IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE PRIMEDIA, INC. SHAREHOLDERS LITIGATION	))	CONSOLIDATED C.A. No. 6511-VCL

MEMORANDUM OPINION

Date Submitted: October 28, 2013
Date Decided: December 20, 2013

Jessica Zeldin, ROSENTHAL, MONHAIT & GODDESS, P.A., Wilmington, Delaware; James S. Notis, Jennifer Sarnelli, GARDY & NOTIS, LLP, Englewood Cliffs, New Jersey; Judith L. Spanier, ABBEY SPANIER, LLP, New York, New York; Harold B. Obstfeld, HAROLD B. OBSTFELD, P.C., New York, New York; *Attorneys for Plaintiffs*.

A. Thompson Bayliss, ABRAMS & BAYLISS LLP, Wilmington, Delaware; Meredith E. Kotler, Boaz S. Morag, CLEARY GOTTLIEB STEEN & HAMILTON LLP, New York, New York; *Attorneys for Defendants Primedia, Inc., Charles J. Stubbs, TPG Capital, L.P., Pittsburgh Holdings, LLC, and Pittsburgh Acquisition, Inc.*

Martin S. Lessner, Danielle Gibbs, Lakshmi A. Muthu, YOUNG CONAWAY STARGATT & TAYLOR, LLP, Wilmington, Delaware; Adam Offenhartz, Gabrielle Levin, GIBSON, DUNN & CRUTCHER LLP, New York, New York; *Attorneys for Defendants Beverly C. Chell, David A. Bell, Meyer Feldberg, H. John Greeniaus, Daniel T. Ciporin, and Kevin J. Smith.*

William M. Lafferty, R. Judson Scaggs, Jr., Susan Wood Waesco, Matthew R. Clark, MORRIS, NICHOLS, ARSHT & TUNNELL, LLP, Wilmington, Delaware; Lewis R. Clayton, Andrew G. Gordon, Jonathan H. Hurwitz, PAUL, WEISS RIFKIND, WHARTON & GARRISON LLP, New York, New York; *Attorneys for Defendants Kohlberg Kravis & Roberts & Co. L.P., KKR Associates, LP, KKR 1996 GP LLC, Perry Golkin, Thomas Uger, and Dean B. Nelson.*

LASTER, Vice Chancellor.

The plaintiffs allege that defendant Kohlberg Kravis Roberts & Co. L.P. ("KKR") traded on inside information when purchasing shares of preferred stock of Primedia, Inc. ("Primedia" or the "Company"). The plaintiffs originally asserted derivative claims against Primedia's board of directors and KKR (the "Derivative Claims"). While the Derivative Claims were pending, TPG Capital, L.P. ("TPG") acquired Primedia through a reverse triangular merger (the "Merger"). The closing of the Merger extinguished the plaintiffs' standing to maintain the Derivative Claims, which were dismissed.

The plaintiffs countered by filing this action, which asserts direct claims challenging the Merger on behalf of a class of Primedia's minority stockholders (the "Class Claims"). According to the class complaint, Primedia's board failed to obtain any value in the Merger for the Derivative Claims. The Merger thus conferred a unique and material benefit on KKR by transferring control over the insider trading claims to an acquirer that would never assert them, and the consideration yielded an unfair price for Primedia's minority stockholders. The defendants moved to dismiss the Class Claims, claiming that the plaintiffs lacked standing to pursue them and that they failed to state a claim on which relief could be granted. That motion was denied. *See In re Primedia, Inc. S'holders Litig.* (*Primedia II*), 67 A.3d 455 (Del. Ch. 2013).

The defendants now move for judgment on the pleadings. They argue that the doctrine of laches barred the Derivative Claims, so there was no underlying litigation asset to confer a unique and material benefit on KKR or to render the Merger consideration unfair. KKR's purchases of preferred stock fall into two categories: (i) purchases made shortly before the public announcement of a material sale of assets and (ii) purchases made in July 2002, before Primedia reported earnings that materially exceeded expectations. As to the former category of purchases, the motion is granted. As to the latter category, the motion is denied.

I. FACTUAL BACKGROUND

The facts are drawn from the Consolidated Amended Class Action Complaint (the "Class Complaint" or "CC") and the documents it incorporates by reference, including the Third Amended and Consolidated Derivative Complaint (the "Derivative Complaint" or "DC"), which was the operative complaint framing the Derivative Claims at the time of the Merger. For purposes of this decision, the Class Complaint's allegations are assumed to be true, and the plaintiffs receive the benefit of all reasonable inferences.

A. Primedia, KKR, And The Preferred Stock

From Primedia's founding until the Merger, KKR was always Primedia's controlling stockholder. At the time of the Merger, two KKR affiliates—KKR Associates, LP and KKR GP 1996 LLC—served as the general partners for investment funds that owned approximately 58% of Primedia's outstanding common stock. Consistent with its status as Primedia's controlling stockholder, KKR maintained a significant presence on the Primedia board.

During the latter half of the 1990s, Primedia raised capital by issuing preferred stock. Three series are pertinent to this case: the Series D Preferred, the Series F Preferred, and the Series H Preferred (collectively, the "Preferred Stock"). The terms of each series contemplated a period during which Primedia would have the option to redeem the Preferred Stock at a premium, followed by a period during which Primedia could redeem without paying a premium, then finally by a date when Primedia was obligated to redeem at a predetermined value. Each series paid annual cash dividends that accrued and were payable in arrears. Each series fixed the annual dividend at a specific amount or as a percentage of the liquidation preference. At the mandatory redemption date, the holders would receive the contractually required redemption payment plus all accrued and unpaid dividends.

The shares of Preferred Stock traded publicly. The annual dividends and mandatory redemption date gave the Preferred Stock an investment profile resembling a bond. As long as Primedia had sufficient funds legally available to make the mandatory redemption payment, the returns on the Preferred Stock could be calculated and then adjusted for the possibilities of non-payment or early redemption.

B. The Preferred Stock Exchange Program

In April 2000, Primedia's common stock closed at a high of $29.25. But Primedia's value rested largely on a portfolio of internet-related media assets, and with the bursting of the technology bubble, the market price of Primedia's shares declined steadily. It reached the low twenties in May 2000, the low teens by February 2001, and the high single digits by September 2001. In March 2002, the stock traded between $2 and $4 per share. By July 2002, it had dipped below $1. The Preferred Stock fell too and traded at steep discounts to face value. The Series D Preferred, for example, had a face value per share of $100 plus accrued and unpaid dividends but traded for $20-30.

During a board meeting on September 21, 2001, management gave a presentation entitled "Exchange of Preferred for Common." DC ¶ 24. Management anticipated that by issuing shares of common stock in exchange for up to $100 million of Preferred Stock, Primedia could save up to $9 million per year in dividends.

On December 19, 2001, the board authorized Primedia to use shares of common stock to repurchase up to $100 million of Preferred Stock at 50-60% of its face value (the "Exchange Program"). Because issuing additional shares of common stock would dilute existing common holders, the board decided that Primedia would not engage in exchanges at an effective stock price below $5 per share. To derive the effective stock price, Primedia divided the face value of the Preferred Stock by the number of shares of common stock issued in exchange. For example, if a holder of Preferred Stock exchanged shares with a face value of $1 million for 40 cents on the dollar, and if Primedia common stock was trading at $2 per share, then Primedia would issue 200,000 shares of common stock in exchange for the Preferred Stock. The effective stock price would be $5 per share, equal to the face value of the Preferred Stock ($1,000,000) divided by the number of common shares exchanged (200,000).

The exchanges began in March 2002. On April 8, Primedia issued a press release announcing the program. The press release noted that Primedia was authorized to acquire Preferred Stock with a face value of up to $100 million and, at that point, had acquired Preferred Stock with a face value of $62 million. The lowest effective stock price in any transaction was $5.16. Primedia continued making exchanges in April.

On May 16, 2002, the board authorized exchanges for another $100 million in face value of Preferred Stock. Exchanges continued through July 2002.

In total, between March and July 2002, Primedia acquired shares of Series D Preferred with a face value of $23 million, shares of Series F Preferred with a face value of $22.7 million, and shares of Series H Preferred with a face value of $29.8 million. In exchange, Primedia issued 14.4 million shares of common stock.

C. KKR Considers Buying Preferred Stock For Itself.

In early 2002, KKR had four representatives on the Primedia board: Henry R. Kravis, George R. Roberts, Perry Golkin, and Joseph Y. Bae. A fifth member of the board, Dean B. Nelson, was the CEO of a consulting company that provided services exclusively to KKR. The Class Complaint and Primedia's public filings conflict over when Nelson joined the board. Given the procedural posture, Nelson is assumed to have been a director at the time, as alleged in the Class Complaint.

On May 21, 2002, five days after the meeting when the Primedia board authorized additional purchases of Preferred Stock, Golkin and Bae co-authored a memo for KKR's Investment Committee and Portfolio Committee (the "May 21 Memo"). Its purpose was to update the KKR committees "on Primedia's performance and revisit the topic of KKR purchasing a portion of Primedia's cash-pay preferred stock." CC ¶ 35 (internal quotation marks omitted).

The May 21 Memo contained nonpublic information about Primedia's performance for both the second quarter of 2002 and the year as a whole. For the second quarter, the May 21 Memo reported that Primedia's EBITDA would be well ahead of publicly disclosed guidance and that the higher EBITDA numbers were nearly assured because of the volume of advertising that already had been sold:

> **Q2 Estimates**
>
> The Company provided 2nd quarter Street guidance for Reported EBITDA of $58-$60 million. The Budget calls for Reported and Cash EBITDA of $66.3 million and $66.1 million, respectively. At this point, most of the second quarter advertising has been sold (with the exception of some weekly publications) and the Company is confident it will meet or exceed Street Guidance.

DC ¶ 31 (quoting May 21 Memo) (internal quotation marks omitted). The May 21 Memo reported that Primedia management projected annual results well above the publicly disclosed figures:

> **2002 Outlook**
>
> The Company's Street guidance for 2002 Reported EBITDA remains at $245-$260 million ($235-$250 million on a Cash basis). This compares to the Company's budgeted Reported and Cash EBITDA of $265 million and $255 million, respectively.
>
> In our recent meetings with the business units, we received a re-forecast for the year of Reported and Cash EBITDA of $271 million and $261 million, respectively, based on first quarter actuals and current business trends. While most business units (with the exception of Enthusiast/EMAP and Haas) have experienced softer market conditions than originally anticipated, the Company's re-forecast is slightly above Budget primarily due to (1) identification and implementation of run-rate cost savings of approximately $60 million ($46 million in 2002), (2) a reversal of $4 million of 2001 bonus accruals and (3) a lower estimate for divested EBITDA, which added $7 million to the new estimates.

Id. ¶ 32 (quoting May 21 Memo) (internal quotation marks omitted). The authors of the May 21 Memo concluded that: "after our discussions with the business unit heads, we are optimistic that the Company is on track to achieve its targeted cost reductions and deliver its Street guidance of Cash EBITDA of $235-$250 million . . . ." *Id.*

The authors of the May 21 Memo recommended that KKR purchase shares of Preferred Stock at then-current market prices, before the market became aware of Primedia's improving performance:

> **<u>Preferred Stock Purchase</u>**
>
> On May 8th, Moody's downgraded the Company's senior debt and preferred stock two notches to B3 and Ca, respectively—one notch below S&P—as a consequence of Primedia not yet delivering on its divestiture goal of $250 million. Both Moody's and S&P have Primedia on negative outlook. Although we do not find the Moody's downgrade to be particularly surprising given Primedia's leverage, we believe the downgrade will put downward pressure on the price of the Company's preferred stock. Two days after the downgrade, the Company swapped $2 million par value of preferred stock at 48% of par value for common stock at $2.52 (the equivalent of Primedia issuing stock at $5.25 per share). To date, the Company has completed $65 million par value of swaps at an average price of 60% of preferred par value for common stock at an average price of $3.19 (the equivalent of Primedia issuing stock at $5.28 per share).
>
> Based on (1) our increased comfort level in the Company achieving Street guidance, (2) our optimism for the Company's future prospects and (3) the implications of the Moody's downgrade on the preferred stock price, we continue to believe the Company's outstanding cash-pay preferred stock offers an attractive risk-reward investment opportunity for the 1996 Fund. Primedia currently has $510 million of cash-pay preferred stock outstanding (three separate issues paying dividend of 8.625%-10.00%). We believe it may be possible to buy a sizeable position of the preferred for cash between 45%-55% of par value due to heightened investor concerns about the Company's financial performance, leverage and future liquidity. At these levels, these securities are yielding anywhere between 15%-20% cash-on-cash returns depending on the tranche of preferred. Assuming the preferreds ultimately returned 100% face value in 2004/2005 when Primedia is unwound, the gross IRR on this investment would be between 30%-50% (See Attachment B). We think

> the 1996 Fund should consider buying up to $50 million of the preferred stock.
>
> We continue to believe that our best chances of acquiring a sizeable block of the preferred stock at a low price will probably be in the next few months before any significant future asset divestitures and/or the Company's business performance improves in 2H02/2003.

DC ¶ 33 (quoting May 21 Memo) (internal quotation marks omitted).

One reasonably conceivable interpretation of the May 21 Memo is that Golkin, Bae, and their co-authors recommended that KKR acquire a "sizeable block of the preferred stock" precisely because they had heard presentations from Primedia management during board meetings, talked with the business units, received the Company's internal forecasts, and knew what Moody's and the market did not yet know about Primedia's prospects. The May 21 Memo plainly indicates the advantage KKR would gain by using this information: buying the Preferred Stock at "45%-55% of par value due to heightened investor concerns about the Company's financial performance, leverage and future liquidity." DC ¶ 33. The authors of the May 21 Memo did not anticipate KKR needing to manufacture an exit from the Preferred Stock position. They believed that KKR could acquire Preferred Stock on the cheap and that the Company's contemplated asset sales and positive performance made redemption highly likely.

D. KKR Enters The Market.

On May 31, 2002, Primedia acquired additional shares of Preferred Stock in exchange for common stock. On June 19, Primedia engaged in two additional exchanges. By the end of June, however, the price of Primedia's common stock had fallen further, closing on June 27 at $1.61 per share. The decline meant that unless Preferred Stock could be exchanged at less than a third of face value, Primedia would have to issue so many shares of common stock that the effective issuance price would drop below the floor of $5 per share. Primedia's final exchange of 2002 took place on June 27.

KKR did not face comparable constraints. On July 3, 2002, KKR formed ABRA III LLC ("ABRA") as a vehicle for purchasing Preferred Stock.

In an effort to mitigate corporate opportunity concerns, KKR approached Primedia about purchasing Preferred Stock. KKR proposed to defer to Primedia if Primedia wanted to acquire Preferred Stock (the "Deferral Agreement"). On July 2, 2002, Primedia management circulated a written consent to directors Meyer Feldberg, H. John Greeniaus, and David Bell, with a copy to Bae. The cover memo stated:

> [I]nvestment partnerships managed by KKR are considering the purchase of outstanding shares of Primedia preferred stock for up to $50 million in cash . . .
>
> You may be aware that there is a doctrine in corporate law call [sic] "usurpation of a corporate opportunity" . . .
>
> The Written Consent states in the first resolution that a cash purchase by Primedia of its outstanding preferred stock would not be in the best interest of Primedia and Primedia waives the opportunity.

DC ¶ 39 (internal quotation marks omitted). The written consent was never executed.

On July 8, 2002, a similar written consent was circulated to the full board. The cover memo stated:

> Attached for your consideration is a written consent of the Board of Directors of PRIMEDIA determining that it is not usurping a corporate opportunity for investment partnerships

> managed by KKR to acquire PRIMEDIA Preferred Stock for cash.

DC ¶ 44 (internal quotation marks omitted). All of the directors eventually executed the written consent, with the last signature page arriving on July 12.

ABRA began buying Preferred Stock on July 8, 2002, before the written consent was fully executed. In July, ABRA made thirteen purchases of Preferred Stock, paying a total of $30.5 million for 189,606 shares of Series D Preferred, 216,500 shares of Series F Preferred, and 548,331 shares of Series H Preferred. On July 31, five days after KKR made a large purchase, Primedia announced EBITDA of $65.1 million for the second quarter, exceeding guidance of $58-60 million. Primedia's common stock traded up from $1.00 to $1.30 per share. On August 8, ABRA paid nearly $5 million for an additional 10,750 shares of Series F Preferred and 138,966 shares of Series H Preferred.

ABRA's thirteen purchases in July were referenced generally in Primedia's Second-Quarter 2002 Quarterly Report on Form 10-Q, which was filed on August 14, 2002 (the "Second Quarter 10-Q"). Primedia did not disclose the exact dates of the July purchases. KKR filed Form 4s with the SEC on August 9 and September 10 that listed the exact dates of the July purchases and the August 8 purchase.

E. The American Baby Sale

On September 26, 2002, the board approved selling the assets of Primedia's American Baby Group to a third party for $115 million in cash (the "American Baby Sale"). KKR representatives Golkin, Bae, and Kravis participated in the board meeting, as did Nelson, KKR's consultant. *See* CC ¶ 38. Primedia did not announce the sale publicly until November 4, 2002.

On the same day that the board approved the American Baby Sale, ABRA paid \$8.5 million for shares of Preferred Stock with a face value of \$22.9 million. On October 7, ABRA paid \$30.7 million for Preferred Stock with a face value of \$84.9 million. Primedia disclosed the October 7 purchase in its Third-Quarter 2002 Quarterly Report on Form 10-Q (the "Third Quarter 10-Q"), which was filed with the SEC on November 14. KKR identified the September 26 purchase on Form 4s filed with the SEC on September 30. KKR identified the October 7 purchase on Form 4s filed with the SEC on October 9.

After the November 4, 2002 public announcement of the American Baby Sale, the trading price of Primedia's common stock rose by 15%. The trading price of the Series D Preferred rose by 38.4%.

On November 5, 2002, a Primedia employee informed Bae that Primedia was resuming its exchanges program. Rather than adhering to the Deferral Agreement, KKR purchased 44,000 shares of Series H Preferred for \$1.5 million.

In December 2002, with the cash from the American Baby Sale available to fund redemptions, the board authorized using up to \$25 million to buy Preferred Stock. But Primedia could not find willing sellers, in part because of KKR's purchases. During all of 2003, Primedia only managed to purchase approximately \$16 million of Preferred Stock.

In total, through ABRA, KKR acquired 35.8% of the Series D Preferred, 57.9% of the Series F Preferred, and 52.7% of the Series H Preferred. KKR spent \$76.4 million for

2,226,197 shares of Preferred Stock with a face value of $222.6 million, paying an average price equal to 34% of face value. KKR's $76 million investment exceeded the $50 million figure in the July 2002 written consent. By contrast, the board authorized Primedia to buy Preferred Stock with a face value of up to $200 million, yet Primedia only managed to acquire Preferred Stock with a face value of $75 million. DC ¶ 59.

F. Primedia Redeems The Preferred Stock.

In February 2005, Primedia sold one of its assets, About.com, for approximately $410 million. By this time, the Preferred Stock was trading at nearly 100% of face value, and Goldman Sachs advised the board that Primedia should consider redeeming the Preferred Stock because of its relatively high dividend. On March 9, the board approved a plan to redeem all of the outstanding shares of the Series D Preferred and Series F Preferred. These issuances were the most expensive for Primedia because they paid dividends of 10% and 9.2%, respectively. On May 11, pursuant to its certificate of designations, Primedia redeemed the Series D Preferred at par plus all accrued dividends, plus the contractual early redemption premium. On the same date, also pursuant to its certificate of designations, Primedia redeemed the Series F Preferred at par plus all accrued dividends.

Later in 2005, Primedia sold another of its assets in a transaction that generated approximately $385 million in cash. This time, Goldman Sachs recommended redeeming the Series H Preferred. The board approved the plan, and on October 31, Primedia redeemed the Series H Preferred at par plus all accrued dividends and paid the contractual early redemption premium.

As a result of the redemptions, KKR realized total proceeds of $222.6 million, representing a capital gain of nearly $150 million on an approximately $76 million investment. In addition, KKR received about $40 million in dividends during the time it held the Preferred Stock, raising its total profits to $190 million.

G. The Filing Of The Derivative Action

On November 29, 2005, a derivative action was filed on behalf of Primedia (the "Derivative Action"). The plaintiffs' main theory at the time was that the Primedia directors breached their fiduciary duties by causing Primedia to sell assets and redeem the Preferred Stock for KKR's benefit.

The defendants moved to dismiss the Derivative Action. In November 2006, Vice Chancellor Lamb denied the motion, holding that the complaint adequately pled that KKR exercised control over Primedia, stood on both sides of the stock redemptions, and received a benefit from those redemptions not shared with other stockholders. *See In re Primedia Inc. Deriv. Litig.* (*Primedia I*), 910 A.2d 248, 256-61 (Del. Ch. 2006).

On May 23, 2007, the board formed a special litigation committee (the "SLC") to investigate the Derivative Claims. The SLC's two members, Daniel T. Ciporin and Kevin J. Smith, were newly appointed directors. The litigation was stayed pending the outcome of the SLC's investigation.

In August 2007, the plaintiffs filed their second amended complaint. The new complaint added a claim that by purchasing Preferred Stock between July 8 and November 5, 2002, KKR usurped corporate opportunities belonging to Primedia.

The SLC thoroughly investigated the redemption claim and the corporate opportunity claim. The SLC and its counsel reviewed some 140,000 documents, conducted twenty-one interviews, consulted with three experts, and held twenty-three formal meetings.

In September 2007, the plaintiffs received a small document production that included the May 21 Memo. In January 2008, after completing its factual investigation, the SLC met with plaintiffs' counsel to review the SLC's preliminary conclusions. The SLC advised the plaintiffs that it planned to recommend dismissal of the Derivative Action and did not intend to pursue any claims based on the May 21 Memo.

The plaintiffs disagreed with the SLC's conclusions and contended that the May 21 Memo supported a strong claim against KKR for insider trading under *Brophy v. Cities Service Co.*, 70 A.2d 5 (Del. Ch. 1949). The SLC had not previously evaluated a *Brophy* claim.

After being notified about the *Brophy* claim, the SLC held its final meeting. The SLC did not conduct any additional investigation, but rather analyzed the *Brophy* claim based on the work it had done to investigate the corporate opportunity theory.

On February 28, 2008, the SLC moved to dismiss the Derivative Action. In support of its motion, the SLC filed a 370-page report and eight volumes of appendices. The report dealt thoroughly and decisively with the redemption claim and the corporate opportunity claim. The report also contained fifteen pages analyzing the *Brophy* claim, concluding primarily that the statute of limitations barred it. The SLC also took the view that there was "no evidence that the inside information was material in light of expert analysis regarding its impact on the market price for Primedia's preferred shares, and no evidence that KKR possessed the requisite scienter given contemporaneous memoranda indicating that KKR planned the purchases months before the inside information was issued." Dkt. 79 at 8 (Defs.' Opening Br. Mot. Dismiss).

For the next year and a half, the plaintiffs conducted discovery to test the SLC's disinterestedness and independence, the thoroughness of its investigation, and the reasonableness of its conclusions. In November 2009, the plaintiffs filed their brief in opposition to the SLC's motion and sought leave to file a third amended complaint—the Derivative Complaint—that formally asserted the *Brophy* claim. Leave was granted, and the plaintiffs filed the Derivative Complaint on March 16, 2010.

H. Dismissal, Revival, and Extinguishment

On June 14, 2010, the SLC presented its motion to dismiss the Derivative Action under the teachings of *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981). *See In re Primedia Inc. Deriv. Litig.*, Consol. C.A. No. 1808-VCL (Del. Ch. June 14, 2010) (TRANSCRIPT). This court granted the motion, and the Derivative Action was dismissed by order dated June 16, 2010.

The plaintiffs appealed the dismissal of the Derivative Action to the Delaware Supreme Court. While the appeal was pending, KKR and the Primedia board began considering strategic alternatives. On May 15, 2011, the board approved a merger agreement with TPG. Later that day, KKR approved the merger agreement by written consent. On May 23, the plaintiffs filed class complaints challenging the Merger in this court, which later were consolidated as the current class action (the "Class Action").

On June 20, 2011, the Delaware Supreme Court reversed the dismissal of the Derivative Action. *See Kahn v. Kohlberg Kravis Roberts & Co., L.P.*, 23 A.3d 831 (Del. 2011). On July 13, the Merger closed. Each share of Primedia common stock, including those held by KKR, was converted into the right to receive $7.10 in cash. The closing of the Merger extinguished the plaintiffs' standing to pursue the Derivative Action, and it was dismissed. *See In re Primedia Inc. Deriv. Litig.,* C.A. No. 1808-VCL (Del. Ch. Aug. 8, 2011) (ORDER).

I. The Motion To Dismiss The Class Claims

The dismissal of the Derivative Action did not affect the Class Action, and the plaintiffs filed the currently operative Class Complaint on December 12, 2011. On January 31, 2012, the defendants moved to dismiss the Class Complaint, contending that the plaintiffs lacked standing to litigate repackaged derivative claims and that the Class Complaint failed to state a claim on which relief could be granted.

The Class Complaint asserted that the defendant directors and KKR breached their fiduciary duties by approving the Merger. The plaintiffs alleged that the Merger conferred a special benefit on KKR, because the right to control the Derivative Action would pass to the acquirer, and KKR knew it was highly unlikely that any acquirer would pursue the *Brophy* claim. Because KKR was Primedia's controlling stockholder and received a special benefit in the Merger, the operative standard of review would become entire fairness. The plaintiffs alleged that the Merger was not entirely fair because the Merger consideration did not include any value for the Derivative Claims.

In *Primedia II*, this court denied the motion to dismiss, holding that the plaintiffs had standing to pursue the claim and that they had pled a reasonably conceivable theory under *Parnes v. Bally Entertainment Corp.*, 722 A.2d 1243 (Del. 1999), and *In re Massey Energy Co.*, 2011 WL 2176479 (Del. Ch. May 31, 2011). The defendants subsequently answered the Class Complaint. They have now moved for judgment on the pleadings on the grounds that the underlying *Brophy* claim was untimely and barred by laches.

II. LEGAL ANALYSIS

Judgment on the pleadings may be entered pursuant to Rule 12(c) "when no material issue of fact exists" and the moving party "is entitled to judgment as a matter of law." *Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund, II, L.P.*, 624 A.2d 1199, 1205 (Del. 1993). As with a Rule 12(b)(6) motion to dismiss for failure to state a claim, "[w]hen considering a Rule 12(c) motion, the court must assume the truthfulness of all well-pled allegations of fact in the complaint and draw all reasonable inferences in favor of the plaintiff." *McMillan v. Intercargo Corp.*, 768 A.2d 492, 499-500 (Del. Ch. 2000) (footnote omitted).

A. The Materials To Be Considered

Through a motion to strike, the plaintiffs have raised a threshold challenge to the scope of the materials to be considered for purposes of the Rule 12(c) motion. Generally, if a party asks the court to consider matters outside the pleadings on a Rule 12(c) motion, then the motion "shall be treated as one for summary judgment and disposed of as provided in Rule 56." Ct. Ch. R. 12(c); *accord Desert Equities*, 624 A.2d at 1204. The doctrine of judicial notice allows documents outside the pleadings to be considered "only in ‘particular instances and for carefully limited purposes.’” *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312, 320 (Del. 2004) (quoting *In re Santa Fe Pac. Corp. S’holder Litig.*, 669 A.2d 59, 69 (Del. 1995)). The bulk of the decisions in this area have addressed Rule 12(b)(6) motions to dismiss, where the same standard for considering material outside the pleadings applies. *McMillan*, 768 A.2d at 500.

Delaware Rule of Evidence 201 empowers a court to take judicial notice of adjudicative facts “at any stage of the proceeding.” D.R.E. 201(f). “A judicially noticed fact must be one not subject to reasonable dispute in that it is either (1) generally known within the territorial jurisdiction of the trial court or (2) capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned.” D.R.E. 201(b).

Rule 201 permits a court to take judicial notice of “documents [outside the pleadings] that are required by law to be filed, and are actually filed, with federal or state officials.” *In re Tyson Foods, Inc. Consol. S’holder Litig.*, 919 A.2d 563, 585 (Del. Ch. 2007) (footnote omitted). When doing so, however, the court only may use the documents or the information they contain in accordance with Rule 201.

In *Santa Fe*, the Delaware Supreme Court explained how a court properly could take judicial notice of documents publicly filed with the SEC for certain purposes but not for others. The plaintiffs in *Santa Fe* alleged that the defendant directors breached their fiduciary duties by omitting material information from the proxy statement issued in connection with a merger. 669 A.2d at 65. In dismissing the disclosure claim, the Court of Chancery considered the entire proxy statement, not just the portions cited in the plaintiffs' complaint. *Id.* at 69. The Delaware Supreme Court agreed that the court properly considered the proxy statement for this purpose "because the operative facts relating to such a claim perforce depend upon the language of the [proxy statement.]" *Id.* For purpose of Delaware Rule of Evidence 201(b), the contents of the proxy statement were "capable of accurate and ready determination" and, for purposes of determining what information had been disclosed publicly, the proxy statement was a source "whose accuracy cannot reasonably be questioned." D.R.E. 201(b). But the Delaware Supreme Court held that the same disclosures in the proxy statement could not be used "to establish the truth of the statements therein" for purposes of the *Revlon* and *Unocal* claims. 669 A.2d at 69-70. For that purpose, the proxy statement was not a source "whose accuracy cannot reasonably be questioned," and the truth of the matters described in the proxy statement was not "capable of accurate and ready determination." D.R.E. 201(b); *accord Abbey v. E.W. Scripps Co.*, 1995 WL 478957, at *1 n.1 (Del. Ch. Aug. 9, 1995) (Allen, C.) ("In deciding a motion to dismiss under Rule 12(b)(6), the court may judiciously rely on proxy statements not to resolve disputed facts but at least to establish what was disclosed to shareholders.").

In *Wal-Mart*, the Delaware Supreme Court held that the trial court improperly considered documents because they were not referred to in the complaint and were not publicly filed. *See Wal-Mart*, 860 A.2d at 320. The underlying claims in the *Wal-Mart* case arose out of Wal-Mart's purchase of corporate-owned life insurance policies. At the time Wal-Mart purchased the policies, the company believed it would be able to deduct the interest payments made in connection with these policies. *Id.* at 315. Congress later disallowed the favorable tax treatment, and the IRS brought several actions "to disallow retrospectively [the interest deductions.]" *Id.* at 316. Wal-Mart sued the insurers who sold the policies, contending that they "failed to disclose material facts and risks" associated with the policies and that Wal-Mart had relied upon the insurers' advice in purchasing these policies. *Id.* at 317. The insurers argued that Wal-Mart's claims were time-barred because Wal-Mart had been on inquiry notice of its claims more than three years before commencing suit. *Id.* To establish inquiry notice, the insurers cited news articles discussing the risks associated with these policies and two IRS technical advisory memoranda issued to companies other than Wal-Mart. *Id.* at 318. The Court of Chancery took judicial notice of the materials and barred Wal-Mart's claims. *Id.* The Delaware Supreme Court reversed, holding that "the trial court was not free to consider the [technical advisory memoranda] and newspaper articles on this Rule 12(b)(6) motion," because the complaint did not incorporate the materials and the record did not "otherwise establish that these documents were publicly filed." *Id.* at 320. It was therefore error for the trial court consider the materials "under judicial notice principles, to resolve conflicting factual inferences" on a pleadings stage motion. *Id.*

Here, the plaintiffs ask the court to strike and give no consideration to the following five categories of documents that the defendants submitted in support of their motion:

- Form 4s filed with the SEC by Golkin, Kravis, Roberts, KKR 1996 Fund L.P., KKR 1996 GP LLC, and KKR Associates 1996 L.P., between August 9 and November 7, 2002 (the "KKR Form 4s");

- Investment updates prepared by Bear Stearns and available to subscribers (the "Bear Stearns Updates");
- Newspaper articles about Primedia (the "Newspaper Articles");
- Transcripts of Primedia's analyst calls on July 31 and October 31, 2002 (the "Analyst Call Transcripts"); and
- Primedia's earnings release dated October 31, 2002 (the "Earnings Release").

The motion to strike is denied as to the KKR Form 4s and granted as to the other documents.

1. The KKR Form 4s

The plaintiffs contend that the KKR Form 4s are documents outside the pleadings that the court cannot consider. The defendants respond that the court can take judicial notice of the KKR Form 4s for the limited purpose of establishing the date on which the purchases of Preferred Stock were disclosed. The plaintiffs counter that because the Form 4s were filed as hard copy documents rather than electronically, they were not readily available to the public and are not suitable for judicial notice.

SEC Rule 16a-3(g) requires that corporate insiders file Form 4s. *See* 17 C.F.R. § 240.16a–3(g) (2013). Rule 16a-3 was issued pursuant to Section 16 of the Securities Exchange Act of 1934. "The primary purpose of Section 16(a) is to expose insiders' trades to public scrutiny and thereby discourage insiders from using nonpublic information gained from their positions for personal trading." Peter J. Romeo & Alan L. Dye, *The Section 16 Deskbook* 8 (Michael Gettelman, ed., 2010). The legislative history behind Section 16 emphasizes the legislative purpose of providing public disclosure of insiders' trades:

> Because it is difficult to draw a clear line as a matter of law between truly inside information and information generally known by the better-informed investors, the most potent weapon against the abuse of inside information is full and prompt publicity. For that reason, this bill requires the disclosure of the corporate holdings of officers and directors and stockholders owning more than 5 percent of any class of stock, and prompt disclosure of any changes that occur in their corporate holdings. . . . The Committee is aware that these requirements are not air-tight and that the unscrupulous insider may still, within the law, use inside information for his own advantage. It is hoped, however, that the publicity features of the bill will tend to bring these practices into disrepute and encourage the voluntary maintenance of proper fiduciary standards by those in control of large corporate enterprises whose securities are registered on the public exchanges.

H.R. Rep. No. 73-1383, at 13 (1934). "Congress believed that prompt public disclosure of changes in beneficial ownership by corporate insiders would be a powerful deterrent to the improper use of inside information," and "[s]uch publicity was designed to encourage voluntary compliance with proper fiduciary standards by subjecting insider trades to public scrutiny." Comm. on Fed. Regulation of Sec., *Report of the Task Force on Regulation of Insider Trading* Part II: Reform of Section 16, 42 Bus. Law. 1087, 1099 (1987) (footnote omitted).

In the pre-electronic filing era when Congress and the SEC established the Form 4 regime, the filings were made in paper form with the SEC. In December 1995, the SEC began allowing voluntary electronic filing of Form 4 as an alternative to filing in hard copy with the SEC. *See* SEC Release No. 33-7241 (Nov. 13, 1995). It was not until June 30, 2003, that electronic filing of Form 4s became mandatory. *See* SEC Release No. 33-8230 (May 7, 2003).

The KKR Form 4s were filed between August and November 2002, before electronic filing became mandatory. The plaintiffs complain that this method made the documents sufficiently inaccessible that they are not suitable for judicial notice. But at the time, filing the KKR Form 4s in hard copy complied with then-existing federal law and regulations. Any member of the public who was interested in the Form 4s could examine the SEC's paper files or obtain the documents by paying a private service to retrieve the SEC filings. Although accessing paper files or arranging for someone to do so is certainly less convenient than simply pulling them up on the Internet, Congress and the SEC determined that hard copy filing was sufficient to "expose insiders' trades to public scrutiny . . . ." Romeo & Dye, *supra*, at 8. In light of the Congressional purpose behind the Form 4 filing requirement, there is no basis to distinguish between Form 4s filed electronically and in hard copy.

The Class Complaint does not attach or incorporate by reference the KKR Form 4s. Nevertheless, the KKR Form 4s are properly subject to judicial notice for the purpose of establishing the dates on which the purchases of Preferred Stock were disclosed. The Form 4s are "documents [outside the pleadings] that are required by law to be filed, and are actually filed, with federal . . . officials." *Tyson Foods*, 919 A.2d at 585. Using the Form 4s to determine when the purchases of Preferred Stock were disclosed is consistent with the intent of the federal regime and falls within the permissible scope of Rule 201. When used to determine when the purchases were disclosed, the KKR Form 4s are sources "whose accuracy cannot reasonably be questioned" and the information they contain is "capable of accurate and ready determination." D.R.E. 201(f). As to the KKR Form 4s, the motion to strike is denied.

2. The Other Categories Of Documents

The other categories of documents that the plaintiffs have moved to strike share a singular trait: they were not required by law to be filed, and were not filed publicly with a state or federal agency. To review, the four categories of documents are the Bear Stearns Updates, the Newspaper Articles, the Analyst Call Transcripts, and the Earnings Release.

Like the insurers in *Wal-Mart*, the defendants point to these extrinsic materials to support their argument that plaintiffs were on inquiry notice of the *Brophy* claim more than three years before they filed the Derivative Action. As with the newspaper articles and technical advisory memoranda addressed in *Wal-Mart*, none of these documents were attached to the complaint or incorporated by reference, and the record does not establish that any of them were publicly filed. Under *Wal-Mart*, these materials cannot be considered, and the motion to strike is granted.

B. Accrual

"The general law in [Delaware] is that the statute of limitations . . . begins to run at the time of the wrongful act, and, ignorance of a cause of action, absent concealment or fraud, does not stop it." *Isaacson, Stolper & Co. v. Artisans' Sav. Bank*, 330 A.2d 130, 132 (Del. 1974). Equity follows the law such that "a party's failure to file within the analogous period of limitations will be given great weight in deciding whether the claims are barred by laches." *Whittington v. Dragon Gp., L.L.C.*, 991 A.2d 1, 9 & n.17 (Del. 2009) (citing *Adams v. Jankouskas*, 452 A.2d 148, 157 (Del. 1982)). The limitations period for a breach of fiduciary duty claim is three years. *See* 10 *Del. C.* § 8106(a);

Wal-Mart, 860 A.2d at 319. Any claim filed more than three years after it has accrued is "presumptively time-barred," unless the limitations period was tolled. *Albert v. Alex. Brown Mgmt. Servs., Inc.*, 2005 WL 1594085, at *13 (Del. Ch. June 29, 2005).

"[A]ffirmative defenses, such as laches, are not ordinarily well-suited for treatment on [a motion to dismiss]" or motion for judgment on the pleadings. *Reid v. Spazio*, 970 A.2d 176, 183 (Del. 2009) (footnote omitted). Laches only can be applied at the pleadings stage if "the complaint itself alleges facts that show that the complaint [was] filed too late." *Kahn v. Seaboard Corp.*, 625 A.2d 269, 277 (Del. Ch. 1993) (Allen, C.).

The KKR Form 4s establish that the last purchase of Preferred Stock was disclosed on October 9, 2002. The original derivative complaint was filed on November 29, 2005, more than three years later. Absent tolling, the *Brophy* claim is presumptively time-barred.

C. Equitable Tolling

"[A]fter a cause of action accrues, the 'running' of the limitations period can be 'tolled' in certain limited circumstances." *Wal-Mart*, 860 A.2d at 319 (footnote omitted). "Under the theory of equitable tolling, the statute of limitations is tolled for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, where a plaintiff reasonably relies on the competence and good faith of a fiduciary." *Weiss v. Swanson*, 948 A.2d 433, 451 (Del. Ch. 2008) (footnote omitted). "Equitable tolling usually applies to claims involving self dealing 'where a plaintiff reasonably relies on the competence and good faith of a fiduciary.'" *Pomeranz v. Museum P'rs, L.P.*, 2005 WL

217039, at *3 n.11 (Del. Ch. Jan. 24, 2005) (quoting *In re Dean Witter P'ship Litig.*, 1998 WL 442456, at *6 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999) (TABLE)); *see also U.S. Cellular Inv. Co. of Allentown v. Bell Atl. Mobile Sys., Inc.*, 677 A.2d 497, 503 (Del. 1996) (discussing equitable tolling). The plaintiffs bear the burden of showing that the limitations period was equitably tolled. *Tyson Foods*, 919 A.2d at 585.

"The obvious purpose of the equitable tolling doctrine is to ensure that fiduciaries cannot use their own success at concealing their misconduct as a method of immunizing themselves from accountability for their wrongdoing." *In re Am. Int'l Gp., Inc. Consol. Deriv. Litig.*, 965 A.2d 763, 813 (Del. Ch. 2009) (footnote omitted), *aff'd sub nom. Teachers' Ret. Sys. of La. v. PricewaterhouseCoopers LLP*, 11 A.3d 228 (Del. 2011) (TABLE). "[E]ven an attentive and diligent investor relying, in complete propriety, upon the good faith of fiduciaries may be completely ignorant of transactions that constitute self-interested acts injurious to the [entity]." *Dean Witter*, 1998 WL 442456, at *6 (internal quotation marks and footnote omitted).

When equitable tolling applies, the limitations period is tolled "until the plaintiff is on inquiry notice of their cause of action." *Microsoft Corp. v. Amphus, Inc.*, 2013 WL 5899003, at *17 (Del. Ch. Oct. 31, 2013); *accord Coleman v. PricewaterhouseCoopers, LLC*, 854 A.2d 838, 842 (Del. 2004). "Inquiry notice does not require full knowledge of the material facts . . . ." *Pomeranz*, 2005 WL 217039, at *3. "[R]ather, plaintiffs are on inquiry notice when they have sufficient knowledge to raise their suspicions to the point where persons of ordinary intelligence and prudence would commence an investigation that, if pursued would lead to the discovery of the injury." *Id.* (footnote omitted).

Determining when a stockholder plaintiff is on inquiry notice for a claim that otherwise would survive a motion to dismiss therefore involves a two-step analysis. First, sufficient information must be available to arouse a reasonable stockholder's suspicions. Second, the reasonable stockholder must be able to commence an investigation and discover the facts necessary to plead the claim and survive the motion to dismiss. If the stockholder could not obtain the information necessary to file a viable complaint, then the stockholder could continue to rely reasonably on the competence and good faith of the fiduciary, and equitable tolling would continue to apply.[1]

To plead a *Brophy* claim, a plaintiff must be able to allege that "1) the corporate fiduciary possessed material, nonpublic company information; and 2) the corporate fiduciary used that information improperly by making trades because she was motivated, in whole or in part, by the substance of that information." *In re Oracle Corp. Deriv. Litig.*, 867 A.2d 904, 934 (Del. Ch. 2004), *aff'd*, 872 A.2d 960 (Del. 2005) (TABLE).

---

[1] *See, e.g.*, *Amphus*, 2013 WL 5899003, at *19 (holding claim was not time-barred where "[a] reasonably diligent investigation . . . would not have led [the plaintiff] to discover that [the insider's] statements" about the company's patents having no value were false); *Gibralt Capital Corp. v. Smith*, 2001 WL 647837, at *10 (Del. Ch. May 9, 2001) (declining to dismiss claim as time-barred where plaintiff had notice of only one component of the transaction which, as a whole, constituted a breach of duty); *In re MAXXAM, Inc./Federated Dev. S'holders Litig.*, 1995 WL 376942, at *6-8 (Del. Ch. June 21, 1995) (tolling limitations period, where plaintiffs' claim was based on the unfairness of loan terms due to the high risk associated with the project securing the loan, until plaintiffs uncovered facts about the project's riskiness because the plaintiffs would not have been able to prevail on motion to dismiss until then).

The factual allegations of the complaint must support a rational inference that the insiders actually possessed material nonpublic information and the trades were motivated by this information. *See, e.g.*, *Guttman v. Huang*, 823 A.2d 492, 505 (Del. Ch. 2003) (dismissing complaint that "fail[ed] to allege particularized facts that support[ed] a rational inference that the[] five directors possessed information about [the company's] actual performance that was materially different than existed in the marketplace at the time they traded, much less that they consciously acted to exploit such superior knowledge").

The Class Complaint alleges that the terms of the Merger were unfair because Primedia's board failed to obtain value for the *Brophy* claim. The purchases on which the *Brophy* claim rests fall into two categories: (i) purchases allegedly based on inside information about the American Baby Sale and (ii) purchases allegedly based on inside information that Primedia's business operations were improving, that its earnings for the second quarter of 2002 would exceed industry guidance, and that Primedia remained committed to its asset divestiture strategy.

1. Purchases Based On The American Baby Sale

The *Brophy* claim based on trades leading up to the American Baby Sale focuses on purchases of Preferred Stock that KKR made through its affiliate, ABRA, in September and October 2002. On September 26, ABRA paid $8.5 million for shares of Preferred Stock with a face value of $22.9 million. This purchase was disclosed on the Form 4s filed on September 30. On October 7, ABRA paid $30.7 million for Preferred Stock with a face value of $84.9 million. This purchase was disclosed both in Primedia's third quarter Form 10-Q and on Form 4s filed on October 9. On November 4, Primedia announced the American Baby Sale, and the trading price of its common stock rose by 15%. The trading price of the Series D Preferred rose by 38.4%—double the increase of the common stock price. In my view, the Form 4s and public disclosures surrounding the ABRA trades, together with the announcement of the American Baby Sale, were sufficient to put the plaintiffs on inquiry notice as of November 4, 2002.

Stockholders must exercise "reasonable diligence" when monitoring corporate filings for potential claims. *Weiss*, 948 A.2d at 452. They are entitled to rely on the "competence and good faith of a fiduciary." *Id.* at 451. But they are not entitled to ignore red flags. "[T]he trusting plaintiff still must be reasonably attentive to his interests. Beneficiaries should not put on blinders to such obvious signals as publicly filed documents, annual and quarterly reports, proxy statements, and SEC filings." *Dean Witter*, 1998 WL 442456, at *8 (internal quotation marks and footnote omitted). "Once a plaintiff is on notice of facts that ought to make her suspect wrongdoing, she is obliged to diligently investigate . . . ." *Pomeranz*, 2005 WL 217039, at *13.

In this case, KKR was Primedia's controlling stockholder, and several KKR representatives served on Primedia's board. The KKR Form 4s showed that KKR was purchasing large quantities of Preferred Stock just weeks before the public announcement of a material sale of assets. In response to the public disclosure of the asset sale, the trading price of Primedia's common stock increased by double digits, and the trading price of one of the series of Preferred Stock increased by a much greater amount. These events were a red flag. Unlike in *Weiss*, where the stockholder plaintiff would have had to "piece[] together the alleged [wrongdoing]," 948 A.2d at 452, a stockholder here could readily see a disturbing connection between KKR's purchases and Primedia's announcement. A reasonable stockholder would have been suspicious, satisfying the first step of the test for inquiry notice.

Once reasonably suspicious, a stockholder could have conducted an investigation that would have uncovered the information necessary to file a complaint. Alerted by the advantageous timing of KKR's purchases, a Primedia stockholder could have used Section 220 of the Delaware General Corporation Law, 8 *Del. C.* § 220, to request board minutes concerning the American Baby Sale. The minutes from the board meeting on September 26, 2002, would have shown that the KKR directors were present when the board "approved the sale of the American Baby Group assets subject to liabilities for approximately $115 million in cash." DC ¶ 55. A reasonable investor reviewing those minutes would have focused on the fact that a KKR affiliate paid $8.5 million for Preferred Stock with a face value of $22.9 million on the same day that KKR representatives approved the American Baby Sale. A reasonable investor also would have noted that, less than two weeks later, ABRA paid an additional $30.7 million for Preferred Stock with a face value of $84.9 million, before the American Baby Sale was announced publicly.

Armed with these facts, a reasonable stockholder could have pled a *Brophy* claim that would have survived a motion to dismiss. A *Brophy* claim requires a showing that (i) a fiduciary possessed material nonpublic information and (ii) the fiduciary was motivated to trade, at least in part, by this information. *See Oracle*, 867 A.2d at 934. A stockholder plaintiff armed with the board meeting minutes and the KKR Form 4s would be able to allege the following facts:

- KKR was an insider, and ABRA was KKR's investment vehicle.
- KKR directors were present when the board approved the sale of American Baby for $115 million in cash on September 26, 2002.
- ABRA purchased Preferred Stock with a face value of $22.9 million on the same day that the board approved the American Baby Sale.
- ABRA purchased Preferred Stock with a face value of $84.9 million less than two weeks after the board approved the American Baby Sale, on October 7.
- Primedia publicly announced the American Baby Sale on November 4, and the common stock price rose by 15% and the Series D Preferred price rose by 38.4%.

These facts would have supported an inference that KKR possessed and used material nonpublic information. At the pleadings stage, the stockholder plaintiff would be entitled to the reasonable inference that information about the American Baby Sale was material, as demonstrated by the increase in the trading prices of Primedia's common stock and the Series D Preferred after the news was announced. The stockholder plaintiff also would have been entitled to an inference that, for pleading purposes, the knowledge possessed by the KKR directors was imputed to KKR and ABRA.

Under the circumstances, a stockholder plaintiff would be entitled to an inference that KKR acted with scienter. A court may infer scienter when a trade is "sufficiently unusual in timing and amount." *Pfeiffer v. Toll*, 989 A.2d 683, 694 (Del. Ch. 2010), *abrogated on other grounds by Kohlberg Kravis Roberts*, 23 A.3d 831; *accord In re Suprema Specialties, Inc. Sec. Litig.*, 438 F.3d 256, 277 (3d Cir. 2006) ("[S]ales of company stock by insiders that are unusual in scope or timing may support an inference of scienter.") (internal quotation marks and citation omitted). "Whether a sale is unusual in scope depends on factors such as the amount of profit made, the amount of stock traded, the portion of stockholdings sold, or the number of insiders involved." *Suprema*, 438 F.3d at 277 (internal quotation marks and citation omitted). "Other factors relevant to scope and timing are whether the sales were normal and routine, and whether the profits were substantial relative to the seller's ordinary compensation." *Id.* (internal quotation marks and citation omitted). KKR's purchases of Preferred Stock, through ABRA, were timed conveniently to occur just before the public announcement of the American Baby Sale. Although KKR could point to a purchase of Preferred Stock on November 5, 2002, just after the announcement, as supporting a competing inference inconsistent with insider trading, the plaintiff would receive the benefit of the doubt at the pleadings stage.

A hypothetical stockholder bringing a *Brophy* claim based on ABRA's purchases on September 26 and October 7, 2002, therefore likely would have overcome a motion to dismiss. Accordingly, the *Brophy* claim based on the American Baby Sale accrued on November 4, 2002, and the claim was not equitably tolled. The *Brophy* claim based on the inside information concerning the American Baby Sale was barred by laches.

2. The July Purchases

The other facet of the underlying *Brophy* claim rests on a series of thirteen purchases that ABRA made in July 2002. The Second Quarter 10-Q referenced these purchases in summary fashion, without the purchase dates or amounts for each purchase.

KKR disclosed the precise dates of the trades on Form 4s filed on August 9. On July 31, Primedia announced EBITDA of $65.1 million for the second quarter, which exceeded industry guidance of $58-60 million. Primedia's common stock traded up from $1.00 per share to $1.30 per share.

As with the purchases leading up to the American Baby Sale, the fact that an insider spent $30.5 million to acquire Preferred Stock during the weeks before the announcement of favorable quarterly results should make a reasonable investor suspicious, satisfying the first requirement for inquiry notice. But unlike with the American Baby Sale, any stockholder who tried to investigate would have been stymied in her efforts to obtain the information necessary to draft a viable complaint.

Spurred by the suspicious trading pattern, a reasonable investor would have used Section 220 to request books and records showing what the KKR directors knew about Primedia's second quarter earnings and when they knew it. If an investor had made such a demand, Primedia could have provided the Deferral Agreement, the July 2, 2002 written consent that the board never executed, and the July 8 written consent that was executed on July 12. These documents would have confirmed what the public filings showed: KKR was interested in purchasing, and then in fact purchased, Preferred Stock during July. But these documents would not have revealed anything about the reasons for KKR's purchases or suggested that KKR made its decision to acquire Preferred Stock based on inside information.

The missing link would be the May 21 Memo, and an investigating stockholder could not have used Section 220 to obtain a copy of that document. The May 21 Memo was an internal KKR document. Primedia did not have it to produce in response to a Section 220 demand.

Without the May 21 Memo, it is perhaps possible, but unlikely, that a stockholder could have pled a viable *Brophy* claim relating to the July purchases. Nothing in the Section 220 documents would have shed light on when the KKR representatives on the board learned of Primedia's better-than-expected earnings results. Nothing in the production would have suggested that KKR had direct access to Primedia personnel and, as demonstrated by the May 21 Memo, gained granular insight into Primedia's prospects by talking with the business units. Nor would KKR's purchases necessarily have given rise to an inference of scienter. KKR owned nearly 60% of Primedia's common stock and purchased the entire Series J Preferred Stock issuance for $125 million in August 2001. Purchasing $30.5 million of another series of Preferred Stock might not be deemed sufficiently unusual in timing or amount to support a claim. Moreover, KKR purchased another $5 million of Preferred Stock on August 8, after the earnings release, which was an amount larger than the purchases on July 12, 15, and 26. Without the May 21 Memo, a court might well think that it was unreasonable to draw the inferences necessary to support a *Brophy* claim.

If a stockholder had attempted to pursue a *Brophy* claim based on the July 2002 purchases using the information that was available in the public domain or that could be obtained using Section 220, it is unlikely that the resulting complaint could have survived a motion to dismiss. A *Brophy* claim based on the July transactions was therefore equitably tolled until the discovery of the May 21 Memo in September 2007.

The plaintiffs filed the original derivative complaint on November 29, 2005. Although that complaint focused primarily on Primedia's redemptions of Preferred Stock, the underlying conduct that the complaint challenged included KKR's earlier purchases. A *Brophy* claim based on KKR's purchases therefore relates back to the original complaint, which was filed within the tolling period. *See* Ch. Ct. R. 15(c)(2) ("An amendment of a pleading relates back to the date of the original pleading when . . . (2) the claim . . . asserted in the amended pleading arose out of the conduct, transaction or occurrence set forth or attempted to be set forth in the original pleading."). In August 2007, the plaintiffs filed a second amended complaint that challenged KKR's purchases of Preferred Stock as the usurpation of a corporate opportunity belonging to Primedia. Assuming for the sake of argument that the *Brophy* claim only could relate back to the first time when the plaintiffs specifically challenged the purchases themselves, the claim would relate back to the second amended complaint, which was filed within the tolling period.

III. CONCLUSION

To the extent the Class Claims rest on the purchases in advance of the American Baby Sale, the defense of laches bars the underlying *Brophy* claim, and the motion for judgment on the pleadings is granted. To the extent the Class Claims rest on the purchases in July 2002, the motion for judgment on the pleadings is denied.