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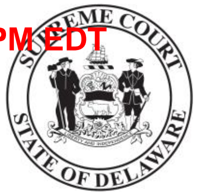

IN THE SUPREME COURT OF THE STATE OF DELAWARE

MARION #2-SEAPORT TRUST U/A/D JUNE 21, 2002, Defendant Below-Appellant, v. TERRAMAR RETAIL CENTERS, LLC, Plaintiff Below-Appellee.	No. 306, 2019 APPEAL FROM THE COURT OF CHANCERY OF THE STATE OF DELAWARE, C.A. NO. 12875-VCL

APPELLANT'S REPLY BRIEF

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Dated: September 24, 2019

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INTRODUCTION

As the record in this action made clear, Seaport Village was extremely profitable at the time Terramar was offered an opportunity to purchase an interest in the property.[1] When the Company was formed in connection with Terramar's purchase, and Terramar was given management authority, all members expected that they would share millions of dollars annually in future cash flows on a *pari passu* basis. Only in the unlikely event the Company did not secure a long-term extension for the Phase I ground lease, the primary objective with which Terramar was tasked as manager, did the members agree that Terramar could earn a priority return on its investment.

Sixteen years of evidence shows that Terramar never intended to operate the Company for the mutual benefit of all members, as Terramar's contractual and fiduciary duties required. Instead, the evidence demonstrated that Terramar extracted virtually 100% of approximately $75,000,000 of net cash flow for itself by, *inter alia*: (i) paying itself approximately $20,000,000 in unauthorized "fees" that allowed the IRR Entitlement to continue growing; (ii) unnecessarily self-funding the Company through a capital call and member loans to create additional priorities, while breaching its obligations to seek and obtain cheaper third party debt;

[1] Capitalized terms shall have the meanings provided in Appellant's Opening Brief (cited as "OB"). Appellee's Answering Brief is cited as "AB."

and (iii) ensuring that the Phase I ground lease was never extended, thereby maintaining the IRR Entitlement in perpetuity.

Unsatisfied, Terramar devised a plan to unilaterally liquidate the Company's assets and collect 100% of the proceeds while circumventing the minority members' consent rights. Knowing that its scheme would prompt the co-members to file suit in California (the State where all members and Seaport Village are located), Terramar filed a pre-emptive complaint for declaratory judgment in Delaware, which raised only narrow issues for resolution and presumed (wrongfully) that Terramar was authorized to unilaterally dissolve the Company.

Terramar filed this action in Delaware because it believed the Court of Chancery was a favorable forum, based on Vice Chancellor Laster's entry of judgment in Terramar's favor in the prior proceeding brought by Limited. The Trust was not a party to that prior action, which did not address the narrow issues raised by Terramar's subsequent declaratory judgment claim. The Trust's Opening Brief detailed how Vice Chancellor Laster's factual determinations and impressions formed in the prior action influenced rulings in this proceeding, even though the Trust had no opportunity to present evidence in the earlier case. (Indeed, before hearing any evidence in this action, the Court commented that it was "familiar with the parties and the underlying facts through its adjudication of the Limited Action." A1320.) The Court's post-trial Opinion in this action ("Op.") drew many inferences

in Terramar's favor based on inaccurate impressions formed in the prior action, rather than undisputed facts developed at trial. Contrary to Terramar's argument, the Trust does not offer "factual assertions directly contrary to the facts found by the trial court" (AB 4); rather, the Trust cites unrebutted evidence ignored by the Court. Terramar's own "statement of facts" ignores, omits or distorts record evidence that refutes Terramar's assertions.[2]

After Terramar took steps to sell Seaport Village, the Trust filed a complaint in California alleging that Terramar did not satisfy the Operating Agreement's conditions with which Terramar must comply before it may dissolve and liquidate the Company. Terramar tried unsuccessfully to stop the California action, filing motions to stay that proceeding and to strike the Trust's claim that Terramar was not authorized to dissolve the Company. The California court denied both motions, finding that California had a substantial interest in adjudicating the Trust's claims.

Later, the Court of Chancery usurped the California court's jurisdiction over the dispute when it denied the Trust's motion to dismiss or stay this action in deference to the California proceeding. The Court effectively re-wrote Terramar's declaratory judgment complaint, injecting the issue of Terramar's compliance with

[2] For example, Terramar deceptively attempts to blur the distinctions between the Trust, M.A. Cohen & Co. and Mr. Cohen by repeatedly and indiscriminately referring to "Cohen." *E.g.*, AB 7, 12-13, 15. It is the Trust (which is irrevocable) that is party to the Operating Agreement, and M.A. Cohen & Co., a licensed real estate broker, is the party that performed brokerage services for the Company.

Section 9.5 into this action, even though (i) Terramar never sought declaratory relief on that issue, and (ii) that issue, as well as predicate issues that should have been resolved before Terramar's secondary claims, already were before the California court. The Court never should have considered whether Terramar was authorized to dissolve the Company, but should have allowed the California court to adjudicate that issue, in the forum where the Trust first raised it. The Court's denial of a stay, and its judgment in Terramar's favor, should be reversed so that the California court may properly determine whether Terramar complied with Section 9.5.

After forcing the Trust to defend claims that Terramar never pled, the Court then compounded its error by incorrectly using a Settlement Agreement and Statutes of Limitation as a basis to disregard years of unrebutted evidence *proving* that Terramar did not comply with Section 9.5. The Court committed reversible error because (i) Delaware courts have no authority to apply the parties' Settlement Agreement, which expressly provides that it can only be interpreted and enforced by the California Superior Court, (ii) the Settlement Agreement's release of "claims" has no effect on the Trust's right to present evidence refuting Terramar's case in chief or supporting the Trust's defenses, and (iii) Statutes of Limitation do not apply to the Trust's defenses or proffer of evidence disproving Terramar's allegations.

When properly considered, the evidence the Court disregarded – and which Terramar made no effort to rebut – establishes that Terramar did not comply with

Section 9.5 and has no authority to dissolve the Company. The Court's contrary ruling should be reversed and judgment should be entered in the Trust's favor. Alternatively, the California court – the forum agreed upon by the parties – should be permitted to adjudicate the effect (if any) of the Settlement Agreement and Terramar's compliance with Section 9.5. Only if the California court finds that Terramar complied with Section 9.5 and is authorized to dissolve the Company would the Court of Chancery have any basis to consider Terramar's demand for 100% of the sales proceeds.

ARGUMENT

I. THE TRIAL COURT SHOULD HAVE STAYED TERRAMAR'S NARROW DECLARATORY JUDGMENT ACTION IN DEFERENCE TO THE CALIFORNIA ACTION.

Terramar's amended complaint only sought declarations that: (i) "under Section 9.5 of the Operating Agreement, Terramar is entitled to unilaterally sell all of [the Company's] property and assets to a third party in connection with [the Company's] dissolution," and (ii) "Terramar has correctly calculated the Waterfall Distribution." A410. Both declarations *presume* Terramar's right to dissolve and only address issues that arise *after* Terramar has satisfied the conditions precedent to dissolving the Company and selling its assets. Neither declaration raises the predicate issue of whether Terramar complied with the requirements of Section 9.5, which must be met before Terramar may dissolve the Company.

In the California action, the Trust asserts that Terramar did not comply with Section 9.5 and contests Terramar's claimed right to dissolve the Company and sell its assets. Whether Terramar may dissolve the Company is an issue that should have been resolved in California before the secondary issues raised by Terramar's declaratory relief claims in Delaware. Terramar's right to dissolve the Company and sell its assets was not raised in Terramar's Delaware pleading but was an issue pending before the California court. The Court of Chancery erred by declining to stay this action pending completion of the California action. *See RWI Acquisition*

LLC v. Todd, 2012 WL 1955279, at *7-10 (Del. Ch. May 30, 2012) (staying first-filed Delaware action pending ruling on predicate contractual issues by sister court); *BW Piezo Holdings LLC v. Phillips*, 2017 WL 1399746, at *4-5 (Del. Super. Apr. 18, 2017) (same).

Terramar sought entry of a case scheduling order while the Trust's motion to stay was pending. OB 21-22. At a hearing on Terramar's request, which occurred before the motion to stay was argued, the Court recognized that Terramar sought a narrow declaration that "*under the contract it can sell to third parties*, period, stop." A2477 (emphasis added). The Court described this action as addressing narrow "Delaware LLC interpretative issues," which could aid the California court in resolving broader issues relating to "factual circumstances … on the ground in California." A2492.

The Court shortly thereafter ordered the Trust to answer Terramar's complaint before ruling on the Trust's pending motion to stay. A2496. In its answer, the Trust made clear that it never disputed whether Terramar may sell the Company's assets to a third party if Terramar satisfied all requirements of Section 9.5. A2622. Whether Terramar had satisfied Section 9.5 was an issue already pending in California and had never been raised in this action; therefore, the Court had only to decide whether Terramar correctly demanded 100% of the sales proceeds following a valid dissolution and sale.

The Court of Chancery must have recognized that addressing compliance with Section 9.5 in the California action was a prerequisite to adjudicating Terramar's Delaware claim and, therefore, should have stayed this action. However, the Court denied a stay (committing reversible error) by improperly *re-writing* Terramar's pleading to request declarations that Terramar "properly exercised a buyout provision" and "has the power to dissolve the Company" (A3275) – precisely the predicate issues that the Trust alleged in California but which Terramar had never raised in its Delaware pleading. Terramar's secondary request for a declaration that it "correctly calculated the Waterfall Distribution" was unripe without a threshold determination that Terramar complied with Section 9.5 and, thus, was authorized to dissolve the Company and sell its assets. Contrary to Terramar's argument, the Trust did not "deliberately ignore" this "waterfall" claim (AB 21); rather, the claim was entirely dependent upon a finding that Terramar complied with Section 9.5 and, therefore, should have been stayed pending the California court's decision.

Terramar's reliance upon *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281, 283 (Del. 1970), is misplaced, since that opinion expresses a preference for litigation in "the forum in which it is first commenced" when there is an action "involving the *same cause of action* in another jurisdiction" (emphasis added). The Trust's California claims raised predicate issues requiring adjudication *before* the secondary issues raised by Terramar's declaratory judgment

claim. The Court thus should have stayed this action in deference to the California action, but instead improperly expanded the scope of Terramar's claim to usurp issues pending before the California court.

Applying the factors under *Gen. Foods Corp. v. Cryo-Maid, Inc.*, 198 A.2d 681, 685 (Del. 1964), the Court of Chancery found that access to evidence and third party witnesses in California favored dismissing or staying this action. A3280-A3284. However, the Court needed to re-write Terramar's pleading in order to find that two other factors – the applicability of Delaware law and the pendency of a similar action in another jurisdiction – were dispositive. *Id.* The Court concluded that these factors weighed "powerfully" in favor of Delaware, but only because the Court had re-written Terramar's complaint to seek a declaration concerning Terramar's "right under the Operating Agreement to dissolve the Company" (A3280), the issue the Trust already had raised in California. Only by improperly expanding the scope of Terramar's claim beyond what was written in the complaint could the Court conclude that the Delaware action "implicates the internal affairs of a Delaware entity." *Id.*

This error is particularly egregious given that the California court twice rejected Terramar's efforts to halt the Trust's claims challenging Terramar's compliance with Section 9.5 and authority to dissolve the Company. First, the California court denied Terramar's motion to stay the California action, holding that

the two actions *raised different issues* and the State of California had substantial public and private interests in resolving the dispute. A1813-A1816; A1825-A1827; A1843-A1844. Then, Terramar unsuccessfully moved to strike the Trust's allegation that Terramar failed to comply with Section 9.5. In denying that motion, the California court held that the Trust alleged a *prima facie* claim that Terramar had not complied with Section 9.5 and, therefore, was not authorized to dissolve the Company. A2879-A2880; A2891.

The Court of Chancery abused its discretion by usurping California's jurisdiction over the Trust's claims against Terramar when it refused to dismiss or stay this proceeding in deference to the California action. *See GTE Mobilnet Inc. v. Nehalem Cellular, Inc.*, 1994 WL 116194, at *5 (Del. Ch. Mar. 17, 1994) (staying Delaware action pending outcome of Oregon action where "Oregon has declared its power to hear this dispute"); *E-Birchtree, LLC v. Enter. Products Operating L.P.*, 2007 WL 914644, at *3 (Del. Super. Jan. 18, 2007) (staying Delaware action pending outcome of Texas action where "[t]he Texas court already has ruled that the action before it shall proceed"). The Court's ruling should be reversed, and its judgment vacated, to allow the California court to adjudicate Terramar's compliance with Section 9.5 and its authority to dissolve the Company.

II. THE TRIAL COURT ERRONEOUSLY RELIED UPON THE SETTLEMENT AGREEMENT TO DISREGARD EVIDENCE THAT TERRAMAR FAILED TO CREDIT RECEIVED DISTRIBUTIONS AGAINST ITS CLAIMED PRIORITIES.

The Trust proved, and Terramar does not dispute, that Terramar breached the Operating Agreement by improperly causing the Company to pay Terramar approximately $20,000,000 in purported "pre-development fees." A5714. Section 5.4(d) permits the Company to pay fees to Terramar, but only if (i) the fees are for certain specified categories of services, (ii) the fees are paid pursuant to a contract between Terramar and the Company, and (iii) the contract provides for "market fees" on reasonable terms and conditions. A78. The undisputed evidence demonstrated that (i) "pre-development" is not a category of services for which the Company may engage and compensate Terramar, (ii) there was no contract between Terramar and the Company for "pre-development" services (in fact, the record showed that Terramar never entered into any contracts with the Company to perform services of any type), and (iii) the "pre-development fees" paid to Terramar exceeded the market rate by millions of dollars. A5714.

These undisputed payments, in actuality, represented approximately $20,000,000 of distributions to Terramar that were improperly labeled as "pre-development fees" to avoid crediting the distributions against the IRR Entitlement. This vastly inflated Terramar's purported IRR Entitlement, which in turn inflated the Purchase Price Terramar demanded for its membership interest pursuant to the

"put" – since Section 9.5(a) ties the Purchase Price for Terramar's membership interest directly to Terramar's "priorities," the largest of which is the IRR Entitlement.

Presented with unrebutted proof that Terramar paid itself these disguised distributions, the Court of Chancery held that *all* such evidence was barred by the Settlement Agreement and by Statutes of Limitation. Op. 37-43. As discussed below, the Court erred by improperly and incorrectly interpreting and enforcing the Settlement Agreement to disregard undisputed record evidence. For the reasons discussed in Section III *infra*, the Court also erred by misapplying Statutes of Limitation to disregard this evidence. Both errors support reversal of the Court's ruling and entry of judgment in the Trust's favor. Alternatively, the judgment should be vacated to permit the California court to (i) interpret and enforce the Settlement Agreement as the parties expressly agreed, and (ii) determine Terramar's compliance with Section 9.5.

A. THE SETTLEMENT AGREEMENT DOES NOT PROHIBIT THE TRUST FROM REBUTTING TERRAMAR'S CASE IN CHIEF.

As the plaintiff, Terramar bore the burden to prove what it claimed to be owed under the IRR Entitlement, which directly affects the Purchase Price Terramar demanded in the Section 9.5 "put" process. By proving that Terramar took approximately $20,000,000 in disguised distributions, the Trust directly refuted

Terramar's case in chief – *i.e.*, the amount that Terramar purportedly is owed under the IRR Entitlement and the corresponding Purchase Price for Terramar's interest.

The Court erred by refusing to consider the Trust's evidence based on the existence of the Settlement Agreement. This evidence proved that Terramar's calculation of the IRR Entitlement was incorrect and that the entire IRR Entitlement was repaid in full years before Terramar issued its Buy-Out Notice. Accordingly, Terramar did not comply with Section 9.5 because Terramar's claimed Purchase Price for its membership interest included an IRR Entitlement that had been repaid and thus was overstated by millions of dollars. Offering evidence to rebut Terramar's case in chief is neither a claim nor an affirmative defense. *See, e.g.*, *Barnes v. AT&T Pension Ben. Plan,* 718 F. Supp.2d 1167, 1173-74 (N.D. Cal. 2010) ("Such a defense is merely rebuttal against the evidence presented by the plaintiff."). The Settlement Agreement cannot and does not prohibit the Trust from offering evidence to rebut Terramar's *prima facie* claim by showing that Terramar had already been paid the money that Terramar claimed to be owed under its priorities and as part of its Purchase Price.

B. DELAWARE COURTS HAVE NO AUTHORITY TO INTERPRET OR ENFORCE THE SETTLEMENT AGREEMENT.

The Court of Chancery also erred by interpreting and enforcing the Settlement Agreement. Under the Settlement Agreement's unambiguous terms, only the California Superior Court is authorized to interpret or enforce the Settlement

Agreement. OB 15; A1950. Such forum selection clauses "must be enforced." *Nat'l Indus. Grp. (Holding) v. Carlyle Inv. Mgmt. L.L.C.*, 67 A.3d 373, 381 (Del. 2013).

Terramar does not and cannot challenge the Settlement Agreement's plain language, or the obvious conclusion that the Settlement Agreement prohibits a Delaware court from enforcing it. Instead, Terramar asserts incredulously that this action is not "related to enforcement or interpretation of [the Settlement] Agreement." AB 23. This is ludicrous, since Terramar has claimed consistently from the outset of this proceeding that the Settlement Agreement bars the Trust from offering (and Delaware courts from considering) evidence proving that Terramar disguised distributions as "fees." Paragraph 17 of Terramar's Amended Complaint alleges plainly:

> The Cohen Trust settled certain claims against Terramar in 2015 and executed a release of claims against Terramar. Claims against Terramar that the Cohen Trust released in 2015 may not be reasserted under the guise of challenging Terramar's entitlement to distribution under the "waterfall" set forth in the Operating Agreement.

A405. As this makes clear, Terramar has always sought to enforce the Settlement Agreement's release in this action. Terramar cannot now evade its agreement to an exclusive forum and the Court likewise should not have ignored the forum selection clause and committed reversible error by interpreting and enforcing the Settlement Agreement.

C. THE SETTLEMENT AGREEMENT DOES NOT PROHIBIT THE TRUST FROM OFFERING EVIDENCE IN SUPPORT OF AFFIRMATIVE DEFENSES.

1. The Settlement Agreement Does Not Release Defenses.

The Settlement Agreement neither prohibits the Trust from asserting affirmative defenses based on Terramar's years of misconduct nor prohibits the Trust from offering evidence in support of those defenses. The Settlement Agreement is unambiguous – the release is limited to "claims, actions or causes of action." A1946-A1947. The Settlement Agreement does not release "defenses." Under California law, a release must be "clear, unambiguous and explicit" and "is interpreted more strictly, so as to favor the party releasing liability." *Solis v. Kirkwood Resort Co.*, 114 Cal. Rptr.2d 265, 269 (Ct. App. 2001).

The Court of Chancery erred by finding that the Trust asserted "claims" barred by the Settlement Agreement. As the Trust explained in its Opening Brief, Terramar did not seek damages or payment of money from the Trust; rather, this action (as expanded by the Court) focused on whether Terramar complied with Section 9.5. In refuting Terramar's declaratory judgment claim, the Trust did not seek "to impose losses on Terramar and recover on [the Trust's] own behalf." Op. 40. Rather, the Trust offered uncontroverted evidence showing that the Purchase Price Terramar demanded from the Trust pursuant to Section 9.5 was vastly overstated because (i) Terramar already had been paid disguised distributions that were not credited against

the IRR Entitlement, and (ii) Terramar's prior misconduct inflated Terramar's claimed priorities.

2. The Trust Never Waived Its Right To Support Its Defenses With Evidence Of Terramar's Misconduct.

Confronted with the Settlement Agreement's clear exclusion of defenses, Terramar argues that the Trust waived defenses relating to Terramar's pre-October 2015 conduct. AB 24-25. Terramar, however, misconstrues and selectively quotes from the Trust's Answer and the Pre-Trial Order, intentionally omitting portions of those documents that clearly place at issue facts and events that occurred before October 2015. For example, Terramar's Amended Complaint alleged "disputes" with the Trust about "payments Terramar is entitled to under the waterfall," "management fees" Terramar was permitted to receive, "how one computes the internal rate of return on Terramar's original $7 million investment," and "whether Terramar is entitled to that return at all." A401. The Trust's Answer "denie[d] that Terramar is 'contractually entitled' to its 'original $7 million investment' [the IRR Entitlement] due to its unlawful conduct" (A2608), and averred that Terramar "refused to use Operating's excess net cash flow to pay down Terramar's purported 'priority' on its original $7 million investment" (A2627-A2629). Terramar's pre-2015 improper conduct was a subject of the Trust's discovery, was identified in the Pre-Trial Order and was highlighted in the Trust's Pre-Trial Brief. *E.g.*, A5336-A5337; A5343-A5353; A5376-A5379; A5481-A5485. Thus, resolving Terramar's

disputed priorities, which had been accruing for years, necessarily required consideration of facts occurring before October 2015. Terramar's claim that the Trust "waived" its right to present evidence of Terramar's pre-2015 misconduct by waiting until trial to "expand" its defenses is meritless.

III. STATUTES OF LIMITATION DO NOT BAR THE TRUST FROM OFFERING EVIDENCE OF TERRAMAR'S PAST MISCONDUCT TO REFUTE TERRAMAR'S CLAIM.

Terramar offers no rebuttal to the "well-established rule that affirmative defenses are not ordinarily subject to the statute of limitations so long as they are properly pled and arise from the same transaction as the claims in the original complaint." *U.S. Philips Corp. v. Samsung Elecs. Co., Ltd.*, 2011 WL 13142645, at *2 (D. Del. Mar. 25, 2011). *See also* OB 32 (citing additional authorities). This rule has not "been considered and expressly rejected by the Delaware courts," as Terramar claims. AB 28. Rather, the two opinions cited by Terramar and the Court of Chancery, *Finger Lakes Capital Partners, LLC v. Honeoye Lake Acquisition, LLC*, 151 A.3d 450, 454 (Del. 2016), and *TIFD III-X LLC v. Fruehauf Prod. Co., L.L.C.*, 883 A.2d 854, 859 (Del. Ch. 2004), merely recognized that a recoupment claim is not barred by statutes of limitations if it "arises out of the same transaction or occurrence as the plaintiff's suit."

Here, the Trust's evidence not only "arises out of the same transaction or occurrence as the plaintiff's suit," it directly rebuts Terramar's case in chief. As discussed above, the Trust's evidence that Terramar took approximately $20,000,000 in disguised distributions refutes Terramar's calculations of both the claimed IRR Entitlement and the claimed Purchase Price and proves that Terramar did not comply with Section 9.5. Offering this evidence is not an affirmative

defense; rather, it is "merely rebuttal against the evidence presented by the plaintiff." *Barnes*, 718 F. Supp.2d at 1173. Delaware's three-year Statute of Limitations, which expressly applies to "actions," 10 *Del. C.* § 8106(a), cannot bar a defendant from rebutting a plaintiff's *prima facie* case. *See Estate of Hogarth v. Edgar Rice Burroughs, Inc.*, 342 F.3d 149, 163 (2d Cir. 2003) ("A defendant who is not seeking any affirmative relief and who asserts a defense only to defeat a plaintiff's claim is not barred by a statute of limitations.").

Unlike the scenarios in *Finger Lakes* and *TIFD*, the Trust's challenges to Terramar's past misconduct "arise out of" and relate directly to Terramar's non-compliance with Section 9.5 based on inflated priorities, which grossly inflated Terramar's demanded Purchase Price. The Trust offered evidence directly rebutting Terramar's assertion that it complied with Section 9.5, and the Court erred by finding that Statutes of Limitation prohibited consideration of that evidence.

IV. TERRAMAR DID NOT COMPLY WITH SECTION 9.5 OF THE OPERATING AGREEMENT.

The Operating Agreement permits Terramar to dissolve the Company and sell its assets only if Terramar complies with Section 9.5 and the "put" process does not result in a purchase of Terramar's membership interest. Section 9.5 required Terramar to, *inter alia*, (i) disclose its opinion of the Company's fair market value, (ii) disclose the amount of proceeds Terramar would receive, based on its priorities, in a hypothetical sale of the Company's assets at the Company's fair market value, and (iii) negotiate with its co-members in good faith to facilitate a purchase of Terramar's interest. A87-A89. If Terramar breached any of these requirements, then it may not unilaterally dissolve the Company. *See Metro. Life Ins. Co. v. Jacobs*, 1 A.2d 603, 606 (Del. 1938) ("[A] party who seeks to recover upon a contract must prove such facts as are necessary to establish a compliance with conditions precedent thereto."). The Trust explained how the Court of Chancery committed reversible error by disregarding uncontroverted evidence and forming conclusions without any evidentiary basis to find that Terramar complied with its contractual and fiduciary obligations. Terramar offers nothing to suggest otherwise.

A. THE RECORD SHOWS THAT TERRAMAR WITHHELD ITS TRUE OPINION OF "COMPANY FAIR MARKET VALUE."

As the Trust explained, the 2015 Valuation Spreadsheet is the *only* piece of documentary evidence in the record reflecting Terramar's internal opinion of the

Company's fair market value. OB 36-38. That document dates from the same time when Terramar issued its Buy-Out Notice (the "end of 2015"), but evidences a gross Fair Market Value of $43,221,916, more than $12 million *less* than the purported Fair Market Value Terramar claimed in the Buy-Out Notice. *Id.* The spreadsheet was created by Terramar's then-CFO (A5496, A5606), and used industry standard valuation methodologies (A5684). The 2015 Valuation Spreadsheet is the only credible, contemporaneous evidence of Terramar's actual opinion of fair market value.

Terramar offers nothing more than Mr. Pettit's uncorroborated testimony to challenge this document's plain import. Mr. Pettit referenced Terramar's audited statements, an appraisal and certain projections, but Terramar refused to produce those documents in discovery. A5608. As the Court itself noted (not the Trust, as Terramar suggests (AB 37 n.6)), Terramar created a "gap in the evidentiary record" by deliberately withholding "underlying calculations" from discovery on purported attorney-client privilege grounds. Op. 23. It was clear, reversible error for the Court to (i) reject the 2015 Valuation Spreadsheet, (ii) accept Terramar's inflated statement of fair market value based solely on Mr. Pettit's testimony, and (iii) fail to draw negative inferences from Terramar's refusal to produce any corroborating evidence or documentation. The Court should have drawn, but did not draw, negative inferences from Terramar's tactical decision to hide relevant evidence. This Court

"discourage[s] the use of the [attorney-client] privilege as a litigation weapon," *Zirn v. VLI Corp.*, 621 A.2d 773, 781-82 (Del. 1993), and litigants may not rely upon "concealed" information as a "sword" at trial after preventing an adversary from pursuing discovery concerning that evidence. *E.g.*, *Chesapeake Corp. v. Shore*, 771 A.2d 293, 301 (Del. Ch. 2000); *In re Pure Res., Inc., Shareholders Litig.*, 808 A.2d 421, 431 n.8 (Del. Ch. 2002).

B. TERRAMAR OVERSTATED ITS PURCHASE PRICE BY IMPROPERLY INFLATING ITS CLAIMED "PRIORITIES."

The trial record showed that Terramar breached the Operating Agreement in several ways that improperly inflated its claimed priorities and therefore caused its demanded Purchase Price to be overstated. OB 39-42. As previously discussed, the Court erred by misapplying the Settlement Agreement and Statutes of Limitation to excuse these admitted breaches. Additionally, Terramar cannot refute the evidence that, when properly considered, shows that Terramar demanded payment for amounts previously received as disguised distributions and therefore demanded an overstated Purchase Price in violation of Section 9.5(a). The Court's contrary holding was clear error and should be reversed. Based on the unrebutted fact record, judgment should be entered in the Trust's favor.

Remarkably, Terramar claims that "[a]t trial, the Trust did not prove that any fees were inappropriate." AB 38. Terramar does not and cannot dispute, as proven at trial, that the Company paid Terramar approximately $20,000,000 in purported

"pre-development fees" in violation of Section 5.4(d). A5714. Nor does Terramar claim, because it cannot, that the record contained a single contract between Terramar and the Company for permitted services, as the Operating Agreement requires. Terramar likewise cites no record evidence rebutting the Trust's expert's determination that Terramar's "pre-development fees" exceeded market by millions of dollars. A287-A289.

C. TERRAMAR DID NOT NEGOTIATE WITH THE TRUST IN GOOD FAITH.

Terramar wrongly characterizes as a "factual finding" the Court of Chancery's legal holding that Terramar's actions (and omissions) satisfied Section 9.5(c)'s requirement that Terramar negotiate with the Trust "in good faith." A88. The relevant facts – *i.e.*, Terramar's actions following the Trust's Notice of Dispute – are undisputed. Whether Terramar's actions satisfied its obligation to act in good faith, as required by Section 9.5(c) or the implied covenant of good faith and fair dealing, is a purely legal question. As such, the Court's legal determination is subject to *de novo* review. *E.g.*, *Oxbow Carbon & Minerals Holdings, Inc. v. Crestview-Oxbow Acquisition, LLC*, 202 A.3d 482, 502 (Del. 2019).

The Court erred as a matter of law by holding that Terramar met the standard of "good faith" mandated by the Operating Agreement and Delaware law. OB 42-48. The Court went to great lengths to excuse Terramar's conduct, finding that the Trust "went silent," or acted unreasonably, despite clear record evidence showing

otherwise. Both Terramar and the Court of Chancery ignore the stipulated fact that the Trust, after receiving the Buy-Out Notice, proposed to purchase Terramar's membership interest in the Company with a well-capitalized third party funding source that had already executed an NDA. A5400 (¶27). Had Terramar truly wanted to sell its interest to a co-member, as the "put" right intended, Terramar would have engaged with the Trust. Instead, the record showed that Terramar breached Section 9.5(c) and unjustifiably rebuffed the Trust's offer, revealing Terramar's clear intent to prevent the Trust from purchasing Terramar's interest so that Terramar could unilaterally liquidate the Company and collect 100% of the proceeds. This cannot constitute "good faith" under Section 9.5(c) or any legal definition of the term.

D. THERE IS NO "JOINT PURCHASE REQUIREMENT."

The Court committed legal error by imposing a "joint purchase" requirement where none exists. Terramar's CEO admitted that Section 9.5 does *not* require a joint purchase. Mr. Zwieg testified in deposition and at trial that the Operating Agreement did not require a "joint purchase" of Terramar's membership interest. A3976-A3977; A5585-A5588. The Court ignored this unambiguous testimony, and Terramar offers no rebuttal for it. Additionally, the Court, *sua sponte*, incorrectly inferred that Section 9.5 required the Company's members to "buy out Terramar while retaining their relative positions vis-à-vis each other," when the Operating Agreement contains no such language. Op. 33. This is inconsistent with Sections

9.1 and 9.4 of the Operating Agreement, which permit transfers of one member's interest to another that would change the members' respective percentage shares. OB 45. The Court erred by adopting the lawyer-made argument, never offered by Terramar before trial, that illogically read a "joint purchase" requirement into Section 9.5.

V. TERRAMAR ADMITTEDLY BREACHED THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING.

Tellingly, Terramar's Answering Brief does not even address the implied covenant of good faith and fair dealing, which "is well-suited to imply contractual terms that are so obvious—like a requirement that the general partner not engage in misleading or deceptive conduct … —that the drafter would not have needed to include the conditions as express terms in the agreement." *Dieckman v. Regency GP LP*, 155 A.3d 358, 361-62 (Del. 2017). Terramar thus concedes (as it must) that its co-members never would have agreed, in a *pari passu* transaction with millions of dollars of annual historical and prospective cash flow, to allow Terramar to create no value and manipulate operations to (i) distribute to itself virtually 100% of $75 million of net cash flow, and (ii) unilaterally liquidate the Company and collect 100% of the proceeds. The Court of Chancery erroneously concluded that Terramar was free to invoke Section 9.5 because it has "independent legal significance" from Section 5.6 (Op. 48), but never considered whether Terramar's predatory conduct over sixteen years frustrated the other members' reasonable expectations – exactly what the implied covenant is intended to remedy. This legal error should be reversed, Terramar should be held to have breached the implied covenant, and judgment should be entered in the Trust's favor.

CONCLUSION

The Court of Chancery committed numerous errors, each of which supports reversal. The Trust respectfully requests that this Court (i) reverse the Final Order and enter judgment in the Trust's favor, (ii) alternatively, reverse the Order denying the Trust's Motion to Dismiss or Stay and vacate the Final Order to permit the California court to adjudicate all issues before it, including Terramar's compliance with Section 9.5 of the Operating Agreement; and (iii) award the Trust reimbursement, as the "prevailing party" pursuant to Section 12.12 of the Operating Agreement, of all attorneys' fees, costs and expenses incurred in this action.

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Dated: September 24, 2019

CERTIFICATE OF SERVICE

I, Thad J. Bracegirdle, hereby certify that on this 24th day of September, 2019, true copies of **APPELLANT'S REPLY BRIEF** were served upon the following via File & Serve*Xpress*:

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