EFiled: Mar 24 2014 08:41PM EDT
Transaction ID 55196049
Case No. 9318-VCL

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

JON SLOTOROFF, Plaintiff, v. KINDER MORGAN, INC.; KINDER MORGAN G.P., INC., Defendants, -and- KINDER MORGAN ENERGY PARTNERS, L.P., Nominal Defendant.	)	C.A. No. 9318-VCL

BRIEF IN SUPPORT OF MOTION TO DISMISS

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Dated: March 24, 2014

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NATURE AND STAGE OF PROCEEDINGS

Parroting recent "short attacks" on nominal defendant Kinder Morgan Energy Partners, L.P. ("KMP")'s enviable record of quarterly distributions to unitholders, plaintiff makes the unusual allegation that his units are "overvalued" (Compl. ¶ 120) and that he has received too much in distributions (Compl. ¶ 3). Relying on a flawed interpretation of the governing partnership agreement, plaintiff claims that KMP's general partner Kinder Morgan G.P., Inc. ("KMGP") has, on a quarterly basis, miscalculated the cash available for distribution and paid "too much" to limited partners and itself. Plaintiff alleges that "excessive" distributions violate the governing partnership agreement and have deprived KMP of capital needed for maintenance and other operational purposes, and that KMP has taken on too much debt and issued too much equity in order to fund its operations. These are classic derivative claims.

Interestingly, plaintiff alleges no change in KMP's business model or KMGP's management of the business in the ten years he has been a unitholder. Plaintiff's complaint is simply a repackaging of a recent "short attack," coupled with a fundamental misinterpretation of the partnership agreement. We leave for another day, if necessary, the correction of plaintiff's many mistakes in interpreting the partnership agreement. On a motion to dismiss, this Court is constrained to accept the facts in the complaint as true, and "it matters not which party's assertions are actually true." *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings, LLC*, 27 A.3d 531, 538 (Del. 2011). On this motion, we address only one (but case-dispositive) issue – plaintiff's standing to assert these claims, including the threshold question yet to be decided by our

Supreme Court: whether the need for a demand on a general partner is determined by an examination of the general partner as a corporate entity or by an examination of the general partner's board of directors. If it is the former, as plaintiff assumes, then demand is excused. If it is the latter, then demand is required, and this case must be dismissed.

Accordingly, on March 3, 2014, nominal defendant KMP and defendants Kinder Morgan, Inc. ("KMI"), which indirectly owns all of KMGP's common stock, and KMGP moved to dismiss this action pursuant to Court of Chancery Rules 23.1 and 12(b)(6).

On March 6, 2014, a second action, alleging derivative claims on behalf of KMP arising out of the same allegations, was filed in the District Court of Harris County, Texas. KMP and the defendants in the Texas action intend to move to dismiss or stay that action in favor of proceedings in this Court.

STATEMENT OF FACTS

The following facts are taken from plaintiff's complaint and publicly filed documents. *See In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 170 (Del. 2006) ("on a Rule 12(b)(6) motion to dismiss, trial courts may consider hearsay in SEC filings 'to ascertain facts appropriate for judicial notice under [Delaware Rule of Evidence] 201'" that are "'not subject to reasonable dispute'") (citations omitted).

A. The Parties

Plaintiff Jon Slotoroff alleges that he has "continuously for over ten years" owned units of nominal defendant KMP, a limited partnership organized under Delaware law and whose principal executive offices are located in Houston, Texas. Compl.

¶¶ 13-15. KMP is an owner and operator of pipelines which transport natural gas, refined petroleum products, crude oil and CO2, as well as liquid and bulk terminal storage facilities. *Id.* ¶ 14.

Defendant KMI is the largest midstream and the third largest energy company in North America. *Id.* ¶ 16. Plaintiff alleges that KMI owns defendant KMGP, the general partner of KMP (*id.*); in fact, KMI owns 100% of Kinder Morgan (Delaware) Inc., which in turn owns 100% of the common stock of KMGP. KMGP has delegated its management of KMP to Kinder Morgan Management, LLC ("KMM"). *Id.* ¶ 16; Feb. 18, 2014 Form 10K at 5 (Ex. A).[1] Plaintiff alleges that KMI owns approximately 13% of KMP's total equity interests (2% through KMGP as general partner and 11% in limited partnership interests) and "an approximately 50 percent economic interest in KMP." Compl. ¶¶ 16-17.

KMP is a master limited partnership ("MLP"), a unique entity. MLPs exist to distribute most of their free cash flow in order to qualify for certain tax advantages of being a "pass-through entity" that enables them to avoid having their investors' income taxed twice. *See generally* Compl. ¶¶ 24-26 (MLPs "combine the tax benefits of a limited partnership with the liquidity of publicly traded securities. . . . Investors are drawn to MLPs because the contracts governing MLPs typically require them to regularly pay out to their unitholders in quarterly cash distributions all earnings not needed for current operations and maintenance of capital assets. . . . [I]nvestors

[1] Citations to "Ex. __" refer to the exhibits to the Transmittal Affidavit of Bradley R. Aronstam in Support of Kinder Morgan, Inc., Kinder Morgan G.P., Inc. and Kinder Morgan Energy Partners, L.P.'s Motion to Dismiss, filed contemporaneously herewith.

typically view MLP units as producing a long-term annuity-like equity stream"). The operations and governance of an MLP are established by a partnership agreement that typically grants the general partner broad discretion in managing its business and affairs. Delaware law allows the partnership agreement to disclaim fiduciary duties, and the scope and extent of the general partner's obligations is instead set forth in the governing partnership agreement. 6 *Del. C.* § 17-1101(d).

Plaintiff alleges no facts concerning the composition of KMGP and KMM's boards. KMP's public filings, of which this Court may take judicial notice, identify five directors of KMGP and KMM: Richard D. Kinder, Steven J. Kean, Ted A. Gardner, Gary L. Hultquist and Perry M. Waughtal. Feb. 18, 2014 Form 10K at 83-84 (Ex. A). Plaintiff does not (and cannot) allege that three of KMGP's five directors – a majority of the board – are not independent. KMP's public filings state that "[t]he board has affirmatively determined that Messrs. Gardner, Hultquist and Waughtal, who constitute a majority of the directors, are independent as described in our governance guidelines and the NYSE rules" and that "each has no family relationship with any of the directors or executive officers" of KMI, KMGP or KMM and "each has no direct or indirect material interest in any transaction or proposed transaction required to be reported under Section 404(a) of Regulation S-K." *Id.* at 98 (Ex. A).

B. <u>The Alleged Wrongdoing</u>

Plaintiff alleges that the governing partnership agreement requires KMGP to calculate cash distributions to limited partners and to KMI by subtracting "maintenance" or "sustaining" capital expenditures ("Maintenance Capex") but not

"expansion" or "growth" capital expenditures ("Expansion Capex") from KMP's total earnings before depreciation and amortization. Compl. ¶¶ 5, 28-30. According to plaintiff, KMGP has allocated expenditures between Maintenance Capex and Expansion Capex "in bad faith," "classifying capital expenditures that should be attributed to Maintenance Capex into the Expansion Capex column" in order to "artificially inflate the amount of money that is available for Distribution" and "maximize KMP's Distributions." *Id.* ¶¶ 2, 7, 51. Plaintiff expressly acknowledges the derivative nature of this lawsuit: "[p]laintiff brings this suit in order to compel KMI to act in accordance with the terms of the Partnership Agreement (by requiring KMI to calculate DCF without preference to its personal interests) and to seek money damages ***on KMP's behalf*** for past harm inflicted by KMI." *Id.* ¶ 9 (emphasis added). Plaintiff alleges that KMP's distribution of too much cash to limited partners and KMGP has harmed KMP by requiring KMP to issue new equity and debt that has "dilut[ed] the ownership interest of existing limited partners" and caused "massive increases in the debt burden that must be borne by KMP." *Id.* ¶¶ 4, 8. In plaintiff's words, "hundreds of millions of dollars exit KMP through improper Distributions and are thereafter not available for maintenance or other operational purposes" and this "leaves KMP vulnerable to, at best, a steady decline in earnings over the coming years and, at worst, an utter inability to respond to problems that may arise." *Id.* ¶ 75; *see also id.* ¶ 77 (KMP's raising new debt "subject[s] KMP to unnecessary and significant annual debt payments"); *id.* ¶ 79 ("KMP exposed to the possibility that market capital will dry up"). Relying on events dating back almost ten years, plaintiff alleges that KMP "is no stranger to serious environmental incidents

resulting from inadequate maintenance and repair of its pipeline systems." *Id.* ¶ 21. Plaintiff claims that because of KMGP's actions, KMP "runs the risk" that it will "be unable to attract new investors, exposing a fundamental lack of sustainability." *Id.* ¶¶ 84-87.

Plaintiff alleges breach of contract by KMGP (Count I), breach of the duty of good faith and fair dealing by KMI and KMGP (Count II), aiding and abetting breach of the duty of good faith and fair dealing by KMI (Count III), and tortious interference with contract by KMI (Count IV). *Id.* ¶¶ 102-120.

C. The Texas Action

On March 6, 2014, a second limited partner filed a second action, this one in the District Court of Harris County, Texas. Ex. B. The plaintiff in the Texas action challenges the exact same conduct alleged here, but asserts claims for breach of duty (Count I), breach of the implied covenant of good faith and fair dealing (Count II), abuse of control (Count III), and gross mismanagement (Count IV). *Id.* ¶¶ 43-60. The claims are alleged to be derivative in nature and are asserted against the defendants here (KMI and KMGP) as well as KMM and the five directors of KMGP and KMM (Messrs. Kinder, Kean, Gardner, Hultquist and Waughtal). *Id.* ¶¶ 1, 16-24. Demand is alleged to be excused on KMGP because Messrs. Kinder, Kean, Gardner, Hultquist and Waughtal lack disinterestedness and independence. *Id.* ¶¶ 42(a)-(o).

KMP and the defendants in the Texas action intend to move to dismiss or stay that action in favor of proceedings in this Court.

ARGUMENT

PLAINTIFF'S CLAIMS ARE DERIVATIVE AND SHOULD BE DISMISSED DUE TO PLAINTIFF'S FAILURE TO MAKE DEMAND

A. The Claims Are Derivative

Plaintiff concedes that his claims are at least in part derivative (Compl. Intro ¶, ¶¶ 90-101, Count II heading, Count III heading, Count IV heading), but contends that he "primarily raises a direct claim that KMI has breached its contractual obligations to Plaintiff and KMP's other Limited Partners." Compl. ¶ 93. It is well settled, of course, that "[p]laintiffs' classification of the suit is not binding"; rather, "[t]he Court will independently examine the nature of the wrong alleged and any potential relief to make its own determination." *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1035 (Del. 2004); *see also Protas v. Cavanagh*, 2012 WL 1580969, at *5 (Del. Ch. May 4, 2012) ("[t]he court gives little weight to the labels the plaintiff assigns to the claim; instead, 'the court must look to the nature of the wrong alleged, taking into account all of the facts alleged in the complaint, and determine for itself whether a direct claim exists'") (quoting *Hartsel v. Vanguard Grp., Inc.*, 2011 WL 2421003, at *16 (Del. Ch. June 15, 2011), *aff'd*, 38 A.3d 1254 (Del. 2012)).

Plaintiff's claims are entirely derivative. Plaintiff alleges that KMGP breached its contractual obligations under the partnership agreement, that KMP has suffered and will continue to suffer in the future due to KMGP's neglect of KMP's maintenance needs and KMGP's overleveraging of KMP through the incurrence of new debt, and that the value of KMP and plaintiff's investment in KMP has suffered as a result of KMGP's alleged misconduct. *See, e.g.*, Compl. ¶ 8 ("massive increases" in debt

"must be borne by KMP"); *id.* ¶ 75 ("hundreds of millions of dollars exit KMP through improper Distributions and are thereafter not available for maintenance or other operational purposes"); *id.* (this "leaves KMP vulnerable to, at best, a steady decline in earnings over the coming years and, at worst, an utter inability to respond to problems that may arise"); *id.* ¶ 77 (new debt "subject[s] KMP to unnecessary and significant annual debt payments"); *id.* ¶ 79 ("KMP exposed to the possibility that market capital will dry up").

These are classic derivative claims: KMP has "suffered the alleged harm" and KMP "would receive the benefit of any recovery or other remedy." *Tooley*, 845 A.2d at 1033; *see also Kramer v. W. Pac. Indus., Inc.*, 546 A.2d 348, 353 (Del. 1988) (actions alleging mismanagement "allege a wrong to the corporation; i.e., the stockholders collectively, to be enforced by a derivative action"); *Protas*, 2012 WL 1580969, at *6 (claim that is "entirely dependent" on "harm to the Fund" is derivative even where "artfully presented as a claim for the unfair treatment of a particular class of stock"); *TIFD III-X LLC v. Fruehauf Prod. Co.*, 883 A.2d 854, 859-60 (Del. Ch. 2004) (claim that the limited partner breached limited partnership agreement was "a derivative claim because any harm suffered was to the Partnership as a whole, and any recovery would go to the Partnership"). Plaintiff claims that KMP has paid out "too much" in distributions, and any relief presumably would require a "return" to KMP of the "too much" allegedly paid to all parties – plaintiff, the other limited partners, and the general partner KMGP.

Plaintiff also alleges the issuance of new units and a resulting dilution of plaintiff's interest in KMP. Compl. ¶¶ 81-82. This allegation is also derivative, and

certainly does not transform otherwise derivative claims into direct claims. "[D]ilution 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.'" *Feldman v. Cutaia*, 951 A.2d 727, 732 (Del. 2008) (quoting *Gentile v. Rossette*, 906 A.2d 91, 99 (Del. 2006)); *see also Carsanaro v. Bloodhound Techs., Inc.*, 65 A.3d 618, 657 (Del. Ch. 2013) (noting "the traditional characterization of stock dilution claims as derivative"); *Feldman v. Cutaia*, 956 A.2d 644, 657 (Del. Ch. 2007) ("the general rule" is that "equity dilution claims are solely derivative"), *aff'd*, 951 A.2d 727 (Del. 2008); *Oliver v. Boston Univ.*, 2006 WL 1064169, at *16 (Del. Ch. Apr. 14, 2006) ("equity dilution does not generally constitute a direct harm, but, instead, a derivative one").

The narrow exception to this rule stated by the Supreme Court in *Gentile* and *Gatz v. Ponsoldt*, 925 A.2d 1265 (Del. 2007), and discussed at length by this Court in its very recent decision in *Carsanaro*, does not apply here. This exception applies only where shares are issued to a controlling shareholder in a self-dealing transaction (or, as this Court concluded in *Carsanaro*, any self-interested fiduciary), and "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*" and "the end result . . . is an improper transfer – or expropriation – of economic value and voting power *from the public shareholders to the majority or controlling stockholder*." *Gentile*, 906 A.2d at 100, *quoted in Gatz*, 925 A.2d

at 1278 (emphasis added). There must be "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" with "the public shareholders . . . harmed, uniquely and individually, *to the same extent that the controlling shareholder is (correspondingly) benefitted*." *Id.*; *see also Gatz*, 925 A.2d at 1274 ("where a significant or controlling stockholder causes the corporation to engage in a transaction wherein shares having more value than what the corporation received in exchange are issued to the controller, thereby *increasing the controller's percentage of stock ownership at the public shareholders' expense*, a separate and distinct harm results to the public shareholders, apart from any harm caused to the corporation, and from which the public shareholders may seek relief in a direct action") (emphasis added).

Plaintiff alleges no facts falling within this narrow exception to the general rule that dilution claims are derivative. Unlike *Gentile*, *Gatz* and *Carsanaro*, this case does not involve alleged issuances of shares or units to a controlling entity in a self-dealing transaction. Although plaintiff alleges that limited partners suffered dilution because KMP issued new units to *third parties*, the issuance of units in public offerings results in no corresponding increase in KMGP (or KMI)'s stake in KMP. To the contrary, to the extent that plaintiff's limited partnership interest was diluted, KMI's substantial limited partnership interests were correspondingly diluted – and certainly *not benefitted*. *See* Feb. 23, 2011 Form 10K at 123-25 (Ex. E) and Feb. 18, 2014 Form 10K at 5-6 (Ex. A) (showing KMI's overall stake in KMP decreasing from 12.8% to 11.6% from Dec. 31, 2010 to Dec. 31, 2013, roughly the alleged class period, and KMM's stake

decreasing from 29.1% to 28.3%). *See also* Compl. ¶¶ 16-17. Limited partners may suffer dilution vis-à-vis other limited partners, but limited partners as a group suffer no dilution vis-à-vis the general partner. Nor does the issuance of new units "(correspondingly) benefit[ ]" (*Gentile*, 906 A.2d at 100; *Gatz*, 925 A.2d at 1278) KMGP's general partnership interest, which remains the same as it always was – an effective 2% interest. Compl. ¶ 16; Feb. 23, 2011 10K at 152 (Ex. E); Feb. 18, 2014 10K at 138 (Ex. A).

At its core, the exception to the general rule embodied in *Gentile*, *Gatz* and *Carsanaro* is for self-dealing transactions used by controlling shareholders to expropriate economic and voting power from and at the expense of the minority. This exception does not apply here. The issuance of equity and debt more frequently and in higher amounts than plaintiff believes prudent, after which the 100% owner of the general partner also owns a smaller percentage of limited partner interests than before, and before and after which the ownership of the general partner interest remains unchanged, does not constitute expropriation of economic and voting interests from and at the expense of the minority. Plaintiff's allegations do not involve the narrow exception to the general rule that dilution claims are derivative claims as stated in *Gentile*, *Gatz* and *Carsanaro*.

For all of these reasons, plaintiff's claims are derivative claims. They are not derivative simply because they are "artfully presented as a claim for the unfair treatment of a particular class of stock." *Protas*, 2012 WL 1580969, at *6. The alleged harm to KMP caused by KMGP's alleged breach of its contractual obligations to KMP,

including KMGP's alleged neglect of KMP's maintenance needs or by KMGP's alleged overleveraging of KMP through the issuance of new units and the incurrence of new units or new debt, is an alleged harm to KMP and can only be challenged derivatively in KMP's name and, if it occurred, could only be remedied by KMP's recoupment of the alleged "improper" distributions.

B. Demand Is Not Excused

To the extent that plaintiff's claims are derivative (entirely, as explained above, or simply in part, as even plaintiff concedes), the Delaware Revised Uniform Limited Partnership Act requires that "[i]n a derivative action, the complaint shall set forth *with particularity* the effort, if any, of the plaintiff to secure initiation of the action by a general partner or *the reasons for not making the effort*." 6 *Del. C.* § 17-1003 (emphasis added). The rules governing the demand requirement – and their importance – in the corporate context are well known to this Court, and "the issues in determining demand futility for partnership law appear identical to those in corporation law." *Litman v. Prudential-Bache Props., Inc.*, 1993 WL 5922, at *3 (Del. Ch. Jan. 4, 1993); *see also Forsythe v. ESC Fund Mgmt. Co. (U.S.)*, 2007 WL 2982247, at *5 (Del. Ch. Oct. 9, 2007) ("Delaware courts look to pleading standards developed in the corporate context to determine whether a limited partner has alleged particularized facts satisfying section 17-1003 requirements"); *Seaford Funding L.P. v. M&M Assocs. II, L.P.*, 672 A.2d 66, 70 (Del. 1995) ("corporate standards apply to limited partnerships in the 'demand excused' analysis") (citation omitted).

Plaintiff alleges that demand is excused on "KMI, as KMP's General Partner," with plaintiff defining KMI to include KMI and KMGP collectively (Compl. ¶ 94 and Intro. ¶), but KMGP is obviously the entity on which a demand would be made in a derivative action on behalf of KMP. Plaintiff alleges that demand is excused on KMGP because KMI has a financial interest in the outcome of this action and KMI "wholly owns and controls KMGP" and "makes all relevant decisions with regard to KMP's accounting and operations" and "would control an investigation of the accounting and other conduct" challenged in this lawsuit. Compl. ¶¶ 97, 99. Plaintiff's allegation that KMI "makes all relevant decisions with regard to KMP's accounting and operations" and "would control an investigation of the accounting and other conduct" challenged in this lawsuit (Compl. ¶¶ 97, 99) is wholly conclusory. The limited partnership agreement and public filings of which this Court may take judicial notice concerning the management of the business and affairs of KMP provide that KMM "manages and controls [KMP's] business and affairs" and KMM's board of directors "performs the functions and acts as [KMP's] board of directors." Feb. 18, 2014 Form 10K at 5, 97-98 (Ex. A); *see also* Compl. ¶ 17 (describing KMM as "the entity to which KMGP has delegated its management of KMP"). KMP's public filings identify five directors of KMGP (and KMM): Richard D. Kinder, Steven J. Kean, Ted A. Gardner, Gary L. Hultquist and Perry M. Waughtal. Plaintiff does not (and cannot) allege that KMGP (and KMM)'s directors – a majority of the board – are not independent. KMP's public filings affirm that "[t]he board has affirmatively determined that Messrs. Gardner, Hultquist and Waughtal, who constitute a majority of the directors, are independent as described in our

governance guidelines and the NYSE rules" and that "each has no family relationship with any of the directors or executive officers" of KMI, KMGP or KMM and "each has no direct or indirect material interest in any transaction or proposed transaction required to be reported under Section 404(a) of Regulation S-K." Feb. 18, 2014 Form 10K at 83-84, 98 (Ex. A); *see also Grobow v. Perot*, 539 A.2d 180, 184 n.1 (Del. 1988) (absent allegations to the contrary, Delaware law presumes that directors are outside, non-management directors).

Plaintiff has failed even to attempt to allege facts excusing demand on KMGP's independent board of directors. Plaintiff's contention that demand is excused thus turns entirely on whether the need for demand is determined by an examination of the general partner as a corporate entity or an examination of the general partner's board of directors. If it is the former, as plaintiff assumes, then demand is excused. If it is the latter, then demand is required.

Our Supreme Court has never considered this question. This Court has twice held, first in a decision by then-Vice Chancellor Steele in *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 1998 WL 832631, at *5 (Del. Ch. Nov. 10, 1998), and more recently in a decision by Vice Chancellor Noble in *Gerber v. EPE Holdings, LLC*, 2013 WL 209658, at *13 (Del. Ch. Jan. 18, 2013), that demand in this context should be assessed "in relation to the corporation itself, not its internal decisionmaking apparatus." *Gotham*, 1998 WL 832631, at *5, *quoted in Gerber*, 2013 WL 209658, at *13. *Gotham*, however, is a dated decision, written at a time when, as then-Chancellor Chandler put it, derivative suits involving limited partnerships were "few and far between." *Dean v.*

Dick, 1999 WL 413400, at *2 (Del. Ch. June 10, 1999). *Gerber* itself acknowledged that "[a]pplying derivative rules to partnership-related claims can be troubling" and followed *Gotham* without substantial discussion of the issue and following briefing of the issue by the defendants limited to a footnote in a reply brief. Ex. C (*Gerber* briefs, footnote 13 in reply brief).[2]

We respectfully submit that the decisions in *Gerber* and *Gotham* were incorrectly decided to the extent they hold that demand is excused as a matter of law in any derivative action brought by a limited partner against a general partner, without regard for the independence of the decision-making structure in place within the general partner. The decisions in *Gotham* and *Gerber* each acknowledge that "'the presence of a majority of interested directors within a corporate general partner might be one way of demonstrating demand futility as to the corporate general partners,'" but instead rely on the statutory reference in 6 *Del. C.* § 17-1003 to "the general partner and not specifically to the general partner's governing body." *Gerber*, 2013 WL 209658, at *13 (quoting

[2] Two additional Court of Chancery decisions have noted this issue without deciding it. In *Brinckerhoff v. Enbridge Energy Co.*, 2011 WL 4599654 (Del. Ch. Sept. 30, 2011), *aff'd*, 67 A.3d 369 (Del. 2013), Vice Chancellor Noble, in a pre-*Gerber* case, did not decide this issue in a case where plaintiff alleged demand futility with respect to both the entity and its board. *Id.* at *7. In *DiRienzo v. Lichtenstein*, 2013 WL 5503034 (Del. Ch. Sept. 30, 2013), a post-*Gerber* case, Vice Chancellor Parsons distinguished *Gotham* and *Gerber* on the ground that *DiRienzo* involved a limited partnership in which limited partners elected the directors of the general partner, while *Gotham* and *Gerber* did not. *Id.* at *18. We respectfully submit that this is a distinction without a difference in light of (1) the *USACafes* discussion below, and (2) the rule in Delaware that "[i]t is the care, attention and sense of individual responsibility to the performance of one's duties, not the method of election, that generally touches on independence." *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984), *quoted in, e.g.*, *In re S. Peru Copper Corp. S'holder Derivative Litig.*, 52 A.3d 761, 770 n.14 (Del. Ch. 2011), *aff'd sub nom. Ams. Mining Corp. v. Theriault*, 51 A.3d 1213 (Del. 2012).

Gotham, 1998 WL 832631, at *5). This Court correctly noted in *Feeley v. NHAOCG, LLC*, 62 A.3d 649 (Del. Ch. 2012), however, that "[b]reach of fiduciary duty is an equitable claim, and it is a maxim of equity that 'equity regards substance rather than form,'" and that "[i]t is the very nature of equity to look beyond form to the substance of an arrangement.'" *Id.* at 668 (quoting *Monroe Park v. Metro. Life Ins. Co.*, 457 A.2d 734, 737 (Del. 1983) and *Gatz v. Ponsoldt*, 925 A.2d 1265, 1280 (Del. 2007)). Applying this maxim, this Court stated in *Feeley* that "Delaware corporate decisions consistently have looked to who wields control in substance." *Id.* Here, it is plainly the independent director controlled boards of KMGP and KMM, not the inanimate KMGP entity itself or KMI, "who wields control in substance."

The Court in *Gotham* also relied on a statement that "it is the general partner who owes the limited partners fiduciary duties, not the management of the general partner, even though they make the decisions for that business entity." *Gotham*, 1998 WL 832631, at *5. *Feeley* speaks to this issue, too, noting that then-Chancellor Allen in *In re USACafes, L.P. Litig.*, 600 A.2d 43 (Del. Ch. 1991), rejected a claim that "the members of the board of the corporate general partner only owed fiduciary duties to its stockholders, not to the limited partners," because "'one who controls property of another may not, without express or implied agreement, intentionally use that property in a way that benefits the holder of the control to the detriment of the property or its beneficial owner.'" 62 A.3d at 670 (quoting *USACafes*, 600 A.2d at 48). The court in *Feeley* noted that this is consistent with "the equitable tradition of looking to the substance of where control lay." *Id.* Then-Vice Chancellor Steele's decision in *Gotham* did not cite or

discuss *USACafes* – but in his subsequent decision in *In re Boston Celtics L.P. S'holders Litig.*, 1999 WL 641902, at *4 (Del. Ch. Aug. 6, 1999), then-Vice Chancellor Steele stated – in words contrary to *Gotham* – that "[i]t is well settled that, unless limited by the limited partnership agreement, the general partner of a Delaware limited partnership and the directors of a corporate General Partner who control the partnership, like the directors of a Delaware corporation, have the fiduciary duty to manage the partnership in the partnership's interests and the interests of the limited partners." *Id.* at *4. Here, the obligations are governed by the limited partnership agreement, which, among other potentially relevant provisions, contains an express procedure for referring issues of conflicts of interest to the independent directors constituting the board's Conflicts and Audit Committee, and sets forth certain standards for these independent directors when so acting. Partnership Agreement ¶ 6.9(a) and Definitions in Art. II (Ex. D). Plaintiff alleges no reason why the demand could not be submitted to the Conflicts and Audit Committee comprised entirely of independent directors.

Any rule assessing the need for demand on a general partner by looking solely at its corporate structure rather than the independence of its decision-making apparatus would excuse demand in all cases involving derivative claims against the general partner, allowing the futility exception to swallow the demand requirement in 6 *Del. C.* § 17-1003. Worse, it would discourage the utilization by general partners of independent decision-making bodies – something plainly not in the interest of limited partners.

For all of these reasons, KMP, KMGP and KMI respectfully submit that *Gotham* and *Gerber* were wrongly decided and that the need for a demand on KMGP should be assessed by examining KMGP's board of directors. Plaintiff does not (and cannot) allege that the majority of KMGP's board lacks disinterestedness or independence or that demand is excused on that board on any other ground.

CONCLUSION

For all of these reasons, this action should be dismissed.

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Dated: March 24, 2014