FALL 2019

The Bulletin is a quarterly newsletter by Kessler Topaz Meltzer & Check to help institutional investors stay

FULLY INFORMED

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KESSLERTOPAZ MELTZERCHECK LLP

DELAWARE CHANCERY COURT DENIES MOTION TO DISMISS LITIGATION CHALLENGING ELON MUSK'S $55.8 BILLION COMPENSATION PACKAGE

Decision Bodes Well for Related Litigation Led by KTMC

Ariel D. Multak, Esquire and Justin O. Reliford, Esquire

In its recent decision in *Tornetta v. Musk*,[1] Vice Chancellor Joseph R. Slights of the Delaware Court of Chancery denied Elon Musk's motion to dismiss a challenge to his Tesla executive compensation package. Citing concerns regarding Musk's control over the directors who approved the package, the Court ruled that the shareholder-plaintiffs could proceed to discovery on their executive compensation claims.

By way of background, in January 2018, the Compensation Committee of Tesla's board of directors (the "Tesla Board")

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[1] *Tornetta v. Musk*, 2019 WL 4566943 (Del. Ch. Sept. 20, 2019).

RECENT ACADEMIC STUDY EXPLORES THE UNDERUTILIZATION OF SHAREHOLDER LITIGATION AS AN IMPORTANT CORPORATE GOVERNANCE TOOL

Naumon A. Amjed, Esquire and Ryan T. Degnan, Esquire

Many of the world's largest institutional investors have embraced "stewardship" programs as a means to maximize investment returns while also promoting good corporate governance within their investment portfolios. To this end, institutional investor groups like the Investor Stewardship Group — which includes more than sixty prominent institutional investors — have adopted stewardship principles recognizing that "[g]ood corporate governance is essential to long-term value creation and risk management by companies" and that "[i]nstitutional investors should hold portfolio companies accountable."[1]

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[1] Investor Stewardship Group, *Stewardship Framework for Institutional Investors*, available at: https://isgframework.org/stewardship-principles/.

KESSLER TOPAZ STRENGTHENS CLASS CLAIMS AGAINST WALGREENS THROUGH A STRATEGIC AND TARGETED AMENDMENT

Stephanie Grey, Esquire

Kessler Topaz serves as class counsel in *Washtenaw Cnty. Emps. Ret. Sys. v. Walgreen Co., et al.*, No. 1:15-cv-03187-SJC-GAF, for the court-appointed lead plaintiff and class representative Industriens Pensionforsikring, A/S ("Plaintiff"), and a putative class of Walgreen Co. ("Walgreens") investors. Pursuant to the then-governing scheduling order in this action, Plaintiff filed an amended complaint in this matter on December 21, 2018 (the "First Amended Complaint"), seeking to broaden the claims for which it was seeking recovery on behalf of a certified class (the "Class") consisting of all persons and entities that purchased Walgreens common stock during the period from March 25, 2014 through August 5, 2014 (the "Class Period"). On September 23, 2019, the Honorable Sharon Johnson Coleman of the United States District Court for the Northern District of Illinois issued an order sustaining the vast majority of new claims alleged in the First Amended Complaint.

When weighing whether to file the First Amended Complaint, Plaintiff understood that doing so may cause a delay in ongoing discovery in support of the Class's claims. Plaintiff weighed this potential risk against the benefits of broadening its claims and improving its prospects for a favorable recovery on behalf of the Class. As discussed herein, Plaintiff's decision to amend its pleading in the midst of discovery was the right strategic choice in furtherance of the best interests of the Class.

Background

This action arises out of the merger between Walgreens and Alliance Boots GmbH, announced in June 2012. In announcing the merger, Walgreens publicly stated certain long-range goals for the combined entity, which included a goal of $9 and $9.5 billion in adjusted earnings before interest and taxes ("EBIT") for its fiscal year 2016 ("FY16").

Walgreens' ability to achieve its FY16 EBIT goal largely depended upon on the business performance of the Company's pharmacy segment, which generated more than 95% of Walgreens' income from third-party payers, such as insurance companies, pharmacy benefit managers, and the government in the form of a fixed reimbursement rate for each type of drug Walgreens sold. With respect to generic drugs, which comprised the majority of Walgreens' prescription drug sales, these reimbursement rates were fixed for a period of two to three years in contracts that Walgreens had entered into with third-party payers, and were based upon a presumption that generic drug prices would decrease in the near term.

Beginning in 2013, however, the retail pharmacy industry experienced unprecedented levels of generic drug price inflation. Because Walgreens' reimbursement contracts presumed generic drug price *deflation*, the inflationary trend negatively affected Walgreens' financial results. In fact, by late 2013, Walgreens' internal long-range financial planning process noted that the FY16 EBIT goal was tracking under $8.5 billion, and that generic drug price inflation, coupled with Walgreens' reimbursement contracts that presumed generic drug price deflation, were the primary source of the shortfall. On the first day of the Class Period, March 25, 2014, Defendants held an investor conference call claiming that Walgreens was tracking "a bit below" the FY16 EBIT goal, but stated that the Company had identified further "opportunities" and "synergies" to "mitigate" the risks to FY16 EBIT goal. Walgreens' presentation slides for this conference call, however, stated that the FY16 EBIT goal remained at $9 to $9.5 billion. Throughout the Class Period, Walgreens continued to reaffirm that its FY16 EBIT goal was attainable, while downplaying any risk that generic drug price inflation posed to the Company or its goals.

Plaintiff alleges that these materially false or misleading statements artificially inflated the price of Walgreens common stock until Defendants disclosed, on August 6, 2014, that the FY16 EBIT goal was tracking at "around $7.2 billion," significantly below the $9 to $9.5 billion goal that Defendants had reaffirmed during the Class Period. In making this significant downward revision to the FY16 EBIT goal, Defendants claimed that the rapid and pronounced generic drug price inflation

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J.P.M.L. CENTRALIZES ZF-TRW AIRBAG CONTROL UNIT MDL IN THE CENTRAL DISTRICT OF CALIFORNIA

Melissa L. Troutner, Esquire and Natalie Lesser, Esquire

Kessler Topaz recently led the effort for the establishment of a multi-district litigation ("MDL"), covering 18 actions that concern defective airbag control units ("ACUs") manufactured by ZF-TRW[1] and incorporated into over 12 million vehicles sold in the United States (the "ACU Defect Actions"). Kessler Topaz filed the first motion seeking to have an MDL created and Defendants filed a series of oppositions to Kessler Topaz's motion. Interestingly, Defendants' positions on the MDL motion varied, with some raising the arguments that no MDL should be created while others argued that separate MDLs should be created for each individual Defendant. On July 25, 2019, Partner Melissa Troutner argued plaintiffs' position to the Judicial Panel on Multidistrict Litigation ("J.P.M.L." or the "Panel") and urged that the ACU Defect Actions should be centralized in a single MDL in the Central District of California before the Honorable John A. Kronstadt. Shortly thereafter, the J.P.M.L. agreed with Ms. Troutner and centralized the ACU Defect Actions as *In re: ZF-TRW Airbag Control Units Products Liability Litigation*, assigned to Judge Kronstadt.

A Common Defect and NHTSA Investigation

The ACUs at issue in this case contain a defect that causes airbags and other safety restraints to fail to properly deploy during an accident, exposing drivers and occupants to serious and life-threatening safety risks. Generally, ACUs are designed to sense vehicle crashes and evaluate whether the deployment of airbags is necessary in the event of an impact. This includes an electronic component — an application specific integrated circuit ("ASIC") — which monitors signals from other crash sensors located in the vehicles and contains electrical wiring and circuitry intended to prevent the transmission of harmful signals that may damage the ASIC. However, the ACUs at issue in *In re: ZF-TRW Airbag Control Units Products Liability Litigation* do not contain sufficient ASIC protection, which

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[1] The ZF-TRW Defendants include ZF-TRW Automotive Holdings Corp., TRW Automotive U.S. LLC, ZF Friedrichshafen AG, TRW Automotive, Inc., TRW Automotive U.S. LLC, and TRW Vehicle Safety Systems, Inc.

AUSTRALIAN COURT ISSUES FIRST JUDGMENT IN SECURITIES CLASS ACTION

Emily Christiansen, Esquire

The shareholder litigation landscape in Australia has been evolving rapidly. Australia first introduced a class action mechanism in 1992 but it was not until 2011 when Australian securities litigation began to accelerate.[1] In 2018 Australia became the number one location outside of North America for securities class actions and as of September 2019, the Federal Court of Australia reported that more than half of the 107 currently pending Australian class actions related to securities, financial products, or investment claims.[2] Despite the ever-increasing number of securities class actions and the fact that around 120 total securities class actions have commenced since 1992, until recently all cases tended to settle and no case had proceeded to judgment.

On October 24, 2019, Australia saw its first ever judgment in a securities class action with the case of *TPT Patrol Pty Ltd as trustee for Amie Superannuation Fund v. Myer Holdings Limited*. TPT Patrol commenced litigation on behalf of all shareholders who had acquired ordinary shares of Myer on or after September 11, 2014 and who continued to hold those shares on March 19, 2015 against Myer Holdings Limited (one of Australia's largest department store groups). The case alleged that Myer violated its continuous disclosure obligations by failing to timely disclose that it would

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[1] The year after the U.S. Supreme Court issued the *Morrison v. National Australia Bank* decision that limited the rights of shareholders who purchased shares on a non-U.S. market from pursuing a recovery in U.S. courts.

[2] *See* https://www.fedcourt.gov.au/law-and-practice/class-actions/class-actions#byNPA

Institutional Investor

15TH ANNUAL

The Rights & Responsibilities of Institutional Investors

MARCH 5, 2020 • NH GRAND HOTEL KRASNAPOLSKY • AMSTERDAM

Keynote Speaker

Al Gore

Vice President of the United States (1993-2001)
Founder and Chairman, The Climate Reality Project
Independent Director, Apple
Chairman, Generation Investment Management
Nobel Peace Laureate (2007)

Kessler Topaz Meltzer & Check and Institutional Investor are pleased to welcome back Former Vice President Al Gore as the keynote speaker at the 2020 Rights & Responsibilities of Institutional Investors Forum. Vice President Gore delivered the keynote session at the very first Forum 15 years ago. Even then he was a forward-looking, prominent thinker and speaker on the rapidly emerging issues of governance and ESG — issues which have only strengthened in their importance over the intervening decade and a half.

Former Vice President Al Gore is the cofounder and chairman of Generation Investment Management, and the founder and chairman of The Climate Reality Project, a nonprofit devoted to solving the climate crisis. Vice President Gore is the author of the #1 New York Times best-sellers ***An Inconvenient Truth*** and ***The Assault on Reason***, and the best-sellers ***Earth in the Balance, Our Choice: A Plan To Solve the Climate Crisis***, ***The Future: Six Drivers of Global Change***, and most recently, *The New York Times* best-seller ***An Inconvenient Sequel: Truth to Power***.

Now, at this critical juncture in the discussion over climate and investors' role in affecting change, we are privileged to welcome back Vice President Gore, one of the foremost and prominent authorities on this all-important issue to address the 15th Annual Rights & Responsibilities of Institutional Investors Forum, March 5 in Amsterdam.

The Promise of Active Engagement in an Era of Profound Change

The 15th Annual Rights & Responsibilities of Institutional Investors will again be held in Amsterdam and co-hosted by Institutional Investor and Kessler Topaz Meltzer & Check LLP. Many of the most pressing issues for engaged investors and active shareholders covered in this day and a half agenda will consider the ways that senior management, including investment, legal and compliance officers from European and, increasingly, North American, Middle Eastern, and Asian public pension, insurance funds and mutual fund companies, are paving a path forward to meet their fiduciary obligations and engagement goals.

Topics for Discussion:

- EU action plan for sustainable finance
- Is it the investor's job to factor in climate risks?
- Taxes: What tax policies do you have in place?
- Data and access to data: How is data being used in investment decisions?
- Why technology is going to keep making your job hell
- ESG in Europe: Do we need less "E" and more "G"?
- Outcomes-based ESG integration
- Whose "voice" is dominating the ESG conversation: Legal, Investments, or Compliance?

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AUSTRALIAN COURT ISSUES FIRST JUDGMENT IN SECURITIES CLASS ACTION

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not reach its forecasted net profit and that the company had engaged in misleading or deceptive conduct. Myer's then CEO, Mr. Bernie Brookes, represented in a presentation on September 11, 2014 that Myer's net profit after tax ("NPAT") in the financial year ending on July 26, 2015 would exceed the NPAT of the previous financial year. However, on March 19, 2015 Myer announced to the ASX a much lower expected NPAT for the year ending July 26, 2015. TPT Patrol alleged that Myer knew or should have known that it would need to revise its NPAT downward on various dates between November 21, 2014 and February 27, 2015.

Justice Beach, the judge overseeing the case, agreed with TPT Patrol that Myer had violated its continuous disclosure obligations but ultimately, after reviewing event studies presented by battling experts and other evidence, found that the shareholders had not suffered any damage and were therefore ineligible for any recovery. Justice Beach noted that although he found the defendant to have violated its obligations under Australian law, "none of this avails the [plaintiff] concerning share price inflation." Justice Beach emphasized that evidence from Bloomberg demonstrated that the market was already tracking and forecasting that Myer's NPAT would be lower than Brooke's stated forecast. As a result of the Bloomberg reports, it was likely that the market price already accounted for the decreased forecast even though the company had not affirmatively corrected its statements or disclosed information to the market. As Justice Beach explained, "So, if such disclosure had been made…the market price would not likely have altered from what it in fact was if these disclosures had been made."

The ultimate judgment in this case turned on the specific facts that were presented. Nevertheless, the judgment provides an initial glimpse as to where Australia's securities jurisprudence may be heading on a few key legal issues and, although plaintiffs lost this case, Justice Beach's conclusions on key legal concepts should give investors confidence that Australia is still a viable jurisdiction for pursuing a recovery for damages sustained due to disclosure violations and other securities fraud. First, Justice Beach determined that causation can be proven on an indirect (market-wide) basis as opposed to on a direct (individual reliance) basis. He declined to adopt the U.S. "fraud on the market" theory and rebuttable presumption finding that, "the US doctrine, if applied in Australia, would impermissibly rewrite the statutory causation tests." Instead, it is sufficient in Australia to demonstrate that the given security trades on an efficient market, trading in the security is relatively liquid (such that investors can quickly buy or sell shares in reaction to news), that the non-disclosure or other deceptive conduct by a company caused the security to trade at a price different from what it would trade at were the market fully-informed, and that an investor executed a trade during that period or under those conditions and suffered a loss. Second, determining whether there is loss causation and the appropriate methodology for calculating the losses can be established in Australia by event studies. Justice Beach devoted a considerable portion of the opinion explaining the utility of event studies and then engaging in a "battle of the economics experts" and comparing and contrasting the different event studies presented by both the plaintiff and the defendant.

It is premature to draw too many conclusions on the state of Australian securities law at this stage. This decision could still be appealed to the Full Federal Court and since securities class actions are fact-specific inquiries, having only one case as established precedent offers only limited guidance. One prediction made by Australian lawyers, however, is that this will not be the last judgment in Australia and more jurisprudence may soon follow. ■

RECENT ACADEMIC STUDY EXPLORES THE UNDERUTILIZATION OF SHAREHOLDER LITIGATION AS AN IMPORTANT CORPORATE GOVERNANCE TOOL

(continued from page 1)

In addition to governance mechanisms like informed shareholder voting, proxy campaigns, and direct engagement with management, shareholder litigation (such as derivative litigation, appraisal actions, and litigation under the federal securities laws) is an important tool that can be used to obtain monetary compensation, implement corporate governance reforms, and broadly deter future malfeasance.[2] The benefits to the financial markets and investors from institutional investors' involvement in shareholder litigation cannot be understated. Indeed, the United States Congress's intention when enacting the Private Securities Litigation Reform Act of 1995 was to "increas[e] the role of institutional investors in [securities fraud] class actions" because their involvement "will ultimately benefit shareholders."[3] Congress reasoned that because institutional investors "are the ones who have the most to gain from meritorious securities litigation," they would be better monitors of shareholder litigation.[4] Congress's intended impact has played out in practice, as studies have demonstrated that institutional investor representation as lead plaintiffs in securities class actions results in larger recoveries for shareholders.[5]

Notwithstanding the importance of shareholder litigation as a means to maximize investment returns, improve corporate governance, and deter malfeasance in the broader market (thereby creating benefits across an entire investment portfolio), a forthcoming paper from Professors Sean Griffith and Dorothy Lund reveals that the largest institutional investors in the United States (specifically, mutual funds) have generally overlooked shareholder litigation as a stewardship tool.[6] In *Toward a Mission Statement for Mutual Funds in Shareholder Litigation*, Professors Griffith and Lund explore the underutilization of shareholder litigation by mutual funds and conclude that mutual funds (and other large institutional investors) should embrace shareholder litigation as "a pillar of corporate governance that can create real value for investors."[7]

Griffith and Lund Find that While Mutual Funds Almost Never Litigate, Their Investors Benefit When They Do

While effective and meaningful stewardship is a stated commitment of many institutional investors — including most large mutual fund companies — these institutional investors have historically ignored one of the most powerful tools at their disposal: shareholder litigation.

In connection with their forthcoming article, Griffith and Lund empirically reviewed the shareholder litigation activity of the ten largest mutual fund companies in the United States between January 2009 and December 2018 and found that these ten mutual fund families collectively filed only ten traditional

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[2] Derivative litigation allows investors to file claims on behalf of a company against directors and officers that have breached their fiduciary duties to shareholders, appraisal litigation allows shareholders to seek "fair value" of a company's shares when a merger undervalues a company's stock, and securities litigation—brought either individually on behalf of a class of investors—allows shareholders to recover damages resulting from false or misleading statements or material omissions.

[3] H.R. Rep. No. 104-369, at *34 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730, 733.

[4] *Id.*

[5] *See, e.g.*, Cornerstone Research, Inc., *Securities Class Action Settlements: 2018 Review and Analysis*, at 10, 2019 (detailing larger settlement sizes in cases led by public pension funds); Michael Perino, *Have Institutional Fiduciaries Improved Securities Class Actions? A Review of the Empirical Literature on the PSLRA's Lead Plaintiff Provision*, at 12, Nov. 2012 ("the presence of an institutional lead plaintiff is correlated with a 58.9% increase in settlement size, even when controlling for institutional investor selection of larger cases with greater potential damages").

[6] Sean Griffith and Dorothy Lund, *Toward a Mission Statement for Mutual Funds in Shareholder Litigation*, at 7 (European Corporate Governance Institute, Working Paper No. 468, 2019) ("*Mutual Funds in Shareholder Litigation*"). Professor Sean J. Griffith is the T.J. Maloney Chair and Professor of Law at Fordham University School of Law, and Professor Dorothy S. Lund is an Assistant Professor of Law at the University of Southern California, Gould School of Law.

[7] *Id.* at 61.

shareholder lawsuits during the analysis period.[8] Critically, these ten lawsuits were further limited to well-publicized litigation against just five corporate defendants: Petrobras; Countrywide; American Realty Capital Partners (n/k/a VEREIT); Valeant; and Dell.[9] As noted in the article, the lack of mutual fund participation in shareholder litigation is particularly noteworthy given that: (1) the mutual funds' large portfolios and sizeable assets result in the funds having claims in nearly every shareholder class action that is filed; and (2) the mutual funds' participation rate was significantly below 1% of all shareholder actions filed during the time period.[10]

Nevertheless, when institutional investors (including mutual funds) do participate in shareholder litigation, the results are largely positive. As an initial matter, securities class actions led by institutional investors provide better representation for the class and typically generate larger recoveries for all class members.[11] In addition to improving shareholder class actions, large institutional investors frequently benefit when they file direct actions — individual lawsuits that seek to recover investment losses solely on behalf of the named plaintiffs. These direct actions allow large institutional investors to "chart their own course" during litigation and, as demonstrated by prior analysis, frequently generate larger (and quicker) recoveries than what the institutional investors would have received had they remained passive class members in the parallel class action.[12]

Griffith and Lund's research confirms these assertions, citing several notable instances where large mutual funds have filed direct actions. For example, in *In re Petrobras Securities Litigation*, No. 1:14-cv-09662-JSR (S.D.N.Y.) ("Petrobras"), Vanguard, Dimensional, and State Street chose to file direct actions instead of passively participating the class action and each received substantial benefits compared to passive class participants. For example, as noted by Professors Griffith and Lund, "although the terms of the direct settlements are confidential, the mutual funds likely did better than they would have under the class action settlement."[13] Additionally, as is the case in many direct actions, each of the funds was paid much faster than the remainder of the class: while Dimensional and State Street settled their lawsuits in November 2016 and Vanguard settled its lawsuit in June 2017, class members are still waiting to receive payment in connection with the class action settlement administration process.[14]

Other opt-out cases provide additional examples of institutional investors recovering higher amounts over what they would have recovered as passive class members. For example, in the $2.4 billion class action settlement in *In re AOL Time Warner, Inc. Securities and "ERISA" Litigation,* several institutional investors secured $764 million in individual settlements and "obtain[ed] far greater amounts than what plaintiffs would have received had they stayed in the class."[15] Similarly, in *In re Qwest Communications International Inc. Securities Litigation*, institutional investors were able to obtain $411 million in individual settlements — nearly the size of the entire $445 million class settlement — including one institutional investor that reported receiving 38 times more than it would have recovered under the class settlement.[16]

In light of these "encouraging" results — not only in securing additional recovery, but in effecting market-wide deterrence — the absence of more examples of large institutional investors taking an active approach to litigation to secure additional benefits for their stakeholders is puzzling. In fact, given that no more than three of the ten largest mutual funds participated in any of the "best" cases (*i.e.*, those claims most likely to result in substantial recovery, like *Petrobras*), it is clear to Griffith and Lund that "the largest mutual funds are leaving investor money on the table."[17]

Moreover, the missed opportunities when ignoring litigation as a stewardship tool extend beyond simply leaving money on the table. Griffith and Lund's research confirms that voting and litigation should be treated as "complementary corporate governance mechanisms, with litigation in many ways the stronger of the two."[18] Indeed, while it is commonly argued

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[8] *See id.* at 23. The ten mutual fund managers studied were (in descending order of equity assets under management): Vanguard, BlackRock, State Street, Fidelity, Capital Group, T. Rowe Price, BNY Mellon Investment Management, Dimensional Fund Advisors, JP Morgan Asset Management, and Invesco. Several of these mutual fund managers are members of the Investor Stewardship Group.

[9] *See id.* at 23-24. Five of the ten largest mutual funds (Fidelity, Capital Group, BNY Mellon, and JP Morgan) did not file any shareholder suits during the studied time period.

[10] *See id.* at 31, 38.

[11] *See supra* n. 5.

[12] *See* Cornerstone Research, Inc. and Latham & Watkins LLP, *Opt-Out Cases in Securities Class Action Settlements*, *2014-2018 Update*, 2019 (finding that a single individual settlement, in one case, was equal to 92.4% of the entire *class* settlement); *see also* Prof. John C. Coffee, Jr., *Accountability and Competition in Securities Class Actions: Why 'Exit' Works Better Than 'Voice'*, Working Paper No. 329, July 2, 2008 (noting that institutional investors that filed direct suits instead of remaining in securities classes often obtained "an order of magnitude" more in recovery than they would have had they stayed in the class).

[13] *See Mutual Funds in Shareholder Litigation*, at 26.

[14] *See id.*

[15] Cornerstone Research, Inc. and Latham & Watkins LLP, *Opt-Out Cases in Securities Class Action Settlements*, 2013.

[16] *See id.*

[17] *Mutual Funds in Shareholder Litigation*, at 29.

[18] *Id.* at 5.

Institutional Investor Legal Forum

Sovereign Investor Institute
A membership organisation of Institutional Investor

3RD ANNUAL

Institutional Governance and Legal Symposium

APRIL 1, 2020 • CENTRAL LONDON

Institutional Investor's Sovereign Investor Institute and Legal Forum membership in partnership with Kessler Topaz Meltzer & Check LLP (KTMC) will hold the third annual gathering of senior legal executives at sovereign wealth funds and asset management firms. This meeting will provide a private, closed-door environment to discuss and debate issues related to governance, shareholder engagement and related legal and compliance issues.

Preliminary Topics

We are excited to bring you the first look of our 2020 discussion topics. Topics under consideration include:

- The Deglobalizing World: CFIUS, Japan and Beyond
- Governance Best Practice for Sovereign Funds and Asset Managers
- Sustainable Finance: Regulatory and Industry Initiatives
- Implementing ESG Strategies: What Investors Want from their Managers
- Managing Regulatory Change in a Global Organisation
- Litigation Case Study

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Keynote Speaker

The Rt. Hon. Theresa May, MP

Prime Minister of the United Kingdom (2016–2019)

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Institutional Investor

KESSLER TOPAZ MELTZER CHECK LLP

J.P.M.L. CENTRALIZES ZF-TRW AIRBAG CONTROL UNIT MDL IN THE CENTRAL DISTRICT OF CALIFORNIA

(continued from page 3)

causes electrical overstress ("EOS") and may lead to system failure (the "ACU Defect"). The ACU Defect causes the ACUs to stop working without warning, results in failure of the airbags and other safety restraints to deploy when needed, and subjects drivers and occupants of the vehicles to injury and death.

The National Highway Traffic Safety Administration's ("NHTSA") Office of Defects Investigation ("NHTSA ODI") has been investigating the ACU Defect and in March 2018 opened a preliminary evaluation ("PE") investigation into the defect based on six frontal crashes where airbags did not deploy, reported via Early Warning Reporting between 2012 and 2017. Those crashes resulted in six injuries and four deaths. ZF-TRW was identified as the supplier of the defective ACUs and the investigation focused on certain vehicles containing the defective ACUs.[2] On April 19, 2019, NHTSA ODI upgraded its PE investigation into the ACU Defect to an Engineering Analysis and expanded the investigation to include additional car manufacturers. While some vehicle manufacturers conducted voluntary recalls in response to NHTSA ODI's initial investigation, none of the approximately 12.3 million vehicles at issue in the ACU Defect Actions have been recalled.

KTMC Files First Complaint

Kessler Topaz has been instrumental in advancing *In re: ZF-TRW Airbag Control Units Products Liability Litigation* by (1) investigating and filing the first class action concerning the defective ACUs, *Samouris, et al. v. ZF-TRW Automotive Holdings Corporation, et al.*, in the Eastern District of Michigan on April 26, 2019;[3] (2) filing two additional class actions in the Central District of California — where the Hyundai America and Kia America Defendants are headquartered — asserting allegations of an enterprise and conspiracy to conceal the ACU Defect in violation of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961(c) and (d);[4] (3) moving the J.P.M.L. to centralize the ACU Defect Actions in a single MDL; and (4) successfully arguing before the Panel that the ACU Defect Actions should be centralized before Judge Kronstadt in the Central District of California.

In addition to the three actions brought by Kessler Topaz and co-counsel, 15 other ACU Defect Actions asserted similar claims on behalf of overlapping nationwide classes of consumers against overlapping defendants. The ACU Defect Actions also named certain vehicle manufacturers (the "Vehicle Manufacturer Defendants")[5] whose vehicles were equipped with the defective ACUs. The ACU Defect Actions assert claims for, *inter alia*, RICO violations, violations of common and statutory law, fraud, misrepresentation, breach of warranties, unfair and deceptive trade practices, and violations of state consumer protection statutes. Plaintiffs allege that although Defendants have long known of the ACU Defect and associated safety risks, they failed to act within a reasonable time to stop the sale of defective ACUs, failed to stop the sale and lease of class vehicles equipped with the defective ACUs, and failed to disclose the ACU Defect to plaintiffs, putative class members and the public. Plaintiffs further allege that, as a result of Defendants' unlawful conduct, millions of consumers unknowingly purchased or leased vehicles equipped with the defective ACUs and have suffered economic damages. The ZF-TRW, Hyundai, and Kia Defendants are also alleged to have participated in a RICO enterprise and conspiracy to conceal the ACU Defect.

KTMC Successfully Argues to the J.P.M.L.

After hearing extensive oral argument, in which Kessler Topaz advocated for transfer to the Central District of California, the Panel issued an order, granting Kessler Topaz's motion, and transferring the ACU Defect Actions to Judge Kronstadt in the Central District of California for coordinated or consolidated pretrial proceedings.[6] The Panel agreed with Kessler Topaz, stating the "actions share factual issues arising from allegations that airbag control units manufactured by the ZF-TRW Defendants are defective, in that an electrical overstress condition can cause a malfunction of the ACU's application specific integrated circuit" and "[b]ecause of this alleged defect — which may affect more than twelve million vehicles made by multiple automakers, including FCA, Honda, Hyundai/Kia, Mitsubishi, and Toyota — there is a risk that the airbag could fail to deploy in an accident."[7] Thus, the Panel found "[c]entralization would eliminate duplicative discovery and other pretrial proceedings, as well as

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[2] NHTSA ODI Resume, Investigation EA 18-003.

[3] *See* Complaint, *Samouris*, No. 2:19-cv-11215 (E.D. Mich. Apr. 26, 2019), ECF No. 1.

[4] *See Altier, et al. v. ZF-TRW Automotive Holdings Corporation, et al.*, 8:19-cv-00846 (C.D. Cal. May 6, 2019), ECF No. 1; *Bell, et al. v. ZF Friedrichshafen AG, et al.*, 8:19-cv-00963 (C.D. Cal. May 21, 2019), ECF No. 1.

[5] The "Vehicle Manufacturer Defendants" include Honda, Hyundai, Kia, FCA, Mitsubishi, Toyota and various subsidiaries of these companies.

[6] The Transfer Order is available on the J.P.M.L. docket, MDL No. 2905, Document 112 ("Transfer Order").

[7] *See* Transfer Order at 2.

DELAWARE CHANCERY COURT DENIES MOTION TO DISMISS LITIGATION CHALLENGING ELON MUSK'S $55.8 BILLION COMPENSATION PACKAGE

(continued from page 1)

agreed to update Elon Musk's incentive-based compensation package. At the time, Musk served as Tesla's CEO, Chairman, and largest shareholder (owning approximately 22% of Tesla). The compensation package consisted of a 10-year grant of stock options that would vest in twelve installments, contingent upon Tesla reaching certain operational and stock price milestones. If all of the options vest, the award has a maximum potential value of $55.8 billion to Musk. In March 2018, Tesla stockholders voted to approve Musk's compensation package.

Vice Chancellor Slights' ruling was significant in several respects. *First*, the Court acknowledged that this executive compensation case was far different from the more typical challenges to executive compensation that courts routinely dismiss at the pleading stage. Courts in Delaware, and across the country, typically view executive compensation as a matter better left to the discretion of directors, rather than courts. In *Tornetta*, however, the Vice Chancellor determined that Musk's potentially coercive influence over the Tesla Board prevented the Court from simply deferring to the Tesla directors' "business judgment" about how much Musk's services are worth to Tesla.

Second, the Court of Chancery ruling stands in stark contrast to recent cases where the Court has refused to review transactions approved by outside stockholders. Reaffirming the holdings of numerous cases that preceded this trend, the Court reasoned that stockholder approval cannot "cleanse" a transaction involving a controlling shareholder. The Court acknowledged that, with certain additional procedural protections for Tesla shareholders, Musk and the Tesla Board might have been able to rely on the stockholder vote to avoid the litigation. More specifically, the Court explained that stockholder approval might have been enough if the compensation package were also conditioned at the outset on the approval of an independent, adequately-empowered "special committee" of the Tesla Board.

Third, this decision will undoubtedly impact related litigation pending before Vice Chancellor Slights that is led by KTMC. Indeed, *Tornetta* is the second case in which the Vice Chancellor has sustained allegations that Musk, who holds only 22% of Tesla common stock, controls Tesla and the Tesla Board. Vice Chancellor Slights issued his first opinion on that score in *In re Tesla Motors, Inc. Stockholder Litigation* ("*Tesla*"), a case filed by Arkansas Teacher Retirement System ("ATRS") and other Tesla stockholders, where Kessler Topaz serves as Co-Lead Counsel.

The *Tesla* action challenges Tesla's 2016 acquisition of SolarCity, a struggling solar energy company founded by Musk's cousins. At the time of the transaction, Musk served as SolarCity's Chairman and largest stockholder. In *Tesla*, Vice Chancellor Slights denied defendants' motion to dismiss in 2018, holding "it is reasonably conceivable that Musk, as a controlling stockholder, controlled the Tesla Board in connection with the Acquisition." Accordingly, the Court rejected similar efforts by Musk to have the case dismissed at the pleading stage because of the stockholder vote approving the deal.

The parties in *Tesla* are currently briefing summary judgment motions, with Musk making a number of the same arguments that Vice Chancellor Slights rejected in *Tornetta*. Consistent with that decision, ATRS argues that Musk must prove at trial that the transaction was fair to all Tesla stockholders given his interest in the transaction and the evidence of Musk's control over Tesla, the Tesla Board, and the transaction process.

Vice Chancellor Slights' pleadings stage ruling in *Tornetta* bodes well for how he might rule on the parties' summary judgment arguments in *Tesla*. After all, Musk and the Tesla Board did not form an "independent special committee" to oversee the transaction process. Meanwhile, ATRS contends that Musk played an active (though largely undisclosed) role in that process and that his domineering involvement directly affected the Tesla Board's decision to pursue the transaction. If Vice Chancellor Slights rejects Musk's motion for summary judgment, trial in the *Tesla* action will begin in March 2020. ■

RECENT ACADEMIC STUDY EXPLORES THE UNDERUTILIZATION OF SHAREHOLDER LITIGATION AS AN IMPORTANT CORPORATE GOVERNANCE TOOL

(continued from page 7)

that some institutional investors do not participate in shareholder litigation because — as long-term equity investors — they would essentially be "paying themselves," Griffith and Lund disagree: "[l]awsuits that actively police managerial misconduct will benefit the fund across its holdings not only by punishing misconduct when it occurs but also by discouraging misconduct at other firms in the portfolio."[19] Similarly, "governance-enhancements extracted through litigation may improve the performance of firms in the portfolio, leading other firms to copy these innovations, and enhancing the value of the portfolio as a whole."[20] Moreover, securities fraud claims may arise as a company exits a mutual fund's portfolio, removing this concern entirely. To Griffith and Lund, the benefits of litigation as a stewardship tool outweigh the costs.

Benefits from Shareholder Litigation Are Available to Other Large Institutional Investors

The benefits of participating in shareholder litigation as part of an institutional investor's stewardship goals are not limited to the ten largest mutual funds companies studied by Griffith and Lund. Indeed, the same benefits inure to increased strategic litigation participation by other institutional investors.

For funds with substantial losses in a given case, the benefits to filing a direct action are clear: secure a larger recovery for the fund's investors and receive the funds faster than absent class members. However, in appropriate circumstances, it is advisable for funds to seek appointment as lead plaintiff in securities fraud class actions. Institutional investor leadership in class action litigation ensures that the claims will be handled by competent counsel, under the institutional investor's supervision, and ensures that the litigation proceeds along the best path for the entire class. Additionally, institutional investor involvement in driving larger class settlements helps provide more effective market-wide deterrence against managerial misconduct, and the leverage of a class plaintiff in settlement negotiations renders demands for meaningful governance reforms all the more powerful.

With the ability to increase recovery for investors, effectuate meaningful governance reform, and deter further misconduct, institutional investors should seek to identify strategic litigation opportunities that both maximize return on investment and promote good corporate governance. ■

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[19] *Id.* at 42.

[20] *Id.*

J.P.M.L. CENTRALIZES ZF-TRW AIRBAG CONTROL UNIT MDL IN THE CENTRAL DISTRICT OF CALIFORNIA

(continued from page 9)

the possibility of inconsistent rulings on class certification, *Daubert* motions, and other pretrial matters, and conserve judicial and party resources."[8]

The Panel found that the arguments by certain Vehicle Manufacturer Defendants in opposition to centralization were "not convincing."[9] Specifically, the J.P.M.L. found that any individual issues, which are "relatively commonplace in products liability MDLs" did not negate the substantial common issues. The Panel further found that denying centralization "would hardly alleviate any trade secret concerns"[10] given the number of cases involving multiple Vehicle Manufacturer Defendants. Moreover, the transferee court could "utilize protective orders and other methods to address confidentiality issues and other defendant-specific matters."[11] The Panel rejected the suggestion of separate, automaker-specific MDLs, echoing Kessler Topaz's argument that the common defect in the ACUs entailed significant overlap of core factual issues, parties and claims, meriting the creation of a single MDL.

Lastly, the J.P.M.L. accepted Kessler Topaz's recommendation that the ACU Defect Actions be centralized before Judge Kronstadt in the Central District of California, highlighting the fact that relevant documents and witnesses were likely to be found within the district, a significant number of actions were already pending within the district, and Judge Kronstadt is an experienced jurist who will steer the litigation on a prudent course.[12]

Following transfer by the J.P.M.L., Judge Kronstadt established a single docket for pre-trial proceedings[13] and scheduled a case management conference for February 24, 2020. Applications for Lead and Liaison Counsel under Federal Rule of Civil Procedure 23(g) are to be filed on January 21, 2020 and will be addressed at the February hearing along with case management issues such as establishing a case schedule and discovery plans, addressing jurisdictional issues, and considering potential early dispute resolution or settlement. ■

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[8] *Id.*

[9] *Id.*

[10] *Id.*

[11] *Id.* at 2-3.

[12] *Id.* at 3.

[13] The MDL docket is 2:19-ml-02905-JAK-FFM (C.D. Cal.).

Institutional Investor

KESSLERTOPAZ MELTZERCHECK LLP

APRIL 28 - 29, 2020 • APELLA • NEW YORK

Litigation & Governance Trends for Asset Management Firms

Special Guest

Chuck Todd

NBC News Political Director and Moderator of Meet the Press and MTP Daily

When is taking action appropriate for your firm and your clients?

As old standards and norms change and new trends and priorities emerge, active investors have a lot to worry about at both the macro and the firm levels. From the fiduciary, legal and investment ramifications of climate change to firm-specific concerns of privacy and data as well as the altered role of the legal team within the decision-making structure from increasing privacy concern to climate change and from cryptocurrency to power shifts within the company, times they are a-changing. And one of those changes is the way an increasing number and diversity of asset management firms are approaching their obligations when it comes to protecting and recovering assets, and integral to this process is the question of when and how to get involved when the need arises.

This year's Litigation & Governance Trends program is going to focus more on the how than the why, reflecting the growing acknowledgement of the value and efficacy of appropriate shareholder litigation and next-generation corporate governance efforts. This day and half event is the third event in a three-part annual global series focusing exclusively on the needs of legal and compliance teams at global asset management firms through the lens of active engagement, shareholder actions, and affirmative litigation.

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Registration is COMPLIMENTARY for qualified delegates

KESSLER TOPAZ STRENGTHENS CLASS CLAIMS AGAINST WALGREENS THROUGH A STRATEGIC AND TARGETED AMENDMENT

(continued from page 2)

and the Company's reimbursement contracts (which presumed a decrease in generic drug prices) were the primary reasons for the approximately $2 billion shortfall. As a result of this disclosure and related matters that Walgreens revealed on August 6, 2014, the price of Walgreens common stock declined by approximately 14.3%, causing substantial investor losses.

Plaintiff's Original Complaint

In August 2015, Plaintiff filed its Consolidated Class Action Complaint (the "Original Complaint") against Defendants Walgreens, the Company's former Chief Executive Officer, Gregory D. Wasson, and Walgreens' former Chief Financial Officer, Wade Miquelon, for violating Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "Exchange Act"), and Rule 10b-5 promulgated thereunder.

Specifically, Plaintiff claimed that Defendants made materially false or misleading statements concerning Walgreens' FY16 EBIT goal and the impact of generic drug price inflation and reimbursement pressure on the Company's performance. Plaintiff alleged that Defendants engaged in a scheme to conceal from investors the reasons for and sources of Walgreens declining margins and shortfall in the FY16 EBIT goal, as well as the negative impact of generic drug price inflation on the Company's performance and financial condition. Plaintiff asserted that, while concealing these adverse facts, Defendants issued materially false or misleading statements touting the Company's ability to achieve and meet the FY16 EBIT goal and falsely claiming that "the most significant factor affecting the pharmacy margin was dramatically slower rate of new generic introductions" and that "management noted that it is seeing nothing unusual at this point" with respect to reimbursement pressures. Plaintiff further alleged that Defendants' misstatements artificially inflated Walgreens' stock price, and that such inflation was not removed until August 6, 2014, when Defendants disclosed that the Company's financial results and the FY16 EBIT goal were negatively impacted by the combined effect of generic drug price inflation and the previously undisclosed unfavorable terms of Walgreens' reimbursement contracts.

All Defendants moved to dismiss the Original Complaint, and briefing on these motions was completed in February 2016.

The Court's First Motion to Dismiss Opinion

In September 2016, the Court denied in part and granted in part Defendants' Motion to Dismiss Plaintiff's Original Complaint. In its order, the Court sustained several statements in which Defendants allegedly concealed the negative impact that generic drug price inflation and reimbursement pressure was having upon Walgreens. The Court found these statements were actionable because Defendants falsely attributed the Company's declining margins and earnings shortfall to the lack of new generic drug conversions (i.e. when a generic form of a branded drug enters the market) and routine reimbursement pressures. Behind the scenes, however, Defendants knew the margin pressure and financial shortfall were primarily due to generic drug price inflation combined with Walgreens' problematic reimbursement contracts that anticipated generic drug price deflation.

Judge Coleman, however, dismissed the allegations based on the statements related to the Company's FY16 EBIT goal of $9 to $9.5 billion. The Court concluded that these statements were not actionable because Plaintiff failed to allege sufficiently that the FY16 EBIT goal was not attainable at the time Defendants made such statements. In other words, the Court concluded that Plaintiff's Original Complaint did not allege adequate facts demonstrating that the FY16 EBIT statements were made with knowledge that they were incorrect or were made without a reasonable basis.

Class Certification and Merits Discovery

On April 21, 2017, Plaintiff moved to certify this action as a class action. Among other things, Plaintiff contended that damages could be measured for the proposed class based upon the 14.3% decline in the price of Walgreens common stock on August 6, 2016, which is when Plaintiff alleges that the truth was revealed underlying Defendants' false or misleading statements concerning the impact of generic drug price inflation and Walgreens' unfavorable reimbursement contracts. Defendants' primary argument in opposing class certification was that Plaintiff's proposed class-wide damages methodology was inconsistent with Plaintiff's liability theory.

In this regard, Defendants contended that Plaintiff could not measure damages based upon the August 6, 2014 decline in the price of Walgreens common stock because Walgreens had earlier disclosed (on June 24, 2014) that the Company was negatively impacted by generic drug price inflation, which Walgreens' fixed reimbursement contracts exacerbated. From this, Defendants argued that the August 6, 2014 price decline was caused by factors other than those underlying Plaintiff's claims, including the $2 billion downward revision of the FY16 EBIT goal (as the Court had dismissed alleged misstatements on that issue in its September 2016 decision on Defendants' Motion to Dismiss Plaintiff's Original Complaint). In granting Plaintiff's Motion for Class Certification, the Court determined, among other things,

(continued on page 14)

KESSLER TOPAZ STRENGTHENS CLASS CLAIMS AGAINST WALGREENS THROUGH A STRATEGIC AND TARGETED AMENDMENT

(continued from page 13)

that Defendants' challenge to Plaintiff's proposed damages methodology was a premature loss causation argument, which is not appropriately addressed at the class certification stage.

During ongoing merits discovery, Defendants argued that information relating to the FY16 EBIT goal was irrelevant to Plaintiff's claims based upon the Court's decision on Defendants' Motion to Dismiss Plaintiff's Original Complaint dismissing Plaintiff's claims based upon statements concerning the FY16 EBIT goal. As a result, Defendants refused to produce any information regarding the FY16 EBIT goal. In response, Plaintiff filed several motions to compel, seeking production of documents responsive to its discovery requests regarding the impact of generic inflation and reimbursement pressure on the FY16 EBIT goal.

In the midst of these discovery disputes, the United States Securities and Exchange Commission ("SEC") issued a September 28, 2018 administrative "cease-and-desist order" (the "SEC Order") in which the SEC found that Defendants "acted negligently in failing to adequately disclose to investors the material increase in risk to the company's ability to achieve the FY16 EBIT Goal." Defendants consented to the entry of the SEC Order without admitting or denying the findings therein. Based on this announcement, which was the first disclosure of the SEC's investigation of Walgreens, Plaintiff immediately served additional discovery requests on Defendants for the documents and information that Defendants produced to the SEC, and Defendants began producing the requested materials.

Plaintiff's First Amended Complaint

After an extensive review of the information produced during discovery, including the materials from the SEC investigation, Plaintiff elected to amend its Original Complaint on December 21, 2018, which was the deadline for doing so under the operative scheduling order in the case. Among other things, Plaintiff's First Amended Complaint sought to revive claims based on Defendants' misrepresentations and omissions concerning Walgreens' FY16 EBIT goal. Defendants moved to dismiss Plaintiff's First Amended Complaint on February 19, 2019, arguing that Plaintiff's new allegations were inadequate. Defendants also challenged Plaintiff's loss causation allegations in an attempt to shorten the Class Period — an argument nearly identical to the loss causation challenges that Defendants raised in opposing Plaintiff's Motion for Class Certification.

In its September 23, 2019 Order, the Court held that the First Amended Complaint adequately pled that Defendants misrepresented and concealed material facts when reiterating Walgreens' FY16 EBIT goal of $9 to $9.5 billion. In this regard, the Court concluded that the First Amended Complaint pled sufficient facts indicating that Defendants knew by March 2014 that the FY16 EBIT goal was tracking far below the $9 to $9.5 billion figure provided to the market. In particular, the Court noted that Plaintiff cured its earlier pleading deficiencies with respect to statements addressing the FY16 EBIT goal because the First Amended Complaint provided sufficient allegations raising a strong inference that by the beginning of the Class Period, Defendants knew the $9 to $9.5 billion earnings goal was not attainable. Further, the Court rejected Defendants' argument that Plaintiff did not adequately allege loss causation, holding that Plaintiff sufficiently pled a direct causal connection between Defendants' misstatements concerning the FY16 EBIT goal and the August 6, 2014 disclosures that caused the price of Walgreens common stock to decline by more than 14%.

Conclusion

Amending a complaint during the discovery phase of litigation can extend the amount of time the case is litigated and delay a recovery for investors. This is particularly true of cases subject to the Private Securities Litigation Reform Act of 1995, where discovery may be stayed or limited while the court considers any motion to dismiss an amended pleading. Deciding to amend, however, can lead to considerable benefits, as it has with the pending case against Walgreens, because it can increase the amount of damages at issue in the action as well as the prospects of recovering such damages. ■

WHAT'S TO COME

JANUARY 2020

National Conference on Public Employee Retirement Systems (NCPERS) Legislative Conference
January 26 – 28
Capital Hilton ■ Washington, DC

Florida Public Pension Trustees Association (FPPTA) Winter Trustee School
January 26 – 29
Hyatt ■ Orlando, FL

FEBRUARY 2020

National Association of Public Pension Attorneys (NAPPA) Winter Seminar
February 19 – February 21
Tempe Mission Palms Hotel ■ Tempe, AZ

MARCH 2020

California Association of Public Retirement Systems (CALAPRS) General Assembly
March 2 – 5
Monterey Marriot ■ Monterey, CA

15th Annual Rights and Responsibilities of Institutional Investors (RRII)
March 5
Amsterdam, Netherlands

Council of Institutional Investors (CII) Spring Conference
March 9 – March 11
Mandarin Oriental Hotel ■ Washington D.C.

Florida Public Pension Trustees Association (FPPTA) Wall Street Program
March 24 - 28
Sheraton Times Square ■ New York, NY

APRIL 2020

3rd Annual Institutional Governance and Legal Symposium
April 1
The Landmark London ■ London

Litigation & Governance Trends for Asset Management Firms
April 28 – 29
Apella ■ New York, NY

MAY 2020

Texas Association of Public Employee Retirement Systems (TEXPERS) 30th Annual Conference
May 3 – 6
Moody Garden Hotel ■ Galveston, TX

National Conference on Public Employee Retirement Systems (NCPERS) Annual Conference & Exhibition
May 10 – 13
Caesars Palace ■ Las Vegas, NV

State Association of County Retirement Systems (SACRS) Spring Conference
May 12 – 15
Paradise Point Resort & Spa ■ San Diego, CA

Pennsylvania Association of Public Employee Retirement Systems (PAPERS) 15th PAPERS Forum
May 30
Hilton ■ Harrisburg, PA

JUNE 2020

National Association of Public Pension Attorneys (NAPPA) Legal Education Conference
June 24 – June 26
Marriott Resort ■ Fort Lauderdale, FL

Florida Public Pensions Trustees Association (FPPTA) 36th Annual Conference
June 28 – July 1
Renaissance Orlando SeaWorld ■ Orlando, FL

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