IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

In re NINE SYSTEMS CORPORATION SHAREHOLDERS LITIGATION	)))	Consolidated C.A. No. 3940-VCN

PUBLIC VERSION OF
DEFENDANTS' OPENING PRETRIAL BRIEF

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PRELIMINARY STATEMENT

The claims to be tried in these consolidated actions were brought by certain former common shareholders of Streaming Media Company ("SMC") against certain former directors and stockholders of SMC and affiliated persons and entities (i) challenging as unfairly dilutive a recapitalization transaction unanimously approved by SMC's board of directors (the "Board") in January 2002 to finance two acquisitions (the "Recapitalization"); (ii) for inadequate disclosure in connection with the Recapitalization; and (iii) in the case of one plaintiff, for fraudulent inducement. The Court has issued opinions addressing three motions to dismiss, a motion for class certification, and a motion for summary judgment in connection with these claims.[1] Accordingly, some familiarity with the facts and contentions is assumed.

After spending years and substantial money defending Plaintiffs' allegations, Defendants are eager for their day in court to present *evidence*—not allegations liberally construed under favorable pleading standards, not inferences drawn against movants, and not creative theories, but actual sworn witness testimony and contemporaneous documents—of the facts surrounding the Recapitalization more than 11 years ago. When the contemporaneous records are examined, the credibility of the witnesses assessed, and the testimony of the unbiased witnesses credited, the evidence will show the following.

At the time of the Recapitalization, SMC was in financial extremis. It had never generated revenues necessary to sustain its operations, let alone make a profit. Its original management team and their successors had failed in their efforts to operate the business on a

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[1] *Dubroff v. Wren Holdings, LLC*, 2009 WL 1478697 (Del. Ch. May 22, 2009) ("*Dubroff I*"); *Dubroff v. Wren Holdings, LLC*, 2010 WL 3294219 (Del. Ch. Aug. 20, 2010) ("*Dubroff II*"); *Dubroff v. Wren Holdings, LLC*, 2011 WL 5137175 (Del. Ch. Oct. 28, 2011) ("*Dubroff III*"); *In re Nine Sys. Corp. S'holders Litig.*, 2013 WL 771897 (Del. Ch. Feb. 28, 2013) ("*Summary Judgment Op*."); *In re Nine Sys. Corp. S'holders Litig.*, 2013 WL 4013306 (Del. Ch. July 31, 2013) ("*Nine Sys. II*"). Capitalized terms not defined herein have the meanings given to them in the *Summary Judgment Op.* and *Nine Systems II*.

standalone basis. In just the six months prior to the Recapitalization, SMC had burned through almost $5 million of capital with no results. Having exhausted all of its investors' equity and failed to raise new capital, SMC's then-CEO proposed a new path to save a company at death's door—a roll-up strategy of acquisitions financed by existing stakeholders. Two of SMC's four principal shareholder groups, Wren and Javva, agreed to fund the new strategy. The other two, Catalyst and Lipper, did not.

In exchange for providing $3.3 million of new capital to fund the acquisitions, and after prolonged deliberations culminating in unanimous approval by the entire Board, Wren and Javva received Series B-1 preferred stock (the "Preferred B-1") amounting to roughly half of SMC's overall equity. Wren and Javva, along with Catalyst and certain Lipper investors, also agreed to convert the SMC secured debt they held into Series A preferred stock (the "Preferred A") amounting to roughly 20% of SMC's overall equity.

After continued financial struggles, then modest improvement, then stability, over four years post-Recapitalization, SMC was sold to Akamai Technologies, Inc. ("Akamai") in a stock-for-stock merger (the "Akamai Merger") that provided a substantial return for *all* investors.

In this opening pre-trial brief, we do not attempt to rebut each of the ever-shifting theories, or to attack each of the strained legal arguments, of which Plaintiffs must persuade the Court to prevail on their claims. We will demonstrate in our responsive brief that neither the evidence nor the law supports Plaintiffs' theories of the case. Here, after presenting what the evidence will show, we primarily focus on the relatively small handful of uncontestable facts and fundamental failures of proof that mandate judgment in favor of *all* Defendants on *all* claims.

First, Wren, Javva, and Catalyst were independent actors unbound by any agreement or legally significant bond. That fact will defeat all of Plaintiffs' claims (other than their disclosure claims and Thomas Murphy's fraud claims). Because all of Plaintiffs' claims (with those two exceptions) are derivative in nature, Plaintiffs must prove, under *Gentile* and its progeny, that Wren, Javva, and Catalyst—three minority shareholders that were virtual strangers to each other and which entered into no agreement amongst themselves—comprised a "control group," one of the most difficult elements of Delaware law to prove. They do not (and cannot) come close.

Second, the Recapitalization was entirely fair. Uncontroverted witness testimony, contemporaneous documents, and unrebutted expert opinion will show that, immediately prior to the Recapitalization, SMC's common stock had no value. Worthless stock cannot be unfairly diluted or expropriated, and, therefore, the Recapitalization, which left Plaintiffs with no less than they had before the transaction, was entirely fair. Beyond that, the Recapitalization was the result of a fair process and attributed more value to the common stock than it was worth. As the Recapitalization was procedurally and substantively fair, judgment on *all* of Plaintiffs' claims (except Thomas Murphy's fraud claims) must be entered for Defendants. Plaintiffs can sustain no claim arising from a transaction, or the disclosure of a transaction, that was entirely fair.

Finally, judgment should be entered against Thomas Murphy on his claims relating to his sale of shares to SMC in 2006 (the "Murphy Stock Sale"). The credible evidence will show that Murphy—a sophisticated, experienced businessman—was not misled in connection with that sale. Furthermore, he agreed in writing that he did not rely upon any of the extra-contractual matters about which he now complains, and he waited too long to bring his claims. For these reasons alone, Plaintiffs cannot prevail on *any* of their claims.

THE EXPECTED TRIAL RECORD

I. THE PARTIES

A. The Class Action Plaintiffs

Sheldon Dubroff and Mervyn Klein brought a putative class action complaint on behalf of a subset of former SMC stockholders in August 2008. After all but their disclosure claims were dismissed in 2009, their subsequent application for class certification was denied in 2010.

B. The Fuchs Plaintiffs

After the Court denied class certification, 43 new plaintiffs filed suit in November 2010 alleging claims substantially similar to those raised in the putative class action. Each of these Plaintiffs was an employee or client of Lipper & Company ("Lipper,") or an acquaintance of Lipper partner, Abraham Biderman. These plaintiffs are collectively referred to as "Lipper" throughout the record. Biderman was the Lipper-designated SMC director from 2001 until the Akamai Merger. JX0117; JX0127. His credibility and bias will be key issues at trial. Despite voting in favor of the Recapitalization and facilitating its consummation, Biderman has not been sued.[2] To the contrary, he is aligned with the Fuchs Plaintiffs, verifying both their pleadings—claiming now that the Recapitalization that he negotiated and voted for was unfair—and, like many of the non-party witnesses relied on by Plaintiffs, "retaining" (at no expense) Plaintiffs' counsel as his own. JX0628 (Biderman) at 12, 15; JX0634 (Biderman) at 272-74.

There are three subsets of Fuchs Plaintiffs. The "SMIG Plaintiffs" purchased membership interests in Streaming Media Investment Group, LLC ("SMIG"), which Lipper formed to purchase SMC shares. Biderman was co-Manager of SMIG and was designated as its

[2] Biderman's approval of the Recapitalization undermines his credibility for at least one of two reasons: either (i) he approved the Recapitalization and assisted with its implementation believing it was unfair at the time, in which case he was complicit in Defendants' alleged misconduct and is now seeking to evade liability; or (ii) he voted for the Recapitalization and implemented it believing that its terms were fair, in which case he is now revising history to assist his former clients and acquaintances. The fact that Plaintiffs, rather than suing him, embrace Biderman shows the latter is the case. But in either case, Biderman's self-serving testimony should not be credited. *See Sutherland v. Sutherland*, 2013 WL 2362263, at *9 (Del. Ch. May 30, 2013) (considering the plaintiffs' decision not to sue a director involved in the challenged decisions as relevant to context); *Gearreald v. Just Care, Inc.*, 2012 WL 1569818, at *14 (Del. Ch. Apr. 30, 2012) (describing two directors' "approving [a] merger and later dissenting from it" as "duplicity" and "troubling").

sole liaison to SMC.[3] The "Preferred A Plaintiffs," who owned only Secured Notes during the Recapitalization, have had their claims dismissed.[4] The remaining four Fuchs Plaintiffs[5] each invested directly in SMC in 2000.

C. The Kim Plaintiffs

The Kim Plaintiffs, despite being on inquiry notice of their claims by late November 25, 2006,[6] did not file their complaint until October 2012. The complaint was amended in December 2012, and largely tracks that of the Fuchs Plaintiffs.[7] Rick Murphy was SMC's first CEO. Thomas Murphy is Rick Murphy's father, and SMC's first financial backer. Rounseville "Skip" Schaum was a founding SMC director and its original CFO. Schaum invested in SMC through Newport Capital Partners, Inc. ("Newport"), which he wholly owns. The Murphys, Schaum, and Newport are collectively referred to as the "Founding Stockholders." The Founding Stockholders (the only remaining Kim Plaintiffs) and the Fuchs Plaintiffs are collectively referred to as "Plaintiffs." The Founding Stockholders and the Kim Plaintiffs form an unusual alliance; prior to authorizing the Fuchs Plaintiffs' counsel to file suit for them,[8]

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[3] JX0628 (Biderman) at 36-37, 195:3-13, 199:11-16; *see also* JX0039 at PLT000360-61; JX0038. The SMIG Plaintiffs are J. Paul Amaden, James P. Amaden, David Horowitz, Howard Horowitz, Steven Horowitz, Carrie Keating, John Keating, Gregory Loprete, Michael Loprete, Caroline Reckler, Gillian Reckler, Jon Reckler, Stephanie Reckler, Shlomo Schon, Edward Strafaci, Linda Strafaci, Joanne Visovsky, and Michael Visovsky. Dubroff, like the SMIG Plaintiffs, was initially a SMIG member, not an SMC stockholder.

[4] *Summary Judgment Op.* at **7-8. The Preferred A Plaintiffs are Susan Abikhzer, Cindy Hassan, Herbert Rausman, Rivkah Rausman, Trust FBO Chaim Abikhzer, Trust FBO Naftali Abikhzer, Nathan Hassan (UGMA acct), Rachel Hassan (UGMA acct), Trust FBO Barry Rausman, Trust FBO Moishe Abikhzer, Trust FBO Jacob Rausman, Emil & Joan Rausman Irrev. Trust, Barry Wien, and Eddy Hsu.

[5] The Greenberg Family Fund d/b/a ASR Ventures LLC ("Greenberg"), Morris Fuchs, Bernard Fuchs, and The Golden Family Fund, LLC ("Golden").

[6] *Nine Sys. II*, 2013 WL 4013306, at *4, *7.

[7] Two of the Kim Plaintiffs, Peter Mountanos and Jenny Kim, had their claims dismissed in their entirety on the grounds of laches. *Id.* at **10-12.

[8] In addition to representing this disparate collection of Plaintiffs, Plaintiffs' counsel also purports to represent several *non-party* witnesses on whom Plaintiffs rely.

certain Founding Stockholders had been critical of the Fuchs Plaintiffs' claims.

D. The Defendants

The Defendants are: (i) Howard Katz, Christopher Shipman, and Dort A. Cameron III (collectively, the "Director Defendants"), three of SMC's five directors when the Recapitalization was approved and whom Plaintiffs allege breached their fiduciary duties; (ii) Troy Snyder, who became an SMC director and its CEO in May 2002, following SMC's acquisition of NaviSite Streaming Media Group ("NaviSite SMG"), and whom Plaintiffs also allege breached fiduciary duties; (iii) Wren Holdings, LLC ("Wren"), Javva Partners, LLC ("Javva"), and Catalyst Investors, L.P. ("Catalyst"), each of which was a minority stockholder of SMC at the time of the Recapitalization and each of which is alleged to have joined together to form the "control group" at the core of Plaintiffs' claims; (iv) Andrew T. Dwyer, a business partner of Cameron's who assisted in the management of SMC, and who indirectly beneficially owns just under half of Wren; and (iv) Cameron Family Partnership ("CFP"), which indirectly beneficially owns the majority of Wren. Wren, Javva, and Catalyst, and their respective principals, are virtual strangers to each other. Their sole meaningful connection to each other is that they each independently determined to invest in SMC and have been involuntarily joined as co-Defendants. They have never otherwise invested or done business with each other.[9] Wren and Javva (whose principals did not know of each other prior to their respective investments in SMC) were personal investment vehicles. But Catalyst was, and remains, an investment manager that would abdicate responsibilities to its investors were it to have done the bidding of Wren and/or Javva.

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[9] In fact, other than one coincidental social connection, Wren, Catalyst, and Javva were completely unknown to each other. The *sole* connection between any of Wren, Javva, or Catalyst prior to their investment is that a Catalyst associate, Tyler Newton, was the college classmate and friend of Dort Cameron's son, Seth. JX0064.

II. THE EVENTS IN QUESTION

The facts to be established at trial concern events that occurred over 11 years ago. Faded memories and witness bias, therefore, render contemporaneous records of undisputed authenticity the most reliable evidence. Witness testimony, of course, should not be disregarded, but we respectfully submit that, given that faulty memories and witness biases tend to increase the likelihood of revisionist history over time, witness credibility should be carefully assessed and testimony scrutinized, with the testimony of truly unbiased witnesses particularly credited. On this basis, the weight of the credible evidence will show the following.

A. SMC's Beginnings

SMC was founded to provide high-speed broadband streaming media services to websites that lacked the capability to stream video. JX0011 at DEFS011386. Such services required the installation and maintenance of facilities with large satellite farms, resulting in high operating expenses. *Id.* at DEFS011389, DEFS011392. In attempting to project these expenses against future revenues, Murphy and Schaum "consistently overpromised [and] underdelivered."[10]

After founding SMC in August 1999, Rick Murphy and Schaum (neither of whom invested any of their own money in SMC) set about raising capital.[11] On April 6, 2000, Klein invested $50,000. JX0578 (Klein) at 6-7; JX0051. Javva was also an early investor. *See* JX0010 at DEFS011421-34. Rick Murphy and Schaum, to whom he was introduced by his son, brought Katz into the investment. Katz joined the Board on November 1, 1999, and by March

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[10] *Compare* JX0072 at CI07531 (projecting November 2000 revenues to be $400,000; December 2000 revenues to be $500,000); JX0073 at CI009581 (projecting January 2001 revenues to be $600,000; February 2001 revenues to be $700,000; and March 2001 revenues to be $800,000) *with* JX0094 at PLT001687 (totaling July-November 2000 revenues as $70,534); JX0114 at CI021133 (noting December 2000 revenues as $47,540; January 2001 revenues as $42,797; February 2001 revenues as $66,534; and March 2001 revenues as $68,079).

[11] JX0601 (R. Murphy) at 16:6-8; JX0610 (Schaum) at 25:23-26:5; *see also* JX0022 at DEFS024159 (resolving to raise $2.4 million in new capital through equity sales).

2000, Javva had invested $550,000 in SMC.[12]

Wren and Lipper invested the following year. Wren purchased 250,000 SMC shares at $4 per share in March 2000, and 93,750 shares for $375,000 in June 2000. JX0769 at DEFS051357. Cameron became a director on August 17, 2000. JX0065. At or about the same time, Lipper was trying to raise equity for SMC. JX0628 (Biderman) at 27-33, 36-42; JX0634 (Biderman) at 306-07. Biderman was introduced to SMC by a neighbor, Morris Friedman, who was an SMC investor. JX0628 (Biderman) at 24-26. Lipper organized SMIG as an investment vehicle to hold SMC shares, and eventually sold membership interests to the SMIG Plaintiffs. *Id.* at 195; *see also* JX0048. In all, SMIG purchased 125,000 common shares at $4 per share in April 2000 pursuant to a Stock Purchase Agreement (the "SMIG SPA"). JX0045. Biderman, SMIG's co-manager, was designated to receive notice on its behalf, and acted for it and its members.[13] The SMIG SPA included a most favored nation ("MFN") clause that gave SMIG certain re-pricing rights for 18 months. *Id.* at DEFS034585-86. Lipper and Biderman also approached Greenberg, Golden, and the Fuchs brothers, each of whom chose to buy SMC common shares directly. Greenberg and Golden signed stock purchase agreements that included the same 18 month MFN clause; the Fuchs brothers did not. JX0050; JX0057; JX0641 (Golden) at 53:21-54:10.

SMC completed its $4 stock offering by the end of June 2000, and in August 2000, attempted to solicit investors for a $5 per share stock offering. JX0067; JX0070; JX0078. Given SMC's limited resources, the offering price was determined without an outside valuation or

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[12] JX0016 at DEFS022277; JX0020 at DEFS022290; JX0010 at DEFS011434; JX0769 at DEFS051349, 051353; JX0601 (R. Murphy) at 142-43.

[13] *See* JX0047 ¶ 1; JX0632 (Grad) at 133:7-134:7, 155-56; JX0045 at DEFS034589; JX0208; JX0119 at DEFS051189 (noting that all board members needed to sign on behalf of their companies to elect Biderman to the board, and stating that "Lipper . . . can sign for their investors").

fairness opinion. The higher offering price notwithstanding, SMC continued to struggle due to high monthly operating expenses and meager revenues. JX0072 at CI007531-32. Wren and Javva each independently purchased 200,000 and 100,000 shares (respectively) in the August 2000 offering. JX0081.

In connection with that same offering, SMC also approached Catalyst, which learned of SMC from Friedman (who was acquainted with Catalyst's managing partner) and Newton.[14] Catalyst agreed in October 2000 to invest $1,500,000 for 300,000 shares on the condition that it receive a seat on SMC's Board and certain price-adjustment protection. JX0078. Shipman joined the Board on October 23, 2000. JX0084.

B. SMC's Financial Struggles

Despite raising over $6.6 million through 2000 from parties to these actions alone,[15] SMC struggled financially and required more capital to sustain itself—a pattern that persisted beyond the Recapitalization. For example, for FY 2001, which ended June 30, 2002, SMC reported a net operating loss of almost $5.8 million and accumulated retained earnings since inception in excess of *negative* $13.1 million. JX0100 at DEFS040218-20. SMC's financial condition was such that it never purchased D&O insurance or compensated its directors for their service (other than a small share grant to Katz in 2000).

In December 2000, SMC sought additional funds through a $1.5 million note offering. JX0094. The "Subordinated Notes" were convertible into SMC common stock at $10 per share, which price could adjust down to no less than half. *Id.* Because of SMC's financial condition, no outside valuation or fairness opinion was obtained. Instead, SMC reached out to its

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[14] JX0064. Newton learned of SMC at a party, when Dort Cameron mentioned some recent internet investments he had made, including SMC.

[15] SMC also raised millions of dollars from other (non-party) sources, such as Friedman and his group. *See* JX0725; JX0148 at AB000341.

constituents via their representatives. Biderman prevailed upon Greenberg to subscribe to $150,000 of the Subordinated Notes. JX0634 (Biderman) at 368-69. He also convinced certain Rausman plaintiffs (whom Biderman had been advising) to purchase a total of $275,000 of Subordinated Notes. *Id.* at 368. Between Greenberg and the Rausmans, Lipper placed $425,000 of Subordinated Notes in December 2000,[16] for which Lipper received $46,250 in kind as a fee. JX0223 at DEFS051318. Javva also purchased $500,000 of the Subordinated Notes. JX0721.

C. SMC's Struggles Continue, And Necessitate Still More Debt

The Subordinated Notes offering did not improve SMC's fortunes. Even before the offering, SMC, in November 2000, retained Daniels & Co. ("Daniels"), an investment bank active in the tech sector, to raise outside capital and identify strategic partners. JX0085 at CI009571. Daniels' efforts, which continued through late 2001, were wholly unsuccessful. JX0625 (Markham) at 33; JX0615 (Granberg) at 59; JX0232 at PLT002003.

In FY 2000, SMC incurred a net loss of $5,657,982. JX0321 at CA008822. Its monthly revenues sank in the latter half of 2001, from a high in May of $95,867 to $71,673 in December.[17] By March 2001, as SMC could not even make payroll (JX0111 at CI008317), Schaum implored Rick Murphy to "talk Catalyst, Javva and [Wren] into" making additional investments. JX0106 at PLT012282. By April 2001, Rick Murphy had convinced Catalyst to make an emergency $217,391.31 loan. JX0109 at DEFS021529-33; JX0111 at CI008316-17. Javva and Wren each also independently funded payroll through small emergency loans of $5,434 and $27,173, respectively. JX0109 at DEFS010130-32, DEFS010148-50.

[16] JX0634 (Biderman) at 368-369; JX0223 at DEFS051311-18. Biderman also obtained a commitment for the Subordinated Notes from another Lipper client, non-party Ace Foundation ("Ace"), which purchased $500,000 of the notes. *See* JX0645 (Biderman) at 687-89, 722.

[17] JX0668 at Ex. 5; JX0615 (Granberg) at 60 (noting that SMC's financial difficulties had created "panic" by the summer of 2001); JX0232 at PLT002002-03.

Rick Murphy also asked Catalyst to lead a $4.6 million equity round. JX0111 at CI008316-17. Again, given its limited resources, SMC did not obtain an outside valuation or a fairness opinion in connection with the raise. To invest further equity, however, Catalyst wanted the Subordinated Notes converted into stock. Biderman insisted that the Subordinated Notes' conversion rights be re-priced so that holders would receive ten times the maximum number of converted shares for which they previously had bargained; he also insisted that he be granted a Board seat as Lipper's representative. JX0111; JX0634 (Biderman) at 435-38.

Catalyst opposed Biderman's demands because Lipper was unwilling to contribute any more equity even under the conditions demanded by Biderman. Shipman (writing for Catalyst) reminded Biderman that SMC was "literally out of money," and but for the emergency funding it and others had provided in April, SMC would not have met its payroll. JX0111 at CI008317. Shipman also noted that "[w]ithout an immediate resolution of this issue [an infusion of cash] [SMC] will be essentially insolvent," and assured Biderman that those investors that had just provided rescue financing "would absolutely welcome new funds from Lipper and its affiliates on the same terms and conditions [at] which we are buying in." *Id.* Lipper would not agree, and (indicative of Biderman's clout) SMC abandoned its efforts to raise equity.

Instead, SMC proposed—once again without an outside valuation or fairness opinion—that Catalyst agent a secured debt offering, with the noteholders receiving a first priority, all-asset lien (the "Secured Notes"). JX0148; JX0098 § 1; JX0118. SMC sold approximately $4,750,000 of the Secured Notes, with Wren purchasing $2,119,374, Javva purchasing $539,202, Catalyst purchasing $1,691,527, and Lipper (specifically, the Preferred A Plaintiffs and two other (non-party) investors) purchasing a total of $400,000. JX0718.[18] In return for Lipper placing Secured Notes with its investors, on June 21, 2001, Biderman was granted a Board seat as Lipper's representative. JX0127 at CI002133; *see* JX0119 at DEFS51191. The Secured Note purchasers each received a Secured Note and a one-cent warrant convertible into two shares of common stock for every dollar of debt (implying a 50 cent per-share valuation of the common). JX0148 at AB000215.[19] Under the Secured Notes, if any "Equity Liquidity Event" (including a change of control or the liquidation or dissolution of SMC) occurred, "an amount equal to four times the aggregate amount of all Advances" would be due immediately. JX0131 at CI010926, CI010934-35; JX0148 at AB000209, AB000217. Accordingly, SMC would owe the holders about $19 million if there were a liquidity event.

Replacing Schaum and Murphy with more experienced executives was a condition to the funding of the Secured Notes.[20] In or around June 2001, Schaum, who had proved ineffective at raising capital and preparing forecasts, was replaced as CFO by Lorain Granberg.[21] Shortly thereafter, Art Williams was chosen to replace Murphy as CEO and a director. JX0232 at PLT002003.[22] The Board was displeased with Murphy's performance and had concerns about

[18] The amounts purchased by Wren, Javva, and Catalyst reflected a rollover of the emergency loans they had each, separately, made to keep SMC operating in May 2001.

[19] Thus, Wren, Javva, Catalyst, and the Lipper investors received warrants to purchase, respectively, 4,238,748, 1,078,405, 3,383,054, and 800,000 additional shares of SMC common stock.

[20] JX0131 § 3.1(d) ("The Borrower shall have replaced its chairman of the board of directors with a new chairman acceptable to its [Board], the Collateral Agent and the Required Lenders."); *accord* JX0148 § 3.1(d); JX0118 at DEFS051186.

[21] *E.g.*, JX0152 at AB000706; JX0615 (Granberg) at 24 (noting that Schaum had been removed because, due to his background and education, he "was not the guy to actually take [SMC] forward").

[22] Upon being hired, Williams committed to purchase $200,000 of the Secured Notes. JX0136. There is no record of him funding any more than $50,000, and, although the April 12, 2002 Board minutes indicate that he funded $50,000 (JX0206 at DEFS047220), Williams has no recollection of putting up any money. JX0618 (Williams) at 43-44, 49.

financial irregularities promptly discovered by Granberg after joining SMC.[23] With excess broadband capacity depressing prices, SMC hired Williams (who had no technical background) to develop higher margin services to be offered with capacity. *See* JX0152 at AB000706. At his first Board meeting on September 26, 2001, Williams raised the possibility of a merger with e-Media Corp. ("e-Media"), a competitor that had more customers and substantially greater revenues. JX0601 (R. Murphy) at 312:10-11; JX0722 at CI002742-43.

D. The Board Approves the Recapitalization

1. SMC's Lack of Equity as of January 2002

Despite the change in executives and infusion of another $4.75 million in 2001, SMC continued to struggle to hit sales and revenue targets, and spent far more than it generated. SMC was losing $300,000 a month, and it had become "obvious that SMC was not booking sales fast enough to avoid running out of money in early 2002." JX0232 at PLT002003. Williams warned the Board that SMC could not continue to operate "unless a new strategy could be executed quickly."[24] Of particular concern was the fact that SMC had already blown through all $9 million of equity raised by the end of 2000, as well as the $1.425 million raised in the Subordinated Notes offering. Now with the $4.75 million proceeds of the Secured Note offering also burned in just a matter of months, not only was all of its equity capital gone, but SMC faced having to pay over $19 million (on account of the four-times preference) to the Secured Note holders if liquidation could not be avoided. JX0100 at DEFS040220; JX0668 ¶ 31.

Between its enormous losses and substantial debt, by January 2002, SMC's common

[23] *E.g.*, JX0615 (Granberg) at 74:18-75:19 (describing an audit that discovered Murphy's use of SMC's cash for "personal reasons"); JX0697 (R. Murphy) at 481-85 (admitting to making personal purchases on SMC's debit card); JX0788.

[24] JX0615 (Granberg) at 125-26; *see also* JX0232 at PLT002004 ("SMC would have to liquidate with a total loss to all investors unless another strategy could be quickly executed.").

stock was worthless. Even Catalyst, which had a financial disincentive as a fund manager to write down the value of its assets, wrote down its SMC common stock to zero. Catalyst's assessment matched that of SMC's management, which estimated SMC's total enterprise value at only $4 million—far less than its debt. JX0770 at DEFS051431; JX0185 at DEFS042952.

The contemporaneous valuations of SMC's management and sole institutional investor are confirmed by Defendants' valuation expert, Professor Jerry Hausman. JX0668 ¶¶ 1, 6. Hausman is the MacDonald Professor of Economics at MIT, where he has taught for over 40 years. Among numerous other credentials, Hausman has routinely advised companies in the telecommunications and Internet sectors (including Akamai), taught a course on the economics of the Internet, and has been qualified as an expert witness in numerous proceedings, including a recent matter in which Chancellor Chandler found his views credible.[25] He will offer his opinion at trial that, as of January 2002, SMC's obligations exceeded its enterprise value (even without considering the Secured Debt preference) by, at least, $4 to $5.3 million and, thus, SMC had no equity value in January 2002. *Id.* ¶¶ 8, 32-33. Notably, his testimony on this point will not be rebutted by any contrary opinion from Plaintiffs' expert.

2. The Board Approves Acquiring e-Media and NaviSite SMG

In this context, on December 20, 2001, Williams called an emergency telephonic meeting of the Board (then comprised of himself, Cameron, Katz, Shipman, and Biderman) for 2:00 p.m. the following day to discuss SMC's cash needs and his rescue plan. With SMC having been unable to raise outside money or generate any significant new business, Williams proposed that SMC pursue possible acquisitions, including of e-Media and NaviSite SMG, as a means to acquire new customers and increase its revenues. JX0770 at DEFS051430. e-Media was a

[25] JX0668 ¶¶ 2-4, Ex. 2; *S. Muoio & Co. LLC v. Hallmark Entm't Invs. Co.*, 2011 WL 863007, at *2, *21 (Del. Ch. Mar. 9, 2011), *aff'd*, 35 A.3d 416 (Del. 2011).

direct competitor. NaviSite SMG also was in the same space, principally as a software platform provider for managing streamed content.

The meeting's timing was driven by the urgency of a potential acquisition of e-Media, which was about to file bankruptcy.[26] The attendees discussed SMC's immediate funding needs and the possibility of growing revenues by acquiring e-Media and NaviSite SMG.[27] Biderman, unavailable for the meeting, did not ask any of his Lipper colleagues to attend on his behalf. JX0645 (Biderman) at 716:19-718:4. The following business day, however, Dwyer called Biderman and briefed him about the call. *Id.* at 718-19, 731-32. After being briefed, Biderman sent the Board a letter dated December 28, 2001 in which he expressed concern over the possible dilution to existing stockholders that could result from Williams's plan. JX0159.

The Board next convened telephonically on January 7, 2002. Biderman and two other Lipper representatives, Emily Christenfeld Grad and Patti Koo, participated.[28] As Granberg explained: "[SMC was] running out of money and something ha[d] to be done." JX0615 (Granberg) at 123. Williams told the directors that SMC would require $2 million in funding to continue operating on a standalone basis, and that its prospect for raising new money based on internal sales growth was not realistic. JX0770 at DEFS051430. Indeed, SMC would be unable

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[26] JX0645 (Biderman) at 728-29, 792:4-15 (noting that the meeting was called to discuss the acquisition of NaviSite SMG); JX0185 at DEFS042951 ("If SMC doesn't close [on e-Media] by 1/10/02 – bankruptcy"); JX0632 (Grad) at 237-38.

[27] JX0185 at DEFS042951 (regarding the e-Media purchase, "It's really revenue we're buying."); JX0615 (Granberg) at 94 (describing the e-Media transaction as basically a purchase of "revenue contracts"); JX0770 at DEFS051429-33; JX0170 at DEFS047198; JX0160 at PLT004704 (regarding the NaviSite SMG purchase, "we are all betting on the revenue growth anyway"); JX0232 at PLT002004.

[28] Grad and Koo both worked with Biderman at Lipper and often attended Board meetings at his request, including those he could not attend. JX0645 (Biderman) at 907, 921-22, 927; JX0632 (Grad) at 46:10-21; JX0615 (Granberg) at 98-99 (not recalling any Board meeting at which neither Biderman nor Grad were present before Lipper imploded). If they attended a meeting without Biderman, they provided him with a full report on what transpired. JX0628 (Biderman) at 55-56, 146. Grad's and Koo's participation in Board meetings was not unusual. While each stockholder constituency had the right to designate a Board member, they also routinely were represented at Board meetings by non-member representatives, such as Newton (Catalyst), Brandfon (Javva), Dwyer (Wren), Grad (Lipper), and Koo (Lipper).

to make its January 15 payroll, pay leases or critical vendors without an *immediate* cash infusion.[29] Absent some other strategy, SMC would have to liquidate with a total loss to all equity investors. JX0166 at CI000191; *see also* JX0232 at PLT002004; JX0615 (Granberg) at 125. Against this backdrop, Williams again proposed the acquisitions of e-Media and NaviSite SMG as an alternative to funding a standalone SMC.[30] The acquisitions were intended to generate significant value for *all* stockholders, who would lose everything if SMC were forced to liquidate. *See, e.g.*, JX0232 at PLT002004.

Management estimated that SMC had an enterprise value of $4 million (which was far less than its debt) and would contribute 30-40% of the total revenues of the combined entity.[31] After discussion, the Board voted 4-0-1 in favor of pursuing the acquisitions, with Biderman abstaining (without offering an alternative for SMC's funding crisis). JX0170 at CI012971; JX0770 at DEFS051432; JX0632 (Grad) at 209-11.

At a January 10, 2002 telephonic meeting, the entire Board discussed "how to reconfigure and clean up SMC's capital structure to: raise new money or notes for the acquisitions . . . and exchange the existing senior debt . . . for some form of equity." JX0170 at DEFS047198; *see* JX0185 at DEFS042951. Williams estimated that SMC needed to raise $2.5 million to carry out the previously-approved acquisition strategy: (i) $1 million in cash for the e-Media purchase; (ii) $1.3 million to purchase NaviSite SMG; and (iii) $200,000 for immediate

[29] JX0770 at DEFS051430; *see also* JX0615 (Granberg) at 137 (stating that SMC did not have any money to pay expenses); JX0632 (Grad) at 197:13-18 (noting the "time urgencies" to resolve the cash shortfall).

[30] JX0166 at DEFS051430-31; JX0185 at DEFS042951; JX0632 (Grad) at 196:23-197:6 (recalling no other solution for solving SMC's cash crisis other than going forward with the acquisitions of e-Media and NaviSite SMG).

[31] JX0770 at DEFS051431; JX0185 at DEFS042952; JX0232 at PLT002004. Dwyer agreed that SMC had an enterprise value of only $4 million. Catalyst believed SMC's value was even less. It was Williams who first suggested a plan to have the new money obtain 50% of SMC's equity in an email he sent on December 28, 2001 to two brokers assisting NaviSite SMG. *See* JX0160 at PLT004703.

needs. JX0170 at DEFS047198. Williams proposed that the new money receive Preferred B stock convertible to 38% of SMC's equity (consistent with a pre-money enterprise value of $4 million) based upon the anticipated relative revenue contributions to the proposed combined entity from SMC (the projections for which were revised down again) and the new acquisitions. *Id.*; JX0185 at DEFS042952; JX2000 at PLT004367.

Williams then "initiated a discussion of investor appetite to fund [the] proposed acquisitions." JX0170 at DEFS047199. The opportunity to provide the new money was offered to all constituencies represented on the call, including Lipper, which, as in the prior offerings, was afforded the opportunity, via Biderman, to participate. Both Catalyst and Lipper declined, citing the lack of diligence and time to consider the deal.[32] Wren agreed to contribute $2 million. *Id.* Javva separately agreed to contribute $500,000.

The Board then voted four-to-one in favor of the e-Media and NaviSite SMG acquisitions (together, the "2002 Acquisitions"), and to borrow a total of $2.5 million from Javva and Wren. *Id.* at DEFS047198-99; JX0185 at DEFS042952. Biderman cast the sole dissenting vote "because of the significant dilution to existing SMC security holders, which was previously assumed to be in the range of 60%-70%." JX0185 at DEFS042952. He again did so without offering any alternative for saving SMC.[33]

3. The Board Unanimously Approves the Recapitalization

At the Board's next telephonic meeting on January 17, 2002, Williams briefed the entire Board concerning changes to the NaviSite SMG transaction. JX0178 at DEFS031029. NaviSite

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[32] JX0170 at DEFS047199 ("Catalyst deferred, saying the deal makes sense, but the timing is a problem and they had not done due diligence. Lipper also deferred, for reasons similar to those of Catalyst."); *id.* at CI000194; JX0181 at CI013106-07, CI013109.

[33] JX0185 at DEFS042952; *see also* JX0170 at DEFS047199; JX0634 (Biderman) at 454:1-11; JX0645 (Biderman) at 844:8-21.

SMG was now being offered for a lump-sum cash price of $2.1 million. *Id.* SMC, however, had committed only $2.5 million cash for both acquisitions, of which $1.2 million was for e-Media and operating expenses,[34] leaving only $1.3 million to close the NaviSite SMG deal. *Id.* The Board discussed a proposal for funding the $800,000 difference. *Id.*[35]

The Board also discussed a revised capitalization plan to address Biderman's concern about potential dilution. *See id.* at DEFS031030. Williams (who conceived the original plan) and Dwyer suggested that two new series of preferred stock be created, with all of the existing Secured Notes being exchanged for Preferred A (representing 20% of SMC) and the new money receiving Preferred B (representing 38% of SMC). *Id.* at DEFS031030, DEFS047202; JX0188 at DEFS051452; JX0741 at CI005038-39. This would increase the existing common stockholders' share in the combined entity to 7% (from the 3% first proposed at the January 10 meeting). JX0178 at DEFS031030, DEFS047202.

Biderman at first continued to object, but then proposed two additional terms: (i) he maintain his Board seat through 2004 absent a change of control; and (ii) if any subsequent equity issuance (other than an IPO) lacked unanimous Board approval, then those stockholders whose Board designee dissented would be able to redeem their Preferred A for cash at 1.5 times its face amount. *Id.* at DEFS031030, DEFS047203; JX0185 at DEFS042953; JX0645 (Biderman) at 864-65. The Board agreed to Biderman's revisions and then voted *unanimously* to approve the Recapitalization. JX0178 at DEFS031030, DEFS047203. The Board voted for a

[34] The e-Media transaction had originally provided for a $1 million cash payment and a $3.6 million promissory note (the "e-Media Note") convertible into common stock, representing 25% ownership of SMC if the NaviSite SMG acquisition were consummated and 15.8% if not. JX0166 at CI000192; JX0176 at DEFS007204-40. The face amount of the note was later reduced to $600,000 because e-Media's receivables (and therefore the stock into which it was convertible) were far less than represented. *See* JX0729 at DEFS000461.

[35] Wren initially agreed to contribute $800,000 to fund the shortfall, although it did not ultimately do so since NaviSite SMG eventually agreed to a lower sale price. JX0185 at DEFS042953. None of Javva, Catalyst, or Lipper was willing to contribute.

second time, again *unanimously*, to proceed with the NaviSite SMG acquisition for $2.1 million. *Id.* at DEFS047203; JX0185 at DEFS042953. The e-Media purchase closed later that day. JX0185 at DEFS042951.

Contrary to Plaintiffs' contention that Wren, Javva, and Catalyst formed a uniform voting bloc, there is *no* evidence that their votes were anything but independently reached. There is no proof of any agreement among the three minority shareholders, or any competent and credible evidence of conspiratorial meetings, e-mails, or telephone calls, all of which are denied.[36]

Shipman voted for the Recapitalization because he believed it to be in SMC's best interest. On the basis of its own independent analysis, which diverged from that of Wren and Javva, Catalyst declined to provide new money, despite knowing that its common stock would be diluted by a factor of three. JX0181 at CI013106. As Catalyst explained in an internal memo, "SMC will run out of money at the end of January. We do not believe that in this market there is any value in SMC's assets or customer list in excess of [SMC's] liabilities, and that a total loss [of our equity investment] would be incurred." *Id.*; *see also* JX0171 at CI025556 (valuing existing SMC at $1.9 million). As an SMC director, Shipman concluded that the acquisition strategy was in SMC's best interests because it would keep the lights on (for the time being) and hopefully result in new assets and revenues. As an SMC stockholder, however, Catalyst did not feel that there had been sufficient diligence, or value to justify risking any more of its investors' money. JX0181 at CI013107.

On summary judgment, Plaintiffs contended that, and the Court found a triable issue of fact as to whether, Catalyst was given a 90-day "option" to put in new money on the same terms

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[36] *See, e.g.*, JX0618 (Williams) at 174:24-175:9 (stating that Wren, Catalyst, and Javva "made independent decisions for themselves" and did not act in "lock step"); JX0615 (Granberg) at 254:7-25 (stating that Catalyst, Wren, and Javva did not act with a "common mind," and that they had "disputes and different ways of doing things," including how to "keep[] the company alive and continuing").

as Wren and Javva. In fact, Catalyst was *not* given any option, and Plaintiffs will present no evidence as to the terms of—or even parties to—the supposed option. The Board did not, as would be required, approve (or even consider) the issuance of an option to Catalyst.[37] Indeed, in an enormous record, the *only* references to an "option" are in two internal Catalyst documents. JX0181 at CI013107; JX0161 at CI025336. Testimony will establish that those isolated references reflected Catalyst's recognition that it would have the continuing "option" to fund SMC's expenses, because neither Wren nor Javva wanted to bear that burden alone. That same "option" was afforded to Lipper.

4. SMC Repeatedly Needs More Capital after the 2002 Acquisitions

The next Board meeting to review the progress of the 2002 Acquisitions was scheduled for February 25, 2002. JX0188. Biderman, who now claims to have been preoccupied with an SEC investigation of Lipper,[38] was informed of the meeting but did not participate. *Id.*; JX0628 (Biderman) at 106:8-22. Grad and Koo participated in his place.[39] Lacking a quorum, the Board did not officially meet. Instead, representatives of Catalyst, Wren, Javva, and Lipper, plus Williams and Granberg, participated in an informational meeting. JX0188 at DEFS047205. Williams informed the participants that the integration of e-Media was taking longer than anticipated, that its revenues were weaker than expected and, that as a result, SMC needed more money. *Id.* The participants then discussed how to fund the $1.3 million shortfall. *Id.* Javva

[37] *See* 8 *Del. C.* § 157 (requiring board action to authorize an option to purchase shares).

[38] In January 2002, Lipper came under SEC investigation, which ultimately led to its demise. The Board did not learn of the investigation until it became public in late February 2002. JX0628 (Biderman) at 91:24-96:5. Biderman now asserts that dealing with the emergency at Lipper preoccupied his time and kept him from attending Board meetings. *Id.* at 105:16-106:7; JX0645 (Biderman) at 889:9-16. Nevertheless, Biderman did not resign from the Board, and continued as co-manager of SMIG. JX0628 (Biderman) at 95:25-96:5; JX0645 (Biderman) at 1090:6-9.

[39] JX0185 at DEFS042953-54; JX0188 at DEFS047205; *see also* JX0645 (Biderman) at 890:24-891:9 (testifying that if Grad or Koo participated in a meeting, then it was at his request).

determined to fund \$100,000. *Id.* at DEFS047206, DEFS051451. Dwyer independently committed Wren to fund \$800,000, but only if the remaining funds could be obtained from another source. *Id.* No one present was willing to fund the remaining \$500,000. *Id.* at DEFS051451; JX0185 at DEFS042954.

At the next telephonic Board meeting, on March 6, 2002, the Board continued to deliberate on how to close the \$1.3 million shortfall. JX0741 at DEFS023083. Once again, Biderman was given notice, failed to participate, and Grad and Koo participated instead. *Id.*; JX0185 at DEFS042954-55. SMC had been unable to raise additional money from outside sources, and Catalyst and Lipper were firm that they would not invest more.[40] Wren no longer insisted that someone else step up with the last \$500,000 and agreed to increase its contribution, but to fund no more than \$800,000 as equity. *See* JX0741 at DEFS023083; JX0185 at DEFS042954; *see also* JX0190 ("We [*i.e.*, Wren] do not want to put in the last \$500K and are only doing it for [SMC]'s benefit and want the money back asap"). Accordingly, the Board unanimously approved SMC borrowing \$500,000 from Wren in the form of an amortizing note plus a \$700,000 contribution as Preferred B-1. JX0741 at DEFS023083-84. The Board also approved a \$100,000 contribution from Javva as Preferred B-1. *Id.*; *see also* JX0223. The Board then discussed the need to obtain *all* Secured Note holders' consent to exchange their debt and warrants for the new Preferred A. JX0185 at DEFS042955. Catalyst and the Lipper Senior Note holders (*i.e.*, the Preferred A Plaintiffs), thus, effectively held veto power over the issuance of the Preferred stock. JX0645 (Biderman) at 925:14-926:5. During the meeting, Grad raised no objection to the funding plan. Nor did Biderman do so subsequently. The NaviSite SMG acquisition closed on March 25, 2002. JX0185 at DEFS042955.

[40] *See* JX0185 at DEFS042954; *see also* JX0632 (Grad) at 207:23-25 (stating that Lipper investors would have been allowed to invest more).

The next Board meeting was held on April 11, 2002. JX0206. Biderman again failed to participate, but Grad did. *Id.*; JX0185 at DEFS042955; JX0645 (Biderman) at 927. At the meeting, Dwyer reported that Williams had resigned (at Cameron's request) as an officer and director, and that current management would run SMC until a new CEO was appointed. JX0206 at DEFS047220; JX0232 at PLT002004. Williams' tenure, notwithstanding his idea for the 2002 Acquisitions, was marked by a continuing failure to grow revenues and generate accurate projections. Dwyer further reported that SMC was *already* facing yet another $1 million cash shortfall because: (i) the NaviSite SMG acquisition closed two months later than anticipated; (ii) Williams failed to fund his $200,000 Secured Note commitment; (iii) e-Media's revenues were significantly lower than expected; and (iv) SMC's own revenues were lower than anticipated. JX0206 at DEFS047220. The opportunity to make up the difference was offered to all present. *Id.* at DEFS047221. Wren agreed to loan SMC $400,000.[41] Javva, separately and independently, agreed to fund $400,000. *Id.* Catalyst and Lipper did not budge from their position of putting in no more money. *Id.* The Board decided to continue to seek outside investment to cover the remaining shortfall.[42]

5. SMC's Common Shares Remained Valueless after the Recapitalization

Immediately prior to the Recapitalization, SMC had zero equity. *See supra* Part D.1. In the Recapitalization, the value to common shareholders of the added assets from the 2002 Acquisitions was offset by the added preferred stock that would come ahead of the common equity. *See supra* Part D.2. Thus, immediately following the Recapitalization, SMC's common

[41] JX0206 at DEFS047221 (Wren and Javva "both committed to continuing to support the business and each agreed to fund approximately $400,000. All other attendees declined on behalf of their respective firms to participate.").

[42] *Id.* At various times after May 2002, Wren, Javva, Katz, and Dwyer (personally) made operating loans (with no equity component) to SMC aggregating in excess of $1.2 million. Plaintiffs have not challenged these loans.

shares were still worth zero.[43] As Hausman opines, whatever additional SMC enterprise value inured from the 2002 Acquisitions was essentially offset dollar for dollar by the obligations that SMC took on to fund the 2002 Acquisitions, resulting in no increase in the value of SMC's common stock. JX0668 ¶¶ 38-39.

6. Meanwhile, SMIG Dissolves

SMIG was cancelled on April 22, 2002. JX0208. Under SMIG's operating agreement, Biderman was required to distribute SMIG's assets (*i.e.*, SMC shares) to its members in kind or cash. JX0041 §§ 1.13, 8.2. He chose the former. Accordingly, SMIG sent letters to its members informing them that SMIG had been "terminated" and that they would be issued SMC shares. *See, e.g.*, JX0211; JX0212; JX0213. On May 30, 2002, SMC issued certificates to each of the SMIG Plaintiffs reflecting each member's *pro rata* portion of SMIG's SMC shares. *See* JX0223; JX0227. Previously, none of the SMIG Plaintiffs had owned SMC stock.[44]

Granberg and Grad also issued additional common shares to certain stockholders on account of the MFN re-pricing triggered by the conversion of Subordinated Notes at $0.50 per share. SMC issued the Fuchs brothers more shares even though they were *not* parties to any stock purchase agreement containing an MFN clause.[45] Compounding SMC's error, it appears that when reprinting the re-set shares, Granberg misread a line on SMC's stock issuance summary, and, instead of issuing him 175,000 common shares (thereby giving each brother 200,000 common shares for his $100,000 investment), gave him a total of 437,000 re-set shares. *See* JX0248; JX0227 at DEFS051362. The result is that he received 462,000 shares for his

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[43] *See* JX0668 ¶ 35 ("If anything, the total value of SMC decreased between January 2002 and August 2002."); JX0207 at DEFS51252 (estimating SMC enterprise value to be $1.5 million).

[44] *Summary Judgment Op.* at *3; *see also* JX0213 ("Each [SMIG member] will now be a direct shareholder in [SMC].").

[45] *See* JX0769 at DEFS051350 (SMC's stock issuance audit does not have an "X" under the "contract" column for the Fuchs brothers).

investment—an unearned increase in his equity of nearly *18.5 times*. JX0796.[46]

7. Snyder Is Elected CEO

At a May 22, 2002 meeting, the Board (with Biderman participating) unanimously voted to hire Snyder as CEO. JX0219; JX0232 at PLT002004. Snyder had run NaviSite SMG, and was asked to join SMC after the acquisition. He had no prior relationship with Wren, Javva, Catalyst, or Lipper. His task as CEO was to transform SMC from a distribution network into a provider of software for manipulating and managing digital video transmission. The Board also unanimously elected Snyder to assume the vacant Board seat formerly held by Williams. JX0219. Except for Board action taken in August 2002 to effectuate the prior approval of the Board, Snyder had no involvement in the Recapitalization.[47]

8. The Secured Note Holders Agree To Convert

As a condition to obtaining the new money from Wren and Javva, Biderman was required to give his assurance that the Lipper Secured Note holders would convert their debt into Preferred A. (As of July 31, 2002, the total amount of Secured Notes, including interest, to be exchanged for Preferred A was $5,330,095.) Notwithstanding Lipper's problems with the SEC, Biderman assumed sole responsibility for obtaining their consent (JX0645 (Biderman) at 925:14-926:5, 946:14-949:3; JX0185 at DEFS42955), and therefore, on June 18, 2002, Biderman sent Rausman a letter on SMC letterhead urging him to sign and return various consent forms for the

[46] Reflective of the fact that the Fuchs brothers received additional shares bearing no relationship to their actual investment, Morris Fuchs reported a gain of $38,296 to the IRS on his $100,000 investment in SMC, and Bernard Fuchs reported a gain of $219,464 on a similar $100,000 investment. JX0549 at PLT001859; JX0548 at PLT001857.

[47] Granberg resigned on or about the day the NaviSite SMG acquisition closed, mainly because she did not want to move to California where SMC's corporate headquarters would be relocated. JX0615 (Granberg) at 11:18-12:5. Granberg agreed, however, to stay on to assist during the transition, working part time mainly from home through September 2002. *Id.* at 10:21-11:5. At the May 22, 2002 meeting, the Board voted unanimously to replace her as CFO with Randy Levine, who had also joined SMC from NaviSite SMG. JX0219.

conversion of his family's Secured Notes and warrants into Preferred A. *See* JX0232.

Notably, in the letter, Biderman made the very same case for the Recapitalization that Plaintiffs, with his assistance, now attack as unfair. Among other things, Biderman described the Recapitalization as necessary "in order to avoid a liquidity crisis and loss of customer support." *Id.* at PLT002005. He gave an overview of the elements of the Recapitalization, and specifically disclosed that "SMC shareholders (who did not finance the acquisitions) will own over 30% of the new company" and that Rausman's Secured Notes would be converted into 1.22% of SMC's equity (although it was ultimately 1.33%). *Id.* at PLT002001, PLT002004.

All of the Secured Note holders subscribed to the Preferred A and executed agreements to surrender their Secured Notes and warrants.[48] Upon surrender, each of the Secured Note holders received their *pro rata* allocation of the Preferred A in direct proportion to the amount of debt and warrants they had owned.

9. SMC Issues Preferred A and B Stock and Reverse Splits Its Stock

Following the agreement by the Secured Note holders to exchange their debt, SMC consummated the previously approved Recapitalization by issuing the Preferred A (in exchange for the Secured Notes and warrants), Preferred B-1, and Preferred B-2. *See* JX0262; JX0294; JX0729. Preferred B-1 was issued to Wren and Javva in exchange for their respective contributions of the $3.3 million they funded for the 2002 Acquisitions. JX0729 at DEFS000460. The Preferred B-2 consisted of 6,000 shares that represented the non-cash consideration paid by SMC for e-Media (*i.e.*, the e-Media Note). *Id.* at DEFS000461; JX0703 at AKAMAI0413; *see also* JX0301.

On August 1, 2002, the directors (Katz, Shipman, Cameron, Biderman, and Snyder)

[48] *See, e.g.*, JX0250 at CI000496-556 (July 31, 2002 Grad letter transmitting signed agreements to SMC and stating to Dwyer had it had been a pleasure working with him).

executed a *unanimous* written consent authorizing the requisite amendments to SMC's Certificate of Incorporation (the "Charter"), and Wren, Javva, and Catalyst executed a written consent as the holders of a majority of the outstanding stock to effectuate the amendments.[49] JX0255. The Board also consented *unanimously* to approve a 20:1 reverse stock split. *Id.* at CI000205-11. The stockholders consented to the reverse stock split (which Plaintiffs concede had no dilutive effect) and Charter amendment. *Id.* at DEFS010356-62; JX0258 at CI011836-40.[50] Following the reverse stock split, and the other Charter amendments, SMC had authorized 28 million shares, of which 25 million were common. JX0298. There had been no change since January in the value of the common shares, which remained worthless. JX0668 ¶ 8.

E. SMC Issues the Fall 2002 Update

In October 2002, SMC sent an update to all stockholders (the "Fall 2002 Update") to inform them about the Recapitalization. JX0774. Snyder, in conjunction with Dwyer, prepared and disseminated the Fall 2002 Update upon the advice, and with the assistance, of counsel. JX0643 (Tallan) at 149:18-150:2, 154:11-20. Among other things, the Fall 2002 Update informed SMC's stockholders of management's intention to re-brand SMC as Nine Systems Corporation ("NSC") and further described certain stockholder actions by written consent, including the issuance of Preferred B. JX0774 at PLT000104, PLT000108.

F. NSC Moves Forward

With the Recapitalization completed, Snyder set about growing the business purchased from NaviSite. JX0728. As discussed earlier in the year, and as reflected in Snyder's

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[49] Counsel advised SMC that a stockholders meeting was not necessary because SMC stockholders could act by written consent. *See* JX0203 (counsel stating that he "found no requirement for a stockholders meeting" as there was no restriction on the ability to act by written consent).

[50] JX0646 (Biderman) at 1063:6-12; JX0640 (Horowitz) at 435:2-15; JX0667 ¶ 9(f)(i) ("[S]tock split is nothing more than a mathematical change in the number of shares outstanding and has no impact on value . . .").

employment agreement, SMC had planned to adopt a new employee stock option plan. JX0200 at DEFS031395. At the September 25, 2002 Board meeting, the Board unanimously approved the "2002 Stock Option Plan," which was also approved by written consent of the stockholders. JX0320; JX0759 at CI00322-25. Pursuant to the 2002 Stock Option Plan, certain employees (including Snyder) were granted options to acquire an aggregate of 1,350,000 shares of common stock at an exercise price of 50 cents per share, or the equivalent of 2.5 cents per share pre-split. JX0320. This price implied an NSC equity value of no more than $500,000. Consistent with its financial results, showing minimal revenue growth through 2004,[51] NSC continued to issue 50 cents/share options through 2004. *See* JX0771.

G. Thomas Murphy Agrees to Sell His Shares to NSC

Thomas Murphy is a career consultant who early on contributed capital to SMC. *See* JX0005. That he is sophisticated cannot seriously be disputed. He has negotiated several hundred consulting contracts, drafted numerous agreements, and negotiated sale transactions. JX0696 (T. Murphy) at 8:11-15, 56-85. He has formed at least sixteen corporations and acted as a director or CEO of at least half. *Id.* at 56-75; *see also* JX0789.

As early as possibly 2004, Murphy thought about trying to sell his NSC common stock because he needed money. JX0696 (T. Murphy) at 10:19-20, 12:16-18, 209:7-9. He telephoned Cameron in or about March 2006 looking to sell his shares. *Id.* at 11:17-12:23; JX0695 (Walpuck) at 431:12-24. Dort Cameron has no recollection of such telephone call. By that time, he had received an invitation to a shareholder meeting in New York City on February 28, 2006,

[51] As reflected on its tax returns, NSC lost almost $7.8 million in FY 2002 (JX0164) and $24,251 in FY 2003 (JX0329). Not until FY 2004 did NSC generate any profit, earning $390,988 of income. JX0352. In FY 2005, NSC realized an operating profit of $897,000 on about $12 million of sales. JX0360. Even after taking into account its nominal operating profits from FY 2005 and 2006, NSC still carried an accumulated deficit of over negative $18,760,000 on its audited June 30, 2006 balance sheet. JX0508 at CI012788.

enclosing copies of NSC's 2004 and 2005 audited financials. JX0420. He might have also spoken to Dwyer. JX0696 (T. Murphy) at 30:24-31:2, 50:4-18. He was ultimately referred to Snyder and NSC's then-CFO, John Walpuck. *Id.* at 13:2-4, 15:1-2. Murphy asked Snyder some "very general questions about the status of the company," to which Snyder allegedly replied that NSC was "getting along . . . but not necessarily moving . . . forward." *Id.* at 20:16-22. Likewise, Murphy claims to have asked Walpuck "something to the effect of how's it going," to which Walpuck allegedly responded that "things were okay, but nothing really outstanding." *Id.* at 35:13-16, 36:17-19. The responses accurately described the actual condition of NSC, which, several years after the 2002 Acquisitions, was generating free cash of only a little more than $50,000 per month. JX0440; JX0677 (Walsh) at 301. Further, SMC was neither pursuing nor discussing any mergers or acquisitions.[52] Murphy also claims to have mentioned to either Snyder or Walpuck (but did not ask them about) some publicity that NSC had purportedly received in the business press. JX0696 (T. Murphy) at 24:15-26:2, 120:20-122:1.[53] Notably, Murphy did not ask *any* specific questions. *Id.* at 36:20-38:2, 145:22-147:9. In fact, he neither asked for nor received any disclosure. *Id.* at 35:11-36:7, 37:24-38:2, 39:24-40:1.

Despite getting a "strange" feeling from these conversations (*id.* at 121:20-21, 122:13-22), on June 2, 2006, Murphy agreed to sell 44,000 of his 45,000 shares of common stock to NSC for $1 per share pursuant to a Stock Purchase Agreement he negotiated with NSC (the "Murphy SPA"). JX0450 at Recitals A-B, §§ 1.1-1.2. While it is unclear who suggested the $1 price, it is clear that (contrary to his allegations) no one told Murphy that $1 was "fair," and no

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[52] JX0695 (Walpuck) at 471:20-472:16 (stating "there w[ere] no merger conversations" before August 8, 2006); *see also* JX0484.

[53] According to Murphy, NSC did not acknowledge the publicity and did not volunteer any additional information. JX0696 (T. Murphy) at 120:13-19, 146:13-17, 147:2-6, 160:18-162:15, 226:12-17, 228:20-231:3. Despite being requested by the Defendants, Plaintiffs have not produced a copy of the alleged "publicity." *Id.* at 156:22-158:6.

one forced him to sell his shares. JX0696 (T. Murphy) at 138:11-21, 167:11-16; JX0695 at 445:6-8. Murphy described the Murphy Stock Sale as a "pretty simple transaction" and understood the entire Murphy SPA.[54] The Murphy SPA contained several provisions by which Murphy expressly disclaimed reliance upon any representations not contained therein.[55] The terms of the Murphy SPA were negotiated through several iterations. JX0696 (T. Murphy) at 7-8.[56]

A few months after the stock sale, Murphy received the Akamai Merger materials (discussed below) distributed to all NSC stockholders in November 2006. *See* Kim Am. Compl. ¶¶ 143-44; JX0696 (T. Murphy) at 247:1-5. Murphy claims that after learning of the Akamai Merger, he had a feeling that the Defendants had not fully informed him of NSC's real condition at the time of his stock sale. JX0696 (T. Murphy) at 41:18-42:17, 151:24-152:3. Indeed, he says he reached the conclusion *in 2006* that there were ongoing merger discussions that had been withheld from him. *Id.* at 236:10-14. He thought he had reason to sue the Defendants, but waited nearly six years to do so. *Id.* at 130:4-132:23.

H. The Akamai Merger

Four years after the Recapitalization,[57] in or about August 2006, NSC (through a banker) first approached Akamai about a potential merger. JX0695 (Walpuck) at 471:20-472:16;

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[54] *Id.* at 8:8, 34:15-16, 216:7-9, 220:19-221:20; *see also* JX0450 § 3.2.1 (Murphy warranting that he "carefully reviewed" and "under[stood]" the Murphy SPA and its terms).

[55] JX0450 § 2.5 (acknowledging that "no promises, representations or warranties whatsoever . . . have been made by [SMC] to induce [him] to execute this Agreement"); *id.* § 3.2.1 (agreeing that he "has not been influenced to any extent whatsoever in making this Agreement by any representations or statements made by any other party or anyone acting on behalf of any other party"); *id.* § 5.6 (acknowledging that "[t]here are no representations, agreements, arrangements or understandings . . . which are not fully expressed herein").

[56] For instance, prior drafts of the agreement show Murphy selling at first all 45,000 shares, and later only 40,000 shares. JX0449; JX0448 at DEFS058069-70; JX0442 at DEFS058074-75.

[57] This Court previously held that "[t]he Akamai acquisition occurred roughly four years after the challenged actions, and it could not have been foreseen, and was not foreseen, when those events occurred." *Summary Judgment Op.* at *5 (footnote omitted).

JX0484 at 4. In November 2006, Akamai agreed to the Akamai Merger, in which it exchanged 3,250,000 Akamai shares for all outstanding NSC shares. JX0499; JX0703. NSC's Board approved the Akamai Merger by a vote of four-to-one, with Biderman dissenting. JX0497 at DEFS047479. Biderman complained that the Recapitalization, for which he had voted four years earlier, resulted in the Lipper investors receiving less merger consideration than he thought they should get. *Id.* at DEFS047478.

The Akamai Merger was disclosed to NSC's stockholders in materials sent on November 25, 2006. Kim Am. Compl. ¶¶ 125-26; JX0512. The materials discussed the merger, including the total consideration, described Biderman's objection, and enclosed a complete set of NSC 2004-06 audited financials and a consent solicitation asking the shareholders to approve the merger. JX0512 at AB000147-99. Nearly all NSC stockholders returned consents in favor of the Akamai Merger.[58]

ARGUMENT

I. THE ABSENCE OF A CONTROL GROUP MANDATES JUDGMENT IN FAVOR OF ALL DEFENDANTS ON ALL CLAIMS (OTHER THAN THE DISCLOSURE AND MURPHY STOCK SALE CLAIMS)

Except for the disclosure claims, all of Plaintiffs' claims relating to the Recapitalization are derivative in nature.[59] No matter how denominated, the claims attack the Recapitalization as being harmful *to SMC*, and seek damages against Defendants for value that they supposedly expropriated from *all* other stockholders.[60] Accordingly, *all* claims except (i) the disclosure claims relating to the Fall 2002 Update (*see* Part II.B and III.D *infra*); and (ii) the Murphy Stock

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[58] JX0523 at DEFS045841 ("[NSC] had received consents to the Merger from holders of in excess of 94% of the issued and outstanding voting stock of the Corporation.").

[59] The Court has held that disclosure claims relating to the Fall 2002 Update are direct. *Dubroff I*, 2009 WL 1478697, at *6; *Dubroff III*, 2011 WL 5137175, at *10 n.48.

[60] *Dubroff III*, 2011 WL 5137175, at *11.

Sale claim (*see* Part IV *infra*) should be dismissed under the continuous ownership rule.

Plaintiffs rely on the *Gentile* exception to the continuous ownership rule.[61] As there is no dispute that SMC had no single controlling stockholder, to invoke *Gentile*, Plaintiffs must prove that Wren, Javva, and Catalyst acted as a single unit or "control group."[62] A control group exists where the stockholders in question are "connected in some legally significant way—*e.g.*, by contract, common ownership, agreement or some other arrangement—to work together toward a shared goal."[63] As this Court has observed, "[p]roving the existence of a control group is one of the most difficult things one has to prove in the absence of the proverbial smoking gun."[64] Proof that separate stockholders voted the same way, had agreements among themselves regarding subjects other than the challenged transaction, had common or parallel objectives, or even stood together on both sides of the same self-dealing transaction are insufficient.[65] Rather, to prove a control group, Plaintiffs must establish the existence of a "blood pact" among different stockholders to act as the functional equivalent of a single, majority stockholder.[66] So stringent is the standard that our research has revealed only *one* case in which this Court found a plaintiff

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[61] *Summary Judgment Op.* at *5 ("Unless the Gentile exception applies, the Plaintiffs' dilution claims are solely derivative, and, because of the intervening [Akamai Merger], their claims must be dismissed"); *see Gentile v. Rossette*, 906 A.2d 91, 99-100 (Del. 2006) (describing the direct right of action as arising "where: (1) a stockholder having majority or effective control causes the corporation to issue 'excessive' shares of its stock in exchange for assets of the controlling stockholder that have a lesser value; and (2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling stockholder, and a corresponding decrease in the share percentage owned by the public (minority) shareholders.").

[62] *Summary Judgment Op*. at *6.

[63] *Id*. at *5 (quoting *Dubroff I*, 2009 WL 1478697, at *3).

[64] *In re Nine Sys. Corp. S'holder Litig.*, C.A. No. 3940-VCN, at 56 (Del. Ch. Sept. 10, 2013) (TRANSCRIPT) (Trans. ID 54170911); *accord Summary Judgment Op.* at *6.

[65] *Summary Judgment Op*. at *6; *see Dawson v. Pittco Cap. Partners*, 2012 WL 1564805, at *16 (Del. Ch. Apr. 30, 2012) (holding that there was no control group: "[a]t best, the Plaintiff has shown that [two of the defendants] stood on both sides of the Merger").

[66] *Summary Judgment Op*. at *5; *In re PNB Holding Co. S'holders Litig.*, 2006 WL 2403999, at *10 (Del. Ch. Aug. 18, 2006) (finding no control group in the absence of an agreement to vote together, and rather finding that "it appears that each [stockholder] had the right to, and every incentive to, act in his or her own self-interest as a stockholder").

to have proved (as opposed to merely pled) the existence of a control group comprised of unaffiliated stockholders; in that case, the stockholders were close friends and parties to a written, *binding* agreement to vote together to advance their shared goal of marginalizing the corporation's third stockholder.[67]

The facts of this case could not be more different. Wren, Javva, and Catalyst were each minority shareholders who were essentially strangers to each other, having never invested or done business with each other, before or after their respective investments in SMC.[68] There is *no* evidence (and certainly no "smoking gun") that they ever entered into an agreement to recapitalize SMC or to steal shareholder value, and each of Defendants' witnesses flatly denies any such agreement. There decidedly is no basis to believe that Catalyst abdicated its independent judgment—and the interests of its own investors—in favor of the dictates of a cartel. In short, to find the existence of a control group on these facts, we respectfully submit, would turn the *Gentile* exception on its head and swallow up the continuous ownership rule.[69] That is especially so where one of the members of the supposed control group (Catalyst) was as detrimentally impacted by the transaction at issue as the plaintiff shareholders who challenge it.[70]

Moreover, Plaintiffs' reliance on isolated references in Catalyst's internal documents to

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[67] *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 26 (Del. Ch. 2010).

[68] *Cf. Aronson v. Lewis*, 473 A.2d 805, 815 (Del. 1984) (holding that, to overcome the presumption of a director's disinterestedness and independence, plaintiffs must show the director to be beholden to the controlling person by personal or other relationships), *overruled on other grounds*, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

[69] *See Summary Judgment Op.* at *8 (describing *Gentile* as a "limited exception" to the continuous ownership rule); *see also, e.g.*, *Ark. Teacher Ret. Sys. v. Countrywide Fin. Corp.*, -- A.3d --, 2013 WL 4805725, at *1 (Del. Sept. 10, 2013) ("reaffirm[ing] the continuous ownership rule" and declining to enlarge an exception to it).

[70] *Cf. Gentile*, 906 A.2d at 102-03 (recognizing a direct action because the transaction benefitted the controlling stockholder and harmed the minority stockholders uniquely).

an "option" as (its sole) proof of a control group is unavailing.[71] Beyond the fact that Plaintiffs cannot prove that Catalyst received any option (*see* Facts, Part II.D.3 *supra*), the mere existence of an option, without more, does not establish a control group. No evidence exists of any agreement between Wren and Javva. And even if Catalyst received an option (which it did not), that mere fact would not prove a legally significant connection toward a shared goal among Wren, Javva, and Catalyst. The fact that Catalyst indisputably did not exercise any option and, further, wrote down all of its common stock to zero demonstrates that any "option" it had to invest new money in SMC would not have been material to it, let alone sufficiently material to induce it to subordinate its own investors' interests to those of a "group."[72] In short, the Plaintiffs cannot come forward with any credible evidence of the existence of a control group, and, for that reason alone, judgment in favor of the Defendants must be entered on all their claims, except for the disclosure claim and Thomas Murphy's fraud claims.

II. JUDGMENT SHOULD ALSO BE ENTERED FOR THE DEFENDANTS ON ALL CLAIMS (OTHER THAN THE MURPHY STOCK SALE CLAIM) BECAUSE THE RECAPITALIZATION WAS ENTIRELY FAIR

A. The Recapitalization Was Entirely Fair

The actions of the Board of Directors, like the Recapitalization, are by default protected by the business judgment rule and, therefore, not subject to challenge. Plaintiffs may rebut the business judgment rule by proving at trial, on a director-by-director basis, that a majority of the directors who approved the Recapitalization were not disinterested and independent.[73] If they carry that burden, then the burden would shift to Defendants to prove that the Recapitalization

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[71] *See Summary Judgment Op.* at *6 n.50 ("Without the 90-day option . . . , the underpinning of [Plaintiffs'] *Gentile* argument may largely fall away.").

[72] *See, e.g.*, *Sutherland*, 2013 WL 2362263, at *7 & n.95 (stating that to establish that a director is interested because of a benefit not equally shared by the stockholders, plaintiff must show that the benefit was material).

[73] *See Aronson*, 473 A.2d at 812; *Cede & Co v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993).

was entirely fair, in which case immunity from challenge would be re-established.[74] Here, it does not matter which standard applies because Defendants meet the entire fairness standard.

Reviewing a transaction for entire fairness entails objective[75] consideration of two factors—fair dealing and fair price—*i.e.*, procedural and substantive fairness.[76] The procedural aspects of fairness include the timing, negotiation, structure, and approval of the transaction.[77] In this case, relevant facts include the information available to the directors at the time the Board approved the Recapitalization, SMC's financial distress, and the time available to act.[78] The substantive aspects of fairness relate to price. This is the predominant factor; if the price was fair, then there can be no damages.[79] The fair price analysis involves consideration of all relevant factors, including evidence of SMC's actions leading up to the Recapitalization, its condition at the time, its actual performance, and expert testimony regarding valuation.[80]

Although entire fairness requires consideration of both procedural and substantive factors, the Court is ultimately called upon to make a unitary fairness conclusion based upon the

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[74] *In re Trados Inc. S'holder Litig.*, 2013 WL 4511262, at *1 (Del. Ch. Aug. 16, 2013).

[75] *Gesoff v. IIC Indus., Inc.*, 902 A.2d 1130, 1145 (Del. Ch. 2006).

[76] *ONTI, Inc. v. Integra Bank*, 751 A.2d 904, 930 (Del. Ch. 1999) (entire fairness "consists of two elements, unfair dealing and unfair price, also known as procedural fairness and substantive fairness, respectively").

[77] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).

[78] *Emerald Partners v. Berlin*, 2003 WL 21003437 (Del. Ch. Apr. 28, 2003) ("*Emerald I*"), *aff'd*, 840 A.2d 641 (Del. 2003) (concluding that the Board acted fairly based upon the information available); *Savin Bus. Mach. Corp. v. Rapifax Corp.*, 4 Del. J. Corp. L. 578, 585 (Del. Ch. 1978).

[79] *Emerald Partners v. Berlin*, 2003 WL 23019210, at *1 (Del. Dec. 23, 2003) (holding that, where the price is fair but the process is not, it did not matter whether defendants were exculpated because "they are not liable for any monetary damages"); *Trados*, 2013 WL 4511262, at *44 ("Although the defendant directors did not adopt any protective provisions, failed to consider the common stockholders, and sought to exit without recognizing the conflicts of interest presented by the Merger, they nevertheless proved that the transaction was fair" because the stockholders received the substantial equivalent of what they had before—meaning the price was fair); *Oliver v. Boston Univ.*, 2006 WL 1064169, at *25 (Del. Ch. Apr. 14, 2006) (awarding the plaintiff nominal damages in an action challenging a transaction that was not entirely fair because, although the process was not fair, the price received was fair).

[80] *See Trados*, 2013 WL 4511262, at **36-44 (considering these factors).

totality of the circumstances.[81] In the final analysis, "the proper 'test of fairness' [is] whether 'the minority stockholder [] receive[d] the substantial equivalent in value of what he had before.'"[82] If after the transaction the value of the plaintiffs' equity was worth the same as or more than it was worth before, then the transaction was entirely fair.[83] That, necessarily, is the result when the value of a plaintiff's shares immediately prior to the challenged transaction was zero.[84] Where a plaintiff's equity was worthless immediately prior to the challenged transaction, then, by definition, the transaction could not have left her with any less than she had before, and the transaction, as a whole, was entirely fair. That is the case here.

1. Unitary Fairness Conclusion

The evidence at trial will admit of only one conclusion: The Recapitalization was entirely fair. Contemporaneous records, credible witness testimony, and unrebutted expert opinion will establish that SMC's common shares had no value before, during, and immediately after the Recapitalization. (*See* Facts, Part II.D *supra*). Among other things, the evidence will show that at the time of the Recapitalization: (i) SMC's revenues were insufficient to maintain its operations, let alone to service its debt; (ii) its debt was suffocating its common shareholders,

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[81] *See Emerald I*, 2003 WL 21003437, at *22; *Wayne County Employees' Ret. Sys. v. Corti*, 2009 WL 2219260, at *11 (Del. Ch. July 24, 2009), *aff'd*, 996 A.2d 795 (Del. 2010).

[82] *Trados*, 2013 WL 4511262, at *44 (quoting *Sterling v. Mayflower Hotel Corp.*, 93 A.2d 107, 114 (Del. 1952)); *accord Union Ill. v. Korte*, 2001 WL 1526303, at *7 & n.14 (Del. Ch. Nov. 28, 2001) ("In other words, it is 'entirely fair' to the corporation that it receive from the directors the most it could have received from outsiders for this small issue of equity—the market value of the shares.").

[83] *See Trados*, 2013 WL 4511262, at *44; *see also In re Tri-Star Pictures, Inc. Litig.*, 634 A.2d 319, 331 (Del. 1993) (relied upon by *Gentile* as establishing a direct action for the difference between the liquidation value of plaintiffs' shares before and after a dilutive transaction sponsored by the controlling stockholder).

[84] *See Trados*, 2013 WL 4511262, at *46 ("The common stock had no economic value before the Merger, and the common stockholders received in the Merger the substantial equivalent in value of what they had before [*i.e.*, nothing]."); *In re Hanover Direct, Inc. S'holders Litig.*, 2010 WL 3959399, at *3 (Del. Ch. Sept. 24, 2010) ("I conclude that the company was in fact 'under water' at the time of the merger. Accordingly, a merger price above $0.00 . . . was entirely fair.").

with some $5 million in secured debt alone, multiplying to $20 million in a liquidation;[85] (iii) SMC had been unsuccessful in raising outside financing; and (iv) it had blown through all of the money it had ever raised, including the roughly $4.75 million raised in the Secured Note offering. In short, SMC was not a going concern, and did not have any prospect of generating a return for its common shareholders.[86] As such, there is nothing that Defendants could have done in the Recapitalization to unfairly dilute, or expropriate "value" from, the Plaintiffs. Put another way, Plaintiffs did not "suffer[] cash value dilution"[87] because their shares had no value to be diluted.[88] Indeed, while Plaintiffs' common shares were worthless, the Recapitalization resulted from careful deliberation and treated the existing common as if it had value, giving the new money only half the common equity. Accordingly, and as confirmed by the procedural and substantive fairness factors, the Recapitalization was entirely fair.

2. The Recapitalization Was Procedurally Fair

a. Initiation and Timing of the Recapitalization

The Recapitalization was conceived and initiated by SMC's management, not the Defendants, and its timing and motivation were driven primarily by three factors, none of which were orchestrated or manufactured by Defendants: (i) SMC's need for an immediate cash infusion; (ii) implementation of Williams's plan to use acquisitions as sources of revenue in an attempt to turn SMC around; and (iii) the emergence of the opportunity to acquire e-Media and

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[85] *See Trados*, 2013 WL 4511262, at *45 (recognizing the fact that the company could not escape the "gravitational pull of [its] large liquidation preference" and dividend obligations as a factor indicating that the company "would [not] yield value for the common [stock]").

[86] *See id.* ("If [SMC] could not self-fund its business plan, then [SMC] could not execute it. Even if it could self-fund, [SMC] had to build value at a rate [sufficient to service debt] to generate a return for the common.").

[87] *See Tri-Star*, 634 A.2d at 331.

[88] Likewise, the allocation of 20% of the post-Recapitalization equity to the Preferred A in exchange for conversion of the Secured Notes was fair because, in the event of liquidation, the Preferred A would have taken everything owing to its $20 million liquidation preference.

NaviSite SMG. (*See* Facts, Part II.D *supra*). The Recapitalization was undertaken for the legitimate purpose of providing SMC with operating capital and to fund the 2002 Acquisitions. It was not designed, with a lucrative exit in sight, to create a windfall or prey upon unsuspecting investors.[89] Accordingly, the initiation and timing of the Recapitalization reflect fair dealing.

b. Negotiation and Structure of the Recapitalization

The terms of the Recapitalization were considered and negotiated over a series of Board meetings in the first quarter of 2002 by all five directors. The Board's deliberations specifically included consideration of the dilutive effect of the Recapitalization on the non-participating stockholders. Over the course of the negotiations, dilution was addressed, both by considering the terms of the transaction in light of SMC's and the 2002 Acquisitions' respective revenues and by adopting Biderman's proposed revised terms. Ultimately the Board decided on terms of the transaction that were unanimously accepted.[90]

Plaintiffs' attack on the procedural fairness of the Recapitalization largely focuses on the absence of outside financial advice and a special committee. "There is no legal requirement that a board consult outside advisors, so long as the board has adequate information to make an informed judgment."[91] In this case, SMC had neither the time nor money to hire a financial advisor, obtain a fairness opinion, or conduct a private offering.[92] No investor would have been willing to invest money to pay for such services, and SMC could not go back to Daniels for

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[89] *See Summary Judgment Op.* at *5 ("The Akamai [Merger] occurred roughly four years after the challenged actions, and it could not have been foreseen, and was not foreseen, when those events occurred.").

[90] *Savin*, 4 Del. J. Corp. L. at 585 ("Where a corporation in financial distress issues stock as a means to raise needed capital, its directors are given considerable latitude in fixing the price for the issuance.").

[91] *Chesapeake Corp. v. Shore*, 771 A.2d 293, 331 (Del. Ch. 2000).

[92] *See Zimmerman v. Crothall*, 2012 WL 707238, at *9 (Del. Ch. Mar. 5, 2012) ("[T]he Company's limited cash position likely would have made it reluctant to incur such an expense [to obtain outside financial advice].").

financial advice because Daniels had not been paid for its previous services. JX0230.[93]

Additionally, forming a special committee to consider the Recapitalization would not have added anything to the fairness analysis because there was no director whose constituency was not given the opportunity to participate in the Recapitalization. In any event, Biderman was at the Board meetings negotiating for the Lipper interests and ultimately voted for the Recapitalization. In this way, Biderman functioned as a check on the negotiation process analogous to a special committee. Likewise, since Catalyst had resolved not to invest more, Shipman served as an additional check on the terms of the Recapitalization.

Moreover, far from Plaintiffs' view of the Recapitalization as a vehicle for Defendants to seize SMC, each of Wren and Javva did not ask for or want the entire burden of funding SMC, and Catalyst did not want to participate at all. The opportunity to contribute new money was extended to *each* constituency represented on the Board (Wren, Javva, management, Catalyst, and Lipper) repeatedly over a four month period. Notably, although it was not required to do so, SMC extended the opportunity to participate to Lipper in the exact same manner as done with respect to the Subordinated Notes and the Secured Notes, by communicating, and negotiating, with Biderman. In short, the negotiation and structure of the Recapitalization show fairness.

c. Director and Stockholder Approval

The transaction was unanimously approved by the Board, including Biderman, whom Plaintiffs claim was disinterested and independent. Dilution to non-participating stockholders was raised and deliberated by the Board throughout the process. The ultimate vote reflected the Board's judgment that the terms were fair. In August 2002, again unanimously, the Board

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[93] Plaintiffs cannot dispute that SMC had neither the time nor the cash to hire a large investment bank to do a fairness opinion in connection with the Recapitalization. Plaintiffs speculate that SMC could have obtained a cheap, fast fairness opinion from a smaller investment bank, but there is no evidence to support the availability of such an opinion for SMC at the time. In addition, there is no evidence that an opinion obtained under those conditions would have added anything material to the fairness analysis.

approved the Charter amendments necessary to create the Preferred shares.

Biderman did not dissent, nor did he tell anyone at the time that he had any misgivings about his approval of the Recapitalization. Indeed, he voted in favor of the terms after several rounds of negotiation, including acceptance of terms he proposed. Biderman also contacted the Preferred A Plaintiffs and encouraged them to convert their Secured Notes. Biderman also consented to the amendments to the Charter to issue the Preferred stock and effectuate the Preferred stock issuance and reverse stock split. These are not the actions of a director who believed that an unfair transaction had been approved over his objection. Thus, assuming, as Plaintiffs contend, that Biderman was disinterested and independent, the Board's repeated, unanimous approval and implementation of the Recapitalization is strong evidence of fairness.

Approval of the Recapitalization did not require a stockholder vote or meeting. SMC did not hold a stockholders meeting to approve the amendments to the Charter based on counsel's advice that such a meeting was unnecessary. As such, the absence of a meeting or vote of the other stockholders is not evidence of unfairness.[94] Moreover, although the Recapitalization was not conditioned on a stockholder vote, the final issuance of the Preferred was effectively conditioned on all Secured Note holders agreeing to convert into Preferred A, which they did.

3. The Recapitalization Was Substantively Fair

SMC performed poorly from its inception through the Recapitalization (and thereafter). In an effort to grow the business, several changes, including the hiring of more experienced executives, were made in mid-to-late 2001. None helped. SMC remained unprofitable, faced severe cash shortfalls, and was in constant need of additional funding. Its business model never gained traction, and its new CEO and CFO met with little more success than did their

[94] *Trados*, 2013 WL 4511262, at *36; *see* 8 *Del. C.* § 141(e).

predecessors in growing SMC's revenues—or predicting them. Moreover, SMC was unable to grow its revenues in 2001 sufficiently to sustain its operations. By the time of the Recapitalization, SMC's revenues had sunk to around $70,000 a month, and it was out of cash. Events subsequent to the Recapitalization, such as NSC's lack of growth and the pricing of options with a stock price of 50 cents per share at least through 2004, and unrebutted expert testimony, confirms that SMC's equity had been rendered worthless.[95] Accordingly, given SMC's distressed financial condition and lack of equity value, the terms of the Recapitalization were financially fair.

B. Judgment Should Be Entered for the Defendants on the Disclosure, Aiding and Abetting, and Unjust Enrichment Claims

The principal attack on the Fall 2002 Update is that it failed to reveal that the Recapitalization was a self-dealing transaction and that Plaintiffs' dilution was caused primarily by increasing the shareholdings of Wren and Javva. Since the Recapitalization was entirely fair, however, the omission of the transaction's self-dealing nature could not possibly be material. Additionally, any non-disclosure could not have caused injury.[96] Plaintiffs' (and Dubroff's and Klein's) sole theory is that they were harmed because the alleged omissions from the Fall 2002 Update precluded them from seeking rescission of the Recapitalization.[97] Because it was entirely fair, however, there was no basis on which to seek rescission of the Recapitalization. Additionally, because judgment should be entered for Defendants on each of the fiduciary duty

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[95] *See S. Muoio*, 2011 WL 863007, at *17 (refusing to disregard "the economic reality which [the company] faced" in concluding that the merger at issue was entirely fair).

[96] *See Dubroff III*, 2011 WL 5137175, at *10 (citing *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 597 (Del. Ch. 2007); *In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 766, 773-74 (Del. 2006)) (limiting damages for non-disclosure to those caused by the disclosure distinct from the Recapitalization).

[97] Fuchs Am. Compl. ¶ 93; Kim Am. Compl. ¶ 109; Dubroff Compl. ¶¶ 83-87; *Dubroff III*, 2011 WL 5137175, at *10 & n.46.

claims, there can be no liability for aiding and abetting.[98] Nor can Plaintiffs sustain an unjust enrichment claim. Unjust enrichment is not an end-run around defined legal standards governing conduct. A transaction that was entirely fair cannot give rise to an "unjust enrichment."[99]

III. JUDGMENT SHOULD BE ENTERED FOR DEFENDANTS ON THE CLAIMS OF THE FOUNDING STOCKHOLDERS, THE SMIG PLAINTIFFS, THE FUCHS BROTHERS, AND FOR DISCLOSURE FOR ADDITIONAL REASONS

A. The Founding Stockholders' Claims Are Barred by Laches

Laches is present (i) where a plaintiff having knowledge of his claim, (ii) delays unreasonably in bringing the claim, and (iii) the delay results in prejudice to the defendant.[100] The Founding Stockholders admit to being on inquiry notice upon receipt of the Akamai Merger materials around November 25, 2006.[101] They delayed unreasonably by waiting for more than a year after denial of class certification to file suit.[102] Accordingly, the first two elements of laches have already been found by this Court, and prejudice is the only showing that remains.

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[98] *See Malone v. Brincat*, 722 A.2d 5, 14-15 (Del. 1998).

[99] *See Monroe County Employees' Ret. Sys. v. Carlson*, 2010 WL 2376890, at *2 (Del. Ch. June 7, 2010) (dismissing an unjust enrichment claim based upon the same facts as a claim for breach of fiduciary duty); *In re Bank of Am. Corp. Sec., Deriv., & Employee Ret. Income Sec. Act (ERISA) Litig.*, 2013 WL 1777766, at *15 (S.D.N.Y. Apr. 25, 2013) (applying Delaware law and holding that because the plaintiff's "unjust enrichment claim [was] premised on defendants' violation of their fiduciary duties, and the breach of fiduciary duty claim [was] dismissed, [the plaintiff's] unjust enrichment claim [was] dismissed as well" (citing *Carlson*)); *see also Nemec v. Shrader*, 991 A.2d 1120, 1130-31 (Del. 2010) (affirming dismissal of an unjust enrichment claim predicated upon an alleged breach of contract that the plaintiffs failed to establish); *Beck & Panico Builders, Inc. v. Straitman*, 2009 WL 5177160, at *7 (Del. Super. Nov. 23, 2009) ("Where the plaintiff cannot satisfy the elements required to make out a tort claim, an argument that the defendant has been unjustly enriched by tortious conduct necessarily fails as well.").

[100] *Nine Sys. II*, 2013 WL 4013306, at *4.

[101] *Id.* at *4, *7; *see also* Kim Am. Compl. ¶¶ 143-44 (conceding that the Shareholder Plaintiffs were on inquiry notice by no later than November 25, 2006).

[102] *Nine Sys. II*, 2013 WL 4013306, at *7 ("The more than fifteen months available to the Shareholder Plaintiffs following denial of classification was sufficient for any diligent plaintiff to present her claims. Dismissal of the Shareholder Plaintiffs' claims because of their dilatory conduct should trigger no equitable handwringing."). This is particularly true with respect to Rick Murphy, who explained during his 2012 deposition—taken more than six months *prior* to him joining the litigation—that he had ample knowledge and even obtained opinions from multiple attorneys regarding his rights. JX0601 (R. Murphy) at 343. Murphy opted not to take any legal action, however, because he "wasn't financially in a position to be able to do that. And [he] did not think it was a good use of [his] time." *Id.* at 342:2-8.

As this Court observed, because this action was pending for more than four years before the Founding Stockholders filed their claims, the passage of time alone is prejudicial.[103]

But even beyond the passage of time, Defendants have been prejudiced by the added costs resulting from the Founding Stockholders' delay.[104] A party causes prejudice when he "suffers his adversary to incur expense, or enter into obligations or otherwise change his position, or in any way by inaction lulls suspicion of his demands to the harm of the other . . . ."[105] The Founding Stockholders delayed, with full notice of their claims, until after fact discovery had been all but completed in the Fuchs litigation. As a result, Defendants incurred the costs of (i) another round of briefing on a motion to dismiss; and (ii) another round of fact discovery, including responding to dozens of new written discovery requests from Plaintiffs.[106] Defendants were again forced to collect information, search for documents, and draft voluminous responses. The delay also necessitated five *re*-depositions (of Dwyer, Snyder, Dort Cameron, Rick Murphy, and a non-party).[107] All of this could have been (and would have been) done concurrently with the Fuchs litigation had the Founding Stockholders not unreasonably delayed their suit. Accordingly, all of the Founding Stockholders' claims challenging the Recapitalization are time-barred.

B. The SMIG Plaintiffs Lack Standing

"As a general matter, when the terms of a transaction are established—not when the

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[103] *Nine Sys. II*, 2013 WL 4013306, at *7.

[104] *See, e.g.*, *Steele v. Ratledge*, 2002 WL 31260990, at *4 (Del. Ch. Sept. 20, 2002) ("If this action is permitted to proceed, the defendants will have suffered significant financial prejudice by reason of the plaintiffs' delay."); *Fike v. Ruger*, 752 A.2d 112, 114 (Del. 2000) (concluding "had Plaintiffs filed suit before 1992, defendants . . . could have avoided significant personal losses").

[105] *Wilkes v. German*, 316 A.2d 200, 205 (Del. 1974).

[106] *See, e.g.*, JX0664; JX0665; JX0691.

[107] Indeed, two of the three individual Founding Stockholders—Rick Murphy and Schaum—were deposed in March and April of 2012, respectively. Both sat on their hands *for more than six months after being deposed in this very case* before finally filing suit.

transaction is carried out—is the proper time for assessing whether a breach of fiduciary duty occurred."[108] Therefore, to have standing, the SMIG Plaintiffs must prove that there was a breach that occurred after they became stockholders on May 30, 2002.[109] For the reasons discussed above in Part II, because, among other things, SMC's common equity had no value in May 2002 (JX0668 ¶¶ 37-38), no such breach occurred.

Moreover, there were no changes to the terms (dilutive or otherwise) of the Recapitalization that occurred after the SMIG Plaintiffs became SMC stockholders that could have injured them. They claim that the percentage of SMC's total equity represented by the Preferred B-1 issued to Wren and Javva was different than the percentage approved by the Board in January and April. This, however, did not result from any change in the terms of the Recapitalization. Rather, the difference resulted from the issuance of fewer Preferred A and B-2 shares because: (i) the face amount of the e-Media Note was reduced, resulting in e-Media receiving fewer Preferred B-2 shares (JX0190); (ii) Williams did not make his committed $200,000 investment in the Secured Notes, resulting in a lower outstanding Secured Notes balance and therefore fewer Preferred A shares being issued;[110] and (iii) Biderman delayed obtaining the Preferred A Plaintiffs' consent to the conversion of their Secured Notes, resulting in slightly more Preferred A shares being issued under the conversion formula. Unable to prove any Board or shareholder action *after* they became SMC shareholders that was unfair or injurious, the SMIG Plaintiffs cannot sustain any claims.

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[108] *Summary Judgment Op.* at *7 (citing *7547 Partners v. Beck*, 682 A.2d 160, 162-63 (Del. 1996)).

[109] *See id*.

[110] Had Williams funded his $200,000 Secured Note subscription, the total amount of Secured Notes convertible to Preferred A would have increased from $5,330,172 to $5,552,868. As such, the percentage of NSC's overall equity attributable to the Preferred B-1 and B-2 would have been reduced accordingly.

C. The Fuchs Brothers Have No Injury Because They Received a Windfall

The Fuchs brothers did not have MFN rights. The only "evidence" to the contrary is the Fuchs brothers' equivocal and self-serving testimony,[111] which falls well short of proving the existence of a written agreement, as they would need to enforce contractual MFN rights.[112] In addition, Bernard Fuchs' testimony that he received MFN rights is contradicted by both his tax returns[113] and SMC's stock audit. Because the Fuchs brothers were mistakenly issued excessive SMC shares in 2001, they were overcompensated in the Akamai Merger by a factor of eight and eighteen, well in excess of the amount by which they claim to have been diluted.[114] This windfall, received at the expense of SMC's other stockholders, bars their further recovery here.

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[111] *See* JX0636 (B. Fuchs) at 35, 66-67 (testifying that he did not sign the agreement); *id*. at 58 (testifying that it was "possible" that he invested in the subsequent round pursuant to the stock purchase agreement); JX0635 (M. Fuchs) at 160-62 (denying knowing of any document establishing an agreement with MFN rights); *but see id*. at 161 (testifying in response to a question by his own counsel, in the midst of the questioning by Defendants' counsel, that he had signed a stock purchase agreement).

[112] *Austin v. Judy*, 2013 WL 1944102, at *2 (Del. May 9, 2013) (affirming the Court of Chancery's determination that oral testimony alone was insufficient to establish the existence of an agreement); *Evans v. Perry*, 2011 WL 3667394, at *4 (Del. Com. Pl. July 29, 2011) ("There is an obvious issue of credibility when the proponent of a contract submits the only testimony regarding the contract's existence. In that scenario, biases exist as to information, selective memory, and interpretation of facts. While none of these biases involve dishonesty or lying, they do affect the weight of a witness's testimony. When testimony is the only evidence a Court has at its disposal, its weight is a significant factor."); *Krenowsky v. Haining*, 1988 WL 90825, at *4 (Del. Ch. Aug. 30, 1988), *aff'd sub nom. Hull v. Krenowsky*, 567 A.2d 421 (Del. 1989) (finding no credible evidence of an agreement where only the "self-serving testimony" of the proponent of the agreement and her daughter was offered to prove that an agreement existed); *Lakeshore Deli, Inc. v. Wilson*, 5 Del. J. Corp. L. 143, 144-45 (Del. Ch. 1978) (holding that plaintiffs failed to meet their burden of proving that a stock agreement existed since they could not provide a written copy of the agreement). The MFN rights that the Fuchs brothers rely on could not be performed within the space of one year, and therefore to be enforceable had to be contained in a written agreement signed by the party to be charged. *See* 6 *Del. C.* § 2714(a).

[113] JX0548; JX0549. Morris Fuchs has no documentary evidence supporting his claim that he was entitled to MFN rights. Both of the Fuchs brothers reported taxable gains on their 2007 tax returns attributable to the disposition of their respective equity interests in NSC. In each case, the reported tax basis in the shares disposed of was $100,000, consistent with NSC's own stock record reconciliation, reflecting total investments in SMC by each of the Fuchs brothers of $100,000. JX0769 at DEFS051353.

[114] *See Summary Judgment Op.* at *10.

D. Judgment Should Be Entered for Defendants on the Fall 2002 Update Claims

1. None of the Defendants Knowingly Disseminated False Information

Because the Fall 2002 Update was not disseminated in connection with a request for stockholder action,[115] it is Plaintiffs' burden to prove that the Director Defendants and/or Dwyer "knowingly disseminated false information" or deliberately misinformed the stockholders.[116] Plaintiffs cannot meet that burden.

To start, Shipman, Katz, and Cameron, who had no part in drafting or disseminating the Fall 2002 Update, did not "knowingly disseminate false information" or mislead anyone. Consequently, they cannot be liable.[117]

Furthermore, Snyder and Dwyer, who collaborated in preparing and disseminating the Fall 2002 Update, also did not act with any intent to deceive. They drafted and distributed the update under the advice and direction of counsel, disproving any intent to deceive. Accordingly, the disclosure claims against them also must fail.[118]

For yet another reason, Snyder did not breach his duty of loyalty in connection with the Fall 2002 Update, and Dwyer did not aid and abet him. Plaintiffs have the burden of rebutting the business judgment rule with respect to Snyder's role in the Fall 2002 Update.[119] To that end, they point to Snyder's receipt in September 2002 (like other employees) of (allegedly underpriced) options to purchase SMC stock, which Plaintiffs contend show Snyder was interested in the Recapitalization. The options, however, were not underpriced: the fair value of

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[115] *Dubroff II*, 2010 WL 3294219, at *6.

[116] *Summary Judgment Op.* at *9 (citing *Malone*, 722 A.2d at 10).

[117] *See, e.g.*, *Harold Grill 2 IRA v. Louis R. Chênevert*, 2013 WL 3014120, at *3 (Del. Ch. June 24, 2013) (dismissing a complaint "devoid of any attempt to plead facts connecting the directors to the disclosures made").

[118] *Summary Judgment Op.* at *9 & n.89 (citing *Malone*, 722 A.2d at 10; 8 *Del. C.* § 141(e)).

[119] *Emerald Partners v. Berlin*, 787 A.2d 85, 89-91 (Del. 2001).

SMC was *less* than the 50 cent per share strike price of the employee options issued to him and others. In addition, Plaintiffs' theory that there was a *quid pro quo* for Snyder's approval of the Charter amendment creating the Preferred is unsupported by any evidence. In the absence of any self-interest in the contents of the Fall 2002 Update, the business judgment rule is not rebutted, Snyder did not breach his duty of loyalty, and Dwyer did not aid and abet him.[120]

2. Plaintiffs Cannot Prove Reliance, Causation, or Damages

Judgment in favor of Defendants must also be entered on the disclosure claims, because neither Dubroff, Klein, nor any of the Plaintiffs can establish that they relied upon the Fall 2002 Update, or that, if they did, such reliance proximately caused them any harm.[121] Most of the Plaintiffs, and Dubroff and Klein, did not even recall the Fall 2002 Update.[122] Moreover, none have any contemporaneous evidence showing that they relied on the Fall 2002 Update or that they would have acted differently were the allegedly omitted facts disclosed. They cannot rely on their own self-serving and speculative testimony (with the benefit of over a decade of hindsight) to establish what they would have done. For these reasons, too, there is no evidence to support a claim in connection with the Fall 2002 Update.

IV. JUDGMENT SHOULD BE ENTERED FOR DEFENDANTS ON THE MURPHY STOCK SALE CLAIMS

A. There Was No Wrongdoing In Connection with the Murphy Stock Sale

The Murphy Stock Sale claims fail because neither Snyder nor Dwyer made any false or misleading statements to Thomas Murphy. He admits that Dwyer made no such statements.

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[120] *See Malone*, 722 A.2d at 14-15.

[121] *See Dubroff II*, 2010 WL 3294219, at *6 ("The plaintiffs' [disclosure] claims are subject to the broader requirements set forth in *Malone* . . . . [T]he elements of reliance, causation and damages will need to be individually established . . ." (footnote omitted)).

[122] JX0578 (Klein) at 91 (specifically denying receipt of the update); JX0579 (Dubroff) at 16; JX0616 (S. Schon) at 124-25; JX0620 (Wein) at 146; JX0621 (G. Loprete) at 158; JX0629 (Visovsky) at 197; JX0633 (M. Loprete) at 118; JX0635 (M. Fuchs) at 215; JX0636 (B. Fuchs) at 135; JX0641 (Golden) at 113; JX0642 (Reckler) at 209; JX0627 (Rausman) at 225.

JX0696 (T. Murphy) at 151. Rather, he claims that Snyder gave him the (supposedly false) impression that "SMC was surviving but by no means prospering." Kim Am. Compl. ¶ 136. This impression (if it was given) is insufficiently definitive to form the basis of a claim of fraud.[123] Moreover, it would not have been false: SMC *was* surviving but not prospering. Its modest revenues were insufficient to grow the business. Thus, neither Thomas Murphy's fraud nor breach of fiduciary duty claims can survive.

Furthermore, to establish actionable fraud by silence, Murphy would need to prove that the prospect of a potential merger between NSC and Akamai (or another partner) was sufficiently concrete to constitute "special knowledge."[124] The record is uncontroverted that there were no merger discussions at that time. Moreover, even if there were (which there were not), the duty to disclose would be borne only by those parties who purchased his stock. In this case, Murphy's stock was purchased not by any of the Defendants, but by NSC itself. The mere fact that a director of NSC may have possessed, but did not disclose, special knowledge would not make that director personally liable in the case of NSC's purchase of Murphy's stock.[125]

B. The Murphy Stock Sale Claim Is Barred Because Murphy Did Not Rely

The *three* non-reliance clauses in the Murphy SPA are enforceable, and extinguish

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[123] *See Lazard Debt Recovery GP, LLC v. Weinstock*, 864 A.2d 955, 970-73 (Del. Ch. 2004) (dismissing fraud count for, among other reasons, failure to plead reasonable reliance where the former partners' alleged statements did not provide any reasonable basis for investors to rely and could not form the basis for any reasonable investor to make an investment decision).

[124] *In re Wayport Inc. Litig.*, -- A.3d --, 2013 WL 5345477, at **20-21 (Del. Ch. May 1, 2013).

[125] *See id.* at *22. In addition, to prevail on a breach of fiduciary duty predicated on disclosure, Plaintiffs have to show Snyder engaged in self-dealing. *See Emerald Partners v. Berlin*, 726 A.2d 1215, 1221-22 (Del. 1999) (holding entire fairness review invoked by allegedly inadequate proxy disclosures). Plaintiffs allege that Snyder induced Thomas Murphy to sell shares so that SMC would have enough unissued shares available to cover the exercise of Snyder's options. Kim Am. Compl. ¶ 139. In fact, SMC had 25 million shares of common stock authorized, of which over 12 million remained unissued even taking into account the conversion of all preferred stock and exercise of all outstanding options. JX0255; JX0703. Thus, there is no a self-dealing charge against Snyder and no basis for a breach of the duty of loyalty claim against him (or an aiding and abetting claim against Dwyer).

Murphy's fraud and misrepresentation claims.[126] Delaware law upholds parties' freedom to order their affairs by contract absent an overriding policy interest.[127] To hold otherwise would permit a party to renege on a promise that he did not rely on anything outside his contract and thus diminish the certainty in commercial dealings that contract law is supposed to protect.[128]

Here, Thomas Murphy specifically acknowledged being given access to all information he considered necessary, and disclaimed reliance on anything outside his SPA. The clauses in the Murphy SPA closely resemble the clauses that barred claims of reliance in *Phoenix Equity*, *Homan*, *Progressive*, and *Great Lakes*,[129] and the result should be the same.

Furthermore, no public policy considerations exist to outweigh holding Murphy to his SPA. Relevant factors include whether Thomas Murphy was advised by counsel, negotiated the SPA, and possessed relevant experience or knowledge.[130] Yet even these factors do not trump the enforceability of a contract.[131] And, unlike the preprinted form residential real estate sale contracts that this Court has sometimes declined to enforce,[132] the Murphy SPA was a negotiated

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[126] *Great Lakes Chem. Corp. v. Pharmacia Corp.*, 788 A.2d 544, 556 (Del. Ch. 2001) (dismissing fraud claims on the basis of "explicit contract disclaimers" of reliance); *see Phoenix Equity Group LLC v. BPG Justison P2 LLC*, 2010 WL 1223619, at *2 (Del. Ch. Mar. 25, 2010).

[127] *Libeau v. Fox*, 880 A.2d 1049, 1056 (Del. Ch. 2005), *aff'd in part*, 892 A.2d 1068 (Del. 2006).

[128] *Great Lakes*, 788 A.2d at 556 ("Were this Court to allow [plaintiff] to disregard the clear terms of its disclaimers and assert its claims of fraud, the carefully negotiated and crafted Purchase Agreement between the parties would . . . not be worth the paper it is written on. To allow [plaintiff] to assert, under the rubric of fraud, claims that are explicitly precluded by contract, would defeat the reasonable commercial expectations of the contracting parties and eviscerate the utility of written contractual agreements."); *Progressive Int'l Corp. v. E.I. Du Pont de Nemours & Co.*, 2002 WL 1558382, at *10 (Del. Ch. July 9, 2002) (stating that Delaware law does not approve of plaintiffs claiming "[b]elieve us now when we tell you we made a false promise . . . then").

[129] *See Phoenix Equity*, 2010 WL 1223619, at *2; *Homan v. Turoczy*, 2005 WL 2000756, at *16 (Del. Ch. Aug. 12, 2005); *Progressive*, 2002 WL 1558382, at *5; *Great Lakes*, 788 A.2d at 552.

[130] *Nine Sys. II*, 2013 WL 4013306, at *10 (citing *Great Lakes*, 788 A.2d at 555; *Homan*, 2005 WL 2000756, at *17 & n.53).

[131] *See Progressive*, 2002 WL 1558382, at *7 (stating only that holding parties to their contractual agreements "holds even greater force" when these factors are present).

[132] *Great Lakes*, 788 A.2d at 555 (discussing *Norton v. Poplos*, 443 A.2d 1 (Del. 1982), and its progeny).

document drafted to reflect the parties' shared intention. JX0450 § 14. Moreover, as Thomas Murphy's business experience and careful scrutiny of the SPA makes clear, he is not a vulnerable consumer.[133] In sum, Murphy should not be permitted to circumvent the disclaimers he knowingly agreed to.

C. The Murphy Stock Sale Claim Is Barred by Laches

The law is settled that "the limitations period begins to run when the plaintiff is objectively aware of the facts giving rise to the wrong, *i.e.*, on inquiry notice."[134] Inquiry notice "does not require full knowledge of the material facts; rather, plaintiffs are on inquiry notice when they have sufficient knowledge to raise their suspicions to the point where persons of ordinary intelligence and prudence would commence an investigation that, if pursued would lead to the discovery of the injury."[135]

Thomas Murphy's testimony makes clear that he was on inquiry notice no later than November 2006, when he learned of the Akamai Merger.[136] Indeed, he confessed to considering filing suit "a number of times" in the months that followed.[137] Once Murphy had notice of his claims, he "could not put the proverbial cat back in the bag and plead ignorance."[138] Instead, he

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[133] *Id.* (distinguishing *Poplos* because plaintiff "does not have the same need for protection" as an unsophisticated buyer of real estate).

[134] *In re Dean Witter P'ship Litig.*, 1998 WL 442456, at *6 (Del. Ch. July 17, 1998); *see also In re Tyson Foods, Inc.*, 919 A.2d 563, 585 (Del. Ch. 2007) ("[N]o theory will toll the statute beyond the point where the plaintiff was objectively aware, or should have been aware, of facts giving rise to the wrong.").

[135] *Pomeranz v. Museum Partners, L.P.*, 2005 WL 217039, at *3 (Del. Ch. Jan. 24, 2005).

[136] *See* JX0696 (T. Murphy) at 137 ("Q. When did you find out about the price of the Akamai merger? A. . . . approximate time I guess would be some time, I think, October/November [of 2006]."); *id.* at 131 ("I thread[ed] it together and said . . . these guys had to know something about this . . . prior to the sale" in June 2006"); *id.* at 247 (confirming receipt and review of proxy materials within "three, four days" of November 25, 2006).

[137] *Id.* at 130-32.

[138] *Petroplast Petrofisa Plasticos S.A. v. Ameron Int'l Corp.*, 2012 WL 3090935, at *12 (Del. Ch. July 31, 2012).

was required to act on his rights.[139] He did not do so for approximately six years. Hence, his claims are time-barred as a result.

CONCLUSION

Judgment should be entered for Defendants on all claims.

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[139] *In re USACafes, L.P. Litig.*, 1993 WL 18769, at *6 (Del. Ch. Jan. 21, 1993).

<u>CERTIFICATE OF SERVICE</u>

I hereby certify that, on October 23, 2013, a copy of the Public Version of the Defendants' Opening Pretrial Brief was caused to be served upon the following counsel of record by File & Serve.

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