

**IN THE SUPREME COURT OF THE STATE OF NEVADA**

\* \* \*

PARAMETRIC SOUND  
CORPORATION, VTB 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 ELIZABETH  
GONZALEZ, District Judge

Respondents,

and

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

Real parties in interest.

Electronically Filed  
Dec 03 2015 03:21 p.m.  
Tracie K. Lindeman  
Clerk of Supreme Court

Supreme Court No.: 66689

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

**BRIEF OF AMICUS CURIAE**  
**BUSINESS LAW SECTION OF**  
**THE STATE BAR OF**  
**NEVADA**

**BROWNSTEIN HYATT FARBER SCHRECK, LLP**

**JEFFREY S. RUGG, ESQ.**

Nevada Bar No. 10978

**MAXIMILIEN D. FETAZ, ESQ.**

Nevada Bar No. 12737

100 North City Parkway, Suite 1600

Las Vegas, Nevada 89106

Telephone: 702.382.2101

Facsimile: 702.382.8135

*Attorneys for Amicus Curiae Business Law Section of the State Bar of Nevada*

## **NRAP 26.1 DISCLOSURE STATEMENT**

Pursuant to Nevada Rule of Appellate Procedure 26.1, the undersigned counsel of record certifies that the following are persons and entities as described in NRAP 26.1(a), and must be disclosed. These representations are made in order that the judges of this court may evaluate possible disqualification or recusal:

1. There are no corporations or entities subject to disclosure; and
2. The only law firm that has appeared for Amicus Curiae Business Law Section of the State Bar of Nevada in this matter is the law firm of Brownstein Hyatt Farber Schreck, LLP.

DATED this 3rd day of December, 2015.

BROWNSTEIN HYATT FARBER SCHRECK, LLP

By: /s/ Jeffrey S. Rugg  
JEFFREY S. RUGG, ESQ.  
Nevada Bar No. 10978  
MAXIMILIEN D. FETAZ, ESQ.  
Nevada Bar No. 12737

*Attorneys for Attorneys for Amicus Curiae Business  
Law Section of the State Bar of Nevada*

## **TABLE OF CONTENTS**

	<b>Page</b>
I. STATEMENT IN COMPLIANCE WITH NRAP 29(D)(3).....	1
A. Statement of the Identity of the Amicus Curiae.....	1
B. Statement Regarding Interests of the Amicus Curiae in This Appeal .....	2
C. Source of Authority for Amicus Curiae to File the Instant Brief in This Appeal.....	3
II. SUMMARY OF DISCUSSION.....	4
A. The Court Should Continue to Apply the Direct Harm Test as Stated in Cohen .....	4
B. The Nevada Legislature Provides Specific Guidance that a Dilution Claim is, if Anything, Derivative .....	5
III. DISCUSSION OF ISSUE ONE .....	6
A. There are Three Tests Used to Distinguish Direct Suits from Derivative Suits .....	6
1. The direct harm test requires the plaintiff to demonstrate a direct injury that is independent from any injury to the corporation.....	7
2. The special injury test requires the plaintiff shareholder to demonstrate an injury special to him or her.....	9
3. The duty owed test requires the plaintiff shareholder to demonstrate that he or she was owed the duty breached .....	10
B. The Test Articulated in Cohen Closely Resembles the Direct Harm Test.....	11
C. The Direct Harm Test as Set Forth in Cohen is the Test the Court Should Continue to Apply.....	12
D. With a Clear Test in Place, Proper Redress Will be Accorded and Unscrupulous Litigation Will be Curbed .....	16
IV. DISCUSSION OF ISSUE TWO .....	18

**TABLE OF CONTENTS**  
**(continued)**

	<b>Page</b>
A. The Directors Hold the Sole Authority Regarding the Issuance of Shares, Which is to the Benefit of the Corporation.....	18
B. A Derivative Claim is a Valid Claim When the Shareholder Maintains His or Her Shares .....	20
V. CONCLUSION .....	22

## TABLE OF AUTHORITIES

	<b>Page(s)</b>
<b>Cases</b>	
<i>Ace Am. Ins. Co. v. Hallier</i> , 2:14-CV-00703-APG, 2015 WL 1326499 (D. Nev. Mar. 25, 2015) .....	9
<i>Bayberry Associates v. Jones</i> , 783 S.W.2d 553 (Tenn. 1990) .....	14, 15
<i>Capital Z Fin. Services Fund II, L.P. v. Health Net, Inc.</i> , 840 N.Y.S.2d 16 (N.Y. App. Div. 2007) .....	9
<i>Carsanaro v. Bloodhound Techs., Inc.</i> , 65 A.3d 618 (Del. Ch. 2013) .....	19
<i>Cohen v. Mirage Resorts, Inc.</i> , 119 Nev. 1, 62 P.3d 720 (2003).....	<i>passim</i>
<i>G &amp; N Aircraft, Inc. v. Boehm</i> , 743 N.E.2d 227 (Ind. 2001) .....	10
<i>Gentile v. Rossette</i> , 906 A.2d 91 (Del. 2006) .....	21
<i>Kollman v. Cell Tech Int’l, Inc.</i> , 279 P.3d 324 (Or. App. 2012) .....	8
<i>Kramer v. W. Pac. Indus., Inc.</i> , 546 A.2d 348 (Del. 1988) .....	8
<i>Lipton v. News Int’l, Plc</i> , 514 A.2d 1075 (Del. 1986) .....	9
<i>Mann v. GTCR Golder Rauner, L.L.C.</i> , 483 F. Supp. 2d 884 (D. Ariz. 2007) .....	8
<i>Marcuccilli v. Ken Corp.</i> , 766 N.E.2d 444 (Ind. Ct. App. 2002) .....	10

<i>New York City Employees' Ret. Sys. v. Jobs</i> , 593 F.3d 1018 (9th Cir. 2010) <i>overruled on other grounds by</i> <i>Lacey v. Maricopa County</i> , 693 F.3d 896 (9th Cir. 2012) .....	8
<i>Parnes v. Bally Entm't Corp.</i> , 722 A.2d 1243 (Del. 1999) .....	8
<i>Schuster v. Gardner</i> , 25 Cal. Rptr. 3d 468 (Cal. Ct. App. 2005) .....	9
<i>Shoen v. SAC Holding Corp.</i> , 122 Nev. 621, 137 P.3d 1171 (2006) .....	20
<i>Spillyards v. Abboud</i> , 662 N.E.2d 1358 (Ill. App. 1996) .....	10
<i>Strassenburgh v. Straubmuller</i> , 683 A.2d 818 (N.J. 1996) .....	10
<i>Tooley v. Donaldson, Lufkin &amp; Jenrette, Inc.</i> , 845 A.2d 1031 (Del. 2004) .....	<i>passim</i>

## **Statutes**

Del. Code Ann. tit. 8, § 102 (West 2005) .....	21
Del. Code Ann. tit. 8, § 152 (West 2005) .....	21
NRS 28.211 .....	17
NRS 48.520 .....	20
NRS 78.120(1) .....	19
NRS 78.138(1) .....	14
NRS 78.138(3) .....	6, 7
NRS 78.138(4)-(5) .....	7, 15
NRS 78.140 .....	21
NRS 78.200 .....	13, 17, 19, 21

NRS 78.200(2) .....	5, 7, 18, 20
NRS 78.211 .....	<i>passim</i>
NRS 78.211(1) .....	5, 18, 19, 20
NRS 78.267 .....	5, 19, 21
NRS 78.330 .....	6, 21
NRS 78.335 .....	6, 21
NRS 92A.120 .....	7
NRS 92A.300-92A.500.....	11
NRS 92A.390 .....	11
NRS Chapter 78 and 92A .....	16
<b>Other Authorities</b>	
2015 Nevada Laws Ch. 514 § 10 .....	19
BLACK’S LAW DICTIONARY 1138-39 (10th ed.).....	17
Nevada BLS § 2 .....	1
Nevada BLS § 9.4 .....	2

**I. STATEMENT IN COMPLIANCE WITH NRAP 29(d)(3)**

**A. Statement of the Identity of the Amicus Curiae.**

Amicus Curiae Business Law Section of the State Bar of Nevada (“BLS” or “Amicus Curiae”) is a section of the State Bar of Nevada whose purpose is (i) to enhance the role and skills of lawyers engaged in the practice of business law through study, collection, development and dissemination of materials on subjects of interest to the business law practitioner, (ii) to assist in the formulation, administration and implementation of programs, forums, and other activities for the education of members of the State Bar of Nevada in matters pertaining to business laws and regulations, (iii) to assist the State Bar of Nevada in the development of a legislative program pertaining to business laws and regulations, and (iv) to act upon all matters germane to its purposes as so described or referred to it by the Board of Governors. *See* AMENDED AND RESTATED BYLAWS OF THE BUSINESS LAW SECTION STATE BAR OF NEVADA at § 2, available at <http://www.nvbar.org/content/business-law-section>.

BLS is also concerned with drafting legislation, or proposing to support or oppose the adoption of legislation by the Nevada Legislature that (i) relates closely and directly to the administration of justice, (ii) involves matters which are not primarily political and as to which evaluation by lawyers would have particular relevance if not related closely and directly to the administration of



justice, or (iii) comes within BLS's special expertise and jurisdiction. *Id.* at § 9.4.

In light of this appeal addressing the interpretation of Nevada's corporate statutes, BLS's role in drafting, supporting, and/or opposing legislation before the Nevada Legislature related to Nevada's corporate statutes is particularly relevant.

This position is being presented only on behalf of the Business Law Section of the State Bar of Nevada. This position should not be construed as representing the position of the Board of Governors or the general membership of the State Bar. The Business Law Section, which takes this position, is a voluntary section with members composed of lawyers practicing in a specified area of law. This position is taken as a result of the affirmative vote of the executive committee of the Business Law Section, which is the governing body of that section. No approval or disapproval of the general membership of this section has been obtained.

**B. Statement Regarding Interests of the Amicus Curiae in This Appeal.**

As discussed *infra*, the Court specifically invited BLS to participate in this appeal because the Court believed BLS's input "may be helpful to the important issues raised by this case." (*See* Order for Supplemental Briefing and Inviting Participation by Amicus Curiae ("Order re Supplemental Briefing"), at

p. 2.) BLS agrees with the Court's belief as the issues raised on appeal directly deal with the interpretation of Nevada's corporate statutes, which BLS has assisted the Nevada Legislature in developing. Moreover, BLS's input will assist the Court in determining the law on future derivative and direct lawsuits brought in this State. Finally, the outcome of this appeal and the questions and issues the Court invited BLS to address are important to Nevada's continued role as a lead state where businesses look to incorporate.

**C. Source of Authority for Amicus Curiae to File the Instant Brief in This Appeal.**

On September 3, 2015, the Court issued an order in this appeal seeking supplemental briefing from the parties on two issues:

First, the parties should address how the test articulated in *Cohen v. Mirage Resorts, Inc.*, 119 Nev. 1, 62 P.3d 720 (2003), compares to the three primary tests—direct harm, special injury, and duty owed—other jurisdictions use to distinguish direct suits from derivative suits. This analysis should include a critique of the tests, the effect, if any, the tests have on opening litigation floodgates against directors, and fairness considerations regarding whether shareholders or surviving entities are entitled to monetary judgments. Further, the parties should recommend the test best for Nevada to use to distinguish direct suits from derivative suits and articulate what facts must be alleged to sustain a direct shareholder lawsuit at the pleading stage.

Second, the parties should address whether share dilution claims can be brought directly or derivatively. If direct suits are sometimes permissible, the analysis

should consider what conditions are necessary to allow a direct suit based on dilution.

(See Order re Supplemental Briefing, at pp. 1-2.)

In addition to the parties providing supplemental briefs, the Court invited BLS to submit an amicus brief on the issues outlined above. Once BLS became aware of the Order re Supplemental Briefing, the BLS executive committee analyzed the Order re Supplemental Briefing and the Court's invitation to address the above issues. Following their analysis, the executive committee voted to accept the Court's invitation to submit an amicus brief. Accordingly, BLS's amicus brief now follows.

## **II. SUMMARY OF DISCUSSION**

### **A. The Court Should Continue to Apply the Direct Harm Test as Stated in *Cohen*.**

In *Cohen*, the Court adopted the direct harm test by holding that in the context of a merger “a former shareholder does not have standing to assert a derivative claim. A former shareholder does. (*sic*) however, have standing to seek relief for direct injuries that are *independent of any injury suffered by the corporation.*” *Cohen v. Mirage Resorts, Inc.*, 119 Nev. 1, 19, 62 P.3d 720, 732 (2003) (citations omitted and emphasis added).

The Court should continue to apply the direct harm test as articulated in *Cohen* because the test provides the clearest path in distinguishing between a

direct and derivative claim. Moreover, neither the special injury test nor the duty owed test are effective to accomplish the desired result—determining whether a claim is direct or derivative.

Additionally, continued use of the direct harm test, as articulated in *Cohen*, provides the courts of this State with an effective tool to curb unscrupulous litigation and avoid opening the litigation floodgates. Rather than adopt a direct versus derivative test hinging on a single word (*e.g.*, “merger”) subject to broad definition, the direct harm test of *Cohen*, based on the nature of the harm caused, is best.

**B. The Nevada Legislature Provides Specific Guidance that a Dilution Claim is, if Anything, Derivative.**

The Nevada Legislature enacted statutes stating that in the absence of “actual fraud” the judgment of the board of directors as to the consideration received for shares issued by the corporation is conclusive. Moreover, the consideration may consist of any tangible or intangible property or benefit to the corporation. *See* NRS 78.211(1); NRS 78.200(2). Therefore, as a matter of Nevada law, the consideration for shares issued by the corporation is for the benefit of the corporation. Further, the legislature eliminated a shareholder’s independent preemptive right to acquire a corporation’s authorized but unissued shares. *See* NRS 78.267.

Thus, as Nevada law ascribes any benefit related to the issuance of the corporation's shares solely to the corporation and eliminates the shareholder's independent preemptive right, dilution claims in Nevada are properly pled only as derivative claims. Of course, if a derivative claim is viable, the shareholder will receive the proportionate benefit from a damages award to the corporation and, regardless of dilution, the shareholder maintains the right to elect or remove the directors responsible for the issuance through normal procedures. *See* NRS 78.330; NRS 78.335.

### **III. DISCUSSION OF ISSUE ONE**

#### **A. There are Three Tests Used to Distinguish Direct Suits from Derivative Suits.**

As the Court noted, there are three tests used to distinguish direct suits from derivative suits in the context of shareholder litigation—the direct harm test, the special injury test, and the duty owed test. Although each of the aforementioned tests will be discussed in turn below, it must first be noted that the Nevada Legislature has provided the Court guidance on this issue.

The Nevada Legislature has stated that “[d]irectors and officers, in deciding upon matters of business, are presumed to act in good faith, on an informed basis and *with a view to the interests of the corporation.*” NRS 78.138(3) (emphasis added). The corporation's interests, therefore, are presumed to sit at the forefront of the directors' decisions related to the business

of the corporation, including, but not limited to, the director's plan for a merger or the issuance of shares. *See* NRS 92A.120; NRS 78.211. That is not to say that the directors do not owe any duties to the shareholders' interests, but the interests of the shareholders is one of several interests that may be considered by the directors in deciding upon matters of business and the shareholders' interest is not a dominant factor. NRS 78.138(4)-(5).

The presumption of NRS 78.138(3) that directors act in "the interests of the corporation" is elevated in the context of the corporation issuing shares or the directors determining the consideration appropriate for the issuance of the shares. In both of those instances, the judgment of the board of directors is conclusive in the absence of actual fraud. *See* NRS 78.200(2); NRS 78.211(1).

1. ***The direct harm test requires the plaintiff to demonstrate a direct injury that is independent from any injury to the corporation.***

Under the direct harm test, the plaintiff must demonstrate a direct injury that is independent from any injury to the corporation:

The stockholder's claimed direct injury must be independent of any alleged injury to the corporation. The stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation.

*Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1039 (Del. 2004).

The direct harm test was established and discussed over the years in the

Delaware Courts. *See Kramer v. W. Pac. Indus., Inc.*, 546 A.2d 348, 351 (Del. 1988) (“For a plaintiff to have standing to bring an individual action, he must be injured *directly* or *independently* of the corporation.”); *Parnes v. Bally Entm’t Corp.*, 722 A.2d 1243, 1245 (Del. 1999) (“Stockholders may sue on their own behalf (and, in appropriate circumstances, as representatives of a class of stockholders) to seek relief for direct injuries that are independent of any injury to the corporation.”).

Although the direct harm test has been discussed for several decades, the *Tooley* Court identified specific questions to be answered when determining whether a claim is derivative or direct:

(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)?

*Tooley*, 845 A.2d at 1033.

Jurisdictions all over the country have adopted the direct harm test articulated by the *Tooley* Court and applied it accordingly. *See New York City Employees’ Ret. Sys. v. Jobs*, 593 F.3d 1018, 1022 (9th Cir. 2010) *overruled on other grounds by Lacey v. Maricopa County*, 693 F.3d 896 (9th Cir. 2012); *Mann v. GTCR Golder Rauner, L.L.C.*, 483 F. Supp. 2d 884, 896 (D. Ariz. 2007); *Kollman v. Cell Tech Int’l, Inc.*, 279 P.3d 324, 333 (Or. App. 2012);

*Capital Z Fin. Services Fund II, L.P. v. Health Net, Inc.*, 840 N.Y.S.2d 16, 23 (N.Y. App. Div. 2007); *Schuster v. Gardner*, 25 Cal. Rptr. 3d 468, 476 (Cal. Ct. App. 2005); *Ace Am. Ins. Co. v. Hallier*, 2:14-CV-00703-APG, 2015 WL 1326499, at \*2 (D. Nev. Mar. 25, 2015).

Thus, in order to bring a direct claim, the direct harm test requires the plaintiff shareholder to demonstrate a direct injury that is independent from any injury to the corporation.

2. ***The special injury test requires the plaintiff shareholder to demonstrate an injury special to him or her.***

The special injury test requires the plaintiff shareholder to suffer a special injury in order to bring a direct claim against the corporation. The special injury is “defined as ‘a wrong inflicted upon him alone or a wrong affecting any particular right which he is asserting, such as his preemptive rights as a stockholder, rights involving the control of the corporation, or a wrong affecting the stockholders and not the corporation.’” *Lipton v. News Int’l, Plc*, 514 A.2d 1075, 1078 (Del. 1986) *disapproved of by Tooley*, 845 A.2d 1031 (quoting *Elster v. American Airlines, Inc.*, 100 A.2d 219, 222 (Del Ch. 1953)). Essentially, the plaintiff must establish “an injury distinct from that suffered by other shareholders or a wrong involving one of his contractual rights as a shareholder.” *Id.*



In adopting the direct harm test, the *Tooley* Court concurrently “disapprove[d]” of the special injury test. *Tooley*, 845 A.2d at 1035. Other jurisdictions, however, still use the test to determine whether a claim is direct or derivative. *See Spillyards v. Abboud*, 662 N.E.2d 1358, 1363 (Ill. App. 1996) (holding that in order “to have standing to sue individually, rather than derivatively on behalf of the corporation, the plaintiff must allege a special injury”); *Strasenburgh v. Straubmuller*, 683 A.2d 818, 830 (N.J. 1996) (“If the breach of duty causes a ‘special injury,’ shareholders may sue directly.”).

Therefore, the special injury test requires the plaintiff shareholder to demonstrate an injury special to him or her that is distinct from the shareholders as a whole or the corporation.

3. ***The duty owed test requires the plaintiff shareholder to demonstrate that he or she was owed the duty breached.***

With the duty owed test, a claim is direct or derivative based on who is owed the fiduciary duty. *See G & N Aircraft, Inc. v. Boehm*, 743 N.E.2d 227, 234 (Ind. 2001) (noting that a direct action may be “brought in the name of the shareholder to redress an injury sustained by, or enforce a duty owed to, the holder.” (internal quotation marks and citations omitted)). Under the duty owed test, “[d]irect actions are typically initiated to enforce a right to vote, compel dividends, prevent oppression or fraud against minority shareholders, inspect corporate books and to compel shareholder meetings.” *Marcuccilli v. Ken*

Corp., 766 N.E.2d 444, 449 (Ind. Ct. App. 2002) (citing *G & N Aircraft*, 743 N.E.2d 227).

Accordingly, the duty owed test requires the plaintiff shareholder to demonstrate that he or she was owed a duty that the defendant breached.

**B. The Test Articulated in *Cohen* Closely Resembles the Direct Harm Test.**

In *Cohen v. Mirage Resorts, Inc.*, the Court analyzed the dismissal of several shareholder claims related to a merger involving a corporation qualifying for dissenter's rights under NRS 92A.300-92A.500.<sup>1</sup> 119 Nev. 1, 62 P.3d 720 (2003). As part of its analysis, the Court considered whether the claims were direct or derivative. *Id.* at 19, 62 P.3d at 732. First, the Court held that “[a] derivative claim is one brought by a shareholder on behalf of the corporation to recover for harm done to the corporation.” *Id.*

Then the Court held that in the context of a merger “a former shareholder does not have standing to assert a derivative claim. A former shareholder does. (sic) however, have standing to seek relief for direct injuries that are *independent of any injury suffered by the corporation.*” *Id.* (citations omitted and emphasis added).

---

<sup>1</sup> Shareholders of a publicly traded corporation do not qualify for these rights. See NRS 92A.390.

The Court further explained:

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.* (citations omitted).

Although the Court’s analysis noted above may create some confusion between the special injury test and the direct harm test, the fundamental precept identified by the Court (*i.e.*, a direct claim requires injuries that are “independent of any injury suffered by the corporation”) more closely tracks with the direct harm test than any other test. Thus, BLS agrees with both the Petitioners and Real Parties in Interest that the test in *Cohen* most closely resembles the direct harm test.

**C. The Direct Harm Test as Set Forth in *Cohen* is the Test the Court Should Continue to Apply.**

The direct harm test provides the clearest path in distinguishing between a direct and derivative claim. Following *Cohen*, a claim is direct if the harm is caused to the “unique personal property” of the shareholder, such as having the shareholder’s interest in the corporation liquidated in a merger. On the other

hand, where a claim is based on harm to the corporation, such as allegedly receiving inadequate consideration for shares issued by the corporation, the claim is derivative and is subject to the statutory standard set forth in NRS 78.200 and NRS 78.211.

Continuation of *Cohen* is consistent with *Tooley*. As the Delaware Supreme Court stated, the answer to the second question (*i.e.*, who would receive the benefit of any recovery or other remedy) “should logically follow” the answer to the first question (*i.e.*, who suffered the alleged harm). *Tooley*, 845 A.2d at 1036. In this manner, the direct harm test seeks to tie the injury suffered to the complainant—either the shareholder or the corporation.

Unlike the direct harm test, the special injury test cannot accomplish what is desired from the Court’s analysis of direct versus derivative claims. *Id.* at 1035. Indeed, identifying individual injuries among several shareholders does not create a clear line for the Court to determine the nature of a claim, while the direct harm test does. *See Tooley*, 845 A.2d at 1038 (noting, while analyzing a decision using the special injury test, that “[i]ronically, the Court could have reached the same correct result by simply concluding that the manipulation directly and individually harmed the stockholders, without injuring the corporation”). Thus, any alleged benefit that comes from using the special

injury test is of no consequence in light of the direct harm test providing the same result in a clearer fashion.

Regarding the duty owed test, the test provides an even less clear distinction between a direct and derivative claim. As the Tennessee Supreme Court noted in *Bayberry Associates*, the duty owed test cannot answer the question of whether a claim is direct or derivative because the duty may be owed both to the corporation and the plaintiff shareholder:

Unquestionably a stockholder may bring suit in his own name to recover damages from an officer of a corporation for acts which are violations of a duty arising from contract or otherwise and owing directly from the officer to the injured stockholder, though such acts are also violations of duty owing to the corporation.

*Bayberry Associates v. Jones*, 783 S.W.2d 553, 559-60 (Tenn. 1990) (quoting *Waller v. Waller*, 49 A.2d 449, 453 (Md. 1946) (citations omitted)).

In congruence with the above, Nevada law declares that a director's duties are owed first to the corporation:

Directors and officers shall exercise their powers in good faith and with a view to the interests of the corporation.

NRS 78.138(1). Further, Nevada law establishes a number of considerations that comprise the interest of the corporation, including the long or short-term

interests of the shareholders, but Nevada law also states that none of these considerations is dominant. NRS 78.138(4)-(5).

The *Bayberry Associates* Court agrees noting that even though directors have duties to both the corporation and the shareholders, a director's duty to the corporation is primary:

It is generally stated that directors occupy a fiduciary relation to the corporation and all its stockholders, but they are not trustees for the individual stockholders. The reason for this distinction is that in law the corporation has a separate existence as a distinct person, in which all the corporate property is vested and to which the directors are responsible for a strict and faithful discharge of their duty, but there is no legal privity or immediate connection between the directors and the individual stockholders.

*Bayberry Associates*, 783 S.W.2d at 560 (Tenn. 1990) (quoting *Waller*, 49 A.2d at 454 (citations omitted)).

In sum, the direct harm test avoids the confusion and lack of clarity found in the special injury test and duty owed test. The direct harm test, as set forth in *Cohen*, allows the Court to focus on the relevant aspects of the claim—who suffered the alleged harm and who would receive the benefit of any recovery or other remedy.

**D. With a Clear Test in Place, Proper Redress Will be Accorded and Unscrupulous Litigation Will be Curbed.**

With the clear focus provided by the direct harm test, the Court will be able to provide the redress to the proper party—either the shareholder or the corporation. The fairness of any award will not be at issue because the award will flow to the party or entity who suffered the alleged harm.

Furthermore, the Court's concern regarding the opening of the litigation floodgates is well taken by the Amicus Curiae. Indeed, as Nevada continues its role as a leader in corporate law and governance through the Nevada Legislature's development of NRS Chapter 78 and 92A and the continued development of case law arising out of this State's Business Courts, the desire to create a corporate environment free of unscrupulous litigation so that both shareholders and directors receive effective and efficient resolutions of their respective disputes is of critical importance. With a clear test that distinguishes between shareholder claims which are derivative from those that are direct, the courts of this State will be equipped to curb unscrupulous litigation and alleviate the concern of opening the litigation floodgates.

Indeed, there is no reason a shareholder with a meritorious grievance cannot pursue a derivative claim unless the plaintiff shareholder is concerned that (1) upon making the required demand, the directors will comply, or (2) the shareholder hopes to convert a claim belonging to the corporation into a

personal windfall. Avoiding these motivations promotes the maintenance of a test that protects the interests of a corporation while simultaneously providing a shareholder a right to pursue wrongdoing. This principle is even more important where the legislature has expressly chosen to defer to the board's judgment in the context of the issuance of shares, including the consideration for such shares. *See* NRS 78.200; NRS 28.211.

Further, determining whether a claim is derivative or direct based on the use of a single word to describe a transaction (*e.g.*, “merger”), would either open the floodgates to litigation involving any number of merger-type transactions or limit management's ability to describe a transaction. Aggressive shareholders will label transactions as “mergers” in their complaints simply to pursue direct claims and the potential windfall, even when the transaction is not formally described as a merger. Notably, the definition of the term “merger” takes over a page in Black's Law Dictionary, and includes 16 sub-varieties of mergers. BLACK'S LAW DICTIONARY 1138-39 (10th ed.). Rather than adopt a direct versus derivative test turning on a single word subject to broad definitions, the direct harm test of *Cohen*, based on consideration of the nature of the harm caused, is best.

In conclusion, the direct harm test, which the *Cohen* Court applied, is the appropriate test for the Court to continue in this jurisdiction. Further, the direct



harm test will provide for the proper redress to complainants—whether individual shareholders or derivatively to the corporation—and minimize the potential for unscrupulous litigation by providing a clear standard for the courts of this State to follow and apply.

#### **IV. DISCUSSION OF ISSUE TWO**

##### **A. The Directors Hold the Sole Authority Regarding the Issuance of Shares, Which is to the Benefit of the Corporation.**

Although case law from other states exists related to the dilution issue, the Nevada Legislature has directly addressed this issue and directed that (i) the directors' judgment as to the consideration received be given deference and (ii) that the consideration is a benefit to the corporation:

The board of directors may authorize shares to be issued for consideration consisting of any tangible or intangible property or benefit to the corporation, including, but not limited to, cash, promissory notes, services performed, contracts for services to be performed or other securities of the corporation. The judgment of the board of directors as to the consideration received for the shares issued is conclusive in the absence of actual fraud in the transaction.

NRS 78.211(1)<sup>2</sup>; *see also* NRS 78.200(2). Moreover, for a corporation formed after October 1, 1991, the Nevada Legislature eliminated any claim by a

---

<sup>2</sup> During the 78th (2015) Session of the Nevada Legislature, NRS 78.211 was amended to allow the directors to determine the amount of consideration received in an issuance through a formula if such is stated in the articles of

shareholder based on dilution absent a right established in the corporation's articles. *See* NRS 78.267. Specifically, the legislature eliminated a shareholder's independent preemptive right to acquire a corporation's unissued shares. *Id.* Thus, in combination with NRS 78.211 and NRS 78.200, any benefit related to the issuance of the corporation's shares runs solely to the corporation.

The above follows the general tenet of Nevada corporate law: "the board of directors has full control over the affairs of the corporation." NRS 78.120(1). The simplicity of Nevada's law on this issue highlights the fact that directors are empowered with significant discretion in their handling of the corporation's business and affairs, including, but not limited to, acquiring assets, raising capital, compensating officers/employees of the corporation, and paying off debts. NRS 78.211(1); *c.f.*, *Carsanaro v. Bloodhound Techs., Inc.*, 65 A.3d 618, 655 (Del. Ch. 2013) (issuing shares has "a variety of corporate purposes, including paying off debts, acquiring tangible or intangible assets, compensating employees, or acquiring other entities").<sup>3</sup> Thus, dilution claims in Nevada are properly pled as derivative claims.

---

incorporation or resolution. *See* 2015 Nevada Laws Ch. 514, at Sec. 10 (S.B. 446).

<sup>3</sup> Nevada law does not provide directors with unlimited discretion in this regard. In the presence of actual fraud, the directors do not enjoy the conclusive

**B. A Derivative Claim is a Valid Claim When the Shareholder Maintains His or Her Shares.**

In derivative suits, shareholders are allowed to “‘compel the corporation to sue’ and to thereby pursue litigation on the corporation’s behalf against the corporation’s board of directors and officers, in addition to third parties.” *Shoen v. SAC Holding Corp.*, 122 Nev. 621, 633, 137 P.3d 1171, 1179 (2006). Moreover, “[a] derivative claim is one brought by a shareholder on behalf of the corporation to recover for harm done to the corporation.” *Cohen*, 119 Nev. at 19, 62 P.3d at 732.

Under Nevada law, when a share issuance is made and there is actual fraud, a shareholder may derivatively bring suit against the directors subject to NRS 48.520 and NRCP 23.1. Necessarily, the recovery of any damages related to the issuance belongs to the corporation as it issued the shares and, if there was actual fraud, is entitled to any additional value for the shares. The shareholders cannot (and should not) directly receive damages caused by the share issuance as the shareholders did not directly suffer any harm from the issuance in the form of lost unique personal property that is independent from any harm to the corporation. Further, when the shareholder is still a shareholder in the corporation, the shareholder will receive the proportionate benefit from a

---

presumption. *See* NRS 78.211(1); NRS 78.200(2). That said, the presence of actual fraud does not convert a derivative claim to a direct claim.

damages award to the corporation and maintains the right to elect or remove the directors responsible for the issuance through normal procedures. *See* NRS 78.330; NRS 78.335.

Although Delaware recognizes a limited exception to establish a hybrid direct/derivative dilution claim, the Supreme Court of Delaware offered no analysis of Delaware's corporate statutes related to share issuance or preemption in reaching its decision.<sup>4</sup> *See generally Gentile v. Rossette*, 906 A.2d 91 (Del. 2006). The *Gentile* Court's failure to analyze its legislature's determination on this issue is not without consequence. In Nevada, the combined effect of NRS 78.200, NRS 78.211, and NRS 78.267 is that a dilution claim is solely derivative, if it exists at all.<sup>5</sup>

---

<sup>4</sup> Delaware law (*i.e.*, Del. Code Ann. tit. 8, § 152 (West 2005) and Del. Code Ann. tit. 8, § 102 (West 2005)) provides similar rights as those ascribed under Nevada law (*i.e.*, NRS 78.267, NRS 78.211 and NRS 78.200).

<sup>5</sup> Moreover, the *Gentile* court created its hybrid claim in the context of a controlling shareholder sitting on both sides of a transaction—a context where the Nevada Legislature has developed a statutory scheme that is distinct from that in Delaware. *See, e.g.*, NRS 78.140.

V. **CONCLUSION**

In response to the Court's request, BLS files this Amicus Brief answering each of the Court's questions posed to it in the Order re Supplemental Briefing.

DATED this 3rd day of December, 2015.

BROWNSTEIN HYATT FARBER SCHRECK, LLP

By: /s/ Jeffrey R. Rugg  
JEFFREY S. RUGG, ESQ.  
Nevada Bar No. 10978  
MAXIMILIEN D. FETAZ, ESQ.  
Nevada Bar No. 12737

*Attorneys for Amicus Curiae Business Law Section of  
the State Bar of Nevada*

## **CERTIFICATE OF COMPLIANCE**

I hereby certify that I have read this amicus brief, and to the best of my knowledge, information and belief, the brief is not frivolous or interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. I further certify that this brief complies with all applicable Nevada Rules of Appellate Procedure, including the requirement of NRAP 28 and 29 that every assertion in the brief regarding matters in the record be supported by a reference to the page and volume number, if any, of the appendix where the matter relied on is to be found. Additionally, as required under NRAP 32(a)(8), I certify that the brief complies with the formatting requirements of Rule 32(a)(4)-(6), including the type face and type style requirements, and is Times New Roman, 14 point font. I further certify that, in compliance with NRAP 29(e), and NRAP 32(a)(7)(A)(ii) and (a)(7)(D)(ii), the brief complies with the type-volume limitation and contains 4,852 words, excluding the disclosure statement, table of contents, table of authorities, Certificate of Service and this Certificate of Compliance.

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 or if this certificate is incomplete or inaccurate.

DATED this 3rd day of December, 2015.

BROWNSTEIN HYATT FARBER SCHRECK, LLP

By: /s/ Jeffrey R. Rugg  
JEFFREY S. RUGG, ESQ.  
Nevada Bar No. 10978  
MAXIMILIEN D. FETAZ, ESQ.  
Nevada Bar No. 12737

*Attorneys for Amicus Curiae Business Law Section of  
the State Bar of Nevada*

## **CERTIFICATE OF SERVICE**

I hereby certify that I electronically filed the foregoing **BRIEF OF AMICUS CURIAE BUSINESS LAW SECTION OF THE STATE BAR OF NEVADA** with the Clerk of the Court of the Supreme Court of Nevada by using the Court's Electronic Filing System on December 3, 2015.

I certify that all participants in the case listed below and are registered electronic filing users and that service will be accomplished by the Court's Electronic Filing system or by U.S. Mail as listed below:

Kelly H. Dove (Snell & Wilmer, LLP/Las Vegas)  
Richard C. Gordon (Snell & Wilmer, LLP/Las Vegas)  
Joshua D. N. Hess (Dechert LLP/San Francisco)  
Brian Raphael (Dechert LLP/San Francisco)  
Neil A. Steiner (Dechert LLP/New York)  
*Attorneys for Petitioners Turtle Beach Corporation and VTB Holdings Inc.*

Robert J. Cassity (Holland & Hart LLP/Las Vegas)  
J. Stephen Peek (Holland & Hart LLP/Las Vegas)  
John P. Stigi, III (Sheppard, Mullin, Richter, & Hamilton LLP)  
*Attorneys for Petitioners Kenneth Potashner, Elwood Norris, Seth Putterman, Robert Kaplan, Andrew Wolfe, James Honore*

Randall J. Baron (Robbins Geller Rudman & Dowd, LLP)  
David A. Knotts (Robbins Geller Rudman & Dowd, LLP)  
David C. O'Mara (O'Mara Law Firm, P.C.)  
Jonathan M. Stein (Saxena White PA)  
Adam Warden (Saxena White PA)  
Joseph E. White, III (Saxena White PA)  
*Attorneys for Real Parties in Interest VITIE RAKAUSKAS, individually and on behalf of all others similarly situated, and Intervening Plaintiffs RAYMOND BOYTHIM and GRANT OAKES*



☒ **BY U.S. MAIL:** by placing the document(s) listed above in a sealed envelope with postage thereon fully prepaid, in the United States mail at Las Vegas, Nevada addressed as set forth below:

Honorable Elizabeth Gonzalez  
Eighth Judicial District Court Regional Justice Center  
200 Lewis Avenue  
Las Vegas, NV 89155

/s/Karen Mandall  
an employee of Brownstein Hyatt Farber Schreck, LLP