

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

PONTIAC GENERAL EMPLOYEES RETIREMENT	:	
SYSTEM, On Behalf of Itself and All	:	
Others Similarly Situated and On Behalf	:	
of Nominal Defendant HEALTHWAYS, INC.,	:	
	:	
Plaintiff,	:	
	:	
v.	:	Civil Action
	:	No. 9789-VCL
JOHN W. BALLANTINE, J. CRIS BISGARD,	:	
MARY JANE ENGLAND, BEN R. LEEDLE JR.,	:	
C. WARREN NEEL, WILLIAM D. NOVELLI,	:	
ALISON TAUNTON-RIGBY, DONATO TRAMUTO,	:	
JOHN A. WICKENS, KEVIN WILLS, and	:	
SUNTRUST BANK,	:	
	:	
Defendants,	:	
	:	
and	:	
	:	
HEALTHWAYS, INC.,	:	
	:	
Nominal Defendant.	:	

- - -
Chancery Courtroom No. 12C
New Castle County Courthouse
500 North King Street
Wilmington, Delaware
Tuesday, October 14, 2014
1:00 p.m.
- - -

BEFORE: HON. J. TRAVIS LASTER, Vice Chancellor.

ORAL ARGUMENT ON DEFENDANTS' MOTIONS TO DISMISS
and RULINGS OF THE COURT

CHANCERY COURT REPORTERS
New Castle County Courthouse
500 North King Street - Suite 11400
Wilmington, Delaware 19801
(302) 255-0522

1 APPEARANCES:

2 JOEL FRIEDLANDER, ESQ.
3 CHRISTOPHER M. FOULDS, ESQ.
4 BENJAMIN P. CHAPPLE, ESQ.
5 Friedlander & Gorris, P.A.
6 -and-
7 MARK LEBOVITCH, ESQ.
8 DAVID WALES, ESQ.
9 of the New York Bar
10 Bernstein, Litowitz, Berger & Grossmann LLP
11 for Plaintiff

12 WILLIAM M. LAFFERTY, ESQ.
13 D. MCKINLEY MEASLEY, ESQ.
14 Morris, Nichols, Arsht & Tunnell LLP
15 -and-
16 W. BRANTLEY PHILLIPS, JR., ESQ.
17 JAMIE L. BROWN, ESQ.
18 of the Tennessee Bar
19 Bass Berry & Sims PLC
20 for Defendant Healthways, Inc. and the Individual
21 Defendants

22 S. MICHAEL SIRKIN, ESQ.
23 Seitz, Ross, Aronstam & Moritz LLP
24 -and-
25 GREGORY J. MURPHY, ESQ.
26 MARK A. NEBRIG, ESQ.
27 of the North Carolina Bar
28 Moore & Van Allen PLLC
29 for Defendant SunTrust Bank

30 -- -- --

31
32
33
34
35
36
37
38
39
40
41
42
43
44
45

1 THE COURT: Welcome, everyone.

2 MR. LAFFERTY: Your Honor, unless anyone
3 else wants to make introductions, I thought I would take
4 the floor first.

5 Did you want to introduce your
6 colleagues?

7 MR. FRIEDLANDER: I am happy to,
8 actually.

9 Good afternoon, Your Honor.

10 THE COURT: Hello.

11 MR. FRIEDLANDER: From the Bernstein
12 Litowitz firm, Mark Lebovitch and David Wales.

13 THE COURT: Good to see you all.

14 MR. FRIEDLANDER: And from my firm,
15 Chris Foulds and Ben Chapple.

16 THE COURT: Gentlemen, good to see you.

17 Mr. Sirkin, how are you?

18 MR. SIRKIN: Good. Mike Sirkin from
19 Seitz Ross. With me from Moore & Van Allen is Greg
20 Murphy and Mark Nebrig.

21 THE COURT: Welcome.

22 MR. SIRKIN: I don't know if you have a
23 preference as far as whether you want to hear all of the
24 defendants and then the plaintiffs or whether you want to

1 hear the Healthways motion first and then ours?

2 THE COURT: It does not matter to me.
3 Why don't we go with all the defendants, and then the
4 plaintiffs can do an omnibus response, just as they did
5 an omnibus answering brief.

6 MR. LAFFERTY: Thank you, Your Honor.
7 That was my slight preference. I told Mr. Lebovitch I
8 only wanted him to speak once, if possible. All in good
9 humor, Your Honor.

10 Your Honor, good afternoon. I represent
11 the individual defendants and nominal defendant,
12 Healthways, Inc. And with me at counsel table are my
13 co-counsel, Brant Phillips and Jamie Brown from Bass,
14 Berry & Sims in Nashville, and Mr. Measley from my firm,
15 Your Honor.

16 THE COURT: Good to see all of you.

17 MR. LAFFERTY: And with those, let me
18 jump right in.

19 We are here on defendants' motion, my
20 clients, the individual defendants, and the company's
21 motion to dismiss on ripeness grounds.

22 Your Honor, in the XL Specialty case,
23 the Delaware Supreme Court recently restated the standard
24 for determining whether an actual controversy exists.

1 And of the four prerequisites identified, one is, of
2 course, that the issue involved must be ripe. The Court
3 in XL explained that "Generally, a dispute will be deemed
4 ripe if 'litigation sooner or later appears to be
5 unavoidable and where the material facts are static.'
6 Conversely, a dispute will be deemed not ripe where the
7 claim is based on 'uncertain and contingent events' that
8 may not occur, or where 'future events may obviate the
9 need' for judicial intervention."

10 Further, the Court held that -- this
11 Court has held that ripeness goes to the simple
12 question -- or that ripeness or the simple question of
13 whether or not a suit has been brought at the correct
14 time goes to the very heart of whether the Court here has
15 subject matter jurisdiction. And in determining whether
16 or not a claim is ripe, this Court has said there are a
17 number of factors to consider.

18 One is "... a practical evaluation of
19 the legitimate interest of the plaintiff in a prompt
20 resolution of the question ... and the hardship that
21 further delay may threaten" Second, "... the
22 prospect of future factual development that [may] affect
23 the determination to be made" Third, "... the need
24 to conserve scarce judicial resources" Fourth,

1 "... a due respect for identifiable policies of the law
2 touching upon the subject matter of the dispute." And I
3 want to use that framework for my presentation today.

4 A little bit of background about the
5 lawsuit. Plaintiff challenges a change-in-control
6 provision contained in Healthways' fifth amended and
7 restated revolving credit and term loan agreement, which
8 is dated June 8th, 2012. And for ease of reference, I'm
9 just going to call it "the 2012 loan agreement." In
10 Section 8.1(m) of that loan agreement, it provides that
11 an event of default will exist upon a "Change in
12 Control." And then Change in Control, in turn, is
13 defined at page 6 of the agreement to mean, "... the
14 occurrence of one or more of the following events ...,"
15 the third of which is "... during [a] period of 24
16 consecutive months, a majority of the members of the
17 board of directors ... of the Borrower cease to be
18 composed of individuals who are Continuing Directors."

19 And forgive me, but I am going to try to
20 paraphrase a little bit the "continuing director"
21 provision, and I am going to paraphrase and not try to
22 quote it. But this is at page 8 of the loan agreement as
23 well. Continuing directors means, "... with respect to
24 any period ... individuals (A) who were members of the

1 board ... of the Borrower on the first day of such
2 period, (B) whose election or nomination to that board
3 ... was approved by individuals referred to in clause (A)
4 ... or (C) whose election or nomination to that board ...
5 was approved by individuals referred to in clauses (A)
6 and (B) above constituting at the time of such election
7 or nomination at least a majority of [the] board or
8 equivalent governing body"

9 And then there is an excluding language.
10 And this is the language that I think plaintiffs take
11 most issue with. It says, "... (excluding, in the case
12 of both clauses (B) and (C), any individual whose initial
13 nomination for, or assumption of office as, a member of
14 that board or equivalent governing body occurs as a
15 result of an actual or threatened solicitation of proxies
16 or consents for the election or removal of one or more
17 directors by any person or group other than a
18 solicitation for the election of one or more directors by
19 or on behalf of the board"

20 Now, turning back to the articulation of
21 the ripeness standard in Schick that I mentioned a few
22 minutes ago, I want to address the first prong, which is
23 the legitimate interests of the plaintiff and a prompt
24 resolution and the hardship that further delay may

1 threaten. The 2012 loan agreement was, as I mentioned,
2 entered into in June of 2012, meaning that the challenged
3 provision -- or the provision challenged by the plaintiff
4 in this case -- has been a matter of public record for
5 nearly two years, or was a matter of public record when
6 the plaintiff filed its 220 demand.

7 THE COURT: When do you think the
8 statute of limitations would have started to run on a
9 claim?

10 MR. LAFFERTY: I would think by the time
11 that it was publicly disclosed, Your Honor. And I think
12 that's -- that's about two years. Again, my point is not
13 a statute of limitations question.

14 THE COURT: No; my question was a
15 statute of limitations question.

16 MR. LAFFERTY: Yes. Yes.

17 I guess my point was -- and I will think
18 on that, if you said that -- my point in raising it goes
19 to whether or not there's an emergency now that requires
20 us to do something in advance of facts developing in
21 connection with the next year's annual meeting.

22 THE COURT: No, no. I get it. But it's
23 odd if ripeness effectively works to allow the statute of
24 limitations to run such that there is then no ability to

1 assert the claim.

2 MR. LAFFERTY: I'll think about that. I
3 mean, I'm not sure. If the statute began to run at the
4 time it was disclosed, they could have brought the claim,
5 obviously, when this was publicly available. They
6 certainly would have had the tools to come into court.

7 THE COURT: Right. But then you would
8 say it was even less ripe.

9 MR. LAFFERTY: It would obviously depend
10 on the facts that existed at the time. But, obviously,
11 yeah, I think if there were no -- if the provision wasn't
12 implicated in any way in connection with a meeting, it
13 might be that we would have made that same -- the same
14 argument. Maybe it would have been in spades; I don't
15 know. I'm trying to deal with facts as they exist, I
16 guess, today.

17 THE COURT: In pondering the
18 implications of the ripeness analysis that you advocate,
19 it did strike me that it would be something that one
20 would have to interact with the principle of our law that
21 generally the claim for breach of fiduciary duty arises
22 upon the action taken.

23 So when the board adopted or entered
24 into the credit agreement, the company entered into the

1 credit agreement, that's when the claim would arise.
2 Now, it might have been tolled until public disclosure,
3 but the claim would arise back then. So I don't think
4 that I can -- or I would resist applying ripeness without
5 any consideration of what it meant for things like
6 laches.

7 MR. LAFFERTY: I do -- I understand
8 where you're going with that, Your Honor, and hopefully I
9 will try to address that as we move forward.

10 The plaintiff -- although the plaintiff
11 here asserts that the change-in-control provision has a
12 "... present deterrent effect ... on Healthways'
13 stockholders ..." -- and that's in their answering brief
14 at 15 -- it actually never really explains why or how the
15 stockholders are suffering any present harm from that
16 provision in the current context, untethered to events
17 that are coming up -- that will come up in connection
18 with the 2015 meeting, none of which have, obviously,
19 occurred yet.

20 THE COURT: I think it's a
21 Sword-of-Damocles theory.

22 MR. LAFFERTY: And I think that is
23 right. But we think it's particularly telling here,
24 where stockholders do have the ability to propose a

1 nominee to the board, or candidates to the board, at a
2 minimum, without triggering -- or without threatening a
3 proxy contest, and the board could approve those nominees
4 such that you wouldn't implicate the change-in-control
5 provision. There is -- there is a possibility of doing
6 that, but we think that that, combined with the fact that
7 nothing has happened yet in connection with the 2015
8 meeting, is strong, you know, support for the notion that
9 the claim is not presently ripe.

10 I'm going to turn to the important of
11 the future factual developments that we think, you know,
12 again, counsel in favor of standing down until the facts
13 develop with respect to next year's meeting. And perhaps
14 recognizing the importance to its claim of the
15 application of the change-in-control provision in the
16 context of the company's annual meeting, plaintiff filed
17 the complaint in this case about a week before the
18 company's 2014 annual meeting. And a significant portion
19 of the complaint focuses on facts that existed at that
20 time regarding the actions of North Tide Capital in
21 advance of the 2014 meeting. The North Tide allegations
22 highlight the importance of allowing the factual record
23 to develop in this case.

24 At the end of 2013, North Tide issued a

1 series of public letters criticizing the board and
2 indicating its interest to pursue a proxy contest. In
3 mid-January, North Tide announced that it would consider
4 nominating a slate of director candidates for election at
5 the June meeting. And on May 13th, 2014, North Tide
6 filed a definitive proxy statement announcing a slate of
7 four director candidates.

8 Although not, you know, seriously
9 addressed in the complaint, on June 2nd, 2014, the
10 company and North Tide executed a nomination and
11 standstill agreement -- and that was attached to our
12 brief, our opening brief -- wherein the company agreed to
13 nominate three director candidates proposed by North Tide
14 for election to directors at the June meeting. In
15 exchange, North Tide agreed not to seek, advise,
16 encourage, or influence the voting of other stockholders,
17 and they agreed not to acquire more than a 15 percent
18 stake and said that it would not assist in any tender
19 offer, exchange offer, or other extraordinary transaction
20 involving the company.

21 And that standstill agreement is going
22 to remain in effect until 10 days prior to the 2015
23 annual meeting deadline for nominating directors and will
24 be extended for an additional 12 months, if the company

1 renominates the North Tide directors in 2015, with North
2 Tide's consent.

3 Despite the allegations in the complaint
4 to the contrary, the board's handling of the competing
5 slate proposed by North Tide did not result in lost
6 opportunities to press for changes to Healthways' board.
7 And although I recognize that the 2014 meeting is on
8 different footing than the 2015 meeting, the board never
9 even made a reference to the change-in-control provision
10 during the process with North Tide or attempted to invoke
11 it in any way in that process. And as plaintiff
12 concedes, the election of directors at the 2015 meeting,
13 some eight months from now, is the first time that the
14 change-in-control provision could possibly come into
15 play. Whether that will occur, you know, however, is
16 impossible to predict with any accuracy and depends
17 entirely on the composition of the possible nominees.

18 In our opening brief, we identified a
19 couple of possible scenarios for the election of
20 directors at the 2015 meeting. And those scenarios, we
21 believe, identify a long series of uncertain and
22 contingent events that have to occur before plaintiff's
23 claim will really ripen.

24 The first scenario would be if you

1 assume that the North Tide directors continue on the
2 board. Under that scenario, the change-in-control
3 provision would only come into play if all of the
4 following events occurred: that the North Tide directors
5 were renominated and a stockholder other than North
6 Tide -- which I will call a nominating stockholder --
7 proposes at least three candidates for the board's
8 consideration. This is an 11-person board, so you need 6
9 to get a majority. Third, the board would have to reject
10 at least three of the nominating stockholder's nominees.
11 Fourth, the nominating stockholder would have to threaten
12 and/or launch an actual proxy contest seeking election of
13 three candidates. The North Tide directors would have to
14 then be reelected. The nominating stockholder would have
15 to win the proxy contest and obtain three seats. And the
16 board and the lending syndicate would have to reach an
17 impasse regarding any waiver of the loan agreement's
18 change-in-control provisions, and the lending syndicate
19 would have to elect, in their discretion, to invoke the
20 default provision in Section 8.1 of the loan agreement.

21 The other scenario would be what we call
22 Scenario 2, which is where the North Tide directors don't
23 continue on the board. In that circumstance, the
24 change-in-control provision would only come into play if

1 the following occurred: that North Tide, or North Tide
2 combined with some other stockholders, propose at least
3 six nominees to the board. The board would have to
4 reject at least six of those nominees. Third would be
5 North Tide, together with other stockholders, would have
6 to threaten and launch a proxy contest for at least six
7 of the eight open seats. Fifth, the North Tide
8 stockholder-proposed dissident slate would have to win,
9 obtaining six out of eight seats on the board. Sixth,
10 the board and its syndicate of lenders would again have
11 to reach an impasse regarding a waiver of the loan
12 agreement's change-in-control provision. And seventh,
13 the lending syndicate would have to elect, in their
14 discretion, to invoke Section 8.1 to declare an event of
15 default.

16 We think these events identified in the
17 scenarios highlight that there are sufficient moving
18 parts to warrant dismissal of the complaint on ripeness
19 grounds. Even the plaintiff's complaint notes various
20 what-ifs that may occur in the future that bear directly
21 on the claims asserted.

22 THE COURT: When you cite these
23 eventualities, you are dealing with them in the context
24 of what would be necessary for the put actually to happen

1 and the debt to come due. Right?

2 MR. LAFFERTY: That's true. That's
3 true.

4 THE COURT: I mean, it doesn't address
5 the bargaining in the shadow of the put concept, does it?

6 MR. LAFFERTY: It does not. It does not
7 directly address that. I don't think all of those moving
8 pieces address that point. But I think they, you know --
9 I guess what you're saying is there's a distinction
10 between whether there is sort of this -- this
11 Sword-of-Damocles point that -- you are saying -- is that
12 somehow is it dampening the ability to actually come
13 forward and nominate somebody.

14 THE COURT: Like, if somebody's got a
15 piece of artillery sitting on a hill overlooking my town,
16 it is definitely true that before a shell can land on my
17 town, people have to go up there, people have to load the
18 weapon, you know, people have to go through the firing
19 sequence, somebody actually has to pull the cord, the
20 shell actually has to fire, the shell has to arc through
21 the air, it has to land, and it actually has to go off.
22 But that's a different thing from how I change my
23 behavior driven by the fact that somebody has a piece of
24 artillery on a hill over my town.

1 So what your list of items describes is
2 what is necessary for the shell, in fact, to go off. But
3 what it doesn't address is, again, the Sword-of-Damocles
4 problem.

5 MR. LAFFERTY: Well, I do think there
6 is -- there is a response to that, which is stockholders
7 do have a way to avoid the Sword of Damocles, which is
8 they have the right to propose to the board a slate of
9 nominees. If they haven't threatened a proxy contest,
10 the change-in-control provision is not implicated. They
11 have the right to nominate directors under the bylaws,
12 and they can do that.

13 Now, that -- that may not be the way
14 most -- I mean, sophisticated investors know how to weave
15 their way around corporate documents -- and I think we
16 presume that in this Court -- you know, and I think they
17 can tailor their behavior that way. And if it turns out
18 that the board accepts them and puts them on the
19 management slate, then you don't have an issue. But,
20 again, that --

21 THE COURT: Then the solution to the
22 Sword of Damocles is the board saying, "Yeah, we have
23 effectively blocked your other route. You've got to come
24 through us"?

1 MR. LAFFERTY: No, I don't -- well, I
2 don't think that's true, because they could still then --
3 if the board says no to the nominees, they have their
4 avenue available to them to then launch a proxy contest
5 and solicit for their own slate. That's not a foreclosed
6 opportunity at all.

7 THE COURT: But it's an opportunity in
8 the shadow of the put.

9 MR. LAFFERTY: Certainly, the put is
10 there. There's no question about that. But I do think
11 stockholders have the ability to -- and the board would
12 have the ability to -- sort of accept those nominees at
13 some point. Again, if you walk your way through the
14 document. And I think it's clearly -- clearly the way
15 the language operates.

16 Your Honor, let me talk just for a few
17 minutes about Amylin and Sandridge. You know, the
18 plaintiffs rely on those two cases in seeking, among
19 other things, a declaratory judgment that the director
20 defendants breached their fiduciary duties by approving
21 the entry into the 2012 loan agreement containing the
22 change-in-control provision. And in relying on those
23 cases, the plaintiff asked this Court to go way beyond
24 the rulings in those cases, I think, and establish a new

1 rule that says that the mere entry into the agreement, an
2 agreement with this type of a provision, is a per se
3 breach of duty.

4 And as Your Honor is aware, this Court
5 has previously addressed challenges to provisions like
6 this in Amylin and Sandridge but, to my knowledge, has
7 never addressed the challenge to one of these provisions
8 outside of the context of an active proxy contest. And
9 that makes this case unique and, I think, qualitatively
10 different from the far more extreme facts in those cases.

11 I want to touch on a few of the facts in
12 Amylin and Sandridge, as I think the Court's rulings in
13 those cases actually support dismissal on ripeness
14 grounds here. In Amylin, the board affirmatively invoked
15 the change-in-control provision in the midst of a proxy
16 contest for the express purpose of thwarting efforts to
17 effectuate a change in leadership. There, two activist
18 stockholders, Eastbourne and Carl Icahn, separately sent
19 notices to the Amylin board of their intent to nominate
20 five directors each due to concern over continuing -- the
21 continuing director provision in the indenture.
22 Eastbourne asked the board to take action to prevent
23 adverse consequences if the provision was triggered,
24 including to approve a slate that included a significant

1 number of Eastbourne and Icahn's nominees and to work
2 with the lender, in that case, to get a waiver.

3 In response, what did the Amylin board
4 do? Well, it issued -- Amylin issued a press statement,
5 a public statement that was specifically intended to
6 highlight the adverse financial impact that would result
7 if stockholders acted in a way that would implicate the
8 change-in-control provision. I guess I won't read it to
9 Your Honor, but I think it suffices to say it's quoted at
10 page 310 and Note 7 at 983 A.2d in the opinion. But it
11 was dead-on designed to take the position that, you know,
12 telling -- warning stockholders that if you support the
13 insurgent slate, you know, there may be all these adverse
14 consequences that come from voting for them, because the
15 change in control could be triggered and we may owe as
16 much -- almost a billion dollars back to the bank.

17 And Eastbourne in that case filed suit
18 only after it became clear that the Amylin board was
19 trying to invoke the change-in-control provision to block
20 its efforts to elect directors. And even in Amylin, on
21 what we think are much different facts than here, the
22 Court did not issue the requested relief after they had a
23 trial.

24 Instead, the Court found that because

1 the dissident stockholders had reduced the number of
2 candidates below the threshold for triggering the
3 change-in-control provision in the indenture, the issue
4 about whether the insurgent nominees were continuing
5 directors wasn't ripe for decision. And the Court stated
6 that a determination as to whether the dissident slate
7 would constitute continuing directors, if elected, might
8 well have a significant effect on the next year's annual
9 meeting, but it had no bearing on the election at hand.
10 And the Court noted that because of the potential for
11 future factual developments -- and this is a quote --
12 "... the issue of Continuing Directors may become
13 irrelevant long before next year's annual ... meeting."

14 The Court went on to tell the parties to
15 return if and when a judicial determination was
16 necessary, saying that, "... the plaintiff or Amylin is
17 free after the 2009 meeting to replead its case that the
18 stockholder nominees, if they are in fact elected, are
19 Continuing Directors by virtue of Amylin's 'approval,'
20 whatever form that approval may ultimately take. [And]
21 at that point, the ... facts will be frozen." And
22 because we believe here all of the relevant facts are
23 still in flux, the reasoning from Amylin applies with
24 equal force.

1 In Sandridge, again --

2 THE COURT: At what point do the facts
3 become frozen?

4 MR. LAFFERTY: Your Honor, I think it
5 would -- again, that's a difficult question to answer, I
6 think, you know, specifically. But I think once we get
7 through the period of figuring out whether or not there
8 are going to be -- you know, there's anybody who is going
9 to nominate directors.

10 THE COURT: Why isn't it that the facts
11 would become -- it sounds to me like the facts would
12 become frozen after it's triggered. I mean, until then,
13 there's always a step in the list of events that you read
14 me off that could negate the potential triggering of the
15 put. So if frozen facts is the standard, aren't we only
16 going to litigate these things in hindsight?

17 MR. LAFFERTY: I think, obviously, you
18 have to take each one of these as you go. I don't think
19 I was suggesting that this case ought to await -- you
20 know, necessarily await -- I think that is certainly a
21 possibility, but that wasn't really what I had in mind,
22 which is -- my view was that as things developed in
23 connection with the annual meeting, we're going to see
24 whether or not we even have a contested election at all.

1 That's going to be one step. The other step would be to
2 see whether or not by that point we have, you know,
3 potentially a waiver that is granted by the bank.

4 You know, again, these things will
5 develop as time -- as time goes on. You know, obviously,
6 in Sandridge and in Amylin, there were active proxy
7 contests where the incumbents tried to use the existence
8 of the change-in-control provision to their advantage in
9 trying to gain an advantage in the election contest.
10 That obviously, you know, to me, that ripened up the
11 issues in that case because of the way the board was
12 attempting to use it in the disclosures in connection
13 with the vote. And certainly that is another way that it
14 certainly would ripen up. But by the time, you know --
15 you will know by the time the nomination process comes
16 whether or not we have any case whatsoever, I think.

17 Your Honor, I won't belabor the
18 Sandridge point. I just think that, again, it's -- it's
19 the Court there made clear that it was what it viewed as
20 pretty egregious conduct on behalf of the board that
21 resulted in the Court granting some injunctive relief
22 there. We don't have those facts here. We don't even
23 know whether we have an election contest yet.

24 Your Honor, again, I'm prepared to stand

1 on my papers on the other issues that they raised. The
2 plaintiffs, you know, rather than going directly at it
3 and, I think, explaining what I think Your Honor has
4 called the Sword-of-Damocles problem -- and I assume
5 Mr. Lebovitch will talk about that more -- the plaintiffs
6 focused on the poison pill cases, mainly. You know,
7 we've explained in our briefs, I think, why those cases
8 are different than the context here, and I'm prepared to
9 stand on my papers on that.

10 You know, again, Your Honor, we would
11 submit that the Court ought to stand down at present and
12 grant the motion to dismiss. Obviously, it's without
13 prejudice to the plaintiff coming back, if and when we
14 have a real dispute here.

15 THE COURT: Thank you, Mr. Lafferty.

16 MR. LAFFERTY: Thank you.

17 MR. MURPHY: May it please the Court.

18 Your Honor, my name is Greg Murphy, and I am with the law
19 firm of Moore & Van Allen in Charlotte, North Carolina.
20 And I represent SunTrust, who was the administrative
21 agent for the bank group that extended credit in the form
22 of a syndicated credit facility in the amount of
23 \$400 million to Healthways.

24 There are two ways that Your Honor could

1 grant our motion to dismiss. The first would be if you
2 granted their motion to dismiss. I will not belabor any
3 of those points, because they've been amply covered here.

4 But I do want to focus on an argument
5 that is really unique to SunTrust. As Your Honor may be
6 aware from the complaint, this credit agreement was
7 actually in place for some period of time. I guess that
8 should be self-evident from the fact that we are now
9 dealing with the fifth amendment to the credit facility,
10 which was entered into in June of 2012.

11 It's important to recognize that from
12 the very beginning of this credit facility, there was
13 always a change-in-control provision contained within the
14 credit agreement. However, that change-in-control
15 provision changed as part of the negotiations between the
16 borrower and the lenders in this fifth amendment.
17 SunTrust and the bank group deems these change-in-control
18 provisions as market. And, in fact, as Your Honor I'm
19 sure is aware, change-in-control provisions appear in
20 every bond indenture, every syndicated credit facility,
21 and so the ramifications of the claim that has been
22 asserted against SunTrust has some fairly far-reaching
23 implications to the lending community.

24 This provision basically is designed to

1 protect lenders from a wholesale change in the
2 composition of the board over a very short period of
3 time. So it's not designed to get to a change in the
4 composition of a board over a three- or four- or
5 five-year period, but it's really designed to sort of
6 give the creditors an opportunity to evaluate the credit
7 situation and the risk situation if either within a
8 one-year period or a two-year period there suddenly is a
9 change in the composition of the board so that the
10 majority is all of a sudden different.

11 THE COURT: Why is that a form of
12 protection that can't be better addressed through actual
13 financial protections, like debt coverage covenants, or
14 other things that would actually go to the
15 creditworthiness of the borrower?

16 MR. MURPHY: Obviously, Your Honor,
17 those covenants existed in this credit agreement and in
18 all other credit agreements. But I think it goes to the
19 fundamental belief that lenders like to know who their
20 borrowers are.

21 THE COURT: That makes sense in a
22 private company or a company with a dominant stockholder,
23 where you can actually know your borrower. But why does
24 that argument -- which I understand is often repeated --

1 translate to a public company with ever-changing float,
2 annual elections, CEO turnover that we're often told
3 average three to five years? The average CEO tenure now
4 is somewhere between three to five years. Explain to me
5 how that know-your-borrower argument translates into that
6 context.

7 MR. MURPHY: Sure. I think it just
8 recognizes a potential acceleration of that concern. And
9 if you have a fundamental change, where a majority of
10 your board turns over, it just gives the borrower the
11 ability to completely clean house, change management,
12 change business direction, which obviously may show up in
13 the form of other covenants, or may not. And I think
14 it's really important to recognize here that these --
15 that this particular change-in-control provision gives
16 the members of the bank group, by a majority vote, the
17 ability, but not the necessity, to invoke in event of
18 default under the credit agreement.

19 THE COURT: That's the logical next
20 question. So to the extent these provisions are market
21 and are providing meaningful protection to creditors, how
22 often are they invoked?

23 MR. MURPHY: Truthfully, Your Honor, I
24 would say infrequently.

1 THE COURT: That's what I think, too.

2 MR. MURPHY: And I think the reason they
3 are invoked infrequently is because in these situations
4 where there is an actual change-in-control provision that
5 is implicated, the borrower and the lenders have at their
6 disposal a variety of tools to address the situation, one
7 of which, of course, is that the lenders could vote, by a
8 majority of the participating lenders, to simply not
9 invoke the event of default.

10 The second, more likely scenario, as
11 Your Honor I'm sure is aware, is that it would lead to a
12 negotiation with the borrower, where we could get the
13 issue on the table, begin to discuss what the lender's
14 concerns are with the fundamental change and turnover of
15 the board, and that could result in either a waiver or an
16 amendment of the provision. That could also involve a
17 renegotiation of the financial terms in the credit
18 agreement.

19 And then, of course, as a point of last
20 resort, if the lender became totally uncomfortable, the
21 borrower would have at its disposal the ability to go out
22 and refinance the credit or the bank could declare a
23 default.

24 So all of those, I think, provide

1 lenders the flexibility, which I think was actually
2 recognized in both Amylin and Sandridge, that there are
3 legitimate business reasons why creditors like to have
4 these provisions.

5 THE COURT: I actually didn't see any --
6 it said that there could be, and it said that it's
7 understandable why creditors like those provisions, but I
8 didn't actually see the reasons, which is why I asked you
9 for the reasons.

10 MR. MURPHY: Sure, Your Honor. I agree
11 with that. It said there could be legitimate reasons.

12 THE COURT: That's different than
13 actually citing reasons.

14 MR. MURPHY: Yes, I agree, Your Honor.

15 So fundamentally, though, I think what
16 makes this case unique and very different from anything
17 that's ever come before it is we are not here at the
18 table because we are simply a counterparty to a
19 transaction in which the board is being accused of a
20 breach of fiduciary duty. We are here and named as a
21 defendant as an aider and abetter of that fiduciary duty.
22 And, Your Honor, that is really the argument that I would
23 like to spend most of my time talking about, because I
24 think it fundamentally goes to the heart of whether or

1 not our motion to dismiss should be granted.

2 Neither Amylin nor Sandridge involve the
3 situation involving a syndicated credit facility and the
4 lender being named as a defendant. Amylin, I believe
5 Bank of America was brought in as a nominal defendant for
6 purposes of ensuring that the Court had the ability to
7 address injunctive relief, and eventually that issue was
8 mooted. Never before in this court, or in any court that
9 we could find in any jurisdiction, has a lender been sued
10 as an aider and abetter of a breach of fiduciary duty in
11 this context.

12 And it's troubling on a number of
13 levels, but it's mainly troubling when you turn, as you
14 must, to the well-pleaded allegations in the complaint
15 and you really look at any nonconclusory facts and see
16 whether or not the Court could sustain this cause of
17 action. And when you really look carefully at the
18 complaint in this action, there are no facts that would
19 give rise to a predicate for an aiding and abetting
20 claim.

21 All it says in the complaint is that
22 SunTrust and the company entered into a credit agreement,
23 SunTrust and the company amended that credit agreement,
24 the fifth amendment contained a change-in-control

1 provision. And the only allegation in the complaint that
2 goes to conduct in any way, shape, or form is paragraph
3 57 of the complaint. Paragraph 57 of the complaint says,
4 and I quote, "The Lenders aided and abetted the Board's
5 breach by including a contractual provision that they
6 knew or should have known was invalid."

7 It goes on to say, "After Amylin, the
8 lender community was put on notice that entering into
9 Dead Hand Proxy Puts would likely violate directors'
10 fiduciary duties unless the borrower was aware of and
11 extracted significant concessions in exchange for
12 agreeing to such provisions."

13 It finally goes on to say, "The Lenders
14 nonetheless allowed the Loan Agreement, which included no
15 such concessions, to include the Dead Hand Proxy Put.
16 Thus, the Lenders have no justifiable expectation that
17 the Dead Hand Proxy Put is enforceable."

18 So, in essence, Your Honor, the sole
19 allegation against our client, SunTrust, is that they
20 allowed a change-in-control provision to be in their
21 credit agreement. And it seems to shift to the lenders
22 the responsibility to ensure that the board members of
23 the borrower are adhering to their fiduciary duties.

24 The problem with that, Your Honor, is

1 many, but one of the problems is that the lenders, of
2 course, have their own shareholders and they have their
3 own duties, including fiduciary duties. And in an
4 arm's-length transaction, such as a credit agreement, it
5 is the bank's duty to try to negotiate the most favorable
6 terms it can in connection with this syndicated credit
7 facility. They owe that duty to the other members of the
8 bank group, and they certainly owe that duty to their
9 shareholders.

10 Independent of how the Court rules on
11 the other motions, the aiding and abetting claim should
12 be dismissed because there are no pleaded facts which
13 support knowing participation, which is required in an
14 aiding and abetting claim in Delaware. In fact, there
15 are also no facts in the complaint from which the Court
16 could conclude that this was anything other than an
17 arm's-length negotiation.

18 Knowing participation requires that they
19 either plead facts that show that SunTrust sought to
20 induce the breach by the members of the board, or they
21 must allege facts from which knowing participation can be
22 inferred. And --

23 THE COURT: That's consistent with being
24 able to plead knowledge generally under Rule 8.

1 MR. MURPHY: I think the standard is
2 heightened in the context that the cases that I've read
3 in Delaware basically say for you to be able to infer
4 knowing participation, you have to be able to show
5 conduct which is inherently harmful. Bad acts, if you
6 will.

7 And here, Your Honor, there is
8 absolutely no suggestion that SunTrust sought to induce a
9 breach by the board. In fact, there is not a single
10 allegation, fact, statement, or otherwise, to suggest
11 that anyone from any member of the bank group, including
12 SunTrust, so much as communicated with anyone from the
13 board of directors or that they even knew anyone on the
14 board of directors. There's no allegation, as there is
15 in many of these aiding and abetting cases, that there
16 was some attempt at improper influence, such as a merger
17 transaction where somebody is promised a lucrative deal
18 in the post-merger environment. There is no evidence
19 that there was a conflict of interest here. There's no
20 evidence --

21 THE COURT: So those last two things I'm
22 stumbling over. Because the idea in basic aiding and
23 abetting law in terms of a third party is you are allowed
24 to negotiate as hard as you want, but you can't take

1 advantage and put your counterparty's fiduciary in a
2 conflict situation.

3 Well, this provision on its face puts
4 them in a conflict situation, because the bank is asking
5 for something that is entrenching. So all of a sudden
6 they have -- again, we can debate whether the bank is
7 asking for it. But the provision itself is entrenching.
8 And so you as a fiduciary on the other side of the
9 negotiation have to say, "Hmm. Okay. Well, this is good
10 for me. So should I take the provision that's good for
11 me, or should I push back on it and get something better
12 in another context, like a lower interest rate or
13 something like that?"

14 It's very different from a purely
15 economic provision that doesn't create that conflict.
16 You just said that this provision doesn't create a
17 conflict. So I'm asking you: In light of the conflict
18 that I've just identified, why isn't there a conflict?

19 MR. MURPHY: I guess, Your Honor, the
20 way I think of it is, I don't think of it as creating any
21 greater conflict than any change-in-control provision,
22 including the changes-in-control provision that existed
23 in this credit agreement since its inception and its
24 first original iteration. And yet no one seemed troubled

1 by that. You know, every single bond indenture contains
2 a change-in-control provision, which at least
3 theoretically has an entrenching effect.

4 THE COURT: That's because they are
5 great for the two sides of the negotiation who are at the
6 table. So, I mean, that's what we know from the history
7 of the '80s. These things come out of the '80s. And
8 both sides of the negotiation at the table, both the
9 banker and -- both the lender and the fiduciaries, had
10 benefit from the entrenching effect. It's a win-win for
11 them. The person for whom it's not a win is the person
12 not at the table, who then has to actually expend
13 resources to monitor, to bring suit, etc.

14 So, I mean, it's not surprising that
15 these things would proliferate, because for the people in
16 the room, it's great.

17 MR. MURPHY: I think the problem that
18 I'm struggling with, Your Honor, is that our clients had
19 fiduciary duties to their own shareholders, and those
20 duties included to negotiate the best terms they could.

21 And I can envision a scenario where this
22 would be highly problematic. And I will give you a
23 couple of examples. If the plaintiff had pled in his
24 complaint that this situation arose by Healthways

1 inserting into a draft of SunTrust's credit agreement a
2 provision that was favorable to the creditors and
3 disfavorable to the shareholders, that would present,
4 perhaps, a concern. I think, similarly, if a scenario
5 were to emerge where the members of the board of
6 directors called the folks from SunTrust and said --
7 nod-nod, wink-wink -- "We want you to put a really
8 onerous change-in-control provision in this agreement."
9 But we have nothing of the sort here.

10 THE COURT: Isn't that what discovery is
11 for?

12 MR. MURPHY: Your Honor, they issued a
13 220 demand in this case. They were able to gather
14 information from our borrower, and they were able to
15 allege upon information and belief anything that they
16 thought they had a basis to allege when they filed this
17 complaint. But they didn't do that. In fact, all they
18 said was we allowed a provision that was favorable to us
19 to go into a negotiated credit agreement with our
20 borrower. Therefore --

21 THE COURT: They said that you allowed a
22 provision to go into the agreement that is not only
23 favorable to you, but also creates a conflict for
24 fiduciaries on the other side. That's the distinction.

1 If all they said was you put in a provision that's
2 favorable to you, that's like saying you put in a higher
3 interest rate. There is a distinction between provisions
4 that don't have conflicting effect and provisions that
5 have conflicting effect.

6 MR. MURPHY: I guess, Your Honor, all
7 provisions that, I think, are pro lender and not pro
8 borrower, to a certain degree, test the members of the
9 board's fiduciary obligations to protect its
10 shareholders. But to a certain degree, what we're doing
11 here, Your Honor --

12 THE COURT: Test the fiduciary's desire
13 to protect their incumbency; that's the conflict. The
14 conflict that's arising here is not between the interests
15 of the lender and the interests of the borrower. The
16 conflict is on the borrower's side and is the conflict
17 between the interests of the entity and the personal
18 interests of the directors in protecting their
19 incumbency.

20 That's -- and so the distinction is
21 between a provision that solely gives rise to the
22 borrower-lender opposition, which is fair game for
23 negotiation. That's perfectly fine. You guys can demand
24 20 percent. You guys can demand, you know, six times

1 coverage. The issue arises when the provision creates
2 the conflict within the borrower's side such that it
3 creates a conflict for the fiduciary with whom you are
4 negotiating against.

5 MR. MURPHY: But to a certain point,
6 Your Honor. At what point do I -- does my client cross
7 the line and have to worry more about protecting the
8 fiduciary obligations of its borrower than itself?

9 THE COURT: At the point of knowing
10 participation.

11 MR. MURPHY: I agree with that. And so
12 there has to be some facts that suggest that either there
13 was some improper influence, there was some improper
14 communication. The complaint is utterly void of any
15 contact whatsoever between the board members and the
16 lenders, which is not uncommon in this situation.

17 I do want to address the fact that this
18 Court -- and as a course -- sort of applied special rules
19 and special status and privilege to agreements that have
20 been reached in an arm's-length negotiation. And there
21 is nothing in this complaint --

22 THE COURT: There's a distinction
23 between the agreement as a whole and aspects of the
24 agreement. So take a standard merger agreement, right.

1 We treat the agreement as a whole differently than we do
2 the defensive provisions of that agreement.

3 So we treat the -- by analogy, we treat
4 the lending agreement differently, where it's exactly the
5 borrower-lender negotiation you are talking about versus
6 provisions within it that are defensive in nature. It's
7 a one-for-one analogy.

8 MR. MURPHY: I understand that. I also
9 think that it's telling, though, that here there is no
10 allegation to suggest anything other than this being
11 purely a business relationship. In other words, it's not
12 like a lot of merger cases, where the acquiring party is
13 ultimately going to have an ongoing and continuous --
14 continuing relationship with members of the
15 board/management, and so there tends to be a possibility
16 for mischief. There really is no --

17 THE COURT: How long did you expect the
18 debt to sit out there?

19 MR. MURPHY: It has a maturity date of
20 2017, I believe.

21 THE COURT: That's ongoing. Right?

22 MR. MURPHY: And it's been refinanced
23 now, I think, seven times. There have been seven
24 amendments. I shouldn't say refinanced, but there have

1 been seven amendments to this agreement.

2 THE COURT: That is an ongoing
3 relationship, isn't it?

4 MR. MURPHY: It is an ongoing
5 relationship, Your Honor, yes. But it is -- it gets back
6 to this, I guess. There's -- there is no rational and
7 articulated basis in the complaint, or that I can think
8 of, why the lenders would be trying to create a situation
9 that gives rise to a breach of fiduciary duty here.
10 They're in the business of loaning money and getting
11 paid, plainly and simply. And this is not one of those
12 situations where there's some longstanding entrenched
13 personal relationship between directors and a third party
14 entering into a contract.

15 So I'll try to wrap up, Your Honor. I
16 do think that the net effect of the claim for aiding and
17 abetting is to essentially create a per se violation that
18 any time you have a change-in-control provision in a
19 credit agreement, that it is not only per se illegal, but
20 that the party that put it in the credit agreement, even
21 if it was in its own best interest, has committed aiding
22 and abetting.

23 THE COURT: Why do you think it's per se
24 illegal?

1 MR. MURPHY: Because I think that's --
2 that has to be the position of the plaintiffs in this
3 case. In other words --

4 THE COURT: We are at the pleadings
5 stage. Right?

6 MR. MURPHY: Yes.

7 THE COURT: So why isn't it their
8 position that they've given notice of a claim, and then
9 they actually have to eventually prove a claim at trial
10 that, based on the facts of what actually went down here,
11 there was a breach? Why do you jump immediately to per
12 se?

13 MR. MURPHY: Simply because there have
14 been no allegations of any of the other conduct that
15 would suggest that only in certain circumstances would
16 you have an aiding and abetting claim for breach of
17 fiduciary duty. The only predicate fact upon which we
18 are here, Your Honor, is that we put a change-in-control
19 provision in our credit agreement. I mean, there hasn't
20 been any contention that we engaged in any mischief with
21 the board, that we had any improper motives, or anything
22 else.

23 THE COURT: So your view of the world is
24 that sufficient to state a claim on which relief can be

1 granted, under Rule 12(b)(6), notice pleading standard,
2 actually means plead facts sufficient to require a
3 judgment in your favor at trial. And that whatever comes
4 out in discovery, that's really superfluous because it's
5 got to be there at the outset?

6 MR. MURPHY: No, Your Honor. I mean, I
7 think my position would be that you do need to plead
8 facts that give rise to a reasonably conceivable, you
9 know, set of circumstances that could give rise to
10 liability.

11 THE COURT: That's what I think. And
12 I'm a guy who's been reversed simply for using the word
13 "plausible." I am very careful never to use that word
14 and to only worry about what I can reasonably conceive.

15 MR. MURPHY: Yeah, and I -- and, again,
16 I could reasonably conceive it if they had alleged things
17 such as, "The bank officer had an improper relationship
18 with board member so and so," or "We know that the board
19 member, because of their response to our 220 demand,
20 actually insisted that this provision be put in a credit
21 agreement." But they've not alleged anything of the
22 sort. All they've alleged here is that it's in the
23 agreement.

24 The last thing I do want to touch on --

1 and then I will be happy to answer any of your
2 questions -- is I think it's important to draw the
3 distinction in Amylin and Sandridge in-between a bond
4 indenture and a credit agreement.

5 In the context of a bond indenture, as
6 we all know, you know, the Armageddon scenario that was
7 painted in both of those cases were real because of the
8 possibility that you can't just pick up the phone, you
9 can't call somebody at SunTrust, and you can't say,
10 "We've got an issue under this covenant. Let's talk and
11 let's see if we can amend the credit agreement." And I
12 think both of those cases acknowledge those distinctions.

13 This is a credit agreement, and so,
14 therefore, this is the first time that I'm aware of that
15 a change-in-control provision in a syndicated loan has
16 been the subject of an aiding and abetting claim. And I
17 do think that that -- that is a distinction of substance,
18 particularly given all the options that exist to both the
19 borrower and the lender.

20 And so unless you have any other
21 questions, Your Honor, I appreciate the time.

22 THE COURT: Thank you.

23 MR. LEBOVITCH: Good afternoon, Your
24 Honor. Thank you for making the time to hear us today.

1 You know, listening to the defendants'
2 arguments, it reminds me of that timeless legal maxim:
3 "If you don't have the facts, argue the law. If you
4 don't have the law, say the word 'hypothetical' and
5 'speculative' a lot and hope the Court gets confused."

6 I hope the Court doesn't get confused
7 here. It's a 12(b)(6) motion. We've plainly pleaded
8 breaches of fiduciary duty, and that's not even really at
9 issue on this motion.

10 But I think what Your Honor just heard
11 is the core defense from all the defendants is
12 essentially that this Court does not have the power to
13 address a dead hand proxy put until a proxy fight is
14 pending, and perhaps even after the proxy fight has taken
15 place and it's been triggered and there's a default.
16 That message tells shareholders everywhere that, in
17 effect, they'll never have the ability to get a judicial
18 ruling about a dead hand proxy put.

19 And they can't reconcile their arguments
20 with the legal analysis that their own lawyers published
21 to their clients right after the Amylin opinion. We
22 quote it. But they say, poison puts "... are no longer a
23 dirty little secret ...," and the Amylin case made clear
24 that boards have a continuing duty to protect their

1 stockholders' interests, notwithstanding a need to incur
2 indebtedness. And the author, Healthways' lawyers
3 acknowledge that after Amylin, "... [c]ourts will likely
4 apply greater hindsight scrutiny" So speaking of
5 all proxy puts, but clearly to dead hand proxy puts.

6 But before I get to ripeness, I want to
7 fill out the facts a little bit. Mr. Lafferty touched on
8 it. Before 2012, as you heard, Healthways' debt did not
9 have a dead hand provision. We have alleged specific
10 facts; nothing per se here. We have alleged specific
11 facts. We have said that on May 31st, 2012, Healthways'
12 shareholders, over the board's objection, voted to
13 destagger the board. Nine days later, Healthways adopts
14 the dead hand provision. The company's outstanding notes
15 have cross-defaults, which is not unusual. What's the
16 effect of the dead hand, okay.

17 THE COURT: Let me interrupt you for a
18 second.

19 Your friends say that Healthways' board
20 actually ended up recommending in favor of the destagger.

21 MR. LEBOVITCH: Well, they opposed it,
22 and they opposed it -- I think our complaint says that
23 they opposed it to the end. But, I mean, sometimes you
24 will oppose it for a couple of years and then change your

1 view. I actually -- my memory of the complaint is that
2 they -- what we allege is that they opposed it the whole
3 way through.

4 But let's think about the effect. It's
5 a freebie to change your view on the staggered board.
6 Because it's a good question, Your Honor. Let's assume
7 they change their view. The dead hand proxy put makes it
8 a freebie. This is the magic trick of a dead hand put.
9 Before the dead hand put, all you had was a staggered
10 board. Under Delaware law, it takes two elections to
11 change a majority of any board. They get rid of the
12 staggered board -- let's give them credit. They even
13 say, "Oh, you can get rid of the staggered board. That's
14 okay." You know why? That's because with the 24-month
15 provision of the dead hand put, it takes three elections
16 to change the board. That's kind of a crafty move, and
17 that's the effect of a dead hand put right there.

18 We have alleged that Healthways didn't
19 need the money. I don't know what kind of need would
20 even suffice. You know, AIG being taken over by the
21 government, maybe. But we have affirmatively alleged
22 they didn't need the money. They actually announced the
23 debt and said, "Credit markets are great. Easy, cheap
24 money. We're refinancing before we have to to take

1 advantage of the good conditions that we have."

2 Now, what triggers proxy puts? Not only
3 shareholder unrest, but also poor performance. So when
4 you have poor performance, you are more likely to face a
5 proxy fight. You know what you are also more likely to
6 face? A bank that doesn't want to give you a waiver or
7 doesn't want to let you refinance. And we've alleged all
8 of that.

9 Now, inferences. Your Honor at the end
10 was speaking about plausible versus reasonably
11 conceivable. In this case -- and I don't know that we
12 needed to do this. I don't know why we should have to --
13 but we actually went belt and suspenders. We're really
14 not asking the Court to make that many inferences at all,
15 because we did send a 220 demand. Now, what we said is,
16 "We can't conceive of when a board really could agree to
17 a dead hand proxy put unless you are in extremis, or
18 something like that." "However," we said, "give us all
19 of your exculpatory evidence." So this isn't your
20 traditional situation where we're asking for inferences.
21 We know that the company did not produce anything showing
22 any consideration for or any consideration of the dead
23 hand proxy put.

24 Now, I'll just touch on some of the

1 facts that relate to SunTrust, and then I'll go into the
2 legal arguments. You know, the timing -- oh. Oh, okay.
3 I just want to correct this as, what we allege in
4 paragraph 37 is -- I see -- there was a vote on May 31st
5 to -- a 10-to-1 vote to declassify the board. And on
6 October 10th, 2013, the board relented. That is fair.
7 So I guess it was like a precatory proposal to destagger.
8 And then eventually the pressure continued, but they
9 adopted the dead hand once they knew they were losing by
10 10 to 1. That's fair.

11 We think that the Section 220 and the
12 timing of the put, all that applies to SunTrust also
13 and, as I'll get to it, there is no way that SunTrust can
14 have the Court accept their version of the facts,
15 whatever those facts might be. And I don't really know
16 that they are putting any facts out there, anyway.

17 THE COURT: Their argument is that you
18 have them. Their argument is that you actually have to
19 come forward and identify something that supports the
20 knowing participation, and that just contracting, just
21 being a party to a contract that contains this type of
22 potentially entrenching provision is not sufficient.

23 MR. LEBOVITCH: Yeah, that's what
24 they're saying. I disagree. I think Vice Chancellor

1 Lamb pretty -- I would say -- unequivocally rejected that
2 argument, that defense. The public policy -- I mean, he
3 has a statement -- I will get to that in a little bit. I
4 think they are just wrong. I think paragraph 58, even if
5 it was a loan, you know, could suffice. But it's not.

6 I mean, we have four versions of this
7 loan agreement without a dead hand. And then three years
8 after this Court says there's an eviscerating effect on a
9 shareholder franchise, then anyone who adopts a provision
10 like this essentially is on notice that this might
11 violate public policy. I think that the facts of putting
12 it in place in 2012, right after the shareholders want to
13 destagger, and the fact of the 220 helps us. Because,
14 again, you don't have to make a leap to say there were no
15 negotiations. There is nothing on the Healthways side.

16 So their only hope is in their records
17 somehow they can show one-sided documentation of
18 negotiations or of this being so essential to providing
19 the loan. And I think that's fair for discovery. I
20 don't think they will ever get it.

21 And I want to highlight two facts which
22 will just touch on Amylin. Again, I don't think these
23 are essential to stating a claim, but they are here. We
24 are past the first election, okay. I think that these

1 claims should be ripe even before any proxy fight is
2 launched.

3 And Your Honor's point about the statute
4 of limitations, I think, hit the problem on the head.
5 And, really, it shows the defendants' position is no
6 matter what, shareholders challenging a dead hand proxy
7 put will always be too early until they're too late.
8 That's the essence of the argument. I think that gets
9 rejected.

10 But here we are after the 2014 election
11 and the three insurgents are on the board. They are
12 noncontinuing directors, okay. Now, the founder, the
13 co-founder of the company resigned in a pretty loud way.
14 We cite that in the complaint. He says, "You're not
15 serving shareholder interests." That's why there's 11
16 people left on the board.

17 With three, admittedly, noncontinuing
18 directors, a shareholder today -- to use Your Honor's
19 example of the artillery on the hill, right -- they have
20 a choice. You know, are they going to do, you know, in
21 effect, an urban protest? Are they going to march in the
22 streets or launch a proxy fight; kind of the same thing.
23 They have a decision to make. Do you do it at all? Are
24 you going to get shot if you try? Or to apply it to the

1 proxy fight, you really want to go for four, you really
2 want four of your nominees on the board, but you know
3 that's going to trigger the proxy put fight. Or your
4 choice is just nominate two and avoid the issue.

5 And, you know, one fact that
6 Mr. Lafferty said, that I think he misspoke, is the proxy
7 contestants don't litigate these things, okay. And there
8 is a pragmatic reason for it. The same way that, you
9 know, ISS says, "We'll support you if you don't go for a
10 majority," and so a lot of activists will not go for a
11 majority. Activists don't want to go out there while
12 they are running a proxy fight and say, "I'm going to die
13 if this proxy put isn't removed." They don't want to do
14 that, so they try to fight through it, or they do what I
15 think the insurgents in the town will do in the face of
16 the gun, and they say, "I'm going to run, too, see what
17 happens." That's not right. That's not Delaware law.

18 Now, the ripeness defense, the XL
19 case -- the Delaware Supreme Court -- I am just going to
20 touch on. It's an indemnity case. It's sort of
21 self-evident that -- I think it should be self-evident
22 that an indemnity claim isn't ripe until there has been
23 an underlying judgment. That's truly an advisory
24 opinion. Frankly, almost all of the ripeness cases that

1 are out there involve something that's speculative and
2 that's kind of anticipatory.

3 Again, here, you know, the argument
4 that's made is, "Well, under XL things can happen that
5 will obviate the claim." Well, Your Honor, any time
6 there is a contractual provision or a board action that's
7 alleged to be a breach of fiduciary duty that hurts
8 shareholders right now, it can be cured. It's possible
9 it will be cured before there is a judicial resolution.
10 It's possible it will be cured before the harm gets any
11 worse. But I don't think the possibility that a board
12 can rectify its existing breach has ever been ruled to
13 prevent the Court from addressing these issues.

14 You know, I'll just touch on Amylin I
15 and Amylin II really quickly, and Sandridge, for that
16 matter. You know, in Amylin I, the quote that Your Honor
17 sees doesn't have anything to do with the dead hand
18 provision. It has to do with the approval of the put.
19 And, actually, the defendants' own quote, I think, kind
20 of shows what Vice Chancellor Lamb was saying. It says,
21 "We're having a trial two days before" -- or maybe ten
22 days before -- "the election." That was the --
23 factually, that was the timing of it, and it's in the
24 opinion. And Vice Chancellor Lamb says, "Okay. Well,

1 I'm going to not deal with the approval right now, but
2 the plaintiff and the company can come back to me if the
3 directors are elected, and then I'll decide any fight
4 about the continuing director provision." So that's
5 exactly what Vice Chancellor Lamb said. And Vice
6 Chancellor Noble in his opinion understood it that way.
7 He said there was essentially a temporal dismissal to see
8 what happens at the election because the election hadn't
9 yet happened.

10 I don't know that that's, again, the
11 necessary requisite, but here we have it. Here, we are
12 after that first election. There is no doubt in my mind,
13 and I don't think that anyone reading the opinion should
14 doubt, that Vice Chancellor Lamb, the day after the
15 election, once those guys were elected, would have
16 allowed someone to file a lawsuit saying "These guys have
17 to be approved. They are noncontinuing as of today. And
18 under the dead hand put, there's no approval necessary.
19 These people who are on the board right now are
20 noncontinuing. They don't have the same rights and
21 powers as other directors." So to me, there's obviously
22 an existing and current harm.

23 You know, the defendants cite the
24 Bebchuk case. I will just touch on that. I mean,

1 Bebchuk, I think, was also very clear. The bylaw at
2 issue hadn't yet been adopted, and so the ripeness ruling
3 says, "Well, if the bylaw is adopted, then we can assess
4 whether it's valid." Here, the proxy put has been in
5 place. And you had the discussion with Mr. Lafferty. So
6 the key event necessary to vest jurisdiction in this
7 Court has happened.

8 You know, again, that's why the
9 hypotheticals don't matter. I mean, I was -- I tried to
10 be a little glib about the hypotheticals and the
11 speculative and all that. But, of course, facts can
12 evolve. That happens all the time when a case is filed.
13 Facts evolve. Companies are real. Things happen.
14 There's harm today. That's the key.

15 Now, the Sandridge, and I guess Amylin,
16 also, there is some effort to say that those cases turn
17 on affirmative invocation of the put. In Sandridge --
18 now, in Amylin, there was an invocation that lasted for a
19 while. Sandridge, it lasted for all of one day. And,
20 actually, what Chancellor Strine said is, "Well, yeah,
21 you came out and you said that this is potentially
22 harmful, and the next day you come out and say, 'Wait.
23 No, no. We can refinance. We can refinance our debt.
24 There's no problem. There's no problem here.'"

1 Now, Chancellor Strine asked, "Well, if
2 there's no problem, how come you're not approving?" Not
3 relevant here, but they weren't invoking anything. Part
4 of their defense, that argument -- which I do recall --
5 was that there's no effect on the vote. So who cares?
6 Why are you deciding this? And what the Chancellor
7 said -- and this is at 68 A.3d at 261 -- I think applies
8 here with full force, and it goes to the shadow point
9 that Your Honor made. "... the incumbent board's
10 behavior is redolent more of the pursuit of an
11 incremental advantage in a close contest, where a small
12 margin may determine the outcome, than any good faith
13 concern for the company"

14 So this is the point about bargaining in
15 the shadow, is if the proxy put has some incremental
16 advantage in getting shareholders to hold off with their
17 proxy fight or to run fewer nominees, that's not fair and
18 that's not right, and we would say that's actionable.

19 We cited -- Your Honor, we cited the
20 Amylin II opinion, where Vice Chancellor Noble says
21 clearly there's a deterrent effect. That's consistent
22 with Carmody. I don't think there's much reasonable
23 debate about that. But to actually get specific, just
24 because we didn't quote it in the brief, I just want to

1 quote Vice Chancellor Noble saying, "... by requesting
2 declaratory relief as to the validity and legality of the
3 continuing director provisions, the Pension Fund sought
4 to remove constraints hindering the effectiveness of the
5 shareholder vote." So this is talking about with no
6 proxy fight pending, no triggering, this is done. So I
7 think that should resolve that.

8 Now, I guess both Healthways and
9 SunTrust try to say this is an issue of first impression,
10 or that maybe SunTrust is trying to take an
11 ignorance-of-the-law defense. I don't know. I was in
12 this courtroom five years ago when this started. This
13 fight has been percolating for five years through
14 numerous opinions. The ignorance excuse may have worked
15 for the Amylin board, and maybe even the Amylin bankers,
16 but it can't work today. Not after what Vice Chancellor
17 Lamb wrote, Vice Chancellor Noble wrote, and what
18 Chancellor Strine wrote.

19 If Your Honor doesn't have any more
20 questions on ripeness, I will turn to the aiding and
21 abetting. The gist of what I heard, and what we saw in
22 the briefs, is essentially representations of facts. I
23 mean, you know, we hear that a lender can't be held for
24 aiding and abetting simply because it bargains for a

1 provision. Because there's company-specific context that
2 relates to the provision, that it could, but doesn't
3 necessarily, implicate the fiduciary duties of the
4 borrower. I mean, we're a 12(b)(6), we have the 220 out
5 there, but there's just no way that anyone can infer
6 there was bargaining here. Maybe they will prove it.
7 They can't infer it.

8 I don't know what contextual facts there
9 are that are unique to this company. I mean, they said
10 it was cheap money. That's why they took the loan. They
11 just threw in the dead hand provision. And I don't
12 think, in light of Amylin I, it's possible for anyone in
13 this field -- and, obviously, that opinion got a lot of
14 publicity -- it's impossible for anyone to question that
15 this provision could implicate fiduciary duties. I might
16 question how it could ever not implicate fiduciary
17 duties, but that's, I guess, a different story.

18 You know, their basic theme is, "We are
19 never going to learn anything in discovery. We are never
20 going to fill out any of the record." You know, they say
21 that change-in-control provision is market. Well, Your
22 Honor, first of all, it's not, because there's a lot of
23 approvable puts. I think the number of these proxy puts
24 actually has gone down since Amylin, because most banks

1 get it. I know, because we've been out there working
2 with other companies that are getting rid of these
3 provisions. But, also, who cares if it's market, Your
4 Honor? Once upon a time, staple financing was market
5 also. And I hope Your Honor understands that the
6 republic didn't crumble to its knees when a wise jurist
7 called into question the practice of staple financing.

8 THE COURT: That wise jurist was our
9 Chief Justice in a case long before anything I wrote.
10 The other thing I remember is, look, I think when Toll
11 Brothers briefed, there were 190-some dead hand pills out
12 there. I mean, corporate attorneys are great imitators.
13 And the fact that something is market is certainly
14 something that we take into account in terms of a factor.
15 But, you know, at the time of a riot, rioting is market.

16 MR. LEBOVITCH: Yes, exactly, Your
17 Honor.

18 SunTrust says, "These provisions have
19 value." Your Honor said, "What value?" And initially
20 SunTrust -- Mr. Murphy didn't answer. He didn't say,
21 "Well, what is the value?" I actually think he answered
22 the question earlier, because what he said was, "These
23 provisions are designed -- I believe it's a quote --
24 "designed to prevent wholesale change in a short period

1 of time." We agree. That's our point. That's the
2 deterrent.

3 He also talks about the options lenders
4 have to deal with a proxy put. He talks about the
5 options a board has. And I think Your Honor touched on
6 it. What about the shareholders? What are their
7 options, really?

8 So, in any event, SunTrust's argument
9 essentially would say that, you know, even if Your Honor
10 says there's heightened review of a board approval of a
11 put, the bank can't be, you know, liable for anything,
12 and presumably can't be subject to relief. So what
13 you're really saying is, even if there's enhanced
14 scrutiny from the board perspective, there's actually no
15 judicial scrutiny. Because without the banks, I'm not
16 sure you can do anything.

17 Their view of knowing participation is
18 not correct. And in their case that they cite a lot,
19 Frank vs. Elgamal, quoting Malpiede, knowing
20 participation doesn't mean you affirmatively know there
21 is a per se breach of duty. The language of the case
22 says that there could be knowing participation where
23 "... the bidder attempts to create or exploit conflicts
24 of interest in the board." That's 2012 WL 1096090 *12.

1 And it's paraphrasing, I believe, the Malpiede case.

2 But when a bank -- and clearly this bank
3 -- asks for a proxy put -- even if Your Honor wants to
4 assume that they asked for it -- they know what they're
5 doing and they understand there is not going to be
6 pushback on that provision. Hey, if you have another way
7 to extract the waiver fee, why not? And by the way, if
8 the company is performing so poorly that it's going to be
9 subject to a proxy fight, why not have the ability to
10 refuse to waive?

11 And, you know, I paraphrased it. I just
12 want to make sure the Court has the quote. The ignorance
13 defense doesn't work after Vice Chancellor Lamb's opinion
14 in Amylin. This is Footnote 32 of his opinion. He says,
15 "A provision so strongly in derogation of the
16 stockholders' franchise rights would likely put the
17 trustee and noteholders on constructive notice of the
18 possibility of its ultimate unenforceability." Of
19 course, there -- because the credit agreement had been
20 waived already -- he's speaking about the trustee and
21 noteholders. But I don't think there's any logical basis
22 to distinguish. And, in fact, Vice Chancellor Lamb says,
23 "A bank agreement would be, at most, somewhat less
24 concerning." So he says -- the notes are Armageddon,

1 right, if you have a dead hand in the notes. He says,
2 "Well, if you have got a bank, it's somewhat less
3 concerning." He's not saying it's okay. And, of course,
4 Healthways' lawyer said you have to be aware of this.

5 Chancery Strine in Sandridge talked
6 about the clear defensive value of these provisions, so I
7 don't think there is a question about that, and banks are
8 on notice of it. Ultimately, I think the law, as it
9 stands, does require the Court to get involved here. And
10 the Court should, because what we've learned is, you
11 know, banks won't stop asking for, or accepting, dead
12 hand proxy puts until they know that there is no waiver
13 fee value and that they can't get this provision.
14 Frankly, boards aren't going to negotiate against it or
15 stop proposing the provision until they know there is a
16 consequence to putting it in place.

17 Just like with dead hand proxy puts,
18 just like staple financing, the republic will not fall to
19 its knees if one provision that's probably a relic of
20 days gone by is, you know, held to state a viable breach
21 of fiduciary duty claim, at least to get to discovery.

22 If Your Honor has nothing else, I
23 will ...

24 THE COURT: Thank you.

1 Reply.

2 MR. LAFFERTY: I will try to -- I will
3 be brief, Your Honor.

4 I guess maybe I'll try to take on the
5 gun-on-the-hill analogy, just briefly, because I don't
6 think I really responded effectively to it the first time
7 around. I guess maybe because I just -- I struggle with
8 those types of analogies when faced with them. My
9 partner, Mr. Nachbar, likes to pick them apart all the
10 time.

11 But I guess I would say this, Your
12 Honor. Is that there's really no allegation here that
13 the board did anything to load the gun, to put it on the
14 hill, and to aim it at anybody. This is not the -- if
15 anything, the gun and the ammunition are sitting
16 somewhere off in a depot, and it's sitting there
17 inchoate, and it may or may not ever get loaded, and it
18 may or may not ever be used in any shape or form or
19 pointed at anyone or fired at anyone. And, indeed, we
20 don't know yet because we don't know what the facts are
21 related to the upcoming meeting. That's the way I look
22 at it. And as history shows, in 2014 the board didn't do
23 anything with this change-in-control provision. It never
24 once raised it, it never once threatened stockholders

1 with it in any way, shape, or form. So that would be my
2 first point.

3 And I think my second point is,
4 obviously, how the facts develop in the future, I think,
5 will allow the Court to see whether or not there is any
6 imminent harm that is threatened to stockholders.

7 On Your Honor's statute of limitations
8 versus ripeness point -- and I confess, I don't have a
9 definitive answer as I stand here. We didn't research --
10 we didn't really brief that issue, per se -- I certainly
11 think -- to me, it's not clear whether or not the statute
12 of limitations necessarily would begin to run on the date
13 that the agreement was adopted or disclosed to
14 stockholders or whether it is at a later point in time
15 when the board does something to invoke it or to use it
16 in some way against the stockholders. I think that
17 depends on the question of whether or not it was or was
18 not a breach of fiduciary duty to simply enter into the
19 contract, you know, in 2012 or not.

20 We don't believe the law is there. And,
21 indeed, the law that is there in Amylin suggests that
22 entering into a provision, even in a circumstance there,
23 where the board didn't know about the provision -- no
24 record was presented to the judge about the board's

1 consideration -- the board -- or Vice Chancellor Lamb
2 concluded that there was no breach of duty of care.
3 Certainly, he had some strong words to future boards that
4 they -- that they need to look at these things, but he
5 certainly did not suggest there that the mere fact that
6 the board didn't consider it specifically was a
7 duty-of-care violation.

8 And, indeed, when the case went up on
9 appeal to the Supreme Court, Justice Jacobs said in a
10 very short order affirming Vice Chancellor Lamb's
11 decision, he said, "... it appears [that]" -- "to the
12 Court that the order and judgment of the Court of
13 Chancery should be affirmed on the basis of and for the
14 reasons set forth in [Vice Chancellor Lamb's]
15 decision"

16 Then he drops a footnote and it says,
17 "The Court of Chancery determined, inter alia, that
18 Amylin Pharmaceuticals' board of directors did not breach
19 its duty of care in authorizing the corporation to enter
20 into the Indenture Agreement, with its 'proxy put'
21 provision. That determination was correct, not only for
22 the reasons made explicit in the Court's opinion, but
23 also for one that is implicit: no showing was made that
24 approving the 'proxy put' at that point in time would

1 involve any reasonably foreseeable material risk to the
2 corporation or its stockholders. That risk materialized
3 months later, and was aggravated by the unexpected,
4 cataclysmic decline in the nation's financial system and
5 capital markets beginning in the Spring of 2008."

6 And, you know, Your Honor, I would just
7 submit that here, that we really -- we don't have -- I
8 don't think we have allegations at this point, or
9 certainly don't have -- well, we certainly don't have a
10 basis to believe that there was a per se breach of
11 fiduciary duty simply by entering into the agreement.
12 And we believe Amylin and the Amylin appeal decision
13 supports that, which, again, we believe then counsels in
14 favor of, you know, an approach that says you have to see
15 where you are with the facts and what the board does, if
16 anything, to invoke the provision.

17 THE COURT: Thank you.

18 MR. LAFFERTY: Thank you, Your Honor.

19 MR. MURPHY: I will be very brief, Your
20 Honor.

21 Our fundamental disagreement with the
22 plaintiffs is not over whether or not they have a
23 potential breach of fiduciary duty claim against the
24 board of the borrowing company. I think that our

1 argument is obviously focused from a very different
2 perspective.

3 And I wanted to just take a moment to
4 mention something that Chancellor Strine said in
5 connection with the Sandridge Energy case. He says,
6 "Thus, this Court in Amylin focused on the nature of the
7 Proxy Put as a provision giving the creditors protection
8 against a new board that would threaten their legitimate
9 interests in getting paid. Such situations could arise,
10 for example, because the proposed new board consists of
11 'known looters' or persons of suspect integrity. Or, the
12 insurgent slate could have plans for the company posing a
13 genuine and specific threat to the corporation and its
14 ability to honor its obligation to its creditors that
15 prevent the incumbent board from approving them in good
16 conscience for [the] purposes of the Proxy Put. By
17 contrast, where an incumbent board cannot identify that
18 there is a specific and substantial risk to the
19 corporation or its creditors posed by the rival slate,
20 and approval of that slate would therefore not be a
21 breach of the contractual duty of good faith owed to
22 noteholders with the rights to the Proxy Put, the
23 incumbent board must approve the new directors as a
24 matter of its obligations to the company and its

1 stockholders"

2 That provision, I think, as much as
3 anything, sort of captures the different perspective
4 between someone sitting there as a creditor, negotiating
5 for a provision that's favorable to it and the people
6 that it has fiduciary obligations to, versus the role
7 that the board of the company has in these types of
8 provisions. And, in essence, what we're being asked to
9 consider is making creditors the police -- the policemen
10 or watchdogs over whether or not their borrowers adhere
11 to their fiduciary obligations.

12 The last thing I will say, Your Honor,
13 is I can almost get to the point and understand where
14 someone would want us to have a seat at the table, since
15 we are the counterparty to the credit agreement which
16 contains the alleged offensive provision. But to take
17 that from an interested-party status to an active aider
18 and abetter of a breach of fiduciary duty, to me, seems
19 like a fairly radical departure from anything in Amylin
20 or in Sandridge. And, in fact, those cases, as Your
21 Honor knows, were really keenly focused on the behavior
22 of the members of the board of directors and not the
23 counterparty to these contracts.

24 Thank you.

1 THE COURT: Great. All right. Thank
2 you all for your presentations today. I appreciate it.
3 I'm going to go ahead and give you my thoughts now.

4 We are here on a motion to dismiss filed
5 by the defendants. There are two groups of defendants.
6 The individual defendants and the company have moved to
7 dismiss on ripeness grounds. The lender, SunTrust, has
8 moved to dismiss, in addition, on failure to state a
9 claim for which relief can be granted, primarily based on
10 the assertion that the complaint doesn't contain
11 sufficient allegations to support a claim for aiding and
12 abetting.

13 The plaintiff, Pontiac General Employees
14 Retirement System, is a stockholder of the nominal
15 defendant, Healthways. Pontiac has sued, principally on
16 a classwide basis, on a putative classwide basis, but
17 alternatively it sues derivatively. The individual
18 defendants are the members of the company's board of
19 directors.

20 The background facts are as follows: In
21 2010, the company entered into a fourth amended and
22 restated revolving credit and term loan agreement. That
23 term loan agreement included what the plaintiffs have
24 described as a proxy put that had a continuing director

1 feature. The proxy put at that time would be triggered
2 when, during any period of 24 consecutive months, a
3 majority of the members of the board of directors ceased
4 to be composed of continuing directors. The proxy
5 provision in the 2010 loan agreement did not contain a
6 dead hand feature.

7 Subsequently, the company came under,
8 and remains under, pressure from stockholders. It faced,
9 and continues to face, the risk of a proxy contest.

10 In 2012, the New York State Common
11 Retirement Fund submitted a proposal to declassify the
12 board. On May 31, 2012, the company's stockholders
13 overwhelmingly approved that precatory proposal to
14 declassify the board, despite the board's opposition.
15 Subsequently, on October 10, 2013, the company did, in
16 fact, amend its articles of incorporation to phase out
17 its classified board structure. By 2016, the entire
18 board will be up for reelection.

19 On June 8th, 2012, days after the
20 stockholder vote that signalled, to at least some
21 degree -- and certainly it's inferable at the pleadings
22 stage -- some degree of stockholder dissatisfaction with
23 the company, the board entered into a fifth amended and
24 restated revolving credit and term loan agreement. That

1 2012 agreement has been amended three times since then.

2 The 2012 loan agreement provided the
3 company with a \$200 million revolving credit facility,
4 including a \$20 million swing-line subfacility and a 75
5 million subfacility for letters of credit, which
6 terminates on June 8th, 2017, as well as a \$200 million
7 term loan facility, which matures on the same date. The
8 2012 loan agreement contained a dead hand proxy put.

9 Subsequently, in 2013, the company
10 issued additional debt. That additional debt, one
11 tranche of 125 million and another tranche of 20 million,
12 was wrapped into the dead hand proxy put by stating that
13 it would be an event of default if the company defaulted
14 on any other loans in excess of \$10 million.

15 Stockholder pressure continued. On
16 December 2nd, 2013, North Tide Capital, an 11 percent
17 stockholder, sent a public letter to the board expressing
18 its concern with the board's leadership and the company's
19 performance and called for the board to remove its CEO.
20 The board rejected that request.

21 In January 2014, North Tide sent another
22 fight letter and stated its intent to wage a proxy fight.
23 There was ultimately a resolution, where North Tide
24 gained representation on the board. Those directors are

1 treated as noncontinuing directors for purposes of the
2 dead hand proxy put.

3 In March 2014, Pontiac served the
4 company with a demand under Section 220, seeking
5 documents and records relating to the dead hand proxy
6 put. According to the complaint, the company failed to
7 produce documents showing that there was substantive
8 negotiation about the proxy put and no documents that
9 suggested, to use the language of Amylin, that the
10 company received "extraordinarily valuable economic
11 benefits" that might justify the proxy put.

12 In this action the plaintiff asserts a
13 claim for a breach of fiduciary duty against the
14 individual defendants, a claim for aiding and abetting
15 against SunTrust, and it also seeks a declaratory
16 judgment that the dead hand proxy put is unenforceable.

17 I'm going to start with the individual
18 defendants and the company who have moved to dismiss on
19 grounds of ripeness. Courts in this country generally,
20 and in Delaware in particular, decline to exercise
21 jurisdiction over cases in which a controversy has not
22 yet matured to a point where judicial action is
23 appropriate, to paraphrase the Stroud case. When
24 considering a declaratory judgment application, for an

1 actual controversy to exist, the issue must be ripe for
2 judicial determination. That's a paraphrase of the XL
3 Specialty Insurance case.

4 "In determining whether an action is
5 ripe for a judicial determination, a 'practical judgment
6 is required.'" That's the Stroud case quoting this
7 Court's decision in Schick. This practical judgment has
8 been described as a common-sense assessment of whether
9 the interests of the party seeking relief outweigh the
10 concerns of the Court in postponing review until the
11 question arises in some more concrete and final form.

12 Here, the defendants argue that the
13 dispute is not ripe because a variety of additional
14 events must take place before the proxy put with its
15 dead-hand feature is actually, in fact, triggered and
16 does actually accelerate the debt.

17 The plaintiffs, however, have cited two
18 different injuries. The first is the deterrent effect of
19 the proxy put. Namely, because the proxy put exists, it
20 necessarily has an effect on people's decision-making
21 about whether to run a proxy contest and how to negotiate
22 with respect to potential board representation.

23 As with other defensive devices, such as
24 rights plans, one necessarily bargains in the shadow of a

1 defensive measure that has deterrent effect. A truly
2 effective deterrent is never triggered. A really truly
3 effective deterrent is one you don't even have to point
4 the other side to because they know it's there. If the
5 deterrent is actually used, it has failed its purpose.

6 Delaware courts have consistently
7 recognized that disputes are ripe when challenging
8 defensive measures that have a substantial deterrent
9 effect. For example, we regularly allow stockholder
10 plaintiffs to litigate defensive measures in merger
11 agreements in the absence of an actual topping bid. Why?
12 Because if truly effective, those defensive measures will
13 deter the topping bid and it won't emerge.

14 Delaware courts, likewise, have held
15 that a similar deterrent effect is sufficient to
16 establish a ripe dispute when dealing with another
17 classic defensive measure that is adoptable in a quite
18 similar format by a board; namely, a rights plan.

19 In Moran, it was the deterrent effect on
20 proxy contests that made the dispute ripe. Now, as the
21 defendants point out, the Court in Moran ultimately held
22 post-trial that the rights plan, in fact, did not
23 interfere with the proxy contest in that case, based on
24 the nature of the plan, the level of its trigger, and

1 other evidence that was presented. That was a
2 merits-stage ruling as to whether the rights plan should
3 be permanently enjoined or otherwise invalidated. It was
4 not an analysis of the ripeness issue. The ripeness
5 issue was decided based on the deterrent effect.

6 The same is true in Leonard Loventhal
7 Account. Most importantly, to my mind, the same is true
8 in Carmody vs. Toll Brothers. I am unable to distinguish
9 Carmody vs. Toll Brothers from this case, and I don't
10 think the defendants have offered any credible
11 justification on which the two cases can be distinguished
12 for ripeness purposes.

13 The problem in Toll Brothers was that a
14 rights plan containing a dead hand feature in a pill
15 would have a chilling effect on, among other things,
16 potential proxy contests such that the stockholders would
17 be deterred, they would have the Sword of Damocles
18 hanging over them, when they were deciding what to do
19 with respect to a proxy contest. There wasn't a
20 requirement that an actually proxy contest be underway.

21 That's exactly what the effect is of the
22 dead hand proxy put in this case. The same analysis, in
23 my view, applies. The same reasoning was followed in KLM
24 Royal Dutch Airlines vs. Checchi and, again, I think it's

1 on all fours here.

2 The second present injury that the
3 plaintiffs have cited, as Mr. Lebovitch reminded me of,
4 is that the noncontinuing directors currently serving on
5 the board are currently designated as such. And hence,
6 they are currently suffering an injury in the form of
7 being treated differently than the other directors on the
8 board. And that was another injury of a type that
9 then-Vice Chancellor, later-Justice Jacobs allowed the
10 stockholders to sue for in Toll Brothers. And he
11 ultimately held on the motion to dismiss that, in fact,
12 it stated a claim for a 141(d) violation. So that is
13 another present injury that's happening now.

14 I do think there is a distinction -- as
15 Mr. Lafferty ably identified -- between the potential
16 future invocation or triggering of the dead hand put, the
17 nonwaiver of the dead hand put, and its adoption now.

18 What I think is ripe now is a claim
19 that, based on the facts of this case, the board of
20 directors breached its duties in a factually-specific
21 manner by adopting this poison dead hand put
22 arrangement -- however you want to call it -- I guess
23 proxy -- you guys have too much jargon -- dead hand proxy
24 put arrangement in the context of the facts and

1 circumstances here, including the rise of stockholder
2 opposition, the identified insurgency, the change from
3 the historical practice in the company's debt
4 instruments, the lack of any document produced to date
5 suggesting informed consideration of this feature, the
6 lack of any document produced to date suggesting
7 negotiation with respect to this feature, etc.

8 This is not a per se analysis. No one
9 is suggesting that. Nor does the denial of the motion to
10 dismiss depend on any theory that entering into an
11 agreement that contains a proxy put is a per se breach of
12 fiduciary duty.

13 Procedurally, that's inaccurate. All
14 we're here on right now is a motion to dismiss. As to
15 one of the motions, we're just asking if the claim is
16 ripe, we're not making any per se adjudication. And as
17 to the other motion to dismiss, all we're asking is has a
18 claim been pled under the Central Mortgage notice
19 pleading standard. We're not asking whether there is
20 some ultimate relief to be granted as a matter of law.

21 And substantively it's inaccurate as
22 well, because a ruling in this case will be based on the
23 facts of this case; namely, what the board did or didn't
24 do or knew or didn't know and what the back and forth

1 was, if there was any, with SunTrust.

2 So in my view, I do think that the
3 dispute is sufficiently ripe to state a claim as to the
4 entry into a credit agreement with the proxy put. It may
5 be that there is another claim down the way based on the
6 potential nonwaiver of the proxy put for future
7 directors, just like there might be a potential claim on
8 down the way regarding the use of a rights plan. But
9 that doesn't mean there's not a claim surrounding the
10 adoption of a rights plan or a claim surrounding the
11 entry into the proxy put. So I think that the dispute is
12 ripe.

13 In terms of whether Pontiac has
14 standing, I think this is a flip side of the ripeness
15 argument. The primary purpose of standing is to ensure
16 the plaintiff has suffered a redressable injury.
17 Standing is the requisite interest that must exist in the
18 outcome of the litigation at the time the action is
19 commenced. The test of standing is whether there is a
20 claim of injury, in fact; and that the interest sought to
21 be protected is arguably within the zone of the interest
22 to be protected or regulated by the -- and I'm going to
23 say -- the legal protection in question. That's a
24 paraphrase of the Gannett case. The concepts of standing

1 and ripeness are, indeed, related.

2 So what I've tried to explain is I think
3 this dispute is ripe as a practical matter because the
4 stockholders of the company are presently suffering a
5 distinct injury in the form of the deterrent effect, the
6 Sword-of-Damocles concept, as well as in the form of the
7 fact that they have directors on the board, some of whom
8 are noncontinuing directors and some of whom are
9 continuing directors.

10 What we know from those cases that I
11 cited on ripeness grounds -- namely, Moran, Leonard
12 Loventhal, Carmody, KLM -- those were all brought by
13 stockholders. Stockholders had standing to bring those
14 claims. So I think the same is true here. So I'm
15 denying the motion to dismiss that was brought by the
16 individual defendants and the company on ripeness
17 grounds.

18 I'm now going to turn to the question of
19 whether the complaint adequately states a claim for
20 aiding and abetting. To state a claim for aiding and
21 abetting, the plaintiff must plead the existence of a
22 fiduciary relationship, a breach of a fiduciary duty,
23 knowing participation in the breach, and damages
24 proximately caused by the breach. That's a paraphrase of

1 the Malpiede case. SunTrust has focused its motion to
2 dismiss on the knowing participation element.

3 It is certainly true, and I agree, that
4 evidence of arm's-length negotiation negates claims of
5 aiding and abetting. In other words, when you are an
6 arm's-length contractual counterparty, you are permitted,
7 and the law allows you, to negotiate for the best deal
8 that you can get. What it doesn't allow you to do is to
9 propose terms, insist on terms, demand terms, contemplate
10 terms, incorporate terms that take advantage of a
11 conflict of interest that the fiduciary counterparts on
12 the other side of the negotiating table face.

13 This is the premise that is true in
14 third-party deal cases. The acquirer is perfectly able
15 to negotiate for the best deal it can get, but as soon as
16 it starts offering side benefits, entrenchment benefits,
17 other types of concepts that create a conflict of
18 interest for the fiduciaries with whom it's negotiating,
19 that acquirer is now at risk. Is the acquirer
20 necessarily liable? No. But does that take the acquirer
21 out of the privilege that we afford arm's-length
22 negotiation? It does.

23 Here, the plaintiffs are not challenging
24 the loan agreement as a whole. They are not challenging

1 the interest rate or other financial terms. They are
2 challenging a proxy put with recognized entrenching
3 effect. There was ample precedent from this Court
4 putting lenders on notice that these provisions were
5 highly suspect and could potentially lead to a breach of
6 duty on the part of the fiduciaries who were the
7 counter-parties to a negotiation over the credit
8 agreement.

9 Given the facts here, as alleged,
10 including that there was a historic credit agreement that
11 had a proxy put but not a dead hand proxy put, and then
12 that under pressure from stockholders, including the
13 threat of a potential proxy contest, the debt agreements
14 were modified so that the change-in-control provision now
15 included a dead hand proxy put, and considering that all
16 of this happened well after Sandridge and Amylin let
17 everyone know that these provisions were something you
18 ought to really think twice about, I believe that, as
19 pled, this complaint satisfies the requirement to survive
20 a motion to dismiss.

21 It may well be that there's ultimately
22 no claim and that SunTrust wins. It may well be that
23 they didn't aid and abet anything. But for
24 pleading-stage purposes, what they are is they're a party

1 to an agreement containing an entrenching provision that
2 creates a conflict of interest on the part of the
3 fiduciaries on the other side of the negotiation. And
4 that provision arose in the context of a series of pled
5 events and after decisions of this Court that should have
6 put people on notice that there was a potential problem
7 here such that the inclusion of the provision was, for
8 pleading-stage purposes, knowing.

9 At the risk of stating what I hope is
10 obvious, I am not making any findings of fact on that,
11 and I do not know if, in fact, these things were
12 responsive to stockholder pressure or if some other
13 driver generated them. All I know is that for
14 pleading-stage purposes, I think that the complaint
15 states a claim. So for that reason I am also denying the
16 SunTrust motion.

17 So I'm sure people have questions.
18 Mr. Lafferty, I'll start with you. What questions do you
19 have for me?

20 MR. LAFFERTY: No questions, Your Honor.

21 THE COURT: All right.

22 Mr. Murphy, what questions do you have
23 for me?

24 MR. MURPHY: No questions, Your Honor.

1 THE COURT: Mr. Lebovitch, what can I
2 clarify for you?

3 MR. LEBOVITCH: I guess when Your Honor
4 would like the parties to submit a schedule for pursuing
5 this case?

6 THE COURT: I'm going to let you talk to
7 your friends on the other side, because everyone in here
8 is good at their job.

9 MR. LEBOVITCH: Thank you.

10 THE COURT: I will let you all deal with
11 that in the first instance.

12 MR. LEBOVITCH: Okay.

13 THE COURT: All right. Thanks,
14 everyone, for bearing with me today. We stand in recess.

15 (Court adjourned at 2:47 p.m.)

16 - - -

17

18

19

20

21

22

23

24

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24

CERTIFICATE

I, DEBRA A. DONNELLY, Official Chancery Court Reporter of the State of Delaware, Registered Merit Reporter, Certified Realtime Reporter, and Delaware Notary Public, do hereby certify that the foregoing pages numbered 3 through 82 contain a true and correct transcription of the proceedings as stenographically reported by me at the hearing in the above cause before the Vice Chancellor of the State of Delaware, on the date therein indicated, except for the rulings at pages 68 through 82, which were reviewed by the Vice Chancellor.

IN WITNESS WHEREOF I have hereunto set my hand at Wilmington, this 17th day of October, 2014.

/s/ Debra A. Donnelly
Official Chancery Court Reporter
Registered Merit Reporter
Certified Realtime Reporter
Delaware Notary Public