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NATURE AND STAGE OF THE PROCEEDINGS

On September 15, 2003, plaintiff Dhruv Khanna commenced this action by filing a Derivative and Class Action Complaint in the Court of Chancery for the State of Delaware. The original complaint asserted various claims against Charles McMinn, Daniel Lynch, Frank Marshall, Rich Shapero, Robert Hawk, Robert E. Knowling, Jr., Debra Dunn, Hellene Runtagh, Larry Irving, Charles Hoffman, L. Dale Crandall, Richard A. Jalkut (together, the "Individual Defendants"), and Crosspoint Venture Partners, L.P. ("Crosspoint"). Plaintiff Khanna also named Covad Communications Group, Inc. ("Covad") as a defendant and nominal defendant.

On December 12, 2003, Covad, the Individual Defendants, and Crosspoint moved separately to dismiss the original complaint on various grounds, including failure to state a claim upon which relief can be granted. In response to the defendants' motions, plaintiff Khanna filed an Amended Derivative and Class Action Complaint on August 3, 2004. Like the original complaint, the amended complaint asserted derivative and/or class action claims against Covad, the Individual Defendants and Crosspoint. The amended complaint, however, also added new plaintiffs and new claims to the case.

On August 23, 2004, Crosspoint filed a motion to dismiss the amended complaint pursuant to Court of Chancery Rule 12(b)(6) for failure to state a claim upon which relief can be granted. This is Crosspoint's opening brief in support of its motion to dismiss. Crosspoint also adopts and incorporates by reference the arguments set forth in the motion to disqualify and motion to dismiss papers filed by Covad ("Covad Mem.") and the Individual Defendants ("Ind. Def. Mem.").

PRELIMINARY STATEMENT

This matter is part of a broader dispute initiated by plaintiff Khanna, the former general counsel of Covad against the Company and a number of its former directors. Mr. Khanna and his fellow plaintiffs generally allege that Covad's directors breached their fiduciary duty of loyalty to the Company by improperly approving a number of purportedly self-interested transactions. The amended complaint then seeks to hold Crosspoint secondarily liable to Covad in connection with certain of those challenged transactions relating to Certive Corporation ("Certive") and BlueStar Communications Group ("BlueStar"). Plaintiffs also assert an additional derivative claim against Crosspoint and certain Covad directors for allegedly usurping a Covad corporate opportunity. As shown below, plaintiffs' three "Counts" against Crosspoint should be dismissed because, in each instance, plaintiffs have failed to state a claim.¹

Count II: Corporate opportunity. Plaintiffs' claim that Crosspoint should be liable to Covad for usurping a corporate opportunity is fundamentally flawed in several respects. As an initial matter, the claim, based on a Crosspoint fund's investment in a 1999 Series A financing, is time-barred. In addition, the allegations of the amended complaint fail to support a key element of a corporate opportunity claim, namely, that Crosspoint owed fiduciary duties to Covad. *See infra* at 8-11.

Count VII: Respondeat superior. Plaintiffs' claim that Crosspoint should be vicariously liable for alleged breaches of the duty of loyalty committed by two of Covad's directors (who also were respectively a "General Partner" and "Special Limited Partner" of Crosspoint) is similarly flawed. Plaintiffs have not stated any viable claim for breach of fiduciary duty against the Individual Defendants (*see generally* Ind. Def. Mem.), and, therefore, there can be no vicarious liability under the doctrine of respondeat superior. Moreover, the respondeat superior

¹ The amended complaint also should be dismissed in its entirety for the reasons set forth in the motion to disqualify and motion to dismiss papers filed by Covad and the Individual Defendants.

claim fails as a matter of law because it runs counter to the well-established principle that only a controlling shareholder owes a fiduciary duty to the corporation. Delaware authority rejects the notion that plaintiffs can circumvent this rule by resort to theories that would, in essence, create vicarious fiduciary duties. *See infra* at 12-17.

Count VI: Aiding and abetting. Plaintiffs' claim against Crosspoint for aiding and abetting supposed wrongdoing by Covad's directors also fails because the amended complaint does not state an actionable claim for breach of fiduciary duty. *See generally* Ind. Def. Mem. Moreover, the amended complaint lacks any well-pleaded factual allegations that Crosspoint "knowingly participated" in purported misconduct by Covad's board – an essential element of aiding and abetting liability. Plaintiffs do not allege (other than in the most conclusory fashion) that Crosspoint participated in Covad's negotiations with Certive or BlueStar or improperly encouraged Covad's directors to approve those transactions. This is not sufficient to state a claim. *See infra* at 17-22.

For all of the foregoing reasons, the claims against Crosspoint should be dismissed.

SUMMARY OF RELEVANT ALLEGATIONS

Crosspoint respectfully refers the Court to the briefs filed by Covad and the Individual Defendants for general statements regarding the parties and facts underlying this dispute. *See* Covad Mem. at 5-14; Ind. Def. Mem. at 1-7. The allegations pertinent to the claims against Crosspoint are as follows:²

A. Crosspoint and the Covad Board

Plaintiffs allege that Crosspoint is a venture capital firm. ¶ 18.³ Plaintiffs assert in conclusory fashion that Crosspoint was a "controlling shareholder" of Covad and note that at one

² Crosspoint disputes many of the allegations of the amended complaint. For purposes of this motion only, however, the well-pleaded, non-conclusory allegations in the amended complaint are taken as true.

³ All paragraph references are to the amended complaint filed August 3, 2004.

time Crosspoint owned up to 5 million shares of the Company's stock. ¶ 151. The amended complaint does not indicate the total number of Covad's outstanding shares, however, or plead any other facts from which this Court could conclude that Crosspoint's holdings constituted a substantial percentage – much less a majority – of Covad's shares at any given time. To the contrary, plaintiffs acknowledge that Crosspoint distributed its shares of Covad stock shortly after the Company's initial public offering in 1999. ¶¶ 18, 178. The amended complaint also concedes that Warburg Pincus – not Crosspoint – was the lead investor in Covad, and trumpets the fact that nominal plaintiff Khanna was the “largest or one of the largest” Covad individual stockholders. ¶¶ 5, 34.

At all relevant times, Covad's board of directors was comprised of no less than seven members. *See* Covad Mem. at 39, 41, 44, 45. Defendant Richard Shapero, a Covad director from July 1997 through May 2002, also was a “General Partner” and “Managing Partner” of Crosspoint. ¶¶ 11, 18, 38. While plaintiffs allege that defendant Robert Hawk, a Covad director since April 1998, was a “Special Limited Partner” of Crosspoint, the amended complaint offers no indication that that role held any particular significance. ¶¶ 12, 18, 36.⁴ Plaintiffs nonetheless conclude that Messrs. Shapero and Hawk “acted as agents of Crosspoint.” ¶ 18.

Plaintiffs also weakly attempt to connect Covad directors McMinn and Marshall to Crosspoint. The amended complaint alleges that defendant McMinn, who was a founder of Covad and a director at various times (from April 1997 to November 1, 1999, and from October 2000 to the present), contemplated pursuing “investment opportunities with Crosspoint” that would be “a win-win for Covad” in the spring of 1999. ¶ 43; *see also* ¶¶ 42, 44, 48; Covad Mem. at 33. Plaintiffs also allege that defendant Marshall, a Covad director from October 1997

⁴ *See* 6 DEL. C. § 17-303 (a limited partner need not be an employee or agent of the limited partnership, and is not required to participate in control of the business); *accord* CAL. CORP. CODE § 15632. While not necessary for purposes of this motion, it bears emphasizing that Mr. Hawk in fact was not an employee of Crosspoint, did not have a carried interest in the partnership, and in no way controlled its business.

to December 2002, was a partner at a different venture capital firm that “invested alongside” Crosspoint in some companies. ¶¶ 10, 35. The amended complaint, however, does not contend that Mr. McMinn or Mr. Marshall were agents of, or controlled by, Crosspoint.

B. The Derivative Claims Against Crosspoint

During the alleged relevant time period, certain Crosspoint venture funds made investments in various broadband infrastructure and e-business services companies, such as Covad (¶ 39), Certive (¶ 49), and BlueStar (¶ 59). Nominal plaintiffs claim that Crosspoint should be held liable to Covad for usurping a corporate opportunity (Count II ¶¶ 149-157) and held secondarily liable for certain purported breaches of fiduciary duty concerning Covad’s transactions with Certive and BlueStar (Counts VI, VII ¶¶ 177-190).⁵

1. The Corporate Opportunity Allegations (Series A Financing)

In 1999, defendant McMinn, a Covad founder, founded Certive Corporation along with two other individuals. ¶¶ 8, 50. According to plaintiffs, Covad’s business was a wholesale digital subscriber line (DSL) business. ¶ 21. By contrast, Certive’s business plan was to provide “computerized data integration services” (¶ 50) in what plaintiffs claim was “[a] highly speculative and dubious new project” (¶ 159). Mr. McMinn and a Crosspoint fund were among the investors in Certive’s Series A financing (“Series A Financing”). ¶ 49. Plaintiffs claim that because Mr. McMinn was a Covad director and employee at the time, and because Crosspoint was a Covad shareholder, that their investments in the Series A Financing usurped a Covad corporate opportunity.

⁵ Plaintiffs also assert claims against various defendants (but not Crosspoint) based on defendant McMinn’s options vesting, a transaction with Dishnet and on various Covad proxy statements. *See, e.g.*, Amended Complaint, Counts I, III-V, VIII-X. While plaintiffs allege that Crosspoint was a shareholder in two of Covad’s vendors, Diamond Lane and Efficient Technologies (¶ 11), and that Mr. Shapero sat on the board of another DSL company, New Edge Networks (*id.*), the amended complaint does not assert any claim for breach of fiduciary duty based on those relationships.

2. The Certive Transaction

In October 1999, Covad's board voted to approve a \$5 million investment in a Series B-1 later round of financing for Certive. ¶¶ 55, 57. Mr. McMinn did not attend the board meeting; Mr. Shapero recused himself from the vote. *See* Covad Mem. at 39; Ind. Def. Mem. at 19. Covad's investment subsequently was written down. ¶ 57. Plaintiffs allege in conclusory fashion that the other directors breached their fiduciary duty of loyalty by approving the Certive Transaction solely to benefit Mr. McMinn and Crosspoint. ¶ 160. Plaintiffs seek to hold Crosspoint secondarily liable for this alleged breach of fiduciary duty.

3. The BlueStar Transactions

In June 2000, Covad agreed to a stock-for-stock acquisition of BlueStar Communications Group (the "BlueStar Merger"), which was liquidated a year later. *See* ¶ 82. BlueStar was a retail DSL provider in geographic and consumer markets that Covad had not entered. *See* ¶¶ 58-59, 67, 69-70. Because certain Crosspoint funds had invested in BlueStar, and Mr. Shapero was also a director of BlueStar, plaintiffs contend that Covad's directors approved the merger to benefit Crosspoint, rather than Covad, in violation of their fiduciary duties. ¶¶ 164-167. Though neither Mr. Shapero nor Mr. Hawk took part in board meetings or voting concerning the BlueStar merger (*see* Covad Mem. at 41, Ind. Def. Mem. at 28-29) plaintiffs allege that Crosspoint must have been substantially involved in the merger discussions, referring to two emails Mr. Shapero sent to Covad CEO Bob Knowing in May 2000. ¶ 62. Plaintiffs claim that Crosspoint thus is secondarily liable for any fiduciary duty breach relating to the BlueStar Merger.

In addition, plaintiffs complain that Covad's directors breached their fiduciary duties by allowing the Company, in 2001, to enter into a negotiated settlement of an earn-out provision in the merger agreement pursuant to which former BlueStar shareholders, including certain Crosspoint funds, received additional shares of Covad stock (the "BlueStar Earn-Out"). ¶ 168. While again, neither Mr. Shapero nor Mr. Hawk had a part in Covad's decision (Covad Mem. at

44), plaintiffs contend that Crosspoint benefited from the BlueStar Earn-Out and thus should be held secondarily liable for any breaches of fiduciary duty.

ARGUMENT

I. LEGAL STANDARDS

Crosspoint moves under Court of Chancery Rule 12(b)(6) to dismiss Counts II, VI and VII of the amended complaint, brought derivatively on behalf of Covad against Crosspoint. On a motion to dismiss, courts consider the allegations in the amended complaint and documents incorporated by reference therein. *Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, Del. Ch., 833 A.2d 961, 970 (2003), *aff'd*, Del. Supr., 845 A.2d 1040 (2004). In determining the sufficiency of claims, courts must accept all well-pleaded factual allegations as true, but is free to disregard conclusory allegations unsupported by such factual allegations. *Id.* (citing cases). Courts will draw only logical and reasonable inferences from the complaint in favor of the plaintiffs. *Id.* Moreover, a claim may be dismissed if allegations in the complaint, documents incorporated by reference, or judicially noticeable facts effectively negate the claim as a matter of law. *See Malpiede v. Townson*, Del. Supr., 780 A.2d 1075, 1083 (2001).⁶

Under this standard, Crosspoint's motion to dismiss should be granted. Plaintiffs cannot prevail on the facts that may reasonably be inferred from the well-pleaded allegations of the amended complaint. Instead, the amended complaint lacks sufficient allegations to support key elements of plaintiffs' claims against Crosspoint, and both plaintiffs' pleading and judicially noticeable facts make clear that several of the claims are time-barred.

⁶ *See also In re Santa Fe Pacific Corp. S'holder Litig.*, Del. Supr., 669 A.2d 59, 69 (1995) (taking judicial notice of documents that were publicly filed with the Securities and Exchange Commission (SEC); "[i]t was certainly proper to consult the Joint Proxy to analyze the disclosure claim because the operative facts relating to such a claim *perforce* depend upon the language of the Joint Proxy"); *In re USACAFES, L.P. Litig.*, C.A. No. 11146, 1993 WL 18769, at *3-4 (Del. Ch. Jan. 21, 1993) (taking notice of reports that were publicly filed with the SEC on Form 10-K in determining whether inquiry notice was triggered and claims were barred by statute of limitations).

II. PLAINTIFFS FAIL TO STATE A CLAIM AGAINST CROSSPOINT FOR USURPING A CORPORATE OPPORTUNITY

Count II of the amended complaint asserts that Crosspoint usurped a corporate opportunity from Covad by investing in Certive's 1999 Series A financing without offering Covad "the contemporaneous opportunity to participate." ¶¶ 149-157.

A. Plaintiffs' Claim Is Time-Barred.

Plaintiffs' corporate opportunity claim is barred by a three-year statute of limitations or its equitable analogue, the doctrine of laches. *See* Ind. Def. Mem. at 8-13. Crosspoint joins in and adopts the arguments presented in detail in the Individual Defendants' brief. In summary, the so-called "corporate opportunity" in the Series A Financing took place in 1999 (¶ 48), and the statutory period began to run from the date of that alleged wrongful act. *Fike v. Ruger*, Del. Ch., 754 A.2d 254, 260 (1999), *aff'd*, Del. Supr., 752 A.2d 112 (2000). At the time, plaintiff Khanna was the general counsel of Covad, yet he did not file his action until September 2003 – more than a year after the limitations period had run. Plaintiffs have pleaded none of the required "specific facts" that could permit the tolling of the statute. *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, C.A. No. 19875, 2004 WL 405913, at *6 (Del. Ch. Mar. 2, 2004). Nor does the filing of a new complaint by new plaintiffs circumvent the statute of limitations. The new plaintiffs' claims are time-barred because they were on inquiry notice of a potential corporate opportunity claim at least by November 2000 (*see* Ind. Def. Mem. at 10), yet they did not assert their claims until August 2004 – more than three years later. Finally, the "relation back" doctrine cannot help plaintiffs because Mr. Khanna's complaint was untimely-filed. *See id.* at 10-11, *citing, e.g., Reyes v. Kent Gen. Hosp.*, Del. Supr., 487 A.2d 1142, 1146 (1984). Accordingly, the corporate opportunity claim should be dismissed.

B. The Corporate Opportunity Claim Should Be Dismissed Because Plaintiffs Do Not Sufficiently Plead that Crosspoint Was a Fiduciary of Covad.

A claim for usurping a corporate opportunity is a type of breach of fiduciary duty claim. *Kahn v. Icahn*, C.A. No. 15916, 1998 Del. Ch. LEXIS 223, at *11-13 (Del. Ch. Nov. 12, 1998),

aff'd, Del. Supr., 746 A.2d 276 (2000). Under the corporate opportunity doctrine, a fiduciary may not take a business opportunity for his own if, *inter alia*, the opportunity is within the corporation's line of business. See *Broz v. Cellular Info. Sys., Inc.*, Del. Supr., 673 A.2d 148, 154 (1996).⁷ Only corporate fiduciaries may be liable for usurping a corporate opportunity; claims against non-fiduciaries must be dismissed. See *Kahn*, 1998 Del. Ch. LEXIS 223, at *11 (“The corporate and partnership opportunity doctrine ‘represents but one species of the broad . . . duties assumed by a fiduciary’”), quoting *Broz*, 673 A.2d at 154; see also *In re The Walt Disney Co. Derivative Litig.*, C.A. No. 15452, 2004 Del. Ch. LEXIS 132, at *18-19 (Del. Ch. Sept. 10, 2004) (granting summary judgment on corporate opportunity claim, on the grounds that, *inter alia*, defendant was not a fiduciary of corporation at time of alleged breaches).

Count II should be dismissed here because the amended complaint does not sufficiently plead that Crosspoint was a fiduciary of Covad. As a shareholder of Covad, Crosspoint “could attain fiduciary status only if it were a majority shareholder or if it actually controlled the affairs of [Covad].” *Emerson Radio Corp. v. International Jensen Inc.*, C.A. Nos. 15130, 14992, 1996 WL 483086, at *20 (Del. Ch. Aug. 20, 1996); *Ivanhoe Partners v. Newmont Mining Corp.*, Del. Supr., 535 A.2d 1334, 1344 (1987) (“a shareholder owes a fiduciary duty [to a corporation] only if it owns a majority interest in or exercises control over the business affairs of the corporation”). While plaintiffs assert that Crosspoint was “a controlling shareholder” and fiduciary of Covad, ¶ 151, the amended complaint contains no well-pleaded facts that support this conclusory (and incorrect) allegation.

⁷ In general, to state a claim for usurping a corporate opportunity, plaintiffs must plead facts that would establish (1) the corporation was financially able to exploit the opportunity, (2) the opportunity was within the corporation's line of business, (3) the corporation had an interest or expectancy in the opportunity, and (4) by taking the opportunity for himself, a fiduciary placed himself in a position inimical to his duties to the corporation. See *Beam*, 833 A.2d at 972-973 (dismissing corporate opportunity claim: while in a “strictly literal sense,” a “consumer products company” had “fundamental knowledge and practical experience” in selling its own stock, that activity was simply not within the company's line of business of “selling advice to homemakers”) (citation omitted).

Plaintiffs urge the Court to infer that Crosspoint was a controlling shareholder of Covad based upon the single allegation that, at some undefined time, Crosspoint owned “between 1.5 million to 5 million of Covad’s outstanding shares.” *Id.* Plaintiffs, however, fail to allege or plead any facts from which this Court could conclude, that this number of shares constituted a substantial interest – much less a majority interest – in Covad. Indeed, the amended complaint concedes that Warburg Pincus was the “lead investor” in Covad. ¶ 34.⁸ A stockholder will not be deemed a fiduciary of a Delaware corporation merely because he owns a minority interest in the corporation. *See, e.g., Oliver v. Boston Univ.*, C.A. No. 16570, 2000 Del. Ch. LEXIS 104, at *5, 20-21 (Del. Ch. July 18, 2000) (dismissing breach of fiduciary duty claim; shareholders did not have fiduciary status merely because they held, collectively, 10% of the corporation’s stock). Indeed, Delaware courts routinely hold that “substantial non-majority stock ownership, without more, does not indicate control.” *In re Western Nat’l Corp. S’holders Litig.*, C.A. No. 15927, 2000 Del. Ch. LEXIS 82, at *21 (Del. Ch. May 22, 2000) (mere allegation that defendant held a 46% equity position in the company insufficient to establish “control” status).⁹

Absent any allegations that Crosspoint owned a majority interest in Covad, “[t]he question becomes whether it is inferable from the [amended] complaint’s well pleaded allegations that [Crosspoint] actually exercised domination and control over [Covad’s]

⁸ In the fall of 1999, there were over 71 million Covad shares outstanding. Declaration of David C. McBride (“McBride Decl.”), Ex. A at 1, filed concurrently herewith. Thus, “1.5 million to 5 million” shares owned by Crosspoint would have amounted to only 7% of Covad’s outstanding stock. Notably, plaintiff Khanna owned nearly as much stock as Crosspoint did. McBride Decl., Ex. B at 58-60 (disclosing that plaintiff Khanna held 4,540,579 shares of Covad stock as of September 30, 1999). *See Jacobs v. Yang*, C.A. No. 206, 2004 Del. Ch. LEXIS 117, at *18 (Del. Ch. Aug. 2, 2004) (recognizing that on a motion to dismiss, the court may take judicial notice of certain facts that are a matter of public record).

⁹ *See also, e.g., In re Shoe-Town, Inc. S’holders Litig.*, C.A. No. 9483, 1990 WL 13475, at *6 (Del. Ch. Feb. 12, 1990) (10% share ownership held insufficient; “a non-majority shareholder owes no fiduciary duty absent specific factual allegations that the minority shareholder dominated and controlled the corporation”); *In re Sea-Land Corp. S’holder. Litig.*, [1988-1989 Tr. Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,923, at 90,186 (Del. Ch. May 13, 1988) (dismissing complaint; 39.5% stock ownership insufficient).

directors.” *Siegman v. Tri-Star Pictures, Inc.*, C.A. No. 9477, 1989 Del. Ch. LEXIS 56, at *10 (Del. Ch. May 5, 1989); *Western Nat’l*, 2000 Del. Ch. LEXIS 82, at *18 (“In the absence of majority stock ownership, a plaintiff must demonstrate that the minority shareholder held a dominant position and actually controlled the corporation’s conduct”). The sole facts that plaintiffs allege respecting Crosspoint’s purported “domination and control” over Covad are that Covad directors Shapero and Hawk were the General Partner and a “Special Limited Partner,” respectively, of Crosspoint during 1999. ¶¶ 11-12, 18, 48. Messrs. Shapero and Hawk, however, were only two members of Covad’s eight member board at the time, and plaintiffs plead no facts to support a conclusion that either man “dominated and controlled” the other Covad directors. See Covad Mem. at 39; Ind. Def. Mem. at 21-23 (discussing director independence).¹⁰ Thus, plaintiffs have failed to meet the standard for pleading that Crosspoint was a controlling shareholder. See, e.g., *Siegman*, 1989 Del. Ch. LEXIS 56, at *10-12 (dismissing fiduciary duty claim; finding that 9% shareholder “had no power to exercise actual board control” because, *inter alia*, “[i]t had only three designees on [the corporation’s] ten person board”); *Oliver*, 2000 Del. Ch. LEXIS 104, at *20-21) (shareholders’ 10% ownership interest and relationship with some of the corporation’s directors and affiliates did not support an inference of control). Because plaintiffs have not sufficiently pleaded that Crosspoint was a fiduciary of Covad, the corporate opportunity claim should be dismissed. See *Walt Disney*, 2004 Del. Ch. LEXIS 132, at *25 n.51; *Kahn*, 1998 Del. Ch. LEXIS 223, at *11.

¹⁰ Plaintiffs’ attempts to connect Crosspoint with directors McMinn and Marshall fall woefully short of pleading domination or control. See *supra* at 4-5. Plaintiffs claim that Mr. McMinn advised Covad CEO Knowling that he was considering pursuing “investment opportunities with Crosspoint” in the spring of 1999. ¶ 43. Plaintiffs allege that Mr. Marshall was associated with another venture fund that “invested alongside” Crosspoint in other companies. ¶ 10. The amended complaint, however, never alleges – even in conclusory fashion – that either Mr. McMinn or Mr. Marshall ever was employed by, controlled by, or acting as an agent of, Crosspoint. See Ind. Def. Mem. at 22, 43, citing, e.g., *Litt v. Wycoff*, C.A. No. 19083, 2003 WL 1794724, at *4 (Del. Ch. Mar. 28, 2003) (“critical issue . . . is whether the director was conflicted in his loyalties with respect to challenged board actions”).

III. PLAINTIFFS' RESPONDEAT SUPERIOR CLAIM SHOULD BE DISMISSED

Count VII of the amended complaint asserts that Crosspoint should be secondarily liable under the respondeat superior doctrine for alleged breaches of fiduciary duty by Crosspoint's General Partner, Shapero, and "Special Limited Partner," Hawk, in connection with the Certive Transaction (Covad's \$5 million investment in Certive's Series B-1 financing) and the BlueStar Transactions. ¶¶ 184-190. This claim should be dismissed for multiple reasons.

A. Plaintiffs Do Not Sufficiently Plead an Underlying Breach of Fiduciary Duty.

An employer can only be liable under the doctrine of respondeat superior where there is an underlying "viable cause of action" against its employee. *See Greco v. University of Delaware*, Del. Supr., 619 A.2d 900, 903-904 (1993) (dismissing respondeat superior claim absent viable claim against employee); *Curtis v. Martelli*, C.A. Nos. 93C-11-064, 94C-06-227, 1996 WL 111168, at *3 (Del. Super. Ct. Jan. 23, 1996) (same).¹¹ Thus, absent a viable cause of action against Mr. Shapero or Mr. Hawk, plaintiffs' respondeat superior claim against Crosspoint must be dismissed. *See Greco*, 619 A.2d at 903-904. Here, the individual defendants have shown that there is no actionable fiduciary duty claim with respect to the Certive Transaction or the BlueStar Transactions for the reasons summarized below and set forth in greater detail in the individual defendants' opening brief. *See generally* Ind. Def. Mem. at 8-33.

1. The Certive Transaction

As an initial matter, any fiduciary duty claims concerning the Certive Transaction in October 1999 are barred by the expiration of the limitations/laches period, for the same reasons that the 1999 corporate opportunity claim is barred. *See supra* at 8; *see generally* Ind. Def. Mem. at 17-19. In addition, plaintiffs fail to state a viable loyalty claim concerning Covad's \$5 million investment in the Series B-1 financing, because that transaction was approved by a majority of Covad's disinterested and independent directors. *See id.* (showing that plaintiffs do

¹¹ Notably, plaintiffs do not even allege that Mr. Hawk was a Crosspoint employee.

not adequately allege director interest and lack of independence with respect to majority of directors); 8 DEL. C. § 144 (providing safe harbor for decisions made by disinterested directors). The amended complaint is devoid of allegations that Certive founder McMinn or Crosspoint General Partner Shapero voted on the Certive Transaction – neither of them took part in this decision. *See* Covad. Mem. at 39; Ind. Def. Mem. at 19. The amended complaint admits that such recusal was the normal practice in situations of director interest. *See* ¶ 80 (“[U]nder normal Covad practice, self-interested directors would have left any Board meeting when matters pertaining to their self-interest [we]re discussed and voted upon”). Accordingly, plaintiffs have failed to state a breach of fiduciary duty claim with respect to Certive.

2. The BlueStar Transactions

The amended complaint also fails to state a fiduciary duty claim based on the BlueStar Merger (¶¶ 164-167) or the BlueStar Earn-Out (¶ 168). *See generally* Ind. Def. Mem. at 25-33. As an initial matter, the claims concerning the BlueStar Merger are untimely. *Id.* at 25-27. The three-year statute of limitations began to run when the BlueStar Merger was approved (and announced) in June 2000, yet plaintiff Khanna did not file his original complaint until September 2003 and the new plaintiffs did not file their new complaint until August 2004. *See id.*, citing *Kahn v. Seaboard Corp.*, Del. Ch., 625 A.2d 269, 271 (1993) (limitations period on alleged fiduciary duty violations stemming from transaction began to run at time contract was executed, rather than when obligations were performed).

Moreover, plaintiffs’ claims concerning the BlueStar Transactions again run afoul of Delaware’s safe harbor for transactions approved by a majority of a corporation’s disinterested directors. *See generally* Ind. Def. Mem. at 27-33 (director disinterest and independence); 8 DEL. C. § 144. While defendants Shapero and Hawk purportedly had indirect financial interests in BlueStar (through Crosspoint), the approval of the BlueStar Merger by directors whom plaintiffs concede were disinterested forecloses any fiduciary duty violation. *See In re Frederick’s of Hollywood, Inc. S’holders Litig.*, C.A. No. 15944, 2000 WL 130630, at *7 (Del. Ch. Jan. 31,

2000) (dismissing fiduciary duty claim; where “interested” director transaction approved by a majority of “disinterested” directors, “the duty of loyalty claim fails for lack of a valid premise”); *see also Orman v. Cullman*, Del. Ch., 794 A.2d 5, 23 (2002) (“[i]f a plaintiff alleging a duty of loyalty breach is unable to plead facts demonstrating that a majority of a board that approved the transaction in dispute was interested and/or lacked independence, the entire fairness standard of review is not applied and the Court respects the business judgment of the board”). Plaintiffs, similarly, must concede that the BlueStar Earn-Out was approved by Covad’s disinterested directors, without defendants Shapero, Hawk, and McMinn. *See* Ind. Def. Mem. at 32-33.

This result is not changed by plaintiffs’ new allegations that Mr. Shapero – who concededly did not participate in board meetings or votes concerning BlueStar – sent two emails about BlueStar to Mr. Knowing during May 2000 that “lobbied” Mr. Knowing to have Covad acquire BlueStar. *See* ¶¶ 62, 80, 164. Delaware courts repeatedly have recognized that a director may even negotiate or participate in a self-interested transaction so long as the board’s disinterested directors ultimately make an informed and independent decision to approve the transaction. *See Yanow v. Scientific Leasing, Inc.*, [1987-1988 Tr. Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,660, at 98,034 (Del. Ch. Feb. 5, 1988) (“disinterested” directors did not breach their fiduciary duty by allowing the company’s “interested” directors to negotiate a merger because “the acquisition agreement was considered at length and in depth by the entire Board, a majority of whom were disinterested, outside directors with no personal stake in the outcome”); *State of Wisconsin Investment Board v. Bartlett*, C.A. No. 17727, 2000 Del. Ch. LEXIS 42, at *14 (Del. Ch. Feb. 24, 2000) (five-member board did not breach its fiduciary duty by delegating to its “interested” chairman the task of negotiating a merger”); *see also In re Ply Gem Indus., Inc, S’holders Litig.*, No. 15779, 2001 Del Ch. LEXIS 84, at *41 (Del. Ch. June 26, 2001) (“There is nothing inherently wrong with an interested chief executive officer negotiating a merger transaction . . . the issue becomes whether the Ply Gem board satisfied its ‘ultimate statutory duty and fiduciary responsibility to make an informed and independent decision’ on whether to

enter into the Nortek merger transaction.”), quoting *McMullin v. Beran*, Del. Supr., 765 A.2d 910, 924 (2000). Thus, as a matter of Delaware law, allegations that Mr. Shapero communicated with Mr. Knowling concerning the BlueStar Merger do not impact the validity of the board’s decision, and plaintiffs state no actionable fiduciary duty claim. See, e.g., *Nebenzahl v. Miller*, C.A. No. 13206, 1996 WL 494913, at *1, 5 (Del. Ch. Aug. 29, 1996) (dismissing duty of loyalty claim under 8 DEL C. § 144 because disinterested board majority approved merger negotiated by three interested directors).

B. The Respondeat Superior Claim Against Crosspoint Fails as a Matter of Delaware Law.

Even assuming plaintiffs could plead an actionable breach of fiduciary duty, the claim against Crosspoint under the doctrine of respondeat superior would still fail as a matter of law. As explained above, plaintiffs have not sufficiently pleaded that Crosspoint was a controlling shareholder of Covad (nor can they).¹² See *supra* at 9-11. Only a majority or controlling shareholder is a fiduciary of the corporation, and courts have rejected attempts to create vicarious fiduciary duties for minority shareholders who do not control the corporation’s business. E.g., *id.*; *USAirways Group, Inc. v. British Airways PLC*, 989 F. Supp. 482, 494 (S.D.N.Y. 1997); *CCBN.com, Inc. v. Thomson Fin., Inc.*, 270 F. Supp. 2d 146, 151 (D. Mass. 2003). Simply put, “[t]he general tort law theory of respondeat superior cannot be used as means of circumventing clear limitations imposed by Delaware corporate law.” *British Airways*, 989 F. Supp. at 494.

In the *International Jensen* case, a class of shareholders of International Jensen, Inc. (“Jensen”) sought a preliminary injunction against a fund that was one of Jensen’s shareholders, in connection with a proposed merger between Jensen and another company. See 1996 WL 483086, at *1. Plaintiffs claimed that the fund was a fiduciary of Jensen because one of Jensen’s

¹² Plaintiffs do not even allege that Crosspoint held any Covad stock at the time Covad’s board approved the BlueStar Merger in June 2000. To the contrary, plaintiffs acknowledge that Crosspoint distributed its shares shortly after Covad’s 1999 IPO. ¶ 178.

directors was also “one of the three general partners who control[led] the entity that [was] the [fund]’s sole general partner.” *See id.* at *20 n.18. The Court of Chancery, however, found that because the fund was not a majority or controlling shareholder of Jensen, plaintiffs’ claim had “no legal foundation.” *Id.* The court explained:

If plaintiffs’ argument were the law, then whenever a director is affiliated with a significant stockholder, that stockholder automatically would acquire the fiduciary obligations of the director by reason of that affiliation alone. The notion that a stockholder could become a fiduciary by attribution (analogous to the result under the tort law doctrine of respondeat superior) would work an unprecedented, revolutionary change in our law, and would give investors in a corporation reason for second thoughts about seeking representation on the corporation’s board of directors.

Id.

In *British Airways*, a New York federal district court applying Delaware law reached a similar conclusion. *See* 989 F. Supp. at 494. That case involved a dispute over an investment agreement between US Airways Group/US Airways, Inc. (“US Air”) and British Airways PLC/Britair Acquisition Corp., Inc. (“BA”). Under the agreement, BA was permitted to appoint three directors to US Air’s board. US Air filed an action against BA’s directors, claiming that the directors had breached their fiduciary duties by withholding material information regarding BA’s intent to breach the investment agreement. US Air also asserted that BA was liable for the directors’ fiduciary breaches under a theory of respondeat superior. Dismissing plaintiff’s claim, the court found that:

[T]he imposition of respondeat superior liability on a corporation for breach of fiduciary duty by its directors on the board of another corporation would completely undermine Delaware corporate law, which limits such fiduciary duty to majority and controlling shareholders. The general tort law theory of respondeat superior cannot be used as means of circumventing clear limitations imposed by Delaware corporate law.

Id. The same principle applies even where a shareholder has multiple associates on a corporation’s board. *See CCBN.com*, 270 F. Supp. 2d at 151 (citing various authority and finding that under Delaware law, non-controlling shareholder could not be liable under doctrine

of respondeat superior for breach of fiduciary duty by its own employees and former executives who sat on corporation's board).¹³

The amended complaint suggests no rationale for this Court to depart from well-established principles of Delaware law and impose vicarious fiduciary duties upon of Crosspoint. Accordingly, plaintiffs' respondeat superior claim should be dismissed.

IV. PLAINTIFFS' AIDING AND ABETTING CLAIM SHOULD BE DISMISSED

Count VI of the amended complaint asserts a claim against Crosspoint for aiding and abetting alleged fiduciary duty violations by Covad's directors in connection with the Certive Transaction and the BlueStar Transactions. *See* ¶¶ 177-183. To withstand a motion to dismiss, however, the amended complaint must provide well-pleaded factual allegations that support the elements of aiding and abetting liability, namely: (1) the existence of a fiduciary relationship between Covad and the Individual Defendants, (2) a breach of duty by the Individual Defendants, (3) Crosspoint's knowing participation in the breach, and (4) damages. *See Malpiede*, 780 A.2d at 1096; *Katell v. Morgan Stanley Group, Inc.*, [1992-1993 Tr. Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,437, at 96,443 (Del. Ch. Jan. 14, 1993). Again, plaintiffs fail to allege facts to support key elements of this claim.

A. Plaintiffs Do Not Sufficiently Plead Any Underlying Breach of Fiduciary Duty.

As shown above, plaintiffs' conclusory allegations fail to state any claim for breach of fiduciary duty by the Covad board in connection with the Certive or BlueStar Transactions, which plaintiffs must concede were approved by a majority of disinterested Covad directors. *See supra* at 12-15; Ind. Def. Mem. at 19-23, 27-33; 8 DEL. C. § 144. The claims concerning the

¹³ *Cf. In re Northgate Computer Sys., Inc.*, 240 B.R. 328, 358 (Bankr. D. Minn. 1999) (finding "no authority under Minnesota law" for imposing respondeat superior liability on a corporation's supplier for breaches of fiduciary duty committed by officers and directors of the corporation who were also officers and directors of the supplier).

Certive Transaction and BlueStar Merger also are time-barred. *Supra* at 8, 12-13; Ind. Def. Mem. at 17-19, 25-27. Because plaintiffs have failed to plead any underlying actionable breach of fiduciary duty, they cannot maintain a claim for aiding and abetting against Crosspoint. *See Moore Bus. Forms, Inc. v. Cordant Holdings Corp.*, C.A. No. 13911, 1995 WL 662685, at *6 (Del. Ch. Nov. 2, 1995) (dismissing aiding and abetting claim “[b]ecause no cognizable breach of fiduciary duty [was] stated”); *Nebenzahl*, 1996 WL 494913, at *7 (“[w]ithout some pleaded facts evidencing a fiduciary breached a duty, a non-fiduciary cannot aid and abet”).

B. Plaintiffs Do Not Sufficiently Plead That Crosspoint Knowingly Participated In Any Breach of Duty.

To state a viable claim for aiding and abetting, “there must be some factual allegations from which ‘knowing participation’ can be inferred.” *L.A. Partners, L.P. v. Allegis Corp.*, [1987-1988 Tr. Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,505, at 97,250 (Del. Ch. Oct. 23, 1987) (granting motion to dismiss), *citing Weinberger v. Rio Grande Indus., Inc.*, Del. Ch., 519 A.2d 116 (1986)); *see Malpiede*, 780 A.2d at 1096. The amended complaint, however, contains no well-pleaded allegations indicating that Crosspoint participated in any breach of fiduciary duty concerning the Certive or BlueStar Transactions, much less that it did so knowingly.

1. Crosspoint is not alleged to have participated in the Covad board’s decisions.

Under Delaware law, the “participation” required to establish an aiding and abetting claim is not merely participation in an underlying transaction, but participation in the alleged wrongdoing. *See In re Telecommunications, Inc. S’holders Litig.*, C.A. No. 16470, 2003 Del. Ch. LEXIS 78, at *11 (Del. Ch. July 7, 2003) (dismissing claim that potential acquiror participated in breach of fiduciary duty by agreeing to terms of merger).¹⁴ The mere fact that

¹⁴ *See also Oliver*, 2000 Del. Ch. LEXIS 104, at *30 (same); *Aaron v. La Moderna*, No. C97-0233, 1997 WL 564064, at *10-11 (N.D. Cal. Aug. 27, 1997) (same; applying Delaware law).

Crosspoint funds owned shares in Certive and BlueStar does not constitute an affirmative act or assistance in furtherance of any fiduciary breach. *See Telecommunications*, 2003 Del. Ch. LEXIS 78, at *11. Plaintiffs do not claim that Crosspoint was involved in negotiating Covad's transactions; nor do they offer any specific allegations indicating that Crosspoint offered incentives to *any* director to approve those transactions. *See Aaron*, 1997 WL 564064, at *11 & n.1 (dismissing aiding and abetting claim where plaintiffs "pled no facts suggesting any actual act of assistance or participation"; distinguishing cases where "specific conduct by the alleged aider and abettor" was alleged); *Shoe-Town*, 1990 WL 13475, at *8 ("[t]he claim that Amex aided and abetted the directors in their breach of fiduciary duty must be dismissed without comment as the complaint makes no allegation of participation of any kind by Amex"); *see also Santa Fe*, 669 A.2d at 72 (dismissing aiding and abetting claim based on conclusory allegations of knowing participation); *Iotex Communications, Inc. v. Defries*, No. 15817, 1998 WL 914265, at *4 (Del. Ch. Dec. 21, 1998) (motion to dismiss aiding and abetting claim granted where "no allegations of fact that [defendant] played any substantial role in the negotiation or execution" of challenged agreements); *Siegman*, 1989 Del. Ch. LEXIS, at *13 (dismissing aiding and abetting claim where defendant "was not (to repeat) a party to the negotiations leading up to the [agreement]").

Unable to point to any actions taken by Crosspoint in connection with the Certive or BlueStar Transactions, plaintiffs instead urge that Crosspoint "participated" by acting through Messrs. Shapero and Hawk. *See* ¶ 179 ("Shapero and Hawk acted on behalf of Crosspoint").¹⁵ Conclusory allegations that Messrs. Shapero and Hawk were Covad directors and "actively encouraged, participated in and/or aided and abetted" the other directors are not an adequate

¹⁵ Again, plaintiffs do not claim that defendants McMinn or Marshall were agents of Crosspoint or acted for Crosspoint with respect to the Certive or BlueStar Transactions. *See supra* at 4-5 & n.10. Plaintiffs cannot allege that Mr. McMinn even participated in the board's decision to approve the Certive or the BlueStar Transactions, because he did not take part in those votes. *See Ind. Def. Mem.* at 19, 28-29.

substitute for the specific “factual allegations” required to state a claim. See ¶ 181; *Allegis*, [1987-1988 Tr. Binder] Fed. Sec. L. Rep. (CCH) at 97,250.¹⁶ The amended complaint lacks any factual allegations from which the Court could infer that Crosspoint instructed those directors to facilitate Covad’s approval of the Certive or BlueStar Transactions. Indeed, as noted above, Mr. Hawk did not vote on the BlueStar Transactions, and Mr. Shapero abstained from voting on BlueStar and Certive Transactions. See *supra* at 6; Covad Mem. at 39, 41, 44.

2. Plaintiffs do not adequately plead that Crosspoint must have known of purported fiduciary duty violations.

In addition, “[a] court can infer a non-fiduciary’s knowing participation only if a fiduciary breaches its duty in an inherently wrongful manner, and the plaintiff alleges specific facts from which th[e] court c[an] reasonably infer knowledge of the breach.” *Nebenzahl*, 1996 WL 494913, at *7. The amended complaint here satisfies neither requirement. There are no allegations indicating Mr. Shapero, Mr. Hawk, or any of Covad’s other directors ever acted in an “inherently wrongful” manner with respect to the Certive or BlueStar Transactions. To the contrary, plaintiffs admit it was “normal practice” for interested directors to abstain from the board’s votes. ¶ 80; see *supra* at 13-15. While plaintiffs allege that Mr. Shapero sent e-mails to defendant Knowling concerning the BlueStar Merger (¶¶ 62), as explained above, such communications were not improper. See *supra* at 14-15; *Ply Gem*, 2001 Del. Ch. LEXIS 84, at *41 (“nothing inherently wrongful” where interested CEO negotiated merger transaction); *Lewis v. Leaseway Transp. Corp.*, C.A. No. 8720, 1990 WL 67383, at *8 (Del. Ch. May 16, 1990) (dismissing aiding and abetting claim because “[t]here [was] nothing inherently wrongful about any of the purported breaches of the Leaseway directors”).

¹⁶ Cf. *Official Committee of Unsecured Creditors v. Donaldson, Lufkin & Jenrette Sec. Corp.*, No. 00 Civ. 8688, 2002 WL 362794, at *11 (S.D.N.Y. Mar. 6, 2002) (under California law, plaintiff could not state aiding and abetting claim merely by alleging that one of defendant’s principals was director of corporation involved in a breach of fiduciary duty).

Plaintiffs also fail to allege specific facts from which the Court could reasonably infer that Crosspoint knew of any fiduciary duty violations by Covad's board. The amended complaint insists that Crosspoint's knowledge should be inferred because Mr. Shapero was a General Partner, and Mr. Hawk was a "Special Limited Partner" of Crosspoint.¹⁷ ¶¶ 180-181. Under Delaware law, however, a director's association with a defendant does not automatically create a reasonable inference that the defendant knew of the director's purported breach. *See, e.g., Barbieri v. Swing-N-Slide*, C.A. No. 14239, 1997 WL 55956, at *3 (Del. Ch. Jan. 29, 1997) (allegation that one member of general partnership violated fiduciary duty to another corporation did not support claim that partnership itself "knew" of or aided and abetted the breach). In *Greenfield v. National Medical Care, Inc.*, Nos. 7720, 7765, 1986 WL 6505 (Del. Ch. June 6, 1986) ("*NMC*"), allegations that a director had strong ties to the shareholder defendant were insufficient to plead knowing participation. *Id.* at *3-5. Former shareholders of NMC filed suit against NMC, its directors, and W.R. Grace & Co. ("*Grace*") in connection with a leveraged buy-out of NMC by Grace and NMC management. Plaintiffs alleged that NMC's directors breached their fiduciary duty by failing to inform themselves about the true value of the company; plaintiffs also asserted an aiding and abetting claim against Grace. One of NMC's directors was also a director of a Grace subsidiary. Notwithstanding these relationships, the complaint did not create an inference of "knowing participation" by Grace:

There is nothing alleged about the timing of the transaction or the nature of the negotiations between NMC and Grace from which it could be inferred that Grace was aware of the defendant directors' alleged failure to properly inform themselves with respect to the transaction.

Id. at *4.¹⁸

¹⁷ Once again, it is worth noting that as a "Special Limited Partner," Mr. Hawk was not (nor is he alleged to have been) an employee of Crosspoint. *See supra* at n.4.

¹⁸ Similarly, in the *Rio Grande* case, Rio Grande engaged in a two-step merger with Anschutz Corporation. Plaintiffs, a class of Rio Grande shareholders, asserted claims for breach of fiduciary duty of disclosure against Rio Grande's directors in connection with the
(continued...)

Here, the mere fact that Messrs. Shapero and Hawk were associated with Crosspoint does not create a reasonable inference that Crosspoint knew of any wrongdoing those individuals allegedly committed *while acting as directors of Covad*. See *NMC*, 1986 WL 6505 at *3-4; *Rio Grande*, 519 A.2d at 122, 131. Plaintiffs fail to allege anything about the structure of Crosspoint's business – *i.e.*, what it meant to be a General Partner or “Special Limited Partner, “the authority and responsibilities of each – from which the Court could reasonably infer that Crosspoint possessed all the knowledge of Messrs. Shapero and Hawk.¹⁹ The amended complaint lacks any allegations that any director updated Crosspoint on internal Covad discussions leading up to the Certive and BlueStar Transactions. The amended complaint's conclusory allegations of Crosspoint's “knowing participation” are inadequate as a matter of law, and the aiding and abetting claim should be dismissed.

(...continued from previous page)
merger. Plaintiffs also asserted claims against Anschutz for aiding and abetting. Plaintiffs drew the court's attention to the fact that three of Rio Grande's directors were also directors of a company in which Anschutz was the principal stockholder. See *Rio Grande*, 519 A.2d at 122. Despite the directors' relationship with Anschutz, the court ruled that plaintiff had failed to plead adequately that Anschutz “knowingly participated” in the alleged disclosure violations. See *id.* at 131; *Cf. Northgate*, 240 B.R. at 359-60 (under Minnesota law, the mere fact that a corporation and one of its suppliers shared officers and directors could not establish that the supplier knowingly participated in breaches of fiduciary duty committed by the corporation's officers and directors).

¹⁹ This defect applies with respect to Mr. Shapero, and even more so to Mr. Hawk, an alleged “Special Limited Partner.”

CONCLUSION

For all of the foregoing reasons, Crosspoint respectfully requests that this Court enter an order dismissing the claims against Crosspoint.

Respectfully submitted,

Dated: October 8, 2004

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CERTIFICATE OF SERVICE


I, Danielle Gibbs, hereby certify that copies of the Opening Brief in Support of Defendant Crosspoint Venture Partners, L.P.'s Motion to Dismiss Amended Derivative and Class Action Complaint, were caused to be served on October 8, 2004, upon the following counsel of record in the manner indicated:

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