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IN THE SUPREME COURT OF THE STATE OF DELAWARE

THOMAS SANDYS, Derivatively on Behalf of ZYNGA INC., Plaintiff below, Appellant, v. MARK J. PINCUS, REGINALD D. DAVIS, CADIR B. LEE, JOHN SCHAPPERT, DAVID M. WEHNER, MARK VRANESH, WILLIAM GORDON, REID HOFFMAN, JEFFREY KATZENBERG, STANLEY J. MERESMAN, SUNIL PAUL and OWEN VAN NATTA, Defendants below, Appellees. -and- ZYNGA INC., a Delaware Corporation, Nominal Defendant below, Appellee.	No. 157, 2016 Court Below: Court of Chancery of the State of Delaware, No. 9512-CB PUBLIC VERSION - Filed: June 28, 2016

OUTSIDE DIRECTORS' ANSWERING BRIEF

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NATURE OF PROCEEDINGS

This is an appeal from the Court of Chancery's dismissal of plaintiff/appellant Thomas Sandys' ("Plaintiff") Verified Shareholder Derivative Complaint (the "Complaint") for failure to comply with the demand requirements of Court of Chancery Rule 23.1. The ruling of the Court of Chancery should be affirmed on the grounds that demand was not futile. As the Court of Chancery properly found, a majority of the Board was composed of independent directors that did not face a substantial likelihood of liability for breach of fiduciary duty. The Outside Directors join the brief filed by Zynga and the Management Defendants.[1]

If, for any reason, the Court were to find that a majority of the demand board lacked independence or faced a substantial risk of liability, the Complaint should nonetheless be dismissed as to the Outside Directors for failure to state a claim. Significantly, an overarching defect pervades each of the counts in the Complaint as to the Outside Directors, as there are no facts pleaded that they were in possession of material non-public information when they approved the Secondary

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[1] The "Management Defendants" consist of Mark Pincus, Reginal Davis, Cadir Lee, John Schappert, David Wehner, Mark Vranesh, and Owen Van Natta.

Offering or when the offering occurred. Plaintiff's conclusory assertions regarding purported possession of material non-public information by the "Defendants" as an undifferentiated group cannot support his *Brophy* claim against Mr. Hoffman, his Secondary Offering claim against all of the Outside Directors, or any finding that the Outside Directors acted in bad faith. Accordingly, even if the Court does not affirm the decision below on demand futility grounds, it should nonetheless affirm the dismissal of the Complaint as to the Outside Directors for failure to state a claim.

SUMMARY OF ARGUMENT

1. Denied. The Court of Chancery properly concluded that it did not need to reach the merits of the insider trading claim because demand was not excused under Court of Chancery Rule 23.1. But, in the event that the Court finds that demand was futile, it should nonetheless affirm the dismissal of Count I of the Complaint as to Mr. Hoffman because Plaintiff failed to adequately allege a *Brophy* claim against him.

2. Denied. In the context of deciding that demand was not excused under Court of Chancery Rule 23.1, the Court of Chancery correctly found that Plaintiff failed to plead a non-exculpated claim against Messrs. Gordon, Katzenberg, Meresman, and Paul in connection with their approval of the Secondary Offering. In the event that the Court does not affirm the Court of Chancery's decision with respect to demand futility, it should nonetheless affirm the dismissal of Count II for the reasons stated by the Court of Chancery—namely, Plaintiff's failure to plead any facts that these individuals consciously disregarded their directorial duties in approving the Secondary Offering. Likewise, though not raised on appeal, the Court should also affirm the dismissal of Count III—which alleges that the Outside Directors breached their fiduciary duties under *Caremark* by allowing the dissemination of statements containing material omissions—on

the alternative ground that the Complaint fails to state a claim as to the Outside Directors.

3. Denied. The Court of Chancery properly concluded that a majority of the Board was sufficiently independent and disinterested such that it could impartially consider a demand at the time the Complaint was filed. The Outside Directors join in the arguments raised by the Answering Brief submitted by the Company and the Management Defendants, making clear that the Court of Chancery was correct that Plaintiff failed to adequately allege demand futility.

STATEMENT OF FACTS AS TO THE OUTSIDE DIRECTORS[2]

A. The Outside Directors

The five distinguished "Outside Directors" on Zynga's board at the time of the Secondary Offering were William Gordon, Reid Hoffman, Jeffrey Katzenberg, Stanley J. Meresman and Sunil Paul.[3]

- Mr. Gordon has been a director on Zynga's Board of Directors (the "Board") since July 2008. ¶ 17 (A020).[4] Mr. Gordon is also a partner at Kleiner Perkins Caufield & Byers ("Kleiner Perkins") and co-founder of Electronic Arts, Inc. B348.

- Mr. Hoffman was a director on the Board since January 2008. ¶ 18 (A020). Mr. Hoffman co-founded, and has served as CEO and is Executive Chairman of, LinkedIn Corporation, was Executive Vice President of PayPal, Inc. and is a partner at Greylock Partners. B349.

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[2] The Outside Directors have not repeated the statement of the facts as set forth in Zynga's answering brief in this case. The facts recited herein are taken from the allegations in the Verified Shareholder Derivative Complaint filed in this Action (the "Complaint"), without conceding their accuracy or Plaintiff's ability to prove them, and the documents which the Complaint incorporates, including the Secondary Offering Prospectus, which appears in the record at B125-60 and B344-49 (the "Prospectus").

[3] The Outside Directors, together with Mark Pincus, John Schappert, and Owen Van Natta, comprised the Board at the time of the Secondary Offering. At the time that the Complaint was filed, the Board consisted of Messrs. Pincus, Hoffman, Gordon, Katzenberg, Meresman, and Paul, and additional members John Doerr, Ellen Siminoff, and Don Mattrick.

[4] Paragraph ("¶") references are to the Complaint, which appears in the record at A012-80.

- Mr. Katzenberg became a director of Zynga in February 2011. ¶ 19 (A020). He is the CEO and a director of DreamWorks Animation SKG Inc. B349.

- Mr. Meresman has served as a director of Zynga since June 2011. ¶ 20 (A021). Mr. Meresman has been serving as a director of multiple public and private companies for many years, and previously served as CFO of Cypress Semiconductor and Silicon Graphics. B349.

- Mr. Paul has served as director of Zynga since November 2011. ¶ 21 (A021). Mr. Paul is a partner at Spring Ventures and the CEO of SideCar Technologies, Inc. (formerly known as Shepherd Intelligent Systems, Inc.). B349[5]

B. The Complaint and the Appeal

On April 4, 2014, after having received hundreds of documents pursuant to an 8 *Del. C.* § 220 demand for books and records, Plaintiff filed the instant Complaint. Plaintiff alleged derivative claims of insider trading and breach of fiduciary duty by the Company's directors and certain executives in connection with the Board's approval of, and certain directors' and executives' participation in, a secondary offering (the "Secondary Offering"). In essence, Plaintiff alleges that both when they approved the Secondary Offering and at the time it occurred, these directors and executives were in possession of material, non-public

[5] At the time of this submission, Messrs. Hoffman, Katzenberg, and Meresman are no longer members of the Zynga Board, having declined to seek reelection.

information regarding: Zynga's projections for future bookings, negative trends in Zynga's Average Bookings Per User ("ABPU"), delays in launching a new game, and a change to the Facebook platform's algorithm (collectively, the "Material Non-Public Information").

On February 10, 2015, all of the defendants, including the Outside Directors, moved to dismiss the Complaint. After hearing argument on the motions on November 17, 2015, and by memorandum opinion dated February 29, 2016, the Court of Chancery dismissed the claims with prejudice, holding that the Plaintiff failed to allege demand futility pursuant to Court of Chancery Rule 23.1.

Plaintiff filed his Notice of Appeal on March 29, 2016 and filed Plaintiff Below-Appellant's Opening Brief on May 13, 2016. On May 24, 2016, Plaintiff filed a corrected version of his Opening Brief (the "Opening Br."). On appeal, Plaintiff disputes the Court of Chancery's holding as to the independence and disinterest of the Board. Plaintiff also attempts to address the sufficiency of his Complaint in stating claims for insider trading and breach of fiduciary duty, an issue that was not reached by the court below.

ARGUMENT

I. THE TRIAL COURT CORRECTLY DISMISSED THE COMPLAINT BECAUSE PLAINTIFF NEITHER MADE A PRE-SUIT DEMAND NOR PLEADED ADEQUATE REASONS FOR FAILING TO DO SO

A. Question Presented

Whether the Court of Chancery correctly dismissed the Complaint for failure to adequately plead demand futility in the absence of particularized allegations sufficient to show that a majority of the Board lacked independence or disinterestedness such that it could not properly consider a demand as to those claims.

B. Standard of Review

The dismissal of a derivative suit under Rule 23.1 is reviewed *de novo*. *Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004). The scope of the Supreme Court's review of such a decision is plenary. *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000).

C. Merits of Argument

The Outside Directors join in the Answering Brief filed by Zynga and the Management Defendants, which argues that the Court of Chancery correctly found that Plaintiff failed to plead particularized facts raising a reasonable doubt that a majority of the Board was sufficiently independent and disinterested such that it could impartially consider a demand at the time the Complaint was filed. These

arguments, which the Outside Directors hereby adopt, dictate that this Court should affirm the Court of Chancery's dismissal of the entire Complaint under Rule 23.1.

In particular, even if the Court here accepts that Messrs. Pincus and Hoffman are "interested" regarding the *Brophy* or Secondary Offering claims, Plaintiff failed to plead *any* particularized facts supporting an inference that a majority of the remaining directors were "beholden to" them in a way that would raise a reasonable doubt as to their ability to consider a demand. The only two Outside Directors whose independence is challenged on appeal are Messrs. Gordon and Paul, but Plaintiff pleads nothing more than generalized business relationships between them and Messrs. Pincus and Hoffman, which will not suffice to defeat independence.

Nor does the Complaint allege facts sufficient to support a reasonable inference that a majority of the Board committed any non-exculpated act such that they face a substantial likelihood of personal liability in this action. As detailed, *infra*, Section II.C.2., Plaintiff fails to show that Mr. Hoffman faces a substantial likelihood of liability for insider trading under *Brophy*. A *Brophy* claim requires particularized facts showing not only that Mr. Hoffman possessed material non-public information at the time he sold in the Secondary Offering, but also that he acted on the basis of that information (i.e. that he acted with *scienter*), and here

Plaintiff pleads no such facts. Furthermore, as detailed, *infra*, Section II.C.3., Plaintiff fails to plead any particularized facts showing that the Outside Directors acted in bad faith when approving the Secondary Offering.

* * * * *

Should the Court nonetheless overturn the Court of Chancery's dismissal, and find that demand was futile, the Outside Directors separately argue that the Court of Chancery's ruling should be affirmed as to the Outside Directors, because the Complaint fails to state a claim against them under Court of Chancery Rule 12(b)(6).

II. PLAINTIFF'S INSIDER TRADING AND BREACH OF FIDUCIARY DUTY CLAIMS DO NOT SERVE AS A BASIS TO REVERSE THE COURT'S RULING

A. Question Presented

Whether the Court of Chancery erred in dismissing the Complaint, given (i) its failure to plead a cognizable insider trading claim against Mr. Hoffman, and (ii) its failure to plead that the non-selling directors breached their fiduciary duties in approving the Secondary Offering.

B. Standard of Review

The Court of Chancery in its decision below did not reach the question of dismissal for failure to state a claim pursuant to Court of Chancery Rule 12(b)(6). Instead, the court based its holding on the Plaintiff's failure to adequately plead demand futility. *Sandys v. Pincus*, 2016 WL 769999, at *5 (Del. Ch. Feb. 29, 2016) ("Because I conclude that demand was not excused for each of the claims thus necessitating dismissal of the Complaint, I do not address any of defendants' other arguments for a stay or dismissal of this case."). Nonetheless, Plaintiff's failure to state a claim here provides an alternative basis for affirming the dismissal. *See, e.g., Central Laborers Pension Fund v. News Corp.*, 45 A.3d 139, 141 (Del. 2012) (holding that "this Court may ***affirm*** the judgment of the Court of Chancery on the basis of a different rationale.") (emphasis added). If this Court were to reverse the Court of Chancery's decision with respect to demand futility, it

should nonetheless affirm the dismissal on the alternative ground that the Complaint fails to state a claim as to the Outside Directors.

This Court reviews the "decision to grant a motion to dismiss under Court of Chancery Rule 12(b)(6)" *de novo*. *Allen v. Encore Energy Partners, L.P.*, 72 A.3d 93, 100 (Del. 2013). In considering a motion to dismiss, Delaware Court of Chancery Rule 12(b)(6) prescribes "reasonable 'conceivability.'" *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings LLC*, 27 A.3d 531, 537 (Del. 2011) (citation omitted). This standard centers on whether there is a "possibility" of recovery. *Id.* at 537 n.13 (citation omitted). Although well-pleaded allegations are accepted as true, the Court should not "credit conclusory allegations that are unsupported by specific facts or draw unreasonable inferences in the plaintiff's favor." *Allen*, 72 A.3d at 100.[6]

C. Merits of Argument

On appeal, Plaintiff advances two claims against the Outside Directors: (i) insider trading under *Brophy*, as to Mr. Hoffman, and (ii) breach of fiduciary duty

[6] The Outside Director Defendants acknowledge this standard but urge the Court to consider adopting the United States Supreme Court's "plausibility" standard. *See Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009); *see also Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings LLC*, 2010 WL 3258620, at *7 (Del. Ch. Aug. 19, 2010), *rev'd*, 27 A.3d 531 (2011). Regardless, under either standard, "[a] trial court is not . . . required to accept as true conclusory allegations 'without specific supporting allegations.'" *In re General Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 168 (Del. 2006) (quoting *In re Santa Fe Pac. Corp. S'holder Litig.*, 669 A.2d 59, 65-66 (Del. 1995)). Here, the Complaint falls short of alleging non-conclusory allegations sufficient to state a claim.

for approving the Secondary Offering, as to all Outside Directors. Among other deficiencies, a fatal flaw pervades both of Plaintiff's claims: namely, the Complaint fails to plead a *single fact* that the Outside Directors approved (and as to Mr. Hoffman, participated in) the Secondary Offering while in possession of Material Non-Public Information. This fundamental failure dooms Plaintiff's claims against the Outside Directors.

1. Plaintiff Failed to Allege Any Facts Showing that the Outside Directors Possessed Material Non-Public Information at the Time of the Secondary Offering

As detailed at length in the underlying briefing, Plaintiff alleges no specific facts to support an inference that the Outside Directors possessed Material Non-Public Information at the time of the Secondary Offering. Instead the Complaint relies entirely on conclusory allegations and misleading citations levied against "Defendants" as a whole (*see, e.g.*, ¶¶ 42, 45, 47, 51, 70, 131 (A032, A034, A036, A046, A076)), overlooking the different information the insiders, as opposed to the Outside Directors, received prior to the Offering.[7] Plaintiff cannot simply rely on a

[7] The Outside Directors invite the Court to closely scrutinize the Complaint paragraphs cited in Opening Brief, which reflect an utter lack of facts regarding the Outside Directors. *See, e.g.*, B442 (Outside Directors' Demonstrative Exhibit Provided to the Court of Chancery and the Parties at the Hearing on Defendants' Motions to Stay and Dismiss (Oral Argument Transcript at A389-90)). The extremes to which Plaintiff goes in this respect is evidenced throughout the pleadings and briefing. For example, Plaintiff alleges that all "Defendants" knew, but failed to disclose, [redacted] (¶ 94, A058), when Plaintiff's own allegations point only to [redacted] ¶ 90 (A056).

presumption that outside directors possess detailed information about the day-to-day operations of the companies they serve.[8]

In particular, Plaintiff alleges four general categories of Material Non-Public Information, (*see* Opening Br. at 15-16), yet his allegations as to each repeatedly rely only on *internal* information, if anything, evincing a glaring failure to show that the Outside Directors received any such information.

- Plaintiff alleges that all Defendants knew of lower, internal projections that varied from Zynga's publicly announced projections, but Plaintiff's own allegations reflect that: (i) [redacted] (¶ 41, A031) (emphasis added) and (ii) [redacted]. ¶¶ 1, 42-44, 46 (A014, A032-34).[9]

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[8] *See In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 971 (Del. Ch. 1996) ("[T]he duty to act in good faith to be informed cannot be thought to require directors to possess detailed information about all aspects of the operation of the enterprise. Such a requirement would simpl[y] be inconsistent with the scale and scope of efficient organization size in this technological age."); *Pfeffer v. Redstone*, 2008 WL 308450, at *10 (Del. Ch. Feb. 1, 2008) ("[D]irectors are not as a matter of general experience presumed to know business operational information that is not of a kind routinely disclosed to boards of directors."), *aff'd*, 965 A.2d 676 (Del. 2009).

[9] *See, e.g.*, ¶ 1 (A014) [redacted] (A032) [redacted]

- Plaintiff alleges that all Defendants knew of declining trends in ABPU data, but Plaintiff's own allegations [redacted] ¶ 75 (A049).[10]

- Plaintiff alleges that all Defendants knew of impending game delays [redacted] but Plaintiffs do not plead a single fact suggesting that any information regarding such delays was ever communicated to the Outside Directors prior to the Secondary Offering. ¶¶ 47, 83 (A034, A054).

- Plaintiff alleges that all Defendants knew of Facebook's upcoming platform change, yet Plaintiff's own allegations [redacted] without any facts suggesting the Outside Directors were privy to the information. ¶ 72 (A047).[11]

In sum, despite Plaintiff's access to hundreds of documents from his Section 220 request, he does not point to a single document showing that the Outside

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[redacted] (emphasis added); ¶ 46 (A034) [redacted] (emphasis added).

10 *See, e.g.*, ¶ 1 (A014) [redacted] (emphasis added); ¶ 53 (A037) [redacted] (emphasis added); ¶ 75 (A049) [redacted] (emphasis added).

11 *See, e.g.*, ¶ 72 (A047) [redacted] (emphasis added); ¶ 73 (A047) [redacted] (emphasis added).

Directors ever had knowledge of alleged Material Non-Public Information at the time of the Secondary Offering. What Plaintiff alleges was known by "management" is not supported by well-pled facts and is insufficient to state a claim. The inference Plaintiff seeks—that everything known by unspecified members of *management* should be imputed to the Outside Directors—is even more attenuated, unreasonable, and unsupported by Delaware law. *South v. Baker*, 62 A.3d 1, 16 (Del. Ch. 2012) ("it is not reasonable to infer that the Board acted in bad faith based on references to 'management,' particularly . . . on nuts-and-bolts operational issues."). Indeed, this inference runs directly contrary to a fundamental premise of this Court's *Cornerstone* decision—that outside directors should not have to bear the burden of litigation absent specific facts *as to them* which justify their inclusion. *See In re Cornerstone Therapeutics Inc., S'holder Litig.*, 115 A.3d 1173, 1182-83 (Del. 2015).[12]

[12] Nor does mere membership on an Audit Committee suffice to create an inference of knowledge. *See In re China Auto. Sys. Inc. Derivative Litig.*, 2013 WL 4672059, at *8 n.96 (Del. Ch. Aug. 30, 2013) ("The Plaintiffs suggested the Audit Committee as a whole, or at least Richardson as its chair and designated financial expert under Sarbanes–Oxley, should be held to a heightened standard of constructive knowledge about the Company's financial statements. The Court declines to entertain this argument because it does not support a claim under Delaware corporate law."); *id.* ("Mere membership on the Audit Committee is not enough for the Court to infer bad faith."); *see, e.g.*, ¶ 48 (A035) (alleging that [redacted]

The central case cited by Plaintiff (*Pfeiffer v. Toll*) only underscores the vast gulf between the facts necessary to sustain his claims, and the allegations in this case. Opening Br. at 19 (citing 989 A.2d 683 (Del. Ch. 2010)). In *Pfeiffer*, plaintiffs brought insider trading claims against directors of Toll Brothers (a designer, builder and seller of luxury homes), alleging that the defendants sold stock while in possession of material inside information. *Pfeiffer*, 989 A.2d at 692-93. At issue in *Pfeiffer* was a key operating metric, central to the company's performance: "the number of communities where Toll Brothers is actively selling homes." *Id.* at 685. Notwithstanding a lack of particularized facts showing knowledge, Vice Chancellor Laster was willing to *infer* that outside directors who sold stock were aware of this key metric. *Id.* at 693-94.

In *Pfeiffer*, the material non-public information at issue—the number of communities where TB was actively selling homes—was a key metric that tied directly to the company's financial performance. *Id.* at 685. The alleged Material Non-Public Information at issue here—alleged negative trends in ABPU—is only *one* of a large number of operational metrics tracked by *management* in order to provide insight into Zynga's business. ¶ 70 (A046).[13] In addition, in *Pfeiffer*, the

[13] *See* B346-47 (discussing key financial metrics (bookings, EBITDA), and operating metrics (DAUs, MAUs, MUUs, MUPs, APBU, unique payer bookings, quarterly unique players, unique payer bookings per quarterly unique payer) that Zynga uses to evaluate its business).

court was willing to infer knowledge of this key metric, because it formed the basis for the Company's projected 20% income growth rate that was repeated for *over fourteen months* "on earnings calls, during media appearances, and in interviews." *Pfeiffer*, 989 A.2d at 685-88, 693. Plaintiff here would have the Court infer knowledge almost *instantly*—presuming that Outside Directors were aware by March 2012 (when the Secondary Offering was approved) of [redacted]

See, e.g., ¶¶ 43, 51 (A033, A036).

Moreover, in *Pfeiffer*, plaintiff pleaded facts suggesting the Company publicly reiterated this 20% growth projection in the face of a wealth of contradictory information, some of which defendants *admitted* they had known for over a year. *Pfeiffer*, 989 A.2d at 685-88. By contrast, Plaintiff here relies entirely on inference to suggest that the Board would have been apprised of internal operational data, without a single fact showing such detailed operational data was ever raised to the Board level.[14] The inference advanced in *Pfeiffer* is wholly inapt here.

[14] In *Pfeiffer*, the court also specifically "regard[ed] the trades made by the Outside Director Defendants as sufficiently unusual in timing and amount." *Pfeiffer*, 989 A.2d at 694. Here, by contrast, four of the five Outside Directors sold *no stock whatsoever*, and Mr. Hoffman sold only 15% of his Zynga holdings. ¶ 110 (A066); *see infra*, note 15 (no facts pleaded suggesting Mr. Hoffman's sale of 15% was usual in timing of amount).

2. Plaintiff Failed to Adequately Allege an Insider Trading Claim Against Mr. Hoffman

Plaintiff's failure to allege that any of the Outside Directors (including Mr. Hoffman) was in possession of Material Non-Public Information dooms his insider trading claim against Mr. Hoffman. At the outset, it bears noting that mere trading is not enough; Plaintiff must plead facts showing that Mr. Hoffman: 1) "possessed material, nonpublic company information"; and 2) "used that information improperly by making trades because []he was motivated, in whole or in part, by the substance of that information." *Kahn v. Kolberg Kravis Roberts & Co., L.P.*, 23 A.3d 831, 838 (Del. 2011) (quoting *In re Oracle Corp. Derivative Litig.*, 867 A.2d 904, 934 (Del. Ch. 2004), *aff'd*, 872 A.2d 960 (Del. 2005)). The Complaint fails as to both elements of this claim.

As detailed at length above, despite access to numerous Board-level documents pursuant to 8 *Del. C.* § 220, Plaintiff pleads no facts showing that Mr. Hoffman possessed Material Non-Public Information at the time of the Secondary Offering. Plaintiff asserts that the so-called "Insider Trading Defendants" "sought to exploit their information advantage," but Plaintiff cites only to sources like [redacted] (¶ 72, A047), an [redacted] (¶ 73, A047) and [redacted] (¶ 75, A049). *See* Opening Br. at 19. There is not a single factual allegation that Mr. Hoffman ever *saw* this

information. Plaintiff's only hope is that the Court will treat the so-called "Insider Trading Defendants" as an undifferentiated mass, and overlook that this group includes Mr. Hoffman—an Outside Director with no management role at the Company—who would not be expected to have access to the same day-to-day operational information as officers of the Company. This is insufficient as a matter of law and the Court need not countenance such efforts. *See e.g.*, *Rattner v. Bidzos*, 2003 WL 22284323, at *10 (Del. Ch. Oct. 7, 2003) ("Rattner merely posits . . . that the Director Defendants knew of inside information, and that they knew of (or directly participated in) the allegedly material misstatements."). Put simply: the fact that Plaintiff defines Mr. Hoffman as an "Insider Trading Defendant" does not make it so.

Second, even if the Complaint adequately alleged that Mr. Hoffman possessed Material Non-Public Information (which it does not) the Complaint fails to demonstrate that Mr. Hoffman—one of the most respected entrepreneurs in Silicon Valley—made such sales "'on the basis of, and because of'" such information. *Guttman v. Huang*, 823 A.2d 492, 505 (Del Ch. 2003) (citation omitted). In effect, this element requires Plaintiff to plead particularized facts evincing scienter. *Id.* Plaintiff cannot dispute that the Complaint pleads no facts whatsoever evincing Mr. Hoffman's state of mind. While Plaintiff asserts that the

so-called "Insider Trading Defendants" "sought to exploit their informational advantage," as noted above (*supra* Section II.C.1.), the Complaint references only internal emails and reports, and there are no allegations that Mr. Hoffman ever *saw*, much less acted upon, this *internal* information.

In place of facts—just as in his briefing below—Plaintiff misapplies *Silverberg* to suggest that the Court may *infer* scienter because Mr. Hoffman: (i) sold stock at a high point; (ii) when others within Zynga were allegedly in possession of material non-public information, and (iii) purportedly failed to disclose such information. Opening Br. at 18 (quoting *Silverberg v. Gold*, 2013 Del. Ch. LEXIS 312, at *49 (Del. Ch. Dec. 31, 2013)). As with their briefing below, Plaintiff's discussion of *Silverberg* omits a key portion of the Court's analysis. The sentence quoted by Plaintiff, when read in full, makes clear that the quoted factors are only relevant when, as a threshold matter, "the Complaint supports a reasonable inference *that [defendants] possessed material, nonpublic information when they sold their shares*." *Silverberg*, 2013 Del. Ch. LEXIS 312, at *49 (emphasis added). Indeed, in *Silverberg*, the Court concluded that the defendant directors were aware of material non-public information because the

complaint pleaded ***detailed, particularized facts*** regarding two presentations ***to the Board*** that touched on the issue. *Id*. at *36-37. No such facts are pleaded here.[15]

The *Brophy* rule against insider trading "is not designed to punish inadvertence, but to police intentional misconduct." *Guttman*, 823 A.2d at 505. "Delaware case law makes the same policy judgment as federal law does, which is that insider trading claims depend importantly on proof that the selling defendants acted with scienter." *Id.* Plaintiff pleads no facts supporting such an inference of knowledge, and cannot bootstrap an inference of scienter by way of his already inadequate allegations. *See id.* at 505. For these reasons, Plaintiff's insider trading claim against Mr. Hoffman fails.

3. Plaintiff Failed to Adequately Allege that the Outside Directors Breached Their Fiduciary Duties by Approving the Secondary Offering

Plaintiff's failure to plead specific facts showing that the Outside Directors possessed Material Non-Public Information prior to the Secondary Offering is also fatal to their claim that the Outside Directors breached their fiduciary duties by approving the Secondary Offering. Plaintiff attempts to muddy the waters with

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[15] Moreover, Plaintiff ignores *Silverberg*'s reliance on the large percentage of holdings sold by the directors immediately after the company's drug was approved by the FDA—two directors sold 77% and 58% of their holdings. *Id.* at *47. These factors were central to the decision and are absent here with respect to Mr. Hoffman, who sold only 15% of his Zynga holdings. ¶ 110 (A066). Indeed, despite citing *Pfeiffer* (Opening Brief at 19) for the proposition that "timing and amount" of trades can support an inference of scienter, Plaintiff pleads no facts as to *how* or *why* Mr. Hoffman's trades were suspicious in timing or amount.

Count II, by conflating his *Brophy* claim and the Secondary Offering claim, arguing that Claim II is "unique" because "Board action was required to enable the Insider Trading Defendants' sale of Zynga stock in the Secondary." Opening Br. at 20. However, regardless of whether the allegation is that the Outside Directors aided the "Insider Trading Defendants" in committing a wrong, or that the Outside Directors consciously disregarded their duties by ignoring Material Non-Public Information leading up to approving the Secondary Offering, the "bad faith" analysis is the same.

As this Court recently clarified in *Cornerstone*, even where a court applies the entire fairness standard to a transaction or decision, a "plaintiff seeking only monetary damages must plead non-exculpated claims against a director who is protected by an exculpatory charter provision" in order to state valid claim against the director. *In re Cornerstone Therapeutics Inc., S'holder Litig.*, 115 A.3d 1173, 1175 (Del. 2015). In light of the Section 102(b)(7) provision in Zynga's certificate of incorporation, to state an actionable claim against the Outside Directors, Plaintiff must plead *particularized facts* showing that they acted in bad faith—i.e. that they "*knew* that they were not discharging their fiduciary obligations"—in approving the Secondary Offering. *Stone ex rel. AmSouth Bancorporation v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (emphasis added). In other words, Plaintiff

must show that the Outside Directors were aware of Material Non-Public Information, which he does not do. *See* Section II.C.1., *supra.*

Plaintiff's reliance on *In re Emerging Communications, Inc. Shareholders Litigation*, 2004 WL 1305745 (Del. Ch. June 4, 2004) only underscores the weakness of Plaintiff's claim with respect to the Secondary Offering. In *Emerging*, certain directors were found liable after it was shown that they *actively* and *knowingly* assisted the controller in breaching his fiduciary duties. For example, one director personally helped the controller structure and obtain financing for a transaction after receiving substantial input that the transaction price was far too low. *Id.* at *39. Another director was found liable because the Court found, based on the evidence presented and its knowledge of the director's "specialized financial expertise," that the director knew, or at the very least had strong reasons to believe, that the transaction price was unfair and failed to act on that knowledge when he voted for the transaction. *Id.* at *39-40.

Plaintiff has not pleaded any such facts here. Indeed, in *Emerging*, certain directors were found to be exculpated by the company's Section 102(b)(7) provision because—just like here—the plaintiff failed to point to any "evidence that [the directors] acted with conscious and intentional disregard of their responsibilities, or made decisions with knowledge that they lacked material

information." *Id.* at *43. Far from supporting Count II, *Emerging* actually undercuts Plaintiff's theory of liability for the Outside Directors in connection with their approval of the Secondary Offering, given Plaintiff's failure to plead facts as to their purported knowledge or bad faith.

Moreover, Plaintiff here pleads no facts explaining why the four non-selling Outside Directors would improperly authorize the Lockup Release, when not only did they not sell stock, but they agreed to additional restrictions on their own ability to sell stock in the future. B155, B158-59 (describing "new lock-up agreements in connection with this offering" under which shares held by selling stockholders *and directors whose lock-ups originally expired on May 28, 2012* agreed to new staggered restrictions locking up shares until July 6, 2012 and August 16, 2012).[16] This further undermines the reasonableness of any finding of bad faith.

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[16] Though not raised on appeal, Count III—which alleges that the Outside Directors breached their fiduciary duties under *Caremark* by allowing the dissemination of statements containing material omissions—fails for precisely the same reasons. Such a claim requires Plaintiff to allege that the Outside Directors made statements while in possession of material non-public information, *Malone v. Brincat*, 722 A.2d 5, 9 (Del. 1998), or otherwise knew about related "red flags." *Stone*, 911 A.2d at 373. As noted throughout, Plaintiff fails to plead any facts supporting such allegations of knowledge. Indeed, with respect to the *Caremark* claim, Plaintiff employs the same tactics as with his other claims, citing paragraphs in the Complaint that purportedly support his claims, which lack the facts attributed to them. For example, Plaintiff alleges that all Defendants were aware that the [redacted] ¶ 90 (A056).

CONCLUSION

The Outside Directors respectfully submit that the judgment of the Court of Chancery should be AFFIRMED.

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CERTIFICATE OF SERVICE

I, Julia B. Ripple, hereby certify that on June 28, 2016, I caused to be served a true and correct copy of the foregoing document upon the following counsel of record in the manner indicated below:

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