IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

JAMES MCRITCHIE Plaintiff, v. MARK ZUCKERBERG, SHERYL K. SANDBERG, ROBERT M. KIMMITT, PEGGY ALFORD, MARC L. ANDREESSEN, ANDREW W. HOUSTON, NANCY KILLEFER, TRACY T. TRAVIS, TONY XU, and META PLATFORMS, INC., Defendants.	:	C.A. No. 2022-0890-JTL

PLAINTIFF'S ANSWERING BRIEF IN OPPOSITION
TO DEFENDANTS' MOTION TO DISMISS

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PRELIMINARY STATEMENT

Conventional Delaware corporations are managed for the benefit of one constituency—the stockholders—with one goal—financial returns. Plaintiff does not challenge that verity. In 2023, however, returns cannot be optimized for the benefit of stockholders if fiduciaries ignore the effect of their decisions on stockholders' portfolios.

Defendants argue that Delaware law demands fiduciaries ignore the effects of their decisions on diversified portfolios and concede that they ignored portfolio effects on Meta's diversified stockholders, despite prominent reports of the economic carnage threatened by Meta's business model and stockholder proposals that they monitor externalities, including a specific proposal for an accounting of the Company's effect on its stockholders' diversified portfolios. *See* Defendants' Opening Brief ("OB") at 10, 13-14, 18.

While fiduciaries have a general obligation to maximize financial value, that obligation must end when it is opposed to stockholder interests. Accordingly, Defendants cannot refuse to consider whether increases in Meta's financial value come from the pockets of typical Meta stockholders through harm to their investments. Just as *Revlon* prioritizes ***stockholder*** return over ***corporate*** cash flows in a sale, fiduciaries must make a good faith effort to address the true cost of corporate operations that tax stockholders' portfolios. Although Delaware courts may not have previously enforced this obligation, they have not rejected it either, and consistent application of longstanding principles demands its recognition. Denying the obligation would deprive fiduciaries of an important tool for serving stockholders; it would also insert corporate law and the courts squarely into the decision-making architecture of corporations, which otherwise permits directors and officers acting in good faith to rationally pursue the best interests of their stockholders.

BACKGROUND

Meta is the largest social media network in the world, with four Platforms—Facebook, Instagram, Messenger and WhatsApp—used by approximately 3.59 billion people every month and 2.82 billion people every day—43% and 35% of the world's population, respectively. Compl. ¶29.[1] Meta undeniably has a global social and economic impact.

A. Meta Leadership Dominated by Concentrated Owner Perspective

1. Zuckerberg Firmly in Control

Zuckerberg's $67.6 billion fortune includes more than 350,000,000 shares of Meta common stock; although those shares account for only 13.6% of the outstanding Meta shares, they have ten times the voting power of publicly held

[1] References herein to the "Complaint" or "Compl." are to the operative Verified Amended Complaint filed on February 7, 2023 (Trans. ID 69093333).

shares, giving him a 54% voting interest and absolute control of the Company. Compl. ¶12.[2] Using that power, he operates unilaterally and without Board guidance on numerous critical issues. *Id.* ¶¶4, 12.[3] Zuckerberg is the controlling stockholder of Meta. *See In re Facebook, Inc. Deriv. Litig.*, Consol. C.A. No. 2018-0307-JTL, Transcript 19:18-20 (May 10, 2023), attached to the Transmittal Affidavit of Gillian L. Andrews ("Andrews Aff.") as **Exhibit A**; *id.* at 26:17-18 ("in each case the road leads to Zuckerberg."), 45:3-4 ("all roads here lead to Zuckerberg."); *United Food & Com. Workers Union v. Zuckerberg*, 250 A.3d 862, 869 (Del. Ch. 2020) ("Mark Zuckerberg is . . . controlling stockholder of nominal defendant Facebook, Inc.").

When the original Complaint was filed, the Meta Board included nine directors named as Defendants here: Mark Zuckerberg, Sheryl K. Sandberg, Robert M. Kimmitt, Peggy Alford, Marc L. Andreesen, Andrew W. Houston, Nancy Killefer, Tracy T. Travis and Tony Xu. Compl. ¶¶16-24.

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[2] Meta Form 8-K at 67 (June 1, 2023) (Zuckerberg's 13.6% ownership calculation). https://www.sec.gov/ix?doc=/Archives/edgar/data/1326801/000132680123000050/meta-20230414.htm#id8aff64984c64035b3e93501af472b14_43.

[3] According to recent public filings, that control position has increased to 61%, due to the buybacks detailed in the Complaint. Meta Form 14A at 67 (Apr. 14, 2023), https://www.sec.gov/Archives/edgar/data/1326801/000132680123000050/meta-20230414.htm.

In the recent *Facebook* opinion, the Court found that Sandberg, Alford, Andreesen and Houston are not independent from Zuckerberg for purposes of demand futility. Ex. A at 29:15-32:7; *see also Zuckerberg*, 250 A.3d at 893 (Sandberg and Andreessen unable to "exercise disinterested and independent judgment" due to their fealty to Zuckerberg); *id.* at 873 (Andreesen "regularly engaged in back-channel communications with Zuckerberg about what the Committee was doing."). Zuckerberg, Sandberg, Alford, Andreesen, and Houston constituted a majority of the Company's Board during the relevant time period.

With Zuckerberg firmly at the helm and four of the other eight directors lacking independence, any independent directors are effectively sterilized and Zuckerberg exercises absolute control over decision-making at Meta.[4] In 2019-2020, Zuckerberg exercised his high-voting power to reconstitute Meta's Board except for Zuckerberg's closest allies, Sandberg, Andreesen and Theil, who remained. Compl. ¶39. The five other former Board members, Jeffrey Zients, Kenneth Chenault, Reed Hastings, Erskine B. Bowles and Susan D. Desmond-Hellmann, all found to be independent of Zuckerberg, left expressing frustration with the control Zuckerberg wielded and the Company's trajectory. *Id.* ¶¶25, 39-40; *Zuckerberg*, 250 A.3d at 892-900.

[4] Plaintiff does not concede the independence of Killefer, Kimmitt, Travis or Troy.

2. Power Shared with Sandberg

Sandberg's key role was evidenced by the Company's Civil Rights Audit, where it was noted that the scope of Meta's engagement in addressing civil rights violations were being controlled by Sandberg and Zuckerberg, including macro-level safety decision-making. Compl. ¶75. Only she and Zuckerberg were permitted to impose safety requirements on certain celebrity users. *Id*. ¶52. At times, she was considered one of the two most important executives in the Company. Ari Levy, *Sheryl Sandberg Was Facebook's Adult in The Room, but It's Always Been a Zuckerberg Production* (June 1, 2022), https://www.cnbc.com/2022/06/01/sheryl-sandberg-was-adult-in-room-of-zuckerberg-production-at-facebook.html ("In 2012, . . . the company's IPO filing named her as one of two key people.").

3. *Zuckerberg and Sandberg Have Immense Undiversified Wealth in Meta Shares*

Zuckerberg owns $67.6 billion of Meta common stock. Compl. ¶12. Sandberg has been compensated with stock over fourteen years; in 2021, she received $93 million in value upon vesting and settlement of restricted stock units, while retaining $115 million in unvested shares or share equivalents. *Id.* As of June 2, 2022, Sandberg held about 1,400,000 shares of Meta stock "worth just under $290 million … and account[ed] for about 17% of her net worth …. About three-quarters of Sandberg's wealth comes from Facebook stock sales over the years."[5]

Sandberg reported to Zuckerberg. It is reasonably conceivable that ownership of $67.6 billion and compensation with hundreds of millions of dollars in equity, respectively, would skew the interests of Zuckerberg and Sandberg towards the financial success of the Meta and away from that of a typically diversified portfolio.

4. The Company is Primarily Owned by Institutions, Many of Whom Are Represented by Diversified Investors

Five institutional holders own 27.84% of the Company's stock. Compl. ¶41.[6] As of June 9, 2023, NASDAQ reports that an estimated 75% of the Company's Class A shares (low-voting stock owned by the public) were held by institutions.[7] Many of these investors are legally required to diversify their investment plans. *Id.* ¶42 n.24. The diversification mandate follows modern portfolio investing theory, which shows that investors can obtain the increased returns available from risky securities while reducing their overall risk—a prudent approach allowing average investors to

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[5] https://www.forbes.com/sites/jemimamcevoy/2022/06/02/billionaire-sheryl-sandberg-has-unloaded-more-than-90-of-her-facebook-stock-over-the-past-decade/?sh=5b405bfe5889.

[6] *See also* FAQ for Forms 13F, https://www.sec.gov/divisions/investment/13ffaq (institutional investors required to disclose holdings of exchange-traded stocks).

[7] https://www.nasdaq.com/market-activity/stocks/meta/institutional-holdings.

own common stock. *Id.* The greatest factor determining diversified portfolio returns is overall market performance, not how the individual companies in a portfolio perform. *Id.* ¶43. A diversified portfolio will rise and fall with GDP, as a measure of the economy's intrinsic value. *Id.* ¶45. But negative externalities produced by companies can significantly reduce GDP. *Id.*

5. Zuckerberg's Control Is Used to Promote Company Profits over User Safety

Zuckerberg used his control to ensure that maintaining user engagement remained paramount; actions designed to increase safety that would decrease user engagement were not an option. Compl. ¶¶52, 55-56, 59-60, 64-66, 69, 82-83; *id.* ¶88 (Zuckerberg "exemplifies his relentless determination to ensure Facebook's dominance, sometimes at the expense of his stated values"); *id.* ¶89 (former employees reported Zuckerberg's "influence goes far beyond what he has stated publicly, and is most felt in countless lesser-known decisions that shaped Facebook's products to match Zuckerberg's values — sometimes, critics say, at the expense of the personal safety of billions of users."); *id.* ¶98 ("the CEO's unique degree of control over Facebook forces him to bear ultimate responsibility for a litany of societal harms caused by the company's relentless pursuit of growth."). Zuckerberg vetoed an algorithm change that would address "misinformation, toxicity, and violent content [that] are inordinately prevalent among reshares" because it would reduce traffic. *Id.* ¶¶65, 69. Zuckerberg assumed responsibility for the Company's policies relating to voter suppression and calls for violence by state actors. *Id.* ¶75.

The concentration of their personal fortunes in Meta shares means Zuckerberg and Sandberg materially benefit from Meta operations that increase Company value but degrade the economy, while typical diversified Meta stockholders would be financially harmed by such strategies. Because a majority of the Board is beholden to Zuckerberg and subject tohis "concentrated stockholder" perspective of what is in the stockholders' best interests, even if it conflicts with the interests of Meta's diversified stockholders.

B. Meta Governance Eschews Consideration of Systemic Risk

1. Traffic and Engagement are Paramount

Advertising revenues drive Meta's bottom line and are directly tied to user engagement. Meta "generate[s] substantially all of [its] revenues from advertising" and the first risk factor listed in Meta's 2022 Annual Report is loss of user engagement: "***If we fail to retain existing users or add new users, or if our users decrease their level of engagement with our products, our revenue, financial results, and business may be significantly harmed***." Compl. ¶32 (emphasis in original). Zuckerberg, with final say over every Meta decision, does not permit tradeoffs of traffic to improve the Company's social or economic impact. *Id*. ¶66.

2. *The Company's Governance Structure Ignores Risks That Do Not Directly Impact the Company*

Despite its global reach, Meta's key governance structures ignore the cost its externalities impose on its own stockholders.

Its Corporate Governance Guidelines, adopted "with a view to enhancing long-term value for Meta shareholders," indicate no regard for the effect of Company operations on diversified stockholder portfolios: the Board and management interpret "long-term value for Meta shareholders" solely in terms of Meta's financial value. Compl. ¶33; OB 1, 10.

The Company's risk management strategy focuses on risks such as community safety and human rights, but only if they pose risks ***to the Company itself***. *Id.* ¶35. There is no independent mandate to monitor or mitigate risks the Company's operations and strategies pose to the global economy or diversified stockholders. *Id*. ¶36. There are no parameters for balancing risks that are minor to the Company but material to Meta's diversified stockholders. *Id*.

Compensation structures follow a similar pattern, incentivizing executives to focus solely on Company financial performance, even if such focus harms the broader economy and, consequently, portfolios of its diversified stockholders. *Id*. ¶37. When assessing the risks of its compensation program, the Board decided not to investigate whether, by awarding millions in equity to executives, the program might incentivize operations that threaten the economy, and thus portfolios of the

Company's diversified stockholders; instead, Board compensation decisions only reflect stand-alone risks to the Company. *Id.*

Not a single of the above parameters is designed to consider the diversified interests of Meta stockholders; instead, each is structured to keep the Company's operations focused on profitability. *Id*. ¶37. The Board could change this at any time but, with Zuckerberg firmly at the helm and with a majority of its members beholden to him, it has chosen not to, even when requested by the Company's own stockholders. *Id*. ¶38; *see also id.* ¶102.

C. <u>Negative Externalities Harm Meta Stockholders' Diversified Portfolios</u>

1. Press Reports Demonstrate Absolute Priority of Profit over Portfolio Effects

In a series of articles entitled *The Facebook Files* published in *The Wall Street Journal*, the negative externalities Meta's Platforms visit upon society were well publicized. Compl. ¶¶49-98. Those articles included information obtained from whistleblower testimony and internal Company documents demonstrating that Meta knew that elements of its Platforms harm users and threaten the rule of law, and that decisions about such features were made without considering the costs imposed on Meta's diversified stockholders. *Id*. ¶49.

On September 13, 2021, the first article was published. It revealed a program called XCheck allowed celebrities to bypass Meta's standards. *Id*. ¶50. XCheck was part of a pattern of harmful practices that Meta continued "for fear of hurting its business." *Id*. ¶56. Imposing safety rules on celebrity users sometimes requires the permission of Sandberg or Zuckerberg. *Id*. ¶52.

2. Engagement Model Exacerbates $16 Trillion Mental Health Issue

The second article published on September 14, 2021, reported that internal analyses at Meta showed Instagram use led to teenage mental health issues. Comp. ¶57. Internal reports noted the Platform made "body images worse for one in three teenage girls." *Id.* According to the article, Meta prioritized its finances over mental health: "Expanding its base of young users is vital to the company's more than $100 billion in annual revenue, and it doesn't want to jeopardize their engagement with the platform." *Id*. ¶58.

Mental health will place an estimated $16.3 trillion burden on the economy between 2011 and 2030.[8] *Id*. ¶62. Defendants refuse to consider the burden this places on the portfolios of the Company's diversified stockholder base. *See id*. ¶¶43-45.

3. Tactics to Increase Engagement and Lower Costs Threaten Rule of Law Globally, Challenging Economic Growth

A third article was published on September 15, 2021, detailing how the Facebook algorithm was altered to emphasize "meaningful social interactions" ("MSI"). Compl. ¶63. The article, along with reporting in *The Washington Post*,

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8 The Complaint incorrectly stated this timeframe as 2011 to 2020. Compl. ¶62.

clarified that the change addressed a drop in user interaction, but made Facebook "an angrier place." *Id*. ¶65. One internal memo noted "[m]isinformation, toxicity, and violent content are inordinately prevalent among reshares." *Id.* The Company rejected fixes because doing so would reduce traffic and revenue. *Id.* ¶66. Zuckerberg would not permit the Company to "tradeoff" traffic in order to improve the Platform's economic effect. *Id*. The changes degraded political discourse across Europe and Asia. *Id*. ¶67-68. Meta consciously chose traffic and revenue over limiting harm: when employees figured out how to address the issue, Zuckerberg vetoed the algorithm change because it would reduce traffic. *Id.* ¶69.

The Facebook Files were not necessary to warn Defendants of the danger. One observer noted before its publication, "Facebook's algorithms are addictive by design and exploit negative emotional triggers. Platform addiction drives earnings, and hate speech, lies and conspiracy theories reliably boost addiction." Robert Frank, *The Economic Case for Regulating Social Media*, N.Y. TIMES, Feb. 11. 2021.[9]

While the first three *Facebook Files* articles demonstrated the Company's traffic-at-any-cost mentality, the fourth, published on September 16, 2021, showed that cost-saving was also prioritized over addressing external harm. Compl. ¶71.

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[9] The Court may take judicial notice of publicly available facts set forth in media reports. Del. R. Evid. 201(b)(1); *see also In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 170 (Del. 2006).

The article reported on Meta's weak responses to drug cartels and human traffickers that use Platforms for illegal activities. *Id*. The Company was not spending enough money to police the Platforms, leading to promotion of human slavery, sex trafficking, ethnic violence, and violent drug cartels. *Id*. ¶¶71-75. In some cases, Meta simply chose not to spend money on translation services. *Id*. ¶78.

Meta's policies to drive traffic and save money threaten the rule of law around the world, by degrading political discourse, enabling law breaking, and stirring ethnic hatred. *Id*. ¶74. ("when riots broke out in Delhi last year, calls to violence against Muslims remained on the site" despite Meta being " told and they didn't do one damn thing about it"). In addition to the tragic human cost of such policies, undermining the rule of law undermines economic growth, *id*. ¶79, threatening the returns of Meta's diversified stockholders, for whom up to 91% of returns are determined by overall market returns, which are a product of the economy's performance. I*d*. ¶¶43-45.

4. Meta Disregarded the Impact its Business Model Had on the COVID-19 Economic Crisis

A fifth article detailed how Meta's policies failed to manage the messaging its Platforms transmitted around COVID-19 vaccines. Compl. ¶80 ("Our ability to detect vaccine-hesitant comments is bad in English, and basically non-existent elsewhere."). The article concluded that the harm resulted from the underlying business model. *Id*. ¶84 ("The vaccine documents are part of a collection of internal communications … that offer an unparalleled picture of how Facebook is acutely aware that the products and systems central to its business success routinely fail and cause harm.”).

Company personnel recognize that vaccine hesitancy is “rampant” on Company Platforms and the “potential to cause severe societal harm.” *Id.* ¶80. That harm was a clear danger to GDP, with the average country losing 7.3% of GDP to COVID-19 in 2020. *Id.* ¶86. Meta ignored the risk its focus on revenue placed on the global economy, a risk borne by its own diversified stockholders.

D. Meta’s Board Rejected Numerous Stockholder Proposals Addressing Negative Externalities

Meta ignored stockholder proposals calling for action on these societal and economic harms as well. Compl. ¶¶99-132. At Meta’s 2022 Annual Meeting, four proposals focused specifically on the types of harms that negatively impact diversified investment portfolios: the External Costs Proposal, the Metaverse Proposal, the Community Standards Proposal and the Human Rights Proposal (“Stockholder Proposals”). *Id.* ¶¶100-102. The Board encouraged stockholders to vote against each Proposal. *Id.* ¶100.

The External Costs proposal highlighted the risk that maximizing engagement would damage economic systems that undergird investment performance generally:

> **RESOLVED,** shareholders ask that the board commission and disclose a report on (1) risks created by Company business practices that prioritize internal financial return

> over healthy social and environmental systems and (2) the manner in which such risks threaten the returns of its diversified shareholders who rely on a productive economy to support their investment portfolios.

Id. ¶102; *see also* ¶114 (Metaverse Proposal states "Meta is dedicating significant resources to the metaverse without fully understanding its potential risks and negative impacts"); *id.* ¶120 (Community Standards Proposal addressed mental health crises and violence); *id.* ¶128 (Human Rights Proposal sought report on impacts of "advertising policies and practices."). In opposing these Stockholder Proposals, the Board never considered the impact of the conduct on the portfolios of Meta's diversified stockholders. *Id.* ¶¶102, 119, 127, 132. Given their opposition, it can be reasonably inferred the Board did not implement the Stockholder Proposals.

Instead of using resources to address harms, the Board authorized billions for share repurchases. Compl. ¶¶136-143, 165. In 2021, the Company distributed $44.81 billion to stockholders through repurchases, and as of the end of that year the Board had authorized an additional $38.79 billion for repurchases. *Id.* ¶30.

While the Board highlighted safety expenditures of $5 billion in response to the External Costs Proposal, it did not acknowledge the decision to spend ***ninefold*** that amount on repurchases that year, rather than further addressing safety. *Id*. ¶142. The Company could have doubled safety spending by reducing buybacks 11%. *Id.*

Some of the repurchase funds could have purchased more translation services, content monitoring, or algorithm research to decrease economic risk. While such actions might decrease profits and the amount available for repurchases, they could benefit the typical diversified Meta stockholder—but the Defendants will never know if they do not ask.

E. Charging into the Metaverse

In October 2021, the Company rebranded as Meta, adopted the term "metaverse" as its theme, and undertook to provide "useful and engaging products that enable people to connect and share with friends and family." Compl. ¶133. The Company intends to double its use of artificial intelligence ("AI") to increase user engagement in the "metaverse." *Id.* ¶134.

The Company will double down on its strategy of no-holds-barred engagement, turbocharged with virtual reality and more AI. *Id.* There is no indication that any thought will be given to the potential for increased risk that strategy will pose to the systemic health that undergirds diversified investments. As Zuckerberg stated, the only factor considered is the bottom line: "Since we're already efficient at monetizing most of these formats, this should increase our business opportunity . . .." *Id.*

ARGUMENT

At the pleading stage, Plaintiff is entitled to all reasonable inferences that can be drawn from the allegations in the Complaint. *See Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 896-97 (Del. 2002). "The standards governing a motion to dismiss for failure to state a claim are well settled: (i) all well-pleaded factual allegations are accepted as true; (ii) even vague allegations are 'well-pleaded' if they give the opposing party notice of the claim; (iii) the Court must draw all reasonable inferences in favor of the non-moving party; and (iii) dismissal is inappropriate unless the plaintiff would not be entitled to recover under any reasonably conceivable set of circumstances susceptible of proof." *Id.* (citations omitted). "Because 'any attempt to require specificity in pleading a condition of mind would be unworkable and undesirable,' a defendant's state of mind and knowledge may be averred generally. … The facts alleged need only support a litigable inference of disloyalty or bad faith. The inference need not be the only possible inference, nor even the most likely inference. The inference need only be reasonably conceivable." *Voigt v. Metcalf*, 2020 WL 614999, *26 (Del. Ch.) (cleaned up).

Delaware follows the liberal notice pleading standard, requiring only "a short and plain statement of the claim showing that the pleader is entitled to relief." Rule 8(a)(1). "'So long as claimant alleges facts in his description of a series of events from which a claim may reasonably be inferred and makes a specific claim for the relief he hopes to obtain, he need not announce with any greater particularity the precise legal theory he is using.'" *Dow Chem. Co. v. Organik Kimya Holding A.S.*, 2018 WL 2382802, *4 (Del. Ch.) (quoting *Michelson v. Duncan*, 407 A.2d 211, 217 (Del. 1979)). Plaintiff asserts direct claims against the Defendants for breach of fiduciary duty and the Complaint is therefore not subject to the heightened pleading standards of Rule 23.1. *See MCG Cap. Corp. v. Maginn*, 2010 WL 1782271, *4 (Del. Ch.).

The 91-page Complaint alleges substantial facts, including the nature of the externalities and threats they pose to Meta stockholders' diversified portfolios. It describes literature from the fields of law, finance, and economics showing that a reasonable corporate fiduciary seeking to act for the benefit of stockholders would believe it necessary to consider how to account for the impact of such externalities.

I. DEFENDANTS MUST MANAGE THE COMPANY FOR THE BENEFIT OF ITS STOCKHOLDERS

A. The Motion Depends Upon a Threshold Issue

Plaintiff requests relief on behalf of diversified Meta stockholders because their portfolios are threatened by Meta's business model. Defendants' arguments for dismissal rely upon a threshold proposition: ***fiduciaries have no duty (or ability) to consider the costs of their decisions on the typical stockholders' portfolios, even if those costs far outweigh any benefit received as holders of company shares***. *See* OB 1 ("[F]iduciaries of Delaware corporations do not owe a duty to oversee, consider, or protect a stockholder's investments in other companies"); *id.* 10 ("Defendants have no duty to consider Plaintiff's investments in other companies.").

Defendants thus admit they willingly ignore the effect of their decisions on diversified portfolios of Meta stockholders. Indeed, they argue that considering these effects would violate their obligations. OB 13-14. If Defendants are wrong about the threshold issue, then they have consciously disregarded a cognizable stockholder interest and have stated their intention to continue to do so, constituting *per se* violations of their fiduciary duties.

Defendants' assert that precedent speaks to this threshold issue, foreclosing Plaintiff's claims, stating "[t]he Amended Complaint does not state a claim under decades-old, black-letter Delaware law." OB 3. Yet Defendants cite no precedent on the issue. Instead, they rely upon cases establishing that fiduciaries must maximize value ***for the benefit of stockholders***, and Plaintiff does not contest that. Instead, Plaintiff contests Defendants' assertion that fiduciaries must ignore the reality that rational investors diversify their holdings to mitigate the risk that accompanies the high return of residual equity. Requiring fiduciaries to ignore the diversified nature of modern shareholdings would erase "for the benefit of," turning the explicitly qualified maximization concept into a dangerous absolutism—requiring Delaware corporations to destroy their stockholders' entire neighborhoods to upgrade a single home.

B. <u>Why Maximization?</u>

Defendants' assertion that fiduciaries cannot protect stockholder investment in other companies, OB 1, 10, 13-14, glosses over the purpose of value maximization, namely, ensuring that fiduciaries protect stockholders. Fiduciary duties respond to the surrender by equity holders of the right to direct their capital:

> Equitable principles act in those circumstances to protect the beneficiaries who are not in a position to protect themselves. One of the fundamental tenets of Delaware corporate law provides for a separation of control and ownership. The board of directors has the legal responsibility to manage the business of a corporation ***for the benefit of its shareholder owners***. Accordingly, fiduciary duties are imposed on the directors of Delaware corporations to regulate their conduct when they discharge that function.

Malone v. Brincat, 722 A.2d 5, 9 (Del. 1998) (emphasis added); *In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 36 (Del. Ch. 2013) ("When exercising their statutory responsibility, the standard of conduct requires that directors seek 'to promote the value of the corporation ***for the benefit of its stockholders***.'") (emphasis added); *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34 (Del. Ch. 2010) ("Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation ***for the benefit of its stockholders***.") (emphasis added).

Value maximization is a means to protecting stockholders, not a freestanding end, as explained in *Trados*:

> [B]y increasing the value of the corporation, the directors increase the share of value available for the residual claimants. Judicial opinions therefore often refer to directors owing fiduciary duties "to the corporation and its shareholders." . . . This formulation captures the foundational relationship in which directors owe duties to the corporation ***For the ultimate benefit of the entity's residual claimants***. ***Nevertheless, "stockholders' best interest must always, within legal limits, be the end.***" . . . In terms of the standard of conduct, the duty of loyalty therefore mandates that directors maximize the value of the corporation over the long-term ***for the benefit of the providers of equity capital*** ….

73 A.3d at 36-37 (emphasis added).

C. Maximizing Value Must Yield to Stockholder Interests as Investors When Fiduciaries Determine the Two Conflict

The precedent most associated with value maximization value is *Revlon v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986). However, the case illustrates that the mandate to maximize the value of a corporation must yield to stockholder interests when the two diverge. *See id.* at 182.

In *Revlon,* defendant directors sought to account for the interests of debtholders while selling the corporation, even if doing so reduced the cash sale price for stockholders. *Id.* The Supreme Court held that because the directors' duty was owed only to stockholders, other constituencies could be considered only to create stockholder value. *Id.* Because the stockholders were being cashed out, accommodating the noteholders could not create such value: "The duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit." *Id*. Because "nothing remained for Revlon to legitimately protect, and ***no rationally related benefit thereby accrued to the stockholders***" the Court found that "obtaining the highest price ***for the benefit of the stockholders*** should have been the central theme guiding director action." *Id.* at 182-83 (emphasis added).

Revlon established that, while directors are generally charged with increasing the value of the corporation, the obligation is only shorthand for protecting stockholders' interests. In a cash sale, stockholders no longer benefit from preservation of the corporation's value, so the general rule of maximizing ***company*** value was discarded in favor of the rule of maximizing immediate ***share*** price. *Id.* at 182. *Revlon* instructs directors to prioritize the interests of stockholders when they diverge from the interests of the corporation as an entity:

> I take it as non-controversial that, under established and conventional conceptions, directors owe duties of loyalty to the corporation and to the shareholders; that ***this conjunctive expression is not usually problematic because the interests of the shareholders as a class are seen as congruent with those of the corporation in the long run*** ….
>
> There is a time, however, when the board's duty becomes more targeted and specific and its range of options becomes narrower. … In that circumstance, the Supreme Court held that the board's duty was the single one: to

> exercise its judgment in an effort to secure the highest price available[.]

TW Servs., Inc. v. SWT Acquisition Corp., 1989 WL 20290, *7 (Del. Ch.) (emphasis added). In other words, when maximizing the value of the corporation is no longer in the best interests of stockholders, fiduciaries should respond accordingly. In this case, Defendants failed to recognize that the interests of the Company in maximizing its own value have diverged from the interests of Meta's diversified stockholders, just as the interest of a target company can diverge from the interests of its stockholders.

Allen v. El Paso Pipeline GP Co., L.L.C, 113 A.3d 167 (Del. Ch. 2014) ("*Allen II*"), is another case where this Court found that fiduciaries must protect equity holders' interests when they diverge from entity interests. *Id.* at 180. The plaintiff argued that even if the amount paid for assets sold to a limited partnership were fair to the company, it was unfair to the limited partners because of the manner in which the profits generated by the new assets were to be split between the limited partners and the affiliates of the general partner. *Id.* at 181. In an earlier ruling denying defendants' motion to dismiss, the Court explained that "at a pleading stage, it's difficult to say 'Ah, that special committee was just there to look at some abstraction called the partnership. And if it believed that the transaction was unfair to the limited partners of the limited partnership, it could approve it as long as at some abstract level the transaction was, in their mind, fair.'" *Allen v. El Paso Pipeline GP Co.,* *L.L.C.*, C.A No. 7520-CS, Transcript at 41:12-20, attached as Andrews Aff., **Exhibit B**; *cf. Theodora Holdings Corp. v. Henderson*, 257 A.2d 398, 405 (Del Ch. 1969) (relatively small cost of charitable contribution to corporation outweighed by "providing justification for large private holdings, thereby benefiting plaintiff [stockholder] in the long run.").

The conduct in the Complaint is another variant of the conflict alleged in *Allen II*: in each case "value" is added to the company, but at the expense of some or all equity holders. Defendants cite to *Allen II* for the proposition that Defendants must seek 'to promote the value of [Meta] for the benefit of its stockholders.'" OB 11 (quoting *Allen II*, 113 A.3d at 179-80). There the Court granted summary judgment ***because plaintiffs had conceded that the limited partnership units would increase in value*** after the asset purchase, *Allen II*, 113 A.3d at 182, suggesting that if the transaction had in fact harmed the limited partners while benefitting the company, i.e., if the interests of the company and the residual equity holders had diverged, then the rule of value maximization would not hold.

D. The Interests of Diversified Investors Not Always Served by Maximizing Company Value

1. Common Stock Ownership is Inextricably Linked to Diversification

Smart investors diversify. *See generally*, Burton G. Malkiel, *A Random Walk Down Wall Street* (2015). Diversification allows investors to obtain the increased returns available from risky securities while limiting overall risk: "Economists are famous for pronouncing gloomily that 'there's no such thing as a free lunch.' Yet finance theory does offer a free lunch: the reduction in risk that is obtainable through diversification." John Y. Campbell, *Diversification: A Bigger Free Lunch* (July 7, 2000), https://www.sfu.ca/~kkasa/diversification.pdf; *see* Jeffrey N. Gordon, *Systematic Stewardship*, 47 Jour. Corp. Law 627, 629 (2022) ("Risk that pertains to a particular company, so-called 'idiosyncratic' risk can be diversified away; risk that will affect returns throughout the portfolio, 'systematic risk,' remains.").

The laws that govern institutional investors often require such diversification. *See* 29 U.S.C. § 1104(a)(1)(C) (federally regulated retirement plan fiduciaries must "diversify[] the investments of the plan"); Uniform Prudent Investor Act, §3 ("trustee shall diversify the investments of the trust unless the trustee reasonably determines that, because of special circumstances, the purposes of the trust are better served without diversifying"); Roger Urwin, *Pension and Fiduciary Investing and Its Impacts on Sustainable Investing*, 277 (Cambridge Handbook of Institutional Investment and Fiduciary Duty 2014) ("[T]hose who manage investments on behalf of others are bound by a number of fiduciary obligations [including] *[d]iversification*: diversify according to the principles of modern investment theory.") (emphasis in original); James P. Hawley, *et al.*, *Reclaiming Pension Fund Fiduciary Duty Fundamentals*, 636 (The Routledge Handbook of Responsible

Investment 2016) ("Fiduciaries are generally required to discharge their duties . . . with the care, skill and prudence exercised by similar fiduciaries, including as to diversification of . . . .").

Investors without fiduciary obligations are not subject to such laws, but remain subject to the realities of investing, so that any investor interested in optimizing risk and return can obtain the "free lunch" of diversification. While not every investor in a widely traded company may be fully diversified, it is a reasonable pleading-stage inference that most of them are, and that those who are not have idiosyncratic reasons for doing so. *Joy v. North*, 692 F.2d 880, 886 (2d Cir 1982) ("Given mutual funds and similar forms of diversified investment, courts need not bend over backwards to give special protection to shareholders who refuse to reduce the volatility of risk by not diversifying."); *Cf.* Richard Booth, *Stockholders, Stakeholder, and Bagholders (or How Investor Diversification Affects Fiduciary Duty)*, 53 Bus. Law. 429, 430 (1998) ("Rational investors diversify.").

Risk reduction inextricably links diversification to the ownership of common stock, which combines the unlimited upside of residual equity with its high-risk, first loss status. For many, ownership of securities like Meta's common stock would be too risky without diversification. Before the advent of Modern Portfolio Theory ("MPT"), which demonstrates the safety of equity ownership in a diversified portfolio, some stockholders were precluded from owning stock.

> For the history of [US public pension funds], until MPT, state legislatures restricted the types of securities that could be owned. For example, stocks were considered risky and often prohibited. . . . . Only in 1996 in the US did the states of Indiana, West Virginia, and South Carolina, the last states to have such restrictions, end the prohibition against their pension funds investing in stocks. . . . . With the rise of MPT's more holistic portfolio theory, all states have now adopted some form of diversification as law, theoretically anchored in MPT.

Jon Lukomnik, *et al.*, *Moving beyond Modern Portfolio Theory: Investing that Matters*, Ch. 1 (Routledge 2021); Hawley, *supra* at 635 ("As recently as the 1970s, stock investments were widely viewed as imprudent for trust fiduciaries.").

Despite the ubiquity of diversification, Defendants refer to Meta's "so-called 'diversified stockholders'" as a "fiction." OB 1. But it is reasonably conceivable that a significant number, if not the majority of, Meta's non-insider investors, have diversified their portfolios, particularly the roughly 75% held by institutions. Few investors can afford to "bet it all" (or even a large portion of it) on Meta stock without talking untenable risks—the privilege to do so is in the province of wealthy individuals, like Zuckerberg and Sandberg, for whom the downside risk of high concentration is financially and legally acceptable. *See* Gregory Scott Crespi, *Maximizing the Wealth of Fictional Shareholders: Which Fiction Should Directors Embrace?*, 32 Jour. Corp. Law 383, 390 (2007) ("While this fictional diversified shareholder concept obviously does not accurately reflect the circumstances of each actual shareholder of a particular corporation, given the reality of widespread investor diversification, it is nevertheless likely to be a somewhat more accurate approximation to the actual circumstances of public corporation shareholders than is the fictional undiversified shareholder concept.”).

2. *For Diversified Investors, the Significance of Individual Company Performance is Overshadowed by Overall Economic Performance*

For a diversified Meta stockholder, the critical factor determining financial return will not be how Meta or any other individual company performs (“alpha”), but rather how the market performs as a whole (“beta”).[10] Compl. ¶43. “Beta drives some 91 percent of the average portfolio’s return.” *Id.*; *see also* Raj Thamotheram, *et al.*, *Whose Risk Counts?*, 212 (Cambridge Handbook*, supra*) (“about 80% of the ability of a fund to meet its liabilities comes from the beta”).

Over time, beta is influenced chiefly by the performance of the economy itself, because the value of the investable universe equals the percentage of the economy that companies in the market represent. *Universal Ownership: Why Environmental Externalities Matter to Institutional Investors*, 59 (2011), https://www.unepfi.org/fileadmin/documents/universal_ownership_full.pdf.

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[10] This use of “beta” differs from its technical meaning, i.e., the difference between overall market volatility and the volatility of an individual security. However, literature describing the importance of overall market returns to investors uses the term to contrast market return with alpha, the individual security return.

While valuation multiples rise and fall, they revert to a mean, leaving GDP as the key determinant of diversified portfolio value: "The long-term price of a universally-owning institutional investor's portfolio represents the Universal Owner's part of the appropriately discounted sum of all future GDP proportions of corporations. … ***[T]he relationship between GDP and the price of the portfolio of a Universal Owner is linear in the long term.***"[11] *Id.* (emphasis added).

As Warren Buffet explains, the ratio of total market capitalization to GDP "is probably the best single measure of where valuations stand at any given moment." Warren Buffett, *et al.*, *Warren Buffett on The Stock Market*, Fortune (Dec. 10, 2001), https://archive.fortune.com/magazines/fortune/fortune_archive/2001/12/10/314691/index.htm; *see also* James Hawley, *et al.*, *The Rise of Fiduciary Capitalism: How Institutional Shareholders Can Make America More Democratic* (2000), at xv ("a universal owner's cumulative long-term return is determined not merely by the performance of each individual firm it owns, but by the performance of the economy as a whole."). In short, threatening GDP threatens diversified portfolios.

[11] "Universal owners" are "the [i]nstitutional investors—pensions, retirement funds, mutual funds [that] all hold highly diversified long-term portfolios that encompass the global market." Christopher Marquis, *Better Business*, 24 (Yale 2020).

3. Meta's Operational Decisions Undermine Beta

Defendants are promoting Company returns at significant risk to the overall market returns upon which the class depends. Systemic problems to which Meta contributes have economic impact. The Complaint recites examples of Company practices that undermine the rule of law, threatening GDP as demonstrated by one recent study:

> We consider 134 countries during the period 1984-2019 and find a significant positive relation between Rule of Law (law and order provided by police and courts, respect for private property rights) and GDP per capita. Notably, this positive relation has improved over time.

Compl. ¶79; *see also* United Nations Global Compact, *Do Business in Ways that Benefit Society and Protect People*, https://www.unglobalcompact.org/what-is-gc/our-work/social ("a lack of social development, including . . . weak rule of law, can hamper business operations and growth.").

Plaintiff has also shown how the Company threatened the mental health of users and cites corresponding evidence for the cost of mental health disorders to the real economy. *See* Compl. ¶62. Facebook contributed to increased vaccine hesitancy, and prolonging COVID creates significant risk to GDP. *Id.* ¶86. Meta's management understood that its operations led to systemic harm but chose to continue the practices because they increased engagement and revenue. *Id.* ¶¶90-

98. Those systemic harms undermine GDP and the overall market returns upon which class members depend to meet their financial goals.

In addition to these examples of past harm, looking forward, the Company does not manage for risks that its operations might pose to the economy and its diversified stockholders, no matter the magnitude, despite the unprecedented reach of its Platforms.

The relationship between GDP, systemic risks, and market returns means that Meta's diversified investors cannot avoid common risks almost all companies face, and that are embedded in the economy. One recent work explained that these systemic risks inevitably "swamp" any alpha strategy:

> It is not that alpha does not matter to an investor (although investors only want positive alpha, which is impossible on a total market basis), but that ***the impact of the market return driven by systematic risk swamps virtually any possible scenario created by skillful analysis or trading or portfolio construction***.

Beyond Modern Portfolio Theory, supra, Ch. 5 (emphasis added).

This interaction between Meta's externalities and the financial returns of its diversified stockholder base can be represented as follows:

Beta is more important to portfolio performance than alpha, and pursuit of alpha by individual companies can threaten beta. Given modern investing practices, that means that the effect that Meta has on the economy can be more important to most of its investors than its own financial performance. Thus, when acting to create value at Meta "for the benefit of" its stockholders, Defendants must consider and, if appropriate, account for those externalities when decisions are likely to have large economic consequences.

4. Diversification Is Critical Aspect of Equity Ownership

Supporting the argument that they cannot consider the impact of Meta's business model on Meta's diversified stockholders, Defendants cite *Riblet Products Corp. v. Nagy*, 683 A.2d 37, 37 (Del. 1996), for the proposition that "although fiduciaries owe 'duties to minority stockholders *qua* stockholders, those duties are not implicated when the issue involves the rights of the minority stockholder [in a different capacity].'" OB 12.[12] Defendants argue that duties are

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[12] The bracketed language replaced "*qua* employee under an employment contract," a much narrower proposition. *Riblet*, 683 A.2d at 37.

owed to stockholders only "*qua* stockholder" as if that settles the question. "*Qua*" is defined as "in the capacity of." BLACK'S LAW DICTIONARY 1252 (7th ed. 1999); *see Frederick Hsu Living Tr. v. ODN Holding Corp.*, 2017 WL 1437308, *17 (Del. Ch.) (duties owed to "stockholders in the aggregate in their capacity as residual claimants, which means the undifferentiated equity as a collective.").

For the reasons given, diversification cannot be realistically disentangled from equity ownership, so that directors considering the interests of stockholders "*qua*" (or "*as*," OB 2) stockholders, should not ignore the effect their decisions have on diversified portfolios when analyzing stockholders' best interests. *See A Legal Framework for Impact: Sustainability Impact in Investor Decision-Making*, 122 (Freshfields Bruckhaus Deringer 2021) (report on investor fiduciary duties stating that "[t]he more diversified a portfolio, the less logical it may be to engage in stewardship to secure enterprise specific value protection or enhancement."); *Active Ownership 2.0: The Evolution Stewardship Urgently Needs* (2019), https://www.unpri.org/download?ac=9721 (report from initiative signed onto by institutional investors with more than $120 trillion in assets explaining risk of "[a] company strengthening its position by externalising costs onto others. The net result for the [diversified] investor can be negative when the costs across the rest of the portfolio (or market/economy) outweigh the gains to the company."); John C. Coffee, *The Coming Shift in Shareholder Activism: From "Firm-Specific" to*

"Systematic Risk" Proxy Campaigns (and How to Enable them), 2 (Aug. 26, 2021) ("recognition that change at one firm can affect the value of other firms in the portfolio implies a new goal for activism: namely, to engineer a net gain for the portfolio, possibly by reducing 'negative externalities' that one firm is imposing on other firms in the investor's portfolio."); Gordon, *supra*, 631 (diversified investor "may regard its risk-adjusted returns as enhanced rather than reduced by measures that reduce expected returns on a portion of its portfolio.").

Chancellor Allen wrote that diversification did not merely benefit investors but increased societal wealth by encouraging risky investments that ultimately created more value. William Allen, *Ambiguity in Corporation Law*, 22 Del. J. Corp. Law 894, 896 (1997). Moreover, he explained, corporate law is designed to encourage diversification. *Id.* ("[T]he elemental purpose of corporation law is the facilitation of cooperative activity that produces wealth.. . . .The interaction of [corporate] characteristics facilitates diversification of investments and centralization of management. This allows capital to subject itself to greater risk.").

One court found that when weighing risk and return (greater risk generally corresponding to greater return), directors should be influenced by the fact that most stockholders are diversified:

> Shareholders can reduce the volatility of risk by diversifying their holdings. In the case of the diversified shareholder, the seemingly more risky alternatives may well be the best choice since great losses in some stocks

> will over time be offset by even greater gains in others. ***Given mutual funds and similar forms of diversified investment, courts need not bend over backwards to give special protection to shareholders who refuse to reduce the volatility of risk by not diversifying.*** A rule which penalizes the choice of seemingly riskier alternatives thus may not be in the interest of shareholders generally.

Joy, 692 F.2d at 886 (emphasis added). *Joy* found a primary reason that courts granted directors discretion was to encourage risk-taking, and that such risk-taking was appropriate because of the modern trend of diversification. *Id.* In other words, the reasoning underpinning the business judgment discretion relies upon diversification. It would thus be strange to prevent directors from exercising that discretion to account for that very diversification.

Similarly, experts have argued that rules governing corporate control transactions should not be designed to protect concentrated stockholders because rules established "in the name of protecting investors who chose not to diversify, penalizes other investors who eliminate risk through diversification, and in the process, it reduces the number of value-increasing control transactions." Frank Easterbrook, *et al.*, *The Economic Structure of Corporate Law*, 122-123 (1991); *see also* Booth, *supra* 434-435 (concluding that directors should not act as if stockholders were diversified but noting that "[m]ost scholars who favor stockholder wealth as the measure of management duty have quite naturally assumed that management should manage with the interests of diversified stockholders in mind because rational investors diversify.”).

II. DEFENDANTS BREACHED THEIR FIDUCIARY DUTIES TO META’S DIVERSIFIED STOCKHOLDERS

A. Defendants Owe Duties of Care and Loyalty

“The standard of conduct describes what directors are expected to do and is defined by the content of the duties of loyalty and care.” *Trados*, 73 A.3d at 35. “[O]fficers of Delaware corporations, like directors, owe fiduciary duties of care and loyalty.” *Gantler v. Stephens*, 965 A.2d 695, 708-09 (Del. 2009); *see also In re McDonald’s Corp. S’holder Litig.*, 289 A.3d 343, 375 (“oversight liability for officers requires a showing of bad faith. The officer must consciously fail to make a good faith effort to establish information systems, or the officer must consciously ignore red flags.”). “A breach of either the duty of loyalty or the duty of care rebuts the presumption that the directors have acted in the best interests of the shareholders, and requires the directors to prove that the transaction was entirely fair.” *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 371 (Del. 1993), *decision modified on other grounds on reargument*, 636 A.2d 956 (Del. 1994). “[T]here is no single blueprint that a board must follow to fulfill its duties. … Rather, a board’s actions must be evaluated in light of relevant circumstances to determine if they were undertaken with due diligence and in good faith.” *Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1286 (Del. 1989) (citations omitted).

The Complaint sets forth facts from which it is reasonably conceivable that (1) each Defendant, in the their roles as directors, officers and/or controlling stockholder, has breached the duty of care and loyalty by ignoring the impact that Meta's business model has on the diversified portfolios of its stockholders; (2) Zuckerberg and Sandberg have interests that diverge from the interests of Meta's diversified stockholders with respect to decisions that externalize economic costs in order to increase Meta profits; and (3) a majority of the Board is not independent of Zuckerberg. Accordingly, Defendants' motion must fail.

B. Failure to Monitor Constitutes Bad Faith and Breach of the Duty of Care

1. Complaint Establishes Direct Claims

As directors and officers, Defendants violated their duties of care and loyalty when they failed to monitor whether decisions to maximize Company value harmed typical stockholders harming the value of their diversified portfolios. Compl. ¶158 (the "Monitoring Claim"). Defendants' argument that the Monitoring Claim is derivative misconstrues the claim. OB 23. When the interests of stockholders diverge from the interests of the corporation, the claim becomes direct—the harm that stockholders suffer derives from something other than a diminution in value of the corporation. *Cf. Allen v. El Paso Pipeline GP Co., L.L.C.*, 90 A.3d 1097, 1111 (Del Ch. 2014) (finding contractual claims direct, not derivative, even though alleged harm to limited partners flowed from transaction at partnership level); *see* *also Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1036 (Del. 2004) (first prong of *Tooley* analysis is "what person or entity has suffered the alleged harm?").

2. *Direct Claims for Failure to Monitor Tested by* **Caremark** *Standard*

Despite the direct nature of the claim, the appropriate standard is analogous to that set forth in *Caremark* and its progeny: "A board's 'utter failure to attempt to assure a reasonable information and reporting system exists' is an act of bad faith in breach of the duty of loyalty." *Marchand v. Barnhill*, 212 A3d 805, 809 (Del. 2019) (quoting *In re Caremark Intern. Inc. Dervi. Litig.*, 698 A.2d 959, 971 (Del. Ch. 1996)); *see also Ontario Provincial Council of Carpenters' Pension Tr. Fund v. Walton*, 2023 WL 2904946, *20 (Del. Ch.) (describing a failure to monitor claim as an "Information-Systems Claim", and where red flags were present, a "Reg Flag Claim", and noting that both "rest on the premise that a conscious decision not to act is itself a decision that can be the product of bad faith."). Plaintiff brings both an Information-Systems Claim and a Red Flags Claim. Here, despite the Company's unparalleled reach, there is no system for monitoring the damage that Meta does to its own investors—or even considering their diversified interests. Just as the failure to monitor for acts damaging to ***corporate*** value constitutes bad faith remediable through a derivative action, failure to monitor for—or even to consider the effects of—acts damaging to stockholders' best interests ***as investors*** gives rise to direct claims for bad faith. *See* Ex. B at 41-42 (finding that pleading that special committee only looked at "abstraction called the partnership" rather than fairness to limited partners overcame contractual presumption of good faith).

3. Defendants Do Not Contest the Factual Predicate of the Bad Faith Claim

While the Defendants argue that the Complaint "offers no *facts*" to support assertions regarding the relative concentration of ownership between Plaintiff and Defendants, OB 17 (emphasis in original), they do not make a similar assertion with respect to the facts regarding the Monitoring Claim. Instead, Defendants argue the allegations were insufficient because "Plaintiff does not allege that the Defendants were motivated by anything other than maximizing Meta's value . . . ." *Id.* 18. But that is simply an argument that Plaintiff is wrong about the threshold issue. Indeed, Defendants' brief buttresses the Monitoring Claim. It repeatedly declares that Defendants have no duty to "monitor, consider, or protect [stockholders'] interests in *other* companies," *id*. 15 (emphasis in original), and that Defendants must seek only "to maximiz[e] Meta's value," *id.* 18. That position implies Defendants believed a monitoring system designed to protect diversified portfolios from value-maximization strategies would ***violate*** their obligations.

4. *It Is Reasonably Conceivable that the Board Utterly Failed to Monitor, or Even Consider, Risks to Diversified Stockholders*

Even if Defendants did contest the factual predicate of the Monitoring Claim, Plaintiff alleges facts from which it is reasonably conceivable that Defendants utterly failed to monitor—or even consider—the risk that Meta's externalized costs caused significant harm to diversified stockholder portfolios. "[A] sustained or systematic failure of the board to exercise oversight" establishes bad faith. *Caremark*, 698 A2d at 971; *see also Marchand*, 212 A.3d at 823.

In *Marchand*, a two-part test of bad faith was set out, with failure to either "***implement an information system***" or heed red flags sufficient. 212 A.3d at 821. The Supreme Court held plaintiff was entitled to "a reasonable inference that the directors consciously failed 'to attempt to assure a reasonable information and reporting system exist[ed].'" *Id.* at 809 (citations omitted). Noting the complete lack of food safety monitoring system, the Supreme Court held that "[c]onsistent with this dearth of any board-level effort at monitoring, the complaint pleads particular facts supporting an inference that during a crucial period … there was no equivalent reporting to the board and the board was not presented with any material information about food safety." *Id.*

It is clear from the design of Meta's governance that there is ***no effort*** to monitor or consider the Company's impact on its stockholders' portfolios.[13] The Corporate Governance Guidelines that overarch the entire governance framework are geared solely to the value of the Company, not risks to stockholder portfolios. Compl. ¶33. The Audit & Risk Oversight Committee oversight of Meta's risk management strategy is concerned only with risks to the Company, not to diversified stockholders. *Id.* ¶35. The Board has affirmatively chosen to incentivize Company executives to focus solely on Company financial performance, even if such focus has a negative impact on the broader economy and, consequently, the portfolios of Meta's diversified stockholders. *Id.* ¶37. The Compensation Report demonstrates that the Board affirmatively decided not to investigate whether its compensation program, by awarding millions in equity to its executives, might be incentivizing them to damage the economy, and thus the portfolios of an average diversified stockholder. *Id.* ¶¶5, 37. When specifically asked to report on the issue, the Board declined, listing reasons that did not address the cost of the Company's externalities to diversified stockholders. *Id.* ¶37. "In short, the complaint pleads that the [Meta] board had made no effort at all to implement a board-level system of mandatory

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13 Defendants' brief refers to other policies and committees, OB 3-10; but there is nothing to suggest that the existence any of these establishes that the Company is monitoring the risk that its absolute prioritization of financial value is harming the portfolios of its stockholders. As noted, Defendants appear to assert that any variance from such prioritization would violate their fiduciary duties. *Id.* 10.

reporting of any kind [as it relates to Meta's diversified stockholders]." *Marchand*, 212 A3d at 813.

Plaintiff also sufficiently alleges facts to support a Red Flag Claim. While generally this involves ignoring issues raised through a reporting system, the Court has recognized that red flags waving outside of a reporting system can also establish bad faith failure to monitor. *See In re Boeing Co. Deriv. Litig.*, 2021 WL 4059934, *34 (Del. Ch.) ("[T]he Board did not require an internal system to learn about the Lion Air Crash and the attendant MCAS failures. The Lion Air Crash and its causes were widely reported in the media; those reports reached the Board; and the Board ignored them."). *Boeing* ultimately found it unnecessary to decide whether the second test was met because the company had clearly failed the first. *Id.* Nevertheless, the decision clarified that, had there been a system in place, the failure to respond to events detailed in the press would have created a monitoring issue under the second element. *Id.* ("But I need not decide today whether Plaintiffs' prong two theory is cognizable in view of my conclusion that the Board utterly failed under prong one. … Assuming Defendants are correct, the Board nonetheless ignored the Lion Air Crash and the consequent revelations about the unsafe 737 MAX.").

The Facebook Files and other press detailed in the Complaint raise myriad red flags that the Company's business model of profits first is creating widespread harm to the economy, and therefore to the Company's diversified stockholders:

> Meta promotes products that drive significant mental health issues;
> A critical algorithm drives harsh political discourse around the world;
> Zuckerberg rejected changes to the algorithm to address negative impact, because it would reduce revenue;
> Company Platforms lure women into abusive situations including sex work and modern slavery;
> Harm in developing countries is treated as a cost of doing business;
> The Company's personnel recognize that vaccine hesitancy is "rampant" on Company Platforms and that it has "potential to cause severe societal harm;"
> The Company "is acutely aware that the products and systems central to its business success routinely fail and cause harm;" and
> A former employee told Congress Meta "won't make the necessary changes because they put their immense profits before people" and "Facebook became a $1 trillion company by paying for its profits with our safety, including the safety of our children."

Compl. ¶159.

Despite public reports that Meta prioritizes profits over systemic risk, endangering stockholders through portfolio impact, the Company continues to maintain a governance system that does not include any mechanisms to account for those costs of systemic risks to stockholders that are not shared by the Company, or its insider stockholders. When directly alerted to those risks through media reports and Shareholder Proposals, the Board refused to consider them.

It is clear from both the pled facts and Defendants' own arguments that the Board has not made a good faith effort to monitor or consider the costs that its value maximization strategy imposes on typically diversified portfolios. Because fiduciaries are only empowered to maximize value "for the benefit of stockholders," this oversight lacuna constitutes bad faith.

C. Decision Made by Defendants Without Consideration of Portfolio Impact Breached the Duty of Care

The duty of care "requires that fiduciaries inform themselves of material information before making a business decision and act prudently in carrying out their duties." *United Food & Com. Workers Union & Participating Food Indus. Emps. Tri-State Pension Fund v. Zuckerberg*, 262 A.3d 1034, 1049-50 (Del. 2021) ("*Zuckerberg II*"). Directors and officers breach this duty through gross negligence. "[T]he core inquiry in this regard is whether there was a real effort to be informed and exercise judgment" and "involves an examination of whether the directors informed themselves, before making business decisions, of all material information reasonably available to them." *In re Zale Corp. S'holders Litig.*, 2015 WL 6551418, *4 (Del. Ch.) (cleaned up). "This Court has consistently held that the breach of the duty of care, without any requirement of proof of injury, is sufficient to rebut the business judgment rule." *Cede & Co.*, 634 A.2d at 371 (citations omitted).

Defendants have abjured consideration of Meta's impact on "investments in other companies," OB 10, as confirmed by their entire corporate governance program, and rejection of Stockholder Proposals about these very concerns. Compl. ¶¶99-132. Defendants have taken no action to inform themselves of any material information reasonably available to them regarding Meta's impact on diversified portfolios. When taken together with Defendants' publicly revealed playbook to reject any measures that interfere with user engagement and profitability, Plaintiff is entitled to the reasonable inference that the Defendants knowingly did nothing to inform themselves of the impact of Meta's negative externalities on its diversified stockholders.

D. Defendants Disloyally Promoted Cost Externalization

The duty of loyalty requires that "the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally." *Cede & Co.*, 634 A.2d at 361. "To plead a viable claim for breach of the duty of loyalty, plaintiff must plead facts supporting a reasonable inference that defendant failed to act reasonably to obtain the best transaction reasonably available ***due to interestedness, because of a lack of independence, or in bad faith***." *Firefighters' Pension Sys. Of City of Kansas City, Missouri Tr. V. Presidio, Inc.*, 251 A.3d 212, 282 (Del. Ch. 2021) (citations omitted) (emphasis added).

1. *As Controlling Stockholder, Zuckerberg Owed Fiduciary Duties to Stockholders*

Controlling stockholders owe fiduciary duties to minority stockholders. *See, e.g., Ivanhoe Partners v. Newmont Min. Corp.*, 535 A.2d 1334, 1344 (Del. 1987) ("Under Delaware law a shareholder owes a fiduciary duty only if it owns a majority interest in ***or exercises control over the business affairs of the corporation***.") (emphasis added); *Weinberger v. UOP, Inc.*, 409 A.2d 1262, 1265 (Del. Ch. 1979) (noting "a fiduciary duty on the part of the majority shareholders to deal fairly with the minority whose property interests are thus controlled."). "A controlling stockholder has the right to act in its own self-interest when it is acting solely in its capacity as a stockholder. This right must yield, however, when a corporate decision implicates a controller's duty of loyalty." *Carr v. New Enter. Assocs., Inc.*, 2018 WL 1472336, *22 (Del. Ch.).

Zuckerberg controls Meta and focuses it on profitability because his multibillion-dollar fortune depends upon Meta—his personal wealth is inextricably tied to its financial success. *See* Compl. ¶¶4, 12; Ex. A at 19:18-20; *Zuckerberg*, 250 A.3d at 869, 893. Zuckerberg demonstrates these interests by routinely striking down safety initiatives that could reduce user engagement. *See* Compl. ¶¶32, 52, 55, 59-60, 64-66, 69, 75, 82-83, 88-89, 98, 133. "[A]ll roads here lead to Zuckerberg." Ex. A at 45:3-4. Zuckerberg defines Meta's business model and controls decision-making at the Company to conform to his user engagement and profitability playbook.

These facts demonstrate Zuckerberg's "direction of corporate conduct in such a way as to comport with [his] wishes or interest." *Orman v. Cullman*, 794 A.2d 5, 24 (Del. Ch. 2002) (quoting *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984)). As detailed above, four of the nine directors have previously been found to lack independence from Zuckerberg: Sandberg, Andreesen, Alford and Houston. *See* Ex. A at 29:15-32:7; *Zuckerberg*, 250 A.3d at 873, 893. Together with Zuckerberg, they constitute a Board majority. At the pleading stage, Plaintiff is entitled to the reasonable inference that the majority of the Board is beholden to Zuckerberg and cannot exercise their independent business judgment to go against Zuckerberg's wishes—zebras do not change their stripes.

2. *The Divergent Interests of Zuckerberg and Sandberg Create a Disabling Conflict of Interest*

a. *Differing Interests among Stockholders Can Create Conflicts for Fiduciaries*

Directors, officers and controlling stockholders that hold divergent interests from the of the rest of the company's stockholder base may misperceive what is necessary to act for the benefit of stockholders. *See Trados*, 73 A.3d at 64-65. *Trados* involved the sale of a company where preferred stock, held by a majority of the board, received consideration while the common stock received nothing.

Plaintiff argued that the board had a duty to continue operating the company to maximize its value instead of selling it. *Id.* at 42. The Court held that "in circumstances where the interests of the common stockholders diverge from those of the preferred stockholders, it is ***possible*** that a director could breach their fiduciary duty by improperly favoring the interests of the preferred stockholders over those of the common stockholders." *Id.* (quoting *In re Trados Inc. S'holder Litig.*, 2009 WL 2225958, *7 (Del. Ch.)) (cleaned up) (emphasis in original). The Court further noted that "[c]onflict blindness and its lesser cousin, conflict denial, have long afflicted the financially sophisticated." *Id.* at 64. "Directors who cannot perceive a conflict or who deny its existence cannot meaningfully address it." *Id.* at 62. The Court noted "[t]he defendants in this case did not understand that their job was to maximize the value of the corporation for the benefit of the common stockholders, and they refused to recognize the conflicts they faced." *Id.*

Conflicting interests can also arise among holders of the same class of stock, such as a desire for liquidity. *See Goldstein v. Denner*, 2022 WL 1671006, *32 (Del. Ch.). "Circumstances [which] may cause the interests of a stockholding director to diverge from the interests of other stockholders" and constitute a breach of the duty of loyalty, including decisions based on "a desire to gain liquidity [that] cause[s] them to manipulate the sales process and subordinate the best interests of the corporation and the stockholders as a whole." *Id.* (citations omitted). Noting the controlling stockholder's reputation for reaping short-term gains using near-term sales, the Court found that "[w]hen a defendant acts in accordance with a known playbook, the plaintiff gets the benefit of an inference at the pleading stage that the defendant is following the playbook." *Id.* at *33; *see also In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022, 1046 (Del. Ch. 2012) (board considered tax impact to single stockholder); *Gilbert v. El Paso Co.*, 575 A.2d 1131, 1148 (Del. 1990) (finding conflict between stockholder who tendered into closed offer and those who had not "unavoidable," but finding no breach where board sought to renegotiate tender offer terms in a manner that served "all its shareholders").

b. <u>Zuckerberg is Conflicted</u>

A director or officer is sufficiently interested where he has a "material financial or other interest in the transaction different from the shareholders generally. 'Material' in this setting refers to a financial interest that in the circumstances created a reasonable probability that the independence of the judgment of a reasonable person in such circumstances could be affected to the detriment of the shareholders generally." *Litle v. Waters*, 1992 WL 25758, *4 (Del. Ch.) (citations omitted); *see also In re MultiPlan Corp. S'holders Litig.*, 268 A.3d 784, 813 (Del. Ch. 2022) ("A greater than half-million-dollar payout is presumptively material at the motion to dismiss stage."); *Orman*, 794 A.2d at 31 (noting "it would be naïve to say, as a matter of law, that $3.3 million is immaterial.").

Zuckerberg's $67.6 billion in Meta stock gives him a material interest that diverges from the interests of Meta stockholders who diversify their portfolios; a business model that makes Meta more valuable while lowering the value of diversified portfolios benefits Zuckerberg to the exclusion and at the expense of diversified stockholders. Zuckerberg has demonstrated his unwavering profit-driven focus for the Company's operations.

c. *<u>Sandberg is Conflicted</u>*

Sandberg's equity compensation, including $93 million in 2021 alone and continuing ownership— $115 million in unvested shares or equivalents in 2021 and $290 million in stock in 2022— creates a disabling conflict. *Litle*, 1992 WL 25758, *4. It is reasonable to infer that a person with such a level of ownership will benefit from Company profits that come at the expense of the broader economy more than would a typically diversified Meta stockholder for whom a healthy economy is the dominant determinant of financial returns.

d. *<u>A Majority of the Board Is Not Independent</u>*

This Court has acknowledged "the difficulties that boards and stockholders have in overseeing the conduct of someone like Zuckerberg who … [i]s a Superstar CEO" and noted "the many reasons why even independent directors have difficulty sufficiently supervising a [S]uperstar CEO …." Ex. A at 36:19-22; 37:4-7. The same issues apply here, except all the independent directors (save Kimmitt) in the

Facebook matter have been replaced with those having more deference towards Zuckerberg. Compl. ¶¶25, 39-40.

It has been established, largely through derivative litigation in this Court, that at least four other directors on Meta's Board are unable to "exercise disinterested and independent judgment" from Zuckerberg. *Zuckerberg*, 250 A.3d at 893 (finding Zuckerberg, Sandberg and Andreessen unable to "exercise disinterested and independent judgment" due to their fealty to Zuckerberg); Ex. A at 29-32 (finding that Sandberg, Alford, Andreessen and Houston lack independence from Zuckerberg for demand futility purposes). Together with Zuckerberg, they constituted a majority of the subject Board. Thus, at the time of and following the press reports and Stockholder Proposals, a majority of the Board has been dominated by Zuckerberg, whose interests diverge from those of Meta's diversified stockholders.

The Stock Ownership Guidelines, which require that Meta directors own at least $750,000 worth of stock, are expressly designed to discourage diversification: the shares must be owned directly by or on behalf of the director or immediate family members; shares held through index funds, mutual funds or any other pooled investment vehicles do not count. Compl ¶34. The magnitude of the requirement, along with the filter designed to discourage diversification, make it reasonably conceivable that the seven directors other than Zuckerberg and Sandberg are conflicted with respect to cost externalization that threatens diversified portfolios.

E. **<u>Due to Defendants' Conflicts, Their Decisions to Ignore the Interests of Meta's Diversified Stockholders is Subject to Entire Fairness</u>**

"Our law presumes that 'in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company.' Those presumptions can be rebutted if the plaintiff shows that directors breached their fiduciary duty of care or loyalty or acted in bad faith. If that is shown, the burden then shifts to the director defendants to demonstrate that the challenged act or transaction was entirely fair to the corporation and its shareholders." *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 52 (Del. 2006). In the context of a direct claim, it has been held that entire fairness is triggered "where the controlling stockholder receives a 'unique benefit' by 'extracting something uniquely valuable to the controller, even if the controller nominally received the same consideration as all other stockholders.'" *Delman v. GigAcquisitions3, LLC*, 288 A.3d 692, 717 (Del. Ch. 2023) (quoting *In re Crimson Expl. Inc. S'holder Litig.*, 2014 WL 5449419, *13 (Del. Ch.)). "The fact intensive nature of th[e entire fairness] inquiry 'normally will preclude dismissal of a complaint on a Rule 12(b)(6) motion to dismiss.'" *Delman*, 288 A.3d at 722 (citation omitted).

Here, Plaintiff's claims rest not so much on the unfairness of any particular transaction(s), but on the unfairness of Meta's entire business model, in which a conflicted controller and a majority of fiduciaries beholden to him refuse to consider the deleterious effects of their decisions on the Company's diversified stockholders. As discussed more fully above, Defendants do not contest that they have made no effort to consider the externalities of their decisions on the diversified beneficiaries of their fiduciary duties. *See* OB 1, 10, 13-14.

F. Plaintiff's Claims Do Not Rely on Showing Damage to Individual Portfolio Companies

Defendants misunderstand the relationship between systemic risk created by Meta's operations and diversified portfolio value when they assert that "there are no facts to show that Plaintiff's investments in other companies were actually harmed." OB 21. The systemic harm that flows from Meta's business model affects the economy as a whole. *The Economic Case for Regulating Social Media, supra* ("If the conscious intent were to undermine social and political stability, [the Facebook] business model could hardly be a more effective weapon."). This means that the threat is to the economy as an entirety, so that the average value of each company's share of that economy is smaller. *See, e.g., Universal Ownership, supra*; Gary W. Cox, *et al.*, *The Violence Trap: A Political-Economic Approach to the Problems of Development* (Feb. 13, 2015) (demonstrating link between political violence and lack of growth on a national basis).

Defendants' objections that Plaintiff "omits any factual allegations that the global GDP has fallen in recent years" and "offers no facts to show how the market as a whole has performed," OB 10, misses the point: the allegation is not that GDP or portfolio values have fallen, but that those values are lower than they otherwise would have been; that value may or may not yet be reflected in market prices. If perceived by the market, these costs may be reflected in lower share prices generally; alternatively, they can manifest in asset prices later, when risks mature. Finally, the risks may lead multiple firms to make costly decisions necessary to mitigate such risks:

> This systemic-risk-as-systematic-risk overhangs stock market prices generally and of course a realization of this risk would produce a dramatic decline in stock prices. Systematic risk can also reduce the expected return on a portfolio if it leads to costly financing or operational decisions that would be avoided in an environment of lower systematic risk.

Systematic Stewardship, *supra*, 651. Nor does the Defendants' claim that the Complaint is deficient because no facts are offered to show "that any poor performance could possibly be attributed to Defendants," hit the mark. OB 10 n.8. The Complaint cites multiple sources for the relationship between GDP, market returns and diversified portfolios, and evidence for how the systems that Meta threatens pose risks to GDP. *See, e.g.,* Compl. ¶¶45-47, 79, 86.

G. <u>Recent Increases in Meta Share Price Irrelevant</u>

Defendants claim that Plaintiff does not allege harm, but that, "[t]o the contrary," comparison of the Original Complaint to the Amended Complaint shows a recent

40% rise in Meta's stock price. But the Complaint is not about Meta's value, but rather external harms from its pursuit of value. In fact, two sources of the price rise were further cost cutting and faster revenue growth, the root of the problem, according to the Complaint. *See Meta Evokes Big Tech's Glory Days With Biggest Surge Since 2013* ("The latest rally comes after Chief Executive Officer Mark Zuckerberg pledged Wednesday to make the social-media company leaner;" "investments are driving faster revenue growth") (Feb. 2, 2023) https://www.bloomberg.com/news/articles/2023-02-02/meta-s-stock-market-rebound-to-surpass-200-billion-in-value?sref=oAmKviWU. While Meta's push for revenue and cost-cutting may have lifted its share price, it continues to threaten enormous harm. On June 7, 2023, it was reported that Instagram connects and promotes "a vast network of accounts openly devoted to the commission and purchase of underage-sex content, according to investigations by *The Wall Street Journal* and researchers at Stanford University and the University of Massachusetts Amherst." *Instagram Connects Vast Pedophile Network* (June 7, 2023) https://www.wsj.com/articles/instagram-vast-pedophile-network-4ab7189?mod=tech_lead_pos1. The 40% stock bump celebrated by Defendants cannot justify the cost: "Instagram doesn't merely host these activities. Its algorithms promote them." *Id.*

H. Meta's Exculpatory Charter Provision Is Inapplicable

Meta's exculpatory provision does not extend to (1) conduct of Zuckerberg or Sandberg in the capacity as officers or controlling stockholder, (2) injunctive relief, or (3) self-interested, disloyal or bad faith conduct. "When a director is protected by an exculpatory charter provision, a plaintiff can survive a motion to dismiss by that director defendant by pleading facts supporting a rational inference that the director 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, S'holder Litig.*, 115 A.3d 1173, 1179–80 (Del. 2015). "While an exculpation clause insulates directors from liability for breaches of the duty of care, such breaches can still support injunctive relief." *In re BioClinica, Inc. S'holder Litig.*, 2013 WL 5631233, *1 n.2 (Del. Ch.).

Plaintiff seeks, inter alia, declaratory and injunctive relief requiring Defendants to consider the interests of diversified stockholders in their decision making. Compl. at 91.

III. THE DUTIES PLAINTIFF SEEKS TO ENFORCE ARE NOT UNWORKABLE

A. No Slippery Slope

Defendants insist that "Meta's directors and officers could not possibly have the unworkable duty to advance every private interest that each Meta stockholder has, however important [*sic*]," OB 13 n.10, and that such a rule would mean that "the decisions of corporate fiduciaries must be guided by not only what is in the best interests of the corporation itself, but also what is in the best interests of every other company," *id.* 3. This slippery slope argument mischaracterizes Plaintiff's position, which is that diversification is a widely shared characteristic of Meta stockholders (and investors generally) that is closely linked to stock ownership. Plaintiff is not asking Defendants to consider idiosyncratic interests of stockholders, or to do analyses of other individual companies or "private interest[s]." OB 13 n.10. There is nothing shocking about considering shared characteristics of stockholders. For example, a board can (and should) consider whether a transaction could be designed to provide a tax-free or low tax transaction to stockholders (even if some stockholders were not taxpayers), without raising the specter that directors must consider every tax impact of every transaction on every stockholder. *See In re Toys "R" Us, Inc. S'holder Litig.,* 877 A.2d 975, 1022 (Del. Ch.) (merger agreement that foreclosed division asset sale not unreasonable where board was aware of negative tax implications of such a sale, including taxes imposed at the investor level); *Cf. Synthes*, 50 A.3d at 1046 (noting that controlling stockholder might have differing interest in timing of transaction due to tax circumstances, but finding no harm to other stockholders from accommodating such interest).

B. **Perfection Not Required**

Defendants overstate the costs of permitting directors to account for the reality of investment diversification in determining what is in the best interests of stockholders. *See* OB 10-13. Fiduciaries must make a good faith effort to incorporate such considerations where they have determined it makes sense to do so. Just as the decision of how much information to consider in maximizing value is a question best left to fully informed fiduciaries, so is the decision of how much information to consider regarding portfolio impact. *See In re RJR Nabisco, Inc. S'holders Litig.*, 1989 WL 7036, *1165 (Del Ch.) ("the amount of information that it is prudent to have before a decision is made is itself a business judgment of the very type that courts are institutionally poorly equipped to make").

Indeed, if an uninitiated observer were told that directors are charged with maximizing firms' long-term value, she might also object that such a job was infeasible, given the almost infinite array of choices and variables that face a business. The feasibility lies in the fact that that directors have broad discretion to pursue value and stockholder benefit within the bounds of the possible.

Denying the Motion will not change the way most corporations operate; even if it is only focused on enterprise value, a well-run corporation should already consider externalities, because of reputational and regulatory risk, among other concerns. Moreover, given the breadth of the global economy and the limited impact of most business models, directors are likely to conclude that the greatest financial impact of corporations on their diversified stockholders is through the corporation's enterprise value, not through broad economic effects that would ripple through a diversified portfolio. Only where a corporation can have outsized economic effects (as in this case) are portfolio effects likely to be material.

C. Recognizing Differing Interests Among Stockholders Is Not Infeasible

It is not infeasible to recognize the diversified nature of many stockholders just because not all stockholders have that status. As Defendants argue:

> Even where there are different groups of stockholders with diverging interests, directors do not breach their fiduciary duties merely by choosing one group over the other. . . . ("Delaware courts have made it clear that it is up to directors . . . to decide whether to favor shareholders who are ***diversified or undiversified***; shareholders who are hedged or unhedged; shareholders who are risk-averse or risk-neutral; shareholders who are affiliated or unaffiliated with the corporation.").

OB 11 n.9 (emphasis in original) (citation omitted).

Defendants mischaracterize Plaintiff's position as seeking singular status for diversified stockholders: "Plaintiff's claim that Meta's 'core constituency' is 'the Company's diversified stockholders.'" *Id.* 13 n.10. In fact, this quotation elides the key article: "The Defendants have disregarded ***a*** core constituency— the Company's diversified stockholders." Compl. ¶6 (emphasis added). Due regard is the message of *Gilbert*, which Defendants cite for the proposition that fiduciaries must "protect and advance the interests of *all* [of a company's] shareholders." OB 13; *Gilbert*, 575 A.2d at 1147-48 (emphasis in original).

Gilbert acknowledges that different groups of stockholders may have different interests. *Id.* at 1148. The board decision in *Gilbert* recommended an improved partial tender offer, which re-opened the tender period, thereby leaving the stockholders who had tendered into the first offer with lower proration. *Id.* at 1133. However, the Court found that the decision was positive-sum when the interests of all stockholders were considered. *Id.* at 1148. The case in no way suggests ignoring the interests of one group. *See Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1389 (Del. 1995) ("distinctions among types of shareholders are neither inappropriate nor irrelevant for a board of directors to make, *e.g.,* distinctions between long-term shareholders and short-term profit-takers, such as arbitrageurs, and their stockholding objectives" and "Board properly recognized that all shareholders are not alike, and provided immediate liquidity to those shareholders who wanted it.").

In any event, Defendants' position—ignore diversified stockholder interests—does not make the divergent interest go away: it just chooses in favor of the concentrated stockholder position occupied by Meta's controlling stockholder. This "one-size-fits-Zuckerberg" approach does not solve, but rather exacerbates the concern over diverging interests.

D. Precluding Consideration of Portfolio Impact Is Increasingly Infeasible Due to Market Realities

1. Adopting Defendants' Position Would Put Directors at Odds with Investors

Defendants posit the absence of a duty to protect investments in other companies, and an affirmative duty to maximize firm value. OB 1, 23. Combined, these rules would require fiduciaries to avert their eyes from any systemic damage their company imposes on stockholders unless such damage can be specifically tied to the corporation's own value. Yet as shown above, stockholders seeking to optimize portfolio returns must address the effect of individual portfolio companies on the rest of their portfolios. A rule forbidding directors from consideration of portfolio impact would pit them against the interests of the beneficiaries whose interests they are meant to serve. *See Legal Framework, supra*, 534 (under federal law "[p]ension funds will need to consider stewardship activity, . . . [to m]itigate a systemic sustainability risk that could adversely impact the performance of its portfolio"); Crespi, *supra*, 389 (" To the extent that the common shareholders of a corporation are diversified … an assessment of their interests that takes into account the impacts of corporate actions on the value of their entire portfolio, rather than only on the value of their subject corporation common share holdings, would be a more accurate guide for maximizing their wealth than would be the fictional undiversified shareholder characterization.").

2. Adopting Defendants' Position Would Impinge on Director Discretion

Such a rule would also severely impinge on the cornerstone of Delaware corporate law, which is the grant of the power to directors to manage the corporation; directors exercise their own rational judgment as to how to best advance the welfare of their stockholders. "When the ***business judgment rule*** applies, the board's business decisions 'will not be disturbed if they can be attributed to any ***rational*** business purpose. A court under such circumstances will not substitute its own notions of what is or is not sound business judgment' for the board's notions." *eBay*, 16 A.3d at 40 (citations omitted). It would stretch the meaning of the English language to suggest that it would be irrational for directors to ever account for the effects the company's business model will have on its stockholders' portfolios, since those stockholders are the beneficiaries who directors and officers are dutybound to protect, and since the stockholding objective of investors is to optimize the overall returns of their portfolios .

* * * *

"Corporate law is not static, but must grow and develop in response to, indeed in anticipation of, evolving concepts and needs." *Grimes v. Alteon, Inc.,* 804 A.2d 256, 264 (Del. 2002) (cleaned up) (quoting *Moran v. Household Int'l, Inc.,* 500 A.2d 1346, 1351 (Del. 1985); *Unocal Corp. v. Mesa Petroleum Co.,* 493 A.2d 946 (Del. 1985). Modern Portfolio Theory and diversification are now commonly accepted as the bases for investment in equity securities and often determine stockholding objectives. Delaware's common law of corporations should reflect this economic reality by requiring fiduciaries to consider the diversified interests of their stockholders.

CONCLUSION

For the foregoing reasons, the Court should deny Defendants' motion to dismiss.

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CERTIFICATE OF SERVICE

Kurt M. Heyman, Esquire, hereby certifies that on June 16, 2023, a copy of the foregoing Plaintiff's Answering Brief in Opposition to Defendants' Motion to Dismiss was served electronically upon the following:

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