EFiled: Feb 27 2015 09:44PM EST
Filing ID 56842867
Case Number 629,2014

IN THE

Supreme Court of the State of Delaware

ROBERT A. CORWIN, *et al.*, Plaintiffs Below, Appellants, v. KKR FINANCIAL HOLDINGS LLC, *et al.*, Defendants Below, Appellees.	**No. 629, 2014** CASE BELOW: COURT OF CHANCERY OF THE STATE OF DELAWARE, C.A. No. 9210-CB

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February 27, 2015

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Pages(s)**

Statutes

Rules

Other Authorities

NATURE OF PROCEEDINGS

This case concerns the merger of KKR Financial Holdings LLC ("KFN") and KKR & Co. L.P. ("KKR"). The proposed merger was announced in December 2013 and was conditioned on the approval of both KFN's independent Transaction Committee and KFN's disinterested stockholders. The Court of Chancery consolidated various actions challenging the merger in January 2014. In February 2014, plaintiffs filed an amended complaint alleging, among other things, that KKR was KFN's controlling stockholder even though it held less than 0.1% of KFN's shares. Plaintiffs did not challenge the disclosures related to the merger or seek an injunction on any basis. The merger closed in April 2014.

In March 2014, defendants moved to dismiss. By Opinion dated October 14, 2014, the Court of Chancery granted the motion. On the basis of the facts alleged in the complaint and documents incorporated therein, the court held: (a) KKR was not KFN's controlling stockholder; (b) KFN's board of directors and the Transaction Committee formed to evaluate the KKR merger were independent and disinterested; (c) the merger proxy did not contain any material misrepresentations or omissions; and (d) the approval of the transaction by KFN's disinterested stockholders independently required application of the business judgment rule.

Plaintiffs filed their Notice of Appeal on November 13, 2014 and their opening brief on January 13, 2015. On appeal, plaintiffs do not dispute the trial court's holdings as to the independence and disinterest of the KFN directors or the sufficiency of the merger proxy, but, as described herein, they do raise several arguments never made below. This is defendants' answering brief.

SUMMARY OF ARGUMENT

1. Denied. The Court of Chancery properly concluded that the complaint failed to allege facts showing that KKR was KFN's controlling stockholder. Under Delaware law, a minority stockholder can be deemed controlling only when it exercises actual control over the business and affairs of a company through control of its board. The complaint does not plead facts showing that KKR controlled KFN's board, which plaintiffs do not now contest was majority independent. Moreover, even if KKR were a controlling stockholder, the complaint should be dismissed because the transaction is subject to business judgment review under *Kahn* v. *M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014).

2. Denied. Plaintiffs did not argue in the Court of Chancery that enhanced scrutiny applied to the challenged transaction. The argument is therefore waived under Rule 8. The argument also fails on the merits because (a) the complaint does not state a non-exculpated claim against KFN's concededly independent directors and (b) the fully informed vote of KFN's stockholders approving the merger requires application of the business judgment rule, as set out in point 3 below.

3. Denied. The Court of Chancery properly held that the fully informed approval of the transaction by stockholders required application of the business judgment rule. Plaintiffs did not argue in the Court of Chancery that *Gantler* v. *Stephens*, 965 A.2d 695 (Del. 2009), required a different result. The argument is therefore waived under Rule 8. The argument also fails on the merits because *Gantler* did nothing to disturb the settled principle that approval of a transaction by informed disinterested stockholders invokes the business judgment rule.

COUNTERSTATEMENT OF FACTS

A. KFN, the Management Agreement, and KFN's board of directors

KFN is a specialty-finance company in the business of investing in corporate debt and other sub-investment grade securities. ¶ 43.[1] KKR formed KFN as a Maryland REIT in 2004, and, in June 2005, KFN's shares were offered to the public in an IPO. ¶ 19. In 2007, upon the affirmative vote of its stockholders, KFN was reorganized as a publicly traded Delaware LLC. Op. 4-5; ¶ 43. At all times relevant to this lawsuit, KKR owned approximately 0.1% of KFN's outstanding shares. Op. 8 & n.13; ¶ 44.

KFN was organized under an LLC operating agreement (the "LLC Agreement"). Section 6.2 of the LLC Agreement provided that "the business and affairs of the Company shall be managed by or under the direction of its Board of Directors." Op. 8; A693. Section 6.3 provided that KFN's directors "shall have the same fiduciary duties to the Company and the Members as a director of a corporation incorporated under the DGCL." A695. Section 6.5 of the LLC Agreement provided that KFN's directors would be elected annually by a plurality of the votes cast. Op. 23 & n.53; A695. The LLC Agreement does not provide KKR with the right to appoint any directors or to direct or veto any board action.

At the time of the merger, KFN had twelve directors. Op. 25. Two (Nuttall and Farr) were employees of KKR; the other ten were not employees of either KFN or KKR. *Id.* In the proceedings below, plaintiffs admitted that all of the

[1] Citations of "¶ _" refer to the paragraphs of the amended Verified Consolidated Class Action Complaint, which appears in the record at A20-68.

directors were disinterested in the merger, but contended that eight directors lacked independence from KKR. Op. 24-25. The Court of Chancery ruled that the complaint failed to rebut the presumption of independence for a majority of the directors. Op. 31. Plaintiffs have not appealed that ruling.

When KFN went public in 2005, and at all times since, it has been a party to a management agreement (the "Management Agreement") with KKR Financial Advisors LLC, an affiliate of KKR (the "Manager"). Op. 3-8; A151, 379. This agreement was publicly disclosed in the 2005 IPO prospectus, in SEC disclosures filed in connection with the 2007 reorganization, and at all other times KFN's shares have publicly traded. Op. 3-8. KFN likewise disclosed at all times that the Manager was responsible for the company's operations and that the Manager had discretion with respect to the company's investment strategies. KFN disclosed throughout its existence as a public company that it was completely reliant on the Manager and that the company "may not find a suitable replacement" if the Management Agreement were terminated. ¶ 45; A151, 157.

Under the terms of the Management Agreement, KFN's independent directors reviewed the Manager's performance annually. ¶ 48. At the end of that review, KFN's independent directors and KFN's stockholders each had authority to terminate the Management Agreement on 180-days' notice if they concluded that the Manager's performance was unsatisfactory or the management fees were unfair. Op. 5; ¶ 48. In the event of such a termination, the company would be obligated to pay a termination fee, calculated under a formula, that is alleged to be over two hundred million dollars. Op. 7; ¶ 5. These termination provisions were

all disclosed to potential investors in connection with the 2005 IPO and repeatedly throughout KFN's existence as a public company. Op. 5-6; *e.g.*, A151-57, 167, 281, 357-58, 404, 454-55, 472. KFN could also terminate the Management Agreement for good cause without paying the termination fee. *See, e.g.*, A455.

The Management Agreement expressly provided that the Manager would in all events remain subject to the supervision of KFN's board of directors:

> The Manager, in its capacity as manager of the assets and the day-to-day operations of the Company, at all times will be subject to the supervision of the Company's Board of Directors and will have only such functions and authority as the Company may delegate to it.

Op. 7-8; A637.

B. KFN's independent Transaction Committee negotiates the merger

In October 2013, KKR expressed interest in offering to acquire KFN. Op. 8. At a board meeting on October 22, 2013, the board granted KKR's request to use confidential KFN information in the Manager's possession in making a bid. Op. 9; ¶ 83. KFN also asked Farr if KKR would consider modifying or waiving the Management Agreement's termination fee provision. Op. 9; ¶ 85. Farr relayed the request to KKR, which said no. *Id.*

On October 30, 2013, KKR submitted a proposal to acquire KFN for 0.46 KKR common units per KFN common share. Op. 9 & n.14; A802. KKR's offer was expressly conditioned on the approval of the transaction by both a committee of independent directors and a majority of KFN's unaffiliated stockholders. *Id.*

The next day, KFN's board formed a transaction committee consisting of directors Edwards, Collins, Finigan, Kari, McAneny, and Ryles, ¶¶ 74, 86, all of

whom plaintiffs now concede are independent and disinterested (the "Transaction Committee" or "Committee"). The Committee retained Sandler O'Neill + Partners L.P. as its financial advisor and Wachtell, Lipton, Rosen & Katz as its legal advisor. Op. 9; ¶¶ 11, 76. On November 21, 2013, the Committee met to evaluate KFN's prospects as a standalone company. ¶ 87. Believing that a cash deal might be more advantageous for KFN stockholders than a stock deal (because KFN's shares were trading near their one-year low while KKR's units were trading near their one-year high), the Committee proposed a cash deal to KKR, but KKR rejected the proposal. Op. 10; ¶ 88.

The Transaction Committee thereafter rejected KKR's 0.46 proposal (and a subsequent 0.48 proposal) and negotiated for improvements to the KKR offer. Op. 10 n.16; ¶ 88. At the Transaction Committee's request, lead independent director Hubbard met with the heads of KKR on December 9 to seek an improved exchange ratio. KKR at that time refused to increase the ratio over 0.50 KKR units per KFN share. ¶ 89. The next day, KKR's top leadership met with the KFN board, and, after the meeting, KKR made what it called its "best and final" offer of 0.51 KKR units per KFN share. ¶ 90. At the Transaction Committee's direction, director Hazen sought another increase to 0.52, but KKR refused. *Id.*

Three days later, on December 13, the Committee and board met to consider KKR's best and final offer. ¶ 91. Sandler presented its opinion that the proposed transaction was fair from a financial point of view to KFN's stockholders, and the Committee voted to recommend the transaction to the board. ¶¶ 91, 129. The board, excluding Farr and Nuttall, accepted the recommendation and voted in favor

of the transaction. ¶ 91. KKR and KFN executed the merger agreement on December 16. ¶ 92. The transaction's 0.51 exchange ratio reflected a 35% premium to KFN's closing price that day. Op. 11; ¶ 53.

C. A majority of KFN's unaffiliated stockholders approve the transaction

On March 24, 2014, KFN filed a definitive proxy statement (the "Proxy"). The Proxy provided stockholders over 200 pages of information about KFN, KKR, and the proposed transaction, and KFN appended to the Proxy and mailed to all stockholders the operative complaints challenging the merger. *See* A757-1132. Plaintiffs "made no effort to challenge the sufficiency or accuracy of the disclosures in the 2014 Proxy before the meeting of KFN's stockholders was held on April 30, 2014, or to seek to enjoin the closing of the transaction on any other basis." Op. 13. On April 30, 2014, KFN's stockholders voted in favor of the proposed merger, including a majority of the outstanding KFN common shares held by stockholders other than KKR and its affiliates. Op. 12.

D. The Court of Chancery dismisses the litigation

Defendants filed briefs in support of their motions to dismiss the action on April 7, 2014. A69-137. Plaintiffs filed an opposition brief on May 7, A1133-89, and defendants replied on May 21, A1199-248. The Court heard oral argument on the motions to dismiss on July 29. A1249-349. On October 14, 2014, the Chancellor issued an Opinion, published as *In re KKR Financial Holdings LLC Shareholder Litigation*, 101 A.3d 980 (Del. Ch. 2014), granting the motions and dismissing the action with prejudice. This appeal followed.

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY HELD THAT PLAINTIFFS FAILED TO PLEAD FACTS SHOWING KKR WAS A CONTROLLING STOCKHOLDER

A. Question Presented

Whether a stockholder holding 0.1% of the voting power of a company with an independent board, who is not alleged to have any veto or affirmative power over board action or to have made any coercive threats, can be a "controlling stockholder" because its affiliate manages the company's operations subject to the supervision of the board of directors and pursuant to a pre-existing management agreement. This issue was presented to the trial court. A95-97, 116-22, 1156-67, 1219-21, 1226-33, 1253-63, 1303-16, 1331-36.

B. Scope of Review

This Court reviews *de novo* the "decision to grant a motion to dismiss under Court of Chancery Rule 12(b)(6)." *Allen* v. *Encore Energy Partners, L.P.*, 72 A.3d 93, 100 (Del. 2013). Although well-pleaded allegations are accepted as true, the Court will not "credit conclusory allegations that are unsupported by specific facts or draw unreasonable inferences in the plaintiff's favor." *Id.*

C. Merits of Argument

Plaintiffs ask this Court to reach the unprecedented conclusion that a 0.1% stockholder with no board-level rights of any kind is a controlling stockholder by virtue of a management agreement that is subject to the supervision and direction of an independent board of directors. The Court of Chancery properly rejected this argument. The allegations do not satisfy Delaware's test for control. Nor do the

allegations of the complaint establish that KKR exercised control over the KFN board with respect to the challenged transaction. Finally, even if KKR were a controlling stockholder, the complaint is still subject to dismissal under the business judgment rule because the transaction satisfies all of the criteria of *Kahn* v. *M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014) ("*MFW*").

1. The allegations of the complaint do not support a finding that KKR is KFN's controlling stockholder

KKR owned less than 0.1% of KFN's stock. Where, as here, a stockholder holding less than 50% of a corporation's stock is alleged to be a controlling stockholder, the plaintiff must allege "that the minority stockholder exercised actual domination and control over the directors." *In re Morton's Rest. Grp., Inc. S'holders Litig.*, 74 A.3d 656, 664-65 (Del. Ch. 2013). As the Chancellor properly framed the issue, "the operative question" in applying this principle is whether "KKR controlled the KFN board . . . such that the directors of KFN could not freely exercise their judgment in determining whether or not to approve and recommend to the stockholders a merger with KKR." Op. 21-22.

This test "is not an easy one to satisfy." *In re PNB Holding Co. S'holders Litig.*, 2006 WL 2403999, at *9 (Del. Ch. Aug. 18, 2006). "[A] minority blockholder is not considered to be a controlling stockholder unless it exercises such formidable voting and managerial power that it, as a practical matter, is no differently situated than if it had majority voting control." *Morton's*, 74 A.3d at 665 (holding that 27.7% stockholder was not a controlling stockholder). An alleged controller must have sufficient voting power that it would "be the dominant

force in any contested . . . election." *In re Cysive, Inc. S'holders Litig.*, 836 A.2d 531, 551-52 (Del. Ch. 2003). "[T]he minority blockholder's power must be so potent that independent directors cannot freely exercise their judgment, fearing retribution from the controlling minority blockholder." *Morton's*, 74 A.3d at 665.

The allegations of the complaint here do not come close to satisfying the test. As the Chancellor held, "KKR's less than 1% position in KFN obviously would create no concern in the mind of KFN's directors that KKR possessed sufficient voting power to remove them from their positions if they rejected the merger proposal or took any other action KKR did not like." Op. 22. The complaint is completely devoid of any allegation that KKR threatened any retribution, let alone that KKR plausibly could make any such threat. There is thus nothing pleaded that could support the unlikely conclusion that KFN's 0.1% holder would "be the dominant force in any contested election," or that KKR is "no differently situated than if it had majority voting control," or that KKR in any way "exercised actual domination and control over [KFN's] directors."

Citing nothing, plaintiffs resort to the brand new claim that "a minority stockholder may control the company even without controlling the company's board." OB 15-16. This is not the law in Delaware. Under the LLC Agreement, "the business and affairs of [KFN] shall be managed by or under the direction of its Board of Directors." A693. Reflecting this broad grant of corporate authority, the Management Agreement made clear that the Manager was terminable by the board of directors and was "at all times" "subject to the supervision of the Company's Board of Directors." Op. 7-8; A637. At KFN, as with every Delaware company,

control rests with the board. *E.g.*, *Quickturn Design Sys., Inc*. v. *Shapiro*, 721 A.2d 1281, 1291-92 (Del. 1998) ("One of the most basic tenets of Delaware corporate law is that the board of directors has the ultimate responsibility for managing the business and affairs of a corporation.").

Confirming this principle, the courts have over and over made clear that in assessing whether a stockholder is controlling, "Delaware case law has focused on control of the board." *Superior Vision Servs., Inc.* v. *ReliaStar Life Ins. Co.*, 2006 WL 2521426, at *4 (Del. Ch. Aug. 25, 2006). Thus, in *Morton's*, the court examined whether the pleaded facts showed minority holder domination "over the directors," 74 A.2d at 665; in *In re Western National Corp. Shareholders Litigation*, the court held that a 46% stockholder was not a controller because no well-pleaded facts showed that the blockholder "dominated the Company's board of directors," 2000 WL 710192, at *25 (Del. Ch. May 22, 2000); in *In re Sea-Land Corp. Shareholders Litigation*, the court rejected a claim of control for lack of any allegation how the controller "influence[d] the . . . directors' conduct," 1987 WL 11283, at *5 (Del. Ch. May 22, 1987); and in *Superior Vision*, the court denied a controller claim because the allegations did not show the alleged controller's ability to influence "actions by the board," expressly noting that the question of control "should be assessed at the board level," 2006 WL 2521426, at *4 & n.38.

Most recently, Vice Chancellor Glasscock reached the same result in *In re Sanchez Energy Derivative Litigation*, holding that "minority stockholders are controllers only where they exercise actual control over the board." 2014 WL 6673895, at *8 (Del. Ch. Nov. 25, 2014). Even though the alleged controllers held

a collective 21.5% stake, were the founders and top executives of the company, had "the authority to direct the management of the Company," and "exercise[d] actual control over the operations of Sanchez Energy," they were nevertheless not controlling stockholders because they did not have "board control." *Id.* at *9.

Plaintiffs offer no authority to undermine the principle that corporate control must be assessed at the board level. Plaintiffs miss the mark with a books-and-records case, *Weinstein Enterprises, Inc.* v. *Orloff*, 870 A.2d 499 (Del. 2005), which they cite for the proposition that a stockholder may be controlling even when its power is "latent" as opposed to "active." OB 16. This Court held there that Weinstein Enterprises controlled another corporation, J.W. Mays, Inc., for purposes of 8 *Del. C.* § 220(a)(3), because Weinstein held 45.16% of Mays' stock directly and another "six or seven percent" through the Weinstein Foundation and because four out of seven Mays' directors were affiliated with Weinstein. 870 A.2d at 503, 507-08. *Weinstein* thus focused on the same factors highlighted in *PNB* and *Morton's*—voting power and control at the board level—finding majority stock ownership and majority board representation. Nothing in *Weinstein* supports plaintiffs' contention that a 0.1% stockholder with no board-level powers is a controlling stockholder with fiduciary duties.

Plaintiffs' reliance on the Court of Chancery's recent decision in *In re Zhongpin Inc. Stockholders Litigation*, 2014 WL 6735457 (Del. Ch. Nov. 26, 2014), fails for the same reason. *Zhongpin* involved a sale of a corporation to its founder, chairman, and CEO who held 17.3% of the stock and who teamed up with other stockholders (including another director) to form a financing group

comprising 26% of the corporation's stock. *Id.* at *1 & n.3. Contrary to plaintiffs' position, *Zhongpin* recognized that a claim of minority control required "specific allegations of domination [that] create an inference that [the minority holder] controlled the board." *Id.* at *7 n.23. Vice Chancellor Noble found that the test was met, because the minority blockholder concededly wielded outsized influence at the board level, including with respect to "the election of directors" and major corporate decisions such as mergers and acquisitions. *Id.* at *9. The court's analysis turned substantially on the blockholder's ability to use its large stake to drive board-level decisions, *id.*, and, in recognition of the blockholder's clout, the corporation in *Zhongpin* asserted in its public disclosures that the chairman/CEO was its "controlling shareholder," *id*. at *7. Here, to the contrary, KKR's minuscule stake negates any claim of electoral influence; KFN's board is concededly majority independent; there are no "specific allegations of domination" (or even general allegations of domination); and KFN always disclosed to its stockholders that control over the company's business and affairs remained vested with the board of directors. *See, e.g.*, A574; A986.

Finally, as they did below, plaintiffs seek to rely on the Court of Chancery's decision in *Williamson* v. *Cox Communications, Inc.*, 2006 WL 1586375 (Del. Ch. June 5, 2006). OB 17-18. In *Williamson*, the court recognized, in denying a motion to dismiss, the possibility that a stockholder group that held 17.1% of a company's voting power, appointed 40% of the board, had veto power over any significant board action, and comprised the company's most significant customers could be a controlling stockholder group. 2006 WL 1586375, at *5. Although

plaintiffs seek to analogize to the "significant leverage" that the group had over the company by virtue of their commercial relationship, OB 18, plaintiffs ignore the other, determinative elements of control alleged in *Williamson* but entirely absent here: meaningful voting power and board-level authority. As the Chancellor here explained below, the "17% stake [in *Williamson*] represents a whole different ballgame than [KKR's] less than 1% stake" in KFN and, unlike in *Williamson*, "the complaint here contains no well-pled facts from which it would be reasonable to infer that KKR could veto any action of the KFN board." Op. 24.

The Court of Chancery thus correctly held that a stockholder with no voting power and no board control cannot be a controlling stockholder under Delaware law. Plaintiffs have conceded (as they must) that no part of their claim of control derives from KKR's trivial share ownership. A1164. Under plaintiffs' theory, KKR could hold no shares at all and the result would be the same. They seek to have this Court ignore the well-settled law of controlling stockholders and create a brand new fiduciary doctrine of "controller," entirely untethered from share ownership, potentially applicable to a corporation's dealings with any contractual or commercial counterparty or even a management team, without regard to the alleged controller's influence in the boardroom or in a contested election. There is neither precedent nor warrant in Delaware law for such an outcome.

2. The complaint does not allege that KKR exercised any control over the board's decisions about the transaction

Plaintiffs also argue that KKR controlled the KFN board's decisions about the transaction. OB 12-14. But the alleged facts do not support this conclusion.

Plaintiffs do not dispute that KFN's directors were disinterested in the transaction and do not contest the Court of Chancery's holding that a majority of the board, and every member of the Transaction Committee, were independent of KKR. Plaintiffs do not allege that the Transaction Committee was unable to, or did not, retain its own advisors. Plaintiffs do not allege that KKR influenced KFN's ability to control the conduct of negotiations. Plaintiffs do not allege that the Committee lacked the unfettered power to say no to any proposed transaction.[2]

Plaintiffs are left to claim that the Management Agreement gave KKR control over the merger negotiations in two ways: first, because the agreement's termination provisions "foreclose[d] a market check," there was no "possibility of a topping bidder" for KFN; and, second, because the "Transaction Committee was negotiating against the same entity upon which it relied for information about KFN's value and operations," "KKR controlled the KFN Board's decisions with respect to the Transaction." OB 13. Neither argument succeeds.

Plaintiffs' contention that KKR controlled KFN because the Management Agreement's termination provisions precluded a higher offer is barred under the settled principle that compliance with a valid contract will not give rise to a fiduciary breach. Plaintiffs do not dispute that KKR fairly bargained for the terms of the Management Agreement, including its termination provisions. As Vice Chancellor Noble explained in *Superior Vision*, and as the Chancellor reaffirmed

[2] Although briefed and argued below, plaintiffs did not appeal dismissal of the aiding and abetting claim against KKR, thereby waiving any appeal on that issue. *See, e.g.*, *Roca* v. *E.I. du Pont de Nemours & Co.*, 842 A.2d 1238, 1242-43 (Del. 2004); Supr. Ct. R. 14(b)(vi)(A)(3). If this Court were to consider the aiding and abetting claim, the dismissal should be affirmed for the reasons argued below. *See* A78-87, 1209-11, 1296-301.

below, "a significant shareholder, who exercises a duly-obtained contractual right that somehow limits or restricts the actions that a corporation otherwise would take, does not become, without more, a 'controlling shareholder' for that particular purpose." 2006 WL 2521426, at *5; *see also* Op. 19-20 (citing *Superior Vision*). And the Court of Chancery has repeatedly held that neither directors nor an alleged controlling stockholder become liable for breach of duty merely by respecting the terms of an enforceable agreement.[3]

Plaintiffs try to distinguish *Superior Vision* in a footnote, saying that its reasoning does not apply here because the complaint in that case contained "no allegations [that] reached beyond exercising of contractual right[s]." OB 16 n.7. But this is the same argument plaintiffs make here. The only pleaded reason that KFN could not undertake a market check is the Management Agreement's termination provision. *See* ¶¶ 7, 49, 57-60, 85, 86, 94, 101, 149, 157. (As the Chancellor aptly put it, "[p]laintiffs' real grievance . . . is that KFN was structured from its inception in a way that limited its value-maximizing options," because of the "terms of the Management Agreement" and the "significant cost" of its termination provisions. Op. 22.) But claiming that a stockholder took "advantage

[3] *See Hokanson* v. *Petty*, 2008 WL 5169633, at *6 (Del. Ch. Dec. 10, 2008) (rejecting fiduciary breach claim: "[p]arties cannot repudiate their contracts simply because they wish they had gotten better terms"); *In re Sirius XM S'holder Litig.*, 2013 WL 5411268, at *5 (Del. Ch. Sept. 27, 2013) (rejecting fiduciary breach claim: "the board's inability to block [a] 'creeping takeover' was merely the manifestation of the bargain struck" years earlier). In rejecting plaintiffs' identical argument below, the Court of Chancery noted that "[e]very stockholder of KFN knew about the limitations the Management Agreement imposed on KFN's business when he, she or it acquired shares in KFN." Op. 22-23. Plaintiffs thus misunderstand the Court of Chancery when they attack this point in their opening brief. OB 16 n.6.

of its contractual rights for its own purposes" is "not sufficient to allege that [the shareholder] is a 'controlling shareholder' bound by fiduciary obligations." *Superior Vision*, 2006 WL 2521426, at *5; *see also Sirius XM*, 2013 WL 5411268, at *9 (rejecting allegations that the "exercise of [a preexisting] contractual right" could impose fiduciary duties on a stockholder); Op. 22 ("[E]very contractual obligation of a corporation constrains the corporation's freedom to operate to some degree, and in this particular case, the stockholders cannot claim to be surprised.").[4]

Plaintiffs also argue that KKR controlled the transaction process because the "Board and the Transaction Committee were entirely dependent on KKR for any and all Company information, including valuations and projections." OB 12-13. This contention is not supported by any factual allegations. The complaint nowhere alleges that KKR or the Manager ever manipulated or withheld information from the board or Transaction Committee or ever threatened to do so, and nowhere alleges that the board or Transaction Committee (or their advisors) lacked any information necessary to informed decision-making. To the contrary, the complaint alleges that KFN's board—which plaintiffs concede was majority independent—"granted KKR permission to use confidential information about KFN that KKR gained solely in its capacity as KFN's manager, in order to make an acquisition proposal." ¶ 83. Thus, plaintiffs allege that KKR was dependent on

[4] Moreover, any claim based on adherence to the terms of the Management Agreement is barred by Section 6.3 of the LLC Agreement, which provides that "any actions or inaction of the Directors . . . that cause the Company to act in compliance or in accordance with the Management Agreement shall be deemed consistent and compliant with the fiduciary duties of such Directors and shall not constitute a breach of any duty." Op. 8 n.12; A695.

KFN's board for information—not the other way around. The contention that KKR controlled the transaction process by its control of information should be dismissed as not only unsupported but indeed contradicted by the complaint. *See In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 170 (Del. 2006).

Plaintiffs' argument reduces to the claim that management controls corporate information and must be assumed to use it in the service of its own interest, even when there are no well-pleaded facts to support that assumption. If accepted, this contention would subject every corporate transaction in which management has an interest (including every management-led buyout) to entire fairness review. But Delaware law holds otherwise. *See, e.g., In re Netsmart Techs., Inc. S'holders Litig.*, 924 A.2d 171, 193 (Del. Ch. 2007) (concluding that company's CEO "did not have anything approaching the clout of a controlling stockholder" despite owning about 4% of company's equity, being financially interested in proposed merger transaction, providing information to a financial advisor, and being permitted to run negotiation process "without close oversight"); *In re Dell, Inc. S'holder Litig.*, C.A. No. 8329-CS, at 8-9 (Del. Ch. June 19, 2013) (trans.) (applying *Revlon* review in denying expedition in case challenging buyout led by CEO who owned over 15% of company, an amount that is "not anywhere close to the level of stock ownership that's ever been considered a controlling stockholder"); *Kohls* v. *Duthie*, 765 A.2d 1274, 1286 (Del. Ch. 2000) (concluding that business judgment review applied to management buyout transaction).

Finally, in this Court plaintiffs tack on the conjecture that the Management Agreement gave KKR potential leverage that plaintiffs speculate could have been

used to bully the board. *See* OB 13 (speculating about the effects of a hypothetical "decision by KKR to sever its arrangement with KFN"). This was not pleaded or argued below and is accordingly waived. Moreover, plaintiffs do not argue (let alone allege) that KKR ever exercised or even threatened to exercise any such potential leverage in such a fashion. Nor do they argue (let alone allege) that KKR could have terminated the agreement without itself incurring substantial economic harm. And, in raising this new and unalleged claim in this Court, plaintiffs fail to mention that it is expressly negated by proxy materials making clear that if there were no transaction, KKR would not make any changes to the Management Agreement and would remain committed to KFN's success. A805.

This argument fails on the law as well as the (un)alleged facts. Delaware law has repeatedly rejected claims (just like this one) that a stockholder could theoretically, but does not actually, dominate corporate affairs. *See, e.g.*, *Sanchez Energy*, 2014 WL 6673895, at *9 (rejecting argument that 21.5% stockholders with managerial authority were controllers where complaint did not allege they had "even attempted to dominate the board through threats, bullying, or the like"); *W. Nat'l*, 2000 WL 710192, at *7-8 (rejecting argument that 46% stockholder was a controller where stockholder did not threaten or attempt to dominate board); *Sea-Land*, 1987 WL 11283, at *5 (rejecting argument that 40% stockholder who had the "potential ability to frustrate a competing bid" was a controller because "the *potential* ability to exercise control is not equivalent to the actual *exercise* of that ability"); *Gilbert* v. *El Paso Co.*, 490 A.2d 1050, 1056 (Del. Ch. 1984) (rejecting argument that stockholder with "potential for control" was a controller because

"breach of fiduciary relationship must subsist on the actuality of a specific legal relationship, not in its potential"), *aff'd*, 575 A.2d 1131 (Del. 1990). Not even "a large blockholder," let alone a 0.1% holder like KKR, can be "considered a controlling stockholder unless they *actually control* the board's decisions about the challenged transaction." *In re Crimson Exploration Inc. Stockholder Litig.*, 2014 WL 5449419, at *12 (Del. Ch. Oct. 24, 2014) (emphasis added).

3. Even if KKR were a controlling stockholder, the complaint should nevertheless be dismissed under *MFW*

In their opening brief, plaintiffs appear to recognize that even controller transactions can be subject to dismissal, but contend that their complaint should not be dismissed under *MFW* because the transaction here failed to satisfy its criteria. OB 23 n.11, 28-29 & n.13. *MFW* held that business judgment review governs "controller buyouts" where "(i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority." 88 A.3d at 645. Contrary to plaintiffs' argument, each of those criteria was satisfied here.

Indeed, plaintiffs appear to concede that elements (i), (ii), (iii), (v), and (vi) were met. OB 28 n.13. They nowhere dispute that the transaction was always and from the beginning conditioned on approval by an independent special committee

and a majority of the non-KFN shares or that the Transaction Committee was empowered to select its own advisors and say no definitively; they have abandoned any challenge to the independence of any Transaction Committee member or the sufficiency of the stockholder vote; and they have never alleged coercion of the minority.

Plaintiffs dispute only item (iv), offering the conclusion that they "alleged that the Transaction Committee breached its duty of care, including by allowing conflicted Board members to negotiate material aspects of the Transaction." *Id.* But the complaint concedes that the Transaction Committee bargained for improved merger terms, ¶ 88, and does not allege that "conflicted board members" negotiated anything. And while plaintiffs assert the conclusion that Hazen was permitted to "lead and control KFN's role in the deal negotiations," ¶ 80, there are no facts pleaded from which this conclusion can be reasonably inferred. *See In re Coca-Cola Enters., Inc. S'holders Litig.*, 2007 WL 3122370, at *2 (Del. Ch. Oct. 17, 2007) ("An allegation is conclusory when it merely states a generalized conclusion with no supporting facts."). All the complaint alleges is that "Hazen raised with Defendant Farr—who serves as President, CEO, and Director of KFN, and is a senior KKR executive—whether KKR would consider modifying or eliminating the Termination Fee in the Management Agreement," ¶ 85, and that Hazen, at the Committee's request, later contacted KKR during negotiations to ask for another price increase, ¶ 90. No other fact is alleged suggesting that Hazen was even involved in negotiations, let alone that he led them. These allegations are not even close to showing the gross negligence necessary to sustain a duty of care

violation. *See Morton's*, 74 A.3d at 665 ("[I]t is not unusual for certain directors or members of management to take an active role in spearheading a sales process."); *Wayne Cnty. Emps.' Ret. Sys.* v. *Corti*, 2009 WL 2219260, at *13 (Del. Ch. July 24, 2009).

Recently confirming that *MFW* permits dismissal at the pleadings stage, the Court of Chancery rejected duty-of-care arguments just like those plaintiffs offer here. In *Swomley* v. *Schlecht*, C.A. No. 9355-VCL (Del. Ch. Aug. 27, 2014) (trans.), Vice Chancellor Laster explained that the "[d]uty of care is measured by a gross negligence standard," which "is a very tough standard to satisfy" and is "only satisfied by conduct that really requires recklessness" or "wanton conduct." The plaintiffs in *Swomley*, like plaintiffs here, tried to establish a care violation by "disagree[ing] with the committee's strategy or tactics," arguing that the committee should have made different choices in its sales process, but the court held that quibbling about negotiation strategy "isn't a duty of care violation." *Id.* The same result is mandated here. Plaintiffs' quibbles with the Transaction Committee's tactics cannot establish "gross negligence" and do not prevent the determinative application of *MFW*.

II. THE COMPLAINT FAILED TO STATE A NON-EXCULPATED CLAIM UNDER ENHANCED SCRUTINY

A. Question Presented

Whether allegations disagreeing with the negotiating tactics of disinterested and independent directors state a non-exculpated claim under enhanced scrutiny. The issue was not presented to the Court of Chancery. A1176.

B. Scope of Review

This Court's review is *de novo*. *See* Section I.B., *supra*.

C. Merits of Argument

Plaintiffs' argument that the transaction must be subjected to enhanced scrutiny was not fairly presented to the court below and is waived. In any event, the Court of Chancery did not commit reversible error, both because the transaction is properly reviewed under the business judgment rule and because the complaint does not state a non-exculpated claim even under enhanced scrutiny.

1. Plaintiffs' *Revlon* argument is barred by Rule 8

Plaintiffs attack the Court of Chancery for its statement that "[e]nhanced judicial scrutiny under *Revlon* is not implicated in this action because the stock-for-stock merger involved widely-held, publicly traded companies." OB 20 (quoting Op. 13). But plaintiffs never argued that enhanced scrutiny applied in the proceedings below. Plaintiffs never even cited *Revlon*, A1136-39, and asserted that "this is not a traditional *Revlon* case," A1176. Instead, plaintiffs' exclusive argument in the Court of Chancery was that entire fairness was the appropriate standard of review, either because KKR was KFN's controlling stockholder, A1156, or because a majority of KFN's directors were not disinterested and

independent, A1170. For the reasons discussed above, plaintiffs' control argument was properly rejected, and plaintiffs have now conceded the independence and disinterest of the Transaction Committee and a majority of KFN's directors. Plaintiffs' argument that *Revlon* should supply the standard of review was not fairly presented to the court below, and plaintiffs do not even try to explain why it should now be heard in the interests of justice. *See* OB 19. The argument is therefore barred by Rule 8. *Sweeney* v. *Del. Dep't of Transp.*, 55 A.3d 337, 342 n.23 (Del. 2012) (holding that appellant's failure to argue in the alternative for "intermediate scrutiny" before the trial court means the "argument is waived on appeal" under Rule 8).

2. Even if *Revlon* applies, the complaint does not state a claim

Even if plaintiffs had preserved their *Revlon* claim below, it would fail on the merits on two independent grounds. First, as discussed below in Section III, even if *Revlon* applied to the transaction at the outset, the Court of Chancery properly held that the fully informed approval of KFN's stockholders lowered the standard of review to business judgment. *See* Op. 31-41. Second, as discussed immediately below, the complaint does not make out a non-exculpated claim.

Plaintiffs seek only monetary damages, A66, but the exculpatory provision in Section 13.3(b) of KFN's LLC Agreement limits the recovery of damages from KFN's directors, A718. As a result, plaintiffs cannot state a claim under enhanced scrutiny unless they plead facts showing the directors acted disloyally or in bad faith. *See In re NYMEX S'holder Litig.*, 2009 WL 3206051, at *6 (Del. Ch. Sept. 30, 2009) ("[E]ven if *Revlon* applied to this case, application of the exculpatory

clause would lead to dismissal unless the Plaintiffs have successfully pleaded a failure to act loyally (or in good faith), which would preclude reliance on the Section 102(b)(7) provision."). Plaintiffs have not done so here.

The complaint did not allege that KFN's directors were interested in the merger, and plaintiffs no longer contest the independence of a majority of the board. There is thus no possible claim of disloyalty. This leaves bad faith as the only avenue available for stating a damages claim. *Id.* "Adequately pleading bad faith conduct on the part of a director requires allegations of an 'extreme set of facts' in order to give rise to the 'notion that disinterested directors were intentionally disregarding their duties.'" *In re Comverge, Inc. S'holders Litig.*, 2014 WL 6686570, at *13 (Del. Ch. Nov. 25, 2014) (quoting *Lyondell Chem. Co.* v. *Ryan*, 970 A.2d 235, 243 (Del. 2009)). To "adequately plead[] bad faith conduct as to the sale process," a complaint must allege facts supporting the inference "that the decision to approve the Merger was so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith." *Id.*

Plaintiffs' complaint does not even approach the gross negligence necessary to state a claim for breach of the duty of care, still less the "extreme" facts necessary to allege bad faith. The complaint does not allege even the conclusion that KKR or anyone associated with it dominated the Transaction Committee or the KFN board. To the contrary, the pleaded facts confirm that the KFN board formed a Transaction Committee empowered to evaluate the proposal and negotiate the best deal possible. ¶ 74. The complaint acknowledges that the

independent Transaction Committee hired outside advisors, ¶¶ 11, 76; sought modifications to the Management Agreement to enable a more robust bidding process, ¶ 85; evaluated its options as a standalone company, ¶ 87; pushed for cash consideration, ¶ 88; structured the transaction to comply with *MFW*, Op. 9 n.14; and ultimately succeeded in securing improvements to the bid so that the final price represented "an approximately 35% premium" that Sandler concluded was fair, ¶¶ 53, 88, 129. These allegations negate any claim of bad faith. *E.g.*, *In re BioClinica, Inc. S'holder Litig.*, 2013 WL 5631233, at *6 (Del. Ch. Oct. 16, 2013) (dismissing "bad faith" claims because the pleaded facts showed the board "satisf[ied] its *Revlon* duties by forming a committee of independent directors, engaging . . . financial advising services, and retaining independent legal counsel").

All that is left is for plaintiffs to disagree with certain of the actions taken by disinterested and independent KFN directors in the course of negotiating the transaction. But "[b]ad faith cannot be shown by merely showing that the directors failed to do all they should have done under the circumstances." *Corti*, 2009 WL 2219260, at *14. For example, plaintiffs take issue with the fact that the board relied on a fairness opinion that was based on information provided by KFN's Manager, which was affiliated with KKR. OB 21. This allegation cannot "establish a non-exculpated breach of fiduciary duty claim," because plaintiffs have not pleaded "non-conclusory facts creating the reasonable inference that the board purposely relied on analyses that were inaccurate for some improper reason." *Morton's*, 74 A.3d at 673. Plaintiffs do not even allege that the

information provided by the Manager was inaccurate or incomplete in any respect, let alone that the KFN board relied on information it knew to be inaccurate.

Nor can plaintiffs survive dismissal by quibbling with the Transaction Committee's decision to involve Hazen and Hubbard in certain aspects of the negotiation. OB 21. "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" even to interested or non-independent individuals. *NYMEX*, 2009 WL 3206051, at *7; *see also In re Plains Exploration & Prod. Co. Stockholder Litig.*, 2013 WL 1909124, at *5 (Del. Ch. May 9, 2013) (rejecting *Revlon* challenge to board's decision to allow interested member of management to "run the negotiations" where majority independent board oversaw negotiation process); *Morton's*, 74 A.3d at 665.

Plaintiffs thus do nothing more than nitpick the decisions of independent and disinterested directors. As this Court recently admonished, however, "*Revlon* was largely about a board's resistance to a particular bidder and its subsequent attempts to prevent market forces from surfacing the highest bid"—"'it is not a license for law-trained courts to second-guess reasonable, but debatable, tactical choices that directors have made in good faith.'" *C&J Energy Servs., Inc.* v. *City of Miami Gen. Emps.' & Sanitation Emps.' Ret. Trust*, --- A.3d ---, 2014 WL 7243153, at *14 n.85, *16 (Del. Dec. 19, 2014) (quoting *In re Toys "R" Us, Inc. S'holder Litig.*, 877 A.2d 975, 1000 (Del. Ch. 2005)).

III. THE COURT OF CHANCERY PROPERLY HELD THAT FULLY INFORMED STOCKHOLDER APPROVAL LOWERED THE STANDARD OF REVIEW TO BUSINESS JUDGMENT

A. Question Presented

Whether the approval of the transaction by the fully informed vote of independent stockholders invokes the business judgment standard of review. Plaintiffs did not contest this issue in the trial court. A1179-85; Op. 37.

B. Scope of Review

This Court's review is *de novo. See* Section I.B., *supra*.

C. Merits of Argument

1. Plaintiffs agreed with defendants in the court below and their new argument is barred by Rule 8

As the Chancellor held below, plaintiffs did "not disagree with defendants' position that the legal effect of a fully-informed stockholder vote of a transaction with a non-controlling stockholder is that the business judgment rule applies and insulates the transaction from all attacks other than on the grounds of waste." Op. 37; Op. 32 (citing A1179-85). Now, relying on *Gantler* v. *Stephens*, 965 A.2d 695 (Del. 2009), plaintiffs try to raise precisely the position they conceded below.

But plaintiffs did not even cite *Gantler* in the trial court, let alone premise an argument on it. In its moving brief below, KFN argued as an independent point that "[t]he fully informed vote of the KFN common shareholders requires application of the business judgment rule." A131-33, 1242-46. Plaintiffs never disputed this rule of law. They argued in response only that the rule did not apply because KKR was a controlling stockholder and because the complaint adequately pleaded a disclosure violation. A1179-85. The Chancellor rejected both arguments, holding

as to the disclosure claims that "the KFN stockholder vote approving the merger was fully informed." Op. 36. Plaintiffs have not appealed that ruling.

KFN thus squarely raised the contention that a fully informed stockholder vote requires application of the business judgment rule; plaintiffs never opposed or even addressed it; and the trial court properly concluded that the issue was not contested. The point is waived and not properly presented on appeal. *See, e.g.*, *In re Phila. Stock Exch., Inc.*, 945 A.2d 1123, 1135 (Del. 2008).

2. Fully informed stockholder approval of a transaction with a non-controlling stockholder lowers the applicable standard of review to business judgment

The point also fails on the merits. Delaware has "a long and sensible tradition" of deferring to stockholders' informed decisions, "invoking the business judgment rule standard of review" in these circumstances and "limiting any challenges to the difficult argument that the transaction constituted waste." *Morton's*, 74 A.3d at 663 n.34. Plaintiffs' argument boils down to the claim that Justice Jacobs' *Gantler* decision overruled this sensible tradition, but their position misreads *Gantler* and the long line of cases preceding and following it.

As far back as 1979, this Court applied the business judgment standard of review to board action approved by an informed, disinterested electorate. *Michelson* v. *Duncan*, 407 A.2d 211, 224 (Del. 1979). Delaware law has been uniform on the point since. Writing as a Vice Chancellor in 1995, Justice Jacobs held that the fully informed stockholder approval of a merger transaction lowered the standard of review to business judgment, with the plaintiffs bearing the burden of proof. *In re Wheelabrator Techs., Inc. S'holders Litig.*, 663 A.2d 1194, 1201-05

(Del. Ch. 1995). Justice Jacobs also noted uncertainty about the use of the term "ratification," *id.* at 1201 n.4—but his ultimate holding made clear that, whatever the terminology, a fully informed stockholder vote generally required application of the business judgment rule.

Following this well-settled principle, Vice Chancellor Lamb in *In re Lukens Inc. Shareholders Litigation* held that the fully informed approval of a merger transaction by stockholders eliminated the court's review of a well-pleaded "*Revlon* claim," because the vote lowered the standard of review. 757 A.2d 720, 738 (Del. Ch. 1999). This Court affirmed that decision by summary order "on the basis of and for the reasons assigned by the Court of Chancery in its well-reasoned opinion." *Walker* v. *Lukens, Inc.*, 757 A.2d 1278 (Del. 2000).

Chancellor Chandler applied the same legal rule in *Solomon* v. *Armstrong*, where he held that "so long as the shareholder vote to approve or disapprove the transaction was made on a fully-informed, non-coerced basis, that vote operates *ex proprio vigore* as an independent foundation for the application of the business judgment rule." 747 A.2d 1098, 1127 (Del. Ch. 1999). This Court affirmed that opinion as well, again "on the basis of and for the reasons assigned by the Court of Chancery in its well-reasoned decision." *Solomon* v. *Armstrong*, 746 A.2d 277 (Del. 2000).

Then-Vice Chancellor Strine reached the same conclusion in *Harbor Finance Partners* v. *Huizenga*, holding that "the effect of untainted stockholder approval of the Merger is to invoke the protection of the business judgment rule and to insulate the Merger from all attacks other than on the ground of waste,"

while at the same time noting the complexities of "nomenclature" regarding the word "ratification." 751 A.2d 879, 890, 900 n.78 (Del. Ch. 1999); *see also In re Gen. Motors Class H S'holders Litig.*, 734 A.2d 611, 616 (Del. Ch. 1999) ("Because the shareholders were afforded the opportunity to decide for themselves on accurate disclosures and in a non-coercive atmosphere, the business judgment rule applies.").

Writing for this Court in *Gantler*, Justice Jacobs undertook to clarify the uncertainty he had identified in *Wheelabrator*, holding "that the scope of the shareholder ratification doctrine must be limited to its so-called 'classic' form; that is, to circumstances where a fully informed shareholder vote approves director action that does *not* legally require shareholder approval in order to become legally effective." 965 A.2d at 713. But because the proxy statement at issue in *Gantler* was held to be materially misleading, the *Gantler* Court had no occasion to consider the legal effect of a fully informed stockholder vote when the vote is statutorily required. *Id.* at 714.

Plaintiffs nevertheless argue that *Gantler* overruled the long-settled rule that fully informed stockholder approval of a transaction—even when statutorily required—lowers the standard of review to business judgment. OB 25. To accept this argument would require the Court to conclude that Justice Jacobs was overruling his own opinion in *Wheelabrator*, Vice Chancellor Lamb's opinion (and this Court's affirmance) in *Lukens*, Chancellor Chandler's opinion (and this Court's affirmance) in *Solomon*, and then-Vice Chancellor Strine's opinions in *General Motors* and *Harbor Finance*—all without ever saying he was doing so, and despite

his otherwise express language overruling only *Van Gorkom*. *See* 965 A.2d at 713 n.54. Such a result is implausible, as Vice Chancellor Laster recently explained:

> [I]f *Gantler* actually held that an organic vote cannot affect the standard of review, then the decision would have represented a radical break with precedent. For the price of clarifying the linguistic confusion that *Van Gorkom* created, the decision would have overruled the parade of precedents—including *Wheelabrator II*—that held that an organic vote does affect the standard of review. Nothing about *Gantler* suggests an intention to overrule so many cases or such a significant aspect of Delaware doctrine. To the contrary, it appears that *Gantler* intended to elevate the trial court level discussion in *Wheelabrator II* to the status of authoritative Delaware Supreme Court precedent.

J. Travis Laster, *The Effect of Stockholder Approval on Enhanced Scrutiny*, 40 Wm. Mitchell L. Rev. 1443, 1488-89 (2014).

For these reasons, courts have not read *Gantler* to have overruled a long line of cases *sub silentio*. To the contrary, the Court of Chancery has continued to hold that the informed vote of disinterested stockholders requires application of the business judgment rule. Thus, in *In re Southern Peru Copper Corp. Shareholder Derivative Litigation*, then-Chancellor Strine explained that "it has long been my understanding of Delaware law that the approval of an uncoerced, disinterested electorate of a merger (including a sale) would have the effect of invoking the business judgment rule standard of review." 52 A.3d 761, 793 n.113 (Del. Ch. 2011). The Chief Justice then went on to note that "[p]erhaps a more nuanced nomenclature is needed to describe the traditional effect that a disinterested stockholder vote has had on the standard of review used to evaluate a challenge to

an arm's length, third-party merger and to distinguish it from 'classic' or 'pure ratification,'" "but I have long understood that under our law it would invoke the business judgment rule standard of review." *Id.*

More recently in *Morton's*, the Court of Chancery explained that "when disinterested approval of a sale to an arm's-length buyer is given by a majority of stockholders who have had the chance to consider whether or not to approve a transaction for themselves, there is a long and sensible tradition of giving deference to the stockholders' voluntary decision, invoking the business judgment rule standard of review, and limiting any challenges to the difficult argument that the transaction constituted waste." 74 A.3d 663 n.34.

The careful analysis below reached the same conclusion. "To read [*Gantler* as plaintiffs now propose]," the Chancellor wrote, "would mean that the Supreme Court intended to overrule extensive precedent, including Justice Jacobs' own earlier decision in *Wheelabrator*." Op. 39. "Had the Supreme Court intended to do so, I believe the Court would have expressly stated such an intention. Instead, I read the Supreme Court's discussion of the doctrine of ratification in *Gantler* to have been intended simply to clarify that the term 'ratification' applies only to a voluntary stockholder vote." Op. 39-40.

Plaintiffs ignore all of this post-*Gantler* learning. OB 22-30. They support their misreading of that case only by misreading another pre-*Gantler* decision—*In re Santa Fe Pacific Corp. Shareholder Litigation*, 669 A.2d 59 (Del. 1995)—which plaintiffs wrongly say held that "a stockholder vote may never lower the standard of review for claims subject to enhanced judicial scrutiny." OB 26-27.

The issue in *Santa Fe* was whether "the fully-informed vote of a majority of Santa Fe stockholders extinguishes the Plaintiffs' claims under *Unocal* v. *Mesa Petroleum Co.*, Del. Supr., 493 A.2d 946 (1985), and *Revlon, Inc*. v. *MacAndrews & Forbes Holdings, Inc*., Del. Supr., 506 A.2d 173 (1986)." 669 A.2d at 67. The Court held only that the vote could not "remove from judicial scrutiny unilateral Board action in a contest for corporate control." *Id.* at 68. *Santa Fe* thus holds that fully informed stockholder approval cannot eliminate judicial review altogether. It says nothing about the effect of such approval on the level of review applied.[5]

The answer to that question—what is the effect of fully informed stockholder approval on the level of judicial scrutiny—has been well-settled in Delaware for decades: when an independent stockholder body approves a third-party merger transaction in a fully informed, uncoerced vote, the standard of review is lowered to business judgment review, with plaintiffs bearing the burden of pleading facts to show that the transaction constituted waste.[6]

[5] Plaintiffs' reliance on *eBay Domestic Holdings, Inc.* v. *Newmark*, 16 A.3d 1 (Del. Ch. 2010), and *Gentili* v. *L.O.M. Med. Int'l, Inc.*, 2012 WL 3552685 (Del. Ch. Aug. 17, 2012), is misplaced. These decisions merely restate *Gantler*'s analysis of "classic ratification." Neither suggests, let alone holds, that a statutorily required vote does not affect the standard of review. *eBay* held that approval of interested stockholders did not change the standard of review, 16 A.3d at 42 n.147, and *Gentili* held that there could be no ratification where "[t]here was no Board action to ratify," 2012 WL 3552685, at *3. Neither decision is relevant here.

[6] Plaintiffs also argue that stockholder approval, without more, does not change the standard of review of a transaction involving a controlling stockholder or a non-independent board. OB 28-30. This contention is not relevant to the appeal, because this transaction did not involve a controlling stockholder (as the Court of Chancery properly held, *see* Section I, *supra*) or a non-independent board (as plaintiffs no longer contest).

CONCLUSION

The judgment of the Court of Chancery should be affirmed.

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