEE'S OPENING BRIEF

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 Counsel for Plaintiff
 Below, Appellee

Dated: February 8, 2013

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NATURE OF PROCEEDINGS

Plaintiff-Appellee Galena Capital Partners, LLC ("Galena"), commenced the underlying proceeding December 21, 2012, in the Delaware Court of Chancery against Defendants-Appellants Callison, Inc. ("Callison"), its directors Timothy Michaels, Clare Lieberman, Rhaneey Patricks, Julio Luis-Rojas, Patrick Austin, Marsha Franklin, Ari Singh, and Callison's controlling shareholder, Allen Enterprises, Inc. ("Allen"). (Mem. Op. 16.)

Galena sought a preliminary injunction to prevent Callison and its board of directors from enforcing a Don't Ask Don't Waive ("DADW") standstill agreement between Galena and Callison. (Mem. Op. 16.) Galena argued in the alternative that if the DADW provision was valid, Callison's directors breached their fiduciary duties to Galena, as a minority shareholder. (Mem. Op. 24.) The parties proceeded with expedited discovery and briefing, culminating in a hearing before the Court of Chancery on Galena's motion for a preliminary injunction on Jan. 10, 2013. (Mem. Op. 17.) Defendants conceded a preliminary injunction would be appropriate if Plaintiffs demonstrated a reasonable probability of success on the merits. (Mem. Op. 17-18.)

The Court held that the use of the DADW provision by the Callison board of directors ("the Board") violated their fiduciary duties to be informed. (Mem. Op. 23.) The Court did not address the second issue regarding whether a liquidity conflict implicated the entire fairness standard. (Mem. Op. 24-25.) The Court of Chancery granted the motion for the preliminary injunction on Jan. 15, 2013. (Prelim. Inj. Order.) This appeal follows.

SUMMARY OF ARGUMENT

This Court should affirm the decision of the Court of Chancery to grant a preliminary injunction because Galena demonstrated a reasonable probability of success on the merits of its claim. In a *Revlon* transaction such as this, the courts apply an enhanced scrutiny standard requiring the Board demonstrate it acted reasonably. The DADW provision prevented the Board from acting reasonably to achieve value maximization for all Callison stockholders by inhibiting the decision-making process and the Board's ability to act reasonably in light of the circumstances. Because the Board cannot contract away its fiduciary duties, the DADW is unenforceable.

If the Court finds that the DADW is enforceable, this Court should view the transaction under the entire fairness standard and hold that Callison directors breached their fiduciary duties to minority shareholders, including Galena. As an initial matter, Allen's need for liquidity in a short amount of time resulted in an undervalued final offer, at the detriment of minority shareholders. This Court should uphold the principle that a liquidity conflict implicates the entire fairness standard—a view that naturally follows from this Court's pronouncements in *McMullin* and subsequent rulings from the Court of Chancery. The Court should not abandon the liquidity conflict concept in light of recent criticism from the lower courts, because *McMullin* and its progeny have applied the rule with reasonable limits. Finally, even if the Court accepts the criticism offered of *McMullin*, the factors involved in this case justify the imposition of the entire fairness standard.

STATEMENT OF FACTS

A. The Parties.

Galena, a Delaware limited liability company, is a private equity firm managing approximately \$18 billion of capital. (Mem. Op. 2.) Galena is a minority stockholder of Callison, owning 10,000 shares of common stock. *Id.* Callison is a Delaware corporation presently having outstanding 85 million shares of common stock traded on the New York Stock Exchange. *Id.* On December 14, 2012, the last trading day prior to the announcement of the transaction challenged in this litigation, Callison's common stock closed at \$27, suggesting then-market capitalization of approximately \$2.3 billion. *Id.*

Allen, a privately-owned company incorporated in Delaware, owns approximately 72% of the outstanding shares of Callison common stock. *Id.* Allen nominated each of the seven members of the Board. *Id.* at 3. Of those members, four are full-time salaried executives with Allen: Timothy Michaels, Clare Lieberman, Rhaney Patricks, and Julio Luis-Rojas. *Id.* The remaining directors are not employed by Allen or Callison: Patrick Austen, Marsha Franklin, and Ari Singh. *Id.*

B. Allen under pressure to liquidate its 72% stake in Callison.

Allen is contractually obligated to purchase Ca' Foscari Italian Grill ("Ca Foscari"), a national restaurant chain, for a cash price of \$2.4 billion no later than March 31, 2013, or face a loss of \$60 million in liquidated damages. *Id.* at 6. Allen's other holdings are worth only a fraction of the Callison stock. *Id.* at 3. The need for this substantial amount of cash was urgent, as the contract to purchase is not subject to a financing condition. *Id.* at 6.

Allen's management, encouraged by its billionaire owner and founder Allen D. Fairmount III, was involved from beginning in the plan to sell its stake in Callison. *Id.* at 2-4. Board members Michaels and Lieberman were already involved in a search for acquisition candidates in late August 2012, before the Board was notified of the imminent sale. *Id.* at 4. Even the three board members without significant ties to Allen were informally made aware of Allen's plans months before they were established as the "Special Committee" in October 2012. *Id.* at 4-5 (citing Deposition of Ari Singh, Dec. 30, 2012 at p. 164). While the Special Committee could negotiate on behalf of Callison, the Board, including its majority of salaried Allen executives, was to approve the transaction. *Id.* at 5.

C. DADW provision used to expedite the sale process.

The Special Committee knew that Allen needed a fast turnaround and that Allen could block any transaction not in its best interest, even though the Special Committee expressed concern that a "protracted auction" would not benefit Callison. *Id.* at 6-7. On October 20, 2012, the Board agreed to privately canvas the market over a relatively short time using DADW agreements. *Id.* at 7. Each party signing the DADW agreement (a "DADW bidder") would agree that submitting their invited bid constituted their "only, best and final" offer, with the highest DADW bidder winning the auction. *Id.* at 8.

A market check would follow announcement of any definitive acquisition agreement, and Callison could solicit topping bids from any other bidder—except any DADW bidder—for 25 days (the "Go Shop period"). *Id.* at 9. After the Go Shop Period, Callison could

receive, but not solicit, topping bids from any other bidder—except any DADW bidder—for 15 days (the “Window Shop period”). *Id.*

D. Private solicitation of DADW bidders.

The Special Committee retained the investment banking firm Bonchek Graycourt Inc. (“Bonchek”) to advise them with regard to any potential transaction involving the sale of the entire Company. *Id.* at 5. Bonchek privately canvassed the takeover market for potential suitors it deemed a good fit for acquiring Callison, and contacted 20 companies throughout November 2012. *Id.* at 7. Of the 20 contacts, 7 expressed interest in conducting due diligence. *Id.* Of the 7 interested parties, one refused to sign the DADW agreement and withdrew entirely. The remaining 6 potential suitors conducted due diligence through the end of November and submitted privately their bids no later than Friday December 14, 2012.

E. Vicente wins auction.

The Special Committee determined Vicente’s \$34 per share, all-cash, all-shares offer was the best proposal. *Id.* at 11. Galena’s bid fell short by \$1.50 per share, and the remaining four bidders offered bids far below the winning bid. *Id.* After Bonchek delivered its written opinion that Vicente’s offer was “financially fair” to Callison and its minority stockholders, the Special Committee unanimously agreed to recommend the transaction to the Board. *Id.*

The Board agreed Vicente’s offer was “superior to all other bids and fair to Callison and all of its stockholders” and authorized management to negotiate an agreement with Vicente involving a first-step tender offer followed by a cash-out merger. *Id.* at 12. As part

of the market check, the Board obtained a fiduciary out permitting termination of the merger in favor of a superior proposal upon payment to Vicente of a termination fee of \$87 million, and amount representing 3% of the \$2.9 billion transaction contemplated by the merger agreement. *Id.* at 13. After public announcement of the merger December 17, 2012, the market for Callison shares rose to \$33 per share and Bonchek immediately began contacting over 100 additional suitors, but no expressions of interest were received. *Id.* at 14-15.

F. Galena makes topping bid.

On December 19, 2012, Galena privately requested Callison to waive the DADW provision so as to permit Galena to make a topping bid of \$35.50 per share and sign an agreement identical to the merger Vicente except for the increased price, representing a 4.4% increase over Vicente's bid, roughly \$128 million in additional consideration. *Id.* at 15. The Board was advised that insisting on the DADW Standstill was within its proper business judgment and the Board decided to hold fast to the literal terms of the provision. *Id.* at 16.

ARGUMENT

I. The Court of Chancery properly determined the DADW Standstill provision is unenforceable because it prevented the Callison Board from fulfilling its fiduciary duties. This Court should affirm the decision to grant a preliminary injunction.

A. Question Presented

The Callison Board ("the Board") had a fiduciary duty to make informed judgments and implicated its *Revlon* duty to maximize shareholder value when it cooperated with Allen to facilitate a sale of the entire company. Is the "Don't Ask, Don't Waive" Standstill

(the "DADW Standstill") provision unenforceable because it prevented the Board from fulfilling its fiduciary duties to stockholders?

B. Scope of Review

Under this Court's well-established standards for evaluating a motion for a preliminary injunction, the moving party must demonstrate (1) a reasonable probability of success on the merits; (2) irreparable harm; and (3) a balance of equities in its favor. *Kaiser Aluminum v. Matheson*, 681 A.2d 392, 394 (1996). Although each element must be proved, a strong demonstration of one element may overcome a weak demonstration of another. *Cantor Fitzgerald, L.P. v. Cantor*, 724 A.2d 571, 579 (Del. Ch. 1998).

Defendants conceded a preliminary injunction would be appropriate if Plaintiffs demonstrate a reasonable probability of success on the merits of the claim. (Mem. Op. 17-18.) Accordingly, this Court need only evaluate *de novo* the legal principles applied by the Court of Chancery on the probability of success element. *SI Mgmt. L.P. v. Winger*, 707 A.2d 37, 40 (Del. 1998). Finally, reasonable probability of success on the merits of a *single* claim is sufficient to satisfy the element. See *In re MONY Grp., Inc. S'holder Litig.*, 852 A.2d 9, 15 (2004).

C. Merits of Argument

- 1. The usual deference of a business judgment rule analysis gave way to enhanced scrutiny when the Board acted to facilitate a sale of the entire company.**

Enhanced scrutiny applies when an action involves the possibility of abuse or a conflict of interest. See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985). The potential for a

conflict of interest is great when, as here, the entire company is up for sale to a single buyer in an all-cash acquisition at the behest of its controlling shareholder. *Id.* ("Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.")

The enhanced scrutiny standard under *Unocal* places the burden upon directors to show their actions were not made in their own best interest and to "identify the proper corporate objectives served by their actions and justify their actions as reasonable in relationship to those objectives." *Mercier v. Inter-Tel (Delaware) Inc.*, 929 A.2d 786, 807 (Del. Ch. 2007). Under this Court's seminal ruling in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, the Board's responsibilities altered significantly when the sale of the entire company became inevitable. 506 A.2d 173, 184 (Del. 1986). "The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at the sale of the company." *Id.*

Further, when the Board was presented with its majority shareholder's proposal to sell the entire company, "the ultimate focus on value maximization [was] the same as if the board itself had decided to sell the corporation to a third party." *McMullin v. Beran*, 765 A.2d 910, 919 (Del. 2000). Even though Allen had the ability to block any final transaction, the Board was obligated to act loyally and make an informed judgment about whether the proposed transaction

would result in value maximization for all Callison stockholders. *Id.* Thus, in order to survive the enhanced scrutiny standard, the Board must demonstrate that it acted reasonably to remain loyal to Callison's stockholders and to make informed judgments in order to maximize stockholder value.

2. The DADW Standstill provision prevented the Board from acting reasonably and from making an informed judgment to achieve value maximization for minority stockholders.

In reviewing directors' conduct in a *Revlon* transaction, the Court must determine whether the decision-making process adequately informed the directors and whether they acted reasonably in light of the circumstances. *Paramount Commc'ns Inc. v. QVC Network Inc.*, 637 A.2d 34, 45 (1993). In discharging the responsibility for managing the business, the Board had an "unremitting obligation" to act in good faith and in an informed and loyal manner to maximize value for all Callison stockholders. *See Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989). Thus, the Board's insistence on the use of the DADW Standstill as part of the sale process for Callison is in direct conflict with the fiduciary duties it owed to all Callison stockholders.

i. The use of the DADW Standstill in the decision-making process failed to adequately inform the Board of the best value reasonably available.

This Court has acknowledged "there is no single blueprint that a board must follow to fulfill its duties." *Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1286 (Del. 1989). Instead, in applying enhanced judicial scrutiny, the courts decide whether the directors' decision was within a "range of reasonableness." *Paramount Commc'ns Inc.*, 637

A.2d at 45. This Court has even upheld a single-bidder approach in the interest of protecting a company's business. *In re MONY Grp. Inc.*, 852 A.2d at 21. However, the courts have established a sales process is reasonable when contractual provisions do not restrict the ability of a board of directors to fulfill known fiduciary duties. *In re Micromet, Inc. S'holders Litig.*, No. 7197, 2012 WL 68175, *9 (Del. Ch. Feb. 29, 2012).

By imposing a DADW Standstill on potential bidders, the Board was effectively ending an active auction and willfully limiting its knowledge of transaction values reasonably available to stockholders. Contractual provisions like the DADW Standstill are intended to "spur[] the bidding to new heights" by encouraging bidders to put their best foot forward. *See Revlon*, 506 A.2d at 181. However, when, as here, the provision acts to the ultimate detriment of shareholders, this Court has upheld the Court of Chancery's decision to grant a preliminary injunction. *Id.* at 185.

The Special Committee expressed concern that a protracted auction would not benefit Callison. (Mem. Op. 7-8.) Even if its concern is legitimate, the use of the DADW agreements was an unreasonably restrictive means of attempting to achieve a quick sale. The DADW Standstill acted to the ultimate detriment of shareholders by reducing the number of prospective bidders from seven to six. (Mem. Op. 10.) Further, by excluding the most interested and qualified bidders from making topping offers, the Board abandoned its duty to act as an auctioneer to obtain the maximum value for stockholders. *See Revlon*, 506 A.2d at 182.

ii. The use of the DADW Standstill prevented the Board from acting reasonably in light of the circumstances.

Even if the sales process was reasonable and adequately informed the Board, the "range of reasonableness" analysis takes into account the Board's behavior in light of the circumstances. "Because no other bidder has emerged during what I have found to be a reasonable sales process, the proposed transaction may represent the shareholders' only and best opportunity to receive a substantial premium for their shares." *In re Micromet*, 2012 WL 681785 at *13.

In Callison's case, another bidder offering a better opportunity for shareholders *did* emerge. Galena offered a materially higher bid for the entire company, but the Board unreasonably refused to waive the DADW Standstill so as to permit the topping bid. (Mem. Op. 15-16.) In making its decision to hold fast to the the DADW provision, the Board improperly assumed its actions were protected under the business judgment rule. *Id.* at 16. Since the sale of Callison is a *Revlon* transaction, heightened scrutiny of the Board's reasonableness applies.

Since Callison's minority stockholders, including Galena, had no power to influence the company's direction with their voting rights, they relied solely on the fiduciary duties owed to them by the Board in making their own decisions. In a corporation merger, minority shareholders rely heavily on information provided by the Board in deciding, for example, whether to vote in favor of the merger or seek an appraisal of the fair value of their stock. See Del. Code Ann. tit. 8, § 262 (2010). Voltaire's infamous words are more than

applicable: "With great power comes great responsibility." Here, the DADW provision inhibited the Board's great responsibility to protect minority interests in light of the changing circumstances.

While the DADW provision was designed to maximize *immediate* value for all Callison stockholders, once Galena commenced its all-cash, all-shares tender offer for Callison shares at a 4.4% over Vicente's bid, disclosing its intention to consummate an *immediate* second-step cash-out merger, the purpose of the provision was rendered moot. Even in light of the termination fee, the higher bid by Galena maximized value for Callison stockholders by \$41 million. (Mem. Op. 13, 15.)

The continued use of the DADW provision at this stage unreasonably prevented a bid materially more favorable than the Vicente Merger. See *In re The Topps Co. S'holders Litig.*, 926 A.2d 58, 63 (Del. Ch. 2007). This complete foreclosure of the opportunity to negotiate with Galena "is the legal equivalent of willful blindness." *Phelps Dodge Corp. v. Cyprus Amax Minerals Co.*, No. 17427, 1999 WL 1054255, *2 (Sept. 27, 1999). Thus, the Board failed to act reasonably in light of the circumstances and squandered its "final opportunity to negotiate on the stockholders' behalf and fulfill [its] obligation to seek the best value reasonably available." *Paramount Commc'ns Inc.*, 637 A.2d at 50.

3. The DADW Standstill agreement is invalid because the Board cannot contract away their fiduciary duties.

Broadly, "a promise that tends to induce [violation of fiduciary duties] is unenforceable on grounds of public policy." Restatement (Second) of Contracts, § 193 (1981). Under Delaware law:

It is therefore perhaps unsurprising that the Delaware law of mergers and acquisitions has given primacy to the interest of stockholders in being free to maximize value from their ownership of stock without improper compulsion from executory contracts . . . that essentially disable to the board and stockholders from doing anything other than accepting the contract even if another much more valuable opportunity comes along. *ACE Ltd. v. Capital Re Corp.*, 747 A.2d 95, 104-105 (Del. Ch. 1999).

This Court has held such provisions invalid and unenforceable “[t]o the extent that [they] purport[] to require a board to act or not act in such a fashion as to limit the exercise of fiduciary duties.” *Paramount Commc’ns Inc.*, 637 A.2d at 51 (citing *Wilmington Trust v. Coulter*, 200 A.2d 441, 452 (Del. 1964)). Several recent Court of Chancery opinions have specifically called into question the validity of DADW provisions. See Peter J. Walsh, Jr. et al., *Delaware Insider: “Don’t Ask, Don’t Waive” Standstill Provisions: Impermissible Limitation on Director Fiduciary Obligations or Legitimate, Value-Maximizing Tool?*, Jan-2013 Bus. L. Today 1 (Jan. 2013).

The *In re Celera Corporation Shareholder Litigation* Court found value in the modification of DADW Standstill agreements, stating “Plaintiffs have at least a colorable argument that these [DADW Standstill] constraints collectively operate to ensure an informational vacuum” for a board executing a sale of control. *In re Celera Corp. S’holder Litig.*, No. 6304, 2012 WL 1020471, *21 (Del. Ch. Mar. 23, 2012), *aff’d in part, rev’d on other grounds*, *In re Celera Corp. S’holder Litig.*, No. 212, 2012, 2012 WL 6707736 (Del. Dec. 27, 2012). Another recent opinion preliminarily enjoined a corporation from enforcing a DADW standstill agreement previously signed with a

potential suitor which otherwise prevented a topping bid while the sale of the entire corporation was still pending. *In re Complete Genomics, Inc. Shareholder Litig.*, No. 7888, 13 (Del. Ch. Nov. 27, 2012)

(Bloomberg Law, transcript of telephonic ruling). The court reasoned:

[A] Don't Ask, Don't Waive Standstill is impermissible because it has the same disabling effect as the no-talk clause, although on a bidder-specific basis. By agreeing to this provision, the Genomics board impermissibly limited its ongoing statutory and fiduciary obligations to properly evaluate a competing offer, disclose material information, and make a meaningful merger recommendation to its stockholders. *Id.* at 18.

Given the "unremitting obligation" of the Board's fiduciary duties, the DADW standstill is invalid because "these principles demand that corporate fiduciaries *absolutely* refrain from any act which breaches the trust reposed in them." *Mills Acquisition Co.*, 559 A.2d at 1280 (emphasis added).

II. Allen's exigent need for liquidity influenced members of the Callison board to breach their fiduciary duties to minority shareholders, including Galena, and thus implicated the entire fairness standard.

A. Question Presented

Callison arranged a sale of control at the behest of its controlling shareholder, Allen, which required a fast exit with liquidity to enter into a multi-billion dollar venture. When the directors, including four salaried executives of Allen, approved a sale despite receiving a higher offer, did they breach their fiduciary duties and implicate the entire fairness standard?

B. Scope of Review

While the proper standard of review for a lower court's decision to grant or deny a preliminary injunction is abuse of discretion, this Court gives no "deference to the legal conclusions of the trial court." *Wininger*, 707 A.2d at 40. To prevail on a motion for a preliminary injunction, a plaintiff must show: "a reasonable probability of success on the merits, irreparable harm, and a balance of equities in its favor." *Id.*

C. Merits of Argument

1. Galena has overcome the business judgment rule by demonstrating a breach of fiduciary duties that implicates the entire fairness standard.

The business judgment rule casts a wide presumption that the decisions of a board of directors were made "on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984), *overruled on other grounds*, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

A plaintiff has the burden to rebut the presumption of the business judgment rule; for example, by showing a conflict of interest is present among the board or individual directors. *See Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993), *modified in part*, 636 A.2d 956 (Del. 1994), *aff'd sub nom. Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. 1995).

The business judgment rule casts wide protection for a board of directors, but it does not apply to every transaction. Delaware courts have long held that the rule does not apply when the plaintiff casts doubt on whether the directors were informed or honestly and in

good faith believed that an action was in the best interest of the corporation. See *Stanziale v. Nachtomi*, 330 B.R. 56 (D. Del. 2004) *aff'd in part, rev'd in part*, 446 F.3d 229 (3rd Cir. 2005). "The directors of Delaware corporations have a triad of primary fiduciary duties: due care, loyalty, and good faith." *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001). In a change of control transaction, the "board must perform its fiduciary duties in the service of a specific objective: maximizing the sale price of the enterprise." *Malpiede v. Townson*, 780 A.2d 1075, 1083 (Del. 2001).

"Essentially, the duty of loyalty mandates that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally." *Technicolor, Inc.*, 634 A.2d at 361. A director who derives personal benefit from supporting a certain transaction is not considered disinterested or independent. *Id.* at 362. "Liquidity has been recognized as a benefit that may lead directors to breach their fiduciary duties." *N.J. Carpenters Pension Fund v. Infogroup, Inc.*, No. 5334, 2011 WL 4825888, at *9 (Del. Ch. Sept. 30, 2011).

Here, the directors breached their fiduciary duties by approving a sale influenced by the controller's need to liquidate its 72 percent stake in Callison. The controller, Allen, had an urgent need for liquidation because it is contractually obligated to tender a cash offer to acquire Ca' Foscari, or face a loss of millions of dollars in liquidated damages. (Mem. Op. 7.) This time-sensitive need for cash creates a conflict that triggers the entire fairness standard. See

McMullin, 765 A.2d 910; see also *In re Answers Corp. S'holders Litig.*, No. 6170, 2012 WL 1253072 (Del. Ch. Apr. 11, 2012).

2. Allen's pressing need for liquidity influenced the process by which Callison sought to sell the company.

Delaware courts have held that a "liquidity conflict" may constitute a breach of fiduciary duties, even in a pro rata transaction, when it drives a controller to seek liquidity at the expense of minority shareholders. *McMullin*, 765 A.2d 910. In *McMullin*, the court allowed minority shareholders to proceed with a claim of breach of fiduciary duty after a controller influenced the hurried sale of the company to fulfill its pressing need for liquidity. *Id.* at 922. The court held that the time constraints imposed on the sale compromised the deliberative process. *Id.* "History has demonstrated that boards 'that have failed to exercise due care are frequently boards that have been rushed.'" *Id.* (quoting *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 67 (Del. 1989)).

The undisputed facts clearly demonstrate that the sale of Callison was motivated by the controller's urgent need for liquidity. First, Allen was in need of \$2.4 billion to finance the sale of Ca' Foscari. (Mem. Op. 3.) Allen's other holdings provided no hope for attaining such a large amount of capital, because they were worth only a fraction of the Callison stock. (Mem. Op. 3.) The need for this substantial amount of cash was urgent, as Allen's bid on Ca' Foscari was not subject to a financing condition. (Mem Op. 6.) Allen needed the entire amount of cash, and Allen needed it soon—a looming deadline

in March 2013 will, if not met, cost the company \$60 million in liquidated damages. *Id.*

The structure of the entire deal, including the deal protection measures imposed by the DADW contracts, were designed *for the very purpose* of expediting the sale of Callison so Allen could get its hands on cash in the fastest manner possible. Allen's need for cash compromised the process so that the rights of minority shareholders were forfeited in favor of a hasty, but unfair, transaction.

3. *Synthes* should not change the principle that a liquidity conflict may, under some circumstances, result in an unfair deal for minority shareholders.

The Court of Chancery recently criticized *McMullin*, all the while holding it did not apply to its analysis. *In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022, 1036 (Del. Ch. 2012). Yet, *McMullin* has earned staying power in Delaware courts because it provides a remedy for minority shareholders who suffer a legitimate wrong.

i. *Synthes*, while critical of *McMullin*, was an inapposite case that did not destroy its central principle regarding the liquidity conflict.

While critical of the liquidity conflict, the *Synthes* court provided an example of where such a conflict would trigger the entire fairness standard. *Synthes*, 50 A.3d at 1036. Such a case might arise when a controller must sell quickly to satisfy an "exigent need," and fails to allow buyers a chance to do due diligence or raise funds to make a bid that reflects the fair market value. *Id.* The court explained:

In those circumstances, I suppose it could be said that the controller forced a sale of the entity at below fair market value in order to meet its own idiosyncratic need for immediate

cash, and therefore deprived the minority stockholders of the share of value they should have received had the corporation been properly marketed in order to generate a bona fide full value bid, which reflected its actual market value. *Id.*

Appellant argues that *Synthes* raises the bar for liquidity conflict claims in a pro rata transaction. For support, appellant quotes the Court of Chancery in *Synthes*, reasoning controlling stockholders are not obligated to commit "self-sacrifice" on behalf of minority shareholders, and that only extreme situations like a "fire sale" could implicate *McMullin*. *Synthes*, 50 A.3d at 1036.

The *Synthes* court openly criticized *McMullin*, calling it a "controversial decision." *Synthes*, 50 A.3d at 1041 n.91. However, this case is distinguished from *Synthes*. In fact, the court wrote that "*McMullin* is inapplicable here" because the alternative deal favored by the *Synthes* plaintiffs was not a pro rata transaction, as in *McMullin*. *Id.*

A breach of fiduciary duties is in no way automatic when the majority shareholder's need for liquidity affects the sale of control when it "deprive[s] the minority stockholders of the share of value they should have received." *Synthes*, 50 A.3d at 1036. Yet, this Court in *McMullin* recognized an important principle: that the structure and timing of a deal can be exploited by a controlling shareholder in need of a fast exit, so that minority shareholders simply do not receive the same advantages as the controller.

- ii. Delaware case law has furthered the principle that a liquidity conflict may require a remedy when a sale is unfair for minority shareholders.**

McMullin prompted the Court of Chancery to move into a more flexible direction regarding the “liquidity conflict” analysis, without sacrificing reasonable limits. It wasn’t always so. In *Sinclair Oil v. Levien*, the Delaware Supreme Court held there was no breach of fiduciary duties where a majority shareholder and minority shareholders received the same treatment. 280 A.2d 717, 722 (Del. 1971). There, the controller influenced the directors to approve dividends so large the company could not expand its operations; however, the court ruled that because the controller and minority shareholders received the same dividends, there was no breach. *Id.* This became the standard rule in Delaware courts for the next several decades, obstructing equitable remedies for minority shareholders.

McMullin set the stage for a rule that recognized the realities facing minority shareholders when a controller’s exigent circumstances influence the board of directors, poisoning the entire fairness of the transaction. Several recent cases reaffirmed this principle. In *New Jersey Carpenters Pension Fund v. Infogroup, Inc.*, a controlling stockholder in desperate need for liquidity—to repay personal loans, judgments, and kick-start a new business—forced a pro rata sale that minority shareholders claimed was below the fair value. 2011 WL 4825888, at *3. The court declined to dismiss the complaint, holding that the plaintiffs demonstrated that a liquidity conflict led to a breach of fiduciary duties. *Id.* at *11.

The court in *New Jersey Carpenters* wrote that the controller’s size, approximately 34 percent of the common stock, far outweighed the holdings of any other shareholder and thus, “while the other

shareholders did receive cash, liquidity was not a benefit to them, as it was to [the controller], because their investment in [the company] stock was already a relatively liquid asset prior to the Merger.” *Id.* at *10. Here, the disparity between Allen and other shareholders is even more pronounced than the facts in *New Jersey Carpenters*. Allen owns a 72 percent share of common stock, far outweighing any other shareholder. Liquidity alone is no benefit to the shareholders, and entire fairness demands a more thorough process to ensure the shareholders receive the highest price available. That price is available. Galena offered a deal exceeding Vincente’s by \$128 million; and perhaps, without the unreasonable deal protection measures imposed by the DADW contract, Company could have solicited even higher offers.

In another recent case, the Court of Chancery declined to dismiss a complaint involving allegations of an unfair sale of a company at the behest of a controlling stockholder with a need for fast cash. *In re Answers*, 2012 WL 1253072. The transaction, which involved many deal protection measures, was approved despite a much higher offer. *Id.* at *7. The court accepted the plaintiff’s claim that the interest in “prompt liquidation” conflicted with the interests of minority shareholders. *Id.*

The Chancery Court again applied the entire fairness test to a transaction involving the fast exit of a majority shareholder. *In re S. Peru Copper Corp. S’holder Derivative Litig.*, 30 A.3d 60 *opinion revised and superseded*, 52 A.3d 761 (Del. Ch. 2011). The court found that there were factors present in the transaction that suggested

shareholders received an unfair price. The court noted that the controller "was operating under a constraint that was not shared by all stockholders, which was his employer's desire to sell its holdings" and that it followed the controller "may not have been solely focused on paying the best price in the Merger... because he had independent reasons for approving the Merger." *Id.* at 99.

The foregoing cases do not erode the principle that a pro rata transaction is generally fair to minority shareholders and remains "a form of safe harbor" under Delaware law. *Synthes*, 50 A.3d at 1024. As the Chancery Court in *Southern Peru* noted:

[I]t would be a mistake to consider . . . [a liquidation] interest as constituting an interest in the formal sense of imposing liability of loyalty absent a showing that the director in bad faith subordinated the best interests of the company in getting a fair price to his desire to have the liquidity available to other stockholders. 2011 WL 6440761, at *19 n.68.

However, the pro rata transaction is not an unconditional safe harbor. The *Synthes* court called for an exception to the business judgment rule involving a pro rata transaction under only "very narrow circumstances." *Synthes*, 50 A.3d at 1036. Even if the Court were to accept the critique offered in *Synthes*, the factors involved the instant case justify the imposition of the entire fairness standard. Allen's pressing need for liquidity sacrificed a higher offer for the sake of a faster turnaround. This is a clear sign of bad faith, because time and liquidity lends no advantage to the minority shareholders, even though they receive the same price as Allen. The presence of additional inequitable factors, like a conflict of interest among directors, strengthens the justification for entire

fairness review. The Court of Chancery is, after all, a court of equity and “[q]uite simply, equity will not suffer a wrong without a remedy.” *Weinberger v. UOP, Inc.*, No. 5462, 1985 WL 11546 (Del. Ch. Jan. 30, 1985).

A board breaches its duty of loyalty when a majority of the board is interested in the sales process. *In re Answers*, 2012 WL 1253072, *7 (holding that directors who sought a sale seeking liquidity for controller were conflicted because they sought a benefit unique to the controller); see also *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993) (“A director is considered interested where he or she will receive a personal financial benefit from a transaction that is not equally shared by the stockholders.”). A majority of the Callison directors were interested executives of Allen, whose need for liquidity compromised the process.

The Callison directors included four salaried executives of Allen. (Mem. Op. 3.) Allen’s management, spurred by Fairmont, was involved from the very start in the plan to sell its 72 percent stake in Callison. (Mem. Op. 3-4.) Callison board members Michaels and Lieberman were involved in a search before the Callison board was officially notified of the looming sale. (Mem Op. 4.) Though the three board members without significant ties to Allen were delegated to a Special Committee, they were by no means cordoned off from Allen’s interests and had been informally made aware of Allen’s plans months before the formation of the Special Committee in October. (Mem. Op. 4-5.)

While the Special Committee expressed concern that a "protracted auction" of Callison could harm the Company, they were well aware of Allen's need for a fast turnaround and its potential to block any transaction "not in Allen's best interest," such as a transaction that didn't deliver quick cash. (Mem. Op. 6-7.) Finally, the Special Committee's role stopped short of approval of the transaction, leaving that step up to the final board, including its majority of salaried Allen executives. (Mem. Op. 5.) For practical purposes, it was difficult for the Callison board to remove itself from the distinct, overwhelming interest of Allen to receive liquidity, even at the cost of turning down a higher offer. This case should trigger an entire fairness standard.

4. A preliminary injunction is the best relief available to minority shareholders.

As the Court of Chancery noted, *McMullin* involved a favorable presumption for the plaintiffs because it was decided on a motion for summary judgment. (Mem. Op. 25.) Here, Galena asks the court to issue a preliminary injunction, which requires that the plaintiff demonstrate a reasonable probability of success on the merits, irreparable harm, and a balance of equities in its favor. *Winger*, 707 A.2d at 40.

At this stage, Galena should prevail under the heightened standard required for a preliminary injunction, because Galena has pleaded facts showing strong support that Allen's need for liquidity to purchase Ca' Foscari compelled the board to engage in a deal resulting in a lower price, detrimental to minority shareholders. In fact, the proof of harm is evident in Galena's own offer, which

surpassed the deal offered by Vincente by \$128 million. (Mem. Op. 15.) In addition, the deal was shrouded in unreasonable protection measures, and involved directors who were salaried employees of Allen and whose own interests for immediate liquidity infected the sale. “[T]he shareholders’ only realistic remedy for certain breaches of fiduciary duty in connection with a sale of control transaction may be injunctive relief.” *Police & Fire Ret. Sys. of Detroit v. Bernal*, No. 4663-CC, 2009 WL 1873144, *3 (Del. Ch. June 26, 2009). Galena respectfully asks this court to affirm the decision of the Court of Chancery to issue a preliminary injunction on the sale of Callison to Vincente.

CONCLUSION

The DADW Standstill is unenforceable because it prevented the Board from fulfilling its fiduciary duties in acting reasonably to achieve value maximization for all Callison stockholders. Even if the Court finds that the DADW is enforceable, the Board breached their fiduciary duties to minority shareholders under the entire fairness standard. For these reasons the Court should affirm the preliminary injunction granted by the Court of Chancery.

Respectfully submitted,

/s/ Team T

Counsel for Appellee