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IN THE SUPREME COURT OF THE STATE OF DELAWARE

BUTTONWOOD TREE VALUE PARTNERS, LP and FRANKLIN VALUE INVESTORS TRUST-FRANKLIN MICROCAP VALUE FUND, Plaintiffs Below-Appellants, v. MICHAEL J. SULLIVAN, STEPHEN E. FUHRMAN, RONALD V. KAZMAR, MICHAEL X. CRONIN, JOHN F. CALHOUN and CHRISTOPHER M. RODGERS, Defendants Below-Appellees, and CENTRAL STEEL AND WIRE COMPANY, Nominal Defendant Below -Appellee.	No. 178, 2015 APPEAL FROM THE COURT OF CHANCERY OF THE STATE OF DELAWARE, CONSOL. C.A. NO. 9552-VCL

INDIVIDUAL DEFENDANTS BELOW-APPELLEES' ANSWERING BRIEF

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NATURE OF PROCEEDINGS

In the action below, Plaintiffs below-appellants Buttonwood Tree Value Partners, LP ("Buttonwood") and Franklin Value Investors Trust-Franklin MicroCap Value Fund ("Franklin") (collectively "Appellants" or "Plaintiffs"), which are two minority stockholders of Central Steel and Wire Company ("Central Steel" or the "Company"), purported to assert individual and derivative claims against the Company and some of its current and former directors. Despite cloaking their complaint as a challenge to the actions of Central Steel's board, Plaintiffs challenged, in substance, a decision by Central Steel's controlling stockholder, a private trust known as the Conserve School Trust (the "Trust"), not to sell its shares of Company stock.

Plaintiffs filed their Second Amended and Consolidated Verified Class Action and Derivative Complaint (the "Complaint") on November 10, 2014. (A 12-45.) The Complaint asserted claims against Michael J. Sullivan, Stephen E. Fuhrman, Ronald V. Kazmar, Michael X. Cronin, John F. Calhoun, and Christopher M. Rodgers, Kevin G. Powers, and James E. Rinn. The individual defendants moved to dismiss for lack of standing, lack of jurisdiction, and failure to state a claim upon which relief may be granted. (Trans. ID 55599825.)

The Court of Chancery granted the motion to dismiss. Relying primarily on *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009), the court held that the directors'

decision not to pursue a sale of Central Steel should be reviewed under the business judgment rule and that Plaintiffs had not stated a viable breach of fiduciary duty claim (Appellants' Br. Ex. A at 70-81) and entered an order of dismissal (*id.* Ex. B). Plaintiffs moved for reargument (Trans. ID 56951597), which the Court of Chancery denied. (Trans. ID 57008534.)

On April 10, 2015, Plaintiffs filed a notice of appeal as to their claims against individual defendants Sullivan, Fuhrman, Kazmar, Cronin, Calhoun, and Rodgers ("Appellees"), but not as to their claims against Messrs. Powers and Rinn. (Trans. ID 57061541.)[1]

[1] Messrs. Powers and Rinn were not directors or trustees during the time period relevant to Plaintiffs' claims, and they argued below that the claims against them should be dismissed on that ground. (B 36 (Defs.' Mot. to Dismiss at 30).) Because the Court of Chancery's judgment as to Messrs. Powers and Rinn has not been appealed, that judgment is final. Supr. Ct. R. 6(a). Accordingly, the individual defendants have omitted arguments particular to Messrs. Powers and Rinn from this brief.

SUMMARY OF ARGUMENT

1. Denied. The Complaint does not plead any viable claim for breach of fiduciary duty against Appellees for declining to pursue a sale of Central Steel. Plaintiffs allege that in June 2011, an entity known as Samuel, Son & Co., Ltd. ("Samuel, Son") submitted an unsolicited proposal to the trustees of the Trust and the directors of the Company offering to purchase the Trust's shares of Central Steel. The individual defendants, who serve as trustees of the Trust, met in their capacity as trustees and declined the Samuel, Son proposal on behalf of the Trust after analyzing the best interests of the Trust. The individual defendants then considered the proposal in their capacity as directors and decided not to pursue it, both because the Company's majority stockholder had already rejected it and because their analysis concluded that the offer did not represent a premium over the Company's actual and projected future value.

Plaintiff has no legal basis to challenge those considered judgments. A controlling stockholder has the right to retain its property and not to sell its shares at the behest of other stockholders or a third party. Once the Trust decided not to sell its shares, it would have been futile for the directors to pursue a sale.

Plaintiffs claim that because the individual defendants served as both trustees and directors—the Trust as the controlling stockholder elects the directors—their duties as directors governed their decisions as trustees and

required them to make paramount the minority stockholders' interests. That is incorrect. The individual defendants' actions as trustees are measured by reference to the Trust's position as controlling stockholder, not by their separate duties as directors of Central Steel.

2. Denied. The Court of Chancery correctly concluded that the rule adopted in *Pogostin v. Rice*, 480 A.2d 619 (Del. 1984), and applied in *Gantler* required dismissal of the Complaint. When directors decline a merger offer, a plaintiff cannot rebut the presumption of the business judgment rule by alleging only that the directors, by virtue of their company positions, had a "motive to retain corporate control." *Gantler*, 965 A.2d at 707. Rather, the plaintiff must allege "*other facts* sufficient to state a cognizable claim that the Director Defendants *acted* disloyally." *See id.* (emphasis added).

Plaintiffs did not satisfy the *Gantler* rule because they did not allege any "other facts" that support the inference that the individual defendants acted disloyally. They allege nothing more than that the individual defendants allegedly did not pursue the Samuel, Son proposal because they had an interest in maintaining control. The Court of Chancery correctly held that this bare allegation was not enough to state a claim.

STATEMENT OF FACTS

A. Central Steel and the Conserve School Trust

Central Steel is a Chicago-based distributor of steel and other metals. Its controlling stockholder is the Trust, which is the legacy of industrialist and philanthropist James R. Lowenstine. Mr. Lowenstine, who was Central Steel's longtime majority owner, created the Trust in 1981 to provide for the disposition of his assets at his death. He amended the Trust Instrument numerous times, with the final amendment on September 19, 1995. (A 46.)

Mr. Lowenstine died in January 1996, leaving the vast majority of his assets, including his controlling interest in Central Steel, to the Trust. He also left the Trust a 1,200-acre parcel in northern Wisconsin that he called "Lowenwood."

Mr. Lowenstine directed that the assets of the Trust be used to create and operate a school at Lowenwood to be known as the Conserve School. (A 51, Art. VI.) The Trust details Mr. Lowenstine's vision for the Conserve School's structure and educational mission. In the years since Mr. Lowenstine's passing, the trustees have overseen the design, construction, and operation of the school, which opened its doors to its first class of students in 2002. *See* www.conserveschool.org.

Mr. Lowenstine appointed the directors of Central Steel—his longtime business colleagues—to serve as the Trust's individual trustees. (A 63, Art. VII ¶ C.) He required that as long as the Trust holds the majority of Central Steel's

stock, the directors of Central Steel would also serve as the trustees of the Trust. (A 64, Art. VII ¶¶ F, G.)[2]

B. Mr. Lowenstine's Recommendation that the Trust Retain Its Interest in Central Steel

Mr. Lowenstine wanted the Trust to retain its interest in Central Steel. In the Trust Instrument, he recommended that the trustees not sell the Central Steel stock because he trusted his fellow directors and had faith in the Company's future. (A 71, Art. VIII ¶ C.) He waived the trustees' duty of diversification with respect to the stock, *id.*, and required them to sell it only if (1) the Internal Revenue Service decides the Trust does not qualify as a charitable trust or (2) the trustees determine that it is "legally impossible or otherwise impractical to operate the Conserve School." (A 55, Art. VI ¶ M.) Neither of those circumstances has occurred.

Mr. Lowenstine also made clear that if the trustees ever were required to sell the Trust's shares in Central Steel, they should not "sell the trust's interest as a single block" unless there was no viable alternative. (*Id.*, Art. VI ¶ M(1).) Rather, they should sell the stock "with a view towards spreading ownership of the shares as widely as possible" and to "use their best efforts" to ensure no entity obtained more than 5% voting power. (A 56-57, Art. VI ¶ M(1)(a)(i)-(ii) & (b).)

[2] Thus, Plaintiffs' assertion that the Trust Instrument "does not contemplate the current situation wherein the [Central Steel] directors are management insiders and are the only individual trustees" is incorrect. (A 22 (Compl. ¶ 28).)

The Trust Instrument further provides that, in the event that the Trust no longer has a majority interest in Central Steel, the trustees will be appointed by The Culver Educational Foundation ("Culver"), which operates an unrelated military school and which is a residuary beneficiary of the Trust. (A 65, Art. VII ¶ I.)[3]

C. The Samuel, Son Proposal to Purchase the Trust's Shares

In June 2011, Samuel, Son submitted an unsolicited proposal to the trustees and directors offering to purchase the Trust's shares of Central Steel. (B 40-45 (Defs.' Mot. to Dismiss, Ex. B).) The proposal was a preliminary, non-binding indication of interest subject to various conditions, and it was contingent upon Samuel, Son's ability to acquire 100% of the Company's stock. (B 41-42, § 5(a).)

On July 18, 2011, the trustees met to discuss the Samuel, Son proposal. They concluded that selling the Central Steel stock would not be in the best interests of the Trust or the Conserve School. Among their reasons were:

(1) The proposal represented a discount from Central Steel's book value after tax and depreciation considerations;

(2) Central Steel had strong strategic initiatives under way that were expected to yield greater value;

(3) The fundamental purpose of the Trust is to support the School, and the Trust's current holdings were sufficient to fulfill the School's needs; and

[3] Contrary to Plaintiffs' assertion, *see* Appellants' Br. at 12, Culver was not created by Mr. Lowenstine. (*See* A 48, Art. VI ¶ C.)

(4) Selling the Central Steel stock could jeopardize the School's continued operation because a sale would put Culver in control of the Trust, and through past litigation Culver had attempted to close the Conserve School and take the Trust assets for itself.

(B 47-50 (Defs.' Mot. to Dismiss, Ex. C).) In addition, the trustees noted that the Trust Instrument reflects Mr. Lowenstine's intent that the Trust retain the Central Steel stock. (B 49.)

The minutes make clear that the trustees' concern as to Culver was not that Culver would be able to replace the trustees, as Plaintiffs contend, *see* Appellants' Br. at 16-17, but that it would likely use that power to the detriment of the School:

> The Trustees noted that the fundamental purpose of the Trust is to support the School. Should there be a sale of the Central stock, Culver would then be able to appoint the Trustees, and Culver has previously argued that operating the School is impractical. Should Culver-appointed Trustees reach that conclusion, the Trust would allow them to cease operating the School. … [B]ased upon experience with Culver to date, it would be reasonable to conclude that a sale of the Central stock would create a significant risk to the future of the School. In two attempts to challenge the Trustees' decisions and so gain control of the Trust's corpus, Culver has evidenced its lack of support for the School in both its past and present formats.

(B 48-49.)[4]

After the trustees had considered and rejected the Samuel, Son proposal, the Company's directors met and resolved not to pursue the proposal, both because the

[4] Culver had previously sued the trustees twice, alleging (unsuccessfully) that the School was impractical and should be shut down and requesting that the Trust assets be distributed to Culver. *See Conserve Cmty., LLC v. Conserve School Trust*, 794 N.W.2d 927 (Wis. Ct. App. 2010) (TABLE); *Culver Educ. Found. v. Blythe, et al.*, Case No. 05 C 6480 (N.D. Ill.).

controlling stockholder had rejected it and because they determined that it was not in the best interests of Central Steel. (B 52-53 (Defs.' Mot. to Dismiss, Ex. D).) The trustees and the directors then informed Samuel, Son that they had discussed the proposal and decided not to pursue it. (B 55 (Defs.' Mot. to Dismiss, Ex. E).)

D. The "Expressions of Interest"

Plaintiffs also allege that during 2011 and 2012, Central Steel received three unsolicited one-page "expressions of interest" addressed to Mr. Cronin asking whether he would be willing to talk with potential buyers. (A 34-38 (Compl. ¶¶ 49-50, 53-54).) None of these letters contains any proposed price or purchase terms, although two state that any transaction would be structured to allow the directors to keep their managerial positions. (A 35, 37 (Compl. ¶¶ 50, 53).)

E. Plaintiffs' Claims

Nearly three years after the trustees decided not to sell the Trust's shares of Central Steel to Samuel, Son, Plaintiffs filed this lawsuit. While the case was styled as a claim against the individual defendants in their capacities as directors, Plaintiffs' allegations focused on the individual defendants' actions as trustees of the Trust. Plaintiffs said they were challenging the individual defendants' conduct because the individual defendants "put their personal interests ahead of the interests of [Central Steel] and its shareholders *against the explicit provision in the Lowenstine Trust instrument* and the law." (A 40 (Compl. ¶ 59 (emphasis added)).)

Throughout the Complaint, Plaintiffs asserted that the individual defendants failed to follow the instructions in the Trust Instrument and that therefore they should be held liable to the minority stockholders of Central Steel. (A 23-24 (Compl. ¶ 31); *see also* A 12-14, 21-24, 39-40 (Compl. ¶¶ 1-3, 27-31, 56-57, 59).)

Despite the fact that Central Steel's controlling stockholder decided not to sell its shares, Plaintiffs also asserted that the individual defendants *as directors* should have more fully analyzed the Samuel, Son proposal and compared its terms to unidentified "alternatives." (*See* A 32 (Compl. ¶ 44).) Plaintiffs claimed that the individual defendants breached their duties of loyalty and care as directors by declining to sell the Company at what Plaintiffs claim was a "premium," and that they should have "investigate[d]" the "expressions of interest." (A 31, 35, 37-38, (Compl. ¶¶ 42, 50, 53-54).) Plaintiffs purported to assert both derivative and direct claims, although their derivative claim did no more than replead the direct claim with perfunctory allegations about demand futility. (A 43-44 (Compl. ¶¶ 69-70).)

ARGUMENT

I. THE JUDGMENT BELOW SHOULD BE AFFIRMED BECAUSE THE INDIVIDUAL DEFENDANTS DID NOT BREACH ANY FIDUCIARY DUTY TO PLAINTIFFS BY DECLINING TO PURSUE A SALE OF CENTRAL STEEL

A. QUESTIONS PRESENTED

1. When a corporation's controlling stockholder decides not to sell its shares to a third party, can the corporation's minority stockholders challenge that decision by questioning the controlling stockholder's internal decision-making?

2. Do a corporation's directors have a fiduciary duty to pursue acquisition proposals that the controlling stockholder has rejected?

3. When the same people are both directors of a corporation and trustees of its controlling stockholder, do their duties to the corporation govern their decision as trustees whether to sell the controlling stockholder's shares to a third party?

4. Did the Court of Chancery correctly conclude that Plaintiffs' allegations concerning the individual defendants' motive to retain control were insufficient to state a claim for breach of the duty of loyalty under *Gantler v. Stephens* and *Pogostin v. Rice*?

B. SCOPE OF REVIEW

This Court reviews these questions of law *de novo*. *Klaassen v. Allegro Dev. Corp.*, 106 A.3d 1035, 1043 (Del. 2014). The Court may affirm the Court of

Chancery's judgment on alternative grounds that were asserted below in support of the individual defendants' motion to dismiss. *See Cent. Laborers Pension Fund v. News Corp.*, 45 A.3d 139, 141 (Del. 2012).

C. MERITS OF ARGUMENT

As stockholders of Central Steel, Plaintiffs cannot challenge the Conserve School Trust's decision not to sell its shares of Central Steel. Longstanding precedent holds that a controlling stockholder does not owe the minority a duty to sell its shares. Plaintiffs try to circumvent this bedrock principle in two ways. Neither has merit.

First, Plaintiffs argue that the Trust forfeited its right to decide whether to sell its shares because the trustees' personal interests are "divorced" from the financial interests of the Company. (B 101 (Pls.' Resp. to Mot. to Dismiss at 30).) Plaintiffs are incorrect. No authority supports their assertion that a controlling stockholder's rights can be stripped away based on the personal interests of the people who make decisions for it, or the manner in which they do so.

Second, Plaintiffs argue that the individual defendants' duties as directors trump their duties as trustees, so they must put the Company's interests first even when making decisions for the Trust. (B 96-98, 100 (Pls.' Resp. to Mot. to Dismiss at 25-27, 29).) This Court rejected that proposition in *Tanzer v. Int'l General Indus., Inc.*, which held that in the "overlapping directors" situation, the

directors of the parent corporation are entitled to vote the parent's shares as they deem best, without regard for either their obligations as directors of the subsidiary or the interests of the subsidiary's minority stockholders. 379 A.2d 1121, 1124 (Del. 1977), *overruled in part on other grounds by Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983).

The Vice Chancellor recognized that there was no precedent for Plaintiffs' attempt to challenge the controlling stockholder's decision not to sell its shares, but he decided the case based on another deficiency in the Complaint: that it did not allege facts sufficient to plead around the rule set forth in *Gantler v. Stephens* and *Pogostin v. Rice*. As the Vice Chancellor correctly held, merely alleging an entrenchment motive in connection with the decision whether to sell a corporation is not enough to rebut the business judgment rule. The judgment below should be affirmed.

1. Plaintiffs Fail to State a Claim Against the Individual Defendants as Trustees.

a. The Conserve School Trust Had No Duty to Sell Its Controlling Stake in Central Steel.

Settled precedent holds that a controlling stockholder (such as the Trust) does not owe minority stockholders any duty to sell its shares. In *Bershad v. Curtiss-Wright Corp.*, 535 A.2d 840 (Del. 1987), this Court held that "a stockholder is under no duty to sell its holdings in a corporation, even if it is a

majority shareholder, merely because the sale would profit the minority." *Id.* at 845. The Court rejected the argument (similar to the one Plaintiffs make here) that a majority stockholder had breached its fiduciary duty to minority stockholders by enforcing a "strict policy" of refusing to sell its shares to a third party. *Id.* at 844-45. The Court explained:

> Stockholders in Delaware corporations have a right to control and vote their shares in their own interest. … It is not objectionable that their motives may be for personal profit, or determined by whim or caprice, so long as they violate no duty owed other shareholders.

Id. at 845.

Our courts have regularly reaffirmed this principle. *See, e.g., Peter Schoenfeld Asset Mgmt. LLC v. Shaw*, 2003 WL 21649926, at *3 (Del. Ch. Jul. 10, 2003), *aff'd*, 840 A.2d 642 (Del. 2003) (TABLE) (majority stockholder "never had a duty to complete the [merger] either for itself or for the benefit of PanAmSat's minority shareholders"); *Mendel v. Carroll*, 651 A.2d 297, 306-07 (Del. Ch. 1994) ("[n]o part" of the fiduciary duty of controlling stockholders "requires them to sell their interest"); *Cincinnati Bell Cellular Sys. Co. v. Ameritech Mobile Phone Serv. of Cincinnati, Inc.*, 1996 WL 506906, at *12 (Del. Ch. Sept. 3, 1996), *aff'd*, 692 A.2d 411 (Del. 1997) (TABLE) (following *Bershad* and holding that "[a]s with a

minority stockholder, [a minority partner] has no right to demand that the majority owner sell all the business assets").[5]

Before the Court of Chancery, as here, Plaintiffs asserted that the settled rule does not apply because the trustees' personal interests are not "identical to other stockholders to maximize the value of [the Company's] shares." (B 101 (Pls.' Resp. to Mot. to Dismiss at 30 (quoting *In re Morton's Rest. Grp., Inc. S'holders Litig.*, 74 A.3d 656, 666-67 (Del. Ch. 2013))); Appellants' Br. at 25.) According to Plaintiffs, because the trustees themselves do not own the Trust's shares in Central Steel, they "cannot credibly argue that the Trust is free to exercise its right to refrain from selling its shares of Company stock." (*See* B 101.)

Plaintiffs cite no authority that supports their assertion that the rights of a controlling stockholder can be stripped away because a minority stockholder questions the loyalty of the controlling stockholder's trustees or directors.[6] Indeed, the longstanding rule is that a majority stockholder such as the Trust has the right to deal self-interestedly with its shares, subject only to its obligation not to self-

[5] *See also Emerson Radio Corp. v. Int'l Jensen Inc.*, 1996 WL 483086, at *17 (Del. Ch. Aug. 20, 1996) (finding no breach of fiduciary duty in opposing one purchase offer or favoring another "because even a majority stockholder is entitled to vote its shares as it chooses, including to further its own financial interest"); *Binks v. DSL.net, Inc.*, 2010 WL 1713629, at *11 (Del. Ch. Apr. 29, 2010) ("even a majority stockholder is entitled to vote its shares as it chooses, including to further its own financial interest") (citation omitted).

[6] The *Morton's* court considered *and rejected* allegations that a large stockholder had a disabling conflict of interest because its motivation to engage in a merger diverged from the interests of other stockholders. *See* 74 A.3d at 666-67.

deal or otherwise take unfair advantage of its majority position. *See Tanzer*, 379 A.2d at 1123; *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971) (minority stockholders cannot challenge parent company's internal decisionmaking where parent is not engaging in a transaction with the subsidiary "in such a way that the parent receives something from the subsidiary to the exclusion of, and detriment to, the minority stockholders of the subsidiary"). Therefore, the Trust (like any other controlling stockholder) is permitted to vote its shares for any reason, including "personal profit … whims or caprice." *See Tanzer*, 379 A.2d at 1123 (quoting *Ringling Bros.-Barnum & Bailey Commercial Shows v. Ringling*, 53 A.2d 441, 447 (Del. 1947)).

b. Plaintiffs Lack Standing to Challenge the Trustees' Decision.

Plaintiffs' Complaint repeatedly invoked the provisions of the Trust Instrument and alleged that the individual defendants breached their duties as trustees by declining (or, purportedly, not properly analyzing) the Samuel, Son proposal. (*See, e.g.*, A 23-24, 39-40 (Compl. ¶ 31 ("[T]he Defendants … by virtue of the Trust, are obliged to put the interests of [Central Steel] and its shareholders before the interests of the controlling shareholder, the Trust. This they have failed to do."); *id.* ¶ 56 ("Prudent trustees seeking to maintain the Conserve School's mission would, at a minimum, explore alternative uses of the endowment that would provide a higher yield."); *id.* ¶ 57 ("The Directors of [Central Steel] have

explicitly ignored the instruction in the Trust Document to place [Central Steel's] interests and those of its shareholders first.")); *see also* A 21-24, 31-33 (Compl. ¶¶ 27-31, 43, 46).)

Plaintiffs are not beneficiaries of the Trust and had no standing to challenge its administration. *See Sergeson v. Del. Trust Co.*, 413 A.2d 880, 882 (Del. 1980) (per curiam) ("'No one except a beneficiary or one suing on his behalf can maintain a suit against the trustee to enforce the trust ... .'") (quoting Restatement (Second) of Trusts § 200 (1959)); *Pollock v. Peterson*, 271 A.2d 45, 49 (Del. Ch. 1970) (applying this principle in the context of a charitable trust); 4 Scott & Ascher on Trusts § 24.4 (5th ed. 2007).[7] This rule has been rigorously enforced where, as here, non-beneficiaries have attempted to bring claims challenging a trustee's disposition of trust-owned shares. *See, e.g.*, *Sergeson*, 413 A.2d at 882.[8] Because neither the Company nor its minority stockholders were beneficiaries of the Trust, the Court should affirm the dismissal of any claim against the individual defendants that depends on action taken by them in their capacity as trustees.

[7] The Trust is governed by Illinois law, which is consistent with Delaware law in this respect. *See Schlosser v. Schlosser*, 618 N.E.2d 360, 363 (Ill. App. Ct. 1st. Dist. 1993).

[8] The mere fact that the Trust owns shares in a public company does not turn the company's other stockholders into beneficiaries or give them standing to sue the trustees for an alleged breach of trust. *See* 3 Scott & Ascher on Trusts § 18.1.8.1 (5th ed. 2007); *Miller & Lux, Inc. v. Anderson*, 318 F.2d 831, 839 (9th Cir. 1963); *Cleveland Trust Co. v. Eaton*, 256 N.E.2d 198, 207-08 (Ohio 1970).

2. Plaintiffs Fail to State a Claim Against the Individual Defendants as Directors.

Plaintiffs also fail to state any claim against the individual defendants in their capacities as directors of Central Steel. Once the Trust made its decision not to sell, any further action by the directors would have been futile, and in any event the Complaint did not allege facts sufficient to survive dismissal under *Gantler*.

a. The Directors Had No Duty to Pursue a Sale the Controlling Stockholder Had Rejected.

In their brief below and at oral argument before the Court of Chancery, Plaintiffs disavowed any challenge to the Trust's decision not to sell its shares. (*See* B 96-97 (Pls.' Resp. to Mot. to Dismiss at 25 ("Plaintiffs do not challenge the individual defendants' actions *qua* trustees"); *id.* at 26 ("Plaintiffs neither assert claims against the Trust *qua* controlling stockholder nor challenge the Trust's rejection of the Samuel offer")); Appellants' Br. Ex. A at 29:16-20 ("[T]o be clear, this case is not about challenging that decision-making at the trust level. As shareholders of Central Steel, the plaintiffs are challenging the decision-making at the board level of Central Steel.").)

That is a fatal concession as to any claim against the individual defendants as directors. Plaintiffs cannot disavow any challenge to the controlling stockholder's actions and then blame the directors for the Trust's decision. Once the controlling stockholder decided not to sell, there was nothing further for the

directors to do. They could not sell Central Steel without the controlling stockholder's support, and Plaintiffs cannot hold them liable for failing to undertake the futile pursuit of a proposal that had already been rejected. The directors had no duty to pursue a sale, nor would it have made sense to do so. *See Bershad*, 535 A.2d at 845 ("[F]rom Dorr-Oliver's standpoint its directors could not have assumed the role of auctioneers after the merger decision was made. That would have been futile. Curtiss-Wright owned approximately 65% of Dorr-Oliver, and could thwart any effort by Dorr-Oliver directors to auction the company."); s*ee also In re Digex Inc. S'holders Litig*., 789 A.2d 1176, 1196 (Del. Ch. 2000).

Plaintiffs contend that "the individual defendants' decision-making as trustees … does not relieve them of their independent fiduciary duties to [Central Steel] and its stockholders." (Appellants' Br. at 25.) Of course not: their role as directors imposed duties of care and loyalty to the corporation for their actions as directors. But the duties they owed as directors do not dictate their actions as trustees. The Company and the Trust are separate and distinct legal entities, and the individual defendants owe them separate and distinct fiduciary duties.

What Plaintiffs are really saying is that because the directors and the trustees were the same people, they had the *de facto* power to cause the Trust to sell its shares, and their duties as directors required them to use that power in service of all the Company's stockholders, not just the Trust. If that were the rule, then any time

there were overlapping boards, the controlling entity's decisions about its interest in the subsidiary would be governed by the duties owed by the subsidiary's board to the subsidiary's stockholders. Such a rule would be inconsistent with decades of precedent, and the Court squarely rejected it in *Tanzer*.

The central question in *Tanzer* was what duties applied to a decision by the representatives of a controlling stockholder (a parent corporation) to vote its shares in favor of a merger between the parent and its subsidiary. *Tanzer*, 379 A.2d at 1123. Although the parent also had "director control" over the subsidiary, the Court held that the parent's decision about the merger had to be measured by its rights as the controlling stockholder, not by its duties to the subsidiary. Because "it is the power and right of [the controlling stockholder] which is really under review[,] … *it would not be fair to [the stockholder] to examine only its director control of [the subsidiary] which is a consequence of its power and not the source thereof*." *Id.* (emphasis added); *see also id.* at 1124 ("[A controlling stockholder] may vote contrary to what other stockholders deem to be the best interest of the corporation, or even detrimental to it. This is equally true of a stockholder who is also a director voting as a stockholder.") (quoting 5 Fletcher Cyc. Corp. § 2031 (Perm. Ed.)); *see also Bershad*, 535 A.2d at 844-45 (holding that controlling stockholder breached no fiduciary duty to subsidiary's minority stockholders by maintaining a strict policy against selling the subsidiary); *Digex*, 789 A.2d at 1196

("Where, as here, a majority shareholder can block proposed transactions involving a sale of control, the courts will not require a board of directors to engage in a futile exercise, *even though the board continues to owe requisite fiduciary duties to its shareholders*.") (emphasis added).

The same rule applies here. The individual defendants' duties to the controlled entity (Central Steel) and its stockholders do not and cannot override their duties to the controlling entity (the Trust).

If it were otherwise (as Plaintiffs contend), the longstanding doctrine that controlling stockholders can decide to sell or not to sell their shares for their own reasons (even whim or caprice) would not apply where the controlling stockholder controls the boards of both entities, as is commonly the case. Such a doctrine would turn every unsolicited inquiry to purchase a company into an opportunity for any minority stockholder to conduct discovery and question controlling stockholders' private internal decision-making. It would introduce tremendous uncertainty, and perversely give controlling stockholders lesser ownership authority over their shares than that of the minority.

Of course there are limits on a controlling stockholder's conduct. If the Trust had compelled a transaction with Central Steel that benefitted the Trust "to the exclusion of, and detriment to, the minority stockholders," the minority would have a right to complain. *See Sinclair Oil Corp.*, 280 A.2d at 720; *Tanzer*, 379

A.2d at 1124 (evaluating whether majority stockholder's interest in selling was subterfuge to eliminate unwanted minority stockholders). But the Complaint did not allege that here. The Trust did not engage in any transaction with the Company at the minority's expense; it did not engage in a transaction at all. It simply decided not to sell its shares. That decision left Plaintiffs and the other minority stockholders in the same position as before: they own their shares and have every right to sell or retain them. What they cannot do is force the controlling stockholder to sell its shares just so they can sell theirs too. *See Bershad*, 535 A.2d at 845 ("a stockholder is under no duty to sell … merely because the sale would profit the minority"); *see also In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022, 1040-41 (Del. Ch. 2012) ("the duty to put the 'best interest of the corporation and its shareholders' above 'any interest ... not shared by the stockholders generally' does not mean that the controller has to subrogate his own interests so that the minority stockholders can get the deal that they want") (footnote omitted).[9]

[9] *Synthes* contemplated an exception for a "fire sale" situation in which the controlling stockholder needs to liquidate its interest right away. 50 A.3d at 1036. In those circumstances, the *Synthes* court indicated that the controlling stockholder's obligations to the minority might prohibit an immediate sale. *See id.* (discussing potential "disabling conflict of interest"). At oral argument below, the Vice Chancellor raised the possibility of what he called an "inverse *Synthes*" exception under which the controlling stockholder might owe a duty to the minority to sell its shares if "everybody in their right mind would sell" but the controlling stockholder has a "specific and personal interest" in not selling. (Appellants' Br. Ex. A at 24.) (footnote continues)

Plaintiffs incorrectly assert that the Trust Instrument "does not … authorize the trustees to favor the Trust's interests where those interests might conflict with the Company's." (Appellants' Br. at 11.) By its very nature, the Trust requires trustees to prioritize the interests of the Trust and its beneficiaries above all else. While the Trust Instrument does not contain a specific provision to that effect, no such authorization is necessary—nor would one expect to see it—because as a matter of law the trustees of an Illinois trust have a fiduciary duty to place the interests of the Trust and its beneficiaries ahead of any other interests. *Rennacker v. Rennacker*, 509 N.E.2d 798, 800 (Ill. App. Ct. 3d Dist. 1987) ("The trustee must keep in mind the beneficiary's interest and the trustee cannot do any act inconsistent with the beneficiaries' interests irrespective of the trustee's good or bad faith."); *see also Janowiak v. Tiesi*, 932 N.E.2d 569, 580 (Ill. App. Ct. 1st Dist. 2010) (trustee must "serve the interests of the beneficiary with complete loyalty").

Ordinarily it would be a breach of duty for the trustees to consider anything other than the purpose of the Trust (which is to operate the Conserve School, not to profit the minority stockholders of Central Steel). But Mr. Lowenstine knew that the trustees he selected were also directors of the Company. To avoid conflict of

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The Vice Chancellor acknowledged that he knew of no precedent supporting such an exception. *Id.* at 26. Creating one would run counter to decades of precedent, cited above, upholding the controlling stockholder's right to make exactly such decisions. In any event, the question is purely hypothetical because the allegations in this Complaint do not come close to establishing that "everybody in their right mind would sell" (essentially a waste standard).

interest claims by the beneficiaries, he waived any conflict that might result from the trustees' dual roles (as Illinois law permitted him to do) and specifically authorized them to consider Central Steel's interests when making their decisions for the Trust. (*See* A 73-74 (Trust Instrument at 28-29, Art. VIII ¶ I); *Dick v. Peoples Mid-Illinois Corp.*, 609 N.E.2d 997, 1002 (Ill. App. Ct. 4th Dist. 1993) ("Where a conflict of interest is approved or created by the testator, the fiduciary will not be held liable for his conduct unless the fiduciary has acted dishonestly or in bad faith, or has abused his discretion.").)

In the Complaint, Plaintiffs asserted that this prophylactic conflict waiver *requires* the trustees to put Central Steel's interests first. (A 21 (Compl. ¶ 27).) They have since abandoned that position, and rightly so: "authorize" does not mean "require." The trustees owe their duties to the Trust and its beneficiaries, and in particular to the Conserve School. Nothing in the Trust Instrument requires the trustees to subordinate the interests of the Trust to those of the Company, much less to those of Company stockholders wishing for an opportunistic exit. Even if it did, Plaintiffs would not have standing to complain because they are not beneficiaries.[10]

[10] Plaintiffs argued below that the individual defendants "answer only to themselves" for their decisions as trustees. (B 73 (Pls.' Resp. to Mot. to Dismiss at 2).) That is false. The trustees owe fiduciary duties to the Trust and its beneficiaries, and because the Trust is a charitable entity, it is also overseen by the

b. The Trial Court Correctly Held that Plaintiffs Failed to Rebut the Business Judgment Rule.

The Vice Chancellor considered the parties' arguments concerning the controlling stockholder issue, but decided the case on a separate and independent ground: that Plaintiffs failed to allege facts sufficient to satisfy the rule set forth in *Gantler v. Stephens*. The judgment should be affirmed for that reason as well.

Gantler reiterated that merely alleging facts showing a "motive to retain corporate control" is inadequate to overcome the business judgment rule because it would implicate every board's judgment on any unsolicited merger proposal. *Gantler*, 965 A.2d at 707. That is why *Gantler* required other disloyal acts or outside conflicts of interest to sustain a loyalty claim. The Vice Chancellor correctly ruled that no such "other facts" are alleged here. The Complaint alleges only that the directors of Central Steel, who received compensation from the Company because they worked there, rejected an unsolicited takeover proposal that the controlling stockholder had already rejected.

A basic premise of this Court's precedent is that directors are presumptively entitled to business judgment rule protection in rejecting a takeover offer. In *Gantler*, the Court rejected a proposed rule that would have imposed a heightened standard of scrutiny when the directors who rejected the takeover offer "stood to

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attorneys general of both Illinois (where the trustees reside) and Wisconsin (where the School is located).

lose the benefits of corporate control if the Company were sold." *See Gantler*, 965 A.2d at 705 (declining to apply intermediate scrutiny under *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985)). Instead, *Gantler* relied on the principle set forth in *Pogostin* that inside directors should not face potential liability every time they reject an offer to purchase the company. *See Pogostin v. Rice*, 480 A.2d 619, 626-27 (Del. 1984) (allegations that insider directors wanted to keep their positions, bonuses, and other company benefits failed to support a reasonable inference that the directors acted solely to retain control), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000). *Pogostin* made clear that a board's opposition to a tender offer is not sufficient to establish an improper motive to retain control because it "would condemn any board, which successfully avoided a takeover, regardless of whether that board properly determined that it was acting in the best interests of the shareholders." *Id.* at 627.

To avoid such a result, *Gantler* required the plaintiff to plead, in addition to a motive to retain corporate control, "other facts sufficient to state a cognizable claim" of disloyal conduct. 965 A.2d at 707.[11] In *Gantler*, the plaintiffs were able

[11] Plaintiffs assert that the trial court misinterpreted *Gantler* as requiring them to plead not only more than an entrenchment motive, but also "more than specific facts demonstrating that a director acted on that motive." (Appellants' Br. at 29.) In their view, under the trial court's interpretation, no allegations would suffice "if they also constituted an act of maintaining control." (*Id.*) Plaintiffs are incorrect. Consistent with *Gantler*, the Vice Chancellor ruled that the act of declining a takeover proposal, coupled with allegations demonstrating an interest

to rebut the business judgment presumption only because they alleged facts showing that the defendants engaged in specific disloyal acts and had personal interests in rejecting the offer beyond keeping control. A comparison of the facts in *Gantler* with Plaintiffs' Complaint demonstrates that Plaintiffs' allegations did not approach the threshold required to plead a breach of the duty of loyalty.

Gantler concerned a bank whose board had decided to put it up for sale. The board received three bids, and an investment advisor opined that all three were within the range suggested by its models and that accepting the two stock-based bids would be superior to retaining the company's shares. *Id.* at 700. The board then directed its investment advisor to conduct due diligence with respect to two of those bids. However, the President and CEO, who was also a director, "sabotaged" the sale process by failing to provide the requested due diligence materials to one of the bidders and then did not disclose his conduct to the board. *Id.* at 700-01, 707. The investment advisor concluded that the director's inaction caused the bid to be withdrawn. *Id.* at 707. The board pursued the other bid, but ultimately rejected it "[w]ithout any discussion or deliberation," despite a memorandum from the investment advisor that positively described the proposal. *Id.* at 701.

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in maintaining control, is not enough. Rather, a plaintiff must plead "other facts" demonstrating disloyalty—in *Gantler* itself, affirmatively sabotaging due diligence and having significant outside interests that would be threatened if the corporation were sold. No such other facts were alleged here.

The directors then terminated the sale process and instead adopted a privatization plan that reclassified the shares of certain minority stockholders to strip them of all voting rights except in the event of a proposed sale of the company. *Id.* at 701-03. The directors admitted in the corresponding proxy that each of them had "'a conflict of interest with respect to [the Reclassification] because he or she is in a position to structure it in a way that benefits his or her interests differently from the interests of the unaffiliated stockholders.'" *Id.* at 702 (alteration in original). The complaint also alleged that the directors made materially misleading statements in the proxy statement. *Id.* at 703.

Finally, the plaintiffs in *Gantler* alleged that two of the director defendants owned separate businesses that serviced the bank and would be significantly injured if the bank were sold. *Id.* at 708. The Court emphasized the magnitude of those outside business interests, noting that the bank was "a major client" of one director's personal business and the other director had a "strong personal interest" because his company "provided title services in nearly all of [the bank's] real estate transactions." *Id.* at 708. Based upon these allegations of sabotage and outside conflicts of interest, the Court held that the plaintiffs' allegations of "other facts" demonstrating disloyalty were sufficient to rebut the presumption of the business judgment rule. *Id.* at 706-08.

No such acts demonstrating disloyalty were alleged in Plaintiffs' Complaint. Plaintiffs identify the supposed disloyal acts in two pages at the conclusion of their brief. (*See* Appellants' Br. at 32-33.) They contend only that (1) the trustees and directors acted "without any analysis" of the best interests of the Trust or Central Steel; (2) the Trust meeting minutes contain a concession that the trustees' personal desire to remain trustees drove their rejection of strategic alternatives; (3) the directors generally did not pursue expressions of interest; and (4) the directors did not otherwise consider acquisitions despite industry consolidation. (*Id.*) These allegations misstate the documentary record incorporated into the Complaint and are insufficient to plead any disloyal act.

The Individual Defendants' Analysis. Plaintiffs' assertion that the trustees performed no analysis is refuted by the Trust minutes. (B 47-50 (Defs.' Mot. to Dismiss Ex. C).) The minutes reflect that the trustees conduct an "annual review of the prudence of continuing to hold" Central Steel stock and considered the Samuel, Son proposal as part of that process in June 2011. (B 47.) In evaluating the proposal, the trustees noted the Trust language recommending that Central Steel shares be retained and assessed financial projections and anticipated dividends for Central Steel through 2015 in light of the Trust's strategic plans. (B 48-49.) They analyzed the likely expenses of the Conserve School and determined that the current stock holdings should be sufficient to fulfill the Trust's mission in

running the school. (B 48.) They analyzed Samuel, Son's alleged premium compared to a recent appraisal of Central Steel stock and determined that the Samuel, Son proposal actually represented a discount from Central Steel's book value when adjusted for Central Steel's LIFO reserve and did not account for Central Steel's highly depreciated fixed assets. (*Id.*) Next, the trustees discussed strategic initiatives under way at Central Steel, including new equipment, expense controls, and sales revitalization plans, and their current assessment of customer orders to analyze the Company's prospects going forward. (*Id.*)

Although Plaintiffs refer to these materials in their Complaint, they misrepresent what the minutes say. Plaintiffs cannot conclusorily assert there was no analysis when the minutes directly contradict that allegation.

Next, Plaintiffs contend that the *directors* (who considered the Samuel, Son proposal after the trustees had rejected it) dismissed the proposal without any analysis. Once again, this allegation contradicts the record on which Plaintiffs base their Complaint. The board minutes reflect that the directors had just evaluated the Samuel, Son proposal as trustees and had considered whether it was in Central Steel's best interests. (B 52-53 (Defs.' Mot. to Dismiss Ex. D).) As the Trust minutes reflect, the trustees concluded that the Samuel, Son proposal did not actually offer a meaningful premium when considered in light of outside valuations and proper accounting for Central Steel's real value as well as future business

plans for growth and expense control. This is another significant difference from *Gantler*, where the board had decided to sell the bank and an outside investment advisor had concluded that all three bids were within an appropriate range and that "accepting the stock-based offers would be superior to retaining" the bank's shares. 965 A.2d at 700.

Furthermore, the context in which the directors made their decision stands in stark contrast to *Gantler*. In *Gantler*, the board had decided to put the bank up for sale and solicited bids, which were recommended by an outside advisor. The CEO then subverted the due diligence process by willful inaction and concealment and the directors, despite their earlier decision to pursue a sale, rejected a bid without explanation notwithstanding the advisor's favorable review. Two of the directors' significant outside business relationships with the bank were at threatened by the proposed sale that they rejected. The board then adopted a stock reclassification plan that favored them personally over non-insider stockholders.

In contrast, Central Steel's directors did not conclude that sale would be in the Company's best interests and then put the Company up for sale. Instead, an unsolicited proposal was directed to both the trustees and the directors. After documented analysis, the veracity of which Plaintiffs do not dispute, the trustees concluded that the proposal was not in the best interests of the Trust or Central Steel. The directors agreed with the assessment as to Central Steel, having already

performed the analysis and deliberated on it in their role as trustees.[12] None of the directors had any outside business interest that was threatened by the Samuel, Son proposal; all Plaintiffs allege is they had a motive to retain control, which is not sufficient to state a claim. Nor do Plaintiffs allege any deceit or concealment akin to the CEO's behavior in *Gantler*. Nothing alleged here approximates the disloyalty present in *Gantler*.

Reasons For Rejecting Proposal. Plaintiffs assert that the Trustees' rejection of the proposal "admittedly was driven by a personal desire to retain their role as trustees." (Appellants' Br. at 32.) This too is a gross misrepresentation of the record. Plaintiffs rely on the statement in the minutes that Culver, the contingent beneficiary of the Trust, would be able to appoint the trustees if the Trust no longer held a majority of Central Steel stock. (B 48; A 65, Art. VII ¶ I.) Plaintiffs characterize that statement as an admission that the trustees were motivated by a desire to keep their positions as trustees, but that ignores the rest of the sentence and paragraph. What the minutes actually say is that Culver previously argued that operating the School is impractical and, if Culver-appointed trustees reached that conclusion, the Trust provisions would allow them to shut down the Conserve School and take the Trust's assets. (B 48.) The trustees were

[12] Plaintiffs also criticize the directors for declining to discuss the Samuel, Son proposal with other minority stockholders after the trustees rejected it, but the directors had no such duty and Plaintiffs cite no authority for imposing one.

well aware that Culver had twice unsuccessfully sued the Trust arguing that the School is impractical and seeking a sale of Central Steel stock and a distribution of the hundreds of millions of dollars of Trust assets to Culver. *See supra* note 4. Far from admitting an improper self-interest, the minutes reflect the trustees' concern for the stated purpose of the Trust (to build and operate the Conserve School) and show that they considered the proposal with that purpose in mind. That approach was required by their duties as trustees; it does not indicate any disloyalty to the corporation.[13]

Response To "Cold Calls." Plaintiffs contend that there is a "pattern" of not considering inquiries, but none of these allegations supports an inference of disloyalty. (Appellants' Br. at 33.) Plaintiffs cite three unsolicited letters to Central Steel, essentially cold calls, containing no proposed price, terms, or (in two instances) identification of the potential buyer, and allege that the directors ignored

[13] At the hearing below, the Vice Chancellor commented that treating the Trust as subordinate to the Company "makes sense" because if a sale benefited the Company and its stockholders, it would also benefit the Trust by providing more money for the Conserve School. (Appellants' Br. Ex. A at 77:8-22.) That logic is too simple because it overlooks, among other things, (1) that the trustees specifically determined that selling would *not* be in the best interests of the Company, (2) the settlor's intent that the Trust retain the stock, and (3) the danger that a sale would result in the demise of the settlor's primary objective—an independent Conserve School—because trustees selected by Culver would deem the school "impractical" and shut it down. In any event, the fact that the Trust's interests and the Company's will often be aligned is not a reason to impose directors' duties on the trustees or disregard the Trust's authority as controlling stockholder.

them. (A 34-38 (Compl. ¶ 49-54).) Boards are under no duty to put companies "in play" every time an unsolicited inquiry—even one of substance—is made. *See Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 242 (Del. 2009) ("The duty to seek the best available price applies only when a company embarks on a transaction—on its own initiative or in response to an unsolicited offer—that will result in a change of control."). The individual defendants did not breach any duty by not doing so here, particularly when the Trust had decided not to sell.

Undefined Acquisitions. Plaintiffs assert that the directors should have pursued acquisitions of other unnamed companies (Appellants' Br. at 33), but identify no particular target or opportunity that the directors supposedly disregarded based on an improper motive.

Ultimately, all the Complaint alleged is that the directors rejected the Samuel, Son offer because they wanted to retain their positions and compensation. Under *Pogostin* and *Gantler*, that is not sufficient to overcome the business judgment rule. The Court of Chancery's judgment should be affirmed.

CONCLUSION

For the foregoing reasons, Appellees respectfully request that this Court affirm the Court of Chancery's order dismissing the Complaint with prejudice.

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