2009

Irving S. Braun v. Nevada Chemicals Inc. : Reply Brief

Utah Court of Appeals

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BEFORE THE UTAH COURT OF APPEALS

IRVING S. BRAUN, Individually and On Behalf of All Others Similarly Situated, Plaintiff, vs NEVADA CHEMICALS, INC., et al., Defendants.	Case No. 20090493-CA

APPELLANT'S REPLY BRIEF

ON APPEAL FROM THE THIRD JUDICIAL DISTRICT COURT
SALT LAKE COUNTY, STATE OF UTAH
HON. SANDRA N. PEULER
Civil No. 080919636

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INTRODUCTION

Defendants-appellees (collectively, "defendants") respond to this appeal with procedural roadblocks. They insist this Court lacks appellate jurisdiction due to the course of events in the trial court. No issue that plaintiff-appellant Irving Braun ("plaintiff") raises has been waived or forfeited, however. Defendants ignore that whether the case is direct or derivative implicates plaintiff's standing to sue. As such, this Court may examine the question apart from how it was resolved in the trial court.

Defendants try to thwart a substantive review because if the direct/derivative issue is considered on its merits, they cannot prevail. Though the legal point appears to be one of first impression here, all pertinent authority (from Utah and elsewhere, particularly Delaware) compels the conclusion this lawsuit is direct. It challenges breaches of fiduciary duty infecting a merger and that adversely affected the public shareholders, ultimately divesting them of ownership. It thus concerns a wrong to plaintiff and the proposed class, not a wrong to Nevada Chemicals, Inc. Precisely because the case challenges misconduct in the merger process – not just the price shareholders received – appraisal is not an exclusive or even sufficient remedy.

Contrary to defendants' suggestion, completion of the merger has not mooted this lawsuit. Even assuming a derivative action could no longer be brought, the shareholders may seek damages in a direct action (as in other civil litigation challenging past events). The dismissal must be reversed.

ARGUMENT

I. DEFENDANTS' PROCEDURAL OBJECTIONS LACK MERIT

Defendants focus on appellate procedure, claiming this Court cannot examine plaintiff's contentions on the merits. In staking out this position, the Brief of Appellees is, more than anything, a critique of how plaintiff chose to litigate the case below. Defendants fault not only the first document filed (the original complaint, framing the suit as direct) but also the last (the notice of appeal), and nearly everything plaintiff did in between. The sundry procedural theories miss the mark.

First, defendants suggest this Court has nothing to review because plaintiff "does not challenge the order from which he is appealing." (Brief of Appellees Nevada Chemicals, Inc., Oaktree Capital Management, L.P., Calypso Acquisition Corp., Cynaco Holding Corp., and OCM Principal Opportunities Fund IV, L.P. ("AB") at 1 (original emphasis deleted).) Asserting that plaintiff "does not contend that the trial court erred in entering the May 11, 2009 order," defendants say this circumstance "alone compels dismissal of this appeal or affirmance of the trial court's order." (AB at 1; *see also id.* at 18 (same contention).) Defendants' argument is a diversion. For purposes of appellate review, the May 2009 order is treated as a final judgment and by appealing from it, plaintiff may challenge all interlocutory acts of the trial court.

"'Notices of appeal are to be liberally construed'" in favor of the right to appeal. *State v. Valdovinos*, 2003 UT App 432, ¶ 17, 82 P.3d 1167, 1170 (citation omitted). All the notice must do is "designate the judgment or order, or part thereof, appealed from."

Utah R. App. P. 3(d). Of course, the judgment or order must have finality, but this hinges on its practical effect. There is no need for a separate piece of paper titled "Judgment." A final judgment or order is simply one that "ends the controversy between the parties litigant." *Salt Lake City Corp. v. Layton*, 600 P.2d 538, 539 (Utah 1979). "To be final, the trial court's order or judgment must dispose of all parties and claims to an action." *Bradbury v. Valencia*, 2000 UT 50, ¶ 10, 3 P.3d 649, 651.

Here, it is undisputed that the May 2009 order, from which plaintiff appealed, disposed of all parties and claims. It ordered the action "dismissed with prejudice upon the merits." (R.1150.) Accordingly, the May 2009 order constitutes the final judgment ending the action. Defendants do not contend otherwise. Instead, they cite off-point case law in which there was no final judgment from which an appeal could be taken – not the situation here. (AB at 19-20.)

Plaintiff certainly had the right to challenge the May 2009 order but, more than this, his appeal enables review of all that preceded the final judgment, including the trial court's handling of the direct/derivative issue. "'When an appellant files a notice of appeal from a final judgment, he may, in his opening brief, challenge all nonfinal prior orders and happenings which led up to that final judgment.'" *Davis v. Goldsworthy*, 2008 UT App 145, ¶ 8, 184 P.3d 626, 628 n.2 (citation omitted). As a federal decision phrased the concept, appealing from a final judgment "always covers the waterfront. The whole case is properly before us for decision." *Librizzi v. Children's Mem'l Med. Ctr.*,

134 F.3d 1302, 1306 (7th Cir. 1998) (Easterbrook, J.); *accord McBride v. CITGO Petroleum Corp.*, 281 F.3d 1099, 1104 (10th Cir. 2002).

In their second major procedural argument, defendants urge this Court to ignore the merits of the direct/derivative issue altogether. As they characterize the record, the trial court made only preliminary "oral remarks" on the subject at a hearing in October 2008. (AB at 2.) To be sure, the trial court did not issue a written ruling at that time on defendants' first motion to dismiss. Still, in dismissing the suit with prejudice on defendants' second dismissal motion, the court held that plaintiff "lacks standing" – a ruling he contests in this appeal. (R.1149.) In any event, the trial court's handling of the issue does not prevent this Court from deciding whether plaintiff's case is direct or derivative. The issue was and remains jurisdictional in nature for, as the trial court recognized, it implicates plaintiff's standing. As a result, this Court may consider the issue – irrespective of how it was resolved below.

Indeed, defendants cannot elude their own description of the issue, which echoes how the trial court framed it. In their first motion to dismiss, defendants challenged plaintiff's position that his suit was direct in nature. Their motion urged dismissal because "[p]laintiff lacks standing," the suit purportedly being "a classically derivative claim that belongs to Nevada Chemicals." (R.115.) Defendants returned to this contention repeatedly in their supporting memorandum. (R.119, 122, 123, 125.) They did not dispute that if plaintiff's case was actually direct, then he had standing to proceed.

Our Supreme Court instructs that "standing is jurisdictional." *Heath Tecna Corp. v. Sound Sys. Int'l, Inc.*, 588 P.2d 169, 170 (Utah 1978). Jurisdictional issues, such as standing, "can be raised at any time by either party or by the court." *Olson v. Salt Lake City Sch. Dist.*, 724 P.2d 960, 964 (Utah 1986). The rule is grounded on a wealth of precedent. *See also Jensen v. Utah Ry. Co.*, 270 P. 349, 362-63 (Utah 1927) (issues "relating to or involving jurisdiction" may be reviewed even when "on the record there were no adverse rulings which could be assigned as error").

In light of these established principles, defendants are wrong that events at the trial level control this Court's authority to examine the direct/derivative question. The jurisdictional essence of standing dictates that appellate review occurs unhindered by what happened in the lower court. *Cf. Californians for Disability Rights v. Mervyn's, LLC*, 138 P.3d 207, 213 (Cal. 2006) (analyzing standing for first time on appeal after law changed). Standing is generally not subject to waiver, forfeiture, acquiescence or estoppel because it goes to whether the court may hear the dispute at all. "In essence the question of standing is whether the litigant is entitled to have the court decide the merits of the dispute or of particular issues." *Warth v. Seldin*, 422 U.S. 490, 498 (1975). Put another way, although parties usually have a view on the subject, the court is ultimately "the exclusive judge of its own jurisdiction." *Miller v. USAA Cas. Ins. Co.*, 2002 UT 6, ¶ 18, 44 P.3d 663, 670. Just as "acquiescence of the parties is insufficient to confer jurisdiction," a litigant cannot disavow or abandon jurisdiction where it exists under the applicable law. *Olson*, 724 P.2d at 964.

Although conceding this appeal presents "questions of law" (AB at 3), defendants treat jurisdiction as though it turns on plaintiff's conduct. In response, and solely out of caution, plaintiff discusses briefly what the record in this case actually shows. It refutes defendants' contention that plaintiff willingly and deliberately gave up his direct action in favor of suing derivatively.

When defendants moved to dismiss plaintiff's original complaint pleading a direct action, he vigorously opposed. (R.507.) Contrary to defendants' description, plaintiff filed a new derivative complaint only after the trial court tipped its hand at oral argument that defendants' first motion to dismiss would be granted. At the October 2008 hearing, the court stated:

> I think number one, that the Motion to Dismiss is well taken. I think that the claim, if it's going to be brought, must be brought as a derivative action. So if I were to hear argument, and unless someone changed my mind for me this morning, which certainly could happen, I would be inclined to grant the Motion to Dismiss.

(R.1167, p. 12:11-17.)

After these remarks, plaintiff repeatedly stated that he wished to file an amended complaint only if defendants' first motion to dismiss was granted:

> [I]n the event the Court grants the Motion to Dismiss, we would ask, you know, that it be without prejudice, and that we'd be allowed the opportunity to file the complaint which would be a derivative complaint.
>
> * * *
>
> [A]s we tried to make clear in our papers . . . wanting to file the amended complaint would fall on the heels of the Court granting – in the event that the Court determined that our claims should [not] have been brought direct.

(R.1167, p. 15:16-20, p. 17:10-14.)

Although claiming it would listen with an open mind, the trial court had plainly telegraphed the outcome. The court even stated: "If you want to waive oral argument, I'll rule right now." (R.1167, p. 17:18-19.)

Rather than continuing this dialog, plaintiff opted to save both the parties and the trial judge time and effort by agreeing to file a new pleading by stipulation. (R.1167, p. 19:6-9.) Contrary to defendants' suggestion, the case was not "voluntarily dismisse[d]." (AB at 20.) Rather, as plaintiff explained:

> I think I'm intelligent enough to see that the tide is rolling against me on this issue. So we would – we'll enter the stipulation to file an amended complaint.

(R.1167, p. 19:6-9.)

Under the classic definition, still timely today, waiver requires an "intentional relinquishment or abandonment of a known right or privilege." *Johnson v. Zerbst*, 304 U.S. 458, 464 (1938). Here, it is apparent plaintiff did not "voluntarily" abandon his original complaint pleading a direct action, to the point of foregoing the issue for all time. He assented to filing a derivative complaint only when it became futile, in the face of judicial resistance, to push further for the direct action he initially sought to bring. In any event, apart from what happened below, this Court may consider the direct/derivative issue because, as explained, "standing is jurisdictional." *Heath Tecna Corp.*, 588 P.2d at 170.

II. PLAINTIFF'S CASE IS DIRECT, NOT DERIVATIVE

In their terse discussion of substance, defendants offer a broad and simplistic rule. They assert: "Utah law clearly states that a claim for breach of fiduciary duties by directors of a corporation belongs to the corporation, not to the individual shareholders, and that such a claim must be brought, if at all, as a derivative claim on behalf of the corporation." (AB at 28.)

Utah law, however, does not recognize a one-size-fits-all proposition, automatically treating breach of fiduciary duty as derivative no matter the circumstances. Indeed, to support their sweeping standard, defendants are forced to cull certain phrases in isolation from judicial decisions, untethered from the facts presented. (*See, e.g.*, AB at 28-29.) This selective approach disregards a time-honored admonition: "'[E]ach case is dependent upon and governed by its own facts, and whatever language or statements may be used or made in the cases must be considered with respect to and in view of the particular facts of the case.'" *Toomer's Estate v. Union Pac. R.R.*, 239 P.2d 163, 168 (Utah 1951).

Notably, defendants' Utah cases do not concern breach of fiduciary duty in the context of a merger, as here. (AB at 28-32.) By contrast, the cases plaintiff has cited all confront the direct/derivative issue on the same factual scenario and hold that where the validity of the merger process is challenged, the suit is direct. *See, e.g.*, *Parnes v. Bally Entm't*, 722 A.2d 1243, 1245 (Del. 1999) (a "stockholder who directly attacks the fairness or validity of a merger alleges an injury to the stockholders, not the

corporation"); *Cohen v. Mirage Resorts, Inc.*, 62 P.3d 720, 732 (Nev. 2003) (a "claim brought by a dissenting shareholder that questions the validity of a merger as a result of wrongful conduct on the part of majority shareholders or directors is properly classified as an individual or direct claim").

Defendants do not dispute that plaintiff attacks the overall validity of the merger and the concomitant failure to disclose material information to shareholders invited to tender their shares in the transaction. (R.1-15, ¶¶1, 4, 19, 34, 37.) In light of these allegations, and the case law actually addressing the direct/derivative distinction in the merger context, defendants are left to argue there is a "crucial distinction" between Utah and Delaware law. (AB at 29.) But, this is an area where there is simply a gap in Utah law, not a viable basis for distinguishing it from what Delaware has done. Defendants' cited Utah decisions do not illustrate a "distinction" as much as materially different situations where the claim was unquestionably derivative – generalized allegations of corporate mismanagement, misappropriation of corporate assets and/or corporate waste.[1]

Defendants' cases are not at odds with decisions such as *Parnes* and *Cohen* in the merger setting. Claims regarding corporate mismanagement and waste are viewed as

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[1] *See, e.g., Dansie v. Herriman*, 2006 UT 23, ¶ 11, 134 P.3d 1139, 1142-1144 (holding that allegations concerning the unlawful transfer by majority shareholder of the company's assets to itself are derivative in nature); *Warner v. DMG Color, Inc.*, 2000 UT 102, ¶ 10, 20 P.3d 868, 872-873 (finding claims concerning conversion of corporate assets, misappropriation of corporate assets, and fraudulent transfer and conveyance of corporate assets are derivative); *Richardson v. Arizona Fuels Corp.*, 614 P.2d 636, 639 (Utah 1980) (holding that allegations of misappropriation of the company's assets injure corporation only and therefore are derivative in nature).

"classically derivative" by nearly all jurisdictions, including Delaware. In *Big Lot Stores, Inc. v Bain Capital Fund VII, LLC*, 922 A.2d 1169 (Del. Ch. 2006), for example, the Delaware Court of Chancery noted that challenges to a merger transaction based on unfair price constitute a direct action because "the purportedly unfair price paid to the shareholders in the merger did not injure the corporation in the way that mismanagement or improper self-dealing does." *Id.* at 1181.

Defendants further assert that plaintiff's case cannot be direct because he "suffered no injury distinct from that of other shareholders of the corporation." (AB at 31.) Defendants, however, cite no authority requiring a plaintiff to aver injuries distinct from other shareholders. In its seminal en banc decision, the Delaware Supreme Court rejected as "confusing" and "inaccurate" the yardstick that defendants urge. *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1037 (Del. 2004). Although defendants ignore *Tooley* entirely, Delaware's ubiquity on corporate law is well established – to the point that defendants rely on Delaware authority when convenient.

In fact, the Utah authority cited by defendants states that a plaintiff seeking to bring a direct action must assert injuries that are "***distinct from the corporation***." *Warner*, 2000 UT 102, ¶ 13 (emphasis added). Here, the injuries that plaintiff has alleged are distinct from the corporation. *See Cohen*, 62 P.3d at 732 (holding that shareholder injuries resulting from an unfair merger process are "direct"); *Big Lot Stores*, 922 A.2d at 1181 n.54 (holding that shareholder injuries resulting from failure to disclose material

information in connection with merger are "direct" claims). Defendants do not argue otherwise.

For all these reasons, plaintiff's suit attacking the validity of the merger process was properly brought as a direct action. Because defendants make no valid argument to the contrary, the dismissal must be reversed.

III. APPRAISAL IS NOT PLAINTIFF'S EXCLUSIVE REMEDY

Finally, defendants contend the courthouse doors should be closed to Nevada Chemicals' former stockholders because the exclusive remedy on the facts here is appraisal. For this proposition, defendants cite *Bingham Consolidation Co. v. Groesbeck*, 2004 UT App 434, 105 P.3d 365. There, however, this Court instructed that shareholders may invoke the judicial system where "'fraud, misrepresentation, self-dealing, deliberate waste of corporate assets, or gross and palpable overreaching are involved.'" *Id.* at ¶ 30 (citation omitted). Defendants fail entirely to mention this Court's holding that "a claim of breach of fiduciary duty should be considered ***outside*** of the appraisal proceeding." *Id.* (emphasis added). Plaintiff's allegations fall squarely within this description. (R.1-15, ¶¶1, 4, 17, 19, 34, 37, 40-43; R.949-971, ¶6.)

Again attempting to recast the suit plaintiff brought, defendants insist that plaintiff's grievance "boils down to nothing more than a complaint about stock price." (AB at 22.) To support this characterization, defendants place great weight on the merger's completion. The closing of the transaction, they posit, moots plaintiff's request

for rescission, injunctive relief and supplemental disclosures – thereby leaving nothing to challenge except the share price. (AB at 22-25.)[2]

While perhaps superficially enticing, this argument is flawed. Defendants cite no authority suggesting a stockholder's standing to bring a direct action turns on relief not yet obtained based on a judgment not yet obtained. The type of relief available often narrows after suit is filed due to subsequent events, but this does not alter the basic character of the case. As discussed above, plaintiff challenges the entire merger process as unfair and invalid and alleges that defendants breached their fiduciary duties, by engaging in self-dealing and failing to disclose material information to shareholders when urging them to tender their shares. (R.1-15, ¶¶1, 4, 19, 34, 37.) Whatever relief plaintiff and other stockholders might eventually receive, this states a direct case, not a derivative one. *See Tooley*, 845 A.2d at 1033, 1039; *Parnes*, 722 A.2d at 1245; *Cohen*, 62 P.3d at 732.

The problem with defendants' position is that shareholders could never challenge the price in a merger transaction without being shoehorned into an appraisal proceeding. Stock price is nearly always a material consideration for shareholders, and its adequacy is often in dispute in litigation stemming from corporate acquisitions. Fundamentally, as the New Mexico Supreme Court observed, "'dissatisfaction with the price paid does not

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[2] Defendants' suggestion that plaintiff took no steps to obtain injunctive relief before the merger is irrelevant to any issue here, and false at any rate. Plaintiff filed a preliminary injunction motion but was forced to withdraw it after the trial court denied him access to needed discovery. (R.939.)

automatically convert the action to a simple demand for the "fair cash value" of a stockholder's shares.'" *McMinn v. MBF Operating Acquisition Corp.*, 164 P.3d 41, 46 (N.M. 2007) (citation omitted). In the Nevada Supreme Court's words, "the mere fact that [plaintiff's] complaint alleges that his stock was worth more than the amount he received under the merger does not constitute grounds for dismissing it under [the appraisal statute] so long as the complaint also contains allegations that the merger was approved through unlawful or fraudulent conduct." *Cohen*, 62 P.3d at 729.

Moreover, unlike the potential effect of a merger on a derivative lawsuit – often the loss of shareholder standing – completion of a merger does not bar a direct action outside an appraisal proceeding. A direct case like the one here may be pursued "even after the merger at issue has been consummated." *Parnes*, 722 A.2d at 1245. Although defendants preemptively try to shackle the judge's discretion on remand, the trial court is free to "fashion any form of equitable and monetary relief as may be appropriate" to remedy breaches of fiduciary duty by wayward corporate insiders. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 714 (Del. 1983).

Notwithstanding some of defendants' rhetoric, the abuses plaguing the financial markets for much of the past decade amply demonstrate the need for a judicial remedy when shareholders step up to challenge corporate malfeasance. Though defendants have

tried everything in this appeal to avoid it, plaintiff welcomes consideration of his direct complaint on its merits.[3]

CONCLUSION

For the reasons given, dismissal of this action was error and must be reversed.

DATED: January 20, 2010

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[3] On a related note, defendants present a partisan statement of facts that essentially seeks to adjudicate the merits of the case, despite their request for a procedural dismissal. (AB at 8-15.) Defendants' one-sided factual statement fails to take plaintiff's allegations as true as required on a motion to dismiss, and therefore should be disregarded. *See Krouse v. Bower*, 2001 UT 28, ¶¶ 1-3, 20 P.3d 895, 897.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this January 20, 2010, I caused true and correct copies of the foregoing **APPELLANT'S REPLY BRIEF** to be served via first-class United States Mail, postage prepaid, to the following:

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