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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

APPELLANTS' OPENING BRIEF

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NATURE OF PROCEEDINGS

Plaintiffs below-appellants Buttonwood Tree Value Partners, LP ("Buttonwood") and Franklin Value Investors Trust—Franklin MicroCap Value Fund ("Franklin" and, together with Buttonwood, "Plaintiffs") brought this action against the directors of Central Steel and Wire Company ("CSTW" or the "Company"), a Delaware corporation. Specifically, Plaintiffs' claims arise from the CSTW directors' self-interested rejection of and outright refusal to consider strategic opportunities for the Company. As Plaintiffs alleged in their Second Amended and Consolidated Verified Class Action and Derivative Complaint (the "Complaint"), these directors – none of whom owns a material number of CSTW shares – continually have favored their own economic interests as lifetime Company insiders in breach of their fiduciary duties to CSTW stockholders.

Plaintiffs filed the Complaint with the Court of Chancery on November 10, 2014. On December 3, 2014, nominal defendant CSTW answered the Complaint while the Company's directors – consisting of defendants below-appellees Michael J. Sullivan, Stephen E. Fuhrman, Kevin G. Powers, James E. Rinn, Ronald V. Kazmar, Michael X. Cronin, John F. Calhoun and Christopher M. Rodgers (collectively, the "Individual Defendants") – filed a Motion to Dismiss pursuant to Court of Chancery Rule 12(b)(6).

Following briefing on the Individual Defendants' Motion to Dismiss, the

Court of Chancery held oral argument on March 17, 2015. At the conclusion of oral argument, the trial court issued a bench ruling granting the Individual Defendants' Motion on the sole ground that dismissal was mandated by this Court's opinion in *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009) (hereinafter, "*Gantler*"). *See* Ex. A. Specifically, the Court of Chancery held that *Gantler* required it to: (i) disregard specific allegations of the Individual Defendants' entrenchment-motivated conduct; and (ii) absent allegations of unrelated self-interest, apply the business judgment rule. As a result, on March 17, 2015, the Court of Chancery entered an Order dismissing the Complaint with prejudice for the reasons it stated on the record earlier that day. *See* Ex. B. Plaintiffs filed a Motion for Reargument of the trial court's ruling, which was denied by Order dated April 1, 2015. *See* Ex. C. Plaintiffs thereafter commenced this appeal on April 10, 2015.

SUMMARY OF ARGUMENT

1. CSTW's ownership and governance structures are unusual. First, a majority of the Company's shares are owned by a charitable trust, The James R. Lowenstine Conserve School Trust (the "Conserve School Trust" or the "Trust"). Second, all directors of CSTW are trustees of the Trust and, conversely, all trustees are CSTW directors. Due to this unique relationship, the Company's directors are self-perpetuating and answer only to themselves. At all times since the Trust was established, no one outside of CSTW's senior management has served as a Director of the Company or as a trustee of the Trust – even though the Trust's governing document does not require that directors or trustees hold senior management positions. None of the Individual Defendants personally holds, or has ever held, a sizable block of CSTW stock; instead, they hold (or held) well-paying senior management positions at the Company, immune from outside review or accountability, with exceedingly generous lifetime benefits. The Complaint rebuts the business judgment rule by alleging specific facts through which the Individual Defendants have acted in their self-interest, consistently and repeatedly rejecting or ignoring all potential strategic alternatives for CSTW based, admittedly, on nothing more than their desire to maintain control over the Company and the Trust.

2. The Court of Chancery rightly expressed concern about the facts alleged in the Complaint, stating that "but for [*Gantler*], I think this case might

well survive a motion to dismiss." Ex. A at 80. The trial court nonetheless dismissed Plaintiffs' claims, stating "I think *Gantler* requires me to apply the business judgment rule at this stage." *Id.* The Court of Chancery erred when it held, in reliance upon *Gantler*, that: (i) only allegations of self-interest unrelated to the Individual Defendants' board and management positions would avoid application of the business judgment rule; and (ii) specific allegations of the Individual Defendants' conduct in furtherance of their entrenchment motive (including an admission that they acted for entrenchment purposes) must be disregarded.

STATEMENT OF FACTS

The facts set forth below are taken from the Complaint (cited as "SAC"). In reviewing a ruling on a motion to dismiss, this Court (i) accepts all well pleaded factual allegations as true, (ii) accepts even vague allegations as "well pleaded" if they give the opposing party notice of the claim, and (iii) draws all reasonable inferences in favor of the non-moving party. *Central Mortgage Co. v. Morgan Stanley Mortgage Capital Holdings LLC*, 27 A.3d 531, 535 (Del. 2011) (hereinafter, "*Central Mortgage*").

I. THE PARTIES.

A. Plaintiffs.

Buttonwood is the record owner of 900 shares of CSTW common stock and has owned shares of the Company's common stock continuously since August 7, 2007. A 14 (SAC ¶ 4). Franklin is the record owner of 6,905 shares of CSTW common stock and has owned shares of the Company's common stock continuously since March 5, 2001. A 15 (SAC ¶ 5).

B. CSTW.

CSTW is a Delaware corporation headquartered in Chicago, Illinois, that distributes and processes ferrous and non-ferrous metal products. A 15 (SAC ¶ 6). Originally, the James R. Lowenstine Trust (the "Lowenstine Trust") was the controlling stockholder of CSTW. *Id.* Later, the Lowenstine Trust directed that its

shares of CSTW common stock be held in the Conserve School Trust, which operated under the umbrella of the Lowenstine Trust. *Id.*[1] The Conserve School Trust currently owns approximately 62.1% of CSTW's outstanding shares of common stock and at all times relevant to Plaintiffs' claims was the Company's controlling stockholder. *Id.*

C. CSTW's Current Board.

Defendant Michael J. Sullivan ("Sullivan") served as a Director of CSTW at all times relevant to Plaintiffs' claims and has served as the Company's Chief Executive Officer and Chairman of the Board since October 6, 2011. A 15 (SAC ¶ 7). Sullivan also serves as a trustee of the Central Steel & Wire Profit Sharing Trust (the "Profit Sharing Plan") and is believed to serve as a trustee of the Conserve School Trust. *Id.* Sullivan personally owns 203 shares of CSTW. *Id.*

Defendant Stephen Fuhrman ("Fuhrman") is President and a Director of CSTW and is believed to serve as a trustee of the Conserve School Trust. A 16 (SAC ¶ 8). Fuhrman became a CSTW Director on October 6, 2011 and personally owns no shares of the Company's stock. *Id.*

Defendant Kevin G. Powers ("Powers") is Vice President, Chief Financial Officer, Treasurer and a Director of CSTW and is believed to serve as a trustee of

[1] It is believed that the Lowenstine Trust ceased to exist after James Lowenstine's death and its shares of CSTW common stock were then distributed to the Conserve School Trust. A 15 (SAC ¶ 6).

the Conserve School Trust. A 16 (SAC ¶ 9). Powers became Chief Financial Officer, Vice President and a Director of CSTW on or after April 21, 2014, and personally owns no shares of the Company's stock. *Id.*

Defendant James E. Rinn ("Rinn") is Vice President, Corporate Secretary and a Director of CSTW and is believed to serve as a trustee of the Conserve School Trust. A 16 (SAC ¶ 10). Rinn became a Vice President and a Director of CSTW on or after April 21, 2014, and personally owns 10 shares of the Company's common stock. *Id.*

Defendant Ronald V. Kazmar ("Kazmar") served as a Director of CSTW at all times relevant to Plaintiffs' claims, and was the Company's Chief Financial Officer and Treasurer of CSTW until Powers succeeded him in those positions on or after April 21, 2014. A 17 (SAC ¶ 11). Kazmar is believed to serve as a trustee of the Conserve School Trust and personally owns 40 shares of CSTW common stock. *Id.*

Defendants Sullivan, Fuhrman, Powers, Rinn and Kazmar constitute CSTW's current Board of Directors and, Plaintiffs believe, also serve as trustees of the Conserve School Trust. A 17 (SAC ¶ 12). These individuals constituted the Company's Board of Directors at the time this action was commenced. *Id.* The current directors own collectively in their individual capacities just 253 shares of the Company's common stock (or 0.096% of all outstanding shares). *Id.*

D. Former Directors of CSTW.

Defendant Michael X. Cronin ("Cronin") served as a Director of CSTW until he resigned from that position on October 6, 2011. A 17 (SAC ¶ 13). Upon Cronin's resignation as a Director, he is believed to have been replaced by Fuhrman as a trustee of the Trust. *Id.* Cronin continued to serve as the Company's Chief Executive Officer until January 1, 2012, when he resigned from that position. *Id.* Cronin personally owns 56 shares of CSTW common stock. *Id.*

Defendant John F. Calhoun ("Calhoun") served as a Director and President of CSTW until April 13, 2013. A 18 (SAC ¶ 14). Calhoun also served as a trustee of the Trust until his resignation from the Company's Board. *Id.* Calhoun personally owns no shares of CSTW stock. *Id.*

Defendant Christopher M. Rodgers ("Rodgers") served as a Director and Vice President of CSTW until April 21, 2014, when Rinn succeeded him to those positions. A 18 (SAC ¶ 15). Rodgers also served as a trustee of the Trust and is believed to have been replaced in that position upon termination of his tenure as a Director of the Company. *Id.* Rodgers personally owns 100 shares of CSTW common stock.

Each of Cronin, Calhoun and Rodgers served concurrently as directors of CSTW and as trustees of the Company's controlling stockholder, the Trust. A 18 (SAC ¶ 16). Collectively, these three former directors are believed to own only

156 shares of CSTW common stock, or 0.059% of all issued and outstanding shares. *See id.* Together, all Individual Defendants are believed to own just 409 shares of the Company's common stock, or 0.15% of all issued and outstanding shares. *See* A 19 (SAC ¶ 17).

II. THE CONSERVE SCHOOL TRUST.

The Second Restatement of James R. Lowenstine Trust Dated August 17, 1981, as amended (the "Trust Instrument"), reflects the faith James Lowenstine placed in the business judgment and integrity of the CSTW directors he selected.[2] Specifically, Mr. Lowenstine stated in the Trust Instrument that, upon his death, "those individuals who at my death are [CSTW] Directors" would become trustees of the Trust. A 63 (Art. VII, ¶ C(1)). Mr. Lowenstine explained his confidence in the directors' qualifications to serve as trustees, and his reliance on their ability to select similarly qualified successors, as follows:

> I anticipate that after the administration of my estate, the trustees hereunder will have control of [CSTW]. By reason of my ownership of and possession of control of [CSTW], I have been able to see to the election of directors of [CSTW] persons who have experience in the operation of the business, are knowledgeable in the industry in which it operates, and whom I believe to be persons of business judgment and integrity who can be expected to choose as their successors persons having those same qualities.

[2] The Conserve School Trust is not governed by a separate written document but derives from and is subject to the terms of the original Lowenstine Trust, as embodied in the Trust Instrument. *See* A 21 (SAC ¶ 27 n.4).

A 71 (Art. VIII, ¶ D). For these reasons, Mr. Lowenstine "*recommend[ed]* that shares of [CSTW] not be sold by the trustees *to raise cash for the purposes of any of the trusts* created under this instrument." *Id.* (emphasis added). Mr. Lowenstine likewise "*recommended*" that the Trust's CSTW stock "not be sold" because "[t]he growth and profitability of [CSTW] has continued at a steady and consistent pace for many years and [CSTW] has proved to be, and I expect it to continue to be, a conservative, steadily improving investment both in dividend return and in appreciation of value." A 71 (Art. VIII, ¶ C) (emphasis added).

Notwithstanding his "recommendations," however, Mr. Lowenstine explicitly authorized the trustees to cause the Trust to sell its shares of CSTW stock. *See* A 71 (Art. VIII, ¶ C) ("If, however, the trustees determine that any [CSTW] stock should be sold …."). Presciently, Mr. Lowenstine further recognized the conflicts inherent in granting CSTW directors full control over their own election to the Company's Board. *See* A 73 (Art. VIII, ¶ I) ("I … anticipate that it may be desirable for the trustees, both in their capacities as trustees and as directors of [CSTW], to make decisions, or refrain from making decisions which are arguably adverse in some respects to the best interest of the beneficiaries of a trust hereunder, but which may be in the best interests of [CSTW]."). Accordingly, the Trust Instrument expressly permits the trustees, in their capacity as CSTW directors, to place the interests of the Company above those of the Trust and

insulates the directors from liability to the Trust for doing so:

> In voting the shares of [CSTW], I authorize the trustees to consider primarily the best interests of [CSTW], since it is my belief that attention to the best interests of [CSTW] ultimately will best serve the interests of the beneficiaries of the trusts hereunder. I further authorize the trustees to take such actions as they deem appropriate with respect to matters involving [CSTW] in which a trustee, or all of the trustees, may be individually interested as a director or officer of [CSTW] notwithstanding that such action may be adverse to the best interests of the beneficiaries of any trust hereunder, provided such action is not in breach of their fiduciary duties in such other capacity or capacities. *Any action taken in those respects shall be binding and conclusive on the beneficiaries of the trusts hereunder as if no such relationship or conflict of interest existed, and the trustees shall be relieved, to the maximum extent permitted by law, of any liability for actions so taken.*

A 73-74 (Art. VIII, ¶ I) (emphasis added). The Trust Instrument does not, however, authorize the trustees to favor the Trust's interests in situations where those interests might conflict with the Company's.

The trustees' authority to favor CSTW's interests over those of the Trust is critical because the Trust Instrument ensures that, for as long as the Trust owns a controlling share of the Company, the directors of CSTW will continually maintain their control over the Trust and its voting power. The Trust Instrument provides that, when a person ceases serving as a Director of CSTW, he or she automatically ceases to be qualified to serve as a trustee of the Trust. *See* A 64 (Art. VII, ¶ F). In such circumstances, the trustees are authorized to designate a temporary replacement for any person who ceases to be qualified to serve as a trustee under

the Trust Instrument. *See* A 64-65 (Art. VII, ¶ G). This replacement serves only until the election of a new CSTW Director, who then automatically succeeds to the formerly vacant trustee position and replaces the appointed substitute. *See id.*

In this way, the Trust Instrument perpetuates the CSTW directors' unfettered control over the Trust's majority shareholdings in CSTW – *but only so long as the Trust owns more than 50% of the shares of the Company*. If, at any time, the Trust does not own control of CSTW, then the right to appoint the trustees of the Trust will pass to the governing body of the Culver Educational Foundation – a separate charitable organization created by the Lowenstine Trust – which then "shall have the power to remove those Individual Trustees who became such by reason of being or becoming [CSTW] Directors." A 65 (Art. VII, ¶ I). Therefore, the Trust Instrument incentivizes the trustees to resist selling control of CSTW, or taking any action that would cause the Trust to lose majority ownership of CSTW, in order to maintain their positions in the Trust and, in turn, the ability to elect themselves as directors of the Company. Recognizing this inherent conflict, Mr. Lowenstine made sure that the Trust Instrument allowed the Company's directors – "persons of business judgment and integrity" – to consider objectively and independently the best interests of CSTW even when those interests run contrary to those of the Trust and its beneficiaries.

III. THE INDIVIDUAL DEFENDANTS' LUCRATIVE PERSONAL BENEFITS AS CSTW INSIDERS.

Historically, concurrent service as CSTW directors and trustees of the Trust has been reserved for Company "lifers." For example, each of the following Individual Defendants has more than two decades "of service" to CSTW:

Sullivan: 23 years
Cronin: 42 years
Fuhrman: 28 years
Calhoun: 38 years
Rinn: 35 years
Rodgers: 38 years
Kazmar: 28 years

A 26 (SAC ¶ 35). The only exception is Powers, the recently named CFO. *Id.*

Though the directors personally own few (if any) shares of Company stock, they are all employed by CSTW in full-time executive positions and are well compensated. The reported "annual compensation" (defined in CSTW's Proxy as combined salary, bonuses, and "other benefits for services regardless of when paid") for the Individual Defendants is as follows:

Name	2009	2010	2011	2012	2013	2014
Sullivan	--	--	--	$324,674	$455,011	$414,590
Fuhrman	--	--	--	$178,630	$313,011	$327,082
Powers	--	--	--	--	--	$261,672
Rinn	--	--	--	--	--	$160,085

Name	2009	2010	2011	2012	2013	2014
Kazmar	--	--	--	$344,364	$389,609	$154,364[3]
Cronin	$559,148	$328,407	$346,516	--	--	--
Calhoun	--	--	$272,464	$342,371	$388,716	--
Rodgers	--	--	$200,670	$284,924	$307,376	--

A 26-27 (SAC ¶ 36). As this chart reflects, the average collective "annual compensation" for the Board over the years 2010 to 2013 was $1.49 million. *Id.* For the same period, the average annual earnings of CSTW were $6.47 million. *Id.* Therefore, during those four years the directors paid themselves cash salaries in amounts that exceeded 23% of the Company's total earnings.

The Individual Defendants receive additional benefits that are not included in these reported annual compensation figures, including participation in the Profit Sharing Plan. A 27 (SAC ¶ 37). The trustees of the Profit Sharing Plan consist of four CSTW directors and one officer of the Company. *Id.* While CSTW does not disclose the value of the Individual Defendants' share of the Profit Sharing Plan Trust, the Profit Sharing Plan is (after the Trust) the Company's second largest stockholder, with 31,660 shares (or 12.2% of all outstanding shares). *Id.* The Company also instituted in 2013 a cash-based long term incentive plan for "certain" officers, the terms of which have not been disclosed. *Id.* The Individual

[3] Kazmar's 2014 compensation was paid after he retired in 2013. A 26 (SAC ¶ 36).

Defendants receive further compensation from the CSTW Pension Plan (which is essentially fully funded) and a fully paid, post-retirement Health Care Plan. A 28 (SAC ¶ 38). These two plans paid an average of $11.1 million each year from 2010 through 2013. *Id.*[4]

The Individual Defendants also receive significant fringe benefits. For example, each CSTW Director is given a company car which, upon retirement, he is entitled to keep. A 29 (SAC ¶ 39). The Company also pays for the Individual Defendants' country club dues and financial advisory expenses. *Id.* Moreover, each Individual Defendant is given Company-funded life insurance in addition to the life insurance policies that all CSTW employees are eligible to receive. *Id.*

The Individual Defendants enjoy other perks as well, including access to a private executive dining room at CSTW's offices with chef-prepared meals. *Id.* They also are entitled to use the 1,200 acre, non-public Lowenstine Estate located in Vilas County, Wisconsin (the property on which the Conserve School is located) to hunt, fish and vacation. A 29-30 (SAC ¶ 40). While at the property, the Individual Defendants may stay at Lowenwood, Mr. Lowenstine's former home,

[4] Given the Individual Defendants' already high level of compensation, the Pension Plan will pay them (according to the formula applied by that Plan) proportionately more than all other CSTW employees. A 28 (SAC ¶ 38). For example, according to the Company's March 2013 proxy statement, each Individual Defendant will receive at retirement 30% of his annual salary from the preceding ten years, plus 19.5% of his average salary in excess of Social Security-covered compensation for the preceding five years. *Id.* Therefore, after 15 years of service, an Individual Defendant receives annually a substantial percentage of peak compensation.

which has been described as a "sprawling estate." *Id.* CSTW also purchased a pleasure boat for the Individual Defendants' use while they vacation at Lowenwood. *Id.*

IV. THE INDIVIDUAL DEFENDANTS' ACTIONS TO PRESERVE THEIR CONTROL AND PERSONAL BENEFITS AT THE EXPENSE OF CSTW'S STOCKHOLDERS.

In June 2011, a third party, Samuel, Son & Co., Limited ("Samuel") submitted a letter to the Company's Board of Directors offering to buy all shares of CSTW for $1,000 per share. A 31 (SAC ¶ 42). Samuel's offer represented a 58% premium over the stock trading price of CSTW and a 27% premium over the Company's own appraised value as of June 30, 2011. *Id.*

On July 18, 2011, however, the CSTW Board of Directors rejected the Samuel offer on the grounds that the Trust had rejected a sale of the Company, and thus the support of a majority of CSTW's shares could not be obtained. A 31-32 (SAC ¶ 43). Just minutes before the CSTW Board meeting, the trustees of the Conserve School Trust – the same individuals, of course, who would act as CSTW directors moments later – met to reject Samuel's offer. *Id.* The minutes of the trustees' July 18, 2011 meeting show that the Individual Defendants turned down the Samuel offer based solely on their personal interests. According to these minutes, Cronin, Calhoun, Kazmar, Rodgers and Sullivan conceded that their only concern was that "[s]hould there be a sale of [the Trust's CSTW stock], Culver

[Educational Foundation] would then be able to appoint the Trustees" of the Trust. *Id.* Of course, had the Samuel offer been pursued those new trustees – rather than the Individual Defendants – would vote the Trust's shares in the election of CSTW's directors.

At the token CSTW Board meeting that immediately followed the trustees' meeting, the Individual Defendants concluded that the Samuel offer should be rejected outright, without further exploration, on the grounds that the Trust (through the actions of the same Individual Defendants) would not approve a sale of the Company. A 32 (SAC ¶ 44). There was no analysis at either meeting of the potential benefits of Samuel's offer to the Trust, CSTW or the Company's stockholders, and the Individual Defendants did not engage or consult an independent advisor to consider such potential benefits. *Id.* The consecutive trustees' and directors' meetings were attended by the same individuals with the same counsel, who purported to represent *both* the Trust and CSTW depending on which meeting was in session at the time. A 32 (SAC ¶ 45). On July 18, 2011, immediately following the trustees' and directors' meetings, Kazmar sent a letter to Samuel informing it "that, after fully discussing the proposal reflected in [Samuel's] letter, the Trustees and the Board of Directors have decided not to pursue the proposal." A 33 (SAC ¶ 47).

On July 27, 2011, Cronin received a letter from Robert Edelman of Edelman

& Co., Ltd., sent on behalf of "client shareholders" of CSTW, inquiring about the Individual Defendants' rejection of the Samuel offer. A 33-34 (SAC ¶ 48). After receiving a perfunctory response from Kazmar on August 3, 2011, Mr. Edelman wrote again on August 11, 2011 to request a meeting with Cronin to "achieve an understanding of … the [CSTW] Board of Directors' long-term plan to deliver value to shareholders, and … the basis for the Board's posture towards the Samuel, Son & Co. proposal to acquire [CSTW] for $1,000 per share in cash." *Id.* Cronin's August 17, 2011 response was telling, stating that "further discussion" of the Samuel offer would not be "fruitful" because "we are mindful that you and the [CSTW stockholders] you represent would not bring to that discussion the perspective that we, who serve as the individual Trustees of the Conserve School Trust pursuant to the Trust's requirements, must bring to a matter such as this." *Id.*

The Individual Defendants' rejection of Samuel's offer was not an isolated incident. In July 2011, Cronin reported that he "regularly" received informal expressions of interest in possible strategic alternatives for CSTW and that he had "every expectation" they would continue. A 34 (SAC ¶ 49). One such expression of interest was sent by Paley Dixon, Inc. ("Paley Dixon") on March 24, 2011, on behalf of a privately-held company with revenues of $2.5 billion. *Id.* At that time, Paley Dixon informed Cronin, in part:

> Our client is looking to acquire a minority, majority, or 100% interest in a business well established as a metal distributor. They believe

> they are in a unique position to further increase the revenue and profitability of [CSTW] through a combination of internal growth and select strategic acquisitions.
>
> The purpose of this letter is to find out if you would be willing to talk with them.

A 34-35 (SAC ¶ 49). Paley Dixon also offered to identify its client and provide further information. *Id.* On April 21, 2011, Paley Dixon again wrote to Cronin:

> I have not received a response to the letter I recently sent you. Please allow me to differentiate our inquiry from others you may have received with regard to selling a portion or all of [CSTW].
>
> We are not investment bankers or brokers seeking to market a company. We represent a single client who specifically asked us to contact you based on your success as a full-line ferrous and nonferrous metal distribution service center. Our client has revenues of $2.5 billion and is looking to acquire a minority, majority, or 100% interest in your business.
>
> In completing a transaction with our client, you and your team can continue to run the business while they utilize their financial capability and global contacts to increase revenue and profitability through accelerated internal growth and selected strategic acquisitions.
>
> I'm hoping you will talk with them to learn who they are and what they have in mind. I assure you that all communications will be strictly confidential.
>
> I would be glad to identify our client and provide detailed information by telephone.

A 35 (SAC ¶ 50). There is no evidence, however, that Cronin responded to Paley Dixon or that the Individual Defendants ever considered investigating Paley Dixon's client's expression of interest. A 36 (SAC ¶ 50).

On September 14, 2011, Robert Edelman wrote again to Cronin and identified ten "industry participants," including Samuel, that had "indicated an interest in purchasing a control or 100% interest in Central Steel" in response to "outreach efforts" conducted by Edelman & Co. A 36 (SAC ¶ 51). Mr. Edelman further informed Cronin:

> Three industry participants told Edelman & Co. of previous attempts to discuss acquisition interest with [CSTW] leadership. Each said the reply was one of clear and immediate disinterest in pursuing or discussing the topic. One noted there had been periodic reminders of the interest, saying "I've always told them that if there's ever a change to please talk to us and I believe they would."

Id. There is no evidence that the Individual Defendants ever altered their stance as communicated to this potential acquirer. *Id.* Instead, all expressions of interest have been routinely ignored or rejected, without consideration of the potential benefits to CSTW and its stockholders.

For example, on November 15, 2011, The Renco Group ("Renco"), a private corporation experienced in the industry, approached CSTW and expressed an interest in acquiring the Company or becoming a significant investor. A 37 (SAC ¶ 53). At that time, Renco informed Cronin, in part:

> Renco is private and acquisitions are made for cash. … Our investments are long term and we support the capital requirements of our companies.
>
> It has been our policy to retain present management on an incentive basis. Each of our companies operates independently and management enjoys autonomy.

> We would welcome the opportunity to explore this matter with you on a highly confidential basis. Our due diligence procedures are expeditious and of minimal disturbance to personnel. It would be a pleasure to hear from you.

Id. As was true with all other proposals, there is no evidence that Cronin responded to Renco or that the Individual Defendants ever considered investigating Renco's expression of interest. *Id.*

On February 17, 2012, Cronin received a letter from Trans American Capital informing him, *inter alia*, that "[a] large buyer wants to open up immediate discussions with [CSTW] to purchase all or a large portion of [CSTW] …." A 37 (SAC ¶ 54). Once again, there is no evidence that Cronin responded to Trans American Capital or that the Individual Defendants ever considered investigating the expression of interest from Trans American Capital's client. A 37-38 (SAC ¶ 54).

The Individual Defendants' conduct has not been limited to the summary rejection of multiple offers and expressions of interest. While CSTW operates in an industry undergoing consolidation, the Individual Defendants have refused to consider any potential acquisitions by CSTW, thereby relegating the Company to the sidelines – and leading predictably to a diminishing ability to compete and poor financial results. *See* A 25 (SAC ¶ 34).

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN CONCLUDING THAT *GANTLER* REQUIRED IT TO DISREGARD SPECIFIC FACTS SUPPORTING THE ALLEGATION THAT THE INDIVIDUAL DEFENDANTS WERE MOTIVATED BY ENTRENCHMENT AND IN FINDING THOSE FACTS INSUFFICIENT TO DEFEAT DISMISSAL OF PLAINTIFFS' CLAIMS.

A. Question Presented.

Did the Court of Chancery err, as a matter of law, in holding that *Gantler* required it to disregard Plaintiffs' specific allegations detailing acts of entrenchment and mandated that it apply the business judgment rule unless Plaintiffs specifically alleged self-interest entirely unrelated to an entrenchment motive? *See* Ex. A at 69-75.

B. Scope of Review.

"A motion to dismiss a complaint presents the trial court with a question of law and is subject to *de novo* review by this Court on appeal." *Malone v. Brincat*, 722 A.2d 5, 9 (Del. 1998). The Court does not affirm dismissal "unless the plaintiff would not be entitled to recover under any reasonably conceivable set of circumstances." *Central Mortgage*, 27 A.3d at 535.

C. Merits of Argument.

1. Plaintiffs' Allegations Rebut The Business Judgment Rule.

Under decades of Delaware precedent, the fiduciary duty of loyalty mandates that a director not consider or represent interests other than the best

interests of the corporation and its stockholders in making a business decision. *See, e.g.*, *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939) ("The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest."). The duty of loyalty also "encompasses cases where the fiduciary fails to act in good faith." *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).

Allegations establishing that directors breached their duty of loyalty will rebut the presumptions of the business judgment rule. *See, e.g.*, *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993), *modified*, 636 A.2d 956 (Del. 1994). Therefore, "[w]here a plaintiff pleads facts demonstrating that a majority of directors have an interest in the outcome of a proposed transaction, the presumptions of the business judgment rule do not attach." 1 R. Franklin Balotti & Jesse A. Finkelstein, *The Delaware Law of Corporations & Business Organizations* § 4.19[B] (3d ed. 2014 Supp.). For example, "[d]irectorial interest … exists where a corporate decision will have a materially detrimental impact on a director, but not on the corporation and the stockholders." *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993). "In such circumstances, a director cannot be expected to exercise his or her independent business judgment without being influenced by the adverse personal consequences resulting from the decision." *Id.* The same is true when a board declines to act:

> When a board addresses a pending takeover bid it has an obligation to determine whether the offer is in the best interests of the corporation and its shareholders. In that respect a board's duty is no different from any other responsibility it shoulders, and its decisions should be no less entitled to the respect they otherwise would be accorded in the realm of business judgment. … There are, however, certain caveats to a proper exercise of this function. Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.

Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (footnote and citation omitted).

Here, Plaintiffs' factual allegations establish the Individual Defendants' self-interest in refusing even to consider strategic alternatives that would threaten their control and positions (including the automatic rejection of proposed acquisitions of CSTW) and, therefore, rebut the business judgment rule. As the trial court recognized (*see* Ex. A at 75-80), this self-interest is not mooted by the Trust's purported unwillingness to entertain strategic offers; rather, given the Individual Defendants' dual roles as trustees and CSTW directors, the Complaint describes a relationship akin to one where directors sit on the boards of both subsidiary and controlling parent corporations. In such situations, the directors affiliated with the parent "still owe[] [the subsidiary] and its shareholders an uncompromising duty of loyalty." *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983). "There is no dilution of this obligation where one holds dual or multiple directorships, as in a

parent-subsidiary context." *Id.* Thus, the Individual Defendants' decision-making as trustees (or the lack thereof) does not relieve them of their independent fiduciary duties to CSTW and its stockholders.

Similarly, the relationship between the Company and the Trust is not simply one of corporation and majority stockholder. The Trust Instrument creates and perpetuates a governance structure under which the Trust, as majority stockholder of CSTW, is controlled by the same individuals who are entrusted with exercising their fiduciary obligations to *all* of the Company's stockholders, but who nonetheless immunize themselves from replacement and appoint their successors. Unlike the Trust itself, these individuals have virtually no financial interest in CSTW's financial performance – but, conversely, have every personal interest in perpetuating their interlocking positions at CSTW and the Trust. Therefore, this case is unlike "most situations, [where] the controlling stockholder has interests identical to other stockholders to maximize the value of its shares." *In re Morton's Restaurant Group, Inc. S'holders Litig.*, 74 A.3d 656, 666-67 (Del. Ch. 2013). To account for this discrepancy, the Trust Instrument expressly gives precedence to the interests of CSTW and its shareholders over the interests of the Trust – a fact the trial court found significant. *See* Ex. A at 77-78.

As the Complaint explains, the Individual Defendants' only motive in refusing to consider any expressions of interest in business combinations, including

rejecting a sale of the Company, arises from preserving their lucrative employment as CSTW officers. Plaintiffs' allegations of self-interest and an entrenchment motive rely not on the receipt of nominal directors' fees, but rather the monetary and non-monetary compensation all Individual Defendants receive for as long as they remain members in the CSTW director/executives' "club," which typically lasts decades. *See* A 26 (SAC ¶ 35). This compensation includes not just hundreds of thousands of dollars in annual officer salaries, but also participation in the very generous Pension and Profit Sharing Plans, a post-retirement Health Care Plan, life insurance, a company car, and free use of the Lowenwood estate for personal vacations. *See* A 26-30 (SAC ¶¶ 36-40). These facts are more than sufficient to rebut the business judgment presumption and state a claim for relief against the Individual Defendants.[5]

[5] While Plaintiffs must establish that a financial benefit is "material" to create a disqualifying self-interest, *In re MFW S'holders Litig.*, 67 A.3d 496, 509 (Del. Ch. 2013), *aff'd sub nom.*, *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014), the personal benefits enjoyed by the Individual Defendants (*i.e.*, their well-compensated jobs) are material by any standard. As noted above, over four years the Individual Defendants paid themselves salaries amounting to more than 23% of CSTW's total earnings. *See* A 26-27 (SAC ¶ 36). Additionally, because each of the Individual Defendants serves or served as a full-time officer of CSTW, it is reasonable to infer that their employment by the Company and/or post-retirement compensation serves as a materially substantial (if not the sole) source of personal income. Plaintiffs' particularized factual allegations detailing this compensation demonstrate the Individual Defendants' incentive to reject all expressions of interest in acquiring CSTW. *See In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 55 (Del. Ch. 2013) (holding that director's receipt of $220,633 in merger consideration, nearly double his annual salary and 3.7% to 5.5% of his estimated net worth, was sufficiently material to establish disqualifying self-interest).

2. *Gantler* Does Not Compel Dismissal Of Plaintiffs' Claims Because The Complaint Alleges Specific Conduct In Furtherance Of The Individual Defendants' Entrenchment Motive.

Viewing the facts alleged in the Complaint on their own merit, the Court of Chancery opined that "this case might well survive a motion to dismiss." Ex. A at 80. The trial court still granted dismissal, however, based solely on its conclusion that *Gantler* mandates application of the business judgment rule *notwithstanding* those facts. *See id.* *Gantler* does not so hold, but rather requires specific allegations of self-interested conduct by directors which substantiates their entrenchment motive to reject strategic, value-maximizing transactions. Plaintiffs here allege ample facts to satisfy this test and support application of entire fairness.

In *Gantler*, this Court reviewed the dismissal of claims arising from directors' rejection of a third party acquisition bid solicited through a sales process. While the *Gantler* plaintiffs argued that the directors' conduct should have been reviewed under an entire fairness standard, the Court of Chancery dismissed their claims on the grounds that they failed to allege facts sufficient to rebut the business judgment rule. *See* 965 A.2d at 704. In its opinion, this Court noted that:

> Our analysis of whether the Board's termination of the Sales Process merits the business judgment presumption is two pronged. First, did the Board reach its decision in the good faith pursuit of a legitimate corporate interest? Second, did the Board do so advisedly? For the Board's decision here to be entitled to the business judgment presumption, both questions must be answered affirmatively.

Id. at 706. Recognizing that "a board's decision to decline a merger is often rooted in distinctively corporate concerns, such as enhancing the corporation's long term share value," the *Gantler* Court posited that "[a] good faith pursuit of legitimate concerns of this kind will satisfy the first prong of this analysis." *Id.* at 706-07 (citing *TW Servs., Inc. v. SWT Acquisition Corp.*, 1989 WL 20290, at *11 (Del. Ch. Mar. 2, 1989)).

The *Gantler* plaintiffs asserted the conclusory allegation that the defendants rejected an acquisition bid "to preserve personal benefits, including retaining their positions and pay as directors." 965 A.2d at 706. On appeal, this Court held that an alleged *desire* to maintain one's place on a board of directors is insufficient *by itself* to establish disloyalty and rebut the business judgment rule:

> A claim of this kind must be viewed with caution, because to argue that directors have an entrenchment motive solely because they could lose their positions following an acquisition is, to an extent, tautological. By its very nature, a board decision to reject a merger proposal could always enable a plaintiff to assert that a majority of the directors had *an entrenchment motive*. *For that reason, the plaintiffs must plead, in addition to a motive to retain corporate control, other facts sufficient to state a cognizable claim that the Director Defendants acted disloyally.*

Id. at 707 (emphasis added) (citing *Pogostin v. Rice*, 480 A.2d 619, 627 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000)).

It is the last sentence of the preceding quotation – requiring plaintiffs to allege "other facts" beyond a director's "motive to retain corporate control" – upon

which the Court of Chancery relied in granting the Individual Defendants' Motion to Dismiss in this case. *See* Ex. A at 71-72. The trial court interpreted *Gantler* as requiring Plaintiffs to plead not only more than an "entrenchment motive," but as also requiring Plaintiffs to plead more than specific facts demonstrating that a director acted upon that motive. *Id.* at 72. Under this view of *Gantler*, no allegations – however strong and factually specific – would rebut the business judgment rule if they also constituted an act of maintaining control.

Contrary to the trial court's interpretation, the *Gantler* Court did not apply business judgment protection notwithstanding specific allegations of conduct in furtherance of (in contrast to the mere existence of) an entrenchment motive. Rather, *Gantler* held that "the plaintiffs must plead, in addition to a motive to retain corporate control, other facts sufficient to state a cognizable claim that the Director Defendants acted disloyally." 965 A.2d at 707. In so holding, the *Gantler* Court did not limit or modify existing law as to what constitutes a "fact" showing disloyalty. The *Gantler* Court then found that the plaintiffs alleged facts "sufficient to establish disloyalty of at least three (*i.e.*, a majority) of the remaining directors, which suffices to rebut the business judgment presumption." *Id.*

As to the first director, William Stephens, the plaintiffs in *Gantler* alleged a direct act to maintain control. Stephens was alleged to have completely failed to respond to a prospective bidder's due diligence requests, inaction that ultimately

caused the bidder to withdraw its proposal. *See id.* The plaintiffs alleged that Stephens was motivated to terminate the sales process to avoid "losing his long held positions as President, Chairman and CEO" of the corporation. *Id.* From these allegations, this Court found "it may reasonably be inferred that what motivated Stephens' unexplained failure to respond promptly to [the bidder's] due diligence request was his personal financial interest, as opposed to the interests of the shareholders." *Id.*

The *Gantler* Court also held that the second and third directors faced disqualifying conflicts of interest because a proposed acquisition would have threatened the corporation's continued use of their personal businesses for HVAC and legal services, respectively. *See id.* at 708.[6] Accordingly, the Court concluded that "the plaintiffs have alleged facts sufficient to establish, for purposes of a motion to dismiss, that a majority of the [corporation's] Board acted disloyally. … Because the claim of disloyalty was subject to entire fairness review, the Court of Chancery erred in dismissing Count I as to the Director Defendants on the basis of the business judgment presumption." *Id.*

Thus, *Gantler* requires that a plaintiff allege facts beyond a mere "motive" to retain one's corporate position – an allegation that could be made in every case

[6] The fact that these allegations raised only the *possibility* that each of the defendants' businesses might lose a *single* client demonstrates that the *Gantler* Court imposed a low threshold upon plaintiffs to plead "other facts" establishing disloyalty. *See* 965 A.2d at 708.

relating to a potential change of control – to establish a director's disloyalty. However, *Gantler* did not *eliminate* the desire to maintain one's position as a ground for self-interest and application of entire fairness; rather, it requires allegation of specific conduct *in furtherance of* the motive to maintain the director's position (as in Stephens' case, the failure to respond to due diligence requests) or an additional personal financial interest. *See id.* at 707.[7]

Here, the Complaint details the Individual Defendants' motives to maintain control – *i.e.*, the lucrative salaries and other benefits they have enjoyed as CSTW "lifers," which they will continue to enjoy indefinitely as long as they remain trustees of the Trust (positions for which the Individual Defendants are qualified pursuant to the Trust Instrument solely by reason of their status as CSTW directors). *See* A 26-30 (SAC ¶¶ 35-41). In this way, the Individual Defendants were motivated by the threat of losing control over the *Trust*, which not only

[7] In denying Plaintiffs' Motion for Reargument, the trial court interpreted *Gantler* incorrectly to require separate and different standards of review for (i) a defendant's "response to [a] merger proposal," and (ii) "subsequent actions during the sale process." Ex. C ¶ 2. The *Gantler* plaintiffs, in Count I of their complaint, challenged the defendants' rejection of a merger bid as one component of a faulty and disloyal sales process. *See* 965 A.2d at 706 (noting that Count I alleged the director defendants "improperly rejected a value-maximizing bid from First Place and terminated the Sales Process"). After determining that enhanced scrutiny under *Unocal* was not warranted, the *Gantler* Court analyzed whether the business judgment rule governed the conduct alleged in Count I of the plaintiffs' complaint based on a board's inherent authority to decline an acquisition proposal. *See id.* at 705-06. Under this analysis, the *Gantler* Court considered whether plaintiffs alleged facts establishing a disqualifying self-interest among a majority of the board in maintaining the status quo. *See id.* at 706-07. Concluding that they had, the *Gantler* Court held that "[b]ecause the claim of disloyalty was subject to entire fairness review, the Court of Chancery erred in dismissing Count I as to the Director Defendants on the basis of the business judgment presumption." *Id.* at 708.

ensures their personal compensation in perpetuity but also insulates them from any minority stockholder challenge.[8]

Like the plaintiffs in *Gantler*, Plaintiffs here allege "other facts" demonstrating that the Individual Defendants acted on those motives. For example, the Individual Defendants' consistent refusal to consider any strategic alternatives for CSTW, even internally, admittedly was driven by a personal desire to retain their roles as trustees of the Trust, rather than the interests of CSTW or its minority shareholders. *See* A 31-32 (SAC ¶ 43) (minutes of July 18, 2011 trustees meeting reflect that Individual Defendants rejected the Samuel offer because sale of CSTW would permit their replacement as trustees).

The Complaint also alleges specific acts to dissuade and thwart all potential strategic alternatives for the purpose of promoting the Individual Defendants' "personal financial interest, as opposed to the interests of the shareholders." 965 A.2d at 707. Specifically, Plaintiffs allege that the Individual Defendants rebuffed the Samuel offer (i) first, in their capacities as trustees, based solely on their desire to remain trustees without any analysis of the best interests of the Trust, and (ii) then, in their capacities as directors, without any analysis of

[8] This distinguishes the present case from *Gantler*, because the directors there did not face the prospect of losing majority stockholder control from an outside acquisition. As detailed in the Court of Chancery's opinion below, the *Gantler* directors held collectively only 11.22% of the total outstanding shares of the corporation's stock. *See Gantler v. Stephens*, 2008 WL 401124, at *1-2 (Del. Ch. Feb. 14, 2008), *rev'd*, 965 A.2d 695 (Del. 2009).

CSTW's best interests. *See* A 31-32 (SAC ¶ 43). Plaintiffs further allege that the Individual Defendants, through their admittedly self-interested act as CSTW directors, peremptorily rejected the Samuel offer without any substantive deliberation and based solely on their refusal (in their concurrent capacities as trustees) to even consider a sale of the Trust's stock. *See* A 32-33 (SAC ¶¶ 44-47). Thereafter, the Individual Defendants (admitting in written correspondence that they act from their unique "perspective" as trustees of the Trust, A 34 (SAC ¶ 48)) flatly refused to engage in any discussion with minority stockholders concerning the Samuel offer. Plaintiffs also allege a pattern of conduct through which the Individual Defendants wholly ignored multiple third party expressions of interest and never considered using CSTW stock to make acquisitions. *See* A 34-40 (SAC ¶¶ 49-57).[9] In an industry undergoing consolidation, the Individual Defendants are causing CSTW to stand on the sidelines solely for the purpose of maintaining their control. *See* A 25 (SAC ¶ 34).

In summary, Plaintiffs' specific factual allegations satisfy any concern, as expressed in *Gantler*, that entire fairness might be applied to a tautological claim

[9] In this way, the Complaint alleges not only that the Individual Defendants refused to consider *acquisitions of* CSTW, but also a failure to consider *any* strategic alternatives (*e.g.*, acquisitions *by* CSTW that would not necessarily cause the Individual Defendants to lose their management or board positions but would threaten the Trust's majority control and require the Individual Defendants to account to someone besides themselves). As a result, the Individual Defendants are not entitled to a "strong presumption in [their] favor," since their repeated inaction enjoys no "statutory authority" such as that found by this Court in 8 *Del. C.* § 251 to implicitly protect a board's decision to decline a merger bid. *Gantler*, 965 A.2d at 706 & n.29.

of entrenchment arising from an unsuccessful acquisition bid. *See* 965 A.2d at 707. Consistent with *Gantler*, the Complaint shows that the Individual Defendants did not engage in a "good faith pursuit of a legitimate corporate interest" and, therefore, acted disloyally. *Id.* at 706. As such, Plaintiffs have rebutted the business judgment presumption and their claims are subject to entire fairness review. *See id.* at 708.

CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that the Court reverse the Court of Chancery's Order granting the Individual Defendants' Motion to Dismiss and remand this action for further proceedings.

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