

IN THE SUPREME COURT OF THE STATE OF DELAWARE

PRAISE VIDEO, INC., a Delaware corporation,	)	
JACOB BISSINGER, FRANCIS PENNOCK, MARK VAN	)	
ZANDT, HOWARD METCALF, PETER HORNBERGER,	)	
NEW HOPE PUBLISHING CO., and PRAISE NEW	)	
HOPE CORP.,	)	
	)	
Defendants-Below,	)	No. 43, 2014
Appellants,	)	
	)	
V.	)	
	)	
MERCER CHRISTIAN PUBLISHING CO. and	)	
SUSAN BEARD,	)	
	)	
Plaintiff-Below,	)	
Appellees.	)	

ON APPEAL FROM
THE COURT OF CHANCERY
FOR THE STATE OF DELAWARE

APPELLEE'S BRIEF

LAW FIRM B
ATTORNEYS FOR PLAINTIFFS BELOW,
APPELLEES

DATE FILED: FEBRUARY 7, 2014

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NATURE OF PROCEEDINGS

On December 13, 2013, Plaintiffs-below Mercer Christian Publish Corporation and Susan Beard ("Mercer and Beard") filed suit in the Court of Chancery of Delaware, Civil Action No. 8974-CD, alleging the Defendants-below, Praise Video, Inc., Jacob Bissinger, Francis Pennock, Mark Van Zandt, Howard Metcalf, Peter Hornberger, New Hope Publishing Co., and Praise New Hope Corp., ("the board") breached their fiduciary duty to Praise Video shareholders by approving the New Hope merger. Mercer and Beard moved for a preliminary injunction to enjoin the board from consummating the merger. On January 14, 2014, the Court of Chancery, by the Honorable Sean Develin, Chancellor, issued an opinion granting Mercer and Beard's motion for a preliminary injunction to enjoin the board from effectuating the merger. The Court of Chancery issued its Preliminary Injunction Order on January 15, 2014.

On January 16, 2014, the board filed an application for certification of the interlocutory order with the court, and Mercer and Beard filed their response on January 17, 2014. The court granted the board's application on January 20, 2014. On January 15, 2014, the board appealed the interlocutory order pursuant to Supreme Court Rule 42, which was granted by Supreme Court of Delaware on January 23, 2014.

This is the Appellees' brief seeking to uphold the Court of Chancery's preliminary injunction.

SUMMARY OF ARGUMENT

I. The Court of Chancery correctly issued the preliminary injunction preventing the board from effectuating the New Hope merger because the

board breached its fiduciary duty to its shareholders by failing to seek the maximum price per share during the sale of a company, under *Revlon*. Furthermore, the board failed the balancing requirement of §362(a). Finally, the board incorrectly considered the religious-oriented conduct of the corporation post merger. Therefore, the Praise New Hope merger agreement is invalid.

II. The merger agreement is invalid, and the proper standard of review in this matter should be the compelling justification standard because the board intentionally deprived its shareholders of an effective vote with the primary purpose of thwarting the shareholder franchise. Thus the board's approval of the New Hope merger was a breach of fiduciary duty of loyalty and good faith to its shareholders.

SUMMARY OF FACTS

Praise Video Inc. (Praise Video) is a newly formed Delaware public benefit corporation ("PBC"). (R. at 3.) Praise Video was originally organized as a Delaware corporation ("Old Praise Video") in the mid-1970s before it merged into Praise Video, PBC., in September 2013. As a PBC, Praise Video identifies its particular public benefit as "a positive effect of a religious nature" through "the promotion of the values articulated in the Confession of Faith in a Mennonite Perspective." (*Id.*) The company engages in "the production and distribution of filmed and digital entertainment" as well as video games with Christian themes; it has recently experienced average earnings around four million dollars (about \$4 per share) and the gaming division accounts for at least 60% of this profit. (R.at 4.)

The company's two hundred and fifty stockholders are almost all members of the Mennonite Church USA. (*Id.*) Its CEO, defendant Jacob Bissinger, owns around 22% of Praise Video's outstanding shares of common stock while defendant directors other than Bissinger "own in the aggregate about 4% of Praise Video's shares." (*Id.*) Plaintiff Susan Beard owns about 3% of Praise Video's outstanding shares while plaintiff Mercer owns about 2%. (R. at 5.) Mercer is an indirect wholly-owned subsidiary of Mercer Media, Inc., and is best known for "best-selling Bibles, inspirational books, resources for church school curricula, and audio and digital Christian faith-based content." (*Id.*) Mercer's particular mission is to "spread inspiration by developing and distributing content that promotes biblical values and honors Jesus Christ." (*Id.*)

The Praise Video board began to explore the possibility of selling the company in early 2013, when Bissinger communicated to the board his intent to retire as CEO of Praise Video within a year and to sell his shares. (R. at 6.) As a result, the board retained financial advisor Norman Stoltzfus to "explore possible alternatives," particularly transactions which would enable Praise Video's stockholders and Bissinger to liquidate their investments. (*Id.*) By early June 2013, Stoltzfus identified several potential bidders, one of which was Mercer, which made explicit "its interest in acquiring and expanding Praise Video's gaming division." (R. at 7.) Mercer suggested an acquisition price "north of \$40" and expressed desire to dramatically expand Praise Video's customer base through synergizing capital investments with its own publications. (*Id.*)

The board met on June 24, 2013, to discuss potential bids from companies with corporate entities appearing to support Christian themes, including Mercer's. (*Id.*) Although the board was pleased with Mercer's suggested price, it balked at Stolzhus' indication that "considerable market growth might be anticipated in the area of combat-oriented video games" when he was asked to explain how Mercer might achieve its predicted expansion of the gaming division. (*Id.*) The directors, particularly Bissinger and Metcalf, were displeased by the idea of expanding into military-type combat games since it "violated the religious obligation[s]" of their Church. (*Id.*)

Holbrook, a non defendant director, correctly suggested it was inappropriate for the board to attempt to dictate the operation of Praise Video after its sale and that shareholders should balance their own interests before voting (R. at 8.) He also asserted that the directors, as stewards of the company, were "obligated to achieve the highest and best sale price" and "had no legal or moral right to impose their individual views about how the company should operate after it is sold." (*Id.*) Once Praise Video's counsel verified these statements, the board and majority of stockholders approved a Reorganization Merger for Praise Video to become a PBC. (R. at 8-9.) The board hoped that by altering Praise Video's status to a PBC, it would have "greater legal flexibility in a sale of the company to take into consideration Mennonite values." (*Id.*)

On December 5, 2013, Mercer and New Hope, Inc., submitted bids, of \$50 per share and \$41 per share, respectively. (R. at 9.) New Hope is a newly organized Delaware corporation, "formed for the

purposes of acquiring Praise Video," by defendant director Francis Pennock (20% stockholder) and Miller Price L.P., a Delaware limited partnership (80% stockholder). (R. at 6.) Pennock plans to serve as CEO of Praise Video post-merger and does not intend to expand the gaming division into "new, religiously questionable forms of digital entertainment." (R. at 9.) Both Mercer and New Hope bids were fully financed and condition on stockholder approval and although Praise Video requested for it, neither bidder agreed to include the public benefit provision in the company's post-merger certificate of incorporation. (R. at 9.)

New Hope's bid contained an additional concession involving the grant by Praise Video of an option (the "Gaming Option") to acquire Praise Video's gaming division if the Praise Video stockholders failed to approve the New Hope merger. (R. at 10.) New Hope would have the right to purchase the gaming division for \$18 million; about \$12 million or some 40% below the actual \$30 million value of the gaming division, which equals roughly \$12 a share. (*Id.*) On December 9, 2014 the board approved the New Hope bid with the Gaming Option and understood that the acknowledged undervaluation reflected in the exercise price would "likely encourage" many stockholders to vote in favor of the Merger, even if they individually would have preferred Mercer's higher cash bid. (R. at 12).

Following the board's approval of New Hope's merger agreement, Mercer and Beard filed suit claiming the board violated its fiduciary duty. (R. @12.)

ARGUMENT

I. Praise Video's board of directors breached its fiduciary duty to its shareholders by failing to seek the maximum price per share during a sale of the company under *Revlon*, by failing to adhere to the balancing requirement of Delaware General Corporation Law § 362, and by attempting to exercise unauthorized control of the corporation post-merger.

A. Question Presented

Whether the Praise Video board of directors breach its fiduciary duty by not seeking the maximum price per share during the sale of its company, by not balancing its shareholders interests, and by attempting to seek control of the corporation post-merger.

B. Scope of Review

This court generally reviews a grant or denial of a preliminary injunction with deference to the trial judge if the legal conclusion is "sufficiently supported by the record and [is] the product of an orderly and logical deductive process." *Levitt v. Bouvier*, 287 A.2d 671, 673 (Del. 1972). Therefore, the applicable standard of review is *de novo* with deference to the trial judge's ruling. *Id.*

C. Merits of Argument

The board of directors breached its fiduciary duties to its shareholders in three ways. First, the board breached its duty under *Revlon* by failing to seek the maximum price per share during a sale of the company. *Revlon v. MacAndrews & Forbes Holding Inc*, 506 A.2d 173, 182 (Del. 1986). Second, the board failed to adhere to the balancing requirement of §362(b) by disregarding the statutory multifactor balancing test and by making the religious interest a dispositive issue. Del. Code Ann. tit. 8, § 362(a) (West 2013). Third, the board attempted to exercise unauthorized control of the corporation post-

merger and approved the New Hope bid without successfully negotiating for assurance that Church values would be furthered.

- i. The board breaches its fiduciary duty to its shareholders under Revlon by failing to seek the maximum price per share during the sale of the company.**

Under Delaware law the "business and affairs" of a Delaware corporation are "managed by or under the direction of a board of directors." Del. Code Ann. tit. 8, § 141(a) (West 2010). This responsibility carries with it certain fundamental fiduciary obligations to the corporation and its shareholders. A fiduciary relationship is a relationship in which one person reposes special trust in another, or where a special duty exists on the part of one person to protect the interests of another. See *In re Bear Stearns Litigation*, 870 N.Y.S.2d 709, 728 (N.Y. Sup. Ct. 2008). In fact, "[t]he board's power to act derives from [this] fundamental duty and obligation to protect the corporate enterprise, which includes stockholders, from harm reasonably perceived, irrespective of its source." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985).

In some contexts the duty of the board changes from preserving the corporate entity to ensuring that shareholders receive maximum profits for their shares. In essence, "[t]he directors' role change[s] from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders in a sale of the company." See *Revlon v. MacAndrews & Forbes Holding Inc.*, 506 A.2d 173, 182 (Del. 1986). This change in the board's role is commonly referred to as the *Revlon* standard. This standard is triggered when (1) "a corporation

initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear break-up of the company;" (2) "in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction involving the breakup of the company;" or (3) "when approval of a transaction results in a sale or change of control."¹ *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 48 (Del. 1993).

In the case at bar, the *Revlon* standard was triggered when the CEO of Praise Video, Jacob Bissinger, retained financial advisor Norman Stoltzfus to help explore his options and find potential bidders for his Praise Video stock. (R. at 6-7.) It was then that it became obvious that there would be a break-up of Praise Video, and that the current board loss of control over the company. At the time of the merger Praise Video had not yet adopted public benefit status. The public benefit amendments became effective on August 1, 2013 (R. at 2.) and Praise Video was formed as a Delaware public benefit corporation in September 2013. (R. at 3.) However, negotiations and bidding with Mercer and New Hope began in June 2013. (R. at 7.) At the time the bids were considered, the board was legally obligated to follow the *Revlon* standard. In fact, the board was well aware of their obligations and had even retained counsel to report back on the

¹ The court in *In re Santa Fe Pacific Corp. Shareholder Litigation* (669 A.2d 59, Del.Supr) held that there is no "sale or change in control" when control of both companies remains in a "large, fluid, changeable and changing market." (at 47). In the case of Praise Video, the board of directors initiated a bidding process for a large share of the corporation's stock, which lead to the loss of control of the daily operations and management of the corporation, and the ultimate break-up of Praise Video. Further, this court held that courts should apply enhanced scrutiny, in the sale of control of a corporate, to ensure directors act reasonably to uphold their legal obligations to to seek the transaction offering the best value reasonably available. (at 43).

board's legal obligations in a sale of the company. (R. at 8.)

Further, as New Hope has refused to incorporate as a public benefit corporation, the public benefit statute will not apply to Praise New Hope post-merger. To apply public benefit corporation law to this transaction would not be recognizing the substance of what the parties were doing, and instead rewarding formalities that ultimately lead to the financial detriment of Praise Video shareholders.

Despite Bissinger and other Praise Video board members' strong feelings about promoting Christian values, there is no legal guarantee that Praise New Hope, under the direction of Pennock, will abide by its promise to do so. Nor did the Praise Video board negotiate harder to convince the bidders to include some variation of the director qualification provision currently in the Praise Video corporate charter. (R. at 4-5.) Instead, the bidders submitted bids they were certain would result in the post-merger corporation falling outside the purview of the public benefit law statute.

When the Praise Video board entered into an auction-ending arraignment with New Hope "on the basis of impermissible considerations at the expenses of shareholders" the directors breached their primary duty of loyalty. *Revlon*, 506 A.2d at 182. Even when a board acts in good faith and considers other permissible factors, there are fundamental limitations upon that prerogative. Once control has shifted, the current Praise Video stockholders will have no leverage to demand another control premium, and thus are entitled to take maximum advantage of the current opportunity to get the best value reasonably available. See *Paramount*, 637 A.2d at 46.

The purpose of the *Revlon* rule is to ensure that, in the context of a corporate break-up or sale of control, directors exercise their fiduciary duties to secure the transaction offering maximum value to stockholders. In fact, "[t]he board must act in a neutral manner to encourage the highest possible price for shareholders." *Barkan v. Amsted Industries, Inc.*, 567 A.2d 1279, 1286 (Del. 1989). Instead, by accepting New Hope's bid, Praise Video's board has not only has left its shareholders with twenty one dollars per share less than true market value of their stock, but it also did not guarantee the continuance of the mission statement post-merger through negotiations. Consequently, the directors allowed their religious, non-profit maximizing considerations, to cloud their judgment and ended the auction for Praise Video to the ultimate detriment of its shareholders. Thus, this Court should instead abide by Delaware's traditional corporate law principles and hold the directors to the standard articulated in *Revlon*.

- ii. The board failed the Balancing Requirement under §362 by ineffectively balancing the stockholders' pecuniary interests and the public benefit identified in Praise Video's certificate of incorporation.**

Even if this Court finds that Praise Video was a public benefit corporation at the time of the merger and was thus subject to DGCL §362, this Court should still find that the board of directors failed to meet the balancing requirement in §362(a). Del. Code Ann. tit. 8, § 362(a) (West 2013). The board of directors of a public benefit corporation have a statutory obligation to "... manage or direct the business and affairs of the public benefit corporation in a manner

that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation." (DGCL §362(a)).

This requires the board to be sensitive to the purpose and mission of the public benefit corporation, but not at the expense of the shareholder's monetary interest.

To fulfill this balancing requirement the board should have done a totality of circumstances analysis, and considered a variety of factors². The language of the statute makes clear that it is the duty of the board of directors to ensure that they leave the corporation and its shareholders in best possible position in light of the factors being considered. In the instant case, the board focused almost exclusively on the bidding company's willingness to uphold Mennonite values. In doing so the board chose to forego considering other important considerations that would result in immediate and long term profits for their shareholders.

After retaining a financial advisor, the board was left with two viable offers: Mercer and New Hope. Mercer, which already owned 2% equity in Praise Video (R. at 5), offered fifty dollars per share and had plans to expand Praise Video's already growing gaming industry. Upon hearing that Mercer merely *anticipated* market growth in the area

² Such factors include: the contents of Praise Video's corporate charter when it was initially formed; the mission of the corporation after it gained public benefit status; the likelihood that the potential buyer would adhere to those goals; the financial stability and consumer base of the bidders; the bid offer per share; the corporate charters and mission statements of the potential buyers; the projected long term effect the buyer's involvement would have on Praise Video and its shareholders; and the buyer's future plans and visions for Praise Video.

³ Even though Praise Video is a public benefit corporation, nothing in the public benefit corporation law, including § 361, purports to override this common law

of combat-oriented video games, the board essentially stopped considering Mercer. Indeed, the board searched for other bidders without negotiating harder with Mercer, did not look at the other benefits Mercer's ownership would bring to Praise Video, and did not inquire further into other plans Mercer had for market expansion. In fact Bissinger was reported having stated during board deliberation that "the possibility that Mercer would expand Praise Video's gaming operations into the combat simulation market space would, even with a generally Christian-themed orientation, be unacceptable in the light of Church doctrine, and that could not support of a merger with Mercer *regardless* of the difference between the Mercer and New Hope bid prices." (R. at 11-12, emphasis added.) This statement supports the notion that the board was only willing to consider other factors of the bid if the bids passed the board's high standards of adhering to Church doctrine. This is not the multifactor balancing analysis § 362(a) contemplates.

Meanwhile, New Hope's bid offered forty one dollars per share, nine dollars less per share than Mercer's bid, and included a highly undervalued Gaming Option. This Gaming Option was priced at twelve million dollars, or about forty percent below market value. Even though the board recognized the Gaming Option severely undervalued the gaming division, it determined that this huge financial setback would be in the best interest of Praise Video's shareholders because of Pennock's promise that as CEO of Praise Video he would "operate Praise Video to the best of his ability in a manner consistent with the values of the Church." (R. at 10.) Notwithstanding Praise New Hope's

refusal to include this promise in its corporate charter, Pennock does not say how he plans to uphold church values, what will happen after Pennock is no longer CEO, or what Praise New Hope plans to do to the gaming division more profitable. With so much uncertainty looming over this offer, it is unreasonable for the directors to accept such grave undervaluation and leave the Praise Video shareholders without any reassurance that their Church values will be respected post merger. Further, one of the two principals of Miller Price L.P., New Hope's Majority stockholder, is not a member of the Church. Even if Pennock's promise was genuine, this fact could severely limit his ability to control Praise New Hope. (R. at 10 n.12.) Although public benefit corporation shareholders may be willing to accept less monetary value for their shares in exchange for furthering their social goals, it would be unreasonable to expect them to accept this financial loss without any reassurance that Praise New Hope will respect the Church doctrine.

The recognition of public benefit corporations allows corporations to focus on creating a positive impact on society, and helps shareholders to pool resources to help further a specific cause they care about. However, shareholders in a public benefit corporation are still first and foremost investors who enter into shareholder agreements with the expectation that they will get a return on their investments. Shareholders could pursue their missions in volunteer groups, community organizations, or by donating money to a charity that shares the shareholder's specific goals. Yet, an individual who instead chooses to invest in a corporation does so in order to further

those public goals in a business transaction. These underlying concerns shape the duties of the board of directors to ensure that they operate the corporation in such a way that the shareholder's monetary expectations are met. The balancing requirement of §362(a) is particularly important in this instance because there is not an established market for trading Praise Video shares. This leaves shareholders that are unhappy with the outcome of the merger without the freedom and flexibility to sell their shares and leave the corporation. (R. at 5.) Thus, the Praise Video board has failed to fulfill its obligation under §362(a), leaving shareholders without maximum profits and reassurance that Praise New Hope will stay true to their Church values.

iii. Praise Video Board of Directors should not have considered the religious-oriented conduct of the corporation post merger.

Because Praise New Hope will not be organized as a public benefit corporation, it was inappropriate for the Praise Video board members to consider the religious-oriented conduct of the corporation post merger. In fact, the court in *Conestoga Wood Specialties Corp. v. Secretary of U.S. Dept. of Health and Human Services* held that secular corporations cannot engage in religious exercise for profit. *Conestoga Wood Specialties Corp. v. Secretary of U.S. Dept. of Health and Human Services*, 724 F.3d 377 (3d. Cir, 2013). Instead, the appropriate time for the board to evaluate the likelihood of the corporation adhering to the values of the Church was during its negotiations with bidders.

Delaware law allows for corporations to include mission

statements and special provisions in their corporate charter (Del. Code Ann. tit. 8, § 101(b) (West 2014)) or in their certificate of incorporation (Del. Code Ann. tit. 8, § 104 (West 2010)) to give the board control over how a corporation is run. See generally Del. Code Ann. tit. 8, § 141(b) (West 2010). By negotiating to include these devices in a corporation's corporate charter the board can ensure certain criteria will be met, even post merger. See Del. Code Ann. tit. 8, § 251(b)(3) (West 2013). Outside of such merger negotiations, the board of a corporation is without authority to control the operation and management of the new corporation post merger.

Although Pennock, CEO of Praise New Hope, promised that the board would abide by its word to uphold Church values, the merger agreement between Praise Video and New Hope lacks any enforcement provision for this promise. The record does not reflect any negotiations with the bidders whatsoever to include even a variation of the qualification provision Praise Video had in its certificate of incorporation before gaining public benefit status. (R. at 4-5.)

To the extent that the board wanted to consider religion, even without such provisions in the corporate charter, Mercer was clearly the stronger candidate for upholding Church values. Mercer's corporate image and customer base reflects comparable values to that of Praise Video. Praise Video's corporate charter identifies "the positive effect of a religious nature" and "the promotion of the values articulated in the Confession of Faith in a Mennonite Perspective" as its specific public benefit. (R. at 3.) Similarly, Mercer is known for best-selling Bibles, inspirational books, resources for church

school curricula, and auto and digital Christian faith-based content. (R. at 5.) Mercer's stated mission is to "spread inspiration by developing and distributing content that promotes biblical values and honors Jesus Christ." (R. at. 5.) The similarities between Mercer and Praise Video's corporate themes should have made the Praise Video board even more optimistic that Mercer would continue to uphold the Church doctrine because it already has a steady consumer base for these products and its associated with Christian values. Unlike Pennock's promise to operate Praise Video in a manner consistent with the Church which cannot be verified in any way before the bid is accepted, Mercer has already demonstrated commitment to these values.

The board may argue that it was acting in the best interest of their shareholders throughout this merger, especially in regards to perpetuating their religious desires by choosing New Hope over Mercer. However, the board still approved the New Hope bid without negotiate for assurance that Church values would be furthered; the main reason Praise Video became a public benefit corporation in the first place.

**II. The Praise Video Board of Directors its fiduciary duty to its
shareholders by approving the New Hope Merger.**

A. Question Presented

Whether the Praise Video board violated its fiduciary duty to its shareholders by approving the New Hope merger and authorizing the undervalued sale of Praise Video's gaming division?

B. Scope of Review

This court generally reviews a grant or denial of a preliminary injunction with deference to the trial judge if the legal conclusion is "sufficiently supported by the record and [is] the product of an orderly and logical deductive process." *Levitt*, 287 A.2d at 673. Therefore, the applicable standard of review is *de novo* with deference to the trial judge's ruling. *Id.*

C. Merits of Argument

This breach of fiduciary duty is two-fold: first, the board of directors breached its duty by depriving the stockholders of their statutorily mandated right to vote on the merger (Del. Code Ann. tit. 8, § 251 (West 2013)); and second, by "intentionally depriv[ing]," without a "compelling justification," the stockholders of their right to vote on the transaction. (R. at 16.); see *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988). Under § 251, shareholders have the right to an effective vote on a merger and this right was violated by the Gaming Option's coercive voting scheme. Title 8, § 251. Furthermore, the board had the time and ability to negotiate the binding terms of the Gaming Option but deliberately approved the merger agreement anyway. See *Blasius*, 564 A.2d.

- i. The board breached its fiduciary duty to its shareholders because the Gaming Option effectively deprived shareholders of their statutory right to an effective vote on the merger.

According to § 251 of the Delaware General Corporation Law, the board of directors must first submit a merger agreement to its stockholders at an annual or special meeting before the agreement is considered and a vote is taken for its adoption or rejection. Title 8, § 251. In other words, § 251 provides stockholders with a statutory entitlement to an "effective vote" on a merger. (R. at 15.) The enactment of § 251 was the codification of the common law principle of "corporate democracy," which dictates that the stockholders have certain enforceable rights that allow them to limit how the board of directors manages corporate affairs. See generally Gregory S. Schaer, *Blasius Industries, Inc. v. Atlas Corp.: Closer Scrutiny of Board Decisions Under the "Compelling Justification" Standard*, 16 Del. J. Corp. L. 639 (1991).³

Corporations are owned by stockholders who invest capital in the company through the purchase of its stocks. *Id.* The stockholders do not manage the everyday affairs of the corporation; indeed, the board of directors is responsible for managing and overseeing corporate affairs. *Id.* at 639. Under Delaware law, corporate directors are provided with broad discretion in managing the business

³ Even though Praise Video is a public benefit corporation, nothing in the public benefit corporation law, including § 361, purports to override this common law principle or the stockholders' entitlement to an effective vote on the merger. [15]. According to § 361, Praise Video is still subject to generally applicable provisions of Delaware corporate law since public benefit corporation laws have thus far not imposed additional or different requirements, particularly in regards to shareholder voting rights for mergers. Therefore, Praise Video stockholders have statutory rights to an effective vote on a merger, even though Praise Video is a public benefit corporation.

and affairs of the corporation. See Del. Code Ann. tit. 8, § 141 (West 2010). This broad discretion is often termed the “business judgment rule” and the only protections that stockholders have against “perceived inadequate business action” by corporate directors is the right to vote to replace incumbent board members or to sell their shares. Schaer, *supra* at 643; 659. These protections play directly into the fundamental principles of corporate democracy in the sense that the shareholders have a check on the power of their board of directors. *Id.* at 640. However, these protections are sometimes not enough to check the board’s decision making, especially if, like in the present case, the stockholders are deprived of an effective vote. See *In re MONY Grp., Inc. S’holder Litig.*, 853 A.2d 661 (Del. Ch. 2004); *Blasius*, 564 A.2d.

The Gaming Option to acquire Praise Video’s gaming division becomes exercisable if (1) the Merger agreement is terminated because the stockholders did not approve it at the same time another proposal to acquire Praise Video is made, and (2) Praise Video is “acquired or enters into a definitive agreement to be acquired” within twelve months of such termination. (R. at 10 n.12.) In other words, if the Praise Video stockholders do not approve of the New Hope merger, and if Praise Video were to enter into a definitive agreement to be acquired by Mercer, the Gaming Option would give New Hope the option of buying Praise Video’s gaming division for \$18 million and Mercer would prospectively lose the gaming division in its merger with Praise Video. (R. at 10.)

The Gaming Option puts Praise Video stockholders in a difficult

position because they are effectively disenfranchised through this coercive voting scheme; they do not have an actual choice in the matter of New Hope purchasing Praise Video's gaming division.

Theoretically, if all of the Praise Video stockholders approve the New Hope merger after balancing their interests then the Gaming Option would be null. As a result, there would be no stockholders to contest the legitimacy of the Gaming Option since the gaming division would already be purchased by New Hope through the merger.

However, if the stockholders did not approve the New Hope merger then the stockholders would effectively have their hands tied from entering into new merger agreements. This is because the gaming division, the most lucrative division of Praise Video, would be sold to New Hope at 40% below market value if and when another company acquired Praise Video. If New Hope exercised the Gaming Option then stockholders would lose at least \$12 a share on the sale of the gaming division. (R. at 10.) Furthermore, the market value of Praise Video stocks would also decrease if analysts found that Praise Video's company, which would only include the production and distribution of religious film and digital entertainment, was not as attractive an investment without the gaming division.

Moreover, the Gaming Option disincentives prospective companies from pursuing a merger with Praise Video, especially companies interested in acquiring the gaming division. This scenario essentially puts the stockholders between a rock and a hard place because it forces the stockholders to approve the New Hope merger or to suffer a drastic reduction in Praise Video stock value and

isolation from other merger proposals.

For the aforementioned reasons, the Gaming Option effectively deprives Praise Video stockholders of a voluntary vote in the merger transaction with New Hope. This coercive voting scheme disenfranchises the stockholders and violates their statutory right to an effective vote under § 251. Therefore, the preliminary injunction should be upheld.

ii. The board of directors breached its fiduciary duties of loyalty and good faith by intentionally depriving its shareholders of this statutory right.

Under Delaware law, the board of directors has fiduciary duties of care, loyalty, and good faith when making business related decisions. See *Brehm v. Eisner*, 746 A.2d 244, 259 n.49 (Del. 2000); *Revlon*, 506 A.2d at 179. The duty of care requires directors to “be diligent” and to “make inquiries before acting on behalf of the corporation.” Ellen Taylor, *New and Unjustified Restrictions on Delaware Directors' Authority*, 21 Del. J. Corp. L. 837, 881 (1996). Meanwhile, the duty of loyalty requires directors to “put the interests of the corporation and its shareholders ahead of their own interests” and the duty of good faith requires directors to act with “honestly-held belief[s].” *Id.* at 880-81. Since the appellees acknowledge that there was nothing material lacking in the directors’ information base when evaluating the bids on December 9, 2013, this brief will only address the board’s breach of loyalty and good faith. (R. at 10.)

a. The board breached its duty of loyalty under *Blasius*.

As previously mentioned, a board of directors can rely on the business judgment rule to protect most of its actions from judicial scrutiny. See generally Lyman Johnson, *Unsettledness in Delaware Corporate Law: Business Judgment Rule, Corporate Purpose*, 38 Del. J. Corp. L. 405, 411 (2013). A board's duty of loyalty is inherently tied to this presumption of the business judgment rule because courts trust a board of directors to act in the best interests of its stockholders when making decisions for the corporation; thus the board should be allowed a certain amount of leeway in decision-making. *Id.* at 412.

However, if a board breaches its fiduciary duties to its stockholders, a court may displace the presumption of the business judgment rule to scrutinize the board's actions. *Id.* at 411. Delaware courts have set aside the presumption of the business judgment rule in the contexts of takeovers and acquisitions. See *Revlon*, 506 A.2d; *Unocal*, 493 A.2d. Most importantly, Delaware courts have also required boards to provide a "compelling justification" for their corporate decision making if it has been demonstrated that a board acted with the primary purpose of thwarting shareholder votes.⁴ *Blasius*, 564 A.2d at 661; see *MM Companies, Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1121 (Del. 2003); *Williams v. Geier*, 671 A.2d 1368 (Del.

⁴ Although this compelling justification standard has not been applied in cases involving "plurality plus" governance policies or cases involving Delaware General Corporation Law § 220 inspection rights (*City of Westland Police & Fire Ret. Sys. v. Axcelis Technologies, Inc.*, 1 A.3d 281, 289 (Del. 2010)), this standard still applies to the case at bar for a number of reasons. First, the Gaming Option was approved with the primary purpose of depriving the shareholders of an effective vote. Second, the Praise Video transaction is factually distinguishable from Westland because there is no plurality plus governance policy or § 220 issue in the case at bar. Thus the compelling justification standard should still apply when analyzing the Praise Video board's actions.

1996).

The case at bar is similar to *Blasius*, where a board of directors intentionally deprived its stockholders of their voting rights. *Blasius*, 564 A.2d at 661. In *Blasius*, the Atlas Corporation board of directors amended its bylaws to increase the size of its board to prevent a particular shareholder from electing a majority of the new board and imposing an ill-timed board restructuring and asset liquidation plan. *Id.* at 654-56. Although the board increased the size of its board with the primary purpose of thwarting *Blasius'* voting rights, the directors claimed that they were motivated only by their desire "to protect the shareholders from the threat of having an impractical... dangerous recapitalization program foisted upon them." *Id.* at 658.

Even though the court found that the board acted in good faith to protect the interests of its other shareholders, the court found that the board still breached its fiduciary duties. *Id.* at 662-63. The court noted that the board "had time (and understood that it had time) to inform the shareholders of its views on the merits of the proposal subject to stockholder vote." *Id.* at 663. The court also noted that the board was not faced "with a coercive action taken by a powerful shareholder against the interests of a distinct shareholder constituency" and was presented only with a consent solicitation by a nine percent shareholder. *Id.* Thus the court found that, even though the action taken was made in good faith, the intentional disenfranchisement of the company's stockholders constituted "an unintended violation of the duty of loyalty that the board owed to the

shareholders" without a compelling justification. *Id.*

The facts in *Blasius* are synonymous to the case at hand. The directors "openly and intentionally" (R. at 2) approved the terms of the Gaming Option to thwart shareholder votes because it "would favor and facilitate the consummation of the bid" that the directors had already approved with New Hope. (R. at 11.) Praise Video's board also had a weak justification for thwarting its shareholder vote. First the board was faced with a much smaller threat to the company's well-being than the *Blasius* board. *See Blasius*, 564 A.2d at 663. While the *Blasius* board was faced with an implied threat of a takeover (*Id.* at 653), the Praise Video board only faced the eventual retirement of its CEO, Jacob Bissinger, and the prospective sale of his stocks. (R. at 6.) Second, Praise Video had an entire year to find alternative methods to this possibility. (*Id.*)

Moreover, it is evident that the board moved too quickly in the bid approval process. Both New Hope and Mercer submitted their bids on December 5, 2013 and although Bissinger was not going to retire for another three months, the board evaluated and approved New Hopes bid within four days of receiving it. (R. at 9-10.) The board asserts that Stolzhus and Praise Video's counsel "painstakingly reviewed" the bidding process, the Gaming Option, and prospects for any further bids. (R. at 11.) Although the Chancellor and the board concluded that there was no foreseeable prospects for future bids, (R. at 10) this proposition ignores the fact that the board still had more than enough time to negotiate the terms of the merger agreement to have a less binding effect on its shareholders.

Furthermore, the board could have approved both Mercer and New Hope's bids and, after dispersal of proxy materials, let the stockholders vote, on the merits, which company to merge with instead of the board aggrandizing this right. The Praise Video board, like the board in *Blasius*, was not so pressed for time that it could not have explored other alternatives or negotiated other contract provisions before approving a bid that deprived its shareholders of an effective vote. Thus the board did not have a compelling justification for disenfranchising its shareholders and breached its fiduciary duty of loyalty.

b. The board breached its duty of good faith according to public policy.

We respectfully disagree with Chancellor Develin's finding that the board acted in good faith by approving the Gaming Option. (R. at 16.) According to the Chancellor, the board approved the Gaming Option in order "to promote the accomplishment of the Merger with New Hope." (*Id.*) However, the very act of depriving stockholders of an effective vote on a merger (one of the most critical voting topics) implies that the board did not trust its stockholders to vote for New Hope on their own; indeed, by agreeing to the Gaming Option, the directors broke the law to ensure that their stockholders voted the way the directors wanted them to. Title 8, § 251. Although the board justified its actions by asserting that it honestly believed that a merger with New Hope would promote the corporation's public benefit, this justification is by no means compelling when evaluated in light

of the illegality of the board's actions. (R. at 11.)

It is clear that the board was not acting in good faith when it intentionally stripped shareholders of the opportunity to determine for themselves "how best to apply their financial and operational assets to satisfy their religious obligations" through an effective vote. (R. at 8.) This intentional disenfranchisement of shareholders without a compelling justification is inherently an action that lacks good faith.

It is doubtful that the board had the honest belief that breaking the law and depriving its stockholders of a statutory right was in the best interest of the stockholders and the company, especially when the board could have explored other less coercive means to achieve a merger with New Hope. By analyzing the board's beliefs on a piecemeal basis, the good faith of the transaction becomes tainted when the board fails to provide a compelling justification for its intentional disenfranchisement of its shareholders. *See Blasius*, 564 A.2d at 661.

Assuming arguendo that the board had acted entirely in good faith, the board still breached its fiduciary duty of loyalty to stockholders by intentionally depriving stockholders of an effective vote on the merger without a compelling justification.

CONCLUSION

For the foregoing reasons, this Court should uphold the preliminary injunction issued by the Court of Chancery.

Respectfully submitted,

Team "B"

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