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Case Number 423,2016

IN THE SUPREME COURT OF THE STATE OF DELAWARE

PHILIP R. SHAWE and SHIRLEY SHAWE,	)	
	)	
Respondents-Below, Appellants,	)	No. 423, 2016
	)	
v.	)	Court Below: The Court of
	)	Chancery of the State of
ELIZABETH ELTING,	)	Delaware, C.A. Nos. 9686-CB,
	)	9700-CB and 10449-CB
Petitioner-Below, Appellee.	)	

BRIEF OF AMICUS CURIAE CITIZENS FOR A PRO-BUSINESS DELAWARE, INC. IN SUPPORT OF APPELLANT PHILIP R. SHAWE

Evan O. Williford (No. 4162)
Andrew J. Huber (No. 6043)
THE WILLIFORD FIRM LLC
901 N. Market Street, Suite 800
Wilmington, DE 19801
(302) 654-5924
Attorneys for Amicus Curiae Citizens for a Pro-Business Delaware, Inc.

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INTRODUCTION

Amicus Curiae Citizens for a Pro-Business Delaware, Inc. ("Citizens") was formed to advocate for employees of TransPerfect Global, Inc. ("TransPerfect") after the Court of Chancery's memorandum opinion of August 13, 2015, subject of this interlocutory appeal, appointing a custodian to sell TransPerfect in this case of alleged deadlock under 8 *Del. C.* § 226. OB Ex. A at 81-85. Some of the persons involved with Citizens consider themselves closer to 50% stockholder Elizabeth Elting, while others consider themselves closer to 49% stockholder Philip Shawe.

The Court of Chancery legally erred by ruling that the custodian should not be given the powers of a provisional director to resolve the deadlock because the two main stockholders in this case (Elting and Shawe) are still relatively young. A number of Delaware cases, including one before this Court, have in the past appointed custodians as provisional directors as a way to resolve deadlock. In some cases a provisional director has been successful in permanently resolving the deadlock and their appointment has ended. In others, if a provisional director is unsuccessful the court can always select a different remedy. In neither set of cases need the involvement of the provisional director, let alone the Court of Chancery, continue for decades.

Such a remedy is appropriate here. Appellant Philip Shawe in his brief has noted that the custodian appointed has already resolved issues regarding

distributions by creating a regularized system for them. This dispute was a main motivation behind many of the disputes upon which the court below relied in holding there to be deadlock, and neither party has challenged the custodian's action. In any event, such relief is also consistent with the appropriate statutory policy of ordering the least intrusive relief that has the potential for dealing with any deadlock.

By contrast, the forced sale the lower court has ordered threatens to roll the dice with the stability and future of this Delaware corporation that has been phenomenally successful during the time of the alleged deadlock, and employs over 3,500 individuals. One or both of Shawe or Elting could leave, individuals who each run multiple departments within TransPerfect that have been critical to its success. A potential acquirer could have its own motives or abilities that could threaten the further growth or even existence of TransPerfect's business.

This brief supports Argument Section I.C.2 of Appellant Philip Shawe's opening brief. Specifically, Citizens respectfully requests and proposes that this Court order the Court of Chancery to appoint a custodian to serve as a provisional director.

IDENTITY, INTEREST, AND SOURCE OF AUTHORITY

Citizens for a Pro-Business Delaware, Inc. ("Citizens") was formed to advocate for employees of TransPerfect Global, Inc. ("TransPerfect") after the Court of Chancery's memorandum opinion of August 13, 2015, subject of this interlocutory appeal, appointing a custodian to sell TransPerfect. OB Ex. A at 81-85. Some of the persons involved with Citizens consider themselves closer to Elting, while others consider themselves closer to Shawe.

TransPerfect's employees, on whose behalf Citizens advocates, may be significantly affected by a sale of TransPerfect, which could conceivably be to a third party as well as the current stockholders. Depending on the purposes and intentions of such acquirer, a potential sale creates uncertainty as to the continued growth of the company and even the employee's jobs.

As more fully stated in the accompanying motion for leave to file this amicus brief, Citizens will assist this Court by supplementing the efforts of counsel in a case of general public interest and by focusing the Court's attention on broader legal or policy implications. Authority for Citizens to file its brief is found in Supreme Court Rule 28.

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN RULING A PROVISIONAL DIRECTOR REMEDY LEGALLY UNAVAILABLE TO YOUNG STOCKHOLDERS.[1]

A. Standard Of Review

Questions of law are reviewed *de novo*. *See Sussex Cty. Dep't of Elections v. Sussex Cty. Republican Comm.*, 58 A.3d 418, 421 (Del. 2013). Where "the appellant claims that the disputed remedy was erroneous as a matter of law, because the trial court erred 'in formulating or applying legal principles'", the appropriate review is *de novo*. *Berger v. Pubco Corp.*, 976 A.2d 132, 139 (Del. 2009).

B. Merits Of Argument

The Court of Chancery discussed three alternatives to resolving what it held to be a deadlock at TransPerfect: to (1) "leave the parties to their own devices"; (2) "appoint a custodian to serve as a third director or some form of tie-breaking mechanism in the governance of the Company"; or (3) appoint a custodian to sell the company. OB Ex. A at 80-81.

The Court of Chancery chose to appoint a custodian to sell the company. In so doing it rejected the second option, appointing a custodian to serve as a provisional director, for the following reasons:

[1] This brief supports the argument made by appellant Philip Shawe in Section I.C.2 of his opening brief.

> I reject this option because it would enmesh an outsider and, by extension, the Court into matters of internal corporate governance for an extensive period of time. Shawe and Elting are both relatively young. Absent a separation, their tenure as directors and co-CEOs of the Company could continue for decades. It is not sensible for the Court to exercise essentially perpetual oversight over the internal affairs of the Company.

OB Ex. A at 81.

1. The Provisional Director Remedy Is A Common And Well-Recognized Remedy For Deadlock.

Appointment of a custodian to serve as a provisional director is a well-recognized remedy for deadlock. Notably, this Court appointed one in *Giuricich v. Emtrol Corp.*:

> A custodian will be appointed by the Court of Chancery under § 226(a)(1) who is strictly impartial and has a proven business and executive background. The custodian will be empowered to act only in situations in which the board of directors of Emtrol have failed to reach a unanimous decision on any issue properly before them. In the event that the board is unable to reach unanimous accord on any such pending issue, the custodian will resolve the issue in such manner as he shall deem appropriate. His decision and action in such case shall be binding upon the officers and directors of Emtrol, and shall be deemed the official action of the corporation. The custodian may call a directors' meeting, or a stockholders' meeting, *sua sponte* or at the request of any director. The custodian shall serve for such time as the Court of Chancery shall deem necessary, or until there is a unanimous request to the Court for his discharge by all shareholders of Emtrol. The compensation of the custodian will be approved by the Court of Chancery and paid by Emtrol.

449 A.2d 232, 240 (Del. 1982); *see also Miller v. Miller*, 2009 WL 554920, at *5 (Del. Ch. Feb. 17, 2009) (appointing custodian with authority "to break material

deadlocks between directors," such authority to expire in two years unless extended);[2] *Bentas v. Haseotes*, 769 A.2d 70, 79 (Del. Ch. 2000) (appointed custodian was to vote at board meetings when board was deadlocked).

A provisional director is a "neutral third party appointed by the court to the board of directors to act as a tie-breaking director." Susanna M. Kim, *The Provisional Director Remedy for Corporate Deadlock: A Proposed Model Statute*, 60 Wash. & Lee L. Rev. 111, 114 (2003). They "possess the same rights and powers of ordinary directors to vote at meetings" and their "role" is "to vote to break deadlocks in the corporation." *Id.*

One value of such a person "lies in their ability to mediate between hostile factions and to encourage both sides to consider new ideas and alternatives for resolving disputes amicably." *Id.*; Steven C. Bahls, *Resolving Shareholder Dissension: Selection of the Appropriate Equitable Remedy*, 15 J. Corp. L. 285, 296, 308-09 (1990) (such appointment is like, "in effect, appointing in-house arbitrators"). Introduction of an "outsider" into the situation "tends to put the parties on their best behavior" and is often effective "because they give the bitterly disputing parties an opportunity to calm down for a period of time". Kim, *supra* at 124, 135.

[2] The authority of the custodian was ultimately extended some seven years. *Miller v. Miller*, 2016 WL 614486 (Del. Ch. Feb. 11, 2016).

A model close corporation statute, and numerous state statutes, specifically require courts to consider appointing a provisional director in deadlock situations before ordering its dissolution. Model Bus. Corp. Act Ann., Model Statutory Close Corp. Supplement, §§ 41-42 (1984); Ga. Code Ann. §§ 14-2-941 to 942; 805 Ill. Comp. Stat. Ann. 5/12.56(b); Mo. Ann. Stat. §§ 351.855 & 860; Mont. Code Ann. §§ 35-9-502 to 503; Or. Rev. Stat. Ann. § 60.952(2); S.C. Code Ann. §§ 33-18-410 & 420; Wis. Stat. Ann. § 180.1833(2)(a); Wyo. Stat. Ann. §§ 17-17-141 to 142.

Delaware has a provisional director statute, though it is limited to corporations specifically electing in their certificates of incorporation to be Delaware close corporations. In any event, courts have the equitable authority to appoint a custodian to serve as one upon a finding of deadlock. *Giuricich*, 449 A.2d at 240; OB Ex. A at 81 (discussing as an "option" appointment of "a custodian to serve as a third director or some form of tie-breaking mechanism"); *Bontempo v. Lare*, 119 A.3d 791, 805-06 (Md. 2015) (statute authorizing court of equity to grant dissolution for oppressive conduct implicitly authorized "less drastic equitable remedies" to that "extreme" remedy).

2. The Court Of Chancery Legally Erred In Ruling A Provisional Director Remedy Unavailable To Young Stockholders.

The Court of Chancery rejected the provisional director remedy on the argued grounds that, because Shawe and Elting are both "relatively young," this

option would "enmesh an outsider and, by extension, the Court into matters of internal corporate governance" for an "extensive" period of time. OB Ex. A at 81.

This ruling and the standard it set forth was legally erroneous. Even to the extent that the lower court's discretion was involved, for the lower court to "apply an incorrect legal standard" such as this on a determination of the correct remedy in a Section 226 case is "to abuse discretion." *Giuricich*, 449 A.2d at 240.

The court seemed to assume that the role of the provisional director in a deadlock is perpetual and, therefore, one should not be appointed as to deadlock between young stockholders because such a role could last as long as the stockholders (i.e., decades).

That assumption is not warranted. The Court of Chancery cited no caselaw for such a rule, Delaware or otherwise. As set forth above, one role of the provisional director is to serve as a mediator for the issues between the stockholders that have resulted in the deadlock. If successful, it is a possibility and to be hoped that the deadlock will be resolved and therefore the provisional director can step down. As explained by Ernest L. Folk, III, author of a significant part of the extensive revisions to the Delaware General Corporation Law in 1967, this remedy "assumes that [the provisional director's] supposedly dispassionate approach, unwarped by prior involvement in the internecine strife, will enable him to work with the other parties towards a resolution of the conflict, and having done

so, that he will bow out without permanently altering the balance of power within the corporation." Ernest L. Folk, III, *Corporation Statutes: 1959-1966*, 1966 Duke L.J. 876, 953 (1966).

In that vein, in *Giuricich* this Court reversed the lower court's decision to grant no remedy but held that the provisional director would only "serve for such time as the Court of Chancery shall deem necessary". 449 A.2d at 240.

If a provisional director resolves all or the main disputes without the need for court involvement, it has served its purpose. If not, the Court of Chancery retains the equitable authority to reconsider and grant a different remedy. This possibility will hopefully serve as a further incentive for the parties to cooperate with the provisional director.

Moreover, any necessity for Court involvement would be greatly reduced, and hopefully mostly or entirely eliminated, by the provisional director. It is their role to discuss and resolve disputes that have resulted in deadlock. The provisional director is not a Delaware Court of Chancery judicial officer, and they are appropriately compensated for their service.

As to any limited disputes that would reach the Court notwithstanding the provisional director's services, one of the court's main roles is to resolve intra-corporate disputes. *See, e.g.*, *Carlton Investments v. TLC Beatrice Int'l Holdings, Inc.*, 1996 WL 608492, at *5 (Del. Ch. Oct. 16, 1996) (noting "the strong interest

that this Court has in assuring the effective administration of the law governing corporations organized in Delaware and, therefore, in hearing cases regarding internal corporate governance issues"). That would be an appropriate, limited role for it to take in attempting, for a limited period of time, to eliminate deadlock in a Delaware corporation, particularly a vibrantly profitable one such as TransPerfect.

As discussed in Philip Shawe's brief, OB at 22-23, custodians appointed by Delaware courts have explored fair solutions in deadlock situations over the course of years in certain cases. *See Miller v. Miller*, 2016 WL 614486 (Del. Ch. Feb. 11, 2016) (seven years); *Bentas v. Haseotes*, 2003 WL 1711856, at *1-3 (Del. Ch. Mar. 31, 2003) (three years).

And if court involvement truly were burdensome, the court could utilize Masters in Chancery or special masters to handle the minutiae. *See, e.g.*, *DiGiacobbe v. Sestak*, 743 A.2d 180, 182 (Del. 1999) (citing Ct. Ch. R. 135-47 and 10 *Del. C.* § 372).

3. The Custodian Should Be Appointed To Serve As A Provisional Director.

This Court should resolve this error of law by instructing the lower court to appoint a custodian to serve as provisional director until such time as that court should instruct otherwise for good cause, or the stockholders shall all stipulate to discharge him or her. *See Giuricich*, 449 A.2d at 240 (custodian empowered to resolve issues on which board is deadlocked "shall serve for such time as the Court

of Chancery shall deem necessary, or until there is a unanimous request to the Court for his discharge by all shareholders of Emtrol").

Appellant Philip Shawe has pointed out, in his opening brief on appeal, that the custodian appointed has already "successfully resolved most of the supposedly intractable 'deadlocks'" – including "by implementing regularized distributions", and that neither party has sought judicial review of such actions. OB at 23. Disputes about distributions made up a large proportion of the factual record which the court below cited in its holding that there was a deadlock. OB Ex. A at 9, 12-13, 16-20, 24, 29-30, 44-45, 53-54, 64, 68-69. This demonstrates the significant possibility that a custodian serving as a provisional director could fully or materially resolve the deadlock.

Should the deadlock continue and the provisional director be unable to resolve it, the Court could grant another remedy. That possibility resolves the concerns of the court below that it could be involved for "decades".

Alternatively, this Court could appoint the provisional director to serve for a specified, three-year period of time. Such a period would also allay the concerns of the court below. It is similar to the period of time in *Bentas* between the court's decision appointing a custodian and the court's decision on a motion to determine a plan of liquidation. *Bentas v. Haseotes*, 769 A.2d 70, 79 (Del. Ch. 2000); *Bentas v. Haseotes*, 2003 WL 1711856, at *3-4 (Del. Ch. Mar. 31, 2003); *see also Miller v.*

Miller, 2009 WL 554920, at *5 (Del. Ch. Feb. 17, 2009) (appointing deadlock-breaking custodian with authority to expire in two years, later renewed to seven years).

The Court in its opinion reasoned that the areas of deadlock were not "easily resolved" because they "reflect systemic divisions in the management of the Company" and the parties failed to resolve them after years. OB Ex. A at 83. As set forth above, however, certain of these "systemic" divisions have already been resolved by the custodian. OB at 23.

All deadlock cases by definition involve disagreements serious and fundamental enough that they have resulted in litigation. That in and of itself should not disqualify a deadlock remedy short of a forced sale, such as a provisional director, from being attempted. Courts have appointed provisional directors in situations involving significant alleged misconduct between the parties, s*ee Abreu v. Unica Indus. Sales, Inc.*, 586 N.E.2d 661, 665 (Ill. App. Ct. 1991) (trial court held defendants had "breached fiduciary obligations by usurping corporate opportunities and repeatedly attempting to acquire secret product formulas" and created another entity to compete with the corporation at issue); or involving deadlock on fundamental issues. *See In re ANNRHON, Inc.*, 21 Cal. Rptr. 2d 599, 605 (Cal. Ct. App. 1993) (noting parties were deadlocked "on whether to expand the business or, in the alternative, sell out"); *compare* OB ex. A

at 88-89 (refusing to award equitable dissolution because "the record does not show that Shawe engaged in self-dealing or financially enriching himself at the Company's expense).

One of the arguments for any alternative remedy such as appointing a provisional director is that "remedy should not be discounted merely because it might not always be the final solution" for deadlock. Kim, *supra* at 136. Rather, "[t]he fact that the remedy may help save the corporation and its shareholders from the devastating effects of deadlock may make it worth a try." *Id.*

While a provisional director remedy can be withdrawn if unsuccessful, a sale is permanent and poses a very real threat to the stability and profitability of TransPerfect and the employment it provides to its employees.

4. The Extreme Remedy Of A Forced Sale Risks Damaging Or Destroying This Profitable Delaware Corporation.

The lower court itself recognized that ordering the sale of a profitable company "should be implemented only as a last resort and with extreme caution". OB Ex. A at 81-82.

The court ordered such a forced sale despite recognizing that TransPerfect is "highly profitable". OB Ex. A at 1. Its revenue grew from $199 million in 2008 to over $500 million in 2015. OB Ex. A at 73; A4334-35 (Q2 2016 revenue of $136 million was largest in its history). It added over 300 new jobs in the second quarter of this year, and 530 during the year to date. A4334-35.

TransPerfect has "more than 3,500 full-time employees" and a "network of more than 10,000 translators, editors and proofreaders". OB Ex. A at 2.

A forced sale to one or the other of 49% stockholder Philip Shawe or 50% stockholder Liz Elting poses grave risks to the company. It is speculative to consider what the fortunes of TransPerfect would be without Shawe. See OB Ex. A at 82 (recognizing "[t]he distinct possibility" that "a third party would be unwilling to acquire the Company without securing his participation and expertise"). By the same token, Elting leads five of the company's divisions. OB Ex. A at 6.

Moreover, a sale to a third-party is also a possibility; such a sale was specifically contemplated in the court's order adopting a modified broad auction "where the Custodian could work with outside bidders who are interested in purchasing TPG." *In re TransPerfect Global, Inc.*, 2016 WL 3477217, at *2 (Del. Ch. June 21, 2016). Such a sale would pose the risks to the company discussed above, except possibly doubled, with TransPerfect losing both Shawe and Elting rather than one or the other.

Moreover, the intentions of a third party to making the acquisition could pose additional threats (e.g., a purchase by a competitor or for break-up value).

In holding there was deadlock, the court specifically stated the alleged deadlock posed "harm to employee morale and retention". OB Ex. A at 74.

Despite that alleged issue, TransPerfect nevertheless experienced phenomenal growth. If Delaware courts are going to consider the effect on employee morale and retention in granting a deadlock remedy, they should certainly consider the (potentially considerably greater) effect a business failure or downsizing would have, whether caused by Shawe or Elting or both departing, or by the decisions of an acquirer, on those very same employees.

This is particularly the case given that a less intrusive remedy exists that stands a real chance of resolving the deadlock. The Delaware courts ***should not needlessly jeopardize the jobs of over 3,500 people***.

5. Cited Cases Are Inapposite.

The court below cited two cases in support of its decision to authorize the custodian to "conduct a sale of the corporation." OB Ex. A at 81-82 & n.320. Neither case supports ordering a forced sale in this action.

The lower court concedes that in one of the cases the parties had agreed on a dissolution remedy. *Id.* (citing *Fulk v. Wash. Svc. Assocs., Inc.*, 2002 WL 1402273 (Del. Ch. June 21, 2002)).

In the second case, *Bentas v. Haseotes*, upon holding there to be deadlock the Court of Chancery initially appointed a custodian to cast a tie-breaking vote on significant disputes – ***as we request in this brief***. 769 A.2d 70, 79 (Del. Ch. 2000). In the stage of that litigation that is comparable to the current stage of this one, the

court ***expressly rejected*** defendants' argument that "the custodian be directed to sell the Company". *Id.* Plaintiffs argued that defendants' proposals "would be highly intrusive and would run counter to the statutory policy, which is to allow the business of the Company to continue in the least invasive manner possible and without regard to the divisions between the stockholders." *Id.*

The Court of Chancery ruled that plaintiffs "have the better position" and directed a custodian to explore all alternatives that might result in a "mutually agreed solution" to the deadlock. *Id.* at 80. More than three years later, after the deadlock still had not been resolved, and the court selected the custodian's and plaintiffs' proposal to auction the company over defendants' proposal to divide the company in half. *Bentas v. Haseotes*, 2003 WL 1711856, at *3-4 (Del. Ch. Mar. 31, 2003).

Indeed, the approach that the two relevant *Bentas* decisions support at this time in this litigation is for the appointment of a custodian to serve as a provisional director to attempt to find a solution to the deadlock that would "allow the business of the Company to continue in the least invasive manner possible and without regard to the divisions between the stockholders." *Id.*

CONCLUSION

Amicus Curiae Citizens respectfully proposes and requests that this Court remand the case with instructions that the Court of Chancery appoint a custodian to serve as a provisional director.

/s/ Evan O. Williford
Evan O. Williford (No. 4162)
Andrew J. Huber (No. 6043)
THE WILLIFORD FIRM LLC
901 N. Market Street, Suite 800
Wilmington, DE 19801
(302) 654-5924
Attorneys for Amicus Curiae Citizens for a Pro-Business Delaware, Inc.

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