2020 WL 1575750 (Del.Ch.) (Trial Motion, Memorandum and Affidavit)
Chancery Court of Delaware.

In re TERRAFORM POWER, INC., Stockholders Litigation.

No. 2019-0757-SG.
March 26, 2020.

Defendants' Opening Brief in Support of Motion to Dismiss and Stay

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Defendants Brookfield Asset Management, Inc. ("Brookfield"), Orion US Holdings 1 L.P. ("Orion"), Brookfield BRP Holdings (Canada) Inc. ("BRP"), Brian Lawson, Harry Goldgut, Richard Legault, Sachin Shah, and John Stinebaugh (together, "Defendants"), by and through their undersigned counsel, hereby respectfully submit this opening brief in support of their motion to dismiss the direct claims asserted in the operative complaint filed by Plaintiff City of Dearborn Police and Fire Revised Retirement System (Chapter 23) ("City of Dearborn" and, together with Plaintiff Martin Rosson, "Plaintiffs") in the above-captioned action pursuant to Court of Chancery Rules 12(b)(1) and 12(b)(6) and to stay the derivative claims pending the outcome of the Proposed Merger (defined below).

PRELIMINARY STATEMENT

This action involves quintessential stockholder derivative claims for breach of fiduciary duty, stemming from a sale of stock by Nominal Defendant TerraForm Power, Inc. ("TerraForm" or the "Company") to affiliates of Defendant Brookfield. In particular, Plaintiffs challenge a June 2018 transaction in which affiliates of Brookfield acquired $650 million of additional Class A common stock of the Company in a private placement (the "Private Placement"). Through the Private Placement, Brookfield's ownership stake in the Company increased from approximately 51% to approximately 65.3%. The Company used the proceeds from the Private Placement to fund a portion of a $1.2 billion acquisition of a Spanish company, Saeta Yield, S.A. (the "Saeta Transaction").

Plaintiffs purport to challenge the Private Placement both derivatively and directly. Under the Supreme Court's decision in *Tooley v. Donaldson, Lufkin & Jenrette, Inc.,* 845 A.2d 1031 (Del. 2004), the determination of whether a claim is derivative or direct focuses solely on (i) "who suffered the alleged harm (the corporation or the suing stockholders, individually)" and (ii) "who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)." [1] All of Plaintiffs' claims are derivative under this test. Indeed, dilution claims are "classically derivative." [2] So too are claims that a corporation received inadequate consideration for its stock: "if a board of directors authorizes the issuance of stock for no or grossly inadequate consideration, the corporation is directly injured and shareholders are injured derivatively." [3] Furthermore, a claim that "the corporation, by issuing additional stock for inadequate consideration, made the complaining stockholder's investment less valuable" is "not normally regarded as direct, because any dilution in value of the corporation's stock is merely the unavoidable result (from an accounting standpoint) of the reduction in the value of the entire corporate entity, of which each share of equity represents an equal fraction." [4]

Plaintiffs' Complaint attempts to side-step this analysis by alleging that "the Company *and* the Company's minority stockholders (through a reduction in economic value and voting power) have been damaged[,]" [5] presumably relying on *Gentile v. Rossette,* 906 A.2d 91 (Del. 2006). [6] But as former Chief Justice Strine recently explained in a concurring opinion in *El Paso Pipeline GP Co., L.L.C. v. Brinckerhoff,* 152 A.3d 1248 (Del. 2016), the *Gentile* decision "muddies the clarity of [Delaware] law in an important context," "is difficult to reconcile with traditional doctrine," and "cannot be reconciled with the strong weight of [Delaware] precedent"-and, therefore, "ought to be overruled." [7] Indeed, after *El Paso,* the question of "[w]hether *Gentile* is still good law is debatable." [8] For these reasons and those set forth below, Plaintiffs' direct claims should be dismissed. *See* Point I, *infra.*

It is important that the Court decide this issue at the pleadings stage because real-world developments are likely to affect Plaintiffs' standing to pursue any derivative challenge to the Private Placement. [9] In January 2020, an affiliate of Brookfield, Brookfield Renewable Partners L.P. ("Brookfield Renewable"), publicly proposed to acquire the outstanding shares of the Company not already owned by Brookfield and its affiliates (the "Proposed Merger"). On March 16, 2020, Brookfield Renewable and the Company announced that they had entered into a definitive merger agreement for Brookfield Renewable to acquire all of the outstanding shares of Class A common stock of the Company not already owned by Brookfield and its affiliates.

If the Proposed Merger is consummated in the third quarter of 2020 as expected, Plaintiffs will cease to be stockholders of the Company and, accordingly, will "lose[] standing to continue a derivative suit." [10] Thus, whether Plaintiffs' claims are derivative or direct is an issue of material importance to this case. It is in the interest of all parties to resolve this threshold legal question now, on the pleadings, before the parties undertake the costs and burdens of discovery and a potential trial on claims that Plaintiffs may soon lose standing to pursue.

For these reasons, Defendants also move to stay Plaintiffs' derivative claims pending consummation of the Proposed Merger. "[T]he power to stay [is] incident to the inherent power of a court to exercise its discretion to control the disposition of actions on its docket in order to promote economies of time and effort for the court, litigants, and counsel." [11] It is more efficient to permit the Proposed Merger process to conclude than to allow Plaintiffs to proceed to discovery on claims they may soon lose standing to pursue. In addition, there is no prejudice to Plaintiffs from a temporary stay of this litigation, brought in September 2019, challenging the June 2018 Private Placement. *See* Point II, *infra.*

NATURE AND STAGE OF PROCEEDINGS

On September 19, 2019, Plaintiff Martin Rosson filed his Verified Stockholder Derivative and Class Action Complaint for Breach of Fiduciary Duties in the action styled *Rosson v. Brookfield Asset Management, Inc.* (C.A. No. 2019-0757-SG) (Del. Ch.) (the "Rosson Action").

On October 14, 2019, Plaintiff City of Dearborn served a demand for books and records pursuant to 8 *Del. C.* § 220, in response to which the Company subsequently produced certain books and records pursuant to a confidentiality agreement containing a customary incorporation by reference clause. On January 27, 2020, City of Dearborn filed its Complaint in the action styled *City of Dearborn Police and Fire Revised Retirement System (Chapter 23) v. Brookfield Asset Management, Inc.* (C.A. No. 2020-0050-SG) (Del. Ch.) (the "City of Dearborn Action").

The Court ordered the consolidation of the Rosson Action and the City of Dearborn Action on February 13, 2020 in the consolidated action styled *In re Terraform Power, Inc. Stockholders Litigation* (Consol. C.A. No. 2019-0757-SG) (Del. Ch.) (the "Consolidated Action") and appointed Plaintiffs Rosson and City of Dearborn as Lead Plaintiffs and their counsel as Co-Lead Counsel (Dkt. 19). With this brief, Defendants move to dismiss Plaintiffs' direct claims and to stay litigation of Plaintiffs' derivative claims pending the outcome of the Proposed Merger.

FACTUAL BACKGROUND [12]

A. *The Parties*

Plaintiffs Martin Rosson and City of Dearborn allege that they are stockholders of TerraForm. [13]

Nominal Defendant TerraForm is a publicly traded Delaware corporation with its principal place of business in New York City, and it "acquires, owns and operates solar and wind assets in North America and Western Europe." [14]

Defendant Brookfield is a Canadian corporation with its principal executive offices in Toronto. [15] Brookfield is an alternative asset manager. [16] Defendants Orion, a Delaware limited partnership, and BRP, a Canadian corporation, are affiliates of Brookfield. [17]

Defendants Brian Lawson, Harry Goldgut, Richard Legault, and Sachin Shah are senior executives of Brookfield and four of the seven members of the Company's Board of Directors (the "Board"). [18] Under the Company's Amended and Restated Certificate of Incorporation (the "Charter"), Brookfield has the right to designate four directors for nomination to the Board. [19]

Defendant John Stinebaugh is also an executive of Brookfield and has been appointed to serve as the Company's Chief Executive Officer ("CEO") pursuant to a 2017 Governance Agreement between the Company and Brookfield. [20]

B. *Background Of Brookfield's Investment In the Company*

In January 2014, the Company was formed as a subsidiary of SunEdison, Inc. ("SunEdison"). [21] In July 2014, the Company completed an initial public offering, which resulted in SunEdison holding equity representing approximately 91% of the Company's voting power. [22] In connection with the offering, the Company entered into a contractual sponsorship arrangement with SunEdison to provide management and administrative services. [23] In April 2016, SunEdison filed for bankruptcy. [24]

In March 2017, SunEdison sold its controlling stake in the Company to Brookfield. The Company entered into a Transaction Agreement with Brookfield pursuant to which Orion and BRP acquired approximately 51% of the Company's outstanding shares of Class A common stock in a merger transaction (the "Original Merger"). [25] In October 2017, the Company's stockholders approved the Original Merger, which closed on October 16, 2017. [26] As a result of the Original Merger, Brookfield became the Company's majority stockholder. [27]

In connection with the Original Merger, Brookfield entered into several agreements with the Company pursuant to which Brookfield acts as the Company's "sponsor." [28] Each of these agreements was negotiated as part of the Original Merger and was approved by the Company's stockholders. [29] Pursuant to a Master Services Agreement, Brookfield provides certain management and administrative services to the Company and has the right to designate the Company's CEO, Chief Financial Officer, and General Counsel. [30] A Governance Agreement requires that the Company's Board have a "Conflicts Committee" comprising three directors not designated by Brookfield. [31] Pursuant to its charter, the Conflicts Committee is responsible for, among other things, reviewing and approving material transactions in which a potential conflict may exist between the Company and Brookfield. [32]

Under the Company's Charter, Brookfield has the right, as long as it retains more than 50% of the Company's Class A common stock, to designate four directors for inclusion in the Board's slate of nominees for director elections. [33] The other three directors of the Company's seven-member [34] Board must be independent and nominated by the Company's Governance Committee after consulting and considering in good faith the views of the entire Board. [35] Under the Governance Agreement, Brookfield is required to vote its common shares in favor of the nominated independent directors in the same proportion as voted by the minority shares. [36] The Company's Charter also contains a supermajority voting provision, requiring an affirmative vote of at least 66-2/3% of the outstanding shares of common stock to amend any of the Charter provisions regarding Class A common stock voting rights, director exculpation and indemnification, removal of directors, or the supermajority requirement itself. [37]

C. *The Company's Proposed Acquisition Of Saeta Yield And The Private Placement*

In January 2018, the Company approved a potential acquisition of Saeta, an owner and operator of wind and solar energy assets. [38] The Company initially anticipated that acquiring Saeta would cost approximately $1.2 billion and would be funded with a combination of "approximately $600-700 million" in new equity and the rest in debt. [39]

In connection with the Saeta transaction, Brookfield agreed that it would purchase a pro rata interest in the newly issued Company Class A shares issued in connection with the funding of Saeta (51%) as well as any other shares not acquired by the public market as a "backstop" to a public offering. [40] Brookfield and the Company memorialized this agreement in a "Support Agreement," which was reviewed and approved by the Company's Conflicts Committee. [41] The Support Agreement specified that the share price of the backstop, if necessary, would be equal to the 5-day volume weighted average price prior to the announcement of the Saeta transaction. [42] This yielded a price of $10.66 per Company Class A share. [43]

On June 4, 2018, the Company's Conflicts Committee approved exercising the backstop in full, [44] and, the next day, the Company announced that it was exercising the backstop and would sell $650 million of Class A common stock to Brookfield in the Private Placement. On June 7, 2018, the Board approved the sale to Brookfield of 60,975,609 shares of Company Class A common stock at a price of $10.66 per share. [45] As planned, the Company used the approximately $650 million it received in proceeds from the Private Placement to fund a portion of its $1.2 billion acquisition of Saeta. [46] The Private Placement increased Brookfield's voting interest from approximately 51% to approximately 65.3% and increased Brookfield's equity interest in the Company's shares by the same amount. [47]

D. *Brookfield Proposes To Acquire The Rest Of the Company*

On January 11, 2020, an affiliate of Brookfield, Brookfield Renewable, delivered an unsolicited, non-binding proposal to acquire all of the Company's outstanding shares not currently held by Brookfield and its affiliates in a stock-for-stock transaction. [48] The Proposed Merger contemplated an exchange ratio of 0.36x that valued the Company's stock at $17.31 per share, representing an approximately 11% premium to the Company's closing price on January 10, 2020. [49] The Proposed Merger was structured to satisfy the requirements of *Kahn v. M & F Worldwide Corp.,* 88 A.3d 635 (Del. 2014) and was conditioned on approval by both a duly empowered special committee of independent Board members and stockholders holding a majority of the outstanding shares of the Company's Class A common stock not held by Brookfield and its affiliates. [50]

On January 13, 2020, the Company publicly announced that it had received the Proposed Merger and formed a special committee of non-executive, independent directors (the "Special Committee") that would retain advisors, review the Proposed Merger, and independently determine the course of action it believed to be in the best interests of the Company's stockholders. [51]

On March 16, 2020, Brookfield Renewable and the Company announced that they had entered into a definitive merger agreement for Brookfield Renewable to acquire all of the outstanding shares of Class A common stock of the Company, other than the approximately 62% owned by Brookfield and its affiliates. [52] Under the terms of the Proposed Merger, each share of Class A common stock of the Company will be acquired for consideration equivalent to 0.381 of a Brookfield Renewable unit. [53] For each share of the Company's Class A common stock held, the Company's public stockholders will be entitled to receive, at their election, either Class A shares of Brookfield Renewable Corporation ("BEPC"), a subsidiary of Brookfield Renewable, or limited partnership units of Brookfield Renewable. [54] The Special Committee unanimously recommended that the Company's stockholders approve the Proposed Merger. [55]

If the Proposed Merger closes, the Company's current stockholders will become, at their election, stockholders of BEPC or unitholders of Brookfield Renewable. [56]

E. *Plaintiffs' Claims Regarding The Private Placement*

On September 9, 2019, Plaintiff Rosson filed a complaint asserting two counts for breach of fiduciary duty, brought derivatively and directly, against Brookfield, Orion, and BRP with respect to the Private Placement. No individual directors or officers of Brookfield or the Company were named as defendants in the original complaint.

On January 27, 2020, subsequent to the Merger Proposal, Plaintiff City of Dearborn filed a complaint asserting three counts for breach of fiduciary duty, also brought derivatively and directly. Count I purports to assert direct and derivative claims for breach of fiduciary duty against Brookfield, Orion, and BRP as the Company's allegedly controlling stockholders. [57] Count II purports to assert direct and derivative claims for breach of fiduciary duty against Messrs. Lawson, Goldgut, Legault, and Shah, the four Brookfield representatives on the Company's Board. [58] Count III purports to assert direct and derivative claims for breach of fiduciary duty against Mr. Stinebaugh as the Company's CEO. [59] The independent directors on the Company's Conflicts Committee who approved the Private Placement were not named as defendants. The two actions have been consolidated, and the City of Dearborn complaint has been designated the operative Complaint. [60]

Plaintiffs allege that the Private Placement was unfair to the Company and its stockholders because, among other things, cheaper and less dilutive financing alternatives were allegedly available to the Company and because the $10.66 per share price Brookfield paid in the Private Placement was allegedly unfair. [61] Plaintiffs also contend that the Private Placement "solidified" Brookfield's control of the Company and "facilitates" Brookfield's effective elimination of a 66-2/3% stockholder vote condition in the Company's Charter with respect to provisions regarding stock voting and dividend rights, liquidation, director indemnification, removal of directors, and the 66-2/3% stockholder vote condition itself. [62] Defendants deny that the Private Placement was unfair. In any event, Plaintiffs' direct claims should be dismissed for the following reasons.

ARGUMENT

Dismissal should be granted pursuant to Rule 12(b)(6) when a complaint does not allege facts that, if proven, would entitle the plaintiff to relief. [63] While the Court must "accept as true all of the well-pleaded allegations of fact" and "draw reasonable inferences in the plaintiffs favor," the Court "is not... required to accept as true conclusory allegations without specific supporting factual allegations." [64] Additionally, the Court must "accept only those reasonable inferences that logically flow from the face of the complaint and is not required to accept every strained interpretation of the allegations proposed by the plaintiff." [65]

I. *PLAINTIFFS LACK STANDING TO CHALLENGE THE PRIVATE PLACEMENT DIRECTLY BECAUSE PLAINTIFFS' CLAIMS ARE ENTIRELY DERIVATIVE.*

It is fundamental that, if a plaintiff lacks standing, its suit must be dismissed. [66] Standing is a "threshold question" that "refers to the right of a party to invoke the jurisdiction of a court to enforce a claim or to redress a grievance." [67] Although a stockholder need not retain its stock to assert direct claims, under the continuous ownership rule, "[a] plaintiff who ceases to be a shareholder, whether by reason of a merger or for any other reason, loses standing to continue a derivative suit." [68] Accordingly, in the merger context, whether a claim is direct or derivative may be case-dispositive. Here, this issue is dispositive of the litigation because consummation of the Proposed Merger would eliminate Plaintiffs' standing to prosecute their derivative claims.

A. *Plaintiffs' Claims Are Exclusively Derivative Under Tooley*

Under *Tooley,* the determination of whether a claim is derivative or direct "turn[s] *solely* on the following questions: (1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of the recovery or other remedy (the corporation or the stockholders, individually)?" [69] "To answer the question[s], the reviewing court must look to the body of the complaint and consider the nature of the wrong alleged and the relief requested." [70] *Tooley's* "simple analysis is well imbedded in [Delaware's] jurisprudence." [71]

Before the Supreme Court's decision in *Tooley,* Delaware courts generally applied "confusing propositions [that] encumbered [Delaware] caselaw governing the direct/derivative distinction." [72] In *Tooley,* the Supreme Court jettisoned these "amorphous," "confusing," and "inaccurate" concepts in favor of injury and recovery inquiries intended to be "clear, simple and consistently articulated and applied by [Delaware] courts." [73] Accordingly, this Court should not deviate from *Tooley's* logical and easy-to-apply analytical framework.

Under that framework, Plaintiffs' claims clearly are exclusively derivative. Here, the injury component of the Complaint is that "the *Company* and the Company's minority stockholders (through a reduction in economic value and voting power) have been damaged" [74] because the $10.66 per share price that Brookfield paid in the Private Placement was allegedly too low and, thus, unfair to the Company. [75] The primary relief that Plaintiffs seek is rescissory damages on behalf of the Company-i.e., for the Company to be paid the "fair value" of the stock sold in the Private Placement. [76] "As the majority opinion [in *El Paso]* makes clear, a claim that an entity has issued equity for inadequate consideration-a so-called dilution claim-is a quintessential example of a derivative claim." [77]

B. *The Gentile Decision Unnecessarily Complicated The "Simple Analysis" Of Tooley*

Two years after deciding *Tooley,* the Supreme Court was called upon to apply *Tooley's* "simple analysis" with respect to "a self-dealing transaction in which the CEO/controlling stockholder forgave the corporation's debt to him, in exchange for being issued stock whose value allegedly exceeded the value of the forgiven debt." [78] The issue of whether the claim was derivative or direct was potentially dispositive of the case because, after the self-dealing transaction, the corporation was acquired by a third party and the plaintiffs no longer had derivative standing. [79]

In reciting the applicable law, the Supreme Court in *Gentile* recognized that "[n]ormally, claims of corporate overpayment are treated as causing harm solely to the corporation and, thus, are regarded as derivative" because "the corporation is both the party that suffers the injury (a reduction in its assets or their value) as well as the party to whom the remedy (a restoration of the improperly reduced value) would flow." [80] The *Gentile* opinion further recognized that "[s]uch claims are not normally regarded as direct, because any dilution in value of the corporation's stock is merely the unavoidable result (from an accounting standpoint) of the reduction in the value of the entire corporate entity, of which each share of equity represents an equal fraction"-and "[i]n the eyes of the law, such equal 'injury' to the shares resulting from a corporate overpayment is not viewed as, or equated with, harm to specific shareholders individually." [81]

In a departure from *Tooley's* "simple analysis," however, *Gentile* then endorsed "at least one transactional paradigm -- a species of corporate overpayment claim -- that Delaware case law recognizes as being both derivative and direct in character":

A breach of fiduciary duty claim having this dual character arises where: (1) a stockholder having majority or effective control causes the corporation to issue "excessive" shares of its stock in exchange for assets of the controlling stockholder that have a lesser value; and (2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling stockholder, and a corresponding decrease in the share percentage owned by the public (minority) shareholders. Because the means used to achieve that result is an overpayment (or 'over-issuance') of shares to the controlling stockholder, the corporation is harmed and has a claim to compel the restoration of the value of the overpayment. That claim, by definition, is derivative.

But, the public (or minority) stockholders also have a separate, and direct, claim arising out of that same transaction. Because the shares representing the 'overpayment' embody both economic value and voting power, the end result of this type of transaction is an improper transfer -- or expropriation -- of economic value and voting power from the public shareholders to the majority or controlling stockholder. For that reason, the harm resulting from the overpayment is not confined to an equal dilution of the economic value and voting power of each of the corporation's outstanding shares. A separate harm also results: an extraction from the public shareholders, and a redistribution to the controlling shareholder, of a portion of the economic value and voting power embodied in the minority interest. As a consequence, the public shareholders are harmed, uniquely and individually, to the same extent that the controlling shareholder is (correspondingly) benefited. In such circumstances, the public shareholders are entitled to recover the value represented by that overpayment -- an entitlement that may be claimed by the public shareholders directly and without regard to any claim the corporation may have. [82]

Under this framework applicable to a corporate overpayment to a controlling stockholder, the *Gentile* opinion recognized that the plaintiffs had direct standing to pursue the corporate overpayment claim against the controller and to receive a direct damages award, amounting to "the value represented by [the corporate] overpayment." [83]

C. *Gentile Should Be Overruled*

1. *There is No Principled Reason to Grant Direct Standing Solely in the Controlling Stockholder Context*

Almost immediately after *Gentile* was decided, courts "struggled with how to interpret *Gentile* and its potential to undercut the traditional characterization of stock dilution claims as derivative." [84] "Early understandings of *Gentile* ... assumed that direct standing was only available in circumstances in which there was a controlling stockholder or, by implication, a functionally equivalent control group." [85] This was an understandable reading of *Gentile,* since it was not the "voting power" component of a dilution claim that had caused the Court to find direct standing-indeed, all dilution claims necessarily involve some level of dilution of voting power-but, rather, the presence of a controlling stockholder who was allegedly using its control to "expropriate" value and voting power from the minority. [86]

As subsequent courts explained, however, if *Gentile* was correctly decided, "the core insight of dual injury" [87] under *Gentile* should logically extend to any situation "when defendant fiduciaries (i) had the ability to use the levers of corporate control to benefit themselves and (ii) took advantage of the opportunity." [88] In other words, as a matter of doctrine, *Gentile* should then also "appl[y] to non-controller issuances in which insiders participate." [89] Accordingly, in *Carsanaro v. Bloodhound Technologies, Inc.,* the Court found direct standing in connection with dilutive venture capital financings in which directors and affiliated funds participated. [90] Similarly, in *In re Nine Systems Corp. Shareholders Litigation,* which found direct standing with respect to a dilutive recapitalization transaction in which the directors and their affiliated funds participated, the Court stated that "it makes little sense to hold a controlling stockholder to account to the minority for improper expropriation after a merger but to deny standing for stockholders to challenge a similar expropriation by a board of directors after a merger" given that "Delaware law endows the board -- not a controller -- with the exclusive authority to manage and direct the corporation's business affairs," including "the power to issue stock." [91]

Likewise, this Court's *El Paso* decisions [92] further expanded the type of corporate overpayment claim that could be brought directly (an expansion that was later overruled by the Supreme Court). [93] In particular, in *El Paso,* this Court determined that a corporate overpayment claim brought on behalf of a partnership against the partnership's general partner and controller could be pursued "dually" or directly. [94] Following the partnership's merger with its parent company, the partnership's limited partners no longer owned partnership units and accordingly lost standing to pursue their claims derivatively under the continuous ownership rule. [95] After a trial in which the general partner was found to have acted in bad faith and to have caused the partnership to overpay for assets it acquired from the parent company, the limited partners attempted to convert the derivative overpayment award of damages-amounting to $171 million-to a direct, *"pro rata* recovery" on behalf of the former limited partners. [96] Among other rulings, this Court relied on *Gentile* and held that the claim could be pursued either "dually" or directly, given that the controlling parent company had expropriated economic value from the public unitholders. [97] This Court further held that the damages award, which was based on the harm to the partnership from overpaying for the assets in the challenged transaction, be paid directly to a class of the former limited partners. [98]

The Supreme Court disagreed and reversed, holding that the *Tooley* analysis governed and that the corporate overpayment claim was derivative because: (i) the partnership was harmed by the challenged transaction; and (ii) the partnership would accordingly be entitled to any recovery. [99] Importantly, the challenged transaction in *El Paso* did *not* fall squarely under the *Gentile* paradigm. As the Supreme Court recognized, the alleged dilution-an "expropriation of economic value to a controller [that] was not coupled with any voting rights dilution"-did "not satisfy the unique circumstances presented by the *Gentile* 'species of corporate overpayment claim[s].' " [100] Accordingly, the *El Paso* defendants did not have any reason to argue that *Gentile* should be overruled, the question presented in the instant case was not briefed for the Supreme Court, and the Supreme Court had no cause to overrule *Gentile* at that time. The Supreme Court nevertheless explicitly "decline[d] the invitation to further expand the universe of claims that can be asserted 'dually.' " [101] To do so, the Supreme Court reasoned, "would deviate from the *Tooley* framework and largely swallow the rule that claims of corporate overpayment are derivative." [102]

The Supreme Court's ruling in *El Paso* not to extend *Gentile* "was not made lightly"; "[t]o the contrary, the ruling resulted in the reversal of a $171 million judgment for damages ... in what the high court described as a 'troubling case.' " [103] The implications of *El Paso* were also significant: the Supreme Court not only "implicitly rejected the reasoning of decisions such as *Carsanaro* and *Nine Systems,* which had extended *Gentile* to any dilutive issuance approved by a conflicted board," but also led this Court to conclude that *"Gentile* must be limited to its facts." [104] Accordingly, since *El Paso,* the Court of Chancery "has exercised caution in applying the *Gentile* framework." [105]

However, as this Court observed in *Sciabacucchi v. Liberty Broadband Corporation,* 2018 WL 3599997 (Del. Ch. July 26, 2018), "limiting *Gentile* to controller situations, rather than expanding it to conflicted board non-controller dilution cases, *or* *overruling it entirely,* is, as a matter of doctrine, unsatisfying."[106] There is simply no principled reason to allow "dilution" or overpayment claims to proceed directly against controllers when the Court rightly refuses to permit such claims to proceed directly in other contexts. Given that the Supreme Court has already refused to apply *Gentile* to the conflicted board scenario (and is unlikely to revisit the issue), the Supreme Court should jettison *Gentile* altogether.

2. *Gentile Contradicts Long-Standing Case Law That A Derivative Harm May Not Be Recovered Directly By Stockholders*

An additional doctrinal defect of *Gentile* is that it allows an asset that belongs to the corporation (a derivative claim and attendant damages award) to be transferred to third parties (the unaffiliated stockholders) for no consideration. As the *Gentile* opinion acknowledged, dilution claims stemming from corporate sales of stock have long been considered derivative claims.[107] Before *Gentile,* courts had overwhelmingly held that economic harms stemming from dilutive transactions were derivative, including in the controlling stockholder context. For example, *Behrens v. Aerial Communications Inc.,* 2001 WL 599870 (Del. Ch. May 18, 2001), which *Gentile* explicitly rejected, rightly held that all stockholders, including a controller, suffer economic dilution when a company is alleged to have issued shares to a controlling stockholder at an unfairly low price.[108] Even *post-Gentile,* this Court has accepted the reality that economic dilution is fundamentally derivative in nature-leading to further cabining of *Gentile.*[109]

Expressed in *Tooley* terms, the reason that dilution claims are traditionally classified as derivative is because the corporation is the party that suffers the injury (inadequate value), and the corporation is also the party to whom the remedy (a repayment to the entity of the amounts overpaid) would flow.[110] Because the corporation is the party injured by the overpayment, any damages recovery should logically revert to the corporation to remedy that overpayment.[111] The *Gentile* decision, however, allowed the stockholders to recover a damages award belonging to the corporation.

The only way to reconcile the Supreme Court's decisions in *Gentile,* which allowed direct and derivative standing, and *El Paso,* which allowed only derivative standing, is that the "voting power" of the public stockholders in *Gentile* was also impacted by the alleged transaction.[112]

Where Delaware courts have found direct rather than derivative claims in the context of corporate equity issuances, such findings have usually turned on a controller's dilution of minority stockholders' voting rights.[113] However, when a company issues equity to a controlling stockholder in exchange for adequate value, the minority stockholders suffer no cognizable harm even though their voting interests are diluted.[114] Even where a company issues equity to a controlling stockholder for inadequate value, the voting power of the minority stockholders is over-diluted *only to the extent that the corporation suffers economic harm* (by virtue of the controller's underpayment) because the company's harm and the minority's over-dilution are inseparable.

Accordingly, a claim for voting power dilution should be treated by the courts as derivative for two reasons. First, in order to state a direct claim, "[t]he stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation."[115] If the stockholder's voting power dilution claim depends on proving an economic harm to the corporation, this showing would not be possible. Second, the recovery (either in the form of cancellation of some shares issued to the controller or payment by the controller to the company to compensate it for the fair value of the shares issued) would more properly go to the corporation, not the stockholders.[116] Applying a simple, clear rule-like the one articulated by the Supreme Court in *Tooley* would save both litigants and the judiciary time and expense.[117]

The fact that a controller's relative voting power increases does not mean that an economic harm to the *company,* which harm would logically be redressed via a payment to the company, should be converted to a claim belonging to the individual unitholders. A plaintiff cannot rely on the harm an entity suffered to meet its burden to show harm to the investors "individually."[118] Indeed, a damages award that reflects harm to the entity *does not* establish damages for a plaintiff's direct claim. [119] Given that the predicate for a direct claim is a separate injury to the investors, it follows that a plaintiff must therefore plead a separate injury. Likely for this reason, some cases prior to *Tooley* recognized standing to sue directly for injunctive or equitable relief (for example, to cancel the voting rights of improvidently issued shares), but did *not* recognize any right of holders to receive an economic recovery that would otherwise go to the corporation. [120] But the *Gentile* opinion effectively allowed individual stockholders to convert (for no consideration) a corporate overpayment claim, which is an asset belonging to the corporation, into an individual claim. This is inconsistent with a long line of cases holding that a “pro rata recovery” of a derivative claim is wholly inappropriate. [121]

3. Gentile Risks a Double-Recovery And Complicates Real-World Commercial Transactions

Aside from the doctrinal issues discussed above, there are practical consequences to the *Gentile* rule which make clear that the case was wrongly decided and should be overruled. Put simply, the rule is unruly in practice because it allows two separate parties-a corporation and its current or former stockholders-to pursue the exact same judicial recovery.

Although derivative claims always involve some struggle for control over the suit between the corporation's board and its stockholders, important rules have developed over time to balance the competing interests of investors with the board's statutory authority to govern the corporation. [122] These rules include the contemporaneous ownership rule, [123] the continuous ownership rule, [124] the demand requirement, [125] pleading burdens for alleging demand futility, [126] and rules governing special litigation committees. [127] But when stockholders are allowed to pursue the exact same judicial recovery as the corporation, that careful balance is thrown into disarray. [128] It is not clear who-between the corporation and its stockholders (current or former)-has the right to recover.

By way of example, in the context of a claim against a controlling stockholder where the board appoints a special litigation committee to consider whether to bring litigation on the corporation's behalf, if each of the committee and the company's stockholders seek to litigate (and, ultimately, recover) on the same overpayment claim, who has the superior right to payment? They both cannot recover, as that would impose a double penalty on the controlling stockholder.

Gentile did not expressly grapple with this problem, but simply supposes that any such claim could be brought *either* directly or derivatively, [129] perhaps suggesting that it could be pleaded in the alternative and then addressed through an election of remedies. [130] But that rubric breaks down when there are two distinct groups-the corporation and its current or former stockholders-jockeying to receive the same economic recovery.

The double recovery problem becomes even more stark in the context of a merger transaction with a third party. In that scenario, derivative claims pass to the corporation's new owner as an asset of the company by operation of law, [131] and the new owner has the right to determine whether to pursue the claims. [132] In the event that both the new owner and the corporation's former stockholders each want to litigate the claims, who has the right to recover? Do the parties race to trial and judgment? Do they consolidate and hope for a global resolution that will likely make neither of them completely whole? [133]

These are impossible questions to answer under *Gentile,* and they are impossible questions to answer in real time, in the marketplace, and by M&A practitioners. [134] A buyer of a company can never know exactly what it is buying if there is a “dual-claim” belonging to the company. Putting aside the merits of the claim, a buyer cannot know whether it, or the stockholders of the counterparty, will have the right to assert that claim after the transaction closes. The market relies on the consistent interpretation of Delaware law, but the *Gentile* rule creates great uncertainty for purchasers as to what post-closing rights and liabilities they actually obtain in a merger.

In short, the *Gentile* framework has caused doctrinal confusion and reintroduced guesswork to an area of law that the Supreme Court has sought to govern by a "standard" that would be "clear, simple and consistently articulated and applied by [Delaware] courts." [135] *Gentile* fractures that foundation, [136] and undermines Delaware's goal of "promoting reliable and efficient corporate and commercial laws." [137] Thus, in addition to its doctrinal deficiencies, *Gentile* should be overruled because the practical uncertainties it creates cause friction in the market for corporate control, impede price certainty, and complicate deal-making for Delaware-incorporated entities.

4. *There Is No "Gap" for Gentile to Fill*

Finally, *Gentile* should be overruled for the simple reason that it is unnecessary. As former Chief Justice Strine stated, "there is no gap in our law for *Gentile* to fill." [138] The law "already accords a direct claim to stockholders when a transaction shifts control of a company from a diversified investor base to a single controlling stockholder[,]" [139] and further subjects such transactions to "enhanced scrutiny" under *Revlon.* [140] And, to the extent derivative standing is extinguished by merger under the continuous ownership rule, a stockholder who loses derivative standing as a result of such a merger is free to challenge that merger on the basis that the selling company's board failed to obtain value for such claims. [141] The fact that a merger may cancel the stockholder's standing to pursue a derivative remedy should not-and does not-change the analysis. Derivative standing rules should not be twisted to escape the application of the continuous ownership rule, a bedrock principle of Delaware law. [142]

In sum, former Chief Justice Strine was correct: *"Gentile* cannot be reconciled with the strong weight of [Delaware] precedent and it ought to be overruled." [143] It has already been noted, in light of former Chief Justice Strine's concurrence in *El Paso,* that "[w]hether Gentile is still good law is debatable," [144] that "[t]he viability of this doctrine has been called into doubt," [145] and that "there is reason to question whether *Gentile* will remain the law of Delaware." [146] Defendants therefore respectfully submit that Plaintiffs' challenge to the allegedly dilutive Private Placement be held exclusively derivative under *Tooley's* "simple analysis."

II. *PLAINTIFFS' DERIVATIVE CLAIMS CHALLENGING THE PRIVATE PLACEMENT SHOULD BE STAYED PENDING THE OUTCOME OF THE PROPOSED MERGER*

"This Court possesses the inherent power to manage its own docket, including the power to stay litigation on the basis of comity, efficiency, or simple common sense." [147] Court of Chancery Rule 26(c) also authorizes the Court to stay discovery "for good cause shown." [148]

Plaintiffs cannot dispute that consummation of the Proposed Merger would deprive them of their standing to challenge the Private Placement derivatively. [149] It is thus efficient and sensible to stay Plaintiffs' derivative claims, which are in their infancy, while the Proposed Merger process unfolds. A stay would not prejudice Plaintiffs but would beneficially avoid subjecting the parties to the potentially wasteful costs and burdens of discovery on claims that Plaintiffs may soon lose standing to pursue.

Courts have ordered stays in analogous circumstances where future events may significantly impact the litigation. In *In re Straight Path Communications Inc. Consolidated Stockholder Litigation,* 2017 WL 5565264 (Del. Ch. Nov. 20, 2017), this Court acknowledged its "inherent authority to stay" a matter "where ... litigants' efficiency so requires" and stayed the case pending the outcome of a proposed merger rather than issue an "advisory opinion" on the viability of direct and derivative claims concerning the merger. [150] Similarly, in *Salberg v. Genworth Financial, Inc.,* 2017 WL 3499807 (Del. Ch. July 27, 2017), a books and records action concerning a proposed merger involving Genworth Financial, Inc., it was appropriate to hold in abeyance a decision on a pending motion to dismiss in a related derivative action brought on behalf of Genworth because of the merger proposal. [151]

It would be highly inefficient and wasteful for the parties to litigate Plaintiffs' derivative claims in the shadow of the Proposed Merger. If the Proposed Merger is not approved by the TerraForm stockholders, then Plaintiffs may continue to pursue their derivative claims. But, if the Proposed Merger is approved and closes, then the costs and burdens of discovery on Plaintiffs' derivative claims would be for naught. Plaintiffs, who did not bring these derivative claims until more than a year after TerraForm disclosed the Private Placement, would not be prejudiced by such a stay. "As this court has held before, loss of standing to bring a derivative action is not irreparable harm." [152]

CONCLUSION

For the reasons set forth above, Defendants respectfully submit that Plaintiffs' claims are exclusively derivative and, thus, Plaintiffs' direct claims should be dismissed pursuant to Rule 12(b)(6).

Because the continuing viability of *Gentile* is a substantial issue of material importance to this case, Plaintiffs standing to challenge the Private Placement should be resolved on the pleadings, including, if necessary, via an interlocutory appeal.

Defendants further submit that Plaintiffs' derivative claims regarding the Private Placement should be stayed pending the consummation of the Proposed Merger.

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Footnotes

1 845 A.2d at 1033.

2 *El Paso Pipeline GP Co., L.L.C. v. Brinckerhoff,* 152 A.3d 1248, 1261 (Del. 2016).

3 *In re J.P. Morgan Chase & Co. S'holder Litig.,* 906 A.2d 808, 818 (Del. Ch. 2005), *aff'd,* 906 A.2d 766 (Del. 2006).

4 *Feldman v. Cutaia,* 951 A.2d 727, 732 (Del. 2008) (internal quotation marks omitted).

5 Verified Stockholder Derivative and Class Action Complaint (the "Complaint" or "Compl.") (C.A. No. 2020-0050-SG, Dkt. 1; C.A. No. 2019-0757-SG Dkt. 17) at ¶ 135 (emphasis added).

6 906 A.2d at 99-100.

7 152 A.3d at 1265-66 (Strine, C.J. concurring).

8 *ACP Master, Ltd. v. Sprint Corp.,* 2017 WL 3421142, at *26 n.206 (Del. Ch. July 21, 2017, corrected Aug. 8, 2017), *aff'd,* 184 A.3d 1291 (Del. 2018) (Table); *see also Sciabacucchi v. Liberty Broadband Corp.,* 2018 WL 3599997, at *10 n.147 (Del. Ch. July 26, 2018) (current state of the law with respect to *Gentile* "is, as a matter of doctrine, unsatisfying.").

9 "Standing is a threshold question that must be answered by a court affirmatively[.]" *Dover Historical Soc'y v. City of Dover Planning Comm'n,* 838 A.2d 1103, 1110 (Del. 2003); *see also Stein v. Blankfein,* 2019 WL 2323790, at *9 (Del. Ch. May 31, 2019) ("Standing is a threshold issue in any litigation.").

10 *Lewis v. Anderson,* 477 A.2d 1040, 1049 (Del. 1984).

11 *Joseph v. Shell Oil Co.,* 498 A.2d 1117, 1123 (Del. Ch. 1985).

12 In deciding a motion pursuant to Rule 12(b)(6), the Court may consider the well-pleaded allegations in the complaint, documents incorporated by reference into the complaint, matters of which the Court may take judicial notice, undisputed facts, and any additional documents the parties have agreed may be considered on a motion to dismiss. *See, e.g., In re MeadWestvaco S'holders Litig.,* 168 A.3d 675, 678 (Del. Ch. 2017). Defendants do not concede the accuracy or completeness of the allegations contained in the Complaint. A motion to dismiss pursuant to Rule 12(b)(6) may also incorporate facts from certain documents that TerraForm provided to Plaintiffs pursuant to 8 *Del. C.* § 220. *See* 2019 Agreement ¶ 8 (Ex. 1); *see also Amalgamated Bank v. Yahoo! Inc.,* 132 A.3d 752, 796, 797 (Del. Ch. 2016) (corporation may condition Section 220 production on stockholder agreement that the "entirety" of the production "is incorporated by reference in any derivative action complaint" to ensure that a complaint "will not be based on cherry-picked documents"), *abrogated on other grounds by Tiger v. Boast Apparel, Inc.,* 214 A.3d 933 (Del. 2019). Citations to "Ex." refer to the exhibits attached to the Transmittal Affidavit of Stephen C. Childs in Support of Defendants' Motion to Dismiss and Stay, dated March 26, 2020.

13 Compl. T 12; Rosson Compl. ¶ 10.

14 Compl. ¶ 13.

15 Compl. ¶ 14.

16 *Id.*

17 Compl. ¶¶ 17-18.

18 Compl. ¶¶ 19-22.

19 Compl. ¶ 37; Charter Art. VI, § 3(b) (Ex. 2). This Court may take judicial notice of a charter provision. *See In re Wheelabrator Techs. Inc. S'holders Litig.,* 1992 WL 212595, at *12 (Del. Ch. Sept. 1, 1992).

20 Compl. ¶¶ 23, 34-36.

21 Compl. ¶ 25.

22 Compl. ¶¶ 26-27.

23 Compl. ¶ 28.

24 Compl. ¶ 29.

25 Compl. ¶¶ 30, 32.

26 Compl. ¶ 30; *see also* October 6, 2017 TerraForm Press Release (Ex. 3).

27 Compl. ¶ 32.

28 Compl. ¶¶ 33-35, 40.

29 Compl. ¶¶ 30, 33; *see also* October 6, 2017 TerraForm Press Release (Ex. 3).

30 Compl. ¶¶ 34-35.

31 Compl. ¶ 40.

32 *Id.*

33 Compl. ¶ 37; TerraForm Charter, Art. VI, § 3(b)(i) (Ex. 2).

34 Compl. ¶¶ 37, 39; TerraForm Charter, Art. VI, § 2 (Ex. 2).

35 TerraForm Charter, Art. VI, § 3(a)(i)(A) (Ex. 2).

36 TerraForm Charter, Art. VI, § 6 (Ex. 2).

37 TerraForm Charter, Art. XIII (Ex. 2).

38 Compl. ¶¶ 3, 44.

39 Compl. ¶ 54 (quoting Jan. 23, 2018 Conflicts Committee Minutes at TERP000315 (Ex. 4)).

40 *Id.* (quoting Jan. 23, 2018 Conflicts Committee Minutes at TERP000316 (Ex. 4)). TerraForm management and Brookfield representatives expressed concern about TerraForm's reputation and stock performance if the equity offering was not successful. *See* Jan. 23, 2018 Conflicts Committee Minutes at TERP000316-17 (Ex. 4).

41 Compl. ¶¶ 5, 61.

42 Compl. ¶ 63.

43 *Id.*

44 Compl. ¶¶ 8, 93; *see also* June 4, 2018 Conflicts Committee Minutes at TERP000442 (Ex. 5).

45 Compl. ¶ 9.

46 Compl. ¶¶ 9, 96.

47 Compl. ¶¶ 2, 94.

48 Jan. 11, 2020 Brookfield Merger Proposal at 1 (Ex. 6).

49 *Id.*

50 *Id.* at 2.

51 Jan. 13, 2020 TerraForm Press Release (Ex. 7).

52 TerraForm March 16, 2020 Press Release (Form 425) at 3 (filed Mar. 17, 2020) (Ex. 8).

53 *Id.*

54 *Id.*

55 *Id.* at 1.

56 *Id.* BEPC shares "are structured with the intention of being economically equivalent to [Brookfield Renewable units]," and each BEPC share "will be fully exchangeable ... for a [Brookfield Renewable] unit on a one-for-one basis." *Id.* at 3.

57 Compl. ¶¶ 131-41.

58 *Id.* ¶¶ 142-45.

59 *Id.* ¶¶ 146-49.

60 Dkt. 19.

61 Compl. ¶¶ 101-04.

62 Compl. ¶¶ 105, 108.

63 Ct. Ch. R. 12(b)(6); *In re Volcano Corp. S'holderLitig.,* 143 A.3d 727, 737 (Del. Ch. 2016).

64 *In re Gen. Motors (Hughes) S'holder Litig.,* 897 A.2d 162, 168 (Del. 2006) (internal quotation marks omitted).

65 *Id.* (internal quotation marks omitted).

66 *Ala. By-Products Corp. v. Cede & Co. ex rel. Shearson Lehman Bros., Inc.,* 657 A.2d 254, 264 (Del. 1995) "[A] party must have standing to sue in order to invoke the jurisdiction of a Delaware court.").

67 *Dover Historical Soc'y,* 838 A.2d at 1110 (standing determination "ensure[s] that the litigation before the tribunal is a 'case or controversy' that is appropriate for the exercise of the court's judicial powers.").

68 *Lewis,* 477 A.2d at 1049; *see also Ark. Teacher Ret. Sys. v. Countrywide Fin. Corp.,* 75 A.3d 888, 889, 894-95, 897 (Del. 2013) (discussing, "ratify[ing]," and "reaffirm[ing]" the continuous ownership rule recognized in *Lewis v. Anderson).*

69 845 A.2d at 1033.

70 *Culverhouse v. Paulson & Co. Inc.,* 133 A.3d 195, 198 (Del. 2016).

71 *Tooley,* 845 A.2d at 1035.

72 *Id.* at 1038. *See Lipton v. News Int'l, Plc,* 514 A.2d 1075, 1078 (Del. 1986) (recognizing the "special injury" test in which a stockholder "may maintain an individual action if he complains of an injury distinct from that suffered by other shareholders or a wrong involving one of his contractual rights as a shareholder").

73 *Id. at* 1035, 1037.

74 Compl. ¶ 135 (emphasis added).

75 *Id.* at ¶ 102.

76 *Id.* at ¶¶ 1,140.

77 *El Paso,* 152 A.3d at 1265 (Strine, C.J. concurring); *see also id.* n.2 (" 'Classically, Delaware law has viewed as derivative claims by shareholders alleging that they have been wrongly diluted by a corporation's overpayment of shares.' " (quoting *Green v. LocatePlus Hldgs. Corp.,* 2009 WL 1478553, at *2 (Del. Ch. May 15, 2009))); *Klein v. H.I.G. Capital, L.L.C.,* 2018 WL 6719717, at *6 (Del. Ch. Dec. 19, 2018) ("Klein's claims are a classic form of an 'overpayment' claim. He disputes the fairness of the consideration paid for the Preferred Stock given its terms, in particular its dividend rate and the implied call option value of its conversion feature .... Such claims are quintessentially derivative."); *Silverberg v. Padda,* 2019 WL 4566909, at *5 (Del. Ch. Sept. 19, 2019) ("[C]laims that a corporation overpaid for corporate financing, thereby diluting the value of its stock, are quintessentially derivative."), *rearg. denied,* 2019 WL 5295141 (Del. Ch. Oct. 18, 2019).

78 *Gentile,* 906 A.2d at 93.

79 *Id.* at 93, 96.

80 *Id.* at 99.

81 *Id.*

82 *Id.* at 99-100.

83 *Id.* at 100-02.

84 *Carsanaro v. Bloodhound Techs., Inc.,* 65 A.3d 618, 657 (Del. Ch. 2013) (citing *Feldman v. Cutaia,* 956 A.2d 644, 657 (Del. Ch. 2007), *aff'd,* 951 A.2d 727 (Del. 2008)), *abrogation recognized sub nom. Sciabacucchi v. Liberty Broadband Corp.,* 2018 WL 3599997 (Del. Ch. July 26, 2018).

85 *In re Nine Sys. Corp. S'holders Litig.,* 2014 WL 4383127, at *26 (Del. Ch. Sept. 4, 2014), *aff'd sub nom. Fuchs v. Wren Hldgs., LLC,* 129 A.3d 882 (Del. 2015) (Order).

86 *Gentile,* 906 A.2d at 99-100.

87 *Carsanaro,* 65 A.3d at 658.

88 *Thermopylae Capital P'rs, L.P. v. Simbol, Inc.,* 2016 WL 368170, at *11 (Del. Ch. Jan. 29, 2016) (quoting *Carsanaro,* 65 A.3d at 658-59).

89 *Carsanaro,* 65 A.3d at 658-59.

90 *Carsanaro,* 65 A.3d at 659 ("[E]ach financing challenged in the complaint was a self-interested transaction implicating the duty of loyalty and raising an inference of expropriation.").

91 *Nine Sys.,* 2014 WL 4383127, at *28-29 ("Plaintiffs may also establish standing by proving that a majority of the Board was conflicted -- here, meaning interested or not independent -- when it approved and implemented the Recapitalization.").

92 *Allen v. El Paso Pipeline GP Co.,* 90 A.3d 1097, 1111 (Del. Ch. 2014); *In re El Paso Pipeline P'rs, L.P. Deriv. Litig.,* 132 A.3d 67, 111 (Del. Ch. 2015), *judgment entered sub nom. In re: El Paso Pipeline P'rs, L.P.,* 2016 WL 451320 (Del. Ch. Feb. 4, 2016), *and rev'd sub nom. El Paso Pipeline GP Co., L.L.C. v. Brinckerhoff,* 152 A.3d 1248 (Del. 2016).

93 *El Paso,* 152 A.3d 1248.

94 *In re El Paso,* 132 A.3d at 86-118.

95 *In re El Paso,* 132 A.3d at 75.

96 *Id.*

97 *Id.* at 92.

98 *In re El Paso,* 132 A.3d at 86-118, 132.

99 *El Paso,* 152 A.3d at 1265 ("Brinckerhoffs overpayment claim is exclusively derivative under *Tooley.").*

100 *Id.* at 1264.

101 *Id.*

102 *Id.* (internal quotations and citations omitted).

103 *Klein,* 2018 WL 6719717, at *7.

104 *Liberty Broadband,* 2018 WL 3599997, at *10.

105 *Klein,* 2018 WL 6719717, at *7; *see also W&MHelenthal Hldg LLC v. Schmitt,* C.A. No. 2018-0505-AB (Del. Ch. June 3, 2019) at 51:11-15 (TRANSCRIPT) ("In its 2016 *El Paso* decision, our Supreme Court made clear that the *Gentile* doctrine is *to be construed narrowly and that the sort of dual claims described in that case only apply in the unique circumstances of that case."*) (emphasis added). The Court of Chancery, in an effort to make conceptual sense of the ruling, has further cabined *Gentile* to situations where a controller "extract[s] a benefit" from the challenged transaction. *Daugherty v. Dondero,* 2019 WL 4740089, at *3 (Del. Ch. Sept. 27, 2019). In *Daugherty,* Vice Chancellor McCormick also found that *"Gentile* and its progeny require that the expropriated benefit inure *exclusively* to the controllers." *Id.*

106 2018 WL 3599997, at *10 n.147 (emphasis added).

107 *Gentile,* 906 A.2d at 99.

108 2001 WL 599870, at *4 ("Although such conduct may constitute a breach of the duty of loyalty, there is no basis ... to conclude [that] any harm caused by that breach affected the minority shareholders' stock exclusively. That is, the pled facts do not show that the share dilution suffered by the minority shareholders differed in any significant way from the 'dilution' suffered by the entire body of [the company's] stockholders."), *overruled by Gentile,* 906 A.2d 91 (Del. 2006); *see also Avacus P'rs, L.P. v. Brian,* 1990 WL 161909, at *6 (Del. Ch. Oct. 24, 1990) ("To illustrate, if a board of directors authorizes the issuance of stock for no or grossly inadequate consideration, the corporation is directly injured and shareholders are injured derivatively."); *Rothenberg v. Santa Fe Pac. Corp.,* 1992 WL 111206, at *3 (Del. Ch. May 18, 1992) ("The alleged harm to the nontendering shareholder class is that the directors authorized the issuance of additional shares for no consideration. But such dilution would have diminished the value of the shares held by *all* Santa Fe stockholders .... Because the alleged dilution would have affected all shareholders equally, only the corporation could recover damages for the injury."); *Agostino v. Hicks,* 845 A.2d 1110, 1124 (Del. Ch. 2004) (finding injury suffered by stockholder, the devaluation of his stock, a natural and expected consequence of the injury initially borne by the corporation).

109 *Almond as Tr. for Almond Family 2001 Tr. v. Glenhill Advisors LLC,* 2018 WL 3954733, at *28 & n.240 (Del. Ch. Aug. 17, 2018) ("[A] transaction does not fit within the *Gentile* paradigm if the controller itself is diluted by that transaction.") (quoting *Dubroffv. Wren Holdings, LLC,* 2011 WL 5137175, at *9 (Del. Ch. Oct. 28, 2011)), *aff'd,* 2019 WL 6117532 (Del. Nov. 18, 2019), *reh'g denied* (Del. Jan. 6, 2020).

110 *See In re J.P. Morgan Chase & Co. S'holder Litig.,* 906 A.2d 808, 818-19 (Del. Ch. 2005) (holding claims derivative where stockholders alleged their interests were diluted when company overpaid in a stock-for-stock merger; claim that an entity overpaid for an asset is "clearly" derivative because any harm is suffered by the entity, and "[t]he only harm to the stockholders would have been the natural and foreseeable consequence of the harm to JPMC"), *aff'd,* 906 A.2d 766 (Del. 2006) (Table).

111 Where the suit is brought on a corporation's behalf, and the only injury is to the entity, the recovery "must go to the" entity and "only to the" entity. *Tooley,* 845 A.2d at 1036; *see also Zapata Corp.,* 430 A.2d at 784 (citing *Keenan v. Eshleman,* 2 A.2d 904 (Del. 1938) (derivative suits "enforce corporate rights and any recovery obtained goes to the corporation")).

112 Notably, the *Gentile* defendants *conceded* that a stock dilution claim was direct "if voting rights were harmed," arguing only that the court should restrict standing to cases "where the loss of voting power is 'material.' " *Gentile,* 906 A.2d at 98. In other words, the defendants in *Gentile* did not argue that the effect on voting power was *de minimis* in contrast to the harm experienced by the company, nor did the defendants argue that the stockholders had no right to the economic recovery of the company. The only issue before the court was whether to apply a materiality threshold to impose direct standing.

113 *See, e.g., In re Tri-Star Pictures, Inc., Litig.,* 634 A.2d 319, 332 (Del. 1993), *as corrected* (Dec. 8, 1993) ("The impact of this loss on voting power of the minority was fully realized at the time of the Sony merger. Coca-Cola's newly acquired shares gave it total voting control of Tri-Star and the minority became powerless to prevent the merger."), *and disapproved of by Tooley,* 845 A.2d 1031; *Behrens,* 2001 WL 599870, at *5 (discussing *Tri-Star's* holding and finding "[h]ere, by way of contrast, the minority-which owned only 20% of Aerial's stock-already inhabited the region of 'virtual [voting power] oblivion,' and thus never had voting power sufficient to block any transaction involving Aerial"); *El Paso,* 152 A.3d at 1263 (*"Gentile* concerned a controlling shareholder and transactions that resulted in an improper transfer of both economic value *and* voting power from the minority stockholders to the controlling stockholder.").

114 For this reason, claims relating to voting dilution are more properly characterized as claims for "over-dilution."

115 *Tooley,* 845 A.2d at 1039.

116 *Id.* at 1036 (finding that determining whether a stockholder's claim is derivative or direct turns on two questions, who suffered the alleged harm and who would receive the benefit of any recovery or other remedy and that in "individual suits, the recovery or other relief flows directly to the stockholders, not to the corporation").

117 *Tooley,* 845 A.2d at 1036 ("Determining whether an action is derivative or direct is sometimes difficult and has many legal consequences, some of which may have an expensive impact on the parties to the action .... Therefore, it is necessary that a standard to distinguish such actions be clear, simple and consistently articulated and applied[.]").

118 *In re J.P. Morgan Chase & Co. S'holder Litig.,* 906 A.2d 766, 773 (Del. 2006) ("Although the $7 billion damage figure would be a logical and reasonable consequence (and measure) of the harm caused to [the entity] for being caused to overpay for [an asset], that $7 billion figure has no logical or reasonable relationship to the harm caused to the shareholders *individually* for being deprived of their right to cast an informed vote."); *see also Feldman,* 951 A.2d at 733 (noting *J.P. Morgan's* questioning of a plaintiffs ability to bring a direct claim by "bootstrap[ping] the harm and damages causatively linked to a derivative claim onto what, according to that plaintiff, was an independently arising direct cause of action").

119 *J.P. Morgan,* 906 A.2d at 772-73 (holding that "any damages recovery would flow *only* to [the entity], not to the shareholder class" and that it "simply cannot be" that "directors of an acquiring corporation would be liable to pay both the corporation and its shareholders the same compensatory damages for the same injury.") (emphasis added).

120 *See, e.g., Grimes v. Donald,* 673 A.2d 1207, 1213 (Del. 1996) ("[C]ourts have been more prepared to permit the plaintiff to characterize the action as direct when the plaintiff is seeking only injunctive or prospective relief."), *overruled sub nom. Brehm v. Eisner,* 746 A.2d 244 (Del. 2000); *Grayson v. Imagination Station, Inc.,* 2010 WL 3221951, at *6 (Del. Ch. Aug. 16, 2010).

121 *See, e.g., Bokat v. Getty Oil Co.,* 262 A.2d 246, 250 (Del. 1970) (holding that derivative claims are an asset of the corporation which pass to the acquirer in a merger, rejecting non-Delaware cases holding that stockholders can continue the suit in their own name, and declining to award pro rata recovery), *disapproved of on other grounds sub nom. Tooley v. Donaldson, Lufkin & Jenrette, Inc.,* 845 A.2d 1031 (Del. 2004); *Levien v. Sinclair Oil Corp.,* 1975 WL 1952, at *3-4 (Del. Ch. Aug. 12, 1975) (denying corporation's application for pro rata distribution even where entity was arguably "for all practical purposes, in a state of virtual liquidation and [was] about to cease to exist as a viable entity for shareholder investment"); *Keenan v. Eshleman,* 2 A.2d 904, 912 (Del. 1938) (holding that paying a derivative award directly to stockholders would be improper because "transform[ing]" a "derivative action into one for the benefit of the individual" would "not accord with ... the inherent nature of the wrong sought to be redressed.").

122 8 *Del. C.* § 141(a) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors ....").

123 8 *Del. C.* § 327 ("In any derivative suit instituted by a stockholder of a corporation, it shall be averred in the complaint that the plaintiff was a stockholder of the corporation at the time of the transaction of which such stockholder complains or that such stockholder's stock thereafter devolved upon such stockholder by operation of law.").

124 *Lewis,* 477 A.2d 1040.

125 Ct. Ch. R. 23.1(a).

126 *Aronson v. Lewis,* 473 A.2d 805, 814 (Del. 1984), *overruled on other grounds sub nom. Brehm v. Eisner,* 746 A.2d 244 (Del. 2000) (setting forth standard for pleading demand futility).

127 *See, e.g., Zapata Corp. v. Maldonado,* 430 A.2d 779 (Del. 1981).

128 Apart from standing issues, the distinction of whether a claim is direct or derivative has myriad collateral effects on litigation, including the form and manner of bringing the suit, the procedures for certifying a class, settlements, and when notice is required to other investors. *See, e.g.,* Ct. Ch. R. 23; Ct. Ch. R. 23.1. And, as the Court of Chancery has recognized, *res judicata* also becomes difficult to apply in the context of "dual" claims. *See In re Ebix, Inc. S'holder Litig.,* 2016 WL 208402, at *10 n.88 (Del. Ch. Jan. 15, 2016) ("A conceptual knot this Court need not attempt to untangle at present is how *[res judicata]* might apply in the context of a claim that is simultaneously direct and derivative. Cleanly applying a bright-line rule may prove problematic in contexts where, as in the case of classifying a given claim as direct or derivative, the lines creating the operative distinction themselves may blur."); *see also* 7C Charles Alan Wright & Arthur R. Miller, Federal Practice and Procedure § 1840 (1969-1985) ("The judgment in a derivative suit will not preclude any right of action that an absent stockholder might have in the stockholder's individual capacity against the corporation or the real defendants in the derivative suit.").

129 *Gentile,* 906 A.2d at 98 n. 16 (concluding that "the debt conversion claim is not exclusively derivative and could have been brought *either* directly or derivatively") (emphasis added).

130 To the extent a direct recovery was favored in such an election of remedies, that result may also be unsatisfying to holders in the public company context, as trading in the corporation's shares in the interim between the challenged transaction and any recovery could result in different stockholders receiving the recovery than would otherwise be the case in the event a damages award was made directly to the corporation.

131 8 *Del. C.* § 259 (without exception, at the time of a merger, the surviving corporation takes "the rights, privileges, powers and franchises of each of said corporations, and all property, real, personal and mixed" as well as "all other things in action or belonging to each of such corporations"). The new owner has the statutory right to continue the suit on behalf of the corporation as if the merger had not happened. 8 *Del. C.* § 261 ("Any action or proceeding, whether civil, criminal or administrative, pending by or against any corporation which is a party to a merger or consolidation shall be prosecuted as if such merger or consolidation had not taken place, or the corporation surviving or resulting from such merger or consolidation may be substituted in such action or proceeding.").

132 *Lewis,* 477 A.2d at 1043 ("The company of which the plaintiff is now a shareholder, DuPont, now owns all of the stock of the present Conoco and, if the original Conoco had a claim for relief against its former officers and directors for the reasons set forth in the complaint in this action, that claim is now owned by the present Conoco. The shareholder beneficiary of such a claim is now DuPont, and not the plaintiff Lewis and the other shareholders of the original Conoco as was the situation when the suit was filed.").

133 Likewise, in the case where a company becomes insolvent and liquidates, the company's creditors or a bankruptcy trustee may wish to assert claims on behalf of the company's estate. It is not clear who between the creditors, standing in the shoes of the corporation as its residual claimants, or the stockholders, acting on their own behalf, would have the right to recover. *See N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla,* 930 A.2d 92, 101 (Del. 2007) (granting standing for creditors to sue derivatively on a corporation's behalf in the event the corporation is insolvent because "[w]hen a corporation is insolvent, ... its creditors take the place of the shareholders as the residual beneficiaries of any increase in value.").

134 As former Chief Justice Strine stated: "by refusing to extend *Gentile* to the alternative entity arena, we implicitly recognize that *Gentile* undercuts the clarity and coherence that *Tooley* brought to the determination of what claims are derivative." *El Paso,* 152 A.3d at 1266 (Strine, C.J., concurring).

135 *Tooley,* 845 A.2d at 1036.

136 Consistency is also particularly important in making direct/derivative distinctions in the M&A context, given that such rulings impact predictability with respect to who may litigate future claims. *Cf: Edgerly v. Hechinger Co.,* 1998 WL 671241, at *2 (Del. Ch. Aug. 27, 1998) (discussing the importance of predictability in the M&A context and reading a corporate statute narrowly because "[a]ny other result would embroil merging corporations in a morass of confusion and uncertainty, none of which was of their making.") (quoting *Enstar Corp. v. Senouf,* 535 A.2d 1351, 1356 (Del. 1987)).

137 *Aspen Advisors LLC v. United Artists Theatre Co.,* 843 A.2d 697, 712 (Del. Ch.), *aff'd,* 861 A.2d 1251 (Del. 2004); *see also Elliott Assocs., L.P. v. Avatex Corp.,* 715 A.2d 843, 854 (Del. 1998) ("The outcome here continues a coherent and rational approach to corporate finance. The contrary result, in our view, would create an anomaly and could risk the erosion of uniformity in the corporation law.").

138 *El Paso,* 152 A.3d at 1266 (Strine, C.J., concurring).

139 *Id.*

140 *Revlon, Inc. v. MacAndrews & Forbes Hldgs, Inc.,* 506 A.2d 173, 184 (Del. 1986).

141 *See, e.g., In re Primedia, Inc. S'holders Litig.* 67 A.3d 455 (Del. Ch. 2013); *see also Morris v. Spectra Energy P'rs (DE) GP, LP,* 2019 WL 4751521, at *1 (Del. Ch. Sept. 30, 2019) (*"Primedia* provides a three-part test for standing to pursue a direct claim challenging a merger price solely on failure to obtain value for a derivative litigation asset[.]").

142 If there ever were a case to depart from the continuous ownership rule, it was arguably *El Paso,* where the Court of Chancery had already determined that the general partner and controller had allegedly acted in bad faith and only reached standing issues *after* the liability determination resulting in a judgment for $171 million. *El Paso,* 152 A.3d at 1250-51. The trial court had determined that in order to hold the general partner "accountable" for the judgment (and thereby prevent a "windfall" to the general partner), it was appropriate to avoid the continuous ownership requirement that mandated dismissal of the plaintiffs claims. *In re El Paso,* 132 A.3d at 2, 75-80. Still, even in that case, the Supreme Court declined to depart from *Tooley* and the rule that the plaintiffs were divested of standing following a merger. *El Paso,* 152 A.3d at 1265.

143 *El Paso,* 152 A.3d at 1266 (Strine, C.J., concurring).

144 *ACP Master,* 2017 WL 3421142, at *26 n.206.

145 *Cirillo Family Tr. v. Moezinia,* 2018 WL 3388398, at *16 n.156 (Del. Ch. July 11, 2018), *aff'd,* 220 A.3d 912 (Del. 2019) (Order).

146 *Mesirov v. Enbridge Energy Co.,* 2018 WL 4182204, at *8 n.77 (Del. Ch. Aug. 29,2018) (*"At the very least, El Paso* makes clear that *Gentile* and its progeny should be construed narrowly.") (emphasis added)).

147 *Paolino v. Mace Sec. Int', Inc.,* 985 A.2d 392, 397 (Del. Ch. 2009) (citing cases).

148 Ct. Ch. R. 26(c).

149 *See Lewis,* 477 A.2d at 1046; *see also Lewis v. Ward,* 852 A.2d 896, 900-01 (Del. 2004) ("Under Delaware law, it is well established that a merger which eliminates a derivative plaintiffs ownership of shares of the corporation for whose benefit she has sued terminates her standing to pursue those derivative claims.").

150 2017 WL 5565264, at *3, 4.

151 2017 WL 3499807, at *1 n.1.

152 *Kohls v. Duthie,* 765 A.2d 1274, 1289 (Del. Ch. 2000).

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