IN THE SUPREME COURT OF THE STATE OF DELAWARE

C.A. No. 12871-CS

D.C. Docket No. 17-123-XXX-XXX

SIERRA GP LLC, SIERRA RESOURCES, INC., THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., SARAH W. BRYANT, ROBERT P. GRAY, RICHARD T. HANSON, ELIZABETH F. PRINCE, and JOHN W. REYNOLDS,

Defendant-Appellant,

v.

NORTH CAROLINA POLICE RETIREMENT FUND, individually and derivatively on behalf of SIERRA PROPERTIES LP,

Plaintiff-Appellee.

Appeal from the Court of Chancery of the State of Delaware

BRIEF FOR THE APPELLEE

Attorneys for Appellee

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I. NATURE OF PROCEEDINGS

Appellee, the North Carolina Police Retirement Fund ("NCPRF"), on behalf of Sierra LP, filed a complaint against Sierra Resources and Sierra GP ("Entity Appellants") and The Bank of New York Mellon Trust Company, N.A. ("BNY Mellon") on January 20, 2016. R. 1, 2, 8. Appellee argued that the "dead hand proxy put" in section 11.01 of Sierra LP's Indenture is invalid because Sierra Resources failed to demonstrate adequate care when it approved of the clause. R. 1-3. Entity Appellant filed a motion to dismiss the complaint arguing that the "dead hand proxy put" served an adequate business purpose and that it did not owe a fiduciary duty to Sierra LP and NCPRF. *Id.*

Additionally, Entity Appellant independently alleged that Sierra Resources' board of directors did not owe Sierra LP any fiduciary duties. R. at 3. Sierra Resources' board members—Sarah W. Bryant, Robert P. Gray, Richard Hanson, and Elizabeth F. Prince, and John W. Reynolds ("Individual Appellants") filed a motion to join Entity Appellants' motion to dismiss. *Id.* at 1.

The Court of Chancery considered Entity Appellant's motion to dismiss as a motion for summary judgment because Entity Appellant included matters not alleged in the initial complaint. R. at 1. Pursuant to Court of Chancery Rule 12(b), the court gave Appellee the opportunity for discovery and both parties subsequently agreed that no genuine issues of material fact existed. *Id.* The Court of Chancery denied Entity Appellant and Individual Appellant's (hereinafter, collectively "Appellant") motions to dismiss and granted Appellee's motion for summary judgment on January 9, 2017. R. at 1.

II. SUMMARY OF THE ARGUMENT

The Indenture agreement is *per se* invalid because it is not entirely fair to Sierra LP and NCPRF. This Court cannot evaluate the Indenture under *Unocal*'s enhanced scrutiny standard because Sierra Resources asserted that it did not know that the agreement contained the "dead hand proxy put" clause. Thus, Sierra Resources did not have "reasonable grounds" for including the clause in the agreement. Moreover, because Sierra Resources was on "both sides" of the Indenture—benefiting by raising capital for re-investment while also controlling how Sierra GP managed the capital—this court is required to apply the "entire fairness" scrutiny standard.

Sierra Resources may not insulate itself from its fiduciary duties to Sierra LP by claiming that it was unaware that the "dead hand proxy put" was included in the Indenture. In a recent line of Delaware cases, courts put corporations and general partnerships on notice that "dead hand" clauses are contentious given its adverse effects on shareholders' investments.

Sierra Resources owed fiduciary duties to Sierra LP because Sierra Resources was the sole member and manager of Sierra GP and exercised exclusive control over Sierra LP. *See* R. 4. Appellant may argue that it is not accountable because it did not "intentionally" act to benefit itself to the detriment of Sierra LP. However, this Court should not give credence to such assertion because Sierra Resources' negotiated and approved the Indenture.

III. Statement of the Facts

In 2008, NCPRF and Sierra Resources entered into a joint venture in real estate development, creating Sierra LP, a limited Delaware partnership, as the investment vehicle. R. 4. NCPRF contributed $80 million in capital and Sierra Resources contributed $20 million. *Id.* Sierra LP's sole general partner was Sierra GP and Sierra GP's sole member and manager was Sierra Resources. R.3. Sierra GP owned 20% of Sierra LP's interest; NCPRF owned an 80% interest. *Id.* In 2013, Sierra Resources and Sierra GP realized that Sierra LP was underleveraged and decided to raise new capital by debt financing. R. 5.

By August 15, 2013, Sierra LP raised $160 million by selling 2% Notes in a public debt offering. R. 5. After Morgan Stanley, the lead underwriter to the agreement, drafted the Indenture, both Sierra LP and Sierra Resources' counsel reviewed the agreement and made comments and edits. *Id.* The critical clause at issue, Section 11.01's "dead hand proxy put" provision, remained untouched during revisions. *Id.* On August 16, 2013, Sierra GP and the 2% Noteholders agreed to the Indenture, to be due in August 2028—a total term of fifteen years. R. 2. The final Indenture agreement included Section 11.01, which allowed the 2% Noteholders to redeem the principal and accrued interest when a "Change of Control" occurred. *Id.* Section 11.01 states that a change of control occurs when:

> "(a) the General Partner is removed pursuant to Section 7.2 of this Indenture, or (b) during any period of 12 consecutive months, a majority of the members of the board of directors or other equivalent governing body of the Parent [Sierra Resources' cease[s] to be composed of individuals (i) who were members of that board or equivalent governing body on the first day of such period, (ii) whose

> election or nomination to that board or equivalent governing body was approved by individuals referred to in clause (i) above constituting at the time of such election or nomination at least a majority of that board or equivalent governing body was approved by individuals referred to in clauses (i) and (ii) above constituting at the time of such election or nomination at least a majority of that board or equivalent governing body (excluding, in the case of both clause (ii) and clause (iii) any individual whose initial nomination for, or assumption of office as, a member of that board or equivalent governing body occurs as a result of an actual or threatened solicitation of proxies or consents for the election or removal of one or more directors by any person or group other than solicitation for the election of one or more directors by or on behalf of the directors).

The "dead hand proxy put" of Section 11.01 is the underlined section above. R. 2. While Sierra Resources and Sierra GP did not eliminate or alter Section 11.01 during the drafting period of the Indenture, neither advocated for its inclusion. *Id.*

Sierra LP and Sierra Resources' hired counsel for the Indenture transaction testified in a deposition that they never discussed Section 11.01 with Morgan Stanley. *Id.* A director on the finance committee of Sierra Resources' board asked counsel if "there were any novel terms that required attention from the committee or the board." *Id.* Counsel for Sierra Resources responded "no." R. 6.

During the negotiating period of the Indenture, Sierra Resources was unaware of any activist hedge fund's intentions to obtain an equity position in the company. However, shareholder activism was a common and well-known occurrence in the real estate industry. *Id.* In 2013, Corvex Management conducted a widely reported and successful takeover that changed the business strategy of a publically-traded investment trust, Common Wealth REI, and the composition of its trustees. *Id.* On October 12, 2015, two months after Sierra Resources completed the Indenture, an

activist hedge fund, High Street Partners, LP ("High Street") acquired a 6.3% equity interest in Sierra Resources. R. 6.

High Street proposed a new business strategy for Sierra Resources and stated that if Sierra Resources' board failed to implement High Street's proposed strategy, High Street would hold contested proxies to replace the Sierra Resources' directors. R. 6. Both parties accept that this case is ripe for review. R. 7. n.3. Sierra Resources stated in press releases and investor presentations that the election of High Street's nominees to a majority of the board would trigger the "dead hand proxy put" in Sierra LP's indenture. When triggered, the "dead hand proxy put" would financially cripple Sierra LP. R. 7. Sierra Resources conceded that the impact to Sierra Resources would be immaterial. *Id.*

I. APPELLANT FAILED TO EXERCISE ADEQUATE CARE WHEN AGREEING TO THE "DEAD HAND PROXY PUT" IN SECTION 11.01 OF THE INDENTURE.

A. Questions Presented

1. Did Sierra Resources have "reasonable grounds" for including the "dead hand proxy put" in the Indenture, even though it did not that the Indenture included the "dead hand proxy put?"
2. Did Sierra Resources and Sierra GP agree to an Indenture that was "entirely fair" to Sierra LP and the NCPRF?
3. Did Sierra Resources take action as a fiduciary to Sierra LP when it hired outside counsel to negotiate a fifteen-year Indenture agreement, in an industry prone to takeovers, with terms that had the potential to decimate Sierra LP?

B. Scope of Review

Reviewing a trial court's decision to apply an enhanced scrutiny standard to a board's action is a question of both law and fact. *RBC Capital Markets, LLC v. Jervis*, 129 A.3d 816, 849 (2015). When reviewing questions of fact, this Court must apply the "clearly erroneous" standard. *Id*. If the trial court permissibly interprets the facts in one way instead of another permissible way, the factfinder's decision is not clearly erroneous. *Id.* In contrast to questions of fact, this Court reviews *de novo* the Court of Chancery's legal conclusions. *Id.*

C. Merits of the Argument

1. Appellant Did Not Have "Reasonable Grounds" For Including Section 11.01 In the Indenture Agreement

Where a shareholder files suit against a director's action, "usually one of three levels of judicial review is applied: the traditional [business] judgment rule, the *Unocal* standard of enhanced judicial review, or the entire fairness analysis." *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361, 1371 (Del. 1995). The business judgment rule derives from the fundamental understanding of corporate law that "the business and affairs of a Delaware corporation are managed by or under its board of directors." *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (overturned on other grounds by *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009)); *see also* Del. Code Ann. tit. 8, § 141(a) (2016).

A board of directors is "charged with an unyielding fiduciary duty to the corporation and its shareholders." *Van Gorkom*, 488 A.2d at 872. The business judgment rule operates under the "presumption that in making a business decision, the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Unocal*, 493 A.2d at 954 (quoting

Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)). Unless such presumption is rebutted, the business judgment rule does not permit a court to "substitute its judgment for that of the board if the latter's decision can be 'attributed to any rational business purpose.'" *Id.* (quoting *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971)).

While affirming the presumption that a board makes its decisions in good faith and with an honest belief, the *Unocal* court also highlighted the inherent conflict of interests prevalent during a takeover situation. *Id.* at 954. A conflict of interest arises during a takeover situation because a board must act in the best interests of its shareholders while also being driven to act in a manner most amenable to the newly controlling takeover corporation. *See id.* Acknowledging such conflict, and in order to ensure that a board continues to act in the best interests of its shareholders, *Unocal* established a heightened standard for scrutinizing transactions. *Id.* The heightened *Unocal* standard requires directors who take defensive measures in the context of a takeover to show how such measures were based on "reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership." *See id.* at 955-54; *see also Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989) ("[D]irectors are required to demonstrate both their utmost good faith and the most scrupulous inherent fairness of transactions in which they possess a financial, business or other personal interest which does not devolve upon the corporation or all stockholders generally.").

The Appellants agreed to the Indenture in the shadow of a potential takeover situation. R. 6. Although there was "no indication specific to

Sierra Resources that any person was planning an election contest . . ." it was commonly accepted that "the phenomenon of shareholder activism was well known in the real estate industry." *Id.* Such phenomenon was particularly apparent around the time Sierra LP's Indenture was signed because a recently successful and widely reported takeover of a publically traded real estate investment trust—similar in structure to Sierra LP—had just occurred. *Id.* Given the prevalence of activist hedge funds within the industry, and the extended length of the Indenture's term, which dramatically increased the probability that Sierra Resources would be subject to a takeover, this Court can reasonably conclude that the conflict of interest concerns highlighted in *Unocal* are similarly present in this case.

Here, upon beginning negotiations for an Indenture agreement, the board was incentivized to entrench its position to prevent usurpation in the foreseeable instance of a takeover. Entrenchment conflicts with a shareholder's best interests because by agreeing to a "dead hand proxy put," shareholders are realistically prevented from holding elections: Holding elections during a contested proxy triggers the Change of Control clause the Noteholders can redeem their investment. *See San Antonio Fire & Police Pension Fund v. Amylin Pharmaceuticals Inc.*, 983 A.2d 304, 319 (Del. Ch. 2009) (discussing the consequences of entrenchment on shareholders' interests).

However, this Court may not apply the enhanced scrutiny standard in *Unocal* because the Appellant claims that it was unaware of the existence of the "dead hand" component of the clause. In other words, the board cannot justify its decision to take the defensive measure—

including the "dead hand" provision—because the board was unaware of the clause's inclusion in the agreement. R. 9-10. Given that neither the traditional business judgment standard nor the enhanced *Unocal* standard can be used to evaluate the board's inclusion of the "dead hand" provision, this Court must determine whether or not the indenture was "entirely fair" to Sierra LP.

2. Section 11.01 is Invalid Because It Does Not Meet the Standard of Entire Fairness.

When a board fails to establish "reasonable grounds" for a defensive measure, the business judgment rule is rebutted and the burden shifts to the board to show how the transaction was "entirely fair." *Shamrock Holdings, Inc. v. Polaroid Corp.*, 559 A.2d 257, 271 (Del. Ch. 1989) (applying the entire fairness standard to an Employment Stock Ownership Plan). When directors of a corporation are on both sides of the transaction, as in the context of a parent-subsidiary relationship, the board "is required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain." *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983). In a parent-subsidiary scenario, showing that the transaction was the product of each contending party exerting its bargaining power at arm's length presents "strong evidence" that the agreement was entirely fair. *Id.* at 715 n.7.

Fairness typically has two aspects: 1) fair dealing, and 2) fair price. *Id.* at 711; *see also Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d at 1280. Fair dealing considers "when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approval of the directors and the stockholders were obtained." *Weinberger*, 457 A.2d at 711. Whether a judgment was made at

a fair price "relates to the economic and financial considerations . . . including all relevant factors assets, market value, earnings, future prospects, and any other elements that affect the intrinsic of inherent value of a company's stock." *Id.* Entire fairness considers the components of price and dealing as whole; however, where fraudulent activity is not alleged, price outweighs other factors in the determination. *Id.*

The parties to the Sierra LP's Indenture did not engage in the sort of arm's length negotiation that tends to show entire fairness. R. 5. Rather, counsel for the parent—Sierra Resources—and the subsidiary—Sierra LP—worked jointly to draw up the terms of the Indenture. *Id.* Sierra Resources stands on both sides of the transaction: on one side, Sierra Resources is profiting indirectly by raising new debt capital for re-investment, and on the other side, Sierra Resources is controlling Sierra LP through Sierra GP's board of directors. R. 3-5.

The Appellants failed to show that the board's approval of the Indenture containing the "dead hand proxy put" provision was entirely fair to Sierra LP. Sierra Resources acted as the sole member and manager of Sierra GP, in a "dual capacity as directors of two corporations," and thus, "owe[d] the same duty of good management to both corporations," which must "be exercised in light of what is best for both companies." *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (1983). Sierra Resources did not exercise its obligation of good management equally to Sierra LP as it did to itself because while Sierra Resources obtain two substantial benefits from the agreement—entrenchment and capital—Sierra LP incurred a severely defensive regulation that could implode at any point upon a showing of interest from an activist hedge-fund.

The proffered affidavit by Morgan Stanley indicating that if Section 11.01 were not included in the agreement, the interest rates on the Notes would have been 'up to 50 basis points' higher than 2%, is insufficient evidence to satisfy "the test of careful scrutiny by the courts." *Sterling v. Mayflower Hotel Corp.*, 33 Del. Ch. 293, 298 (Del. 1952); R. 5, 9. While the interest rates on the Notes may have been higher if the "dead hand" component of Section 11.01 was not included, such a hypothesis is uncertain and not supported by any of the quantitative assessments necessary to demonstrate "fair price." *See Weinberg*, 457 A.2d at 711. In stark contrast to such speculative increase in interest rates stands the admitted consequences of a triggered Change of Control provision upon Sierra LP. *See* R. 9-10. Moreover, the fact that the Indenture had a long term of fifteen years incrementally escaladed the likelihood that Section 11.01 would be triggered given the nature of the real estate industry. *See* R. 6. Sierra Resources did not exercise good management, or "fair dealing," because it negotiated the Indenture under the pretenses that if Sierra LP ever failed, Sierra Resources would always be able to—as it did—cut its loses without considerable injury to itself.

3. Appellant May Not Insulate Itself from Fiduciary Duties by Delegating Authority to Outside Parties and by Remaining Ignorant of the Contents of an Agreement It Signed.

A board may not avoid fiduciary duties to its stockholders by remaining ignorant of the terms in a negotiated indenture agreement. *See Amylin Pharmaceuticals Inc.*, 983 A.2d at 319. As highlighted by this Court, *Amylin* serves as a recent example for how Change of Control clauses within debt agreements should be interpreted and what fiduciary

duties are implicated by "dead hand" provisions contained within such agreements. *North Carolina Police Retirement Fund v. Sierra GP LLC*, Del. Ch., C.A. No. 12871-CS, Snyder, C. (Jan. 9, 2017) (Mem. Op.). Both in *Amylin*, as in here, the board of directors were unaware of the inclusion of a Change of Control provision within its debt agreements; however, the differences in the actual terms of agreements clarify why Sierra Resources, but not Amylin corporation, not only acted as a fiduciary, but also broke its fiduciary duty.

In *Amylin*, the court reviewed the two agreements entered into by Amylin corporation: 1) a credit agreement signed with Bank of America, N.A. ("BANA"), in December 2007, for $140 million total credit facilities, expiring in December 2010, and containing a "two-year sliding look back"; and 2) an indenture agreement issued in 2007, for 3.00% Notes, due in 2014. *Amylin*, A.2d at 308-10; Answering Brief of Defendant Below, Appellee Bank of America, N.A. at 7, *San Antonio Fire & Pension Fund v. Amylin Pharmaceuticals, Inc.*, C.A. No. 4446-VCL, (July 8, 2009). The credit agreement in *Amylin* contained a Change of Control provision identical to the Section 11.01 clause negotiated on behalf of Sierra LP. *See Amylin*, A.2d at 309. Separately, the indenture agreement in *Amylin* was similar to the indenture in Sierra LP; however, the indenture in *Amylin* did not contain a "dead hand" clause. *See id.* at 308.

The fact that the indenture in *Amylin* did not have a "dead hand" provision meant that Amylin's board could avoid triggering the "Continuing Directors" clause. *Id.* at 314. The *Amylin* court highlighted that if the board could not "approve" of the dissident slate while also "endorsing" its own slate, the Continuing Directors clause would have

such eviscerating effects on the shareholders' franchise that it would call into question whether or not the corporation had met its obligations as a fiduciary in agreeing to the stated terms. *See Amylin*, A.2d at 308-10. The court noted that if the board could not prevent triggering the Continuing Directors clause, the board would need to show that it "believed in good faith that, in accepting such a provision it was obtaining in return extraordinary valuable economic benefits for the corporation that would not otherwise be available to it." *Id.* at 315. Moreover, the Court noted that it would be required to consider whether such a provision "might be unenforceable as against public policy." *Id.*

The rejected interpretation of the Continuing Directors provision in *Amylin* is the Change of Control provision included in Sierra LP's indenture. *Id.* Here, Sierra GP is unable to prevent triggering the Change in Control clause, which consequently has 1) eviscerating effects on Sierra LP, 2) does not portend to be the product of any fair exchange exuding an enormous economic benefit for Sierra LP, and 3) raises public policy concerns related to entrenchment and the unescapable loss of shareholders' investments. *See* R. 6-7 (discussing how triggering the "dead hand" Change of Control clause will have severe consequences on Sierra LP).

Appellant might improperly seek to compare the enforceable credit agreement in *Amylin*, which contained a "dead hand" provision, to Sierra LP's indenture agreement; however, such a comparison would be misguided. In *Amylin*, BANA agreed to waive its rights to redeem its debt under the Continuing Directors provision for a fee in the event that the contested proxy elections triggered the provision. *Amylin*, 983 A.2d at 312. Unlike

in private lending situations, a waiver or consent in the context of an indenture agreement—or a public debt instrument—is not similarly obtainable. *Id.* at 14 n.30. Another difference between *Amylin*'s credit agreement and Sierra LP's Indenture is that Amylin's credit agreement contained a "two-year sliding look back," which allowed "non-continuing directors" to become "continuing directors" after two years. *Amylin*, 983 A.2d at 314. "Non-continuing directors" in Sierra LP's indenture remained so for the entire term of the Notes. *Id.* The "dead hand" provisions in *Amylin*'s credit and indenture agreements do not contain the same acutely defensive terms as does Sierra LP's indenture.

Unlike in *Amylin*, here, mitigating the consequences of accidentally including a Change of Control provision is not possible like in *Amylin*—Sierra LP will not be able to obtain a waiver from its Noteholders, its "non-continuing directors" will never become "continuing directors," and approving of dissident nominees will not prevent triggering the "dead hand proxy put." *Amylin*, A.2d at 314. Sierra Resources broke its fiduciary duty to Sierra LP and NCPRF because it entered into a more restrictive agreement compared to the debt agreements addressed in *Amylin*, whereby the consequences of the Change of Control provision in Sierra LP's indenture are unescapable.

A board cannot take a secondary role in negotiations in order to isolate itself from its duties as a fiduciary to its shareholders. In *RBC Capital Markets, LLC v. Jervis*, the court found a corporation's financial advisor guilty of aiding and abetting the breach of duty of care committed by the board during the sale of the company. 129 A.3d 816, 853-54. Although the court in *RBC Capital Markets, LLC* acknowledged

the harmful role the financial advisor played in the sale, the court highlighted the lack of oversight by the board and its failure to takes "steps to address or mitigate RBC's conflicts." *Id.* at 30. The court noted that "[w]hile a board may be free to consent to certain conflicts . . . directors needs to be active and reasonably informed when overseeing the sale process."

Even more, while acknowledging a board's use of professional third parties, the court warned, "in change of control situations, sole reliance on hired experts and management can 'taint the design and execution of the transaction.'" *Id.* at 855 (quoting *Citron v. Fairchild Camerica & Instrumental Corp.*, 569 A.2d 53, 66 (Del. 1989)). During change of control situations, the court looks "particularly for evidence of a board's active and direct role in the sale process." *Id.* Here, Sierra Resources did not take a direct role in the indenture negotiations, which led to an oversight at the expense of Sierra LP.

Sierra Resources should have been especially conscious of the possibility of a Change of Control provision within an indenture given the industry the fund engages in and the extended length of the debt's term, which would commit Sierra LP to the contract for several years. Sierra Resources should have known that "dead hand" provisions can have crippling effects on an investment fund, and should have been stringently attentive to the terms within that specific area of the agreement. *See Pontiac General Employees Retirement System v. Healthways, Inc.*, C.A. No. 9789-VCL at 80 (Del. Ch. Oct. 14, 2014) (transcript ruling) (refusing to grant a defendant's motion to dismiss over the inclusion of a "dead hand proxy put," asserting that "[t]here was ample precedent

from this Court putting lenders on notice that these provisions were highly suspect and could potentially lead to a breach of duty on the part of the fiduciaries who were the counterparties to a negotiation over the credit agreement."). Although the *Amylin* court acknowledges that "no one suggests that the directors' duty of care requires them to review, discuss, and comprehend every word of the 98-page Indenture," this court should hold the board responsible, specifically, for not reviewing the section of the contract containing the single provision capable of decimating the entire LP. *See Amylin*, 983 A.2d at 319.

II. APPELLANT OWED AND BROKE ITS FIDUCIARY DUTY TO SIERRA LP TO NOT TO ACT IN A MANNER BENEFITING ITSELF AT THE EXPENSE OF SIERRA LP.

A. Question Presented

1. Does Sierra Resources, a corporation that exercises indirect but exclusive control over Sierra LP through Sierra GP, have a fiduciary duty not to use its control over Sierra LP's investment to benefit the board of Sierra Resources at the expense of Sierra LP?

B. Scope of Review

The Supreme Court of Delaware reviews a decision on a motion for summary judgment by examining "the entire record to determine whether the Chancellor's findings are clearly supported by the record and whether the conclusion drawn from those findings are the product of an orderly and logical reasoning process." *In re Walt Disney Co. Derivative Litigation*, 906 A.2d 27, 48 (2006). This Court does not review factual conclusions made by the trial court unless such findings are "clearly wrong and justice so requires." *Id.* Whether or not the Court of Chancery applied the correct legal standard for determining whether or not a

fiduciary duty exists presents a question of law that is reviewed *de novo*. *Id.*

C. Merits of Argument

1. Appellant Owed Sierra LP and NCPRF Fiduciary Duties because Appellant Exercised Exclusive Control Over Sierra LP.

Given that Appellant directly managed and controlled Sierra LP and the NCPRF's investment through Sierra GP, Appellant owes Sierra LP the traditional fiduciary duties a general partner owes its limiting partner. *See* R. 4-5. Corporations cannot strategically create a general partnership, controlled by the corporation's board, to insulate itself from its fiduciary duty to the limited partnership. *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 172 (Del. 2002) (finding a parent corporation and its directors jointly and severally liable with the general partner for its breach of fiduciary duty to the limited partnership); *In re USA Cafes, L.P. Litig.*, 600 A.2d 43, 48-49 (Del. Ch. 1991) (holding that directors of a corporate general partner owed fiduciary duties to its limited partners).

Further, historically, this court heavily scrutinizes "efforts by a fiduciary to escape a fiduciary duty." *Gotham Partners, L.P.*, 817 A.2d at 168 (Del. 2002). Appellant argues that it should be able to insulate itself from its fiduciary duties to Sierra LP by using Sierra GP as a shield. This Court should not allow such a manipulative management strategy to interfere with a parent corporation's duties to the limited partnership under its control. *See* R. 4.

In *USACafes*, the court held that a general partner and the individual members of its board of directors owed the corporate limited partner fiduciary duties because the general partner and its directors

"dominated and controlled" the affairs of the limited partner. *In re USA Cafes, L.P. Litig.*, 600 A.2d 43, 49-50 (Del. Ch. 1991). In this landmark decision, the court reasoned that the "theory underlying fiduciary duties is consistent with [recognizing] that a director of a corporate general partner bears such a duty towards the limited partnership." *Id.* at 49. Here, Sierra Resources "dominated and controlled" the affairs of Sierra LP because Sierra GP solely acted as a vessel for Sierra Resources' decisions—no other controlling shareholder influenced Sierra GP's decisions with regards to Sierra LP's investments. R. 4-5.

In *James-River Pennington,* the court found that a corporation, as the controller of a general partner, owed fiduciary duties to that general partner's limited partner. *See, James-River Pennington, Inc., v. CRSS Capital, Inc.,* Del. Ch., Steele, V.C., C.A. No. 13870, slip op. at 22–23, 1995 WL 106554 (March 6, 1995); *accord, Barbieri v. Swing-N-Slide Corp.,* Del. Ch., Steele, V.C ., C.A. No. 14239, slip op. at 7–8, 1997 WL 55956 (Jan. 29, 1997). The court reasoned that the separate corporate entity (and its directors), owed the limited partnership fiduciary duties because it controlled the general partner indirectly through its directors' votes. *See James-River Pennington, Inc., v. CRSS Capital, Inc.,* Del. Ch., Steele, V.C., C.A. No. 13870, slip op. at 11, 1995 WL 106554 (March 6, 1995); *compare Brinckerhoff v. Enbridge Energy Company, Inc.,* C.A. No. 5526-VCN, slip op. at 18 (Del. Ch. Sept. 30, 2011) (finding that when an entity did not exercise control over a general partnership, that entity did not owe the limited partnership a fiduciary duty).

The court further stated in *In re Boston Celtics L.P. Litigation* that "it is well settled that . . . the general partner of a Delaware limited partnership and the directors of a corporate General Partner who control the partnership . . . have the fiduciary duty to manage the partnership in the partnership's interests and the interests of the limited partners." *In re Boston Celtics L.P. Litigation*, Del. Ch., Steele, V.C., C.A. No. 16511, mem. op. at 4, 1999 WL 641902; *see also Wallace ex rel. Cencom Cable Income P'rs II, Inc., L.P. v. Wood*, 752 A.2d 1175, 1180 (Del. Ch. 1999) (holding that 1) the general partner, 2) the general partner's parent and affiliated corporations, and 3) the officers of the general partner, all owed the limited partner fiduciary duties).

Here, like in *James River-Pennington*, Sierra Resources controlled the affairs of a limited partner (Sierra LP) through its direct control of the limited partner's general partner (Sierra GP). *See* R. 3. Sierra Resources dominated and controlled Sierra LP's affairs, similar to the corporation that controlled the limited partner in *USACafes*. *See* R. 4, 8 (noting that "Sierra Resources exercises indirect but exclusive control over Sierra LP"). Given Sierra Resources' direct control over Sierra LP, through Sierra GP, Sierra Resources owes Sierra LP the same fiduciary duties that Sierra GP owes Sierra LP. *See generally In re Boston Celtics L.P. Litig.*, V.C., C.A. No. 16511, mem. op. at 4.

2. Sierra Resources and its Board of Directors Breached its Fiduciary Duties to Sierra LP when it Acted Detrimentally towards Sierra LP For Its Own Benefit.

Sierra Resources and its board of directors used its exclusive control over Sierra GP to commit Sierra LP to a fifteen-year Indenture

agreement that entrenched its board and raised capital for a potential profit increase. *See* R. 4-5. If triggered, the "dead hand" clause in the indenture agreement would be catastrophic for Sierra LP, and would inescapably cause NCPRF to incur a significant loss in its investment. *See id* at 6-7. While refraining from delineating the full scope of a board's fiduciary duty to its shareholders, the Court of Chancery in *USACafes* asserted that a breach of fiduciary duty occurs when a controlling entity uses its "control over a partnership's property to advantage itself at the expense of the partnership [it controls]." *See In re USA Cafes, L.P. Litigation*, 600 A.2d 43, 49 (1991). Here, Sierra Resources' board incurred the benefit of entrenchment and capital gain at the cost of obligating Sierra LP to a potentially catastrophic "dead hand proxy put". R. 5-6.

Sierra Resources' and its board of directors may claim that it did not breach its fiduciary duties to Sierra LP because it did not "*intentionally* use . . . [the limited partnership's] property in a way that benefits the holder of the control to the detriment of the property or its beneficial owner." *See In re USACafes, L.P., Litig.*, 600 A.2d at 48 (emphasis added). However, this Court held that when "directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith." Stone ex rel. AmSouth Bancorporation v. Ritter, 911 A.2d 362 (Del. 2006); See also In re Walt Disney Co. Derivative Litigation, 906 A.2d 27, 67 (Del. 2006) (articulating that directors' intentional dereliction of duty constitutes a breach of a fiduciary duty).

Moreover, this Court held in *Brehm v. Eisner*, that a board cannot purposefully remain ignorant of material information critical to its subsidiary's investments by hiring outside counsel. *See Brehm v. Eisner*, 746 A.2d 244, 264 n. 66 (Del.2000) (finding that when information is both material and reasonably available to a board, the board's failure to consider the information violates its fiduciary duties, regardless of a hired expert's advice or lack of advice). Therefore, given the well-known phenomenon of shareholder activism in the real estate industry, Sierra Resources' and its board breached its fiduciary duties by consciously disregarding its responsibility to prevent the inclusion of a fatal "dead hand" clause. *See Amylin Pharmaceuticals Inc.*, 983 A.2d at 319 (warning parties of the public policy implications and financial consequences associated with "dead hand" clauses); See R. 5-6.

CONCLUSION

For the foregoing reasons, Sierra LP, on behalf of NCPRF, respectively requests that the Supreme Court of Delaware affirm the Court of Chancery's order granting Sierra LP's motion for summary judgment.