Matter of Handy & Harman Ltd.
2018 NY Slip Op 30894(U)
May 9, 2018
Supreme Court, New York County
Docket Number: 654747/2017
Judge: Barry Ostrager

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: HON. BARRY R. OSTRAGER **PART** 61
Justice

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IN RE HANDY & HARMAN LTD. STOCKHOLDER LITIGATION

INDEX NO. 654747/2017

MOTION DATE 2/2/2018

MOTION SEQ. NO. 002

DECISION AND ORDER

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The following e-filed documents, listed by NYSCEF document number 28, 29, 30, 31, 32, 33, 34, 35, 36, 37, 38, 39, 40, 41, 42

were read on this application to/for DISMISSAL

OSTRAGER, BARRY, J.S.C.,

Plaintiffs in this putative class action are former stockholders of Handy & Harman Ltd. (the "Company") who challenge the Company's acquisition by its controlling stockholder, Steel Partners Holding LP ("SPLP"). Before the Court is a pre-answer motion by defendants SPLP and Robert Frankfurt to dismiss this action pursuant to CPLR 3211. For the reasons set forth herein, the Court grants the motion in part based on the papers submitted and extensive oral argument on the record in the So Ordered transcript entered April 19, 2018 (NYSCEF Doc. No. 44).

Background Facts

Defendant SPLP is a publicly traded global holding company that owns and operates businesses and has investments in companies across various industries. Handy and Harman Ltd. (the "Company"), a Delaware corporation, is now a wholly-owned subsidiary of SPLP. Before a merger was effectuated in or about October 2017 (the "Merger"), SPLP and its affiliates owned

approximately 70% of the Company's outstanding common stock. The plaintiffs in this action represent a class of minority stockholders who owned the balance of the Company's common stock prior to the Merger. Defendant Robert Frankfurt was a member of the Company's seven-person Board of Directors from 2008 until the effective date of the Merger. Frankfurt and two other directors served as the Special Committee that negotiated the terms of the Merger.

SPLP presented the terms of the proposed Merger to the Company's Board of Directors in March 2017. The Merger offer was conditioned on both (i) approval by a Special Committee comprised of independent directors; and (ii) approval by a majority of the non-SPLP stockholders, commonly known as a "majority-of-the-minority" ratification provision. In response to the offer, the Company's Board formed a Special Committee consisting of three directors, Robert Frankfurt, Patrick A. DeMarco, and Garen W. Smith, with Frankfurt as the Chair. The Special Committee was empowered to establish a process to review the Merger offer, negotiate terms, and determine whether the proposed Merger or any alternative was "advisable and fair to, and in the best interest of, the Company's unaffiliated stockholders." (See Ex H to Fleming Aff). The Special Committee retained Graubard Miller as legal counsel and Duff & Phelps, LLC as financial advisor to assist in the process.

Upon the completion of its process, the Special Committee approved a deal whereby the non-SPLP shares of the Company would be exchanged for 5,432,000 SPLP Preferred Units, valued at approximately $128.3 million. On June 26, 2017, the Company Board met and approved the terms proposed by the Special Committee and then announced the execution of a Merger Agreement by which SPLP would commence a tender offer to the Company's minority stockholders, subject to acceptance by a majority of the non-SPLP stockholders. Following some additional procedures, SPLP and the Company consummated the Merger pursuant to the terms of the October 12, 2017 Merger Agreement.

However, before the Merger was consummated, this litigation was commenced in July 2017 by Susan Paskowitz on behalf of Company stockholders challenging the fairness of the Merger and alleging that the Board and SPLP had breached their fiduciary duties to minority stockholders by recommending the Merger and entering into the Merger Agreement. In December, stockholders David Pill and Alan R. Kahn commenced a second action under index number 657304/17. The two actions were consolidated for all purposes under the above caption and index number early this year (NYSCEF Doc. No. 23).

Analysis

The Court of Appeals set forth the standard of review applicable to a pre-answer motion to dismiss in *Leon v. Martinez*, 84 N.Y.2d 83, 87-88 (1994) (with citations omitted):

> On a motion to dismiss pursuant to CPLR 3211 [for failure to state a cause of action], the pleading is to be afforded a liberal construction … [The Court is required to] accept the facts alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory … Under CPLR 3211(a)(1), a dismissal is warranted only if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law.

Defendants assert that they have established their right to dismissal of this action based on the holding of the Supreme Court of Delaware in *Kahn v M & F Worldwide Corp.*, 88 A.3d 635 (2013). Determining "a question of first impression," the *M & F* Court held that "business judgment is the standard of review that should govern mergers between a controlling stockholder and its corporate subsidiary, where the merger is conditioned *ab initio* upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders." 88 A.3d at 642, 644. Spelling out in greater detail and with emphasis both the procedure to be followed by the court and the criteria to be applied, the *M & F* Court stated (at 645-46) that:

> in controller buyouts, the business judgment standard of review will be applied *if and only if:* (i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority.
> If a plaintiff can plead a reasonably conceivable set of facts showing that any or all of those enumerated conditions did not exist, that complaint would state a claim for relief that would entitle the plaintiff to proceed and conduct discovery. If, after discovery, triable issues of fact remain about whether either or both of the dual procedural protections were established, or if established were effective, the case will proceed to a trial in which the court will conduct an entire fairness review.

Defendants assert that all the above-stated criteria for the application of the business judgment rule have been met here. They acknowledge plaintiffs' allegations in the Complaint that the Special Committee was not independent, that the Committee did not meet its duty of care, and that the minority stockholders were not fully informed, but they argue that the allegations were either too conclusory to state a claim or that they are belied by the documentary evidence. For example, whereas the Complaint alleges that only Mr. Frankfurt was conflicted, the law presumes the independence of the Special Committee unless the *majority* of the directors had an interest in the outcome, or that the other directors "were dominated or controlled by a materially interested director." *Orman v Cullman,* 794 A.2d 5, 22 (Del. Ch. 2002) quoting *Crescent/Mach I Partners, L.P. v Turner,* 846 A.2d 963, 979 (Del. Ch. 2000). And even as to Frankfurt, defendants cite various cases to support their assertion that plaintiffs' allegations of a prior personal and business relationship between Frankfurt and Lichtenstein of SPLP do not rise to the level of a conflict.

Defendants further assert that the Complaint fails to allege that the Special Committee violated its duty of care, as the focus must be on the decision-making process, as opposed to the merits of the decision, and the test is whether the directors were "grossly negligent". *In re Walt Disney Co. Derivative Litigation,* 907 A.2d 693, 750 (Del. Ch. 2005), *aff'd* 906 A.2d 27 (Del. 2006). Plaintiffs' allegations fail to rise to that level, defendants contend. The Special Committee hired experienced legal counsel and an outside financial advisor who prepared a "fairness opinion" and proceeded in a reasonable manner, meeting multiple times over a period of months.

The process resulted in the negotiation of a fair price, defendants contend, and the basis for the valuation by Duff & Phelps was fully disclosed. In fact, defendants claim, the stockholders were fully informed about all aspects of the Merger. Plaintiffs have failed to point

to any omitted fact that was so significant that there was "a substantial likelihood that the undisclosed information would significantly alter the total mix of information already provided," defendants argue. *Skeen v Jo-Ann Stores, Inc.*, 750 A.2d 1170, 1174 (Del. 2000).

Under the business judgment rule, "the court is precluded from inquiring into the substantive fairness of the merger, and must dismiss the challenge to the merger unless the merger's terms were so disparate that no rational person acting in good faith could have thought the merger's terms were so disparate that no rational person acting in good faith could have thought the merger was fair to the minority." *In re MFW S'holders Litig.*, 67 A.3d 496, 500 (Del.Ch. 2013). Applying this standard, defendants urge the dismissal of this action.

Plaintiffs vigorously oppose dismissal, disputing each and every point raised by defendants, beginning with the standard of review. Rather than the business judgment rule urged by defendants, plaintiffs urge the Court to apply the "entire fairness" standard of review set forth in *Kahn v Lynch Communication Systems, Inc.*, 628 A.2d 1110 (Del. 1994). Quoting *Americas Mining Corp. v Theriault*, 51 A.3d 1213, 1239 (Del. 2012), plaintiffs assert that: "When a transaction involving self-dealing by a controlling shareholder is challenged, the applicable standard of judicial review is entire fairness, with the defendants having the burden of persuasion. In other words, the defendants bear the burden of proving that the transaction with the controlling stockholder was entirely fair to the minority stockholders."

As plaintiffs correctly note, the Delaware Supreme Court in *M&F Worldwide, supra*, held that defendants may escape the entire fairness standard and have the Court apply the business judgment rule applies *if and only if* defendants satisfy all six of the factors specified above (at p 3). Where, as here, the plaintiffs "plead a reasonably conceivable set of facts showing that any or all of those enumerated conditions did not exist, that complaint would state a claim

for relief that would entitle the plaintiff to proceed and conduct discovery." *M&F Worldwide*, 88 A.3d at 645-46.

Turning to the factors, the facts alleged by plaintiffs sufficiently call into question the independence of the Special Committee based on Frankfurt's long-standing personal relationship with Warren G. Lichtenstein, the founder, Chair and CEO of SPLP, as well as their prior business relationship. The two men were college classmates and roommates, roommates after college, and business partners for five years in the predecessor of SPLP. Any conflict on the part of Frankfurt, the Chair of the Special Committee and lead negotiator of the Merger, calls into question the independence of the entire Committee and the fairness of their process.

Plaintiffs have similarly alleged facts sufficient to raise issues as to whether the Special Committee breached its duty of care in negotiating a fair price by allowing Frankfurt to take the lead not only in the negotiations but in the selection of advisors. Questions have been raised as to whether Duff & Phelps, the financial advisor selected by the Committee, was itself conflicted in that it previously did work on behalf of SPLP. In addition, plaintiffs charge Duff with "fundamentally flawed valuation analyses" (Memo at p 19) that, for example, overstated the value of SPLP preferred units while depressing the value of the Company, leading to an inadequate Buyout price for minority stockholders.

Legitimate issues have been raised as to whether the minority stockholders were fully informed as to all material facts. A fact is material "if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *Rosenblatt v Getty Oil Co.*, 493 A.2d 929, 944 (Del. 1985) (quoting *TSC Indus., Inc., v Northway, Inc.*, 426 U.S. 438, 449 (1976). Proof is not required that the omitted information would have caused the stockholder to change his or her vote. *Id.* Plaintiffs point to omitted information such as

Frankfurt's relationship with Lichtenstein, which suggests a lack of independence. They also point to certain financial information and explanations of methodology that should have been included in the Duff fairness opinion, and they cite case law for the proposition that an injunction may lie when defendants fail to accurately disclose how certain calculations were made. *See, e.g., Maric Capital Master Fund, Ltd. v Plato Learning, Inc.*, 11 A.3d 1175 (Del. Ch. 2010).

Accepting the allegations in the Complaint as true, as the Court must on a motion to dismiss, the Court finds that plaintiffs have alleged "a reasonably conceivable set of facts" that raise issues as to whether all six of the *M&F* conditions have been met, thereby allowing this action to survive dismissal and proceed to discovery. As the *M&F* Court stated: "If, after discovery, triable issues of fact remain about [any of the six conditions], the case will proceed to a trial in which the court will conduct an entire fairness review." *Id.* The documents proffered by defendants do not establish a defense as a matter of law, but plaintiffs have a heavy burden to establish any actionable wrongdoing.

The Court now turns to the claims against defendant Frankfurt individually for breach of fiduciary duty. Defendants assert that any claim against defendant Frankfurt individually is barred by the exculpatory provision in the Company's Amended and Restated Certificate of Incorporation, effective as of January 3, 2011 (Fleming Aff, Ex A). That provision, which effectively absolves the Company's directors of any personal liability for monetary damages for breach of fiduciary duty, states in relevant part that:

> **TENTH:** The personal liability of the directors of the Corporation is hereby eliminated to the fullest extent permitted by paragraph (7) of subsection (b) of Section 102 of the General Corporation Law of the State of Delaware …

Citing cases such as *In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022 (Del Ch. 2012), defendants submit that Frankfurt individually is protected by Section 102(b)(7) from any claim

against him personally for damages related to his conduct as a director, and the claims against him must be dismissed, unless the plaintiffs have pled non-exculpated claims for breach of the duty of loyalty, which requires a higher showing than a violation of the duty of care. Similarly, to state a non-exculpated bad faith claim, "a plaintiff must show either an extreme set of facts to establish that disinterested directors were intentionally disregarding their duties, or that the decision under attack is so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith." *In re Chelsea Therapeutics Int'l Ltd. S'holders Litig.*, 2016 WL 3044721 at 7 (De. Ch. May 20, 2016). Defendants assert that plaintiffs have failed to allege sufficient facts to support either type of claim.

Plaintiffs appear to agree that Section 102(b)(7) exculpates a director from personal liability for breach of the duty of care, but not for breach of the duty of loyalty or for bad faith. However, they insist the Complaint sufficiently pleads "facts supporting a rational inference that the director [Frankfurt] harbored self-interest adverse to the stockholders' interests, acted to advance the self-interest of an interested party from whom they could not be presumed to act independently, or acted in bad faith." *In re Cornerstone Therapeutics, Inc.*, 115 A.3d 1173, 1179-80 (Del. 2015); *see also In re Orchard Enters., Inc.*, 88 A.3d 1, 32 (Del. Ch. 2014) (Section 102(b)(7) is intended to eliminate director liability only for duty of care violations but not for other wrongful conduct). They point in particular to allegations that "Frankfurt's undisclosed relationship with Lichtenstein and SPLP, who were on both sides of the Buyout and had a financial interest in acquiring [the Company's] minority shares at the lowest possible price, conflicted with Frankfurt's duties as a director --- and as Chairman of the Special Committee --- to act in the best interest of the corporation and its stockholders. (Memo in Opp at p 31).

Although best practices perhaps suggest that Frankfurt should have disclosed his relationship with Lichtenstein, the Court finds that liability against defendant Frankfurt personally is barred under the circumstances presented here by the above-quoted Article Tenth of the Company's Amended and Restated Certificate of Incorporation and Section 102(b)(7) of the General Corporation Law of the State of Delaware. The cause of action asserted against Frankfurt is denominated as one for breach of fiduciary duty, which is akin to a claim for breach of the duty of care that is indisputably barred by the exculpation clause, the governing statute, and the case law cited by defendants.

While the Complaint does allege within that cause of action (at ¶81) a breach of the "duty of loyalty, in addition to any attendant breaches of the duties of care, good faith, fair dealing or candor," the specific allegations amount to no more than the breach of fiduciary duty claim asserted against the corporate defendant. Frankfurt was at all times acting within the scope of his duties as a director and Chair of the Special Committee, and the Complaint lacks any specific allegation that he somehow benefitted personally from the Merger or otherwise acted in bad faith. While Frankfurt's non-disclosure of his personal relationship with Lichtenstein of SPLP may be considered as part of the Court's evaluation of the Merger, it did not rise to the level of a breach of the duty of loyalty or bad faith so as to subject Frankfurt to personal liability for his role on the Special Committee negotiating the Merger. Thus, the motion to dismiss claims against defendant Frankfurt is granted.

Accordingly, it is hereby

ORDERED that defendants' motion to dismiss this action is granted as to defendant Robert Frankfurt individually, and the Clerk is directed to sever and dismiss the claims against Frankfurt; and it is further

ORDERED that the motion to dismiss the claims against defendant Steel Partners Holdings L.P. is denied; and it is further

ORDERED that defendant Steel Partners Holdings L.P. shall efile an Answer by May 21, 2018 and appear in Room 232 for a preliminary conference on May 29, 2018 at 9:30 a.m.

5/9/2018
DATE

BARRY R. OSTRAGER, J.S.C.

BARRY R. OSTRAGER
JSC

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