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Case Number 208,2016

IN THE SUPREME COURT OF THE STATE OF DELAWARE

ADRIAN DIECKMAN, on behalf of himself and all others similarly situated, Plaintiff Below, Appellant v. REGENCY GP LP, REGENCY GP LLC, ENERGYTRANSFER EQUITY, L.P., ENERGYTRANSFER PARTNERS, L.P., ENERGYTRANSFER PARTNERS, GP, L.P., MICHAEL J. BRADLEY, JAMES W. BRYANT, RODNEY L. GRAY, JOHN W. McREYNOLDS, MATTHEW S. RAMSEY and RICHARD BRANNON, Defendants Below, Appellees.	No. 208, 2016 Appeal from the Memorandum Opinion and Order dated March 29, 2016 of the Court of Chancery of the State of Delaware, C.A. No. 11130-CB

APPELLANT'S OPENING BRIEF

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NATURE OF PROCEEDINGS

Plaintiff was a unitholder in Regency Energy Partners LP ("Regency" or the "partnership"), a limited partnership whose general partner, Regency GP LP ("Regency GP") was directly or indirectly owned and controlled by Energy Transfer Equity, L.P. ("ETE"). In 2014, Regency GP proposed that the partnership be acquired by Energy Transfer Partners L.P. ("ETP"), another affiliate of ETE (the "Merger"), on grossly unfair terms that benefitted only ETE and its affiliates.

The Limited Partnership Agreement ("LPA") (A53-144) requires the general partner to act in "good faith," LPA §7.9(b) (A106), *i.e.*, it must believe its acts are "in the best interests of the Partnership." *Id.* The Complaint[1] alleges that "Regency GP has breached the express terms of the [LPA] by acting in bad faith when it agreed to the Merger, which it knew not to be in the best interests of the Partnership." A40; *see* A39 ("the terms were less favorable than those that would have been available from an unrelated third party; and the terms were not fair and reasonable to the Partnership"); A40 ("Regency GP knew that the Merger was in the best interests of ETE and ETP, which timed the Merger to take advantage of the artificially depressed trading price of Regency's common units"); *see also* A13, A28. As the Court below recognized, the "Complaint asserts that the General Partner breached this provision because the General Partner knew that the Merger

[1] Verified Class Action Complaint ("Complaint") (A11-47).

was not in the best interests of the Partnership and that it instead favored the interests of the General Partner's affiliates (ETE and ETP)." Opinion ("Op.") 15.

The LPA provides, however, that a conflict-of-interest transaction would be deemed not to violate the LPA if any of several "safe harbors" in LPA §7.9(a) (A105) are satisfied. Defendants chose to try to satisfy two of the safe harbors: (i) Special Approval by a Conflicts Committee and (ii) unitholder approval.

Here, the Conflicts Committee was clearly conflicted. The LPA prohibits Conflicts Committee members from serving on affiliate boards and also requires compliance with the audit committee member independence rules of the New York Stock Exchange ("NYSE"), where Regency's units were traded. However, one of the Conflicts Committee's two members, Richard Brannon, was also serving on the board of Sunoco LP (a Regency GP affiliate). Brannon resigned from the Sunoco board four days *after* he began to evaluate the deal and was *reappointed* to the Sunoco board on *the very day* that the Merger closed. The only other Conflicts Committee member, James W. Bryant, was also appointed to the Sunoco board *on the day* the Merger closed. Due to Brannon's service on the board of ETP-controlled Sunoco, and Bryant's and Brannon's expectation of joining/rejoining such board when the Merger closed, neither Brannon nor Bryant qualified for Conflicts Committee membership. Predictably, Brannon and Bryant, who were both loyal to ETE, quickly agreed to an unfair transaction that benefited only ETP

and ETE. However, because the Conflicts Committee was itself conflicted, its approval of the Merger does not provide a safe harbor.

Defendants' attempt to invoke the unitholder approval safe harbor also fails. In order to persuade unitholders to vote for the deal, Defendants told them that Special Approval, as defined in the LPA, had been granted by an independent Conflicts Committee. But Defendants misled the unitholders by failing to disclose that the Conflicts Committee did not satisfy the LPA's requirements and consisted of members who were not independent, including one slipping off an affiliate's board just long enough to give "thumbs up" to the Merger. The vote by misled unitholders does not provide a safe harbor to Defendants to absolve them of their wrongdoing.

Lacking cover from the LPA's safe harbors, Defendants are left to show that they acted in subjective good faith, which they cannot do, and which, in any event, raises questions of fact not properly resolved on a motion to dismiss.

The Court of Chancery, however, dismissed the Complaint, holding that the unitholder approval safe harbor was satisfied. The Chancellor recognized that "it may seem harsh to shield a conflicted transaction from judicial review under Delaware law based on a vote of unitholders without requiring the disclosure of all material information." Op. 26. But the Court held that the LPA only required that unitholders be given a copy of the Merger Agreement and that anything else was of

no legal relevance. Op. 20. Since the Merger Agreement was, in fact, provided to unitholders, the Court held that Defendants could rely on the unitholders' approval as a safe harbor to this conflicted transaction. Given this disposition, the Court did not find it necessary to decide whether the safe harbor regarding special approval by a conflicts committee was also satisfied.

SUMMARY OF ARGUMENT

1. The Court below erred in concluding that the safe harbor based on unitholder approval was satisfied where Defendants induced such vote through false and misleading statements to unitholders. While the LPA may have specified only that unitholders be given a copy of the merger agreement, Defendants did not stop there. Instead, in order to induce a vote in favor of the merger, Defendants elected voluntarily to make misleading statements that the Conflicts Committee members were independent and that Special Approval in accordance with the LPA had been obtained. The limited partners never consented to being lied to. Nothing in the LPA provides, and the parties to the LPA could not have intended, that Defendants could rely on the unitholder approval safe harbor where the vote was obtained through misleading statements and material omissions.

2. Nor can Defendants rely on the safe harbor regarding Special Approval by a Conflicts Committee. The LPA prohibits Conflicts Committee members from serving on affiliate boards and also requires compliance with the NYSE independence rules for audit committee members. However, Brannon was a director of Sunoco LP, a Regency GP affiliate. He resigned from the Sunoco board four days after he began to evaluate the deal and was reappointed to the Sunoco board on the very day that the Merger closed. The other Conflicts Committee member, Bryant, was also appointed to the Sunoco board on the day

the Merger closed. Thus, Brannon was on an affiliate board during a portion of the time that he served on the Conflicts Committee, and neither Brannon nor Bryant was independent. In any event, assuming, *arguendo*, that there was no violation of the express terms of the LPA, the charade whereby Brannon briefly left the Sunoco board and then quickly rejoined it upon the closing of the Merger violates the implied covenant of good faith and fair dealing.

3. Lastly, LPA §7.10(b) (A106), which provides that acts taken in reliance on a financial advisor are conclusively presumed to have been done in good faith, is inapplicable to conflict-of-interest transactions, especially where, as here, the advisor is selected by a sham conflicts committee. If that provision applied to such transactions, the detailed safe harbors in LPA§7.9(a) (A105) would be wholly superfluous.

STATEMENT OF FACTS

A. REGENCY AND ITS RELATIONSHIP TO ETE AND ETP

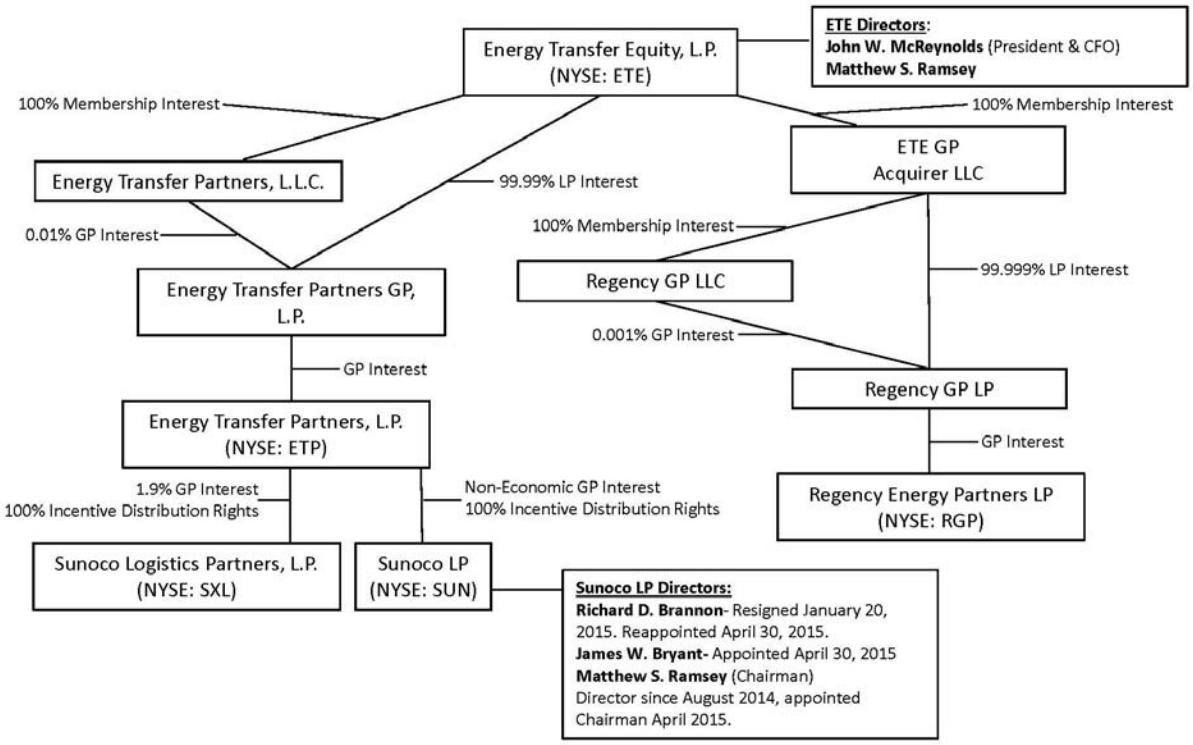
Regency is engaged in gathering, processing, and transporting natural gas. A19-20. It delivered strong results in 2013 and throughout 2014 despite declining oil and gas prices. A20-22. Regency's CEO informed investors on November 9, 2014 that Regency was "in a good position" and expected "strong continued growth with additional projects coming online" in 2015 and 2016 and "a current backlog of around $2 billion in approved organic growth projects." A23-24.

Regency GP, is owned by ETE, a master limited partnership at the head of the Energy Transfer family. A17.[2] ETE also owns the general partner of Regency GP, Regency GP LLC, and the general partner of Regency's acquirer, ETP. A17. Several of ETE's senior executives serve as directors of ETP, including ETE's president and ETE's chief financial officer. Even prior to the Merger, two of the five members of Regency GP LLC's board were also directors of ETE. A18. Defendant Ramsey, in addition to being a director of ETE, was a member of the Sunoco board during the Merger negotiations, and was appointed chairman of the Sunoco board on April 30, 2015, the day the Merger closed.[3] The ownership

[2] The Energy Transfer family consists of ETE, ETP, Sunoco LP, and Sunoco Logistics Partners L.P., with ETE owning the general partner and 100% of the incentive distribution rights of ETP. ETP, in turn, owns the general partners and 100% of the distribution rights of each of Sunoco LP and Sunoco Logistics Partners L.P. A17-18.

[3] *See* A498.

structure of Regency and Sunoco and the relevant board memberships of the Regency Board are as follows:



A177; A494; A498.

B. THE LPA'S PROVISIONS CONCERNING CONFLICT-OF-INTEREST TRANSACTIONS

The LPA contains detailed provisions concerning the resolution of potential conflicts between the interests of common unitholders and the interests of ETE and ETP. A27-28. LPA §7.9, entitled "Resolution of Conflicts of Interest; Standards of Conduct and Modification of Duties," provides several mechanisms to account for the interests of common unitholders in a conflicted transaction, such as the Merger. Specifically, the conflict can be resolved if the course of action is:

> (i) approved by Special Approval, (ii) approved by the vote of a majority of the Common Units (excluding Common Units owned by the General Partner and its Affiliates), (iii) on terms no less favorable to the Partnership than those generally being provided to or available from unrelated third parties, or (iv) fair and reasonable to the Partnership, taking into account the totality of the relationships between the parties involved (including other transactions that may be particularly favorable or advantageous to the Partnership).

A27; LPA §7.9(a) (A105). Here, Defendants elected to proceed with the "Special Approval" process under §7.9(a)(i) and a unitholder vote under §7.9(a)(ii).

Special Approval is defined in the LPA as "approval by a majority of the members of the Conflicts Committee," which is defined as:

> a committee of the Board of Directors of the general partner of the General Partner composed entirely of two or more directors *who are not* (a) security holders, officers or employees of the General Partner, (b) *officers, directors or employees of any Affiliate of the General Partner*, or (c) holders of any ownership interest in the Partnership Group other than Common Units *and who also meet the independence standards required of directors who serve on an audit committee of a board of directors established by the Securities Exchange Act of 1934, as amended, and the rules and regulations of the Commission thereunder and by the National Securities Exchange on which the Common Units are listed or admitted to trading.*

A28-29; A62.[4] Members of the Conflicts Committee are thus prohibited from serving on the board of any affiliate of Regency GP. The term "affiliate" is defined in the LPA as any person "that directly or indirectly through one or more intermediaries *controls, is controlled by or is under common control with*, the

[4] Unless otherwise noted, all emphasis in quoted material has been supplied.

Person in question." A29. Sunoco and Regency GP, are both controlled by ETE and therefore "affiliates," under the LPA. A30. Accordingly, Sunoco board members were not eligible to serve as members of the Conflicts Committee. A30.

C. THE MERGER AND THE COMPROMISED CONFLICTS COMMITTEE

ETE and ETP seized upon the opportunity to acquire Regency at bargain basement prices precisely at the moment that Regency's stock price hit a three-year low. A13; A16. On January 16, 2015, the ETE and ETP boards held a joint meeting and approved a proposal to merge Regency into ETP for a combination of cash and stock reflecting an exchange ratio of 0.4044 ETP common units per one common unit of Regency and a $137 million cash payment. A33. The proposal significantly undervalued Regency for the benefit of ETE and ETP. A13; A25.

ETE and ETP implemented an improper scheme to secure this benefit for themselves at the expense of Regency common unit holders. ETE and ETP ensured that the Conflicts Committee would consist of ETE and ETP loyalists: Brannon and Bryant. On January 16, 2015, ETE installed Brannon on the board of Regency GP LLC to become a member of the two-person Conflicts Committee. A29-30; A34. As he was also a director of ETP-controlled Regency affiliate Sunoco, Brannon was ineligible to serve on the Conflicts Committee. A30-32. However, Brannon nevertheless began acting immediately as a *de facto* member of the Conflicts Committee to lay the groundwork for a transaction that would benefit

ETE and ETP at the expense of Regency's common unitholders. A34. On January 20, Brannon resigned temporarily from the Sunoco board for the duration of the Conflicts Committee process, only to rejoin the Sunoco board on April 30 – the very same day that the Merger closed. A29-30.[5] Leaving nothing to chance, ETE and ETP ensured that the Conflicts Committee's only other member, Bryant was co-opted too, appointing him along with Brannon to the Sunoco board on the same day that the Merger closed. A18; A31. Brannon and Bryant also failed to satisfy the NYSE's independence standards for audit committees, as required by the LPA. The NYSE rules disqualify directors who have "[m]aterial relationship[s] with the [listed] company." A15; A31-32; A412. Brannon and Bryant, who were doubtlessly aware of their impending appointment to the Sunoco board, A14, fail to meet the NYSE's independence standards.

ETE and ETP also ensured that the Conflicts Committee's financial advisor would support a deal that favored their interests. On January 16, 2015, the same day that Regency received ETE's and ETP's proposal, Regency's CFO, Long, asked JP Morgan to serve as financial advisor to the Conflicts Committee. A207. It was known that Long was "expected to become the Chief Financial Officer of ETP GP LLC," A235, and hence JP Morgan knew that pleasing Long would help

[5] Nobody was appointed to the Sunoco board to take Brannon's place after he "resigned" on January 20, 2015, and his Board seat remained vacant, awaiting his return. *See* A505-07 (describing Sunoco's board members, all of whom were appointed in August 2014).

cement its long-term relationship with the Energy Transfer family.

D. THE CONFLICTS COMMITTEE'S SHAM NEGOTIATIONS

Since Regency's unit price is intrinsically tied to the price of natural gas, time was of the essence to do the deal before gas prices begin to rise, causing a concomitant increase in the value of Regency. A13. Hence, negotiations between Regency and ETP lasted only a few days. A13; A35.

The Conflicts Committee set a goal of realizing a meager 15% premium to the artificially depressed closing price of common units, which they used as the basis for a slightly increased counter-offer. A25; A35; A211. On January 23, ETP rejected the Conflicts Committee's perfunctory counter offer and refused to offer the 15% premium to that day's closing price for common units that the Conflicts Committee had purportedly resolved to achieve. A211. The Conflicts Committee quickly backed off its goal and acceded to ETP's insistence on a mere 13.2% premium over January 23's closing price. A35; A211. The Conflicts Committee recommended that the Board pursue the transaction and, on January 25, the Board approved the Merger. A35.

The entire process from ETP's initial offer to the Board's approval lasted nine days. A35. The Conflicts Committee did not solicit any potentially interested buyers and did not conduct any market check. The Conflicts Committee also agreed to a no-solicitation clause in the Merger agreement prohibiting Regency

from sharing confidential information with any potentially interested party.

E. THE UNITHOLDER APPROVAL INDUCED BY DEFENDANTS' MISLEADING STATEMENTS

On March 24, Regency filed a final proxy statement seeking unitholder approval for the Merger. The Proxy did not disclose to Regency's unitholders Brannon's and Bryant's conflicts. A16. Unitholders were not informed that Brannon had just resigned from an affiliate's board or that Brannon and Bryant would rejoin/join the Sunoco board immediately after the closing of the transaction that pitted the unitholders' interests against the interests of Sunoco's controller, ETP. A32. Instead, unitholders were told that the "Conflicts Committee consists of two *independent* directors: Richard D. Brannon (Chairman) and James W. Bryant." A215. They were further told that the Conflicts Committee unanimously approved the Merger as fair and reasonable, and that such "approval *constituted 'Special Approval' as defined in the Regency partnership agreement*." *Id*. Thus, as the Complaint alleges, "[i]n announcing the terms of the Merger and in soliciting votes from Regency's common unit holders, the Defendants claimed that these terms … were negotiated and approved by an independent and valid Conflicts Committee of the Regency GP LLC Board.… [T]his was untrue." A25. Having been misled regarding the Conflicts Committee and the purported Special Approval, the unitholders approved the Merger Agreement on April 28, and the Merger closed on April 30. *Id*.

ARGUMENT

"To allege a breach of a contractual duty to act in good faith, a complaint need only allege facts related to the alleged act taken in bad faith, and a plausible motivation for it." *Clean Harbors, Inc. v. Safety-Kleen, Inc.*, 2011 WL 6793718, at *7 (Del. Ch. Dec. 9, 2011) (internal quotation marks omitted) (noting that this is a minimal standard, the purpose of which is to give defendants notice of the claims against them).[6] The allegations in the Complaint are plainly sufficient to allege a breach of the LPA's requirement that the general partner act in good faith,[7] and the Court below did not hold otherwise. *See* A3; A28; A39; A40; Op. 15.

Instead, the Court held that Defendants' conduct cannot constitute a breach of the LPA because they satisfied a safe harbor in the LPA – approval by a vote of the disinterested unitholders pursuant to LPA §7.9(a)(ii) (A105). Op. 2, 17-25. As discussed below, this was error.

[6] *See Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund, II, L.P.*, 624 A.2d 1199, 1206 (Del. 1993) (finding that plaintiff's allegation that defendants "acted in bad faith and in a retaliatory manner" was sufficient to satisfy the notice pleading threshold).

[7] LPA §7.9(b) (A106).

I. THE COURT OF CHANCERY ERRED IN HOLDING THAT THE UNITHOLDER APPROVAL SAFE HARBOR WAS SATISFIED

A. QUESTION PRESENTED

Did the trial court err in holding that the general partner of a limited partnership can rely on a unitholder vote to bless a conflict-of-interest transaction despite the fact that the proxy provided misleading information to unitholders by falsely indicating that an independent conflicts committee had given the transaction special approval in accordance with the partnership agreement? Op. 2, 17-25; A454-59; A602-04; A607-08.

B. SCOPE OF REVIEW

This Court's review of the decision on a motion to dismiss under Ch. Ct. R. 23.1 is *de novo* and plenary. *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000). The Court must accept all well-pleaded allegations of the complaint as true and draw all reasonable inferences in Plaintiff's favor. *Beam v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

C. MERITS OF ARGUMENT

The Court below erred in holding that the unitholder vote approving the Merger satisfied the safe harbor of LPA §7.9(a)(ii) (A105). The Court recognized that "the doctrine of stockholder ratification requires stockholders to be fully informed in order for ratification to have legal effect." Op. 17 & n.30. *See, e.g.*, *Michelson v. Duncan*, 407 A.2d 211, 220 (Del. 1979) ("Shareholder ratification is

valid only where the stockholders so ratifying are adequately informed of the consequences of their acts and the reasons therefor ….").[8] Here, Defendants misled the unitholders about the independence of the Conflicts Committee and failed to disclose Brannon's service on the Sunoco board and that both Bryant and Brannon would join/rejoin that board upon consummation of the Merger. A32.

The Court below, however, held that the foregoing principles regarding stockholder ratification were inapplicable, because the LPA eliminated the fiduciary duty of disclosure and contains only one disclosure requirement relevant to the approval of a merger: "'A copy or a summary of the Merger Agreement shall be included in or enclosed with the notice of a special meeting or the written consent.'" Op. 20 (quoting LPA §14.3(a) (A124-25)). Therefore, the Chancellor held that Defendants could effectively lie and mislead the unitholders by falsely representing that Bryant and Brannon were independent, and failing to disclose that Brannon had been a Sunoco director immediately before he joined the Conflicts Committee and for a few days thereafter, or that Bryant and Brannon would join/rejoin Sunoco's board immediately after the Merger closed, and still rely on the unitholder approval safe harbor. This was error.

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[8] *See also Sample v. Morgan*, 914 A.2d 647, 664-65 (Del. Ch. 2007) ("In order for directors to access the safe harbor of ratification, they must meet an affirmative 'burden of demonstrating full and fair disclosure.'"); *Citron v. E.I Du Pont de Nemours & Co.*, 584 A.2d 490, 502 (Del. Ch. 1990) ("It is axiomatic that for shareholder ratification of any corporate action to be valid, the vote of the minority shareholders must be fully informed.").

Assuming, *arguendo*, that Defendants initially had no duty to disclose any facts concerning Brannon, Bryant, the Conflicts Committee or Special Approval, in order to induce unitholder approval of the Merger, Defendants chose voluntarily to make numerous statements in the Proxy concerning these matters. While the Court below characterized the situation as one in which the unitholders were "uninformed," Op. 2, 17, it goes much further than that; the unitholders were affirmatively misled. Trying to convince unitholders to vote for the Merger, the Proxy contains approximately a dozen pages detailing the composition of the Conflicts Committee, its activities, and its grant of Special Approval. *See* A207-19. The Proxy touts that the "Conflicts Committee consists of two independent directors: Richard D. Brannon (Chairman) and James W. Bryant." A215. It further states that the Conflicts Committee unanimously approved the merger as fair and reasonable, and that such "approval constituted 'Special Approval' as defined in the Regency partnership agreement." *Id*.; *see* A10; A25; A32.

Defendants thus voluntarily asserted to unitholders that the Conflicts Committee members were independent and that their approval of the merger satisfied the LPA's Special Approval safe harbor. Regardless of whether Defendants had, *ab initio*, any disclosure obligations, the LPA should not be construed to allow Defendants to take advantage of the unitholder approval safe harbor where Defendants induced that approval by affirmatively misleading the

unitholders regarding the Conflicts Committee and failing to disclose the facts regarding Brannon's and Bryant's conflicts, which facts were necessary in order to avoid making Defendants' statements misleading. *See* A602-03.

It is one thing for a contract to provide for only limited disclosure obligations; it is another thing entirely to say that the contract permits a party to rely on a vote induced through false and misleading statements. Nothing in the LPA provides that the limited partners consented to being lied to. To construe the LPA to allow Defendants affirmatively to mislead the unitholders and nevertheless rely on the unitholder approval safe harbor for conflicted transactions would be an absurd result that could not have been intended. Courts reject an interpretation of a contract that "produces an absurd result or one that no reasonable person would have accepted when entering the contract." *Estate of Osborn v. Kemp*, 991 A.2d 1153, 1160 (Del. 2010). Furthermore, this Court applies to limited partnership agreements involving multiple investors "the principle of *contra proferentem*," whereby "ambiguous terms in the Agreement should be construed against the General Partner as the entity solely responsible for the articulation of those terms." *SI Mgmt. L.P. v. Wininger*, 707 A.2d 37, 42-43 (1998).

The LPA should be interpreted to be consistent with the established principle that "though there is no general duty to speak, if a person undertakes to speak he has a duty to make a full and fair disclosure as to the matters about which he

presumes to speak." *Bank of Delaware v. Wright Construction Co.*, 1986 WL 5866, at *2 (Del. Super. Ct. Apr. 28, 1986); *accord Lock v. Schreppler*, 426 A.2d 856, 862 (Del. Super. Ct. 1981); *see Voilas v. General Motors Corp.*, 170 F.3d 367, 378 (3d Cir. 1999) ("Even where no duty to speak exists, one who elects to speak must tell the truth when it is apparent that another may reasonably rely on the statements made.") (internal quotation marks omitted).

In re Cencom Cable Income Partners, L.P. Litig., 1997 WL 666970 (Del. Ch. Oct. 15, 1997), applied these principles to a limited partnership. The case involved a proposed sale of partnership assets to affiliates of the general partner, which under the partnership agreement required a vote by the limited partners. The partnership agreement did not require the general partner to hire a law firm to represent the interests of the limited partners or to render an opinion concerning the proposed transaction, but the general partner did so anyway and stated in the disclosure statement provided to the limited partners that this firm would deliver an opinion regarding the fairness of the transaction. When the firm did not do so and the limited partners sued, the general partner moved for summary judgment, arguing that it had no duty under the partnership agreement to retain a law firm to provide such an opinion. Vice Chancellor Steele rejected this argument, holding that the general partner had "voluntarily assumed a duty," even though the agreement did not impose any such duty, in order "to convince the [Limited

Partners] the self-interested transaction would conform to the terms of the Partnership Agreement." *Id*. at *5. Later in the litigation, the general partner again moved for summary judgment, and the Court again denied the motion, noting that "[i]t is reasonable to read the disclosure to be an attempt to convince the prospective voting Limited Partners that special measures had been taken to protect their interests and correspondingly that their level of comfort with both the process and the terms of the sale would be enhanced." *In re Cencom Cable Income Partners, L.P. Litig*., 2000 WL 640676, at *3 (Del. Ch. May 5, 2000).

Similarly here, Defendants chose voluntarily to make statements that the Conflicts Committee members were independent and that Special Approval as provided for in the LPA had been obtained. Whether or not the LPA imposed a duty to disclose facts regarding the Committee, the LPA should not be construed to allow reliance on the unitholder approval safe harbor where the approval was obtained through misleading statements about the Committee made to provide the unitholders a "level of comfort" concerning the self-interested transaction.

The *Cencom* analysis was endorsed in *Sonet v. Timber Co., L.P.*, 722 A.2d 319 (Del. Ch. 1998), which involved a limited partnership agreement that replaced traditional fiduciary duties with certain specific contractual obligations. *Id*. at 323. The agreement provided that the general partner could, in its "sole discretion," enter into various transactions and mergers, subject to a supermajority vote of the

unitholders. *Id*. at 324. Relying on *Cencom*, the plaintiffs argued that even if the general partner did not owe any fiduciary duties as a matter of law or by virtue of the partnership agreement, when the general partner voluntarily appointed a special committee to oversee the transaction, it undertook to conduct the process in a fair and independent manner. *Id*. at 326. Chancellor Chandler dismissed the case, distinguishing *Cencom*, but in so doing reinforced the vitality of *Cencom* and its applicability to the situation here. Chancellor Chandler noted that "[c]entral to the holding in *Cencom* is the fact that the general partner circulated a disclosure statement that described what the independent counsel was supposed to do." *Id*. at 326-27. In contrast, in *Sonet* that proxy had "not yet been distributed" and defendants had "not yet sought unitholder action." *Id*. at 327. Thus, the Court held, "without misleading affirmative disclosures professing the fairness and independence of the special committee," *Cencom* did not apply. *Id.* Here, Defendants did circulate a proxy professing the independence of the Conflicts Committee and asserting that Special Approval had been properly obtained, but failed to disclose facts needed to make the proxy not misleading.

The LPA should not be construed to allow reliance on the unitholder approval safe harbor where the vote was obtained through misleading statements. The holding below that the safe harbor was satisfied should be reversed.

II. THE SPECIAL APPROVAL GIVEN BY THE CONFLICTS COMMITTEE DOES NOT PROVIDE A BASIS FOR DISMISSAL

A. QUESTION PRESENTED

Where a limited partnership agreement provides a safe harbor for conflict-of-interest transactions if special approval is given by a conflicts committee comprised of members who are not directors of the general partner's affiliates and who meet the NYSE independence requirements, does it violate this provision, or the implied covenant of good faith and fair dealing, where

- one of the members resigned from an affiliate's board four days *after* he began to evaluate the transaction and was reappointed to the affiliate's board on the same day that the transaction closed, and
- the other member was also appointed to the affiliate's board on the same day that the transaction closed?

Op. 16, 29-30; A448-54; A466-77; A620-29.

B. SCOPE OF REVIEW

This Court's review of the decision on a motion to dismiss under Ch. Ct. R. 23.1 is *de novo* and plenary. *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000). The Court must accept all well-pleaded allegations of the complaint as true and draw all reasonable inferences in Plaintiff's favor. *Beam v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

C. MERITS OF ARGUMENT

In the Court below, Defendants argued that they also satisfied the safe harbor of LPA §7.9(a)(i): Special Approval by a Conflicts Committee (A105). The Court noted this issue but held that in light of its decision to dismiss the Complaint on the basis of the safe harbor of LPA §7.9(a)(ii), there was no need to address the Special Approval safe harbor. Op. 16; *see also* Op. 29-30. In the event that this Court finds that the safe harbor of §7.9(a)(ii) is not satisfied and proceeds to address § 7.9(a)(i), it is respectfully submitted that the Court should hold that Defendants cannot invoke § 7.9(a)(i) to shield the transaction.[9]

1. The Appointment of Brannon and Bryant to the Conflicts Committee Violated the Express Terms of the LPA

Under the LPA, directors who served as board members of affiliates or did not meet the NYSE independence requirements were not permitted to be members of the Conflicts Committee. A28-29; A62. Here, however, this provision was not satisfied because Brannon served as a director of Regency affiliate Sunoco while serving on the Conflicts Committee and neither Brannon nor Bryant met the contractually-required NYSE independence requirements.

[9] This Court can, "in the interest of justice and for the sake of judicial economy," decide issues not reached below. *Bank of N.Y. Mellon v. Commerzbank Cap. Funding Trust II*, 65 A.3d 539, 553 (Del. 2013). The Court might also consider remanding on this issue since the Chancellor did not rule on it. *See, e.g.*, *Ross v. Dep't of Correction of the State of Delaware*, 697 A.2d 377, 378 (Del. 1997).

(a) Brannon Served as a Member of the Conflicts Committee While He Was a Member of the Sunoco Board

The Conflicts Committee was actually convened on January 16, 2015 when Brannon was appointed to the Regency GP LLC Board. A207.[10] Brannon did not resign from the Sunoco board until January 20. A522. Five days after Brannon's resignation from the Sunoco board, the Conflicts Committee approved and recommended the Merger. Thus, for approximately half the time he served as a Conflicts Committee member, Brannon was also a board member of an affiliate.

Prior to resigning from the Sunoco board, Brannon commenced work as a Conflicts Committee member. On January 16, Regency received an initial draft of the Merger agreement and contacted a representative of Akin Gump Strauss Hauer & Feld LLP ("Akin Gump") to discuss potential engagement as Conflicts Committee counsel. A207. It is not reasonable to infer that the Merger Agreement was withheld from Brannon, or that Brannon was not involved in selecting counsel. Further, Brannon was still a member of the Sunoco board when he participated in a meeting with Bryant, Akin Gump and Regency management on January 19, "to discuss … strategy with regard to the proposed transaction." A34.

[10] According to the proxy, on January 16, the Regency Board decided that ETP's "proposal would be subject to approval of the Regency Conflicts Committee and that it would be appropriate to delegate authority to the Regency Conflicts Committee to review the proposed transaction." A207. Formal resolutions delegating authority to the Conflicts Committee were adopted on January 22 and were "consistent with the deliberations of the Regency Board on January 16, 2015." *Id.*

Later that same day, Akin Gump met with "representatives of [ETP's counsel] … to discuss issues identified in the initial draft of the merger agreement and related matters" and had "a call with representatives of [ETP's counsel] to discuss the status and timing of the proposed transaction." A207-08. Akin Gump would not have performed these functions if there were no Conflicts Committee.[11]

The Proxy notes that during a January 20 call, Akin Gump, Brannon and Bryant discussed "the independence of the members of the Conflicts Committee." A208. Brannon immediately resigned from the Sunoco board, and not coincidentally, the Proxy begins to refer to Brannon and Bryant as the "Conflicts Committee." It can be inferred that on January 20, after Brannon and Bryant had been serving on the Conflicts Committee for four days, their counsel Akin Gump belatedly identified Brannon's ineligibility because of his simultaneous service on the Sunoco board.

While a four-day overlap of service on the Conflicts Committee and on the Sunoco board may seem insignificant, in this case it accounts for nearly half the duration of the Conflicts Committee's deliberation of the Merger, which was approved just five days after Brannon's Sunoco board resignation. A212.

[11] Furthermore, on January 20, the Conflicts Committee "had a call with representatives of Akin Gump to *confirm* their engagement by the Regency Conflicts Committee," A208, suggesting that Akin Gump had been *de facto* counsel to the Conflicts Committee prior to "confirmation" on January 20.

Brannon's simultaneous service on the Sunoco board and on the Conflicts Committee violates the express terms of the LPA.

(b) Neither Brannon Nor Bryant Was Independent Under NYSE Rules

Brannon's and Bryant's service on the Conflicts Committee also violated the LPA because neither met the NYSE requirements for independence for service on audit committees, as required to by the LPA. A31-32.

Pursuant to §303A.07(a) of the NYSE Listed Company Manual: "[a]ll audit committee members must satisfy the requirements for independence set out in Section 303A.02 and, in the absence of an applicable exemption, Rule 10A-3(b)(1)" of the rules promulgated under the Securities Exchange Act of 1934 (the "Exchange Act"). Section 303A.02(a)(i) of the NYSE Listed Company Manual provides that "[n]o director qualifies as 'independent' unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company)." A412. The NYSE's official commentary further notes (*id.*):

> It is not possible to anticipate, or explicitly to provide for, all circumstances that might signal potential conflicts of interest, or that might bear on the materiality of a director's relationship to a listed company (references to "listed company" would include any parent or subsidiary in a consolidated group with the listed company). Accordingly, it is best that boards making "independence" determinations broadly consider *all relevant facts and circumstances.*

> In particular, when assessing the materiality of a director's relationship with the listed company, the board should consider the issue *not merely from the standpoint of the director, but also from that of persons or organizations with which the director has an affiliation. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships, among others.*

Under these standards, Brannon and Bryant did not meet the NYSE requirements for independence for service on audit committees as required by the LPA. Brannon was participating in a "revolving door" with the Sunoco board simply to approve the Merger for the benefit of Sunoco's controller, ETP. Bryant joined the Sunoco board the day the Merger was consummated. Both were doubtlessly aware of their impending reappointment/appointment to the Sunoco board, A14, and neither was independent.

2. Defendants' Appointment of "Revolving Door" Directors as Members of the Conflicts Committee Violates the Implied Covenant of Good Faith and Fair Dealing

The implied covenant, which "attaches to every contract," *Dunlap v. State Farm Fire & Cas. Co.*, 878 A.2d 434, 442 (Del. 2005), requires that a party "refrain from arbitrary or unreasonable conduct which has the effect of preventing the other party to the contract from receiving the fruits of the bargain." *ASB Allegiance Real Estate Fund v. Scion Breckenridge Managing Member, LLC*, 50 A.3d 434, 440-42 (Del. Ch. 2012), *aff'd in part, rev'd in part on other grounds*, 68 A.3d 665 (Del. 2013). The implied covenant is a contractual gap-filler that

"requires more than just literal compliance with [the contract]"). *Dunlap*, 878 A.2d at 444. "[A] partnership agreement may not limit or eliminate liability for any act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing." 6 Del. C. § 17-1101(d). And, in particular, with respect to a partnership agreement like the LPA, "the implied covenant constrains how the Special Approval process may be carried out." *Gerber v. Enterprise Prods.*, 67 A.3d 400, 424 (Del. 2013); *see In re Kinder Morgan, Inc. Corporate Reorganization Litig.*, 2015 WL 4975270, at *9 (Del. Ch. Aug. 20, 2015) ("the implied covenant constrains the Special Approval process").

On an implied covenant claim, the issue is whether it is "clear from what was expressly agreed upon that the parties who negotiated the express terms of the contract 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." *Katz v. Oak Indus., Inc.*, 508 A.2d 873, 880 (Del. Ch. 1986).

The purpose of the Special Approval process, along with the definition of "Conflicts Committee," is to protect Regency's unitholders' interests while permitting Regency's GP to engage in a conflicted transaction. The lynchpin of this safeguard is the assurance that the Conflicts Committee members are themselves free from any conflict that would disable them from evaluating the conflicted transaction impartially. Pursuant to the LPA, individuals disqualified

from service on the Conflicts Committee include, *inter alia*, (1) officers, directors or employees of any Affiliate of Regency GP; and (2) anyone who does not "meet the independence standards required of directors who serve on an audit committee of a board of directors" of the Exchange Act and the NYSE. A62.

The parties to the LPA did not anticipate that formation of a conflicts committee consisting of (1) one member who resigned from a Regency GP affiliate board on the same day that he was formally appointed to the Conflicts Committee, and then was reappointed to the affiliate board on the very day the conflicted transaction closed, and (2) another member who likewise was appointed to the affiliate board on the same day that the transaction closed. Thus, although the LPA does identify certain categories of persons ineligible to sit on a conflicts committee, it leaves a gap.

Regency's unitholders could not have anticipated this gap when deciding to invest in Regency. *Gerber*, 67 A.3d at 422, is instructive. That case involved a challenge to a limited partnership's sale of an asset to an affiliate of its general partner. The plaintiffs claimed that the asset was sold at an unfairly low price, to their detriment and to the benefit of the affiliate. *Id.* at 406. The defendants pointed to a limited partnership agreement provision which stated that reliance upon a qualified expert's fairness opinion created conclusive evidence of "good faith." *Id.* at 410-11. However, this Court determined that the fairness opinion did

not perform its intended function to value the asset that was sold. *Id.* at 421-22. "At the time of contracting ... [the unitholder] could hardly have anticipated that [the general partner] would rely upon a fairness opinion that did not fulfill its basic function – evaluating the consideration the LP unitholders received for purposes of opining whether the transaction was financially fair." *Id.* at 422. Similarly here, the Special Approval process did not fulfill its "basic function" of providing a disinterested review of a conflicted transaction, and the Regency unitholders could not be "fairly ... charged with having anticipated" that Defendants would engage in a charade to feign compliance with the LPA's safe harbor. *Id.* at 423.

Once an unanticipated contractual gap is found, the next inquiry is to determine what the parties would have bargained for had they anticipated the gap. A guiding principle is that "[t]he implied covenant requires that a party refrain from arbitrary or unreasonable conduct which has the effect of preventing the other party to the contract from receiving the fruits of its bargain." *ASB Allegiance*, 50 A.3d at 440 (internal quotation marks omitted); *see also eCommerce Indus., Inc. v. MWA Intelligence, Inc.*, 2013 WL 5621678, at *34 (Del. Ch. Sept. 30, 2013) (finding that party was "denied ... the fruits of its bargain" where the offending party "encouraged and benefitted from the sale of competing ... software, ... the very thing that the non-compete provision was intended to prevent"); *Gerber*, 67 A.3d at 421 (analyzing whether defendant "'acted arbitrarily or unreasonably,

thereby frustrating the fruits of the bargain that [plaintiff] reasonably expected'"). The standard here is low, requiring only facts showing that it is "*reasonably inferable* that, had the parties focused on that question at the time of contracting, they would have proscribed such conduct." *Id.* at 425; *see also Renco Group, Inc. v. MacAndrews AMG Holdings LLC*, 2015 WL 394011, at *7 (Del. Ch. Jan. 29, 2015) (refusing to dismiss claims where the Court could not "foreclose the *reasonably conceivable* claims" that the alleged misconduct frustrated plaintiff's "reasonable expectations").

Here, the "fruit of the bargain" and the "contractual expectations" of the unitholders was to have a Conflicts Committee unbeholden to any Regency GP affiliates when negotiating a transaction involving the interests of Regency GP and its affiliates. The decision to appoint Brannon, who only temporarily left the Sunoco board in order to vote for the Merger and who was immediately reappointed to the Sunoco board upon the closing of the Merger, frustrated the "contractual expectations" of §7.9(a)(i) and violated the implied covenant.

III. DEFENDANTS' PURPORTED RELIANCE ON THE OPINION OF A FINANCIAL ADVISOR DOES NOT PROVIDE A BASIS FOR DISMISSAL

A. QUESTION PRESENTED

Should Regency GP be conclusively presumed to have acted in good faith because it allegedly relied on a financial advisor? Op. 16 n.26; A459-61; A637-40.

B. SCOPE OF REVIEW

This Court's review of the decision on a motion to dismiss under Ch. Ct. R. 23.1 is *de novo* and plenary. *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000). The Court must accept all well-pleaded allegations of the complaint as true and draw all reasonable inferences in Plaintiff's favor. *Beam v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

C. MERITS OF ARGUMENT

Defendants argued below that under LPA §7.10(b) (A106), Regency GP is conclusively presumed to have acted in good faith because it supposedly relied on an opinion by a financial advisor.[12] Plaintiff argued that that provision did not apply. A637-40. The Court did not reach this issue, in light of its decision to

[12] LPA §7.10(b) (A106) states:

> The General Partner may consult with legal counsel, accountants, appraisers, management consultants, investment bankers and other consultants and advisers selected by it, and any act taken or omitted to be taken in reliance upon the opinion (including an Opinion of Counsel) of such Persons as to matters that the General Partner reasonably believes to be within such Person's professional or expert competence shall be conclusively presumed to have been done or omitted in good faith and in accordance with such opinion.

dismiss the Complaint on the basis of the safe harbor of LPA §7.9(a)(ii). Op. 16 n.26. In the event that this Court proceeds to address §7.10(b), it is respectfully submitted that the Court should hold that that provision does not protect conflict-of-interest transactions as to which the safe harbors of §7.9(a) would apply. This issue was raised in this Court in *Allen v. Encore Energy Partners, L.P.*, 72 A.3d 93 (Del. 2013), but in light of the way the Court disposed of the appeal in that case, the Court did not need to reach the issue. *Id*. at 103.

Defendants' position is that under §7.10(b), if Regency GP obtains an opinion of a financial advisor, a conflict-of-interest transaction is conclusively presumed to be entered into in good faith, even if none of the safe harbors of §7.9(a) are satisfied, *i.e.*, there is no need for a conflicts committee, special approval, unitholder approval, etc., as long as there is an opinion of a financial advisor. This "magic bullet" argument proves too much. Virtually every transaction will involve an opinion of a financial advisor. If that is all that is necessary to bless a conflict-of-interest transaction, then the detailed safe harbor provisions are, as a practical matter, mere surplusage, provisions that rarely if ever will come into play. That could not be the intent of the parties. "'Under general principles of contract law, a contract should be interpreted in such a way as to not render any of its provisions illusory or meaningless.'" *Estate of Osborn v. Kemp*, 991 A.2d 1153, 1159 n.17 (Del. 2010) (quoting *Sonitrol Holding Co. v. Marceau*

Investissements, 607 A.2d 1177, 1183 (Del. 1992)). "'In upholding the intentions of the parties, a court must construe the agreement as a whole, giving effect to all provisions therein, in order not to render any part of the contract mere surplusage, and, if possible, reconcile all the provisions of the instrument.'" *Akzo Nobel Coatings, Inc. v. Dow Chem. Co*., 2015 WL 3536151, at *8 n.48 (Del. Ch. June 5, 2015) (quoting *Commercial Bank v. Global Payments Direct, Inc*., 2014 WL 3567610, at *8 (Del. Ch. July 21, 2014)). A far more reasonable construction of the LPA is that §7.10(b) does not apply to conflict-of-interest transactions to which the safe harbors of §7.9(a) apply, especially where, as here, the financial advisor was hired by a sham conflicts committee.

Furthermore, §7.10(b) applies only where the general partner acts "*in reliance upon* the opinion" of the financial advisor. A106. But reliance is an issue of fact not susceptible to resolution on a motion to dismiss. *See North Am. Philips Corp. v. Aetna Casualty & Sur. Co.*, 1995 WL 626047, at *9 (Del. Super. Ct. Apr. 18, 1995) ("NAPC's alleged reliance upon Travelers' advice should be submitted to the trier of fact."). "Whether … reliance actually occurred is a question of fact that cannot be determined at" the motion to dismiss stage of a case. *Zazzali v. Alexander Partners, LLC*, 2013 WL 5416871, at *9 n.12 (D. Del. Sept. 25, 2013).

Defendants' alleged reliance on the opinion of a financial advisor does not provide a basis for dismissal.

CONCLUSION

The decision below should be reversed, with costs.

Dated: June 9, 2016

Respectfully submitted,

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CERTIFICATE OF SERVICE

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