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PARAMETRIC SOUND CORPORATION, TB HOLDINGS, INC., KENNETH POTASHNER; ELWOOD NORRIS; SETH PUTTERMAN; ROBERT KAPLAN; ANDREW WOLFE; and JAMES HONORE,

Petitioners,

vs.

THE EIGHTH JUDICIAL DISTRICT COURT, in and for the County of Clark, State of Nevada, and THE ELIZABETH GONZALEZ, District Judge,

Respondents,

and

VITIE RAKAUSKAS, individually and on behalf of all others similary situated, and Intervening Plaintiffs RAYMOND BOYTIM and GRANT OAKES,

Real parties in interest.

No. 66689

District Court No. A-13-686890-B
Dept. No. XI

FILED

FEB 17 2015

TRACIE K. LINDEMAN
CLERK OF SUPREME COURT
BY S. Young
DEPUTY CLERK

ANSWER OF REAL PARTIES IN INTEREST TO THE PETITION FOR WRIT OF MANDAMUS OR, IN THE ALTERNATIVE, WRIT OF PROHIBITION

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15-05106

CORPORATE DISCLOSURE STATEMENT

Pursuant to Nevada Rule of Appellate Procedure 26.1, the undersigned counsel certifies the following. The Plaintiffs are not corporations.

Lead Counsel for Plaintiffs in the Eighth Judicial District Court and the Nevada Supreme Court consists of Robbins Geller Rudman & Dowd LLP and Saxena White PA. The O'Mara Law Firm PC is Plaintiffs' Liaison Counsel.

DATED: January 16, 2015

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I. COUNTERSTATEMENT OF ISSUE PRESENTED

The Supreme Court ruled in *Cohen v. Mirage Resorts, Inc.*, 119 Nev. 1, 62 P.3d 720 (2003) that "if the complaint alleges damages resulting from an improper merger, it should not be dismissed as a derivative claim," in part because the shareholder has lost "his or her interest in a specific corporation." *Id.* at 19. Plaintiffs and the proposed class members were shareholders of the target company in an improper merger transaction that resulted in a different combined company with a different name, different products, different owners, different management, and a different board of directors. Did the district court properly follow *Cohen* in ruling that the Complaint states a direct claim?

II. INTRODUCTION AND SUMMARY OF ARGUMENT

Here is what Defendants claimed this case is about in their Writ Petition: "Parametric Was Not a Party to A 'Merger' . . . Parametric did not merge with any company, nor was it the surviving entity of a merger. Consequently, its shareholders were not asked to approve a merger, but only to approve the issuance of shares to [Turtle Beach's] shareholders. . . . Thus, Plaintiffs necessarily are not, as in *Cohen*, 'dissenting shareholder[s]' to a merger; they are, instead, merely objectors to a dilutive stock issuance." Petition for Writ of Mandamus or, in the Alternative, Writ of Prohibition ("Writ Petition" or "Writ Pet.") at 20, 23.

Here is what the case is really about, in Defendants' own words, from their press release announcing the merger of Parametric Sound Corporation and Turtle Beach (the "Merger"):

Parametric Sound Corporation to Merge with Turtle Beach

Combined Company to Bring Advanced Products to Market That Redefine Audio for Consumers and Businesses

SAN DIEGO, Calif. – August 5, 2013 – Parametric Sound Corporation (NASDAQ: PAMT), a leading innovator of audio products and solutions, and Turtle Beach, the market leader in video game audio, today announced that the companies have reached a Definitive Agreement to merge in a stock for stock transaction. The merger will combine Parametric's audio innovations with Turtle Beach's significant financial, technical, design, sales and marketing resources. . . .

Under the terms of the agreement, former Turtle Beach stockholders are expected to own approximately 80 percent of the combined

> company's shares outstanding at closing, and Parametric stockholders are expected to own approximately 20 percent of the combined company's shares, subject to adjustment as provided in the merger agreement. The new company will continue to operate under the name Parametric Sound Corporation and will be headquartered in San Diego. . . .[1]

And here is what Defendants told Plaintiffs and Parametric's other public shareholders in the Definitive Proxy (the "Proxy") when campaigning for their votes on the Merger:

> The Parametric board of directors, referred to as the "Parametric Board," has determined that the merger agreement and the transactions contemplated thereby, including the issuance of shares pursuant to the merger and the corresponding change of control of Parametric, are fair to, advisable and in the best interests of Parametric and its stockholders. ***The Parametric Board recommends that Parametric stockholders vote "FOR" the merger proposal. . . . Your vote is important. The affirmative vote of the holders of a majority of the votes cast on the merger proposal at the Special Meeting (assuming a quorum is present in person or by proxy), excluding abstentions, is required for approval of the merger proposal.***

PA102 (emphasis added.) Indeed, Defendants used the term "Merger" 1,390 times in the Proxy and related exhibits in connection with asking Parametric shareholders to vote in favor of the Merger with Turtle Beach. PA612:19.

The Writ Petition's inaccurate factual description of the case, while perhaps manufactured to pique the Supreme Court's interest in granting review, cannot support the issuance of a writ. The Supreme Court has defined a direct claim in this context as follows: "A claim brought by a dissenting shareholder that questions the validity of a merger as a result of wrongful conduct on the part of majority shareholders or directors is properly classified as an individual or direct claim. The shareholder has lost unique personal property – his or her interest in a

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[1] Defendants' Merger Announcement, emphasis in original, is available at the following publicly available link: http://hypersound.com/press_release_details.php?id=83. Plaintiffs request judicial notice of the undisputed fact that Defendants publicly made these statements. *See, e.g., Itcaina v. Marble*, 56 Nev. 420, 437, 55 P.2d 625, 631 (1936) (taking judicial notice of matters of public knowledge).

specific corporation." *Cohen*, 119 Nev. at 19. Thus, "if the complaint alleges damages resulting from an improper merger, it should not be dismissed as a derivative claim." *Id.* Put differently, "allegations [that] involve wrongful conduct in approving the merger and/or valuing the merged corporation's shares . . . are not derivative claims." *Id.* at 7.

The Class Action Complaint in Intervention ("Complaint") fits squarely within that definition of a direct claim. The Complaint alleges that the Merger is invalid and improper, which is a direct claim. A majority of Parametric directors were conflicted and engaged in repeated improprieties when negotiating, structuring, and voting on the Merger. ¶¶22-115.[2] When faithless directors engage in intentional misconduct, fraud, or a knowing violation of the law, as the Parametric Board did here, they are liable to stockholders. NRS 78.138(7) (permitting individual liability of directors or officers to "stockholders" in the event of breach of fiduciary duty involving "intentional misconduct, fraud or a knowing violation of law"); *Cohen*, 119 Nev. at 14.

The Complaint also alleges Defendants, through wrongful conduct, used the Merger to divest Parametric shareholders of their personal interest in a "specific corporation," *id.* at 19, for inadequate consideration. ¶¶91-109. The new combined company is not the same specific corporation as the one in which Plaintiffs invested. After the Merger, the new combined company, renamed as "Turtle Beach," manufactures different products, is controlled by different stockholders, is run by a different board of directors, is operated by a different management team, and is in a different and deteriorating financial state. ¶¶4-7, 26-29, 101-106. As Plaintiffs argued in the district court, as a result of the Merger "you folks who [collectively] are controlling shareholders of a cool sound

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[2] All "¶" and "¶¶" references are to the Complaint, which is contained at PA001-49.

company [Parametric] will now be 20 percent owners of a cool headphone company [Turtle Beach] that is not doing nearly as well as that cool sound company was." PA612:14-17.

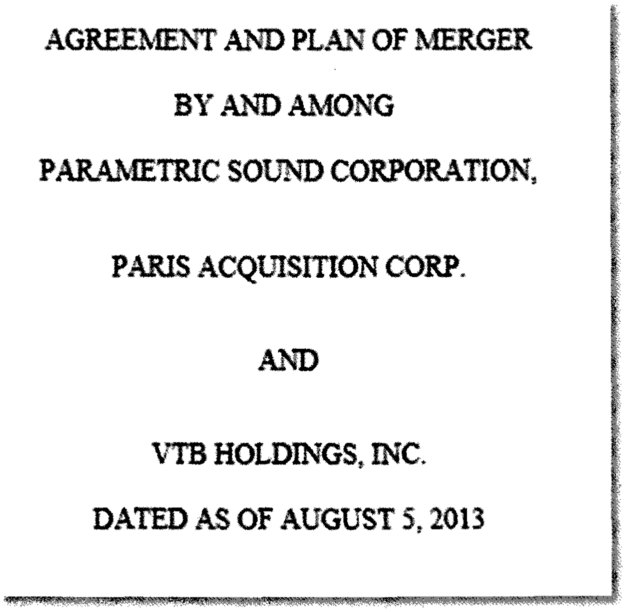
Defendants choose not to confront these allegations. Instead they argue that by creating a shell entity to effectuate the Merger, they created for themselves full immunity to direct shareholder claims. Not so. The transactional creativity of deal lawyers does not fundamentally alter the pragmatic effect of the Merger, or the duties owed to shareholders in connection with that Merger. As the Supreme Court explained in *Cohen*, "the Model Act and Nevada's statutes are designed to facilitate business mergers, while protecting minority shareholders from being unfairly impacted by the majority shareholders' decision to approve a merger." *Cohen*, 119 Nev. at 10. Under Nevada law, as well as Delaware and New York jurisprudence, the Complaint pleads a direct claim for relief. For the reasons stated herein, the district court did not err in denying Defendants' motions to dismiss.

III. FACTUAL AND PROCEDURAL BACKGROUND

This is a shareholder class action brought by Plaintiffs Grant Oakes and Kearney IRRV Trust, as well as multiple other shareholder plaintiffs in the underlying consolidated actions, on behalf of the public shareholders of Parametric common stock against Parametric, its six member Board of Directors, and its now-wholly owned subsidiary VTB Holdings, Inc. ("Turtle Beach" or "VTBH"). The Complaint alleges that the Parametric Board members each breached their fiduciary duties in connection with the Merger between Turtle Beach and Parametric and that Turtle Beach and Parametric aided and abetted in those breaches of duty.

A. Background of the Merger

On August 2, 2013, Parametric's Board voted to cause Parametric – the publicly traded entity in which Plaintiffs held stock – to enter into an Agreement and Plan of Merger ("the Merger Agreement"). Parametric was a signatory to the Merger Agreement – the following is a screenshot of its opening page:


AGREEMENT AND PLAN OF MERGER

BY AND AMONG

PARAMETRIC SOUND CORPORATION,

PARIS ACQUISITION CORP.

AND

VTB HOLDINGS, INC.

DATED AS OF AUGUST 5, 2013

PA285.

Under the Merger Agreement, Turtle Beach, formerly a privately held company from New York, merged with Parametric, a publicly traded Nevada corporation, in order to provide Turtle Beach with access to the public markets without incurring the expense and governance requirements of a separate Initial Public Offering.[3] The overall Merger transaction involved seven basic steps:

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[3] Other jurisdictions have viewed such transactions with skepticism: "[U]sing a defunct Delaware corporation that happens to retain a public listing to evade the regulatory regime established by the federal securities laws is contrary to Delaware public policy. Delaware has no interest in facilitating reverse mergers with defunct but still publicly registered shell corporations as a means to circumvent the regulatory protections provided by the federal securities laws." *In re China Agritech, Inc.*, No. 7163-VCL, 2013 Del. Ch. LEXIS 132, at *3-*4 (Del. Ch. May 21, 2013) (quotations and citations omitted). While Parametric was not a "defunct" company, but was a company with live shareholders and extremely valuable hypersound technology, the egregious destruction in shareholder value present in this transaction is, as a matter of public policy, even more concerning than a merger into a public shell with no assets.

1. Parametric created a shell subsidiary, Paris Acquisition Corp. ("Paris");

2. Turtle Beach merged into Paris;

3. Paris was merged out of existence;

4. Turtle Beach continued as the surviving entity in that aspect of the transaction;

5. Parametric issued millions of shares to Turtle Beach, giving Turtle Beach approximately 80% of the post-Merger entity while relegating Parametric's former shareholders to a 20% minority ownership;

6. Turtle Beach took control of Parametric and instituted its own board of directors and management team; and

7. Turtle Beach changed Parametric's name to "Turtle Beach."[4]

As a result of those steps, "[a]fter the close of the Merger, the [Parametric] shareholders' majority voting interest in the pre-Merger standalone Company ceased to exist." ¶7. Defendants treated Turtle Beach as the acquirer of Parametric for accounting purposes as well. Defendants' Proxy stated:

> Based on the relative voting interests of Parametric and [Turtle Beach] in the combined company whereby the [Turtle Beach] stockholders will have a majority voting interest, that the board of directors of the combined entity will be composed of five board members designated by former [Turtle Beach] stockholders and two directors designated by Parametric stockholders and that the chief executive officer of the combined entity will be the former chief executive officer of [Turtle Beach], ***[Turtle Beach] is considered to be the acquiror of Parametric for accounting purposes.***

PA187 (emphasis added). Defendants also told Parametric shareholders:

> Q: What vote is required to approve the merger proposal?
>
> A: ***Approval of the merger proposal requires the affirmative vote of a majority of the votes cast on the proposal, excluding abstentions, at a meeting at which a quorum is present.***

4 ¶¶4-7, 26-29, 101-106.

PA121 (emphasis added.)

In connection with that vote, the Merger was effectuated through a fraud on Parametric's shareholders. The Complaint alleges that Defendants misled shareholders about multiple material issues in the Proxy. ¶114. These issues include, as described further below: (a) the value of the SIIG/Optek project; (b) the Board's attempts to angle for personal payments in the hours leading up to, and during, the final Merger vote; (c) the Board's actions in stalling other potential acquirers and licensing discussions; (d) the positive Company announcements the Board chose not to make during Merger negotiations, and their intention that withholding positive news would keep Parametric's stock price down and thus make "the premium on the [Turtle Beach] deal look better"; (e) the details behind Potashner's threats to the rest of the Board; and (f) the fact that the Board's financial advisors did not provide any opinion, informal or otherwise, on the terms of the Break-Up License. *Id.*[5]

B. Abbreviated Procedural Summary of the Litigation

After announcement of the Merger in August 2013, multiple Parametric shareholders viewed the Merger as unfair and filed suit in San Diego, California (Parametric's place of business) and Nevada (Parametric's state of incorporation). Plaintiffs from both jurisdictions cooperated and submitted briefs in support of a motion for preliminary injunction in Nevada. The Honorable Elizabeth Gonzalez,

[5] Defendants' contention that the Merger obtained "overwhelming approval" of Parametric stockholders" (Writ Pet. at 8) is also incorrect. Of 6,837,321 shares eligible to vote on the Merger, only 3,801,508 voted in favor, or just 55.6%. Irrespective of the shares present at the December 2013 meeting, if just Potashner, for example, had not voted in favor of the Merger, it would not have received majority support. To be sure, the Merger was technically approved (as all completed mergers are), but it did not receive the level of support that Defendants imply. In any event, technical approval of a merger is irrelevant to the direct/derivative determination. *See Cohen*, 119 Nev. at 7 ("On May 27, 1998, the Boardwalk convened a special shareholder meeting to consider the offer. A majority of the shareholders approved the merger.").

Eight Judicial District Court Judge, heard the matter on December 26, 2013. Defendants' Writ Petition correctly points out that the district court denied Plaintiffs' motion for preliminary injunction, but omits that, in doing so, Judge Gonzalez stated that "these findings are preliminary as they are based on the limited evidence presented in conjunction with the preliminary injunction hearing after limited discovery conducted by the parties on an expedited basis" and that the ruling was made "without prejudice to pursue any other remedies that are appropriate."

The California plaintiffs intervened in the consolidated Nevada action and the district court designated the Complaint as the operative complaint. PA002. The Complaint incorporated far more facts and substantial allegations than any prior pleading, including the motions for preliminary injunction, even though it was still based on partial, limited expedited discovery. ¶¶22-115. Defendants filed motions to dismiss the Complaint on June 10, 2014, and full briefing ensued. PA503-586. Yet Defendants did not contend – as they do now, for the first time, in their Writ Petition – that Parametric was not a "constituent entity" to the Merger, nor did Defendants argue anything regarding "dissenter's rights." Those issues were never raised or addressed by the trial court. *Id.* Plaintiffs substantively responded with a 39-page Omnibus Opposition to Defendants' Motions to Dismiss. PA529-575. After a hearing on August 28, 2014, the district court entered an order denying Defendants' motions to dismiss on September 10, 2014. PA631-632. By denying all Defendants' motions to dismiss, the district court necessarily ruled that the Complaint sufficiently alleged that Parametric's Board breached their fiduciary duties of loyalty to Parametric's shareholders and engaged in intentional misconduct, fraud, or a knowing violation of the law in connection with their effectuation of the Merger. NRS 78.138(7); 9/10/14 Order Denying Motions to Dismiss. The district court also necessarily ruled that the Complaint sufficiently alleged that Defendants Turtle Beach and Parametric "knowingly participated" in those intentional breaches of fiduciary duty. *In re AMERCO Derivative Litig.*, 252 P.3d 681, 702 (Nev. 2011); 9/10/14 Order Denying Motions to Dismiss. These issues were briefed and argued extensively at the trial court level. PA529-576, PA587-623. Defendants do not contend that these rulings were in error.[6]

Nonetheless, a review of the claims at issue is necessary to understand the nature of those claims and thus to determine whether they directly challenge wrongful conduct in connection with a merger or, alternatively, derivatively challenge unrelated decisions that independently harmed the corporation itself. Defendants' Writ Petition, in contrast, attempts to characterize the claims for relief without ever facing the substance of the allegations. That is not how the analysis of a claim on a motion to dismiss works. While the description that follows is predominantly factual, certain sections are introduced by this Court's corresponding descriptions of direct allegations from *Cohen.*

C. The Factual Allegations in the Complaint

"Challenges to the validity of a merger based on fraud usually encompass either or both of the following: (1) lack of fair dealing or (2) lack of fair price. Both involve corporate directors' general duties to make independent, fully informed decisions when recommending a merger and to fully disclose material information to the shareholders before a vote is taken on a proposed merger." *Cohen*, 119 Nev. at 11-12. The Complaint pleads both lack of fair dealing and lack of fair price.

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[6] By not addressing the issue in their Writ Petition, Defendants have conceded that the Complaint sets forth viable and non-exculpated claims for breach of the duty of loyalty, as well as aiding and abetting, against each of the defendants. *See, e.g., Wyeth v. Rowatt*, 244 P.3d 765, 778 n.9 (Nev. 2010); *Mainor v. Nault*, 120 Nev. 750, 777, 101 P.3d 308, 326 (2004) (an appellant who fails to provide authority to support an argument abandons the issue).

1. The Merger Is Invalid Because It Was Not Approved by a Majority of Disinterested Directors

"Cases involving [a lack of] fair dealing frequently contain claims that directors ... had conflicts of interest or were improperly compensated or influenced in return for their approval of the merger . . . ." *Cohen*, 119 Nev. at 12. At the time it voted to approve the Merger, the Parametric Board was comprised of six members, all of whom are Defendants in this case: Kenneth Potashner; Elwood "Woody" Norris; Andrew Wolfe; Dr. Robert Kaplan; Seth Putterman; and James Honore. ¶¶14-19. Each of Parametric's six directors was personally conflicted or was improperly influenced when voting on the Merger. This subjects the transaction to "entire fairness" scrutiny. "Where actual self-interest is present and affects a majority of the directors approving a transaction, a court will apply even more exacting scrutiny to determine whether the transaction is entirely fair to the stockholders." *Paramount Commc'ns v. QVC Network*, 637 A.2d 34, 42 n.9 (Del. 1994).[7]

a. Potashner Was Not "Disinterested" When Negotiating and Voting on the Merger

Executive Chairman Potashner was unquestionably the domineering force in the Parametric boardroom. Potashner was personally conflicted, however, because he attempted to utilize the Merger with Turtle Beach to effectuate his "personal

[7] Nevada has adopted the "entire fairness" standard of review for board-majority-conflicted transactions as well. In *Cohen*, the Court stated that "higher scrutiny" is warranted in "mergers where ... the majority of . . . directors have conflicts of interest." *Cohen*, 119 Nev. at 17-18; *see also Shoen v. Sac Holding Corp.*, 122 Nev. 621, 640 n.61, 137 P.3d 1171, 1184 (2006) ("Generally, when an interested fiduciary's transactions with the corporation are challenged, the fiduciary must show good faith and the transaction's fairness."). *Cf. Foster v. Arata*, 74 Nev. 143, 155, 325 P.2d 759, 765 (1958) (recognizing an interested fiduciary's burden to prove the good faith and inherent fairness of any transactions with the corporation) (citing *Pepper v. Litton*, 308 U.S. 295, 306, 60 S. Ct. 238, 84 L. Ed. 281 (1939)); *Oberly v. Kirby*, 592 A.2d 445, 469 (Del. 1991) (noting that, when approval of an interested director transaction by an independent committee is not possible, the interested directors carry the burden of proving that transaction's "entire fairness").

plans to transition to a role overseeing Parametric's hearing-related initiatives." ¶23. Potashner had created a subsidiary of Parametric called Hypersound Health, Inc. ("HHI") and saw great personal "liquidity" in that entity, later admitting that "I believe over time the hhi component will be worth a billion." *Id.* In fact, at a December 13, 2012 Board meeting, Potashner "outlined the longer-term plans for him to transition more time to HHI" and that, as a result, Parametric itself would need a new CEO." *Id.* Thus, "[a]t the time Potashner began negotiations and at the time he voted on the Merger, Potashner believed that the Merger would offer a better vehicle for his continued management of Parametric's hearing-related initiatives." *See* ¶¶23-25. Potashner also received golden parachute compensation of a total of $2,807,738 in the Merger, which further motivated him to complete the deal rather than step down as CEO when the Company eventually found a replacement. ¶26. The day the Merger vote took place, "[o]n August 2, as the Board finalized its intent to enter into the Merger Agreement, the 'Compensation Committee' met Potashner's cash demands. It agreed to pay his 2013 bonus payments at the maximum target rate of $210,000." ¶63. This cash severance and change of control package also renders Potashner interested. *Id.*

Potashner was so determined to protect his own interests that he engaged in a disturbing pattern of threats and misrepresentations to the Parametric Board throughout the Merger negotiations. ¶25. During the Merger sale process, after misrepresenting and concealing information from the rest of the Parametric Board, Potashner defied the Board's orders not to discuss certain issues with Turtle Beach on several occasions, threatened to displace the entire Board, and threatened to sue the Board if they did not pay Potashner and one of Potashner's cronies $250,000 in cash. ¶¶23-25, 59-63. At one point in the process, another Board member, referencing Potashner, wrote regarding a draft of the Merger Agreement: "I needed this as I feel we have been left in the dark and have had misrepresentations presented to us." ¶51. In sum, "Potashner's repeated threats, misrepresentations, concealments, and outright lies to the rest of the Board are not the hallmark of a disinterested, independent director." ¶25.

b. Kaplan and Putterman Were Not "Disinterested" When Voting on the Merger

Defendants Kaplan and Putterman, while subservient to Potashner, were also conflicted in their own right. Rather than stepping up and protecting shareholders against Potashner's obvious misconduct, Kaplan and Putterman demanded their own fee before voting on the Merger. "Despite not participating in a single discussion with Turtle Beach, Kaplan voted on the Merger while vying for a personal payment to 'get even' with Potashner. The day of the most significant vote in Parametric's corporate existence, Kaplan spent his time emailing about the personal bonus he felt the independent directors should receive." ¶30. The Parametric Board voted on the Merger at a 4 p.m. meeting on August 2, 2013. One hour before the meeting, Kaplan wrote to propose the following resolution:

> $50,000 is to be paid to each of the independent directors as compensation for their continuing efforts and activity in Corporate Development. This money is to be paid immediately." I mentioned this thought to you previously and have discussed it with Seth [Putterman]. Since it should not be tied to the merger, I have described it differently.

Id. "Like Kaplan, Putterman also voted on the Merger with the expectation of receiving a cash bonus. At 4:50 p.m. on August 2, 2013, during the very meeting while Putterman and the rest of the Board were voting on the Merger, Putterman agreed with Kaplan's bonus request in general, but offered a different rationale: 'Can the bonus be made contingent on successfully raising the 5-15M$ that we seek prior to closing but that we need in any event!'" ¶33.

After voting on the Merger, the Board adjourned at 5:00 p.m. *Id.* The directors still believed they would receive a cash bonus. *Id.* At 7:35 p.m. that evening, Kaplan continued in his personal quest for a Merger-related bonus, upping the ante:

> I used 50K as a starting point. . . . My real suggestion is to have an average of all the executive bonuses and that figure is what the IDs [Independent Directors] should get, Ken has granted himself rather large bonuses. This will get even with him, not that I want to get even, I really just want equality.

Id. Kaplan demonstrated the same self-interested approach earlier in the Merger negotiation process as well, requesting "healthy golden parachutes to all the BoD members." ¶32. The day of the Merger vote, Kaplan and Putterman did not spend their time drafting emails about substantive deal terms, negotiations with Turtle Beach, or the interests of Parametric shareholders; they spent their time drafting requests for personal payouts. Kaplan and Putterman's deliberate actions gave rise to the reasonable inference that these requested payments were a material and motivating factor when voting for the Merger.

c. Norris Was Not "Disinterested" When Voting on the Merger

Defendant Norris was unduly influenced when voting on the Merger. In light of Norris's vying for employment in the post-Merger entity and his resulting financial interest in completing the Merger with Turtle Beach, Norris was particularly susceptible to Potashner's threats. ¶27. The Complaint alleges that "Potashner recognized these conflicts and pounced, threatening Norris that he would personally lose millions if Norris did not go along with the planned Merger. On March 29, 2013, as Potashner was working out a deal with Stark, Potashner emailed Norris privately to state that the Merger was in doubt and that, ***The Bod is on the verge of losing you at least $10m personally***." *Id.* Norris responded, "***Is this blackmail or what[?]***" ¶48. Norris was also conflicted when voting on the Merger because he knew that his employment "was a term of the then-current Merger Agreement." *Id.* Norris fell in line and voted in favor of the Merger, despite its harmful effect on Parametric stockholders. *Id.* Thus, the deal left Norris "susceptible to Potashner's threats and [Norris's motivations] existed in direct contrast to the impact on Parametric's public shareholders generally, who have all lost significantly." *Id.*

d. Wolfe Was Not "Disinterested" When Voting on the Merger

Potashner held an enhanced influence on Wolfe specifically, which left Wolfe interested in the Merger through Potashner's conflicts. "Wolfe was beholden to Potashner in light of their prior relationship in threating boards for personal compensation and Potashner's continued improper incentivizing of Wolfe to do Potashner's bidding." ¶28. Wolfe previously served as CTO of SonicBlue, a position he owed to Potashner in light of Potashner's position as CEO. *Id.* After promoting Wolfe, Potashner then "procured company-issued loans for himself and Wolfe to purchase 654,717 and 171,179 shares of a SonicBlue subsidiary." *Id.* "When SonicBlue's board later voted to convert their own loans (but not Potashner's and Wolfe's) to non-recourse, Potashner publically demanded the board pay up or resign. Potashner then sued his own board. As a result, SonicBlue agreed to pay Wolfe a ten-month salary when SonicBlue terminated Wolfe in October 2002." *Id.* "Wolfe was in Potashner's debt and Potashner continued this pattern by personally luring Wolfe to the Parametric board in February 2012." ¶29. Potashner continued his pattern of incentivizing Wolfe by repeatedly pushing for himself and Wolfe to occupy the two post-merger board seats during substantive Merger negotiations. *Id.* "In light of their mutual history of bad faith threats and incentives, Wolfe was in a position to comport with the wishes and interest of Potashner, rather than Parametric stockholders generally." *Id.*

e. Potashner Collectively Dominated and Controlled All Other Directors With Respect to the Merger

All five directors, Wolfe, Norris, Kaplan, Putterman and Honore, each also established a lack of independence from the Board Chairman, Potashner, when repeatedly caving to Potashner's threats during the sale process. In addition to the conduct referenced above, Potashner also threatened the Board with "very aggressive claims against individuals" that will "result in substantial corporate and personal legal exposures." ¶58. In light of that threat and "in fear of their jobs, the Board immediately caved and asked Potashner how many Parametric shares he would accept in exchange for his HHI stock options." ¶56. The Board relented and allowed Potashner, Wolfe, and the CFO to jointly call Turtle Beach and convey Potashner's demands, which included "cash payments to Potashner and Todd at 100% of 2013 bonus levels (whether or not they were entitled to such amounts or not) and not to restructure the HHI license agreement." ¶61. Potashner got exactly what he demanded. ¶¶61-63. The Board ultimately complied with Potashner's threats and voted in favor of the deal, but not without requesting their own personal payouts. The Board succumbed to Potashner's control after being cowed by threats and hostile, erratic behavior. *Id.*

2. The Board Breached Its Fiduciary Duties by Unfairly Negotiating and Structuring the Merger

Post-merger damage claims for unfair dealing may involve "merger negotiations [and] how the merger was structured." *Cohen*, 119 Nev. at 12. Where directors "'bias the process' in favor of certain bidders and against others" in furtherance of self-interest, "'they commit a breach of fiduciary duty.'" *In re Rural Metro Corp. Stockholders Litig.*, 88 A.3d 54, 91-92 (Del. Ch. 2014). Indeed, "[t]his is precisely the type of 'evidence of self-interest . . . that calls into question the integrity of the [Merger] process."' *Id.* (citing *In re Del Monte Foods Co.*

S'holders Litig., 25 A.3d 813, 831 (Del. Ch. 2011)). The Parametric Board did just that here.

"In order to roll out the red carpet for his preferred merger partner, Turtle Beach, Potashner – and by their acquiescence, the rest of the Board – stalled discussions with other licensing partners and potential acquirers as soon as Turtle Beach arrived on the scene." ¶36. The Complaint contains significant detail regarding this intentionally wrongful scheme. For example, "[o]n April 7, 2013, Potashner wrote: 'On the positive side I would be able to announce the license and buy additional time both with the parties that we have stalled . . . I have several things going on including defining a financing and the pressures of the license activities we put on hold.'" *Id.* Potashner admitted to the harm caused by his stalling efforts. On April 9, 2013, Potashner wrote to his CFO and Turtle Beach: "***My stock is taking a beating due to me deferring signing licensing deals. Any ideas?***" ¶37. These efforts biased the process away from other existing and "capable buyers interested in purchasing Parametric," including Amazon. ¶39.

All Board members acted with wrongful intent on this issue as well. The rest of the Parametric Board finally noticed Potashner's stalling efforts three months later and, on July 6, 2013, Kaplan wrote to Honore, Norris, Putterman, and Wolfe:

> Personally I think this has gone on far too long. We need to get on with the business of running the business. What has been going on since this [Turtle Beach] idea surfaced? Where are our licensing agreements, where are sales (incremental improvement due to David), Epsilon, Amazon, The Chinese, McDonalds, The Bear stores (still in beta mode), Sony, Samsung, etc.? AND WE HAVE SURE BURNED THROUGH A HELL OF A LOT OF MONEY. . . . It is time for the BOD to step up and take charge! We have been far too passive in the past. It is good to have a strong leader but not a dictator.

¶40 (emphasis in original). Despite that direct challenge, the Board chose not to step up and protect Parametric stockholder interests. Instead, they asked for hush money. "While Kaplan's email demonstrated a brief glimpse of spirit, the next day, July 7, 2013, Kaplan embarked on his above-described personal quest for an additional bonus in connection with the Merger. After realizing the potential for personal benefit, Kaplan fell in line and never again questioned Potashner's unreasonable and improper hindrance of Company progress in order to effectuate the Merger." ¶41.

Defendants also engaged in a lack of fair dealing when they structured a Merger Agreement that contained a series of draconian deal protection provisions that precluded other bidders and would penalize Parametric shareholders if they were to vote against the Merger. ¶¶64-90. "As a result of the combination of these provisions, Parametric's former stockholders were coerced into voting in favor of the Merger. Had the stockholders voted against the Merger, the former Parametric stockholders would have been crippled by the one-sided Break-Up License." ¶65.

In addition, the Board ran a sham "go-shop" process in bad faith that again impermissibly biased the process towards their preferred acquirer, Turtle Beach. "Indeed, when Parametric's attorneys drafted a paragraph about the go-shop paragraph in the Merger's press release, Stark echoed all defendants' distaste for a higher offer: '***You're not looking for an alternative and neither are we***.'" ¶84. Houlihan Lokey, the Board's financial advisor, did not contact all potential acquirers during the go-shop process. *Id.* "Rather, Potashner referred at least one serious contact directly to Stark and Turtle Beach. Stark would then swat them away in order to usurp the interest post-Merger." *Id.* This misconduct in connection with the Merger "go-shop" process is detailed at length in the Complaint. ¶¶85-90.

3. The Board Breached Its Fiduciary Duties to Parametric Shareholders by Deliberately Undervaluing Parametric Shares in the Merger

"Lack of fair price may involve similar allegations plus claims that the price per share was deliberately undervalued . . . ." *Cohen*, 119 Nev. at 12. Similarly, allegations that "involve wrongful conduct in . . . valuing the merged corporation's shares" may state a post-close claim for damages. *Id.* at 6-7. The Complaint alleges that "[t]he misconduct described herein resulted in an unfair and inadequate Merger valuation for Parametric's stockholders." ¶6.

The Board "deliberately undervalued" Parametric shares in the Merger and engaged in "wrongful conduct in . . . valuing [Parametric's] shares," *id.*, in at least two crucial respects. First, Potashner delayed positive company announcements in an attempt to create a manipulated and depressed price on the Merger, mislead Parametric stockholders, and appease Turtle Beach. ¶¶43-47. "Potashner knew that the 80%/20% ratio undervalued Parametric, but attempted to keep Parametric's pre-Merger-Announcement stock price low so that the stock would not plummet an even higher percentage when the Merger was announced." ¶46. Potashner did so on multiple occasions, all of which were directly related to the Merger proposal under discussion. ¶¶43-46. The Board has a duty not to "deliberately undervalue" the Merger and is not permitted to manipulate the stockholder vote through misinformation and suppression of Parametric's pre-Merger stock price. *Cohen*, 119 Nev. at 12. The Board violated those duties here.

Second, Potashner, Wolfe, Norris, Kaplan, Putterman and Honore all "deliberately undervalued" Parametric shares in the Merger by approving that valuation through the conscious disregard of a known component of Parametric's standalone value – the so-called "SIIG/Optek Soundbar project." ¶¶92-100. "The Board approved the Merger based on Craig-Hallum analysis the Board knew excluded potential Optek revenue (or any licensing revenue for that matter)." ¶92. Worse, "Potashner encouraged Turtle Beach CEO Stark to negotiate with Optek for Turtle Beach's benefit two weeks into the Go-Shop process and months before shareholders voted on the Merger." *Id.* Like the rest of the Merger-related misconduct, the entire Board was complicit:

> The Board voted on the merger while failing to value the revenue to be received from the Optek soundbar issue. The projections on which Craig-Hallum based its "fairness opinion" included no revenue from Optek, and egregiously, no licensing revenue at all, even though [the Parametric CFO] admitted that "we fully expect" that revenue stream. Digital signage and HHI were the only sources of revenue included in the final projections. The Board knew, or should have known, that the SIIG/Optek soundbar was an existing project likely to generate revenue, but acted in bad faith when it approved the Merger based on flawed financial projections with a gaping omission.

¶98. Kaplan knew that Potashner had buried the project in July 2013, but "never followed up on the issue." ¶99.

4. Parametric and Turtle Beach Aided and Abetted the Parametric Board's Breaches of Fiduciary Duty in Connection with the Merger

The aiding and abetting claims against Parametric are more fully described in the Complaint and Plaintiffs' Motion to Dismiss opposition. PA002-49, PA571-574. In sum, while Potashner and the rest of his Board engaged in repeated bad acts, Turtle Beach and Parametric were involved every step of the way, exploiting, encouraging, emboldening, and assisting.[8]

As a result of the foregoing allegations, the Complaint "alleges damages resulting from an improper Merger." ¶7. The Complaint further alleges that "[u]nder well-established Nevada law, plaintiffs and the shareholder class are entitled to monetary damages including the difference between the Merger valuation and the fair value of their shares." ¶9.

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[8] The Complaint makes clear that only the Individual Defendants, *i.e.*, the Board, owed fiduciary duties to Parametric shareholders. *See, e.g.*, ¶¶2, 119, 125, 127-128, 132-134. Nowhere does it specifically allege that Parametric or Turtle Beach, the corporate entities, owed duties directly to shareholders. Nevertheless, to the extent the First Cause of Action was unclear and stated that it was brought against "All Defendants," Plaintiffs clarified in their Motion to Dismiss Opposition that only the aiding and abetting claim was asserted against the corporate entities, Parametric and Turtle Beach.

IV. STANDARD OF REVIEW

"Normally, this court will not entertain a writ petition challenging the denial of a motion to dismiss but we may do so where . . . the issue is not fact-bound and involves an unsettled and potentially significant, recurring question of law." *Buckwalter v. Eighth Judicial Dist. Court*, 234 P.3d 920, 921 (Nev. 2010). Extraordinary writ relief is purely discretionary with the court to which the application is made. *See Smith v. Eighth Judicial Dist. Court*, 107 Nev. 674, 677, 818 P.2d 849, 851 (1991) (issuance of writ of mandamus or prohibition is "purely discretionary"). The burden of establishing the propriety of extraordinary relief is "a heavy one." *Paulos v. Eighth Judicial District Court*, 98 Nev. 453, 455, 652 P.2d 1177, 1178 (1982).

The district court's September 10, 2014 Order Denying Motions to Dismiss, which Defendants approved as to form, does not contain the grounds for dismissal, but a trial court's judgment may be affirmed on a ground other than those expressly relied upon by the trial judge. *See Nelson v. Sierra Constr. Corp.*, 77 Nev. 334, 343, 364 P.2d 402, 406 (1961); *Hotel Riviera v. Torres,* 97 Nev. 399, 403, 632 P.2d 1155, 1158 (1981). Ultimately, this is still a challenge to a complaint. On a motion to dismiss for failure to state a claim for relief, courts must construe the pleading liberally and draw every fair inference in favor of plaintiff, and allegations in the complaint must be accepted as true. NRCP 12(b)(5); *Brown v. Kellar*, 97 Nev. 582, 636 P.2d 874 (1981). "Nevada is a notice-pleading jurisdiction and pleadings should be liberally construed to allow issues that are fairly noticed to the adverse party." *Nevada State Bank v. Jamison Family P'Ship*, 106 Nev. 792, 801, 801 P.2d 1377, 1383 (1990).[9]

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9 In the district court, without formally requesting judicial notice or attaching a declaration of anyone with supporting knowledge, Defendants included an unexplained "appendix" in support of their briefs, which attached nine exhibits totaling 419 pages of documents in support of their arguments. At both the district

V. THE COMPLAINT PLEADS A DIRECT CLAIM FOR DAMAGES ON BEHALF OF A SHAREHOLDER CLASS

A. The Parametric Board Owed Fiduciary Duties Directly to Parametric Stockholders

Defendants' Writ Petition is premised on a misunderstanding of Nevada corporate governance doctrine regarding the relationship between stockholders and individual corporate fiduciaries. Despite this Court's consistent holdings to the contrary, Defendants call it a "fundamental tenet of [Nevada] corporate law" that directors of a Nevada corporation owe no duties to shareholders. (Writ Pet. at 1.) That is wrong. Nearly a century ago, this Court referred to the rule that corporate fiduciaries owe direct duties to shareholders as "so well defined that it would be a matter of supererogation to incumber [an] opinion with a review of" the issue. *Smith v. Gray*, 50 Nev. 56, 68, 250 P. 369, 373 (1926). This Court went on to state:

> The directors and managing officers of a corporation, says Pomeroy, occupy the position of quasi trustees towards the stockholders alone, and not at all towards the corporation with respect to the shares of stock. Since the stockholders own these shares, and since the value thereof and all their rights connected therewith are affected by the conduct of the directors, a trust relation plainly exists between the stockholders and the directors, which is concerned with, and confined to, the shares of stock held by the stockholders. . . . Undoubtedly it is the law that, where the majority stockholders are oppressively and illegally pursuing a course, in the name of the corporation, which is in violation of the rights of the minority, and which can only be restrained by the aid of a court of equity, a stockholder may sue in equity on behalf of himself and other stockholders who may come in for appropriate relief.

Id. at 68-69 (citing 3 Pomeroy Eq. Jur. §1090 (4th ed.); Clark & Marshall, Private Corporations, §536 at 1661).[10] Later, in 1957, when holding that fiduciary duties

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court level and in the Supreme Court, such hearsay is of course improper on a motion to dismiss and should not be considered.

[10] *Smith* is good law and was cited for the same proposition by this Court in *Cohen*, 119 Nev. at 19, as well as the District of Nevada in *Horwitz v. Southwest Forest Indus., Inc.*, 604 F. Supp. 1130, 1134 (D. Nev. 1985).

did not exist between partners and an assignee, the Supreme Court explained that: "There can be no question of the rule [implementing a fiduciary relationship] in such cases or where a partnership or agency relationship exists ***or that of corporate shareholder and officer***. In such cases the fiduciary duty is clear." *Bynum v. Frisby*, 73 Nev. 145, 149, 311 P.2d 972, 974 (1957) (emphasis added). More recently, the Supreme Court in *Cohen* faithfully applied these principles in holding that directors owe fiduciary duties directly to shareholders. 119 Nev. at 19. And in *Shoen*, the Supreme Court continued to affirm that directors owe fiduciary duties to the stockholders themselves:

> The board's power to act on the corporation's behalf is governed by the directors' fiduciary relationship with the corporation ***and its shareholders***, which imparts upon the directors duties of care and loyalty. In essence, the duty of care consists of an obligation to act on an informed basis; the duty of loyalty requires the board and its directors to maintain, in good faith, the corporation's ***and its shareholders'*** best interests over anyone else's interests.

122 Nev. at 632 (emphasis added) (citing *Foster*, 74 Nev. at 155; *Cede & Co. v. Technicolor*, 634 A.2d 345, 360-61, 367 (Del. 1993); *Horwitz*, 604 F. Supp. at 1134; *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984)); *see also AMERCO*, 252 P.3d at 700-01 (same). The decision in *Cohen* did not appear out of the blue and "create[] a narrow exception" to Defendants' supposed – and non-existent – rule that directors owe no fiduciary duties to stockholders. (Writ Pet. at 2-3.) *Cohen* was, and still is, well-rooted in decades of Nevada law.

Defendants proffer unsound support for their "fundamental tenet" that corporations owe duties "to companies, not shareholders." (Writ Pet. at 1.) First, defendants cite an unpublished opinion from the District of Nevada, *Sweeney v. Harbin Elec., Inc.*, No. 3:10-cv-00685-RCJ-VPC, 2011 U.S. Dist. LEXIS 82872 (D. Nev. July 26, 2011), which has never been cited or approved by any recorded decision. The inappositeness of the *Sweeney* decision is addressed in greater detail below. Next, Defendants quote a Delaware case employing this sentence: "It is well settled that directors owe fiduciary duties to the corporation." *See N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d 92, 101 (Del. 2007). But the court in *Gheewalla* also recognized that "[i]t is well established that the directors owe their fiduciary obligations to the corporation and its shareholders . . . shareholders rely on directors acting as fiduciaries to protect their interests . . . while not technically trustees, directors stand in a fiduciary relationship to the corporation and its shareholders." *Id.* at 99 & n.22 (citing *Guth v Loft*, 5 A.2d 503, 510 (Del. 1939)). Last, Defendants rely on a quote from a general Massachusetts practice guide, repeated in *Jernberg v. Mann*, 358 F.3d 131, 134 (1st Cir. 2004), which surmises that officers owe duties to the corporation, rather than shareholders individually. *Id.* (quoting 14A Howard J. Alperin and Lawrence D. Shubow, Massachusetts Practice Series, Summary of Basic Law §8.85 (3d ed. 1996)). *Jernberg*, however, used that quote when declining to hold an officer to a higher burden of proving enhanced scrutiny when purchasing stock directly from an individual stockholder. 358 F.3d at 134-38. No similar facts are present here. Rather, in Massachusetts, like Delaware, New York, and Nevada, corporate fiduciaries owe duties directly to stockholders and permit stockholders to directly enforce those duties, especially in connection with a merger. *Coggins v. New Eng. Patriots Football Club, Inc.*, 492 N.E.2d 1112, 1118-19 (Mass. 1986) ("the right to 'selfish ownership' in a corporation . . . must be balanced against the concept of the majority stockholder's fiduciary obligation to the minority stockholders") (cited in *Cohen*, 119 Nev. at 15 n.44, 19 n.75, 22 n.77, 23 n.82).

In sum, the self-interested conduct of directors and officers of Nevada corporations is governed by fiduciary relationships, both to the company and to its shareholders. *See, e.g.*, NRS 78.138(7). Defendants' request to uproot those longstanding relationships finds no support in Nevada corporate governance doctrine.

B. Under *Cohen*, Plaintiff Shareholders May Pursue their Claims Directly

The parties agree that the Supreme Court's decision in *Cohen* is central to the resolution of this writ. *Cohen* ultimately holds that claims regarding influences of directors' merger votes, improper incentives, and obtaining a fairness opinion on a merger that undervalued the target's stock "go to the validity of the merger" and are "all proper to support a claim for rescission or monetary damages caused by an invalid merger." *Cohen*, 119 Nev. at 22, 24. On the other hand, the claims involving mismanagement resulting in a loss of revenue, overpayment for land acquisitions, the impairment of the target's expansion, and recovery of fees paid for the fairness opinion were derivative, as such claims were plainly directed at "harm to the corporation." *Id.* at 21-22, 24. Put simply, claims on behalf of the shareholders are direct, while claims on behalf of the company are derivative. *Id.* The Court summarized the distinction as follows:

> We conclude that some of the allegations and causes of action seek damages for lost profits, usurpation of corporate opportunities, or mismanagement of the corporation, and that these claims were properly dismissed as derivative claims. However, the remaining allegations involve wrongful conduct in approving the merger and/or valuing the merged corporation's shares. These are not derivative claims. . . .
>
> It is true that a former shareholder has no standing to sue for breach of fiduciary duty on a derivative claim. A derivative claim is one brought by a shareholder on behalf of the corporation to recover for harm done to the corporation. Because a derivative claim is brought on behalf of the corporation, a former shareholder does not have standing to assert a derivative claim. A former shareholder does, however, have standing to seek relief for direct injuries that are independent of any injury suffered by the corporation.
>
> A claim brought by a dissenting shareholder that questions the validity of a merger as a result of wrongful conduct on the part of majority shareholders or directors is properly classified as an individual or direct claim. The shareholder has lost unique personal property – his or her interest in a specific corporation. Therefore, if the complaint alleges damages resulting from an improper merger, it should not be dismissed as a derivative claim. On the other hand, if it seeks damages for wrongful conduct that caused harm to the corporation, it is derivative and should be dismissed.

Id. at 6-7, 19 (footnotes with citations omitted).

Like in *Cohen*, the Complaint alleges: "In addition to their conflicts of interest, the Board engaged in multiple instances of bad faith conduct in breach of their fiduciary duties. All of the bad faith acts described below were directly related to the Merger and its process, impacted negotiations with Turtle Beach, and harmed Parametric shareholders." ¶35. The Complaint further alleges that "[t]he misconduct described herein resulted in an unfair and inadequate Merger valuation for Parametric's stockholders." ¶6. In sum, "[t]his complaint alleges damages resulting from an improper Merger." ¶7. When ruling on the motion to dismiss, the district court was right to credit these allegations. *Brown*, 97 Nev. at 583-84.

And like the shareholders in *Cohen,* Plaintiffs lost their ownership "in a specific corporation." 119 Nev. at 19. As described above, the new combined company is not the same entity in which Plaintiffs invested. The new company is majority controlled by former Turtle Beach stockholders, run by a new board of directors, and its new management team largely consists of former Turtle Beach officers. ¶¶4-7, 26-29. The new company is broadly focused on manufacturing headphones and other video game accessories, while the old Parametric was developing a very specific hypersonic sound technology. ¶¶6, 103-106. The new company is larger than old Parametric but is financially distressed. ¶101. To be clear: Plaintiffs do not bring claims on behalf of that other, new and different entity, which is called "Turtle Beach" and is controlled by Turtle Beach; rather, they bring claims for damages suffered directly by Parametric shareholders as a result of the Merger and Defendants' misconduct in connection therewith.

Defendants ignore these allegations, but make a new argument in their Writ Petition by bootstrapping the phrase "dissenting shareholders" in *Cohen* well beyond the Supreme Court's intended meaning. (Writ Pet. at 16, 22.) Defendants focus on the following two sentences: "This case involves the rights of dissenting shareholders to challenge the validity of corporate mergers . . . . A claim brought by a dissenting shareholder that questions the validity of a merger as a result of wrongful conduct on the part of majority shareholders or directors is properly classified as an individual or direct claim." *Cohen*, 119 Nev. at 9, 19. Defendants now use those sentences to contend that Parametric shareholders lose standing to challenge the Merger because they are allegedly not "dissenting shareholders" and Parametric was allegedly not a "constituent entity" to the Merger, under Defendants' view of the statutory meaning of both phrases. (Writ Pet. at 16, 22.)

There are several problems with that argument. First, the phrase "constituent entity" is a red herring. The Supreme Court in *Cohen* did not even consider the phrase "constituent entity," nor can Defendants point to any case that has done so when dismissing an otherwise direct claim for relief.

Second, the Supreme Court permitted the plaintiff, Harvey Cohen, to bring a direct claim for relief even though he was not a "dissenting shareholder" under the meaning of the statute. *Compare Cohen*, 119 Nev. at 14 ("Cohen concedes that he and the other class members failed to exercise their dissenters' rights under the statutes.") *with* NRS 92A.315 (defining "[d]issenter" as "a stockholder who is entitled to dissent from a domestic corporation's action under NRS 92A.380 ***and*** who exercises that right when and in the manner required by NRS 92A.400 to 92A.480, inclusive") (emphasis added). Under plain meaning of the word "dissent" in *Cohen*, Plaintiffs here dissented to the Merger by filing a lawsuit challenging the Merger, just like Mr. Cohen. *See* http://www.merriam-webster.com/dictionary/dissent ("dissent: to publicly disagree with an official opinion, decision, or set of beliefs").

Third, a shareholder's *ab initio* eligibility for appraisal is not a condition precedent to a direct claim for breach of fiduciary duty. No such rule can be found in *Cohen* and, if that were the rule, a Nevada board could eliminate liability for a fraudulent merger simply by enacting an appraisal-exclusion bylaw within ten days of the transaction. Indeed, despite this Merger's initial eligibility for appraisal under NRS 78.3793, the Parametric Board enacted a bylaw the day of the Merger that cut off Plaintiffs' appraisal rights. *See* ¶115. With respect to appraisal-eligible transactions, acceptance of Defendants' argument would eviscerate the Nevada legislature's choice to hold directors liable to "stockholders" for breaches of fiduciary duties that involve "intentional misconduct, fraud or a knowing violation of law." *See* NRS 78.138(7). No matter how egregious their Merger-related malfeasance, if Defendants' arguments were correct – which they are not – then a board could simply create a shell entity to effectuate a transaction, or deprive stockholders of appraisal rights, then obtain a free pass from liability in either scenario. That is not the law in any jurisdiction.

Fourth, Defendants' rigid, formulaic approach fails to consider the pragmatic nature of the transaction as a whole. As the Delaware Supreme Court has recognized when analyzing whether shareholders could directly challenge a similar two-step transaction, the substance of the transaction, rather than its technical form, is what matters:

> That is how equity views the Recapitalization, despite the fact that as a matter of form, the Recapitalization consisted of two transactions that occurred simultaneously, with the result that to an outside observer, the controlling stockholder never held the benefits of the expropriation for any length of time that the naked human eye could discern. ***In our view, that difference in form, which is a product of transactional creativity, should not affect how the law views the substance of what truly occurred, or how the public shareholders' claim for redress should be characterized***. In both cases the fiduciary exercises its control over the corporate machinery to cause an expropriation of economic value and voting power from the public shareholders. That the fiduciary does not retain the direct benefit from the expropriation but chooses instead to convert that benefit to cash by selling it to a third party, is not a circumstance that can justify depriving the injured public shareholders of the right they would otherwise have to seek redress in a direct action.

Gatz v. Ponsoldt, 925 A.2d 1265, 1281 (Del. 2007) (emphasis added) (finding that stockholders may directly bring claims surrounding stock issuance to third party). Likewise, the Supreme Court's case citations in *Cohen* also demonstrate that precise legal structure of a merger, whether it is reverse, reverse triangular, stock-for-stock, or cash, is not sufficient by itself to deprive plaintiff shareholders of standing. When determining that the merger-related claims were direct, *Cohen* relied on cases involving a variety of merger structures, some of which involved a retaining interest in the "surviving entity" and all of which held that a plaintiff had pleaded a direct claim for relief:

- ***Stock-for-stock merger agreement that involved surviving ownership in the acquiring company***. *Parnes v. Bally Entm't Corp.*, 722 A.2d 1243, 1246 (Del. 1999) (cited by *Cohen* in support of sentences 2, 3, and 4 above) (holding that claims were direct where claims alleged that "(i) [a domineering CEO] breached his fiduciary duty of loyalty by preferring himself over Bally and its stockholders; and (ii) the other Bally directors breached their fiduciary duties of loyalty by acquiescing in [the CEO's] self-interested negotiations and by approving a merger at an unfair price"). The claims in *Parnes* echo Potashner and the rest of the Board's conflicts here, particularly with regard to Potashner's threats, domination, and multiple Board members' requests for personal incentive payouts in order to support the Merger.

- ***Stock-for-stock proposed merger that would carry surviving ownership in the acquiring company, which minority stockholders rejected, continued to hold their shares, and argued the merger would render their shares worthless***. *Smith*, 50 Nev. at 72-73 (cited by *Cohen* in support of sentence 3 above) (affirming post-trial judgment for defendants but noting that plaintiffs had standing in light of allegations of fraud and that defendants sought "to oppress plaintiffs and other minority stockholders into exchanging their stock for stock in the [acquirer]").

- ***All-cash freeze-out merger***. *Coggins*, 492 N.E.2d at 1119-20 (cited by *Cohen* in support of sentence 3 above) (affirming ruling that merger was undertaken "for the personal benefit of" a controlling stockholder, affirming certification of class action of minority stockholders, and remanding for determination on damages).

- ***Merger entitling minority shareholders to "earnout certificates" based on net profits of post-merger entity over a three-year period***. *Hoggett v. Brown*, 971 S.W.2d 472, 482 (Tex. App. - Houston [14th Dist.] 1997, pet. denied) (cited by *Cohen* in support of sentence 3 above) (holding that plaintiff is "entitled to sue for the fair value of his stock, plus any special damages for losses caused by any alleged fraud or irregularity in the merger transaction that affected the fair value of his stock" but plaintiff "cannot sue for wrongful acts unconnected to the merger or for wrongs done to [the corporation]").

Fifth, in any event, Defendants did not make this argument at the district court – the phrases "dissenting shareholder" and "constituent entity" appear nowhere in Defendants' briefing below. PA503-523. Defendants therefore waived this argument and it should not be considered on their Writ Petition. *See, e.g., California State Auto. Ass'n Inter-Ins. Bureau v. Eighth Judicial Dist. Court*, 106 Nev. 197, 199, 788 P.2d 1367, 1368 (1990); *Cordova v. State*, 116 Nev. 664, 666, 6 P.3d 481, 482 (2000).

C. The Claims Are Direct Under Delaware and New York Law, Which Follow the Direct/Derivative Definition of *Cohen*

"Because the Legislature relied upon the Model Act and the Model Act relies heavily on New York and Delaware case law, we look to the . . . law of those states in interpreting the Nevada statutes." *Cohen*, 119 Nev. at 9. The parties agree that the Supreme Court should look to Delaware and New York law in the analysis. But Defendants' claim that the district court's ruling represents a "dramatic departure from the corporate law of . . . Delaware and New York" (Writ Pet. at 3) is a dramatic misrepresentation of the law of both Delaware and New York.

In Delaware, like Nevada, "[a] stockholder who directly attacks the fairness or validity of a merger alleges an injury to the stockholders, not the corporation, and may pursue such a claim even after the merger at issue has been consummated." *Parnes*, 722 A.2d at 1245.[11] As the Delaware Court of Chancery recently held in a decision squarely on point, "the Plaintiff directly challenges the

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[11] The Supreme Court's decision in *Cohen* frequently cited to *Parnes* when analyzing the direct/derivative issue. 119 Nev. at 19-23 (citing *Parnes*, 722 A.2d 1243 on five occasions).

merger, and alleges that the merger was invalid due to the fact that a majority of the Board was interested or lacked independence. As such, it is a clear case of a direct claim." *N.J. Carpenters Pension Fund v. infoGROUP, Inc.*, No. 5334-VCN, 2011 Del. Ch. LEXIS 147, at *41 (Del. Ch. Sept. 30, 2011). Put simply, "the alleged wrong here was suffered by the shareholders, whose company was sold in an allegedly tainted transaction." *Id.* As in Nevada, this premise holds true regardless of the technical structure of the merger. *Parnes* concerned a stock-for-stock merger where the stockholders retained an interest in the surviving corporation. 722 A.2d at 1245. *infoGROUP* involved an all-cash merger. 2011 Del. Ch. LEXIS 147. And in *In re Celera Corp. S'holder Litig.*, 59 A.3d 418, 425, 437 (Del. 2012) the Delaware Supreme Court recently affirmed the Court of Chancery's grant of class certification on a direct claim on a "reverse triangular merger" and a top-up option issuance of shares in order to effectuate the merger. *Id.*

Moreover, the Complaint pleads a direct claim under Delaware law because it alleges that Defendants impaired the stockholder franchise, coerced minority stockholders, and caused a woefully uninformed shareholder vote. Where a deal protection device, such as the Break-Up License here – "is preclusive of a stockholder-bidder or coercive of stockholder-purchasers as voters, [Delaware] case law would already dictate an individual, as well as derivative, characterization of an attack on the fee." *In re Gaylord Container Corp. S'holders Litig.*, 747 A.2d 71, 81 n.12 (Del. Ch. 1999). Thus, "where plaintiffs challenge the substantive unfairness of a merger protected by defensive measures, their claims are said to be direct." *Id.* Similarly, "[w]ith respect to the disclosure claim, such claims are quite obviously individual as they affect the right to vote or the personal right to determine if one will sell or not one's investment." *Wells Fargo & Co. v. First*

Interstate Bancorp, No. 14696, 1996 Del. Ch. LEXIS 3, at *24 (Del. Ch. Jan. 18, 1996).

While *Parnes* remains good law, the Delaware Supreme Court has since updated the shape of the direct/derivative analysis through a two-part test in *Tooley v. Donaldson, Lufkin, & Jenrette, Inc.*, 845 A.2d 1031, 1039 (Del. 2004).[12] That two-part test asks: "(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)?" *Id.* at 1033. New York courts have followed suit. In 2012, the Supreme Court of New York, First Appellate Division recognized that "New York has lacked a clear approach for determining" the direct/derivative distinction and admitted that, prior to *Tooley*, "our jurisprudence consists of case by case analyses that are sometimes difficult to apply to new fact patterns." *Yudell v. Gilbert*, 949 N.Y.S.2d 380, 381 (N.Y. App. Div. 2012). Consequently, the New York court held: "we adopt the test the Supreme Court of Delaware developed in *Tooley* . . . . The *Tooley* test is consistent with New York law and has the added advantage of providing a clear and simple framework to determine whether a claim is direct or derivative." *Id.*[13]

Tooley is consistent with Nevada law. Indeed, Nevada was a first-mover and deserves the credit for adopting this general framework ahead of Delaware. As

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[12] The Delaware court in *Tooley* also explained that "[t]he proper analysis has been and should remain that stated in . . . *Parnes*." 845 A.2d at 1039.

[13] Despite making dramatic statements about New York law in the introduction of their Writ Petition, Defendants cite to just two New York cases in that section, both of which are irrelevant and predate New York's adoption of the *Tooley* test. In *Auerbach v. Bennett*, 393 N.E.2d 994 (N.Y. 1979), the plaintiffs brought a derivative claim for relief and the court did not even address the direct/derivative distinction. (Writ Pet. at 2 n.2.) Even less persuasive, *Davis v. Magavern*, 654 N.Y.S.2d 517 (N.Y. App. Div. 1997), is a two paragraph decision making the obvious ruling that a claim was derivative when brought by stockholders against a corporation's law firm regarding the law firm's advice during a dissolution proceeding.

quoted above, the Supreme Court explained in *Cohen* it was dismissing derivative claims which "[1] seek damages [on behalf of the corporation] for wrongful conduct [2] that caused harm to the corporation." 119 Nev. at 19. That phrase captures the *Tooley* test in reverse order and was articulated by this Court a year prior to *Tooley* itself.

Importantly, when adopting the two-part test in *Tooley*, the Delaware Supreme Court discarded the old "special injury" test. The "special injury" analysis, which was created in a Delaware Court of Chancery decision from 1953, asked whether the injury was a wrong that was "'separate and distinct from that suffered by other shareholders.'" 845 A.2d at 1035-37. When discarding the "special injury" test, the Delaware Supreme Court called it an "amorphous and confusing concept" and held: "In our view, the concept of 'special injury' that appears in some Supreme Court and Court of Chancery cases is not helpful to a proper analytical distinction between direct and derivative actions. We now disapprove the use of the concept of 'special injury' as a tool in that analysis." *Id.* at 1035.

By repeatedly invoking the "special injury" test in their Writ Petition arguments, Defendants ask this Court to disregard clear legal developments in Nevada, Delaware, and New York rejecting that test. Defendants want the Court to go back in time to resurrect an unclear, confusing, and awkward standard from the archives of Delaware corporate jurisprudence. *See, e.g.*, Writ Pet. at 21 ("every single Parametric shareholder had their voting interest reduced in equal proportions and thus there was no 'unique' and 'personal' harm to any one shareholder"); *id.* at 24 ("But a loss in market value of stock is not a unique harm."). The Supreme Court should decline Defendants' invitation and instead continue to apply the

Cohen standard, which has since evolved into the two-part test from *Tooley* utilized by Delaware and New York.[14]

Under *Tooley*, both prongs weigh heavily in favor of these claims being direct. First, Parametric's shareholders at the time of the Merger suffered the harm. The court in *Tooley* noted that the following question is helpful in analyzing the first prong of the analysis: "'Looking at the body of the complaint and considering the nature of the wrong alleged and the relief requested, has the plaintiff demonstrated that he or she can prevail without showing an injury to the corporation?'" 845 A.2d at 1036. The answer is a resounding "yes." Plaintiffs' claims seek redress for their injuries as a result of the unfair 80%/20% valuation on their individual shares pursuant to the Merger. Plaintiffs could still prevail even if Parametric, as an entity, received an overall benefit by obtaining a larger company, Turtle Beach, as a subsidiary through the Merger.[15] It would not matter to Parametric, the entity, if the ratio on the Merger were 80/20, or 50/50, or 99/1, or vice versa, the dilution ratio valuation of stock is an issue that pertains exclusively to shareholders, not the Company. Thus, the undervaluation of their individual shares, the misrepresentations in connection with the Merger, and the public

[14] The statement in *Cohen* that "harm to the corporation, shared by all stockholders and not related to an individual stockholder" are "derivative in nature," 119 Nev. at 21, is not inconsistent with *Tooley*. If the harm is "to the corporation" rather than stockholders, *Tooley* would demonstrate that the claim is indeed derivative. But "individual stockholders" suffer the harm, as here, the claims are direct under both *Cohen* and *Tooley*. *Id.*

[15] As it turns out, Parametric did not benefit from the Merger. Turtle Beach's current market capitalization currently stands at just less than $130 million (as of two days prior to the filing of this brief) and it stood at just less than $130 million prior to the Merger announcement.

To put this in perspective, prior to the Merger, Parametric shareholders collectively owned 100% of a nearly $130 million company. As a result of the unfair Merger, those same shareholders collectively own less than 20% (less than $27 million) of Turtle Beach. Plaintiffs, however, are not pursuing injury on behalf of the corporation itself and can recover despite the deteriorated current state of the post-Merger entity.

shareholder class's loss of collective control of Parametric are all injuries to the shareholders – those are not injuries to Parametric, or Turtle Beach, the entity. *See, e.g.*, *infoGROUP*, 2011 Del. Ch. LEXIS 147, at *41-*42 ("If the Plaintiff's loyalty claim succeeds, it is the shareholders who would be entitled to compensatory damages for the value they lost when the Company was improperly sold.").

Second, if continued as a direct stockholder class action, the damages recovered in this case will go specifically to Plaintiffs and Parametric's other public stockholders at the time of the Merger. *See* ¶¶3, 9 ("plaintiffs and the shareholder class are entitled to monetary damages including the difference between the Merger valuation and the fair value of their shares"). Again, *Cohen* was ahead of *Tooley* and recognized that on a direct stockholder claim, if a plaintiff "is successful in proving that the merger was the result of wrongful conduct, his monetary damages may include the difference, if any, between the merger price and the fair value of the shares." *Cohen*, 119 Nev. at 14. This result makes sense, as it squares the recovery with those who were injured. On the other hand, if this case were maintained as a derivative action, damages belonging to the individual stockholders would go back to the corporation, *i.e.*, the current version of the acquired entity now called "Turtle Beach." That different current entity is at least 80% controlled by former-Turtle Beach insiders and, thus, the vast majority of the recovery in a derivative case would be usurped by many of the same parties that wrongfully carried out the Merger. Such a result is not supported by logic nor equity and it is squarely rejected by the analysis in *Tooley* and *Cohen*.

When addressing this issue on page 20 of their Writ Petition, Defendants miscite the holding of *AHW Inv. P'ship v. CitiGroup Inc.*, 980 F. Supp. 2d 510, 525 (S.D.N.Y. 2013). The *AHW* decision, however, is fortuitously illuminating on the *Tooley* test, as it rejects Defendants' argument that a decline in stockholder value is exclusively a derivative claim:

> Conveniently ignoring the second question [of *Tooley*] entirely, defendants contend that because all shareholders suffered when the price of Citigroup stock fell subsequent to the contemplated May 2007 sale, any claim seeking redress for that loss in value is necessarily derivative. This reasoning invokes the bright-line test that *Tooley* "expressly disapprove[d]," *id.* at 1039: that a suit must be maintained derivatively if the injury falls equally upon all stockholders," *id.* at 1037 (abrogating *Bokat v. Getty Oil Co.*, 262 A.2d 246 (Del. 1970)). That bright line and defendants' argument mistake a necessary condition for a sufficient one. "[A] direct, individual claim of stockholders that does not depend on harm to the corporation can also fall on all stockholders equally, without the claim thereby becoming a derivative claim." *Id.* These are two such direct claims. Defendants' contentions to the contrary ignore *Tooley*'s instruction that a "court should look to the nature of the wrong and to whom the relief should go." *Id.* at 1039. . . . To put it simply, plaintiffs, not Citigroup, are the victims of Citigroup and the officer defendants' alleged deception, and therefore plaintiffs are the ones with standing to sue.

AHW, 980 F. Supp. at 516-17. In contrast, in the portion of the opinion that Defendants cite (Writ Pet. at 20 n.12), the *AHW* court dismissed a common law fraud claim because so-called "'paper "los[ses]" . . . are not actually losses for purposes of New York common law fraud injuries.'" 980 F. Supp. at 525-26.[16] In the more pertinent aspect of the opinion, quoted above, the *AHW* court held that the claims in that case were direct, not derivative. *Id.* at 517-19. So too here, the district court properly held that the claims are direct.

D. The Decision in *Sweeney* Is Unpersuasive

Defendants' only authority concerning a Nevada corporation is factually inapposite and does not employ a contemporary legal analysis of the direct/derivative distinction. In *Sweeney*, 2011 U.S. Dist. LEXIS 82872, the court

[16] Defendants' related cite to *Starr Found. v American Int'l Group, Inc.*, 901 N.Y.S.2d 246 (N.Y. App. Div. 2010) suffers from the same problem. Defendants' cited language references the "paper loss" rule of a New York common law fraud claim and the New York court specifically held that because the fraud claim was insufficient, "we need not reach the question of whether the claim is direct or derivative." *Id.* at 248 n.2.

held that claims brought in the absence of a merger agreement were derivative. The decision is inapposite factually because no merger agreement had been signed in *Sweeney* and there was no merger, valid or invalid, to challenge – the directors had merely announced that they received an offer for all outstanding shares. *Id.* at *2. The court in *Sweeney* also based its decision on the concern that the "impossibly speculative" nature of computing damages was exacerbated where "there has been no sale." *Id.* at *7. However, where a merger is completed, as here, it is axiomatic that a damages computation "may include the difference, if any, between the merger price and the fair value of the shares." *Cohen*, 119 Nev. at 14.

The *Sweeney* decision also does not contain an updated view of direct/derivative jurisprudence in Nevada or Delaware. In its short analysis, *Sweeney* did cite to *Cohen*, but the *Sweeney* decision did not substantively address *Cohen's* description of the difference between a direct and derivative claim. And after citing to a Delaware case, the *Sweeney* decision resurrected the old "special injury" test that has since been discarded in Delaware. The *Sweeney* decision held: "Plaintiff here does not allege any special injury, but only an injury suffered by all shareholders in proportion to their interest in the corporation. The Complaint is therefore derivative." 2011 U.S. Dist. LEXIS 82872, at *8. *Sweeney* is thus unpersuasive factually and legally and should not impact the analysis here.

E. Even if the Merger Is Viewed as a Dilution, the Claims Are Direct, Not Derivative

Defendants seek to avoid *Parnes, Cohen*, and *Tooley* by framing the Merger as a non-merger related dilutive stock issuance. (Writ Pet. at 26-27.) But this re-framing of the transaction still does not change the result here. While the Supreme Court has yet to address the issue, the Delaware Supreme Court has held that stockholders can bring direct claims challenging a dilutive stock issuance, even where the ultimate transferee and beneficiary is a third party. *See Gatz*, 925 A.2d at 1280-81 (Del. 2007) (quoted above).[17] Likewise, the Delaware Court of Chancery recently held that with respect to a non-merger-related dilutive stock issuance, direct "[s]tanding will also exist if the board that effectuated the transaction lacked a disinterested and independent majority." *Carsanaro*, 65 A.3d at 618. As noted above, the Complaint adequately alleges that a majority of the Parametric Board was conflicted when structuring and voting upon the Merger. *Supra*, §III.C.1.a.-e. Defendants do not contend the trial court was in error for crediting those allegations. *Supra*, §III.B.

Since the motion to dismiss ruling, the Delaware Chancery Court issued an opinion even further cementing the direct nature of a dilution claim accompanied by a breach of the duty of loyalty. In *Nine Sys.*, 2014 Del. Ch. LEXIS 171, the plaintiff stockholders challenged a recapitalization plan that diluted all of the company's non-insider stockholders on a pro rata, equally shared fashion. *Id.* at *68. After a detailed analysis of the law, the Delaware Chancery Court concluded that, with respect to the non-merger related stock issuance, two alternative grounds for direct stockholder standing existed. The first involves a claim of disloyal expropriation by a control group of stockholders. *Id.* at *69-*77. The second

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[17] Defendants' citation to *Feldman v. Cutaia*, 951 A.2d 727 (Del. 2008), is inapposite. In that case, the plaintiff did "not attack the Merger price or the process used by the [target] board in obtaining that price." *Id.* at 735. Rather, that plaintiff attacked certain stock option grants which "do[] not relate to the fairness of the merger itself." *Id.* Those allegations exist in stark contrast to the claims here. Defendants' citation to *Penn Mont Secs v. Frucher*, 502 F. Supp. 2d 443, 464 (E.D. Pa. 2007) also does not assist their argument. In that case, the Pennsylvania court recognized that dilution claims are "typically" derivative claims, but noted that: "Delaware law recognizes an exception to this rule when a controlling shareholder causes minority shareholders to lose share value and voting power." *Id.* at 465. The Pennsylvania Court did address the second exception, as recognized by *Carsanaro v. Bloodhound Techs., Inc.*, 65 A.3d 618 (Del. Ch. 2013), and *In re Nine Sys. Corp. S'holders Litig.*, No. 3940-VCN, 2014 Del. Ch. LEXIS 171 (Del. Ch. Sept. 4, 2014), which renders these claims direct – a majority-conflicted Board effectuated the dilutive stock issuance for self-interested reasons.

scenario is implicated here: "as an alternative ground, the Plaintiffs may also establish standing by proving that a majority of the Board was conflicted – here, meaning interested or not independent – when it approved and implemented the Recapitalization." *Id.* at *85-*86. This Complaint so alleges. ¶¶23-34.

Consequently, whether the Merger is framed as a merger or whether, for the sake of argument, the Merger is framed as a dilutive stock issuance in which Plaintiffs retained shares in the Company, the claims are still direct and the district court properly denied Defendants' motions to dismiss.

VI. CONCLUSION

For the reasons set forth herein, Plaintiffs respectfully request that the Court decline to issue a writ.

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CERTIFICATE OF COMPLIANCE

1. I hereby certify that this Answer of Real Parties in Interest to the Petition for Writ of Mandamus or, in the Alternative, Writ of Prohibition, complies with the formatting requirements of NRAP 32(a)(4), the typeface requirements of NRAP 32(a)(5), and the type style requirements of NRAP 32(a)(6) because this Answer has been prepared in a proportionally spaced typeface using Word in 14 font size and in Times New Roman.

2. I further certify that this Answer complies with the limitations set forth by this Court's Order because, excluding the parts of the Answer exempted by NRAP 32(a)(7)(c), the brief is less than 14,000 words.

3. I hereby certify that I have read this Brief and to the best of my knowledge, information, and belief, it is not frivolous or interposed for any improper purpose. I further certify that this brief complies with all applicable Nevada Rules of Appellate Procedure, in particular NRAP 28(e), which requires every assertion in the brief regarding matters in the record to be supported by a reference to the page of the transcript or appendix where the matter relied on is to be found. I understand that I may be subject to sanctions in the event that the accompanying brief is not in conformity with the requirements of the Nevada Rules of Appellate Procedure.

DATED: January 16, 2015

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CERTIFICATE OF SERVICE

I hereby certify under penalties of perjury that on this date I served a true and correct copy of the foregoing document by sending the document via email to the addresses listed below.

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