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IN THE SUPREME COURT OF THE STATE OF DELAWARE

JEAN-MARC ROUSSET AND SUSAN VANCE, Plaintiffs-Below, Appellants, v. CLYDE B. ANDERSON, TERRENCE C. ANDERSON, RONALD G. BRUNO, RONALD J. DOMANICO, EDWARD W. WILHELM, TERRANCE G. FINLEY, R. TODD NODEN, JAMES F. TURNER, FAMILY ACQUISITION HOLDINGS, INC., and FAMILY MERGER SUB, INC., Defendants-Below, Appellees.	)	No. 515, 2016 Court Below: The Court of Chancery of the State of Delaware Consol. C.A. No. 11343-VCL

APPELLANTS' OPENING BRIEF

Dated: December 5, 2016

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NATURE OF PROCEEDINGS

Plaintiffs-Below/Appellants Jean-Marc Rousset and Susan Vance (collectively, "Plaintiffs"), by their attorneys, respectfully submit this Opening Brief in support of their appeal from the Delaware Court of Chancery's October 10, 2016 Memorandum Opinion (the "Opinion" or "Op.") and subsequent Orders granting the Defendants-Below/Appellees' motions to dismiss the Verified Consolidated Amended Class Action Complaint (the "Amended Complaint").

On July 13, 2015, Books-A-Million, Inc. ("BAM" or the "Company") entered into an agreement and plan of merger (the "Merger Agreement") with certain entities formed by BAM's majority stockholders, the Anderson family (the "Controllers" or the "Anderson Family"),[1] pursuant to which the Anderson Family took the Company private (the "Transaction") and BAM's public, minority stockholders received $3.25 per share in cash (the "Merger Consideration"). A138-39. In connection with the Transaction, the Andersons and certain members of BAM's management, including Terrance G. Finley ("Finley"), R. Todd Noden ("Noden"), and James F. Turner ("Turner") (together, the "Management Defendants"), entered into rollover agreements (the "Rollover Agreements") to contribute all of their BAM shares to an entity formed by the Andersons, which

[1] The Anderson Family includes BAM's Executive Chairman, Clyde B. Anderson ("Anderson"); his brother and fellow BAM director, Terrence C. Anderson ("T. Anderson") (together, the "Andersons"); and certain other affiliates and family members. A138-39.

continued to own, among other things, the Company's valuable real estate development and management activities and was wholly-owned by these Defendants following the close of the Transaction.[2] A141.

Following the announcement of the Transaction, Plaintiffs filed lawsuits in the Court of Chancery, alleging that the Transaction was subject to entire fairness review and that BAM's Board of Directors (the "Board"),[3] the Andersons (as BAM's majority stockholders), and the Management Defendants breached their fiduciary duties owed to the Company's minority stockholders. A16-74. Plaintiffs also alleged that the entities formed by the Andersons to facilitate the Transaction, Family Acquisition Holdings, Inc. ("Parent") and Family Merger Sub, Inc. (together, the "Acquisition Entities"), aided and abetted the other Defendants' breaches of fiduciary duties. *Id*.

On March 23, 2016, each of the Defendants filed their respective motions and briefs to dismiss Plaintiffs' then-operative Verified Class Action Complaint. A75-137. On April 27, 2016, Plaintiffs filed the Amended Complaint (A138-76)

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[2] Also following the close of the Transaction, Anderson continued to serve as Executive Chairman and a director of the post-close company; T. Anderson continued to serve as a director; Finley continued to serve as CEO and President, and was appointed as a director; and another member of the Anderson Family, Joel R. Anderson, was appointed as a director. A141-42.

[3] BAM's Board was comprised on the following individual defendants: Anderson, T. Anderson, Ronald G. Bruno ("Bruno"), Ronald J. Domanico ("Domanico"), and Edward W. Wilhelm ("Wilhelm"). Domanico and Wilhelm served on a special committee (the "Special Committee") that was formed to evaluate the Transaction.

and, on May 11, 2016, Defendants re-filed their respective motions and briefs to dismiss the Amended Complaint pursuant to Court of Chancery Rule 12(b)(6). A177-568.

On October 10, 2016, after full briefing and a hearing (A569-738), the Court of Chancery issued the Opinion, finding that the Transaction qualified for business judgement review under *Kahn v. M&F Worldwide Corp*., 88 A.3d 635 (Del. 2014) and dismissed the Amended Complaint with prejudice. Ex. A. On October 12, 2016, the Court of Chancery entered Defendants' respective orders granting their motions to dismiss. *Id*.

On October 19, 2016, Plaintiffs timely filed their Notice of Appeal.

SUMMARY OF ARGUMENT

1. The Court of Chancery, relying on evidence not in the record and drawing significant inferences in favor of Defendants, committed numerous legal errors in holding that Plaintiffs did not plead a reasonably conceivable set of facts sufficient to demonstrate that the Special Committee members violated their fiduciary duty of care in negotiating a fair price. On the contrary, Plaintiffs more than adequately alleged that the Special Committee breached its duty of care (and loyalty) in negotiating a fair price with the Anderson Family by alleging sufficient facts to demonstrate that (i) the price negotiated by the Special Committee was demonstrably unfair, and (ii) the Special Committee was ineffective and at least grossly negligent.

STATEMENT OF FACTS

For over two years prior to the Transaction, an unnamed entity, "Party Y," made several efforts to buy BAM all at prices superior to those offered by the Anderson Family.[4] A153-54. In early 2014, Party Y proposed to acquire all of BAM's outstanding shares for $4.15 per share for the retail and trade and electronic commerce trade segments of BAM. *Id*. On March 24, 2014, Party Y submitted a revised proposal to Anderson to acquire 100 percent of the shares of the Company for $4.15 per share in cash, subject to the Anderson Family agreeing to provide a backstop commitment to acquire the Company's real estate holdings for at least $19 million and to acquire certain other assets for approximately $2.8 million. *Id*. On April 1, 2014, Anderson informed the Board that the Anderson Family would not support Party Y's proposal. *Id*.

On April 18, 2014, Party Y submitted a final non-binding indication of interest to acquire 100 percent of the Company for an increased price of $4.21 per share in cash. A155. The Board, however, determined to terminate discussions

[4] On September 24, 2013, Party Y submitted an indication of interest to Anderson to acquire the shares of the Company held by the Anderson Family for $3.30 per share in cash, and indicated that it might be willing to consider acquiring all of the Company's outstanding shares. A154. On or about October 22, 2013, Party Y reaffirmed its interest in potentially acquiring all of the shares of the Company and, on December 3, 2013, Anderson informed the Board that discussions with Party Y would be discontinued. *Id*.

with Party Y because of, among other things, the Anderson Family's unwillingness to sell their shares of the Company. *Id.*

On January 29, 2015, three weeks after BAM announced its successful holiday sales results, the Anderson Family submitted a proposal to acquire the shares of BAM common stock they did not already own for $2.75 per share in cash, which was *$1.46 per share lower* than Party Y's most recent proposal and $0.30 per share lower than the Anderson Family's previous, rejected proposal. *Id.*

The Anderson Family's $2.75 per share proposal was contained in a letter from Anderson dated January 29, 2015, (the "Proposal Letter"), and stated that the Anderson Family would not move forward with the proposal unless it was approved by a special committee of independent directors and approved by a majority-of-the-minority vote of the Company's stockholders. A155, 258. The Proposal Letter also stated:

> You should be aware that we are interested only in acquiring the outstanding shares of the Company that we do not already own. We are not interested in selling our shares in the Company to a third party or any merger or other strategic transaction involving any third party and do not intend to vote in our capacity as shareholders in favor of any such transaction.

A155. According to the Proposal Letter, "[t]he transaction would be financed through borrowings available under the Company's existing credit line." *Id.*

The following day, the Board determined to form the Special Committee of purportedly independent directors to review, evaluate, and negotiate the potential

transaction with the Anderson Family. A155-56. The Special Committee originally consisted of Bruno, Domanico, and Wilhelm, but, according to the Revised Schedule 14A Definitive Proxy Statement filed with the U.S. Securities and Exchange Commission on October 23, 2015 (the "Proxy"), Bruno had "social and civic relationships with the Anderson Family." A156, 259. After the Special Committee met several times, selected its legal advisor, and discussed the engagement of its financial advisor, the Special Committee determined that "it would be preferable for the independence of the Special Committee if Mr. Bruno did not serve on the Special Committee." *Id*. Bruno subsequently resigned from the Special Committee on February 6, 2015. *Id*.

The Special Committee subsequently retained Houlihan Lokey Capital, Inc. ("Houlihan Lokey") as its financial advisor, despite the fact that Houlihan Lokey performed transaction advisory services to an entity affiliated with the Anderson Family in 2012 and 2013. A156. In late March and early April 2015, despite knowing that the Anderson Family were not sellers, the Special Committee nonetheless directed Houlihan Lokey to contact Parties X, Y, and Z, each of which had previously communicated with Houlihan Lokey regarding a potential transaction with BAM in the preceding weeks, "to confirm if such parties planned on submitting formal proposals with respect to a transaction with the Company." A156-57, 261.

In late April 2015, this effort succeeded as Party Y submitted an indication of interest to Houlihan Lokey proposing to acquire 100 percent of the Company for $4.21 per share in cash. A157. There is no record evidence that this offer, or in fact any offer made by Party Y, contained a "control premium."[5] The proposal was conditioned on Party Y's completion of due diligence on the Company, the transaction being financed using the Company's existing credit facility, and the Company agreeing to include a "no shop" provision in a definitive merger agreement. *Id*. Unlike its March 2014 proposal, Party Y's current proposal did not contain a backstop commitment condition. *Id*.

After an unnamed employee from the office of the Anderson Family (the "Anderson Family Representative") called Houlihan Lokey in late April 2015 and restated that the Anderson Family was only interested in acquiring all of BAM's shares not already owned by them, and would not sell any of their BAM shares, the Special Committee determined to reject Party Y's $4.21 per share proposal. A157-58.

On April 30, 2015, rather than refuse to sell the Company for anything less than $4.21 per share or otherwise use Party Y's $4.21 per share offer as negotiating leverage, the Special Committee submitted a counterproposal to the Anderson Family for only $3.36 per share, an $0.85 per share or 25% discount to Party Y's

[5] *See infra* notes 18-21 and accompanying text.

offer. A158. On May 4, 2015, the Anderson Family Representative contacted Houlihan Lokey and made a revised proposal of $3.10 per share, conditioned on the right of the Anderson Family not to close the Transaction in the event that the holders of five percent or more of the outstanding shares of Company common stock exercised appraisal rights.[6] *Id*.

The next day, on May 5, 2015, the Special Committee countered the revised Anderson Family proposal at only $3.25 per share, a $0.96 per share or 30% discount to Party Y's $4.21 per share offer. *Id*. Shortly thereafter, the Special Committee and the Anderson Family ultimately agreed to squeeze out the Company's minority stockholders for the unfair $3.25 per share Merger Consideration. A263-64. At no time did the Special Committee make a $4.21 per share counteroffer to the Controllers or inform the Controllers that it would not sell the Company unless the Controllers increased their offer to match or come close to Party Y's offer.

The Special Committee also agreed to the Controllers' proposed conditions to the Transaction, including, among other things, that the Transaction was subject to the Anderson Family being able to secure $18 million in financing under the Company's existing credit facilities, and an appraisal-out condition that allowed the Anderson Family to terminate the Transaction if the holders of ten percent or

[6] Party Y's proposal did not carry a similar limitation on the ability of the Company's minority stockholders to exercise their appraisal rights. A158.

more of the outstanding shares of Company common stock, including those shares owned by the Anderson Family, exercised appraisal rights in connection with the Transaction. A159, 246.

Beginning on May 14, 2015, the Special Committee's advisors discussed and negotiated the terms of the Merger Agreement and Rollover Agreements with the Anderson Family's representatives. A158. Also on May 14, 2015, the representatives of the Special Committee and the Anderson Family negotiated the terms of a voting agreement (the "Voting Agreement") among the Andersons, the Anderson Family, Parent, and BAM, pursuant to which the Anderson Family voted all of their BAM shares in favor of the Transaction, constituting approximately 57.6 percent of the Company's total outstanding voting power. A158, 160.

On May 28, 2015, Houlihan Lokey advised the Special Committee that Party Y "remained interested in exploring a strategic transaction with the Company." A158-59, 264. On May 29, 2015, Party Y sent a letter to Houlihan Lokey reaffirming its interest in acquiring 100 percent of the shares of BAM for $4.21 per share in cash, subject to the same conditions indicated in its April 2015 letter of intent. A159. On June 2, 2015, Houlihan Lokey informed the Special Committee that Party Y called to reiterate that its proposal remained valid. *Id*.

On July 13, 2015, the Special Committee met, with conflicted Bruno in attendance and participating, to discuss the Transaction and Party Y's offer. *Id*.;

A266. After discussion with Bruno present, the Special Committee concluded that the substantially higher proposal from Party Y was "not viable" because of the Anderson Family's refusal to sell their ownership interest, and the following "conditions imposed": (i) Party Y's desire to complete due diligence; (ii) that the transaction be financed using the Company's existing credit facility; and (iii) that the Company agree to include a no shop provision in a definitive merger agreement. *Id.* These conditions, however, were identical to conditions to the Transaction. A159. Thus, the Special Committee had no credible basis to reject Party Y's offer because the conditions it cited for rejecting it were the same as those included in the Transaction, and with regard to the appraisal-out, even more onerous. *Id.*

Also at the July 13 meeting, Houlihan Lokey provided its fairness opinion and presentation to the Special Committee and Bruno; the Special Committee's legal counsel discussed, among other things, the terms of the Merger Agreement and other ancillary documents; and BAM's Chief Financial Officer, Noden, discussed the potential engagement of a valuation firm that would render a solvency opinion in accordance with the Merger Agreement. A160, 266. Following these presentations, Bruno was excused and the Special Committee determined to recommend approval of the Transaction to the Board, and, later that

day, the Board, with the Andersons abstaining, approved the Transaction. A160, 266-67.

There were no extenuating circumstances or concerns regarding insolvency that would have compelled a sale of the Company to the Controllers. The Company was performing well financially. A150-53. BAM also received a favorable solvency opinion prior to the closing of the Transaction, which was obtained in light of the fact that the Controller was financing the Transaction through the use of the Company's own credit facility. A265-66.

ARGUMENT

Question Presented

Under *Kahn v. M&F Worldwide Corp*., 88 A.3d 635 (Del. 2014), are the well-pled facts alleged in the Amended Complaint that (i) the Merger Consideration was demonstrably unfair (particularly in light of a contemporaneous third party offer that was 30% higher than the Merger Consideration) and (ii) the negotiation process employed by the Special Committee was not conducted as though the Special Committee had actually exerted arm's-length bargaining power, sufficient to demonstrate that the Special Committee breached its duty of care in negotiating a fair price and therefore sufficient to subject the Transaction to entire fairness review? *See, e.g*., A588-608.

Scope of Review

This Court reviews a trial court's ruling on a motion to dismiss *de novo* to "determine whether the trial judge erred as a matter of law in formulating or applying legal precepts."[7]

Merits of Argument

If Plaintiffs can plead a reasonably conceivable set of facts showing that *any* of the six conditions enumerated in *Kahn v. M&F Worldwide Corp*., 88 A.3d 635, 645 (Del. 2014) did not exist, including that the Special Committee is

[7] *Gantler v. Stephens*, 965 A.2d 695, 703 (Del. 2009) (quotation omitted).

"independent" and "meets its duty of care in negotiating a fair price," then Plaintiffs have stated a claim for relief that would entitle them to proceed with the litigation and conduct discovery.[8]

The Court of Chancery erred as a matter of law when it determined that Plaintiffs failed to plead sufficient facts to demonstrate that the Special Committee failed to act with the requisite due care and good faith when negotiating the transaction price.[9] In so ruling, the Court of Chancery made several erroneous legal and factual determinations, and improperly failed to draw all reasonable inferences in favor of Plaintiffs.

Plaintiffs have alleged more than sufficient facts to show that the Special Committee failed to satisfy at least its duty of care in negotiating a fair price because Plaintiffs have demonstrated that (i) the Merger Consideration negotiated by the Special Committee was demonstrably unfair; and (ii) the negotiation process employed by the Special Committee evidences the Special Committee's gross negligence and ineffectiveness. A153-63. In addition to demonstrating that the Special Committee did not meet its duty of care in negotiating a fair price, Plaintiffs have also alleged and demonstrated that the Special Committee members breached their duties of loyalty in that they failed to act in good faith or were

[8] *M&F Worldwide*, 88 A.3d at 645.

[9] Op. at 38-41.

beholden to the Controllers. In the Opinion, the Court of Chancery suggested that alleging "subjective bad faith" fits within the "special committee's independence" factor of *M&F Worldwide*.[10] To the extent this Court agrees, Plaintiffs' well-pled allegations that the Special Committee members breached their duty of loyalty (*i.e.*, failed to act in good faith or be independent) demonstrate that Defendants also failed to satisfy the "special committee's independence" factor of *M&F Worldwide*.

I. Plaintiffs Alleged That the Special Committee Breached Its Duty of Care in Negotiating a Fair Price Because the Merger Consideration Is Unfair

In *M&F Worldwide*, this Court stated that, if a plaintiff pleads facts that demonstrate the merger consideration was insufficient, then the plaintiff would effectively call into question a special committee's fulfillment of their duty of care obligations in negotiating a fair price such that plaintiff would survive a motion to dismiss.[11] This Court, moreover, indicated that the well-pled allegations in that case regarding the financial fairness of the buyout price – four indirect indicators of financial unfairness – would have survived a motion to dismiss because they called "into question the adequacy of the Special Committee's negotiations,

[10] Op. at 23-24.

[11] *M&F Worldwide*, 88 A.3d at 645, n.14.

thereby necessitating discovery on all of the new prerequisites to the application of the business judgment rule."[12]

Plaintiffs here rely on much more direct evidence of financial unfairness. The Amended Complaint alleges that the Special Committee solicited third party offers for the Company to test the market and pricing knowing that the Anderson Family was not a seller, and received such an offer from Party Y, which was willing to pay 30% more than the ultimate Merger Consideration offered by the Anderson Family, and yet the Special Committee sold BAM for an inadequate price even though there was no exigent need to sell the Company to anyone. A140, 150-53. Delaware courts have long recognized that "[v]alues derived in the open market through arms-length negotiations offer better indicia of reliability than [] interested party transactions[.]"[13] Indeed, even the Court of Chancery explicitly recognized that the price a company could obtain from a third party on the open market is highly probative of the company's fair price.[14] From this, the Court of Chancery concluded that "the Committee decided to solicit offers for BAM from

[12] *Id*.

[13] *M.P.M. Enterprises v. Gilbert*, 731 A.2d 790, 796 (Del. 1999); *see also Van De Walle v. Unimation, Inc*., 1991 Del. Ch. LEXIS 27, *50 (Del. Ch. Mar. 6, 1991).

[14] Op. at 40 ("A decent respect for reality forces one to admit that [a financial advisor's opinion] is frequently a pale substitute for the dependable information that a canvas of the relevant market can provide.") (quotation omitted).

various other parties, which would enable the Committee to better assess the value of BAM and the attractiveness of the Anderson Family's offer."[15]

As a result of the Special Committee's outreach, Party Y submitted its $4.21 per share offer. Unlike the situation in *M&F Worldwide*, or indeed in any case decided since then, the Special Committee's market check here – limited to only three potential purchasers – revealed that a third party was willing to pay at least 30% more for the Company. This allegation concerning the inadequacy of the Controllers' offer price *viz-à-viz* Party Y's offer alone is sufficient to defeat Defendants' dismissal motions.

In addition to Party Y's materially higher offer, the Amended Complaint contains other detailed allegations pertaining to the unfairness of the Merger Consideration and therefore the Special Committee's breach of duty in negotiating a fair price. For example, BAM owned properties with an appraised value of $50.3 million (compared to the Transaction value of $21 million) (A150), and it had consistent positive financial performance prior to the announcement of the Transaction. A150-53, 161. Further, according to *Yahoo! Finance*, as of the time of the announcement of the Transaction, at least one analyst had set a price target for BAM stock at $12.00 per share. A161. Additionally, the Amended Complaint alleged that Houlihan Lokey's own valuation analyses supported a finding that the

[15] *Id*. at 9.

Merger Consideration was unfair. *Id.* For example, Houlihan Lokey's *Selected Companies Analysis* yielded an implied per share value as high as $4.21 per share, or $0.96 per share higher than the Merger Consideration. *Id.* Further, the Amended Complaint alleged that Houlihan Lokey's Discounted Cash Flow Analysis ("DCF"), which relied upon financial projections provided by the conflicted Management Defendants, was flawed and should have resulted in a higher valuation of BAM, which the Special Committee members should have known in light of their substantial executive and financial experience. A162-63, 591-594, 604-05.

Notwithstanding established precedent and Plaintiffs' well-pled allegations that the final merger price was unfair (particularly in light of Party Y's superior offer), the Court of Chancery held that Plaintiffs failed to allege sufficient facts to demonstrate, among other things, that the Special Committee met its duty of care in negotiating a fair price. Although the Court of Chancery properly acknowledged that evidence of an unfair merger price can demonstrate a special committee's lack of care or bad faith, the Court of Chancery determined that Party Y's superior offer could not, as a matter of law, reflect the Company's fair price because that offer was for control of the entire Company and therefore contained a "control premium." The Court of Chancery instead determined that the Controllers' inferior offer reflected BAM's fair price, notwithstanding the fact that

the Court of Chancery recognized that the Controllers' offer price reflected a "minority discount,"[16] which may not be considered when determining a company's "fair price" in the entire fairness context or "fair value" in the appraisal context.[17]

The Court of Chancery committed legal error in concluding that Party Y's offer contained a control premium, holding: "On the facts alleged, *one can reasonably infer* that Party Y's offer was higher because Party Y was seeking to acquire control. . . ."[18] On a motion to dismiss, however, the Court of Chancery must draw all reasonable inferences in favor of Plaintiffs, not Defendants.[19] There is nothing in the Amended Complaint or the Proxy to support the Court of

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[16] Op. 32-34 (stating that minority shares "trade at a discount when a dominant or controlling stockholder is present" and that "the Anderson Family's offer was lower because it took into account the family's existing control over the Company").

[17] *See Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1145 (Del. 1989) ("The application of a discount to a minority shareholder is contrary to the requirement that the company be viewed as a 'going concern.'"). This Court's precedent establishes that the fair price and fair value inquiries "call for equivalent economic inquiries." *In re Orchard Enters., Inc. S'holders Litig*., 88 A.3d 1, 30 (Del. Ch. 2014) (citations omitted). "They differ only in the appraisal statute's insistence on a point calculation when awarding fair value." *Id*. Accordingly, the appraisal cases cited herein are probative.

[18] Op. at 34 (emphasis added).

[19] *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings LLC*, 27 A.3d 531, 536 (Del. 2011). Delaware, moreover, uses the "conceivability" standard, and not the higher "plausibility" standard, which "invites judges to 'determin[e] whether a complaint states a plausible claim for relief' and 'draw on . . . judicial experience and common sense.'" *Id*. at 537 (quotation omitted).

Chancery's inference that Party Y's offer contained a control premium (as opposed to simply reflecting the Company's fair going concern price), and there is no evidence that the Special Committee or its financial advisor, Houlihan Lokey, considered or performed any analysis to determine whether Party Y's offer in fact contained a control premium or that such an analysis was presented the Special Committee or the Board.[20] As such, Plaintiffs are entitled to the reasonable inference that Party Y's offer did not contain a control premium.[21]

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[20] The purported existence of a control premium was an *ex post*, lawyer-driven argument. Defendants never raised the issue in their initial dismissal brief. The argument appeared for the first time in Defendants' second opening dismissal brief, after Plaintiffs filed the Amended Complaint pursuant to Rule 15(aaa) to rebut Defendants' initial, primary assertion that Party Y's offer was rejected due to the conditions imposed by Party Y, which Plaintiffs made clear in the Amended Complaint were the same as the Controllers' conditions but without the onerous appraisal-out condition imposed by the Controllers. *Compare* A123-24 (initial brief), *with* A226-28 (second brief).

[21] Indeed, offers to acquire control of a company do not necessarily or inherently contain control premiums. *See, e.g.*, *In re Toys "R" Us, Inc., S'holder Litig*., 877 A.2d 975, 1012 (Del. Ch. 2005) ("There is no guarantee that Babies "R" Us will command a control premium later."); *see also* Philip Saunders, Jr., Ph.D., *Control Premiums, Minority Discounts, and Marketability Discounts*, at 2 ("In short, the mere fact of control does not lead to any specific premium. Indeed, it does not necessarily lead to any premium at all.") (available at http://www.philipsaunders.com/Portals/1/PDF/Ch16_Control_Prem_Min_Dct_LOMD.pdf); Aswath Damodaran, *The Value of Control: Implications for Control Premia, Minority Discounts and Voting Share Differentials*, at 41 (June 2005) ("Since the control premium is the difference between the status-quo value of a firm and its optimal value, it follows that the premium should be larger for poorly managed firms and smaller for well managed firms. In fact, the control premium should be zero for firms where management is already making the right decisions.") (available at http://people.stern.nyu.edu/adamodar/pdfiles/papers/controlvalue.pdf).

Moreover, even assuming Party Y's offer did reflect a control premium, neither the Court of Chancery nor Defendants can cite any information in the record to show how much of Party Y's offer was attributable to a control premium and how much reflected the Company's going concern value. Houlihan Lokey only prepared and presented the Special Committee with three presentations on April 15, 2015 (A491), April 29, 2015 (A522), and July 13, 2015 (A526). Despite receiving Party Y's $4.21 per share offer on or around April 22, 2015 (A261), Houlihan Lokey's presentations only mention Party Y's offer on one page in the "Transaction Background" section of its final fairness presentation (A529), and it contains no analysis of Party Y's offer.

Indeed, the Court of Chancery expressly acknowledged that "[i]t is not possible to infer the exact amount of the premium" reflected in Party Y's offer.[22] Notwithstanding this conclusion, the Court of Chancery determined—as a matter of factual certainty—that the $0.96 (or 30%) difference between Party Y's $4.21 per share offer and the Controllers' $3.25 per share offer was entirely attributable to a control premium. According to the Court of Chancery, the $0.96 difference was "not so facially large as to suggest that the Committee was attempting to facilitate a sweetheart deal for the Anderson Family."[23] In so concluding, the

[22] Op. at 34.

[23] *Id*. at 35-36.

Court of Chancery relied on academic authority that generally indicate that when existent, control premiums can range between approximately 30% and 50%, and determined that the "bargained-for consideration falls within a rational range of discounts and premiums."[24] This holding is erroneous for several reasons.

First, as noted, there is no evidence the Special Committee considered or relied upon this information and made the same determination as the Court of Chancery to justify selling the Company to the Controllers at an inferior price. Second, the authorities cited by the Court of Chancery do not definitively demonstrate that control premiums must be between 30% and 50%.[25] Indeed, past transactions for control have generated no, or even negative, control premiums.[26] Making these unsupported factual findings and drawing these inferences against Plaintiffs on a motion to dismiss was inappropriate, and constituted reversible legal error.[27]

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[24] *Id*. at 35.

[25] Damodaran, *supra* note 21, at 41 ("Since control premium will vary across firms, there can be no simple rule of thumb that applies across all firms. Thus, the notion that control is always 20-30% of value cannot be right.").

[26] Saunders, *supra* note 21, at 1-2 ("The full range of premiums has been anywhere from double or more the market price to zero, and some controlling interests were acquired at discounts from the publicly traded market prices."); FactSet Mergerstat, *Control Premium Study 1st Quarter 2012*, at 2 (2012) (noting the low premium in a domestic transaction was negative 77.1%) (available at https://data.bvresources.com /pdf/CPS1q12Sample.pdf).

[27] *See Cent. Mortg. Co*., 27 A.3d at 537.

Additionally, even accepting the Court of Chancery's conclusion that control premiums – as a matter of law – must range from approximately 30% and 50%, the Court of Chancery erred by analyzing the wrong premium for Party Y's offer. That is, the Court of Chancery derived Party Y's premium by reference to the Controllers' offer of $3.25 per share, as opposed to comparing Party Y's offer to the Company's unaffected share price of $1.70 on January 28, 2015 (the date before the Controllers submitted their going-private offer) (A467), as is typical when calculating control premiums.[28] Using the Company's unaffected stock trading price as the appropriate measure to calculate the premium offered by Party Y, Party Y's offer actually reflected a premium of 148%, which is well above the premiums cited by the Court of Chancery, thus suggesting that a large portion of Party Y's offer did not reflect some purportedly impermissible "control premium," but rather simply reflected the Company's fair price as a going concern.

In addition to the Court of Chancery's improper and erroneous factual determinations, the Court of Chancery also made several erroneous legal conclusions. At the core of the Court of Chancery's holding is its implicit assumption that a company's fair price cannot reflect a "control premium" as a matter of law. Control premiums are the difference between "(1) prices that buyers are willing to pay for stock that will give a buyer control of a corporation . . . and

[28] *See* FactSet Mergerstat, *supra* note 26, at 72 (calculating control premium as: (Purchase Price - Unaffected Stock Price) / (Unaffected Stock Price)).

(2) prices that buyers are willing to pay for stock that does not convey control of the corporation. . . ."[29] "Control premiums can be attributed to a number of sources which vary depending on the acquiror, the target, the quality of the target's management, the reasons for the acquisition, the financial and legal structure of the acquisition, and general economic and legal factors."[30]

However, there is no rule of law that control premiums cannot be considered when determining a company's fair price or fair value.[31] Rather, in determining a company's fair price, Delaware courts are tasked with determining a company's "control" or "going concern" value.[32] "In determining 'going concern' value, the central inquiry is: what would the asset command in the market, if synergistic elements of value are excluded?"[33] Under this standard, courts "must take into consideration all factors and elements which reasonably might enter into the fixing

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[29] John C. Coates IV, *"Fair Value" As an Avoidable Rule of Corporate Law: Minority Discounts in Conflict Transactions*, 147 U. PA. L. REV. 1251, 1273 (1999).

[30] *Id*. at 1274.

[31] *See Prescott Group Small Cap, L.P. v. Coleman Co*., 2004 Del. Ch. LEXIS 131, *99 (Del. Ch. Sept. 8, 2004) (stating that one expert's contention that "any control premium" is impermissible and cannot be considered under Delaware appraisal law runs "blatantly counter to the settled Delaware precedent on the subject").

[32] *Id*. at *98.

[33] *Id*. at *95; *but see M.P.M. Enterprises*, 731 A.2d at 797 (suggesting that synergies may be taken into consideration when determining a company's fair price in the entire fairness context, but not in the appraisal context).

of value," including, but not limited to, "market value, asset value, dividends, earning prospects, [and] the nature of the enterprise."[34]

Moreover, Delaware courts have recognized that a company's "'sale value,' meaning the sale of an entire subject company, can be a 'very strong indication of fair value,' if there is evidence that that value does not include synergistic elements—meaning, 'the value of the company to one specific buyer.'"[35] Thus, an offer from a third party such as Party Y, which might (or must, according to the Court of Chancery) include a control premium, is "a very strong indication of fair value." Under Delaware law, "there is only one principled basis to disregard the price actually derived from the sale of a company as a whole: where, but only to the extent that, the sale price or 'sale value' contains synergistic elements,"[36] which Defendants cannot show here. Thus, the Court of Chancery's implicit conclusion that BAM's fair price cannot reflect a control premium is erroneous.

To support its conclusion that Party Y's third party offer could not reflect the Company's fair price because it contained a control premium, the Court of Chancery erroneously relied on that Court's prior decision in *Mendel v. Carroll*, 651 A.2d 297 (Del. Ch. 1994). That case, however, is inapposite as it involved a

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[34] *Tri-Continental Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950).

[35] *Prescott Group*, 2004 Del. Ch. LEXIS 131, at *97 (quoting *M.P.M. Enterprises*, 731 A.2d at 796).

[36] *Id*. at *96.

very different set of facts and questions of law. In *Mendel*, Katy Industries, Inc. ("Katy") and its majority stockholders, the Carroll family, entered into a merger agreement, pursuant to which the Carroll family would take Katy private for $25.75 per share.[37] Unlike the situation here, after a third party, Pensler Capital Corporation ("Pensler"), subsequently submitted a superior offer of $29 per share (later reduced to $27.80), *the special committee withdrew its recommendation of the going-private merger and the Carroll family terminated the merger agreement and abandoned the transaction*.[38] To get around the Carroll family's refusal to sell its shares, Pensler proposed that Katy issue it an option to purchase 1.8 million Katy shares at $27.80 so that, if exercised, the Carroll family's ownership would be reduced to approximately 40%.[39] Over the Carroll family's objections, the special committee pursued Pensler's idea, but ultimately determined not to grant the option because its counsel could not opine that granting such an option was legal.[40]

After the discussions with Pensler were terminated, stockholder-plaintiffs filed a lawsuit and sought an "unprecedented remedy: an order requiring the board of directors of a Delaware corporation to grant an option to buy 20% of its stock to

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[37] *Mendel*, 651 A.2d at 300.

[38] *Id*. at 301.

[39] *Id*. at 302.

[40] *Id*. at 302-03.

a third party for the primary purpose of diluting the voting power of an existing control block of stock."[41] Specifically, the order sought to direct the Katy board to grant Pensler an option to purchase up to 20% of Katy's stock for $27.80 per share, the last price Pensler submitted to acquire Katy.[42] Plaintiffs' "theory" in that case was that the board was required to maximize stockholder value under *Revlon*[43] when the Carroll family submitted its going-private offer, and that the board breached its fiduciary duties when it denied plaintiffs the ability to realize Pensler's higher offer by failing to approve the dilutive option proposed by Pensler.[44]

Mendel is inapposite for several reasons. As an initial matter, the Court of Chancery ignored the fact that the special committee in *Mendel* actually complied with their fiduciary duties by refusing to accept the controlling stockholders' inferior-priced offer in the face of a higher third party offer. Indeed, after Pensler submitted its higher offer following the execution of a merger agreement, the special committee determined that it could no longer rely on its banker's fairness opinion to approve the controlling stockholders' offer and determined that it could

[41] *Id.* at 298.

[42] *Id*.

[43] *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

[44] *Mendel*, 651 A.2d at 303-04.

not go forward with the agreed-to going-private merger.[45] Following the withdrawal of the special committee's recommendation of the Carroll family's offer, the Carroll family terminated the merger agreement. Moreover, following the termination of the going-private merger and in the face of the Carroll family's repeated objections and refusal to sell their Katy shares, the special committee continued to pursue alternative transactions with Pensler, including the merger and dilution transactions, and only ceased conversations with Pensler when the special committee finally determined, after fully informing itself, that no transaction (with either the Carroll family or Pensler) was in the stockholders' best interest. This is the type of arm's-length negotiations that this Court has determined evidences an effective special committee.[46]

Thus, the transactions involved, and the board's resulting duties, in each case are starkly different. In *Mendel*, there was no impending going-private transaction by the Carroll family, and the special committee therefore was under no obligation to engage in a transaction or maximize the minority stockholders' value, particularly when doing so would violate the board's duties to the controlling stockholders. Moreover, unlike the situation here, the plaintiffs in *Mendel*, as the

[45] *Mendel*, 651 A.2d at 301. Pensler's offer was only 12.6% higher than the Carroll family's offer, compared to Party Y's offer which was 30% higher than the Controllers' offer here.

[46] *See Kahn v. Lynch Communication Sys*., 638 A.2d 1110, 1120-21 (Del. 1994).

moving parties seeking an "unprecedented" mandatory injunction, had the burden of demonstrating a reasonable likelihood that the board breached its fiduciary duties and that the Carroll family's offer was unfair, which plaintiffs failed to do.

In contrast, because the Controllers here were attempting to exploit the minority stockholders by squeezing them out of the Company, the Special Committee (unlike the special committee in *Mendel*) was under a duty "to seek the alternative that maximized the value of [the minority's] residual claims without regard to the particular interests of the controller," bearing in mind that "[t]hat alternative could well have been no transaction at all."[47] Defendants, moreover, as the moving parties, have the burden of rebutting Plaintiffs' well-pled allegations that the Special Committee failed to maximize stockholder value and negotiate a fair price. In light of Party Y's superior offer and Plaintiffs' other unfair price allegations, Defendant cannot carry this burden. As such, the Court of Chancery's reliance on *Mendel* is inapt and its holding is contrary to more analogous Delaware cases that hold "[a] merger price resulting from arms-length negotiations where

[47] *Orchard*, 88 A.3d at 36; *see also Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989). Indeed, the *Mendel* Court noted that, "*if* the board were to approve a proposed cash-out merger, it would have to bear in mind that the transaction is a final-stage transaction for the public shareholders," and thus the board would have been obliged "to maximize the current value of the minority shares." *Id*. (emphasis in original). *Mendel*, 651 A.2d at 306.

there are no claims of collusion is a very strong indication of fair value."[48] Accordingly, the Court of Chancery erred when it ignored Party Y's superior offer as evidence that the Special Committee failed to negotiate a fair price with due care.

II. The Negotiation Process Employed by the Special Committee Demonstrates the Special Committee's Ineffectiveness and Lack of Care or Good Faith

Plaintiffs also have pled sufficient facts that the process employed by the Special Committee demonstrates that its members breached their duty of care (and good faith) in negotiating the Merger. A153-60, 598-99, 605-06. These well-pled facts were improperly ignored by the Court of Chancery.

To be entitled to business judgement review under *M&F Worldwide*, "the controlling stockholder must do more than establish a perfunctory special committee of outside directors."[49] Rather, the special committee must be "effective," meaning that it must "**function in a manner which indicates that the controlling stockholder did not dictate the terms of the transaction and that the committee exercised real bargaining power 'at an arms-length.'**"[50] This

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[48] *M.P.M. Enterprises*, 731 A.2d at 797; *see also Unimation*, 1991 Del. Ch. LEXIS 27, at *51 ("[A]n auction market (or its equivalent, in the form of an effective market canvass) can provide important, highly reliable, evidence of the best available transaction for such a sale.").

[49] *M&F Worldwide Corp.*, 88 A.3d at 646 (quotation omitted).

[50] *Id*. (emphasis added, quotation omitted).

Court has noted that this determination "merits careful judicial scrutiny"[51] and that "deciding whether an independent committee was effective in negotiating a price is a process so fact-intensive and inextricably intertwined with the merits of an entire fairness review (fair dealing and fair price) that a pretrial determination of burden shifting is often impossible."[52]

Significantly, after receiving Party Y's $4.21 per share offer, the Special Committee never indicated to the Controllers that it would not accept an offer lower than Party Y's $4.21 per share offer, and never even made a $4.21 per share counter-offer to the Controllers; instead, the Special Committee countered the Controllers' offer with only $3.36 per share, *an $0.85 per share or 25% discount to Party Y's offer*.[53] A158, 606. The Special Committee, moreover, determined to reject Party Y's offer and accept the Controllers' even lower $3.25 per share offer, which was a $0.96 per share or 30% discount to Party Y's offer. *Id*. Thus, the Special Committee plainly did not act as though it "had in fact exerted its

[51] *Lynch*, 638 A.2d at 1118.

[52] *M&F Worldwide Corp.*, 88 A.3d at 646.

[53] As noted *supra*, there is no evidence that the Special Committee or Houlihan Lokey determined that Party Y's offer contained some purportedly impermissible "control premium" to justify this substantially discounted counteroffer.

bargaining power against the [Controllers] at arm's length."[54] These facts, standing alone, are more than sufficient.

In addition, the record shows that the Special Committee either misrepresented the truth or misunderstood the facts. The Proxy states that, in addition to the Anderson Family's refusal to sell (which it knew all along), the Special Committee rejected Party Y's offer due to the "conditions imposed" by Party Y's offer. A266. However, because the conditions imposed by Party Y and the Controllers were the same (with the exception of the appraisal-out condition imposed by the Controllers), the Special Committee could not credibly reject Party Y's offer on that basis. A159.

Further demonstrating its lack of care, the Special Committee allowed Bruno—who was conflicted as a result of his at least twenty-three year long business and personal relationship with the Andersons (A143-44, 608-09), and specifically removed from the Special Committee as a result of his "social and civic relationships with the Anderson Family" (A156, 259)—to be present and

[54] *Weinberger v. UOP*, 457 A.2d 701, 709 n.7 (Del. 1983). *See also Rabkin v. Philip A. Hunt Chem. Corp*., 498 A.2d 1099, 1106 (Del. 1985) (finding the special committee ineffective in light of "the apparent absence of any meaningful negotiations as to price"); *cf. Rosenblatt v. Getty Oil Co*., 493 A.2d 929, 938 (Del. 1985) (noting that the target company's "attempt to obtain the highest possible value, irrespective of the inconsistencies in its approach, nearly caused the collapse of negotiations on at least two occasions"); *M&F Worldwide Corp.*, 88 A.3d at 652 (noting the special committee submitted a "very aggressive counteroffer" of $30 per share over the controller's $24 per share offer).

participate in its final meeting before approving the Transaction on July 13, 2015. A159, 266. Not only was Bruno allowed to participate in Houlihan Lokey's final presentation regarding the fairness of the Transaction, he was also present and allowed to participate in discussions with: the Special Committee's legal counsel about, among other things, the terms of the Merger Agreement and other ancillary documents; BAM's Chief Financial Officer, Noden (who agreed to rollover his BAM shares in the Transaction), about the potential engagement of a valuation firm that would render a solvency opinion in accordance with the Merger Agreement; and, significantly, *the Special Committee when they discussed, and determined to reject, Party Y's superior offer*. A266-67, 612-13. In fact, the only portion of the meeting from which Bruno was excused was when the Special Committee voted to approve the Transaction, which by then was a foregone conclusion. A266-67.

The Court of Chancery suggested that Bruno was invited to participate "as a matter of efficiency"[55] and that the "directors decided to avoid the need for a repeat performance by having Bruno sit in when Houlihan Lokey made its presentation to the Committee."[56] This characterization of the reason Bruno was allowed to participate in the Special Committee's final meeting is not found in the Proxy, but

[55] Op. at 11.

[56] *Id*. at 22.

rather originated in Defendants' Brief. A221. The Court of Chancery did not and could not have had any factual basis to presume that it was "efficient" for a conflicted director to participate in the part of the meeting where the Special Committee rejected Party Y's offer. Indeed, there is nothing in the Proxy stating that the Board even considered Party Y's offer when it later met to approve the Transaction. A267.

Although the Court of Chancery acknowledged that this was not a "pristine process" and that "the participation of a director whose independence was compromised might be problematic,"[57] it nonetheless determined that these facts, as a matter of law, did not "support a reasonably conceivable inference that having Bruno present solely for Houlihan Lokey's fairness presentation" prevents the Transaction from satisfying the *M&F Worldwide Corp*. conditions.[58] The Court of Chancery is incorrect, as these facts, particularly when considered in conjunction with Plaintiffs' other well-pled facts, are sufficient to demonstrate that the Special Committee breached at least its duty of care in negotiating the Transaction.

These indisputable facts demonstrate the Special Committee's ineffectiveness, as it did not act as though the Controllers did not dictate the terms of the Transaction or act as if it in fact exerted bargaining power against the

[57] *Id*. at 22.

[58] *Id*. at 22-23.

Controllers at arm's-length.[59] Indeed, the Special Committee's actions (or lack thereof) demonstrate the directors' lack of care and conscious disregard and "indifference to their duty to protect the interests of the corporation and its minority shareholders."[60] These facts exemplify the long-recognized concern behind controlling stockholder transactions and the justification for the entire fairness standard due to "the risk that when push comes to shove, directors who appear to be independent and disinterested will favor or defer to the interests and desires of the majority stockholder."[61] Oftentimes, when a controlling stockholder is present, members of special committees, such as those here, "are rarely comprised of independent directors whose own financial futures depend importantly on getting the best price and, history shows, are sometimes timid, inept, or . . ., well, let's just say worse."[62]

Instead of carefully reviewing the Special Committee's price negotiations (as this Court has required), the Court of Chancery ignored these well-pled facts and concluded that the Special Committee's decision to solicit third party offers supported a finding that the Special Committee satisfied its duty of care and acted in good faith, notwithstanding the fact that Party Y submitted a much higher $4.21

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[59] *See M&F Worldwide Corp.*, 88 A.3d at 646; *Lynch*, 638 A.2d at 1120-21.

[60] *Strassburger v. Earley*, 752 A.2d 557, 581 (Del. Ch. 2000).

[61] *Orchard*, 88 A.3d at 36.

[62] *In re Cox Communs., Inc. S'holders Litig.*, 879 A.2d 604, 619 (Del. Ch. 2005).

per share offer on three separate occasions over the span of approximately fourteen months prior to the Board's approval of the Transaction.[63] This conclusion is erroneous. It is well established that the utility of conducting a market check is to demonstrate the fairness of an offer when there is an open opportunity to buy a company and no topping bidders come forward.[64] Conversely, it necessarily follows that, if a materially higher offer does emerge as a result of a market check, the initial, inferior offer is demonstrably unfair and the directors' decision to accept the inferior offer likely will constitute a breach of fiduciary duty.

Rather than accept this established principle, the Court of Chancery suggested that there were other salutary reasons for performing a market check here, including that it "allowed the Committee to test the Anderson Family's conviction about not being a seller" and it "also helped the Committee negotiate, because the offer would be a data point in any post-closing appraisal action, giving the Anderson Family a reason to bump their offer to decrease the risk that dissenting stockholders would seek appraisal."[65] These suggestions, however, are

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[63] Op. at 32, 40.

[64] *Barkan v. Amsted Industries, Inc.*, 567 A.2d 1279, 1287 (Del. 1989); *Unimation, Inc.*, 1991 Del. Ch. LEXIS 27, *50 ("The most persuasive evidence of the fairness of the . . . merger price is that it was the result of arm's-length negotiations between two independent parties, where the seller . . . was motivated to seek the highest available price, and a diligent and extensive canvass of the market had confirmed that no better price was available.").

[65] Op. at 40.

mere conjecture and are not supported by the record. There is no evidence that the third party offers were solicited or used for any of those purposes. The Proxy simply states that Houlihan Lokey, at the Special Committee's directive, reached out to Parties X, Y, and Z "to confirm if such parties planned on submitting formal proposals with respect to a transaction with the Company." A261.

The Special Committee, moreover, did not use Party Y's offer as negotiating leverage, use it to reject the Controllers' offer, or have Houlihan Lokey perform any other analyses of the Company's fair value in light of Party Y's superior offer. Houlihan Lokey's presentations to the Special Committee contained no analysis of Party Y's offer, and simply mentions Party Y's offer on one page in the "Transaction Background" section of its final fairness presentation. A529. The only reasonable inference for reaching out to the three potential bidders was to determine the Company's fair market value, and, having been informed about the Company's true value through the receipt of Party Y's higher offer, the Special Committee should have refused to sell out the minority stockholders for anything less.

Moreover, in light of Party Y's superior offer, the Special Committee could not have relied in good faith or with due care on Houlihan Lokey's fairness presentation to accept the Controllers' substantially inferior offer.[66] Each of the

[66] *See Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1281 (Del. 1989).

Special Committee members, Domanico and Wilhelm, have substantial executive and financial experience, including currently or formerly working as a chief financial officer.[67] As such, they cannot claim that they were ignorant or that they blindly relied upon Houlihan Lokey's fairness presentation, and in fact they should have known that the fairness presentation was flawed when objective market evidence suggested that the Controllers' offer was unfair.[68] For similar reasons, the fact that the Special Committee met several times, submitted two (low) counteroffers, and agreed to a price that was a premium to the stock's trading price is not sufficient evidence to demonstrate that the Special Committee acted with due care and in good faith.[69]

CONCLUSION

For the reasons stated herein, the Court of Chancery erred in concluding that Defendants satisfied all six conditions enumerated in *M&F Worldwide*. Because the entire fairness standard of review applies to the Transaction, the Court of

[67] *See* Op. at 3-4; *see also* A325, 604-05.

[68] *See e.g.*, *In re Emerging Communs., Inc. S'holders Litig*., 2004 Del. Ch. LEXIS 70, *143-147 (Del. Ch. May 3, 2004) (finding a director, Muoio, liable for failing to act in good faith when that director had "strong reasons to believe" that the merger consideration was unfair in light of his financial background and notwithstanding Houlihan Lokey's fairness opinion); *see also Unimation, Inc*., 1991 Del. Ch. LEXIS 27, *50 ("The fact that a transaction price was forged in the crucible of objective market reality (as distinguished from the unavoidably subjective thought process of a valuation expert) is viewed as strong evidence that the price is fair").

[69] *See, e.g.*, *Lynch*, 638 A.2d at 1121.

Chancery's decision must be reversed and this case must be remanded to allow Plaintiffs to conduct discovery.

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