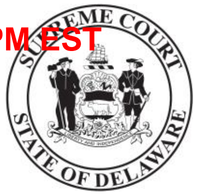
EFiled: Jan 21 2020 01:52PM EST
Filing ID 64615908
Case Number 489,2019



IN THE SUPREME COURT OF THE STATE OF DELAWARE

PAUL MORRIS, on behalf of all similarly situated unitholders of SPECTRA ENERGY PARTNERS, L.P., Plaintiff-Below, Appellant, v. SPECTRA ENERGY PARTNERS (DE) GP, LP, Defendant-Below, Appellee.	Public Redacted Version Efiled January 21, 2020 No. 489,2019 Court Below: Court of Chancery of the State of Delaware C.A. No. 2019-0097-SG

APPELLANT'S OPENING BRIEF

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Dated: January 7, 2020

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NATURE OF PROCEEDINGS

In *Parnes v. Bally Entertainment Corp.*, 722 A.2d 1243 (Del. 1999), this Court ruled that stockholders have direct standing to challenge the fairness of the process of a merger that results in an unfair price. In a series of decisions, Delaware courts have applied *Parnes* to permit stockholders to raise post-merger challenges to the fairness of mergers in which fiduciaries fail to obtain fair value for those stockholders' viable pending derivative claims. This appeal entails a watershed determination of whether that doctrine will remain intact, and the Court's decision will dictate whether Delaware law will abandon its longstanding policy of preventing controllers and directors from immunizing themselves from liability on meritorious derivative claims by orchestrating a squeeze-out in a process that deliberately ignores the value of that claim.

This matter arises from a controller's decision to acquire Spectra Energy Partners, L.P. ("SEP"), of which Plaintiff/Appellant Paul Morris ("Plaintiff") was a public unitholder. That squeeze-out transaction extinguished Plaintiff's pending derivative claim (the "Derivative Claim"), which had challenged the approval by SEP's general partner ("SEP GP") of a prior transaction in which SEP's then-controller clawed back from SEP natural gas pipeline assets worth $1.5 billion in exchange for consideration worth, at most, approximately $946 million—$554

million less than the assets' unequivocal fair market value (the "Reverse Dropdown").

On June 27, 2017, the trial court sustained Plaintiff's Derivative Claim and substantially denied defendants' motion to dismiss, finding that because SEP GP "seized ... a Partnership asset, which it knew was worth $1.5 billion, in return for a payment of less than $1 billion, it is reasonably conceivable that [SEP GP] acted in subjective bad faith."[1]

Roughly fifteen months later, however—after discovery ***bolstered*** the Derivative Claim—Plaintiff lost standing in his derivative action (the "Derivative Action") when SEP's controller squeezed out Plaintiff and SEP's other public unitholders (the "Roll-Up").[2] Thus, on February 8, 2019, Plaintiff filed the action that is the subject of this appeal (the "Direct Action").[3] In his Complaint, Plaintiff asserted a direct claim against Defendant/Appellee Spectra Energy Partners (DE)

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[1] A0776.

[2] Enbridge Inc. ("Enbridge") acquired Spectra Energy Corp. ("SE Corp") in a merger that closed on February 27, 2017, in which SE Corp became a wholly-owned subsidiary of Enbridge. At that time, SE Corp owned 75% of the outstanding units of SEP. On January 22, 2018, Enbridge and SEP announced an agreement pursuant to which the parties agreed to cancel Enbridge's 2% GP interest and rights to all future IDR distributions in exchange for the issuance of 172.5 million SEP LP units. As a result of the issuance of these new common units, Enbridge owned 83% of the outstanding LP units of SEP. A0785 at ¶2.

[3] A0020-A0080 (the "Complaint") (cited herein as ¶__).

G.P., L.P. ("Defendant" or "SEP GP"), alleging that SEP GP had breached SEP's limited partnership agreement because the committee charged with negotiating the Roll-Up—two of the three members of which were the perpetrators of the bad faith conduct that gave rise to the Derivative Claim—did not act in the best interest of SEP by deliberately failing to obtain ***any*** value for the Derivative Claim.

On September 30, 2019, the trial court granted Defendant's motion to dismiss the Direct Action upon finding that Plaintiff lacked standing to pursue a direct claim (the "Opinion" or "Op."). The trial court rejected Plaintiff's argument that he possessed standing under *Parnes* for a single reason: it determined that the value of the Derivative Claim was immaterial in the context of the Roll-Up. In doing so, the trial court acknowledged the Derivative Claim's $112+ million value to SEP's public unitholders (equal to roughly 3.4% of the Roll-Up's total value). And yet, defying Plaintiff's well-pled allegations and without discussing or analyzing any of the evidence within the limited and curated pleading-stage record, the trial court discounted the Derivative Claim's value by an arbitrary ***75%***, and deemed the claim immaterial. Plaintiff appeals that decision.

SUMMARY OF ARGUMENT

1. The trial court erred in holding that Plaintiff lacked standing to prosecute his Direct Action challenging the Roll-Up based on its determination that the Derivative Claim's $112 million value to SEP's public unitholders was immaterial as a matter of law. *Parnes* "permits a plaintiff to attack a merger directly if the target board agreed to a materially inadequate, and therefore unfair, price because the price did not reflect the value of certain assets ... [including] Derivative Claims."[4] Here, Plaintiff alleged that SEP's controller forced the Roll-Up through at an unfair price because, in approving the deal, the committee charged with negotiating the Roll-Up—two-thirds of which (including the Chairman) stood credibly accused of bad faith misconduct in the Derivative Action—did not seek or secure ***any*** value for Plaintiff's Derivative Claim. The trial court acknowledged that the Derivative Claim was meritorious. However, the trial court then applied a 75% discount to account for "the chance of success of the Derivative Claim"[5] and determined that the Derivative Claim's potential value to SEP's public unitholders was immaterial in the overall context of the Roll-Up. That decision was reversible error for three reasons:

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[4] *In re Massey Energy Co.*, 2011 WL 2176479, at *17 (Del. Ch. May 31, 2011).

[5] Op. at 33.

2. *First*, Defendant never made, and therefore waived, any argument that the value of the Derivative Claim should be discounted to account for litigation risk. To the contrary, the parties ***agreed*** that the Derivative Claim's potential value to SEP's public unitholders was approximately $112 million, or 3.4% of the value of the Roll-Up.[6] The trial court erred by rejecting this undisputed fact in the context of a motion to dismiss.

3. *Second*, in applying the 75% risk-adjustment discount to the undisputed value of Plaintiff's derivative claim, the trial court defied the standard of review applicable to the direct standing inquiry under *Parnes* and its progeny by (i) failing to draw reasonable factual inferences in Plaintiff's favor, and (ii) making a case-dispositive factual determination based on the limited pleadings-stage record that Defendant curated through a manipulated Section 220 production. Indeed, the trial court did so without even discussing or analyzing any of the evidence within the restricted pleadings-stage record.

4. *Third*, the trial court's holding undermines Delaware's well-established policy—manifested in *Parnes* and its progeny's endorsement of the right to directly

[6] As discussed *infra*, Defendant's only suggestion that the materiality analysis should involve a value ***other than*** $112 million / 3.4% was Defendant's argument that if pre-judgment interest is excluded, the value of the Derivative Claim would be $94.18 million (i.e., 2.85% of the value of the Roll-Up). A0121-A0122.

challenge the failure to obtain value for extinguished but meritorious derivative claims—of vindicating stockholder rights. Affirmance would disincentivize plaintiffs from investing the time and resources to pursue derivative claims in the context in which such actions are most critical (i.e., the controller context), and would incentivize fiduciaries to insulate themselves from derivative liability by squeezing stockholders out of their investment. This would leave any number of corporate wrongs without a remedy. Conversely, reversing the trial court will not open the litigation floodgates. Rather, reversal would merely preserve stockholders' ability under *Parnes* to secure value for already-filed, meritorious, meaningful and valuable derivative claims in the narrow subset of cases, like this one, in which minority stockholders are squeezed out by the corporate controller that faces liability on those derivative claims, which are extinguished without obtaining fair value for the minority stockholders.

STATEMENT OF FACTS

A. The Underlying Litigation

Plaintiff's cause of action in the matter below (i.e., the Direct Action) arose from his 2016 challenge (i.e., the Derivative Action), as a unitholder of a Delaware master limited partnership (i.e., SEP), to the repurchase of some of SEP's assets (the "Assets") by SE Corp, the controller of SEP's general partner (i.e., SEP GP). Plaintiff initiated the Derivative Action on behalf of SEP because SEP GP's conflicts committee approved the transaction (i.e., the Reverse Dropdown) despite SEP receiving over half-a-billion dollars ***less*** in the exchange than the Assets were worth. After Plaintiff's Derivative Claim survived a motion to dismiss, SEP's then-controller acquired SEP in the Roll-Up, thereby extinguishing the Derivative Claim. This litigation challenges the fairness of that acquisition.

1. The Initial Dropdown

Until the Roll-Up, SEP was a Delaware master limited partnership ("MLP") formed by SE Corp (the predecessor-in-interest to Enbridge) and managed by SEP GP, an SE Corp subsidiary. AA0030 at ¶16, A0032 at ¶25. In August 2013, SE Corp dropped down (i.e., sold) various natural gas pipeline assets, including the Assets, to SEP (the "Initial Dropdown"). A0069 at ¶92.

2. The Reverse Dropdown

SE Corp is a 50/50 participant with energy company Phillips 66 in a joint venture called DCP Midstream, LLC ("DCP"). DCP is a natural gas processor and producer. As of 2015, Phillips 66, DCP and SEP each owned 1/3 interests in certain natural gas pipelines known as "Sand Hills" and "Southern Hills" (SEP having acquired its 1/3 interest in the pipelines from SE Corp in the Initial Dropdown). A0034 at ¶31.

In the fall of 2015, DCP was struggling financially and needed an asset infusion. *See, e.g.*, A0036-A0037 at ¶35, A0039-A0040 at ¶¶41-42. On September 8, 2015, SE Corp and Phillips 66 jointly announced that they would each make $1.5 billion contributions to DCP (the "Matching Contributions"). A0036-A0037 at ¶35. Phillips 66 agreed to contribute $1.5 billion in cash. SE Corp agreed to "match" Phillips 66's $1.5 billion cash contribution by contributing SEP's 1/3 interest in the Sand Hills and Southern Hills pipelines (i.e., the Assets). To contribute the Assets to DCP, however, SE Corp first needed to reacquire them from SEP in the Reverse Dropdown. A0036-A0037 at ¶¶35-36. SE Corp proposed to pay for the Assets by cancelling a certain number of limited partner units and reducing its incentive distribution rights ("IDR") payouts for a three-year period. A0036 at ¶34.

SEP's limited partnership agreement (the "LPA") required SEP and any conflicts committee formed in connection with any related-party transaction to act in "good faith," which the LPA defined as "in the best interests of the Partnership." A0032-A0033 at ¶¶26-29. The SEP GP board ignored that mandate. In forming a conflicts committee to review the Reverse Dropdown on September 7, 2015 (the "Old Committee"), the SEP GP Board charged the Old Committee with negotiating a deal with the "aim" of holding SEP "net cash neutral," instead of receiving fair market value and profiting from a sale of the Assets. A0037-A0038 at ¶¶37-38 & n.10. Indeed, SE Corp's initial offer on September 8, 2018 (which included a unit redemption and reduction in IDR payments that did not substantially change over the course of the process) had the explicit "aim of holding SEP net cash neutral[.]"[7]

On October 8, 2015, the SEP GP board, upon the recommendation of the Old Committee, approved the Reverse Dropdown through which SEP agreed to transfer the Assets to SE Corp in exchange for (i) 21.56 million limited partner units (the "LP Unit Redemption"), and (ii) a reduction in IDRs payable to SEP GP of $4 million per quarter through September 30, 2018 (the "IDR Give-Back"). A0043-A0044 at ¶¶46-47.

[7] A0303.

The LP Unit Redemption and IDR Give-Back were intended not to provide SEP the full value of the Assets consistent with the Old Committee's contractual mandate to act "in the best interests of the partnership," but merely to keep SEP "net cash neutral" by keeping the total cash available for distributions to public unitholders the same following the Reverse Dropdown as would be available if the Assets stayed with SEP. A0037-A0038 at ¶¶37 & n.10, A0066-A0067 at ¶88 & n.31.

According to a final presentation provided by the Old Committee's financial advisor, Simmons & Co. ("Simmons"), the cancelled LP units had a value of $904 million based on the publicly traded price of those units. A0043 at ¶45.[8] Simmons explained that the $16 million in annual IDR Give-Backs had a present value at the time of the Reverse Dropdown of approximately $41 million. The total value of this consideration, therefore, was $946 million. A0043 at ¶45.[9] Everyone was aware, however, that the Assets had a fair market value of $1.5 billion, as evidenced by the contemporaneous Matching Contributions that SE Corp negotiated at arms-length with Phillips 66. A0036 at ¶35. Indeed, Simmons's final presentation to the Old

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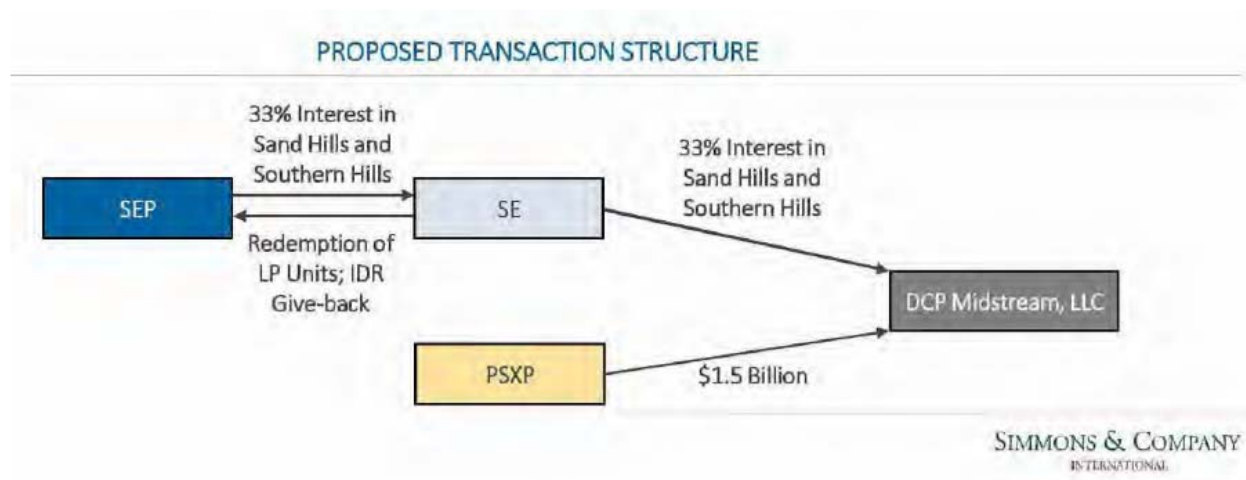
[8] *See also* A0484.

[9] *See also* A0483.

Committee graphically explained the nature of the deal, highlighting the Assets' $1.5 billion fair market value:



The Reverse Dropdown closed on October 18, 2015. On the ***same day*** that SE Corp acquired the Assets from SEP for consideration worth approximately $946 million, SE Corp contributed those very Assets to DCP in a transaction that valued those Assets at $1.5 billion.[10] In doing so, SE Corp realized an immediate windfall of roughly ***$554 million***.[11] Particularly where SEP had substantial negotiating leverage, knowingly bestowing that massive windfall on SEP's controller could not have been "in the best interests of the Partnership." A0032-A0033 at ¶¶26-29.

[10] A0346.

[11] A0346.

3. Plaintiff Commences the Derivative Action

After serving a books-and-records demand upon SEP, Plaintiff filed the Derivative Action on March 16, 2016. A0045 at ¶48.

On June 27, 2017, the trial court partially denied SEP GP's motion to dismiss the Derivative Action, finding a viable breach of contract claim because "a reasonable inference can be drawn that the [Reverse Dropdown] was made in subjective bad faith." A0046 at ¶50 (citing A0776). Specifically, the trial court held:

> Plaintiff ... has made adequate allegations showing that under reasonably conceivable circumstances a facially unreasonable gap in consideration exists sufficient to infer subjective bad faith. In other words, in authorizing a self-dealing transaction in which the General Partner seized ... a Partnership asset, which it knew was worth $1.5 billion, in return for a payment of less than $1 billion, it is reasonably conceivable that the General Partner acted in subjective bad faith.[12]

4. Discovery In The Derivative Action Confirms Defendants' Bad Faith

Although the combined value of the LP Unit Redemption and the IDR Give-Back was just $946 million, the Old Committee was well aware that, as evidenced by the contemporaneous Matching Contributions, the Assets had a fair market value of $1.5 billion. A0036-A0037 at ¶35. To bridge this glaring half-billion dollar gap

[12] A0776.

in the consideration, the Defendants in the Derivative Action pointed to something they called "Reduced GP Cashflow." A0041-A0042 at ¶44.

In its original presentation to the Old Committee, Simmons posited that SEP's cash distributions to SEP GP would decrease in perpetuity as a result of the Reverse Dropdown, and opined that the present value of that perpetual decrease was $575 million.[13] However, recognizing that the reduction was simply the inevitable mathematical consequence of removing cash-producing Assets from SEP, Simmons eliminated[14] "Reduced GP Cashflow" as an element of consideration, and its final presentation confirmed the consideration paid by SE Corp in the Reverse Dropdown included only two elements (i.e., the LP Unit Redemption and the IDR Give-Backs), which were collectively valued by Simmons at just $946 million. A0043 at ¶45.

During the Derivative Action, Defendants' premised their entire defense on their argument that "Reduced GP Cash Flow" was an incremental element of

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[13] A0333-A0334.

[14] Simmons relegated Reduced GP Cash Flow to an appendix (A0043 at ¶45, n.15; A0068 at ¶89), a step which the trial court characterized as "notabl[e]" in sustaining the Derivative Action. A0769. Indeed, the trial court later noted that Simmons "[p]erhaps recogniz[ed] th[e] reality" that Reduced GP Cash Flow "is not an element of consideration," and then "switched gears, excluding 'Reduced GP Cash Flow' from its final presentation and estimating in its fairness opinion that SEP would receive only $946 million in the transaction." A0803 (citations and internal quotation marks omitted).

consideration—i.e., that cancellation of the LP units resulted in "savings" to SEP that provided ***incremental*** consideration that was not reflected in the value of the LP Unit Redemption and constituted valid additional consideration to SEP in the Reverse Dropdown.[15] Evidence obtained in the Derivative Action, however, revealed this argument to be a mathematical fallacy.

First, SEP's LPA required the distribution of available cash through a waterfall formula. A0034-A0035 at ¶33. This formula required distribution of available cash at contractually specified distribution levels among all outstanding LP and GP units. A0034-A0036 at ¶¶33-34. Elementary school math confirms that, given the same amount of cash available for distribution, a reduction in the number of LP units would cause a corresponding ***increase*—**rather than decrease—in both the per-unit distributions and the total payments to all unitholders, including SEP GP.[16] Because standing alone, reducing the number of units through the LP Unit Redemption would ***increase*** the payments to SEP GP, the ***decrease*** in payments to

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[15] A0983-A0988.

[16] For example, $100 divided among 50 units is $2 per unit. A unitholder with 10 units would see a distribution of $20. But $100 divided among 25 units is $4 per unit. The same unitholder with 10 units would see a total distribution of $40. Lowering the denominator by redeeming units, therefore, *increases* per-unit and total distributions to individual unitholders, and higher per-unit distributions result in higher distributions to SEP GP under the waterfall mandate mandated in the LPA.

SEP GP as a result of the Reverse Dropdown was not incremental "consideration" provided by SE Corp through the LP Unit Redemption, but instead was simply the economic consequence of reducing the total cash available for distribution by removing the cash-producing Assets from SEP.

Second, SE Corp's original September 8, 2015 proposal to the Old Committee demonstrates that the LP Unit Redemption and IDR Give-Back replaced the cash flow that SEP would lose by surrendering the Assets. Critically, this analysis already accounted for "Reduced GP Cash Flow" on distributions that SEP would no longer make to SEP GP on a *pro forma* basis:

Sand Hills and Southern Hills (1/3 Interest)			
($ mil)	**Q4-15E**	**2016E**	**2017E**
EBITDA		95.1	113.2
Maintenance Capex		(1.7)	(1.7)
Taxes		(0.4)	(0.5)
Change in Cash from Customer/Credit		(3.5)	(9.0)
DCF	**$20.6**	**$89.5**	**$101.9**
Source: Q3-15 DCP Management Committee forecast.			
Growth Capex		$23.8	$25.0
Debt Funding (50%)		11.9	12.5
Equity Funding (50%)		11.9	12.5
Interest Expense(1)		(0.5)	(1.1)
Incremental Distributions(2)		(0.9)	(2.0)
Total Net Cash	**$20.6**	**$88.1**	**$98.8**
SEP Status Quo Distributions (Declared)			
LP / LP Unit	0.64	2.68	2.88
GP / LP Unit	0.23	1.03	1.23
Total / LP Unit	**$0.86**	**$3.71**	**$4.11**
LP Units Retired	20.0	20.0	20.0
Implied LP Savings	$12.8	$53.6	$57.6
Implied GP Savings	4.5	20.6	24.6
GP Giveback Schedule	4.0	16.0	16.0
Total Savings	**$21.3**	**$90.2**	**$98.2**

A0303; *see also* A0037-A0038 at ¶37, A0066-A0067 at ¶88 & n.31. As demonstrated above, the Assets would have accounted for $88.1 million of net cash flows to SEP in 2016, and those cash flows would be replaced by $90.2 million in cash-flow "savings" to SEP comprised of: (i) the cancellation of 20 million units (i.e., the LP Unit Redemption) worth $74.2 million, and (ii) the IDR Give-Back worth $16 million. The chart above clearly shows that $20.6 million of cash flows saved by the LP Unit Redemption already included "implied GP savings" (i.e.,

"Reduced GP Cash Flow")—a reduction in total distribution (including IDRs) to SEP GP. Thus, Simmons's calculation of Reduced GP Cash Flow as a separate and additional measure of consideration ***double counted*** the decreased GP distributions resulting from removing the cash-producing Assets, and improperly treated those illusory "savings" as an additional form of consideration to SEP.

Third, Defendants' arguments that SE Corp was somehow justified in paying something ***less*** than fair market value for the Assets because distributions to SEP GP were projected to ***decrease***, was contradicted by the fact that when SEP acquired the Assets from SE Corp in the Initial Dropdown, SEP paid the full fair market value for those assets even though distributions to SEP GP were projected to ***increase***. A0069 at ¶92. In other words, when SEP bought the Assets from SE Corp, it paid the full fair market value. And yet, when SEP sold the same Assets back to SE Corp, it sold them at a massive discount to fair market value.

Fourth, the suggestion that SE Corp was somehow "paying" SEP an additional over $500 million for the Assets in the form of perpetual "reduced distributions" from SEP caused by the Reverse Dropdown makes no sense. In the Reverse Dropdown, SE Corp acquired from SEP a 100% interest in the Assets. A0034-A0035 at ¶33, A0038 at ¶40. Thus, although SE Corp would no longer receive ***from SEP*** a ***fraction*** of the cash flows from the Assets, by acquiring those

same Assets through the Reverse Dropdown, SE Corp owned ***100%*** of the cash flows from those Assets. SE Corp did not "pay" "reduced distributions" to SEP. SE Corp bought 100% of the Assets.

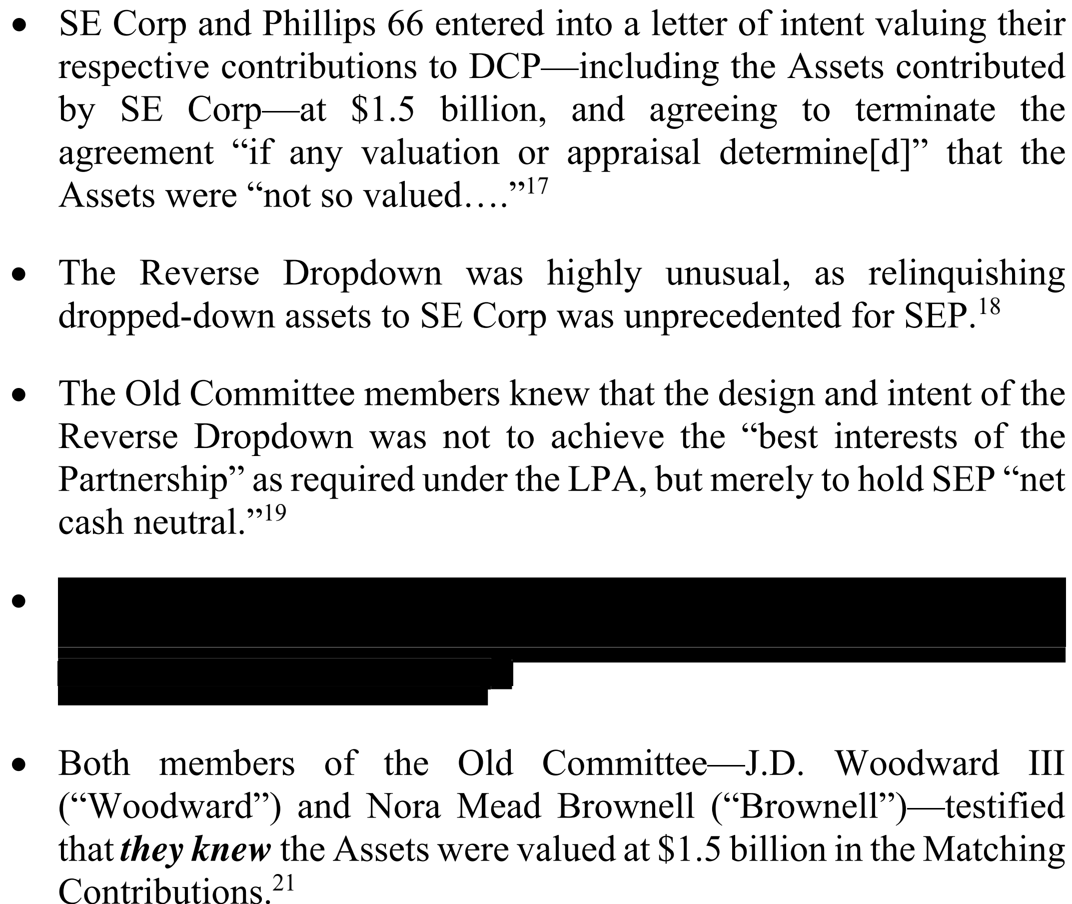
Finally, Defendant's view of Reduced GP Cash Flow is demonstrably illogical, and produces multiple absurd conclusions. For example, under Defendant's view, SEP could have given away the Assets to SE Corp or a third party ***for free***, yet would still receive over $500 million in "consideration" in the form of "Reduced GP Cash Flow." *See* A0066-A0067 at ¶88. Alternatively, SE Corp could have sold the Assets to SEP for $1.5 billion, then SEP could have sold the Assets back to SE Corp the very next day for just $1 billion, and Defendant would call both transactions "fair." The parties could then repeat those two transactions into perpetuity—transferring $500M of value to SE Corp each time—and Defendant would call all those transactions "fair" as well. Moreover, Defendant never addressed the fact that even if "Reduced GP Cash Flow" were a proper measure of consideration (it is not), then SEP could have sold the Assets to a third party at the Assets' $1.5 billion fair market value, and this $1.5 billion in consideration combined with the $500 million in purported "Reduced GP Cash Flow" would total $2 billion in consideration—$500 million ***more*** than SE Corp purportedly paid for the Assets. This makes no sense.

The discovery record also included substantial other evidence demonstrating that the Old Committee failed to act in good faith in approving the Reverse Dropdown. For example:

- SE Corp and Phillips 66 entered into a letter of intent valuing their respective contributions to DCP—including the Assets contributed by SE Corp—at $1.5 billion, and agreeing to terminate the agreement "if any valuation or appraisal determine[d]" that the Assets were "not so valued…."[17]

- The Reverse Dropdown was highly unusual, as relinquishing dropped-down assets to SE Corp was unprecedented for SEP.[18]

- The Old Committee members knew that the design and intent of the Reverse Dropdown was not to achieve the "best interests of the Partnership" as required under the LPA, but merely to hold SEP "net cash neutral."[19]



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- Both members of the Old Committee—J.D. Woodward III ("Woodward") and Nora Mead Brownell ("Brownell")—testified that ***they knew*** the Assets were valued at $1.5 billion in the Matching Contributions.[21]

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[17] A0449.

[18] A0280.

[19] A0283, A0286.

[20] A0062-A0065 at ¶¶83-85.

[21] A0285.

- In its final presentation to the Old Committee, Simmons opined that ***the value of the consideration to SEP was only $946 million***.[22]

B. The Roll-Up

On March 15, 2018, the Federal Energy Regulatory Commission ("FERC") announced plans to eliminate a tax benefit of the MLP structure (the "FERC Announcement"), triggering a significant decline in SEP's trading price. A0046-A0047 at ¶52.

On May 17, 2018, Enbridge proposed the Roll-Up to squeeze out SEP's public unitholders, offering "1.0123 Common Shares of Enbridge in exchange for each issued and outstanding publicly-held Common Unit of SEP[.]" A0048 at ¶54 (citing Enbridge Schedule 13D, filed with the SEC on May 17, 2018). That offer represented no premium to SEP's public unitholders. A0048 at ¶54.

Shortly after receiving Enbridge's offer letter, the SEP GP Board formed the New Committee to consider the Roll-Up. A0048-A0049 at ¶55. Despite their obvious conflicts given the ongoing Derivative Action through which they stood credibly accused of bad faith misconduct, the SEP GP Board appointed Woodward and Brownell (along with Michael Morris) to the New Committee, and appointed Woodward as Chairman. *Id.*

[22] A0492.

One day after Enbridge announced the Roll-Up, Plaintiff's counsel contacted the New Committee to request a meeting to discuss preserving the value of the Derivative Action for SEP's public unitholders. A0050-A0051 at ¶60. The Committee essentially ignored Plaintiff's counsel and made no attempts to independently value the Derivative Action.

Rather, shortly after the SEP GP Board formed the New Committee, Sidley Austin LLP began discussions directly with—and received information on the Derivative Action from—Skadden, Arps, Slate, Meagher & Flom LLP ("Skadden"), defense counsel in the Derivative Action. A0051 at ¶61. While the New Committee permitted Skadden to make a presentation regarding the Derivative Action to "the Committee itself" and its advisors on July 20, 2018, Plaintiff's counsel was restricted to a single call with the New Committee's advisors nearly a week later, on July 26, 2018. A0051 at ¶61, A0517. That call constituted the only substantive contact Plaintiff's counsel had with the New Committee's advisors, and Plaintiff's counsel was never permitted to directly address the New Committee.

Based on Skadden's and its own self-interested assessment of the Derivative Action (though notably, Skadden "declined to quantify [the defendant's] chances of

success" in the Derivative Action),[23] the majority-conflicted New Committee ultimately declared Reduced GP Cash Flow valid consideration in the Reverse Dropdown. A0058 at ¶74. The New Committee then declared the Derivative Action valueless to SEP aside from litigation avoidance costs. *Id.* Thus, the Committee decided that Plaintiff had a ***zero percent*** chance of recovery in the Derivative Action.

In addition to obtaining no value for the Derivative Action, the New Committee's process was flawed and failed to produce a fair exchange ratio for SEP's public unitholders. On July 17, 2018, the New Committee made its first counteroffer—an exchange ratio of 1.25 Enbridge shares for every SEP share—to Enbridge's opening offer of 1.0123x. One day later, on July 18, 2018, FERC finalized the policy change contemplated in the FERC Announcement. A0049 at ¶57.[24] Contrary to expectation, the new policy ***did not*** have the anticipated negative tax impact on MLPs (A0049 at ¶57), and thus provided a material benefit to SEP.

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[23] *See Massey*, 2011 WL 2176479 at *15 ("[T]he reality is that Cravath was the same law firm that was representing the Massey Board in defense of the Derivative Claims. It was therefore an awkward source of advice for the Board in considering what consideration, if any, to give to the Derivative Claims in negotiating the Merger. No doubt the better practice would have been for the Advisory Committee to have had its own independent counsel, Weil Gotshal, provide the Board with advice on this subject.").

[24] A0558.

FERC's change of course prompted "updated financial projections for ... the Partnership that took into account the positive impact of the July FERC Announcement," and projected long-term increases in cash flows for the partnership as compared to its projections after the FERC Announcement.[25] The news also predictably lifted SEP's trading price. A0049 at ¶57. Despite recognizing this increase in SEP's value, the New Committee did not increase its offer to Enbridge. Rather, the New Committee provided Enbridge ***decreasing*** counteroffers of exchange ratios of 1.15x, 1.13x and 1.111x, and never meaningfully asserted SEP's new projections as leverage.[26]

On August 24, 2018, SEP announced that the New Committee had approved the Roll-Up and that SEP had entered into a definitive merger agreement (the "Merger Agreement") whereby Enbridge would acquire all publicly-held SEP units at an exchange ratio of 1.111 shares of Enbridge stock—significantly ***below*** the New Committee's initial counterproposal of a 1.25x exchange ratio—for each publicly-held unit of SEP. A0049-A0050 at ¶58. The Roll-Up represented a mere 5.7% premium for SEP public unitholders based on the respective August 23, 2018 closing

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[25] A0524, A0546.

[26] A0547-A0548, A0550, A0554.

prices of Enbridge stock and SEP units, well below market averages for similar transactions.[27]

Upon approval of the Roll-Up and SEP's announcement that the parties had signed the Merger Agreement, extinguishment of Plaintiff's standing to assert the Derivative Action was a virtual certainty because: (i) Enbridge beneficially owned approximately 83% of SEP's common units; (ii) approval of the Roll-Up only required the affirmative consent of a majority of the outstanding SEP common units; and (iii) Enbridge had irrevocably agreed to support the Roll-Up.

After unsuccessfully moving to accelerate the trial date for the Derivative Action following the announcement of the Roll-Up, to avoid unnecessary expenditure of resources, Plaintiff sought Defendant's consent to stay the Derivative Action. When Defendant refused, Plaintiff filed a stay motion with the court.[28] On September 18, 2018, the court granted Plaintiff's stay motion, citing "the risk of the parties -- and the party I am most concerned with, the Court -- sinking a lot of time into this matter and having it be mooted."[29]

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[27] *See* A0296 (citing Morgan Stanley study which demonstrates that the average first-year premiums paid in seven MLP roll-up transactions over the last four years exceeded 13.5%).

[28] A0784-A0796.

[29] A0662.

The Roll-Up received a tepid response from SEP's public unitholders, who voted only 32,065,987 of the 81,907,009 publicly-held units—approximately 39%—in favor of the Roll-Up. A0050 at ¶59. The Roll-Up closed on December 17, 2018 (A0029-A0030 at ¶15), extinguishing Plaintiff's Derivative Action.

Enbridge's 83% control over SEP allowed it to force through an unfair deal, and stands in marked contrast to a substantially similar roll-up transaction that Enbridge concurrently negotiated with SEP's sister MLP, Enbridge Energy Partners, L.P. ("EEP"). Unlike the New Committee, the committee in that "most comparable"[30] roll-up of EEP (i) formed an independent subcommittee to analyze the underlying derivative action, (ii) hired independent Delaware counsel with relevant expertise to evaluate the underlying derivative action,[31] and (iii) met directly with plaintiff's counsel to discuss the underlying derivative action. A0053-A0055 at ¶¶66-67. Consistent with its vastly superior process, the EEP committee's review produced a vastly superior result, as the EEP committee valued the derivative action along a range of potential outcomes then used that assessment to negotiate significant additional value for the partnership and its public unitholders. A0028-A0029 at ¶10, A0053-A0057 at ¶¶66-71.

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[30] A0558.

[31] A0053 at ¶66.

C. Plaintiff Commences the Direct Action

Plaintiff filed this Direct Action on February 8, 2019[32] and on April 8, 2019, SEP GP filed its motion to dismiss (the "Direct Action MTD"). In its brief, SEP GP acknowledged that unless pre-judgment interest is excluded, the relevant value of the derivative claim for purposes of assessing materiality is ~$112 million, or 3.4% of the Roll-Up consideration.[33]

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[32] Before filing the Direct Action, Plaintiff served a books-and-records demand on SEP pursuant to the LPA and 6 *Del. C.* §17-305. Defendant only produced certain selected documents in response to the demand, then opposed Plaintiff's request to import the discovery record from the Derivative Action into the Direct Action. Thus, in drafting the Complaint and in contesting the Direct Action MTD, Plaintiff was limited to the documents Defendant chose to include in its books-and-records production.

[33] *See, e.g.*, A0093 **(**"Because ***3.4%*** is not material in the context of the Roll-Up transaction, Plaintiff lacks standing."); A0122 (discussing the materiality of "the 2.85% [i.e., excluding pre-judgment interest] or 3.4% [i.e., including pre-judgment interest] calculations here"). Thus, the relevant issue as briefed by the parties was whether the ***$122 million/3.4%*** value of the Derivative Claim was material. *See, e.g.*, A0122; A0234 ("[T]he value of the Derivative Action exceeds $112 million, or roughly 3.4% of the total Roll-Up Transaction value."); A0234-A0235 ("[T]his 3.4% value was material in the context of the merger." (quotations omitted)); A0235-A0238 (presenting various arguments for the materiality of the 3.4% number); A0243-A0244 (discussing the materiality of the 3.4% number); A0675 (claiming the Derivative Action "represented no more than 3.4% of the total value of the Roll-Up"); A0700-A0701, & A0700 n.66 (discussing the materiality of the 3.4% number).

Nevertheless, despite acknowledging that the derivative claim had a potential value of greater than $112 million,[34] the trial court dismissed the Direct Action solely on the basis that "[t]he potential value must be reduced to reflect … the prospect of ultimate recovery in light of the difficulties of proof inherent therein."[35] Specifically, without ***any*** analysis or discussion of the limited and curated pleading-stage evidentiary record, the trial court summarily stated that "I find that the chance of success on the Derivative Claim was slim, and certainly less than one in four."[36] Applying an unsubstantiated 75% discount to the $112 million damages number, the trial court deemed the remaining damages number immaterial.[37]

[34] Op. at 32.

[35] Op. at 3.

[36] Op. at 33.

[37] Op. at 32-33.

ARGUMENT

I. THE TRIAL COURT ERRED IN FINDING THAT PLAINTIFF LACKED STANDING TO CHALLENGE THE FAIRNESS OF THE ROLL-UP BASED ON THE NEW COMMITTEE'S FAILURE TO SECURE VALUE FOR PLAINTIFF'S DERIVATIVE CLAIM

A. Question Presented

Whether the trial court erred in concluding that Plaintiff failed to allege that the value of the Derivative Claim was material in the context of the Roll-Up such that the New Committee's failure to allocate ***any*** value to the claim resulted in an unfair price, where:

1) Defendant never contested that the potential damages in the Derivative Claim, including pre-judgment interest, exceeded $660 million, and would have represented greater than $112 million for SEP's public unitholders (approximately 3.4% of the deal price);
2) The trial court's application of an arbitrary adjustment for litigation risk contravenes the Rule 12(b)(6) standard applicable at the motion to dismiss stage, particularly given Defendant's curation of the motion to dismiss record; and
3) The dismissal of this case undermines the strong policy rationale underlying the bestowment of direct standing under the *Parnes* doctrine

and incentivizes fiduciaries to immunize themselves from derivative liability by squeezing out minority stockholders.

This issue was preserved for appeal. *See, e.g.*, A0209, A0233-A0245; A0731, A0751-0752.

B. Scope of Review

This Court's review of a trial court's grant of a motion to dismiss under Rule 12(b)(6) is *de novo*.[38]

C. Merits of the Argument

Parnes made clear that "[a] stockholder who directly attacks the fairness or validity of a merger alleges an injury to the stockholders, not the corporation, and may pursue such a claim even after the merger at issue has been consummated."[39] Applying this rule, the Court of Chancery has recognized that *Parnes* "permits a plaintiff to attack a merger directly if the target board agreed to a materially inadequate, and therefore unfair, price because the price did not reflect the value of certain assets—in this case, the Derivative Claims."[40] In *In re Primedia, Inc. Shareholders Litigation*, 67 A.3d 455, 477 (Del. Ch. 2013), the Court of Chancery provided a framework for evaluating whether a corporate board's failure to

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[38] *Brinckerhoff v. Enbridge Energy Co.*, 159 A.3d 242, 252, 261 (Del. 2017).

[39] *Parnes*, 722 A.2d at 1245.

[40] *Massey*, 2011 WL 2176479, at *17.

appropriately value a pending derivative claim would give rise to a stockholder's standing to directly challenge the consideration offered in a merger:

> First, the plaintiff must plead an underlying derivative claim that has survived a motion to dismiss or otherwise could state a claim on which relief could be granted. Second, the value of the derivative claim must be material in the context of the merger. Third, the complaint challenging the merger must support a pleadings-stage inference that the acquirer would not assert the underlying derivative claim and did not provide value for it.[[41]]

The Court of Chancery's analysis in *Primedia* makes sense and is consistent with the rule articulated by this Court in *Parnes*. "Any board negotiating the sale of a corporation should attempt to value and get full consideration for all of the corporation's material assets."[42] Where a pending meritorious derivative claim represents a potential recovery that is material in the context of the merger, a seller's board's decision to ignore the value of that claim in negotiating the merger price can result in materially unfair and inadequate consideration, giving rise to a direct claim as recognized under *Parnes*.[43] This is particularly true where, as here, the controller with the ability to force the merger and eliminate the minority faced financial liability on the derivative claim being extinguished.

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[41] *Primedia*, 67 A.3d at 477.

[42] *Massey*, 2011 WL 2176479, at *3.

[43] *Parnes*, 722 A.2d at 1245.

In the context of a claim under the LPA here, the New Committee's failure to extract ***any*** value for the Derivative Claim—and instead to knowingly confer an immediate $554 million windfall on SEP's controller—could not have been "in the best interests of the Partnership" and constituted a breach of the LPA.[44] There was no question that the Derivative Claim was meritorious: the claim had survived a motion to dismiss and, as discussed above, Defendant's only defense was premised on a mathematical lie. Defendant also conceded that (a) the New Committee failed to extract any meaningful value for the Derivative Claim, and (b) Enbridge would not pursue the claim following the Roll-Up. Indeed, as successor to SE Corp, Enbridge was incentivized to eliminate the Derivative Claim entirely, as Enbridge would have borne responsibility for any adverse ruling in that case. So the ***only*** question for purposes of a motion to dismiss under Rule 12(b)(6) is whether the Complaint articulated sufficient facts to give rise to an inference that the Derivative Claim was material, such that the New Committee's failure to secure ***any*** value for that claim constituted a breach of the LPA.

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[44] *See* A0032-A0033 at ¶¶26-29; *see also* A0186.

The threshold for pleading materiality is not high. In *Riverstone*, for example, the Court of Chancery determined that a claim valued at as little as 5% of the total merger consideration would be material under *Primedia*.[45]

The potential damages in the Derivative Action exceeded $660 million.[46] Even adjusting to account for the 83% of SEP owned by Enbridge, the Derivative Claim had a value to the public unitholders of SEP of greater than $112 million,[47] representing approximately 3.4% of the value of the $3.3 billion Roll-Up.[48]

In the M&A context, experienced corporate actors have treated amounts of around 3.4% of a transaction's value as sufficiently significant to influence conduct, i.e., to be material. For example, sophisticated parties negotiating strategic transactions typically impose termination fees, which often are less than 3.5% of the

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[45] *In re Riverstone Nat'l S'holder Litig.*, 2016 WL 4045411, at *15 (Del. Ch. July 28, 2016); *see also In re El Paso Pipeline Partners, L.P. Deriv. Litig.*, 132 A.3d 67, 117 (Del. Ch. 2015) (indicating that the plaintiff had "the stronger of the argument" on materiality "because the *pro rata* value of the Liability Award, plus interest, approximates 2.8% of the value of the Merger consideration that the unaffiliated holders of common units received"), *rev'd on other grounds sub nom.*, *El Paso Pipeline GP Company, LLC v. Brinckerhoff*, 152 A.3d 1248 (Del. 2016).

[46] Op. at 32.

[47] The $112 million figure reflects pre-judgment interest only through July 26, 2018, a date on which the trial court held a teleconference with the parties. By the time of the consummation of the transaction, an additional ~$19 million in interest had accrued.

[48] Op. 34, n.148 (acknowledging $3.3 billion value of the Roll-Up).

transaction value. "A variety of studies has shown that the median termination fees as a percentage of transaction or equity value consistently fell between 3.2% and 3.4% over the course of the last four years. Fees measured by enterprise value have been similarly stable between 3.1% and 3.3%."[49] And the Court of Chancery, in considering when termination fees become so large as to essentially be ***preclusive***, has determined that a 3.5% termination fee was "at the high end" of what would be permitted.[50] The fact that values at or around this level affect parties' behaviors demonstrates their materiality. Similarly, litigation recoveries for stockholders of far less than 3% of the value of a merger—including recoveries of just 0.5%—have been heralded by the Court of Chancery.[51]

Further, the New Committee's conduct here demonstrates the materiality of the value of the Derivative Claim. In setting the exchange ratio for the Roll-Up, the New Committee calculated it to the thousandth decimal place. In its response to

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[49] *See* A0852.

[50] *McMillan v. Intercargo Corp.*, 768 A.2d 492, 506, n.62 (Del. Ch. 2000).

[51] *See, e.g.*, A0889, A0890, A0892, A0893; A0900 (counsel referencing a 2.1% increase in merger consideration); A0948, A0949, A0950 (court indicating that the settlement was an "excellent" result, a "good, very solid recovery," and "it is apparent [to the court] that it would be unreasonable to oppose this settlement on grounds that it was insufficient to the class").

Enbridge's offer of 1.11x, the New Committee counter-offered 1.111x.[52] This strongly suggests that the New Committee recognized that .001x—equating to an increase in value for the public unitholders of about $3.8 million—was material.[53]

In the proceedings below, the parties never disputed that, including pre-judgment interest, the Derivative Claim represented a potential recovery of 3.4% of the value of the Roll-Up, or greater than $112 million for the public unitholders of SEP. And in its decision, the trial court itself did not contest that the 3.4% value represented by the Derivative Claim was material in the context of the Roll-Up. Instead, the trial court improperly applied a 75% "litigation risk" discount for which it had no basis. Without discussing any underlying evidence and in contravention of its pleadings-stage duty to draw factual inferences in Plaintiff's favor, the trial court simply concluded that whatever the evidence might show, Plaintiff's underlying claim—which had survived a motion to dismiss, and for which a liability finding would indisputably[54] entitle Plaintiff to the ***full*** damage amount—should be

[52] A0553-0554.

[53] A0553-0554.

[54] *Compare* A0122 n.12 *to* A0146-A0147 (referring to the "all-or-nothing proposition" and "binary premise" of Plaintiff's claim that "Reduced GP Cash Flow could not be valuable to the Partnership").

massively discounted. This Court should reverse the trial court's decision for several reasons.

1. In Discounting the Value of Plaintiff's Derivative Claim the Trial Court Endorsed an Argument that Defendant Waived, and Deviated from the Factual Predicate Presented by the Parties to the Trial Court

It is an established rule of Delaware law that arguments not briefed by the parties are waived.[55] In its motion to dismiss briefing before the trial court, Defendant never argued that the trial court should discount the $112 million value of the Derivative Claim through a risk-adjusted valuation analysis.[56] Indeed, Defendant's arguments revolved around—and cited—Plaintiff's $112 million / 3.4% damages figure (or, at a minimum, $94.18 million or 2.85% if pre-judgment

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[55] *See, e.g.*, *Emerald v. Berlin*, 726 A.2d 1215, 1224 (Del. 1999) ("Issues not briefed are deemed waived."); *Ark. Teacher Ret. Sys. v. Alon USA Energy, Inc.*, 2019 WL 2714331, at *16 n.92 (Del. Ch. June 28, 2019) (holding that defendants waived Rule 12(b)(6) arguments with respect to certain claims by failing to brief them); Sup. Ct. R. 8 ("Only questions fairly presented to the trial court may be presented for review"); *see also Plummer v. Sherman*, 861 A.2d 1238 (Del. 2004) (reversing a trial court decision because the court considered a personal jurisdiction argument that the defendant had waived).

[56] *See supra* Statement of Facts at 25 & n.33.

interest were excluded). In doing so, Defendant waived any argument for a risk-based discount to that number.[57]

Even though Defendant never argued that Plaintiff's damages calculation should be reduced to reflect litigation risk, the trial court nevertheless applied such a reduction *sua sponte*. By deciding—without discussion or apparent analysis of any evidence—to apply a 75% discount to the Derivative Claim's agreed-upon value, the trial court decreased the value to less than 1% of the value of the Roll-Up, which the trial court deemed immaterial under *Primedia*.

For this independent reason, the Court should reverse the trial court's decision.

2. The Trial Court's Discounting Exercise Contravenes the Rule 12(b)(6) Standard Applicable to the Direct Standing Inquiry Under *Parnes* and *Primedia*

When evaluating at the pleadings stage whether a stockholder may assert a direct claim for failure to obtain value of an underlying derivative claim, the trial court applies the Rule 12(b)(6) standard. As a consequence, the court is required to

[57] *See Seaport Village Ltd. v. Terramar Retail Centers, LLC*, 148 A.3d 1170 (Table) (Del. 2016) (acknowledging that an "argument not fairly presented to the Court of Chancery in the plaintiff's trial briefs below [] is waived").

"accept all of [the plaintiff's] factual allegations as true and give her the benefit for all inferences that may be drawn from these facts."[58]

Because the trial court must accept all well-pled allegations as true and give the plaintiff the benefit of all reasonable inferences drawn therefrom, it is incongruous at best to reduce the value of a claim on the basis that the plaintiff's allegations have not been proven within the four corners of the plaintiff's complaint, and therefore carry risk. This is particularly true where, as here, the trial court has already properly recognized that Plaintiff's Derivative Claim was viable.

Here, the trial court's decision to conduct a pleadings-stage discounting exercise is particularly prejudicial because of the limited, skewed record available to the court. The evidentiary record on which the trial court ruled was plainly incomplete: Defendant only produced a limited set of documents in response to Plaintiff's books-and-records demand, and then rejected Plaintiff's request to import the full discovery record from the Derivative Action into the Direct Action. Thus, the evidence available to the trial court consisted of documents hand-picked by Defendant (which "evidence" the trial court did not even discuss or analyze in

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[58] *Parnes*, 722 A.2d at 1247 (citing *In re Tri-Star Pictures, Inc.*, 634 A.2d 319 (Del. 1993)); *In re Straight Path Commc'ns Inc. Consol. S'holder Litig.*, 2018 WL 3120804 (Del. Ch. June 25, 2018) (referring to the standard applicable in a motion to dismiss on the basis that a derivative claim has been extinguished, and citing *Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 894-97 (Del. 2002)).

applying its 75% discount). Attempting to divine the fate of the underlying claim—and therefore to reject a large swath of the value of an admittedly viable claim on which a finding of liability would entitle Plaintiff to the ***full*** damages amount—on a substantially incomplete and one-sided record effectively permits corporate defendants to manipulate the courts to immunize themselves.

For example, the trial court apparently determined that it would be difficult for Plaintiff to establish scienter, yet the procedural posture foreclosed Plaintiff from presenting the evidentiary record from the Derivative Action, much less pursue discovery in this case. Perhaps more strikingly, none of the relevant facts underlying the trial court's conclusion in this case appear to have played any role in its decision. Indeed, the trial court reaffirmed that whether Reduced GP Cash Flow was a false and illusory construct is "a litigable question,"[59] but nevertheless seems to have merely divined and applied an arbitrary one-in-four chance of success to Plaintiff's Derivative Claim.

It is notable that this Court has never endorsed a predicted risk-based discounting exercise in connection with determining whether a plaintiff has direct standing under *Parnes*. Nor should it. Such an exercise is fraught with hazards, as it requires the trial court to prematurely engage in an analysis of the prospects of a

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[59] Op. at 32.

case in which the facts have not been fully discovered or presented. Indeed, as here, in selectively producing documents pursuant to a books-and-records demand, the defendant can curate a pre-discovery, pleadings-stage record upon which the trial court would make a fact-intensive determination regarding the derivative claim's ultimate likelihood of success. The trial court's determination essentially becomes dispositive, allowing an arbitrary and/or highly defendant-friendly assessment of risk to decide whether stockholders' claims go forward and, therefore, whether corporate defendants are ever held accountable.

The Court of Chancery has only ever engaged in such an exercise where the factual circumstances were categorically different. For example, in *Massey* but not here, substantial collection issues and affirmative harm to the company resulting from the successful prosecution of the derivative claim that the plaintiff sought to prosecute directly led the court to conclude that it would have defied "economic reality" to prosecute the claims through trial.[60] Indeed, Defendant in this case conceded below that "*Massey* focused on the $95 million D&O insurance policy ... and regulatory risks presented by that derivative litigation."[61] For these unique and

[60] *Massey*, 2011 WL 2176479, at *24.
[61] A0702.

case-specific reasons, the *Massey* court considered the predicted risk of the litigation.[62]

3. Policy Reasons Strongly Militate Against the Discounting Exercise Undertaken by the Trial Court

Delaware courts have recognized that permitting certain meritorious direct claims for failure to value an extinguished derivative claim serves essential interests under Delaware law.[63] In the absence of such direct standing, stockholders would be foreclosed from vindicating their rights and corporate wrongdoers would remain free to engage in wrongful conduct harmful to the company and its stockholders, secure in the knowledge that the accomplishment of a merger would extinguish any claims and thereby immunize themselves from liability.[64]

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[62] Notably, *Primedia* itself did not state that the trial court must engage in any sort of risk-adjusted analysis by discounting the damages based on predictions about the outcome of the claim. Instead, the *Primedia* court merely noted that ***if*** one were to take the same approach as in *Massey* and adjust the claims at issue on the basis of risk, the value of the damages would still be material. *Primedia*, 67 A.3d at 483.

[63] *Primedia*, 67 A.3d at 476-77.

[64] *See In re El Paso Pipeline Partners, L.P. Deriv. Litig.*, 132 A.3d 67, (Del. Ch. 2015), *rev'd on other grounds El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248 (Del. 2016) ("At the same time, the risk that a plaintiff will invest resources in a viable claim only to lose standing through a merger disincentivizes stockholders from engaging in monitoring under circumstances where it is already 'likely that in a public corporation there will be less shareholder monitoring expenditures than would be optimum from the point of [view of] the shareholders as a collectivity.'" (quoting *Bird v. Lida, Inc.*, 681 A.2d 399, 403 (Del. Ch. 1996))).

Any trial court considering the prospects of a claim that is still in a stage of litigation infancy seems unlikely to assign to it anything greater than a 50% chance of success. Thus, even assuming full damages, the application of a risk-based adjustment to the damages figure would inevitably result in a drastic reduction in the value of the underlying derivative claim, making it substantially more difficult—if not nearly impossible—to establish materiality in relation to the value of an entire transaction. Such an approach would largely eradicate the availability of direct standing under *Parnes*, thereby fundamentally undermining the purpose for this Court's decision to establish that limited exception to the extinguishment of standing where a controller squeezes out minority stockholders.[65]

Simply put, affirming the trial court's discounting approach would strip away a critical judicial safeguard. It would turn upside down Delaware law's recognition that in certain limited circumstances, stockholders must be able to vindicate their right to challenge the fairness of a self-serving transaction that extinguishes their derivative claims. Such a decision would encourage controllers, as well as the

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[65] *See Hamilton Partners, L.P. v. Englard*, 11 A.3d 1180, 1206 (Del. Ch. 2010) ("If derivative actions promote firm value, even marginally, then a rule that forecloses some number of both meritorious and meritless derivative actions will, all things being equal, inherently transfer some degree of wealth from corporations to the individuals who commit corporate wrongs. The resulting wealth transfer confers a windfall on the faithless fiduciaries and creates perverse incentives for misbehavior.").

boards of the controlled companies, to immunize themselves from meritorious derivative claims by squeezing out stockholders. The Court should reverse the trial court's decision and thereby avoid ratifying such dangerous incentives.

Finally, reversing the trial court would in no way open the litigation floodgates. To the contrary, in the limited subset of cases where a controller squeezes out minority stockholders with viable and valuable pending derivative claims, reversal would merely preserve those stockholders' ability to secure value for those meritorious claims.

CONCLUSION

The trial court's Order Granting Motions to Dismiss, dated October 25, 2019, should be REVERSED.

Dated: January 7, 2020

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