



IN THE SUPREME COURT OF THE STATE OF DELAWARE

JACK L. MARCHAND II,

Plaintiff-Below,
Appellant,

v.

JOHN W. BARNHILL, JR., GREG BRIDGES,
RICHARD DICKSON, PAUL A. EHLERT, JIM E.
KRUSE, PAUL W. KRUSE, W.J. RANKIN,
HOWARD W. KRUSE, PATRICIA I. RYAN,
DOROTHY MCLEOD MACINERNEY, AND BLUE
BELL CREAMERIES USA, INC.

Defendants-Below,
Appellees.

No. 533,2018

Court Below:
The Court of Chancery of
the State of Delaware

C.A. No. 2017-0586-JRS

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APPELLANT'S OPENING BRIEF

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NATURE OF PROCEEDINGS

This action asserts derivative claims for breaches of fiduciary duty against two Officers and 10 Directors of Blue Bell Creameries USA, Inc. (“BB USA” or “Company”), relating to the deadly bacterial contamination crisis at the Company, which was discovered by regulatory authorities in early 2015. All three of the Company’s production facilities and ice cream products distributed by the Company around the country were found to be contaminated with *Listeria monocytogenes*. A total product recall resulted. Humans were sickened, and some died. The contamination required a months-long business shutdown and extensive facilities remediation and overhaul of operating procedures. In addition, to the enormous costs to the Company resulting from the contamination, the *Listeria* crisis [REDACTED]

[REDACTED]

Plaintiff below Appellant, Jack L. Marchand II, owns [REDACTED] of BB USA common stock, on which the Company paid dividends of approximately [REDACTED] per share per quarter prior to the *Listeria* crisis. Plaintiff made a demand and obtained Company documents pursuant to 8 *Del. C.* §220 (“220 Demand”). The Verified Stockholder Derivative Action Complaint (“Complaint”), based on information from the Company’s internal documents, asserts two counts. Count I is a claim against the Company founder’s grandsons, Paul Kruse and Greg Bridges (“Officer

Defendants”), for breach of their fiduciary duties as the Company’s Officers with direct responsibility for the operations including the detection, prevention and correction of contamination problems and health and safety compliance. Count II is a so-called *Caremark*¹ claim against 10 of the Company’s Directors for their failure to institute and maintain a Board-level system of controls for oversight, in breach of the Directors’ duties of loyalty.

Defendants moved to dismiss the Complaint under Rules 12(b)(6) and 23.1. At oral argument on March 19, 2018, the Court of Chancery requested Defendants to submit additional Board of Directors minutes. (Tr. at 82-83). In addition, on May 11, 2018, the Court of Chancery requested supplemental submissions from the parties on certain questions relating to Counts I and II, generally related to Defendants’ fiduciary duties as BB USA Officers and Directors where the Company’s key operations are held at the subsidiary level in a limited partnership structure. (A0275-A0283). The parties filed their submissions on June 13, 2018. (A006, A0284-A0302).

On September 27, 2018, the Court of Chancery issued an Opinion and Order (“Opinion” or “Op.”) (filed herewith as Exhibit A), granting Defendants’ motions to dismiss under Rule 23.1. (Op. at 1-2, 29, 51-52). The Court held that demand was not excused as to Count I or Count II. The Court of Chancery’s ruling

¹ *In re: Caremark Int’l*, 698 A.2d 959, 968 (Del. Ch. 1996).

expressly did not address the Rule 12(b)(6) motions. (Op. at 29). Appellant appeals from the Opinion.

SUMMARY OF ARGUMENT

1. The Court of Chancery erred in holding that the Complaint “failed [under the *Rales* standard²] to plead particularized facts that raise a reasonable doubt as to whether a majority of the BB USA Board could impartially consider a demand [to bring Count I, because] [t]he Compliant offers no reason to doubt that [Directors] Reimann, Ryan, Ehlert and Rankin [,who hold eight of the Board’s fifteen votes,] are independent of the Officer Defendants and would have been capable of impartially considering a demand.” (Op. at 43). The Court rejected the particularized facts alleged regarding Rankin’s close career-long relationship with the Kruse family, based on a vote Rankin cast as a Director in 2016 in favor of

[REDACTED]. In doing so, the Court improperly failed to “consider all the particularized facts pled ... about the relationships between the director and the interested party in their totality and not in isolation from each other, and draw all reasonable inferences from the totality of those facts in favor of the plaintiffs.” *See Del. County Emples. Ret. Fund v. Sanchez*, 124 A.3d 1017, 1019 (Del. 2015). The 2016 vote on the governance reform issue does not rebut

² Under *Rales*, the Court determines whether the particularized facts create a reasonable doubt that, if a demand had been made to bring Count I, the Board of Directors could have properly exercised its independent and disinterested business judgment in responding to it. *Rales v. Blasband*, 634 A.2d 927, 934 (Del. 1993).

the reasonable doubt regarding Rankin's impartiality created by the strong relationship allegations on the matter at issue: the consideration a demand to sue Paul Kruse and Greg Bridges for potentially enormous personal liability. The Court of Chancery also failed to consider the totality of the facts alleged and draw all reasonable inference in favor of Plaintiff regarding Director Ehlert's family's long and close relationship with the Kruse family in the context of the small community of Brenham, Texas, characterizing the allegations as "routinely [found to be] conclusory" and not to raise a reasonable doubt regarding director impartiality. (Op. at 41). In doing so, the Court failed to give Plaintiff the due benefit of the reasonable inference that, under the particular facts alleged, Ehlert's relationship with the Kruse family was of the kind of relationship "likely considered precious by many people" supporting "a pleading stage inference ... that it is important to the parties." *See Sanchez*, 124 A.3d at 1022. A majority of the Directors requires eight votes. Reimann and Ryan are concededly impartial for demand futility purposes, but together hold only six votes. The Opinion therefore must be reversed on Count I.

2. The Court of Chancery erred in holding that the Complaint failed to state a claim for breach of the duty of loyalty against the 10 BB USA Directors to excuse demand on Count II. The Court rejected the allegations and reasonable inferences supporting a conscious lack of any system of Board-level controls and

reporting, based on manuals, procedures and testing at the operations level that were never considered or monitored by the Board. The Board-level oversight function is crucial where, as here, the Company's key operations are held at the subsidiary level. *See Grace Bros. v. Uniholding Corp.*, 2000 Del. Ch. LEXIS 101, *43-44 (July 12, 2000). The Complaint alleges that Company internal records including nearly two years of Board minutes evidence that the Company lacked any Board-level system of controls and reporting for oversight, and that the Board consciously left reporting and controls completely to the discretion of management to determine what controls were necessary and sufficient and when and whether to bring information to the Board. Ten of the Company's 11 Directors (excluding Reimann) face a substantial likelihood of liability for Count II. The Opinion therefore must be reversed on Count II. (A0298-A0300).

STATEMENT OF FACTS

This Statement of Facts is based on the allegations of Complaint and the reasonable inferences therefrom, including the exhibits to the Complaint and the documents produced to Plaintiff and submitted to the Court of Chancery in response to the Court's requests in connection with the motions to dismiss.

A. THE COMPANY HAS BEEN CONTROLLED AND RUN BY THE KRUSE FAMILY FOR NEARLY 100 YEARS

Although the Kruse family has held a substantial but less than a majority stock interest in the Company,³ the Company has been ██████████ run for nearly 100 years by the family of the Company's founder, E. F. Kruse. (A0020-A0022, A0028). E. F. Kruse founded the Company in 1919, in the small town of Brenham, Texas. (A0020-A0021). The Company's headquarters and original production facility have remained in Brenham. (A0020-A0022). Brenham currently has a population of approximately 17,000. (A0245).

E. F. Kruse died unexpectedly in 1951. (A0021). His sons, Ed F. Kruse and Howard Kruse, took over control of the business. (*Id.*). Ed F. and Howard spent their lives and careers controlling and running the business. (A0014-A0015, A0017, A0028-A0029, A0031). Ed F. Kruse held the positions of Chairman, President and Chief Executive Officer until he passed the position of President to

³ Defendants represented that members of the Kruse family control at least ██████████ of the Company stock. (A0266-A0267).

Howard Kruse in 1986 and the position of CEO to Howard in 1993. (A0018, A0031). Howard Kruse became a Director in 1985. (A0018). [REDACTED]

[REDACTED] (A0031). Ed F. Kruse remained a Director and Officer in the position of “Chairman Emeritus,” until his death in September 2015. (A0014-A0015, A0031). Howard Kruse remained as a Director and Officer in the position of “President Emeritus.” (A0018, A0028-A0029).

Howard Kruse’s son, Jim Kruse, has served as an Officer and a Director of the Company. (A0016). Jim has been a Director since 2004. Jim was Controller and became Secretary of the Company in 2004. (*Id.*). Jim served as Vice President of Information Technology from 2013-2015. (*Id.*). Jim resigned as an Officer in 2015 to become President of the Bank of Brenham (of which Director John Barnhill is Chairman), and remained as a Director. (*Id.*). Jim Kruse became Chairman in 2017, succeeding Paul Kruse, who remained a Director. (*Id.*).

Greg Bridges is the son of Howard Kruse’s and Ed F. Kruse’s sister, Mildred. (A0014-A0015). Bridges joined the Company in 1985 and worked in the Brenham plant under Paul Kruse. (*Id.*). In 2011, Bridges became a Director and Officer, Vice President of Plant Operations, in charge of all aspects of plant operations. (*Id.*).

[REDACTED]

The Board of Directors has been populated with members of the Kruse family and individuals with close relationships with the Kruse family. For the three years leading up to the *Listeria* crisis, the Board of 11 Directors included five Kruse family members: Ed F. Kruse, Howard Kruse, Paul Kruse, Jim Kruse and Bridges. (A0014-A0015, A0028-A0030).

Five of the other Directors had long-standing close special relationships with the Kruse family. (A0013-A0015, A0017-A0019, A0029-A0030, A0064-A0066). Director John Barnhill worked in the business for Ed F. Kruse since 1954 before college, and began as a full time employee in 1960. (A0013-A0014). Barnhill spent his career working under Ed F. Kruse, and has been a Director for over 40 years, since 1974. (*Id.*). Ed F. Kruse promoted Barnhill to Vice President in 1986. (*Id.*). Barnhill retired from the Company in 2000, was appointed “Vice-President Emeritus,” remained in Brenham as a Director and has operated a bed and

breakfast business. (*Id.*). Barnhill is Chairman of the Bank of Brenham, and hired Jim Kruse as President. (A0013-A0014, A0064-A0065).

Ed F. Kruse hired Director W. J. Rankin as his administrative assistant in 1981. (A0017-A0018). Ed F. Kruse promoted Rankin and made Rankin a Director, Chief Financial Officer and Treasurer in 1986. (*Id.*). Rankin served as CFO and Treasurer under Ed F. Kruse, Howard Kruse and Paul Kruse, until his retirement at the end of 2014. (A0016-A0018, A0028-A0029). Rankin continued as a Director following his retirement. (A0017-A0018). Ed F. Kruse demonstrated his admiration and respect for Rankin in the naming of a new Brenham college facility in Rankin's honor. In 2010, Ed F. Kruse joined with Rankin to present a check from "Ed Kruse and Friends" in the amount of \$450,000 to the Blinn College Foundation for a newly- constructed agricultural facility on the Brenham campus named the W. J. "Bill" Rankin Agricultural Complex, in honor of Rankin. (A0017-A0018, A0065).

Director Richard Dickson began in the business as an employee in 1981 and has remained continuously employed under the Kruse family for his entire career. (A0015). He is currently President and CEO, having succeeded Paul Kruse in 2017. (A0015-A0017). In 2010, Paul Kruse promoted Dickson to Vice-President of Sales and Marketing, and Dickson was nominated and elected to be a Director. (A0015, A0064, A0244).

Director Dorothy McLeod MacInerney has been a Director for 24 years, since 1994. (A0019). She is a professional author. (*Id.*) While she was a Director, she wrote and published two books praising the history of the Company and the Kruse family. (*Id.*) The first book is “Blue Bell Ice Cream: A Century at the Little Creamery in Brenham, Texas 1907-2007” (published in 2007). (*Id.*) The second book is a biography of Ed F Kruse, entitled “Ed F. Kruse of Blue Bell Creameries” (published in 2016), which went to print just prior to the death of Ed F. Kruse in September 2105. (*Id.*) In her books, MacInerney thanked Paul Kruse for his support and praised him and his having followed in his father’s footsteps in the business. (*Id.*) [REDACTED]

Director Paul Ehlert has been a Director for over 15 years, since 2002. (A0015-A0016). Ehlert is a Brenham businessman and has been a director of two Brenham banks. (*Id.*) [REDACTED]

[REDACTED] Ehlert’s uncle, Melvin Ehlert, was a long-time friend of founder E. F. Kruse, and served as a pallbearer in the funeral of E. F. Kruse, in 1951. (A0064).

Plaintiff conceded that the allegations regarding Director Patricia Ryan are not sufficient to satisfy the demand futility standard. (A0143, A0246). Ryan, however, has also been a long-time Director for over 20 years, since 1997. (A0018). MacInerney wrote in her biography of Ed. F. Kruse that for years Ryan begged Ed F. Kruse to write his memoir, further evidencing the close-knit Kruse-centric culture of the Company. (*Id.*).

B. PAUL KRUSE AND GREG BRIDGES HAD DIRECT RESPONSIBILITY FOR COMPANY OPERATIONS AND THE DETECTION AND CORRECTION OF CONTAMINATION PROBLEMS

The Company produced and distributed ice cream products. By 2015, the Company had three manufacturing plants: Brenham; Sylacauga, Alabama; and Broken Arrow, Oklahoma. (A0021-A0022). The Company also had 50 sales and distribution centers in 23 states. (*Id.*). As a food manufacturer and distributor, the Company was subject to federal and state health and safety laws and regulations. (A0022-A0025). The applicable laws provide steep penalties for non-compliance, including possible criminal prosecution. (A0023). In addition to the penalties for legal non-compliance, pathogenic contamination of food production facilities and edible products distributed to the public poses an obvious risk with potentially deadly consequences to consumers and potentially catastrophic financial consequences to the Company and its stockholders. (A0025-A0026).

Paul Kruse and Bridges were the Company's senior Officers with direct acknowledged responsibility for the Company's operations, including the detection, prevention and correction of contamination problems. (A0032-A0033). By 2014, Paul Kruse held the positions of Chairman, President and CEO. (A0016-A0017, A0031-A0032). Bridges held the second most senior Officer position responsible for all aspects of Company operations, Vice-President Plant Operations. (A0014-A0015, A0031-A0032). Paul Kruse and Bridges acknowledged themselves to regulatory authorities as the persons most responsible for maintaining safety and sanitary operations. (A0032-A0033). A July 2009 FDA report stated:

Mr. Kruse identified himself as the most responsible person at the firm. Mr. Kruse is normally present on a day-to-day basis, oversees management of production, manufacturing and quality control unit and has overall authority to detect, prevent and correct problems at the facility.

(A0033). Bridges reported to the FDA that he was the next most responsible person for operations under Paul Kruse. (A0032). Paul Kruse and Bridges are identified in a March 30, 2011 FDA report as the responsible Company Officers for the Broken Arrow facility. (*Id.*).

The Company had a shallow and direct management structure under Paul Kruse and Bridges. The managers of the production facilities reported directly to Bridges, and Bridges reported directly to Paul Kruse. (A0032-A0033).

C. THE COMPANY HAD NEARLY TWO YEARS OF ESCALATING AND INCREASINGLY FREQUENT POSITIVE TEST RESULTS EVIDENCING POSSIBLE CONTAMINATION AND INEFFECTIVE SANITIZING PROCEDURES

Plaintiff claims that Paul Kruse and Bridges breached their fiduciary duties as Officers of BB USA with direct acknowledged responsibility for operations and the detection, prevention and correction of contamination problems. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] The history of the positive test results the Company had in its possession were cited by the FDA in its reports following the discovery of the *Listeria* contamination and the ensuing FDA investigation. (A0039-A0040, A0050, A0077-A0080, A0082-A0092, A0094-A0098).

More particularly, in early 2015, South Carolina Health discovered *Listeria* bacteria in Company products and [REDACTED]. (A0036). On February 13, 2015, Texas health authorities notified the Company. (A0054-A0055, A0077). [REDACTED]

[REDACTED]
[REDACTED] (A0036-A0041). Human cases of *Listeria* infection were connected to Company products. (A0036-A0037). In April 2015, the Center for Disease Control and Prevention (“CDC”) stated that tests indicated Company products from the manufacturing plants in Texas and Oklahoma were the source of a *Listeria* outbreak that had infected five adults in Kansas, three of whom had died, and that three adults in Texas had been sickened by the *Listeria*. (A0037). [REDACTED]

[REDACTED]
[REDACTED]

By late April 2015, the Company recalled all products. (A0037). The Company ceased all production operations for extensive remediation. (A0041-A0042). [REDACTED]

[REDACTED]
[REDACTED]

[REDACTED]

[REDACTED]⁴

As noted above, the FDA investigation following the *Listeria* discovery found that the Company had nearly two years of increasingly frequent positive tests for possible *Listeria* contamination at the Broken Arrow facility, test results showing coliform contamination in products above the regulatory limit and test results evidencing the inadequacy of the Company's sanitation procedures to resolve the problem. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

⁴ A report aired by CBS in October 2015 included allegations by former employees of a lack of sanitary operating conditions. (A0035-A0036).

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] of Kansas tested a product as positive on March 22, 2015.

(A0049-A0050). [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Texas authorities notified the Company on February 13, 2015. (A0054-A0055). [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

D. REQUIRED EMERGENCY FUNDING DILUTED THE COMPANY STOCKHOLDERS

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

5 [REDACTED]

[REDACTED]

E. BOARD RECORDS EVIDENCE A LACK OF ANY BOARD-LEVEL SYSTEM OF CONTROLS AND REPORTING FOR BOARD OVERSIGHT

Plaintiff obtained, among other things, all BB USA and BB GP Board minutes for 2014-2016 pursuant to the 220 Demand. The minutes evidence a complete lack of any Board-level system for oversight. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] While the Court of Chancery also cites a second reference to “a good report from TCEQ” in the April 29, 2014 minutes, (Op. at 17, 47), which the Court “assume[d] was a reference to the Texas Commission on Environmental Quality,” (Op. at 17 n.70), the more reasonable inference is that the “good report” was related to the environmental impact of construction projects rather than health and safety or sanitary production conditions.⁷

⁷ [REDACTED]

[REDACTED]

In addition, the Board records support an inference that the lack of a Board-level system was a conscious Board decision. [REDACTED]

[REDACTED]

Thus, the allegations including information from Board records support the reasonable inference that the Board consciously lacked any Board-level system for oversight of management and operations, not merely that the Board had an inadequate system that malfunctioned.

F. THE CLAIMS

Count I is a claim against Paul Kruse and Bridges for breach of their fiduciary duties as BB USA Officers. The Complaint alleges Paul Kruse and Bridges disregarded nearly two years of evidence of a possible escalating and unresolved contamination problem and ineffective sanitization procedures, and failed to inform the other Directors regarding the potential problem in a crucial aspect of the business within their direct responsibilities as Officers. Moreover, in early 2015, *all three* production facilities were found to be contaminated to the extent of requiring complete shut-down and extensive remediation, evidencing a Company-wide failure to maintain safe and sanitary operations.

Count II is a so-called *Caremark* claim against 10 of the Company's Directors for the conscious failure to institute and maintain any Board-level system of oversight, in breach of the Directors' duties of loyalty. Reimann was not a Director during the period of the alleged breach.

G. THE COURT OF CHANCERY OPINION

The Opinion dismissed Count I and Count II with prejudice under Rule 23.1. (Op. at 4-5, 52). The Court of Chancery did not address the grounds asserted by Defendants or the parties' positions and arguments under Rule 12(b)(6). The Court held "As for Count I, even assuming Plaintiff has pled a viable fiduciary claim against the Officer Defendants, an assumption that may or may not be valid,

Plaintiff has failed to plead particularized facts to raise a reasonable doubt that a majority of the BB USA Board members could have impartially considered a pre-suit demand to prosecute Count I.” (Op. at 4-5). The Court held that “[t]he Complaint offers no reason to doubt that Reimann, Ryan, Ehlert and Rankin are independent of the Officer Defendants and would have been capable of impartially considering a demand,” and that these Directors hold eight of fifteen Board votes constituting a majority of the Board. (Op. at 43).

“As for Count II, [the Court held] Plaintiff has failed to state a *Caremark* claim against the Director Defendants and, consequently, has failed to plead particularized facts to raise a reasonable doubt that a majority of the otherwise disinterested BB USA Board could have exercised their business judgement in responding to a demand.” (Op. at 5). The Court held that the allegations of the Complaint show that the Company had a manual for reporting and testing and cleaning procedures at the operations level, and that Paul Kruse and Bridges provided regular reports regarding operations at the Company Board meetings, “including reports from the TCEQ and Silliker (a third party food safety auditor).” (Op. at 46-47). The Court found this to be “undisputed evidence that risk management measures have been taken in the company’s operational theater and the Board received reports regarding operations at regular intervals.” (Op. at 48).

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN HOLDING THAT THE COMPLAINT FAILED TO SATISFY THE DEMAND FUTILITY STANDARD FOR COUNT I

A. QUESTION PRESENTED

Does the Complaint “create a reasonable doubt” regarding the impartiality of a majority of the Company Directors to respond to a demand to sue the Officer Defendants on Count I, had a demand been made? (A0013-A0041, A0061-A0066, A0115-A0121, A0136-A0143, A0224-A0229, A0239-A0246, A0270, A0285-A0297).

B. SCOPE OF REVIEW

This Court’s review of the decision on a motion to dismiss under Ch. Ct. R. 23.1 is *de novo* and plenary. *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000). The Court must accept all well pleaded allegations as true and draw all reasonable inferences in Plaintiffs’ favor. *Beam v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

C. MERITS OF THE ARGUMENT

Under *Rales*, “the court ‘must determine whether or not the particularized factual allegations of ...[the] complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could have properly exercised its independent and disinterested business judgement in responding to a demand.’” 634 A.2d at 934. At the time of the Complaint, the Board consisted of 11 Directors

including Reimann, who held five votes. Plaintiff conceded the impartiality of Reimann and Ryan for the purposes of demand futility on Count I. The Court of Chancery held that “the Complaint offers no reason to doubt that Reimann, Ryan, Ehlert and Rankin are independent of the Officer Defendants and would have been capable of impartially considering a demand.” (Op. at 43). For the reasons below, the Court of Chancery erred in holding that the Complaint offers no reason to doubt the impartiality of Directors Ehlert and Rankin to respond to a demand.

1. Rankin

Rankin spent his entire professional career working for Ed F. Kruse and Paul Kruse, for over 25 years, since Rankin began as Ed F. Kruse’s administrative assistant in 1981, and continuing as Rankin was promoted by the Kruses to CFO and Treasurer in 1986, in which positions Rankin continued until his retirement in late 2014, after which he remained a Director. (A0017-A0018).⁸ In addition, the Complaint alleges that Ed F. Kruse honored Rankin in joining with him to present a \$450,000 donation from “Ed Kruse and Friends” for the new Blinn College agricultural facility in Brenham named for Rankin. The Court of Chancery rejected these particularized allegations, based on Rankin’s vote as a Director in

⁸ The Opinion states that “Rankin worked for Blue Bell for 28 years, serving as CEO from 1986 through 2014.” (Op. at 41). In fact, the Complaint alleges that Rankin was CFO and Treasurer during this period, reporting directly to the Kruses. (A0016-A0018, A0028-A0029).

February 2016 in favor of [REDACTED], reasoning that the allegations in paragraph 115 of the Complaint regarding the vote provide “full comfort that Rankin is independent of Paul Kruse and his family” for purposes of considering a demand to bring Count I. (Op. at 42, citing Complaint ¶115 (A0058-A0060)). In doing so, the Court impermissibly failed to “consider all the particularized facts pled ... about the relationships between the director and the interested party in their totality and not in insolation from each other, and draw all reasonable inferences from the totality of those facts in favor of plaintiffs.” *Sanchez*, 124 A.3d at 1019.

As the Court of Chancery concluded with respect to analogous allegations regarding Directors Barnhill and Dickson,⁹ Rankin’s career-long employment under the Kruse family and continuation as a Director after his retirement creates a reasonable doubt regarding Rankin’s impartiality to consider a demand to sue Paul Kruse and his cousin, Bridges, for personal liability, had a demand been made. (A0139-A0140). *See In re Freeport-McMoran Sulpher S’holder Litig.*, 2005 Del. Ch. LEXIS 96, *12 (June 30, 2015) (“Latiolais had worked for the Common Directors for almost twenty years and had become a wealthy individual in their employ. To argue that Latiolais was independent of the Common Directors

⁹ The Court of Chancery concluded that the Complaint satisfied the demand futility standard for Barnhill and Dickson. (Op. at 40 n.167, citing *Freeport*, 2005 Del. Ch. LEXIS 96, at *12).

because he formally severed ties with some Freeport entities does not take into account the nature and extent of his overwhelming, career-long involvement with Freeport entities...”).

Moreover, the allegations regarding the donation to name a building in honor of Rankin are not “conclusory” or lacking support for the “materiality of the gesture.” (Op. at 42). The donation by “Ed Kruse and Friends,” which Ed F. Kruse joined with Rankin to present, specifically for the purpose of the new college building in Brenham named in Rankin’s honor, is the kind of “gesture” a career employee would find material from his employer.

The allegations in paragraph 115 of the Complaint cited by the Court of Chancery do not support rejection of these allegations for purposes of whether the Complaint supports a pleading stage reasonable doubt regarding Rankin’s impartiality to consider a demand to sue Paul Kruse and Bridge for potentially enormous personal liability. The vote was on a governance reform proposal, which did not carry and in any event, did not expose Paul Kruse to any personal economic risk or liability. And the vote did not implicate Bridges, at all. Nor would have the vote, even if it had carried, ousted Paul Kruse from the Company or diminished the status of his position. Contrary to the Court of Chancery’s statement, Paul Kruse did not “threaten[] to resign.” (Op. at 42). [REDACTED]

[REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED] (A0016-A0017).

In considering the totality of the alleged facts and the reasonable inferences in Plaintiff's favor on the issue of demand futility for Count I, the substance at issue on Rankin's 2016 vote must be considered regarding whether and to what extent it implicates Rankin's impartiality to consider a demand to sue Paul Kruse and Bridges for potentially enormous personal liability. For example, in *Khanna v. McMinn*, the court rejected the assertion that allegations that a director demonstrated partiality by votes in alignment with an interested director for purposes of demand futility. *Khanna v. McMinn*, 2006 Del. Ch. LEXIS 86, *75 (May 9, 2006). The Court noted that the substance of the votes must be analyzed for the particular interests at stake. *Id.* at *57. Here, the alleged facts show that Paul Kruse's interest at stake on Rankin's vote and the governance issue is vastly different in kind from Paul Kruse's interest in a decision whether to sue him and Bridges and expose them to enormous personal liability. Rankin's vote therefore does not demonstrate impartiality to consider a demand to sue, given Rankin's career-long close relationship with the Kruse family.

2. Ehlert

The Complaint alleges the Ehlert and Kruse families [REDACTED]

[REDACTED] Ehlert's uncle was a long-time friend of founder E.F. Kruse, and served as a pallbearer in E.F. Kruse's funeral. (A0064). Plaintiff submits that this longstanding close familial relationship in the context of this Company in the small Brenham community is a relationship for demand futility purposes of the kind that is likely to compromise Ehlert's impartiality to sue these immediate members of the Kruse family. *Cf. Sanchez*, 124 A.3d at 1022-1023. These facts and this relationship are easily distinguishable from allegations of merely traveling in the same social circles that have been rejected as insufficient to establish demand futility in some cases. *See e.g., Beam*, 845 A.2d at 1051-1052.

The Court of Chancery's erroneous holdings regarding Rankin and Ehlert require reversal of the Opinion on Count I. The Court assumed without deciding that Paul Kruse and Bridges face a substantial likelihood of liability on Count I. (Op. at 35).¹⁰ The Court concluded that the Complaint satisfied the test for demand

¹⁰ Paul Kruse and Bridges, as BB USA Officers, have the same fiduciary duties as Directors and are not insulated from liability under 8 *Del. C.* §102(b)(7). *Gantler v. Stephens*, 965 A.2d 695, 708-709 (Del. 2009). The Complaint alleges with particular facts that Paul Kruse and Bridges were BB USA Officers with direct responsibility for the Company's operations and compliance, and that they ignored nearly two years of evidence of a possible escalating *Listeria*

futility for Directors Howard Kruse, Jim Kruse, Bridges, MacInerney, Barnhill and Dickson. A majority of the Board requires eight votes. Therefore, Reimann and Ryan together hold only six votes, and the Opinion must be reversed on Count I.

contamination problem without even disclosing the testing results or possibility of a problem to the rest of the Directors. The fact that the Company held its operations at the BB LP level does not obviate their fiduciary duties as Officers of BB USA in the context of the particular governance and conferred responsibilities in this Company concerning in the Company's operations and their reporting to the BB USA Board. (A0291-A0297).

II. THE COURT OF CHANCERY ERRED IN HOLDING THAT THE COMPLAINT FAILS TO SATISFY THE DEMAND FUTILITY STANDARD FOR COUNT II

A. QUESTION PRESENTED

Does the Complaint satisfy the demand futility standard for Count II by alleging a conscious failure by the Board to institute and maintain any Board-level system of controls for oversight, in breach of the Directors' duties of loyalty? (A022-A028, A0032-A0041, A0048-A0061, A0066-A0069, A0122-A0136, A0143-A0154, A0224, A0229-A0238, A0247-A0262, A0270-A0271, A0285-A0301).

B. SCOPE OF REVIEW

This Court's review of the decision on a motion to dismiss under Ch. Ct. R. 23.1 is subject to *de novo* and plenary review. *Brehm*, 746 A.2d at 253. The Court must accept all well-pleaded allegations as true and draw all reasonable inferences in Plaintiffs' favor. *Beam*, 845 A.2d at 1048.

C. MERITS OF THE ARGUMENT

A breach of the duty of loyalty for Directors' failure to exercise oversight can be pleaded by factual allegations and reasonable inferences supporting a conscious failure by the Board to adopt or implement any system of controls and reporting. The BB USA Board's oversight function required the Board "to attempt in good faith to assume that a corporate information and reporting system, which

the Board concludes is adequate, exists ...” to enable the Directors to apprise themselves of compliance at the operations level. *Caremark*, 698 A.2d at 970. *Accord Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006); *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 67 n.111 (Del. 2006). Where, as here, the key operations of the Company are held at the subsidiary level, the Board’s oversight function is critical. *Grace*, 2000 Del. Ch. LEXIS 101, at *43-44 (the parent...here held all of its key operations at the subsidiary level making oversight of subsidiaries a crucial aspect of the parent board’s function.”).¹¹

[REDACTED]

[REDACTED] During this period, as discussed above, the Company was receiving increasingly frequent test results evidencing a possible

¹¹ The fact that the Company’s operations are held at the BB LP level does not obviate the Board’s duty to institute and maintain a system of controls and reporting for BB USA Board-level oversight. (A0297-A0301).

escalating contamination and unresolved sanitization problem. (A0036-A0041).

In addition, after Reimann joined the Board, [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] Further,

the allegations support a reasonable inference that the Board consciously failed to

adopt and maintain a Board-level system. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

The Court of Chancery rejected the allegations and reasonable inferences therefrom, based on allegations and documents incorporated by reference that show that a manual and testing and cleaning procedures were implemented at the operations level, and that Bridges and Paul Kruse provided regular reports regarding operations to the BB USA Board, “including reports form TCEQ and Silliker (a third-party food safety auditor).” (Op. at 47, citing April 29, 2014 BB USA Board Minutes and Complaint ¶¶96, 100, 101, 104-105 (A0049-A0053)).

The Court's holding failed to give due deference to the allegations and reasonable inferences therefrom. Plaintiff submits that the existence of testing, procedures and manuals at the operations level does not satisfy the crucial Board-level oversight function. For nearly two years leading up to the discovery, the Company had increasing frequent test results evidencing a possible escalating unresolved problem. Paul Kruse and Greg Bridges delivered monthly reports to the Board. Yet Paul Kruse and Bridges mentioned none of the problems to the Board. The two non-specific references in minutes to third party reports support no system of controls or reporting regarding test results that evidence a possible escalating unresolved contamination problem. Further, the Complaint alleges that *all three* production facilities were discovered in early 2015 to be contaminated to the extent of requiring extensive remediation, evidencing a Company-wide problem. Plaintiff submits that the Board's consciously leaving the contents and subjects of controls and reports completely up to management's discretion, is effectively no system of oversight at all. (A0250-A0253). Ten of the 11 Directors (excluding Reimann) are subject to a substantial likelihood of personal liability on Count II. The Opinion therefore must be reversed on Count II.

CONCLUSION

For the foregoing reasons, the Court of Chancery's Opinion should be reversed in its entirety.

Respectfully submitted,

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