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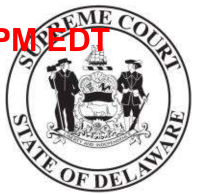

IN THE SUPREME COURT OF THF STATF OF DFLAWARE

THE FIRE AND POLICE PENSION FUND, SAN ANTONIO, Appellant, Plaintiff-Below, v. ARRIS GROUP INC., Appellee, Nominal Defendant-Below.	No. 131, 2015 On appeal from the Court of Chancery of the State of Delaware, C.A. No. 10078-VCG

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NATURE OF THE PROCEEDING

This is an appeal by plaintiff-appellant The Fire and Police Pension Fund, San Antonio ("San Antonio" or "Plaintiff") from the Court of Chancery's award of $128,000 in legal fees to Plaintiff's counsel. Plaintiff obtained the full relief sought – elimination of a provision in the credit agreement of defendant ARRIS Group, Inc. ("Arris") that entitled bank lenders to accelerate almost $1.6 billion of Arris debt if the stockholders elected a new board majority in a proxy contest. A provision in a debt instrument entitling banks to declare a default upon the election of a dissident slate is known as a "Proxy Put." *Kallick v. SandRidge Energy, Inc.*, 68 A.3d 242, 244 & n.8 (Del. Ch. 2013). Unlike the provision in *SandRidge*, which allowed the incumbent directors to disable the Proxy Put by approving the dissident slate (an "Approvable Proxy Put"), the Arris credit agreement barred such approval. Such a provision is known as a "Dead Hand Proxy Put." *Pontiac Gen. Emps. Ret. Sys. v. Ballantine*, C.A. No. 9789-VCL, tr. at 74, 80 (Del. Ch. Oct. 14, 2014) [hereinafter, "*Healthways*"] (Tab 6).[1]

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[1] A compendium of unreported decisions and secondary authorities is filed contemporaneously herewith. Attachments are cited herein as "Tab __".

San Antonio pursued this action to vindicate a paramount principle of Delaware corporate law: "If the stockholders are displeased with the action of their elected representatives, the powers of corporate democracy are at their disposal to turn the board out." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985). The threat of debt acceleration was a potent deterrent to removing the Board of Directors of Arris, because the amount of debt outstanding under the credit agreement was large and far exceeded Arris's cash and short-term investments.

Plaintiff's claims were novel. No court had ruled on the enforceability of a Dead Hand Proxy Put. No court had been asked to adjudicate the validity of a Dead Hand Proxy Put in the absence of a pending proxy contest.

Before filing suit, San Antonio made a demand to Arris pursuant to Section 220 of the Delaware General Corporation Law (the "DGCL"). Arris refused to produce any documents, arguing that any breach of fiduciary duty claim respecting the Dead Hand Proxy Put was meritless.

San Antonio filed its Verified Class Action and Derivative Complaint (the "Complaint") on September 3, 2014, alleging that the Arris Board of Directors, aided and abetted by Bank of America, N.A. ("BANA"), breached

their fiduciary duties in approving a credit agreement containing a Dead Hand Proxy Put. Rather than defend the Dead Hand Proxy Put on the merits, the defendants mooted the claims by eliminating the Dead Hand Proxy Put. Arris devoted its legal resources to opposing a fee application.

San Antonio sought a fee award of $750,000, based on the significance of the benefit and the risk of bringing the case. No Arris stockholders objected. Arris argued that no fee should be awarded because the case was not meritorious when filed. In the alternative, Arris argued that a fee award of $30,000 was appropriate, because Plaintiff's counsel supposedly incurred no risk. The Court of Chancery awarded $128,000.

Vice Chancellor Glasscock's short transcript ruling of February 25, 2015 (*see* Exhibit A hereto) contains two rationales for the award. *First*, the Vice Chancellor characterized elimination of the Dead Hand Proxy Put as a "modest benefit," stating that (i) debt acceleration triggered by the replacement of a board majority in a given year "leav[es] much of the stockholders' franchise intact" and (ii) the value of removing a Dead Hand Proxy Put has decreased over time in light of developing case law. (Ex. A at 7-8.) *Second*, the Vice Chancellor deemed *San Antonio Fire & Police Pension Fund v. Bradbury*, 2010 WL 4273171 (Del. Ch. Oct. 28, 2010), to

be "squarely on point," and, "in the interest of consistency," awarded a fee based on the "implied hourly rate" of the fee award in *Amylin II*. (Ex. A at 9.) The fee award in *Amylin II* was $2.9 million, more than twenty-two times the fee award here.

This is San Antonio's appeal from the fee award, as reflected in the Order of Dismissal and Resolution of Plaintiff's Fee Application entered on February 26, 2015. (*See* Exhibit B hereto.) Arris has abandoned on appeal its arguments below that the underlying action was not meritorious when filed and created no benefit sufficient to warrant a fee award.

SUMMARY OF ARGUMENT

1. The Vice Chancellor erred as a matter of law in setting a fee award based on a determination that eliminating the Dead Hand Proxy Put was a "modest benefit." The DGCL and consistent case law speak to the fundamental importance of, and the substantial benefit associated with, vindicating the right of a stockholder majority to elect a new board majority at an annual meeting. The Vice Chancellor also erroneously stated that the value of removing a Dead Hand Proxy Put has decreased over time, due to developments in the law. The Court of Chancery was incorrect in concluding that eliminating a Dead Hand Proxy Put is "less like chaining up a vicious bulldog and more like chaining up a toothless bulldog." (Ex. A at 8.) Demand for Dead Hand Proxy Puts actually increased following the ruling in *Kallick v. SandRidge Energy, Inc.*, 68 A.3d 242 (Del. Ch. 2013), which imposed fiduciary constraints on incumbent directors in deciding whether to approve a dissident slate and thereby disable an Approvable Proxy Put. The Arris Dead Hand Proxy Put was adopted shortly after *SandRidge*.

2. The Court of Chancery erred as a matter of law in basing the fee award on the implied hourly rate in *Amylin II*. Applying mechanically

an implied hourly rate from a prior case that involved far more hours is inconsistent with Delaware Supreme Court precedent, because it places excessive weight on hours expended and places insufficient weight on the magnitude of the benefits achieved. The Vice Chancellor's methodology also contradicts *Amylin II*, because that fee award of $2.9 million was based on "the central importance of considering the benefits created by the litigation," a finding that "significant and substantial benefits unquestionably accrued to Amylin's stockholders from this litigation," and an evaluation of all relevant factors. *Amylin II*, at *7, *12-13. The decision below also creates perverse incentives. If meritorious challenges to Dead Hand Proxy Puts can be mooted at the outset for a minimal fee, such cases will not be brought, and lenders will be incentivized to continue to market Dead Hand Proxy Puts to other borrowers without fear of judicial scrutiny.

STATEMENT OF FACTS

A. Arris and BANA Enter Into a $1.925 Billion Credit Agreement Containing a Dead Hand Proxy Put

On March 27, 2013, Arris entered into a $1.925 billion credit with a syndicate of lenders, including BANA as administrative agent (the "Credit Agreement"). (A53.) The borrowings under the Credit Agreement were used to finance Arris's acquisition of General Instrument Corporation. (A53.) That acquisition was a major transaction for Arris, as the target's business had far higher revenues than did Arris, and the transaction value for the acquisition ($2.35 billion) was greater than Arris's market capitalization (approximately $1.6 billion). (A159 ¶ 3.) Thus, it was in question from the outset whether Arris could repay the full amount of the indebtedness if the lenders could demand accelerated repayment.

According to an affidavit filed by Arris shortly before the hearing on the fee application, the original commitment letter supplied by BANA in December 2012 "provided that a change of control would be an event of default, although the letter did not define what constituted a change of control." (A161 ¶ 6.) Despite the lack of clarity in the commitment letter, agents of Arris agreed to, and the Board of Directors of Arris approved, a Credit Agreement containing a Dead Hand Proxy Put. Arris's affiant did not

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say whether Arris tried to negotiate for no Proxy Put or an Approvable Proxy Put, or if Arris obtained anything specific in return for agreeing to inclusion of a Dead Hand Proxy Put. (A163 ¶ 10.)

The Dead Hand Proxy Put operates through a series of provisions of the Credit Agreement. Section 8.01(k) includes a "Change of Control" among the Credit Agreement's list of "Events of Default." (A58.) Section 1.01 defines a "Change of Control" to include stockholders electing a new board majority through a proxy fight:

> during any period of 12 consecutive months, a majority of the members of the board of directors or other equivalent governing body of the Company cease to be composed of individuals ... (iii) whose election or nomination to that board or other equivalent governing body was approved by [the incumbent directors] ... (**excluding ... any individual whose initial nomination for, or assumption of office as, a member of that board or equivalent governing body occurs as a result of an actual or threatened solicitation of proxies** or consents for the election or removal of one or more directors by any person or group other than a solicitation for the election of one or more directors by or on behalf of the board of directors).

(A54-55 (emphasis added).) It thus required two annual meetings to elect a majority of new directors nominated by a dissident stockholder to avoid triggering the Dead Hand Proxy Put.

Declaration of an event of default could be catastrophic to Arris and its stockholders. As of May 29, 2014, Arris had $1.589 billion in debt

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outstanding under the Credit Agreement. (A60.) Arris's market capitalization in 2014 was between $3.5 billion and $5.1 billion (A62), and as of March 31, 2014, Arris had cash, cash equivalents and short-term investments of just $521 million. (A66.) The cost and uncertainty of forced immediate repayment of that amount of debt posed severe harm to stockholders. Especially if Arris's performance weakened over time, and its value declined, or if credit markets weakened, the loss to Arris's stockholders could be catastrophic if they exercised their franchise rights to replace a majority of the incumbent Board and triggered the Dead Hand Proxy Put. Absent judicial invalidation of the Dead Hand Proxy Put, it operated as a deterrent to the nomination and election of a new board majority at an annual meeting.

Arris's fiduciaries, managers, and advisers were certainly aware of the potential threat of stockholder activism in March 2013, when they obtained the entrenching benefits of the Dead Hand Proxy Put. They knew that Arris had a new stockholder profile due to its acquisition of General Instrument Corporation, that Arris had been the target of the Shamrock Activist Value

Fund three years earlier,[2] and that stockholder activism had become commonplace.[3]

B. Arris Fails to Produce Documents in Response to a Section 220 Demand and Fails to Respond to a Section 220 Action

On May 13, 2014, San Antonio served a demand letter (the "Demand Letter") pursuant to Section 220 of the DGCL. (A68.) The Demand Letter gave Arris's Board an opportunity to demonstrate its justification for agreeing to the Dead Hand Proxy Put and to show what valuable consideration, if any, it received for doing so. (A44 ¶ 10.)

The Company refused to provide San Antonio with any documents. Arris's May 22, 2014 response to the Demand Letter raised hyper-technical quibbles with the Demand Letter, such as that San Antonio's documentary evidence of ownership was insufficient because it was dated "two full weeks prior to the date of the Section 220 Demand." (A84.) Arris also contended that San Antonio failed to provide a credible basis of possible wrongdoing, and attempted to distinguish the case law on which San Antonio relied, *San*

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[2] *See* Shamrock Activist Value Fund, L.P., 13D Holdings Report (Schedule 13D) (Mar. 10, 2010) (Tab 11).

[3] *See* Marc Weingarten and David Rosewater, *Shareholder Activism: 2013 and Beyond*, Activist Investing, 5 (2014) (Tab 13).

Antonio Fire & Police Pension Fund v. Amylin Pharmaceuticals, Inc., 983 A.2d 304 (Del. Ch. 2009) ("*Amylin I*"), and *SandRidge*. (A85-86.)

San Antonio provided Arris with another statement under oath and supporting documents establishing San Antonio's standing to serve the Demand Letter. (A89.) On June 10, 2014, Arris again rejected San Antonio's demand, contending that the existence of the Dead Hand Proxy Put was itself no credible basis of possible wrongdoing. (A99.)

On June 27, 2014, Plaintiff filed suit against Arris under Section 220 of the DGCL and moved to expedite. (A101-118.) Arris did not respond to the Section 220 Complaint. (A45 ¶ 16.)

C. Plaintiff Files Suit for Breach of Fiduciary Duty and the Defendants Capitulate

Rather than pursue the Section 220 action, on September 3, 2014, San Antonio filed a Complaint alleging that the members of the Arris Board, aided and abetted by BANA, breached their fiduciary duties by approving the Credit Agreement containing a Dead Hand Proxy Put. (A120-46.) San Antonio sought an order declaring that the Dead Hand Proxy Put was invalid, unenforceable, and severable from the Credit Agreement. (A145.) San Antonio did not seek damages.

Defendants did not defend the validity of the Dead Hand Proxy Put. Instead, defendants capitulated. On October 27, 2014, Arris and Bank of America amended the Credit Agreement to eliminate the Proxy Put at no cost to Arris. Election of a new board majority would no longer be a "Change of Control." (A148 § 2(a); *see* A54.)

Eliminating the Dead Hand Proxy Put mooted San Antonio's claims. On December 8, 2014, the parties filed a Stipulation and Order Establishing the Procedure for Considering the Dismissal of the Litigation and Plaintiff's Fee Application (the "Stipulation for Considering Dismissal"), which the Court entered on December 11, 2014. (A153-157.) Arris publicly filed the Order and posted it on its website, providing notice to stockholders of their right to object to San Antonio's application for attorneys' fees in an amount not exceeding $750,000. (A155 ¶¶ 2-3.)

D. Disposition of the Fee Application

No stockholders objected to the fee application. Arris and the director defendants filed a 58-page opposition brief requesting that no fee be awarded. (Dkt. #17.) Arris argued that the case was not meritorious when filed and was subject to a motion to dismiss. In the alternative, Arris argued

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that "no risk [was] being undertaken" by San Antonio's counsel, because the outcome of the case was "controlled by *Amylin* and *SandRidge*." (A242.)

The Vice Chancellor ruled that the Complaint was meritorious when filed, reasoning that the Dead Hand Proxy Put "could discourage a majority of the board's replacement in any given year" and that adopting a Dead Hand Proxy Put "is an inherently conflicted act," which "raised a sufficient, reasonable allegation of entrenchment supporting a claim of a breach of the duty of loyalty at the motion to dismiss stage." (Ex. A at 5-6.)

The Vice Chancellor's *Sugarland* analysis reads as follows:

> The most important and heavily weighted factor in determining a fee award is the significance of the benefits achieved in the litigation. I find the elimination of the proxy put a cognizable but modest benefit. Although, as I have found, the provision did infringe on the stockholders' franchise by potentially discouraging the stockholders from bringing a dissident slate of directors, the narrowed focus of the proxy put at issue here, both in terms of the provision resetting every year and requiring a majority of dissident directors to be elected to take effect, dilute the provision's harmful effect, leaving much of the stockholders' franchise intact. Moreover, as our case law describing the use of similar proxy puts as problematic becomes more developed, the value of removing such a device decreases. The situation begins to be less like chaining up a vicious bulldog and more like chaining up a toothless bulldog.
>
> I need not be creative in evaluating a proper fee here, because Vice Chancellor Noble recently faced a similar situation in *Amylin II*, and I look for guidance to his fee award there. Because the benefit here, as there, is difficult to quantify,

> I turn, consistent with *Sugarland*, to the time spent on the case, mindful of the fact that this matter was taken on a contingent fee and that I must take that risk into account to encourage wholesome litigation. I am also mindful that relying on compensation based solely on time spent could encourage churning, but it is clear that such is not the case here.
>
> In my analysis, I consider only the time plaintiff's counsel spent in obtaining the benefit supporting the fee application. The plaintiff's counsel's records show that they spent 159.7 hours on the matter as of the date the parties submitted the settlement to the Court. Similar intangible corporate benefit cases, as the defendants point out and the plaintiff does not dispute, generated fee awards implying hourly fees in the range of $790 to $1800. In *Amylin II*, Vice Chancellor Noble ultimately approved an award of $2.9 million to compensate for 3,339 hours of work, representing an implied hourly rate of approximately $790 after expenses.
>
> By the plaintiff's own admission, *Amylin II* is squarely on point, presenting similar facts and legal issues as the present case. There, as here, it was appropriate to consider a *quantum meruit* analysis considering the time expended as a check on the fee.
>
> Consequently, in the interest of consistency and of awarding fees that are fair and reasonable, I find it appropriate to award the plaintiff's counsel $128,000 in fees and expenses, which is consistent with an hourly rate of approximately $800. I find such a fee to be appropriate in light of the benefit conferred and consistent with the other factors of *Sugarland* as well.

(Ex. A at 7-10.) The Vice Chancellor's award excluded all time incurred after the filing of the Stipulation for Considering Dismissal.

ARGUMENT

I. THE COURT OE CHANCERY ERRED AS A MATTER OE LAW IN HOLDING THAT FLIMINATING A $I.6 BILLION DEAD HAND PROXY PUT IS A "MODEST BENEFIT"

A. Question Presented

Did the Court of Chancery err in categorizing the elimination of a $1.6 billion proxy put as a "modest benefit," given the fundamental importance of preserving stockholder voting rights and the deterrent effect of the Dead Hand Proxy Put on a potential proxy contest to replace a majority of directors? (A30-33; A187-89.)

B. Scope of Review

This Court reviews awards of attorneys' fees for abuse of discretion. *See William Penn P'ship v. Saliba*, 13 A.3d 749, 758 (Del. 2011). This Court reviews *de novo* the legal principles the Court of Chancery applied in reaching its decision. *Alaska Elec. Pension Fund v. Brown*, 988 A.2d 412, 417 (Del. 2010) ("We review [the trial court's] denial of … attorneys' fees and costs for abuse of discretion, but we review *de novo* the legal principles applied in reaching that decision."); *Dover Historical Soc'y, Inc. v. City of Dover Planning Comm'n*, 902 A.2d 1084, 1089 (Del. 2006) ("Where it is in

issue, we review the [trial court's] formulation of the appropriate legal standard *de novo*.").

C. Merits of Argument

This Court considers the familiar *Sugarland* factors in fashioning an appropriate fee award for a corporate benefit conferred by stockholder litigation, including "(1) the results achieved; (2) the time and effort of counsel; (3) the complexity of the issues; (4) whether counsel were working on a contingent fee basis; and (5) counsel's standing and ability." *Loral Space & Commc'ns. Inc. v. Highland Crusader Offshore Partners, L.P.*, 977 A.2d 867, 870 (Del. 2009) (citing *Sugarland Indus., Inc. v. Thomas*, 420 A.2d 142,149 (Del. 1980)). In applying these factors, the Court's goals are "to align counsel's interest with those of their clients and encourage entrepreneurial plaintiffs' lawyers to identify and litigate real claims." *In re Sauer-Danfoss Inc. S'holders Litig.*, 65 A.3d 1116, 1141 (Del. Ch. 2011).

The Court of Chancery's erroneous classification of the benefit achieved as "modest" was a "heavily weighted" reason for the fee award of only $128,000. (Ex. A at 7.) If not reversed, that fee award and that characterization will discourage meritorious challenges to Dead Hand Proxy Puts and encourage their proliferation.

1. Eliminating a $1.6 Billion Dead Hand Proxy Put Is a Substantial Benefit

"Delaware courts have assigned the greatest weight to the benefit achieved in litigation." *Americas Mining Corp. v. Theriault*, 51 A.3d 1213, 1254 (Del. 2012) (collecting cases). *See also In re Del Monte Foods Co. S'holder Litig.*, 2011 WL 2535256, at *14 (Del. Ch. June 27, 2011) ("Delaware decisions have sought to align the interests of entrepreneurial plaintiffs' counsel with the classes they represent by granting minimal fees for minimal benefits and major fees for major results."); *In re Topps Co. S'holders Litig.*, 924 A.2d 951, 962 n.39 (Del. Ch. 2007) ("Nor can stockholder-plaintiffs believe that their lawyers will not receive appropriate remuneration in this court for achieving an important benefit for the corporation or a class of stockholders.").

In corporate benefit cases, the classification of the benefit achieved as either "substantial" or "modest" has been a critical factor in the determination of an appropriate fee award. The Court of Chancery has awarded multi-million dollar fees when contingently retained counsel for a stockholder plaintiff has conferred a "substantial" corporate benefit respecting voting rights. By way of contrast, a $128,000 fee award is at the

low end of the fee award scale for procuring "modest" corporate benefits, such as immaterial supplemental disclosures.

In *In re Yahoo! S'holders Litig.*, C.A. No. 3561-CC, let. op. (Del. Ch. Mar. 6, 2009) (Tab 3), Chancellor Chandler reasoned that the benefit bestowed "was significant and sufficient" to support the award of $8.4 million fee plus expenses. *Id.* at 2. The case concerned Yahoo's adoption of expensive change in control employee severance plans. A key aspect of the settlement was "elimination of the dead-hand provision that ... would have prevented a new slate of directors from changing the severance plan." *Id.* at 2. That dead-hand provision deterred proxy contests, because incumbent directors could reduce the scope and expense of the employee severance plan, while a newly elected dissident slate would have no such power.[4]

Chancellor Chandler analogized the *Yahoo* settlement and fee award to *Minneapolis Firefighters' Relief Association v. Ceridian Corp.*, C.A. No. 2996-CC (Del. Ch. Mar. 24, 2008) (Order) (Tab 5), in which the Court awarded $5.14 million. As in *Yahoo*, the fee award in *Ceridian* was justified by the significance of the settlement terms, which "empowered a potential buyer to present a leveraged recapitalization proposal, and eliminat[ed] a

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[4] *See* Dawn Kawamoto, *Icahn's proxy fight could trigger Yahoo's severance plan*, CNET (June 3, 2008 3:16 PM) (Tab 8).

termination right for the merger partner in the event a new slate of directors was elected before the merger closed." *Yahoo*, let. op. at 2. The dead-hand provision in the Ceridian merger agreement deterred stockholders from electing a new slate of directors, because their election would trigger a termination right by the merger partner.

In *Amylin II*, Vice Chancellor Noble awarded $2.9 million, in large part because "significant and substantial benefits unquestionably accrued to Amylin's stockholders from this litigation." 2010 WL 4273171, at *7. The Court of Chancery explained that "influences on the voting calculus of Amylin's stockholders resulting from the continuing directors provisions of the Credit Agreement and the Indenture have been removed or, at least, limited." *Id.* Among the benefits obtained was the waiver of a Dead Hand Proxy Put in Amylin's credit agreement. *Id.* at *8.

In *EMAK Worldwide, Inc. v. Kurz*, 50 A.3d 429 (Del. 2012), this Court affirmed a fee award of $2.5 million, characterizing as "sizeable" the benefit of "preserving the EMAK shareholders' voting rights," including the rescission of an exchange transaction that "'fundamentally changed the corporate governance landscape.'" *Id.* at 434 (quoting *Kurz v. Holbrook*, C.A. No. 5019-VCL, tr. at 107 (Del. Ch. July 19, 2010) (Tab 4)). $1.7

million of the fee award was attributable to rescission of the exchange transaction, which had made a consent solicitation realistically unobtainable, in part because a successful insurgent consent solicitation would trigger a liquidation preference for the preferred stockholder (*i.e.*, a Proxy Put). *Kurz v. Holbrook*, tr. at 91-92, 106.

In *Forsta AP-Fonden v. News Corp.*, C.A. No. 7580-CS, tr. (Del. Ch. Apr. 26, 2013) (Tab 1), the Court of Chancery awarded $1.3 million, reasoning as follows: "This was really a case about the fundamental voting rights of the non-American investors in News Corp., and the extent to which they would get to exercise those rights, and I think the plaintiffs achieved substantial success in protecting those rights, and I give them credit for that in terms of the fee award." *Id.* at 10.

The result here is of a similar magnitude as in *Yahoo*, *Ceridian*, *Amylin II*, *EMAK*, and *Forsta AP-Fonden*. Eliminating a $1.6 billion Dead Hand Proxy Put creates accountability at the ballot box. It is a substantial benefit that is similar to the elimination of dead-hand provisions in *Yahoo*, *Ceridian*, *Amylin II*, and *EMAK*. Stockholders of Arris now possess their full voting rights for purposes of corporate control. The incumbent fiduciaries and managers of Arris are no longer entrenched by the threat of

massive debt acceleration if stockholders nominate and elect a dissident slate to replace a board majority.

The Court of Chancery's characterization of the benefit as "modest," and concomitant fee award of $128,000, means that elimination of a $1.6 billion Dead Hand Proxy Put is on par with, or even below, the ubiquitous stockholder challenges to acquisitions that are resolved by the issuance of immaterial supplemental disclosures. In *In re Talbots, Inc. S'holders Litig.*, Cons. C.A. No. 7513-CS, tr. (Del. Ch. Dec. 16, 2013) (Tab 2), for example, the Court of Chancery awarded $237,500 for "disclosures of such a modest value" that the Court could not "get anywhere close to finding that these things are a material disclosure." *Id.* at 14. *See also In re Sauer-Danfoss Inc.*, 65 A.3d at 1136-37 ("This Court has often awarded fees of approximately $400,000 to $500,000 for one or two meaningful disclosures .... Disclosures of questionable quality have yielded much lower awards.").

As discussed below, the Court of Chancery's categorization of the removal of a $1.6 billion Dead Hand Proxy Put as a "modest benefit," rather than a "substantial" benefit, rests on two separate legal errors.

2. The Court of Chancery's Classification of the Benefit As "Modest" Rests on Two Legal Errors

a. The Dead Hand Proxy Put Did Not "Leav[e] Much of the Stockholders' Franchise Intact"

The Vice Chancellor recognized the coercive effect of the Arris Dead Hand Proxy Put. It "did infringe on the stockholders' franchise by potentially discouraging the stockholders from bringing a dissident slate of directors[.]" (Ex. A at 7.) Nonetheless, the Vice Chancellor stated that the Dead Hand Proxy Put "le[ft] much of the stockholders' franchise intact" because it could only be triggered if a majority of directors were nominated by a dissident and elected at a single annual meeting. (Ex. A at 8.)

The Vice Chancellor's reference to "leaving much of the stockholders' franchise intact" apparently refers to the ability of stockholders to elect a minority of directors in a proxy contest at a single annual meeting, or to elect a majority of directors in proxy contests spread out over annual meetings held over one year apart. Yet, because of the Dead Hand Proxy Put, stockholders could not hope to elect, or credibly threaten to elect, a majority of new directors at a single annual meeting.

This practical constraint on stockholder voting rights is a radical infringement. In the absence of a staggered board, stockholders are

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statutorily entitled to elect a full slate of new directors annually. 8 *Del. C.* § 211(b). Leading cases recognize that no right is more critical than the right to replace a board majority at an annual meeting. "This Court has repeatedly stated that, if the stockholders are not satisfied with the management or actions of their elected representatives on the board of directors, the power of corporate democracy is available to the stockholders to replace the incumbent directors when they stand for re-election." *MM Cos. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1127 (Del. 2003) (citing *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984), and *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985)).

Delaware case law treats infringement of stockholders' right to elect a new slate of directors as a matter of utmost gravity:

> **Shareholder voting rights are sacrosanct.** The fundamental governance right possessed by shareholders is the ability to vote for the directors the shareholder wants to oversee the firm. Without that right, a shareholder would more closely resemble a creditor than an owner....
>
> **Preserving shareholder voting rights produces a fundamental corporate benefit.** Public policy supports discouraging director and officer manipulation by encouraging plaintiffs to challenge actions that frustrate the shareholder voting franchise.

EMAK, 50 A.3d at 433 (citation omitted) (emphasis added). In *Amylin II*, the Court of Chancery recognized the importance of obtaining relief from Proxy Puts that could prevent election of a new Board majority:

> Most importantly, **the Credit Agreement and the Indenture no longer frustrate the stockholders' ability to elect a new majority of directors to the Company's board – a fundamental stockholder right without which the legitimacy of board power comes into question**. Vindication of the shareholder franchise is a major public policy objective; as a core value in corporate governance, steps undertaken to protect the stockholder franchise may be recognized as having a very real, even if unquantifiable, benefit.

2010 WL 4273171, at *13 (emphasis added).

Board approval of a Dead Hand Proxy Put for a highly indebted company such as Arris is the practical equivalent of a board's unilateral imposition of a staggered board, in derogation of Delaware law. *See* 8 *Del. C.* § 141(d) (specifying means of adopting staggered board, which do not include a bylaw amendment by the board). The *de facto* classification of a board of directors by means of a Dead Hand Proxy Put has radical implications for corporate governance. Among other things, it may render a company impervious to the election of a new board majority. *See* Guhan Subramanian, *Delaware's Choice*, 39 Del. J. Corp. L. 1, 6 (2014) ("[T]here is not a single instance where a bidder has successfully won two proxy

contests, one year apart, in order to gain control of a target company.") (Tab 12).

The *Amylin* litigation and *SandRidge* show that incumbent boards have used overt threats of debt acceleration from Proxy Puts to coerce stockholder voting.[5] Even in the absence of overt Board threats, a Dead Hand Proxy Put operates insidiously. Vice Chancellor Laster recently observed: "because the [dead hand] proxy put exists, it necessarily has an effect on people's decision-making about whether to run a proxy contest and how to negotiate with respect to potential board representation." *Healthways*, tr. at 72.

As discussed above, in *Yahoo* and *Ceridian* the voting rights at stake were the ability to elect a new slate of directors without the coercion of triggering an adverse consequence (*i.e.*, locking in the terms of an expensive employee severance plan or giving a merger partner a termination right).

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[5] *See Amylin II*, at *3 ("As disclosed in Amylin's annual report filed on February 27, 2009, a proxy contest resulting in the election of a majority of new directors to Amylin's board would trigger the continuing director provisions of both the Credit Agreeement and the Indenture."); *SandRidge*, 68 A.3d at 261 ("[T]he incumbent board's behavior is redolent more of the pursuit of an incremental advantage in a close contest, where a small margin may determine the outcome, than of any good faith concern for the company, its creditors, or its stockholders.").

Yahoo let. op. at 2. Chancellor Chandler did not suggest that stockholders should be content with the right to elect a minority of new directors.

We are not aware of any case suggesting that franchise rights are mostly intact if stockholders are practically foreclosed from electing a majority of directors to a non-classified board at a single annual meeting. No case before this one has suggested that eliminating the coercive effect of a Dead Hand Proxy Put is a modest benefit.

b. Evolution of the Law Has Not Decreased the Value of Eliminating a Dead Hand Proxy Put

The Vice Chancellor stated that the value of eliminating a Dead Hand Proxy Put "decreases" over time as case law over Proxy Puts "becomes more developed." (Ex. A at 8.) In the Vice Chancellor's colorful analogy, "[t]he situation begins to be less like chaining up a vicious bulldog and more like chaining up a toothless bulldog." (*Id.*) This perspective on the vitality of Dead Hand Proxy Puts is, we believe, erroneous and premature.

SandRidge rendered *Approvable* Proxy Puts largely toothless bulldogs, by recognizing that stockholders could sue to require incumbent directors to approve a slate of dissident nominees, unless there is a "specific and substantial risk to the corporation or its creditors posed by the rival slate." *SandRidge*, 68 A.3d at 260. That ruling did not reduce the

effectiveness of Dead Hand Proxy Puts, or suggest that they were invalid or toothless. If anything, *SandRidge* created new demand for Dead Hand Proxy Puts, because they are not susceptible to a lawsuit to compel approval of a dissident slate.

A leading lawyer for banks recently explained the effect of *SandRidge* on the market for Dead Hand Proxy Puts:

> **As a consequence of the Court's decision in *SandRidge*, lenders began to more frequently include so-called "dead hand" change of control default provisions in credit agreements**. The inclusion of a dead hand change of control default provision preserves the ability of lenders to declare a default in the event of the election of a dissident stockholder's nominees as a majority of the board of the borrower, regardless of whether the current board ultimately approves the dissident stockholder's nominees as they did in *Amylin* and were required to do in *SandRidge*.[6]

The Arris Dead Hand Proxy Put was adopted nineteen days after the issuance of *SandRidge*.

The dramatic recent increase in stockholder activism, including the rising number of proxy contests and settlements of activist campaigns for large-cap companies, also drives a demand for Dead Hand Proxy Puts. A recent practitioner presentation collects data on rising stockholder activism

[6] Kevin Miller, *Food for Thought: Conflicting Views on the "Knowing Participation" Element of Aiding & Abetting Claims*, Deal Lawyers, Mar.-Apr. 2015, at 2 (emphasis added) (Tab 9).

and explains that due to the "current shareholder activism wave and the large number of [proxy contest] settlements," some lenders are continuing to "push[] hard for the 'dead hand' feature."[7]

The Vice Chancellor may have been referring to the recent decision in *Healthways* as support for the proposition that a Dead Hand Proxy Put is now akin to a "toothless bulldog." In *Healthways*, a case that parallels this action, Vice Chancellor Laster denied motions to dismiss filed by the director defendants (on ripeness grounds) and by the lender (for failure to plead knowing participation). There are several reasons why the *Healthways* decision did not lessen the value or importance of eliminating the Dead Hand Proxy Put at Arris.

First, *Healthways* was not rendered until October 14, 2014, more than one month after the filing of this case. According to Arris's affiant, the defendants had already agreed to moot this lawsuit at the time *Healthways* was rendered. (A168 ¶¶ 23-24.)

Second, notwithstanding *Healthways*, certain lenders continue to "push[] hard" for Dead Hand Proxy Puts. *See Poison Put Provisions in Debt*

[7] Kai Haakon E. Liekefett *et al.*, *Poison Put Provisions in Debt Financing: Lesson on Enforceability from Recent Cases*, Strafford, 52 (Feb. 4, 2015) [hereinafter "*Poison Put Provisions in Debt Financing*"] (Tab 10).

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Financing, *supra*, at 52. Indeed, according to a recent empirical study: "use of dead hand clauses remained steady between 2012 and 2014. We found no evidence that *Amylin*, *Kallick* or *Healthways* had an impact on their use."[8]

Third, *Healthways* did not deter Arris from arguing below that this action was not meritorious when filed. Arris contended that *Healthways* was distinguishable and always maintained that its own $1.6 billion Dead Hand Proxy Put was invulnerable from legal challenge.

For all of these reasons, the Court of Chancery erred in concluding that developments in the law made a Dead Hand Proxy Put a depreciating asset of little value. Market evidence points in favor of the opposite conclusion that market participants valued Dead Hand Proxy Puts. By this lawsuit, San Antonio took out of the hands of the incumbent directors and BANA a powerful weapon to prevent proxy contests.

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[8] Craig Eastland, *Siege Mentality: Proxy Puts in S&P 100 Credit Agreements in the Wake of Healthways*, Thomson Reuters (Apr. 21, 2015) (Tab 7).

II. THE COURT OE CHANCERY ERRED IN ADOPTING THE IMPLIED HOURLY RATE FROM THE $2.9 MILLION FEE AWARD IN *AMYLIN II*

A. Question Presented

Did the Court of Chancery err in basing its $128,000 fee award on the implied hourly rate of the $2.9 million awarded in *Amylin II*, given the widely disparate absolute fee awards and widely disparate incentive effects, and the similarity of the benefits achieved and the similarity of the contingent risk litigating novel claims? (A187-90.)

B. Scope of Review

This Court reviews awards of attorneys' fees for abuse of discretion. This Court reviews *de novo* the legal principles the Court of Chancery applied in reaching its decision. *See supra* Part I.B.

C. Merits of Argument

This Court has made clear that the number of hours devoted to achieving a given benefit is of "secondary importance": "In applying *Sugarland,* the Court of Chancery understood that it had to look at the hours and effort expended, but recognized the general principle from *Sugarland* that the hours that counsel worked is of secondary importance to the benefit achieved." *Americas Mining Corp.*, 51 A.3d at 1258 (internal quotations

and footnotes omitted). Applying that principle in *Olson v. ev3, Inc.*, 2011 WL 704409 (Del. Ch. Feb. 21, 2011), the Court of Chancery gave "no weight to the hours expended," reasoning: "Counsel achieved via settlement all of the relief that they could have obtained by litigating through a merits hearing. Counsel should not be penalized for achieving complete victory quickly." *Id.* at *15.

Here, the Court of Chancery did not subordinate the hours expended to the benefit achieved, and thereby penalized San Antonio's counsel for achieving victory quickly. The Court of Chancery observed that "[s]imilar intangible corporate benefit cases [*i.e.*, *Yahoo*, *Ceridian*, *EMAK*, *Amylin*, and *Forsta AP-Fonden*] generated fee awards implying hourly fees in the range of $790 to $1800." (Ex. A at 9.) "[I]n the interest of consistency," the Court of Chancery applied the approximate implied hourly rate of $790 per hour of *Amylin II*, because *Amylin II* "is squarely on point, presenting similar facts and legal issues as the present case." (*Id.*)

For *Sugarland* purposes, *Amylin II* did not "present[] similar facts." There were 3,338.55 compensable hours in *Amylin II*, including an appeal that resulted in the affirmance of a dismissed claim, the time for which was "not wholly disregard[ed]" for purposes of arriving at a fee of $2.9 million.

Amylin II, at *12. In setting that $2.9 million fee award, Vice Chancellor Noble "recognize[d] the central importance of considering the benefits created by the litigation" and engaged in an estimated lodestar analysis "only as a reference point" and "as something of a check." *Id.* at *12 & n.14. Vice Chancellor Noble also noted that "Amylin may be entitled to some credit for the outcome here." *Id.* at *13 n.107. Nothing in *Amylin II* suggests that $790 is an appropriate implied hourly rate if far fewer hours are needed to accomplish the "major public policy objective" of "[v]indication of the shareholder franchise." *Id.* at *13.

If the shareholder franchise is vindicated in relatively few hours, then the logic of *Sugarland* suggests that the fee award should have a relatively high implied hourly rate. In such circumstances, a high implied hourly rate appropriately compensates Plaintiff's counsel for undertaking the considerable risk of litigating a novel claim and achieving a substantial benefit. *See supra* at 17. Applying mechanically the implied hourly rate of *Amylin II* is tantamount to disregarding the magnitude of the benefit achieved, disregarding the risk of undertaking the contingent representation, and disregarding the experience and efficiency of counsel, who had previously represented San Antonio in the *Amylin* litigation.

The risk here was unusually high. Never before had a law firm sought to invalidate a Dead Hand Proxy put in litigation that did not accompany an active proxy contest. Never before had any litigant invalidated a Dead Hand Proxy Put. San Antonio's counsel did not know how, if at all, the defendants had taken *Amylin I* and *SandRidge* into account when approving the Credit Agreement, how the defendants would respond, on what timetable the litigation would proceed, or whether defendants would feel any practical pressure, prior to a judicial ruling, to eliminate the Dead Hand Proxy Put. (*See* A44-45 ¶¶ 10, 18.)

The Court of Chancery's mechanical application of the implied hourly rate from *Amylin II* not only places excessive weight on hours expended, it creates perverse incentives and discourages meritorious challenges to Dead Hand Proxy Puts. Lenders and counsel for stockholder plaintiffs are repeat players in the world of Proxy Puts. If challenges to Dead Hand Proxy Puts yield only a minimal fee if mooted at the outset, then there is little incentive to file suit. A quick victory for a minimal fee is not worth the risk of a potentially drawn-out litigation of uncertain result. Lenders will be incentivized to moot strong cases early and thereby avoid adjudication on the merits that could be used against them in a subsequent case. Affirmance

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of the mechanical application of an implied hourly rate of $790 per hour should be expected to result in the continued proliferation of unchallenged Dead Hand Proxy Puts that have been implemented without fear or expectation of judicial scrutiny.

CONCLUSION

For all the foregoing reasons, Appellant Plaintiff-Below San Antonio respectfully requests reversal of the decision of the Court of Chancery.

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CERTIFICATE OF SERVICE

I hereby certify that on May 4, 2015, I caused a copy of the **Appellant's Opening Brief** to be served upon the following counsel by File & ServeXpress:

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