THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE THE DOW CHEMICAL COMPANY DERIVATIVE LITIGATION, Plaintiff.	))))))	CONSOLIDATED C.A. No. 4349-CC

DEFENDANTS' MEMORANDUM IN SUPPORT OF THEIR MOTION TO DISMISS

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INTRODUCTION

Nominal defendant The Dow Chemical Company ("Dow") and defendants Andrew N. Liveris, Geoffrey E. Merszei, Arnold A. Allemang, Jacqueline K. Barton, James A. Bell, Jeff M. Fettig, Barbara Hackman Franklin, John B. Hess, Dennis H. Reilley, James M. Ringler, Ruth G. Shaw, Paul G. Stern, Michael Gambrell, William Banholzer, and David E. Kepler (collectively, the "Individual Defendants") file this memorandum in support of their motion to dismiss the complaint for failure to properly plead demand futility under Court of Chancery Rule 23.1 and failure to state a claim under Rule 12(b)(6).

INTRODUCTION AND NATURE AND STAGE OF PROCEEDINGS

In July 2008, after an intense auction, Dow entered into a strategic merger agreement with the Rohm & Haas Company ("R&H"), pursuant to which Dow agreed to acquire all of R&H's stock for $78 per share. In a press release announcing the transaction, Dow's Chairman and CEO described the R&H acquisition as a "defining step in our transformational strategy to shape the 'Dow of Tomorrow,' creating the largest specialty chemicals company in the United States with a leading global position in performance products and advanced materials." *See* Ex. A hereto.[1]

Because certainty was "fundamental" to R&H's decision to accept Dow's bid,[2] closing was not conditioned on Dow's ability to obtain financing for the approximately $15.6 billion purchase price. At the time the R&H deal was signed, Dow had a variety of potential sources of financing. In December 2007, it had signed a Memorandum of Understanding with

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1 This announcement is referred to in paragraphs 46 and 52 of the Complaint, and thus may be considered by the Court on this motion to show what was disclosed. *In re Santa Fe Pac. S'holders Litig.*, 669 A.2d 59, 69-70 (Del. 1995).

2 *See* Compl. ¶ 56. All references herein are to the *Meier* complaint, which plaintiffs have selected as the operative pleading.

the Petrochemical Industries Company of the State of Kuwait ("PIC") to enter into a joint venture agreement (the "K-Dow Joint Venture"), which was expected to generate approximately $9.5 billion in value to Dow.[3] Dow expected another $4 billion to come from investments by Berkshire Hathaway Inc. and the Kuwait Investment Authority. Ex. A. In addition, a syndicate led by Citibank, N.A had committed $13 billion of debt financing for the R&H acquisition under a one-year term agreement, providing a "bridge" and a "backstop" if the R&H transaction closed before the K-Dow Joint Venture. Ex. A; Compl. ¶68.

Over the course of the next six months, a series of unforeseeable economic events led to a dramatic change in circumstances. Hit hard by the global recession, Dow's sales plummeted 30%, leading to a net loss for the fourth quarter of $1.6 billion. *See* Compl. ¶ 11. Still, Dow worked toward closing both the K-Dow Joint Venture and the R&H transaction. *See* Compl. ¶ 13. On December 28, 2008, however, Kuwait's Supreme Petroleum Council rescinded its approval of the K-Dow Joint Venture and PIC declined to close as expected on January 2, 2009. Compl. ¶¶ 13-14. Thereafter, rating agencies cut Dow's credit rating. Faced with continuing declines in sales, frozen credit markets, and the possibility of a near-term credit default if it used the $13 billion bridge loan to finance the purchase of R&H, Dow's Board concluded that it would not be prudent to proceed with the R&H closing unless and until new financing arrangements could be made. Compl. ¶¶ 14, 84-85.

On January 26, 2009, R&H sued Dow in this Court, seeking immediate specific performance of the merger agreement. Compl. ¶ 86. The lawsuit was settled on the eve of trial, and the merger closed on April 1, 2009, on substantially altered financial terms.

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[3] This amount originally consisted of approximately $9 billion in pre-tax cash proceeds and an additional $500 million through the joint venture's proposed assumption of existing debt.

Shortly after the R&H lawsuit was filed, two individual shareholders filed the two virtually identical derivative actions that have been consolidated in this action, challenging the wisdom of the Board's July 2008 decision to enter into the R&H transaction. Plaintiffs do not allege that the acquisition of R&H was ill-conceived. On the contrary, they grudgingly admit that the idea of expanding Dow's higher-margin, less-cyclical specialty chemical business through the R&H deal while at the same time "monetizing" its basic chemicals business through ventures like K-Dow "may have been sound." Compl. ¶ 4. Plaintiffs also admit that R&H would not have accepted Dow's bid absent the certainty that an unconditional agreement provided. Compl. ¶ 56. Nevertheless, plaintiffs contend that the Dow Board acted imprudently by agreeing to purchase R&H without any financing condition. *Id.* ¶¶ 4-14. In a classic example of 20-20 hindsight, plaintiffs allege that the Dow Board should have anticipated the cascade of events that led to Dow's refusal to close the R&H deal in January 2009 and should have declined to take the risk of entering into an unconditional deal to acquire R&H. Compl. ¶ 10. For the reasons outlined below, these allegations are woefully inadequate, either to plead demand futility under Rule 23.1 or to state a claim against the Individual Defendants under Rule 12(b)(6).

Because plaintiffs' primary challenge is to a Board decision, the two-fold test set forth in *Aronson v. Lewis*, 473 A.2d 805, 814 (Del.1984), applies in evaluating their demand futility allegations. Under *Aronson*, plaintiffs have the burden of providing "particularized factual allegations that raise a reasonable doubt that '(1) the directors are disinterested and independent [or] (2) the challenged transaction was otherwise the product of a valid exercise of business judgment.'" *In re Citigroup Inc. Shareholder Derivative Litig.*, 964 A.2d 106, 120 (Del. Ch. 2009). Plaintiffs have not come close to showing demand futility under either prong.

First, plaintiffs do not allege that *any*, let alone a majority, of Dow's directors had any conflicting interests that would have prevented them from acting in Dow's best interests in evaluating the R&H transaction. Thus, they do not meet their burden under the first *Aronson* prong.

Second, plaintiffs do not offer any other reason to doubt that the decision to approve the R&H merger agreement was the product of a valid business judgment. Significantly, plaintiffs do not allege any facts suggesting that there were inadequacies in the process the Board followed in considering the proposed transaction. Instead, plaintiffs attack the *substance* of the Board's decision, claiming that entering into the agreement without a financing condition was so obviously "wanton and grossly reckless" that it necessarily raises a reasonable doubt as to whether the directors were acting in good faith. This argument fails as a matter of law. As this Court recently explained in *In re Citigroup Inc. Shareholder Derivative Litig.*, 964 A.2d at 126-26 (Del. Ch. Feb. 24, 2009), plaintiffs cannot evade the business judgment rule by asking the Court, with the benefit of 20-20 hindsight, to second-guess the wisdom of the board's risk-benefit analysis. *Id.* at 126. The protections of the business judgment rule are "designed to allow corporate managers and directors to pursue risky transactions without the specter of being held personally liable if those decisions turn out poorly." *Id*. at 125. "To impose liability on directors for making a 'wrong' business decision would cripple their ability to earn returns for investors by taking business risks. Indeed, this kind of judicial second guessing is what the business judgment rule was designed to prevent. . . ." *Id*. at *126.

The remainder of plaintiffs' demand futility allegations also fail to satisfy the requirements of Rule 23.1. Plaintiffs seek to hold the directors liable under a *Caremark* theory for a variety of alleged monitoring failures. But plaintiffs have not pleaded facts giving rise to a reasonable inference that *any* directors — let alone a majority of the Board — consciously disregarded their fiduciary duties and thus face a "substantial likelihood" of liability. And even if the Court were to assume, for purposes of argument, that the three directors on the Dow Board who are not "independent" under Dow's definition of that term were somehow disqualified from responding to a shareholder demand, plaintiffs' attempts to show that Dow's Chairman and CEO dominated and controlled some or all of the nine independent directors fail as a matter of law under the standard articulated in *Beam v. Stewart*, 845 A.2d 1040, 1050-51 (Del. 2004).

Finally, the same pleading inadequacies that require dismissal under Rule 23.1 would also require dismissal of plaintiffs' claims against the Individual Defendants under Rule 12(b)(6).

STATEMENT OF FACTS[4]

I. THE R&H MERGER AGREEMENT.

For more than a century, Dow has been "one of the giants of the American chemical industry." Compl. ¶ 1. "The Company historically has been extremely profitable." Compl. ¶ 2. Plaintiffs allege, however, that competition eroded profit margins on the commodities side of Dow's business, leading the Company to embark on a strategy of shifting its focus to what plaintiffs describe as the more profitable and less cyclical specialty chemicals business. *Id.* ¶¶ 43-44. Plaintiffs allege that one step in this process was to "monetize" Dow's interest in the commodities side of its business, by selling off 50% interests in various commodity chemical assets to third parties, who would then partner with Dow in joint ventures.

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[4] As they must under Rules 23.1 and 12(b)(6), defendants assume the truth of plaintiffs' allegations for purposes of this motion. Defendants believe that many of these "facts" are not true, and reserve the right to contest them should any part of the complaint survive the present motion to dismiss.

Id. ¶ 3. The proceeds of the joint venture deals would then be used to invest in expanding the higher margin and less cyclical specialty chemical side of the business. *Id.* ¶¶ 3, 44. As noted above, plaintiffs do not criticize the soundness of this strategy. *Id.* ¶¶ 4, 45. Instead, they quarrel with the way the strategy was implemented.

In December 2007, Dow announced that it had signed a memorandum of understanding with PIC to form the K-Dow Joint Venture. Compl. ¶ 47. Under that MOU, which was subject to the execution of a definitive agreement, customary conditions, and regulatory approvals, PIC would purchase a 50% interest in five global Dow businesses for approximately $9.5 billion of total value and both parties would contribute their shares of those businesses to K-Dow in return for a 50% interest in the new company. *Id.* ¶ 48. Dow stated that it expected the K-Dow transaction to close in late 2008. *Id.* ¶ 49.

Dow continued to be very profitable in the first half of 2008. Its reported $31.2 billion in revenues for the first two quarters of 2008 represented a 21% increase over the same period in 2007. See Ex. B hereto.[5] Net income for the period was down to $1.7 billion from $2 billion for the same period in 2007. *Id.* But in light of increasing oil prices, which were close to all-time highs of $150 a barrel, Dow's Chairman and CEO, Andrew Liveris, was quoted as saying that Dow had done "remarkably" well in the first half of the year. *Id.* ¶ 54.

In July 2008, Dow announced the acquisition by merger of R&H, a specialty chemicals company. Compl. ¶ 52. The agreement followed an intense bidding contest. *Id.* ¶

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[5] This press release announcing Dow's second quarter 2008 results is quoted in part in ¶54 of the Complaint, and thereby incorporated by reference. *See* n.2, *supra.*

53.[6] Ultimately, Dow prevailed, agreeing to pay $78 per share in an all-cash deal. According to the complaint, a key element in R&H's willingness to sign an agreement with Dow was the fact that there was no financing condition in the agreement. R&H wanted certainty, and the absence of a financing condition was "fundamental to its decision to accept Dow's bid." Compl. ¶ 56.[7]

Dow's bid letter to R&H stated that Dow intended to finance the merger with "our available cash balances and a fully committed financing facility." Compl. ¶ 56. As noted above, Dow had secured a $4 billion commitment from Berkshire Hathaway Inc. and the Kuwait Investment Authority to purchase preferred stock when the R&H transaction closed and expected the K-Dow Joint Venture to generate another $9 billion in cash proceeds. Ex. A. As a "bridge" if the R&H merger closed before the K-Dow Joint Venture (Compl. ¶ 68) and as a "backstop" (*id.* ¶ 68), Dow arranged a $13 billion term loan facility through a syndicate led by Citibank. Dow's officers emphasized in public statements made shortly after the R&H deal was announced that Dow's ability to close that deal was not contingent on closing K-Dow. Compl. ¶ 57.

The R&H merger was unanimously approved by Dow's Board. Compl. ¶ 52. It was subject to approval by R&H's shareholders and also subject to customary conditions regarding regulatory approvals. The parties predicted that it would take about six months to obtain the necessary approvals and that the transaction would close in early 2009. *Id.* ¶ 73.

The Court can take judicial notice of the fact that over the course of the next six months the U.S. and world economies experienced conditions unprecedented since the Great

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6 Plaintiffs allege that the bidding contest "pitted Dow against its much larger rival in the chemical industry, DuPont." Compl. ¶53. In fact, Dow's rival was BASF, not DuPont. But the fact that there was a spirited bidding contest for R&H is correct and undisputed.

7 In its proxy statement to R&H shareholders, R&H explained that, even though Dow had made the higher initial proposal of the two bidders, the R&H board decided to pursue a "competitive process between Dow and Company A with a goal of achieving the best possible price with the greatest certainty of closing." Proxy Statement at 20.

Depression. In the course of a single week in mid-September, Lehman Brothers declared bankruptcy, Merrill Lynch avoided bankruptcy by agreeing to be absorbed by Bank of America, the government launched its first effort to bail out AIG, and the nation's oldest money market fund (the Reserve Primary Fund) announced that it had "broken the buck," triggering a run on money market funds. Oil prices crashed, the credit markets froze, and stock prices plummeted. While there were certain "storm clouds" in the summer of 2008 (Compl. ¶ 52), no one expected nor predicted the depth or suddenness of the financial meltdown that ensued. Compl. ¶¶11, 51.

In light of these changed conditions, Dow agreed to reduce the price PIC would pay in the K-Dow deal, although Dow still expected to realize $9 billion from the closing.[8] *Id.* ¶ 62. On November 24, 2008, the Supreme Petroleum Council of Kuwait approved the proposed joint venture, and a Joint Venture Formation Agreement was signed on November 28, 2008. The K-Dow closing was set for January 2, 2009. *Id.* ¶ 74.

Throughout the fall, economic conditions continued to deteriorate. In response to plummeting revenues, Dow announced cost-cutting measures and lay-offs. Nevertheless, Dow continued to plan for the R&H merger. *See,* Compl. ¶¶ 60-63. If the closing of the K-Dow transaction had gone through, Dow would have had no difficulty, despite the dramatic downturn it was experiencing, financing the merger. But on December 28, 2008, PIC informed Dow that the Supreme Petroleum Council had rescinded its approval of the deal and ultimately PIC refused (wrongfully) to close the joint venture. *Id.* ¶ 76.

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8 As renegotiated, the purchase price was to consist of $7.5 billion in pre-tax cash proceeds and $1.5 billion in the form of a dividend to be paid by the joint venture.

As noted above, Dow reported a $1.6 billion net loss for the fourth quarter of 2008. Rating agencies cut its debt ratings. Compl. ¶ 103. In light of that downgrade, the extremely difficult nature of the credit markets, and its own uncertain prospects for the future, Dow's Board concluded that it would not be prudent for the Company to close the R&H transaction in January 2009 by drawing down on the term loan it had negotiated with the Citibank syndicate. *Id.* ¶¶ 84-85. As Dow explained in its Answer to R&H's complaint, proceeding with the merger in January could have resulted in further downgrades and the loss of its investment grade debt rating, triggering an almost immediate default under the term loan and cross-defaults under other credit agreements. Under those circumstances, Dow's Board concluded that it needed more time to work out a new plan to finance the acquisition. *Id.* ¶ 85. Ultimately, a new plan was in fact negotiated and, as this Court is aware, the deal was closed on April 1, 2009.

II. PLAINTIFFS' CLAIMS.

The *Meier* complaint, which plaintiffs have designated as the operative pleading, alleges three claims. Count I is brought against six of the Individual Defendants (all of whom are officers or non-independent directors)[9] and seeks damages for alleged insider selling. The only specific "inside" information plaintiffs allege relates to Dow's ability to finance the R&H merger. Yet, remarkably, virtually all of the stock sales plaintiffs challenge were made in April 2008, months *before* Dow even approached R&H about a potential acquisition. Plaintiffs offer

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[9] Two of the Individual Defendants named in Count I (Mr. Liveris and Mr. Merszei) are management directors. The third director named in Count I (Mr. Allemang) does not qualify as "independent" under the standards Dow has adopted because of his former service as a Dow officer. *See* Complt. ¶125(c).

no explanation as to how the Individual Defendants who sold in April could possibly have been selling on the basis of this alleged "inside" information.[10]

Count II is a claim for breach of fiduciary duty against all of the Individual Defendants. The Court can take judicial notice of the fact that Dow's charter contains an exculpatory provision, as authorized by Del. Corp. Code. § 102(b)(7), which requires proof of disloyalty or bad faith to hold the directors liable for damages.[11] Plaintiffs ramp up their rhetoric in an attempt to show that they can meet this standard, accusing the Dow directors of "knowing abdication of duty" in approving the R&H Agreement without any financing contingency. Plaintiffs contend that committing Dow to a "transaction that it was unable to finance" was "in and of itself, a flagrant breach of the Direct Defendants' fiduciary duties, and could not have been the product of an informed business judgment." Compl. ¶ 97.

In addition to challenging the R&H transaction, Count II alleges a number of other breach of fiduciary duty claims:

- Citing speculation in newspaper reports from politicians in Kuwait, plaintiffs allege that Dow may have engaged in bribery in connection with the K-Dow deal. Based on that speculation, plaintiffs seek to hold the defendants liable for supposedly allowing the Company to "conduct itself with Kuwait government and industry officials in a manner which foreseeably put the K-Dow venture at risk." Compl. ¶ 144(c).
- Plaintiffs allege that the Individual Defendants caused or allowed the Company to make supposedly misleading statements, by stating before December 2008 that both the R&H

10 Plaintiffs allege only two sales by two Individual Defendants after the merger agreement was signed, one in August 2008 and the other in September, before the credit markets crashed.

11 *See, e.g., Malpiede v. Townson*, 780 A.2d 1075, 1090-92 (Del. 2001).

merger and the K-Dow deal were on track and that financing for the R&H merger did not depend on the closing of the K-Dow deal. Compl. ¶¶ 61-63; 144(e).

- Plaintiffs allege that the directors failed to prevent the payment of "excessive and wasteful" compensation to officers and directors, although they do not say whose compensation was supposedly excessive, let alone try to explain how they can meet the stringent test for waste. Compl. ¶¶ 134, 144(g)
- Finally, plaintiffs accuse all of the Individual Defendants of "allowing" insider trading by the six individuals named as defendants in Count I. Compl. ¶ 144(h).

Count III of the Complaint is a claim for contribution and indemnification against all of the Individual Defendants with respect to any claim that has been brought or might be brought in the future against Dow arising out of the R&H agreement or the K-Dow agreement. It is unclear whether this was intended as an attempt to obtain contribution or indemnity with respect to the claims asserted by R&H. In any event, any such claims are moot, since the R&H lawsuit has been dismissed, and no other claims are pending against Dow that could give rise to claims for contribution or indemnity.

Plaintiffs acknowledge that they did not make a demand on the Board before filing their lawsuits, but argue that demand was excused. Significantly, plaintiffs do *not* allege that any of the directors, whether independent or not, had any personal interest in entering into a transaction with R&H. Instead, plaintiffs contend that the Board's decision to enter into the R&H transaction was so clearly reckless that it was "not, and could not have been, the product of the Board's good faith, informed business judgment." Compl. ¶ 123. The complaint is devoid of any specific allegations concerning the process the Board followed in deciding to approve the R&H merger agreement. Instead, plaintiffs are apparently relying on a theory of *res ipsa* *loquitur* – that the decision itself was supposedly so egregious that it is indicative, on its face, of a failure to make a valid business judgment.

As to their other allegations of claimed breaches of fiduciary duty, plaintiffs allege that the Board is subject to many conflicting interests, "governance defects" and "other features" that supposedly would have prevented a majority of the directors from properly considering a demand. Plaintiffs implicitly acknowledge that nine members of the 12-person Dow Board meet Dow's criteria for being independent of management.[12] But they argue that at least three of the independent outside directors should be deemed to have been dominated and controlled by Dow's Chairman and CEO, Mr. Liveris. In support of that claim, plaintiffs point to the fact that a number of directors were appointed or elected after Mr. Liveris became the CEO; plaintiffs make the conclusory assertion that they were "hand picked or approved by Liveris, and are beholden to him for their positions." Compl. ¶125(d). Plaintiffs offer no facts to support these assertions, however, let alone any facts to suggest that Mr. Liveris has or had any ability to remove any director from office. Further, under Article 5.3 of Dow's Certification of Incorporation, since 2007 all of Dow's directors have served only one-year terms and are voted on annually by Dow's shareholders, meaning that all twelve directors were elected to their positions in May 2008 by the stockholders of Dow – not "appointed" by or at the behest of Mr. Liveris.

Plaintiffs also allege a variety of business connections (discussed in greater detail below) between and among certain directors, including service on the same "prestigious" business or professional councils or boards. Plaintiffs do not explain how or why these

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12 Plaintiffs allege that three members of the Board, two of whom are officers and one of whom was formerly an officer, are not independent under Dow's own stated criteria. Compl. ¶ 125(c).

connections would lead any of the independent directors to abdicate their fiduciary obligations in order to protect Mr. Liveris or anyone else. Indeed, as demonstrated below, plaintiffs fail to allege any facts suggesting that Mr. Liveris himself would have been unable to properly respond to a demand.

ARGUMENT

I. PLAINTIFFS BEAR A HEAVY BURDEN OF ALLEGING PARTICULARIZED FACTS SHOWING THAT DEMAND WOULD BE FUTILE.

Whether a corporation should bring a lawsuit is a business decision that must ordinarily be made by the directors. The demand requirement "is a recognition of the fundamental precept that directors manage the business and affairs of corporations," including its litigation decisions. *Aronson v. Lewis*, 473 A.2d 805, 812 (Del.1984). Demand is deemed futile and therefore excused only if a majority of the directors have such a personal stake in the matter at issue or the proposed litigation that they would be unable to make a proper business judgment in response to a demand. *Id.* at 814.

Under Chancery Court Rule 23.1, allegations of demand futility "must comply with stringent requirements of factual particularity that differ substantially from the permissive notice pleading[]" requirements of Rule 8. *Brehm v. Eisner*, 746 A.2d 244, 254 (Del. 2000). This standard is designed to ensure that a derivative action is not allowed to proceed unless there is a reasonable factual basis for questioning the directors' ability to make an independent judgment as to whether litigation is in the best interests of the corporation. *See id*. at 266 (the particularity requirement is designed to prevent a stockholder from "caus[ing] the corporation to expend money and resources in discovery and trial in the stockholder's quixotic pursuit of a purported corporate claim based solely on conclusions, opinions or speculation").

As this Court recently explained in *Citigroup*, the two-pronged *Aronson* test applies to board decisions. To the extent plaintiffs challenge the board's failure to act, rather than a specific decision, the test articulated in *Rales v. Blasband*, 634 A.2d 927, 934 (Del. 1993), applies. Under *Rales,* the only issue is whether "the board that would be addressing the demand can impartially consider its merits without being influenced by improper considerations." *Id*. at 934. In order to meet their burden of pleading demand futility under *Rales,* plaintiffs must plead "particularized factual allegations" that "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 judgment in responding to a demand." *Id*.

It is clear that the *Aronson* standard applies to plaintiffs' claims arising out of the Board's approval of the R&H merger agreement. The remainder of plaintiffs' claims appear to based on a failure to supervise, rather than on affirmative Board action, and therefore should be governed by the standard set forth in *Rales*. Regardless of which standard applies, however, plaintiffs have failed to meet their burden of pleading demand futility.

II. PLAINTIFFS HAVE NOT PROPERLY PLEADED DEMAND FUTILITY WITH RESPECT TO THEIR CLAIM THAT THE DIRECTORS ACTED IN BAD FAITH IN APPROVING THE R&H TRANSACTION.

A. Plaintiffs Have Failed To Establish Demand Futility Under The First Prong Of *Aronson*.

Aronson's first prong requires plaintiffs to plead particularized facts that raise a reasonable doubt that a majority of the directors who approved the transaction in question were disinterested and independent. To meet that burden here, plaintiffs would have to plead particularized facts showing that at least six of the twelve Dow directors either (i) had personal interests that were not aligned with Dow's interests in the R&H transaction or (ii) were not independent, but rather were dominated or controlled by an interested director or directors. *See*

Brehm v. Eisner, 746 A.2d at 257-58. Plaintiffs have not even attempted to meet that pleading burden.

The complaint is devoid of any allegation that any Dow director, whether independent or not, suffered from any conflict of interest when the Board voted to approve the R&H transaction. There is no claim, for example, that any member of the Board owned R&H stock or otherwise stood to gain personally from the decision to approve the merger agreement. Thus, there is no reason to believe that the Dow Board approached the proposed transaction with any goal in mind other than to achieve the best possible result for Dow and its shareholders.

Plaintiffs' failure to identify any director who was interested in the R&H transaction precludes them from relying on the first prong of *Aronson.* That is true even though plaintiffs have detailed various associations certain directors had with Mr. Liveris in an attempt to show that he dominated and controlled a majority of the Board. As the Supreme Court explained in *Brehm*, if the supposedly dominant director was himself disinterested in the transaction at issue (as Mr. Liveris plainly was here), there is no need for the Court to inquire whether the other directors were capable of independently making their own business judgment. 746 A.2d at 258.

B. Plaintiffs Have Failed To Plead Demand Futility Under *Aronson's* Second Prong.

Plaintiffs contend that even if the directors were disinterested and independent, the Board's decision to approve the R&H transaction nevertheless "[was] not and could not have been, the product of the Board's good faith, informed business judgment." Compl. ¶ 124. In evaluating this claim, the Court must begin with the presumption that "in making a business decision the directors . . . acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation." *Aronson*, 473 A.2d at 812. To overcome that presumption, plaintiffs must be able to plead particularized facts showing that the directors either failed to properly inform themselves or failed to act in good faith. It is clear, however, that plaintiffs cannot establish demand futility under *Aronson's* second prong by second-guessing the substantive merits of the directors' decision. As the Delaware Supreme Court explained in *Brehm*:

> As for the plaintiffs' contention that the directors failed to exercise "substantive due care," we should note that such a concept is foreign to the business judgment rule. Courts do not measure, weigh or quantify directors' judgments. We do not even decide if they are reasonable in this context. Due care in the decisionmaking context is *process* due care only. Irrationality is the outer limit of the business judgment rule. Irrationality may be the functional equivalent of the waste test or it may tend to show that the decision is not made in good faith, which is a key ingredient of the business judgment rule.

746 A.2d at 264 (emphasis in original; footnotes omitted).

Under *Brehm*, plaintiffs relying on the second *Aronson* prong can plead demand futility by alleging particularized facts showing that the *process* the directors employed was fundamentally flawed because the directors were grossly negligent in failing to consider all material information reasonably available to them. 746 A.2d at 259. Plaintiffs can also establish demand futility if they can plead facts creating a reason to believe that the directors were guilty of waste – that is, of "irrationally squander[ing] or giv[ing] away corporate assets" – or irrationality. *Id*. 263-64. In this context, "irrationality" means that the decision in question cannot be "attributed to any rational business purpose." *Id*. at 264 n. 65 (quoting *Sinclair Oil Corp. v. Levien*, Del. Supr., 280 A.2d 717, 720 (1980)). What plaintiffs may *not* do, however, is to predicate their demand futility allegations on a claim that the Board's decision was so plainly wrong or unreasonable that it could not be deemed a proper business judgment.

In this case, plaintiffs try to do precisely what *Brehm* forbids. They do not allege any lapses in "process due care." Indeed, plaintiffs say nothing at all about the process the Board employed in deciding to approve the R&H transaction. Nor do they allege any facts that would suggest that the transaction constituted waste or was otherwise irrational. As plaintiffs acknowledge, acquiring R&H was part of a sound business strategy. And as plaintiffs also acknowledge, R&H was not willing to be acquired absent the kind of certainty that an agreement without a financing condition provided. *See*, p. 7, *supra*. Thus, there was clearly a rational business purpose both for the merger agreement and for the particular provision of the agreement (regarding financing) that plaintiffs now find objectionable. Plaintiffs' characterization of that provision as "reckless" is precisely the kind of attack on the substantive merits of the Board's decision that the business judgment rule precludes.

This Court's recent decision in *Citigroup* is dispositive on this issue. As the Court explained, the business judgment rule "prevents judicial second guessing of the decision if the directors employed a rational process and considered all material information reasonably available"[13] – as they must be presumed to have done in this case. *Aronson*, 473 A.2d at 812. In support of this conclusion, this Court quoted former Chancellor Allen's opinion in *Caremark*:

> [C]ompliance with a director's duty of care can never appropriately be judicially determined by reference to *the content of the board decision* that leads to a corporate loss, apart from consideration of the good faith *or* rationality of the process employed. That is, whether a judge or jury considering the matter after the fact, believes a decision substantively wrong, or degree of wrong extending through "stupid" to "egregious" or "irrational", provides no ground for director liability, so long as the court determines that the process employed was either rational or employed in a *good faith* effort to advance corporate interests. To employ a different rule—one those permitted an 'objective'

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[13] 964 A.2d at 122.

> evaluation of the decision— would expose directors to substantive second-guessing by ill-equipped judges or juries, which would, in the long-run, be injurious to investor interests.

964 A.2d at 122, *quoting Caremark*, 698 A.2d at 967-68 (emphasis in original). Under this reasoning, the Citigroup directors could not be held personally liable for failing to "fully recognize the risk posed by subprime securities." Nor could the fact that their business decisions "in hindsight, turned out poorly for the Company" provide a basis for concluding that the protections of the business judgment rule did not apply.

"The essence of the business judgment of managers and directors is deciding how the company will evaluate the trade-off between risk and return. Businesses . . . make returns by taking on risk; a company or investor that is willing to take on more risk can earn a higher return." In *Citigroup*, this Court recognized that "hindsight bias" would make it impossible for a judge or jury to "properly evaluate whether corporate decision-makers made a 'right' or 'wrong' decision" in taking certain risks in order to achieve a particular goal. Moreover, allowing such second-guessing would be directly contrary to the fundamental purpose of the business judgment rule, which is to "allow corporate managers and directors to pursue risky transactions without the specter of being held personally liable if those decisions turn out poorly." 964 A.2d at 125.

These principles require dismissal of plaintiffs' claim that the Dow directors violated their fiduciary duties by approving the R&H transaction. The Dow Board made a business judgment that it should take the risk of entering into a merger agreement that was not conditioned on acceptable financing being available at closing. Plaintiffs' own complaint acknowledges that the reward the Dow Board was seeking – taking a "defining step" in Dow's "transformational strategy" by acquiring R&H – would not have been possible without taking that risk. Weighing the risk of an unconditional agreement versus the reward if all goes as planned is precisely the kind of good faith business judgment this Court had in mind in *Citicorp*.

Plaintiffs' attempt to second-guess the Dow Board's business judgment is particularly egregious because it is plainly based on hindsight. At the time the directors unanimously approved the R&H transaction, there was no reason for them to believe that Dow would have difficulty closing the R&H merger. Dow was on a pace to have over $60 billion in revenues in 2008 and close to $4 billion in net income; despite a tightening credit market, it had also lined up $4 billion in financing through the sale of preferred stock and a $13 billion term loan to provide bridge financing for the R&H acquisition. Dow was also moving toward the completion of the K-Dow Joint Venture, which was expected to produce $9 billion in cash. Under those circumstances, the Board's decision that it was worth taking the risk of agreeing to proceed without a financing condition was well within the protections of the business judgment rule. The fact that the directors failed to anticipate a global economic meltdown that was both unforeseen and unforeseeable does not provide any basis for impugning their judgment, let alone their good faith.

A recent Delaware Supreme Court decision provides further support for this analysis. In order to show that a disinterested and properly informed Board acted outside the bounds of the business judgment rule, plaintiffs would have to prove that the directors acted in bad faith. In *Lyondell Chemical Co. v. Ryan*, the Supreme Court clarified the concept of bad faith, which requires proof of an intentional dereliction of duty. The Court noted that "[i]n the transactional context, [an] extreme set of facts [is] required to sustain a disloyalty claim premised on the notion that disinterested directors were intentionally disregarding their duties." *Lyondell Chemical Co. v. Ryan*, 2009 WL 1024764, at *7 (Del.) (*quoting In re Lear Corp. S'holder Litig.*, 2008 WL 4053221 at *11 (Del. Ch.)). Thus, the right question to ask in a case where the directors had *Revlon* duties was not "whether disinterested, independent directors did everything that they (arguably) should have done to obtain the best sale price"; instead, "the inquiry should have been whether those directors utterly failed to *attempt* to obtain the best sale price." *Id*. (emphasis added).

So too in the present case, to raise a reasonable doubt about the disinterested directors' good faith in approving the R&H transaction, plaintiffs would have to allege particularized facts showing that the directors did not even *attempt* to make a decision in the best interests of Dow. Plaintiffs have not met and cannot meet that burden. Accordingly, plaintiffs' claims arising out of the execution of the R&H merger agreement must be dismissed both for failure to properly plead demand futility and failure to state a claim under Rule 12(b)(6).

III. PLAINTIFFS HAVE ALSO FAILED TO MEET THEIR BURDEN OF PLEADING DEMAND FUTILITY UNDER *RALES*.

In order to properly plead demand futility under *Rales*, plaintiffs must allege specific facts showing that a majority of the Dow directors at the time the lawsuit was brought were either themselves subject to a "substantial likelihood" of liability or were dominated and controlled by directors who fell into that category and therefore could not be trusted to make a disinterested business decision in response to a shareholder demand. In *Citigroup*, this Court explained that in order to establish oversight liability "a plaintiff must show that the directors *knew* they were not discharging their fiduciary obligations or that the directors demonstrated a *conscious* disregard for their responsibilities as such by failing to act in the face of a known duty to act." 964 A.2d at 123. This test "is rooted in concepts of bad faith; indeed, a showing of bad faith is a *necessary condition* to oversight liability." *Id*. at 122. Furthermore, because Dow has adopted a § 102(b)(7) provision in its charter, plaintiffs must be able to plead particularized facts showing bad faith in order to establish a substantial likelihood of liability on the part of the directors, no matter what plaintiffs' theory might be. *See Stone v. Ritter*, 911 A.2d 362, 369-70

(Del. 2006). As demonstrated below, plaintiffs have failed to meet that burden with respect to any of the remaining claims asserted in their complaint.

A. Plaintiffs Have Failed To Plead Demand Futility With Respect To Their Insider Trading Claims.

Plaintiffs allege that six of the Individual Defendants — three officers and three directors — engaged in insider trading. There is no claim that any of the nine independent directors on the Dow Board sold stock at any relevant point in time. Nevertheless, plaintiffs seek to hold all of the directors liable on the theory that they improperly "allowed" the alleged insider sales to occur.

For purposes of the demand futility analysis, the allegations against the three officers who were not directors are irrelevant, as financial interests of non-Board members cannot excuse a demand on the Board. *See Guttman v. Huang*, Del. Ch., 823 A.2d 492, 503 n.22 (2003). Plaintiffs must alleged particularized facts giving rise to an inference that the three directors they accuse of insider trading were in fact knowingly trading on material non-public information. *Id*. at 505 (plaintiffs must allege "particularized facts that support a rational inference that these . . . directors possessed information about [Dow] . . . that was materially different than existed in the marketplace at the time they traded" and that "they consciously acted to exploit such superior knowledge"). Even that would not be enough to establish demand futility, however, because even if the three directors who sold stock were deemed "interested," there would still be nine disinterested directors. Thus, to establish demand futility with respect to their insider trading claims, plaintiffs would have to allege particularized facts giving rise to a rational inference that at least three of the independent outside directors had either (i) "consciously disregarded" their obligation to prevent directors and officers from engaging in insider trading or (ii) were so dominated or controlled by those who had engaged in insider trading that they could not have made an independent judgment in response to a demand. *See Guttman v. Huang*, 823 A.2d at 506*; In re InfoUSA, Inc.*, 2007 WL 3325921, at *13 (Del. Ch.).

Plaintiffs' allegations fail each step of the way. First, plaintiffs have not alleged sufficient facts to support an insider trading claim against *any* of the directors. As Vice Chancellor Strine explained in *Guttman*, a director is not deemed "interested" "whenever a derivative plaintiff cursorily alleges that he made sales of company stock in the market at a time when he possessed material, non-public information." 823 A.2d at 502. Rather, to show that a director was "interested" because of selling activity, plaintiffs must allege specific information that gives rise to a reasonable inference that the insiders sold stock "on the basis of and because of" adverse material non-public information. *Id*. at 505.

In this case, plaintiffs do not identify any material non-public information that the three directors who sold stock had in their possession in mid-April 2008, when Messrs. Liveris and Allemang made all of their alleged insider sales and Mr. Merszei made the larger of his two sales. Plaintiffs allege that these directors knew about the Company's progress toward closing K-Dow and funding the R&H merger and knew that Dow's ability to close the R&H transaction was dependent on K-Dow closing. Compl. ¶113. These allegations are nonsensical, however, as applied to sales in April 2008, since at that point in time Dow had not yet even *approached* R&H about the possibility of an acquisition. Thus, all of the April 2008 sales must be disregarded.

That leaves only one sale by one director that *possibly could have been* based on the kind of inside information plaintiffs allege – Mr. Merszei's August 29, 2008 sale of 12,241 shares for total proceeds of $421,212. Compl. ¶109. Plaintiffs allege that Mr. Merszei, Dow's CFO, was monitoring the financing for the R&H merger. But they do not allege any facts to suggest that in August 2008 there was any reason for him to believe that the K-Dow transaction was not "on-track." At that point in time, the worldwide credit crisis had not yet begun and the price reduction and eventual termination of the K-Dow Joint Venture at the end of 2008 was still months away. Without a crystal ball, Mr. Merszei could not have known what would happen in the future. Thus, plaintiffs have failed to allege sufficient facts to show that *any* of the directors face a substantial likelihood of liability with respect to their insider trading claims.

But even if we assume, for purposes of argument, that plaintiffs have alleged enough to show that Mr. Merszei should be deemed "interested" with respect to their insider trading allegations, that allegation alone would not be nearly enough to support their demand futility allegations. Plaintiffs would still have to show that at least five other directors were either dominated and controlled by Mr. Merszei or faced a "substantial likelihood" of liability for failing to prevent his allegedly improper activity. Plaintiffs do not allege that Mr. Merszei dominated or controlled anyone. And although they claim that the outside directors are liable for failing to prevent the alleged insider trading, plaintiffs offer no facts to support that conclusory assertion. Plaintiffs do not allege, for example, that the directors failed to put in place appropriate systems for preventing insider trading. Nor do they allege any facts from which the Court could infer that the directors "consciously disregarded" obvious evidence that Dow insiders were engaged in improper trading activity. Thus, Count I of the complaint would have to be dismissed for failure to plead demand futility even if the Court were to conclude that plaintiffs had pleaded enough to raise a reasonable doubt with respect to Mr. Merszei's trading activity in August 2008.

Indeed, the same result would apply even if the Court were to credit, for purposes of argument, plaintiffs' nonsensical allegations of insider trading against Mr. Liveris as well. Plaintiffs claim that Mr. Liveris dominates and controls enough of the outside directors on the

Board to ensure that there is no independent majority. Compl. ¶ 125(a). But their allegations of domination and control are woefully inadequate. As the Supreme Court observed in *Aronson*, "the shorthand shibboleth of 'dominated and controlled directors' is insufficient." 473 A.2d at 815. "[T]o render a director unable to consider demand, a relationship must be of a bias-producing nature. Allegations of mere personal friendship or a mere outside business relationship, standing alone, are insufficient to raise a reasonable doubt about a director's independence." *Beam v. Stewart*, 845 A.2d at 1050. Instead, "[t]o create a reasonable doubt about an outside director's independence, a plaintiff must plead facts that would support the inference that because of the nature of the relationship . . . the non-interested director would be more willing to risk his or her reputation than risk the relationship with the interested director." *Id.* at 1052. Plaintiffs have not come close to meeting that burden here.

Plaintiffs allege that Mr. Liveris dominates and controls the four outside directors who joined the Dow Board after 2005 because Mr. Liveris was the Chairman and CEO when they joined. Plaintiffs allege, without citing any particularized facts, that these directors were either "hand-picked or approved by Liveris" and therefore are "beholden to him for their positions." Compl. ¶ 125(d). A virtually identical allegation – that "'Defendant Panic controls and dominates the Board of Directors of ICN' because all of the directors were appointed 'at the explicit direction and request of' Panic" – was held to be "legally insufficient to raise a doubt about the independence of a majority of the directors" in *White v. Panic*, 783 A.2d 543, 551 (Del. 2001). Indeed, in *Beam*, this Court held that plaintiffs had not sufficiently alleged that Martha Stewart dominated the outside directors on her company's board even though she controlled over 94% of the company's voting power and thus could "remove or replace any or all of the directors" at will. 833 A.2d at 978-79. Here, of course, there is no allegation that Mr. Liveris has voting control of Dow or any power to remove a director from office. On the contrary, the directors must stand for election by the shareholders each year.

Plaintiffs' remaining allegations of domination and control depend on an assumption of "structural bias" – that is, that directors will be reluctant to sue other directors if they serve together on Dow Board Committees or on "prestigious" business or professional councils.[14] Thus, for example, plaintiffs point to the fact that Mr. Liveris serves on two "prominent business councils" with one outside director, on the "prestigious American Chemistry Council" with another, and that he also serves on a "prominent international business council" (the U.S.-China Business Council) with outside director Barbara Hackman Franklin and with the Chairman and CEO of Boeing, who is the "boss" of Boeing CFO and Dow director James A. Bell. Compl. ¶ 125(j)(ii). Plaintiffs speculate that Mr. Bell would not pursue claims against Mr. Liveris because he would be fearful that Mr. Liveris might "disparage" him to his boss. Plaintiffs also speculate that Ms. Franklin, who served as Secretary of Commerce under President George H.W. Bush and was closely identified with efforts to increase trade with China, would not sue other directors because "her very livelihood depends on being identified as a counselor and advocate for the Boards of Directors of American companies doing business in international markets, especially China, and instituting these claims would destroy her reputation among her customer base." *Id.* ¶ 125(i).

14 Plaintiffs contend that Dow's Board committees violate good governance principles because there are a variety of overlaps in the membership of the various committees. Compl. ¶125(e). Plaintiffs do not event attempt to explain what is wrong with having overlapping committees. In any event, as the Supreme Court observed in *Brehm,* demand futility allegations cannot be based on deviations from "aspirational goals of ideal corporate governance practices." 746 A.2d at 256.

Similar claims were rejected in *Beam*. There, the Supreme Court reiterated that demand futility cannot be based on these kinds of "structural bias" arguments, which "presuppose[] that the professional and social relationships that naturally develop among members of a board impede independent decision-making." 845 A.2d at 1050-51. Thus, plaintiffs must do more than characterize directors as "close friends" or claim that service on the same boards or professional associations would dissuade directors from suing each other. In addition, plaintiffs must plead particularized facts, such as specific financial ties, familial relationships, particularly close or intimate personal or business affairs, or past instances where the directors acted in a non-independent fashion with respect to an interested director. *Id*. at 1051. Here, there are no allegations of any specific financial ties between Mr. Liveris and the outside directors. Nor are there any factual allegations that would suggest that Mr. Liveris has the kind of particularly close relationship with any of the directors that raises a reasonable doubt about whether they would be more willing to risk their reputations than risk their relationship with him.

Plaintiffs do try to use a past Board decision to demonstrate that Mr. Liveris in fact dominated and controlled the Board. They allege that in 2007, two high-ranking Dow executives who had clashed with Mr. Liveris over delays in implementing the specialty chemicals strategy described above secretly attempted to negotiate a leveraged buy-out of the company without first obtaining the approval of either the Board or Mr. Liveris. Compl. ¶ 125(b). Plaintiffs claim that the fact that the executives were quickly fired, without the Board forming a special committee to investigate whether their strategy was the correct one, somehow shows that the Board was dominated and controlled by Mr. Liveris. *Id.* This is not the type of incident, however, that the Court had in mind in *Beam*. For one thing, there is no reason to believe that Mr. Liveris was "interested" in the challenged decision. According to the complaint, Mr. Liveris had business disagreements with the executives in question and decided to fire them after they ignored both the corporate chain of command and the Board's prerogatives. That the Board agreed with Mr. Liveris' handling of the matter does not suggest that the directors would have protected his personal interests had they diverged from the Company's best interests. Rather, it simply shows that the directors agreed with Mr. Liveris' common-sense business judgment that renegade officers who tried to sell the company without Board approval should be fired.[15]

Plaintiffs have failed to allege any facts that would create a reason to doubt the independence of Dow's nine outside directors. That is reason enough to dismiss Count I of plaintiffs' complaint.

B. Plaintiffs' Allegations Concerning Possible Bribery Relating to K-Dow Are Insufficient to Meet Their Burden of Pleading Demand Futility.

In Count II of their complaint, plaintiffs seek to hold the Individual Defendants liable for failing to prevent alleged bribery of Kuwaiti officials in connection with the K-Dow Joint Venture. The first problem with this claim is that there are no particularized facts alleged to suggest that there was in fact any bribery. Plaintiffs' only support for their "bribery"

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15 Plaintiffs quote a June 2, 2008 press release issued after the former executives had settled claims against Dow in which Dow publicly acknowledged the two executives' "substantial contributions to Dow over their lengthy and illustrious careers." Compl. ¶125(b). But plaintiffs ignore the fact that in the very same press release the former executives acknowledged "participating in discussions which were not authorized by nor disclosed to Dow's Board concerning a potential LBO of Dow" and admitted "that the actions taken [in April 2007] by Dow's Board [terminating their employment] were appropriate under the circumstances." *See* Ex. D (June 2, 2008 Press Release). In light of these admissions, it is absurd for plaintiffs to claim that Mr. Liveris acted improperly or that the Board's decision to terminate the executives was somehow evidence of their lack of independence.

allegation is a quote from the *Kuwait Times*, reporting that, after the PIC refused to proceed with the deal at the end of December 2008, there were questions raised in Parliament about why an agreement had been signed at the end of November, but then approval had been withdrawn a month later.[16] Some members of the Kuwaiti Parliament voiced "very strong suspicions that commissions had been taken in the Dow deal" and recommended setting up a panel to investigate the matter. Compl. ¶ 79. But there are no factual allegations to suggest that these suspicions had any basis in fact. *Compare American Int'l Group, Inc. Consolidated Derivative Litig.*, 965 A.2d 763 (Del. Ch. 2009), where the Company had admitted that its prior financial statements were misstated by billions of dollars and the complaint included "well-pled allegations of pervasive, diverse, and substantial financial fraud involving managers at the highest levels of AIG." 965 A.2d at 776.

Furthermore, plaintiffs do not allege any facts that would give rise to a reasonable inference that the directors were aware of any misconduct in connection with the negotiation of the K-Dow Joint Venture. Plaintiffs repeatedly emphasize their allegation that the entire Board traveled to Kuwait for a final negotiating session and to celebrate the new joint venture. Compl. ¶ 47. But that is hardly a basis for accusing the directors of consciously approving or allowing

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[16] Dow has vigorously denied engaging in any improper actions. In a story reporting Dow's denial on January 31, 2009, the Middle East Company New Wire stated that the allegations "seem to stem from parliament and are likely to have been brought up to undermine Dow's legal case, as well as to weaken those who have accused the deal's critics of wreaking havoc for Kuwait's international business reputation. If such indications [of improper conduct] existed – they still seem very imprecise – they would have been expected to have played a role in the earlier criticism of the deal. Now they sound more like a part of the inter-factional smear campaigns that increasingly plague the country's parliament." *See* Ex. E hereto. The conclusion that the charges are completely bogus is supported by the fact that the scant details provided were identical to charges that the same members of Parliament had previously made with respect to an entirely different and unrelated deal — demonstrating that they were merely recycling allegations, with no regard for the truth.

Dow management to engage in bribery. Plaintiffs do not allege, nor could they allege, that the Dow Board has failed to set up policies or systems to prevent improper dealing with third parties, including bribery. On the contrary, the Court can note Dow's Code of Ethics, which is cited in the complaint (¶ 115) and available on Dow's website, which expressly prohibits any unethical payments to third parties. Nor are there any allegations that the directors saw, but ignored, red flags suggesting that the November 2008 agreement had been procured through misconduct.[17]

Because there are no particularized allegations in the complaint giving rise to an inference that a majority of the Dow Board would have been unable to respond properly to a shareholder demand that it investigate the possibility of bribery related to the K-Dow Joint Venture, any claim for breach of fiduciary duty based on a failure to prevent the alleged bribery must be dismissed.

C. Plaintiffs Have Not Properly Pleaded Demand Futility With Respect To Their Allegations Of Misstatements.

On July 10, 2008, at a press conference to announce the R&H merger agreement, Mr. Liveris was asked whether Dow was "counting on" the proceeds of the K-Dow Joint Venture to close the R&H deal. Mr. Liveris responded that Dow was not "counting on it. We can do this deal without the Kuwait money, and we will stay at investment grade." Compl. ¶ 57. Mr. Merszei, Dow's CFO, agreed, stating that "[t]his deal is certainly not contingent on the closing of our Kuwait joint venture." *Id*. That statement was repeated in an article in *Chemical News and Intelligence*, published on September 23, 2008, although it is unclear whether the article was

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17 Indeed, plaintiffs' own complaint offers an alternative explanation for the unraveling of the K-Dow deal within a month of the signing of the definitive agreement. Plaintiffs quote a *Wall Street Journal* article stating that Dow had dealt only with state oil-company officials and did not pay sufficient attention to the Kuwait Parliament, which "increasingly has been flexing its muscles since 2006." Compl. ¶ 98.

merely quoting statements made months before or whether it was quoting newly-made statements. Compl. ¶ 60. In late October 2008, an article in *Chemical Week* reported that both deals were "on track." Compl. ¶ 61. After a definitive agreement was signed for the K-Dow Joint Venture, Mr. Liveris was quoted in a December 1, 2008 *MarketWatch* article as saying "[w]e have effectively set the stage for our next major landmark – completing the proposed acquisition of R&H in early 2009." Compl. ¶ 62. A week later, Mr. Liveris stated in a webcast that Dow was "'on track to close the [R&H] acquisition,' that Dow 'remain[ed] committed to the deal,' and that Dow had 'plenty of financing resources available' to do so." Compl. ¶ 63.

Plaintiffs claim that all of these statements were false or materially misleading when they were made and seek to hold the directors liable for either making or approving them. In order to hold directors liable for these kinds of alleged misstatements, plaintiffs would have to prove that the directors "*deliberately* misinform[ed] shareholders about the business of the corporation, either directly or by public statements.'" *Citigroup*, 964 A.2d at 132 (quoting *Malone v. Brincat*, 722 A.2d 5, 14 (Del. 1998). Dow's certificate of incorporation (Ex. C hereto) exculpates the directors from personal liability except for breaches of the duty of loyalty and acts or omissions not in good faith or that involve intentional misconduct or knowing violation of law. "Thus, to show a substantial likelihood of liability that would excuse demand [as to plaintiffs' claims based on the alleged misstatements], plaintiffs must plead particularized factual allegations that support the inference that the disclosure violation was made in bad faith, knowingly or intentionally." *Id.* In addition, as the Court noted in *Citigroup*, the directors are "fully protected in relying in good faith on the reports of officers and experts." *Id*.

Plaintiffs have failed to meet their burden. First, as this Court held in *Citigroup*, "[p]leading that the director defendants 'caused' or 'caused or allowed' the Company to issue certain statements is not sufficient particularized pleading to excuse demand under Rule 23.1." 964 A.2d at 133, n.88. Here, as in *Citigroup*, plaintiffs have not offered any "specific factual allegations that reasonably suggest sufficient board involvement in the preparation of the disclosures that would allow [the Court] to reasonably conclude that the director defendants face a substantial likelihood of liability." *Id*. at 132. All of the statements plaintiffs challenge were made by Dow officers in answering questions in the press; none of them were formal corporate disclosures. There is nothing in the complaint to suggest that the board had any involvement whatsoever in making the statements in question.

Moreover, plaintiffs have not alleged any particularized facts to reasonably suggest that the statements were false or materially misleading at the time they were made – let alone that the outside directors knew they were false or misleading or acted in bad faith by not adequately informing themselves. Plaintiffs assume that, from the beginning, Dow was "counting on" the K-Dow Joint Venture to close in order to finance the R&H merger. But there is no reason to believe that was the case in July 2008. At that point in time, Dow's sales were up from the previous year, it was generating billions in net income, and it had sufficient bridge financing for the R&H deal that it believed it could access while "still stay[ing] at investment grade." Compl. ¶ 57. That circumstances changed dramatically over the course of the next six months and that, by January 2009, Dow concluded that it could *not* use the bridge financing it had arranged without risking a credit default does not mean that the statements plaintiffs quote were false or materially misleading at the time they were made.

The same is true of statements in October and early December that both K-Dow and the R&H transaction were "on track" to close in late 2008 and early 2009, respectively. Plaintiffs do not cite any facts to suggest that that Dow's management or the directors thought that either deal had gone off track at those particular points in time. Plaintiffs note that in November Dow had agreed to reset the price for the K-Dow Joint Venture. But the very fact that a definitive agreement was signed in late November 2008 supported the officers' stated belief that both deals were on track to close on time.

In any event, plaintiffs have failed to offer any "analysis of the state of mind of the individual director defendants" or point to any "red flags" that would have made it obvious to the directors that Dow would not be able to go forward with the transactions as planned. Plaintiffs allege that as early as July 2008 the Dow Board must have been aware that credit markets were stressed and that many businesses (including Dow's) were being buffeted by record hydrocarbon prices. But, as this Court observed in *Citigroup,* "[m]erely alleging that there were signs of problems" in the economy "is not sufficient to show that the director defendants knew that [Dow's] disclosures were false or misleading." 964 A.2d at 135. In July 2008, no one could have foreseen what would happen to the world economy over the course of the next six months. Thus, absent clairvoyance, the Dow directors could not have known the difficulties the company would later encounter before finally closing the R&H transaction.

D. Plaintiffs Have Not Pleaded Demand Futility With Respect To Their Claim For Waste.

Plaintiffs have included a perfunctory claim for waste in their laundry list of claimed breaches of fiduciary duty, alleging that the directors "fail[ed] to prevent the payment of excessive and wasteful compensation to Company officers and directors at a time when Dow faced grave and foreseeable risks to its solvency." Compl. ¶ 144. Nowhere in their complaint, however, do plaintiffs explain *whose* compensation should be deemed "excessive and wasteful," let alone attempt to explain why whatever compensation they have in mind meets the stringent requirements for stating a claim for waste.

Waste occurs only when there is "an exchange that is so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration." *Citigroup*, 964 A.2d at 136 quoting *Brehm*, 746 A.2d at 263. "To prevail on a waste claim . . . the plaintiff must overcome the general presumption of good faith by showing the board's decision was so egregious or irrational that it could not have been based on a valid assessment of the corporation's best interests." *Citigroup*, 964 A.2d at 136, quoting *White v. Panic*, 783 A.32d 543, 554 n.36 (Del. 2001).

In this case, plaintiffs do not allege that the Board approved any compensation arrangements that were wasteful at the time they were made. Instead, their claim seems to be that the Board should have taken action at some unidentified point in time to reduce the compensation of unidentified individuals in an unidentified amount in light of the Company's financial difficulties. This vague assertion falls far short of stating a claim for waste. Accordingly, plaintiffs have failed to show that the directors were subject to a substantial likelihood of liability for waste.[18]

IV. COUNT III OF PLAINTIFFS' COMPLAINT SHOULD ALSO BE DISMISSED.

For all of the foregoing reasons, the Court should dismiss Counts I and II of the complaint for failure to properly allege demand futility. Count III should be dismissed for the same reason. Count III does not seek relief for specific alleged misconduct. Instead, it seeks to assert claims for contribution or indemnity against the Individual Defendants arising out of unidentified claims that have been or might be asserted in the future against Dow. Count III adds

[18] In fact, on February 17, 2008, the Company announced that, at management's suggestion, the Board had decided that Mr. Liveris and his direct reports will not be receiving cash performance bonuses for 2008.

nothing substantive. In addition, it is obviously not a ripe claim, inasmuch as there are no claims currently pending against Dow that could give rise to a claim for contribution or indemnity.

Accordingly, Count III should also be dismissed, both for failure to plead demand futility under Rule 23.1 and failure to state a claim under Rule 12(b)(6).

CONCLUSION

For the foregoing reasons, the complaint should be dismissed.

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