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IN THE SIXTH CIRCUIT COURT FOR DAVIDSON COUNTY, TENNESSEE
TWENTIETH JUDICIAL DISTRICT, AT NASHVILLE

In re DOLLAR GENERAL CORPORATION SHAREHOLDER LITIGATION	)))	Master Docket Case No. 07MD-1 (Consolidated Action)
	)	CLASS ACTION
This Document Relates To:	))	Judge Brothers
ALL ACTIONS.	)))	PLAINTIFFS' MEMORANDUM IN OPPOSITION TO THE MOTION FOR SUMMARY JUDGMENT OF DEFENDANTS DOLLAR GENERAL CORPORATION, THE DIRECTORS, AND KOHLBERG KRAVIS ROBERTS & CO. L.P.

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Plaintiffs City of Miami General Employees' & Sanitation Employees' Retirement Trust (the "City of Miami Trust") and William Hochman, IRA, respectfully submit this Memorandum in Opposition to Defendants' Motion for Summary Judgment.[1]

I. PRELIMINARY STATEMENT

The record in this case presents extensive material factual disputes and questions of credibility. Defendants cannot carry their burden to prevail on their motion. The evidence requires a trial, at which Plaintiffs will prove that Dollar General was sold to private equity firm KKR via a sales process that was corrupted from start to end by the personal greed of senior management. Dollar General's senior most executives kept secret their improper dealings with and passing of confidential information to KKR, and they misled the Board, the Board's bankers, and the Company's public shareholders about Dollar General's long-term store growth prospects. As a result of their misconduct, today KKR owns the Company, is now benefitting from one of the few successful businesses in the current down market, and will continue to prosper as a result of the long-term benefits that were concealed from the shareholders and other parties who most needed that information.[2]

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[1] Defendants in this action are Kohlberg Kravis Roberts & Co. L.P., Buck Holdings, L.P., Buck Acquisition Corp. (collectively, "KKR"); Dollar General Corporation ("Dollar General"), and individual members of Dollar General's Board of Directors (collectively, the "Dollar General Defendants").

Defendants' Motion for Summary Judgment is hereinafter referred to as the "Motion" or "Defs' Mem." References to "SAF" are to the paragraphs of Plaintiffs' Response to Defendants' "Statement of Undisputed Facts" and Plaintiffs' Statement of Additional Material Facts

[2] The record shows that KKR's acquisition of Dollar General has been a tremendously successful move for the fund and its investors Dollar General has historically performed exceptionally well in economic downturns and is doing so today. In 2008, Dollar General exceeded even the most optimistic (and undisclosed) of management's pre-closing expectations. SAF ¶¶271-73. As Dollar General's current CEO stated on September 3, 2008, the Company is "benefitting" from "current economic conditions." SAF ¶¶271-73. The Company's same store sales were up over 10% from the prior year, while its operating profit (as measured by adjusted EBITDA) increased by more than 55% from the prior year. *Id.*

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Dollar General CEO David Perdue initiated secret discussions with KKR about a sale of Dollar General in the spring of 2006, withholding this information from his Board and putting his own financial interests ahead of the interests of the Company or its shareholders. Motivated by the prospect of personal riches and encouraged to do so by KKR executive Michael Colbert, Perdue thereafter passed confidential information about Board deliberations to KKR.[3] As admitted by Board member Dick Thornburgh: ***"I think [Perdue's] behavior ... suggested that [he] was looking to line his pockets with money as opposed to maybe doing the right thing for the company."*** SAF ¶135. Defendants' own corporate governance expert concludes that Perdue's conduct – if true – was "inappropriate," "improper" and "ill-advised.[4] *See generally* Section II.B.

The evidence shows that Dollar General's senior management analyzed and anticipated significant profitable store growth opportunities for many years to come. In support of their goal of selling the Company to KKR, Perdue and Chief Operating Officer David Beré withheld this crucial information about future store growth from the Board, the Board's banker (Lazard), and the public shareholders. Lazard's fairness opinion, presented to the Board, rested on the assumption that Dollar General would have no store growth after 2011. Perdue and Beré never advised the Board otherwise, despite knowing and privately advising KKR that the existing corporate plans supported profitably adding over 7,000 new stores. As a result, the Proxy issued to shareholders on May 21, 2007 misleadingly

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[4] Perdue and KKR executive Michael Calbert tell conflicting stories about the numerous conversations in which Perdue passed confidential information to KKR, SAF ¶¶104-05, 112-13, 115-16, 121-124, 130. This, in itself, raises credibility issues for trial

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represented that Dollar General would have no store growth after 2011 – a claim that was also represented as having been reviewed and approved by Dollar General management. *See* Section II.C, below. At the very same time, Perdue and Beré, along with KKR, were privately touting to potential equity investors and lenders in the new private company, as well as debt rating agencies, the ability to open between 7,000 and 11,000 new stores on an extremely profitable basis – enjoying an internal rate of return ("IRR") in excess of 20%. *See* Section II.C.2, below.

Defendants are internally conflicted on whether there was, in fact, a plan for store growth. While Defendants now devote an entire section of their brief to arguing that Dollar General's store growth plans were fully disclosed to all interested parties, they argued in their brief opposing injunctive relief that: "***There is no plan by Dollar General to open 7,103 to 10,903 future stores.***"[5] Nevertheless, their current argument rests not only on the Board's supposed knowledge of this strategy, but also on market research analysts who publicly speculated about the Company's store growth prospects. In other words, Defendants suggest that shareholders should have known that the Proxy's assertion of no growth after 2011 was false. *See* Section II.C.1, below.

Either way, the facts show that the information in the market was conflicting and insufficient to draw reliable conclusions. Indeed Michael Calbert of KKR testified that the publicly available information raised concerns about potential store growth, forcing KKR to

[5] All emphasis in this Memorandum is added, unless otherwise noted.

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privately commission an expert study to verify whether the optimistic growth prospects disclosed by Perdue were in fact achievable. *See* Section II.C.3, below.

The record regarding the Board's knowledge is also disputed. Director Bottorff suggests that he (and possibly other) board members had actually been informed about Dollar General's post-2011 growth prospects. Director Thornburgh, one of three members of the Strategic Planning Committee ("SPC"), testified to the contrary, stating that the Board had not done an analysis of the number of stores the Company could open nationwide, and that he was unaware whether management had done that analysis. Similarly, Director Knuckles testified that none of the discussions at the board level regarding store growth addressed expectations beyond the year 2011. *See* Section II.C.2. Put simply, Defendants themselves cannot demonstrate that the Outside Directors were, or were not, informed about the key store growth information. That said, no director claims that store growth opportunities were considered and rejected in approving and recommending the merger – a consideration that would have led them to realize that KKR was underpaying for Dollar General upwards of a billion dollars.[6]

Despite this evidence, the Dollar General Defendants – who owed fiduciary duties of loyalty, good faith, and candor to shareholders – ask this Court to shield them from a trial at which they would be called on to defend their actions. Defendants invoke four primary

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[6] Defendants do not argue for summary judgment on the basis that the price was fair and adequate, so we do not address that issue here. At trial, Plaintiffs will present expert testimony on value, including that the $22 price was inadequate, that the Company's value, when taking growth into account was over $27 per share and that Lazard's fairness opinion analysis (which assumed no store growth beyond 2011) rested on false assumptions SAF ¶¶213-14. Indeed, Defendants' own valuation expert, Professor Lehn stated his agreement with Ms. O'Connor that "[i]f you feel there is more opportunity for value [ ] creation" after 2011, "then you should extend the forecast period until you think that it's been exhausted " SAF ¶212.

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affirmative defenses: the exculpatory provisions of Dollar General's charter; the presumption of the "business judgment rule"; a defense of the corporate sales process; and ratification. All of these affirmative defenses raise material issues of fact and none justify a dismissal as a matter of law.

First, the exculpatory provisions of Dollar General's charter, barring money damages for breach of fiduciary duty, only protects ***innocent*** Directors from liability, as testified to by Defendant's own expert, Professor Coffee. It does not protect Directors who personally participated in bad faith or disloyal breaches of their fiduciary duties or third parties like KKR, who aid and abet those breaches. The evidence is that Defendants Perdue and Beré breached their duties to shareholders in the pursuit of personal gain, and having breached their duties, they are not entitled to exculpation.[7] Moreover, although Plaintiffs have long believed that the Outside Directors did not know of the Company's store growth plans, Defendants' most recent submissions, including the affidavit of Dennis Bottorff, raise questions of whether those Directors knew of the misstatements in the Proxy.[8]

While Defendants argue that denying summary judgment would have a chilling effect on innocent Directors, the opposite is the case: if the actions of the outside Directors were tainted by the misconduct of Perdue and Beré, the outside directors would be personally entitled to the exculpatory provisions. If they were knowing participants, they were not

[7] Plaintiffs' expert, Professor Black, testified that Perdue and Beré should be held liable for their conduct, and the presence of outside directors who may be innocent of wrongdoing is no basis to deny shareholders a proper remedy. SAF ¶138; Johnston Ex. 58 at 12-13.

[8] Plaintiffs have long been, and remain, willing to dismiss from the case the Director Defendants other than Perdue, Beré, and Bottorff, if they agree to be available to appear as witnesses at trial, and are willing to represent they did not approve of the Proxy representations of zero store growth after 2011 while knowing of Dollar General's true store growth potential.

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innocent and should be held liable. Holding the wrongdoers liable, however, encourages outside directors to serve with confidence that insiders are held to proper standards of disclosure to Tennessee boards.

Second, in Tennessee the application of the business judgment is not intended to insulate violations of fiduciary duties of loyalty, good faith, and candor. *Summers v. Cherokee Children & Family Services.* 112 S.W.3d 486,527 (Tehn. Ct. App. 2002). This record contains significant evidence of misconduct by Perdue and Beré. Indeed, admissions by Thornburgh, Calbert and Coffee as to Perdue's conduct are sufficient, standing alone, to establish material issues of fact as to whether Perdue breached his duties. The evidence is that Perdue and Beré discussed the Company's aggressive store growth plans with KKR (and with potential investors in the KKR deal) while simultaneously failing to so inform either the Board, its financial advisors, or the shareholders (in the Proxy) that such substantial future store growth potential existed and should be considered. When the processes of an otherwise independent board are tainted by the breaches of their peers, the business judgment rule cannot shield the transaction from judicial scrutiny.[9]

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[9] As the Delaware Supreme Court stated in another case involving KKR "[W]hen a board is deceived by those who will gain from such misconduct, the protections girding the decision itself vanish. Decisions made on such a basis are voidable at the behest of innocent parties to whom a fiduciary duty was owed and breached, and whose interests were thereby materially and adversely affected" *Mills Acquisition Co v MacMillan, Inc.*, 559 A 2d 1261, 1284 (Del 1989); *see also City of Pontiac*, slip op at 2 ("If a director or officer does not inform itself, prior to voting on the acquisition, of all material information reasonably available to it or has a material interest in the transaction or fails to provide candid disclosure to the shareholders in connection with the vote, the assumptions of the business judgment rule do not hold true In such a case, the business judgment rule does not apply to shield the directors' decision Instead, the defendants bear the burden of demonstrating the entire fairness of the transaction to the company's shareholders.").

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Third, Defendants' argument that the sales process was "exemplary" rests on a tower of disputed facts. Among other things, KKR had a long and meaningful "head start," and Bain, the only other party invited to bid for Dollar General, may well have had a limited interest in acquiring Dollar General for various reasons, including its existing ownership of discount retailer Dollarama.[10] There is no question the parties vigorously dispute the nature of the sales process, and that this question can only be resolved through a trial.

Finally, Defendants argue ratification, pointing to the presence of a majority of purportedly independent directors and a percentage of shareholders who voted in favor of the transaction. Under Tennessee law, even approval by fully informed directors – and the record on this score is hotly disputed – would not provide for ratification warranting summary judgment. As the Tennessee Court of Appeals held when ruling on a "conflicted transaction" pursuant to a corporate statute identical to Tennessee's statute, Tenn. Code Ann. §48-18-302(a), "the purpose of [a ratification statute] is to create a framework within which corporations can enter into binding agreements, even where conflicts of interest arise from such agreements, ***not to shield corporate directors from liability for breaches of their fiduciary duties***." *McRedmond v Estate of Marianelli*, 46 S.W.3d 730, 741 (Tenn. Ct. App. 2000). Moreover, ratification is unavailable as a defense where the shareholder vote was not fully informed due to a misleading Proxy or where loyalty or bad faith violations are at issue. *See Iseman v Liquid Air Corp.*, C.A. No. 9694, 1993 Del. Ch. LEXIS 24 (Del. Ch. Feb. 11, 1993). Given the factual dispute between the parties over what was disclosed to the Outside

[10] As Plaintiffs' expert Robert Reilly testified, private equity firms enter and pull out of bidding processes for various reasons other than price, and Bain's decision to pull out of the bidding is not a reason to infer KKR paid a fair price. SAF ¶¶197-202

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Directors and the material disclosures in the Proxy, ratification is unavailable to Defendants on summary judgment.

In sum, Defendants' arguments are without merit. There is substantial evidence of breaches of duty, and critical disputes as to the truthfulness, meaning, and interpretation of that evidence, both between Plaintiffs and Defendants, and among Defendants themselves. The record in this case is not, as Defendants assert in requesting summary judgment, susceptible of only benign interpretations. Defendants' Motion should be denied.

II. SUMMARY OF DISPUTED FACTS

A. Overview of Dollar General and the Going Private Transaction

By mid-2006, Dollar General was one of the nation's leading discount retailers, with over 8,000 stores. SAF ¶2. In late November 2006, Dollar General announced the implementation of "Project Alpha" – a comprehensive program designed to increase the Company's long-term profitability by modifying the way the Company handled its inventory and by improving its real estate operations, including closing hundreds of stores. SAF ¶15.

Just three months later, on March 12, 2007, without any previous public announcements, Dollar General published a press release announcing that its Board had approved the sale of the Company to an affiliate of KKR for $22 per share in a "going-private" transaction. SAF ¶70. At no time prior to this announcement had Dollar General publicly disclosed that it was interested in selling the Company, that it was in discussions with potential buyers, that it had received overtures from private equity firms, or that it was pursuing strategic alternatives that could end its existence as an independent public company.

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On May 21, 2007, the Company sent the Proxy to shareholders. SAF ¶266. The Proxy included projections of Dollar General's future financial performance that were endorsed by company management as being reasonable and relied upon by Lazard, the Board's financial advisor, in opining that the transaction was fair. SAF ¶205. These projections reflected "no additional store openings in perpetuity" beyond the year 2011, and a "perpetuity growth rate" less than the rate of inflation. SAF ¶204. Contrary to Defendants' arguments throughout their motion, these dismal growth projections were contrary to the true belief of Dollar General management (SAF ¶¶214-241) and resulted in a shareholders being told that $22 per share was a fair price for the Company when, in fact, it undervalued Dollar General by as much as $3 - $4 per share. SAF ¶213.

The Proxy also omitted the serial process failure detailed below. Not surprisingly, given the intentionally misleading and incomplete information they had been provided, on June 21, 2007, the shareholders of Dollar General voted to approve the going-private transaction.

B. The Sales Process was Compromised from the Start by Perdue's Self-Interested Breaches of Fiduciary Duty

Contrary to Defendants' representations that the transaction with KKR was a product of an unsolicited, arms-length transaction, the record evidences serious misconduct by Dollar General's CEO and Chairman of the Board of Directors, David Perdue, in a sales process that favored KKR to the detriment of Dollar General's public shareholders.

From the outset, it was Perdue's intention to take the Company private in an exclusive deal with KKR, with the expectation that he would be CEO of the newly-private company and in a position to reap enormous personal rewards. During a meeting that took

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place in New York in April 2006 with John Wood, a Managing Director at executive recruiting firm Spencer Stuart, Perdue expressed an interest in taking Dollar General private. SAF ¶86 Wood steered Perdue to senior KKR executive and long-time Spencer Stuart client Mike Calbert, (SAF ¶88), and directly communicated Perdue's interest to Calbert by email. SAF ¶88.[11]

Thereafter, in June 2006, Perdue sought to meet privately with KKR founder George Roberts at the Bohemian Grove in San Francisco. SAF ¶89. Perdue subsequently met on August 11 at KKR's San Francisco office with Roberts and Calbert to discuss a potential acquisition of Dollar General. SAF ¶90. Following the meeting, KKR proposed entering into a confidentiality agreement and starting due diligence, as confirmed in a follow-up email sent by Calbert to Perdue on Sunday, August 13:

> David –
>
> George… and I appreciate you stopping by for lunch on Friday. We all enjoyed meeting you and are excited about working together to see if we can be helpful to you in achieving your objectives. You have made a lot of progress in "professionalizing" and moving the business forward. We think there is a real opportunity to accelerate this progress as a private company.
>
> ***We will turn around a confidentiality agreement next week and schedule a follow-up meeting to get started. . . .***

SAF ¶91.

Perdue's response demonstrated his desire to engage exclusively with KKR (which is well known for engaging in management-friendly deals), and his reluctance to come clean with his Board. As stated in an August 17 email from Calbert to Roberts:

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[11] Lehman, retained as management's financial advisor, also claimed credit for steering Perdue to KKR at the outset of the process *See* SAF ¶174

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> We received a call from Perdue this morning....
>
> He repeated he has met with TPG (Bonderman) and Goldman PIA (Adrian Jones) and that ***he wants to pursue a transaction exclusively with us.***
>
> He [Perdue] wants to wait until after his board mtg week after next (8/29) before he engages in due diligence. ***He is concerned he will get in "too deep" before the meeting and feel compelled to tell the board...***

SAF ¶93.

To accommodate Perdue's desire to keep the Board in the dark until he could better assure support for a management-led buyout with KKR, no confidentiality agreement was entered into at that time. SAF ¶96.[12] Nonetheless, according to contemporaneous emails, Perdue shared important information with KKR at this meeting, including the fact that Dollar General was embarking on a major strategic shift, later known as Project Alpha. SAF ¶91.

Defendants contend that minutes of Dollar General's August 29 Board meeting reflect that Perdue informed the Board about the substance of his contacts with KKR. (Defs' Mem. at 5 n.6). Facts elicited in discovery dispute this assertion. Director Thornburgh testified that Perdue did not inform the Dollar General Board of his August meeting with KKR. SAF ¶134. Directors Bowles and Bottorff concurred. SAF ¶134. Indeed, even the minutes themselves dispute this assertion as they neither mention KKR nor a possible going-private transaction. And the minutes clearly do not reflect any disclosure that Perdue had worked for months to set up meetings and had specific discussions with KKR about selling the Company, much less that KKR proposed entering a confidentiality agreement and starting

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[12] The parties also dispute the motivations and meaning of Perdue in telling KKR he did not want to "get in too deep" and feel "compelled to tell the Board." *See* SAF ¶93. Indeed, Defendants' own corporate governance expert, Professor Coffee, opined that the paper record in this case was insufficient to allow him to reach conclusions about Perdue's or Calbert's true motivations. SAF ¶132.

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due diligence. Instead, the minutes merely state that Perdue "summarized his discussions with certain investment bankers and private equity firms regarding the Company's position in light of its stock price and the active mergers and acquisitions market." SAF ¶96.

It was not until a month later, on September 19, that Perdue apparently first approached a single Board member to lay the groundwork for an *exclusive* KKR bid. Perdue immediately relayed the substance of this sensitive conversation to KKR, as reflected in a September 20, 2006 email from Calbert to Roberts:

> George
>
> I had a good conversation with David Perdue last night. He had just left a meeting with his 'most influential board member' (not technically lead director [Wilds]) who was very supportive of him engaging ***exclusively with us***. The director encouraged David to preview the idea with Cal Turner (family owns roughly 17%) and one other director (former CSFB banker [Thornburgh]). David plans on having both conversations over the next few days.
>
> As we discussed, I offered up you and I walking Cal though how a buyout would work. . . . David appears very excited about moving forward. . . .

SAF ¶98.

There is even dispute over who the "most influential board member" with whom Perdue purportedly met and whose views were relayed to KKR. Perdue testified that he did not "remember the conversation specifically," so he could not confirm the identity of this Director. SAF ¶103. Thornburgh thought that this was in reference to Bottorff, which would accord with Bottorff's long-standing and dominant role on the Board of Directors. SAF ¶102. Bottorff, on the other hand, testified that he only became aware of the conversations with KKR, on October 5, more than two weeks after the aforementioned email, at which point he claimed to immediately bring the issue to the Board. SAF ¶109.

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In any event, on October 5 Calbert and Roberts flew to Nashville to meet with Perdue, Cal Turner Jr. (Dollar General's largest shareholder, former CEO, and member of the founding Turner family) and Defendant Wilds (the lead Board member and Turner family advisor). SAF ¶106. Other than Defendants Perdue and Wilds, none of the remaining members of the Board were apparently advised that any meeting was going to take place or authorized the meeting, much less were they informed of the long-running efforts by Perdue and KKR to arrange a sale of the Company. SAF ¶134.

The next day, Calbert emailed Roberts to relate a follow-up call with Perdue. In that call, Perdue again disclosed confidential information to Calbert about his discussions with Board members and their views of a potential transaction. Calbert – despite knowing that Perdue was not authorized to reveal the contents of confidential Board discussions – coached Perdue on how to persuade the other Directors to support Perdue's and KKR's common goal:

> David Perdue called this afternoon…
>
> … David Wild (lead director) is requesting a board meeting Sunday night during which he wants to disclose the conversation with KKR, form a special committee and recommend we be allowed to begin our due diligence…
>
> ***Perdue and Wild spoke with Denny Bottorff, board member and head of governance committee, today and according to Perdue, Denny is in favor of the transaction.***
>
> Dick Thornburgh… appears to not be excited about the transaction. ***David and I spoke about the need to get him on [our] side.***
>
> ***David and I went through his "pitch" to the board again focusing on the positive merits of the transaction….***

SAF ¶111.

On October 8, 2006, the full Board, having been informed of the October 5 meeting in Nashville with KKR, held a teleconference. SAF ¶114. Only then did it become evident to

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the full Board that Perdue should not be the Company representative in connection with dealing with KKR and that his prior conduct was not the proper way to act as CEO. Indeed, Director Thornburgh flatly acknowledged that Perdue's actions were self-interested and constituted a breach of fiduciary duty, testifying that Perdue's "behavior was inappropriate as a process" and that Perdue was looking to "line his pockets with money as opposed to maybe doing the right thing for the company." SAF ¶135.[13]

In light of Perdue's conduct, the Board agreed to establish a "Strategic Planning Committee" (the "SPC"), originally consisting of Directors Bottorff, Thornburgh, Beré, and Bowles. SAF ¶117-18.

Perdue, in turn, wasted no time reporting to KKR. He called Calbert the morning after the October 8 meeting to once again leak information about the Board's deliberations, including the highly confidential and strategically invaluable views expressed by individual Directors. According to an email Calbert wrote to Roberts on October 9:

> I caught up with David [Perdue] this morning. ***He said the board call last night was controversial with 2 directors (Thornburgh and one other) expressing views that going private wasn't the right course of action . . . David Wilds and Denny [Bottorff] (head of governance committee) led the charge for the transaction. There also were views expressed that Perdue and Wilds are conflicted and our meeting Thursday was inappropriate. . . .***
>
> The board is using the governance committee as the special committee to review the transaction. The ***official*** response from the board to us is "... we have taken your proposal under consideration."
>
> ***Perdue is off having one on one meetings with the directors to make his case. He said that Cal, Wilds and Denny all want to do the transaction...***

[13] Similarly, Defendant Beré expressed shock ***when learning for the first time at his deposition*** of Perdue's long-running, covert communication with KKR. SAF ¶135.

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SAF ¶120.

Having been informed by Perdue of the Board's deliberations, Calbert complained to Perdue that he had heard of a banker expressing an interest in Dollar General and indicating that KKR might face competition for Dollar General – in Calbert's words, that "[t]his opportunity is starting to get a lot of attention." SAF ¶120. In response, Perdue promised Calbert he would ***"call and put a gag"*** on the bankers at Lehman that Perdue had hired (without first obtaining Board approval) for advice, and assured Calbert that KKR was ***"the only firm he is speaking with."*** SAF ¶120.

Three days later, on October 11, 2006, Perdue had a conversation with Calbert in which Perdue went through the position of each Director – "for and against" – a potential transaction with KKR. He also told Calbert what the Board had directed Perdue to tell to "other" bidders. In return, Calbert once again coached Perdue on how best to get the Board in favor of a transaction with only KKR. SAF ¶126. As stated by Calbert in an update to Roberts:

> [I] spoke with Perdue . . . . The BOD gave him a message to deliver to ***other*** bidders – "Pursuing strategic plan, not interested in looking at anything else." Perdue doesn't think the BOD will do anything before 11/3 board mtg when he will outline the restructuring plan. ***He went through the BOD identifying for and against. I encouraged him to get 2 directors to be his advocates for the transaction*** . . . .

SAF ¶126.

On November 9, 2006, over a month ***after*** Defendants claim the SPC took complete control over the process and took any authority to deal with potential bidders (including purportedly KKR) away from Perdue, Perdue gave Calbert another update on the Board's

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feelings toward a buy-out as well as other strategic alternatives. SAF ¶128.[14] Perdue again divulged important information regarding the Company's plans for restructuring and improving the business, plans that were not fully disclosed to Dollar General shareholders until November 29, 2006. *Id.* Perdue also informed Calbert that he "continue[d] to think that the lead director of the special committee [Defendant Bottorff] [was] supportive of going private and believe[d] it [was] the right solution for the company." *Id.*

Defendants argue that these backchannel communications between Perdue and Calbert – characterized by their own expert, Professor Coffee as "inappropriate," "ill-advised" and "improper" (SAF ¶136) – were essentially meaningless and harmless, and had no "impact on the process subsequently initiated by the Board and the SPC in December 2006." (See Def. Memorandum at 31-21). This too is disputed. Professor Black, Plaintiffs' expert, will testify that it was not only highly improper for Perdue to divulge Board discussions and non-public information, but it in and of itself was a breach of fiduciary duty. SAF ¶138. To a buyout firm like KKR, the type of inside information and assistance provided by Perdue was unattainable anywhere else and harmed shareholders by denying them an unbiased process relating to the sale of the Company. Perdue not only acted as KKR's "inside man" at Dollar General, providing confidential information about the sales

[14] The November 9 email is the last in the immediate trail of emails from Calbert to Roberts, in which Calbert describes conversations with Perdue. Defendants argue this means that the "discussions" between Calbert and Perdue ended (Defs' Mem at 31) However, Defendants offer no support for this conclusion, and it is belied by the evidence In February, Perdue gave a critical presentation to the KKR deal team, including Calbert, in which Perdue stated that the company would be able to expand to as many as 15,000 - 20,000 total stores. SAF ¶222 In addition, the evidence is that Calbert and other members of the KKR deal team had continued access to Perdue throughout the process

Indeed, the equally likely inference is that Calbert and Perdue continued their communication, but that Calbert did not continue reporting on those communications by email.

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process, about Board meetings, and about the thought process of individual directors, he further made efforts to dissuade "other" bidders, and to "gag" Dollar General's own investment bankers in his efforts to promote an "exclusive" process with KKR.

Defendants attempt to deflect from this improper relationship, or any conflict of interest, on the basis that, ultimately, Perdue did not, in fact, become CEO of the newly-private Dollar General. (Defs' Mem. at 4, 21). The evidence, however, reveals that (i) Perdue, at all relevant times, believed and acted as if he would be the CEO of Dollar General post-acquisition by KKR; and (ii) KKR never said or did anything to dissuade Perdue of this belief, but rather encouraged it. SAF ¶139-145. In fact, Perdue testified that he "hoped" he would have a future opportunity with the Company post-acquisition and he did not learn until April 2007 – after the deal was approved – that KKR had no further use for his services. SAF ¶139.

Indeed, in April 2007 – a month ***after*** the Board approved the deal – Perdue had another meeting with John Wood of Spencer Stuart for the purpose of discussing a possible assignment Perdue was going to give to Spencer Stuart to find a new head of stores for Dollar General where Perdue still maintained the strong expectation of remaining CEO. SAF ¶140 Calbert emailed Wood on April 12 to ask whether Perdue had "come to see him," and Wood responded on April 13 as follows:

> Yes, Tuesday. Very cordial. Big fan of KKR, and specifically you. ***Told us . . . he looks forward to working with you.*** Asked us to consider finding a new head of stores . . . .

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SAF ¶141.[15]

Unfortunately for Perdue, Calbert had long before decided to fire Perdue and retain a new CEO and had relayed this information to Wood. Calbert was, however, interested in learning from Wood whether Perdue "had any idea what was coming." SAF ¶142. Wood responded: "From every indication, I am convinced he [Perdue] has no idea of his fate." SAF ¶142. In a follow up email the same day, Wood was even clearer: "No way he knows. He came across as large and in charge." SAF ¶138. Calbert, having successfully kept Perdue in the dark about his already-planned termination, responded dryly, saying that Perdue "clearly has a 'self-awareness' issue" and further that "I'm sure when I have the 'not moving forward' conversation with him [Perdue] he will reach out for you." SAF ¶¶140-43. In fact, despite knowing as early as February of 2007 that it had no intention of keeping Perdue as CEO post-acquisition, (SAF ¶145), KKR waited until late-April 2007 – once Perdue was no longer useful to KKR – to inform Perdue of his fate. SAF ¶145.

Notably, the Proxy failed to disclose the truth about Perdue's dealings with KKR, Lazard, and the Board.

C. Dollar General Management and KKR Concealed the Company's Store Growth Plans from the Company's Shareholders, Outside Directors and Lazard

The Proxy issued by Dollar General to shareholders on May 21, 2007 was materially misleading regarding the critical issue of the Company's future growth. The Proxy stated:

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[15] Wood's handwritten notes from his April 2007 meeting with Perdue also provide insight into David Perdue's thoughts about the value of the deal. The first line of Wood's notes, which capture Perdue's words, state emphatically: "***KKR slam dunk at 22***." SAF ¶144. Perdue, who still expected to be CEO of the private Dollar General at this time, was evidently expressing the view that $22 was a great outcome for KKR and for himself, as he expected to participate in the equity.

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> In calculating the terminal value of Dollar General, Lazard assumed perpetuity growth rates ranging from 2.00% to 2.50% for the projected free cash flows for periods subsequent to 2011. The perpetuity growth rates were applied to the projected free cash flow for 2011, ***as adjusted to reflect no additional store openings in perpetuity***, resulting in a lower sales growth rate and lower capital expenditures.

SAF ¶204.

In other words, Lazard's valuation of the Company – one of the most important data points shareholders look to in assessing the offer – represented that there would be no store growth after 2011. The Proxy is also clear that these projections of no store growth post-2011 were reviewed and approved by Dollar General's management:

> The extrapolated projections for the fiscal years 2010 and 2011 for the Alpha Case and the Alternative Case, respectively, which were prepared by Lazard, ***were reviewed by Dollar General's management and deemed reasonable by them.***

SAF ¶205.

While Defendants may dispute the degree and extent of store growth opportunities at Dollar General, they do not and cannot dispute that it is axiomatic that a retailer's plans for future store growth is one of the key metrics to evaluate the future prospects, and value, of the Company. SAF ¶206. Faced with this reality, Defendants (i) take contradictory positions about future store growth plans, as set forth in section II.C.1 below; (ii) dispute the significance of Dollar General's actual store growth plans, as detailed in Section II.C.2; and (iii) falsely claim that their own misleading statements are somehow cured by other, purportedly more forthright, disclosures in the "market," as discussed in Section II.B.3. Defendants' factual support for their arguments about store growth is disputed by other evidence in the record.

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1. Defendants' Own Contradictory Positions Regarding Dollar General's Long-Term Store Growth Strategies

Defendants' Motion argues that Dollar General's long-term growth strategies were known to the market, and that this defeats Plaintiffs' disclosure claims (Defs' Mem. at 39-43). However, prior to making the current Motion, Defendants had contended throughout this litigation that Dollar General had no future growth strategies, and certainly not on the scale that Plaintiffs allege. Defendants' contradictory positions –first, that there was no long-term store growth strategy; and second, that, not only was there a strategy, but it was fully disclosed to investors – are alone a sufficient dispute of material fact to deny summary judgment.

Specifically during expedited discovery, prior to the June 13, 2007 preliminary injunction hearing in this case, Plaintiffs learned that KKR and Dollar General management were informing ratings agencies and potential investors in the privatized Dollar General that the Company had very strong store growth opportunities. These facts were inconsistent with the projections disclosed to Dollar General's shareholders in the Proxy. In particular, Plaintiffs focused on an April 2007 presentation to potential equity co-investors in the privatized Dollar General, which laid out (on page 24 of the presentation) a plan to profitably increase the number of stores by 8,000 – 11,000. SAF ¶235-34 At the time of the preliminary injunction hearing, however, Plaintiffs' evidence of the growth prospects rested solely on documents, such as the April presentation, that were created by KKR after the signing of the merger agreement, and Plaintiffs could only raise the inference that the plans pre-existed the merger agreement.

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At the preliminary injunction hearing, Defendants argued that there was no basis for the Court to accept that inference. In their Memorandum in Opposition to Plaintiffs' Motion for a Temporary Injunction ("Opp. To Injunction"), Defendants stated as follows:

> **<u>There is no plan by Dollar General to open 7,103 to 10,903 future stores</u>**
>
> Plaintiffs falsely accuse defendants of hiding an April 2007 "management" presentation' that supposedly "shows that the Company's prospects are far greater than shareholders are being led to believe." Pl. Br. 30-31
>
> * * *
>
> Moreover, page 24 of the April 2007 presentation is not a "plan" for Dollar General. Rather, it is an analysis by a KKR consultant, Applied Predictive Technologies, of an "opportunity" that may exist at some point in the future for the Company. ***There is no evidence of a plan by Dollar General (or KKR for that matter) to open up 7,103 to 10,903 additional Dollar General stores.***

Opp. to Injunction, page 35.

Defendants' insistence that there was no store growth plan among Dollar General's management continued until the filing of their summary judgment papers. As recently as September 19, 2008, Defendant's expert Professor Coffee opined that Plaintiffs' claims regarding store growth were mere "fabrications" and a "phantom theory":

> Here, Plaintiffs press a theory of materiality based on their claim that DG planned to grow "from 8,000 stores to 15,000-18,000 stores – more than doubling in size." . . . ***[T]his alleged store expansion plan seems simply a fabrication of Plaintiffs*** . . . . Project Alpha [] actually contemplated store closings and a restructuring, not a willy-nilly expansion and a doubling of stores.
>
> [T]here is no credible evidence that Dollar General's board had any concealed plan to increase store openings (and would have done so but for the KKR merger). In fact, Plaintiffs, themselves, assert that the Dollar General board knew nothing of any plans to double, or even increase, their number of stores.
>
> * * *

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> ***So much for Plaintiffs' phantom theory about a plan to double the number of stores!***

SAF ¶263.

At his deposition, Professor Coffee argued yet again on behalf of Defendants that there was no future store growth strategy after Project Alpha was approved by the Board in late 2006. In critiquing the conclusions of Plaintiffs' expert, Coffee stated:

> [Professor Black] tends to assume that there was a plan for secret growth and I think that is very much an issue here and I regard it as a fiction. I don't think there was any plan. I think your own filings have shown that you have alleged that the board of directors knew nothing about any secret plan for growth and I think you're quite correct, none of the directors did.....

SAF ¶264.

Defendants' summary judgment motion incorporates both Coffee's report and testimony that there was no store growth plan. At the same time, Defendants argue at length that, not only was the Board aware of these issues, but that the investing community knew as well. *See* Defs. Mem. at 39-43.

The contradictions between Defendants' own longstanding position that long-term store growth was a non-issue – as put forward at the preliminary injunction stage, and as expressed by Professor Coffee – and the positions now taken in Defendants' summary judgment brief are sufficient in themselves to defeat summary judgment.

2. Dollar General's Management Had A Strategy For Future Store Growth, Which Was Not Disclosed to Shareholders, Lazard or the Outside Directors

Store growth opportunities and plans for store growth were, in fact, central to Dollar General's long-term strategy both before and after entering into the merger agreement with KKR, and while shareholders were being solicited to vote in favor of the merger. In April

2007, after the merger agreement was signed, but before the Proxy was drafted, Dollar General senior management, including Perdue and Beré made private presentations urging certain sophisticated investors to co-invest along with the management team and KKR in the $22/share acquisition. SAF ¶239. Dollar General management presented to potential investors the following slide regarding store growth:

Real Estate – New Store Growth Opportunity

DOLLAR GENERAL

Current Economic Model		Sensitivity on Improved Margins (200bps)	
IRR Hurdle	New Store Potential	IRR Hurdle	New Store Potential
20%	7,103	20%	10,903
30%	315	30%	9,084
40%	3	40%	1,577

Potential for over 7,000 new stores at a 20% IRR hurdle rate

Potential for almost 11,000 stores at a 20% IRR hurdle rate

Approx. 60% of new stores projected to be in DG's current markets →DG's core markets provide a tremendous amount of opportunity.

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SAF ¶234.

The column headed "Current Economic Model" shows that under Dollar General's current business model, 7,000 new stores could be opened with a 20% or greater internal rate of return. The "Sensitivity on Improved Margins" column tells potential investors in the privatized Dollar General that if KKR could improve store margins by 200 basis points, then

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10,903 new stores could be opened with the same 20% internal rate of return. SAF ¶234-236.

Evidence learned ***after*** the preliminary injunction hearing shows that this slide did not show just a possibility or a new strategy created by KKR, but a long-standing plan to add 7,000 plus stores at 20% or greater returns. Several years ago, Dollar General management commissioned a detailed, national, county-by-county study to evaluate the precise number of stores the Company could open over time before reaching a state of "saturation," *i.e* , the point at which opening new stores would not be profitable. SAF ¶¶214-16.

Management incorporated this study into its internal development of strategy. Beré testified that the plan to grow stores at a 20% hurdle rate had long been in place at Dollar General, stating "[w]e had a plan – a new store growth plan. The company's had it for years." SAF ¶219. He went on, "The real estate – to go through the real estate models, I believe it had to be in the 20 percent range." SAF ¶219 Beré further testified that, after Project Alpha, there was "absolutely" room for store growth up to over 16,000, SAF ¶220; and that, just as the Company had room for significant store growth five years ago, the same opportunity for growth "will be true five years from now" SAF ¶220

This information is fully consistent with information Perdue provided to Calbert and Raj Agrawal of KKR on February 12, 2007, well prior to KKR submitting its offer, where Perdue disclosed there was a new Dollar General store opportunity of 15,000 to 20,000 total

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stores.[16] SAF ¶222 That KKR thought this disclosure was material is evidenced by the fact that both Calbert and Agrawal wrote it down in their notes of the meeting. *Id.*

In order to confirm the accuracy of the information Perdue had privately conveyed to them, KKR retained a consulting firm, Applied Predictive Technologies ("APT") to independently analyze Dollar General's store growth potential. APT then produced a lengthy report that verified the Integras study and Perdue's representations about Dollar General's prospects. SAF ¶224-226.

Just as the April 2007 slide shown to potential investors refers to the "Current Economic Model" and "Sensitivity on Improved Margins," the APT report reaches the same conclusions with regard to a "base case" and "upside case," respectively. SAF ¶226-228. In its "Base Case," APT concludes that approximately 7,000 new stores can be built with an IRR of 20%, and in its "Upside Case," APT concludes that approximately 11,000 new stores can be built with an IRR of 20%. *Id.* KKR's Calbert testified that the "base case" in the APT report rested on continuing the Company's operations in accordance with pre-transaction performance while the "upside case" assumed improvements at KKR's efforts:

Q: The base – the base case is there's no margin improvement?

---

[16] At the time of the KKR acquisition, Dollar General had approximately 8,260 stores. SAF ¶2. As Perdue's disclosure to Calbert and Agrawal reveals, management believed the "saturation point," based on the Company's existing strategic plan, was somewhere in excess of 15,000 to 18,000 stores nationwide. In other words, while Perdue was shopping the Company to KKR, senior management believed that Dollar General, under its existing plans, could open at least another 7,000 stores before hitting the saturation point. As noted above, the Company had commissioned a study from a consulting firm, Integras, in 2003, just after Perdue's arrival at Dollar General. The Integras study concluded that there were "10,125 [new store] opportunities" for Dollar General. SAF ¶217 At the time the study was prepared, Dollar General had 6,103 existing stores. (SAF ¶218), meaning Integras was projecting that Dollar General's could profitably open a total of approximately 16,000 stores, comporting closely with the information provided by Perdue to Calbert and Agrawal in February 2007, that Dollar General had a total store opportunity of 15,000 – 20,000 stores SAF ¶222

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A: That is correct.

Q: The upside case is KKR comes in and, with new management, you're able to improve the margins at Dollar General?

A: I mean, I don't know if they made any assumption about management, but the case is 200 basis points improved margin, what would the numbers tell us.

SAF ¶228.

KKR's belief in this store growth plan was one of its key reasons for acquiring Dollar General. Indeed, just as management knew that the prospect of strong store growth was both realistic and attainable, KKR internally justified its pursuit of Dollar General on the prospect of doubling the Company's store count. In a March 5, 2007 memo prepared to obtain the approval of the KKR Investment Committee in support of the acquisition, Calbert justified the proposed purchase at $22 - ***or even $23*** - per share by stating: "***Potential to up to double the company's number of stores (from 8,300 today) while maintaining 20% [internal rates of return].***" SAF ¶229.

Further supporting the importance of the plan, KKR and Dollar General senior management prepared a script that Beré, Perdue, and CFO Tehle were to use during "road shows" to investors in the deal and ratings agencies. A key piece of the script was an explanation of the actual feasibility of Dollar General's growth numbers. SAF ¶232. The script included the following Q & A:

How could you possibly put up another 7,000 stores, mostly in existing markets – aren't you at saturation?

a. No – remember our stores typically draw customers from only a 5-mile radius, so lots of room for more stores even without existing footprint

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b. We believe our stores need to draw from a population based of only ~5,000 people in order to be profitable

c. We/KKR did a detailed study of demographics around our existing store locations, and identified 7,000 of 200,000 districts in the U.S. as being well-suited for our stores, 60% of which are in our core markets

SAF ¶232

Dollar General senior management and KKR continued to present this store growth plan to different interested constituencies. In May 2007, the same slide that had been used in the April presentation to investors was used in presentations to Moody's credit rating agency (SAF ¶237), and to Standard & Poor's. SAF ¶238. In June 2007, the slide was again used in a presentation to KKR's prospective lenders. SAF ¶239.

This information was also used to convince lower-level managers to co-invest with senior management and KKR in the going private transaction. SAF ¶240. In a "strictly confidential" presentation to management, held after the Proxy was issued but before shareholders were required to vote on the merger, invitees were told – in direct contrast to what shareholders were simultaneously being told - that Dollar General presented a unique chance to capitalize on the massive growth Dollar General had in its future. According to the presentation, Dollar General represented a:

> **Substantial growth opportunity, particularly in current markets**
> – Our analysts suggest the potential for 7,000-11,000 new stores depending on financial performance
> – A large portion of these sites would be in DG's current markets

Id. (emphasis in original). As discussed in Section II.D below, many members of management seized on this opportunity to invest their own funds in the KKR-owned Dollar General.

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Even the lending arm of Lehman was informed by management, sometime prior to February 5, 2007, that the Company had the potential to grow to 20,000 stores. SAF ¶241 Based on this information, in addition to financial projections provided by management showing growth well into 2016, Lehman eagerly agreed to provide debt financing for the transaction. SAF ¶241. The evidence shows that Lehman had this information as early as December 2006. *Id.* Notably, while the store growth information was important to Lehman in providing debt financing to the deal, none of the bankers who were presenting to the Board actually provided this information to the Outside Directors.

In sum, Dollar General's store growth plan was a prominent aspect of every presentation to every constituency that had a post-merger interest in the Company – from the KKR investment committee, to potential equity investors in the deal, to management who would be co-investing with KKR, to lenders who were asked to finance the acquisition, to debt rating agencies. ***Long-term store growth was not, however, shared with the Board, the SPC, or Lazard.*** As Director Thornburgh testified in deposition:

> Q: Did the board have an analysis done of the total number of stores Dollar General could open nationwide?
>
> A: No.
>
> Q: Do you know if management had that analysis done?
>
> A: You mean what's the total – is the question from here to infinity how many stores could we open and have a saturation point?
>
> Q: Correct.
>
> A: I'm not aware of that.

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SAF ¶245.[17]

Beré, who made many of the presentations to potential investors and the ratings agencies, similarly acknowledged that the Board was never provided with the information regarding the number of stores possible at a 20% IRR rate. SAF ¶246. Board Member Barbara Knuckles agreed:

> Q: So as – as of the board meeting where you approved the merger, you have no idea whether or not there was potential store growth from 2011 forward; is that a fair statement?
>
> A: That's correct.
>
> Q: So you had no opinion whether that was possible or not?
>
> A: Correct.
>
> Q: And nobody at management ever told you whether it was possible or not?
>
> A: Not that I can recall.

SAF ¶252.[18]

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[17] The other outside directors have also admitted that they never saw the various materials showing Dollar General's tremendous growth prospects. *See* Johnston Aff. Ex. WW to the Affidavit of Douglas S. Johnston, Jr. in Support of Plaintiffs' Omnibus Memorandum in Opposition to the Motion for Judgment on the Pleadings, Responses of Bottorff, Bowles, Dickson, Gee, Knuckles, Purcell, Robbins, Thornburgh and Wilds to Plaintiffs' First Set of Requests for Admission. Of course, had the outside directors testified to the contrary, they would be conceding affirmative knowledge of growth that they did not disclose to shareholders, thus admitting that they did not act in good faith. *See, Section III.F, below, see also*, Tenn. Code Ann. §48-18-301(c), *City of Pontiac*, slip op. at 11; *Summers v. Cherokee Children & Family Servs.*, 112 S.W.3d 486, 529 (Tenn. Ct App 2002.

[18] Knuckles's testimony is also notable for its internal inconsistency during the short deposition. She initially testified the Board had no discussions with Lazard or Lehman regarding Dollar General's store growth opportunities or the value implications of those store growth opportunities. (SAF ¶247); that, in approving the merger, she did not consider Dollar General's potential store growth; (SAF ¶248); that she had no knowledge of how many stores Dollar General could build before approaching saturation, and that she never had a discussion with anyone regarding that issue (SAF ¶247) On questioning from defense counsel, after a break, she testified that store growth was discussed and considered by the Board at various times, including in connection with the merger. (SAF ¶250) On reexamination by Plaintiffs' counsel, she began to testify that she believed that Dollar General had the potential for profitable store growth after 2011; she finally testified, however, that she had "no idea whether or not there was potential store growth from 2011

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Contrary to being told about "significant growth opportunities," in November 2006, Lazard and Lehman made a presentation to the Board in which they stated that saturation could be an issue for Dollar General. SAF ¶256. At no time then or thereafter did Perdue, Beré or any other member of senior management or Lehman tell Lazard (or any Board member) of the known and expected store growth opportunity. SAF ¶247-252.

Indeed, Michael Wilkerson, the lead banker from Lazard, the firm that authored the fairness opinion upon which the Board's approval of the Merger was based, testified unambiguously that Lazard did not receive the store growth information shared with Lehman:

> Q: Were you aware in December of 2006 that there was an opportunity for profitable growth that included 10 percent annual store growth achievable in the foreseeable future?
>
> A. First of all, this isn't my statement.
>
> Q. I understand that.
>
> A. And I would not have expected this statement to be true based on what we knew and believed at that time.

SAF ¶258.

Wilkerson further testified that at no time did Company management relate to Lazard any information regarding the potential for 7,000 or more new Dollar General stores at an

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forward" and that she could not recall anybody at "management [telling] her that was possible or not SAF ¶252.

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IRR hurdle rate of 20% or higher. SAF ¶257.[19] Thus, Lazard could not have incorporated management's belief in future store growth into the fairness opinion.

3. There Are Material Factual Disputes Whether Shareholders Were Adequately Informed About The Company's Store Growth Plans

At the same time that they argue that Plaintiffs allegations of future store growth plans are a "fabrication," Defendants simultaneously argue that the market knew of the plan.[20]

The Proxy, as noted above, stated that Lazard had made the assumption that Dollar General would not have store growth after 2011, and that this assumption was deemed to be reasonable and confirmed by Dollar General's management. SAF ¶204-205 Nevertheless, Defendants argue that the store growth plans (that were not disclosed to the Board and were not shared with Lazard in connection with its valuation analysis) were so prevalent and publicly-available that the misrepresentation in the Proxy is somehow immaterial as a matter of law.

To start, Plaintiffs note that the one investor with the greatest incentive to scour the publicly-available information – KKR – found the public record regarding Dollar General's future growth prospects to be, at best, conflicting and insufficient to draw reliable conclusions. Calbert testified:

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[19] Wilkerson also testified that that had information come to Lazard's attention that called its conclusions into doubt prior to the shareholder vote, Lazard would have been required to assess appropriate action because its "obligations to the board and the company extended even beyond the point of this fairness opinion at least through the point where the merger proxy went out and shareholder vote had been placed...." SAF ¶259.

[20] While Defendants now argue that the market "knew" of the store growth plans, they failed to ask either of their experts to opine that the market was efficient.

In fact, one of Defendants' experts, Paul Gompers, has regularly opined that large corporations whose stock traded on either the NYSE (like Dollar General's did before the deal) or the NASDAQ nevertheless were not efficient for judicial purposes. SAF ¶262

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> ***So, you know, part of our assessment of any retail buyout is what's the saturation point. And there – there were a lot of analyst reports on this particular company that they had reached – with 8300 stores, they had reached saturation.***
>
> So.... we asked the question, "Is this format saturated?"
>
> So they ran some analytics to say, you know, if you're successful in growing the margin of this business, the four-wall EBITDA margin – so, you know, we think of – of profitability at the store level, and then you have corporate costs and then you have corporate profitability. So just the four-wall EBITDA level.
>
> If, instead of margins coming down as they had been, if you can increase margins by 200 basis points and you'll accept a 20 percent internal rate of return, you can – we think you can build "X" number of stores throughout the country. And I forgot what the number is, but this indicates that we could double the base, store base.

SAF ¶223.

In addition, as noted above, one of the key questions from the other sophisticated investors that KKR and management solicited when management went on the "roadshow" was: "How could you possibly put up another 7,000 stores, mostly in existing markets – aren't you at saturation?" SAF ¶232

Defendants' theory about pre-Proxy statement disclosures suffers from two fatal, factual flaws. First, general discussions of saturation points – a core metric by which retail companies are valued and a subject on which any analyst could offer speculation –is not the same as the Company-specific future store growth analysis and plan with specific IRR hurdle rates, discussed by Defendants Perdue and Beré. Second, the majority of analysts that covered Dollar General expressed the opposite concern that Dollar General was, in fact, at or approaching saturation levels. These analysts, for example, noted:

- ***"We are bearish on the dollar store industry because of saturation."*** SAF ¶254

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- The dollar store market "***was much more saturated than the operators believed***" and that "Dollar General was unwise to charge ahead with its plan to open 800 stores in a year." SAF ¶254
- "[N]egative fundamental environment within the Discount Store sector including ***market saturation in many regions***," SAF ¶254
- "[O]ur preference would be for [Dollar General] to slow [square] footage [growth]," SAF ¶254
- "We believe there are ***increasing indications that the company could pare back its pace of square-footage growth beyond 2006***" and "***While management maintained its 2006 plan for 800 new core Dollar General stores, we continue to believe that this goal may be too optimistic***, particularly given the considerably slower pace of openings year-to-date." SAF ¶254
- "Market Saturation. ***Many markets across the U.S., especially in the Sun Belt states, are saturated*** with different retail options, increasing the level of competition for dollar store operators." SAF ¶254

Further, David Perdue himself raised the specter of saturation concerns on the November 29, 2006 analyst conference call, when he said that "most people have been worried about saturation" and indicated that the plan to close stores was linked to those very concerns. SAF ¶261.

Against this contradictory information, the Proxy affirmatively represented that there would be no growth after 2011 and omitted any reference to the detailed long-term store growth analysis that Perdue, Beré and KKR were touting privately to potential investors in and supporters of the soon-to-be private company. Moreover, the Proxy, which was the most recent, definitive and well-informed statement on the Company's future prospects – would certainly be deemed credible to shareholders in evaluating whether to approve the going-private transaction.

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D. Senior Management's Strong Personal Financial Incentive to Support KKR At the Expense of Dollar General's Public Shareholders

From the day David Perdue first approached KKR, senior management was motivated to favor a deal with KKR at a price below the best price for public shareholders. From the start, KKR intended to provide management with a valuable equity stake in Dollar General if the merger went forward – something that is typical when KKR takes a company private. SAF ¶¶150, 157. Defendants' expert, Harvard Business School Professor Paul Gompers, testified that it is typical for private equity firms to offer to company management equity (including options) in the newly-private company on favorable terms – so called "sweet equity" in the words of a leading treatise relied upon by Professor Gompers.[21] Similarly, executive recruiter John Wood of Spencer Stuart testified that going private transactions typically offer management the opportunity for significant personal financial gain. SAF ¶150.

Dollar General's senior management team was well aware of the opportunities, as one of their own, Defendant Beré, had become rich via a prior private equity takeover. Before joining Dollar General, Beré had been a senior executive with Quaker Oats. SAF ¶153 In 1998, Quaker Oats sold its private label pancake business to a private equity firm and Beré became President and CEO of the newly private entity called Bakery Chef. SAF ¶154. Beré invested approximately $500,000 in the Bakery Chef deal and received additional equity for

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[21] According to Gompers, the equity is offered on attractive terms because, among other reasons, management may not have the personal financial resources to independently invest in the deal. SAF ¶152.

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working as CEO. SAF ¶155 After five years as a private company, Bakery Chef was sold, with Beré receiving approximately $13 million for his equity stake. SAF ¶156

KKR set forth its intentions with respect to management equity in a post-acquisition Dollar General in the offer letter KKR sent to the Board on March 8, 2006, in which KKR proposed to purchase the Company. The letter stated, in relevant part:

> We have spent a significant amount of time with the Company's senior management team and have been impressed by their knowledge and enthusiasm for the business. We would be excited to work with management and will provide them the opportunity to participate in the upside of the Company. ***As is typical in our investments, we would provide management the opportunity to invest alongside us in the transaction as part of an overall stock and option equity incentive plan.*** We believe that this will provide management with an exciting opportunity to further participate in the growth of the Company. We would be happy to discuss the specifics of our proposed arrangements with management at the appropriate time.

SAF ¶157

This paragraph, otherwise irrelevant in an offer to the Dollar General Board to acquire the Company, was included in KKR's offer letter in order to make clear to management (including Board members Perdue[22] and Beré), that they would have the opportunity to obtain personal wealth through participation in the deal if the offer was accepted. In fact, shortly after the Board accepted KKR's offer, KKR began discussing and negotiating with senior management and their attorneys, the specifics of the plan under which management would participate in the post-acquisition equity of the Company. SAF ¶158

The KKR deal offered Beré the rare opportunity for a lucrative repeat while giving other members of management their own opportunity to strike it rich. Even prior to the

[22] Perdue, as discussed above, remained confident that he would continue as CEO in the private Dollar General SAF ¶141,142.

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shareholder vote, a management equity plan was in place. SAF ¶158 Pursuant to that plan, Beré could, and would, invest approximately $2.25 million in the newly private Dollar General, consisting of personal funds of approximately $600,000 to $700,000, and a rollover of existing shares. SAF ¶160. Beré expects, if Dollar General simply meets its business plan, to turn his $2.25 million investment into $26 million over a five-year period (SAF ¶160) – an ***annual*** rate of return in excess of 60%. Other members of Dollar General's senior management are projected to earn similar returns. SAF ¶161.

KKR's offer of this lucrative post-acquisition equity placed senior management's interests, including Perdue's and Beré's, in direct conflict with the interests of the Company's public shareholders, who were being cashed out with no opportunity to participate in the private company. This is more than a theoretical conflict. The way KKR and management structured the deal, ***the lower the price paid by KKR to the public, the more money senior management stood to make personally***. SAF ¶162.

Plaintiffs' executive compensation expert, Brian Foley, has calculated the expected returns to senior management at different potential deal prices. SAF¶¶ 163-65. Beré's investment provides an example. Foley's calculations, unimpeached by Defendants at his deposition, show that if KKR had paid an additional dollar to the Company's public shareholders then, (depending on exactly how the $1 extra was funded) Beré would be projected to make $1.45 million less on his investment at the end of five years, while he would have received only an additional $215,000 from the sale of his pre-deal shares. SAF ¶163. At a $23 per share price, the financial impact on the other five senior offices would be similar: The $1 increase would result in approximately $2.59 million reduction in the

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projected collective value of their private Dollar General shares investments, versus a $1.25 million increase in value in their prior public Dollar General holdings. SAF ¶164. Thus, rather than being motivated to maximize shareholder value, Perdue and Beré were strongly incentivized to keep the merger price down.

The lucrative co-investment plan which was being discussed and negotiated with management and their attorneys in April and May 2007, was not properly disclosed in the Proxy, which was filed on May 21, 2007 and voted on in June 2007. Rather, the Proxy stated:

> As of the date of this proxy statement, ***none of our executive officers has entered into any agreement, arrangement or understanding with KKR***, Parent or Merger Sub or any of their respective affiliates ***regarding employment with, or the right to purchase or participate in the equity of, the surviving corporation***. However, prior to the closing, some or all of our executive officers may discuss or enter into such arrangements and /or amendments to their existing agreements.

SAF ¶165

While it may be true that no written agreements had been signed at the time the Proxy was filed, it was surely misleading to state that none of the executive officers had ***an understanding with KKR*** regarding equity participation. It was quite clear by May 21, 2007 (indeed, long before that), that Beré and other members of senior management were going to participate in the equity of the new Dollar General in a way that projected to afford them great personal wealth.

E. The Sales Process Was Artificially Limited and Biased Towards KKR

Defendants argue the sales process conducted by the SPC and the Board was "exemplary." (Defs' Mem at 26-33). In so arguing, Defendants ignore (or must dispute),

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material pieces of contradictory evidence. The facts are that ***no effort*** was ever made by the Board or the SPC to open the sales process up to any strategic buyers, to solicit potentially interested financial acquirers (except for Bain), or let it be known that Dollar General was potentially for sale. Rather, the Board conducted a closed process that is akin to putting your house up for sale by showing it without public listing to two bidders, one of whom was favored, and claiming success when the favored bidder submitted the only bid.

Indeed, in electing to pursue a two-bidder process, the Board ignored Lazard's express warning that by limiting the bidding to two parties, the process could be compromised if one bidder dropped out. SAF ¶179. This, of course, is exactly what happened when Bain elected not to submit a bid.

Both Lehman and Lazard presented lengthy lists of potential strategic acquirers to the Board and to the SPC. SAF ¶185. It would have been a simple matter for Lazard to reach out to prospective strategic buyers, gauge their interest and increase the odds of a vigorous auction process. That is what investment bankers do, and Lazard was quite willing to do so here. SAF ¶186. As Plaintiffs' expert, Mr. Reilly, testified, considerations (including synergies) for strategic buyers are different than those for private equity buyers. SAF ¶188. However, Lazard stated that the Board instructed them not to reach out to potential strategic buyers. SAF ¶186.

Neither did the Board authorize a legitimate "search" for a financial buyer. Lehman presented the Board with a list of 20 potential financial buyers. SAF ¶185. Lazard presented the Board with a similar list of 15 potential financial buyers, divided into two tiers. However, other than Bain, ***none*** of the potential financial buyers identified by Lehman or

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Lazard were ever contacted. SAF ¶177. Once again, this was at the direction of the Board and the SPC. SAF ¶177 Interestingly, and in direct contradiction with Wilkerson's testimony, Director Richard Thornburgh testified that he believed that Lazard, acting as the Board's financial advisor, had contacted other potential buyers. SAF ¶187.

The invitation to Bain was late and compromised. By the time Bain was brought in as a potential bidder at the end of 2006, KKR already possessed a sizeable informational and strategic advantage as a result of Perdue's desires to complete a deal with KKR. SAF ¶187,181. Indeed, months before informing the market of the Company-wide strategic shift embodied in Project Alpha, Perdue had already informed KKR that the Company intended to embark on the strategic shift. SAF ¶90 In a candid email, Perdue even admitted that KKR "[knew] more about us and has an idea [of] what they would do" while Bain would struggle to catch up. SAF ¶181[23] Moreover, Bain already owned a chain of dollar stores, Dollarama, and there is serious question as to whether Bain would be interested in adding another dollar store to its portfolio. SAF ¶200.

Defendants argue that the involvement of Blackstone and TPG raised the number of "bidders" to four and that the decision of Blackstone and TPG not to submit a bid is probative on value. Defs' Mem at 12. This is of dispute on all accounts. Lazard never

[23] Further, Lazard was well-aware that Bain was far behind KKR in its preparation to bid, and Bain needed more time to conduct due diligence. SAF ¶195 Rather than delay the (apparently-arbitrary) deadline to bid to ensure that there would be at least two bidders, the Board maintained the existing bidding date, effectively tilting the field towards KKR for no obvious reason

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sought out Blackstone or TPG or any other private equity bidders.[24] Rather, at one point in the "process," Bain requested that they be allowed to team up with Blackstone, and KKR later did the same with TPG, thereby reducing the number of possible competitors that might be interested in Dollar General. SAF ¶183-84. Notably, in 2006, the Department of Justice launched a probe of the private equity firms with respect to possible collusion involved in teaming up on bids. SAF ¶189.

As to the "probative value" of Blackstone and TPG not submitting bids, Plaintiff's expert, Robert Reilly, has testified that there are any number of reasons, other than value, why private equity firms choose to bid or not on companies. As noted by Reilly, "the investment decisions of private equity firms are driven by buyer-specific investment considerations that are unrelated to the target company business enterprise value." SAF ¶201. Each private equity firm is driven by its own unique investment criteria. SAF ¶199,200. Other significant factors include the private equity firm's extant industry concentration – this is particularly relevant here, where Bain had recently taken over the dollar store chain Dollarama. SAF ¶198. Prior industry concentration helps determine the firm's chosen "investment value" for a potential takeover target. SAF ¶200. If a firm has concerns about over concentration in a particular sector, then their chosen investment value would be less than otherwise. SAF ¶200.

Compounding the extremely limited nature of the "sales" process, Dollar General entered into compensation arrangements with both Lazard and Lehman under which they

[24] Wilkerson testified that the only "contacts" Lazard had with Blackstone and TPG were in early January, and only in their capacity as potential "equity partners to the existing participants in the process." SAF ¶182

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were strongly incentivized to favor a sale of the Company as opposed to remaining private. Lazard's fee agreement provided for it to be only $1 million unless there was a deal, in which case it would be $5 million ***when*** it provided a fairness opinion in favor of a deal, and an additional $10 million upon closing of a transaction SAF ¶175: Similarly, Lehman was to be paid .45% of the transaction price if a deal was made, but only $150,000 if not. SAF ¶170. Under this deal, Lehman was eventually paid approximately $30 million. In addition, Lehman was provided the opportunity to participate in syndicating the debt (and earning fees for so doing), under terms where KKR agreed to provide Lehman with "no less than 1/3 [of the] economics across bank and bond." SAF ¶172. Notably, information about Lehman's fee arrangements, and the conflicts they presented, were not disclosed in the Proxy.

In sum, Defendants are left defending on summary judgment an extremely limited and closed sales process, biased from the start towards KKR by the desires and actions of Perdue.

While the Proxy discloses that KKR and one other private equity firm entered into due diligence, and that each of the firms brought in a potential partner (SAF ¶203), the Proxy entirely ***omits*** the critical information that no other private equity firms or financial buyers were invited to bid, and that no effort at all was made to contact potential strategic buyers. Nor does the Proxy disclose the enormous financial incentives in Lehman's fee agreement in favor of supporting a deal.

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F. Deal Protections in the Merger Agreement Further Tilted the Playing Field Toward KKR

The Board further ensured that KKR would be the winning bidder by entering into lock-up provisions in the merger agreement that made the emergence of any competing bids a practical impossibility:

First, notwithstanding that the Board contacted only two private equity firms to bid and never publicly announced interest in selling the Company, the Board agreed to a "no shop" provision in the merger agreement that explicitly forbade them from engaging with other potentially interested bidders, except under exceptional circumstances. Further, the Board promised the potential bidders ahead of time that it would not pursue other bidders after signing a merger agreement. SAF ¶193. The agreement to enter into such a clause further restrained what was already an extremely limited process. Indeed, the "no shop" clause ran directly counter to the expectation of the Company's own banker, Lehman, which had expected that because there was only a single bidder prior to the deal's announcement, any merger agreement would include a "go shop" clause affirmatively allowing the Board to seek out higher bids. SAF ¶191.

Second, the agreement severely limited the Board from even engaging with any potential bidders that emerged as a result of the announcement of the KKR Deal. Specifically, the Merger Agreement says that the Company will not "initiate, solicit, knowingly encourage (including by providing information) or knowingly facilitate any inquiries, proposals or offers" and will not engage in any negotiations concerning a possible competing bid, except in narrow circumstances. SAF ¶267.

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Finally, if the Board attempted to obtain a higher price for the shareholders or simply withdraw its recommendation to shareholders to approve the KKR Merger, the Company was subject to a $225 million termination fee that would have to be paid before any new bidder could offer greater consideration to shareholders. Again, while termination fees are not *per se* illegal, the circumstances must be considered. At the time of the Merger Agreement, KKR had only $90 million in cash on its balance sheet (SAF ¶270); and the deal had been entered into without any prior announcement that the company was for sale, without any attempt to contact strategic bidders, and with only the most limited competition by two potential buyers.

* * *

In sum, as a result of Perdue's and Beré's misconduct and the failure of the Outside Directors to rectify those wrongs and protect Dollar General's former public shareholders, KKR now owns Dollar General and has appropriated for itself the benefits of growing that asset into the future.[25] Plaintiffs seek an opportunity to prove at trial that former shareholders should receive additional compensation for the value that was taken from them.

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[25] The record also shows that KKR's acquisition of Dollar General has been a tremendously successful move for the fund and its investors. Dollar General has historically performed exceptionally well in economic downturns and is doing so today. In 2008, Dollar General exceeded even the most optimistic (and undisclosed) of management's pre-closing expectations. SAF¶¶271-73. As Dollar General's current CEO stated on September 3, 2008, the Company is "benefitting" from "current economic conditions." SAF ¶¶271-73. The Company's same store sales were up over 10% from the prior year, while its operating profit (as measured by adjusted EBITDA) increased by more than 55% from the prior year. *Id.*

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III. ARGUMENT

A. Standards on a Motion for Summary Judgment

Rule 56.04 of the Tennessee Rules of Civil Procedure provides that summary judgment is appropriate only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Tenn. R. Civ. P. 56.04. Summary judgment is appropriate only in cases which can "be resolved on legal issues alone." *Byrd v. Hall*, 847 S.W.2d 208, 210 (Tenn. 1993). "[T]he procedure is clearly not designed to serve as a substitute for the trial of genuine and material factual matters." *Id.*

The moving party carries the burden of persuading the Court that no genuine issue of material fact exists and that it is entitled to judgment as a matter of law. *Id.* at 211. If the moving party has made a prima facie showing that there are no genuine issues of material fact, then the non-moving party must demonstrate, by affidavits or discovery materials, that there is a dispute as to genuine, material facts that warrants trial. *Id.* "[T]he trial court must take the strongest legitimate view of the evidence in favor of the nonmoving party, allow all reasonable inferences in favor of that party, and discard all countervailing evidence." *Id.* at 210-11. Summary judgment is appropriate only when, "after being given a reasonable opportunity to substantiate its claims, the nonmoving party is unable to establish any essential element of its case on which it will have the burden of proof at trial." *Id.* at 213. As shown below, there are numerous genuine issues of material fact that preclude summary judgment in this case.

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B. Plaintiffs' Fiduciary Duty Claims Are Fact-Intensive and Ill-Suited for Summary Adjudication

Dollar General was incorporated under the laws of the State of Tennessee. The Individual Defendants, as directors and officers of Dollar General, owed fiduciary duties to Plaintiffs and the Class that have been described as "the highest duty known to the law."[26] Tennessee's courts have explained:

> "In a broad sense the directors and officers of a corporation are its agents. While they may not be in the strict sense trustees, it is well established that they occupy a fiduciary, or more exactly a quasi-fiduciary, relation to the corporation and its stockholders. . . . ***They are required to act in the utmost good faith***, and in accepting the office they impliedly undertake to give to the enterprise the benefit of their care and best judgment and to exercise the powers conferred solely in the interest of the corporation or the stockholders as a body or corporate entity, and ***not for their own personal interest***. Clothed with the power of controlling the property and managing the affairs of the corporation, without let or hindrance, as to third persons the directors and officers are its agents, but as to the corporation itself, equity holds them liable as trustees. Indeed, it is the view frequently and broadly taken that the officers and directors of a corporation are, at least in substance and in many respects, trustees for the corporation or its stockholders."

Hayes v. Schweickart's Upholstering Co.,, 402 S.W.2d 472, 463 (Tenn. Ct. App. 1965)(quoting 19 Am. Jur. 2d *Corporations* §1272, at 679). *Accord Heffernan v. Heffernan, Ballinger, Pounds, & Yarbrough, Inc* , C.A. No. 02A01-9504-CH-00080, 1996 Tenn. App. LEXIS 567, at *11-*12 (Tenn. Ct. App. Sept. 11, 1996) ("It is well established that officers and directors of a corporation owe a fiduciary duty to the corporation and its members or shareholders and, while occupying such a position of trust, must act in the utmost good faith. . . . '[They are] bound to the exercise of the ***utmost good faith, loyalty, and honesty*** . . . .'"); *May v. Nat'l Bank of Commerce*, 387 F. Supp. 2d 770, 779 (W.D. Tenn. 2004) ("Directors

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[26] *In re Estate of Tannenbaum*, 248 N.Y.S 2d 749, 756 (N.Y. App. Div. 2d Dep't 1964).

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and officers of a corporation are fiduciaries to the corporation and its shareholders. Specifically, a director or officer of the corporation ***must act in good faith and remain loyal*** to the corporation and its shareholders. Directors and officers 'are not permitted to deal with the corporation or its assets for their own private gain and cannot deal for themselves and for the corporation at one and the same time. . . .'").

As Tennessee's courts have held, "the duty of a fiduciary to act with undivided loyalty . . . is one of the manifestations of the general rule that demands of an officer or director the utmost good faith in his relation to the corporation which he represents." *Venture Express, Inc. v. Zilly*, 973 S.W.2d 602, 605 (Tenn. Ct. App. 1998); *see also Summers*, 112 S.W.3d at 503 n.20 ("[T]he general duty of loyalty is found in the requirement that directors act in good faith and in a manner they reasonably believe is in the best interest of the corporation.")

The fiduciary duties owed to shareholders by directors of Tennessee corporations have been codified in Tennessee's corporate statutes. Specifically, in 1986, Tennessee adopted the Model Business Corporation Act. *See Kradel v. Piper Indus., Inc.*, 60 S.W.3d 744, 749 (Tenn. 2001) ("the Tennessee Business Corporation Act . . . was patterned in large part after the Revised Model Business Corporation Act of 1984"). Tennessee's Business Corporations Act requires that "[a] director shall discharge all duties as a director, including duties as a member of a committee . . . [i]n good faith . . . [w]ith the care an ordinarily prudent person in a like position would exercise under similar circumstances[], and [i]n a

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manner the director reasonably believes to be in the best interests of the corporation." Tenn. Code Ann. §48-18-301(a).[27]

Where, as here, the plaintiff shareholders raise questions about loyalty and good faith, summary judgment is rarely appropriate. "The question of whether a director or officer has breached their duty of loyalty is one of fact and depends on all of the surrounding circumstances." *Hall v Tennessee Dressed Beef Co* , Appeal No. 01-A-01-9510-CH-00430, 1996 Tenn. App. LEXIS 384, at *18-19 (Tenn. Ct. App. June 28, 1996), *aff'd in pertinent part, Hall v. Tennessee Dressed Beef Co.*, 957 S.W.2d 536 (Tenn. 1997). Consequently, summary judgment is generally not appropriate in duty of loyalty or bad faith cases, as they inherently involve "question[s] of fact best left to the jury." *Hall*, 1996 Tenn. App. LEXIS 384, at *23; *Tennessee Farmers Mut. Fire Ins. Co. v. Thompson*, 12 Tenn. App. 591, 600 (Tenn. Ct. App. 1930) (whether a defendant acted in bad faith is a fact-based "question for the jury").[28] As Tennessee's courts long have held, "questions of materiality and good faith are ordinarily questions of fact, and therefore for the jury." *Hartford Life Ins. Co v Stallings*, 72 S.W. 960, 961-62 (Tenn. 1903). Accordingly, summary judgment can only be

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[27] Numerous other states have, like Tennessee, adopted the Model Act "Thirty states have adopted all or substantially all of the Model Act as their general corporation statute [while] [m]any other states have adopted selected provisions of the Model Act." ABA Model Bus. Corp. Act Ann., at ix (4th ed. 2008). Notably, Delaware, unlike Tennessee, is not a Model Code state. Nevertheless, Tennessee's courts look to Delaware law for guidance in certain situations where the laws do not conflict.

[28] *See also Wager v. Life Care Ctrs. of Am , Inc.*, No. E2006-01054-COA-R3-CV, 2007 Tenn. App. LEXIS 743, at *24 (Tenn. Ct. App Nov 30, 2007) ("'[t]he existence of bad faith is a question of fact'" which must be based upon the credibility of the witnesses) (quoting *Sun Splash Painting, Inc. v Homestead Vill., Inc.*, No. M2002-00853-COA-R3-CV, 2003 Tenn. App. LEXIS 723, at *2 (Tenn. Ct App. Oct. 15, 2003)); *Snodgrass v. Freemon*, No. M2002-01247-COA-R3-CV, 2003 Tenn. App LEXIS 531, at *9 (Tenn. Ct. App July 29, 2003) ("Whether [a] Defendant . . . is acting in bad faith is a question of fact."); *Hartford Life Ins. Co v. Stallings*, 72 S.W. 960, 961-62 (Tenn 1903) ("questions of materiality and good faith are ordinarily questions of fact, and therefore for the jury ").

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granted in a breach of fiduciary duty context when "'the uncontroverted facts and inferences to be drawn from [the facts] make it so clear that all reasonable persons must agree on the proper outcome.'" *Hall*, 1996 Tenn. App. LEXIS 384, at *23.

As shown below, Defendants have not demonstrated, and cannot demonstrate, as a matter of law, that they are entitled to summary judgment on Plaintiffs' claims. The facts and inferences uncovered by Plaintiffs establish that Defendants breached their fiduciary duties to Plaintiffs and Dollar General's other public shareholders, or, at a minimum, raise sufficient genuine issues of material fact to preclude summary judgment in Defendants' favor.

C. Genuine Issues of Material Fact Preclude Summary Judgment on the Issue of Whether Certain Directors Faced Conflicting Interests and Breached Their Duty of Loyalty

The evidence in this case raises genuine issues of material fact that preclude summary judgment as to whether Defendants Perdue and Beré succumbed to their self-interest and breached their duty of loyalty to the Company's public shareholders. The duty of loyalty requires directors and officers to:

> [A]ct[] at all times in the best interests of the corporation and its shareholders, whose interests must take precedence over any self-interest of the director, officer, or controlling shareholder that is not shared by the stockholders generally. The duty of loyalty to the corporation imposed on its officers and directors includes the duty to avoid conflicts of interest. The duty of loyalty also prohibits faithlessness and self-dealing.

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18B Am. Jur. 2d *Corporations* §1480 (2008).[29] A classic example of disloyalty is where a director or officer hopes to receive economic benefits from a transaction that are not shared by the company's public shareholders. *See, e.g., Holmes Fin. Assocs , Inc v. Jones*, 1991 Tenn. App. LEXIS 983, at *21-*22 (Tenn. Ct. App. Dec. 18, 1991) (conflict of interest transactions include those from which directors expect to receive a benefit, even where the transaction in question is not directly between the director and the corporation); *cf. City of Pontiac*, slip op. at 9 (holding no breach of duty of loyalty pled; "nowhere does the First Amended Complaint allege that Mr. Moore or Mr. Hyatt have [or expect to have] an ownership interest in the acquiring entity").[30]

As discussed in detail above at Section II.B, it was clear from the outset and, indeed remained true after Board approval of the takeover, that Perdue expected to be CEO of the

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[29] Tennessee's courts regularly look to American Jurisprudence for guidance on issues of corporate law. *See, e g , Hayes*, 402 S W.2d at 482.

[30] Delaware law is in agreement with Tennessee law on this point. *See, e.g., Wisconsin Inv. Bd. v. Peerless Sys Corp* , Civ. A. No. 17637, 2000 Del. Ch. LEXIS 170, at *56 (Del. Ch. Dec. 4, 2000) (denying summary judgment; "[D]irector action that is self-interested or for selfish reasons is a breach of the fiduciary duty of loyalty. When a director uses his office to promote, advance, or effectuate a transaction that is in the personal financial interest of the director, the director has the burden of establishing good faith as well as the "most scrupulous inherent fairness" of the transaction. When faced with this question of divided loyalties, the director has the burden of establishing the entire fairness of the transaction to survive careful judicial scrutiny."); *Krasner v. Moffett*, 826 A.2d 277, 283 n 19 (Del. 2003) (reversing dismissal of complaint; plaintiff adequately alleged loyalty claims where director "expected to benefit from increased consulting fees provided to the Services Company as a result of the MEC merger"); *Rothenberg v. Santa Fe Pac Corp* , Civ. A. No. 11749, 1992 Del. Ch. LEXIS 106, at *18-*19 (Del. Ch. May 18, 1992) (allegations that directors anticipated receiving subsequent benefits sufficient to state claim for breach of duty of loyalty); *In re Marriott Hotel Props. II Ltd P'ship Unitholders Litig.*, Consolidated Civ. A. No. 14961, 2000 Del. Ch. LEXIS 17, at *44 (Del. Ch Jan. 24, 2000) (denying defendants' motions to dismiss and for summary judgment on breach of duty of loyalty claim where expectation of post-transaction benefits provided motive to act against shareholder interests).

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private company, [31] and was motivated by the prospect of personal financial gain. Beré was similarly aware of the home run potential provided by a KKR acquisition, having personally made $13 million from a prior private equity takeover. It is further clear that KKR intended to provide management with an equity stake in Dollar General if the merger went forward – something that is typical when KKR takes a company private. SAF ¶157 This intention was memorialized in the offer letter KKR provided to the Board. Indeed, soon after the Board approved the merger, Beré and senior management negotiated a rich co-investment deal under which Beré, for one, was projected to earn $26 million on a $2.2 million investment over five years if Dollar General met plan. Other senior members of management expected similar returns. (Ex. LL, DG_168029-06). For example, David Tehle, the Company's CFO, projected to turn an $800,000 initial investment into over $12 million. *Id.*

This equity participation, and the powerful financial incentives attendant to it, placed management's interests (including those of Perdue and Beré) squarely opposite those of the Company's public shareholders. The courts have recognized that management participating in a buyout of their company are "heavily burdened with a conflict of interest." *Glidden Co. v Jandernoa*, 173 F.R.D. 459, 477 (W.D. Mich. 1997). "Management's personal motivation as a potential buyer is to pay as little as possible. Management's duty as a fiduciary is to obtain the highest available value for the stockholders." *Id.*

Indeed, simple math demonstrates, and Plaintiffs' expert has testified, that this conflict motivated management to push for a ***lower*** per share purchase price so that their

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[31] Perdue's admission that he "hoped" he would remain as CEO with the private company is alone sufficient to demonstrate his interest in the transaction and at a minimum, raises genuine issues of material fact sufficient to defeat summary judgment. *See, e.g., Holmes 1991 Tenn App* LEXIS 983, at *21-*22

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post-merger returns could be maximized. As discussed in Section II.D above, Beré could earn $5 million *less* on his equity in the private company if KKR had paid $23 rather than $22. And if KKR had paid $24 per share, Beré's take would be as much as $6.4 million *less* than at $22 per share. The next five most senior executives would have seen similar diminished returns if KKR had paid a higher price for Dollar General. Thus, senior management stood to miss out on ***millions*** of dollars of profits if KKR paid only a dollar or two more for Dollar General. Rather than being aligned with shareholders and motivated to maximize shareholder value – as their fiduciary duties required – Perdue, Beré, and senior management, were strongly incentivized to keep the merger price down.

Thus, Defendants' arguments that these Company insiders were aligned with public shareholders by virtue of their own stock ownership cannot withstand scrutiny. *See* Def. Mem. at 21.

D. Genuine Issues of Material Fact Preclude Summary Judgment on the Issue of Whether Perdue, Beré, and Senior Management Concealed Material Facts From the Outside Directors, Lazard, and Dollar General's Public Shareholders

1. The Presence of Independent (But Uninformed) Directors Does Not Immunize Breaches of Fiduciary Duty

Defendants cannot credibly contest the conflicts of interest of Perdue and Beré in their Motion. Indeed, even their corporate governance expert, Professor Coffee, criticizes the conduct of Perdue in connection with the merger and offers no opinion regarding whether the inside directors – Perdue and Beré – breached their fiduciary duties to Dollar General's shareholders. SAF¶263; Johnston Ex. 33; Johnston Ex. 57.

Instead, Defendants argue that Plaintiffs cannot state a claim because, even if these two directors were conflicted, they comprised only two of the eleven Dollar General Board

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members and the other nine members cured the conflict pursuant to Tenn. Code Ann. §48-18-302(a). *See* Def. Mem. at 21 n.4.[32] However, as discussed below, §48-18-302(a) does not protect Defendants because (a) the statute plainly requires that all material facts regarding the transaction be disclosed to the non-conflicted Board members (and/or to the Company's public shareholders) for its curative effects to take place and (b) even if the transaction were ratified pursuant to Tenn. Code Ann. §48-18-302(a), under Tennessee law that would only foreclose Plaintiffs' ability to void the merger; it would not cut off Plaintiffs' breach of fiduciary duty claims. *See McRedmond v. Estate of Marianelli*, 46 S.W.3d 730, 741 (Tenn. Ct. App. 2000) ("the purpose of [a ratification statute] is to create a framework within which corporations can enter into binding agreements, even where conflicts of interest arise from such agreements, ***not to shield corporate directors from liability for breaches of their fiduciary duties***.").

Specifically, Tennessee's corporate statute defines a conflict-of-interest transactions as one "in which a director or officer of the corporation has a direct or indirect interest." Tenn. Code Ann. §48-18-302(a).[33] The statute further provides that:

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[32] Defendants cite several Delaware cases for the proposition that the business judgment rule applies unless a majority of the Board is interested in the transaction. *See* Def. Mem. at 20-22. For the reasons discussed below, those cases do not apply here; unlike the present case, the opinions cited by Defendants for the "majority interested" proposition did not involve allegations of material information being concealed from outside Board members by interested insiders Furthermore, under Tennessee law, there is no requirement that a majority of the Board be interested in the transaction, or lack independence, for a breach of fiduciary duty claim to lie. Thus, Defendants' authorities are inapposite.

[33] Tennessee's courts have clarified that conflict of interest transactions include those from which directors hope to receive a benefit, even where the transaction in question is not directly between the director and the corporation. *See, e.g.*, *Holmes*, 1991 Tenn. App. LEXIS 983, at *21-*22

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> A conflict of interest transaction is ***not voidable*** by the corporation solely because of the director's or officer's interest in the transaction if any one (1) of the following is true:
>
> (1) The material facts of the transaction and the director's or officer's interest were disclosed or known to the board of directors or a committee of the board of directors and the board of directors or committee authorized, approved, or ratified the transaction;
>
> (2) The material facts of the transaction and director's or officer's interest were disclosed or known to the shareholders entitled to vote and they authorized, approved, or ratified the transaction; or
>
> (3) The transaction was fair to the corporation.

Tenn. Code Ann. §48-18-302(a). Absent full disclosure of the material facts, an unfair transaction is voidable by the company's public shareholders (*i.e.*, it can be rescinded or damages can be awarded where rescission is impracticable, *see, e.g.*, *Summers*, 112 S.W.3d at 528-29).

Similarly, Delaware law is clear that when wrongdoing by officers or directors are approved in good faith by a majority of other directors, but those directors have not been fully informed of all material information relating to the approved conduct, the business judgment rule does not insulate the challenged conduct from judicial scrutiny. As the Delaware Chancery Court, stated after trial, in a case in which a CEO breached his duties but claimed protection from judicial challenge because the deal was approved by a majority of independent directors:

> Even where it initially applies, the business judgment rule is rebutted if there is evidence of disloyalty, including . . . "***fraud upon the corporation or the board***. . . ." Naturally, the Court's "reluctance to assess the merits of a business decision ends in the face of illicit manipulation of a board's deliberative processes by self-interested corporate fiduciaries."

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Bomarko, Inc. v. Int'l Telecharge, Inc, 794 A.2d 1161, 1178 (Del. Ch. 1999), *aff'd*, 766 A.2d 437 (Del. 2000). As the Delaware Supreme Court held in *Mills*, 559 A.2d 1261:

> [W]hen corporate directors rely in good faith upon opinions or reports of officers and other experts "selected with reasonable care," they necessarily do so on the presumption that the information provided is both accurate and complete. Normally, decisions of a board based upon such data will not be disturbed when made in the proper exercise of business judgment. However, ***when a board is deceived by those who will gain from such misconduct, the protections girding the decision itself vanish. Decisions made on such a basis are voidable at the behest of innocent parties to whom a fiduciary duty was owed and breached***, and whose interests were thereby materially and adversely affected. This rule is based on the unyielding principle that corporate fiduciaries shall abjure every temptation for personal profit at the expense of those they serve.

Id at 1283-84.[34]

This same principle is embodied in Tennessee's corporate statutes, which remove protection from officers and directors who conceal material information regarding conflict-of-interest transactions from otherwise independent Board members and/or the company's shareholders. *See* Tenn. Code Ann. §48-18-302(a).

2. Perdue and Beré Concealed Information from the Board, Lazard and Shareholders

The record shows serious breaches of duty by Perdue, which remained hidden to the other Directors until their depositions in this case. In sum, as detailed in Section II.B above, Perdue expected to be CEO of the private company, and in the course of pursuing that goal, he breached his fiduciary duty by repeatedly passing confidential Board information to KKR, by taking steps to "gag" Lehman Brothers from contacting other potential bidders and by

[34] 8 Del C. §141(e), cited by the *Mills* court, is similar to Tenn. Code Ann. §48-18-301(b), and provides that a director is normally entitled to rely on information and reports from company insiders and outside experts

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withholding material information regarding store growth plans from the Board (as discussed below).[35] The evidence is further that Calbert and KKR knowingly encouraged and participated in Perdue's conduct.

The record also shows that Perdue, Beré and other members of Dollar General's senior management concealed the Company's long-term store growth strategies from the Board, Lazard and shareholders. This information was hidden due to self-interest. As noted above, management, including Perdue and Beré, wanted Board and shareholder approval of the merger at the lowest possible price. *See Glidden*, 173 F.R.D. at 477 ("'Management's personal motivation as a potential buyer is to pay as little as possible.'"). As the Delaware Supreme Court held in *Mills*, a case in which management favored KKR because (like here) KKR was going to provide management with an ownership interest in the company post-merger:

> Evans and Reilly [Mills' CEO and COO], as participants in the leveraged buyout, had significant self-interest in ensuring the success of a KKR bid. Given this finding, Evans' and Reilly's deliberate concealment of material information from the Macmillan board must necessarily have been motivated by an interest adverse to Macmillan's shareholders.

559 A.2d at 1279.

During the period in which the Board was evaluating the merger, management's belief in the Company's growth prospects was withheld from the Board, the SPC and Lazard. As discussed above (Section II.C.2):

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[35] In fact, Defendants' expert Coffee made it clear that "talking about views of individual directors to outsiders who is going to be in arms-length negotiations with you is undesirable, ill advised." SAF ¶137. As Defendant Director Richard Thornburgh testified at deposition, the evidence is that Perdue was looking to: "line his pockets with money as opposed to maybe doing the right thing for the company." SAF ¶135.

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- Thornburg, a member of the SPC, testified the Board did no analysis of the number of stores Dollar General could open, and he was "not aware" if management had such an analysis prepared.
- Beré acknowledged that the Board was never presented with the information regarding the number of stores that could be opened at a 20% IRR.
- Board member Knuckles agreed that she had "no idea whether or not there was potential store growth from 2011 forward," and that in approving the merger, she did not consider Dollar General's future store growth.
- When Lehman and Lazard began meeting with the Board in November 2006, Lehman and Lazard expressed the opposite concern – that Dollar General was nearing market saturation. Knuckles testified that she did not recall anyone on the Board (which included Perdue and Beré) expressing disagreement with Lehman and Lazard regarding Dollar General nearing market saturation. Knuckles Tr. at 18.
- Lazard's Michael Wilkerson, testified that Lazard did not believe there was an "opportunity for profitable growth that included 10 percent annual store growth…" for the foreseeable future, and that at no time did Company management relate to Lazard any information regarding the potential for 7,000 or more new Dollar General stores at an IRR hurdle rate of 20% or higher.

Thereafter, subsequent to the Board's approval of the merger, but before shareholders voted on it, Perdue and Beré, along with other members of senior management, made presentations throughout April, May and June 2007 touting the company's plan for store growth to prospective equity investors, ratings agencies, potential lenders, and lower-level management who were being offered an equity stake in the post-merger Company. At the same time, the Proxy reviewed and approved by management was issued to shareholders (on May 21, 2007). The Proxy, however, highlighted Lazard's management-endorsed projection that there would be "no new store growth after 2011." See Section II.C.2[36]

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[36] Defendants also assert that "[n]othing in the Proxy Statement suggests that management reviewed or offered any opinion with respect to Lazard's post-2011 assumptions underlying its terminal value analysis."

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When the issue of growth was directly raised by Plaintiffs at the preliminary injunction hearing, Defendant's opposed Plaintiffs' motion, stating that "[t]here is no evidence of a plan by Dollar General (or KKR for that matter) to open up 7103-10,903 additional Dollar General stores." Importantly, management continued to sit silently, letting shareholders cast their votes in June 2007 based on Proxy materials were contradicted by the simultaneous presentations they were making to equity investors, ratings agencies, lenders and lower-level management.[37]

The failure to apprise the Outside Directors of this information bars the application of the business judgment rule to protect the wrongdoing of Beré and Perdue.[38] The decision in *In re Emerging Communications, Inc Shareholders Litigation, Consolidated Civ. A* No. 16415, 2004 Del. Ch. LEXIS 70 (Del. Ch. May 3, 2004) is particularly instructive here. In

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Again, untrue. Perdue and Bere telling the opposite story to numerous constituencies. And Perdue and Bere, as Board members, reviewed and authorized the misleading proxy materials containing the "no new stores after 2011" language to be sent to shareholders. Knuckles at 15-16.

[37] Notably, even though at the time of the preliminary injunction hearing, Plaintiffs had only a general idea of the depth of Defendants' non-disclosures because key evidence – including critical emails and the Company's own store growth analyses – had not yet been produced, management had knowledge of and access to the store growth data.

[38] The duty of disclosure is an outgrowth of the duty of loyalty. *See City of Pontiac*, slip op. at 11 ("Encompassed within the duty of loyalty is the duty of disclosure A board of directors has a fiduciary duty to disclose fully and fairly all material facts within its control that would have a significant effect upon a shareholder vote."). *City of Pontiac* is an unpublished trial court opinion. Because trial court opinions are not reported, "such opinions are not generally considered authority." *State v. Franklin*, 919 S.W.2d 362, 366 (Tenn. Crim. App 1995). As the court held in *State v Frazier*, No. 03C01-9904-CC-00146, 1999 Tenn Crim App LEXIS 1144 (Tenn Crim. App. Nov. 18, 1999), with regard to a Tennessee trial court order, "the impact of this decision is of no legal consequence as the circuit court's opinion merely constitutes persuasive authority and is not binding, under the theory of *stare decisis*, upon other judicial circuits" *Id* at *7. Nevertheless, although it is unpublished and involved inapposite facts, *City of Pontiac* is instructive on certain general points of Tennessee law (Thomas Nelson was a Tennessee corporation). The other unpublished trial court opinion Defendants cite in their brief – *Indiana State Dist. Council of Laborers and HOD Carriers Pension Fund v. Brukhardt*, No. 05-1302-II, slip op. (Tenn. Ch. Aug. 27, 2007) – by Chancellor McCoy – involved a Delaware corporation and purports to apply Delaware, not Tennessee, law. It also is factually inapposite Thus, it is of no value to the analysis of the present Motion

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that case, the court held that material information regarding the company's prospects had been withheld and thus the board was not properly informed:

> The Special Committee and a majority of ECM's minority shareholders voted to approve the merger, but their votes were not fully informed. A highly material fact was not disclosed either to the Special Committee or to the minority stockholders, namely, that the most recent projections – the June projections – had been provided to Prosser and his financial advisor (Prudential) and his lender (RTFC) but not to the Special Committee. Members of the Special Committee testified that they and Houlihan should have been provided with the June Projections. Moreover, the June Projections were not disclosed in the proxy statement, and the proxy disclosures relating to that issue falsely and misleadingly suggested that the shareholders were being provided with all of the projections to which Prosser and his advisers had been privy.

Id. at *112- 113. Here, the Company's store growth prospects were concealed, and the Proxy misleadingly stated that there were no such prospects after 2011.

The *Emerging Communications* court disregarded the efforts of otherwise-independent outside directors:

> There are several reasons why Mr. Goodwin's efforts as the Special Committee's chairman, and as its sole functioning member, were doomed to failure. . . . The first is that Prosser withheld the June projections, and knowledge of their existence, from the Committee and its advisors, Houlihan and Paul Hastings. As a consequence, ***Goodwin and Houlihan were deprived of information that was essential to an informed assessment of the fair value of ECM*** and of the gross inadequacy of merger price Prosser was offering.

Id. at *129. Similarly, here the conflicted insiders deprived outside directors, advisors and shareholders of key information.

3. The Concealed Information Was Material

The Proxy failed to disclose Dollar General's store growth prospects, which was a material fact. The Proxy also failed to disclose that Perdue had initiated contact with KKR in the spring of 2006, had private meetings with KKR without the Board's knowledge, and

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passed confidential information to KKR in support of KKR's attempts to take the Company private. And the Proxy failed to disclose that neither the Board, nor any of the advisors working on behalf of the Board or the Company, made any effort to contact potential strategic buyers for the Company and only the most minimal and belated efforts to expand the universe of potential private equity buyers beyond KKR. In 1976, the United States Supreme Court set forth the test under federal proxy laws for "materiality." The court held:

> An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote.... ***It does not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote.*** What the standard does contemplate is a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available.

TSC Indus. v Northway, 426 U.S. 438, 449 (1976) (hereinafter "*TSC*") (underlining emphasis in the original). Virtually all jurisdictions, including Tennessee and Delaware, follow *TSC* in determining the materiality of proxy disclosures under state law, including fiduciary duty law. *See* Dollar General Mem. at 12-13 (citing *TSC*); *City of Pontiac*, slip op. at 11; *Rosenblatt v. Getty Oil Co.*, 493 A.2d 929, 944 (Del. 1985).[39] *See also* 18A Am. Jur. 2d *Corporations* §938 (2008).

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[39] *See also Banton v. Hackney*, 557 So 2d 807, 817 (Ala. 1989) (following *TSC* and holding that "it is not necessary to prove that disclosure of the omitted facts would have caused a reasonable investor to ***change*** his decision") (emphasis in original), *State of New York v. McLeod*, 819 N.Y.S.2d 213 (N.Y. Sup. Ct. 2006) (same; materiality "'does not require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote'"); *Isroff v Westhall Co* , C.A. No. 15063, 1991 Ohio App. LEXIS 5856, at *5-*6 (Ohio Ct. App. Summit Cty. Nov. 27, 1991) (same); *accord Blackmon v. Nexity Fin Corp.*, 953 So 2d 1180, 1191-92 (Ala. 2006) (following *TSC*); *Meidinger v Komag, Inc* , 31 P.3d 77, 84 (Alaska 2001) (same); *Van Schaack Holdings, Ltd v Van Schaack*, 867 P.2d 892, 899 (Colo. 1994) (same),

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Courts considering the importance of growth prospects agree that post-merger growth is vital to determining fair value. As Chancellor Lyle stated in *City of Pontiac*, "[f]air price relates to the economic and financial considerations of the proposed merger, including all relevant factors such as assets, market value, earnings, ***future prospects***, and any other elements that affect the intrinsic or inherent value of a company's stock." *City of Pontiac*, slip op. at 3.

In *Delaware Open MRI Radiology Associates, P.A v. Kessler*, 898 A.2d 290 (Del. Ch. 2006), the court considered the issue of post-merger expansion of the business from two radiology centers to five. The court held:

> Delaware law is clear that "elements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered." Obviously, when a business has opened a couple of facilities and has plans to replicate those facilities as of the merger date, the value of its expansion plans must be considered in the determining fair value.

Id. at 314-15. The court concluded that the new stores were material to value, that the merger price was thus unfair, and it awarded damages to the plaintiffs. *Id.* at 291; *accord ONTI, Inc. v Integra Bank*, 751 A.2d 904, 911 (Del. Ch. 1999) (holding that future plans are properly considered in valuation analysis and observing, by way of analogy, that shareholders would be "entitled to a valuation that reflects the value of a company that owns

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Enservco, Inc v Indiana Sec Div, 623 N.E.2d 416, 423 (Ind. 1993) (same); *Marram v. Kobrick Offshore Fund, Ltd*, 809 N.E 2d 1017, 1029-30 (Mass. 2004) (same); *Qualcomm Inc v Am Wireless License Group, LLC*, 980 So.2d 261, 272 (Miss. 2007) (same), *Everts v Holtmann*, 667 P.2d 1028, 1032-33 (Or. Ct App. 1983) (same); *Anthony v Padmar, Inc*, 465 S.E.2d 745, 753 (S.C. Ct. App. 1995) (same), *overruled in part on other grounds by Olson v Faculty House of Carolina, Inc*, 580 S E 2d 440 (S C. 2003); *Bridwell v. Texas*, 804 S W 2d 900, 903-04 (Tex. Crim. App. 1991) (same); *Kin-Sing Au v. ADSI, Inc.*, 74 Va Cir 219, 223 (Va Cir Ct. 2007) (same), *Guarino v. Interactive Objects, Inc*, 86 P.3d 1175, 1185 (Wash. Ct. App. 2004) (same) A number of these jurisdictions, like Tennessee, have adopted all or part of the Model Act. *See supra* n.76

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a cornfield that can be developed into a major office center"). A similar issue was considered in *Isroff*, 1991 Ohio App. LEXIS 5856, (applying *TSC*). In that case, the trial court, applying Ohio's version of the Model Act, concluded that the possible addition of six stores presented a question of material fact for the jury in a shareholder suit. *Id.* at *6.

In analyzing whether knowledge of a business's true value is required for protection under a Model Act statute similar to Tenn. Code Ann. §48-18-302(a), the Northern District of Illinois held as follows:

> Fait next claims Ronsen did not approve the offering with knowledge of all material facts. Under the [Illinois Business Corporation Act], Ronsen was required to have knowledge not only of his fellow board members' interest in the offering, but also knowledge of "the material facts of the transaction." 805 ILCS 5/8.60(a)(1)....
>
> At the time of the vote, Ronsen had been a member of the board for approximately seven days. Fait disputes whether Ronsen had enough time to familiarize himself with Pentech's financial condition, including Pentech's search for capital, prior to the vote. Drawing all reasonable inferences in Fait's favor, a genuine issue of material fact exists as to whether the offering was approved by Ronsen with knowledge of all material facts. The burden then shifts to defendants to prove the offering was fair to Pentech.

Fait v. Hummel, No. 01 C 2771, 2002 U.S. Dist. LEXIS 4963, at *14 (N.D. Ill. Mar. 21, 2002). Thus, the court denied defendants' motion for summary judgment.[40] *See also*

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[40] Similar to Tenn. Code Ann. §48-18-302(a), 805 ILCS 5/8.60 states: "Director conflict of interest. (a) If a transaction is fair to a corporation at the time it is authorized, approved, or ratified, the fact that a director of the corporation is directly or indirectly a party to the transaction is not grounds for invalidating the transaction or the director's vote regarding the transaction; provided, however, that in a proceeding contesting the validity of such a transaction, the person asserting validity has the burden of proving fairness unless: (1) the material facts of the transaction and the director's interest or relationship were disclosed or known to the board of directors or a committee of the board and the board or committee authorized, approved or ratified the transaction by the affirmative votes of a majority of disinterested directors, even though the disinterested directors be less than a quorum; or (2) the material facts of the transaction and the director's interest or relationship were disclosed or known to the shareholders entitled to vote and they authorized, approved or ratified the transaction without counting the vote of any shareholder who is an interested director."

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Paramount Commc'ns v. QVC Network Inc., 637 A.2d 34, 44 (Del. 1994) ("[T]his Court has stressed the importance of the board being adequately informed in negotiating a sale of control: 'The need for adequate information is central to the enlightened evaluation of a transaction that a board must make.'").

The materiality of the information concealed by Perdue and Beré from shareholders, from Lazard, and from at least some of the Company's directors, cannot be seriously questioned. Indeed, there is no better evidence of materiality than that Dollar General management and KKR discussed Dollar General's growth plans prominently in every presentation to every constituency with a post-merger interest in the Company during the spring of 2007. The materiality of Dollar General's store growth analysis is further evidenced in the testimony of Plaintiff's financial expert, Mary O'Connor, who, working with the financial projections of Dollar General's management, and incorporating the expected store growth, reached the opinion that the fair value of Dollar General was over $1 billion more than that paid by KKR. SAF ¶213; O'Connor Summ. II.D.

Indeed, Defendants do not deny that to properly value a company, you must take into account its growth prospects. As Defendants' own expert, Professor Lehn, admitted:

> [O]ne area where perhaps there is some degree of agreement between Ms. O'Connor and me, is that ***you want your forecast period to extend to a point at which you think the company has settled into steady state.*** And at the end of that forecast period then your terminal value should reflect that steady state reality. Now ***when one thinks about steady state, a realistic assumption is that the company has exhausted or come close to exhausting their value creating growth opportunities***, which means all growth beyond the end of that steady state, beyond the forecast period is neither value additive or value destructive, that it's largely value neutral, which means that the value of a

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> company at the end of a forecast period is largely coming from all the good things it's invested in to that point.

SAF ¶ 211, Lehn I Tr. at 176.[41] Lehn reiterated this point in his second deposition:

> I have an opinion that whatever the forecast period is in a given scenario, the assumption, either implicit or explicit, is that at the end of that period the company has achieved steady state which then requires one to constrain that terminal value in an appropriate way.

SAF ¶212, Lehn II Tr. at 261.

Lazard expressly premised its opinion regarding the value of Dollar General on the belief that there would be no additional Dollar General store openings after 2011. *See* Proxy at 22. Defendants do not dispute that Lazard's assumption was incorrect. Further, Defendants' experts did not address how the store growth information would affect valuation. *See* SAF ¶221. (Lehn Oct. 28 Tr. at 261 ("As to whether or not Dollar General would achieve steady state after five years, ten years, 15 years or 20 years, I have no opinion."); Gompers Tr. at 11 ("Q. So am I also correct that you have not analyzed Dollar General's growth potential? A. That is correct.").)

Defendants' argument that the Proxy's "no growth" statement is not a materially misleading misstatement or omission because it accurately describes what Lazard did is equally without merit. The fact that Lazard accounted for no growth does not mean there ***was*** no growth, it just means that Lazard was misled about that, along with shareholders. Indeed, "misrepresentation may be found in statements which are literally true, but which create a false impression in the mind of the hearer, as is sometimes the case where a

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[41] Professor Lehn also identified "steady state" as "achiev[ing] a state of maturity such that the opportunity to identify lots of new projects that create value is greatly limited" Lehn I Tr. at 181.

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complicated financial statement is issued by a seller of securities." Page Keeton et al., *Prosser & Keeton on the Law of Torts* §106 at 736-37 (5th ed. 1984). The United States Supreme Court similarly held in *Virginia Bankshares, Inc. v Sandberg*, 501 U.S. 1083 (1991):

> [N]ot every mixture with the true will neutralize the deceptive. If it would take a financial analyst to spot the tension between the one and the other, whatever is misleading will remain materially so, and liability should follow. . . . ***The point of a proxy statement, after all, should be to inform, not to challenge the reader's critical wits.***

Id. at 1097; *see also Bennett v Trevecca Nazarene Univ* , No. M2004-01287-COA-R3-CV, 2005 Tenn App. LEXIS 641, at *17-*18 (Tenn. Ct. App. Oct. 7, 2005) (reversing motion for summary judgment against plaintiff) ("'if [one] does speak with reference to a given point of information, voluntarily or at the other's request, he is bound to speak honestly and to divulge all the material facts bearing upon the point that lie within his knowledge. Fragmentary information may be as misleading . . . as active misrepresentation, and half-truths may be as actionable as whole lies . . . .'"). Having taken it upon themselves to discuss the Company's store growth prospects in the Proxy, Defendants were obligated to disclose the ***whole*** truth about those prospects.

In sum, the evidence shows that Defendants made material misstatements or omissions in breach of their duty of loyalty and good faith, and which resulted in uninformed decisions by Dollar General's Board and its shareholders. At a minimum, there are genuine issues of fact in this regard that preclude summary judgment. *See Hartford Life Ins. Co.*, 72 S.W. at 961-62; *Hall*, 1996 Tenn. App. LEXIS 384, at *17-*18 (issues regarding breaches of fiduciary duty are questions of fact for the fact-finder).

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4. The Concealed Information Was Not Publicly Known

Defendants attempt to argue that the true information regarding Dollar General's growth prospects that was misrepresented in the Proxy was nevertheless publicly known. Def. Mem. at 39-43. That is simply untrue; at a minimum, it is a question of material fact unsuitable for determination on summary judgment.

Where the information released to investors is mixed or inconsistent, summary judgment is not appropriate. In Delaware, the disclosures made in the proxy control the outcome of a dispute. *See, e g , O'Malley v. Boris*, 742 A.2d 845, 851 (Del. 1999) (Delaware Supreme Court reversed Chancery Court finding that a reasonable investor could not miss material facts implied by disclosures, stating that "[i]nvestors should not be required to correctly 'read between the lines' to learn all of the material facts relating to the transaction at issue"); *In re Trans World Airlines, Inc. S'holders Litig.*, Civ. A. No. 9844, 1988 Del. Ch. LEXIS 139, at *29 (Del. Ch. Oct. 21, 1988) ("Nor can I agree that if a fact is material ... a failure to disclose it is necessarily cured by reason that it could be uncovered by an energetic shareholder by reading an SEC filing."); *Turner v. Bernstein*, 776 A.2d 530, 544 (Del. Ch. 2000).

Other courts also treat mixed signals of the type here as a question of fact, unsuitable for summary judgment. For example, the Fourth Circuit Court of Appeals, held in *Cooke v. Manufactured Homes, Inc* , 998 F.2d 1256 (4th Cir. 1993):

> Appellants assert that the misrepresentations and/or omissions by MH created a conflicting mix of information on which the market justifiably relied and that the reliance of the market on this mix of information led to an artificially inflated stock price, thereby giving rise to a genuine issue of material fact.... The promising representations in the press releases issued by MH do not wholly comport with the representations announcing declining earnings and

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> rising costs or with the articles detailing the precarious state of the finances of MH.
>
> This total mix of information of failing finances and fiscal growth, prior to December 17, 1988, sufficiently gives rise to different interpretations as to whether the representations and/or omissions made by MH were materially misleading to the market. The impression that this mix of information conveyed cannot be resolved as a matter of law. We therefore conclude that Appellants have presented sufficient evidence to raise a genuine issue of material fact with respect to the mix of information prior to December 17, 1988.

Id. at 1262.

The information in the market regarding Dollar General's potential store growth was decidedly mixed, leaving investors with no clear answer on the Company's future. Among other things, and as discussed above at Section II.C.3:

- Lazard expressed concern to the Board that the Company was nearing saturation, and did so from the beginning to the end of its involvement in the deal.

- Calbert testified that the market viewed Dollar General as being saturated: "there were a lot of analyst reports on this particular company that they had reached -- with 8300 stores, they had reached saturation" and KKR hired a third party consulting firm to independently research the Company's growth potential.

- The reports of analysts took conflicting views on the issues of growth and saturation. Even Goldman Sachs – which initiated coverage in early September 2006 and discussed a model showing a potential for 18,000 stores – two weeks later downgraded Dollar General stock, calling its plans and potential into question.

- On the same day as Dollar General issued its press release announcing Project Alpha, Perdue participated in a conference call in a conference call during which he conceded that everyone was concerned about saturation and intimated that the saturation issue was related to the decision to close certain stores. SAF ¶261.

Finally, the last thing shareholders heard from the Company regarding growth was the Proxy projecting no new stores after 2011. In short, there was at best a mix of information

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regarding the Company's growth prospects in the market, and the most definitive statement of all – the last – was the merger Proxy itself.

E. Under Tennessee Law, Even if the Outside Directors (or Shareholders) Ratified the Transaction, Plaintiffs' Breach of Fiduciary Duty Claims Would Survive Summary Judgment

In *McRedmond v. Estate of Marianelli*, 46 S.W.3d 730 (Tenn. Ct. App. 2000), the court applied a Kentucky statute that is identical to Tenn. Code Ann. §48-18-302.[42] The trial court had granted summary judgment based on this ratification statute, holding that because the transaction had been ratified by fully informed, independent directors, the transaction could not be voided and plaintiffs could not proceed with their breach of fiduciary duty claims.

On appeal, the Tennessee Court of Appeals affirmed in part and reversed in part. The court held that because the transaction had been properly ratified under the statute, the transaction could not be voided. *Id.* at 737-38. However, the court reversed summary judgment as to the fiduciary duty claims. *Id.* at 738-39. On a petition for rehearing, the Tennessee Court of Appeals clarified, in no uncertain terms, that the purpose of a ratification

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[42] Specifically, Ky. Rev. Stat. § 271B.8-310 states:

> (1) A conflict of interest transaction shall be a transaction with the corporation in which a director of the corporation has a direct or indirect interest. A conflict of interest transaction shall not be voidable by the corporation solely because of the director's interest in the transaction if any one of the following is true:
>
> (a) The material facts of the transaction and the director's interest were disclosed or known to the board of directors or a committee of the board of directors and the board of directors or committee authorized, approved, or ratified the transaction;
>
> (b) The material facts of the transaction and the director's interest were disclosed or known to the shareholders entitled to vote and they authorized, approved, or ratified the transaction; or
>
> (c) The transaction was fair to the corporation.

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statute "is to create a framework within which corporations can enter into binding agreements, even where conflicts of interest arise from such agreements, ***not to shield corporate directors from liability for breaches of their fiduciary duties.***" *McRedmond*, 46 S.W.3d at 741. The court continued:

> It appears to us that the plaintiffs have raised genuine questions of fact as to whether in formulating, investigating and acting upon the [transaction], the individual defendants have conducted themselves in accordance with the [applicable standard of fiduciary duty] statute. We are not saying that they have not, but simply that they are not entitled to summary judgment on that question, and that the plaintiffs are entitled to their day in court.

Id. at 741-42.[43]

Thus, in Tennessee, ratification does not extinguish fiduciary duty claims; it merely forecloses rescission, or similar relief that would void the transaction in question. This is similar to how other types of voidable claims are treated in Tennessee. *See, e.g., Vance v. Schulder*, 547 S.W.2d 927, 931 (Tenn. 1977) ("An individual induced by fraud to enter into a contract may elect between two remedies. He may treat the contract as voidable and sue for the equitable remedy of rescission or he may treat the contract as existing and sue for damages at law under the theory of 'deceit.'").

In this regard, Tennessee law and Delaware law are in conflict, because in Delaware, fully informed ratification may extinguish fiduciary duty claims. *See, e.g., Orman v. Cullman*, Civ. A. No. 18039, 2004 Del. Ch. LEXIS 150 (Del. Ch. Oct. 20, 2004). For this

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[43] The referenced statute, Ky. Rev. Stat. § 271B 8-300, is virtually identical to Tenn. Code Ann. § 48-18-301, which states "A director shall discharge all duties as a director, including duties as a member of a committee. (1) In good faith; (2) With the care an ordinarily prudent person in a like position would exercise under similar circumstances, and (3) In a manner the director reasonably believes to be in the best interests of the corporation."

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reason, Defendants' Delaware law-based arguments, including their arguments regarding a supposed requirement that Plaintiffs establish that a majority of the Board was somehow interested or lacked independence, are ***not*** applicable under Tennessee law. To hold otherwise would not only contradict *McRedmond* but Tenn. Code Ann. §48-18-302 as well.

In other words, the ratification statute of Tenn. Code Ann. §48-18-302 is not intended to shield individual directors who breach their fiduciary duties from all potential liability. Rather, the statute serves only to shield the transactions that are approved by an otherwise independent (and informed) board or shareholders from judicial unwinding. Together with the exculpatory provisions (discussed below), this State's policy choice becomes clear: directors innocent of bad faith or disloyal wrongdoing are shielded from personal liability, and transactions approved by a majority of innocent directors are shielded from judicial disruption after closing; ***however,*** directors who breach their duties in bad faith, must face personal liability to aggrieved shareholders.

To hold otherwise would either impermissibly add a "majority of the board" condition to the definition of "conflicted transaction" set forth in Tenn. Code Ann. §48-18-302, or would render Tenn. Code Ann. §48-18-302 and/or *McRedmond* a nullity. Neither result is consistent with Tennessee law. Moreover, as shown herein, there are genuine issues of material fact implicating a majority of the Board in breaches of fiduciary duty, thus precluding summary judgment no matter what.

F. Under Tennessee Law, There Are Genuine Issues of Material Fact Regarding Whether Defendants Breached Their Duty of Good Faith

The record amply demonstrates disputed facts that suggest that the Outside Directors were deceived by Perdue, Beré and others. Defendants' most recent submissions, including

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the Bottorff Affidavit, now create a question whether, in fact, the Outside Directors approved the merger, then issued a misleading Proxy Statement in a manner inconsistent with a finding that they acted in good faith. The "good faith" concept is codified by the Tennessee Business Corporations Act. Specifically, Tenn. Code Ann. § 48-18-301(c) states: "A director is not acting in good faith if the director has knowledge concerning the matter in question that makes reliance otherwise permitted by subsection (b) unwarranted." Here, Lazard's fairness opinion was expressly premised on no store growth after 2011. Proxy at 22. Defendants admittedly relied on that fairness opinion. As Knuckles testified:

> Q. And in the proxy, it indicates that the board of directors acting with the advice and assistance of its outside legal counsel and financial advisers approved the merger, correct?
>
> A. Yes.
>
> Q. And is it your understanding that one of the basis for you recommending the merger to shareholders as being fair was based upon the advice you were given by your financial advisers?
>
> A. Yes.

Knuckles Tr. at 8. *See also* Proxy at 19.

Yet, if Bottorff is to be believed – that the Board was fully aware that Dollar General had the potential to grow from 8,000 stores to 17,000 stores – then the Board necessarily knew that Dollar General, contrary to the fundamental basis of Lazard's fairness opinion, had significant growth opportunities after 2011. Thus, the Board had "knowledge concerning the matter in question that ma[de] reliance [on Lazard's fairness opinion] unwarranted." Under Tennessee law, such conduct was a breach of the Board's duty of good faith.

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Putting aside Bottorff's Affidavit, not all directors seem to have possessed this information. Thornburgh testified that he had no knowledge of it.[44] As for Knuckles, depending on which part of the deposition transcript one reads, she either had no knowledge of potential growth, some knowledge of potential growth, or significant knowledge of potential growth; either did or did not believe that the Company had store growth potential beyond 2011; and either was or was not told by management that the Company had such growth potential. *See* Knuckles Tr., *passim*. At a minimum, these conflicting stories amongst the directors give rise to genuine issues of material fact regarding whether the Board, or some of its members, acted in bad faith.

In *Stone ex rel. AmSouth Bankcorporation v. Ritter*, the Delaware Supreme Court held that "the fiduciary duty of loyalty is not limited to cases involving a financial or other cognizable fiduciary conflict of interest. It also encompasses cases where the fiduciary fails to act in good faith." 911 A. 2d 362, 370 (Del. 2006) The Delaware Supreme Court added that: "***Where directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith***." *Id* The Chancery Court, in the recent *Ryan v. Lyondell Chemical Co.* case, cited the above law in holding: "One consequence if directors act disloyally or not in good faith is that the protections of an exculpatory charter

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[44] Defendants try to explain away Thornburgh's lack of knowledge in their motion by arguing that Thornburgh did not know because he had only recently joined the Board. This may be true, but if so, it is an indication that neither the Board nor the Strategic Planning Committee, of which Thornburgh was a member, discussed the Company's growth plan and prospects as part of the merger deliberations. There also is no evidence that the Board, or anyone acting on the Board's behalf, ever performed valuation calculations taking Dollar General's future growth potential into account.

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provision do not attach." C.A. No. 3176-VCN, 2008 Del. Ch. LEXIS 105, at *87 (Del. Ch. July 29, 2008).

Consideration of growth potential is not the only area where there are genuine issues of material fact regarding whether the Board acted in good faith. Like here, the court in *Ryan* faced a challenge to a merger in which there was a single bidder, no widespread auction process, and a merger agreement that contained a 3% termination fee, a no shop clause, and a matching rights provision. *Compare* 2008 Del. Ch. LEXIS 105, at *31 *with* Section II.F above (detailing deal protections in the Merger Agreement). Defendants moved for summary judgment, arguing that their conduct in connection with the merger was protected by various defenses. The court disagreed.

> [A]lthough deal protections are part of the mergers and acquisitions landscape and can serve numerous important purposes for both the target and the acquirer, the reasonableness of the Board's decision to grant this particular mix of deal protections under the circumstances presented is a question of fact that cannot be resolved on summary judgment. After trial, or perhaps on a more complete summary judgment record, the Court may be satisfied that the Board in fact secured the "best" deal available to the shareholders, or, at the very least, that it undertook to discharge its *Revlon* duties in good faith under the circumstances.... On summary judgment, however, where the Court cannot weigh the evidence presented and is required to draw any reasonable inference in favor of Ryan, the non-moving party, and where there is considerable doubt as to the adequacy of the Board's efforts under *Revlon*, the Court cannot conclude that the Board's decision to agree to this particular mix of deal protections was reasonable. Accordingly, summary judgment is denied.

Id. at *83-*84

Here, the facts show that Defendants decided to limit the process to only two teams of private equity bidders (and to refuse to engage other private equity entities that Defendants knew had expressed a recent interest in the Company, or to involve potential strategic

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bidders). At the end of that "process," only a single bid was received. As the Delaware Supreme Court observed in *Barkan v Amsted Industries, Inc.*, 567 A.2d 1279 (Del. 1989):

> When the board is considering a single offer and has no reliable grounds upon which to judge its adequacy, this concern for fairness demands a canvas of the market to determine if higher bids may be elicited. As the Chancellor recognized, the circumstances in which [a] passive approach is acceptable are limited. "A decent respect for reality forces one to admit that . . . advice [of an investment banker] is frequently a pale substitute for the dependable information that a canvas of the relevant market can provide." The need for adequate information is central to the enlightened evaluation of a transaction that a board must make.

Id. at 1287. Dollar General was in the midst of a turnaround. Certain directors pointed this out, when they learned that KKR was looking at acquiring the Company, and advocated that it was the wrong time to sell the Company to a bottom-fisher. Worse, the Board appears to have lacked adequate information regarding Dollar General's true value. Under these facts, there are, at a minimum, genuine issues of material fact regarding whether the Board exhibited a conscious disregard for its duty to maximize shareholder value in this circumstance. *See Bayberry Assocs. v. Jones*, 783 S.W.2d 553, 561 (Tenn. 1990) (states that directors have a duty to get "'the best price for the stockholders at a sale of the company'"); *City of Pontiac*, slip op. at 1 ("Another governing principle is that maximizing the shareholders' interest is a paramount concern of the directors.").

G. Under Tennessee Law, There Are Genuine Issues of Material Fact that Preclude Application of the Business Judgment Rule on Summary Judgment

Defendants also seek to escape liability by invoking the "business judgment rule." Under Tennessee law, the business judgment rule does not apply to the issues in controversy

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here. "Tennessee courts recognize and follow the business judgment rule in certain circumstances." *Summers*, 112 S.W.3d at 527. The court elaborated:

> Where it applies, the business judgment rule is a presumption that a corporation's directors, when making a business decision, acted on an informed basis, in good faith, and with the honest belief that their decision was in the corporation's best interest. . . . The rule does not apply when the director or officer has an interest in the decision, did not actually make a decision, or made an uninformed decision.

Id. at 528. The court further explained that "[b]ecause of the reasons for its creation, the rule does not apply to decisions which breach the duty of loyalty. The business judgment rule was developed by the courts to protect corporate management from liability for mistakes in business judgment. ***Thus, the duty of care is implicated, not the duty of loyalty.*"** *Id.*

The court concluded:

> Because the rule was developed to analyze duty of care issues, "courts do not typically apply the business judgment rule to duty of loyalty issues. . . ." [I]f the directors or officers are unable to prove full disclosure or fairness, they may be liable in damages or the court may rescind the transaction. The business judgment rule provides no shelter for directors and officers who breach the duty of loyalty.

Id at 528-29.

Indeed, *City of Pontiac*, an unpublished trial court opinion by Chancellor Ellen Lyle – upon which Defendants heavily rely in their Motions – acknowledges these limitations. Chancellor Lyle noted that:

> The business judgment rule . . . assumes that directors of a corporation act on an informed basis, in good faith and in the honest belief that the action taken was in the best interest of the company. If a director or officer does not inform itself, prior to voting on the acquisition, of all material information reasonably available to it or has a material interest in the transaction or fails to provide candid disclosure to the shareholders in connection with the vote, the assumptions of the business judgment rule do not hold true. In such a case, the business judgment rule does not apply to shield the directors' decision.

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> Instead, the defendants bear the burden of demonstrating the entire fairness of the transaction to the company's shareholders. . . .

City of Pontiac, slip op. at 2. The evidence here shows that certain directors (and senior officers) had an interest in the acquisition and breached the duty of loyalty. The evidence also shows that certain directors breached their duty of good faith, and/or failed to make an informed decision regarding the acquisition. This failure was the result of intentional manipulation of a board process. *See Mills*, 559 A.2d at 1284.

The outside directors and their financial advisor, Lazard, were deprived, through the actions of management, of the ability to make an informed assessment, negotiate appropriately, and, if necessary, shut down the negotiations unless a fair price were offered. *See id.* At a minimum, there are genuine issues of material fact regarding breaches of the duty of loyalty, good faith and full disclosure that preclude application of Tennessee's business judgment rule on summary judgment.

For all of these reasons, the business judgment rule does not apply and Defendants' arguments to the contrary are without merit. The Motions should be denied.

H. Under Tennessee Law, There Are Genuine Issues of Material Fact Precluding Application of Defendants' Tenn. Code Ann. §48-12-102(b)(3) Affirmative Defense on Summary Judgment

Defendants argue that Dollar General's corporate charter protects the Board from liability. Tenn. Code Ann. §48-12-102(b)(3) permits the charter of a Tennessee corporation to include:

> A provision eliminating or limiting the personal liability of a director to the corporation or its shareholders for monetary damages for breach of fiduciary duty as a director; provided, that such provision shall ***not*** eliminate or limit the liability of a director:

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> (A) For any ***breach of the director's duty of loyalty*** to the corporation or its shareholders;
>
> (B) For acts or omissions ***not in good faith*** or which involve ***intentional misconduct*** or a knowing violation of law . . . .

In other words, the statute shields only corporate directors from having to pay money damages resulting from breaches of the duty of care. This is determined on an individual by individual basis and can not result in a dismissal of the action as a whole. Defendants' corporate governance expert, Professor Coffee, agreed that the exculpatory provision must be applied on a director by director basis, and that it may protect innocent directors while not immunizing other directors – like Perdue and Beré – for their bad faith conduct. SAF ¶¶148-49. Coffee also agrees that the exculpatory provision has no bearing on the liability of third parties who aid and abet the breaches of disloyal insiders (even if a majority of the board is protected from personal liability because of their own ignorance of the wrongdoing at issue). Id. Johnston Ex. 33 at 100:4-101:11; see also *id.* at 105:15-106:7 (agreeing that third party that is "stage managing" CEO's deception of the board can be liable for knowing participation in the CEO's breaches of duty). It does ***not*** shield any individual defendant from liability for breaches of the duty of loyalty or good faith. It does not shield officers, such as Perdue and Beré from having to pay money damages and it does not shield third parties who aid and abet breaches by exculpated directors. SAF ¶149

This is an important distinction because Plaintiffs allege breach of fiduciary duty claims against officers, for loyalty and good faith, and against KKR and Dollar General for aiding and abetting. So even if the trier of fact were to determine that the Board breached its duty of care rather than its duty of loyalty or good faith, and that Dollar General's public shareholders were damaged as a result, the aiders and abetters would be liable for damages

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notwithstanding the fact that the directors were excused from payment of damages pursuant to Tenn. Code Ann. §48-12-102(b)(3).

For example, in *Brandt v. Hicks, Muse & Co. (In re Healthco International Inc.)*, 208 B.R. 288, 308-09 (Bankr. D. Mass. 1997), the court held, "[t]he statute's exemption from liability for lack of care extends only to directors. Section 102(b)(7) [of the Delaware General Corporation Law] purports to grant no protection to third parties who aid and abet directors in the violation of their obligations of either care or loyalty."[45] Accordingly, "a determination that the director defendants are exculpated from paying monetary damages can be made only ***after the basis*** for their liability has been decided," *i.e.*, at trial. *Emerald Partners v. Berlin*, 787 A.2d 85, 94 (Del. 2001) (emphasis in original); *Emerging Communications*, 2004 Del. Ch. LEXIS 70, at *103.

In any event, the basis for Defendants' liability cannot be decided on the present motion because, as detailed above, there are genuine issues of material fact regarding whether Defendants breached their duties of loyalty and good faith, and engaged in intentional misconduct. Accordingly, Tenn. Code Ann. §48-12-102(b)(3) does not shelter Defendants from liability for their breaches of fiduciary duty on summary judgment.

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[45] *See also* Anne E. Conaway, *The Multi-Facets Of Good Faith in Delaware: A Mistake In The Duty of Good Faith and Fair Dealing, A Different Partnership Duty of Care, Agency Good Faith and Damages; Good Faith and Trust Law*, 10 Del. L. Rev. 89, 123 (2008) (Delaware exculpatory clause, similar to Tennessee's, "only eliminates monetary *liabilities and not duties* and it grants no protections to persons beyond directors. As a result . . . secondary liability, or aiding and abetting, remains a viable cause of action notwithstanding the exculpation of the directors.")

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I. There Are Genuine Issues of Material Fact Precluding Application of Defendants' Ratification Affirmative Defense on Summary Judgment

To the extent there is any ratification defense in Tennessee beyond what is set forth in Tenn. Code Ann. §48-18-302(a), that defense would not apply here – and even if it did, under *McRedmond* it could only operate to insulate the merger from being rescinded. It would not bar Plaintiffs' fiduciary duty claims.

The courts to consider the issue have made clear that to establish shareholder ratification "the burden clearly remains on those relying on the vote to show that they ***completely disclosed all material facts relevant to the transaction***." *Weinberger v. UOP, Inc*, 457 A.2d 701, 703 (Del. 1983); *accord Yiannatsis v. Stephanis by Sterianou*, 653 A.2d 275, 280 (Del. 1995). A ***single*** material non-disclosure is sufficient to defeat a shareholder ratification defense. *O'Malley*, 2002 Del. Ch. LEXIS 33, at *24-*28.

Defendants have not shown, and cannot show, that they fully disclosed all material information to the Company's public shareholders. Indeed, Plaintiffs have pled – and can prove – that Defendants concealed material information from shareholders, including information regarding the Company's huge growth prospects and an unlevel playing field created by Perdue. Nevertheless, Defendants rely on *Indiana State* (an opinion from Chancellor McCoy ostensibly applying Delaware law), to say that any breaches of fiduciary duty were somehow ratified because the Proxy disclosed the existence of this litigation.

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With all due respect to Chancellor McCoy, this holding – which is currently on appeal – misstates the law.[46]

Moreover, a couple of lines in a Proxy regarding the existence of a lawsuit simply cannot get Defendants over the high hurdle they must clear to establish ratification. Indeed, the Proxy's disclosure of this litigation is even less detailed than the litigation disclosures in the *Santa Fe* and *Ryan* proxies, a couple of exemplar cases in which Delaware courts rejected ratification defenses. The Court should reach the same result here, and should reject the anomalous approach in *Indiana State*.

Finally, Defendants argue that nondisclosures cannot cause injury unless shareholders would have voted the merger down and shareholders would have been better off had the merger not gone forward. *See* Defs' Mem. at 14. In support of this argument, Defendants quote *In re Transkaryotic Therapies, Inc*, 954 A.2d 346, 362 n. 55 (Del. Ch. 2008) for the proposition that to state a disclosure claim, Plaintiffs must show "that the vote would have been different but for the allegedly bad disclosure."[47] Dollar General Mem. at 14; *Transkaryotic*, 954 A.2d at 362 n. 55. Were this true, it would be directly contrary to the Delaware Supreme Court and the U.S. Supreme Court, both of which acknowledge that the

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[46] In support of the holding, *Indiana State* cites two "storm warning" cases: *Benak ex rel. Alliance Premier Growth Fund v. Alliance Capital Management L.P.*, 435 F.3d 396, 400 (3d Cir. 2006) and *DeBenedictis v Merrill Lynch & Co.*, 492 F.3d 209, 216 (3d Cir. 2007). ***But these cases address the issue of when the statute of limitations in securities fraud cases begins to run – they have nothing whatsoever to do with the ratification defense under fiduciary duty law***

[47] Defendants also cite *Indiana State* for this proposition. However, *Indiana State* does not cite any authority for this proposition and in any event would be controlled by Delaware law, which does not require any showing that the merger would have been voted down when there is evidence of a breach of the duty of loyalty or good faith by the directors who authorized the disclosures *Transkaryotic*, 954 A. 2d at 362 Thus, *Indiana State* does not support Defendants' arguments.

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duty of candor demands only that the undisclosed information be material – i.e., it is considered important in deciding how to vote; it need not change the outcome of the vote. *TSC*, 426 U.S. at 449.

Defendants quote *Transkaryotic* out of context. The footnote from which Defendants quote comes at the end of the following sentence: "I hold that this Court cannot grant monetary or injunctive relief for disclosure violations in connection with a proxy solicitation in favor of a merger three years after that merger has been consummated and ***where there is no evidence of a breach of the duty of loyalty or good faith by the directors who authorized the disclosures***." 954 A. 2d at 362. Here, by contrast, as detailed above, Plaintiffs have pled – and can prove – that Defendants breached their duties of loyalty and good faith. Thus, *Transkaryotic* does not apply.

Defendants cite a series of cases for the proposition that damages cannot be recovered for disclosure violations. These cases all involve director elections and/or derivative claims for which any recovery would go to the Company, not individual shareholders, with class claims stemming from an unfair merger, and thus are irrelvant. *See Loudon v. Archer-Daniels-Midland Co.*, 700 A.2d 135 (Del. 1997) (challenging the disclosures in a proxy statement for an annual meeting to elect directors); *In re J P. Morgan Chase & Co. S'holder Litig v Harrison*, 906 A.2d 766, 773 (Del. 2006) (suit was derivative claim for waste, not class claim, so no individual damages awardable); *In re Tyson Foods, Inc. Consol. S'holder Litig*, 919 A.2d 563, 602 (Del. Ch. 2007) ("Plaintiffs' allegations demonstrate harm to the corporation that accrued from the lack of disclosure in the 2004 proxy"). Defendants' other cases are inapposite as well.

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As discussed above, *Transkaryotic* specifically premised its ruling on the fact that – unlike here – there were no bad faith or disloyalty claims attendant to the disclosure claim at issue. *Zoren v. Genesis Energy, L.P.*, 836 A.2d 521 (Del. Ch. 2003), is to the same effect – "the Amended Complaint does not state a claim for relief as to the fairness of the economic terms of the Restructuring. Thus, there is no possibility that the court would award actual damages to Zoren or the class because they suffered no economic injury as a result of the vote to approve the Restructuring." *Id.* at 531. As for *In re Staples S'Holders Litig.*, 792 A.2d 934 (Del. Ch. 2001). It does ***not*** hold that money damages cannot be recovered for disclosure violations; it merely stands for the unremarkable proposition, like a host of other Delaware cases, that injunctive relief "is ... the preferred remedy, ***where practicable***." *Id.* at 960. Injunctive relief is no longer practicable here, but damages for an unfair merger that includes, but is not based solely on, disclosure violations as part of various breaches of fiduciary duties – including the duties of loyalty and good faith – are patently appropriate, and none of Defendants' cases support a contrary conclusion.

Defendants also argue, citing cases such as *In re JCC Holding Co. S'holders Litig.*, 843 A.2d 713, 721 (Del. Ch. 2003), that Plaintiffs' claims regarding the concealed growth information amount to nothing more than quibbling with Lazard's methodologies. Not true. The methodology is not the issue; it is that Lazard's valuation was based on a premise that Lazard was led to believe was true, but that some (and perhaps all) of the Board knew was in fact false, all of which raise genuine issues of material fact precluding summary judgment. These Board members, at a minimum, sat silent while Lazard, other Board members, and shareholders, premised their evaluations of Dollar General on this false information.

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J. The Acquiescence Affirmative Defense Does Not and Cannot Bar Plaintiffs' Claims, on Summary Judgment or Otherwise

Defendants argue that, because the City of Miami Trust's investment advisor voted the Trust's shares in favor of the merger, it somehow acquiesced to Defendants' breaches of fiduciary duty and is barred from pursuing claims in this litigation. *See* Def. Mem. at 19-20. Defendants' argument is without merit.

Where there is a dispute as to whether a shareholder was fully informed at the time of the vote – and much of Plaintiffs' key evidence was not produced to them by Defendants until well after the vote – summary judgment on the basis of acquiescence is wholly inappropriate. As the Court held in *Iseman v Liquid Air Corp.*, C.A. No. 9694, 1993 Del. Ch. LEXIS 24 (Del. Ch. Feb. 11, 1993), a possible acquiescence defense is no basis for summary judgment:

> Defendants argue that Iseman and Gruenberg have acquiesced by accepting the $ 37 per share merger consideration with knowledge of defendants' alleged unfair dealing and misleading statements. Defendants point out that Gruenberg believed the merger price was grossly inadequate from the outset and that plaintiffs must have been aware of the alleged misstatements in the Information Statement before tendering their shares since specific disclosure allegations were included in the Amended Complaint.
>
> I find defendants' argument unpersuasive. Following *Bershad*, the question of acquiescence turns on whether plaintiffs were "informed" stockholders at the time they tendered their shares for the merger consideration. From the allegations in the Amended complaint, it appears that plaintiffs were not fully informed. They claim that the Information Statement contained material omissions and misrepresentations. The fact that plaintiffs were able to make such allegations does not mean that they had somehow learned all of the information that had been withheld from or misrepresented to the stockholders of Liquid Air. It only means that they had been able to piece together enough from what the Information Statement did and did not say to satisfy the standards of Chancery Court Rule 11 in making allegations upon information and belief. Accordingly, I am not prepared to make a finding of acquiescence

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> on this record either for purposes of denying class certification or granting defendants' motion for summary judgment.

Id at *6-*7.

As in *Iseman*, summary judgment would be inappropriate here because neither the City of Miami Trust, nor the Company's other public shareholders, "had somehow learned all of the information that had been withheld from or misrepresented to the stockholders of" Dollar General. *Id.* at *7. The Court should reject Defendants' motion for summary judgment on the acquiescence affirmative defense.

Indeed, defendants' own case law does not support their position. Specifically, Defendants quote *In re PNB Holding Co. Shareholders Litigation*, No. Civ. A. 28-N, 2006 WL 2403999, at *21 (Del. Ch. Aug. 18, 2006). But the premise of the analysis in that case assumes that the plaintiff shareholder's vote was ***informed.*** *Id* Here, there are genuine issues of material fact regarding whether Defendants fully and fairly disclosed all material information to Dollar General's shareholders, including the City of Miami Trust, in connection with their vote on the merger.

K. There Are Genuine Issues of Material Fact Regarding Whether KKR and Dollar General Aided and Abetted the Other Defendants' Breaches of Fiduciary Duty, Which Preclude Summary Judgment on Those Claims

Tennessee's courts recognize "the common law civil liability theory of aiding and abetting." *Allen v McPhee*, 240 S.W.3d 803, 818 (Tenn. 2007). To establish such a claim, a plaintiff must allege "that 'the defendant knew that his companions' conduct constituted a breach of duty, and that he gave substantial assistance or encouragement to them in their acts.'" *Id.* (quoting *Cecil v. Hardin*, 575 S.W.2d 268, 272 (Tenn. 1978)). This theory is recognized in Delaware as well, in the merger context. As the court held in *Rand v. Western*

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Airlines, Civ. A. No. 8632, 1989 Del. Ch. LEXIS 118 (Del. Ch. Sept. 11, 1989), "if there were objective evidence that the transaction benefits the fiduciaries at the stockholders' expense, knowing participation by a third party might be inferable." *Id.* at *14. *See also Liquidation Trust v. Fleet Retail Fin. Group (In re Hechinger Inv. Co of Del.)*, 278 Fed. Appx. 125, 130 (3d Cir. 2008) (indicating that "trying to create, exploit, or otherwise profit from fiduciaries' conflicts [is] knowingly participating").

Here, there is certainly objective evidence that the transaction was designed to benefit Perdue, Beré and the rest of management – they are now owners of the Company (except for Perdue, who learned well after the merger was approved by the Board that he was not going to be retained after all) with arrangements to make huge profits on their investments. The evidence further shows that KKR knowingly participated in Defendants' breaches, from the confidential information that KKR obtained from Perdue prior to and during the Board's discussions regarding the acquisition, to KKR's illicit involvement with Lehman (which, in hopes of getting a large portion of the post-merger financing, claimed to have initially steered Perdue to KKR. Indeed, as explained in Section II.B above, KKR Calbert repeatedly advised Perdue on how to manipulate the Board and encouraged Perdue to divulge confidential information. In other words, KKR worked to "create, exploit, or otherwise profit from fiduciaries' conflicts" and thus "knowingly participat[ed]." *Fleet Retail*, 278 Fed. Appx. at 130. These facts are more than sufficient to state a claim for aiding and abetting; at a minimum, they create a genuine issue of material fact that precludes summary judgment.

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Dollar General's arguments regarding the aiding and abetting allegations against it fare no better. Dollar General argues that a corporation owes no fiduciary duties to shareholders, then complains that only a third party, not a fiduciary, can aid and abet a fiduciary's breach. *See* Dollar General Mem. at 29-30. But by arguing that it is not a fiduciary, Dollar General is essentially conceding that it *is* a third party, and thus can be liable for aiding and abetting. Dollar General's arguments thus make no sense. Moreover, the facts show that Dollar General, for example, filed a materially misleading Proxy with the SEC and mailed it to shareholders. Given that "[i]t is well established that a corporation is chargeable with the knowledge of its agents and employees acting within the scope of their authority," *Western Diversified Servs. v. Hyundai Motor Am , Inc.*, 427 F.3d 1269, 1276 (10th Cir. 2005), Plaintiffs have elicited sufficient facts to create a genuine issue regarding whether Dollar General knowingly participated in Defendants' breaches of fiduciary duty.

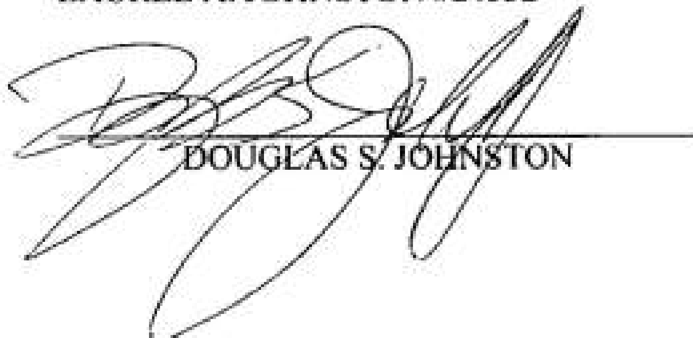
IV. CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that the Court deny Defendants' Motions for Summary Judgment on the Pleadings.

DATED: November 7, 2008

Respectfully submitted,

BARRETT, JOHNSTON & PARSLEY
DOUGLAS S. JOHNSTON, JR., #5782
TIMOTHY L. MILES, #21605
GERALD E. MARTIN, #20193
LAUREL A. JOHNSTON #24532



DOUGLAS S. JOHNSTON

COPY

217 Second Avenue, North
Nashville, TN 37201-1601
Telephone: 615/244-2202
615/252-3798 (fax)

Liaison Counsel

BERNSTEIN LITOWITZ BERGER &
GROSSMANN LLP
MARK LEBOVITCH
JONATHAN HARRIS
KATHERINE M. SINDERSON
1285 Avenue of the Americas, 38th Floor
New York, NY 10019
Telephone: 212/554-1400
212/554-1444 (fax)

COUGHLIN STOIA GELLER
RUDMAN & ROBBINS LLP
DARREN J. ROBBINS
RANDALL J. BARON
A. RICK ATWOOD, JR.
DAVID T. WISSBROECKER
655 West Broadway, Suite 1900
San Diego, CA 92101
Telephone: 619/231-1058
619/231-7423 (fax)

Co-Lead Counsel for Plaintiffs

KLAUSNER & KAUFMAN, PA
ROBERT D. KLAUSNER
10059 N.W. 1st Court
Plantation, FL 33324
Telephone: 954/916-1202
954 916-1232 (fax)

Additional Counsel for Lead Plaintiff City of Miami General Employees' & Sanitation Employees' Retirement Trust

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CERTIFICATE OF SERVICE

I hereby certify that on this 7th day of November 2008, a true and exact copy of the foregoing *Plaintiffs' Memorandum in Opposition to the Motion for Summary Judgment of Defendants Dollar General Corporation, the Directors, and Kohlberg Kravis Roberts & Co LP* was served via FedEx on the following:

Peter E. Kazanoff
SIMPSON THACHER & BARTLETT LLP
425 Lexington Avenue
New York, New York 10017
mchepiga@stblaw.com
pkazanoff@stblaw.com

Counsel for Dollar General Corporation, Kohlberg Kravis Roberts & Co , Buck Holdings, L P , and Buck Acquisition Corp

And was served via hand delivery on the following:

Steven A Riley
RILEY, WARNOCK & JACOBSON, PLC
1906 West End Avenue
Nashville, Tennessee 37203
sriley@rwjplc.com

Counsel for Dollar General Corporation Kohlberg Kravis Roberts & Co , Buck Holdings, L P , and Buck Acquisition Corp.

Wallace W. Dietz
Matthew M Curley
BASS, BERRY & SIMS
315 Deadrick Street, Suite 2700
Nashville, Tennessee 37238
wdietz@bassberry.com
mcurley@bassberry.com

Counsel for Individual Defendants

DOUGLAS S. JOHNSTON, JR.