IN THE SUPREME COURT OF THE STATE OF DELAWARE

TALBOT INC., TIMOTHY GUNNISON, FRANCOIS PAYARD, NAOMI ROTHMAN, ROSARIA GABRIELLI, MARSHALL CANNON, AJEET GUPTA, DANIEL LEMON, CLARE LEONARD, and PATRICK RHANEY,	:	No. 162, 2015
Defendants Below Appellants,	:	Court Below: Court of Chancery of the State of Delaware in and for New Castle County
v.	:	
ALPHA FUND MANAGEMENT L.P.,	:	Civil Action No. 10428-CJ
Plaintiff Below, Appellee.	:	

APPELLANTS' OPENING BRIEF

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Appellants

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NATURE OF THE PROCEEDINGS

This case comes before the Court on appeal from the Court of Chancery interlocutory order granting a preliminary injunction. Plaintiff-Appellees, Alpha Fund Management L.P., brought suit against the Defendant-Appellants, Talbot Inc., Timothy Gunnison, Francois Payard, Naomi Rothman, Rosaria Gabrielli, Marshall Cannon, Ajeet Gupta, Daniel Lemon, Clare Leonard and Patrick Rhaney. Plaintiff-Appelees allege that Appellants' Fee Shifting Bylaw is facially invalid. While the lower court declined to rule on this issue, the Court of Chancery granted the preliminary injunction to prevent the fee shifting bylaw from taking effect. The Court of Chancery held that Defendant-Appellants had acted improperly and inequitably by enacting the fee shifting bylaw.

On January 15, 2015, the Court of Chancery filed the Preliminary Injunction Order. On January 22, 2015, appellants filed a Notice of Appeal from the Interlocutory Order. On January 29, 2015, the Supreme Court of the State of Delaware accepted the interlocutory appeal.

SUMMARY OF THE ARGUMENT

I. Defendant-Appellants' Proxy Fee Shifting Bylaw is valid under the standards applied in *ATP.* Litigation fee shifting bylaws are facially valid under *ATP*. *ATP* provides that bylaws are facially valid if they (1) are authorized by the Delaware Code, (2) consistent with the corporation's

certificate of incorporation, and (3) not otherwise prohibited by law. *ATP Tour, Inc. v. Deutscher Tennis Bund*, 921 A.3d 554, 558 (Del. 2014). As applied, the bylaw was not inequitably implemented, nor was it adopted with the primary purpose of inhibiting the voter franchise.

II. In the alternative, the court should apply *Unocal's* enhanced judicial scrutiny. The *Unocal* standard, as applied in *Unitrin*, is an appropriate standard for evaluating the validity and equity of the Proxy Fee Shifting Bylaw. *Gilbert* resolves the ambiguity and overlap of the *Blasius* and *Unocal* standards, which apply to issues of corporate control and shareholder franchise. It clearly holds that a reviewing court must apply *Unocal* where the board "adopts any defensive measures taken in response to some threat to corporate policy and effectiveness which touches upon issues of control." *Gilbert v. El Paso Co.*, 575 A.2d 1131, 1144 (Del. 1990). The *Unitrin* court evaluated defensive measures taken by corporations through an inquiry into whether the measures were reasonable or draconian. *Unocal* and *Unitrin* account for the problems addressed in *Blasius*, *Schnell*, and *Stroud* while preserving the board's right to take defensive measures when necessary.

III. Applying *Unocal*, the Defendant-Appellants' Proxy Fee Shifting Bylaw is valid because the board's actions meet

the *Unocal* standard. *Unocal* requires the court to apply enhanced review to determine whether the directors "had reasonable grounds for believing that a danger to corporate policy and effectiveness existed …" and that the board's response was "reasonable in relation to the threat posed." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985). Talbot's board reasonably responded to the threat of Alpha Fund's restructuring plan, which would have sold off key assets and destroyed the board's long term plans. The board perceived that the disinterested shareholder's proxy vote could be threatened by claims of supposed short term gains that did not take into account the long term cost cutting measures the Talbot's board already had in place to address the weaknesses Alpha Fund identified. Talbot's response was proportional to the threat because it was not preclusive and did not impermissibly interfere with the shareholder voting franchise. Thus, the Talbot board, having met its *Unocal* responsibilities, is subject merely to the business judgment rule and under the business judgment rule, the court will not substitute its judgment for that of the board. *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

STATEMENT OF FACTS

Defendant Talbot Inc. is a publicly traded Delaware corporation headquartered in Chestertown, Maryland. The nine individual defendants comprise the Talbot Board. Of the nine, only one is an inside director: Chairman and Chief Executive Officer Timothy Gunnison.

By June 2014, activist investors Alpha Fund, Inc. had acquired a 4% stake in Talbot, and Alpha representative Womack contacted CEO Gunnison and suggested a restructuring proposal. This proposal ran contrary to the long-term goals of Talbot and aimed to spin off assets for short-term gain. Gunnison rejected the proposal after determining that it both underestimated the aggregate benefits of Talbot's three divisions and failed to incorporate the already existing cost-cutting measures into its analysis.

Between July and December, 2014, Alpha Fund continued to acquire Talbot shares. On December 10, 2014, Alpha Fund filed a Schedule 13D with the Securities and Exchange Commission disclosing that Alpha Fund held 7% of Talbot shares outstanding. Alpha Fund also publicly revealed that they had proposed a restructuring plan to Gunnison and had been rebuffed, leading them to attempt to nominate four directors for the Talbot's board at the annual stockholders meeting in May 2015.

CEO Gunnison immediately called for a special Board meeting on December 18, 2014, solely to discuss the developments surrounding Alpha Fund's Schedule 13D filing. Under the guidance of in-house and outside legal counsel, the board discussed the costs of a proxy contest and the implications for the well-being of the corporation and

the shareholders should such a contest be unsuccessful. Outside counsel presented evidence showing that proxy contests can impose on corporations' expenses ranging from $800,000 to $14 million dollars. Based on that guidance, the board determined that the long term goals would be best served by keeping the company's three divisions intact. The board decided that the Proxy Fee Shifting Bylaw would effectively deter ill-thought out proxy battles that already possessed little chance of success. The board did not waive Alpha's fees at that time, but reserved the discretion to waive the fees in accordance with their fiduciary duties.

ARGUMENT

I. TALBOTS' PROXY FEE SHIFTING BYLAWS ARE VALID UNDER ATP

A. Question Presented

Whether defensive implementation of Proxy Fee-Shifting Bylaws by a stock corporation infringe on stockholder franchise to the degree of being inequitable.

B. Scope of Review

This Court reviews the Court of Chancery's decisions involving legal conclusions for error under a *de novo* standard. *See Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 394 (Del. 1996).

C. Merits

i. The Proxy Fee Shifting Bylaw is Facially Valid under the ATP standard.

ATP provides that bylaws that (1) are authorized under Delaware Corporation Law, (2) are consistent with the respective certificate of incorporation, and (3) are not otherwise prohibited by law are facially valid. *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554, 557 (Del. 2014). No Delaware law forbids the enactment of fee shifting bylaws. *Id.* at 558. A bylaw is not rendered facially invalid simply because it could be in conflict with the law. *Id.* at 577.

Here, the bylaws are not forbidden by Delaware Law. They are consistent with the certificate of incorporation insofar as they serve to promote the best interests of the corporation. Although a fee shifting bylaw could be inequitable, and therefore unlawful under some circumstances, this is insufficient for rendering the bylaw facially invalid. Accordingly, the Proxy Fee Shifting Bylaw is facially valid under *ATP*.

ii. The Proxy Fee Shifting Bylaw Does Not Involve the Inequitable Purposes Contemplated by the ATP Court and Illustrated by *Blasius* and *Schnell*.

Neither *Blasius* nor *Schnell* should apply to the instant case, because the Proxy Fee Shifting Bylaw was not adopted for any inequitable purpose, much less the primary purpose of thwarting corporate democracy. As such, the inequitable purpose qualification

ATP addressed does not impact the validity of the Proxy Fee Shifting Bylaws here.

When determining whether a fee-shifting bylaw is unlawful, an analysis of inequities is required. *See ATP Tour, Inc.*, 91 A.3d at 558. In *Blasius*, the court held that actions creating new board positions, undertaken for the primary purpose of interfering with stockholder votes, were subject to closer scrutiny than those undertaken for the legitimate purpose of "defeating a threatened change in corporate control." *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988). The *Blasius* court refused to find a *per se* rule invalidating actions undertaken for the primary purpose of inhibiting voter franchise; instead, it held that certain actions, if taken in paternalistic good faith, may be sufficient to validate stockholder voting infringement as an equitable primary purpose. *Id.* at 662 (acknowledging that certain facts could justify this sort of "extreme action").

Furthermore, *Blasius* distinguished the case before it from one in which a board was faced "with coercive action taken by a powerful shareholder against the interests of a distinct shareholder constituency." *Id.* The court also pointed out that Blasius straightforwardly prevented stockholders from effectively employing their franchise rights, and distinguished as permissible situations where a board attempts to persuade stockholders to vote in a different way, even if the board spends corporate funds to do so. *See id.*

Here, the Talbot board's primary purpose was not thwarting stockholder votes. In contrast to the expansion of the board in

Blasius, Talbot simply took measures to shift the costs of an unsuccessful proxy battle onto those who stood to benefit should the insurgents win the battle. The level of control enjoyed by Alpha should they win the proxy battle was in no way diminished by the new bylaws. Rather, the board acted to ensure that the stockholders as a whole would not be held responsible for the costs of a shortsighted plan that ultimately turned out to be unsuccessful. This, the board reasoned, would make Alpha "think twice" about waging a proxy battle, as they would have to shoulder the true costs of the risks. *Alpha Fund Mgmt. v. Talbot Inc.*, No. 10428-CJ at *8 (D. Del. Jan. 14, 2015) (order granting preliminary injunction). Those who planned the proxy battle would not be able to do so thoughtlessly and simultaneously have their efforts subsidized by the other stockholders. To gain control, any insurgents would have to take a risk.

Such a bylaw separates the wheat from the chaff, avoiding costly and time-consuming proxy battles that are destined to fail, and promoting careful consideration and cost/benefit analysis of massive restructuring changes. The stockholders retained the same right to vote; indeed, Alpha argued below that the negative impact of the bylaws was that stockholders would be persuaded to vote differently, not that stockholders would be prevented from meaningful voting *Id.* at *15. Alpha decided not to proceed if the bylaws remained intact because it did not believe it could win, not because the bylaw inhibited voting. The sort of action the Talbot board engaged in was in paternalistic good faith, as contemplated by *Balsius*. Additionally, the primary purpose was never to thwart voter franchise, but to

protect the company from shortsighted and careless efforts. What Alpha actually argued below is that the board passed the bylaws in an effort to persuade the stockholders to vote differently. *Id.* This is the very sort of action recommended by the *Blasius* court as an alternative to prohibitive actions like expanding the board.

The *ATP* court described *Schnell* as a "landmark case" in determining whether a bylaw is used for assessing inequitable purposes. *ATP Tour, Inc.*, 91 A.3d at 558. In *Schnell*, a board changed the date of its annual stockholder meeting, preventing stockholders from engaging in a proxy contest by precluding them from having sufficient time to clear materials with the S.E.C. *See Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971). The court held this action, undertaken for the purpose of obstructing stockholder's rights, to be inequitable. *Id.*

Should Alpha move forward with the contest, the bylaws do not impact its ability to win. The bylaws did not limit the time available to Alpha to prepare, nor do they give Talbots an inequitable advantage. Instead, they properly allocate the risks of the change in corporate control to the parties that stand to benefit from the change: Alpha. Such fee-shifting is not preclusive. Far from being inequitable, it holds the corporation as a whole harmless for the costs of raiders and insurgents, while permitting well-thought out and meritorious proxy contests. In fact, the bylaws incentivize proxy contests that have the support of stockholders, imposing no financial liability for actions if firmly grounded in stockholder support.

The bylaws ensure these proxy contests will be more meaningful by dis-incentivizing proxy contests not grounded in stockholder support. Essentially, they protect the stockholder franchise, shielding it from exploitative and costly gambling ventures while giving the changes in corporate control that stockholders vote for the wholehearted endorsement of the board. Plaintiffs have plenty of time to engage in a proxy contest, and the board does not discourage such contests or thwart efforts to vote in them. The board will not, however, promote or subsidize proxy contests that cannot win at the expense of the stockholders. Indeed, it appears more inequitable to permit insurgents to try to overthrow the board risk-free, encouraging them to gamble on random chances of success, than to encourage such challengers to ensure they have voter support before moving forward and wasting time and money. Surely, making it more difficult to run a proxy contest is different from actually taking away the ability of stockholders to "freely vote." *Yucaipa Am. Alliance Fund II v. Riggio*, 1 A.3d 310, 335 (Del. Ch. 2010) *aff'd*, 15 A.3d 218 (Del. 2011).

II. IN THE ALTERNATIVE, THE COURT OF CHANCERY ERRED IN CONCLUDING THAT THE ATP STANDARD OF REVIEW WAS APPLICABLE TO THE PROXY FEE-SHIFTING BYLAW AND INSTEAD SHOULD APPLY *UNOCAL*.

A. Question Presented

Whether the board of director's defensive decision, in response to a corporate raider's hostile proxy battle, to enact a Fee Shifting Bylaw, is subject to *Unocal* enhanced judicial scrutiny. The Fee Shifting Bylaw requires unsuccessful proxy contestants to reimburse the corporation for reasonable professional fees and expenses incurred by the corporation in resisting the proxy battle.

B. Standard of Review

This Court reviews the Court of Chancery's grant of preliminary injunction for an abuse of discretion, "without deference to the embedded legal conclusions of the trial court." *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 394 (Del. 1996). Legal conclusions are subject to *de novo* review. *Id.*

C. Merits of the Argument

i. Enhanced judicial scrutiny under Unocal is the proper standard to evaluate the Fee Shifting Bylaw because Unocal is better able to address the voting franchise concerns of *Blasius* and *ATP* in a corporation under the threat of hostile takeover.

Under, *Gilbert* the ambiguity and overlap of *Blasius* and *Unocal* is resolved. The court clearly held that reviewing court must apply

Unocal where the board "adopts any defensive measures taken in response to some threat to corporate policy and effectiveness which touches upon issues of control." *Gilbert*, 575 A.2d at 1144. However, this does not render *Blasius* meaningless. In certain circumstances, a court should recognize the special importance of protecting the shareholder franchise within *Unocal's* proportional requirement.

The *Unocal* analytical framework is fully able to address the voting franchise concerns that animated *Blasius* and *ATP*. Enhanced judicial scrutiny, as opposed to the business judgment rule, is applied when the court is concerned with board entrenchment and the improper interference with the shareholder vote. *Blasius Industries, Inc. v. Atlas Corp.*, 564 A.2d 651, 661 (Del. Ch. 1988). The board is not permitted to "perpetuate[e] itself in office" and "obstruct [] the legitimate efforts of dissident stockholders in the exercise of their rights to undertake a proxy contest against management." *ATP Tour, Inc. v. Deutscher Tennis Bund*, 91 A.3d 554, 558 (2014) (quoting *Schnell v. Chris-Craft Industries*). Such findings of inequitable purpose should be "based on an extensive review of the facts …" *ATP Tour, Inc.* 91 A.3d at 559 (quoting *Hollinger Int'l, Inc. v. Black*, 844 A.2d 1022, 1029 (Del. Ch. 2004)).

The Unocal analytical framework is able to address the voting franchise concerns that animated *Blasius*, so long as the court applies Unocal "with a gimlet eye out for inequitably motivated electoral manipulations or for subjectively well-intentioned board action that has preclusive or coercive effects." *Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 56

BUS. LAW. 1287, 1316 (2001) (quoting *Chesapeake Corp. v. Shore*, 771 A.2d 293, 323 (Del. Ch. 2000). "The fine analytical distinctions required by having parallel, coexisting standards of review that are similar in operation and result...[is] functionally unhelpful and unnecessary," especially has *Stroud* and *Unitrin* have folded the *Blasius* standard into *Unocal*. *Id.*

Unocal recognizes that directors are often faced with an "inherent conflicts of interests" during contests for corporate control "[b]ecause of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders...." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985). Thus, *Unocal* requires the court to apply enhanced review to determine whether the directors "had reasonable grounds for believing that a danger to corporate policy and effectiveness existed..." and that the board's response was "reasonable in relation to the threat posed." *Id.* at 955. If the board's defensive measures meet the *Unocal* standard, the board is given the protection of the business judgment rule. *Id.*

Under the business judgment rule, the court will not substitute its judgment for that of the board. *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984). It is a fundamental principle that the court will not interfere with the board of director's management of the business affairs of a corporation so long as they "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." *Id.* at 812. Because Talbots is responding to a hostile threat to its corporate policy and

effectiveness, the court should apply the *Unocal* standard with an emphasis on inequitably motivated electoral manipulators and preclusive or coercive effect.

ii. The Unocal framework is an appropriate standard in the instant case.

Because defensive actions that incidentally chill proxy contests can be equitable, the standards of *Unocal* and its progeny are superior than vague balancing of the equities for evaluating the Proxy Fee Shifting Bylaws. Plainly, the primary purpose of the bylaws was to shift fees, not to inhibit stockholder franchise. The board's implementation of the Proxy Fee Shifting Bylaw was a defensive measure in a response to a perceived threat, and it did not have the primary purpose of stockholder disenfranchisement; thus, it should be reviewed under standard outlined in *Unocal* and applied in *Unitrin*. To succeed under *Unocal*, the board must show that it had (1) "reasonable grounds for believing that a danger to corporate policy and effectiveness existed," and (2) that its "defensive response was reasonable in relation to the threat posed." *See Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1373 (Del. 1995)(citing *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985)).

Unitrin proposes an enhanced scrutiny framework for evaluating defensive measures under *Unocal* that is preferable here to the vague inequity standard employed by the lower court, especially in light of the fact that the lower court agreed that *Blasius* did not apply. The relevant questions under *Unitrin* are whether the defensive measures

are draconian—preclusive or coercive—and whether, if not draconian, the defensive measures were within the "reasonable range of responses." *Id.* at 1367. *Unitrin* and *Unocal* are appropriate standards because they both balance the importance of stockholder franchise with the necessity of defensive measures, especially here, where even the appellees do not assert that the primary purpose of the bylaws was to inhibit the voter franchise.

In *Stroud*, the court held that the primary purpose of a defensive action could not be interference with the voter franchise when the board would maintain a majority regardless of whether it took the defensive action. *See Stroud v. Grace*, 606 A.2d 75, 92 (Del. 1992). The court came to this conclusion even though the defensive action provided the board with "unfettered discretion to disqualify the shareholders' candidates without recourse." *Id.* at 94. The *Stroud* opinion made clear that the injury, at best, was hypothetical, and that the validity of the facially valid bylaw could not be determined until the bylaw was actually used. *Id.* at 96.

Here, the matter is similar. Even prior to the enactment of the Proxy Fee Shifting Bylaws, Plaintiff intended to nominate a maximum of four stockholders to a nine person board. As this would not give Plaintiffs a majority, it cannot be that the board's primary purpose was to deprive stockholders of their franchise rights. Furthermore, Plaintiffs argue that the bylaws would persuade stockholders to vote against them, not that it necessarily precludes them from holding a proxy contest. This, like in *Stroud*, is a hypothetical injury; indeed, the bylaw allows for fee shifting exceptions within the discretion of

the board. At present, Plaintiffs cannot know whether or not they will receive such an exception, and mean to question the equitable validity of corporate action before it even occurs. This is impermissible under *Stroud*.

Unitrin provides a means of assessing the validity of corporate defensive actions without waiting for the hypothetical injury to become an actual injury. As such, it is an appropriate standard here. *Unitrin* considers the future and the hypotheticals with a clear framework, based on whether measures are reasonable or draconian. This is the means this Court should employ to analyze the equitable balance at hand, because no actual injury has occurred and, as the lower court agreed, the *Blasius* standard is inappropriate. *Unitrin* solves the problems contemplated in *Stroud* without resorting to vague equity balancing or the inappropriate *Blasius* standard.

III. APPLYING *UNOCAL* TO THE INSTANT CASE, THE FEE SHIFTING BYLAW IS VALID BECAUSE THE TALBOT'S BOARD MEETS THE TWO PRONG *UNOCAL* REASONABLE THREAT, REASONABLE RESPONSE STANDARD.

A. Question Presented

Whether Talbot's Fee Shifting Bylaw meets the two prong *Unocal* standard.

B. Standard of Review

This Court reviews the Court of Chancery's grant of preliminary injunction for an abuse of discretion, "without deference to the embedded legal conclusions of the trial court." *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 394 (Del. 1996). Legal conclusions are subject to *de novo* review. *Id.*

C. Merits of the Argument

i. Talbot had reasonable grounds to believe that Alpha Fund, a corporate raider, was a danger to corporate policy and effectiveness.

Reasonably, Talbot perceived a threat that Alpha Fund's restructuring plan might deceive shareholders into voting for a new board, as the plan did not take into account the cost cutting measures Talbot already had under way. Under *Unocal*, the directors must demonstrate they had "reasonable grounds for believing that a danger to corporate policy and effectiveness existed" by "demonstrating good faith and reasonable investigation. *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140, 1153 (Del. 1989). "Refusal to entertain an offer may comport with a valid exercise of a board's business

judgment." *Id.*; *See, e.g., Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1285 n. 35 (Del. 1989); *Smith v. Van Gorkom*, 488 A.2d 858, 881 (Del. 1985), *overruled on other grounds*, *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009); *Pogostin v. Rice*, 480 A.2d 619, 627 (Del. 1984), *overruled on other grounds*, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) The *Unocal* standard is flexible, and it's open-ended analysis is intended to "militate against the court engaging in a process of attempting to appraise and evaluate the relative merits of a long-term versus a short-term investment goal for shareholders." *Paramount Communications, Inc.* 571 A.2d at 1154.

The Talbot board was addressing an imminent takeover by an organization various media sources had described as a "determined activist investor that had successfully caused other companies to undergo one form of restructuring or another." *Alpha Fund Mgmt. v. Talbot Inc.*, No. 10428-CJ at *5 (D. Del. Jan. 14, 2015) (order granting preliminary injunction). Talbot reasonably investigated the threat at the special meeting of the Board on December 18, which was exclusively devoted to the Alpha Schedule 13D filing. *Id.* The meeting lasted more than two hours and included detailed presentations from outside counsel about the terms of the restructuring as well as the ongoing cost cutting plans for Talbot three divisions. *Id.* The presence of a majority of outside independent directors on the Talbot board materially enhanced the evidence of a threat. *See Unocal*, 493 A.2d at 955. *Accord Paramount Communications, Inc. v. Time, Inc.,* 571 A.2d 1140, 1154 (Del. 1989); *Polk v. Good,* 507 A.2d 531, 537 (Del.

1986); *Moran v. Household Int'l, Inc.*, 500 A.2d 1346, 1356 (Del. 1985).

For the above reasons, the Talbot board's investigation was reasonable. It is the board's place to make business decisions on behalf of the corporation. The board may balance short term versus long term benefits and perceive an activist raider as threat. So long as the board's response to the reasonably perceived threat was proportional and not preclusive, the board may properly make business decisions on behalf of the corporation.

ii. Talbots' response was reasonable in relation to the threat posed because it was not preclusive and did not overly interfere with the shareholder voting franchise.

In responding to the threat of a hostile raider with short term cash out goals in mind, Talbot acted proportionally and did not preclude a takeover or overly interfere with the shareholder voting franchise. The reasonableness of a defensive action is in proportion to the nature of the threat: this "requires an evaluation of the importance of the corporate objective threatened; alternative methods of protecting that objective; impacts of the 'defensive' action, and other relevant factors." *Paramount Communications, Inc.* 571 A.2d at 1154 (quoting *In Re: Time Incorporated Shareholder Litigation*, Del.Ch., 1989 WL 79880 (July 14, 1989)).

Delaware law confers on corporate directors a fiduciary duty to act in the best interest of the corporation's stockholders; this duty extends

to protecting the corporation and its owners from perceived harm. 8 Del.C. §§ 141(a), 160(a); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985). A board of directors addressing a pending takeover has the obligation to determine what is in the best interests of the corporation and its shareholder, and in that respect it is no different from any other responsibility the board shoulders and is entitled to no less respect than would otherwise be accorded in business. *Id.*, *Dodge v. Ford Motor Co.*, 170 N.W. 668 (Mich. 1919), *Aronson v. Lewis,* 473 A.2d 805, 812 (Del. 1984). The fiduciary duty to manage a corporation "includes the selection of a time frame for achievement of corporate goals" and "[d]irectors are not obligated to abandon a deliberately conceived corporate plan." *Paramount Communications, Inc.* 571 A.2d at 1155. However, even in response to a reasonable threat, "management actions that are coercive in nature or force upon shareholders" may be struck down as an unreasonable and non-proportionate response. *Id.* at 1154.

The Talbot Fee Shifting Bylaw has not precluded shareholders from voting in a proxy contest, nor has it stopped the initiation of a proxy contest; it merely allocates risk. This is contrasted with *Schnell*, where the court found that moving up the shareholder meeting so a raider could not have its proxy votes pass SEC muster was preclusive. *Schnell v. Chris-Craft Industries, Inc.*, 285 A.2d 437, 439 (1971). Here, there is nothing to stop a proxy vote with outside candidates on the ballot. However, by allocating the risk of failure to the challenger, the fee shifting bylaw does ensure that outside candidates must be serious and have a reasonable chance of success on

the merits of their challenge; it also ensures they are not merely wasting the board's time and corporate money in defense.

For the above reasons, the Talbot board acted reasonably and proportionally in response to a reasonably perceived threat and did not preclude a proxy contest. Thus, *Unocal* is satisfied, and the Talbot board's actions are reviewed under the presumption of the Business Judgment Rule. *Smith v. Van Gorkom*, 488 A.2d 858, 881 (Del. 1985), *overruled on other grounds, Gantler v. Stephens*, 965 A.2d 695 (Del. 2009). Under that rule, the Talbot board's actions are reasonable unless grossly negligent, which the plaintiff's have not alleged in this case. Thus, the Fee Shifting Proxy Bylaw is legal.

CONCLUSION

For the foregoing reasons, Defendant-Appellant respectfully requests that this Court reverse the Chancery Court's order granting Plaintiff-Appellee's motion for preliminary injunction.