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Case No. 9318-VCL

IN THE COURT OF CHANCERY IN THE STATE OF DELAWARE

IN RE KINDER MORGAN ENERGY PARTNERS, L.P. CAPEX LITIGATION	)))	CONSOLIDATED CASE No. 9318-VCL

LEAD PLAINTIFF'S SUPPLEMENTAL BRIEF IN SUPPORT OF MOTION FOR FINAL APPROVAL OF SETTLEMENT, CLASS CERTIFICATION AND APPLICATION FOR AN AWARD OF ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES

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INTRODUCTION

Lead Plaintiff Jon Slotoroff ("Lead Plaintiff"), on behalf of himself and the former common unitholders of Kinder Morgan Energy Partners, L.P. ("KMP" or the "Company"), respectfully submits this supplemental memorandum in support of his Motion for Final Approval of: (1) the proposed $27.5 million Settlement of this consolidated class action (the "Action" or "Litigation"); (2) the proposed Plan of Allocation of the Settlement proceeds; (3) the Settlement Class; and (4) an award of $6.875 million in attorneys' fees and expenses to Plaintiff's counsel.

At the settlement hearing held on November 23, 2015 (the "November 23 Hearing"), the Court asked Co-Lead Counsel to submit supplemental briefing explaining (1) the rationale for the Class Period;[1] (2) why some Class members are entitled to compensation under the Plan of Allocation while others are not;[2] (3) why the Plan of Allocation is a reasonable method of compensating Class members for the value of their claims;[3] (4) why the direct claims at issue in this Settlement do not "travel with" the securities;[4] (5) why Lead Plaintiff agreed to a

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[1] In re Kinder Morgan Energy Partners Capex Litigation, C.A. No. 9318-VCL (Del. Ch. Nov. 23, 2015) Settlement Tr. ("Transcript") at *42-43.

[2] *Id.*

[3] *Id.* at *43.

release that includes federal securities claims;[5] and (6) further details of Co-Lead Counsel's litigation efforts and the hours expended on this Action.[6]

DISCUSSION

I. THE CLASS PERIOD IS REASONABLE AND APPROPRIATE

The proposed Class Period begins February 5, 2011, and ends November 26, 2014. This is the period during which Defendants' alleged misconduct gave rise to legally cognizable claims. Lead Plaintiff filed his Complaint on February 5, 2014, stating claims arising from Defendants' alleged breach of the Partnership Agreement due to a failure to correctly allocate capital expenses ("capex") as between "Maintenance" and "Expansion" or "Growth" expenditures. The failure properly to allocate capex created two distinct harms affecting KMP's unitholders: (1) a destabilizing of the entity itself that created a risk of significant devaluation in the event KMP would not be able to continue to grow distributions—which claim was akin to a traditional derivative claim for mismanagement; and (2) the shortchanging of individual unitholders who received less distributed cash than they would have but for the misallocations—which claim is a traditional direct claim for personal investor harm.

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[4] *Id.* at *43-44.

[5] *Id.* at *44.

[6] *Id.* at *44-45.

Given the three-year statute of limitations for contractual claims found in 10 Del. C. § 8106, the earliest breaches of the Partnership Agreement that Lead Plaintiff could assert began on February 5, 2011. Despite potential wrongful misallocation of capex prior to that date, the statute of limitations cuts off those claims. *See, e.g.*, *Desimone v Barrows*, 924 A.2d 908, 924 n.39 (Del. Ch. 2007) ("a plaintiff can only challenge those transactions, or other wrongful acts, that occurred within the limitations period"); *Bean v. Fursa Capital Partners, LP*, 2013 WL 755792, at *5 (Del. Ch. Feb. 28, 2013) ("When a plaintiff challenges a discrete set of individual transactions, 'the statute of limitations for each discrete wrongful transaction begins to run upon the occurrence of each transaction.'").

The Class Period ends on November 26, 2014, with the Consolidation of KMP into KMI. As there were no public unitholders of KMP after that point, and no further distributions, there could be no further breach of contract claims.

II. THE PLAN OF ALLOCATION REASONABLY COMPENSATES ONLY THOSE CLASS MEMBERS WHOSE DISTRIBUTIONS WERE REDUCED DUE TO MISALLOCATION

At the November 23 Hearing, there was confusion regarding Lead Plaintiff's theory of the case. Although Lead Plaintiff originally alleged that Defendants harmed KMP by improperly paying out too much partnership cash as distributions, discovery and discussions with Lead Plaintiff's experts led Lead Plaintiff to adopt a different theory. At the time of the Settlement, Lead Plaintiff recognized that it

was not that KMP's distributions were too large, but rather that Defendants' misallocation of capex allowed KMI to allocate a significant portion of KMP's distributions to favor KMI, in breach of its contractual obligations. KMI failed to characterize that portion of the distribution representing a return of capital as such, which properly would have resulted in a 99%-to-1% split favoring unitholders, rather than the 50%-to-50% split that KMP actually paid out.

Under the Partnership Agreement, any cash that KMP distributed had to be characterized as either:

- Cash from Operations, which essentially represents a distribution from earnings, and was defined as cash receipts less the sum of operating expenses plus maintenance capex; or
- Cash from Interim Capital Transactions ("Cash from ICT"), which essentially represents the return of invested capital, and was defined as cash distributed to unitholders in excess of KMP's ***cumulative*** Cash from Operations over the life of the partnership.

See Atkins Affidavit (attached to November 6, 2015 Haendler Transmittal Affidavit as Ex. E) at ¶¶ 5-6; Partnership Agreement (attached to March 24, 2014 Aronstam Transmittal Affidavit as Ex. D) § 5.3(a).

Whether KMP "deemed" distributions as Cash from Operations or Cash from ICT had important financial consequences for unitholders. The Partnership Agreement required that Cash from Operations be distributed roughly 50% to KMI and 50% to all of KMP's unitholders. *See* Atkins Affidavit at ¶¶ 5-6*;* Partnership Agreement § 5.4; *see also* Kinder Morgan Energy Partners L.P. Form 10-K Annual

Report of the Period Ending December 31, 2013 ("KMP 2013 10-K") (attached to December 10, 2015 Transmittal Affidavit of David M. Haendler ("Haendler Transmittal Affidavit") as Ex. A) at 142-43. By contrast, the Partnership Agreement required that KMP split Cash from ICT by allocating ***99%*** to unitholders ***and 1%*** to KMI. *See* Atkins Affidavit at ¶¶ 5-6; Partnership Agreement § 5.5.

Because KMI (acting as KMP's general partner) failed properly to allocate KMP's capex, KMP's Cash from Operations was overstated. Thus, during the Class Period, KMP was distributing more Cash from Operations than it was actually earning on a quarterly basis. Beginning with the 4th Quarter 2012 Distribution, each of KMP's quarterly distributions exceeded cumulative Cash from Operations. *See* Atkins Affidavit at ¶¶ 8-10.

While the alleged wrongful capex allocations occurred continuously during the three years prior to the filing of the Complaint, (*i.e.*, the Class Period) due to the mechanics of KMP's Partnership Agreement, Defendants' wrongful capex misallocations did not actually affect the amounts paid out in distributions until the fourth quarter of 2012. The reason that misallocation in the early quarters of the Class Period did not actually alter the amounts paid to investors is that at the beginning of the Class Period, Lead Plaintiff's experts determined that KMP had a

$1.1 billion "cushion" of cumulative Cash from Operations.[7] *See* Atkins Affidavit at ¶ 10. Until that cumulative sum was exhausted, KMP was not required to deem any of its distributions as Cash from ICT. *See id.* Based on information learned through discovery, publicly available information, and consultation with Lead Plaintiff's experts, Co-Lead Counsel determined that the $1.1 billion cushion was exhausted beginning in the fourth quarter of 2012, such that the Partnership Agreement required KMP to deem a portion of its actual distributions as Cash from ICT beginning in that quarter, and distribute the excess cash using the 99%-to-1% split more favorable to unitholders.

Despite misallocations of capital expenditures during the first seven quarters of the Class Period, KMP appropriately characterized the source of the entire sum it distributed as Cash from Operations, and each unitholder received the correct distributions for those quarters. On that basis, the Plan of Allocation would not provide payments to investors based upon distributions received before the fourth quarter of 2012. Beginning in the fourth quarter of 2012, however, a portion of the distributions to unitholders should have been deemed as Cash from ICT, *i.e.*,

[7] As an MLP, KMP was required to distribute 100% of its "Available Cash" every quarter. Available Cash can be thought of as Distributable Cash Flow net of changes in reserves. The reserves lowered Available Cash and over time the reserves created a cushion that allowed KMP to pay distributions in excess of DCF.

return-of-capital distributions. Through the rest of the Class Period, quarterly distributions shorted individual unitholders by amounts ranging from $0.02 to $0.16 per unit.

Paying those Class members who have compensable claims while dismissing without consideration the claims of Class members with little or no entitlement to receive a recovery is reasonable and permissible under Delaware law. *See, e.g., In re Triarc Cos., Inc.*, 791 A.2d 872, 876 (Del. Ch. 2001) ("If it appears that . . . claims are weak or of little or no probable value or would not likely result in any recovery of damages by individual stockholders, it is fair to bar those claims as part of the overall settlement."); *In re Cox Radio, Inc. S'holders Litig.*, 2010 WL 1806616, at *19 (Del. Ch. May 6, 2010) (same) (*quoting In re Philadelphia Stock Exchange, Inc.*, 945 A.2d 1123 (Del. 2008) ("*PHLX I*")).

III. THE PLAN OF ALLOCATION SATISFIES THE RANGE OF REASONABLENESS STANDARD OF REVIEW

During the November 23 Hearing, the Court also asked for a better explanation of why the Plan of Allocation falls into the "range of reasonableness," given that it compensates persons who sold their units during the Class Period. *See* Transcript at 43-44. Delaware Supreme Court precedent establishes that a Plan of Allocation may reasonably and equitably compensate class members who have sold some or all of their holdings of the securities at issue. Here, where unitholders were harmed directly and personally, the fact that they may have sold their units

after they were harmed should not preclude their receipt of a portion of the recovery.

A settlement class may "encompass[] multiple constituencies – holders, buyers, and sellers," and "even if there were no settlement and the class was being certified for litigation purposes, the inclusion of holders, buyers and sellers within the class would not defeat certification." *PHLX I*, 945 A.2d at 1141. In *PHLX I*, the Court overruled an objection to a settlement class that included sellers, noting that "[t]he Objectors are unable to identify any controlling legal authority that prohibited the Chancellor from certifying a settlement class that includes buyers, sellers, and holders." *Id*. at 1142. The Court noted that "the complaint allege[d] that all class members were injured . . . by the same events," and it was not clear that "holders, buyers, and sellers . . . will . . . be found to have conflicting claims to the settlement recovery." *Id.* at 1141. The Court later made clear that, although "[a]n allocation plan must be fair, reasonable, and adequate," "[t]he plan does not need to compensate Class members equally to be acceptable," and "[a] reasonable plan may consider the relative values of competing claims." *Schultz v. Ginsburg*, 965 A.2d 661, 667 (Del. 2009) ("*PHLX II*"). There is no genuine question, then, that sellers may equitably be compensated in a settlement.

Here, where Co-Lead Counsel worked with their experts to create a Plan of Allocation that is designed to directly compensate former KMP unitholders based

on the harm that they personally suffered as a result of Defendants' alleged improper return of capital, the proposed plan should be approved as fair, reasonable, and equitable.[8]

IV. THE DIRECT CLAIMS AT ISSUE DO NOT TRAVEL WITH THE KMP UNITS

Defendants' alleged misallocation of capital expenditures harmed certain KMP unitholders by depriving them of the 99%-to-1% split required for cash distributions exceeding quarterly "Cash from Operations" plus cumulative retained cash. Unlike a dilution claim or a derivative claim for mismanagement, which would be priced into and "travel with" the KMP securities, the contractual claims asserted in the Complaint belong personally to the short-changed unitholders.

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[8] Even if the Court does not agree that the Plan of Allocation is reasonable, the Court should still approve the Settlement, which secured $27.5 million for wronged unitholders, and either direct Lead Plaintiff to develop a different plan of allocation or devise its own plan. *See PHLX I*, 945 A.2d at 1136 ("A decision that a settlement will not include a plan of allocation is a matter of judicial discretion," "so long as the distribution scheme does not affect the obligations of the defendants under the settlement agreement"). If the Court determines to alter the Plan of Allocation, it may do so without requiring additional notice. *See* Notice (attached to November 6, 2015 Haendler Transmittal Affidavit as Ex. Q) at ¶54 ("The Court may approve this plan as proposed or it may modify the Plan of Allocation without further notice to the Class"); *see also, e.g.*, *PHLX I*, 945 A.2d at 1136; *Shingala v. Becor W. Inc.*, 1988 WL 7390, at *6 n.2 (Del. Ch. Feb. 3, 1988) (holding no further notice necessary where "[t]he notice that was sent alerted all class members that the Court might modify the class or the settlement terms without further notice").

Here, Lead Plaintiff is settling claims on behalf of investors who did not receive what they contracted to purchase – distributions that properly paid unitholders at a 99%-to-1% ratio when returning capital, as opposed to the 50%-to-50% split when distributing earnings. In contrast to a dilution claim (which was originally asserted in the Complaint, but which Co-Lead Counsel and their experts ultimately determined required assumptions about stock price movements that made it difficult to sustain a damages claim), which affects the value of the investor's ongoing stake in the corporation and therefore travels with the securities, the underpayment to unitholders here had no effect on the units' value. *See* Atkins Affidavit at ¶¶ 18-19 (explaining why Lead Plaintiff is not pursuing a dilution-based damages model). Instead, for each quarter beginning with the 4th Quarter 2012 Distribution, unitholders were directly and personally underpaid, which would recur in ensuing quarters only if Defendants again misallocated capex between maintenance and expansion in violation of the Partnership Agreement.

When unitholders purchased or sold their units, they did not purchase or sell any "deficit." Rather, the harm occurred to whomever held the unit at the time of the distribution and therefore did not receive the 99%-to-1% distribution that the Partnership Agreement specified.

Based on this Court's ruling in *Allen v. El Paso Pipeline GP Co., L.L.C.*, 90 A.3d 1097 (Del. Ch. 2014), Co-Lead Counsel believe that Delaware law supports a

Plan of Allocation that reasonably seeks to compensate unitholders for the direct harm they suffered from the contractual breaches alleged by Lead Plaintiff, whether or not they held shares as of the Consolidation. *See id*. at 1110 (holding that limited partners' claims that defendants breached their MLP partnership agreement were direct and "support[ed] awarding relief to the class of innocent unitholders"). Co-Lead Counsel's objective in structuring the Plan of Allocation was to provide a recovery to unitholders who actually received a lower quarterly distribution than they would have had the required portions of KMP's distributions been classified as Cash from ICT.

The nature of harm to KMP's unitholders means that Lead Plaintiff's claims – which the Plan of Allocation is designed to address – are personal in nature, rather than claims that travel with the securities. This Court recently discussed when investors' claims travel with securities, and when those claims are personal (such that recovery to Class Period sellers is appropriate). *See In re ActivisionBlizzard, Inc. Stockholder Litig.*, 2015 WL 2438067 (Del. Ch. May 20, 2015). The Court discussed derivative, direct, and "dual-attribute" stockholder claims concerning the defendant's improper payments to insiders, dilution, and voting rights, and correctly recognized that none of those claims was personal because each was incorporated into the share price. *Id*. at *14-24. However, the Court also recognized that its discussion of the particular claims at issue in

Activision "does not mean that an individual holder of shares cannot have personal claims," just that "[t]here simply were not any advanced or litigated in this case." *Id*. at *24. The Court stated that personal stockholder claims arise when "the nature of the underlying property does not matter," although "[t]he property happens to be shares." *Id*. at *25.

Because KMP mischaracterized the basis for distributing partnership cash, and thereby failed to pay the portion that should have been attributed to Cash from ICT, this case is analogous to a company declaring a dividend but not paying the amount promised. Courts have recognized that claims to recover declared dividends are personal and do not travel with the security. *See In re Sunstates Corp. S'holder Litig*, 2001 WL 432447, at *3 (Del. Ch. Apr. 18, 2001) ("the declaration of a lawful dividend has long been understood to give stockholders as of the record date standing as creditors to sue at law for the recovery of the amount due . . . the right to receive payment of a lawfully declared dividend is a separate property right of the record stockholders"); *see also Martindell v. Fiduciary Counsel*, 30 A.2d 281, 285 (N.J. 1943) ("Upon declaration, the dividend becomes instanter the property of the shareholder, although payable in the future. It is separate and distinct from the stock, and does not pass as an incident of the shares if sold before the payment of the dividend.").

Cases where the Delaware courts have held that claims travel with securities, and are not personal in nature – and about which the Court inquired during the fairness hearing (Transcript at 8) – involve claims that squarely implicate the securities' value (for instance, derivative claims or claims for equitable relief). For example, in *Triarc*, where "the only available relief [wa]s either equitable or directed to the benefit of the corporation," and the harm affected the share price and the company's value, "persons who sever[ed] their economic relationship with the corporation . . . w[ould] not benefit from a settlement or a judgment in favor of the class." *In re Triarc*, 791 A.2d at 879.

Similarly, in both *Prodigy* and this Court's recent *El Paso* decision, the Court determined that claims related to the fairness of strategic transactions travel with securities because they harm investors only by virtue of altering the value of the securities those investors hold. *See In re El Paso Pipeline Partners, L.P. Derivative Litig.*, C.A. No. 7141-VCL (Del. Ch. Dec. 2, 2015) (Slip Op.), at 105-109; *In re Prodigy Commc'ns Corp. S'holders Litig.*, 2002 WL 1767543, at *4 (Del. Ch. July 26, 2002) (objector made "a conscious business decision to sell [his] shares into a market that implicitly reflect[ed] the value of the pending and any prospective lawsuits") (quotation marks omitted). Because the KMP unit price did not meaningfully incorporate the value of any prior underdistribution, the harm

suffered was both direct and personal – affecting sellers as well as holders – and the recovery should, as an economic and legal matter, go directly to unitholders.

At the November 23 Hearing, the Court raised the issue of whether this three-year proposed Class Period is appropriate in light of this Court's holding in *Activision* that direct claims travel with the shares. As described above, Lead Plaintiff believes that this is a very different circumstance than *Activision* and thus KMP unitholders who sold before the merger date have standing to assert a claim that the distribution paid at any point during the three year period was insufficient. But even if the Court disagrees, Lead Plaintiff respectfully submits that the Class, and the corresponding releases granted Defendants, should not be limited only to those unitholders who sold in the November 2014 Consolidation. Defendants insisted throughout the negotiations that the class period include all persons who held at any point during the proposed Class Period, and have indicated that they are not willing to pay the settlement consideration if they continue to face the risk of — and exposure to — potential claims arising out of the same capex allocations in another jurisdiction that might not follow this Court's decision in *Activision*. The parties' resolution of this issue, which provides Defendants with the certainty they seek in return for the substantial consideration the Class is receiving, is entirely reasonable, was reached through good faith bargaining and accordingly should be approved. *See PHLX I*, 945 A.2d at 1140

("To exclude from the class any persons who contend that they have rights in the claims being settled, would create the risk that those persons would be free to sue in another forum—a risk that the Appellees are unwilling to take."); *In re Activision*, 2015 WL 2438067, at *32 (citing *PHLX I*, 945 A.2d at 1136) ("when evaluating a settlement, a trial court can determine initially whether the settlement consideration as a whole provides adequate consideration for a global release").

V. THE RELEASE OF FEDERAL SECURITIES CLAIMS IS PROPER UNDER DELAWARE LAW, AND AS APPLIED IN THIS CASE

Delaware law permits the release of related federal securities claims, even in non-opt out litigation such as the instant case. Co-Lead Counsel made an informed and appropriate judgment that the release of securities claims in this case is not a significant sacrifice. Indeed, no potential Class member has objected to the scope of the release, and no such claims are pending or are even apparently viable.

A. Delaware Law Permits The Release Of Federal Securities Claims In A Non-Opt-Out Class Action

This Court has the power to release federal securities claims. *See In re Countrywide Corp. S'holders Litig.*, 2009 WL 2595739, at *5 (Del. Ch. Aug. 24, 2009). In *Countrywide*, this Court concluded that "[b]oth the United States Supreme Court and the Delaware Supreme Court have recognized the validity of executing a general release that encompasses federal claims in the settlement of a

state law class action." *Id.* (*citing In re MCA, Inc.*, 598 A.2d 687, 691 (Del. Ch. 1991)); *Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367, 381 (1996).[9]

Here, where the federal claims lack merit (as explained below) and no investor has pursued them despite ample notice of the opportunity to do so, such claims may be released. *Id.* at *4 ("Because [defendant]'s potential federal securities law claims possess no obvious value, surrendering them in the context of this settlement for only therapeutic disclosures is neither unfair nor unreasonable"); *see also In re Cox Radio*, 2010 WL 1806616 (allowing release of pending federal claims that lacked merit).

B. The Facts Alleged In The Complaint Do Not Support Federal Securities Claims

The Complaint sets forth claims of breach of contract, breach of the duty of good faith and fair dealing, aiding and abetting such breaches, and tortious interference in connection with KMI's (as KMP's general partner) misallocations of KMP's capex between maintenance and growth. Complaint ¶¶ 102-120. Lead Plaintiff did not assert any disclosure-related claims, because it believed (and

[9] In *Matsushita*, the U.S. Supreme Court addressed the release of exclusively federal claims by the Delaware Court of Chancery and held that: "[w]hile § 27 prohibits state courts from adjudicating claims arising under the Exchange Act, it does not prohibit state courts from approving the release of Exchange Act claims in the settlement of suits over which they have properly exercised jurisdiction." *Id.* at 381.

discovery and expert analysis have further confirmed) that no such claim is feasible. Indeed, despite significant public coverage of both the present case and the underlying issues, no plaintiff in any forum has ever proposed raising any disclosure-based claims, and no objectors expressed any concern regarding releasing their potential federal securities law claims.

This is not surprising, since the facts do not support a federal securities claim. Such a claim would require proof of, *inter alia*, economic loss and loss causation, *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 341-42 (2005), which are not present here. *First*, a federal securities claim would require, among other things, proof of a material misrepresentation or omission. Here, however, KMP's and KMI's public statements contain no apparent misrepresentations concerning the capex-related conduct alleged by Lead Plaintiff. Rather, KMP and KMI appear to have accurately described the Company's practices. For example, KMP's 2013 Annual Report (the last before the Consolidation) disclosed that all allocations were "made on a project level," and KMP did not allocate capex within specific projects (as Lead Plaintiff alleged the general partner was contractually required to do). KMP 2013 10-K at 74.

Second, in *Dura*, the United States Supreme Court determined that to recover under the federal securities laws, a plaintiff must prove a stock-price decline resulting from the revelation of truthful information that corrected a prior

misrepresentation. *Dura*, 544 U.S. at 347; *see also, e.g.*, *Glaser v. Enzo Biochem, Inc.*, 464 F.3d 474, 477 (4th Cir. 2006) ("*Dura* requires plaintiffs to plead loss causation by alleging that the stock price fell after the truth of a misrepresentation about the stocks was revealed"); *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 175 (2d Cir. 2005). The mere existence of inflation in a stock caused by a misrepresentation – without a subsequent decline related to corrective information reaching the market – is insufficient. *Dura*, 544 U.S. at 347 ("The complaint's failure to claim that Dura's share price fell significantly after the truth became known suggests that the plaintiffs considered the allegation of purchase price inflation alone sufficient. . . . [H]owever, the 'artificially inflated purchase price' is not itself a relevant economic loss.").

Co-Lead Counsel identified only two even arguable corrective disclosures of KMP's improper capex misallocations – the Hedgeye Report on September 10, 2013, and the filing of Lead Plaintiff's Complaint in this matter on February 5, 2014. Neither date appears to support a corrective disclosure. On September 10, 2013, the date the Hedgeye Report was released, KMP unit prices opened at $80.64 per unit and closed ***higher***, at $81.32 per unit. Similarly, On February 5, 2014, KMP's unit price opened at $78.60, and closed ***higher***, at $78.95. Absent any apparent evidence of loss causation tied to the price of KMP units, a securities fraud claim would fail.

Finally, the federal securities laws provide that in any private securities fraud action, the award of damages shall not exceed the difference between the price paid by the plaintiff, and the mean trading price of the security during the 90-day period beginning on the date when corrective information was disclosed to the marketplace. *See* 15 U.S.C. § 78u-4(e). In other words, if the mean trading price of a security during the 90-day period following the corrective disclosure is greater than the price at which the plaintiff purchased his stock, then the plaintiff cannot recover damages. *See Acticon AG v. China North East Petroleum Holdings Ltd.*, 692 F.3d 34, 39 (2d Cir. 2012). The times that KMP's stock price traded below its 90-day look-back period during the Class Period were limited. *See* Haendler Transmittal Affidavit Ex. B. Therefore, it would be extremely difficult to bring a viable claim that Class members had suffered damages under the federal securities laws.

Defendants nevertheless negotiated to include the federal securities claims in the release on the grounds that, in return for the substantial consideration they are paying, they are entitled to "global peace" with respect to any potential claims arising out of the capex allocations that Lead Plaintiff is challenging. It bears emphasis that the release here does not bar all securities claims that could be asserted against the Defendants for any alleged misstatements during the class period. Rather, the Release is narrowly tailored to the issues in this action: the

payment of distributions and the allocation of capital expenses. *See* Stipulation of Settlement (attached to November 6, 2015 Haendler Transmittal Affidavit as Ex. A) ¶ 1(ll) (definition of "Released Plaintiff Claims"). Including the federal securities claims in the release, which resulted from good faith bargaining among experienced counsel, is entirely reasonable and should be approved. *See Activision*, 2015 WL 2438067, at *14 (approving a settlement that released theoretical causes of action including federal securities claims because "a settlement can release claims of negligible value to achieve a settlement that provides reasonable consideration for meaningful claims") (citing *PHLX I*, 945 A.2d at 1140), as revised (May 21, 2015); *In re Triarc*, 791 A.2d at 876 ("If it appears that those claims are weak or of little or no probable value or would not likely result in any recovery of damages by individual stockholders, it is fair to bar those claims as part of the overall settlement.").

VI. CO-LEAD COUNSEL'S EFFORTS WERE REASONABLE AND NECESSARY IN LITIGATING THE ACTION AND OBTAINING THE SETTLEMENT

Consistent with Delaware law, Co-Lead Counsel request a fee consisting of a percentage of the recovery in this matter. Co-Lead Counsel respectfully request attorneys' fees in the amount of 25% of the $27,500,000 recovery, totaling $6,875,000. Notably, unlike what was set forth in Co-Lead Counsel's initial fee request, this figure includes the nearly half-million dollars in expenses incurred by

Co-Lead Counsel in prosecuting this litigation. Co-Lead Counsel initially proposed that expenses should be paid separately in this case because of their extraordinary nature. While normal case prosecution expenses are typically paid for out of any fee award, Co-Lead Counsel believed that when a case is especially expensive to prosecute, particularly when the expense relates to necessary experts, taxing those expenses out of counsel's fee award creates a disincentive to expending the sums needed to effectively prosecute the matter. Nevertheless, based on the Court's comments at the November 23 Hearing, Co-Lead Counsel do not seek an award of expenses separate from their fee request.

Once including the approximately $450,000 in expenses that Co-Lead Counsel incurred, Co-Lead Counsel's fee request, modified from Co-Lead Counsel's initial request for attorneys' fees, represents slightly over 23% of the total recovery. That amount is independent of the number of hours worked on the case by Co-Lead Counsel, because Co-Lead Counsel request only a percentage of the total recovery. As attorneys who regularly litigate on a contingency basis in the Delaware courts, Co-Lead Counsel were keenly aware that any attorneys' fees would be awarded under Delaware law based on benefits to the Class rather than in relation to counsel's lodestar. However, Co-Lead Counsel also understood that they must invest sufficient time and resources to prosecute this highly complex

matter to a successful resolution. Thus, it was not in Co-Lead Counsel's economic interest to expend more hours than was necessary to achieve a successful result.

A. The Document Review Was More Complex Than The Typical Case

Investigating and litigating the Action required understanding and analyzing complicated accounting issues concerning KMP's capital allocations. In contrast to a typical litigation challenging, for example, the fairness of a proposed merger – which may involve documents concerning a limited number of discrete topics presented to a limited number of custodians over a limited time frame – the prosecution of the claims asserted in this action required a labor-intensive, project-by-project analysis of thousands of the Partnership's capital projects. Specifically, Defendants produced highly technical documents in connection with tens of thousands of projects; even after Co-Lead Counsel decided to focus only on projects exceeding $1 million, there were more than 1,700 projects to review and analyze.

After Lead Plaintiff filed his Complaint, Co-Lead Counsel continued their investigation of misconduct at KMI and KMP, including the misallocation of capital expenditures and the implications of misallocated capex for KMP's operations and distributions. Co-Lead Counsel accordingly reviewed and analyzed publicly available documents setting forth and discussing numerous key financial

metrics, as well as KMI's and KMP's corporate documents and public filings, and writings by securities analysts and other public commentators.

On June 11, 2014, Defendants began their production of documents. Along with numerous subsequent productions, Defendants produced documents including among other things spreadsheets, Authorization for Expenditure ("AFE") forms, supporting documentation describing key aspects of KMP's capital projects, e-mail traffic and organizational documents.

It quickly became apparent that both the volume and technical nature of Defendants' production required dedicated staff who could focus exclusively on understanding the complex operational and accounting issues at the core of this Action, including identifying issues for further discussion with Lead Plaintiff's retained experts and aggregating and analyzing data. In addition, because Defendants did not produce project-related documents together, and instead produced AFEs and the various related documents for each project across several productions, gathering the necessary and appropriate documents for each project was unusually cumbersome.

In order to prove that KMP inappropriately characterized capex in violation of the Partnership Agreement and on a systemic basis, Co-Lead Counsel had to engage in an in-depth analysis of KMP's numerous expansion projects. Given the enormous size of KMP's infrastructure (during the Class Period, KMP owned an

interest in or operated approximately 52,000 miles of pipelines and 180 terminals) and the fact that its capital expenditures were split between thousands of diverse and complex projects on a project-by-project basis, developing a factual record that KMP had misallocated maintenance capex as expansion capex was an unavoidably time- and labor-intensive exercise.

In conjunction with their experts, Co-Lead Counsel decided that the most effective way to analyze and understand whether KMP properly characterized its putative "expansion" projects was to focus on AFEs. For every capital project that KMP engaged in, KMP personnel generated an AFE containing, amongst other things, a description of the project, the project's anticipated cost, and whether the cost was to be treated as expansion or maintenance capex. Defendants produced tens of thousands of AFEs, covering diverse projects ranging in cost from less than $10,000 to more than $1.6 billion. For every single AFE, Co-Lead Counsel had to understand and evaluate the nature of the project, which entailed outside research and consultation with experts to interpret shorthand engineering terminology, the context for the project, and the impact of the project on KMP's financial statements.

An example of an AFE that Co-Lead Counsel considered to be significant and potentially subject to challenge is attached hereto. *See* Line Reversal AFE, attached to Haendler Transmittal Affidavit as Ex. C. This particular project (the

"Line Reversal") entailed, among other things, the reversal of a particular pipeline system's flow direction at an estimated cost of hundreds of millions. As demonstrated by the "E" in the "Project Type" box, this project was booked as expansion capital. *See id.* Lead Plaintiff did not believe that money spent reversing the direction of an existing pipeline's flow constituted expansion capex under the definitions set forth in the Partnership Agreement.

Review of the AFEs was enormously complicated by the fact that the AFEs did not provide clear indications as to whether they were draft or final documents. Thus, for every AFE reviewed, it was necessary to follow up with keyword searches to confirm that it was the final document and not a draft or duplicate. In addition, when AFEs were identified, such as the AFE for the Line Reversal project discussed above, that reflected potential misallocation of expansion capital, follow-up keyword searches for additional supporting information were conducted, including to determine: (i) whether a request was part of a larger project; (ii) what line of business was responsible; (iii) which Kinder Morgan subsidiary was responsible; and (iv) whether any of the people named on the request had any additional information about the AFE in the custodial documents that were produced. In many instances, the name of the project discussed in an AFE was so general that numerous results had to be reviewed and analyzed to determine whether they were related.

While the amount of supporting documentation for an AFE varied on a project-by-project basis, supporting materials included summaries, initial estimates of project costs, spreadsheets describing the economics of projects, spreadsheets describing how projects fit into regional-division or business-line budgets, emails, and presentations.[10] In light of these considerations, documents would often have to be reviewed several times to determine whether they did (or did not) belong to a specific AFE that was being evaluated. For selected projects, Co-Lead Counsel also did extensive research of materials in the public domain, including internet, news, and regulatory searches to further investigate the true nature of the capex projects.

Given the high number of projects, Lead Plaintiff suggested to Defendants that a statistical sampling would allow both the parties and the Court to better understand and evaluate whether Defendants breached the Partnership Agreement

[10] Further complicating matters, documents regarding a particular project may have been split between several productions and separated by thousands of Bates numbers. For example, in the case of the Line Reversal project, the supporting documents included an AFE summary and estimate with additional narration included in Defendants' fifth production (attached to Haendler Transmittal Affidavit as Exs. D and E); a spreadsheet laying out the economics of the project included in Defendants' fifth production (attached to Haendler Transmittal Affidavit as Ex. F); two sets of board minutes and a board presentation referencing the project included in Defendants' sixth production (attached to Haendler Transmittal Affidavit as Exs. G, H, and I); and spreadsheets referencing the pipeline in question included in Defendants' thirteenth, twenty-first and twenty-ninth productions (attached to Haendler Transmittal Affidavit as Exs. J, K and L).

in connection with KMP's Class Period capex allocations. Defendants, however, would not agree that statistical sampling would be useful or even acceptable to evaluate whether misallocation had occurred, or to determine the amount of any misallocated capital. As a result, Co-Lead Counsel had little choice but to review each and every AFE of a material amount, along with the supporting materials produced. Co-Lead Counsel decided to focus only on projects exceeding $1 million, which still left more than 1,700 projects to review and analyze.

At the time counsel agreed to the Settlement, Co-Lead Counsel had reviewed more than 246,000 pages of documents, following Defendants' production of 44 rolling batches of documents. The review included over 24,000 native spreadsheet documents (the analysis of which, as discussed above, was at the heart of this litigation), which – although listed as single page documents – each include between one and fifteen worksheets, which in turn held as much as ***hundreds*** of pages of raw data.[11]

[11] Additionally, as Co-Lead Counsel began reviewing these spreadsheets/workbooks, it quickly became apparent that there were often hidden tabs with additional information that bore on the relevancy of the documents, which required extra measures to extract and check.

B. The Staff Attorneys Assigned To The Case Performed Many Of The Tasks Essential To Prosecuting Lead Plaintiff's Claims

During the November 23 Hearing, the Court asked Co-Lead Counsel about the role that staff attorneys played in this litigation. See Transcript at 50. The significant majority of the document review and cross-referencing work described above was conducted by staff attorneys at both BLB&G and G&E.[12] A staff attorney is a full-time employee, who is a non-partner track attorney, doing junior associate work, but oftentimes has substantially more experience than a junior associate.[13] The staff attorneys were at the center of the extensive, multi-component AFE-review process. The staff attorneys were also responsible for first-level review of the other discovery materials produced by Defendants, including board presentations and e-mails.[14]

For example, BLB&G staff attorney Brian McGrath reviewed and analyzed Defendants' document production, and otherwise researched and helped develop

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[12] Staff attorneys at Robbins Arroyo LLP also participated in document review at the direction of Co-Lead Counsel.

[13] The rates charged for staff attorneys are comparable to those charged for junior associates.

[14] Additionally, because Defendants did not produce any organizational charts, the staff attorneys were charged with creating and maintaining a developing list of key players and potential witnesses, including individuals throughout Kinder Morgan's hierarchy and across the Company's several business lines. This ongoing task enabled counsel to understand certain employees' involvement and to make determinations about what depositions might be needed.

Lead Plaintiff's case. Mr. McGrath worked exclusively on this case from mid-June 2014 until mid-June 2015. BLB&G staff attorneys David Carlet and Robert Stinson worked alongside Mr. McGrath. Mr. Carlet worked full-time on the case between mid-August and late-September 2014, and again between mid-January and mid-June 2015. Mr. Stinson worked full-time on the case from mid-August to mid-November 2014, and again from mid-January to late-May 2015.

Messrs. McGrath, Carlet, and Stinson spent significant time reviewing and analyzing the AFEs for KMP's 1,700 capital projects over $1 million. The staff attorneys were tasked with recreating, based on project-level technical documents, the process and basis for capex allocation decisions by KMI and KMP. Staff attorneys at G&E performed similar roles.

Staff attorneys at G&E and BLBG also assisted in the preparation of deposition outlines and exhibit selection. As discussed in §VI.D, *infra*, Co-Lead Counsel had taken five depositions and substantially prepared for six more at the time the Settlement was reached.

C. Co-Lead Counsel Spent Significant Time Working With Their Experts to Develop A Damages Model

In addition to working with their experts to prove that systematic misallocations had occurred, Co-Lead Counsel also required expert assistance in developing a damages model that would quantify how those misallocations translated into individual damages. Co-Lead Counsel worked closely with their

experts to develop a damages model that would fairly and adequately quantify the direct harm that Defendants' capex misallocations caused both on a Class-wide basis, and to individual Class Members. Through frequent conference calls to discuss the relative strengths and weaknesses of different damages models, and work to constantly refine the various models, Co-Lead Counsel was ultimately able to develop a strong damage theory.

D. Co-Lead Counsel Performed Numerous Additional Tasks In Prosecuting This Case

In addition to researching and analyzing KMP's numerous projects and formulating an appropriate and defensible damages model, Co-Lead Counsel conducted significant additional work. Among other things, Co-Lead Counsel took the Rule 30(b)(6) deposition of KMI's Chief Financial Officer, Kimberly Dang, as well as depositions of Jesse Arenivas (President – Kinder Morgan CO2), Lanny Schoeling (Vice President – Kinder Morgan CO2), James Douglas McMurrey (Vice President – Kinder Morgan CO2), and Darrell Ricketson (Chief Operating Officer – Kinder Morgan CO2). In total, Co-Lead Counsel noticed thirty depositions to be completed by August 10, 2015, and had already scheduled and substantially prepared for six of those depositions at the time a preliminary settlement was reached on June 15, 2015. Additionally, at the time that the parties reached the Settlement, Co-Lead Counsel had researched and drafted a motion for

class certification (due June 22, 2015), and a motion for partial summary judgment as to liability, which they planned on filing imminently.

Co-Lead Counsel also propounded a set of interrogatories and six requests for production of documents on Defendants, drafted papers opposing a motion to dismiss (which was fully briefed but pulled on the eve of oral argument, after Co-Lead Counsel had already prepared for said argument), researched the applicable law to formulate litigation and negotiation strategies, negotiated the terms of the Settlement, and prepared the Settlement documents.

Finally, even if the number of hours worked by Co-Lead Counsel on this case were cut in half, the requested fee, which is based solely on a percentage of the recovery, would still be appropriate. While the Court may believe that Co-Lead Counsel put in more hours than was necessary, this is Co-Lead Counsel's cost to bear. Had Co-Lead Counsel been as efficient as the Court feels they could have been, this case might have cost Co-Lead Counsel less, but the same fee would be requested.

The Delaware Supreme Court has "expressly rejected the use of time expended as the principal basis for determining fees awarded to plaintiff's counsel. Instead, [it] held that the benefit achieved by the litigation is the common yardstick by which a plaintiff's counsel is compensated" in a successful representative action. *Americas Mining Corp. v. Theriault*, 51 A.3d 1213, 1257-58 (Del. 2012)

(quotation omitted). As set forth in Lead Plaintiff's opening brief, the "lodestar" value of the time Co-Lead Counsel expended on this matter is $6,024,793, such that the fee requested represents only approximately 1.14 times the lodestar, or $495 per hour. Even if Co-Lead Counsel had spent half as much time on this matter, the requested fee on an hourly basis would still be well within the ranges that this Court has approved as reasonable. *See* Op. Br. at 38-39 (listing cases).

CONCLUSION

For the foregoing reasons, and as discussed in Lead Plaintiff's opening brief and supporting papers, the proposed Settlement is fair, reasonable, and adequate and should be approved. In addition, Co-Lead Counsel's request for a Fee and Expense Award of $6,875,000 (which includes expenses of $456,468) should be granted.

Dated: December 10, 2015

Respectfully submitted,

GRANT & EISENHOFER P.A.

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IN THE COURT OF CHANCERY IN THE STATE OF DELAWARE

IN RE KINDER MORGAN ENERGY PARTNERS, L.P. CAPEX LITIGATION	)))	CONSOLIDATED CASE No. 9318-VCL

CERTIFICATE OF COMPLIANCE WITH
TYPEFACE REQUIREMENT AND TYPE-VOLUME LIMITATION

1. This brief complies with the typeface requirement of Ct. Ch. R. 171(d)(4) because it has been prepared in Times New Roman 14-point typeface using Microsoft Word 2010.

2. This brief complies with the type-volume limitation of Ct. Ch. R. 171(f)(1) because it contains 7,324 words, which were counted by Microsoft Word 2010.

Date: December 10, 2015

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CERTIFICATE OF SERVICE

I hereby certify that, on December 10, 2015, I caused the foregoing *Lead Plaintiff's Supplemental Brief in Support of Motion for Final Approval of the Proposed Settlement, Certification of the Class, and An Award of Attorneys' Fees* and supporting *Transmittal Affidavit of David M. Haendler* to be electronically filed and served through File & Serve Xpress on the counsel listed below:

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