IN THE SUPREME COURT OF THE STATE OF DELAWARE

ELDON KLAASSEN, *Plaintiff and Counterclaim-Defendant Below, Appellant,* v. ALLEGRO DEVELOPMENT CORPORATION, RAYMOND HOOD, GEORGE PATRICH SIMPKINS, JR., MICHAEL PEHL, and ROBERT FORLENZA, *Defendants and Counterclaimants Below, Appellees.*	**No. 583, 2013** On appeal from the Court of Chancery of the State of Delaware, C.A. No. 8626-VCL

APPELLANT'S OPENING BRIEF

R. Judson Scaggs, Jr. (#2676)
Kevin M. Coen (#4775)
Frank R. Martin (#5636)
MORRIS, NICHOLS, ARSHT & TUNNELL LLP
1201 N. Market Street
P.O. Box 1347
Wilmington, DE 19899-1347
(302) 658-9200
Attorneys for Plaintiff and Counterclaim-Defendant

OF COUNSEL:

George Parker Young
Anne Johnson
Kelli Larsen Walter
HAYNES AND BOONE, LLP
201 Main Street, Suite 2200
Fort Worth, Texas 76102
(817) 347-6600

November 11, 2013

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Rules and Statutes

EXHIBIT A: FINAL JUDGMENT

EXHIBIT B: MEMORANDUM OPINION DATED OCTOBER 11, 2013

NATURE OF PROCEEDINGS

This is an appeal from the October 18, 2013 Final Judgment (Ex. A) of the Court of Chancery (Laster, Vice Chancellor) in an action brought by Eldon Klaassen under 8 *Del. C.* § 225 to determine the CEO and the board of directors of Allegro Development Corporation ("Allegro"). Allegro founder, director and majority stockholder Klaassen claims that during a November 1, 2012 board meeting he was improperly removed as CEO and replaced with Director-Defendant Hood. Klaassen was given no notice that these actions would occur at the meeting, was not allowed to participate in the meeting, and was excluded from pre-November 1 "board" meetings where these decisions were actually made.

After expedited discovery and a three-day trial, the Court of Chancery declined to determine the core notice, deception and fiduciary duty issues. Instead, the Court held that even if meritorious, Klaassen's claims would render the November 1 board actions voidable, not void, and so were barred by laches and acquiescence. Though the Court gave partial effect to Klaassen's later consent changing the board, Klaassen was denied any relief related to the actions taken at the November 1 board meeting. By this appeal, Klaassen challenges the portions of the Memorandum Opinion ("Opinion" or "Op.") (Ex. B) and Final Judgment upholding his removal as CEO, recognizing Hood as Allegro's CEO, and refusing to recognize Klaassen's removal of Hood as a director.

SUMMARY OF ARGUMENT

1. Fundamental board actions such as CEO removal and selection of a new CEO, when done by secret pre-arrangement, deception of and with no prior notice to a director, violate core Delaware corporate law precepts and are "void." With prior notice, Klaassen could have insured that the issues of CEO removal and replacement were considered only after full deliberations including directors acting in Allegro's best interests. Separately, covert *decisional* pre-meetings by all but one director held in violation of a bylaw notice provision make actions taken pursuant to those secret decisions likewise "void." A void action is not subject to defenses of laches and acquiescence.

2. Alternatively, Defendants did not meet their burden to establish the equitable defenses of laches or acquiescence. Almost two-thirds of the interim between the November 1, 2012 meeting and the filing of suit was spent on buyout discussions intended to avoid litigation. Just as these failed, the Director-Defendants forced Klaassen to change lawyers, and the process of hiring new counsel and preparing suit took the rest of that time. The Opinion fails to identify any causal link between the period of alleged unreasonable delay and any resulting prejudice, which in any event is so vague and general in nature that it could bar almost any Section 225 action. The surrounding circumstances omitted from the Opinion demonstrate that Klaassen did not unequivocally accept his removal.

STATEMENT OF FACTS

This appeal centers on the actions taken at the November 1, 2012 meeting of the Allegro board, the events leading up to it, and the parties' actions in the immediate aftermath. The key facts through November 1 are largely undisputed. However, the Opinion omits several important post-November 1 facts noted below.

A. At the November 1, 2012 Board Meeting, the Director-Defendants Implemented Their Prearranged Plan to Remove Klaassen and Make Hood CEO.

At a board meeting on November 1, 2012, the four Director-Defendants formalized two pre-agreed actions: (1) terminate the current CEO, Klaassen, and (2) make another director, Hood, the new CEO. The Director-Defendants spent the preceding three months deciding what would happen at this critical meeting. Klaassen, their fellow director and the majority stockholder of Allegro, was taken completely by surprise. The Director-Defendants deliberately kept Klaassen in the dark, providing him no advance notice that replacement of the CEO was even under consideration by the Allegro board, much less a done deal. The Director-Defendants also engaged in overt deception of Klaassen about what was coming November 1.

The November 1 meeting started like any other board meeting. Towards the end of the meeting, the Director-Defendants asked director Klaassen, general counsel Christopher Ducanes, and CFO Jarett Janik to leave the room. The

Director-Defendants then reaffirmed—without discussion of pros and cons—their prior decisions to replace Klaassen with Hood. Op. at 24. Those matters had already been discussed and decided, although never with Klaassen present. *Id.* The Director-Defendants asked Janik and Ducanes to return and told them that Hood was replacing Klaassen as CEO. *Id.*

The Director-Defendants then asked Klaassen to return. Michael Pehl, one of the two Series A Directors and the leader of the effort to oust Klaassen, immediately informed Klaassen that the four Director-Defendants had decided to replace him with Hood and handed Klaassen a prepared resolution that the Director-Defendants had already approved. Op. at 24; A209-12; A2776-77, A3071-72. Pehl called for a vote on the resolution, allowing no time for debate and no input from Klaassen on who would become Allegro's new CEO. The Director-Defendants voted in favor of the resolution, and Klaassen abstained. Op. at 24. Klaassen then made it clear that he disagreed with his replacement, the Director-Defendants had made an extremely poor decision, and their actions may not be legal. A2468, A2592.

The chain of events leading up to the November 1, 2012 meeting began in 2007, when the Series A shareholders invested in Allegro.

B. In 2007 and 2008 the Series A Investors Put $40 Million into Allegro.

Klaassen founded Allegro in 1984 to provide energy trading and risk management and served as its CEO and majority stockholder from inception.

In 2007 and 2008, two private equity funds, North Bridge Growth Equity 1, L.P. ("North Bridge") and Tudor Ventures III, L.P. ("Tudor") invested $40 million in Allegro in return for shares of Series A Preferred stock. Post-transaction, Klaassen owned 70% of the Company's as-converted equity. North Bridge and Tudor ("Series A Investors") owned approximately 30% of the Company on an as-converted basis. Op. at 2. The transaction conferred four categories of rights significant to this appeal.

The Composition of the Allegro Board. Following an initial deadlock on who would control Allegro's board, Allegro's key governing documents reflected an important compromise: neither the Series A Investors nor Klaassen would control the board.[1] The Series A Investors could elect three directors, and Klaassen (as the agreed-to CEO) would serve as a director. Klaassen (as holder of a majority of the common stock) could elect one common director. Klaassen (as CEO) could designate two independent directors, subject to the Series A Investors'

---

[1] Three documents governed Allegro after the transaction: (1) Allegro's Amended and Restated Certificate of Incorporation (A65-88, the "Charter"), (2) Allegro's Bylaws (A89-102, the "Bylaws"), and (3) the December 2007 Stockholders' Agreement between Klaassen and the Series A Investors (A31-64, the "Stockholders' Agreement"). Op. at 3.

approval, which was "not to be unreasonably withheld," and then election by the majority stockholder (Klaassen). A70-71 at § 3.3.1. The seven-director (3-2-2) arrangement was never implemented; the board in 2012 had five directors: (1) Pehl, a managing director from North Bridge, (2) Forlenza, a managing director from Tudor, (3) CEO Klaassen, (4) Hood, as independent director, and (5) Simpkins, as independent director.

Klaassen's Rights to Remove and Replace Allegro Directors. As Allegro's majority stockholder, Klaassen has the right to remove *any* director for cause. A93 at Art. II §10. As "designating" "Person" for the independent director seats, Klaassen also had the right to remove the independent directors without cause and without the Series A Investors' approval. A51-52 at §§ 9.2, 9.4. Klaassen, as CEO, could designate new independent directors and after approval by the Series A Investors "not to be unreasonably withheld," as majority shareholder he could elect his designees. *Id.*

The Series A Investors' Redemption Right and Liquidation Preference. The Series A Investors had the right to require Allegro to redeem their shares at any time after December 20, 2012 at a price which would be the greater of (i) the initial investment price of $40 million or (ii) "Fair Market Value," in each case plus accrued and unpaid dividends. *See* A83 at §§ 6.1-6.2; Op. at 5. In the event of a sale, the Series A Investors receive an initial liquidation preference equal to two times their investment of $40 million, plus all accrued and unpaid dividends. Op. at 6.

Klaassen's Right to Block a Sale. Klaassen had the right to block any sale of Allegro for less than $390 million. A44-45 at § 4.2; Op. at 6-7.

C. By 2012, the Series A Investors Needed an Exit Strategy That Yielded $80 Million, an Amount They Could Not Get By Redemption.

From the beginning the Series A Investors' goal was to exit Allegro in 2012. Pehl consistently told his North Bridge partners that *redemption* would yield at least $80 million ("2X"). A2706-11; A104, A111; A118, A123; A167, A169, A171. In 2012, Pehl knew that a 2X redemption exit was impossible; the only option was to convince, or coerce, Klaassen to pay $80 million. A2405 (Pehl intended for Series A to get $80 million "whatever way they could"), A2712, A3318; A138-39; Op. at 12, 27.

Independent valuations of Allegro in 2012 did not support a buyout of the Series A shares in an amount even close to $80 million. One valuation obtained by Allegro valued the Series A shares at between $39 and $47 million; a later one valued the shares at $54 million. A140-162; Op. at 12-13. Based on the first of these, Klaassen offered $60 million to buy out the Series A Investors. Op. at 12-13; A2723, A3317. The Series A Investors never obtained a valuation, but demanded $92 million (their liquidation preference). Op. at 13.

During a July 31, 2012 board meeting in which Klaassen compared Allegro's growth to its two largest competitors (who grew by acquisition), Pehl lost his temper, said he would "not listen to this anymore," and left the room. Op. at 17; A2415.[2] The Series A Investors then demanded a buyout at $80 million or a sale of the company. Klaassen would not approve a sale and again offered $60 million. Op. at 16. The parties were deadlocked. The Series A Investors that same day adopted a new strategy: replace Klaassen as CEO. *Id.* at 17-18; *see also* A163.

D. Prior to November 1, 2012, the Director-Defendants Secretly Decided to Replace Klaassen with Hood, Promising Hood the CEO Position and Other Benefits that Created a Conflict of Interest for an Independent Director.

Immediately following the July 31 board meeting, Pehl scheduled the first in a series of secret "board"/"BOD" meetings (telephonic and in person) between the Director-Defendants "excluding Eldon [Klaassen]." A164; A176; A177; A184; A186-86; A202; A1832; A530, A646. At least four such meetings were held—on August 7, August 17, October 19 and October 26—to address: (1) ousting Klaassen as CEO and (2) electing Hood as his replacement. Despite a bylaw requirement of advance notice to *all* directors of the place, date, time and

[2] Pehl denied that he lost his temper at the meeting and could not recall other parts of the meeting, but the Vice Chancellor found Pehl's testimony not credible. Op. at 17; A2722-23.

purpose(s) of special meetings, the Director-Defendants deliberately excluded Klaassen. A93 at Art. II § 7.

The Director-Defendants were vague, evasive, and contradictory about their "Board" meetings excluding Klaassen and exactly when they decided to remove Klaassen and replace him with Hood. A2731, A2736, A2759-69, A2954, A2962-63, A3296, A3326; A177; A184; A185-86; A202. All four admitted it was well before November 1, and the Court of Chancery found that "Pehl was the first to conclude that terminating Klaassen was necessary." Op. at 21-23. On August 8, 2012, Pehl emailed himself and stated "!!" and "have a board meeting, discuss the issues and remove him as CEO," and give no notice. A178; A2738-39. Pehl testified that he was "50/50" on replacing Klaassen going into the November 1 meeting, A2756-57, A2768-69, more testimony that the Court of Chancery found "not credible." Op. at 22, n. 4.

By late August, aware that they needed Hood's vote to remove Klaassen, the Series A Investors offered to make Hood the CEO. They conducted no due diligence on Hood and never looked into his shaky track record at Qumu and other companies.[3] With his job at Qumu in jeopardy, Hood quickly accepted the Series

[3] Hood had been CEO at four companies in the preceding ten years—during that period none of the four made a profit, one went into bankruptcy and one shut down, each on Hood's watch. A2976-81. Hood told Klaassen that his job at Qumu was in jeopardy because he overstated Qumu's revenue. A103; A127-37; A2392, A2985-86. In September, 2012 Hood failed to alert the Series A Investors to an overture from Allegro CFO Janik that suggested a buyout number of

A Investors' offer to be Allegro's CEO, taking a $280,000 pay cut in the process. A2392, A3065.

After being promised the CEO position Hood had a "conflict of interest," and he knew it. Op. at 19. By late September 2012, Hood knew he would replace Klaassen. A2963. Pehl not only promised Hood the CEO job once Klaassen was removed, but Hood was also promised an incentive plan tied to the Series A Investors' exit. A2971-74. Despite that clear conflict of interest, Hood continued the pretense that he was an "independent director," though Pehl knew he now had Hood's vote. Hood did not recuse himself from any vote or discussion on Klaassen's removal or even disclose to the full board the "promises" Pehl made to him. A2969, A2974-75; A538-39, A714-15. Pehl denied making these promises to Hood, but the Court rejected his testimony. A2793; Op. at 20.

Hood confirmed his secret bargain with the Series A Investors in an email he sent just before November 1 to a member of his new management team:

> Re: the comp, I am totally aligned with your position since I am in the same boat. I will have *<u>my hands on the controls after the board meeting</u>* this week. The risk, of course, is the *<u>investors back out on their promises</u>* to me. Unlikely, but possible.

A203 (emphasis added).

$70 million, a number Hood claimed he had been seeking as a "neutral mediator" because it "bridge[d] the gap" between buyout positions. A3006; Op. at 21.

The Director-Defendants had no excuse for not allowing director Klaassen—Allegro's founder, majority stockholder and the person with the most knowledge about Allegro's business—to participate in the selection of Allegro's next CEO. A2752-55, A3326-29.

E. The Director-Defendants Hid Their Plan From Klaassen and Deceived Him About What to Expect at the November 1 Meeting.

The Director-Defendants decided as a "Board" that Klaassen would be given no advance notice of their plan. *See* A178; A187-88; A362; A379; A398-99; A417; A436-37; A448; A449; A2964-65. They were reminded by legal counsel that Klaassen could change the composition of the board (also stating that not giving notice to Klaassen could look like an "ambush"). Op. at 51-52; A31, A179-83; A188.

The Director-Defendants also engaged in active deception. *See* A2450-52, A3066, A3288-89. First, the Director-Defendants postponed the scheduled October 18 board meeting multiple times, telling Klaassen that the postponements were due to scheduling conflicts. A2458-59. But in fact, the Director-Defendants needed more time to prepare their ambush, including preparing a resolution replacing Klaassen with Hood that the Director-Defendants approved before the meeting. *Id.*; A205-08. The Director-Defendants also practiced ("role-played") using a script for the November 1 meeting prepared by the Series A Investors' counsel. A187-95; A2755, A2974-75.

The subterfuge continued on the morning of November 1, when Hood sent an email to Klaassen asking about Ducanes's attendance at the meeting in connection with redemption discussions. A204; A2776-77, A3068-69, A3180-81. Hood could not tell Klaassen the real reason he asked for Ducanes's presence at the board meeting—to help effect the CEO transition—because it would have "tipped [Klaassen] off" to the ambush. A3068-69. Hood admitted that his email was "false." *Id.*; A3180-81. The Director-Defendants' ambush plan worked. Klaassen was completely blindsided.

F. Klaassen Protested His Removal, But Continued to Actively Put Allegro's Interests First.

At the November 1 meeting and in the months following, Klaassen repeatedly made clear his objections to the November 1 actions. In December, Klaassen addressed with the Series A Investors the lack of fair and full process involved in his removal and Hood's appointment and warned of shareholder litigation if a buyout resolution was not reached. A272; A242; A2467-69. The Director-Defendants discussed the possibility of Klaassen bringing litigation. A237. Klaassen also told employees that he was still CEO. A1192.

At the same time, Klaassen could not simply abandon Allegro. After Klaassen's termination, he, Hood and Ducanes discussed a consulting agreement and a possible role as "Chairman and Founder." Klaassen placed external conditions on any such agreement, including a "definitive plan for increasing the revenue and EBITDA of the company" and an agreement for an "exit" by the Series A Investors. A226-28; A234; A236; A243-72; A275-76. Disparate drafts of an agreement were exchanged, with Klaassen's mark-up eliminating an explicit reference to Hood as CEO. A216. Klaassen's external conditions were never satisfied, and no agreement was ever "approved." A226-28; A229-33. Hood drafted two alternative announcements of the CEO change, one if Klaassen was "cooperating," one "where he is not." A213-214. Due to Klaassen's continued opposition, on November 19, 2012, the Director-Defendants went with the latter announcement. A226-28; A229-33. By November 28, Hood acknowledged that the stay-on agreement discussions were dead, giving reasons in addition to hours and compensation. *Compare* Op. at 25 *with* A242. Hood also said: "Eldon has not accepted his fate. He needs time to process the fact that he is not in charge anymore." A242. The idea of a stay-on agreement was dropped.

Klaassen also attended the December 7 audit committee meeting only as an "invitee." A3048; A278. The only other relevant "audit committee" discussion occurred as part of the regular April board meeting, which all directors attended. A3046-48; A298. Klaassen attended some compensation committee meetings, as did Hood. Klaassen did not vote at any of those meetings. A2490. Klaassen was excluded from other compensation committee meetings, including one at which Hood's employment contract was allegedly approved. A2489-90, A3081. And the

Director-Defendants took steps in March 2013 to ensure that Klaassen had no role on those committees. *See* A1420-23.

The Allegro bylaws require board election of any Vice-Presidents. A95 at Art. III § 1. The Director-Defendants violated this provision, simply calling Hood's new hires "managing directors," although they had Vice-Presidents reporting to them. A2487-88; A1642-44. At some unknown point, Hood's status was secretly changed from "acting" CEO to full CEO, again without Klaassen's input or a full director vote. A2780-81, A2791-92.

G. Klaassen Worked Over Four Months on a Solution Short of Litigation, and After Allegro Forced Him to Hire New Counsel, Filed Suit on June 5, 2013.

Klaassen did not want to file a lawsuit, as he knew litigation would be slow, expensive, and public. A2470. Instead, he sought a business solution first. In late November and early December 2012, Klaassen approached the Series A Investors to again discuss a buyout of the Series A shares. A234; A236; A243-72; A273-76; A2476-77, A2781-82, A3304. Klaassen submitted a proposal of over $60 million, explaining that a buyout would "avoid shareholder litigation." A243-72; A2471-76, A2784-86, A3304.

Having applied the pressure of firing Klaassen, the Series A Investors continued to insist on an $80 million buyout price. A2122-23. Klaassen then teamed with an outside investor to offer $62.5 million, which was again rejected.

A2123. Not until early March 2013 did it become clear that Klaassen's buyout efforts had failed. A2479-82. Just as this was becoming clear, Allegro objected to Klaassen's then-choice of legal counsel, based on an alleged conflict of interest. A294-96; A2480-81. Klaassen interviewed several new law firms, and the undersigned firms were engaged to investigate Klaassen's litigation options in mid-April 2013. A3364; A3584. Within weeks this suit was filed.

No Director-Defendant testified about what would have been done differently if Klaassen more firmly proclaimed his objection to Hood as CEO. Indeed, one called that "speculation," as did the Series A Investors' lawyer. A1507. No witness testified about relying on any act or statement by Klaassen which supposedly showed acquiescence. The Director-Defendants admit that Klaassen was "adverse" to them from November 1 on. *See* A810-20; A821-86; A887-927; A928-52; A1676-78.

By letter dated June 5, 2013, Klaassen confirmed again that his removal as CEO was improper and delivered a written consent to the Company that (1) removed Hood and Simpkins as independent directors and (2) filled the resulting vacancies with non-parties Dave Stritzinger and Ram Velidi. A344-54 (the "June 2013 Consent"). The June 2013 consent also filled the Common Director seat. That same day Klaassen filed this Section 225 action. Op. at 27.

ARGUMENT

I. The Court of Chancery Erred in Holding That the Board Actions Replacing Klaassen With Hood Were Voidable, Not Void.

A. Question Presented.

Did the court err in holding that the actions of the Allegro board in removing Klaassen and making Hood CEO were voidable and not void? If void, then the only two grounds on which the Opinion holds for Defendants, laches and acquiescence, do not apply. This issue was preserved for appeal. A3439, A3462; *see also* A1540; A2220, A2246, A2252-53, A2260, A2246.

B. Standard of Review.

The Court of Chancery misapplied settled principles of Delaware law which this Court reviews *de novo*. *Bank of New York Mellon Trust Co., N.A. v. Liberty Media Corp.*, 29 A.3d 225, 236 (Del. 2011).

C. Under Delaware Law the November 1 Ambush is Void and Not Subject to Equitable Defenses.

The Director-Defendants' decisions to remove Klaassen as CEO and replace him with Hood, with no advance notice to, and deception of, Klaassen violated fundamental Delaware corporate governance precepts, and render those actions void. Separately, the Director-Defendants decisional pre-November 1 non-regular "board" meetings without notice to Klaassen also violated Allegro's bylaw requiring notice of special meetings to all directors, and likewise rendered the November 1 actions void.

1. The Director-Defendants' Actions Resulted From a Process Lacking Candor in Violation of Fundamental Precepts of Corporate Governance.

Directors of Delaware corporations owe fiduciary duties of care, loyalty and good faith to both the corporation and its stockholders. *Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998). Those duties include a director's "unremitting obligation" to deal candidly with fellow directors. *HMG/Courtland Props., Inc. v. Gray*, 749 A.2d 94, 119 (Del. Ch. 1999) (citing *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1283 (Del. 1989)).

Four opinions, with facts extraordinarily similar to those here, hold that the removal of an officer/director (or other corporate action) by ambush violates fundamental principles of Delaware law. *See Fogel v. U.S. Energy Sys., Inc.*, 2007 WL 4438978, at *3 (Del. Ch. Dec. 13, 2007); *Adlerstein v. Wertheimer*, 2002 WL 205684, at *9-12 (Del. Ch. Jan. 25, 2002); *VGS, Inc. v. Castiel*, 2000 WL 1277372, at *3-5 (Del. Ch. Aug. 31, 2000), *aff'd*, 781 A.2d 696 (Del. 2001); *Koch v. Stearn*, 1992 WL 181717, at *5 (Del. Ch. July 28, 1992), *dismissed and remanded with direction to vacate as moot,* 628 A.2d 44 (Del. 1993). This Court affirmed one of these cases, stating that the legal issues were "controlled by settled Delaware law, which was properly applied." *See VGS, Inc. v. Castiel*, 781 A.2d 696 (Del. 2001).

A director (especially when also the majority shareholder and CEO with rights to alter board composition) must be given sufficient advance notice of matters to be considered at an upcoming meeting to allow "an adequate opportunity to protect [his or her] interests." *Fogel*, 2007 WL 4438978, at *3 (quoting *Adlerstein*, 2002 WL 205684, at *10) (invalidating impermissible "ambush"); *see also VGS, Inc.*, 2000 WL 1277372, at *5; *Koch*, 1992 WL 181717, at *4-5. A director's right to advance notice "derives from *a basic requirement of [Delaware] corporation law* that boards of directors conduct their affairs in a manner that satisfies minimum standards of fairness." *Adlerstein*, 2002 WL 205684, at *9 (emphasis added). A key consideration is whether the ambushed CEO/Director could have acted to prevent his termination with prior knowledge of the other directors' plans. *See Adlerstein*, 2002 WL 205684, at *11; *Koch*, 1992 WL 181717, at *5; *Fogel*, 2007 WL 4438978, at *3-4. Whether or not the director *would have* exercised those rights is immaterial. The director must be given the *opportunity*. *See Adlerstein*, 2002 WL 205684, at *9 (stating, "[the ousted director] may or may not have exercised this power had he been told about the plan in advance. But he was fully entitled to the opportunity to do so . . . .").

This notice requirement does not run afoul of Delaware's "board-centric" system of corporate governance, but actually supports it; candor and the absence of deception are essential to any properly functioning board. Enforcing these core principles does not make Klaassen a "super-director" (Op. at 29); rather, it prevents him from becoming a second-class director and honors his bargained-for rights. Here, Klaassen's ability to insure a functioning board with truly independent directors, without conflict of interest, was rendered meaningless by the ambush.

The Opinion expresses uneasiness with the *Koch/VGS/Adlerstein/Fogel* line of cases, but avoids "grappling" with them except in a couple of footnotes by deciding the case solely on laches and acquiescence. Op. at 29-30, n.6, 9; A3530-31. Nevertheless, in a subsequent lengthy opinion (the "SQO Opinion"), the Court recognized that *Adlerstein* "[a]t first blush, appears to be a strong precedent for Klaassen" and "with four trial court decisions in his quiver, Klaassen has certainly raised fair questions that warrant further litigation on appeal." *Klaassen v. Allegro Dev. Corp.*, Del. Ch., C.A. No. 8626-VCL, Laster, V.C., at 25, 35 (November 7, 2013). The SQO Opinion spends thirty pages grappling with *Koch, VGS, Adlerstein,* and *Fogel*, even while acknowledging that "*Adlerstein* remains good law." *Id.* at 6-35. The SQO Opinion acknowledges that the core rationale of pre-*Koch* cases is to insure "meaningful participation" by all directors in major corporate decisions. *See Id.* at 9, 15-16 ("it is presumed that if the absent members had been present they might have dissented and their arguments might have convinced the majority of the unwisdom of their proposed action…") (quoting *Lippman v. Kehoe Stenograph Co.*, 95 A. 895 (Del. Ch. 1915); *Pepsi-Cola Bottling Co. of Cincinnati v. Woodlawn Canners, Inc.*, 1983 WL 18017, at *12-13 (Del. Ch.

Mar 14, 1983). Here, Klaassen was given no opportunity to participate in any meaningful fashion in two crucial decisions, either before or on November 1. He was ambushed and presented with a *fait accompli*.

The Opinion questions *Koch* because it was vacated. Op. at 29-30, n.6. Koch was vacated as moot after the removed CEO, Stearn, voluntarily resigned during the pendency of the appeal. *Stearn v. Koch*, 628 A.2d 44, 45-47 (Del. 1993) (dismissing appeal and remanding with directions to vacate as moot, but confirming that the lower court was not "precluded from again reaching the conclusion that Stearn's removal at the April 7 Meeting was invalid."). *Koch* continues to be cited by courts (most notably *Adlerstein* and *Fogel*) and law review articles nationwide, none of which have indicated that *Koch* is not good law.

As the *Koch/VGS/Adlerstein/Fogel* line of cases make clear, the CEO's performance and the company's economic circumstances are irrelevant. *See, e.g.*, *Adlerstein*, 2002 WL 205684, at *11.

In sum, the reasoning and holdings of *Koch*, *VGS*, *Adlerstein*, and *Fogel* and other Delaware cases show that the Director-Defendants' ambush violated a fundamental precept of Delaware corporate law.

2. The Opinion's Conclusion That Klaassen's Removal was Voidable, Not Void, was Flawed.

The *Koch/VGS/Adlerstein/Fogel* ambush cases uniformly also hold that when a board of directors uses deception (including what *Fogel* calls deceiving by omission) to prevent a fellow board member from validly exercising his or her rights to influence the outcome, any resulting corporate action is void or invalid. *See Fogel*, 2007 WL 4438978, at *3-4; *Adlerstein*, 2002 WL 205684, at *8; *VGS, Inc.*, 2000 WL 1277372, at *5; *Koch*, 1992 WL 181717, at *5. The Opinion dismisses these cases because they do not explicitly cite to *Michelson v. Duncan*, 407 A.2d 211 (Del. 1979). Op. at 34-35 n.9. But *Koch, Fogel,* and *VGS* all follow *Michelson's* reasoning to find the action void. Indeed, for deciding what is "void" *Fogel* cites to *Moore Bus. Forms, Inc. v. Cordant Holdings Corp.*, 1998 WL 71836 (Del. Ch. Mar. 5, 1998) which expressly followed *Michelson*. *Fogel*, 2007 WL 4438978, at *4; Op. at 35.

Pushing aside the ambush cases, the Opinion formulates a new bright-line rule that a failure to give bylaw-required notice renders an action void, but lack of notice violating a fundamental precept of Delaware board governance renders an action merely voidable. Op. at 38. This rule finds no support in Delaware law.

In *Koch v. Stearn*, three of four directors terminated Stearn, the CEO and controlling stockholder, at a meeting that had been called in accordance with the bylaws. 1992 WL 181717, at *3. Despite compliance with the bylaws, the Court held that the termination was "void and of no effect" because the other directors concealed their plan to terminate Stearn, who had the power to remove the other directors from the board, so he "was disadvantaged by the other directors' failure to communicate their plans to him." *Id.* at *5.

Similarly, in *VGS* the Court found that the defendants' purported approval of a merger by written consent was invalid, even though it complied with the notice requirements in the Delaware Limited Liability Company Act and the company's LLC agreement. 2000 WL 1277372, at *1, *5 (Del. Ch. Aug. 31, 2000), *aff'd*, 781 A.2d 696 (Del. 2001). The Court relied on the fact that the defendants had "acted in secret, without notice" in order to prevent their fellow manager from exercising his rights to block the planned action, and concluded that they "failed to discharge their duty of loyalty to [him] in good faith." *Id.* at *4. The Delaware Supreme Court affirmed the legal conclusions in *VGS,* finding that they were "controlled by settled Delaware law, which was properly applied." 781 A.2d 696. In *Adlerstein*, the Court of Chancery alternated between tenses in using variations of the word "invalid," and at one point uses the word "voidable." *See Adlerstein*, 2002 WL 205684, at *9, n.28 (the action "must be undone," following *Koch* and *VGS*).

In *Fogel*, the board (excluding Fogel) secretly met in the weeks leading up to a board meeting and decided to terminate Fogel. 2007 WL 4438978, at *1. Under the corporation's bylaws, Fogel could have called for a special meeting of stockholders to attempt to remove the other directors prior to the board meeting had he known of the secret meetings. *Id.* At the board meeting, the board "communicated [their] predetermined conclusion to Mr. Fogel by ambush." *Id.* at *4. The Court held that the board's "deceiving Mr. Fogel about their intentions by omission [was] not appropriate" and "[t]he *deception* render[ed] the meeting and any action taken there *void*." *Id.* at *3-4 (emphasis added).

Finding no support for its bright-line rule in the ambush cases, the Opinion turns to *Moore Bus. Forms, Inc. v. Cordant Holdings Corp.*, 1998 WL 71836 (Del. Ch. Mar. 5, 1998), and *Nevins v. Bryan,* 885 A.2d 233 (Del. Ch. 2005), *aff'd*, 884 A.2d 512 (Del. 2005). But neither of those cases draws the distinction in the Opinion between violation of a bylaw and violation of a fundamental principle of corporate governance. The Opinion incorrectly states that *Moore* found the conduct "void" because it involved a bylaw, but *Moore* contains no discussion of the company's bylaws, other than to point out that the board had no right under the bylaws (or any other document) to limit the plaintiff's right to information. 1998 WL 71836, at *7; Op. at 35. The same is true here. In *Moore*, a board of directors "violated Delaware corporate law precepts" when, through the use of deception, it "purposely concealed from Moore and Rogers" actions they had taken to prevent Moore from exercising any "preemptive rights" it had. *Moore*, 1998 WL 71836, at *3, *6. *Moore* actually supports Klaassen's position that the actions taken at the November 1 Meeting were void *ab initio* without a bylaw violation.

Nevins similarly does not support the Court's analysis, as it involves a bylaw violation and dramatically different circumstances of a CEO of a non-profit board accused of criminal conduct. *See Nevins*, 885 A.2d at 240-41, 246 (a non-profit board's failure to give bylaw-required notice to its recently-arrested CEO was voidable and could be statutorily ratified by shareholder approval).

The appropriate analysis is whether the board's conduct violates fundamental Delaware principles of corporate law. *See Moore*, 1998 WL 71836, at *3-6. If so, the action should be void. Chancellor Chandler's Opinion in *Solomon v. Armstrong* is instructive:

> Void acts are those acts that the board, or more generally the corporation, has no implicit or explicit authority to undertake *or* those acts that are *fundamentally contrary to public policy*. As defined by decisional law, void acts are those acts that are not performed in the interest of the corporation, irrespective of whether or not they are authorized by a corporation's certificate of incorporation.

747 A.2d 1098, 1114 (Del. Ch. 1999) (emphasis added), *aff'd*, 746 A.2d 277 (Del. 2000). The Court of Chancery's bright-line rule, in addition to ignoring *Koch*, *VGS*, *Adlerstein, Fogel*, Moore, *Solomon*, and even *Michelson*, is too rigid and formulaic to protect Delaware directors and stockholders from actions that are so fundamentally unfair that they should be void. Secrecy and deception (overt or "by omission") are the antithesis of open deliberation. In short, the Director-Defendants' failure to adhere to undeniably fundamental precepts of Delaware law renders the actions taken at the November 1 meeting void.

3. Because Allegro's Bylaws Were Violated, Klaassen's Removal is Void Even Under the Opinion's Void/Voidable Reasoning.

Even if the Opinion's distinction between bylaw violations (void) versus violations of fundamental Delaware corporate law principles (voidable) is correct, the Opinion still erred because there were serial bylaw violations. The Opinion incorrectly says, "Klaassen does not contend that the Board violated a mandatory bylaw." Op. at 39. To the contrary, in numerous places Klaassen contended, and showed, that he was deliberately excluded from secret "Board"/"BOD" meetings throughout August, September, and October, 2012, at which key corporate decisions were made. *See* A1523; A1539; A3436, A3457-58; A2253, A2261-62; A2315. These meetings violated Allegro's bylaws on special meetings and were void. *See* A93 at Art. II § 7; *see also Schroder v. Scotten, Dillon Co.*, 299 A.2d 431, 435 (Del. Ch. 1972).

II. Even if the Removal of Klaassen is Only Voidable, the Court of Chancery Erred in Holding that the Defendants Established Laches and Acquiescence.

A. Question Presented.

Did the court err in holding that the facts here constitute laches and acquiescence? This was also preserved for appeal. A3425-28; A3462-68; A2261-63; A2293-A2301.

B. Standard of Review.

The Court of Chancery's decisions on laches and acquiescence are mixed questions of law and fact, and depend on a fact-intensive application of the laches and acquiescence standards. *Poliak v. Keyser*, 65 A.3d 617, at *2 (Del. 2013) (Table) (laches); *Julin v. Julin*, 787 A.2d 82, 84 (Del. 2001). The trial court's findings of fact are accepted if not "clearly erroneous." *Poliak*, 65 A.3d 617, at *2. Once the facts are established, the issue becomes whether the trial court properly concluded that a rule of law is or is not violated, which is reviewed *de novo*. *Id.* What constitutes unreasonable delay and prejudice for laches purposes depends on the totality of circumstances. *Hudak v. Procek*, 806 A.2d 140, 153 (Del. 2002).

C. The Court of Chancery Erroneously Concluded Klaassen's Claims Were Barred by Laches and Acquiescence.

The Opinion's analysis of laches and acquiescence was based on omission of critical facts. When the entire surrounding circumstances are considered, Defendants did not meet their burden to establish either laches or acquiescence.

And in fact, the inequitable and admittedly deceptive nature of the Director-Defendants' conduct bars them from asserting an equitable defense.

1. The Defendants Did Not Establish Laches.

The affirmative defense of laches requires knowledge by the claimant, unreasonable delay in bringing the claim, and prejudice to the defendant. *Homestore, Inc. v. Tafeen*, 888 A.2d 204, 210 (Del. 2005). The Director-Defendants failed to establish any of those elements, especially the latter two.

a. Klaassen Did Not Unreasonably Delay in Filing Suit.

"Under ordinary circumstances, a suit in equity will not be stayed for laches before, and will be stayed after, the time fixed by the analogous statute of limitations at law . . . ." *Whittington v. Dragon Grp., L.L.C.*, 991 A.2d 1, 8 (Del. 2009); *see also ICA/InterActiveCorp v. O'Brien*, 26 A.3d 174, 177 (Del. 2011). Only unusual or extraordinary circumstances make the statute of limitations inequitable requiring a plaintiff to file in a shorter timeframe. *Whittington*, 991 A.2d at 8. Klaassen filed suit well within the three-year limitations period. *See Keyser v. Curtis*, 2012 WL 3115453, at *15 (Del. Ch. July 31, 2012), *aff'd sub. nom.*, *Poliak v. Keyser*, 65 A.3d 617 (Del. 2013) (Table). The Defendants' burden of proving unusual or extraordinary circumstances is not mentioned in the Opinion.

As a threshold matter, delay caused by a plaintiff's attempt to settle a dispute does not support a finding of laches. *See Poliak*, 65 A.3d 617, at *2; *see also*

Keyser, 2012 WL 3115453, at n.141; *cf. Doskocil Cos., Inc. v. Griggy*, 1988 WL 81267, at *3 (Del. Ch. Aug. 4, 1988). Klaassen engaged in settlement negotiations with the Series A Investors for several months after November 1. A2469-71, A2475-77, A2781-82, A2785-86, A2922-23; A234; A235; A243-72; A273-76; A291-93. Those negotiations—during which Klaassen made clear that the November 1 actions were not proper and could lead to "shareholder litigation"—ended in early March, 2013. A272; A2481.

Although the Court of Chancery acknowledged Klaassen's settlement attempts, it said Klaassen provided no explanation for delay after those negotiations broke down. Op. at 41. The evidence, however, shows that as buyout negotiations failed, Allegro objected to Klaassen's legal counsel based on an alleged conflict of interest. A294-96; A2480-81. Klaassen then interviewed several new law firms and hired the undersigned firms by mid-April. A3364; *see also* A793-98; A3584. This suit was filed approximately six weeks later. A344-54.

In sum, the seven-month timeframe at issue in this case, almost two-thirds of which was spent negotiating a solution short of litigation, does not support a finding of laches. *See Poliak*, 65 A.3d 617, at *2-3 (holding that delay of one year in Section 225 action did not support laches). The cases cited by the Court of Chancery do not show otherwise. *See Whittington v. Dragon Grp. L.L.C.*, 2009

WL 1743640, at *12 (Del. Ch. June 11, 2009) (delay of over two years), *remanded by*, 991 A.2d 1 (Del. 2009); *U.S. Virgin Islands v. Goldman, Sachs & Co.*, 937 A.2d 760, 808 (Del. Ch. 2007) (delay of over ten years), *aff'd*, 956 A.2d 32 (Del. 2008); *In re Sirius XM Shareholder Litig.*, 2013 WL 5411268, at *5 (Del. Ch. Sept. 27, 2013) (delay of over three years); *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 714 A.2d 96, 105-06 (Del. Ch. 1998) (finding potential laches defense did not warrant allowing party to amend complaint because the defense could be fully attacked on the merits if raised later); *Skouras v. Admiralty Enters., Inc.*, 386 A.2d 674, 682 (Del. Ch. 1978) (allowing inspection of books and records after the date the plaintiff left the company board, even though the plaintiff waited years to make the request); *Stengel v. Rotman*, 2001 WL 221512, at *1-2, 6-7 (Del. Ch. Feb. 26, 2001), *aff'd sub nom.*, *Stengel v. Sales Online Direct, Inc.*, 783 A.2d 124 (Del. 2001) (plaintiff agreed to the process he later challenged as a tactic to preserve an unrelated claim).

b. The Defendants Were Not Prejudiced as a Result of the Timing of Klaassen's Suit.

Defendants claim that vague customer and employee concerns and "perceived instability" resulted in prejudice from alleged delay. A3194-97, A3238, A3345-46. But those were non-specific hearsay and admittedly resulted, if true, from the mere *fact* that Klaassen filed suit, not from any alleged delay. A3356-57. Hood began assembling his executive team long before he took over on November 1. *See*, *e.g.*, A203. There was no evidence offered about valid, bylaw-conforming "new management" decisions that were made before or *after* buyout discussions broke down in early March. There was no direct testimony or document from any customer indicating confidence in or reliance on Hood's continued management. *See Poliak*, 65 A.3d 617, at *2 (no reliance). Under the Opinion's reasoning, if "prejudice" arises from simply putting in some portion of a new management team, a Company making unspecified commitments to customers or general concerns about "disruption" and "chaos," then ambush defendants potentially could always assert laches in a Section 225 proceeding—even when suit is filed within a week.

The Director-Defendants knew Klaassen objected to the events of November 1 and that "shareholder litigation" remained a possibility if buy-out negotiations failed. *See* A237; A272. No Director-Defendant testified at trial about what could or would have been done differently if Klaassen had sued earlier. The Director-Defendants admitted that Klaassen was "adverse" to them from November 1 on. Yet the Opinion does not state the latest date by which Klaassen should have filed suit. The Opinion fails to link even the general notion of "prejudice" to a specific period of "unreasonable" delay. The laches defense fails.

2. Klaassen Did Not Acquiesce to the Director-Defendants' Actions.

"Acquiescence arises where a complainant has full knowledge of his rights and the material facts and (1) remains inactive for a considerable time; or (2) freely does what amounts to recognition of the complained of act; or (3) acts in a manner inconsistent with the subsequent repudiation, which leads the other party to believe the act has been approved." *NTC Grp., Inc. v. West-Point Pepperell, Inc.*, 1990 WL 143842, at *5 (Del. Ch. Sept. 26, 1990). "Acquiescence will clearly bar an action when a plaintiff has shown his approval of the challenged act *by sharing in its benefits*." *Id.* (emphasis added).

"Acquiescence properly speaks of assent . . . during the progress of a transaction, while ratification suggests an assent after the fact." *Frank v. Wilson*, 32 A.2d 277, 283 (Del. 1943); *see also Giammalvo v. Sunshine Mining Co.*, 1994 WL 30547, at *10 (Del. Ch. Jan. 31, 1994) (same), *aff'd*, 651 A.2d 787 (Del. 1994). Klaassen's conduct at the November 1 meeting did not show acquiescence. A2467-68; A1498-99; A209-12. And none of the post-November 1 conduct relied on by the Court of Chancery suggests that Klaassen gave his "unequivocal approval of the transaction." *Bakerman v. Sidney Frank Importing Co., Inc.*, 2006 WL 3927242, at *18 (Del. Ch. Oct. 10, 2006) (citation omitted).

After November 1, Klaassen told employees he was still the CEO, and he warned the Series A Investors of the possibility of shareholder litigation if a resolution was not reached. A1192; A2469, A2471-75; A272. The Director-Defendants fully acknowledged the possibility of litigation and the fact that Klaassen had not "accepted his fate." A237; A242; A729. Given Klaassen's warnings, the Director-Defendants could not reasonably believe that Klaassen had accepted the validity of his removal and Hood's installation as CEO. Tellingly, no Director-Defendant or Allegro employee testified to relying in any way on an indication of acceptance by Klaassen.

That Klaassen helped Hood learn about the industry-related conference room names or suggested an industry reference work was not acceptance of the validity of the Director-Defendants' actions. Klaassen was still the majority stockholder and a director, and could not abandon Allegro or let Hood embarrass Allegro, whether he agreed that Hood was lawfully CEO or not. That Klaassen worked on drafts of a stay-on contract or that he provided comments to Hood's employment agreement [which were completely ignored] did not "freely . . . amount[] to recognition of the complained of act . . . ." *NTC Grp.*, 1990 WL 143842, at *5. Klaassen needed to watch Hood and remain informed and involved while he negotiated a buy-out of the Series A shares. No draft of any stay-on contract was ever "approved," and the Opinion simply ignores Klaassen's written preconditions to any such contract, conditions never met. A2645-46; A226-28. The breakdown in those discussions told the Director-Defendants that Klaassen was not cooperating, as evidenced by Hood's telling email stating that: "[Klaassen] has not accepted his fate." A242. That is the opposite of acquiescence.

Klaassen's actions related to the audit and compensation committees also did not show a "definite apparent assent to the acts complained of." *Frank v. Wilson*, 9 A.2d 82, 86-87 (Del. Ch. 1939), *aff'd*, 32 A.2d 277 (Del. 1943). The Director-Defendants never relied on any Klaassen-signed written consent, but sought at every turn to ignore and undermine any participation by him on those committees. Further, the April 2013 audit discussion that Klaassen attended occurred *during* the board meeting, and all directors, including Hood, were in attendance. A2489-91, A3046-50. The Court also erred in finding that Klaassen was treated as a member of the compensation committee, as he was excluded from some meetings, ignored in others, and did not vote in any. Far from looking at the totality of the circumstances, the Court ignored substantial evidence showing Klaassen did not acquiesce.

The cases cited by the Court of Chancery do not support its acquiescence holding. In *Nevins v. Bryan*, the plaintiff *officially ratified the specific actions* he later challenged. 885 A.2d at 238. The plaintiff knew the board would be discussing his employment status at a board meeting and did not contest his removal when it happened. He only brought suit in response to an attempt to dissolve the company much later. *Id.* at 242-43. Similarly, in *Papaioanu v.*

Commissioners of Rehoboth, 186 A.2d 745, 748-50 (Del. Ch. 1962), not a corporate governance case, the court found acquiescence because the plaintiff attended and participated in all relevant meetings and stood silently by even though he was asked at every meeting whether he had any objections. The Defendants even confirm that they considered Klaassen "adverse" to them from November 1 on. The Court of Chancery erred as a matter of law in holding that the acquiescence defense barred Klaassen's claims.

CONCLUSION

Klaassen respectfully requests that this Court reverse the Court of Chancery's Final Judgment and render judgment that the Director-Defendants' ambush actions—including Klaassen's removal and Hood's selection as CEO—were void and, therefore, the defenses of laches and acquiescence do not apply. Alternatively, if the ambush actions are merely voidable, Klaassen respectfully requests that this Court reverse and render judgment that Defendants failed to establish laches or acquiescence as a matter of law and, with instructions to follow the *Koch/VGS/Adlerstein/Fogel* line of cases, remand for further proceedings on Klaassen's core claims. Klaassen further requests any and all other relief to which he may be entitled.

MORRIS, NICHOLS, ARSHT & TUNNELL LLP

R. Judson Scaggs, Jr. (#2676)
Kevin M. Coen (#4775)
Frank R. Martin (#5636)
1201 N. Market Street
P.O. Box 1347
Wilmington, DE 19899-1347
(302) 658-9200

Attorneys for Plaintiff
and Counterclaim-Defendant

OF COUNSEL:
George Parker Young
Kelli Larsen Walter
HAYNES AND BOONE, LLP
201 Main Street, Suite 2200
Fort Worth, Texas 76102
(817) 347-6600

November 11, 2013

CERTIFICATE OF SERVICE

I hereby certify that on November 11, 2013, a copy of APPELLANT'S OPENING BRIEF was caused to be served upon the following counsel of record via File and Serve*Xpress*:

Peter J. Walsh, Esq.
Ryan T. Costa, Esq.
Potter Anderson & Corroon, P.A.
Hercules Plaza
1313 North Market Street 6th Floor
Wilmington, Delaware 19801

Gregory P. Williams, Esq.
Lisa A. Schmidt, Esq.
A. Jacob Werret, Esq.
Adrian D. Boddie, Esq.
Richards Layton & Finger
One Rodney Square
920 North King Street
Wilmington, Delaware 19801

R. Judson Scaggs, Jr. (#2676)