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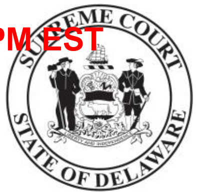

IN THE SUPREME COURT OF THE STATE OF DELAWARE

GAMCO ASSET MANAGEMENT INC., Plaintiff Below-Appellant. v. iHEARTMEDIA INC., iHEARTCOMMUNICATIONS, INC., BAIN CAPITAL PARTNERS, LLC, THOMAS H. LEE PARTNERS, L.P., ROBERT W. PITTMAN, VINCENTE PIEDRAHITA, BLAIR HENDRIX, DANIEL G. JONES, OLIVIA SABINE, CHRISTOPHER TEMPLE, DALE W. TREMBLAY and DOUGLAS L. JACOBS, Defendants Below-Appellees, -and- CLEAR CHANNEL OUTDOOR HOLDINGS, INC. Nominal Defendant Below-Appellee.	No. 593, 2016 D Court Below: Court of Chancery of the State of Delaware No. 12312-VCS **PUBLIC VERSION 3/2/2017**

PLAINTIFF BELOW-APPELLANT'S CORRECTED OPENING BRIEF

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February 15, 2017

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NATURE OF PROCEEDINGS

This is an appeal from a Court of Chancery decision dismissing derivative claims for breach of fiduciary duty brought by Plaintiff Below-Appellant GAMCO Asset Management Inc. ("GAMCO") on behalf of publicly-traded Clear Channel Outdoor Holdings, Inc. ("CCOH" or the "Company") against, among others, the Company's board of directors (the "Board Defendants") and its 90-percent controlling shareholder iHeart Communications, Inc. ("iHC").

Pursuant to an intercompany cash management arrangement, CCOH's cash is swept daily into iHC's accounts and recorded as a balance on a revolving promissory note (the "Revolving Note") in favor of CCOH. While CCOH does not have autonomy over its swept cash, the terms of the agreement entitle it to demand repayment of all or part of the Revolving Note balance at any time for any reason.

At the time of GAMCO's May 9, 2016 Verified Stockholder Derivative Complaint (the "Complaint"), Defendant iHC's indirect parent, iHeartMedia, Inc. ("iHM"), had sustained ***eleven (11) consecutive quarters of negative net income*** going back to July 2013, had lost from $606 million to $793 million per year, and, together with iHC (the "iHeart Defendants"),[1] was ***$20.8 billion*** in debt.

The cash management arrangement (and Revolving Note) was never intended to be a financing source for the iHeart Defendants, but that is what it has become.

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[1] iHC is non-public and does not separately report financial results.

The balance has increased steadily (to $640 million as of the date of the Complaint) as the iHeart Defendants' financial health has deteriorated and they have needed liquidity to service debt and to continue operations. Nevertheless, the board of directors of CCOH (the "Board") has failed (and continues to fail) to demand repayment on the Revolving Note to protect CCOH and its minority shareholders from exposure to the iHeart Defendants' potential bankruptcy.[2] The Complaint adequately pled that this failure was (and is) an actionable breach of fiduciary duty.[3]

Moreover, in late 2015 into 2016, the Board abandoned CCOH's stated growth and acquisition strategy in order to implement transactions that served no purpose other than to provide liquidity to the iHeart Defendants. In December 2015, the Board Defendants caused CCOH, through an indirect wholly owned subsidiary, to issue $225 million in notes (the "Note Offering") and to dividend the proceeds, of which iHC received 90%. CCOH kept none of the proceeds. In January 2016, CCOH sold assets in eight strategic U.S. markets (the "Asset Sales"), which likewise funded a dividend back to iHC (and other shareholders), despite the fact that just months earlier the Board Defendants had determined that CCOH was best served by

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[2] As discussed herein, the Board did demand partial repayment on the Promissory Note in January 2016 as part of a dividend in which 90% of the demanded amount was returned to iHC.

[3] GAMCO also asserted its breach of fiduciary duty claim and an aiding and abetting breach of fiduciary duty claim against the iHeart Defendants' private equity sponsors, Bain Capital Partners, LLC ("Bain Capital") and Thomas H. Lee Partners, L.P. ("THL Partners"), which together own 67% of iHM and control iHC's board of directors (the "Private Equity Defendants") (collectively with the Board Defendants and iHeart Defendants, the "Defendants").

expanding into new markets, the antithesis of liquidating assets in strong existing markets. While iHC's other shareholders, including GAMCO, received *pro rata* dividends funded by these transactions, the sole reason for and function of the Note Offering and Asset Sales was to provide crucial liquidity to the iHeart Defendants. The Complaint adequately pled that the Board Defendants' approval of these transactions to the detriment of CCOH (and to the minority shareholders' investments in the Company) was a breach of fiduciary duty.

On November 23, 2016, the Court of Chancery dismissed GAMCO's claims. GAMCO respectfully asserts the court erred in ruling that a release from a 2013 settlement of a prior derivative litigation by another shareholder for past breaches (the "2013 Settlement"), and the doctrine of *res judicata* based on that settlement, bars GAMCO's claims arising from the Board Defendants' failure to demand repayment on the Revolving Note. The trial court also erroneously applied the business judgment rather than entire fairness standard to the Note Offering and Asset Sales by discounting the fact that the sole purpose of these conflicted transactions was to provide the iHeart Defendants a unique benefit – crucial liquidity – not needed by CCOH or the minority, which mandates review of the transactions under the entire fairness standard. This appeal followed.

SUMMARY OF ARGUMENT

I. The Court of Chancery erred by ruling that that GAMCO's breach of fiduciary duty claims based on the Board Defendants' failure to demand repayment of the Revolving Note as the iHeart Defendants' financial condition deteriorated was released by the 2013 Settlement and barred by *res judicata.* The 2013 Settlement agreement expressly released only claims existing *as of the date* of that settlement, it did not release any *new* claims arising from circumstances *after* the settlement. The Court of Chancery's ruling suggests a prior settlement release immunizes corporate defendants from liability for subsequent breaches of fiduciary duty arising from new facts and circumstances. This cannot be the law.

II. The Court of Chancery also erred by applying the business judgment rather than the entire fairness standard of review to the Note Offering and Asset Sales because, as alleged in the complaint, the entire function of these transactions was to provide the iHeart Defendants with a "unique benefit" not shared with CCOH or its minority shareholders: namely crucial liquidity to continue operations. While, concededly, minority shareholders received *pro rata* proceeds, the transactions' sole reason and function was to provide crucial operating liquidity to the iHeart Defendants, and the Board Defendants' decision to confer that benefit required CCOH to forego identified business opportunities to its detriment and the detriment

of minority investors. Trial court improperly weighed facts and inferences to conclude otherwise.

STATEMENT OF FACTS

I. FACTUAL BACKROUND

A. THE PARTIES

GAMCO is a Delaware corporation providing investment advisory services to funds, institutional and private wealth management investors, and investment partnerships. (¶15; A25).[4] At the time of the Complaint, GAMCO and its affiliates owned 4,600,558 shares of CCOH's publicly-traded Class A common stock – constituting 9.9% of all outstanding Class A shares. (¶15; A25).

CCOH is a Delaware corporation that is among the largest providers of outdoor advertising in the U.S. and worldwide. (¶16; A25). The public stockholders of CCOH, including GAMCO, own approximately 72% of the Company's Class A shares but, due to 315,000,000 Class B shares owned by iHC, control less than 1% of the vote on corporate matters. (¶17; A26).

Defendant iHC is a non-public company which owns approximately 90% of CCOH's outstanding shares, including more than 10,000,000 Class A shares and 315,000,000 Class B shares, and controls approximately 99% of the total voting power of the Company. (¶20; A26-27). iHC is an indirect wholly-owned subsidiary of iHM. (¶20; A26).

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[4] Citations to "¶__" refer to paragraphs in the Complaint.

Defendant iHM is a publicly-trade American mass media company and the holding company of iHC controlled by the Private Equity Defendants. (¶18; A26).

The Private Equity Defendants control and own 67% of iHM's stock and control iHC through their power to elect all but two of iHC's directors and to appoint management.[5] (¶24; A27).

B. THE CONTROLLING SHAREHOLDERS' DOMINANCE OVER CCOH

In addition to controlling 99% of the CCOH's voting power, iHC otherwise controls CCOH's operations through intercompany agreements originating from CCOH's 2005 initial public offering. (¶37; A30). The intercompany agreements include a cash management arrangement under which CCOH's cash is swept daily into iHC's accounts and reflected in the Revolving Note balance. (¶41; A32). CCOH has no free access to its own cash and CCOH cannot seek external sources of financing, but it is entitled to demand repayment from iHC at any time. (¶42; A32-33).

The Revolving Note was not intended to serve as a liquidity facility for iHC. (¶51; A35). Nevertheless, hundreds of millions of dollars of CCOH's cash has been swept to iHC since 2013 and the Company has rarely made repayment demands.

[5] The "Board Defendants" are Robert W. Pittman, Vicente Piedrahita (a Principal in THL's Strategic Resources Group), Blair E. Hendrix (Managing Director of Bain Capital), Daniel G. Jones (a Managing Director at THL), Olivia Sabine (an Executive Vice President of Bain Capital), Christopher M. Temple, Dale W. Tremblay, and Douglas L. Jacobs.

(¶44; A33). The Revolving Note balance has consequently escalated as the iHeart Defendants' financial condition has deteriorated. (¶44; A33). As of the date of the Complaint, the balance stood at $640 million. (¶44; A33).

C. THE 2013 SETTLEMENT OF PRE-2013 BREACHES

The Revolving Note was due to expire by its own terms on August 10, 2010. (¶57; A37). In December 2009, however, CCOH's board (the "Board") agreed to extend the note through December 15, 2017 and amend its terms. (¶57; A37). In 2012, a minority shareholder of CCOH filed a derivative action challenging the board's decision to approve the amendment on terms alleged to be commercially-unreasonable. (¶56; A36-37).

In June 2013, the 2013 Settlement was reached requiring the Board to make a $200 million repayment demand on the Revolving Note and to declare a simultaneous $200 million *pro rata* dividend to CCOH stockholders. (¶59; A37-38). In addition, the Board was required to establish a special independent note committee (the "INC") to monitor the Revolving Note balance. (¶59; A37-38). If the loan balance or certain ratios involving CCOH's liquidity exceeded trigger points, the INC had the right to demand repayment to accompany a shareholder dividend equal to the repayment. (¶59; A37-38).

Critically, nothing in the 2013 Settlement absolved, relieved or released the Board of its long-standing fiduciary obligations to CCOH, or prevents the Board

Defendants from demanding appropriate repayment on the Revolving Note *as CCOH is contractually entitled to do at any time*. (¶61; A38-39). Moreover, any repayment demand by the Board Defendants does not require declaration of a corresponding dividend. (¶60; A38)

Significantly, the 2013 Settlement only released claims "from the beginning of time through the date of th[e] Stipulation." (*See* Stipulation of Settlement ("Settlement Stip."), dated July 8, 2013, ¶23; A353-354). Accordingly, in their application for approval of the 2013 Settlement, plaintiffs made it clear that "the Settlement is not intended and does eliminate the [ ] Board's ability (or obligation) to demand immediate repayment of some or all of the outstanding Loan balance if such action would otherwise be required by the Board's fiduciary duties." (*See* Plaintiffs' Brief in Support of Proposed Settlement and Application for Attorneys' Fees and Reimbursement of Expenses, dated August 19, 2013 ("2013 Settlement Brief") at 16 n.3; A269). Counsel for the INC acknowledged during the approval hearing that the CCOH Board maintains the right (and the duty) "before the triggers set forth in the settlement are hit to demand repayment of all or a portion of the due from the balance." (*See* Transcript of September 9, 2013 Settlement Hearing ("9/9/13 Hr. Tr.") at 32:13-21; A328).

D. THE BOARD DEFENDANTS' FAILURE TO DEMAND REPAYMENT

In its 11 fiscal quarters from the 2013 Settlement to the time of GAMCO's

Complaint, Defendant iHM reported negative net income[6] and yearly losses on a consolidated basis of $606 million in 2013, $793 million in 2014, and $737 million in 2015 (iHC does not separately report financial results). (¶63; A39-40).

iHM's consistent losses and iHC's ***$20.8 billion*** in debt preclude restructuring except on highly unfavorable terms or as part of a bankruptcy. (¶64; A40). In 2015 alone, the iHeart Defendants paid a staggering $1.74 billion in interest, driving a net loss of hundreds of millions of dollars despite $6.5 billion in 2015 revenue. (¶64; A40). Moreover, nearly $8.5 billion in debt (other than amounts owed under the Revolving Note) comes due in the next three years, consisting of at least $193 million in notes maturing in 2016 and $8.3 billion in 2019 bonds and term loans. (¶65; A40).

Despite the iHeart Defendants' deteriorating financial condition since the 2013 Settlement and the new circumstances and risks to CCOH and its minority shareholders, the Board Defendants have failed to demand repayment on the Revolving Note. (¶68; A41).

E. THE TRANSACTIONS TO BENEFIT THE iHEART DEFENDANTS

1. The Note Offering

In December 2015 and January 2016, the CCOH Board engaged in the Note

[6] iHM's negative net income has now reached 14 consecutive quarters as of September 2016. *See* iHM, Quarterly Report (Form 10-Q) (Nov. 9, 2016). *See also* Transcript of September 12, 2016 Oral Argument on Motion to Dismiss at 104:6-15 (A530).

Offering in which a CCOH subsidiary issued issue $225 million in 8.75% Senior Notes due 2020 that will cause CCOH to incur $98.4 million in interest expense over the life of the notes. (¶¶85-86, 89; A48-49, 50).

The Asset Sales

In the first quarter of 2016, the Board Defendants authorized the Asset Sales in eight strategic U.S. markets that generated $602 million in cash. (¶93; A51). In 2015, these assets generated $105 million in revenue and $29 million in operating income for CCOH. (¶93; A51).

3. The Transactions Did Not Benefit CCOH

In February 2016, the CCOH Board made a repayment demand of $300 million on the Revolving Note and contemporaneously declared a special cash dividend of $540 million. (¶¶70-72; A42-43). However, any benefit to CCOH from the $300 "repayment" was illusory. (¶¶72-73; A42-43). CCOH retained none of the proceeds of the repayment demand or Asset Sales, which funded the dividend. (¶¶87, 101, A49, 56). As 90% owner of CCOH's stock, iHC received approximately $486.7 million of the $540 million February dividend. (¶72; A42).

Effectively, Defendants created a "round trip" transaction where a wholly-unnecessary sale of CCOH's assets allowed the Board Defendants to couple the proceeds of those transactions with the $300 million "repayment" to fund a dividend, 90% of which would go back to iHC. (¶72; A42-43).

F. THE COMPLAINT AND COUNTS AGAINST THE DEFENDANTS

Based on the Board Defendants' failure to demand repayment on the Revolving Note and approval of the Note Offering and Asset Sales to provide liquidity to the iHeart Defendants, on May 9, 2016, GAMCO filed the Complaint alleging: (i) breach of fiduciary duty against the Board Defendants, iHeart Defendants and Private Equity Defendants; (ii) in the alternative, aiding and abetting breach of fiduciary duty against the iHeart Defendants and Private Equity Defendants; (iii) unjust enrichment against the iHeart Defendants and Private Equity Defendants; and (iv) corporate waste against the Board Defendants, iHeart Defendants and Private Equity Defendants. (¶¶130-160; A65-71).

On July 20, 2016, Defendants moved to dismiss the Complaint.

G. THE COURT OF CHANCERY DECISION BELOW

On November 23, 2016, the Honorable Joseph R. Slights III issued his Memorandum Opinion (the "Decision") dismissing the Complaint with prejudice. The court drew five main conclusions, each of which was erroneous.

1. The Court of Chancery Expanded the Reach of the 2013 Settlement Agreement to Cover Post-Settlement Breaches for Failure to Demand Repayment on the Revolving Note

First, the Court of Chancery ruled that GAMCO's post-Settlement Revolving Note claims were released by the terms of the 2013 Settlement. The court concluded that the 2013 Settlement encompasses GAMCO's breach of fiduciary duty claims

stemming from the CCOH Board's *post-2103* refusal to demand repayment on the Revolving Note. (Dec. at 22-23).[7] The court acknowledged that "many of the facts on which [GAMCO] bases its claims relating to the Revolving Note occurred after the 2013 Settlement" (Dec. at 22), but nevertheless concluded that the 2013 Settlement bars claims relating to the intercompany agreements because such claims "were prosecuted in the 2012 Litigation and released in the 2013 Settlement." (Dec. at 23). In so doing, the court reasoned, wrongly, that the scope of the 2013 Settlement was intended to include any post-2013 increase in the Revolving Note balance, as well as the ongoing deterioration of iHC's financial condition (Dec. at 29), because both of these post-2013 events "are extensions of the same operative facts that were the foundation of the plaintiff's claims in 2012 and at the heart of the 2013 Settlement." (*Id.*).

Second, the Court of Chancery found that even assuming the 2013 Settlement does not bar GAMCO's breach of fiduciary duty claims arising out of the intercompany agreements, no such actionable claim has been pled. Specifically, the Court noted that GAMCO has not alleged a default on the Revolving Note by iHC, or a failure by the INC to "implement or honor the forward-looking elements of the 2013 Settlement." (Dec. at 30).

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[7] Citations to "Dec." refer to the Decision.

2. The Court of Chancery Applied *Res Judicata* to GAMCO's Claims for Failure to Demand Repayment on the Revolving Note

Third, the Court of Chancery held that GAMCO's breach of fiduciary duty claims are barred by the doctrine of *res judicata* stemming from the 2013 Settlement. Specifically, the court found that CCOH was a real party in interest to both litigations, plaintiffs in the 2012 litigation did not prevail on most of their claims, and the 2012 litigation was resolved when the 2013 Settlement was approved. (Dec. at 34). The Court further concluded that the same essential issues were decided in the 2012 litigation and the instant action (Dec. at 36-37), namely, that the 2012 litigation addressed the ongoing increase in the Revolving Note balance and iHC's worsening financial condition. (*Id.*).

3. The Court of Chancery Misapplied the Business Judgement Standard to GAMCO's Claims Based on the Note Offering and Asset Sales

Fourth, the court applied the business judgment standard to its review of the Note Offering and Asset Sales. In so doing, the court ruled that because GAMCO had not adequately alleged that either the Note Offering or the Asset Sales yielded a "unique benefit" to iHC not otherwise shared by CCOH's minority shareholders, the Court rejected the application of the "entire fairness" doctrine to assess the CCOH Board's approval of these transactions. (Dec. at 46-50).

Fifth, the court erroneously engaged in a weighing of facts and drew impermissible inferences for Defendants. From that improper exercise the court concluded that the Complaint failed to plead facts "that would allow a reasonable inference that the iHeart Defendants extracted a unique benefit from CCOH at the expense of the other CCOH stockholders." (Dec. at 49).

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN RULING THAT GAMCO'S POST-SETTLEMENT REVOLVING NOTE CLAIMS WERE RELEASED BY THE 2013 SETTLEMENT AND BARRED BY *RES JUDICATA*

A. QUESTION PRESENTED

Can a previous settlement involving derivative claims brought by a different plaintiff on behalf of the same corporation against the same defendants be extended to release or bar under *res judicata* current claims brought by another plaintiff arising from new facts and circumstances affecting that corporation, even where the previous settlement agreement expressly applied only to claims existing at the time of the settlement and the parties to that settlement acknowledged it did not cover future torts?

GAMCO argued this issue below so it is ripe for appeal. (*See* Plaintiff's Answering Brief in Opposition to Defendants Motion to Dismiss the Verified Stockholder Derivative Complaint, dated August 19, 2016 ("Pl. Opp. Br.") at 18-26, A211-219).

B. STANDARD OF REVIEW

This Court's review of the decision on a motion to dismiss under Ch. Ct. R. 12(b)(6) is *de novo* and plenary. *See Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000). The Court must accept all well-pleaded allegations of the Complaint as true, draw all reasonable inferences in plaintiff's favor, and should not affirm a dismissal

"unless the plaintiff would not be entitled to recover under any reasonably conceivable set of circumstances." *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings LLC*, 27 A.3d 531, 536 (Del. 2011).

C. Merits of Argument

As the trial court seemed to recognize, the Complaint raised two separate theories of liability relating to the Revolving Note, which are demonstrably separate and distinct. The first challenged the enforceability of the Revolving Note itself and, for example, whether the Board Defendants breached their fiduciary duty to CCOH and the minority shareholders by failing to seek to unwind the intercompany notes and cash management agreement. The Court of Chancery ruled that this claim is substantively the same as the prior litigations claims arising from, for example, the Board's decision to extend the Revolving Note. GAMCO concedes that this claim was settled with the 2013 Settlement, and is not appealing the Court of Chancery's dismissal of this aspect of the Revolving Note claims.

The Court of Chancery, however, erred by conflating its assessment of the enforceability of the Revolving Note, which is not at issue in this appeal, with its assessment of GAMCO's second theory of liability involving the Revolving Note. The latter theory asserts that the CCOH Board breached its fiduciary duties by refusing to demand repayment under the Revolving Note, as it indisputably is entitled to do, when iHC's financial condition deteriorated *after* the 2013 Settlement.

GAMCO's theory on this score was direct: based on iHC's financial deterioration post-dating the 2013 Settlement, no CCOH Board member (controlled or otherwise) could in good faith decline to demand repayment of the Revolving Note, and otherwise take action to protect CCOH and its stockholders from the increased likelihood of an iHC default. By dismissing this aspect of the Revolving Note claims, the Court of Chancery erred. First, while the 2013 Settlement gave the INC powers to demand repayment under certain conditions even if the rest of the Board did not and without the rest of the Board's support, the 2013 Settlement expressly preserved all fiduciary duties otherwise applicable to the Board as a whole, so that the entire Board could face liability for refusing to demand repayment if circumstances so warranted.

If upheld, the Court of Chancery's opinion declares that a settlement release from a prior litigation can give corporate defendants *carte blanche* to breach their fiduciary duties in the future, regardless of the emergence or occurrence of new facts. This cannot be Delaware Law.

1. The 2013 Settlement Did Not Release GAMCO's Revolving Note Claims

The Court of Chancery's ruling that the 2013 Settlement releases GAMCO's claim as to the Board's recent refusal to make a repayment demand conflicts with the plain language of the release.

The 2013 Settlement released claims that could have been asserted "from the

beginning of time through the date of this Stipulation."[8] Defendants were parties to and executed the 2013 Settlement, and agreed (as did all other parties to the settlement) that the settlement did not modify or eliminate the Board's fiduciary duties. The 2013 Settlement did not affect, and was not intended to affect, the Board's fiduciary duties going forward. It merely established liquidity triggers that enable the INC to demand repayment on behalf of CCOH without full Board approval. This created a contractual right that allowed supposedly independent directors to exercise the authority of the full (and admittedly conflicted) Board to demand repayment under the Revolving Note in certain specially defined situations. Empowering a subset of the Board (*i.e.,* the members of the INC) to take action it would not otherwise have authority to undertake—demand a repayment irrespective of the wishes of the non-independent directors that dominate the Board—is hardly permission for the Board to forsake its duties.

Since the 2013 Settlement did nothing to relieve the full Board of its independent and unyielding fiduciary duties, when iHC's financial condition deteriorated following the 2013 Settlement, the full Board had a fiduciary responsibility to demand repayment under the Revolving Note. *Corporate Prop. Assocs. 6 v. Hallwood Grp. Inc.*, 817 A.2d 777, 779 (Del. 2003) (When determining

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[8] *See* Settlement Stip. at 14-15 (A353-354). Thus, Plaintiff is not appealing the Court of Chancery's ruling that the 2013 Settlement bars a challenge to the existence or enforceability of the Revolving Note.

whether a release covers a claim, "the intent of the parties as to its scope and effect are controlling.") (quotation omitted).

GAMCO's assertion that iHC's financial deterioration in the years following the 2013 Settlement triggered a fiduciary obligation for the Board to demand a repayment could not have been asserted in that prior action and the Defendants cannot unilaterally broaden the scope of the release to absolve their post-2013 Settlement breaches of fiduciary duty. *See*, *e.g.*, *Seven Invs., LLC v. AD Capital, LLC*, 32 A.3d 391, 396 (Del. Ch. 2011) ("[W]here the language of the release is clear and unambiguous, it will not lightly be set aside.") (alteration in original) (quotation omitted).

To be sure, the parties to the 2013 Settlement expressly confirmed their intent to preserve the full Board's future responsibilities in numerous ways. As the plaintiffs explained in their application for final settlement approval:

> [T]he Settlement is not intended and does not eliminate the [ ] Board's ability (or obligation) to demand immediate repayment of some or all of the outstanding Loan balance if such action would otherwise be required by the Board's fiduciary duties.[9]

The 2013 plaintiffs reiterated this point at the settlement hearing:

> [T]here is nothing in this settlement that lets [the Board] off the hook to say, 'Well, gee, now we don't have to regularly reassess the amount of cash there.' It's not like, okay, as long as you're under this threshold, you don't have to give it back. You always have to be mindful of your

[9] *See* 2013 Settlement Brief at 16 n.3 (A269).

fiduciary duties.[10]

Counsel for the CCOH Special Litigation Committee agreed that, irrespective of the 2013 Settlement, "the [CCOH] board always has the right before the triggers set forth in the settlement are hit to demand repayment of all or a portion of the due from the balance."[11]

Therefore, the parties to the 2013 Settlement made clear that as new facts occurred related to iHC's financial condition and the Revolving Note, the CCOH Board still had a fiduciary obligation to demand repayment under certain circumstances. GAMCO in the current action alleges such circumstances have occurred due to iHC's post-2013 Settlement financial difficulties and the enormous amount outstanding under the Revolving Note. (¶¶63-67). While a factfinder could disagree with GAMCO on this score, Defendants cannot avoid review of the merits of this claim based on the 2013 Settlement.

Indeed, if the release in the 2013 Settlement released claims based on future events, it would be overbroad and unenforceable. *See In re Phila. Stock Exch., Inc.*, 945 A.2d 1123, 1146 (Del. 2008) ("a release is overly broad if it releases claims based on a set of operative facts that will occur in the future. If the facts have not yet occurred, then they cannot possibly be the basis for the underlying action . . . In

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[10] *See* 9/9/13 Hr. Tr. at 24:7-13 (A320).

[11] *See* 9/9/13 Hr. Tr. at 32:13-21 (A328).

other words, a release is overly broad if it releases claims based on a common set of tangential facts, as opposed to operative or core facts.”). Since GAMCO alleges that the members of the CCOH Board breached their fiduciary duties by refusing to demand repayment under the Revolving Note ***because of*** the financial state of iHC and size of the outstanding balance in the years following the 2013 Settlement, the 2013 Settlement did not, and could not, release this aspect of the Revolving Note claims.

2. *Res Judicata* Does Not Bar GAMCO’s Revolving Note Claims

Nor is GAMCO’s Revolving Note demand claim barred by *res judicata.* The doctrine of *res judicata* “serves to prevent multiplicity of needless litigation of issues by limiting parties to one fair trial of an issue or cause of action which has been raised or should have been raised in a court of competent jurisdiction.” *LaPoint v. AmerisourceBergen Corp.*, 970 A.2d 185, 192 (Del. 2009) (citation omitted).

To assert a successful *res judicata* defense, Defendants must show that “the same transaction formed the basis for both the present and former suits” and that the plaintiff “neglected or failed to assert claims which in fairness should have been asserted in the first action.” *Id.* at 193-194; *Kossol v. Ashton Condo. Ass’n*, *Inc.*, 637 A.2d 827 (Table), 1994 WL 10861, at *2 (Del. 1994). GAMCO does not appeal the Court of Chancery’s ruling that any challenge to the existence of the Revolving Note itself is barred by *res judicata*.

The Court of Chancery, however, also ruled that GAMCO's claim as it related to the Board's failure to make a repayment demand as the Company's financial condition deteriorated is also barred by *res judicata* because the fact that "the Revolving Note balance has increased and iHC's financial condition has worsened [ ] reflects a continuation of the 'common nucleus of operative facts' that were at the heart of the 2012 Litigation, not a separate transaction for purposes of *res judicata*."[12] With respect to this ruling, the Court of Chancery erred because this theory of liability is predicated solely on the emergence of facts that postdated the 2013 Settlement. The 2013 Settlement was concerned with the balance of the Revolving Note and iHC's financial condition as each stood at the time. As explained above, the 2013 Settlement did not, and could not, give the Board license to ignore the balance of the Revolving Note and iHC's financial condition going forward. As the theory of liability GAMCO is currently advancing in this action is solely concerned with the balance of the Revolving Note and iHC's financial condition ***following*** 2013 Settlement, it cannot be barred by *res judicata*. *See LaPoint*, 970 A.2d at 195 (holding claims not barred by *res judicata* as they were based on "facts [that] were not, and could not have been, known to plaintiffs in the second action at the time of the first action").

[12] *See* Dec. at 37.

As in *LaPoint*, GAMCO's claim that the Board breached its duty by failing to make a repayment demand under the Revolving Note is based on events that had not yet occurred at the time of the 2013 Settlement. GAMCO was not repeating its challenge to the existence of the Revolving Note or CCOH's decision to enter into the Revolving Note. Rather, GAMCO challenges the Board's refusal to demand repayment under the note once iHC's financial condition severely deteriorated following the 2013 Settlement. Absent the invention of a flux capacitor, the plaintiff in the prior action could not have asserted this claim.[13] Accordingly, the claim currently before the Court is not barred by *res judicata*. *See Dover Historical Soc'y, Inc. v. City of Dover Planning Comm'n*, 902 A.2d 1084, 1092 (Del. 2006) (holding that *res judicata* ruling of the Superior Court was "legally erroneous" because the claim rested entirely on upon facts that did not arise until after the prior litigation); *see also Storey v. Cello Holdings, LLC*, 347 F.3d 370, 384 (2d Cir. 2003) ("Where the facts that have accumulated after the first action *are enough on their own* to sustain the second action, the new facts clearly constitute a new 'claim,' and the second actions is not barred by *res judicata*.") (emphasis added); *Moore's Federal Practice* § 131.22[1], at 131-55 (3d ed. 2006) (same).

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[13] A flux capacitor is a fictional device from *Back to the Future* that makes time travel possible. *See DeLorean Time Machine*, Wikipedia (Jan. 39, 2017), https://en.wikipedia.org/wiki/DeLorean_time_machine.

II. THE COURT OF CHANCERY ERRED IN APPLYING THE BUSINESS JUDGMENT STANDARD TO THE NOTE OFFERING AND ASSET SALES THAT PROVIDED UNIQUE BENEFITS TO THE IHEART DEFENDANTS

A. QUESTION PRESENTED

When the board of directors of a dominated company approves conflicted transactions solely for the purpose of providing to majority shareholders the unique benefit of crucial liquidity to service the majority shareholders' debt and avoid bankruptcy, is it proper for the Court of Chancery to apply the business judgment standard merely because minority shareholders nominally received *pro rata* benefits from the transactions that were otherwise detrimental to the company and the minority shareholders' investment in the company?

GAMCO argued this issue below so it is ripe for appeal. (*See* Pl. Opp. Br. at 27-35, A220-227).

B. STANDARD OF REVIEW

As stated above, the Court's review of the decision on a motion to dismiss is *de novo* and plenary. *Brehm*, 746 A.2d at 253. The Court must accept all well-pleaded allegations of the complaint as true, draw all reasonable inferences in Plaintiff's favor, and should not affirm a dismissal unless the plaintiff cannot recovery under any reasonably conceivable circumstances. *Cent. Mortg.*, 27 A.3d at 536.

C. MERITS OF ARGUMENT

Delaware courts evaluating conflicted transactions have routinely held that "[i]f a challenged transaction would confer a unique benefit," such as liquidity, "on a party exercising . . . control, then entire fairness is the standard of review." *OTK Assocs., LLC v. Friedman*, 85 A.3d 696, 724 (Del. Ch. 2014); *In re Activision Blizzard, Inc. S'holder Litig.,* C.A. No. 8885-VCL (Del. Ch. June 6, 2014) (holding that entire fairness governed a transaction between company and its controlling stockholder because the transaction "confer[red] a benefit on a controlling stockholder that was not shared with the rest of the stockholders. That benefit was liquidity."). Likewise, where corporate fiduciaries cause a corporation to undertake a transaction in order to serve the unique or divergent interests of a large stockholder – such as that stockholder's need for cash or liquidity – those fiduciaries breach their duty of loyalty.

As Vice Chancellor Laster explained in *In re PLX Technology Inc. Shareholders Litigation*:

> Delaware law recognizes, for example, that investors who hold common stock may labor under circumstances that cause their interests to diverge, ***with liquidity being a prominent case***. Liquidity may lead directors to breach their fiduciary duties and stockholder directors may have been found to breach their duty of loyalty if the desire to gain liquidity causes them to manipulate a . . . process.

Transcript of Oral Argument at 26-27, *Id.*, C.A. No. 988-VCL (Del. Ch. Sept. 3, 2015) (emphasis added). *See also N.J. Carpenters Pension Fund v. Infogroup, Inc.*,

C.A. No. 5334-VCN, 2011 WL 4825888, at *9 (Del. Ch. Sept. 30, 2011) ("Liquidity has been recognized as a benefit that may lead directors to breach their fiduciary duties.") (citing *McMullin v. Beran*, 765 A.2d 910, 922-23 (Del. 2000)); *In re Answers Corp. S'holders Litig.*, C.A. No. 6170-VCN, 2012 WL 1253072, at *7 (Del. Ch. Apr. 11, 2012) (same). Under Delaware law, this is the rule *regardless* of whether the challenged transaction results in all stockholders nominally receiving the same transaction consideration.

For example, in *McMullin*, the Delaware Supreme Court sustained claims for breach of the duty of loyalty, and held that entire fairness was the applicable standard of review, where the plaintiff alleged that the board of directors of ARCO Chemical Company ("Chemical") approved a sale of Chemical that accommodated the "immediate need for cash" of Chemical's parent company and 80% stockholder, Atlantic Richfield Company. 765 A.2d at 920-23.

Likewise, in *N.J. Carpenters*, the Court of Chancery sustained claims for breach of fiduciary duty against a 37% stockholder and director of *info* GROUP, Inc. ("infoGROUP"), Vinod Gupta ("Gupta"), where the plaintiff alleged the sale of infoGROUP was "orchestrated so that Gupta could obtain desperately needed liquidity." 2011 WL 4825888, at *2. In denying Gupta's motion to dismiss, the Court held that "[w]hile all of the shareholders received cash in the Merger, *liquidity* was a benefit unique to Gupta." 2011 WL 4825888, at *10; *see also Answers Corp.*,

2012 WL 1253072, at *7 (holding same where two directors of Answers Corporation "sought a sale of the Company in order to achieve liquidity for Redpoint," a 30% stockholder of Answers).

1. The Complaint Establishes the Notes Offering and Asset Sales Were Consummated Solely to Provide Liquidity to the iHeart Defendants

The Complaint alleges that the CCOH Board undertook the Note Offering and Asset Sales for the sole purpose of funneling cash to iHC [redacted] [redacted]. (¶¶74-101; A43-56). [redacted]

[redacted]

[redacted] And while the Note Offering and Asset Sales ultimately led to the payment of a *pro rata* dividend, because those transactions provided – and indeed were conceived, structured, and implemented to provide – iHC the unique benefit of liquidity, GAMCO has stated a claim for breach of fiduciary duty.

2. *Sinclair* and *Synthes* Do Not Support the Court's Conclusion

The Court of Chancery relied on *Sinclair Oil Corp. v. Levien*, 280 A.2d 717 (Del. 1971) and *In re Synthes, Inc. Shareholder Litigation*, 50 A.3d 1022 (Del. Ch. 2012) to dismiss the claims arising from the Note Offering and Asset Sales. Both cases are distinguishable.

In *Sinclair*, a minority stockholder of Sinclair Venezuelan Oil Company ("Sinven"), a subsidiary of 97%-stockholder Sinclair Oil Company ("Sinclair"), challenged a series of *pro rata* dividends paid by Sinven over the course of six years. The plaintiff alleged "Sinclair caused Sinven to pay out such excessive dividends that the industrial development of Sinven was effectively prevented, and [Sinven] became in reality a corporation in dissolution." *Sinclair*, 280 A.2d at 720. Because the plaintiff failed to establish that the dividend was "in essence self-dealing by the parent," the Court found that entire fairness did not govern the plaintiff's claims. (*Id.* at 720-21). The Court further held that the plaintiff did not otherwise rebut the presumptions of the business judgment rule because the plaintiff could not establish any "gross overreaching" on the part of Sinclair. (*Id.* at 722). Among other things, the "plaintiff contend[ed] only that the dividend payments drained Sinven of cash to such an extent that it was prevented from expanding," but could not point to a single business opportunity or strategy of which the subsidiary was deprived. Nor could

the plaintiff show "that the dividend payments resulted from improper motives and amounted to waste." (*Id.*).

Unlike in *Sinclair*, the Note Offering, Asset Sales, and resulting dividends constitute quintessential "self-dealing" transactions because through those transactions iHC was able to "'derive [] a[] personal financial benefit'" – in the form of liquidity – that did not "'devolve[] upon the corporation or all stockholders generally." *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 363 (Del. 1993) (quoting *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984)).

Likewise, GAMCO has alleged "overreaching" by the iHeart Defendants in causing CCOH to undertake the Note Offering and Asset Sales, and pay the resulting dividends. Unlike in *Sinclair,* where the plaintiff failed to establish that the challenged dividends prevented Sinven from engaging in any business opportunities, here, GAMCO has specifically alleged that [REDACTED] in order to funnel cash to iHC and the iHeart Defendants. (¶¶75, 78-79; A44, 45-46). GAMCO has also established an "improper motive" in connection with those transactions because they were intended to unnecessarily divert CCOH assets to another entity, iHC, with which CCOH Board members were associated. *See, e.g.*, *Teachers' Ret. Sys. of La. v. Aidinoff*, 900 A.2d 654, 659 (Del. Ch. 2006) (finding "pled facts also suggest[ed] an improper motive" for an arrangement whereby AIG made unnecessary payments to a third-party, Starr, "as Starr was

controlled and owned by top AIG executives who stood to benefit, at AIG's expense, from the revenue streams diverted into Starr").

Synthes similarly fails to provide a basis to dismiss the Complaint. There, the Court of Chancery found "no basis to conclude that the controlling stockholder" of Synthes, Inc. ("Synthes") "had any conflict with the minority" stockholders in connection with the sale of Synthes such that it would justify "the imposition of the entire fairness standard." *Synthes*, 50 A.3d at 1024. Among other things, the Court found that there were "no well-pled facts" to suggest that the controller caused Synthes to undertake the sale "in order to satisfy some urgent need for cash." (*Id.* at 1036). Likewise, the plaintiff there had pled "no facts suggesting that [the controller] faced a solvency issue" and its complaint was "devoid of allegations suggesting that [the controller] was in any particular rush to [enter the transaction at issue]." (*Id.*). Nor were there any "pled facts in the complaint" that would "support a basis for conceiving that [the controller] wanted or needed" Synthes to undertake the allegedly unfair transaction, "as opposed to having billions of reasons to make sure" that the company undertook a value-maximizing transaction in stockholders' best interests. (*Id.* at 1037).

Finally, the Court of Chancery was incorrect when it found that that, under *Synthes*, a plaintiff can challenge a third-party transaction designed to benefit a controller only in "'very narrow circumstances,'" involving a "crisis, fire sale"

undertaken to satisfy the controller's "idiosyncratic need for immediate cash." (Def. Br. at 40-41). In *Synthes*, the Court merely hypothesized the "sort of uncommon scenario" involving a third-party ***sale of a company*** that would nevertheless require a controller to establish that that third-party sale was entirely fair to the corporation. *See, e.g., Id.,* 50 A.3d at 1036 (describing "a crisis, fire sale . . . ***of the corporation***") (emphasis added). Nowhere in *Synthes* did the Court hold that where, as here, a board of directors sells assets and issues high-interest debt solely to funnel cash to its near-insolvent controlling stockholder, but then distributes the proceeds of those self-dealing transactions *pro rata* to all stockholders, that the transaction is protected by the business judgment rule. To the contrary, as the Court of Chancery has more recently held, "[u]nder current law, the entire fairness framework governs any transaction . . . in which the controller" as here, "receives a non-ratable benefit." *In re Ezcorp Inc. Consulting Agreement Derivative Litig.*, C.A. No. 9962-VCL, 2016 WL 301245, at *11 (Del. Ch. Jan. 25, 2016), *reconsideration granted in part,* 2016 WL 727771 (Del. Ch. Feb. 23, 2016).

3. The Court of Chancery Engaged in Inappropriate Weighing of Facts and Drew Impermissible Inferences for Defendants

The Court of Chancery described as "conclusory" the Complaint's allegations that the Note Offering and Asset Sales were perpetrated solely to benefit the iHeart Defendants, and that the allegations are "a far cry from the 'very narrow circumstances' where this Court will find that an arms-length transaction with a third party yielded the kind of unique benefit to a controller that would justify entire fairness review." These conclusions are the result of weighing of facts and drawing of inferences in favor of Defendants that, as has long been the case, were inappropriate.

The Complaint alleges, supported in detail by public documents and internal CCOH board minutes alike, that, among other things:

- The iHeart Defendants have been in financial crisis since 2013, including suffering $606 to $793 million per year in sustained losses and owing $20.8 billion (¶63; A39-40);

- iHM's debt has been trading around 35 percent of par and its stock price has fallen from $7.50 per share in June 2015 to around $1 (¶67; A41);

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- In December 2015, CCOH consummated that Note Offering that caused it incur unneeded interest expense while retaining none of the proceeds (¶¶85-87; A48-49);

These well-pleaded facts, which the Court of Chancery was required to take as true (a task which should have been made easier by the fact the allegations were taken from CCOH's Board minutes), are a more than adequate demonstration at the motion to dismiss stage that: (i) the transactions were the result of conflicting interests between the iHeart Defendants and CCOH; (ii) the sole purpose of the transactions was to provide liquidty to the iHeart Defendants that CCOH did not need, request, or recieve (all the proceeds were dividended); (iii) the transactions were detrimental to CCOH in that it was forced to incur unncessary interest obligations and for no tangible benefit; and (iv) the transactions were detrimental to CCOH's minority shareholders in that their

investment in CCOH is being impared by the unncessary transactions Defendants are forcing on the Company. Put another way, the Complaint alleges the Note Offering and Asset Sales were solely considered and consumated to provide a "unique benefit" to the iHeart Defendants.

In the face of these facts, the Court of Chancery noted that: (i) "CCOH's financial advisers believed the process and price [for the Asset Sales] were fair"; (ii) "the Board concluded 'that, separate and apart from [iHM's] liquidity position, such transactions are in the best interest of [CCOH] and all of its stockholders in light of the prices offered by the bidders for such non-core assets'"; (iii) "the Complaint alleges nothing that would support the notion that the Note Offering was of the nature of a fire sale"; and (iv) "the Board in fact considered and discussed the negative consequences for CCOH should the iHeart Defendants be forced into bankruptcy." (Dec. at 47-49).

The Court of Chancery's weighing of these "competing facts" (if indeed the Court of Chancery's interpretation of them is correct), including the court's crediting of the Board's self-serving statements, and drawing inferences in favor of the Defendants at the motion to dismiss stage was reversible error.

4. The Court of Chancery Erred By Dismissing GAMCO's Aiding and Abetting and Unjust Enrichment Claims

The Court of Chancery dismissed GAMCO's aiding and abetting breach of fiduciary duty claims against the iHeart and Private Equity Defendants solely due to the purported failure of the Complaint to plead underlying breaches of fiduciary duty. (Dec. at 49-50). Similarly, the trial court dismissed GAMCO's unjust enrichment claim against the iHeart and Private Equity Defendants on the basis that the claim is purportedly "duplicative" of the breach of fiduciary duty claims and thus the court's conclusions applied equally. (Dec. 50-51). Because, as set forth herein, the Court of Chancery erred in dismissing the breach of fiduciary duty claims, it likewise erred in dismissing GAMCO's aiding and abetting breach of fiduciary duty and unjust enrichment claims.

CONCLUSION

GAMCO's Complaint satisfies the Court of Chancery Rule 12(b)(6) standard to allege a claim that Defendants breached their fiduciary duties to CCOH and the Company's minority shareholders. The Court of Chancery's conclusion to the contrary, and the bases underlying that conclusion, were in error. GAMCO respectfully asserts that the Decision should be reversed, and the case remanded to the Court of Chancery for further proceedings.

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