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Case No. 6623-VCN

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE BJ'S WHOLESALE CLUB, INC.	:	Consolidated
SHAREHOLDERS LITIGATION	:	C.A. No. 6623-VCN

MEMORANDUM OPINION

Date Submitted: October 4, 2012
Date Decided: January 31, 2013

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NOBLE, Vice Chancellor

Lead Plaintiffs, a collection of individual and institutional former shareholders of Defendant BJ's Wholesale Club, Inc. ("BJ's" or the "Company"), bring a direct shareholder class action against BJ's former board of directors (the "Board" or "Defendant Directors"), for breach of their fiduciary duties in connection with the September 30, 2011 sale of all of BJ's outstanding shares to private equity firms Defendant Leonard Green & Partners, L.P. ("LGP") and Defendant CVC Capital Partners ("CVC") for $51.25 per share (the "Buyout"). The Plaintiffs also allege that LGP, CVC, and Defendant Beacon Holding, Inc., an affiliate of LGP and CVC ("Beacon Holding"), and Defendant Beacon Merger Sub, a wholly owned subsidiary of Beacon Holding used to effectuate the Buyout (collectively, the "Buyout Group"), aided and abetted the Defendant Directors' breach of their fiduciary duties. Defendants have filed a joint motion to dismiss Plaintiffs' Second Amended Complaint. For the following reasons, their motion is granted.

I. BACKGROUND

A. *The Parties*

Lead Plaintiffs in this consolidated class action are Norfolk County Retirement System, Employees' Retirement System of the Government of the

Virgin Islands, Freddie Wayne Baumgartner, and Maxine Phillips, all of whom were—at all relevant times—holders of BJ's common stock.[1]

BJ's, formerly a publicly traded Delaware corporation, is a membership based warehouse club that offers, among other items, food, apparel, office equipment, and household products. Its principal competitors are Costco and Sam's Club (a division of Wal-Mart Stores, Inc.).[2] As the third-largest wholesale retailer in the United States, BJ's operates 190 stores in 15 eastern states.[3]

Defendant Laura J. Sen ("Sen") was BJ's President and Chief Executive Officer from February 2009 and served as a director from January 2008.[4] As of May 2010, Defendant Herbert J. Zarkin ("Zarkin") was the non-executive Chairman of the Board and served as a consultant to Sen (the CEO) and senior management of the Company. Previously, he had served as Chairman of the Board for almost 13 years and, for a short period, as President and CEO of the Company.[5] Defendant Thomas J. Shields ("Shields") was a director of the Company from July 1997 until the Buyout. The Plaintiffs cursorily challenge Shield's independence from Zarkin and Sen (both of whom are allegedly interested in the transaction) because of his long-term professional relationship with them, which dates as far

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[1] Verified Consolidated Second Am. Class Action Compl. (the "Complaint" or "Compl.") ¶ 11.
[2] *Id*. at ¶ 32.
[3] *Id*. at ¶ 12.
[4] *Id*. at ¶ 13.
[5] *Id*. at ¶ 14.

back as 1992.[6] Also, the other members of the Board at the time of the Buyout are Defendants.[7]

LGP is a private-equity investment firm specializing in organizing, structuring, and sponsoring management buyouts of established companies.[8] CVC is one of the largest private equity firms in the world. Beacon Merger Sub, the entity into which BJ's was merged, is a subsidiary of Beacon Holding, which is an affiliate of LGP and CVC.[9]

B. *LGP Expresses Interest in Acquiring BJ's*

On July 1, 2010, LGP filed a Schedule 13D with the Securities & Exchange Commission (the "SEC") disclosing its 9.5% beneficial ownership of the Company's common stock and signaling its interest in a private buyout of the Company.[10] On July 7, 2010, the Company engaged Greenhill & Co., Inc. ("Greenhill") as its financial advisor to assist the Company in exploring strategic alternatives. Before August 24, 2010—when the Board formed a special committee charged with evaluating potential strategic alternatives (the "Special

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[6] *Id*. at ¶ 68 n.3.

[7] Those Defendants are: Christine M. Cournoyer ("Cournoyer"), Paul Danos ("Danos"), Edmond J. English ("English"), Helen Frame Peters ("Peters"), Leonard A. Schlesinger ("Schlesinger"), and Michael J. Sheehan ("Sheehan").

[8] At least as alleged in the Complaint, LGP was the most serious bidder until late in the sales process when it joined forces with CVC. Many of the allegations in the Complaint refer exclusively to LGP and not to the Buyout Group as a whole. In any event, that distinction does not matter here because Plaintiffs have failed to state a claim against any of the Defendants.

[9] *Id*. at ¶¶ 23-26.

[10] *Id*. at ¶ 61.

Committee")—Zarkin exclusively discussed with LGP the prospect of a going private transaction.[11] As of September 1, however, Zarkin was prohibited from communicating with LGP except under the direction of the Special Committee, which was led by Shields, and included four other directors: Schlesinger, Cournoyer, Peters, and Sheehan.[12]

By early November, Shields, allegedly at Zarkin's request, had abruptly terminated Greenhill's engagement when he decided to hire Morgan Stanley instead.[13] Discussions between LGP and the Special Committee followed in late December and early January 2011.[14] On February 3, the Company issued a press release announcing that the Board, based on the Special Committee's recommendation, had decided to explore strategic alternatives.[15]

C. *Other Expressions of Interest*

Shortly thereafter, Party A, a strategic competitor of BJ's, repeatedly expressed interest to Morgan Stanley about a potential acquisition. According to Sen, Morgan Stanley was dismissive about Party A's expression of interest because it had no prior history of acquiring domestic companies. Sen also

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[11] *Id*. at ¶¶ 66, 68.
[12] *Id*. at ¶¶ 68, 70.
[13] *Id*. at ¶¶ 67, 72. The Special Committee hired Morgan Stanley as its financial advisor on November 10, 2010.
[14] *Id*. at ¶ 75.
[15] *Id*. at ¶ 76.

characterized Party A's interest as "something to shrug off."[16] Nevertheless, the Board discussed Party A's interest during a March 7, 2011 board meeting. The next day, Morgan Stanley informed Party A that BJ's would not be comfortable sharing material, non-public information with a direct competitor at that stage. In contrast, the Board provided a confidential offering memorandum ("offering memorandum") to twenty-three private equity firms.[17]

In early April, Party A sent a letter to BJ's proposing, subject to certain conditions, to acquire it in an all-cash transaction at a purchase price in the range of $55 to $60 per share. Among other things, the letter noted that Party A had retained Gibson Dunn & Crutcher ("Gibson Dunn") as its corporate and regulatory counsel and that Party A had conducted an extensive review of the regulatory risks. The letter requested that BJ's regulatory counsel confer with Gibson Dunn, which occurred on April 15.[18] Also in response to that letter, BJ's held a meeting with representatives from Party A on April 18, 2011, which was attended by Zarkin, Sen, Shields, English, and Schlesinger. On that same day, BJ's later determined that it would not be in the best interests of the Company to pursue the expression of interest by Party A.[19] No other negotiations with Party A occurred and the

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[16] *Id*. at ¶ 78.
[17] *Id*. at ¶ 79.
[18] *Id*. at ¶ 80.
[19] *Id*. at ¶ 81.

Complaint provides no indication that Party A continued to pursue its interest in acquiring the Company.

Party B, a private equity firm, first contacted BJ's in July 2010 after LGP's Schedule 13D filing, and made further overtures to Morgan Stanley in November. Following receipt of the offering memorandum, Party B proposed a hybrid transaction that valued BJ's between $60 and $72 per share (the "recapitalization proposal"). In addition to a one-time $20 per share dividend, the recapitalization proposal called for BJ's to acquire Party B's warehouse club franchise. The Board rejected this proposal two days after receiving it. Undeterred, Party B then submitted on April 25 an all-cash proposal to buy BJ's at a price range from $50 to $53 per share. However, Party B never advanced to the final round of bidding, and none of the other four private equity firms which had expressed some interest ultimately submitted a bid.[20]

D. *LGP & CVC Complete the Buyout*

On May 8, LGP was allowed to submit a joint acquisition proposal with CVC even though the Board had previously prohibited proposed partnerships between Bain and Ares and between LGP and Party B. On June 16, Morgan Stanley received a final joint proposal from the Buyout Group to acquire the

[20] *Id*. at ¶¶ 83-86.

Company for $50 per share in an all-cash transaction.[21] At a meeting on June 20, the Special Committee rejected that offer as insufficient and countered with a $55 per share offer. In response, the Buyout Group increased its offer to $50.75 on June 23. The next day the Special Committee countered at $52.50 and the Buyout Group immediately responded with its "best and final" offer of $51.25, which the Board ultimately accepted.[22] In accepting the Buyout Group's offer, the Board relied upon Morgan Stanley's fairness opinion (the "fairness opinion").[23]

On June 28, 2011, BJ's publicly announced that it had agreed to be acquired by the Buyout Group in an all-cash, going private transaction valued at $2.8 billion or $51.25 per share (the "Merger Agreement").[24] That price represented a 6.6% premium to the $48.08 closing price of BJ's common stock on June 28, 2011, the day before BJ's publicly announced the Buyout, and a 38% premium to the closing price of BJ's common stock on June 30, 2010, the day before LGP announced its 9.5% ownership stake.[25] The Merger Agreement included various deal protection

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[21] *Id.* at ¶ 87.
[22] *Id.* at ¶¶ 88, 90.
[23] *Id.* at ¶ 89.
[24] *Id.* at ¶ 95.
[25] *Id.* at ¶¶ 95, 131. Plaintiffs attempt to discount this substantial premium by arguing that most, if not all, of this increase can be explained by changes in the market, and not the typical run-up based on merger rumors. Specifically, they argue that, as of June 20, 2011, BJ's cumulative returns since June 30, 2010 were 23.14% while the S&P 500's returns for the same period were 24.03%. *Id.* at ¶ 132. This argument has no merit. Just because the S&P 500 closely tracked the returns of BJ's, a company that had been considering strategic alternatives since at least early 2011, does not necessarily mean that BJ's returns were attributable to or caused by the overall market returns. What causes a stock price to go up (or down) is an imprecise science, one that is not reliably explained by reference to a standard market measure.

devices on behalf of the Buyout Group, including a no-shop provision that prevented the Company from soliciting a better offer, information rights, bid matching rights, a termination fee of $80 million, and a force-the-vote provision, by which BJ's was required to hold a shareholder vote on the Buyout even if it received a bona fide superior proposal.[26]

The first of the actions challenging the Buyout was filed on June 29, 2011, the day after it was announced.

The Board filed a proxy statement with the SEC on August 4, 2011. After the Plaintiffs' moved for a preliminary injunction on August 24, the proxy statement was supplemented on August 29, 2011 with additional information, including the expressions of interest by Party A and Party B and the proposals that the Buyout Group made to management on June 27, 2011.[27] A second supplementary proxy was filed on August 31, 2011.[28] As a result of these disclosures, the Plaintiffs withdrew their motion for a preliminary injunction, and the transaction was consummated on September 30, 2011.[29]

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[26] *Id*. at ¶¶ 135-38. Defendants argue that the Merger Agreement did not contain a "force the vote" provision because, while Section 6.5(b) required BJ's to proceed with a stockholder meeting even if the Board changed its recommendation, the Company had the unilateral right to terminate the agreement under Section 8.1(f). Defs.' Br. in Supp. of their Joint Mot. to Dismiss Pls.' Verified Consolidated Second Am. Class Action Compl. ("Defs.' Br.") 31 n. 24. The Court need not address this argument because the deal protection devices, even with a force the vote provision, are not unreasonably preclusive.

[27] Compl. ¶ 145.

[28] *Id*. at ¶ 147.

[29] *Id*. at ¶ 148.

E. *Shareholder Class Allegations*

In Count I of their Complaint, the Plaintiffs allege that the Defendant Directors breached, in bad faith, their fiduciary duties of loyalty and care by agreeing to a buyout that did not provide the best available value to BJ's former shareholders (the "Bad Faith Claim").[30] In support of this contention, the Plaintiffs allege that the Defendant Directors (1) were improperly motivated to support the Buyout Group; (2) intentionally shunned Party A and Party B to secure a deal with the Buyout Group; (3) knowingly ignored an inaccurate valuation analysis in the fairness opinion to create an illusion that the Company was less valuable; (4) filed a misleading and deficient proxy statement; and (5) agreed to unreasonably preclusive deal protection measures.

First, they allege that Sen and Zarkin were motivated by financial incentives and future employment to support a deal with LGP. Sen, for instance, was to receive $9 million in payments or benefits upon a change of control, and allegedly was promised, as early as January 2011, that she could remain in her current post following the Buyout.[31] As for Zarkin, he apparently sent an email to Shields the day before the Company accepted the Buyout Group's offer noting that LGP still had open questions about management's package and complaining that LGP had

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[30] *Id*. at ¶¶ 150-52.
[31] *Id*. at ¶ 103.

only offered management five percent equity.[32] With the exception of the two officer-directors (Sen and Zarkin), however, the Complaint does not allege that any of the other directors were interested in the transaction.

Second, the Plaintiffs allege that the Board, led by Sen and Zarkin, shunned Party A (in favor of a deal with LGP) despite its superior offer of $55 to $60 per share. As objective evidence of bad faith, the Plaintiffs point to the fact that the Board (1) did not share non-public information with Party A, as it did with the private equity suitors, and (2) dismissed Party A's proposal in a mere ten days, demonstrating that BJ's could have done more to resolve the regulatory obstacles to that offer.[33] The Plaintiffs similarly allege that the Board spurned Party B and its recapitalization proposal valued at more than $60 per share.[34]

Third, the Plaintiffs allege that the Board justified its acceptance of an inferior offer by (1) knowingly relying upon improper assumptions and valuation metrics employed by Morgan Stanley in its fairness opinion[35] and (2) intentionally and improperly lowering the Company's own financial projections.[36] As to the fairness opinion, the Complaint disagrees with various assumptions utilized by Morgan Stanley. The Plaintiffs argue that these "errors" were so blatant that the Board knew that the fairness opinion was inaccurate and misrepresented the true

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[32] *Id*. at ¶ 93.
[33] *Id*. at ¶ 108.
[34] *Id*. at ¶ 87.
[35] *Id*. at ¶ 109.
[36] *Id*. at ¶ 116.

value of the Company. For instance, the Plaintiffs argue that the terminal growth rate of 2.8% used in the discounted cash flow analysis undervalued the Company and that Morgan Stanley should have used 4.0% as the growth rate because that was the projected long-term growth rate in the United States.[37] The Complaint also disagrees with Morgan Stanley's comparisons in its public company analysis. Instead of comparing BJ's to only other membership warehouse clubs—such as Sam's Club and Costco—the Plaintiffs claim that it improperly compared BJ's to two supermarkets, which do not receive membership fees. The improper inclusion caused the group average multiple to be lower, resulting in a lower valuation of the Company.[38]

As to the Company's own financial projections, the Plaintiffs allege that Sen modified its five-year plan projections immediately after LGP's initial expression of interest in order to paint a less "rosy" picture of the Company's future outlook.[39] Sen allegedly manipulated the numbers to facilitate a deal with LGP. The Plaintiffs also point to the fact that cash flow projections used by Morgan Stanley were significantly lower than those utilized in a May 2011 presentation by BJ's management.[40] They also allege that the Board knew that the fairness opinion did

[37] *Id*. at ¶ 113. Plaintiffs also argue that the 2.8% terminal growth rate is "nonsensical" considering that Morgan Stanley assumed BJ's would grow its free cash flows by 20% in 2015, 17% in 2016, and then drop to 2.8% in 2017, and thereafter. *Id*. at ¶ 114.
[38] *Id*. at ¶¶ 118-19.
[39] *Id*. at ¶¶ 62-65.
[40] *Id*. at ¶ 116.

not include the efficiencies related to the information technology system, and therefore, did not properly value the Company.[41]

In further support of the Plaintiffs' allegations that BJ's shareholders should have received a higher price and that the Board knew that the Company was worth more than $51.25 per share, they cite various analyst reports and commentary suggesting that BJ's fair value was at least $55 per share and as high as $60 per share.[42]

Fourth, the Plaintiffs contend that the Board, although it eventually acquiesced in disclosing all of the Plaintiffs' requested disclosures, exhibited bad faith by issuing initially a misleading and inaccurate proxy statement.[43] Finally, the Plaintiffs allege that the deal protection devices, when considered collectively, unreasonably limited the Board's ability to pursue alternative superior transactions.[44]

In Count II of their Complaint, the Plaintiffs claim that the Buyout Group knowingly participated in, and thereby aided and abetted, the Defendant Directors' breach of their fiduciary duties (the "Aiding and Abetting Claim").[45] Specifically, the Plaintiffs assert that the Buyout Group rendered "substantial assistance to the

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[41] *Id*. at ¶ 117.
[42] *Id*. at ¶¶ 121-30.
[43] *Id*. at ¶¶ 143-44.
[44] *Id*. at ¶¶ 135-42.
[45] *Id*. at ¶¶ 155-60.

Defendant Directors in their breaches of their fiduciary duties to BJ's former shareholders."[46]

II. ANALYSIS

A. *Applicable Standard*

Before the Court is Defendants' motion to dismiss the Complaint. "Pursuant to [Court of Chancery] Rule 12(b)(6), this Court may grant a motion to dismiss for failure to state a claim if a complaint does not assert sufficient facts that, if proven, would entitle the plaintiff to relief."[47] "[T]he governing pleading standard in Delaware to survive a motion to dismiss is reasonable conceivability."[48]

> When considering a defendant's motion to dismiss, a trial court should accept all well-pleaded factual allegations in the Complaint as true, accept even vague allegations in the Complaint as 'well-pleaded' if they provide the defendant notice of the claim, draw all reasonable inferences in favor of the plaintiff, and deny the motion unless the plaintiff could not recover under any reasonably conceivable set of circumstances susceptible of proof.[49]

While the Plaintiffs have repeatedly emphasized (in their briefs and at oral argument) that this standard is a minimal one, the Court will not credit conclusory allegations or draw unreasonable inferences in favor of the Plaintiffs.[50] If the complaint states facts that could explain otherwise inexplicable bad faith conduct,

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[46] *Id*. at ¶ 159.
[47] *In re Alloy, Inc. S'holder Litig.*, 2011 WL 4863716, at *6 (Del. Ch. Oct. 13, 2011).
[48] *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Hldgs. LLC,* 27 A.3d 531, 537 (Del. 2011).
[49] *Id.* at 536 (citation omitted).
[50] *In re Alloy, Inc.,* 2011 WL 4863716, at *6 (quoting *Price v. E.I. DuPont de Nemours & Co., Inc.,* 26 A.3d 162, 166 (Del. 2011)).

the Court will not ignore those reasonable explanations.[51] However, a motion to dismiss will be denied "as long as there is a reasonable possibility that a plaintiff could recover."[52]

B. *The Bad Faith Claim*

A fundamental principle of Delaware law is that directors of a corporation manage and direct the business and affairs of the company.[53] "In exercising these powers, directors are charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders."[54] When directors decide to engage in a change of control transaction, their fiduciary duties of loyalty and care require that they seek to maximize the sale price of the enterprise.[55]

Where, as here, a corporation's certificate of incorporation contains an exculpatory provision authorized by 8 *Del. C.* § 102(b)(7), which immunizes directors from damages arising from a breach of the duty of care, plaintiffs must "plead sufficient facts to show that *a majority of the Board of Directors* breached

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[51] *Id.*, 2011 WL 4863716, at *7.

[52] *Hamilton P'rs, L.P. v. Highland Capital Mgmt., L.P.,* 2012 WL 2053329, at *2 (Del. Ch. May 25, 2012); *see In re Alloy, Inc.,* 2011 WL 4863716, at *6 (citing *Cent. Mortg. Co.,* 27 A.3d at 537 n. 13) ("Delaware's reasonable 'conceivability' standard asks whether there is a 'possibility' of recovery.").

[53] 8 *Del. C.* § 141(a).

[54] *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993).

[55] *See Malpiede v. Townson*, 780 A.2d 1075, 1083 (Del. 2001) (citing *Revlon, Inc. v. MacAndrews & Forbes Hldgs., Inc.*, 506 A.2d 173, 182-83 (Del. 1986)).

the fiduciary duty of loyalty."[56] Accordingly, the Defendant Directors "are entitled to dismissal unless the [P]laintiffs have pled facts that, if true, support the conclusion that the [Defendant Directors] failed to secure the highest attainable value as a result of their own bad faith or otherwise disloyal conduct."[57] As applied to this case, the facts alleged in the Complaint must show that (1) a majority of the Board was not both disinterested and independent or (2) "that the [Board] did not act in good faith."[58]

First, the Plaintiffs have not pleaded facts sufficient to show that the Board was not disinterested and independent. Under Delaware law, "[a] director is considered interested where he or she will receive a personal financial benefit from a transaction that is not equally shared by the stockholders."[59] That benefit must be "significant enough 'in the context of the director's economic circumstances, as to have made it improbable that the director could perform her fiduciary duties to the . . . shareholders without being influenced by her overriding personal interest.'"[60] "Independence means that a director's decision is based on the

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[56] *In re NYMEX S'holder Litig.*, 2009 WL 3206051, at *5 (Del. Ch. Sept. 30, 2009).
[57] *McMillan v. Intercargo Corp.*, 768 A.2d 492, 502 (Del. Ch. 2000).
[58] *In re Alloy, Inc.*, 2011 WL 4863716, at *7.
[59] *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993) (citing *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984)).
[60] *Orman v. Cullman*, 794 A.2d 5, 23 (Del. Ch. 2002) (italics omitted) (quoting *In re Gen. Motors Class H S'holders Litig.*, 734 A.2d 611, 617 (Del. Ch. 1999)).

corporate merits of the subject before the board rather than extraneous considerations or influences."[61]

In their Complaint, the Plaintiffs did not seriously challenge the disinterestedness and independence of the Board. The Buyout was approved by all nine of BJ's directors. The Complaint fails to make any allegations that six of the directors were interested. Four of the six concededly disinterested directors were members of the Special Committee that ultimately recommended the transaction (Schlesinger, Cournoyer, Peters, and Sheehan). The two other disinterested directors were Danos and English. The Plaintiffs also did not make any well-pleaded allegations that the six disinterested directors were somehow dominated or controlled by the two allegedly interested directors (Zarkin and Sen).[62] As for Shields, the Complaint only cursorily challenges his independence from Zarkin and Sen.[63]

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[61] *Aronson*, 473 A.2d at 816.

[62] The Court need not determine whether Zarkin and Sen were in fact interested, although the Court acknowledges that they, as officers of the Company, had a significant interest in continued employment and the receipt of significant benefits conditioned upon a change of control transaction.

[63] The Complaint alleges that Shields has "nearly twenty years of Board service alongside Zarkin and a long-term relationship with Sen." Compl. ¶ 68. This type of allegation does not raise a reasonable doubt as to the independence of a director under Delaware law. *See Beam v. Stewart*, 845 A.2d 1040, 1050-52 (Del. 2004) (directors were independent despite having longstanding personal and professional relationships to allegedly interested directors).

The Plaintiffs offer conclusory allegations that management (supposedly Sen and Zarkin) influenced the Company's disinterested directors,[64] but the Complaint lacks any facts buttressing that conclusion. Without more, the Court is not persuaded that the balance of the Board is beholden to management or that management controls and directs the corporation to the exclusion of the Board—a position contrary to the fundamental structure of corporations.[65] Thus, the Plaintiffs have not pleaded a duty of loyalty claim against the Defendant Directors arising from any disabling interest or lack of independence.

Second, "bad faith will be found if a 'fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties.'"[66] The Delaware Supreme Court has emphasized that an "extreme set of facts" is "required to sustain a disloyalty claim premised on the notion that

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[64] Compl. ¶ 2 ("Board . . . acted in bad faith by yielding to the will of self-interested management"), ¶ 69 ("all significant decisions concerning the Company's evaluation of strategic alternatives were made by the Board, along with members of BJ's management"), ¶ 93 ("The obvious reason the Board approved the takeover is because it was influenced by management").

[65] *See In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 808, 821 (Del. Ch. 2005), *aff'd*, 906 A.2d 766 (Del. 2006) ("The board is dominated by outsiders. Eleven of the twelve directors are not employees of JPMC. Harrison [the CEO of JPMC] cannot fire any of them. Additionally, Harrison is not a controlling stockholder of JPMC and therefore has no power to oust them as directors through a stockholder vote. On the contrary, it is the eleven outside directors who collectively have the power to dismiss Harrison and the rest of his management team. The plaintiffs allege that the defendant directors are beholden to Harrison, but they fail to demonstrate why that is so. Even in cases in which the CEO had a supermajority of voting power, courts have upheld outside directors' independence in the face of additional relationships. Here, Harrison reports to a board of directors that he cannot fire or remove, a fact that appears lost in the allegations that each director, no matter how indirectly, has some external relationship to JPMC.") (footnote omitted).

[66] *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 243 (Del. 2009) (quoting *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 67 (Del. 2006)).

disinterested directors were intentionally disregarding their duties."[67] A breach of the duty of loyalty may also exist, notwithstanding approval by a majority of disinterested and independent directors, "where the decision under attack is so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[68]

The Complaint does not allege facts that support a reasonable inference that the Board consciously disregarded its so-called *Revlon* duties. Indeed, the conduct of the Board and the Special Committee, as described in the Complaint, militates against such a claim. For instance, the Board met regularly to discuss strategic alternatives and formed an independent Special Committee to steer the process. The Special Committee retained its own financial and legal advisors, conducted a publicized review of strategic alternatives, and met with every party which made a serious overture. As important, after receiving only one formal offer for $50 per share, the Board drove the price up before agreeing to the Buyout Group's "best and final offer" of $51.25. The Board relied upon Morgan Stanley's opinion that the price was fair. It also negotiated some favorable deal terms, including a fiduciary out clause and a reverse termination fee. These actions sufficiently counter any inference that the Defendant Directors "utterly failed to attempt to

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[67] *Lyondell Chem. Co.*, 970 A.2d at 243 (internal quotation marks omitted) (quoting *In re Lear Corp. S'holder Litig*., 967 A.2d 640, 654-55 (Del. Ch. 2008)).
[68] *In re Alloy, Inc.*, 2011 WL 4863716, at *7 (internal quotation marks omitted).

obtain the best sale price."[69] Therefore, in order for the Plaintiffs to succeed on a claim that the Board acted in bad faith, they must allege that the decision to sell the Company was "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[70]

1. <u>The Board's Treatment of Party A and Party B</u>

First, the Plaintiffs generally contend that the Board exhibited bad faith when it did not sufficiently explore preliminary expressions of interest from Party A and Party B. As an initial matter, allegations that the Board should have done more, even if supported by well-pleaded facts, would, at best, only support a duty of care claim. A complaint that criticizes the "Special Committee for not evaluating fully alternative transactions . . . does not support an inference that the Special Committee acted disloyally or in bad faith."[71] To the extent that the Plaintiffs' allege that the Board's treatment of Party A and Party B was in bad faith, those allegations are not supported by facts in the Complaint sufficient to draw a reasonable inference of bad faith.

The Plaintiffs' contention that the Board acted in bad faith by summarily rejecting Party B's recapitalization proposal that valued BJ's shares between $60 and $72 does not support a reasonable inference that the Board acted disloyally.

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[69] *Lyondell Chem. Co.*, 970 A.2d at 244.
[70] *In re Alloy, Inc.*, 2011 WL 4863716, at *10 (internal quotation marks omitted).
[71] *Id.* at *8.

The Board was considering the sale of the Company, not the purchase of Party B's affiliate. It had no obligation under its *Revlon* duties to pursue this fundamentally different proposal based upon Party B's speculative estimation of what the value of such a transaction would be worth to BJ's shareholders. Thus, the Board's rejection of this different proposal in only two days supports no inference that it acted in bad faith. The Complaint also does not carry an inference that the Board treated Party B different from LGP or any other bidders. Party B was given access to BJ's confidential information and the opportunity to submit formal bids after completing its due diligence. Although Party B submitted a preliminary proposal to acquire BJ's for between $50 and $53 per share, it never submitted a formal bid, and never offered to top the Buyout Group's best and final offer.[72]

Furthermore, the Plaintiffs' contention that the Board acted in bad faith by shunning Party A also fails for similar reasons. As recited in the Complaint, Morgan Stanley was "dismissive" about Party A's expression of interest and Sen characterized that expression of interest as "amusing" or "something to shrug off."[73] That the proxy statement failed to disclose Party A's interest, and even disclosed inaccurately that there was no interest from a strategic buyer, is evidence, the Plaintiffs argue, that the Defendant Directors were attempting to hide Party A's

[72] *See* Compl. ¶¶ 82-86.
[73] Compl. ¶ 78.

interest and somehow thwart its opportunity to acquire BJ's.[74] The Board also allegedly acted in bad faith when it directed Morgan Stanley to solicit interest only from private equity firms. Consequently, the offering memorandum was not shared with Party A, while it was shared with twenty-three private equity firms. The Plaintiffs further contend that the Board acted in bad faith when, after only ten days, it decided not to pursue Party A's preliminary expression of interest (valued in a range of $55 to $60 per share) due supposedly to regulatory concerns.[75]

Morgan Stanley's dismissive disposition toward Party A and Sen's characterization of Party A's interest, as told to her by a banker at Morgan Stanley, does not support a reasonable inference that the Board acted in bad faith. First, why the Court should attribute Morgan Stanley's attitude toward Party A to Sen, the Special Committee or the Board is not adequately pleaded in the Complaint. Even assuming that Sen believed and communicated to the Board that Party A's interest was "something to shrug off," her statement is not necessarily indicative of bad faith. Nor does it reasonably show the Board's disposition toward Party A as a

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[74] Pls.' Answering Br. in Opp'n to Defs.' Joint Mot. to Dismiss Pls.' Verified Consolidated Second Am. Class Action Compl. ("Pls.' Answering Brief") 8-9.

[75] In its recent opinion, *In re Novell, Inc. S'holder Litig.*, 2013 WL 322560 (Del. Ch. Jan. 3, 2013), the Court held that the Novell's board's unexplained disparate treatment of a bidder to acquire the company was explicable only as bad faith. *Id.* at *10. In contrast, the Board's disparate treatment of Party A is explained by facts in the Complaint that tend to show that the Board's actions were reasonable under the circumstances. Perhaps the crucial difference is that in *Novell* the board's actions, which resulted in an asymmetrical distribution of information, occurred after the board had determined that the bidder was a serious participant. In this case, however, the Board was making an initial assessment, in its business judgment, whether pursuit of Party A's expression of interest was in the best interest of the Company and whether a transaction with Party A raised serious regulatory issues.

possible acquirer. Something of a negative attitude toward a competitor is not unusual. Second, and more importantly, the Defendant Directors had no reason not to rely upon Morgan Stanley's advice that strategic buyers, including Party A, would not likely be interested or that their interest would not likely lead to a serious offer.[76] Thus, even if the Board had adopted an indifferent attitude toward Party A, that attitude would not have been unreasonable given the fact that Party A, according to Morgan Stanley, had no history of acquiring domestic companies. At the very least, any judgment that the Board did make that Party A was not a serious bidder was not "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[77]

Similarly, the Board's decision not to share confidential information with Party A does not raise an inference of bad faith. Because Party A was one of only two direct channel competitors to BJ's, the Board could reasonably have had concerns about sharing confidential business information with a competitor, especially where, as here, the seriousness of Party A's interest was in doubt. That

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[76] *See* Compl. ¶ 74; Transmittal Affidavit of P. Bradford deLeeuw, Esq. ("deLeeuw Aff."), Ex. A (Sen Dep. Tr.) at 82 ("Q. Okay. What did he tell you? A. He told me [Party A] called, and at that time he thought it was mildly amusing, insofar as they have some sort of M&A group in Party A; and they don't do domestic M&A, have no history of doing domestic M&A, and he thought that that was almost, you know, something to shrug off."); Pls.' Answering Br. 7-8. As this testimony makes clear, Sen was describing what a banker at Morgan Stanley had told her, not necessarily her own firsthand knowledge of Party A's interest.

[77] *In re Alloy, Inc.*, 2011 WL 4863716, at *10 (internal quotation marks omitted).

decision, therefore, was also not "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[78]

The Board's decision not to pursue further an acquisition transaction with Party A after it made a preliminary expression of interest is also not supported by facts necessary to sustain a duty of loyalty claim. Just the opposite of bad faith, the Board's conduct, as alleged in the Complaint, seems entirely reasonable. Although its offer for BJ's shares was higher than any previous offer, Party A's proposal was subject to further due diligence and regulatory analysis that would require "non-public information to be provided by BJ's management."[79] In response to Party A's request, the Special Committee directed its legal counsel to confer with Party A's regulatory advisors. A few days later, members of the Board met with representatives from Party A to discuss a potential transaction and the antitrust risks. Thereafter, the Board determined that it would not be in the best interests of the Company and its shareholders to pursue a transaction with Party A.[80]

Contrary to the Plaintiffs' contention, the Board did not summarily reject Party A's offer without due consideration. Rather, the only reasonable inference

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[78] *Id.* (internal quotation marks omitted).
[79] Defs.' Br. Ex. 5 (Letter from Party A), at 2. Plaintiffs rely on and selectively quote from both Morgan Stanley's March 8, 2011 email to Party A (Compl. ¶¶ 79-80) and Party A's April letter to BJ's outlining its proposal (Compl. ¶ 80). "When a plaintiff expressly refers to and heavily relies upon documents in her complaint, these documents are considered to be incorporated by reference into the complaint." *Freedman v. Adams*, 2012 WL 1345638, at *5 (Del. Ch. Mar. 30, 2012). Accordingly, both documents will be considered incorporated by reference to the Complaint and may be considered by the Court.
[80] Compl. ¶ 81.

that can be drawn from these facts is that the Board had legitimate concerns about the potential antitrust risks inherent in a transaction between two of the three largest players in the warehouse club industry.

> The need for potential regulatory approvals relating to antitrust considerations presents a legitimate risk factor for the Board to consider in determining whether a proposed transaction would maximize stockholder value. If regulatory approval is denied or drawn out in a costly delay, then a higher bid price does not necessarily mean a greater return for stockholders.[81]

The antitrust risks here were self-evident. Those concerns were considered by the Board and informed by legal advisors. Accordingly, the Board's decision is entitled to a presumption of good faith.[82]

The Plaintiffs have failed to rebut that presumption. Without more, the Plaintiffs' argument that the Board should have done more to resolve the regulatory concerns does not implicate bad faith. Moreover, the Complaint fails to

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[81] *In re Cogent, Inc. S'holder Litig.*, 7 A.3d 487, 512 (Del. Ch. 2010); *see also In re J.P. Stevens & Co., Inc. S'holders Litig.*, 542 A.2d 770, 781 n. 6 (Del. Ch. 1988) ("That, of course, does not mean that material factors other than 'price' ought not to be considered and, where appropriate, acted upon by the board. Such consideration might include form of consideration, timing of the transaction or risk of non-consummation. Thus, although it hardly needs to be said, the Special Committee was entirely justified in considering any legitimate threat that the antitrust laws posed to the consummation of any West Point proposal.").

[82] *See McMillan*, 768 A.2d at 505 n. 55 ("The board's reliance upon an investment banker (whose independence and qualifications are not challenged in the complaint) is another factor weighing against the plaintiffs' ability to state an actionable claim that the defendant directors breached their fiduciary duties by failing to secure the highest value reasonably attainable."); 8 *Del. C.* § 141(e). To the extent that the Board reasonably relied upon its legal advisors, such reliance is entitled to the same effect as a board's reliance upon an investment banker's fairness opinion. Because the Plaintiffs have not challenged the independence, qualifications, or legal advice of the Board's legal counsel, they have not rebutted the presumption that the Defendant Directors acted in good faith. For the same reasons, the Court need not examine the likelihood that the transaction would have stalled because of regulatory issues.

allege a bad faith motive for why a disinterested majority of the Board would use regulatory concerns as a pretext for shunning Party A in favor of the Buyout Group. As this Court has stated before, "the absence of an illicit directorial motive and the presence of a strong rationale for the decision . . . makes it difficult for a plaintiff to state a loyalty claim."[83] Finally, that it took only ten days for the Board to decide against attempting a transaction with Party A states, at best, a duty of care claim.[84] Delaware law does not require that a board consider a proposal for a certain length of time.[85] Thus, the Board's decision to terminate discussions with Party A was not "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[86]

2. Manipulation of the Sales Process

Second, the Plaintiffs allege that the self-interested directors Sen and Zarkin[87] manipulated the sales process in favor of the Buyout Group and that the

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[83] *In re Lear Corp. S'holder Litig.*, 967 A.2d at 654 n.62.
[84] The Court does not decide whether these allegations state a duty of care claim. The Court acknowledges, however, that the Board received legal counsel, met with senior representatives of Party A, and had known about and presumably discussed Party A's interest for some time before Party A's proposal.
[85] *See Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1286 (Del. 1989). "[T]here is no single blueprint that a board must follow to fulfill its duties . . . a board's actions must be evaluated in light of relevant circumstances to determine if they were undertaken with due diligence and in good faith. If no breach of duty is found, the board's actions are entitled to the protections of the business judgment rule." *Id.*
[86] *In re Alloy, Inc.*, 2011 WL 4863716, at *10 (internal quotation marks omitted).
[87] For purposes of this analysis, the Court assumes that Sen and Zarkin were interested in the Buyout.

remaining Defendant Directors knowingly acquiesced.[88] Because of this self-interest, the Plaintiffs allege that Sen and Zarkin conspired to sell the Company to LGP. They also allege that Sen, shortly after LGP first expressed interest in acquiring BJ's, revised sales downward in the Company's five-year plan to make it appear more pessimistic. For his part, Zarkin began communicating with LGP in the months before the Board formed the Special Committee, despite the Company's retention of Greenhill as its financial advisor. This initial conduct allegedly set the stage for the *pro forma* sales process that followed.[89] Then, cutting short Greenhill's engagement, Zarkin, through Shields, handpicked Morgan Stanley, which, in concert with their plans, immediately dismissed the possibility that strategic buyers would be interested in acquiring BJ's.[90] The Complaint also alleges that during discussions with LGP that Zarkin and Sen sought and obtained material benefits for themselves, including equity interests in the new private

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[88] According to the Plaintiffs, Sen had a significant financial incentive to promote the sale of the Company because she would receive more than $9 million in potential payments and benefits upon a change of control. Sen was supposedly further conflicted because she was informed, perhaps as early as January 2011, that she would be retained to run LGP's post-takeover business. Her interest in future employment, however, allegedly only applied to financial buyers because, unlike strategic acquirers, they typically retain management following a buyout. *See* Defs.' Br. Ex. 5, at 1; *see supra* note 62 (This may not be true in this case. Party A's proposal stated: "We view the Company's management team and employees as significant assets and would expect to retain a significant portion of the existing team following the consummation of this transaction."). As for Zarkin, the Plaintiffs allege that because he was a consultant to Sen and senior management at BJ's, he could expect to retain his role following the sale of the Company. Compl. ¶ 75. Zarkin also allegedly had an interest in promoting the best interests of Sen because of his long-term professional relationship with her.
[89] Compl. ¶¶ 66-67, 71.
[90] *Id.* at ¶ 74.

company. In sum, the Plaintiffs would have this Court hold that it is reasonably conceivable that the Defendant Directors' year-long sales process, in which they solicited over twenty-three buyers, and met with all interested acquirers, was nothing but "window dressing" to legitimize the Company's sale to the Buyout Group at a wholly disproportionate price.

Allegations that the Defendant Directors manipulated the sales process are largely unsubstantiated by facts in the Complaint. Moreover, they are belied by a year-long sales process, reasonable explanations for the Board's conduct with respect to Parties A and B, and the fact that the Buyout was ultimately approved by a majority of disinterested and independent directors. The Plaintiffs' remaining arguments in support of a sham sales process also fall short. The Plaintiffs make much of the fact that Zarkin communicated with LGP prior to the formation of the Special Committee, but that does not provide an inference of bad faith. "It is well within the business judgment of the Board to determine how merger negotiations will be conducted, and to delegate the task of negotiating to the Chairman."[91] The Plaintiffs also do not explain why the disinterested and independent directors would disregard their fiduciary duties in order to secure Sen's future employment. The Board's adjustment to the five-year plan, even assuming that the timing of the

[91] *In re NYMEX S'holder Litig.*, 2009 WL 3206051, at *7.

adjustment is suspicious,[92] does not square with the Plaintiffs' bad faith theory: the adjustment took place months before Party A entered the negotiations and could not have favored the Buyout Group because the private equity bidders had access to the same confidential information as the Buyout Group. In short, the Plaintiffs have failed to allege how Sen's and Zarkin's personal interest in the Buyout caused a majority of independent and disinterested directors to shirk their fiduciary duties.

The Plaintiffs rely heavily on the Court's decision in *In re Answers Corporation Shareholders Litigation* to support their theory that the sales process was manipulated.[93] In *Answers*, the complaint alleged that the board consciously acquiesced in the desire of three interested directors to expedite the sales process so that the merger agreement could be consummated before the company's stock price rose above the bidder's offer.[94] It did so apparently to aid one director who "knew that he would lose his job as Answers' President and CEO if he did not sell the Company" and to help two directors who "sought a sale of the Company in order to achieve liquidity for" their separate company, a significant shareholder of Answers.[95] The Court held that it was reasonably conceivable that the board

[92] Plaintiffs would have this Court draw inferences of bad faith from comparing the optimistic statements made by Sen in the Company's 2010 Annual Report with her decision to modify the internal sales projections in the five-year plan in August 2010. Pls.' Answering Br. 15-16. That inference is too tenuous.
[93] 2012 WL 1253072 (Del. Ch. Apr. 11, 2012).
[94] *Id*. at *7-8.
[95] *Id*. at *7.

breached its duty of loyalty by depriving the company's shareholders of the increased stock price as a standalone company.[96]

Unlike in *Answers*, however, where the company's financial advisor warned that its increasing stock price might derail the proposed deal,[97] here there was no reasonable indication or certainty that BJ's stock price would soon rise above the offer price. Moreover, unlike *Answers*, where the board allegedly "agreed to speed up the sale process" to ensure consummation of the deal, [98] there are no allegations that the Board agreed to sell the Company quickly with knowledge that a superior offer was likely or with a reasonably certain standalone prospect that offered a higher value than the Buyout Group's final offer. The Plaintiffs' reliance on *Answers* is therefore unavailing.[99]

3. <u>The Board's Reliance on Morgan Stanley's Fairness Opinion</u>

The Plaintiffs next argue that the Defendant Directors knowingly (1) approved the Buyout at an unfair price and (2) relied upon an inaccurate analysis of BJ's value in Morgan Stanley's fairness opinion. In support of these claims, the Plaintiffs make various arguments. First, they cite an April 18, 2011

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[96] *Id*. at *8.
[97] *Id*. at *3.
[98] *Id*. at *8.
[99] In denying reconsideration of the *Answers* decision, the Court noted that the "case [was] not typical," stating: "[m]ost cases do not involve a company's board speeding up a sales process to get a deal done because the company's investment advisor had told the board that, with a failure to act quickly, the market will learn the company is worth more than the deal price and the deal will be scuttled." *In re Answers Corp. S'holders Litig.*, 2012 WL 3045678, at *2 (Del. Ch. July 19, 2012).

presentation to the Board in which management stated that it was confident of its ability to develop and execute a strategic plan that would deliver more than an 11% premium (a share price of $52) to shareholders over the long-term.[100] Second, the Complaint alleges that the Board knew that Morgan Stanley's terminal growth rate assumption of 2.8% in its discounted cash flow analysis was "nonsensical" given that the long-term growth rate projection for the United States economy was roughly 4.0%.[101] Third, the Complaint alleges that the Board knowingly provided Morgan Stanley with financial projections that were negatively adjusted and that did not account for efficiencies related to the information technology system, undermining Morgan Stanley's estimated value of the Company.[102] Fourth, the Complaint alleges that the Board knew that Morgan Stanley's use of supermarket comparables in its public company analysis was inappropriate because supermarkets have significantly lower earnings multiples than membership warehouse companies like BJ's.[103] Finally, the Plaintiffs allege that the Board knew that Morgan Stanley's analysis was flawed because various third-party analysts had valued the Company at a higher price.[104]

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[100] Compl. ¶ 91.
[101] *Id*. ¶¶ 110-15.
[102] *Id*. at ¶¶ 116-17.
[103] *Id*. at ¶¶ 118-19.
[104] *Id*. at ¶ 120.

First, management's April 18, 2011 presentation to the Board does not offer enough to infer that the Defendant Directors knew that the fairness opinion, issued in June 2011, was flawed. The Complaint offers no facts which suggest that the Board was not skeptical to some extent of management's aspirational, forward-looking statements. Moreover, assurances, however confident, of future performance are inherently speculative and easily modified in light of changing business circumstances. Thus, the inference that the Plaintiffs would have this Court draw is untenable.

Second, the Plaintiffs suggest that the Board's reliance on the 2.8% terminal growth rate (*i.e.*, an allegedly nonsensical assumption) is only explicable as bad faith. But there is no reason, that the Plaintiffs offer or that the Court can surmise, why the Board must have known that the proper terminal rate was at least 4.0%, as the Plaintiffs claim.[105] The Defendant Directors may have simply relied upon Morgan Stanley's analysis. For purposes of stating a duty of loyalty claim, what the Defendant Directors *should have known* is substantively less culpable, for liability purposes, than what they *actually knew*. It is not inconceivable, or perhaps that unlikely, that a director, relying in good faith on an expert, could accept and rely upon a misguided assumption in the expert's financial analysis, without

[105] Terminal values by their nature reflect growth rate estimates of future earnings, but, therefore, are also speculative in nature. Determining what constitutes an unreasonable estimation or speculation is not something this Court, or perhaps even a financial practitioner, can easily discern.

necessarily knowing of that error. So, even accepting that the 2.8% terminal rate was nonsensical, the Plaintiffs have only pleaded facts suggesting that the Board should have known that the rate was improper, not that they actually knew that it was. Accordingly, this alleged flaw in the fairness opinion does not raise an inference of bad faith.

Third, the Plaintiffs' argument that the Board knowingly provided Morgan Stanley with pessimistic financial projections is not supported by the Complaint. The Plaintiffs allege that Morgan Stanley was given and used lower financial projections than management had used in a May 2011 presentation.[106] But that alone does not provide a reasonable inference that the Board knew that the financial projections used by Morgan Stanley were inappropriate. Similarly, Sen's alleged downward adjustment to the five-year-plan in August 2010 also does not support a reasonable inference that the Board knew that Morgan Stanley used inappropriate financial projections in its fairness opinion issued ten months later.

For similar reasons, the Plaintiffs' remaining arguments also do not support a loyalty claim. While the Plaintiffs quibble with Morgan Stanley's use of supermarkets in its public company analysis, they fail to allege that the Board actually knew that the analysis resulted in an incorrect fairness opinion. Moreover,

[106] Compl. ¶ 116.

the Board had no reason not to rely upon Morgan Stanley as its valuation expert.[107] The Plaintiffs' final argument, that the Board knew BJ's was worth more based on third-party analysts' price targets, overlooks the fact that (1) those analysts' estimates were not based on the confidential business information provided to the Buyout Group and available to the Board and (2) no other bidders offered (after nearly a year-long sales process) a higher bid.

4. Misleading & Inaccurate Proxy Statement

According to the Plaintiffs, the Board acted in bad faith when it issued a misleading and inaccurate proxy statement. Specifically, they contend that the Board purposefully attempted to conceal Party A's interest in purchasing BJ's from its shareholders. Except for conclusory allegations, however, the Complaint "pleads nothing reasonably supportive of the proposition that any omission from the merger proxy statement resulted from disloyalty (including bad faith) on the part of the [D]efendant [D]irectors."[108] The closest the Plaintiffs come to alleging bad faith is not based on the Complaint, but is taken from the Company's proxy

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[107] To the extent that the Plaintiffs argue that the improper assumptions and valuation metrics in the fairness opinion support a claim for bad faith, that argument may be further precluded by 8 *Del. C.* §141(e), which creates a protection for directors "in relying in good faith upon" an expert's report. The Plaintiffs have not alleged any facts that raise an inference that the Board did not rely upon Morgan Stanley in good faith or that it did not exercise reasonable care in selecting Morgan Stanley as its financial advisor. *See* 8 *Del. C.* §141(e). That, coupled with the fact that Plaintiffs have not raised a reasonable inference that the Board relied on "what it knew was an inaccurate analysis," strongly supports the Court's conclusion that the Complaint does not adequately allege that the Board did knowingly sell BJ's at an unfair price. *In re Celera Corp. S'holder Litig.*, 2012 WL 1020471, at *25 (Del. Ch. Mar. 23, 2012), *aff'd in part, rev'd in part*, 2012 WL 6707736 (Del. Dec. 27, 2012).

[108] *McMillan*, 768 A.2d at 499.

statement, which the Plaintiffs quoted in their answering brief.[109] The Plaintiffs are seemingly correct that the proxy statement inaccurately disclosed that the Company's "public announcement of its strategic review process had elicited no indications of interest from strategic buyers" when in fact a strategic buyer—Party A—had expressed interest. Although knowingly issuing an inaccurate proxy statement is conduct that may qualify as bad faith under Delaware law,[110] drawing that inference is not warranted here. First, the Complaint contains no facts suggesting that the false statement was material or would have otherwise affected a shareholder's vote. Tellingly, even after disclosing Party A's interest, BJ's shareholders almost unanimously approved the Buyout. Second, the Company's subsequent truthful revision mitigates against a finding of bad faith. Thus, the Plaintiffs' disclosure allegations do not support a reasonable inference of bad faith.

5. <u>Deal Protection Devices</u>

The Plaintiffs also allege that the Board acted in bad faith by agreeing to a combination of deal protection devices that collectively and unreasonably

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[109] "The Proxy states that on March 7, 2011, '[a]fter reviewing a list of possible strategic buyers, the board also determined that no strategic buyers should be solicited in view of the low likelihood that any of them would be interested in pursuing an acquisition of the Company [and] the fact that the Company's public announcement of its strategic review process had elicited no indications of interest from strategic buyers to acquire the entire Company.'" Pls.' Answering Br. 8-9. The Plaintiffs claim that the latter part of this statement was blatantly inaccurate, as Party A had indicated interest in the Company.

[110] *In re Walt Disney Co. Deriv. Litig.*, 907 A.2d 693, 754 (Del. Ch. 2005), *aff'd*, 906 A.2d 27 (Del. 2006) ("one cannot act loyally as a corporate director by causing the corporation to violate the positive laws it is obliged to obey").

precluded a higher bid. The allegedly preclusive devices in the Merger Agreement were: a "no-shop" provision,[111] matching and information rights,[112] a termination fee representing 3.1% of the deal value,[113] and a "force-the-vote" provision.[114] However, under Delaware law, these deal protection measures, individually or cumulatively, have routinely been upheld as reasonable, especially where, as here, the Board negotiated a $175 million reverse termination fee and obtained a fiduciary out clause.[115] The Plaintiffs do not contest this point of law. Instead, they quote *In re Answers Corporation Shareholders Litigation* for the proposition that, although this claim may not have "independent viability," it should not be dismissed here because it may "increase Plaintiffs' recovery" if the Court ultimately finds a breach of fiduciary duty.[116] Because the Plaintiffs have not

[111] Compl. ¶ 135.
[112] *Id.* at ¶ 136.
[113] *Id.* at ¶ 137.
[114] *Id.* at ¶ 138.
[115] *See, e.g., McMillan*, 768 A.2d at 505 (dismissing loyalty claim based on deal protection devices because inclusion of a "standard no-shop provision" and a 3.5% termination fee do not provide "any support for the plaintiffs' *Revlon* claims"); *In re 3Com S'holders Litig.*, 2009 WL 5173804, at *7 (Del. Ch. Dec. 18, 2009) (noting that merger agreement with a no-solicitation provision, matching rights, and a termination fee in excess of 4% of the deal value "have been repeatedly upheld by this Court"); *In re Orchid Cellmark Inc. S'holder Litig.*, 2011 WL 1938253, at *7 (Del. Ch. May 12, 2011) (noting that comparable deal protections "are unremarkable," that "the no-shop provision . . . is balanced by a fiduciary out," and that the "matching and informational rights" as well as a termination fee, "would not preclude a serious bidder from stepping forward."); *In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022, 1049 (Del. Ch. 2012) (noting that a 3.05% termination fee, a no-solicitation provision (with a fiduciary out), matching rights, a force-the-vote provision, and a voting agreement that locked up at least 33% of the company shares in favor of the merger were not unreasonably preclusive deal protection devices).
[116] *In re Answers Corp. S'holders Litig.*, 2012 WL 1253072, at *8 ("If the Court ultimately determines that the decision to enter into the Merger Agreement was a breach of fiduciary duty,

stated a duty of loyalty claim, and any duty of care claim is exculpated, the Court rejects this argument.

In conclusion, the Complaint fails to allege a reasonably conceivable set of circumstances that the Board acted in bad faith. Moreover, the Board's decision to sell the Company at a 38% premium to its unaffected stock price and after a lengthy sales process was not "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[117]

C. *Aiding and Abetting Claim*

Count II of the Complaint alleges that the Buyout Group aided and abetted the Defendant Directors breach of their fiduciary duties. To state a claim for aiding and abetting a breach of fiduciary duty, a plaintiff must plead "(1) the existence of a fiduciary relationship, (2) a breach of the fiduciary's duty . . . , (3) knowing participation in that breach by the defendants, and (4) damages proximately caused by the breach."[118] Even though the Plaintiffs have not

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then the fact that the Board received benefits from the Merger that it had locked up might increase the Plaintiffs' recovery. Thus, the Court will not, at this time, dismiss the Plaintiffs' claims that the Board breached its fiduciary duties by locking up the Merger and using the Merger to extract benefits for itself, even though such claims may not have independent viability."). The deal protection devices in *Answers* included: "(1) a 'no shop' clause; (2) a 'no-talk' provision limiting the Board's ability to discuss an alternative transaction with an unsolicited bidder; (3) a matching rights provision; (4) a termination fee plus expense reimbursement worth approximately 4.4% of the Merger's equity value; and (5) a force-the-vote provision pursuant to 8 *Del. C.* § 146." *Id.* at *8 n. 50. Of those devices, the Court noted: "[t]here is nothing inherently unreasonable, individually or collectively, about the deal protection measures at issue here." *Id.*

[117] *In re Alloy, Inc.*, 2011 WL 4863716, at *10 (internal quotation marks omitted).

[118] *Malpiede*, 780 A.2d at 1096 (internal quotations marks omitted).

adequately alleged a breach of the duty of loyalty, the aiding and abetting claims against the Buyout Group *might* still survive a motion to dismiss if the Court eventually finds that the Plaintiffs have adequately stated a duty of care claim, notwithstanding the Defendant Directors' exculpation from that claim under 8 *Del. C.* §102(b)(7).[119] However, the Court need not decide whether the Plaintiffs have stated a duty of care claim because they have failed to allege adequately that the Buyout Group "knowingly participated" in a fiduciary breach.

To plead knowing participation adequately, the Plaintiffs must allege facts that the Buyout Group directly "sought to induce the breach of a fiduciary duty" or "make factual allegations from which knowing participation may be inferred."[120] Knowing participation may be inferred where "it appears that the defendant may have used knowledge of the breach to gain a bargaining advantage in the negotiations" or "where the terms of the transaction are so egregious or the magnitude of the side deals is so excessive as to be inherently wrongful."[121] The Delaware Supreme Court has elaborated that "a bidder's attempts to reduce the

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[119] *See Malpiede*, 780 A.2d at 1096-97 (noting that while the complaint did not adequately plead a duty of loyalty claim, a claim for aiding and abetting may still be viable if a duty of care claim is stated). Whether an aiding and abetting claim is viable where only a duty of care claim is stated and where there is an 8 *Del. C.* §102(b)(7) provision is uncertain. The Court in *Answers* considered this theoretical issue, ultimately concluding that "it is not clear that a claim for aiding and abetting a breach of fiduciary duty could survive a motion to dismiss if a complaint only pleads an underlying breach of the duty of the care by the fiduciary." 2012 WL 1253072, at *9 n.59.

[120] *In re Telecommc'ns, Inc. S'holders Litig.*, 2003 WL 21543427, at *2 (Del. Ch. July 7, 2003).

[121] *Id.*

sale price through arm's-length negotiations cannot give rise to liability for aiding and abetting, whereas a bidder may be liable . . . if the bidder attempts to create or exploit conflicts of interest in the board."[122]

The Plaintiffs allege that the Buyout Group pressured the Board to accept a lower price and engage in a hasty sale.[123] To support this claim, the Plaintiffs cite deposition testimony not pleaded in the Complaint, from a representative of LGP, stating that "we [*i.e.*, LGP] as the company's largest shareholder would be extremely disappointed if, for example, there was $54 bid from somebody else and the board held out for $55."[124] This testimony hardly shows that LGP pressured the Board. Moreover, nothing in the Complaint suggests that Buyout Group's actions were not otherwise hard-bargaining on the part of an arm's-length third-party bidder.

The Plaintiffs next argue that the Buyout Group was somehow complicit in the alleged downward adjustment to the five-year business plan.[125] But the only fact alleged in the Complaint in support of this alleged scheme is the suspicious timing of the adjustment and LGP's expression of interest. The Complaint does

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[122] *Malpiede*, 780 A.2d at 1097-98 (citation omitted) ("Similarly, a bidder may be liable to a target's stockholders for aiding and abetting a fiduciary breach by the target's board where the bidder and the board conspire in or agree to the fiduciary breach.").
[123] *See* Pls.' Answering Br. 28; Compl. ¶ 61 ("LGP contacted . . . Zarkin, . . . several times, instructing him to urge the Board to conduct an exploration of 'strategic alternatives' so that its proposed buyout of the Company could be presented to BJ's shareholders as if it were the result of a thorough auction procedure.").
[124] deLeeuw Aff. Ex. D (Seiffer Dep. Tr.) at 119-20; Pls.' Answering Br. 28.
[125] *See* Pls.' Answering Br. 28; Compl. ¶¶ 62-64.

not allege any facts suggesting that LGP convinced the Board to adjust the five-year plan or that LGP was aware that the adjustment was inappropriate.[126]

The Plaintiffs also seek to demonstrate knowing participation by alleging that the Buyout Group conspired with the Board to purchase the Company at a discounted price.[127] But the only facts pleaded in support of that theory is that both the Buyout Group and the Board knew that BJ's was worth substantially more than $51.25 per share. Without more, those facts do not provide a reasonable inference that such a scheme existed between the Buyout Group and the Board. Moreover, the Buyout Group's conduct, again, amounts to nothing more than hard bargaining, which in an arm's-length transaction does not constitute knowing participation in a fiduciary breach.[128]

Finally, the Plaintiffs allege that the Buyout Group somehow knew that the Board was manipulating the sales process in its favor, perhaps, in part because of the promise of future employment to certain members of BJ's management

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[126] The Plaintiffs argue that "[e]ven if the Buyout Group did not direct management to change its projections, the Buyout Group had access to the data room, and thus knew that the projections were changed in their favor and that the previous higher projections were never shared with BJ's other shareholders." Pls.' Answering Br. 28. This does not show knowing participation.

[127] *See* Pls.' Answering Br. 29.

[128] *See In re Lukens Inc. S'holders Litig.*, 757 A.2d 720, 735 (Del. Ch. 1999), *aff'd sub nom. Walker v. Lukens, Inc.*, 757 A.2d 1278 (Del. 2000) ("[I]t should be obvious that 'an offeror may attempt to obtain the lowest possible price for stock through arms'-length negotiations.'") (quoting *Gilbert v. El Paso Co.*, 490 A.2d. 1050, 1058 (Del. Ch. 1984), *aff'd*, 575 A.2d 1131 (Del. 1990)).

team,[129] and that the Buyout Group's pressure on the Board to engage in a hasty sale caused it to consider only financial buyers.[130] Where, as here, the Complaint does not allege that a third party (the Buyout Group) "played any role" in the Board's decision to sell BJ's, or used that knowledge to their bargaining advantage, knowing participation cannot be inferred.[131] And, as to the Plaintiffs' contention that the inducement of future employment provides a sufficient inference to find knowing participation, the Court declines to make that inference where, as here, there is no allegation that those terms were unreasonable, and where doing so would "only undermine [reasonable] business practices."[132]

In conclusion, the Plaintiffs fail to allege adequately that the Buyout Group knowingly participated in a breach of fiduciary duty. The Plaintiffs' aiding and abetting claim must therefore be dismissed.

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[129] In support of that claim, the Plaintiffs argue that the Buyout Group "knew that management and the Board would be tempted to push its deal through and thwart strategic buyers because it was offering management future employment and equity positions that it would not receive in a strategic sale." Pls.' Answering Br. 29. This also does not approach establishing knowing participation.

[130] *Id.*

[131] *See Katell v. Morgan Stanley Gp., Inc.*, 1993 WL 10871, at *8 (Del. Ch. Jan. 14, 1993).

[132] *Morgan v. Cash*, 2010 WL 2803746, at *5 (Del. Ch. July 16, 2010). In *Morgan*, this Court observed that: "[R]etaining management is a routine occurrence for the obvious reason that an acquiror often wants to keep existing management in order to ensure that the acquired assets continue to be managed optimally. To view the retention of management on reasonable terms with suspicion would only undermine business practices that often facilitate the difficult transitions required when two businesses merge." *Id.* (footnote omitted).

III. CONCLUSION

Adequately pleading a duty of loyalty claim is especially difficult where, as here, the Board consisted of a majority of disinterested and independent directors, and it actively solicited interest from other bidders, the Special Committee—in good faith—relied upon financial and legal advisors, no other topping bids emerged after a lengthy public sales process, the Board drove the price up, and the shareholders received a 38% premium to the Company's unaffected stock price. The bad faith inferences that the Plaintiffs would have this Court draw are simply not reasonable in light of the rational explanations for the Board's conduct. Accordingly, based on the facts in the Complaint, it is not reasonably conceivable that the Board acted in bad faith or that the Buyout Group knowingly participated in a breach of fiduciary duty. Defendants' joint motion to dismiss the Complaint is granted.

An implementing order will be entered.