UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

Michael Tate, Joseph Shuster, Lyle Evanson and John Ayers, individually and on behalf of all other individuals similarly situated,

Plaintiffs,

vs.

Restaurant Technologies, Inc., Parthenon Capital LLC, Jeffery R. Kiesel, John C. Rutherford, Jonathan O. Grad, Zachary F. Sadek, Philip A. Clough and Robert E. Weil,

Defendants.

Civil File No. 09-cv-02076 (MJD/JJG)

PLAINTIFFS' MEMORANDUM IN OPPOSITION TO DEFENDANTS' MOTION FOR PARTIAL SUMMARY JUDGMENT AND IN SUPPORT OF PLAINTIFFS' RULE 56(f) REQUEST FOR CONTINUANCE

[FILED UNDER SEAL]

INTRODUCTION

Plaintiffs Mike Tate, Joseph Schuster, Lyle Evanson and John Ayers ("Plaintiffs") file this Memorandum in Opposition to Defendant Restaurant Technologies, Inc.'s ("RTI") Motion for Partial Summary Judgment. RTI's motion seeks dismissal of Count IX of the First Amended Complaint which calls for a declaration that the recapitalization which took place in June of 2009 is void.

RTI's premature motion is not premised upon the argument that the recapitalization process engineered by the Individual Defendants was legal, much less equitable. RTI does not present *any* facts attempting to justify the propriety of the recapitalization which was employed to strip the putative Class of its ownership in RTI and the rights which accompany such ownership. Apparently indifferent to the legal

significance of the pervasive self-dealing and misrepresentations that occurred, RTI simply argues that the prospect of declaratory relief poses an "unnecessary risk" which is "interfering" with sales plans. (*See* Defendant RTI's Memorandum in Support of Summary Judgment ("Def. Mem.") (Dkt. # 74 at 2).) RTI's motion is based solely on the notion that it may be difficult to unwind the recapitalization which was employed to enrich RTI's major shareholder, Defendant Parthenon Capital ("Parthenon"), at the expense of the putative Class.[1]

As set forth below, material facts support the assertion that the 2009 recapitalization was tainted by self-dealing and misrepresentations resulting in the improper conversion of RTI's equity. Plaintiffs request that the Court not reward such wrongful conduct by prematurely limiting Plaintiffs' remedies and thereby tacitly acknowledging the false claim of ownership by Defendants. It is counterintuitive to suggest that the Court should limit the form of equitable relief it can grant before it has considered (or even been thoroughly presented with) Plaintiffs' claims on their merits. Plaintiffs are entitled to the full scope of potential equitable relief implicated by the claims of their Amended Complaint. Defendants motion should be denied.

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[1] RTI's request to dismiss one of Plaintiffs' claims is solely premised on the hope that a sale will actually occur. RTI does not advise what happens if the Court follows its lead, dismisses the rescission claim and then no sale occurs ... do the claims get reinstated?

BACKGROUND

A. PROCEDURAL BACKGROUND.

1. Pleading Status.

The Complaint was originally filed in State Court in July 2009 shortly after Plaintiffs learned that the recapitalization closed. The Defendants removed the case to federal court. (Dkt. # 1.) A motion to dismiss was filed, briefed, heard and ruled upon. (Dkt. # 54.) A motion for class certification is pending and is scheduled to be heard before this Court on June 24, 2010.[2] (Dkt. # 63.) A motion to permit the assertion of punitive damages is also pending and is scheduled to be heard by Judge Graham on June 23, 2010. (Dkt. # 82.)

2. Discovery Status.[3]

The parties have been operating under a Pretrial Order (Dkt. # 21) setting forth a factual discovery cutoff of July 1, 2010, a subsequent exchange of expert reports, a dispositive motion deadline of October 1, 2010 and a trial ready date of February 1, 2011. By agreement of the parties, the Court recently moved back a few of the deadlines. (Dkt. # 97.) However, while certain discovery remains to be completed, consistent with the Pretrial Order, a considerable amount of discovery has occurred as set forth below.

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[2] Defendants do not oppose class certification. Rather, Defendants attempt to accomplish within that motion practice what they are also trying to accomplish in the instant motion by arguing that declaratory relief is unavailable as a class-wide remedy. (Dkt. # 69.)

[3] A portion of Plaintiffs' argument involves Rule 56(f). Accordingly, an overview of the discovery activities which have occurred and which are yet to take place is necessary.

a. Third-Party Document Discovery

The following document subpoenas were issued to third parties and responded to:

Third-Parties	Document Production Date
Chartwell Financial	11/05/09
Cargill	11/05/09
McDonald's	11/10/09, 11/20/09, 12/02/09
Burger King	10/30/09, 12/08/09
Jack in the Box	12/02/09, 12/08/09
Wells Fargo	11/20/09
Golden State Foods	04/10/10
Yucaipa	02/19/10, 02/22/10
Piper Jaffray	12/21/09
Robert W. Baird	01/25/10, 01/28/10
Gemini Investors	11/20/09, 12/02/09
St. Paul Commodities	11/20/09
William Blair & Co.	05/27/10

In addition, the following third-party document subpoenas are currently outstanding:

	Status
Sankaty Advisors LLC	- Objection to any production
KPMG Peat Marwick	- Subpoena recently issued/no response to date
Wells Fargo	- Request to review original proxy documents being processed[4]

b. Production of Party Documents

The production of documents by the Defendants has not proceeded in nearly as an efficient fashion as third-party production. Prior to the commencement of the litigation,

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[4] For more details regarding the status of these productions, *see* Affidavit of Robert C. Moilanen (hereinafter "Moilanen Aff.") submitted in support of Rule 56(f) argument. While Plaintiffs firmly believe that the affidavits submitted by Defendants are immaterial to the relief which they request, the Moilanen Aff. is provided to explain why information is unavailable to contest the immaterial assertions made within the affidavits.

Defendant RTI produced certain documents in response to a books and records request. In response to that request, RTI initially "rolled out" documents slowly as set forth below:

5/15/09:	**431-page proxy materials concerning recapitalization received by shareholders. The proxy materials included a merger agreement which stated that a condition of the recapitalization/merger was the no more than 10% of common shareholders vote against it** (Dkt. # 11, Ex. 1 at p. 21);
5/22/09:	**Books and records request delivered to RTI** (Affidavit of Nathan P. Brennan (hereinafter "Brennan Aff.") at Ex. 1);
6/1/09:	412 pages of documents produced by RTI in response to the books and records request;
6/2/09:	1,426 additional pages of documents produced by RTI in response to the books and records request;
6/3/09:	**The date of a shareholder informational meeting concerning the recapitalization** - 540 pages of additional documents produced by RTI in response to the books and records request;
6/4/09:	**The date of a shareholder letter stating "We do not believe the proposal is fair to the common shareholders but, as discussed below, have not been given adequate time or information to fully assess the proposal."** (Brennan Aff. at Ex. 2) - 238 pages of additional documents produced by RTI in response to the books and records request;
6/5/09:	185 pages of additional documents produced by RTI in response to the books and records request;
6/8/09:	96 pages of additional documents produced by RTI in response to the books and records request;
6/10/09:	1,079 pages of additional documents produced by RTI in response to the books and records request;

6/12/09: **The date of the vote on the recapitalization in which over 34% of RTI common shareholders voted against the recapitalization** (Brennan Aff. at Ex. 3);

6/16/09: **The date the RTI Board of Directors waived the 10% opposition voting condition** (Brennan Aff. at Ex. 4);

6/24/09: **The date the recapitalization transaction closed;**

7/17/09: **Complaint filed and served in state court along with document requests to Defendants.**

Plaintiffs served document requests on RTI with the initial filing and service of the Complaint in July 2009. Plaintiffs also subpoenaed the RTI attorneys who handled the recapitalization transaction. Defendants' removal of the action to federal court (which required that a Rule 26 conference must occur prior to the commencement of discovery) and RTI's motion to dismiss delayed the production of records from RTI and its attorneys. Thereafter, Defendants engaged in a "rolling" production process which hindered Plaintiffs' ability to join issues and engage in deposition discovery.[5] Production of documents from RTI and its counsel occurred on the following dates:

11/4/2009: RTI produces 2,055 pages of documents;

11/20/2009: RTI produces 26,132 pages of documents;

12/14/2009: RTI produces 34,703 pages of documents;

12/28/2009: RTI produces 3,101 pages of documents;

1/15/2010: RTI produces 3,535 pages of documents;

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[5] Plaintiffs had no initial objection to a "rolling" production, but did not appreciate the fact that Defendants would roll out documents over a period of six months. As many as 17,000 pages of documents were "rolled out" within the last two weeks, nearly nine months after the document requests were initially served. *See* Moilanen Aff. at ¶ 10.

1/20/2010: RTI produces data room disk;

1/26/2010: RTI produces 91,738 pages of documents;

2/9/2010: RTI produces an additional 2,385 pages of documents;

2/19/2010: RTI produces an additional 17,255 pages of documents;

3/5/2010: RTI produces an additional 45 pages of documents;

4/21/2010: RTI produces an additional 258 pages of documents;

5/4/2010: RTI produces an additional 23 pages of documents;

5/11/2010: RTI produces an additional 2,456 pages of documents;

5/24/2010: RTI produces an additional 14,700 pages of documents.[6]

While Defendants have now confirmed that all responsive documents have been produced, on May 28, 2010 and June 3, 2010, after the close of business, Plaintiffs received certain revised privilege and redaction logs showing that hundreds of documents are still being withheld. (*See* Moilanen Aff. at Ex. D.) Plaintiffs anticipate addressing this issue with the Magistrate Judge in the coming weeks, but are still making an effort to meet and confer.

c. **Deposition Discovery**

Limited deposition discovery has occurred thus far. The depositions which have occurred include:

John Ruelle – Former RTI CFO
Jack Grunewald – RTI Board member
Kenneth Larson – RTI Board member
Molly Simmons – Gemini investor

[6] In addition, Defendant Parthenon Capital produced approximately 75,000 pages of documents on March 5, 2010 in response to a subpoena served in November 2009.

Shane Grutsch – St. Paul Commodities
Thomas Corvelli – McDonald's Corp.
Wilford Becker – Chartwell Financial
Jack Ayers – Plaintiff/Class Representative
Joseph Shuster – Plaintiff/Class Representative
Lyle Levinson – Plaintiff/Class Representative
Michael Tate – Plaintiff/Class Representative
David Wolf – RTI controller
Peter Kies – Robert W. Baird
Kelley Drake – William Blair & Co.[7]

Pursuant to agreement of the parties, the following depositions are currently scheduled:[8]

Deponent	**Date**
Lisa Merryfield	(TBD)
Eric Larson	June 7, 2010
J.T. Haines	June 8, 2010
Timothy Hearn	June 9, 2010
Defendant Robert Weil	June 11, 2010
Gordon Griffin	June 15, 2010
Defendant Zachary Sadek	June 16, 2010
Defendant John Rutherford	June 18, 2010
Defendant Jonathan O. Grad	(TBD)
Bill Sanderson	(TBD)
Defendant Jeffrey Kiesel	June 25, 2010

[7] The depositions of Mr. Kies and Mr. Drake occurred on June 2 and 3, 2010, respectively, and final transcripts are not yet available.

[8] In addition, in light of the belated production of 17,000 pages of documents within the last two weeks, Mr. Grunewald and Mr. Larson may have to be recalled. Further, Defendants have recently expressed an interest in taking several additional depositions.

Deponent	**Date**
James Athanasoulas	June 28, 2010
Defendant Philip A. Clough	June 30, 2010

FACTUAL BACKGROUND

The following section provides a few of the material facts pertaining to the 2009 recapitalization of RTI and the reasons Plaintiffs are seeking declaratory relief as one of the available remedies for Defendants' wrongdoing.[9]

After a proposed [redacted] sale of RTI fell through in late 2008, the controlling shareholder of RTI (Defendant Parthenon) decided to engage in a recapitalization process.[10] In October 2008, Defendant Jon Grad, a Parthenon principal and member of the RTI board, wrote an internal Parthenon email stating:

> . . . you guys know enough to assume that if we went down a path in which we put a large slug of additional equity (say $25M) into RTI but did in which that was technically a change of control transaction, but in which we still ended up as control shareholders, that they would be okay rolling over? I ask because it's likely that the best way to solve our shareholder issues is to do a merger proceeded by a shareholder meeting and vote in which shareholders would vote to cram themselves down.

[9] A more complete account of Defendants' improper conduct is set forth in Plaintiffs' Memorandum in Support of Assertion of Punitive Damages (Dkt. # 82.) and the accompanying Affidavit of Larina A. Alton (Dkt. # 83.).

[10] Parthenon and ABS appointed a majority of the RTI Board and ran the RTI Board for their own interest during this time period. Parthenon and ABS were holders primarily of preferred stock in RTI.

(Brennan Aff. at Ex. 5.)[11] Shortly after Grad's email was circulated, Parthenon put several million dollars into RTI at a 30% accretion rate with 100% conversion rights in a recapitalized RTI (Series B-2 stock). No alternative financing was seriously considered at the time and no fairness opinion was obtained at the time.

The RTI Board sought and obtained legal advice from Dorsey & Whitney on their fiduciary obligations when the interests of various classes of capital stock diverge. Specifically, it appears that Parthenon was looking to obtain legal advice permitting them to avoid meeting their fiduciary obligations to common shareholders. (Brennan Aff. at Ex. 7 (RTI 206214).) However, the advice they received included the following:

> Generally, (<u>assuming a party is not on both sides of a transaction</u>) the business judgment rule protection applies to such decisions . . . if a board's duty with regard to diverging interest between shareholders is to act without self interest and the BJR applies, this does not then, I presume preclude decisions that are ultimately favorable to the preferred and not the common. Simply put, the board owes a fiduciary duty to all stakeholders.
>
> ***
>
> Regarding the <u>Equity-Linked</u> case and the Chancellor Allen quote that it is generally the board's duty to *prefer the interest of the common stock* (as it sees them) to the interest created by the special rights of the preferred where there is a conflict – *it does appear to be good law.*

(Emphasis added) (Brennan Aff. at Ex. 8.)

[11] The candor of Defendant Grad's email is surprising in light of the fact that he had earlier advised his colleagues at Parthenon that they should "discuss matters live versus email given legal situation." (Brennan Aff. Ex. 6.)

Parthenon then began negotiations with RTI's lenders — Sankaty Advisors — and, in complete disregard of the legal advice they received, conducted self-serving negotiations which included the following terms:

- RTI's agreement to conduct a recapitalization and force common shareholders to sign releases in order to maintain any equity interest in recapitalized RTI.[12]
- Having RTI pay $400,000 of closing costs to Parthenon at the time of the recapitalization.
- Having RTI agree to enter into a Management Services Agreement with a Parthenon subsidiary (PCap) in which RTI would pay PCap $450,000 annually.
- Agreeing that Parthenon would receive 1% of any subsequent sale price when RTI was eventually sold.
- Employing, for purposes of the merger, a $140 million enterprise value that would wipe out existing shareholder value while quietly supplying the lenders with warrants to purchase equity in recapitalized RTI.
- Agreeing that, when a recapitalization occurred, the Series B-1 preferred stock, like the Series B-2 preferred stock, would be converted at 100% of value including liquidation preferences.[13] In order to do that, the recapitalization would have to be misnomered a "merger" even though no change of control occurred.[14]

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[12] Forcing RTI common shareholders to sign releases appears to have originated with Parthenon and its counsel. (Alton Aff., Ex. 9, Req. Nos. 200-201.) However, counsel at Dorsey & Whitney approved the use of releases which were designed to require shareholders to release all claims if they attempted to maintain their ownership in RTI. (Brennan Aff. at Ex. 9.)

[13] While Parthenon held 43% percent of the Series B-1 offering, Sankaty also owned certain Series B-1 preferred stock making the agreement that the B-1 stock would get 100% of accreted value in the recapitalization not surprising since the negotiations carving up RTI's equity were conducted between Parthenon and Sankaty.

[14] In his recent deposition, RTI controller David Wolf admitted that no real change of control occurred when he testified to the relatively simple shifting of RTI's cash and equity among existing preferred shareholders, Parthenon and RTI's lenders. (Brennan

After negotiating an arrangement with the bank on these terms, a Special Committee was formed which was entrusted to "review and approve of" the fairness of the recapitalization transaction. As set forth in detail in Plaintiffs' Memorandum in Support of Motion for the Assertion of Punitive Damages (Dkt. # 82), the Special Committee was not "independent" because its chairman, Defendant Kiesel, was compromised by his own self-interest in obtaining options in recapitalized RTI and had already agreed to the terms negotiated with Sankaty. (*See* Plaintiffs' Memorandum in Support of Assertion of Punitive Damages (Dkt. # 82).) Further, one of the other members entrusted to protect the interests of RTI common shareholders, Kenneth Larson, had told Parthenon "he didn't want to cause a problem" *before* the Special Committee was formed and he was selected to be on it. (Brennan Aff. at Ex. 12.) Finally, the third member of the Special Committee had been a Parthenon representative on the RTI Board for eight years.[15] The Special Committee, comprised of a less than independent membership, spent a cumulative total of three hours reviewing this "complex" transaction and approved it without serious debate or any meaningful change.[16]

Soon after, RTI shareholders received false and misleading proxy materials. Documents produced thus far in the litigation show that positive information about RTI

Aff. at Ex. 10 at 94:14-98:18.) Further, Defendant Kiesel admitted in a memorandum that no real change of control occurred. (Brennan Aff. at Ex. 11.)

[15] For more detail about the fact that the Special Committee was little more than an artifice created to merely ratify — not review — the recapitalization transaction, *see* Plaintiffs' Memorandum in Support of Punitive Damages at pages 17–22 . (Dkt. # 82.)

[16] Consistent with the legal advice they had received, Dorsey & Whitney recommended setting up the Special Committee in anticipation of litigation. They noted that such a Committee should be "truly" independent. (Brennan Aff. at Ex. 8 (RTI 206367).)

was stripped out of the proxy memorandum and other material information, like the number of options Defendant Kiesel (chairman of the Special Committee) would receive in recapitalized RTI, was taken out. (*See generally* Plaintiffs' Motion in Support of Punitive Damages (Dkt. # 82) at 18–19 and Plaintiffs' Supplemental Memorandum in Support of Punitive Damages (Dkt. # 90).)

Over 34% of the RTI common shareholders voted against the transaction on June 12, 2009. (Brennan Aff. at Ex. 3.) That percentage, in accordance with the Merger Agreement, should have prevented the recapitalization from occurring. The Merger Agreement provided:

> The obligation of the Company to consummate the transaction contemplated by this Agreement is subject to the satisfaction of the following conditions at or before the closing:
> b) The aggregate amount of dissenting shares (i) with respect to common stock, shall be less than 10% of the shares of common stock entitled to vote on the merger . . .

(Dkt. # 11, Ex. 1 at p. 21 (Langdon Declaration).)

However, on June 16, 2010, the RTI Board controlled by Parthenon and ABS quietly waived the 10% condition.[17] The transaction closed on June 24, 2009. Plaintiffs, who thought they won the vote and effectively stopped the recapitalization from

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[17] Defendant RTI was exceedingly slow to produce these Board minutes. The Board minutes showing this waiver finally emerged as Document No. RTI 174202 in February 2010 as part of Defendants' "rolling" production. Similarly, Defendants did not even produce the Special Committee minutes until the same time period.

occurring, were formally informed of the closing by letter dated June 30, 2010. (Brennan Aff. at Ex. 13.)[18]

The recapitalization resulted in the conversion of RTI's equity. There were numerous obstacles erected to hinder the ability of RTI shareholders to maintain their equity position in recapitalized RTI. First, a grim picture had been painted regarding RTI's value in an effort to discourage interest. Second, RTI common shareholders seeking to convert their shares were wrongfully required to sign releases designed to insulate Defendants, including Parthenon, of liability. Third, RTI shareholders were given the wrong appraisal statute to review for purposes of exercising their rights. Fourth, RTI shareholders had to vote in favor of the recapitalization in order to convert their shares into shares in the new entity. Fifth, to purchase stock in the recapitalized entity, a shareholder was required to not simply purchase stock, but also had to meet additional obligations beyond being an accredited investor. The proxy had the following example:

> By way of example, a purchase of $100,000 of Class Z Stock will require the delivery by such Purchaser at or prior to the Initial Closing of (i) $100,000 (for the Shares), **plus** (ii) $26,667 (pro rata share of $100,000/$15,000,000 (or 0.667%) * $4,000,000 for the Committed Shares of Participations), **plus** (iii) up to $33,333 (pro rata share, or 0.667%, in support of the LOC, which, if drawn down in full ($5,000,000), would result in the issuance to the Purchaser of a Convertible Note in a principal amount of $33,333 ($5,000,000 * 0.667%). These requirements are detailed further below.

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[18] Plaintiffs were first informed that the RTI Board of Directors might consider "waiving" the condition a few days prior to the vote when RTI's counsel wrote a letter implying that was a possibility. (Brennan Aff. at Ex. 14.) That letter, and the subsequent action, serves as further evidence that Plaintiffs "won" the vote.

(Dkt. # 11, Ex. 1 at p. 32.) Barriers were erected that helped ensure that the vast majority of equity in RTI would be transferred/upstreamed to Parthenon and ABS, and that is precisely what occurred.

According to the proxy memorandum, ABS and Parthenon owned the following percentages of outstanding stock of RTI prior to the recapitalization:

Parthenon	45.4%
ABS	11.6%
Total:	**57%**[19]

Knowing that the entire process would likely result in few people buying more RTI shares, the following footnote was buried on Page 58 of the proxy memorandum after a chart showing Parthenon and ABS percentage ownership in RTI:

> As noted above this number assumes that all qualified Stockholders purchase their full Pro Rata allotment in the Offering. If, however, none of the qualified Stockholders purchase their Pro Rata allotment in the Offering, Parthenon will own 63.4% and ABS will own 17.6% of the Post-Recap Capital Stock on an as-converted basis. (Dkt. # 11, Ex. 1 at p. 58 n.1.)

Not surprisingly, Parthenon and ABS now claim to own the following percentages of the recapitalization entity today:

Parthenon	62.3%
ABS	17.4%
Total:	**79.7%**

(Brennan Aff. at Ex. 15.)

[19] The remaining outstanding stock was owned by RTI common shareholders (17%) and others (26%). (Dkt. # 11, Ex. 1 at pp. 56–58.)

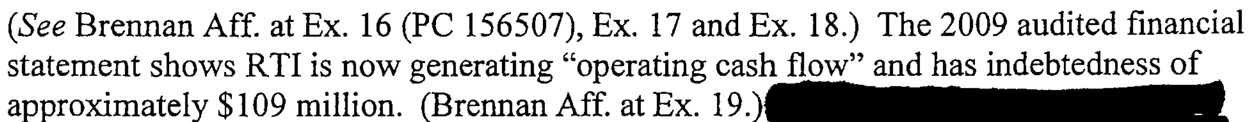
This upstreaming accomplished precisely what Parthenon intended when the recapitalization was initially discussed: namely, to protect and enhance its own investment interest even though that interest "diverged" from the interests of the other RTI shareholders whose interests they were obliged to protect. By upstreaming RTI's equity, Parthenon and ABS assured themselves of recovering their investment in any subsequent sale or initial public offering while the investment of other shareholders in RTI was destroyed.[20]

The above represents a short history of some material facts relating to whether or not Plaintiffs may be entitled to obtain rescission relief in the future. Defendant RTI presented no material facts on these issues and has merely told the Court that they wish to sell the company.

[20] The approximate total dollar amount of the respective investments of Parthenon, ABS, RTI common shareholders and others prior to the recapitalization was as follows:

Parthenon	$46 million
ABS	$17 million
Common	$15 million
Others	$14 million

(*See* Brennan Aff. at Ex. 16 (PC 156507), Ex. 17 and Ex. 18.) The 2009 audited financial statement shows RTI is now generating "operating cash flow" and has indebtedness of approximately $109 million. (Brennan Aff. at Ex. 19.)



ARGUMENT

A. THE STANDARD FOR SUMMARY JUDGMENT AND RULE 56(f).

The moving party carries the burden of proving they are entitled to summary judgment. *See* Fed. R. Civ. P. 56(c). The moving party must first make a preliminary showing that there are no issues worthy of trial. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 330 (1986). The burden of production then shifts to the nonmovant, who must identify evidence demonstrating a genuine issue of material fact. *Id.* at 324. Unlike the burden of production, the ultimate burden of persuasion remains on the moving party. *Id.* at 330. "Credibility determinations, weighing of evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of the Court at the summary judgment stage . . . . The evidence of the nonmoving party is to be believed and all justifiable inferences are to be drawn in its favor." *United States v. Minnesota*, 97 F. Supp. 2d 973, 977 (D. Minn. 2000) (*citing Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986)); *see also Beckmann v. CBS, Inc.*, 192 F.R.D. 608, 617 (D. Minn. 2000); *Callanan v. Runyun*, 903 F. Supp. 1285, 1293 (D. Minn. 1994).[21]

Federal Rule of Civil Procedure 56(f) permits a Court to extend discovery deadlines "[i]f a party opposing [a motion for summary judgment] shows by affidavit that, for specified reasons, it cannot present facts essential to justify its opposition." Fed.

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[21] The burden in this summary judgment setting is particularly acute for Defendant RTI as the allegations are that those who controlled it engaged in self-dealing transactions. In such a setting, the burden of showing that a less than arm's-length transaction was beneficial to the company rests with the Defendants themselves. *See Gentile v. Rossette*, C.A. No. 20213, 2010 WL 2171613, at *8 (Del. Ch. May 28, 2010). Defendants have not made any showing in that regard.

R. Civ. P. 56(f). Thus, Rule 56(f) "allows a summary judgment motion to be denied ... if the nonmoving party has not had an opportunity to make full discovery." *Celotex Corp.* 477 U.S. at 326. To obtain a continuance under Rule 56(f), "a party must file an affidavit describing (1) what facts are sought and how they are to be obtained; (2) how these facts are reasonably expected to raise a genuine issue of material fact; (3) what efforts the affiant has made to obtain them; and (4) why the affiant's efforts were unsuccessful." *Johnson v. United States*, 534 F.3d 958, 965 (8th Cir. 2008).

As set forth above, a great deal of discovery has occurred. However, as set forth in the Moilanen Affidavit, as of the filing of this Memorandum, certain critical discovery remains.[22] Specifically with respect to third-party discovery, document subpoenas issued to Sankaty Advisors and KPMG Peat Marwick have not been responded to, 11,000 pages of material from William Blair & Co. was just received on May 27, 2010, and, as late as this week, Defendants RTI and Parthenon have continued to produce documents and

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[22] One of the principal reasons RTI provides as a basis for its Summary Judgment motion is that the recapitalization is "so inextricably intertwined with two other transaction critical to the financial survival of [RTI] that it cannot be undone without severely harming all parties." (Dkt. # 74 at p. 8; *see also id.* at 9–10 (asserting that the "[m]erger cannot be undone").) Their assertions are based solely on facts the Plaintiffs have not had the opportunity to discover since lenders have not been deposed or produced documents. (*See* Moilanen Aff. at Ex. B.) What the Plaintiffs have discovered is that this was a "simple" transaction that could be "undone" by realigning the equity of RTI. (Brennan Aff. at Ex. 10 at 94:14-98:18.) As described elsewhere herein, this does not only raise a Rule 56(f) issue, it is a fact issue that precludes the application of summary judgment.

privilege logs.[23] The outstanding discovery is pertinent for the pending motion in the following ways:

- Sankaty Advisors, RTI's lender, engaged in negotiations with Parthenon representatives in 2009 regarding the recapitalization. Defendant Robert Weil ("Weil) now states in his affidavit that "Sankaty personnel advised (in 2009) if RTI failed to accomplish the recapitalization merger and to raise additional capital, Sankaty would immediately exercise" any remedies available to it under the Note Purchase Agreement. Weil provides no documentary support for this assertion and, it appears from other documents that Sankaty was not going to "immediately exercise the remedies". Internal Parthenon documents suggest that Parthenon viewed itself as having the upper hand in the negotiations with Sankaty Advisors, were not going to get "bullied" in 2009 and were not rushed to reach an agreement with Sankaty. (*See* Brennan Aff. at Ex. 20.) Further, the RTI controller, who interacted with Sankaty, could not recall Sankaty even threatening RTI with involuntary bankruptcy which was one of the remedies it purportedly could exercise. (*See* Brennan Aff. at Ex. 10 at 75:16-76:8.) Plaintiffs are seeking documents from Sankaty. (*See* Moilanen Aff. at ¶ 4 and Ex. B.)

- KPMG Peat Marwick issued annual financial reports suggesting that, upon a sale or IPO, preferred shareholders would only receive their investment back, not their investment <u>and</u> liquidation preferences. (*See* Brennan Aff. at Ex. 21 (RTI 0078609-10 and RTI 0076670).) This language suddenly changed in their year-end 2007 report when Parthenon, who owned large portions of preferred stock and held Board positions, decided to sell RTI rather than pursue an IPO. *See* Memorandum in Support of Punitive Damages at pp. 6–10. (Dkt. # 82.) Further discovery is required on this issue in order to resolve the instant motion as it may present an issue of fact regarding the distribution of equity in the 2009 recapitalization process. Plaintiffs are seeking documents from KPMG. (*See* Moilanen Aff. at ¶ 10 and Ex. E.)

- William Blair & Co. has served as a financial advisor to RTI regarding a number of transaction. Kelley Drake, whose affidavit Defendants rely on in connection with this motion is a principal of William Blair & Co.

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[23] The massive privilege logs just recently produced (*see* Moilanen Aff. at Ex. D) will result in some motion practice given Defendants' position that they relied on counsel with regard to the recapitalization.

> William Blair & Co. was initially subpoenaed in April 2009 but only recently produced 11,000 pages of documents on May 27, 2010. (*See* Moilanen Aff. at ¶ 6.)

In addition, no deposition of any individual Defendant has yet occurred as a result of the slow "rolling" out of documents by the Defendants, though the depositions have been scheduled.[24] (*See* Moilanen Aff. at ¶ 4.) As recently as May 28, 2010 and June 3, 2010, Defendants provided updated privilege and redaction logs showing that hundreds of documents have been withheld and the propriety of the withholding of those documents will most likely need to be reviewed by the Court. (*See* Moilanen Aff. at ¶ 10 and Ex. D.)

B. DEFENDANT RTI RELIES UPON IMMATERIAL EVIDENCE AND ISSUES OF FACT PRECLUDE SUMMARY JUDGMENT.

A genuine issue of fact is material if it "might affect the outcome of the suit under the governing law." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). In ruling on a motion for summary judgment, "[t]he district court must base its determination regarding the presence or absence of a material issue of factual dispute on evidence that will be admissible at trial." *Firemen's Fund Ins. Co. v. Thien*, 8 F.3d 1307, 1310 (8th Cir. 1993). "[G]enuine issues of material fact cannot be determined on the basis of affidavits." *Evans v. McDonnell Aircraft Corp.*, 395 F.2d 359, 362 (8th Cir. 1968). Affidavits submitted in favor of summary judgment "are to be carefully scrutinized." *Bryan v. Aetna Cas. & Sur. Co.*, 381 F.2d 872, 875 (8th Cir. 1967).

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[24] For example, Defendant Weil, who submitted an affidavit in this matter, is currently to be deposed on June 11, 2010. Defendant Kiesel is scheduled for June 25–26, 2010. (*See* Moilanen Aff. at Ex. A.)

Defendant RTI has not provided the Court with *any* evidence regarding any material fact related to Plaintiffs' Declaratory Judgment claim (Count IX of the Amended Complaint). That claim states:

> The merger/recapitalization process … included numerous false or misleading statements and/or material omissions. These false or misleading statements and/or material omissions … and tainted the merger process with badges of fraud and other wrongful conduct, including self-dealing conduct. Further, the merger/recapitalization was misrepresented as an event triggering liquidation preferences. A real and justiciable controversy exists between the parties … as it involves definite and concrete assertions of rights that emanate from a legal source … a genuine conflict in tangible interests between two parties with adverse interests, and is capable of specific resolution by judgment rather than presenting hypothetical facts that would form an advisory opinion. Plaintiffs are entitled to a declaratory judgment determining and declaring that the merger … is null and void and without any effect … and declaring that their shares in RTI are to be reinstated and returned upon the return/cancellation of any consideration such shareholder may have received in connection with the merger/cancellation.

(Am. Compl. ¶¶ 95–97.) Defendant RTI's affidavits are devoid of any facts that address Plaintiffs' claims or raise a defense to them. Instead, Defendant RTI relies on the following facts in support of its motion for Summary Judgment: (1) RTI's current business plan is to be sold (Dkt. # 74 at pp. 2–3; Dkt. # 77 at ¶¶ 2–7; Dkt. # 76 at ¶¶ 2–7); (2) that if rescission relief is granted, RTI may have to seek bankruptcy (Dkt. # 74 at ¶ 11; Dkt. # 75, at ¶¶ 10–11); (3) that the RTI Board has determined that a sale of RTI is in the best interest of the class (Dkt. # 74 at pp. 2–3; Dkt. # 76 at ¶ 2); and (4) that the recapitalization is "complex" (Dkt. # 74 at pp. 9–10; Dkt. # 75 at ¶¶ 7–8). None of these issues are material.

1. RTI's assertions regarding a sale and potential bankruptcy are immaterial to whether Summary Judgment should be granted.

First, whether or not RTI wishes to be sold is a factual constant, as RTI has sought to be sold for several years. Several investment firms have now advised against such a sale and any such desire must be viewed in light of Parthenon's desire for an "exit strategy" for the benefit of its own funds. In January of 2009, Piper Jaffray advised RTI that RTI was better off conducting an IPO *in 2011*. (Brennan Aff. at Ex. 23.) [redacted]

[redacted]

[redacted] (Brennan Aff. at Ex. 24.) The current desire urging an immediate sale must be viewed against the backdrop of the 2008 sale in which Parthenon placed its own interest ahead of the company. (Dkt. # 82 at pp. 6–10.) Further, Kelley Drake has an economic incentive to push a sale which he did not disclose in his affidavit and which raises a credibility issue. His company stands to make at least several million dollars if a sale goes through. (*See* Brennan Aff. at Ex. 25.) Additionally, Kenneth Larson owns 1.8% of the recapitalized entity and clearly has an economic incentive to push a sale. (*See* Brennan Aff. at Ex. 15.)

Furthermore, whether or not RTI would face bankruptcy should Plaintiffs win their lawsuit has nothing to do with whether the Plaintiffs have alleged claims that give rise to liability or rescission relief.[25] Even though the Board has apparently decided that

[25] Indeed, Plaintiffs claims carry potential liability of millions of dollars, which are equally likely to cause bankruptcy. But whether or not liability for wrongs might cause

it is in the "best interests of all shareholders" for a sale to go forward, that has nothing to do with the merits or whether the court should grant summary judgment on the rescission claim. (Dkt. # 74 at pp. 2–3.) Defendants' assertion that "all shareholders" benefit from a sale is disingenuous since Defendant Parthenon and ABS now falsely claim 80% of the ownership of the recapitalized entity and the shareholders involved in this matter were frozen out. Whether or not Defendants view a proposed sale to be in the "best interests" of all shareholders is irrelevant to whether there was pervasive self-dealing involved in the underlying transaction such that it should be rescinded.

2. **Plaintiffs' Failure to Seek Injunctive Relief Is Not Dispositive of Whether Rescissory Relief is a Potential Remedy and the Transaction is Not Too "Complex" To Be Undone.**

i. **Caselaw supports voiding the transaction.**

Defendants contend that the recapitalization cannot be undone because it is "impossible to unscramble the eggs." (Dkt. # 74 at p. 10.) But Defendant has failed to explain that the recapitalization did not involve any "eggs" that have been scrambled. Unlike Defendants' cited cases, the recapitalization did not introduce a single new individual or entity to the capital structure of RTI — there was no second party to the transaction; there were no public shareholders or exchanges involved; there was no change in control; there was no cessation or expansion of operations, etc. The recapitalization was, at its core, simply an equity raise and the only "egg" scrambled to the benefit of Defendant Parthenon was RTI's equity. *See Nagy v. Bistricer*, 770 A.2d

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bankruptcy is not relevant to whether there is legal liability for wrongs or whether there are material issues of fact such that summary judgment should be granted.

43, 63–64 (Del. Ch. 2000) (refusing to rule out rescission where defendants provided no reasoned basis to conclude that such a remedy is impractical or unwarranted and "the record suggests that the Merger was simply an easily undone card shuffle involving two decks of cards controlled by Defendants, the sole purpose of which might well have been to put pressure on [plaintiff] to depart by way of an expensive appraisal proceeding"). Instead, Delaware courts have concluded that "[q]uite simply, equity will not suffer a wrong." *Weinberger v. UOP, Inc*, No. 5642, 1985 WL 11546, at 9, 10 Del. J. Corp. L. 945, 957 (Del.Ch. Jan. 30, 1985) (granting equitable relief to wronged minority shareholders even though a monetary damage award could not be ascertained).

RTI's controller's testimony clearly did not suggest that the recapitalization was "complex." (*See* Brennan Aff. at Ex. 10 at 94:14-98:18.)[26] Further, unlike Weil's affidavit suggesting that a rescission would somehow bankrupt the company, RTI was sitting with cash of more than $10 million at the end of 2009 and was cash flowing. (*See* Brennan Aff. at Ex. 19 (RTI 193313).)[27] The simple fact is that, after getting back the monies given to Parthenon and the law firms, the financial impact on RTI does not appear to be overwhelming should the Court order a rescission.

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[26] It should be noted that this allegedly "complex" transaction was approved by a Special Committee after a cumulative total of three hours. The recapitalization merely involves a lender (Sankaty Advisors) agreeing to forebear on technical violations of loan covenants and a reshuffling of equity orchestrated by Defendant Parthenon. The closing documents which show sources and uses of funds is hardly "complex." (*See* Brennan Aff. at Ex. 26.)

[27] RTI's cash position was strong enough to pay out hefty bonuses to its officers including Defendant Kiesel, who received a $200,000 bonus at year-end 2009 on top of his $325,000 salary. (Brennan Aff. at Ex. 10 at 30:8-31:1; 37:1-38-2.)

Here, Plaintiffs have promptly asserted that the recapitalization should be voided, have diligently sought relevant discovery, and have vigorously conducted a complex litigation with no delay or disruption. Like in *Nagy*, the Plaintiffs have shown that part of the rationale behind the recapitalization freeze out was to take care of the "shareholder issues." (*See* Brennan Aff. at Ex. 5.) These facts undermine any legal basis for summarily excluding the possibility of rescission as a remedy. *See Ginsburg v. Philadelphia Stock Exch., Inc.*, No. Civ. A. 2202, 2007 WL 1662661, at *3 (Del. Ch. May 31, 2007) ("Although I reserve the right to conclude, after trial, that plaintiff's delay was unreasonable and, thus, to deny rescission or rescission damages at that time, the record at present does not suggest, as a matter of law, that plaintiff moved so slowly as to exclude the possibility of rescission as a remedy. Defendants' [summary judgment] motion is denied.").

Defendants also argue that the "appropriate time for Plaintiffs to complain about the Recapitalization Merger was before it was consummated by moving for an injunction." (Dkt. # 74 at p. 11.) This argument rings hollow, as Plaintiffs were given no actual notice, despite repeated requests, that the merger would be consummated even though one of the conditions for the merger to occur – that no more than 10% of common shareholders vote against it – was not met. (*See* Brennan Aff. 3, and *supra* pp 12–14.) In other words, Defendants themselves did not forthrightly provide Plaintiffs with the information that would have notified Plaintiffs that there actually was a transaction to enjoin, yet have the temerity to assert that Plaintiffs' possible rescission relief should be discarded because Plaintiffs did not seek an injunction. Plaintiffs' potential remedies

should not be dismissed on the basis of circumstances created overwhelmingly by Defendants' wrongful actions. *See Nagy,* 770 A.2d at 63–64 (refusing to dismiss rescission claim where "[t]he behavior of the defendants left Nagy with no practical choice ... Nagy's choice to seek appraisal could be seen as a rational decision to turn down a deal about which he knew nothing. But the fact that Nagy made a rational choice in a ridiculous situation does not render [defendants'] conduct less inconsistent with their fiduciary duties.")

ii. Defendant's cases are distinguishable.

Defendant claims that the lone fact that plaintiffs did not seek injunctive relief determines that rescission or equitable relief is finally and forever foreclosed. For instance, RTI cites *Winston v. Mandor*, 710 A.2d 831 (Del. Ch. 1996), in support of its contention that the potential rescission remedy should be eliminated. But RTI fails to mention the facts and rationale for the *Winston* court's decision that make it distinguishable. First, contrary to the implication in RTI's citation, the defendants in *Winston* sought to dismiss the rescission claim in a *motion to dismiss* after conducting a two-factor analysis: "1) the current circumstances of the challenged transaction, and 2) whether the plaintiff would be unfairly prejudiced in some way by determination *at this early stage of litigation*, that he is foreclosed from obtaining a particular form of relief." *Winston* at 831, 833 (emphasis added). When compared to the circumstances to be analyzed here, the *Winston* court's conclusion is predicated on readily distinguishable facts.

RTI made no effort to address its concerns regarding the appropriate form of relief when it fully briefed and argued a motion to dismiss when RTI's would certainly have been aware of fear that the recapitalization "cannot be undone without essentially destroying the Company." (Dkt. # 74 at p. 9.) Nowhere in the multiple briefs submitted by Defendants over the last 10 months has RTI ever even mentioned to the Court the mortal danger presented by Plaintiffs' rescission claim.

Further, similar to this case, the challenged transactions in *Winston* were completed nearly one year prior. *Id.* But unlike this case the *Winston* plaintiff waited over seven months after the transaction closed before asserting a rescission claim in an amended complaint. *Winston,* 710 A.2d at 832. Here, in contrast, Plaintiffs immediately sought rescission in their original Complaint filed promptly after they learned that Defendants had waived the voting condition under which Plaintiffs had defeated the recapitalization, putting Defendants on immediate notice of their intentions. (Dkt. # 1.) Further, like many of the other cases relied upon by Defendant, the *Winston* court found rescission to be impractical for reasons not present here: Namely, because the *Winston* transaction involved stock traded on a national securities exchange. *Id.* In contrast, RTI stock is not publicly traded, and, precisely because of Defendants' misconduct, RTI has *fewer* shareholders and option holders today than did prior to the recapitalization that Plaintiffs seek to rescind. (*See* Brennan Aff. at Ex. 22.)

RTI's other cited case involve similar distinguishing characteristics. In *In re Lukens Inc. Shareholders Litigation,* the plaintiffs actually filed their lawsuit *before* the merger was voted on by shareholders, but the complaint did not seek injunctive relief of

any kind nor did it allege that any of the proxy materials sent to shareholders were misleading. 757 A.2d 720, 723 (Del. Ch. 1999). Further, the court found that the plaintiffs' complaint "typif[ied] only a claim of negligence or gross negligence," and "provide[d] no support for any inference of bad faith or disloyalty." *Id.* at 728–29. In contrast, Plaintiffs' pleadings chronicle, in vivid detail, extensive bad faith and disloyalty in addition to gross negligence. (*See generally* Am. Compl. (Dkt. # 58) and Mem. Supp. Punitive Damages (Dkt. # 82).) This difference is critical where plaintiffs seek equitable relief like rescission because a breach of the duty of loyalty only *broadens* and *enhances* the court's ability to provide appropriate relief. *In re Primedia Inc. Derivative Litigation*, 910 A.2d 248 (Del. Ch. 2006) ("If the plaintiffs ultimately prove such a breach of the duty of loyalty, this court should not unduly narrow the scope of their recovery.").

Similar distinctions exist with respect to other cases cited by Defendants. For instance, in *Weinberger v. UOP, Inc.*, the court flatly stated

> [W]e do not intend any limitation on the historic powers of the Chancellor to grant such other relief as the facts of a particular case may dictate. The appraisal remedy we approve may not be adequate in certain cases, *particularly where fraud, misrepresentation, self-dealing, deliberate waste of corporate assets, or gross and palpable overreaching are involved.* Under such circumstances, the Chancellor's powers are complete to fashion any form of equitable and monetary relief as may be appropriate, including rescissory damages.

457 A.2d 701, 714 (Del. 1983) (citations omitted and emphasis added).

Additionally, the transaction in *Weinberger* and the cases on which Defendants attempt to rely are all also distinguishable because they all involved publicly traded stock or they involved two or more distinct entities selling or acquiring stock through the

challenged transaction. *See Weinberger*, 457 A.2d at 704 (challenged transaction involved two publicly traded companies); *Lynch v. Vickers Energy Corp.*, 429 A.2d 497, 504, 508 (Del. 1981) (involving stock traded on open market and a transaction that had been closed for over six years); *Goodwin v. Live Entertainment, Inc.*, No. Civ. A. 15765, 1999 WL 64265, at *1 and *6 n.3 (Del. Ch. Jan. 25, 1999) (involving a third-party purchaser and a rescission claim that appeared to be little more than an attempt to circumvent 8 Del. § 102(b)(7) protection for defendant directors); *Arnold v. Society for Sav. Bancorp, Inc.*, No. 12883, 1995 WL 376919, at **3–4 (Del. Ch. June 15, 1995) (involving a third-party acquirer and a pre-merger denial of injunctive relief).

The only relevant issue for consideration is whether or not there are undisputed facts before the Court suggesting that the recapitalization process should be rescinded. Defendants have provided no evidence on that issue, and therefore summary judgment should not be granted.[28]

C. RESCISSION IS A REMEDY ALSO AVAILABLE TO PLAINTIFFS UNDER COUNTS I, IX AND X MAKING DEFENDANTS' MOTION INEFFECTUAL.

RTI has *only* moved for summary judgment with respect to Count IX, which seeks to declare the corrupt recapitalization void, arguing that such relief may have a negative effect on RTI's ability to sell itself. Defendant incorrectly asserts in its memorandum

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[28] While there is a plethora of evidence suggesting that the recapitalization was filled with misrepresentation and self-dealing (*See* Plaintiffs' Memorandum in Support of Punitive Damages and Affidavit of Larina A. Alton at Dkt. # # 82 and 83.), certain discovery remains to be done. Again, Plaintiffs offered to join this rescission issue by considering the filing of cross motions <u>at the conclusion of discovery</u>, but Defendants declined that approach. (*See* Moilanen Aff. at ¶ 11.)

that the declaratory-judgment claim is Plaintiffs' "one equitable claim." (Dkt. # 74 at p. 2.) While Count IX would have the impact of voiding the recapitalization, Counts I (Duty of Loyalty) and X (Entire Fairness) also allow the court to exercise broad equitable authority and could result in an equitable remedy which would restore the parties to their positions prior to the recapitalization. Though relief granted pursuant to these claims would also presumably inconvenience RTI, RTI has not sought summary judgment regarding those claims making the current motion of limited effect.

It is clearly established under Delaware law that rescission is an available remedy for breach of fiduciary duty claims. *See Lynch v. Vickers Energy Corp.*, 429 A.2d 497, 500 (Del. 1981) ("[A] claim founded on a breach of fiduciary duty permits a different form of relief, that is, an accounting or rescission or other remedy afforded for breach of trust by a fiduciary."). Because an entire-fairness analysis encompasses the fiduciary obligations of defendants, Delaware courts do not casually relinquish the ability to fashion rescission-based relief for violation of entire fairness. *See Nagy*, 770 A.2d at 63–64 (Del. Ch. 2000) ("Although the defendants would have me rule out the option of rescission now, they have provided me with no reasoned basis to conclude that such a remedy is impractical or unwarranted. . . .[Defendants] have the burden to show that the Merger is entirely fair and have already fallen short of that standard. They had the economic motive to advantage themselves at the expense of [Plaintiff] and structured the Merger in a highly unusual and eyebrow-raising way."); *see VGS, Inc. v. Castiel*, No. C.A. 17995, 2000 WL 1277372, at *5 (Del. Ch. Aug. 31, 2000) ("I also find that [defendants] failed to discharge their duty of loyalty ...[.] Accordingly, I declare that the

acts taken to merge the LLC into VGS, Inc. to be invalid and the merger is ordered rescinded.").

Therefore, even if a request to dismiss Count IX (Declaratory Judgment) based upon Defendant's contentions had merit, the Court could still effectively rescind the transaction pursuant to the other equitable claims in the Amended Complaint. However, there is no rationale for precluding the relief allowed pursuant to three of the claims of the Amended Complaint *before* any determinations on the merits have been (or can be) made, and Defendant has made no effort to show that the transaction was fair such that the other forms of relief sought in other counts should be foreclosed.

CONCLUSION

For all the above reasons, Plaintiffs request that Defendants' motion be denied.

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