



IN THE SUPREME COURT OF THE STATE OF DELAWARE

SUSAN M. BLAUSTEIN; HILDA K.)
BLAUSTEIN TRUST, F/B/O SUSAN M.)
BLAUSTEIN, U/A DATED 8/2/72, by)
and through its Trustee SUSAN M.)
BLAUSTEIN; MORTON K.)
BLAUSTEIN TRUST U/W ITEM XVII-)
A F/B/O SUSAN M. BLAUSTEIN, by)
and through its Trustee SUSAN M.)
BLAUSTEIN; MORTON K.)
BLAUSTEIN TRUST U/W ITEM XVII-B)
F/B/O SUSAN M. BLAUSTEIN, by and)
through its Trustee SUSAN M.)
BLAUSTEIN; MORTON K.)
BLAUSTEIN TRUST U/W ITEM XVII-C)
F/B/O SUSAN M. BLAUSTEIN, by and)
through its Trustee SUSAN M.)
BLAUSTEIN; and MORTON K.)
BLAUSTEIN TRUST U/W ITEM XVIII-)
C F/B/O SUSAN M. BLAUSTEIN, by)
and through its Trustee SUSAN M.)
BLAUSTEIN,)

Plaintiffs Below/Appellants,)

v.)

LORD BALTIMORE CAPITAL)
CORPORATION and LOUIS B.)
THALHEIMER)

Defendants Below/Appellees.)

No. 272, 2013

APPEAL FROM THE
OPINION AND ORDER
DATED APRIL 30, 2013
AND THE OPINION
AND ORDER DATED
MAY 31, 2012 OF THE
COURT OF CHANCERY
OF THE STATE OF
DELAWARE IN C.A.
NO. 6685-VCN

APPELLEES' ANSWERING BRIEF

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NATURE OF PROCEEDINGS

This appeal involves a stockholder's efforts to invoke equity to obtain stock redemption rights that she failed to secure contractually. The heavily-negotiated, fully-integrated Shareholders' Agreement¹ ("Agreement") provides that Lord Baltimore Capital Corporation ("LBCC") *may* repurchase shares on terms acceptable to it and a stockholder, provided that any repurchase must be approved by a Board majority or the holders of a supermajority of LBCC's outstanding shares. In *LBCC I*, the Court of Chancery (the "Court") held that the Agreement foreclosed Susan's demand that LBCC repurchase her shares for a specific price and dismissed her Complaint in its entirety, except insofar as Susan alleged that Louis had acted as a roadblock to the Agreement's repurchase provision by denying Susan access to LBCC's Board.

Following *LBCC I*, the Board considered Susan's latest repurchase proposals (the "Proposals"). After lengthy discussion, and with the advice of its independent advisors, the Board rejected the Proposals. Susan sought leave to bring fiduciary duty claims in connection with that decision, and to "restate" a claim that Louis and LBCC failed to negotiate a stock repurchase in good faith.

¹ Unless otherwise noted, capitalized terms are as defined in Appellants' Opening Brief, cited as "AOB." Defendants refer to the 2012 Opinion as *LBCC I* and the 2013 Opinion as *LBCC II*. Unless otherwise indicated, all emphasis is added.

The Court denied Susan's motion, holding that she had failed to allege a viable fiduciary duty claim and that the Agreement does not imply a duty to negotiate.

Susan appeals that determination, but does not appeal the entry of judgment against Plaintiffs on the original promissory estoppel and fiduciary duty claims or the entry of summary judgment against Plaintiffs on the claim that Louis breached the implied covenant of good faith and fair dealing by acting as a roadblock to Board consideration of the Proposals. Susan's continuing goal, however, remains a hope to involve Delaware's courts in compelling LBCC to repurchase her shares, although for a "reasonable" price rather than one pegged to LBCC's net asset value. Susan's arguments on appeal necessarily fail because they ignore uncontested facts, they misrepresent the Court's opinion below (arguing, by way of example, that the Court held that the Agreement "displaced common law fiduciary duties" (AOB at 14), when the Court in fact held that the Agreement "does *not* necessarily foreclose Susan's fiduciary duty claim" (*LBCC II* at 34)), and they avoid any mention of binding precedent, such as this Court's decision in *Nemec v. Shrader*, 991 A.2d 1120 (Del. 2010), notwithstanding the Court's repeated citation to it.

This is Appellees' Answering Brief.

SUMMARY OF ARGUMENT

1. Denied. The Court correctly held that LBCC’s fiduciaries owe duties to LBCC and its stockholders generally, *qua* stockholders, and that their fiduciary duties do not include an obligation to Susan—an adverse party attempting to sell shares to LBCC—to repurchase her stock. To the extent Susan alleged that LBCC’s fiduciaries breached a duty to LBCC and the stockholders generally, the Court correctly held that such a claim is derivative, and properly determined that Susan failed to plead demand futility.

2. Denied. The Court correctly determined in *LBCC I* that the Agreement does not impose upon Louis and LBCC an implied obligation to repurchase Susan’s shares for consideration equal to her proportionate share of LBCC’s net asset value. In *LBCC II*, the Court properly rejected Susan’s efforts to “restate” this claim to allege that Louis and LBCC breached an implied obligation to negotiate a stock repurchase in good faith for a “reasonable” price. The Court correctly determined that such a claim would be futile, as the Agreement does not grant Susan a right to put her shares to LBCC, but grants both LBCC and any selling stockholder discretion in determining whether and at what price to buy or sell stock.

STATEMENT OF FACTS

A. Lord Baltimore Adopts a Corporate Structure Protective of Minority Interests.

In the 1930's members of the Blaustein, Thalheimer and Rosenberg families formed Atapco to consolidate their business activities. A528-29. In 1998, the families considered splitting Atapco's assets into separate companies, each owned by a different shareholder group (the "Reorganization"). A529. Although affiliated with the Blaustein group, Susan and Jeanne invested their share of Atapco assets with the business model proposed by Louis, which would become LBCC. A529, A533. Susan alleges that Louis promised her and Jeanne that they could withdraw their investment, after expiration of the 10-Year Waiting Period, through a stock repurchase and for consideration equal to their share of LBCC's net asset value. A1448-49.

Susan and Jeanne retained Cravath, Swaine & Moore to represent them in connection with the Reorganization, including by negotiating LBCC's Certificate of Incorporation ("Charter"). *See* A1381-A1405; *see also* A1702 at n.7. The Charter reflects enhanced protections for Susan and Jeanne. For example, although they each own only 17.59% of LBCC's stock (A526-27), the Charter entitles each of Susan and Jeanne to elect one member of the seven-member Board, and together elect a third independent director (A959). And although the

Thalheimer Shareholders collectively own 64.82% of LBCC's stock and have the right to appoint the remaining four directors, the Charter requires that one of those directors also be independent. A959. Thus, despite Susan's allegations of Thalheimer control, a majority of the Board is either independent or appointed by Susan and her sister. See A17, 264, 1444, 1464.

Cravath also drafted and negotiated the Agreement (A1381, A1393), which LBCC and its stockholders entered into to preserve LBCC's Subchapter S election and govern other stockholder matters, including repurchases. A76. To continue that election, the Agreement contains a number of stockholder eligibility requirements and transfer restrictions, and requires that LBCC repurchase shares at a particular price if a stockholder violates the Agreement. A83-87. Section 7(d) of the Agreement, however, makes clear that "[n]otwithstanding" its various transfer restrictions, "the Company *may* repurchase Shares upon terms and conditions agreeable to the Company and the Shareholder who owns the Shares to be repurchased" A88-89.

Like the Charter, the Agreement includes provisions that limit the authority of the Thalheimer Shareholders. For example, a stock repurchase must be approved either by (i) a majority of the Board, "being at least four" or (ii) LBCC stockholders owning at least 70% of its outstanding shares. A88-89. The Court noted that "[u]nder this structure the Thalheimer Shareholders cannot

cause Lord Baltimore to repurchase shares without the consent of Susan or Jeanne or one of the [two] independent directors” *LBCC II* at 45 n.110.

Susan alleges that she and her sister “inquired on several occasions about whether the commitment to allow [LBCC] shareholders to have their respective stock positions bought out on a full value basis, after the 10-Year Waiting Period, could be memorialized in the [Agreement].” A1449. According to Susan, Louis told her that including such a provision might jeopardize certain tax attributes of LBCC and the Reorganization, but orally assured her in October 1998 (approximately 60 days before the date of the Agreement) that the repurchase promise would be honored after expiration of the 10-Year Waiting Period. A1449-50. The Agreement, executed effective January 1, 1999, contains no right to put shares to LBCC, but it does contain an integration clause (A94), and Susan has never claimed that the Agreement fails to reflect the parties’ understanding, or is ambiguous, invalid or unenforceable. *See LBCC I* at 10, 16; *LBCC II* at 32 n.78.

B. Susan Sues to Compel a Stock Repurchase On
Certain Pricing Terms.

Susan and Louis discussed a potential repurchase on multiple occasions after the Reorganization. A536-37. Those discussions continued following expiration of the 10-Year Waiting Period, with the parties exchanging proposals for a possible repurchase of Susan’s shares, none of which led to a

transaction. A542. In July 2011, Susan sued LBCC and Louis, alleging that Louis had “failed and refused” to negotiate a repurchase of her shares “for consideration reflecting [her] proportionate share[] of the then-current value of [LBCC’s] net assets.” A15.

Susan raised three equitable claims, all directed toward enforcement of the alleged promise. *See* A286 (“[W]hether it be on a joint venture theory . . . on a promise theory [or] . . . on breach of the implied duty, that promise has to carry over to be a promise of Lord Baltimore . . .”). In addition to promissory estoppel and fiduciary duty claims, Susan alleged that Louis and LBCC breached the implied covenant of good faith and fair dealing by (a) failing to negotiate the repurchase of her stock “in good faith and consistent with the promises and representations made to induce her investment”; and (b) insisting on an “inadequate redemption price intended and designed solely to support aggressive personal tax planning objectives of the Thalheimer shareholders.” A33-34; *see also* A278.

The Court dismissed Susan’s equitable claims, concluding that the Agreement “directly addresses when [LBCC] may repurchase a stockholder’s shares and Susan’s claimed right to put her shares to Lord Baltimore at a specific price would contradict Section 7(d).” *LBCC I* at 12. In addressing Susan’s implied covenant claim, the Court invoked this Court’s precedent and explained

that one “generally cannot base a claim for breach of the implied covenant on conduct authorized by the agreement.” *Id.* (quoting *Nemec v. Shrader*, 991 A.2d 1120, 1125-26 (Del. 2010)). It noted that the Agreement grants both LBCC and the selling stockholder “discretion in determining at what price to repurchase shares,” and distinguished the Agreement from contracts where one party has unilateral discretion to take some action affecting the other’s rights, and thus the counterparty must look to the implied covenant to ensure fair treatment. *See id.* Accordingly, there could be no implied obligation on LBCC to repurchase Susan’s shares for a specific price. *Id.* at 13.

The Court dismissed the Complaint almost in its entirety, except to the extent it alleged that Louis had prevented Board consideration of Susan’s repurchase proposals because such conduct could breach the implied covenant of good faith and fair dealing inherent in the Agreement. *Id.* at 13-14. Accordingly, the Court issued an implementing order dismissing the Complaint in its entirety except to the extent Susan alleged “breach of the implied covenant of good faith and fair dealing arising out of the Shareholders’ Agreement with respect to the presentation to, and the consideration by, the Board . . . of Plaintiffs’ repurchase proposals.” *See* AOB, Ex. A.

C. Defendants Demonstrate That Louis Never
Precluded Susan's Access to the Board.

Defendants moved for summary judgment, and submitted *uncontested* evidence showing “unequivocally” that Susan’s proposals, both during and after the 10-Year Waiting Period, “were presented to, and discussed by, the Board.” *LBCC II* at 9-10. This evidence included a January 20, 2011 report from Louis to the Board regarding the “status of discussions regarding the potential redemption” of Susan’s shares, and evidence showing that in 2005 the Board approved the voluntary repurchase of Susan’s interests in an LBCC affiliate—at fair market value and at a 52% discount to net asset value. *Id.* at 9-10; A1088; A1377.

To dispel any suggestion that Louis had precluded Board consideration of Susan’s proposals, the Board met on July 5, 2012 to review, consider and formally vote on Susan’s latest repurchase proposals (*i.e.*, the Proposals), which Susan set forth in correspondence dated April 6, 2010 and June 16, 2010 (and renewed in a July 2, 2012 “position statement”). *See* A1200; A1215-25. Before the meeting, management also circulated to the Board Susan’s July 2, 2012 position statement which, among other things, set forth Susan’s narrative of the facts leading up to the Proposals and gave Susan’s recommendations. *See* A1200; A1213.

During the July 5 meeting, the Board engaged in a robust, three-hour discussion and consideration of the Proposals. *See* A1199, A1213. The Board reviewed LBCC's audited financial statements as of December 31, 2011 and management-prepared financial statements as of March 31, 2012, along with an equity "roll-forward" to May 31, 2012. *See* A1227-68. The Board also reviewed materials provided by several independent, outside advisors—specifically, reports provided by American Appraisal Associates and McGladrey LLP, *see* A1270-1355, as well as the analysis of Cambridge Associates, which advised the Board regarding the implications of a repurchase on LBCC's investment policy goals and liquidity. *See* A1358-75.

In addition to copies of *LBCC I* and its implementing order, the Board also considered the fact that the pricing of prior Board-approved spin-offs, distributions and repurchases by LBCC affiliates had taken into account lack of control and lack of marketability discounts, *see* A1377, and other facts related to claims asserted in the litigation, *see* A882-925, A944-49, A1379-1405. At the conclusion of the meeting, only two (and in one case three) directors favored Susan's repurchase proposals, with a majority of the directors concluding that the Proposals were inadvisable and not in the best interests of Lord Baltimore and its stockholders. *See* A1208-10. Moreover, only three directors favored Susan's request—set forth in her position statement and brought to a vote at the July 5

meeting—that her Proposals be considered by a committee of independent directors. *See* A1211.

D. Susan Again Attempts to Secure a Court-Ordered Repurchase of Her Shares and Seeks Leave to “Restate” Her Implied Covenant Claim.

Although presenting no evidence in opposition to Defendants’ motion for summary judgment, Susan also sought leave to supplement her Complaint (or what little remained of it) to challenge the Board’s decisions not to buy-back her shares on her terms or to appoint a committee. Specifically, Susan alleged that the Thalheimer Shareholders and the Director Defendants had personal, self-interested reasons for rejecting her Proposals, which she claims compromised their duty of loyalty to her. A1625-26; A1635-36. She claimed that the Individual Defendants “breached this fiduciary duty of loyalty to Susan” by (1) rejecting her request that the Proposals be considered by a committee of independent directors; and (2) voting to “reject a [repurchase] proposal by Susan that was, on its face, reasonable and in the interest of [LBCC] and all of its shareholders.” A1636.

Susan also sought leave to amend or “restate” that portion of her implied covenant claim that the Court dismissed in connection with *LBCC I*. Susan no longer claimed that the Agreement imposed an obligation to repurchase her shares on specific price terms that were “consistent with the promises and representations made to induce her investment,” but now asserted an implied

obligation to negotiate “in good faith” for “fair and reasonable terms.” A1633-35. Whereas Susan originally alleged that she expected to “receive consideration of, or close to, her full *pro rata* share of the then-current asset value of the corporation,” she now claimed that she believed her stock would be repurchased “in a fair and reasonable manner—or at a minimum, that Louis would negotiate in good faith toward such a result.” A1619. And rather than seeking an order requiring LBCC to repurchase her stock for consideration equal to her proportionate share of net asset value, Susan now asked that the Court order LBCC and the Director Defendants “to consider, evaluate, respond to, and negotiate in good faith with respect to” her repurchase proposals. A1637-38.

E. The Court Grants Defendants’ Motion for
Summary Judgment.

The Court decided both Defendants’ motion for summary judgment and Susan’s motion for leave to file an amended and supplemental complaint in *LBCC II*. With respect to the summary judgment motion, the Court held that the “record amply demonstrates that the Board was more than aware of the buyout discussions between [Susan] and Louis,” and noted that Susan’s “representatives on the Board could have—at any time—requested a vote on Susan’s offers.” *LBCC II* at 15. The Court found as well that the July 2012 Board meeting “supports [LBCC’s] contention that Susan was not denied access to the Board.”

Id. Accordingly, the Court decided that “Defendants were entitled to judgment as a matter of law on Susan’s implied covenant claim that Louis has precluded Susan access to the Board,” (*Id.* at 15-16), a decision Susan does not appeal.

F. The Court Denies Plaintiffs’ Motion for Leave to
File a Supplemental Breach of Fiduciary Duty
Claim as Futile.

With respect to Plaintiffs’ motion, the Court rejected Susan’s newly-minted fiduciary duty claims, determining that such claims could not survive a motion to dismiss, and would thus be futile. The Court turned first to Susan’s allegation that the Individual Defendants breached fiduciary duties of loyalty to Susan in voting against her proposal that the Board delegate its authority to approve a stock repurchase to a committee of “one or more truly independent directors,” which Susan proposed should include Mr. Kilpatrick. *See id.* at 32-33; A1626, A1637-38. It noted that the Agreement expressly requires that any stock repurchase be approved by either “(1) at least four of the directors (a majority) or (2) 70 percent or more of the beneficial shareholders,” and concluded that this provision precluded Susan’s fiduciary duty claim as a matter of law. *LBCC II* at 32 & n.76 (“Indeed, the creation of an independent committee would, as the Defendants argue, sanction a ‘process that is inconsistent with Section 7(d) of the Shareholders’ Agreement.’”).

The Court then addressed Susan’s allegations that the Defendants breached their fiduciary duty of loyalty to her by rejecting her repurchase proposals. *Id.* at 33. Although Susan argues on appeal that the Court held that the Agreement “displaced common law fiduciary duties” (AOB at 14), the Court in fact held that the Agreement “does *not* necessarily foreclose Susan’s fiduciary duty claim that alleges that the Board had a duty to accept a reasonable repurchase proposal.” *LBCC II* at 34. The Court addressed—on the merits—the core question of whether the Individual Defendants “owed a fiduciary duty to Susan, as a minority shareholder, to accept her reasonable repurchase proposal.” *Id.* at 35.

The Court answered that question in the negative. Relying on this Court’s precedent in *Nixon v. Blackwell* and *Riblet Products Corp. v. Nagy*, the Court explained that the fiduciary duties owed by directors and controlling stockholders to minority stockholders are those that the fiduciaries of a corporation “owe to all shareholders generally” *LBCC II* at 42. It further explained that “*Nixon* and *Nagy* confirm that Delaware law does not recognize that a majority stockholder has a special fiduciary duty to minority stockholders in a closely-held corporation,” and accordingly, “a controlling stockholder generally does not have a fiduciary duty to buy back a minority stockholder’s shares.” *Id.* at 41-42.

The Court also noted that, in this case, Susan and LBCC have been engaged in “arms-length negotiation over the terms by which [LBCC] might

repurchase her shares” *Id.* at 43. In that connection, Susan’s interests “in obtaining a higher redemption price [are] in opposition to the interests of [LBCC] and its shareholders generally.” *Id.* Citing to this Court’s decision in *Crosse v. BCBSD, Inc.*, the Court noted that a fiduciary relationship typically cannot exist between parties where they stand at arms-length, and their interests are not aligned. *Id.* at 43 & n.107. In these circumstances, the Court opined that granting “Susan the right to be bought out would turn the relationship between majority and minority stockholders on its head.” *Id.* at 44. It determined that Susan had failed to set forth a viable claim for breach of fiduciary duty, concluding that “Susan has not shown—as a matter of law—that there is a special fiduciary duty owing to her particularly, as opposed to all shareholders generally.” *Id.* at 46.

The Court recognized, however, that the Individual Defendants owe LBCC and its stockholders, *qua* stockholders, fiduciary duties with respect to their consideration of Susan’s repurchase proposals. In this regard, the Court observed that the supplemental complaint might be read as alleging that the Individual Defendants breached a fiduciary duty to LBCC insofar as they deprived it “of a valuable investment opportunity (the purchase of [Susan’s] shares at the discount she offered)” due to their alleged personal self-interest. *Id.* at 46-47. The Court explained, however, that “unlike [Susan’s] previous claims, this allegation is derivative because the corporation suffered an alleged harm and would benefit

from any recovery of monetary damages.” *Id.* at 47. The Court held that Susan’s supplemental allegations were fatally defective in that regard, as she had not made a demand on the Board, nor adequately alleged demand futility. *Id.* It further held that Susan failed to allege that the Director Defendants breached their duty of care to LBCC and its stockholders generally, reasoning that Susan failed to allege facts suggesting that the Director Defendants failed to act in an informed manner with respect to her repurchase proposals. *Id.* at 48 n.118

G. The Court Holds That the Agreement Does Not
Include an Implied Obligation to Negotiate in
Good Faith.

The Court also properly denied Susan’s motion to amend the Complaint to “restate” her claims that Defendants failed to negotiate with her in good faith toward a reasonable price, as opposed to a price certain. It recognized that in *LBCC I* it “did not specifically address whether the Defendants breached the implied covenant of good faith and fair dealing by failing to negotiate in good faith toward a reasonable price, ” and suggested “that Susan failed to make this claim in her [original] Complaint.” *LBCC II* at 16 & n.27.

But regardless of whether the claim originally had been alleged, the Court concluded that it would not survive a motion to dismiss for the same reasons offered in *LBCC I*. *Id.* at 20-21. Specifically, “as [it] observed before,” the Agreement affords LBCC discretion in determining at what price to repurchase

shares, and Susan discretion in determining what price she will accept. *Id.* It concluded that an obligation to negotiate in good faith would “contradict the language and purpose of the Shareholders’ Agreement, which is to afford the parties bilateral discretion in determining whether to buy or sell shares.”² *Id.* at 21.

The Court also explained that even if Susan originally alleged an implied obligation to negotiate in good faith, and even if that claim survived *LBCC I*, Susan had submitted no showing that Louis and LBCC acted in bad faith. *Id.* at 19. Although Susan conclusorily alleged that Louis and LBCC insisted that any repurchase be at a 52% discount to net asset value, and that such discount is unconscionable, she offered no evidence that LBCC determined it would never repurchase Susan’s shares or had repurchased shares from others on terms not offered to Susan, and failed to rebut evidence showing that Susan “previously accepted similar discounts in other transactions with [LBCC] and that the fifty-two percent discount was supported by independent third party analysis.” *Id.* at 19-20; *see also* A1377; A1301, 1316. The Court accordingly had ample justification to reject Susan’s revised implied covenant claim.

²

Contrary to Susan’s argument on appeal, the Court did not determine that the repurchase provision in the Agreement “entirely eclipses the implied covenant” (AOB at 31), but rather that, in these circumstances, the implied covenant of good faith and fair dealing does not give rise to a “right (or obligation) to negotiate at all.” *LBCC II* at 20. Susan simply conflates a determination that there is no implied covenant (which the Court did not do) with a determination as to the scope of its obligations (which the Court did).

ARGUMENT

I. THE COURT OF CHANCERY PROPERLY REJECTED SUSAN'S BREACH OF FIDUCIARY DUTY CLAIMS ARISING OUT OF THE JULY 5, 2012 BOARD MEETING.

A. Question Presented

Did the Court of Chancery properly determine that the Individual Defendants have no fiduciary obligation to Susan (1) to authorize a process for the consideration and approval of repurchase proposals at complete variance with the process set forth in the parties' negotiated Agreement and (2) to cause LBCC to repurchase her shares on the terms she had proposed?

B. Scope of Review

A trial court's decision to grant or deny a motion to amend or supplement a pleading is ordinarily reviewed for abuse of discretion. *See Shiveley v. Klein*, 551 A.2d 41, 44 (Del. 1988). But where, as here, the trial court denies leave to amend on the ground that the supplemental allegations are futile, and would not survive a motion to dismiss, its determination is reviewed *de novo*. *See Price v. E.I. DuPont de Nemours & Co.*, 26 A.3d 162, 166 (Del. 2011) (explaining that an amendment is futile where it would be subject to dismissal under Rule 12(b)(6) and that the grant of a Rule 12(b)(6) motion to dismiss is reviewed *de*

novo to “determine whether the trial judge erred as a matter of law in formulating or applying legal precepts”).

C. Merits of Argument

The Court properly rejected Susan’s motion to supplement. Insofar as Susan alleged that the Individual Defendants breached a fiduciary duty to her by refusing to form a special committee to consider her repurchase proposals, that claim is precluded by the Agreement, which was agreed to by Susan and the other LBCC stockholders, and which sets forth a specific approval mechanism with respect to stock repurchases. Moreover, the Individual Defendants owe fiduciary duties to LBCC and its stockholders generally, *qua* stockholders, and do not owe Susan a special fiduciary obligation to accept her stock repurchase proposals. And to the extent the Individual Defendants’ conduct at the July 5, 2012 meeting implicated their fiduciary duties, any claim in that regard would be derivative, but Susan has failed to plead demand futility.

1. The Agreement Precludes Susan’s Demand That Her Repurchase Proposals be Considered by a Committee.

Susan’s claim that the Individual Defendants breached their fiduciary duties by voting against her request that the Board impanel a committee of “one or more” independent directors to “evaluate and decide on matters relating to redemptions as recommended in Susan’s Position Statement” violates the express

terms of the Agreement and accordingly fails as a matter of law. A1463-64, A1466-67.

As this Court made clear in *Nemec v. Shrader*, it “is a well-settled principle that where a dispute arises from obligations that are expressly addressed by contract, that dispute will be treated as a breach of contract claim.” 991 A.2d at 1129. *Nemec* explained that, in such circumstances, “any fiduciary claims arising out of the same facts that underlie the contract obligations would be foreclosed as superfluous.” *Id.*

Here, Susan agreed that share repurchases may *only* be approved by a majority of the full Board—*i.e.*, not less than four directors—or the holders of a supermajority of LBCC’s shares. A88-89. As the Court noted in *LBCC II*, the creation of a special committee to consider Susan’s repurchase requests would sanction a process inconsistent with the Agreement. *LBCC II* at 32 n.76. Accordingly, the Court correctly held that “to the extent [Susan] complains about the procedure employed by the Board in considering her repurchase proposals, that claim is foreclosed by the plain language of the Shareholders’ Agreement, which governs the parties’ dispute in this respect.” *Id.* at 32-33.

2. The Individual Defendants Do Not Owe Susan a Fiduciary Duty to Repurchase Her Shares.

Susan also fails to state a claim that the Individual Defendants breached their fiduciary duty of loyalty to *Susan* by rejecting her repurchase proposals at the July 5, 2012 meeting. This is because the Individual Defendants do not owe Susan—a would-be seller with interests adverse to those of LBCC—a fiduciary duty to repurchase her shares apart from the duties owed LBCC or its stockholders generally, in their capacity as stockholders.

It is well-settled that a “director’s fiduciary duty runs to the corporation and to the entire body of shareholders generally, as opposed to specific shareholders or shareholder subgroups.” *Gilbert v. El Paso Co.*, 1988 WL 124325, at *9 (Del. Ch. Nov. 21, 1988), *aff’d*, 575 A.2d 1131 (Del. 1990). Thus directors do not owe “unique” duties to individual shareholders apart from the duties owed to the “Company and the other shareholders.” *Nemec v. Shrader*, 2009 WL 1204346, at *4 (Del. Ch. Apr. 30, 2009), *aff’d*, 991 A.2d 1120 (Del. 2010).

Riblet Products Corp. v. Nagy is instructive. There, this Court was asked to consider whether majority stockholders of a closely-held corporation owed fiduciary duties to a minority stockholder in connection with that stockholder’s position as the Company’s chief executive officer. 683 A.2d 37, 37 (Del. 1996). Although it noted that the majority stockholders “may well owe

fiduciary duties” to the minority stockholders, this Court nonetheless held that the stockholder’s rights as an employee “are separate from his rights as a stockholder.” *Id.* at 40. Put simply, the allegations in *Riblet*, like Susan’s claims as a would-be seller of an asset, did not implicate fiduciary duties owed minority stockholders *qua* stockholders. *Id.*

Susan’s reliance on *Nixon v. Blackwell*, 626 A.2d 1366 (Del. 1993), further highlights the infirmities in Susan’s proposed supplemental pleading. In *Nixon*, certain of the company’s stockholders challenged the board’s decision to issue an employee stock option plan (ESOP) and key man life insurance policies, which provided the corporation’s employee-stockholders (including its directors) with a means of liquidating their equity, but did not provide similar liquidity options to the nonemployee stockholders. *Id.* at 1370-73. This Court affirmed the trial court’s decision to apply entire fairness review to the ESOP and life insurance policies, reasoning that because the “defendants benefited from the ESOP and could have benefited from the key man life insurance *beyond that which benefited the other stockholders generally*, the defendants are on both sides of the transaction . . . [and] [f]or that reason . . . entire fairness review applies.” *Id.* at 1375.

Nixon thus stands for the proposition that fiduciary duties are implicated where controlling stockholders and directors take an action that provides them a personal benefit not shared by the corporation or its stockholders

generally, and not—as Susan contends—whenever the corporation’s or majority stockholders’ interests diverge from those of a particular stockholder. This Court in *Nixon* made clear that a stockholder’s right to have his or her shares purchased—or any other asset for that matter—should be governed by contract, not fiduciary duty, and expressly warned against the very outcome Susan seeks in this litigation. *See id.* at 1380 (explaining that it would “do violence to normal corporate practice and our corporation law to fashion an ad hoc ruling which would result in a court-imposed stockholder buyout for which the parties had not contracted”); *cf. Crosse v. BCBSD, Inc.*, 836 A.2d 492, 495-96 (Del. 2003) (holding that the relationship of an insurer and its insured is one of a contractual, not fiduciary nature, since the parties have divergent interests). Indeed, this Court in *Nixon* quoted with approval the trial court’s disclaimer that its opinion *does not* “suggest[] that there is some generalized duty to purchase illiquid stock at any particular price.” *Nixon*, 626 A.2d at 1375.

In short, where, as here, Susan seeks to sell an asset to LBCC (be it her home, a car, or in this case, stock), she does not have a personal “right to a non-conflicted corporate decision on whether a repurchase will be approved and at what price.” AOB at 26. The Individual Defendants owe fiduciary duties to LBCC and its stockholders, *qua* stockholders, but not to Susan as an arms-length commercial counterparty with interests adverse to those of the corporation.

Accordingly, the Court correctly concluded that Susan failed to state a claim that the Individual Defendants owe her a fiduciary duty to repurchase her stock.

3. To the Extent Susan Claimed a Breach of Fiduciary Duty to LBCC and its Stockholders Generally, That Claim is Derivative, and Susan Failed to Allege Demand Futility.

Although Susan primarily based her proposed fiduciary duty claim upon an alleged duty of loyalty owed to her in her capacity as a would-be seller of stock, she nevertheless claimed that the Individual Defendants furthered their personal tax interests, “rather than the best interests of [LBCC] and its shareholders as a whole,” and in doing so engaged in “corporate decision-making that was not entirely fair to [LBCC] and its shareholders as a whole” A1635-37.

To the extent Susan sought to allege that the Individual Defendants deprived LBCC of a favorable opportunity to repurchase her stock, and did so for personal reasons, the claim would be derivative. *See Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004). But Susan did not make a pre-suit demand on the Board and has failed to allege facts creating a reasonable doubt that a majority of the Board lacks independence, such that demand would be excused as futile. *See Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

Of the seven directors, Susan does not challenge the independence of her and Jeanne's three Board designees, and with respect to Donald Kilpatrick—a fourth director who qualifies as independent under LBCC's governing documents and who Susan argues should have been included on a committee of independent directors to consider her repurchase proposals—claims only that he “was appointed by the Thalheimer Shareholders and owes his continued position as director to the Thalheimer Shareholders.” AOB at 5. Such allegations, without more, are insufficient to impugn a director's independence under Delaware law. *See Beam*, 845 A.2d at 1054 & n.37 (explaining that the fact that a stockholder “who nominates or elects the directors is not sufficient to raise a reasonable doubt about a director's independence”) (citation omitted).

II. THE COURT CORRECTLY HELD THAT THE IMPLIED COVENANT DOES NOT INCLUDE AN OBLIGATION TO NEGOTIATE IN GOOD FAITH TOWARD A “REASONABLE” PRICE.

A. Question Presented

Does the Agreement imply an obligation upon LBCC and Louis to negotiate with Susan a stock repurchase in good faith where it otherwise provides that LBCC “*may*” repurchase shares and where it gives both LBCC and a selling stockholder discretion in determining the price at which the shares may be bought or sold?

B. Standard of Review

In this appeal, Susan has argued that her claim for an implied obligation to negotiate in good faith was part of “her original allegations” or (inconsistently) that it was a “new” claim she sought to add after the decision in *LBCC I*. See AOB at 29.

Although Susan originally demanded that LBCC repurchase her stock based on LBCC’s net asset value (premised upon Louis’s alleged promise), and not that Defendants be compelled to negotiate an indeterminate “reasonable” price—to the extent she originally alleged a duty to negotiate simply in good faith, and to the extent the Court dismissed that claim in *LBCC I*—the decision should be reviewed *de novo*. See *Schoon v. Smith*, 953 A.2d 196, 200 (Del. 2008). Similarly, to the extent the claim had been originally alleged, but survived *LBCC I* and was thus

part of the operative pleadings at the time Defendants moved for summary judgment requesting that the action be dismissed with prejudice and judgment be entered against Plaintiffs on all claims, the Court's grant of summary judgment is subject to *de novo* review, and its factual findings will be affirmed if they are clearly supported by the record and the conclusions drawn from the findings are the product of an orderly and logical reasoning process. *See In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 48 (Del. 2006).

To the extent Defendants' motion for summary judgment "pre-dated" Susan's "new implied covenant claim" (AOB at 27, 29), the Court's decision to deny Susan leave to add the claim—after she stood on her original complaint in the face of Defendants' motion to dismiss—is subject to review for an abuse of discretion under Court of Chancery Rule 15(aaa). *See Braddock v. Zimmerman*, 906 A.2d 776, 783 (Del. 2006) (explaining purpose of Court of Chancery Rule 15(aaa), noting that a plaintiff must make an election and that "if a plaintiff chooses to file answering brief in opposition to a motion to dismiss rather than amend the complaint, any subsequent dismissal pursuant to the motion is with prejudice" absent a finding of good cause).³

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The Court also concluded that the proposed amendment would be futile (*LBCC II* at 17 n.30), a determination subject to *de novo* review.

C. Merits of Argument

1. The Agreement Does Not Imply an Obligation to Negotiate in Good Faith Toward a Reasonable Repurchase Price. _____

Regardless of whether the implied covenant claim was included in her original complaint or proffered as a new claim, the judgment below should be affirmed because the Agreement, as a matter of law, does not imply an obligation to negotiate in good faith toward a “reasonable” price. As the Court held below, a requirement that LBCC (or Susan for that matter) negotiate in good faith toward a reasonable repurchase price would contradict the discretion afforded to both parties under the Agreement, and is accordingly fatal to Susan’s implied covenant claim.

Delaware law calls for judicial restraint when analyzing allegations that a party has breached the implied covenant of good faith and fair dealing. See *Nemec v. Shrader*, 991 A.2d at 1125 (explaining that the implied covenant of good faith and fair dealing “involves a cautious enterprise”). This Court in *Nemec* made clear that the implied covenant cannot be “used to circumvent the parties’ bargain, or to create a ‘free-floating duty . . . unattached to the underlying legal document.’” *Id.* at 1126 & n.18 (citation omitted).

Susan’s claim that LBCC and Louis owe her an obligation to negotiate in good faith toward some reasonable repurchase price is an attempt to create a free-floating duty separated from the approval requirements of Section

7(d). The parties entered into the Agreement to preserve LBCC’s Subchapter S election. To that end, the Agreement contains a number of stock transfer restrictions, but nonetheless allows LBCC to repurchase stock on terms agreeable to it and a selling stockholder, provided the repurchase is approved by a majority of the Board or holders of a supermajority of the stock.

The Agreement makes clear that LBCC *may* repurchase stock on terms agreeable to it and a selling stockholder, and nowhere “connotes an expectation of cooperation” toward a repurchase as Susan suggests. AOB at 32. That the Agreement cannot logically support the implied covenant for which Susan argues is confirmed by her gross mischaracterization of the Agreement; Susan contends (at pages 31-32 of her brief) that it “sets forth a process for redemption, but it postpones for a later day the price determination to be made with the simple statement the repurchase *will* occur on terms and conditions ‘agreeable to the Company and the Shareholder’” Susan’s slight-of-hand—changing “may” to “will”—is an attempt to create an implied put right that is absent from, and inconsistent with, the unambiguous terms of a heavily-negotiated and fully-enforceable Agreement.⁴

⁴ As the Court explained in *LBCC I*, “[t]his case does not present a situation where only one party to a contract has discretion, and thus, the other party must look to the implied covenant to obtain any sort of relief.” *LBCC I* at 12. Nor does this case present a
(Continued . . .)

2. Susan Cannot Use the Implied Covenant to Secure a Better Bargain Than She Negotiated for Originally.

That Susan specifically negotiated for, but failed to secure, a right to require LBCC to repurchase her stock further undermines her claim.

In *Nemec*, this Court made clear that the implied covenant applies “only to developments that could not be anticipated,” and explained that in “conducting this analysis,” courts should “assess the parties’ reasonable expectations at the time of contracting and not rewrite the contract to appease a party who later wishes to rewrite a contract he now believes to have been a bad deal.” 991 A.2d at 1126; *see also id.* at n.20 (“[A] court can only imply a contractual obligation when the express terms of the contract indicate that the parties would have agreed to the obligation had they negotiated the issue . . .”). Indeed, this Court in *Nemec* cautioned against the very position Susan has taken in this litigation, instructing that the “implied duty of good faith and faith dealing is not an equitable remedy for rebalancing economic interests after events that could

(. . . continued)

situation where one party has a right to a first offer and where an implied obligation may be necessary to ensure that the counterparty offers good faith terms. *See LBCC II* at 20. Here, there are no such gaps to fill. Under these circumstances, “Susan cannot leverage her status as a minority stockholder to compel the Company to offer her favorable repurchase terms.” *LBCC II* at 44.

have been anticipated, but were not, that later adversely affected one party to a contract.” *Id.* at 1128.

This Court’s recent opinion in *Gerber v. Enterprise Products Holdings, Inc.*, relied upon heavily by Susan in her brief, echoes the concerns raised in *Nemec*. In *Gerber*, this Court explained that the implied covenant “does not ask what duty the law should impose on the parties given their relationship at the time of the wrong, but rather what the parties would have agreed to themselves had *they considered the issue in their original bargaining positions at the time of contracting.*” 67 A.3d 400, 418 (Del. 2013). Put simply, a court “confronting an implied covenant claim asks whether it is clear from what was expressly agreed upon . . . [whether] the parties would have agreed to proscribe the act later complained of as a breach of the implied covenant of good faith—*had they thought to negotiate with respect to that matter.*” *Id.*

According to Susan’s own allegations, at the time of the Reorganization, she and Jeanne inquired on several occasions whether the Agreement could contain a right to put stock to LBCC at a set price, but Louis refused. A1449-50. By Plaintiffs’ own admission, the issue of stock repurchases was certainly considered at the time of contracting, and the fact that the Agreement speaks no more to the issue other than to give LBCC and a selling stockholder complete discretion with respect to share repurchases is fatal to Susan’s claim. An

implied right to cause LBCC to repurchase stock, or negotiate to that end, when the parties' rights with respect to repurchases were considered and expressly negotiated, but ultimately not incorporated into the final agreement, would serve only to provide Susan with economic benefits which she and her sophisticated counsel (who drafted the Agreement (*see* A1381, A1393)) sought but did not obtain at the time of the Reorganization.

3. Defendants Submitted Uncontroverted Evidence That They Have Acted in Good Faith, and Susan Failed to Show Good Cause for the Proposed Amendment.

Even if one assumes that Susan originally pled a duty to negotiate in good faith and that such claim had survived *LBCC I* and its implementing order, and further assumes that the implied covenant claim does not fail as a matter of law, the Court's judgment nonetheless should be affirmed because Susan failed to rebut evidence, submitted in connection with Defendants' summary judgment motion, which demonstrates that Defendants have acted in good faith.

Susan argues not only that the Agreement requires Defendants to negotiate in good faith toward a reasonable stock repurchase, but that they acted in bad faith by allegedly insisting upon a 52% discount to net asset value. *See* A1633-34. Susan claims that such discount is "unconscionable" because it "would have resulted in a redemption price even more severe than the penalty under the

Shareholder Agreement for acts threatening [LBCC's] qualification as an 'S' corporation." AOB at 9-10. In connection with their summary judgment motion, however, Defendants put forth un rebutted evidence that the 52% discount was supported by third-party analyses (*see* A1301, A1316) and that Susan accepted similar discounts for other transactions involving LBCC affiliates based on similar discount criteria (*see* A1071-81, A1088 & A1377). And, contrary to Susan's arguments, the effective price available to Susan was higher than the price that would result from a violation of the Agreement's stockholder restrictions. *See* A1933-35. Nor was there any evidence (or even an allegation) that Defendants refused to repurchase Susan's shares at any price or that any other stockholder's shares had been repurchased on terms that were more favorable than those offered to Susan.

Defendants' summary judgment motion (and proposed order) sought dismissal of the case with prejudice, and entry of judgment against Plaintiffs on all claims, and was thus directed to any and all remaining claims. *See* A552-53; B1. Moreover, Defendants' briefing and oral argument expressly addressed the restated implied covenant claim *See* A1713-15, A1932-36.⁵ In opposing Defendants'

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During the proceedings in the Court below, Defendants also noted that any claims based on events occurring more than three years before the filing of the Complaint would be time-barred under 10 *Del. C.* § 8106, a conclusion not challenged by Plaintiffs. A1895.

summary judgment motion, Susan presented no facts to rebut Defendants' evidence. Nor did she file an affidavit pursuant to Court of Chancery Rule 56(f) requesting discovery to justify her opposition. It was therefore not erroneous—if, as Susan argues, the claim was part of her original Complaint—for the Court to consider uncontested facts that were before it. In all events, none of these facts was necessary to a conclusion that Susan's proposed implied covenant claim is legally-infirm, as the Court expressly held, citing *LBCC I*, that Susan's claim "would contradict the language and purpose of the Shareholders' Agreement, which is to afford the parties bilateral discretion in determining whether to buy or sell their shares." *LBCC II* at 21.

Susan's original complaint offered three equitable theories for enforcing her claimed right to have LBCC repurchase her shares for her portion of LBCC's net asset value, including one based on the implied covenant. The Court dismissed the original implied covenant claim in its entirety in *LBCC I*, except insofar as Susan alleged "that there might be an implied covenant in the Shareholders' Agreement requiring repurchase proposals to be presented to the Board" *LBCC I* at 14; *see also* Order Implementing *LBCC I*.

Because Susan already had asserted an implied covenant claim, her attempt to add a self-described "new" implied covenant claim must comply with the Court of Chancery's Rules. Under Rule 15(aaa), the Court's dismissal was

with prejudice, *and without leave to amend*, unless Susan could establish “good cause” that dismissal with prejudice would not be just under all the circumstances. *Braddock*, 906 A.2d at 783; *see also Stern v. LF Cap. P’ners*, 820 A.2d 1143, 1146 (Del. Ch. 2003). Susan made no showing of good cause and, accordingly, the Court appropriately denied Susan’s motion.

CONCLUSION

For the foregoing reasons, Defendants respectfully submit that the judgments of the court below should be affirmed in all respects.

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CERTIFICATE OF SERVICE

I, Adam M. Kress, hereby certify that on August 1, 2013, the foregoing Appellees' Answering Brief was served by hand delivery and electronically via File & ServeXpress on the following counsel of record:

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