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Case Number 330,2016

IN THE SUPREME COURT OF THE STATE OF DELAWARE

THE WILLIAMS COMPANIES, INC.,	)	
	)	
Plaintiff Below-Appellant,	)	No. 330, 2016
	)	
v.	)	Court below: Court of Chancery of the State of Delaware
	)	
ENERGY TRANSFER EQUITY, L.P., et al.,	)	C.A. Nos. 12168-VCG and 12337-VCG
	)	
Defendants Below-Appellees.	)	
	)	

APPELLANT'S OPENING BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes & Rules

Other Authorities

NATURE OF THE PROCEEDINGS

This is an appeal from a partial final judgment of the Court of Chancery (Glasscock, V.C.), by Memorandum Opinion and Order dated June 24, 2016 (Ex. A), denying a request by The Williams Companies, Inc. ("Williams") to enjoin Energy Transfer Equity, L.P. ("ETE") from terminating their agreed-upon merger (the "Transaction") on the basis that ETE's tax counsel at Latham & Watkins LLP ("Latham") refused to deliver a routine opinion that was a condition to closing. The Court of Chancery's decision was the result of legal error that, if not corrected by this Court, would render "commercially reasonable efforts" and "reasonable best efforts" provisions in Delaware-law merger agreements meaningless and, more generally, would provide a blueprint for parties to escape their obligations under such agreements without consequence.

After aggressively pursuing the Transaction and signing the agreement and plan of merger (the "Merger Agreement") in September 2015, ETE developed severe buyer's remorse, due largely to the $6.05 billion cash payment upon which ETE had insisted in negotiations. By January 2016, ETE was searching for ways to avoid closing the Transaction and making that payment. As part of these efforts, ETE had Latham inform Williams' tax counsel at Cravath, Swaine & Moore LLP ("Cravath") on April 12, 2016 that Latham had conclusively determined that it was unable to provide an opinion, which was a condition to closing, that the

Transaction should qualify as tax-free under Section 721(a) of the federal tax code (the "721 Opinion"). This surprise disclosure followed weeks of secret discussions that ETE orchestrated among ETE, Latham and ETE's specially retained tax counsel at Morgan, Lewis & Bockius LLP ("Morgan Lewis")—but from which ETE *excluded* Williams and Cravath, and also largely excluded its own lead deal counsel at Wachtell, Lipton, Rosen & Katz ("Wachtell") after Wachtell expressed skepticism about Latham's position. ETE did not inform Williams that a purported issue with the 721 Opinion had even been *identified* until Latham presented its determination as final on April 12. ETE then announced Latham's position publicly—filing a disclosure within days—thereby boxing Latham in and ensuring it would not change its views. Williams' efforts to engage with ETE, including by proposing simple fixes on April 14 (before the public disclosure of Latham's position), were ignored for weeks, thanks to ETE's instruction to Latham not to respond to Williams until after Latham had finalized its rejection of the proposals. Consistent with its goal to get out of the deal, ETE made no meaningful effort to work with Williams to solve the purported tax problem and close the Transaction.

Williams sued to enjoin ETE from terminating the Transaction in breach of the Merger Agreement. Following a two-day trial, the Court of Chancery found substantial failures by ETE relating to the 721 Opinion, including that

> "[ETE] did not direct Latham to engage earlier or more fully with Williams' counsel, failed itself to negotiate the issue . . . directly with

> Williams, failed to coordinate a response among the various players, went public with the information that Latham had declined to issue the 721 Opinion, and generally did not act like an enthusiastic partner in pursuit of consummation of the . . . Transaction." (Op. 49-50.)

These findings should have led to the entry of judgment against ETE.

Instead, the Court of Chancery held that none of these failures constituted a breach of ETE's duty to use "commercially reasonable efforts" to obtain the 721 Opinion. In contrast to prior Delaware cases, such as *Hexion Specialty Chemicals, Inc. v. Huntsman Corp.*, 965 A.2d 715 (Del. Ch. 2008), which held that efforts provisions impose obligations on parties to try to achieve the contracted result, the trial court erroneously interpreted these obligations as imposing on ETE nothing more than a duty not to *prevent* Latham from giving the 721 Opinion.

Instead of focusing on ETE's conduct, the Court of Chancery focused on that of Latham, which is not a party to the Merger Agreement. Because the trial court found that Latham held its tax position "in good faith" (Op. 45), the trial court ruled that ETE did not breach the Merger Agreement (Op. 50). But the issue here is *ETE's* compliance with its efforts obligations, not Latham's good faith. The trial court's misinterpretation of ETE's efforts obligations, and its conflation of the breach and causation elements of contract law, were legally erroneous.

The Court of Chancery also erroneously rejected Williams' argument that ETE was equitably estopped from terminating the Transaction on the basis of the failure of the condition for delivery of the 721 Opinion. In the Merger Agreement, ETE represented and warranted to Williams that the facts in ETE's possession at signing were not reasonably expected to prevent the Transaction from qualifying under Section 721 (the "Tax Representation"). Williams relied on the Tax Representation in agreeing to ETE's proposed Transaction structure and to the 721 Opinion condition, comforted that ETE (advised by the very firm charged with delivering the 721 Opinion) saw no tax issue on then-existing or foreseeable facts. As a result, ETE was estopped from taking actions inconsistent with the Tax Representation—here, terminating the deal based on the failure of the 721 Opinion condition, where that failure was based on the *same facts* known to ETE at signing. The Court of Chancery's decision to permit ETE to terminate was legal error.

The Court of Chancery recognized that the timing of ETE's discovery of the purported tax issue "may arouse our suspicions." (Op. 4.) "[I]t is only *after* the economics of the deal changed significantly and [ETE] was manifestly interested in a low-cost exit from the Merger Agreement that Latham determined that it was unable to issue the 721 Opinion." (Op. 33.) Nevertheless, the Court of Chancery concluded that ETE just got lucky, reasoning that "even a desperate man can be an honest winner of the lottery." (Op. 4.) This view of the case ignores the fact that ETE did *nothing* to try to obtain the 721 Opinion. While ETE surely was desperate and (thus far) has won the lottery, its actions are inconsistent with an honest effort to comply with its contractual obligations and close the Transaction.

SUMMARY OF ARGUMENT

The Court of Chancery committed two sets of legal error requiring reversal:

1. The Court of Chancery erred in concluding that ETE's behavior complied with its obligations to use "commercially reasonable efforts" and "reasonable best efforts" to obtain the 721 Opinion (the "efforts obligations"). *First*, the trial court lowered the standard required by ETE's efforts obligations when it focused on whether ETE tried to *prevent* issuance of the 721 Opinion, and ignored ETE's failure to try affirmatively to *obtain* the 721 Opinion. *Second*, the trial court imported a causation requirement into its breach analysis. Had the trial court applied the correct legal standard, it would have concluded that its factual findings established a breach of ETE's efforts obligations, and then shifted the burden to ETE to prove that its breach did not materially contribute to the failure of the 721 Opinion condition. ETE could not carry that burden. (*See infra* Section I.)

2. The Court of Chancery erred in permitting ETE to terminate based on the failure of the 721 Opinion, notwithstanding ETE's Tax Representation that it did not "know[] of the existence of any fact that would reasonably be expected to prevent" qualification under Section 721. Having induced Williams to agree to sign the Merger Agreement in reliance on the Tax Representation, ETE was estopped from terminating on inconsistent grounds, *i.e.*, on the basis of facts known to ETE at the time it made the Tax Representation. (*See infra* Section II.)

STATEMENT OF FACTS

Williams sets forth below the facts relevant to this appeal, incorporating by reference the more detailed statement of facts in Williams' Proposed Findings of Fact filed with the Court of Chancery on June 23, 2016. (*See* A2994-3074.)

A. ETE Agreed in the Merger Agreement To Use Commercially Reasonable Efforts To Obtain the 721 Opinion and Reasonable Best Efforts To Close the Transaction.

On September 28, 2015, after "fervently" pursuing a transaction for months (Op. 54), ETE entered into the Merger Agreement, governed by Delaware law, by which ETE, a Delaware limited partnership, would acquire Williams, a Delaware corporation, in a two-step transaction (Op. 1, 4-5). In the first step, Williams would merge into Energy Transfer Corp LP ("ETC"), a newly created Delaware limited partnership taxable as a corporation. (Op. 1, 7.) Williams' stockholders would exchange their stock for approximately 81% of the total outstanding stock of ETC and $6.05 billion in cash. (Op. 8-9.) The remaining 19% of ETC's stock would be issued by ETC to ETE in exchange for the $6.05 billion, which would be paid immediately to Williams' stockholders. (Op. 8-9.) In the second step, ETC would contribute Williams' assets to ETE (the "Contribution") in exchange for Class E units in ETE (the "Parent Class E Issuance"). (Op. 8, 15.) The number of ETE Class E units and ETC shares would be identical, and the two were expected to have the same value. (Op. 10.) This Transaction structure was ETE's idea.

(*See* A54; A312; A2833-34/192:13-193:5 (Whitehurst).)

The parties intended the second step—the Contribution in exchange for the Parent Class E Issuance—to be tax-free under Section 721, which provides that "[n]o gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership." (Op. 15 (quoting 26 U.S.C. § 721(a)).) Section 6.01(h) of the Merger Agreement provides that Latham's issuance of the 721 Opinion is a condition to closing; and ETE—advised by Latham (*see* A2027/106:1-6 (Fenn); A2545/15:24-16:5 (Stein))—represented and warranted that it did not "know[] of the existence of any fact that would reasonably be expected to prevent . . . the Contribution and Parent Class E Issuance from qualifying" under Section 721 (A652 § 3.02(n)(i)). Williams agreed to ETE's proposed Transaction structure and to the 721 Opinion condition in reliance on the Tax Representation. (A2871/342:21-343:15, A2889/412:14-413:7 (Needham).)

In the Merger Agreement, ETE promised to "use its commercially reasonable efforts" both "to cause . . . the Contribution and the Parent Class E Issuance to qualify" under Section 721 and "to obtain the Tax opinion[] described in Section[] 6.01(h)". (A680 § 5.07.) ETE further promised that it would "not tak[e] or fail[] to take any action which action or failure to act [ETE] knows is reasonably likely to prevent" qualification under Section 721. (A680 § 5.07(a).)

Similarly, the Merger Agreement obligated ETE to "use reasonable best efforts" to consummate the Transaction in the most expeditious manner practicable, and to "assist and cooperate" with Williams in doing so. (A671 § 5.03(a).) These efforts specifically include "using reasonable best efforts to accomplish . . . the taking of all acts necessary to cause the conditions to [c]losing to be satisfied as promptly as practicable". (*Id.*)

B. ETE Developed Buyer's Remorse and Searched for Ways To Get Out of the Transaction.

Due to a severe decline in the energy sector following the execution of the Merger Agreement, the "Transaction quickly became financially unpalatable to [ETE]", and "[i]t became clear to the parties and to the interested public that [ETE] desired an exit from the Merger Agreement as strongly as it had desired to enter [into] the agreement in the first place." (Op. 2.)

> "In December 2015, [ETE Chairman Kelcy] Warren led discussions within [ETE] that highlighted the problems with the . . . Transaction. He suggested that [ETE] seek to renegotiate the terms of the Merger Agreement. Further, [ETE's] former CFO Jamie Welch testified that, by January 2016, Warren would have preferred terminating the Merger Agreement to restructuring." (Op. 11 (footnotes omitted).)

On January 7, 2016, Warren convened an "all-hands meeting" to discuss "whether or not ETE had to close the [T]ransaction". (A2814/114:2-8, 116:1-10 (Welch).) The meeting was attended by "the entire [ETE] leadership team", including Warren, Welch, General Counsel Tom Mason and Head of Tax Bradford

Whitehurst, as well as outside litigation counsel. (A2814-15/116:19-117:10 (Welch); A2834/195:11-196:4 (Whitehurst).) Whitehurst testified that he was well aware, as of January 2016, that for non-tax reasons ETE wanted to eliminate the $6.05 billion payment or get out of the deal altogether. (A2834-35/196:22-197:2.)

C. ETE Formulated a Problem with the 721 Opinion and Took Steps To Box Latham In.

As of late March, "Latham was preparing to issue the 721 Opinion and had never considered that it would be unable to issue it." (Op. 19.) Indeed, a draft memorandum from March 29 concluded that Latham was "of the opinion that the Contribution and the Parent Class E Issuance should qualify as an exchange to which section 721(a) of the Code applies." (A898; *see* A2856/281:8-15 (Fenn).)

Whitehurst had different plans. At around that time, Whitehurst testified, he had a purported "epiphany" concerning the structure of the Transaction, which led him to question whether the Contribution and Parent Class E Issuance would in fact qualify as tax-free under Section 721. (Op. 34.) Specifically, Whitehurst claims to have realized for the first time in late March 2016 that the number of ETC shares that were to be issued to ETE in exchange for the $6.05 billion in cash was fixed based on the price of publicly traded ETE units at the time of signing—rather than floating based on whatever the price might end up being at the time of closing. (Op. 17.) Because ETE's units (and, therefore, ETC's shares) had lost much of their value since signing, Whitehurst wondered whether the IRS might view a portion of the $6.05 billion not as payment for the shares, but as payment for the asset Contribution. (Op. 18.) Following this purported realization, Whitehurst instructed Latham to analyze, in light of Whitehurst's supposed "epiphany", whether "we have an issue" and whether Latham "can or cannot give an opinion". (A2819/134:2-12, A2820-21/140:18-141:8 (Whitehurst).)

The Court of Chancery was careful not to rule on whether Whitehurst was credible when he testified that he—ETE's Head of Tax—had misunderstood the structure of the Transaction until *six months* after signing. (Op. 34-35.) There are good reasons to disbelieve the testimony: "he had reviewed drafts of transaction documents and other deal-related materials that said otherwise" and "no one else shared his views". (Op. 17; *see also* A3007-08 ¶¶ 24-25; A3017-20 ¶¶ 47-56.)[1] At a minimum, "Whitehurst's epiphany, if such it was, was reached in a context where the deal no longer made economic sense to [ETE], and by which time [ETE] was clearly in search of a soft exit from the Merger Agreement." (Op. 34.)

Latham knew at this time that the economics of the deal were no longer attractive to ETE and that the $6.05 billion payment in particular—conveniently, the same aspect of the Transaction that, in Whitehurst's theory, risked jeopardizing

[1] Furthermore, the view Whitehurst claims to have held until March—that the number of ETC shares ETE would obtain would "float" based on ETE's unit price—is absurd, as ETE's other witnesses testified. (A2512-13/175:2-178:13 (Warren); A2866/321:19-322:6, A2696/38:20-41:8 (Preiss); *see also* A900.) ETE's other witnesses understood precisely how the Transaction worked. (A2811/103:15-104:6 (Welch); A2476/33:8-16 (Warren); A2689-90/12:14-14:14 (Preiss).)

the 721 Opinion—was "causing problems" for ETE. (A2036/145:14-20 (Fenn).) Thus, when potential fixes to the supposed Section 721 problem were raised at Latham, they were not pursued because Latham was aware that "[Whitehurst] would [not] be delighted with the suggestion". (A913.)

On April 7, Latham—with Whitehurst on the line (A2864/314:13-316:6 (Preiss))—spoke with Wachtell about the Section 721 issue. (Op. 19.) Latham shared its new concern that the post-signing decline in the value of ETE's (and, by extension, ETC's) equity jeopardized the tax-free status of the Transaction. Eiko Stange, a tax partner at Wachtell, "expressed skepticism" with this view—as he did again in a subsequent call, on April 11. (Op. 19 n.65; A2867/327:15-328:9 (Preiss); A907; A899; A915.)[2] Later the same day as Wachtell first communicated its skepticism regarding Latham's position (A2928/568:24-569:3 (McKee); A1033), Whitehurst reached out for backup to Bill McKee of Morgan Lewis—Whitehurst's former colleague and mentor (A2934-35/595:23-596:1 (McKee)). ETE made clear to McKee, however, that he was not to speak with Latham until after Latham had conclusively determined not to provide the 721 Opinion. (A2930/577:3-11, A2932/585:13-16 (McKee).) After Wachtell—ETE's lead deal

[2] After initially representing to Williams that Wachtell had been uninvolved with the Section 721 issue, ETE produced handwritten notes just 7 days before trial revealing Wachtell's very critical views of Latham's supposed concerns. ETE thereafter refused Williams' request for depositions of two Wachtell attorneys. After the Court of Chancery ordered that ETE make both witnesses available (A2451-57), ETE stated that Stange was traveling abroad and would be unavailable until after the trial. As a result, Williams was unable to examine Stange, and relied at trial on testimony from his partner Alison Preiss, who heard Stange express his views.

counsel and a firm with a well-regarded tax practice—expressed skepticism about Latham's position, ETE *never* asked Wachtell "to do any analysis" of Section 721. (A2865/318:16-19, 319:21-320:3 (Preiss).) Wachtell, like Latham, was also not permitted to talk to McKee. (A2800/59:18-60:1 (Van Ngo).)

Despite extensive testimony at trial about Latham's process in late March and early April of "spit-balling", "playing devil's advocate", "pressure testing" and "throwing out theories" concerning Section 721 (A2847/246:21-247:11 (Fenn); A2820/138:22-139:11 (Whitehurst); A2939/614:18-23 (McKee)), *neither Williams nor its advisors were permitted to participate in any of these discussions.* It was not until April 12 that Latham first reached out to Cravath concerning the Section 721 issue, informing the Cravath tax lawyers that Latham had already conclusively determined that it would not issue the 721 Opinion absent a full recovery in ETE's unit price. (*See* Op. 18, 20-21; A2857/285:6-14, A2862/305:20-23 (Fenn) ("[Latham] waited until we had reached our conclusion before we called Cravath."); A926 (Latham call script).) While Latham internally had identified potential fixes to the issue, it never once raised those with Williams or its advisors. (A2862/306:23-307:7 (Fenn).)

Cravath strongly disagreed with Latham's newfound, surprise concerns. Nevertheless, just two days later, on April 14, Cravath proposed two solutions—referred to as "Proposal A" and "Proposal B"—to address Latham's concerns by way of minor changes to the Transaction structure. (Op. 22.) This commenced a two-week period during which Latham searched frantically for support permitting it to reject the proposals. During this period, Latham tax partner Larry Stein emailed his partner Tim Fenn to note that he was "getting increasingly concerned at what McKee is saying to Cravath", as ETE was not allowing Latham to speak with McKee. (A928.) The internal emails suggest that Latham was trying to reach the result that ETE could walk away from the deal. Stein confessed that he "could see us getting pushed hard on Proposal B. We all agree it helps"; he suggested that "it might make sense to have one of the associates beat up the Court Holding line [of cases]", which relate to the efficacy, for tax purposes, of structural changes to a transaction. (*Id*.) Fenn responded: "On Court Holding, that is exactly what I told [the associate]. *Go find some rulings*/TAMs/etc. where the government pushed back on simply using some entity in a related chain to try to side step some result." (A927 (emphasis added).) Stein replied that this was "Great", continuing: "And someone on the team is continuing to *scour the earth* on the post-signing/pre-closing value fluctuation point?" (*Id*. (emphasis added).) At no point did Latham reach out to Williams or Cravath to discuss its concerns. Nor did ETE, Latham or anyone else on ETE's side ever suggest any alternative solutions, or make any effort of any kind to resolve the issue. (A2878/368:13-370:4 (Needham).)

In the meantime, ETE pushed as quickly as possible to make a public disclosure of Latham's position on the 721 Opinion. On April 18—less than a week after Latham had first disclosed its view to Cravath (Op. 21), four days after Cravath had responded with proposed fixes (Op. 22) and while Williams and its advisors were still awaiting a response on those fixes (A2878/368:13-370:4 (Needham))—ETE issued an amendment to the proxy, disclosing publicly that Latham had advised it that "if the closing of the merger were to occur as of the date of this proxy statement/prospectus it would not be able to deliver the 721 Opinion". (Op. 22.) With that disclosure, ETE further boxed Latham in, making it very difficult for Latham to change its mind about the tax consequences.[3] As Whitehurst himself conceded, this public disclosure of Latham's opinion "poison[ed] the well. Once that genie gets out of the bottle, you can't put it back in." (A2433/238:19-21 (Whitehurst).)

Only on April 26, after the amended proxy had been filed, did Whitehurst allow Latham and McKee to speak to each other for the first time (A1026; *see* A2940/617:1-6 (McKee); A2067-68/269:12-270:18 (Fenn))—albeit (again) with Whitehurst, who at times "dominat[ed]" the call (A937; A1025-32). On that call, McKee's partner, Will Nelson, expressed the view that "there is a good

[3] When asked on direct examination by ETE whether he would "ever fail to deliver a Section 721 opinion for a client because the client asked you not to", McKee could not say, but did state, "I can't imagine being in that box." (A2940/618:19-619:2.) At his deposition, McKee testified that, in his nearly 50 years of practice, he had never heard of a deal that failed to close due to the failure of a law firm to provide a tax opinion. (A2746/118:21-119:5.)

argument that" Williams' Proposal A "works" if the Merger Agreement requires ETE to accept an amendment to the structure of the deal. (A2938/609:5-610:19 (McKee); A1028.) McKee agreed. (A2939/613:16-614:12.) Rather than permit them to explore that line of inquiry, however, Whitehurst cut it off:

> "Whitehurst said that Energy Transfer's corporate counsel—Wachtell, [Vinson & Elkins LLP], and others—are pretty confident that this restructuring is not required under the merger agreement. So Morgan Lewis's gating issue of whether the change is required is where we stop. Because no change is required, the analysis ends there." (A1028.)

Joshua Brady, another of McKee's partners, noted that, "if a Delaware judge decided that there was no obligation to restructure, it's the end of the analysis. But he questioned what would happen if a judge said the opposite", and "asked whether it was likely that there would be any Delaware decision" before the "Outside Date" in the Merger Agreement of June 28 on whether ETE had to restructure to resolve the purported Section 721 issue. (A1029.) "Whitehurst replied that . . . the June 28 deadline for the deal closing makes it unlikely that the parties would get a judgment in time." (*Id*.)

McKee testified that he understood it to be a good thing from Whitehurst's perspective that the Court of Chancery was unlikely to rule in time. (A2938/611:19-23.) According to McKee, Morgan Lewis did not pursue any analysis of Williams' proposals because ETE instructed the firm not to do so:

> "Whitehurst expressed the view that he didn't have to make the

> change and that his corporate counsel had told him that he didn't have to make the change, so he didn't think he needed to spend what would be very substantial amounts of money to have his tax lawyers chase down this particular issue." (A2940/616:19-24.)

It was not until April 29 that ETE permitted Latham to speak to Cravath concerning Proposal A and Proposal B, which had been made 15 days earlier. (A2862/306:13-22 (Fenn).) This failure to engage was driven by ETE, which instructed Latham not to speak to Cravath until after (i) Latham had fully analyzed Williams' proposals and solidified its view rejecting them and (ii) ETE's deal counsel had sent Williams proposed proxy language (which happened on April 28) disclosing Latham's rejection of the proposals. (*See* A2066/262:21-265:4 (Fenn).)

ETE never engaged with Williams to try to find a solution to Latham's purported concerns; ETE never asked Latham to "find a way to fix this problem" or to propose alternative solutions (A2918-19/531:15-532:16 (Stein)); ETE never asked Morgan Lewis to do "all the work that would be necessary to be able to reach a conclusion whether it could give a should-level opinion on Proposal A or Proposal B" (*see* A2934/592:11-18 (McKee)); and ETE never asked Wachtell to "identify potential modifications to the Merger Agreement that would permit Latham to issue the 721 opinion" or to "analyze what would need to be done in order to implement either" of Williams' proposed solutions (A2865/320:4-19 (Preiss)). What ETE *did* do was prevent Latham from speaking with Williams or Cravath until Latham's position was finalized; immediately disclose Latham's decision to the public; restrict its advisors from speaking with one other; and shut down consideration of Williams' (as well as Latham's own) potential fixes.

D. As a Result of ETE's Conduct, Latham Adopted a Position on Section 721 That Makes No Sense.

The result of ETE's actions to isolate Latham was that Latham adopted a position on Section 721 that makes no sense, and with which even ETE's other advisors disagree. ETE deprived Williams and Cravath, or even ETE's other advisors, of the opportunity to talk Latham out of its mistaken position. While the Court of Chancery expressly declined to make any findings on the merits of the underlying tax issue (Op. 35), the peculiarity of Latham's position is an important reason why ETE cannot bear its burden to prove that its actions did not materially contribute to the failure of the 721 Opinion condition. (*See infra* Section I.C.3.)

As noted above, the parties intended the Contribution of Williams' assets to ETE for the Parent Class E Issuance to qualify as tax-free under Section 721. (Op. 15-16.) The question that Whitehurst raised in late March 2016 is whether—despite this intent—a portion of the $6.05 billion in cash, which ETE was paying for 19% of ETC's shares, would be reallocated to the Contribution. (Op. 18.)

As a general matter, the tax law permits parties to two or more exchanges to specifically identify which consideration is being exchanged for which asset so long as the exchanges (as they are here) are a product of arm's-length bargaining or are motivated by a non-tax business purpose. (A1934.) Here, however, Latham took the position that the form of the Transaction, involving two separate steps, might not be respected for tax purposes—even though it saw no such problem at signing, on the same deal structure. *First*, and most important to Latham, Latham now argued that some portion of the $6.05 billion in cash (which was designated for the ETC shares) might be reallocated to the Williams assets because the value of ETE units (and hence ETC shares) had declined since signing. (Op. 20-21; A2175/119:25-120:18 (Needham); A920-21; A980.) *Second*, Latham asserted that the likelihood of such a recharacterization was heightened by the presence of what it described as a "perfect hedge". Latham's perfect hedge argument is that, if there is a gap in the value of one leg of the transactions between ETE and ETC (*i.e.*, the exchange of $6.05 billion in cash for ETC shares), then (supposedly) there is necessarily an "equal and opposite . . . gap on the other leg" (*i.e.*, the exchange of ETE units for Williams' assets). (A2899-900/454:23-456:18 (Stein); *see also* Op. 20 & n.69; A3040-48 ¶¶ 118-136; A918-20; A980-83.) Neither of these arguments has any merit. (*See generally* A3014-48 ¶¶ 39-46, 57-61, 67-79, 88-90, 118-36.)

Latham confirmed at trial that it was the first purported concern—relating to the decline in ETE's publicly traded unit price—that prevented Latham from delivering the 721 Opinion, and that the "perfect hedge" alone would not have prevented it from doing so. (*See* A2859/295:23-296:2 (Fenn); A2914/514:11-515:11 (Stein).) However, Latham's view that the decline in ETE's unit price between signing and closing would change the tax treatment of the Transaction is flatly inconsistent with generally accepted tax principles. ETE's own lawyers at Wachtell expressed disagreement with Latham's analysis on this score, recognizing that the lower price "gives no reason to recast [the] transaction" (A2866/323:1-5, 16-19 (Preiss); A899-902) and that ETE's "lower value today [is] no reason to revisit [the] deal struck [between] 3rd parties" (A907; *see* A899). Similarly, McKee testified that Latham's position that it "would be unable to deliver the should-level Section 721 opinion at today's prices, but [it] would be able to do so if ETE's unit price were to recover, by the time of closing, to the price that it had [been] at the time of signing" did not "make any sense" to him. (A2935/597:6-15.) Even ETE's litigation experts disagree with Latham's view that an otherwise tax-free exchange can lose that status due to a post-signing decline in value. (*See* A1870; A1911; A2275/66:21-67:2 (Yale).)[4]

As for Latham's so-called "perfect hedge" theory, it is a tautology that,

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[4] While ETE's litigation experts each opined that there was a substantial risk that the Transaction would be recharacterized—albeit for reasons different from Latham's—they reached their opinions based on erroneous factual assumptions given to them by ETE. Whitehurst told both tax experts there was "no non-tax motive" for the hook stock (the shares that ETE would receive in ETC). (A2230/27:8-10 (Shashy); A2264/23:20-24, A2265/27:25-28:9, A2276/72:20-21 (Yale).) But the Court of Chancery expressly found to the contrary, concluding that both Williams and ETE had "another reason": that the hook stock "aligned interests between [ETE] and ETC". (Op. 36-37; *see also* A2787/7:24-8:7 (MacInnis); A2797/47:1-13 (Van Ngo); A2812/106:24-107:13 (Welch); A2114/92:16-20 (McReynolds).) ETE's experts both testified that they may well have reached different conclusions had they been aware of facts that led them to conclude that there was a non-tax business purpose for the cash-for-stock transaction. (A2244/82:23-83:8 (Shashy); A2926/562:18-563:4 (Yale).) Thus, the opinions of ETE's experts do not correspond to the facts of this case, and no weight can be placed on them.

again, neither Wachtell nor McKee understands. (A2709/92:12-18 (Preiss) ("I never really got it."); A2937-38/605:14-608:11 (McKee) ("[W]e didn't, and I still don't, understand the argument"; after reviewing materials from Latham, he has "stopped trying to understand the perfect hedge").) Professor Howard Abrams, Williams' expert, testified at trial that no reasonable tax attorney would propound the theory. (A2898/449:5-11.) That is because Latham's "perfect hedge" argument assumes the conclusion it purports to demonstrate—namely, that the two sides of the transaction must necessarily balance—and backs into an implied value of the Williams assets on the basis of that assumption. (*See* A3040-48 ¶¶ 118-136.) The absurdity of Latham's position is clear from the conclusion it drew in its memorandum on the subject from May 9: "There is, therefore, *no real economic risk being worn by [ETE] or [ETC]* when the [cash-for-ETC-stock t]ransaction and the Contribution and Parent Class E Issuance are viewed together." (A983 (emphasis added).) That is manifestly false. Because the $6.05 billion cash component was fixed, in exchange for ETC shares, ETE was exposed to changes in the value of its own equity between signing and closing. As ETE's publicly traded unit price declined, the value of the ETC shares (which were designed to be equivalent to ETE units) that ETE would receive for the $6.05 billion in cash also declined, and ETE was economically worse off.[5] (*See* A730-31; A872; A819;

[5] The economic risk went both ways. If ETE's unit price had increased, the value of the

A2111-12/81:19-85:18 (McReynolds); A2517/195:4-21 (Warren); A2893/430:17-22 (Abrams); A2874/354:1-355:4 (Needham).) It is astounding that Latham took the position that ETE could terminate a $30-plus billion transaction without legal consequence based on the fiction that ETE bore "no real economic risk". Of course ETE bore risk. The fact that the bet turned out to be a bad one for ETE is why ETE sought to get out of the deal.

Simply put, Latham held an unreasonable position that *no one else* shared. There was not, as the Court of Chancery suggested, some "range of opinion" into which Latham neatly fit (Op. 41); Latham was the outlier. On this record, ETE's actions to prevent Latham from talking to the other tax practitioners involved in the deal were a material contributing cause to the failure of the 721 Opinion condition.

E. ETE Terminated the Transaction.

On June 24, the Court of Chancery issued its Opinion and Order finding that ETE had not breached its efforts obligations and denying Williams' request for an injunction to prevent ETE from terminating the Transaction. The next business day, on June 27, Williams' stockholders voted overwhelmingly to approve the Transaction—with more than 80 percent of the votes cast in favor. On June 28, Latham confirmed that it would not deliver the 721 Opinion. ETE terminated the following day.

ETC shares would have exceeded $6.05 billion, and ETE would have been better off.

ARGUMENT

I. THE COURT OF CHANCERY APPLIED THE WRONG LEGAL STANDARD IN RULING THAT ETE WAS NOT IN BREACH OF ITS EFFORTS OBLIGATIONS WITH REGARD TO THE 721 OPINION.

A. Question Presented

Did the Court of Chancery err in ruling that ETE did not breach its efforts obligations when the trial court (i) interpreted "commercially reasonable efforts" and "reasonable best efforts" as requiring nothing more than merely "allow[ing]" the closing condition to be satisfied and (ii) conflated the breach and causation inquiries while placing the burden on causation on the non-breaching party? (A2626-56; A2759-67; A2965-75; A2984-88.)

B. Standard of Review

This Court reviews the Court of Chancery's legal conclusions *de novo*. *In re Peierls Charitable Lead Unitrust*, 77 A.3d 232, 235 (Del. 2013).

C. Merits of Argument

The Court of Chancery got off on the wrong foot by devoting most of the analysis in its Opinion to the ancillary question of whether Latham acted in good faith, rather than the determinative issue in the case, which is whether ETE complied with its contractual obligations.[6] Indeed, the Opinion devotes 14 pages

[6] While the Opinion suggests that Williams' arguments led the Court of Chancery to focus on the question of Latham's good faith (*see* Op. 31), Williams acknowledged below that "Latham may believe in good faith . . . that it cannot deliver the 721 Opinion" but argued that "the key question in this litigation . . . is whether *ETE* lived up to its obligations to try to obtain the 721 Opinion". (A2952 (emphasis in original).)

to Latham's good faith (Op. 31-45) before turning to a much briefer discussion of only 6 pages about ETE's compliance with its efforts obligations (Op. 45-51).

When it did turn to ETE's conduct, the Court of Chancery improperly decided that ETE did not breach its efforts obligations because the trial court interpreted "commercially reasonable efforts" and "reasonable best efforts" as imposing only a negative duty not to obstruct performance of the contract, rather than also an affirmative duty to help ensure performance (*see infra* Section I.C.1); and, relatedly, because the trial court elided the breach and causation inquiries, reasoning that there could not have been a breach because (having placed the burden of persuasion on the wrong party) there was no causation (*see infra* Section I.C.2). Following Delaware law, the Court of Chancery should have (i) recognized that ETE's numerous acts and omissions failed to comply with its affirmative obligations to try to obtain the 721 Opinion, and then (ii) shifted the burden to ETE to prove that those acts and omissions did not materially contribute to the failure of the closing condition. Had the Court of Chancery conducted a proper analysis, ETE would have been unable to meet its burden, and Williams would have prevailed. (*See infra* Section I.C.3.)

1. <u>The Court of Chancery Erred By Looking Only at Whether ETE Tried To Prevent Delivery of the 721 Opinion, and Ignoring Whether ETE Made Efforts To Obtain the 721 Opinion.</u>

The Court of Chancery applied the wrong legal standard to ETE's conduct.

The trial court should have followed the *Hexion* case and asked whether ETE's acts and omissions complied with its obligations to make commercially reasonable efforts to obtain the 721 Opinion and reasonable best efforts to consummate the Transaction. *See Hexion*, 965 A.2d at 755. It did not do this. Instead of asking what steps ETE took to try to *obtain* the 721 Opinion, the trial court focused exclusively on whether ETE tried to "*torpedo*[]" it. (Op. 51 (emphasis added).)

The trial court's analysis is inconsistent with the Merger Agreement, which imposes on ETE clear affirmative obligations (to obtain the 721 Opinion), not just negative obligations (not to obstruct the 721 Opinion). ETE had to "use its commercially reasonable efforts to *obtain*" the 721 Opinion (A680 § 5.07(b) (emphasis added)); and ETE had to use "reasonable best efforts to . . . *take*, or *cause to be taken*, all actions, and to *do*, or *cause to be done*, and to *assist* and *cooperate* with the other parties in doing, all things necessary, proper or advisable to consummate and make effective" the Transaction, including by "*taking* . . . all acts necessary to cause the conditions to [c]losing to be satisfied" (A671-72 § 5.03(a) (emphases added)).[7] In response to Williams' proposed modifications,

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[7] The conduct demanded by a promise to undertake either "commercially reasonable efforts" or "reasonable best efforts" is essentially the same. *See WaveDivision Holdings, LLC v. Millennium Digital Media Sys., L.L.C.*, 2010 WL 3706624, at *18 (Del. Ch. Sept. 17, 2010) (Strine, V.C.) (using "commercially reasonable efforts" and "reasonable best efforts" interchangeably); *Hexion*, 965 A.2d at 749 (interpreting "reasonable best efforts" clause to mean "commercially reasonable"); *see also* Kenneth A. Adams, *A Manual of Style for Contract Drafting* 163 (3d ed. 2013) ("U.S. courts have overwhelmingly rejected . . . the notion that *best efforts* represents a more onerous standard than *reasonable efforts*."); *id.* at 162 ("Other *efforts*

ETE also had to "*cooperate*" and "use its commercially reasonable efforts to *cause*" the Transaction to qualify under Section 721, "including by not taking or failing to take any action which action or failure to act [ETE] knows is reasonably likely to prevent such qualification". (A680 § 5.07(a) (emphases added).)

Thus, the Court of Chancery's decision in favor of ETE on the grounds that ETE did not "obstruct" Latham from issuing the 721 Opinion (Op. 49) misconstrues the efforts provisions in the Merger Agreement, which unambiguously require ETE to engage in affirmative acts "to obtain" the 721 Opinion (A680 § 5.07(b); *see also* A671-72 § 5.03(a)).

Delaware law is clear that provisions like these require the promisor affirmatively to take acts that are "both commercially reasonable and advisable to enhance the likelihood" of achieving the desired result (here, delivery of the 721 Opinion). *Hexion*, 965 A.2d at 749. *Hexion* holds that a buyer's failure to approach its counterparty and discuss a problem "alone would be sufficient to find" a breach of an efforts provision. *Id.* at 750. As set out in *Bloor v. Falstaff Brewing Corp.*, 601 F.2d 609, 614 (2d Cir. 1979) (Friendly, J.), a case discussed with approval in *Hexion*, efforts provisions demand more than just good faith.[8]

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standards . . . are concoctions that add nothing to *reasonable efforts* other than confusion."); *Monex Fin. Servs. Ltd. v. Nova Info. Sys., Inc.*, 657 F. Supp. 2d 447, 454 (S.D.N.Y. 2009) ("New York courts use the term 'reasonable efforts' interchangeably with 'best efforts.'").

[8] *See also* 2 E. Allan Farnsworth, *Farnsworth on Contracts* § 7.17c, at 405 (3d ed. 2004) ("Good faith is a standard that has honesty and fairness at its core and that is imposed on every

Reasonable efforts require the promisor, among other things, affirmatively:

- To place completion of the contract ahead of its own independent economic interests, *Hexion*, 965 A.2d at 755 ("Hexion simply did not care whether its course of action was in Huntsman's best interests so long as that course of action was best for Hexion."); *Bloor*, 601 F.2d at 614 ("It was sufficient to show that [the defendant] simply didn't care about [the licensed products' sales] volume and was content to allow this to plummet so long as that course was best for [the defendant's] overall profit picture . . . .");

- To communicate and cooperate with its counterparty when issues and obstacles arise, *Hexion*, 965 A.2d at 750 ("Hexion did nothing to approach Huntsman management, either to discuss ways the solvency problems might be addressed, or even to put Huntsman on notice of its concerns. This choice alone would be sufficient to find that Hexion had knowingly and intentionally breached its covenants under the merger agreement."); and

- To disclose relevant information to its counterparty and work together cooperatively, *WaveDivision*, 2010 WL 3706624, at *18 ("Despite [the plaintiff's] repeated offers to assist [the defendant] with gathering the necessary consents, [the defendant] never told [the plaintiff] about its involvement in stimulating an alternative refinancing deal . . . . This clandestine approach employed by [the defendant] . . . guts its claim to have been actively pursuing consents in good faith.").

In considering ETE's conduct, the Court of Chancery ignored ETE's affirmative duties, focusing exclusively on ETE's separate, negative obligation not to obstruct Latham's delivery of the 721 Opinion. That is, instead of enforcing ETE's promise to work diligently to try to obtain the 721 Opinion, the Court of Chancery held that ETE had only to engage in "reasonable behavior designed to

party to a contract. Best efforts is a standard that has diligence as its essence and is imposed on those contracting parties that have undertaken such performance. The two standards are distinct and that of best efforts is the more exacting . . . .").

allow Latham to give the 721 Opinion". (Op. 46 (emphasis added).) This ignores the affirmative acts required by reasonable efforts under the plain language of the Merger Agreement, as well as *Hexion* and other case law.

Based on this incorrect legal standard, the Court of Chancery concluded:

> "Williams has not pointed to other facts which [ETE] *withheld from or misrepresented to Latham* that have caused it to withhold the 721 Opinion. There is simply nothing that indicates to me that [ETE] has *manipulated the knowledge or ability of Latham* to render the 721 Opinion, or *failed to fully inform Latham*, or do anything else, whether or not commercially reasonable, *to obstruct Latham's issuance* of the condition-precedent 721 Opinion, or that had a material effect on Latham's decision. *Therefore, I have no basis to find that [ETE] is in material breach of the commercially reasonable efforts requirement* . . . ." (Op. 48-49 (emphases added).)

Tellingly, the trial court placed importance on the fact that "Williams does not point to any direct evidence [that ETE] *instructed Latham, directly or indirectly, to fail to satisfy the condition precedent*." (Op. 49 (emphasis added).)

But the factual findings in the Opinion are sufficient to conclude that ETE failed to comply with its efforts obligations, if those provisions are given their proper legal meaning. The Court of Chancery found the following to be "True":

> "the fact that [ETE] did not direct Latham to engage earlier or more fully with Williams' counsel, failed itself to negotiate the issue . . . directly with Williams, failed to coordinate a response among the various players, went public with the information that Latham had declined to issue the 721 Opinion, and generally did not act like an enthusiastic partner in pursuit of consummation of the . . . Transaction." (Op. 49-50.)

Yet the trial court disregarded these clear breaches of ETE's affirmative duties on the ground that ETE could breach its efforts obligations only by taking steps to *prevent* issuance of the 721 Opinion. In other words, in deciding whether ETE used reasonable efforts to obtain the 721 Opinion, the trial court overlooked its own factual findings that ETE did nothing at all. That was legal error.

ETE's secrecy, its refusal to permit Latham to engage with Cravath, its decision to box Latham in by quickly publishing Latham's views, its refusal to explore potential solutions to Latham's concerns, its failure to explore Williams' proposed fixes or to ask its tax advisors to try to come up with their own and, generally, its decision to place its own economic interest in terminating the Transaction ahead of its contractual commitments all plainly breached ETE's efforts obligations. *See WaveDivision*, 2010 WL 3706624, at *18 (a party's "clandestine approach" breached commercially reasonable efforts obligation); *Hexion*, 965 A.2d at 750 (a promisor's failure to communicate with its counterparty regarding concerns breached reasonable best efforts obligations); *Bloor*, 601 F.2d at 614 (putting the promisor's economic interests ahead of its contractual promise constituted breach of best efforts obligations).[9]

Notably, this fundamental error—interpreting the Merger Agreement's

[9] A useful way of thinking about efforts obligations is that they require the buyer "to consider the best interests of the seller and itself as if they were one firm." *Tigg Corp. v. Dow Corning Corp.*, 962 F.2d 1119, 1125 (3d Cir. 1992) (Alito, J.); *see also* 2 Farnsworth, *Contracts* § 7.17c, at 407 (courts "imagine the promisor and the promisee to be united in a single entity and . . . ask what efforts such an entity would exert on its own behalf"). Needless to say, ETE did not act as if it and Williams were one firm, and did not even begin to make the efforts that Williams would have made—and did make—to obtain the 721 Opinion.

efforts clauses as imposing only a negative duty not to *preclude* satisfaction of the closing condition—infected the Court of Chancery's consideration of the closely analogous precedent of *Hexion*. In that case, Hexion promised to use "reasonable best efforts" to obtain financing for its proposed acquisition of Huntsman. *Hexion*, 965 A.2d at 724. Instead, having decided that it no longer wanted to close, Hexion secretly raised insolvency concerns with and obtained an insolvency opinion from a third-party valuation expert, thereby rendering financing for the deal essentially impossible. *Id*. at 726-27, 730. Throughout, Hexion failed to communicate with Huntsman regarding its insolvency concerns and failed to search for solutions that might avoid insolvency. *Id*. at 750, 754-56.

The Court of Chancery rejected the clear parallels with *Hexion*, reasoning:

> "Unlike the record in this case, in *Hexion* the buyer actively and affirmatively torpedoed its ability to finance. If the record here reflected affirmative acts by [ETE] to coerce or mislead Latham, by which actions it prevented issuance of the 721 Opinion, the facts here would more resemble *Hexion*, and the outcome here would likely be different." (Op. 51.)

But the trial court misread *Hexion* and ignored the weight that the *Hexion* court put on the facts—equally present here—that the buyer made no effort to try affirmatively to achieve the relevant result, for example communicating with its counterparty concerning its insolvency concerns or exploring potential solutions to those concerns. *Hexion* holds that the buyer's failure to approach its counterparty and discuss the problem "alone would be sufficient to find" a breach of the efforts provision. 965 A.2d at 750. The further actions that the buyer took in that case to "scuttle the financing"—the kind of actions that the Court of Chancery here held were necessary for breach—only "compound[ed] its breach further". *Id.* at 751-52. Had the Court of Chancery properly understood the nature of ETE's obligations, it would have had no trouble finding a breach, consistent with *Hexion*.

The Court of Chancery's error, if not corrected, will have far-ranging and unfortunate consequences. Absent reversal, the Opinion will render efforts clauses in Delaware merger agreements next to meaningless by signaling to any merger party with buyer's remorse that, so long as it avoids actively "torpedo[ing]" the deal, it may safely avoid taking steps to help ensure contract performance. Press coverage of the decision has noted, correctly, that "[t]he decision is a big one in M&A circles. Few mergers give cold-footed buyers the ability to walk away cleanly. But many hinge on receiving law firm opinions on everything from taxes to regulatory matters. Those may become de facto escape hatches for regretful acquirers, deal lawyers said."[10]

Post-signing impediments to closing arise frequently in complex merger

[10] Liz Hoffman & Alison Sider, *Energy Transfer Can Escape Williams Takeover, Judge Rules*, The Wall Street Journal (June 24, 2016), *available at* http://www.wsj.com/articles/energy-transfer-can-escape-williams-takeover-judge-rules-1466801256; *see also* Keith Goldberg, *ETE-Williams Merger Flop A Blueprint For Energy Deal Exits*, Law360 (July 1, 2016) ("ETE's success in pulling out provides a road map for other energy companies faced with closing a merger that makes less financial sense than when the deal was first struck."), *available at* https://www.law360.com/tax/articles/812663/ete-williams-merger-flop-a-blueprint-for-energy-deal-exits.

deals, and parties often must cooperate and take proactive steps to ensure that such obstacles do not derail the transaction. As Williams' deal lawyer testified:

> "Parties that enter merger agreements are committed to closing the deal. And parties that are committed to closing deals behave in a certain way. They take certain actions. If there is an issue, they pick up the phone and they promptly call the counterparty, start working on a solution. They cooperate. They engage. They engage early. They engage regularly. They engage in real-time. And they throw all their resources at trying to fix anticipated problems." (A2800/60:9-18 (Van Ngo).)

The Opinion, however, eliminates any obligation to take such affirmative steps to ensure closing. This permits merger parties—through their own inaction—to seize upon any supposed difficulties to scuttle a deal that has not worked out in their favor, rather than use reasonable efforts to overcome such difficulties.[11]

The Opinion will also further increase negotiation and drafting costs to merger parties. By eliminating broad affirmative duties from efforts obligations, the Opinion puts added pressure on closing conditions and forces merger parties to undertake the inefficient (and likely futile) exercise of trying to catalog the specific acts and omissions each party is charged with taking and avoiding under each of the many unpredictable contingencies that may arise prior to closing. This will make negotiating a Delaware merger agreement a more costly and less certain

[11] *Cf.* Seth E. Zuckerman, *The Need for Carefully Tailored M&A Strategies in an Economic Downturn, in* Aspatore, *Mergers and Acquisitions Law 2010: Top Lawyers on Trends and Key Strategies for the Upcoming Year*, 2010 WL 543732, at *1 (Feb. 2010) (noting that, to the extent *Hexion* "requires ongoing communications between the parties to avoid a breach of the agreement . . . , the purchaser and seller have encouragement to work together to resolve issues and ultimately consummate the transaction, as opposed to subsequently litigating its collapse").

enterprise. But the Court of Chancery's unwillingness to give meaning to and enforce broad, express affirmative duties has that unfortunate result.

2. The Court of Chancery Erred by Improperly Conflating Causation and Breach and by Wrongly Placing the Burden of Proof of Causation on Williams.

The Court of Chancery further erred by placing the burden of proof of causation on Williams and by making its causation analysis dispositive of the separate issue of whether ETE's conduct breached its efforts obligations. Specifically, having found that Latham acted in good faith, the Court of Chancery erroneously treated this finding as conclusive on the unrelated question of breach by ETE. Instead, the trial court should have analyzed (under the proper standard (*see supra* Section I.C.1)) whether ETE breached and, then, whether ETE proved that such breach did not materially contribute to Latham's conclusion that it could not provide the 721 Opinion.

Where, as here, a plaintiff alleges that a contract condition has failed due to a defendant's breach of an efforts obligation, the first inquiry is whether the defendant's behavior fell below the standard of conduct agreed upon by the parties. *See WaveDivision*, 2010 WL 3706624, at *15. In this analysis, the plaintiff is *not* required to show what (if any) alternative course of conduct was available to the defendant that might have led to satisfaction of the condition. *See Bloor*, 601 F.2d at 614 (where a licensee had promised to use best efforts to maintain a high volume of sales for licensed products, the "[p]laintiff was not obliged to show just what steps [the defendant] could reasonably have taken to maintain a high volume for [the] products"). Instead, the court asks simply whether the defendant's conduct complied with its contractual duty. *See id*. (to establish a breach, "[i]t was sufficient to show that [the defendant] simply didn't care about [the licensed products' sales] volume and was content to allow this to plummet so long as that course was best for [the defendant's] overall profit picture").

"[O]nce it has been determined that [the defendant] breached the [a]greement[], the burden of showing that that breach did not materially contribute to the [failure of the contracted result] is properly placed on [the defendant]." *WaveDivision*, 2010 WL 3706624, at *15. "[I]t is not necessary that the [desired result] would have [occurred] 'but for' [the defendant's] conduct, but only that [the defendant's] actions contributed materially to the [failure]." *Id.* at *14.[12]

Again, *Hexion* is instructive. In addressing Huntsman's argument that Hexion breached its efforts obligations, the trial court concluded as follows:

> "Huntsman was not obligated to show that Hexion had viable options to avoid insolvency while performing its obligation to close, *it merely needed to show (which it succeeded in doing) that Hexion simply did*

[12] *See also* Restatement (Second) of Contracts § 245 cmt. b (1981) ("Although it is implicit in the rule that the condition has not occurred, it is not necessary to show that it would have occurred but for the [defendant's] lack of cooperation. It is only required that the breach have contributed materially to the non-occurrence. . . . The burden of showing this is properly thrown on the party in breach."); *Shear v. Nat'l Rifle Ass'n*, 606 F.2d 1251, 1257 (D.C. Cir. 1979) (explaining that burden-shifting is required because almost all such cases "will involve speculation as to what would have happened had the defendant's conduct not taken place").

> *not care whether its course of action was in Huntsman's best interests* so long as that course of action was best for Hexion. *At that point the burden shifted* to Hexion to show that there were no viable options it could exercise to allow it to perform without disastrous financial consequences." *Hexion*, 965 A.2d at 755 (emphases added).

In other words, the trial court asked first whether Huntsman had shown that Hexion's behavior fell below the objective "reasonable best efforts" standard. This was achieved by, among other things, Huntsman's showing that Hexion put its own interests ahead of its contractual duties to Huntsman. The burden then shifted to Hexion to demonstrate that there was no action it could have taken to avoid insolvency, and that its breach, therefore, did not materially contribute to the failure of the deal's financing.[13]

In the present case, the Court of Chancery committed legal error by turning this inquiry on its head. The trial court *began* its inquiry by concluding that "*Williams can point to no commercially reasonable efforts that [ETE] could have taken* to consummate the . . . Transaction; specifically, in this context, actions available to [ETE] that would have caused Latham, acting in good faith, to issue the 721 Opinion." (Op. 46-47 (emphasis added).) This is directly contrary to the holdings of *Hexion* and *Bloor*—that the beneficiary of a reasonable efforts

[13] Judge Friendly's landmark decision in *Bloor*, on which *Hexion* relies, is similar. There, the court held that, once the plaintiff had established a breach of the best efforts obligation, the "[p]laintiff was not obliged to show just what steps [the defendant] could reasonably have taken" to accomplish the desired result (there, to maintain a high volume of beer sales). *Bloor*, 601 F.2d at 614. Rather, "[t]he burden then shifted to [the defendant] to prove there was nothing significant it could have done". *Id.* at 614-15.

obligation is *not* required "to show just what steps [its counterparty] could have taken" to achieve a different result. *Bloor*, 601 F.2d at 614; *see also Hexion*, 965 A.2d at 755. In other words, the Court of Chancery improperly placed the burden on *Williams* to show that ETE's acts and omissions caused the failure of the closing condition, rather than on *ETE* to show that its acts and omissions did not materially contribute to that result. *See WaveDivision*, 2010 WL 3706624, at *15; *Hexion*, 965 A.2d at 755; *Bloor*, 601 F.2d at 614-15; Restatement (Second) of Contracts § 245 cmt. b; 2 Farnsworth, *Contracts* § 8.6, at 458-59.

After deciding that Williams had not carried the burden of proving causation, the trial court concluded—*on that basis*—that ETE's conduct must not have breached its efforts obligations. The Opinion noted a litany of acts and omissions by ETE that are clearly inconsistent with commercially reasonable and reasonable best efforts (Op. 49-50); but it nevertheless held that those acts and omissions did not breach the Merger Agreement because Williams had not "demonstrat[ed] that [ETE's] activity or lack thereof *caused, or had a material effect upon*, Latham's current inability to issue the 721 Opinion" (Op. 50 (emphasis added).)

Thus, the Court of Chancery's analysis improperly collapsed the separate questions of breach and causation into a single determination. It was legal error for the subsequent issue of causation to control the precedent issue of breach—an error particularly prejudicial to Williams because the burden of proof on causation should have been shifted to ETE.

3. Application of the Correct Legal Principles Leads to a Different Result.

The Court of Chancery erroneously viewed its finding of Latham's supposed good faith as conclusive of both the breach and the causation analysis. Had the trial court applied the appropriate legal standards, it would have ruled that ETE's conduct breached the efforts provisions of the Merger Agreement, and it would then have shifted the burden to ETE to demonstrate that such breach did *not* materially contribute to Latham's decision not to render the 721 Opinion. This is a burden that ETE did not meet on the record at trial. We simply do not know how Latham ultimately would have resolved the issues if, contrary to fact, ETE had engaged meaningfully with Williams and otherwise complied with its efforts obligations. Indeed, although ETE maintains that Latham's failure to render the 721 Opinion was inevitable, *none* of ETE's tax practitioners or experts was able to name *any* other instance where, absent a change in tax law, a merger transaction has been terminated due to the failure of a tax opinion. (A2081/323:12-20 (Fenn); A2746/118:21-119:5 (McKee); A2288/119:9-15 (Yale).)

Because ETE breached its efforts obligations and failed to show that such breach did not materially contribute to the failure of the 721 Opinion condition, ETE was not entitled to terminate based on the failure of that condition. *See, e.g.*, *WaveDivision*, 2010 WL 3706624, at *14 n.11 ("[A] contractual condition precedent is deemed excused when a promisor hinders or precludes fulfillment of a condition and that hindrance or preclusion *contributes materially* to the nonoccurrence of the condition." (internal quotation marks omitted)).

Although the Opinion states, in a footnote, that the Court of Chancery would have arrived at the same result "no matter how I allocate the burden of proof" on causation (Op. 47 n.130), that view was driven by the Court of Chancery's misunderstanding of ETE's contractual duties and the causation standard. The trial court understood *WaveDivision*, 2010 WL 3706624, at *14-15, to stand for the proposition that "once a plaintiff has demonstrated a breach *leading to adverse consequences*, it is an affirmative defense that the consequences were otherwise unavoidable." (Op. 47 n.130 (emphasis added).) That is wrong. *WaveDivision* has nothing to do with an affirmative defense that the consequences were unavoidable. Rather, *WaveDivision* applies the "established principle of contract law that '[w]here a party's breach by nonperformance contributes materially to the non-occurrence of a condition of one of his duties, the non-occurrence is excused.'" 2010 WL 3706624, at *14 (quoting Restatement (Second) of Contracts § 245); *see also Hexion*, 965 A.2d at 755; *Bloor*, 601 F.2d at 614-15. The Court of Chancery erred by holding that the only way Williams could prove a breach was by also proving that such breach caused Latham's failure to deliver the

721 Opinion (what the trial court called "a breach leading to adverse consequences"). That is not the law.

The trial court's statement that "the record is barren of any indication" that any "action or inaction" by ETE "contributed materially to Latham's inability to issue the 721 Opinion" (Op. 47 n.130) is belied by the trial court's own lengthy list just two pages later of ETE's meaningful misconduct (Op. 49-50)—the impact of which ETE could not possibly disprove. As explained (*see supra* Section I.C.1), the trial court's analysis was focused entirely (and erroneously) on the question of whether ETE took steps to *prevent* Latham from issuing the 721 Opinion. The appropriate inquiry was whether ETE could prove that its secrecy, its failure to engage with Williams or its advisors, its decision to immediately publicize Latham's view, and so forth, did *not*, individually or in the aggregate, materially contribute to the failure of the condition. ETE did not carry that burden at trial.

As explained above (*see supra* pages 17-21), Latham's failure to provide the 721 Opinion was grounded in its view that, although the Transaction at signing qualified as tax-free and merited the 721 Opinion, the post-signing decrease in the price of ETE's units changed the tax analysis such that Latham no longer could opine that the Transaction should qualify under Section 721. Latham was alone in that view, as none of the tax experts and practitioners who testified in the litigation agreed with that analysis. Moreover, the Merger Agreement did not require that

Latham issue a "will" opinion—*i.e.*, one that would require near certainty that the Transaction would qualify under Section 721. It required only a "should" opinion, which can be rendered while still believing there is a significant level of risk. (A2872/344:18-24 (Needham); A2838/211:16-19 (Fenn).)

Unsurprisingly, ETE took steps to insulate Latham from dissenting voices, thereby ensuring that Latham would not muster even a "should" level of confidence. It refused to allow Latham to speak with McKee—who testified that Latham's price-change rationale made no sense to him (A2935/597:6-15) and that he "didn't, and I still don't, understand the [perfect hedge] argument" (A2937/607:11-14)—until after Latham's view had been finalized and publicly disclosed (A2920/538:6-11 (Stein); A929 (Stein email to Fenn concerning "reach[ing] out to [Whitehurst] about allowing us to talk to McKee")). Similarly, Latham did not engage with Cravath until after Latham's position had been finalized (A2857/285:6-14, A2862/305:20-23 (Fenn); A926 (Latham script for the April 12 call with Cravath, stating that Latham had already "concluded as a firm" that it would not deliver the 721 Opinion)); and ETE instructed Latham not to respond to Cravath concerning Proposals A and B until after Latham's position had been publicly disclosed and Latham had formed a conclusive position against those proposals (*see* A2066/262:21-265:4 (Fenn)). And, after Wachtell expressed skepticism of Latham's position, Wachtell was "never asked to do any analysis".

(A2865/318:16-19, 319:21-320:3 (Preiss).)

The Court of Chancery should have required ETE to bear the burden of demonstrating that these efforts by ETE to sideline dissenting voices did *not*, either individually or in the aggregate, materially contribute to Latham's adoption of a rationale with which no one else agreed, to Latham's rejection of Proposals A and B, and to the resulting failure of the 721 Opinion condition. ETE did not meet that burden. In light of Wachtell's immediate skepticism and McKee's emphatic rejection, they may well have been able to talk Latham out of its idiosyncratic (and objectively unreasonable) view that the decline in ETE's unit price meant that Latham could not deliver even a "should"-level opinion.

Similarly, ETE should have borne the burden of proving that its decision to publicize Latham's position immediately after communicating it to Cravath did not materially contribute to Latham's subsequent refusal to reconsider or to engage with Williams' Proposals A and B. Whitehurst himself testified that he believed this public disclosure "poison[ed] the well" and that, "[o]nce that genie gets out of the bottle, you can't put it back in." (A2433/238:19-21 (Whitehurst).)

ETE should also have borne the burden of proving that its refusal to instruct any of its counsel to search for potential solutions to Latham's concerns and its decision to prohibit Morgan Lewis from further exploring the question of whether Proposals A or B would work if the Merger Agreement required such an amendment did not, individually or in the aggregate, materially contribute to the failure of the closing condition.[14]

The Court of Chancery did not consider these or any of the other questions ETE should have had to answer about how it can prove its consistent lack of effort to obtain the 721 Opinion had no material effect on Latham's refusal to deliver it.

* * *

The Court of Chancery's conclusion that ETE's conduct was consistent with its efforts obligations was the product of significant legal error, creating troubling precedent for public company merger parties and their stockholders. It is, after all, the stockholders of Delaware corporations who ultimately shoulder the costs imposed by decreased deal certainty. This is vividly illustrated in the present case, where more than 80% of Williams' participating stockholders voted to approve the Transaction only to be informed that ETE, having won the "lottery", was terminating and walking away. This Court should vacate the Court of Chancery's conclusion that ETE did not breach its contractual duties and that such breach did not materially contribute to the failure of the closing condition, and either enter judgment on the record of the trial below or remand for further proceedings.

[14] The Court of Chancery expressly did not decide whether ETE's duty to use "commercially reasonable efforts to cause . . . the Contribution and the Parent Class E Issuance to qualify" under Section 721 (A680 § 5.07(a)) included a duty to make amendments to the Merger Agreement that would permit qualification without changing the economic terms of the deal. (Op. 48.) To be clear, that was ETE's obligation. The trial court was able to avoid deciding the question only because it erroneously found Latham's "good faith" determinative. (Op. 43-44.)

II. THE COURT OF CHANCERY ERRONEOUSLY REJECTED WILLIAMS' ARGUMENT THAT ETE'S TAX REPRESENTATION EQUITABLY ESTOPPED ETE FROM TERMINATING BASED ON THE FAILURE OF THE 721 OPINION CLOSING CONDITION.

A. Question Presented

Did the Court of Chancery err in holding that ETE was not equitably estopped from terminating the Merger Agreement based on facts known to ETE and its counsel at the time ETE made the Tax Representation, when Williams relied on that representation in agreeing to ETE's proposed Transaction structure and to the 721 Opinion condition? (A2660-63; A2767-69; A2958-60; A2988-89.)

B. Standard of Review

This Court reviews the Court of Chancery's legal conclusions *de novo*. *Peierls*, 77 A.3d at 235.

C. Merits of Argument

In the Tax Representation, ETE represented and warranted that it did not "know[] of the existence of any fact that would reasonably be expected to prevent . . . the Contribution and Parent Class E Issuance from qualifying as an exchange to which Section 721(a) of the Code applies". (A652 § 3.02(n)(i).) Latham (ETE's tax counsel and the law firm designated to deliver the 721 Opinion) reviewed the language of the Tax Representation before ETE agreed to it. Latham understood that it was "important" for Latham to "make sure" that ETE could make the representation (A2027/106:1-6 (Fenn)) and that it was Latham's "job . . .

to raise the red flag if [Latham] saw any issues" with it (A2545/15:24-16:5 (Stein)). Williams then relied on the Tax Representation when it agreed to ETE's proposed Transaction structure and to the 721 Opinion condition. (*See* A2871/342:21-343:15, A2889/412:14-413:7 (Needham).) The Tax Representation gave Williams comfort that, absent a change in facts or law, Latham—having gained sufficient comfort on the issues to allow its client to make the representation—would deliver the 721 Opinion. (*See* A2871/343:1-19 (Needham).) As Latham tax partner Tim Fenn testified, "[W]hat this [Tax Representation] tells me is, again, at the time that the deal is signed, I'm saying Latham & Watkins is prepared to render . . . the 721 opinion." (A2841/222:9-17.)

Six months later—with the Transaction now "manifestly unattractive" to ETE (Op. 3)—ETE changed its mind about the 721 Opinion. *But there were no new facts, and the law had not changed*. Rather, ETE's newfound concern about Section 721 was based on the *same* facts on which the Tax Representation had been based. When it made the Tax Representation, ETE knew all relevant facts about the Transaction structure, which were in the Merger Agreement (A604-720) and the attached form of Contribution Agreement (A721-29; *see* A2832/188:10-24 (Whitehurst); A2855/279:23-280:13 (Fenn)). ETE also knew that stock prices go up and down, so that—if this is relevant to the tax analysis, as Latham now says it is—ETE knew the value of ETE's publicly traded units at closing was expected to be different from that at signing. (A2857/287:23-288:10 (Fenn); A2916/520:1-3 (Stein); A2101/39:9-40:2 (McReynolds); A2478-79/41:17-42:2 (Warren).) By April 2016, ETE's position—based on those same facts—had changed.

Having made the Tax Representation based on advice from the very law firm (Latham) that the parties agreed would deliver the 721 Opinion, having conveyed to Williams through the representation that the facts in ETE's possession when the Merger Agreement was signed provided no reasonable basis for concern about the 721 Opinion and having induced Williams to enter into the Transaction in reliance on the representation, ETE was equitably estopped from terminating on the ground that the same pre-existing facts caused the failure of the 721 Opinion.

The trial court misapprehended Williams' estoppel argument, and then erred in rejecting it. Williams made two arguments based on ETE's Tax Representation:

1. That ETE breached the Tax Representation and, therefore, could not terminate the deal (*see* A2656-60; A2767-69); and

2. That ETE was equitably estopped from terminating based on the failure of the 721 Opinion condition because ETE's basis for terminating was inconsistent with the Tax Representation on which Williams relied (*see* A2660-64; A2767-69; A2958-60, A2988-89).

Yet the Court of Chancery understood Williams' claim to be only for breach of the Tax Representation (argument 1), not for equitable estoppel (argument 2).[15]

[15] *See* Op. 51-55 (addressing Williams' arguments relating to the Tax Representation under the heading "[ETE] is Not in Material Breach of its Representation and Warranty"); Op. 51-52 ("Williams makes an argument that [ETE] is 'in breach' of a required representation and

Due to this misunderstanding, the reasoning in the Opinion is inapplicable to Williams' claim for equitable estoppel. For example, the Court of Chancery found "no facts here that [ETE] failed to disclose." (Op. 52.) But Williams' equitable estoppel argument does not depend on any omission or misrepresentation by ETE. It is not that ETE failed to tell the truth; it is that, after inducing Williams to enter into the Transaction based on the Tax Representation, ETE could not take actions inconsistent with that representation—that is, without any of the premises underlying the representation having changed—to Williams' detriment.

The Court of Chancery characterized Williams' position on the Tax Representation as instituting "a waiver of any subsequent reliance [by ETE] o[n] a failure of the 721 Opinion condition precedent", which, in the trial court's view, would render "the provision for a 721 Opinion . . . surplussage". (Op. 54-55.) But Section 6.01(h) is not surplusage, and Williams does not claim that it is. The 721 Opinion condition existed to protect the parties from unexpected, intervening changes in law (for example, IRS regulations or judicial decisions) or facts (for example, facts about the corporate structure of Williams or ETE) that would alter the Section 721 analysis. What the parties were not permitted to do was represent and warrant that the facts known to them at signing were not reasonably expected to lead to a Section 721 problem and then terminate the Merger Agreement due to

warranty that, as of the date the Merger Agreement was signed, it knew of no actions or facts indicating the 721 Opinion could not issue.").

a failure of the 721 Opinion stemming from those *very same facts*.

To be sure, ETE and its advisors maintain that they did not "put two and two together" (A2833/191:14-19 (Whitehurst); A2918/530:13-17 (Stein))—in other words, that when it made the Tax Representation, ETE did not *subjectively* realize the import of the facts in its possession. But that is not what the Tax Representation says. It imposes an objective test for whether, on the facts known to ETE, the Transaction "would reasonably be expected" to qualify under Section 721. That is, ETE represented and warranted that (1) it did not *subjectively* know of facts that (2) would *objectively* be expected to prevent Section 721 qualification. *See Frontier Oil v. Holly Corp.*, 2005 WL 1039027, at *33 (Del. Ch. Apr. 29, 2005) (holding that the phrase "reasonably be expected to" in a warranty required an "objective" analysis).[16] While ETE contends that it did not appreciate at signing that the facts available to it could lead to a Section 721 issue, that is beside the point. Where a representation and warranty includes an objective component, even a good faith failure by the warranting party to appreciate the relevant result provides that party no protection. *See Frontier*, 2005 WL 1039027, at *33 n.210. Furthermore, because equitable estoppel arises from Williams' reasonable expectations at signing, not from ETE's state of mind, any change in

[16] *See also Allen v. Encore Energy Partners, L.P.*, 72 A.3d 93, 104 (Del. 2013) (ruling that "believes" imposes a subjective test while "reasonably believes" imposes an objective test in a contract); *Rohn Indus., Inc. v. Platinum Equity LLC*, 911 A.2d 379, 382-85 (Del. 2006) (interpreting "reasonable basis" in a contract to impose an objective test under New York law).

ETE's view of the tax issue is irrelevant. *See Nevins v. Bryan*, 885 A.2d 233, 250 (Del. Ch. 2005) ("The law is clear that even unintentional conduct which induces reliance of another to his detriment is sufficient to create an estoppel." (internal quotation marks and alterations omitted)), *aff'd*, 884 A.2d 512 (Del. 2005).

Williams established equitable estoppel under Delaware law, by demonstrating that Williams (i) "lacked knowledge or the means of obtaining knowledge of the truth of the facts in question", (ii) "reasonably relied on the conduct of the party against whom estoppel is claimed" and (iii) "suffered a prejudicial change of position as a result of [that] reliance." *Id.* at 249.

First, Williams did not know—nor could it have known—that ETE would terminate based on a failure of the 721 Opinion condition due to facts that existed at signing. In fact, the Tax Representation led Williams to believe ETE would *not* do so. Thus, while the Court of Chancery rejected Williams' argument on the ground that "knowledge of [ETE's tax] theory is no more chargeable to [ETE] than to Williams" (Op. 54), that is not the relevant inquiry. Whether or not Williams could have cooked up the same surprise tax theory that ETE has now adopted—a theory with which Williams strongly disagrees—the relevant inquiry is whether Williams could have known that ETE would *rely* on that tax theory to terminate the Transaction. Williams could not possibly have known this. In the Tax Representation, ETE (advised by Latham) told Williams that then-existing facts would not reasonably cause a Section 721 problem. Knowledge that ETE would rely on the *opposite* conclusion—which ETE adopted only after turning against the deal—is not "chargeable" to Williams. Even Whitehurst recognized the inconsistency between the Tax Representation and ETE's new position, conceding that ETE would not make the representation today. (A2833/191:1-2.)

Second, Williams actually and reasonably relied on the Tax Representation, which was important to Williams because it forced ETE "to disclose anything that [it] may be aware of that could potentially have the effect of causing the transaction to fail." (A2871/342:21-343:15 (Needham).) Relying on this, Williams agreed to the 721 Opinion condition and the overall Transaction structure. (*See* A2889/412:14-413:7 (Needham); A2841/222:22-223:2 (Fenn).) This reliance was reasonable; at signing, *everyone* expected the Transaction to be tax free. (A608-09 ("[T]he Contribution and the Parent Class E Issuance are intended to qualify as an exchange described in Section 721(a)"); A2819/135:14-17 (Whitehurst); A2856/282:12-15 (Fenn); A2903/468:16-469:2 (Stein); A2871/340:15-341:4, A2872/346:8-11 (Needham); A2338/151:10-13 (Rackley).)

Third, Williams suffered a prejudicial change of position in reliance on the Tax Representation. Williams lost the opportunity for an alternatively structured deal with ETE—in particular one that would have precluded ETE from later terminating due to the failure of the 721 Opinion condition. The evidence at trial indicated that Latham would have delivered the 721 Opinion if the Transaction had been structured like Proposal A or B from the outset. (*See* A932 (Latham stating that "[Proposal B] might have been helpful (on the margin) had we done it from the start"); A2939/612:7-21 (McKee) ("[W]e all agree that the deal would work" if initially structured like Proposal A).) Had ETE raised tax concerns before signing, the parties would have agreed to an alternative structure to address the issue.[17]

Because ETE was equitably estopped from terminating on the basis of the 721 Opinion condition absent a change in law or facts, its termination was a breach of the Merger Agreement. *See* 13 Richard A. Lord, *Williston on Contracts* § 39:29, at 687-88 (4th ed. 2013) ("A condition precedent to performance may be said to be waived by estoppel when a promisor's words or conduct justify the promisee in believing that a conditional promise will be performed despite the failure of the condition to occur or be performed, and the promisee relies on the promisor's manifestations to its substantial detriment."). This understanding of the Tax Representation effectuates the parties' intent at signing, encourages parties to consider their representations and warranties before inducing their counterparties to rely on them and prevents unjust results stemming from inequitable conduct.

[17] Williams also lost the opportunity for a merger transaction with Williams Partners L.P. ("WPZ") or other potential partners. Before executing the Merger Agreement, Williams had entered into a merger agreement with WPZ. (A1164.) As a requirement to executing the Merger Agreement, ETE insisted that Williams terminate its agreement with WPZ. (*See* A1187-88.) Had Williams known that ETE would terminate the Merger Agreement based on then-existing facts, Williams would not have terminated its agreement with WPZ.

CONCLUSION

For the foregoing reasons, the decision of the Court of Chancery should be vacated on the grounds that the Court of Chancery: (i) erroneously concluded that ETE did not breach its "reasonable best efforts" or "commercially reasonable efforts" obligations, (ii) erroneously concluded that ETE's acts and omissions did not materially contribute to the failure of the 721 Opinion condition and (iii) erroneously permitted ETE to terminate on the basis of facts that ETE had represented and warranted did not provide a basis to terminate. The partial final judgment of the Court of Chancery should be reversed, or vacated with the matter remanded for further proceedings pursuant to correct legal principles.

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CERTIFICATE OF SERVICE

I hereby certify that on August 11, 2016, the foregoing was caused to be served upon the following counsel of record via File & Serve*Xpress*:

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