IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

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

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

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

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

APPEARANCES:

JOEL FRIEDLANDER, ESQ.
CHRISTOPHER M. FOULDS, ESQ.
BENJAMIN P. CHAPPLE, ESQ.
Friedlander & Gorris, P.A.
-and-
MARK LEBOVITCH, ESQ.
DAVID WALES, ESQ.
of the New York Bar
Bernstein, Litowitz, Berger & Grossmann LLP
for Plaintiff

WILLIAM M. LAFFERTY, ESQ.
D. McKINLEY MEASLEY, ESQ.
Morris, Nichols, Arsht & Tunnell LLP
-and-
W. BRANTLEY PHILLIPS, JR., ESQ.
JAMIE L. BROWN, ESQ.
of the Tennessee Bar
Bass Berry & Sims PLC
for Defendant Healthways, Inc. and the Individual Defendants

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

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THE COURT: Welcome, everyone.

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

Did you want to introduce your colleagues?

MR. FRIEDLANDER: I am happy to, actually.

Good afternoon, Your Honor.

THE COURT: Hello.

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

THE COURT: Good to see you all.

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

THE COURT: Gentlemen, good to see you.

Mr. Sirkin, how are you?

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

THE COURT: Welcome.

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

hear the Healthways motion first and then ours?

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

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

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

THE COURT: Good to see all of you.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

MR. LAFFERTY: Yes. Yes.

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

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

assert the claim.

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

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

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

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

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

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

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

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

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

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

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

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

At the end of 2013, North Tide issued a

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

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

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

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

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

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

The first scenario would be if you

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

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

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

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

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

and the debt to come due. Right?

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Instead, the Court found that because

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

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

In Sandridge, again --

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

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

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

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

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

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

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

Your Honor, again, I'm prepared to stand

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

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

THE COURT: Thank you, Mr. Lafferty.

MR. LAFFERTY: Thank you.

MR. MURPHY: May it please the Court. Your Honor, my name is Greg Murphy, and I am with the law firm of Moore & Van Allen in Charlotte, North Carolina. And I represent SunTrust, who was the administrative agent for the bank group that extended credit in the form of a syndicated credit facility in the amount of $400 million to Healthways.

There are two ways that Your Honor could

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

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

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

This provision basically is designed to

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

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

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

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

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

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

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

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

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

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

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

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

So all of those, I think, provide

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

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

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

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

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

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

not our motion to dismiss should be granted.

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

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

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

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

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

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

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

The problem with that, Your Honor, is

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

THE COURT: At the point of knowing participation.

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

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

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

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

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

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

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

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

THE COURT: That's ongoing. Right?

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

been seven amendments to this agreement.

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

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

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

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

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

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

MR. MURPHY: Yes.

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

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

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

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

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

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

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

The last thing I do want to touch on --

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

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

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

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

THE COURT: Thank you.

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

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

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

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

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

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

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

THE COURT: Let me interrupt you for a second.

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

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

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

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

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

advantage of the good conditions that we have."

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

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

Now, I'll just touch on some of the

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

MR. LEBOVITCH: Yes, exactly, Your Honor.

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

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

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

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

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

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

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

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

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

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

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

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

THE COURT: Thank you.

Reply.

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

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

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

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

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

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

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

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

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

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

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

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

THE COURT: Thank you.

MR. LAFFERTY: Thank you, Your Honor.

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

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

argument is obviously focused from a very different perspective.

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

stockholders ...."

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

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

Thank you.

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

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

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

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

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

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

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

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

2012 agreement has been amended three times since then.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

on all fours here.

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

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

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

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

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

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

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

was, if there was any, with SunTrust.

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

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

and ripeness are, indeed, related.

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

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

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

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

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

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

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

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

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

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

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

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

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

MR. LAFFERTY: No questions, Your Honor.

THE COURT: All right.

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

MR. MURPHY: No questions, Your Honor.

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

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

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

MR. LEBOVITCH: Thank you.

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

MR. LEBOVITCH: Okay.

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

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

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CERTIFICATE

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

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

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