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Case No. 2018-0307-JRS

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

KAREN SBRIGLIO and FIREMEN'S RETIREMENT SYSTEM OF ST. LOUIS, derivatively on behalf of Nominal Defendant FACEBOOK, INC.,	
Plaintiff,	
v.	C. A. No. 2018-0307-JRS
MARK ZUCKERBERG, SHERYL SANDBERG, MARC ANDREESSEN, ERSKINE B. BOWLES, SUSAN DESMOND-HELLMANN, REED HASTINGS, JAN KOUM, PETER A. THIEL, and PRICEWATERHOUSECOOPERS LLP,	[redacted] [redacted] **PUBLIC VERSION November 16, 2018**
Defendants,	
- and –	
FACEBOOK, INC.,	
Nominal Defendant.	

PLAINTIFFS' OMNIBUS OPPOSITION TO DEFENDANTS' MOTIONS TO DISMISS OR, IN THE ALTERNATIVE, STAY THESE PROCEEDINGS

[redacted]

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November 8, 2018

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INTRODUCTION

In the span of a ten-year period, Facebook Defendants directed, enabled and/or disregarded Facebook's illegal sharing of the private data of 2.2 billion users with millions of different types of third parties, including application ("app") developers, "integration partners," and "whitelist" companies, all of whom were fed user data without Facebook ever notifying its users or obtaining their consent. The Board had numerous warnings about these practices from regulatory actions, regulatory settlements, whistleblowers within Facebook, and media reports. The illegal practices created a snowball of liability that logically culminated in the largest data breach in history and Facebook now faces enormous liability as a result.

These illegal practices were adopted so that the user base would grow, despite that they violated: (a) consumer and privacy laws in the United States, the European Union and other countries around the world; (b) certifications to comply with the Privacy Shield Frameworks; (c) Facebook's Terms of Use with its users; (d) its policies on data security and user privacy; and (e) regulatory orders and settlements, including a consent decree that Facebook entered with the U.S. Federal Trade Commission ("FTC") that became a final order on July 26, 2012

(the "Consent Order"). Facebook, as a result, is the subject of intense investigation and regulatory scrutiny by governments the world over.[1]

None of this should have come as a surprise. Indeed, there was warning flag after warning flag, but the Facebook Defendants stuck their heads in the sand and ignored the warnings. Plaintiffs Karen Sbriglio ("Sbriglio") and Firemen's Retirement System of St. Louis ("FRS") (collectively, "Plaintiffs"), derivatively on behalf of Facebook, seek to hold Facebook Defendants responsible because their loyalties to Zuckerberg prevent them for impartially assessing whether to bring the claims arising from Zuckerberg's and their misconduct.

The record, including investigative reporting, whistleblowers, hearings before the United States House of Representatives and the United States Senate, hearings before the British Parliament, corporate records produced pursuant to Section 220 of the DGCL, and Facebook's now-public written responses to more than 2,000 questions posed by members of Congress, demonstrates that Facebook Defendants repeatedly violated their most basic fiduciary duties, and that the Court's intervention is required to prevent further harm to the Company and to

[1] Investigations were initiated by the U.S. Senate, U.S. House of Representatives, Department of Justice ("DOJ"), Federal Bureau of Investigations ("FBI"), Securities and Exchange Commission ("SEC"), FTC, and a coalition of 37 State Attorneys General. ¶¶27, 342. Foreign nations, including the United Kingdom ("UK") Information Commissioner's Office ("ICO"), the European Union ("EU"), Canada, and Israel, also opened independent investigations. ¶342.

remedy past harms. In addition, Plaintiffs seek relief that is both monetary and equitable.

Facebook Defendants and PwC move to dismiss on a host of grounds, including, *inter alia*, (1) failure to plead demand futility; (2) failure to state claims upon which relief can be granted; (3) claims of exculpation through Facebook's charter provision; and ripeness. Facebook Defendants seek to narrowly frame this case as solely Caremark and solely about Cambridge Analytica. They entirely ignore the allegations of how Officer Defendants made the decision to illegally share data with millions of app developers through 2014/2015, 60 companies on a secret "white list" through 2016, and 52 device makers through 2018 as part of their grow plans. Facebook Defendants then concealed and misled users, investors, U.S. Congress and British Parliament about these illegal practices. They also seek to marginalize the recurring alarm bells that were sounded off by regulators and news media about Facebook's illegal data sharing with third parties. However, even if this action were solely about *Caremark* duties and Cambridge Analytica, they would still lose.

STATEMENT OF FACTS

A. ZUCKERBERG DOMINATES EVERY FACET OF FACEBOOK

Facebook is a social media company founded by Zuckerberg in 2004. ¶78. Facebook's core asset is user data, which it uses to sell directed advertisements. ¶87. In 2017, the sale of direct advertisements accounted for over 98% of Facebook's $40.6 billion revenue. ¶88.

Zuckerberg has served as the CEO and director since he founded Facebook, and the Chairman of its Board since January 2012. ¶53. Zuckerberg is responsible for Facebook's day-to-day operations, and its overall direction and strategy. *Id*. In addition, Zuckerberg is the majority stockholder of Facebook, owning more than 53.3% of its voting power as of April 13, 2018, even though he only owns 16% of its total equity. *Id*. Zuckerberg's deep influence over Facebook's governance and affairs has been widely chronicled and has never been challenged because no one– either individually or as a group– has the power to do so. *See, infra*, Section I.B at 21-28.

B. OFFICER DEFENDANTS DECIDE TO OPEN FACEBOOK'S PLATFORM TO THIRD PARTIES IN PURSUIT OF HYPER-GROWTH

By 2007, Facebook's user-base plateaued to 50 million daily Facebook users. Frustrated, Zuckerberg decided on a "dramatic shift in business practice," inviting outside third parties to develop Facebook apps on its platform. ¶22. Facebook had previously been the "sole developer of its applications." *Id.*

[redacted]

Facebook gave third party apps free and open access to Facebook users' data while giving users only illusory controls over data and privacy, as no privacy setting could actually prevent unauthorized harvesting and misuse of a Facebook user's data. ¶¶22-23, 81-82, 99-101.

In 2008, Sandberg joined Facebook to execute Zuckerberg's "highly-aggressive growth plan." Under Sandberg's direction, Facebook attracted an estimated ***one million*** app developers by 2010. ¶¶19, 22, 83, 176. Also around that time, Officer Defendants entered Facebook into data sharing agreements with 52 "integration partners" from around the globe, each of which had unfettered access to user data without their users' knowledge or consent. ¶¶102, 250, 255-56. Officer Defendants similarly entered into data sharing agreements with 60 "whitelist" companies. ¶259.

Their plan worked. Facebook's open data sharing practices led to explosive growth in the user base, going from millions to billions of users. ¶23. As its user base increased, so too did Facebook's collection and sharing of personal user data, to the point where Facebook claimed it collects 29,000 data points on every user." ¶¶87-88 (citing Facebook 6/8/2018 Senate Response, 100-101). Facebook monetized these data points and thus its $40.6 billion dollars in revenue in 2017 hinge on Facebook's ability to collect this data. ¶¶85-86, 88. If users do not trust

that their data is secure, protected, and used only for authorized purposes, then users will stop providing Facebook data that it can convert into user advertisements and revenue. ¶89. Facebook's entire existence could be threatened. *Id.*

Zuckerberg and Sandberg instilled into their workforce a culture of relentless pursuit of growth at any cost (Zuckerberg's motto: "move fast and break things"). 43, 78-89, 123. The fuel for its hyper-growth was Facebook's most precious asset, the millions of terabytes of personal user data. ¶¶82-84, 263. Zuckerberg's second lieutenant, Vice President Andrew "Boz" Bosworth, explained this relentless pursuit of growth at any cost:

> We connect people. . . Maybe it costs someone a life by exposing someone to bullies. . . Maybe someone dies in a terrorist attack coordinated on our tools. . . We connect people. Period. That's why all the work we do in growth is justified. All the questionable contact importing practices. All the subtle language that helps people stay searchable by friends. . . .

¶123 (citing Ex. K, Andrew Bosworth, Facebook, Internal Employee Memorandum, dated 6/18/2016). When asked by the U.S. House about the "disturbing" Bosworth memorandum and Zuckerberg's "failed obligation to enforce ethics," Facebook responded: "We recognize that we have made mistakes, and we are committed to learning from this experience to secure our platform further and make our community safer for everyone going forward." *Id.* n.60

[redacted]

(citing Letter from Facebook to Chairman Greg Walden and Ranking Member Frank Pallone, U.S. House Energy and Commerce Committee, dated 6/29/2018).[2]

C. DIRECTOR DEFENDANTS CONSCIOUSLY DISREGARDED FACEBOOK'S ILLEGAL DATA SHARING

The Director Defendants enabled Zuckerberg's "move fast and break things" ethos. ¶¶43, 79-82, 105-106. Zuckerberg convinced users to share their personal private data (and that of their friends) under the guise that privacy mattered and that protections were in place, and then turned around and gave ***millions*** of unvetted, unknown third party app developers and device makers access to Facebook's platform. ¶¶90-107. Third parties could collect data for nearly any purpose. ¶106. Facebook was not watching. ¶¶117-23. Zuckerberg's indifference was described by the British Parliament as follows:

> It is extraordinary: if Facebook were a bank, and somebody was laundering money through it, the response to that would not be, "Well, that is a matter for the person who is laundering the money and for the authorities to stop them doing it. It is nothing to do with us. We are just a mere platform through which the laundering took place." That bank would be closed down and people would face prosecution. What you are describing here is the same attitude. . . .[3]

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[2] *https://docs.house.gov/meetings/IF/IF00/20180411/108090/HHRG-115-IF00-Wstate-ZuckerbergM-20180411.pdf.*

[3] ¶122 (citing Milner Tr. at Q421).

[redacted].

¶122. Meanwhile, at the core of every U.S. privacy and consumer law and regulation, the EU's General Data Protection Regulation ("GDPR"), and the various Privacy Shield Frameworks, ¶¶108-10, were the requirements that users must: (1) be given ***notice*** of any data sharing, (2) provide ***informed consent*** for how their data would be used, and (3) ***control*** their data and, in particular, personal identifiable information (PII). ¶¶110-11.

Facebook's Terms of Service also promised to protect users' data and give users "control" over how their information was "shared through privacy and application settings." ¶¶92-93, 97, 100. The Terms of Service claimed that users controlled "how their data was collected, used, and shared…" with third parties, ¶¶95, 100, and that Facebook "provided sufficient controls to users to protect their own privacy." ¶¶95, 97, 100. These Terms strictly prohibited sharing of PII with third parties and "harvest[ing] or collect[ing] email addresses or other contact information for the purposes of sending unsolicited emails or other unsolicited communications" was strictly prohibited. ¶¶94, 99.

Over the years Facebook's directors and officers were confronted with ample evidence of Facebook's illegal data sharing with third parties. ¶¶124-212. For example, in 2009, the Canadian Internet Policy and Public Interest Clinic ("CIPPIC") filed a complaint alleging, in relevant part, that Facebook's privacy

settings did not protect users' private information, which was being collected and used for unauthorized advertising. ¶¶128-29. CIPPIC ***explicitly*** sought to end the unlawful "open access by developers to users' personal information." *Id.* The Office of the Privacy Commissioner of Canada, which adjudicated the complaint, reached a settlement with Facebook in 2010 ("Canadian Regulatory Settlement") in which Facebook "agreed. . . [to] implement[] significant changes to its site. . . in order to give its users granular control over what personal information developers may access and for what purposes" and promised to "roll out the permissions model by September 1, 2010" and, until the "roll out" took place, "oversee the applications developers' compliance with contractual obligations." ¶129. Facebook failed to meet those obligations in the Canadian Regulatory Settlement in 2010. ¶130. No steps to ensure developers' compliance were taken. *Id.*

Facebook continued giving third parties unfettered access to user data without notice or consent and failed to "oversee the application developers' compliance with contractual obligations." ¶¶129, 144-64. Zuckerberg and Sandberg continued growing the developer community to more than one million unvetted entities that were given free and open access to the platform and its users' data (PII, friend lists, private messages, and the 29,000 data points collected by Facebook). ¶¶83, 84. Former Facebook Operations Manager Sandy Parakilas

testified that *anyone* could create a Facebook application, there was no background check. ¶¶145-46. Christopher Wylie, a whistleblower formerly associated with Cambridge Analytica, corroborated Parakilas's statement, testifying that "all kinds of people had access to the data." ¶153. No one at Facebook read the app developers' terms and conditions before giving them entrance onto its platform and access to any data. According to Facebook's Chief Technology Officer Mike Schroepfer, "it was not a requirement that we read them." ¶¶24, 147, n. 73. According to Schroepfer (and confirmed by Parakilas), "[o]nce the data left Facebook servers there was not any control, and there was no insight into what was going on." ¶¶24-25, 121, 151.

The Board *again* received notice of the illegal data sharing and lack of controls in 2011, when a complaint was filed with Ireland's data protection authority, which regulates privacy on behalf of the entire EU. After continuous complaints about Facebook's privacy and data sharing practices with third parties (¶¶125-37), the FTC sued Facebook for unlawfully sharing user information with third parties without notice to users or their informed consent. ¶¶113, 138-40. The parties reached a settlement memorialized in the FTC's Final Order and Decision, served on August 15, 2012 ("FTC Order"), given to each Director Defendant. ¶¶114-16, 130-42. Facebook was barred from misrepresenting the extent to which

[redacted]

it shared user information with third parties and the extent to which it protected user information. ¶¶114-15. Facebook was also required to obtain users' "affirmative express consent" before "sharing private data" or "overriding privacy settings" *Id.*

Facebook retained PwC as its privacy auditor to certify compliance with the FTC Order for the initial assessment in 2013 and for every privacy audit thereafter. As FTC Associate Director James Kohm stated, the FTC Order required that "the auditor needs to be someone who is objective and independent. We don't want someone who is going to just rubber stamp their procedures." ¶326. Yet rubber-stamp Facebook's procedures is precisely what PwC did. PwC issued three certified reports, the most recent covering the period of February 12, 2015 through February 11, 2017 (the "2017 Report"). ¶327 and Ex. J thereto. The Board discussed the FTC Order (¶142), which required Facebook to create a "privacy program." ¶¶32, 115, 324. Facebook hired PwC under a lucrative contract to conduct superficial biannual reviews of a program limited to Management Assertions about Facebook's practices which were accepted, not verified, by PwC. ¶¶327, 331, 333, 335-337. In fact, PwC redacted Management's Assertions from its audit reports and has represented that it will not produce unredacted reports at

[redacted].

any phase of this case absent a court order compelling it to do so.[4] As PwC admits, it was required to follow American Institute of Certified Public Accountants (AICPA) auditing standards. ¶329. PwC was required to assess and certify whether Facebook's privacy controls were designed effectively, and "operating effectiveness" through a four-step process. ¶333. PwC knowingly failed to test the operating effectiveness of Facebook's controls by skipping the fourth and most important step; there was no independent verification. [redacted]. Meanwhile despite this program, Facebook continued sharing data with third parties and turning a blind eye towards third parties. *See, e.g.*, Section C (165-177).

Had PwC complied with its admitted obligations, the FTC (and thereafter, investors) would have been alerted to Facebook's data sharing practices much earlier. Despite PwC's presence, Facebook continued sharing data with third parties without controls over who was collecting data, what data was being collected, or how data was being used. ¶¶143, 147, 339-40. In 2011 and 2012, Parakilas warned top senior executives of the Company, including Zuckerberg, Sandberg, former CTO Bret Taylor, and others that Facebook's practice of third

[4] Am. Compl., Ex. J.

[redacted].

party data sharing was "***horrifying***" and violated obligations to protect users' privacy. ¶¶149, 150, 154-56. None of these senior executives responded to his warnings. Facebook continued not to vet developers or conduct audits (¶158), which Sandberg confirmed was a mistake. ¶338. Indeed, during Parakilas' 16-month tenure, not "a single physical audit" occurred, including of known offenders. ¶158. Parakilas left Facebook in 2012 out of frustration, but not before warning senior executives, including Zuckerberg and Sandberg, about Facebook's data sharing being illegal. They did not care, however.

In 2012, despite the Canadian Regulatory Settlement, the FTC Order, Parakilas' warnings, Facebook continued sharing data with third parties without monitoring these parties' data collection or use. ¶143(a)-(g). Facebook claimed its procedures gave users control over their data, but it had no procedures, system or controls over third party data sharing, including what data was being collected and for what reason. ¶¶98-100, 176, 245. Officer Defendants adopted the position that they were not responsible for the actions of third parties, even though they had invited them onto Facebook's platform, gave them open access to user data, failed to vet them or conduct background checks, and even when there were suspicions (or confirmations) of abuses. ¶¶145-164. The Company-wide policy was "***turn a blind eye***" because the "***less you know, the better.***" ¶164. According to Parakilas

[redacted]

(and others) this internal policy was common knowledge throughout Facebook. ¶163.

In 2015, Director Defendants received their third notice of Facebook's illicit data sharing practices with third parties, while PwC received its first notice. ¶¶181-183. With campaign advertising on the rise and rapidly growing, the *Guardian* published an article revealing that Ted Cruz's presidential campaign "was using psychological data based on research spanning tens of millions of Facebook users, harvested largely without their permission. . . ," ¶182, and identified Cambridge Analytica as the third party responsible. ¶183, n.92.

Zuckerberg testified that he learned about Cambridge Analytica's data breach through the 2015 *Guardian* article and, according to a Facebook representative, an investigation was launched. ¶188. [redacted]

[redacted]

PwC did not note Cambridge Analytica in its 2017 report which covers February 2015 through January 2017. Thus, PwC issued a clean opinion that included the time period when Facebook first improperly gave Cambridge Analytica access to the private user data of 87 million subscribers and whitelisted data sharing with another 60 companies. Yet the 2017 Report makes no mention of it. ¶337. [redacted] Meanwhile, the British Parliament uncovered evidence that Facebook employees were "aware of the data harvesting" and aided the improper data transfer to Cambridge Analytica in 2014. ¶171 n.95.

Cambridge Analytica was also aided by a senior employee of Palantir, a company co-founded by Thiel and backed by Thiel and Andreessen. ¶¶56,61,153,172, 189. Furthermore, mere weeks before the 2015 *Guardian* article was published, Facebook hired the co-founder of Global Science Research Ltd. ("GSR"), a Cambridge Analytica accomplice. ¶180. Facebook employees were stationed at the Trump campaign headquarters working alongside Cambridge

[redacted]

Analytica and deciding how best to spend $100 million on Facebook advertising. ¶202.

Then, in late 2016, one of Zuckerberg's earliest investors and mentors, Roger McNamee, noticed that Facebook's news feed was becoming increasingly negative. ¶197. McNamee warned Zuckerberg and Sandberg that the problem was "systemic" and that Facebook was being manipulated by "bad actors." *Id.* Zuckerberg and Sandberg dismissed McNamee's warning and directed him to a "longtime Facebook executive" who denied the problem and explained that Facebook "was not responsible for the actions of third parties." ¶198.

By early 2017, Facebook's Chief Security Officer Alex Stamos became a vocal internal critic of Facebook's policies and lack of action. ¶205. He co-authored a "White Paper" titled "Information Operations and Facebook," which set forth that Facebook's lax data security practices were pervasive and supported by management. ¶206. The "White Paper" confirmed that Facebook's public statements about its business practices, infrastructure, and systems were false and misleading, and misrepresented that Facebook had "no evidence of any Facebook accounts being compromised" in connection with the 2016 election, as of the date it was published on April 27, 2017. *Id*. The original report to Facebook executives, including Zuckerberg and Sandberg, also discussed the circumstances that led to

the Cambridge Analytica leak. ¶207. Instead of taking appropriate action and disclosing the truth about its data sharing practices and the data breach, the report was rewritten and presented as a hypothetical scenario, appearing in the whitewashed "White Paper" that Facebook published. *Id.* The relationship between Stamos, Zuckerberg, and Sandberg began deteriorating shortly thereafter. *Id.* Despite the news of Cambridge Analytica's massive data sharing and the sharp criticism of Stamos, PwC issued its 2017 Report certifying that Facebook's controls were effective.

[redacted]

By mid-2017, Facebook's legal department reached out and obtained non-disclosure agreements ("NDA") from Cambridge Analytica, its affiliates, and certain individuals. ¶¶13, 201. In exchange for silence and a promise that they destroyed the data, Facebook released them from any liability. Facebook never notified the FBI, DOJ, FTC, ICO or the 87 million users impacted. ¶191. Schroepfer testified that he did not know why that decision was made. *Id.*

[redacted]

[redacted]

On February 8, 2018, in the continued effort to conceal Facebook's data sharing practices with third parties, Facebook executive Simon Milner claimed

[redacted]

before the British Parliament that Cambridge Analytica neither had, nor was provided Facebook data. ¶¶214-15. The British Parliament later noted that Milner's testimony had been misleading, and repeatedly commanded Zuckerberg to appear before its committee, but Zuckerberg refuses to do so. ¶¶223-27.

D. THE TRUTH ABOUT FACEBOOK'S PRIVACY AND DATA SHARING PRACTICES COME TO LIGHT

On March 17, 2018, with the aid of whistleblower Wylie, the *Guardian* and the *New York Times* detailed how millions of Americans' private information was used by Cambridge Analytica to target them in the 2016 election without consent. ¶¶16, 219-23. Approximately 40% of American voters were impacted. ¶170. The media reports revealed the magnitude and severity of the Cambridge Analytica data breach, details known to Director Defendants since 2015 or soon thereafter, which Director Defendants intentionally concealed from users, regulators, and investors. ¶¶219-23.

In reaction to this news, Facebook lost $100 billion of its market value in a single day. ¶223. The U.S. Senate and House of Representatives commanded Zuckerberg to appear and testify about Facebook's data sharing practices. ¶240. Zuckerberg misled Congress by claiming that the data sharing practices that led to the Cambridge Analytica debacle had stopped in 2014. ¶¶240-243, 247.

[redacted]

Then, on June 8, 2018, in a written submission to Congress, Facebook recanted, admitting that it continued sharing user data with 113 "whitelist" companies and "integrated partners" following the 2014 change to Facebook's data sharing practices. ¶¶20, 248, n.16. Following this disclosure, a multiagency investigation was launched by the FTC, SEC, Department of Justice, and Federal Bureau of Investigation. ¶27. Cambridge Analytica quickly became the poster child of Facebook's continued unlawful third party data sharing practices. It will take substantial resources and many years to resolve the problems created by these unlawful practices.

PROCEDURAL BACKGROUND

Plaintiff Sbriglio commenced her derivative suit on behalf of Facebook on April 25, 2018 and, on August 7, 2018, was joined by institutional investor FRS in filing the Amended Complaint (D.I. # 32), adding PwC as a defendant. The Amended Complaint integrates information from dozens of public sources, including: transcripts of detailed accounts of whistleblowers who worked at Facebook and Cambridge Analytica; Facebook correspondence and interrogatory responses; hearing transcripts of testimony by Facebook and Cambridge Analytica executives and employees and documentary evidence amassed from government proceedings before the U.K. House of Commons, the U.S. Senate, and the U.S.

[redacted]

House of Representatives. *See* Amended Complaint, Ex. A-T. Plaintiffs also seek equitable relief in advance of the next annual shareholder meeting to be held in or around May 2019.

On September 28, 2018, Facebook Defendants Mark Zuckerberg, Sheryl Sandberg, Marc Andreessen, Erskine B. Bowles, Susan Desmond-Hellmann, Reed Hastings, Jan Koum, and Peter A. Thiel[6] moved to dismiss the Amended Complaint or in the alternative stay the proceedings ("MTD"). PricewaterhouseCoopers LLP ("PwC") (Dkt. #s 55 and 57) joined Facebook Defendant's brief and filed its own brief (collectively, "PwC MTD").

Plaintiffs respond to both briefs herewith. For the reasons below, the Court should deny PwC and Facebook Defendants' motion to dismiss and allow the matter to proceed to discovery immediately.

ARGUMENT

I. DEMAND ON THE BOARD IS FUTILE

[6] "Officer Defendants" refers to Mark Zuckerberg and Sheryl Sandberg. "Auditor Committee Facebook Defendants" refers to Marc Andreessen, Erskine B. Bowles and Susan Desmond-Hellmann. "Director Defendants" refers to Zuckerberg, Sandberg, Andreessen, Bowles, Desmond-Hellmann, Reed Hastings, Jan Koum, and Peter A. Thiel. The "Board" refers to the following directors seated on Facebook's Board on April 25, 2018: Zuckerberg, Sandberg, Andreessen, Bowles, Desmond-Hellmann, Hastings, Koum, Thiel, and non-party Kenneth I. Chenault.

[redacted]

The Amended Complaint provides substantial reason to doubt the majority of the Board would have been able to impartially assess a pre-suit demand predicated on the claims and allegations of misconduct and asserted herein.

A. THE STANDARD FOR ASSESSING DEMAND FUTILITY

Prior to filing suit, Delaware law requires a shareholder in a derivative action first to make a demand on the corporation's board to allow the board an opportunity to examine the facts in light of the alleged grievance and determine whether pursuing the action is in the best interest of the corporation. *Ryan v. Gifford*, 918 A.2d 341, 352 (Del. Ch. 2007). This requirement, however, is excused if demand would have been futile. *Id.* (explaining, "a question is rightfully raised over whether the board will pursue these claims with 100% allegiance to the corporation, since doing so may require that the board sue itself on behalf of the corporation.") (quoting *Sanders v. Wang*, 1999 WL 1044880, at *11 (Del. Ch. Nov. 10, 1999)).

In assessing whether to excuse the demand requirement, this Court "balance[s] the interests" between "strike suits" "[with the interest of encouraging] suits reflecting a reasonable apprehension of actionable director malfeasance that the sitting board cannot be expected to objectively pursue on the corporation's behalf." *Ryan*, 918 A2d at 352. (quoting *Aronson v. Lewis*, 473 A.2d 805, 812

(Del. 1984)). In balancing these interests, the Court emphasizes facts pertaining to the board's impartiality. *Aronson*, 473 A.2d at 809. The Amended Complaint emphasizes a series of material missteps and blunders of corporate action and inaction. Consequently, the applicable test is *Rales v. Blasband*, 634 A.2d 927 (Del. 1993).

The *Rales* test assesses whether "the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand." *Id.* at 934. Director independence turns on "whether a director is, for any substantial reason, incapable of making a decision with only the best interests of the corporation in mind. That is, the independence test ultimately focuses on impartiality and objectivity." *In re Oracle Corp. Deriv. Litig.*, 824 A.2d 917, 920 (Del. Ch. 2003) (internal quotations omitted).

A director is "interested" and face a substantial likelihood of liability where: (a) a director consciously failed to act after finding evidence of illegality (*i.e.*, "red flags"); or (b) there was a "sustained or systematic failure of the board to exercise oversight" over a particular corporate function. *David B. Shaev Profit Sharing*

Account v. Armstrong, 2006 WL 391931, at *5 (Del. Ch. Feb. 13, 2006); *In re Caremark Inter. Deriv. Litig.*, 698 A.2d 959, 972 (Del. Ch. 1996).

In analyzing demand futility, Delaware courts apply a "contextual" analysis that consider allegations "in their totality," thereby "draw[ing] all reasonable inferences from the totality of those facts in favor of the plaintiffs." *Del. Cty. Employees Ret. Fund v. Sanchez*, 124 A.3d 1017, 1019-21 (Del. 2015); *see also Marchand v. Barnhill*, 2018 WL 4657159, at *14 (Del. Ch. Sept. 27, 2018) (Slights, V.C.). For the reasons below, eight members on the relevant nine-member Board were incapable of impartially assessing pre-suit demand.

B. THE MAJORITY OF THE BOARD LACKS INDEPENDENCE

1. Zuckerberg's Interests Are Directly Implicated

Facebook Defendants contend that Zuckerberg is not "interested" even though Zuckerberg publicly testified before the U.S. Congress that "I started Facebook, I run it, and, at the end of the day, I am responsible for what happens [at Facebook]." Am. Compl., Ex. F at 1, Ex. H at 6. And that makes sense. Zuckerberg is the controlling shareholder, the CEO, and the Chairman of the Board. In that capacity, as alleged throughout the Amended Complaint, Defendant Zuckerberg directed, concealed, and then profited (to the tune of billions of dollars) through

[redacted]

these improper means.[7] Zuckerberg should be held to answer for these breaches of his fiduciary duty to "his" company.

The two cases cited by Facebook Defendants are inapposite. *In re Dow Chemical Co. Deriv. Litig*., involved an arms-length merger in which none of the directors held an interest beyond that of regular shareholders. 2010 WL 66769, at *8 (Del. Ch. Jan. 11, 2010). Similarly, *Brehm v. Eisner* involved a challenge to the *former* CEO's severance package, and therefore, the court held the *current* CEO's control of the board's majority was not relevant. 746 A.2d 244, 266 (Del. 2000). Unlike *Dow* and *Brehm*, the Amended Complaint alleges a direct link between the dominant director and the challenged misconduct— failing to protect private user data, which is the crown jewel asset of the Company.

Indeed, Zuckerberg is widely reported as having instilled a culture at Facebook that emphasized growth and profits above all else. Moreover, the Amended Complaint specifies that Zuckerberg not only knew about the pervasiveness of the misappropriation of user data, but sought to conceal it and misled users, investors, and the U.S. government. *See, e.g.*, ¶¶9-13, 19-20, 26, 35,

[7] *See Am. Int'l Group, Inc. v. Greenberg,* 965 A.2d 763, 798-99 (Del. Ch. 2009) (finding founder CEO dominated and controlled company with an iron fist, knew it had internal control weaknesses, and allowed employees to exploit those so that the company appeared more profitable in violation of *Caremark* and other fiduciary duties) [hereinafter, "*AIG*"].

[redacted]

40, 44, 75, 81, 93, 142, 188, 191, 198, 207, 212, 215, 231-36, 249, 255, 257, 264, 271, 296, 383-85. Unlike in *Dow* and *Brehm*, there is a substantial link between the misconduct alleged and the director's interests. The Court must therefore analyze whether the Board's allegiance to Zuckerberg is so powerful that it renders them incapable of assessing pre-suit demand in this case.

2. Zuckerberg Dominates The Board

Here, the Amended Complaint demonstrates Zuckerberg "dominates" Sandberg, Andreessen, Bowles, Desmond-Hellmann, Hastings, Koum, and Thiel, or seven of the remaining eight members by the sheer fact of his shareholdings and voting interest. In addition, the Board's history of dealing with Zuckerberg demonstrates Zuckerberg's dominion.

The Company is dominated and controlled by its 34-year-old creator, founder, CEO, Chairman and majority shareholder, Defendant Zuckerberg. Indeed, in 2017, he controlled 53% of the shareholder vote though he owned 16% of Facebook's stock. ¶357. Facebook is thus "controlled" under NASDAQ rules, and is not required by the exchange to have an independent board. *Id.* (citing Ex. T).

Few public company boards in modern Delaware jurisprudence have the level of dominion and control that Zuckerberg has over this Board. The most comparable example is AIG's Hank Greenberg and Oracle's Tom Ellison. In *AIG*,

the board was forced to form a special litigation committee when Greenberg and his fellow directors were sued for breaching their fiduciary duties because only two of its twenty-one-person board were even arguably independent. *AIG*, 965 A.2d at 798-99. Similarly, in *Oracle*, the Court found "reasonable doubt" that two of the three-member special committee were independent given their ties to Ellison because some professional and personal friendships "border on or even exceed familial loyalty and closeness." *In re Oracle Corp. Deriv. Litig*, 2018 WL 1381331, at *15 (citation omitted) (Del. Ch. Mar. 19, 2018). Indeed, the *Oracle* court emphasized that in every annual stockholder meeting from 2012 to 2016 the majority of Oracle's stockholders rejected the company's executive pay practices, and more recently, had withheld votes for Compensation Committee members to express disapproval of the board's handling of excessive executive pay. *Id.* at *4. The Court further noted that these directors were not forced to resign because of Ellison's continuing support. *Id.* at *16.

But unlike here, neither Greenberg nor Ellison owned a majority interest in their respective companies. Here, Zuckerberg can unseat any director any time he chooses. *Cf. TVI Corp. v. Gallagher*, 2013 WL 5809271, at *10 (Del. Ch. Oct. 28, 2013) (explaining that because "the Founders would remove any directors who opposed them, Plaintiffs have raised a reasonable doubt that the non-Founder

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Board members . . . were beholden to the Founders as of the filing of the Original Complaint."); *see also In re Morton's Rest. Gp., Inc. S'holders Litig*., 74 A.3d 656, 665-66 (Del. Ch. 2013) (explaining that controller "not only held 35% of the company's stock, but he was the company's visionary founder, CEO and chairman" and had "influence over even 'the ordinary managerial operations of the company'"); *In re Cysive, Inc. S'holders Litig.,* 836 A.2d 531, 552 (Del. Ch. 2003) (finding domination and control at technology company where insider served hands-on roles of Chairman and CEO and, by admission, was involved in all aspects of business, was the company's creator, and inspirational force).

Furthermore, there is significant evidence and history showing Facebook's Board cannot be impartial when it comes to Zuckerberg. Delaware courts assess director independence based on "whether the plaintiffs have pled facts from which the director's ability to act impartially on a matter important to the interested party can be doubted because that director may feel either subject to the interested party's dominion or beholden to that interested party." *Sandys v. Pincus*, 152 A.3d 124, 128 (Del. 2016). Moreover, the "confluence of voting control with directorial and official decision-making authority" is "consistent with control of the board," and is a basis for establishing demand futility when "coupled with [allegations] that 'directors are beholden to the controlling person.'" *Friedman v. Beningson*,

1995 WL 716762, at *5 (Del. Ch. 1995) (Allen, C.) (quoting *Aronson*, 473 A.2d at 815).

Delaware courts find past conduct instructive in evaluating whether directors are able to act independently. *See Marchand*, 2018 WL 4657159, at *15.[8] In *Marchand*, plaintiffs alleged that the company's founder and CEO violated his fiduciary duties by failing to oversee and properly manage the company's facilities, which was closed due to listeria outbreak following health code violations. *Id.* at *4-7. The Court held that one of the directors was independent, despite his cozy relationship with the founder because the director stood up and voted against the founder's interests during a vote to rescind a prior resolution separating the CEO and Chairman positions. *Id.*

Here, the exact opposite is true; there is a long history that demonstrates Facebook's Board cannot be impartial when it comes to Zuckerberg. For example, and unlike in *Marchand*, Zuckerberg led the Board to reject Facebook shareholders common-sense proposals to improve corporate governance, including the proposal to separate the CEO and Chairman position. ¶¶278-86. The proposal had overwhelming support from non-interested and non-director shareholders, and

[8] Facebook Defendants do not cite *Marchand* in their papers because in that case this Court assessed board independence in a case asserting *Caremark*-like violations against the founder CEO– the assessment Facebook Defendants wish to avoid here.

[redacted]

upon being voted down, influential pensions systems protested. ¶¶287-90. The comptroller of the New York City pension fund described "[t]he idea that there should be an autocrat in charge of a gigantic public company, which has billions of dollars of shareholder money invested in it, is an anachronism."

The Board's submissiveness to Zuckerberg was further demonstrated in June 2015 when Zuckerberg approached the Board about his plan to sell most of his Facebook stock while maintaining ***lifetime voting control*** over Facebook through the issuance of new no-vote shares to minority shareholders. ¶¶361-64.[9] The Board formed a special committee to assess this plan. Through discovery in non-vote shareholder action, it was revealed that the committee (comprised of Bowles, Andreessen, and Desmond-Hellmann) failed to negotiate or demand money or some differential distribution for minority shareholders. Weaver Aff. at 1, Plaintiffs' No-Vote Pre-Trial Brief at 23-24, 30. According to Desmond-Hellmann, "the Committee believed that it had no real ability to say 'no' to Zuckerberg['s] [demand for lifetime control]." *Id.* at 13-14, 16. It was also revealed that

[9] *See* Transmittal Affidavit of Thaddeus J. Weaver, at Ex. 1, filed simultaneously herewith ("Weaver Aff."), Plaintiffs' Pre-Trial Brief, *public version filed* Sept. 22, 2017 at 9-10, *In re Facebook, Inc. Class C Reclassification Litig.*, No. 1286-BCL (Del. Ch.) [D.I. # 237] [hereinafter "Plaintiffs' No-Vote Pre-Trial Brief"]. The Court may take judicial notice of information set forth in public litigation dockets. *See* Del. R. Evid. 202(d)(1)(C); *Indem. Ins. Corp. v. Cohen*, 2018 WL 3253997, at *2 n. 7 (Del. Ch. Jul. 3, 2018) (judicially noticing motion to dismiss counterclaim filed by plaintiff in federal district court).

Zuckerberg, through his mole Andreessen, kept a watchful eye on the committee during the process by Andreessen staying in constant communication with Zuckerberg, leaking private details, '"coach[ing],'" and "repeatedly reassure[ing] Zuckerberg. . . that the Committee would ultimately agree to the reclassification." *Id.* at 31. The Board approved the reclassification in April 2016 and recommended it to shareholders, 76.7% of whom cast their ballot against the proposal. *Id.* at 36. The Board only canceled the reclassification plan on the eve of trial, and only because it faced public disclosure of damaging discovery and deposition testimony. This ordeal is a shining example that Andreessen, Bowles, and Desmond-Hellman are willing to abdicate their duties to Facebook and its shareholders to demonstrate loyalty and protect Zuckerberg.

The no-vote shareholder litigation is not the only time the Board has demonstrated its unwavering loyalty to Zuckerberg. Indeed, Zuckerberg has famously made major corporate decisions unilaterally and without his Board's input, including when he negotiated the $1 billion purchase of Instagram over dinner with Instagram's founder. ¶360. This history of unwillingness to object, vote against, or challenge Zuckerberg, emphasizes Zuckerberg's dominance.

[redacted]

3. Sandberg (An Insider) Has A Disabling Conflict

Sandberg is Zuckerberg's lieutenant, Chief Operating Officer, and a close friend. The two have worked together closely since 2008, and Sandberg joined the Board in June 2012. Sandberg knows that she serves in these roles at Zuckerberg's whim and that he can terminate her at any time. ¶¶357-359. Sandberg owes her wealth and career to Zuckerberg. ¶301; Am. Compl., Ex. N (2018 Proxy Statement) at 55.

Given Sandberg's subordinate status to and close working relationship with Zuckerberg, Sandberg cannot be considered independent of him. Indeed, for these reasons, "[u]nder the great weight of Delaware precedent, senior corporate officers generally lack independence for purposes of evaluating matters that implicate the interests of a controller." *In re Ezcorp Inc. Consulting Agreement Deriv. Litig.*, 2016 WL 301245, at *35 (Del. Ch. Jan. 25, 2016). Sandberg, like Zuckerberg, is also responsible for exposing users to misappropriation through unauthorized data sharing. ¶¶35, 338. Sandberg was aware of the misconduct alleged but refused to change course because closing access to their data would have directly interfered with her plans for hyper-growth. ¶¶10, 35, 44, 75, 121, 142, 191, 198, 207, 212, 236, 300, 338, 383-84.

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4. Outside Directors Have Disabling Conflicts

a. Andreessen

Andreessen is likewise self-interested given his ties to Palantir Technologies Inc. ("Palantir"), the private data-technology company which has been linked to and implicated in the Cambridge Analytica scandal. ¶56. Senior Palantir employees "aided in the construction of Cambridge Analytica's psychological profile models using illegally obtained Facebook Data." *Id.*

Andreessen is also interested due to his ties to Zuckerberg. He has a personal bias in favor of founder-controlled companies. He is the co-founder and principal of Andreessen Horowitz, a venture capital firm that provides seed, venture, and growth stage funding to the "best new technology companies." ¶367. Andreessen's philosophy is to "enable founders to run their own companies" without interference from financial backers. *Id*. Andreessen was asked to join Facebook's Board on or around June 2008 and has served Zuckerberg dutifully since. ¶55. He has also served on Facebook's Audit Committee since June 2008. *Id.*

Andreessen has admitted that Zuckerberg is one of his best friends. He uses his relationship with Zuckerberg, and the Facebook story and prestige, to access other lucrative technology deals. After linking up with Zuckerberg, Andreessen received opportunities that he would not have otherwise had, which made his firm "the talk of the town." ¶370. Andreessen and his firm were involved in and

substantially enriched by two portfolio companies, Instagram and Oculus VR, in particular and both were ultimately purchased by Facebook. ¶369. Andreessen would not have had been able to invest in or sit on Oculus VR's board if Zuckerberg had not convinced Oculus's CEO to permit it. *Id.* Andreessen turned his firm's several hundred-thousand-dollar investments in Instagram and Oculus into multi-million dollar investments when Zuckerberg acquired each entity. ¶368.

b. Thiel

Thiel has been a member of the Board since April 2005 and serves on Facebook's Compensation & Governance Committee. ¶61. He has been a partner of the venture capital firm Founders Fund since 2005 and was among Zuckerberg's earliest financial backers, netting him hundreds of millions of dollars in profits. *Id*.

Thiel co-founded Palantir which has been implicated in the Cambridge Analytica scandal. ¶56. Thiel has financially benefited from his relationship with Zuckerberg by hundreds of millions of dollars and is one of the select few in Zuckerberg's inner circle given the ability to purchase the coveted Class B shares. ¶372. The Founders Fund gets "good deal flow" from this high-profile association. *Id*. Moreover, Thiel's belief is that founders should continue to run their businesses through voting control mechanisms even when they controls work in a founders

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self-interest to a company's and shareholders' detriment. *See, supra*, Section I.A.3; ¶371.

c. Bowles

Bowles has been a member of the Board since September 2011. ¶57. As set forth above, Bowels has shown through his service on the special committee that he lacks independence from Zuckerberg when he voted to approve Zuckerberg's lifetime control over Facebook without owning a single share of Facebook common stock. ¶¶361, 363. He has also served as the Chair of the Audit Committee since 2011 [redacted]. Bowles is also a politician and professional outside director serving on the boards of many public companies. ¶57. He has a history of favoring CEOs' financial interests and has collected tens of millions of dollars in personal wealth for his services on Facebook and other high-profile boards. ¶374. While companies on whose boards were underperforming, he consistently voted to approve lavish payouts to CEOs. *Id*.

d. Desmond-Hellmann

Desmond-Hellmann has been a member of the Board since March 2013 and is purportedly the "Lead Independent Director" of the Board. ¶58. She has a close [redacted]

business and personal relationship with Zuckerberg, acting as liaison between Zuckerberg and the Board's Outside Directors. ¶377. Desmond-Hellmann previously displayed her allegiance to Zuckerberg when she sat on the recapitalization committee and agreed to give Zuckerberg lifetime control of Facebook without any corresponding benefits for shareholders. ¶¶361, 363. According to Desmond-Hellman, saying "no" to Zuckerberg is not an option.[10] *See In re Oracle Corp. Deriv. Litig.*, 2003 WL 21396449 (Del. Ch. June 17, 2003) (finding committee member abdicated corporate duties, had a close friendship, did each other favors, served as a longtime director of Oracle and another company owned by Ellison amount to a disabling personal relationship).

Desmond-Hellman also sat on the Audit Committee [redacted] Her *only* action was one of self-preservation, when she stepped down from the Audit Committee in May 2018. ¶58.

Finally, Desmond-Hellmann is the Chief Executive Officer of the Bill and Melinda Gates Foundation (the "Gates Foundation"), which has a history of partnering with Facebook and collaborating on various philanthropic initiatives

[10] *See*, *supra*, n. 13.

[redacted]

with the Chan Zuckerberg Initiative, a foundation founded and controlled by Zuckerberg and his wife. Am. Compl., Ex. N (2018 Proxy Statement) at 13. Desmond-Hellmann's professional success relies in part on these continued collaborations with Zuckerberg. *Id.*; *Sanchez*, 124 A.3d at 1022-23 (finding director lacked independence because founder had sufficient control of the company that employed the director).

e. Koum

Koum was a member of the Board from October 2014 through April 2018. ¶60. Koum was the co-founder and CEO of WhatsApp Inc. ("WhatsApp") a cross-platform mobile messaging application company and Facebook's wholly-owned subsidiary. *Id*. Facebook acquired WhatsApp in 2014 for billions of dollars. *Id.* According to Facebook's website, Koum was "responsible for the design and interface of WhatsApp's service and the development of its core technology and infrastructure." *Id.* Koum, like the other Board members, voted in favor of Zuckerberg's lifetime entrenchment when he voted in favor of the recapitalization. When Zuckerberg purchased WhatsApp with shares of Facebook, he made Koum billionaire ten times over. *Id*. Koum netted almost $8 billion in illegal profit from the sale of his Facebook shares based on confidential information. ¶¶60, 303, Ex. Q.

[redacted]

f. Hastings

Hastings has been a member of the Board since June 2011 and is the Chair of Facebook's Compensation & Governance Committee. ¶59. For his services to Facebook, which are at the behest of Zuckerberg, he owns Facebook stock valued at over $20,000,000.[11] As co-founder, CEO and Chairman of Netflix, he understands Zuckerberg's need for control personally. ¶375. In addition to such sympathies, Hastings relies on and benefits from Facebook's business relationship with Netflix. ¶¶375-376. As a result of Facebook-Netflix's "Friends and Community" initiative launched in March 2013, Netflix obtained invaluable metrics and insights into its customers using the platform and technology that only Facebook possesses. ¶*Id.* This initiative was so powerful that the Netflix's stock price increased by 6% as a result. *Id*. Facebook Defendants argue that this one business interest was insufficient to deem Hasting's conflicted in the action *In re Facebook, Inc. IPO Securities and Deriv. Litig.,* 922 F. Supp. 2d 445 (S.D.N.Y. 2013) ("*Facebook IPO*"). While this allegation on its own may be insufficient, the totality of the demand futility allegations asserted against Hastings in the Amended Complaint, including many allegations that are not present in the *Facebook IPO* pleading, point to the exact opposite conclusion here.

[11] Am. Compl., Ex. N (2018 Proxy Statement) at 55.

[redacted]

Moreover, the Board members' relationships with Zuckerberg earned them millions of dollars of Facebook stock.[12] Sandberg owns Facebook Class A and B shares worth well over half a billion dollars, Andreessen and Thiel own hundreds of millions of dollars in Facebook stock and were part of the inner-circle entrusted to own 10-to-1 vote Class B shares.[13] Koum received Facebook Class A shares in the sale of WhatsApp which made him billions of dollars. ¶60. Bowles, Desmond-Hellmann, and Hastings received lucrative salaries and stock awards worth over $30 million dollars.[14] *Cf. In re Ebay, Inc. S'holders Litig*., 2004 WL 253521 (Del. Ch. Feb. 11, 2004) (holding board was dominated by group of insiders who controlled 50% of the company and determined who would remain on the board, putting outside directors stock compensation that was worth potentially millions of dollars, at risk). Bowles and Desmond-Hellmann's wealth has substantially derived from their relationship with Zuckerberg. ¶¶57, 58, 374; Am. Compl., Ex. N (2018 Proxy Statement) at 55. With the exception of Chenault, every other member of the Board has disabling personal conflicts of interest that render them incapable of making an impartial decision with respect to this litigation. ¶356. Thus, demand would be futile.

[12] *Id.*

[13] *Id.*

[14] *Id.*

C. THE MAJORITY OF THE BOARD FACES A SUBSTANTIAL LIKELIHOOD OF LIABILITY

Defendants face substantial likelihood of liability from varied breaches of their fiduciary duties, disclosure violations that resulted in securities fraud, and/or insider trading.

Facebook Defendants' motion to dismiss reflects a fundamental disconnect with the Amended Complaint. The well-pled allegations rest on conscious and deliberate acts of misconduct by the Officer Defendants, the Audit Committee and the Board which go well beyond mere inattentiveness. *In re Walt Disney Co. Deriv. Litig*., 906 A.2d 27, 66 (Del. 2006) (noting that "[c]ases have arisen where corporate directors have no conflicting self-interest in a decision, yet engage in misconduct that is more culpable than simple inattention or failure to be informed of all facts material to the decision").

In *Walt Disney*, the Delaware Supreme Court specifically pointed to two scenarios of bad faith, both of which are relevant here: "[1] the fiduciary acts with the intent to violate applicable positive law, or [2] the fiduciary intentionally fails to act in the face of a known duty to act." *Id.* at 67. Under either scenario, the fiduciary demonstrates "a conscious disregard" of his or her duties. *Id.*

In addition, the Court in *In re Caremark Int'l Inc. Deriv. Litig*., 698 A.2d 959, 971–72 (Del. Ch. 1996), recognized a third theory of liability stemming from

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the failure to comply with oversight duties. Such liability arises when: "[1] the directors utterly failed to implement any reporting or information system or controls; or [2] having implemented such a system, or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention." *Stone ex rel. AmSouth Bancorporation v. Ritter*, 911 A.2d 362, 369 (Del. 2006) (adopting the *Caremark* standard of oversight liability) ("*AmSouth*"). Here, all three theories of liability are implicated in the Amended Complaint and serve as the basis for finding that the majority of the Board faces substantial likelihood of liability and, therefore, is not sufficiently disinterested under *Rales* to assess pre-suit demand.

1. Officer Defendants Breached Their Fiduciary Duties By Engaging In Acts Intended To Violate Positive Law

"Delaware law does not charter law breakers." *In re Massey Energy Co.*, No. 5430, 2011 WL 2176479, at *20 (Del. Ch. 2011). Thus, officers do not have the discretion to act beyond their lawful powers. As one treatise has explained:

> The business judgment rule does not protect decisions by directors that Constitute . . . illegality, or ultra vires conduct. Therefore . . . a decision by directors that a violation of law or fraudulent or ultra vires conduct would serve the best interests of the corporation is not protected by the business judgment rule.

[redacted]

D. Block, N. Barton & S. Radin, *The Business Judgment Rule: Fiduciary Duties of Corporate Directors*, 41-42 (4th ed. 1995); *see also* S. Arsht, *The Business Judgment Rule Revisited*, 8 HOFSTRA L. REV. 93, 129 (1979) ("Bad faith may preclude application of the business judgment defense where directors knowingly violate a statute or comparable expression of public policy, even if such a violation is undertaken in the corporation's best interests.").

The Amended Complaint alleges that Facebook was bound by the Terms of Use and U.S. privacy and consumer laws and regulations, EU's General Data Protection Regulation ("GDPR"), various Privacy Shield Frameworks, the Canadian Regulatory Settlement, and the FTC Order to give users ***notice*** of Facebook's data sharing, obtain users' ***informed consent*** for how their data is used, and protect users' data, including personal identifiable information (PII). ¶¶109-11.

The Amended Complaint further alleges that Officer Defendants caused Facebook to violate all three of these overarching legal obligations when they opened Facebook's platform to whitelist companies, ¶259, entered into data-sharing partnerships with device makers, ¶102, and failed to police application developers thereby allowing over 200 applications to misappropriate user data, ¶20. Facebook's practices were simply not designed to comply with its legal

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obligations relating to privacy. Facebook's open platform and data sharing practices represented a dramatic departure from the Company's business practice of developing applications in-house. *Frederick Hsu Living Trust v. ODN Holding Corp.*, 2017 WL 1437308, at *31 (Del. Ch. April 25, 2017) (noting company's stark departure from historic business practice evinces bad faith). By 2010, Facebook had attracted over one million third party app developers and gave device makers open access to user data, ¶83, and as a result was able to grow its user base from 50 million to 2.2 billion users from 2008 to 2018. When Facebook's user base grew, so too did its profits enabling Zuckerberg to grow his personal net worth to over $53 billion.

Giving millions of third parties unfettered access to user data was not the only corner cut by Officer Defendants. The Amended Complaint details how Facebook was not vetting or monitoring these third parties while on its platform. Parakilas called these practices horrifying and gave a detailed presentation to top senior executives, including Officer Defendants, of his concerns in allowing third parties to collect any data they wanted without background checks or oversight into their collections or use. He identified known bad actors and steps to addressing oversight, but his entire plan was rejected by Officer Defendants. ¶¶154-162. *In re Tower Air, Inc*., 416 F.3d 229, 239 (3d Cir. 2005) ("The officers'

[redacted]

alleged passivity in the face of negative maintenance reports seems so far beyond the bounds of reasonable business judgment that its only explanation is bad faith."). Officer Defendants instead adopted a policy of the "***the less you know, the better***" or willful blindness, ¶385.

Officer Defendants also received warnings of third party abuses from organizations such as CIPPIC in 2010, ¶128, the FTC in 2011, ¶¶138-142, the media, ¶¶181-187, 190, Parakilas in 2011-2012, ¶¶144-164, McNamee in 2016, ¶¶192-198, Stamos in 2016 and 2017, ¶¶205-212, and numerous other complaints about misuse of user data. *See* Am. Compl. at 53-95. However, Officer Defendants took the narrow view, as they do now in the MTD at 25, that they owed no duty to oversee third parties. But Officer Defendants cannot fully ignore Facebook's role in the misconduct of third parties (opening the platform to third parties, not vetting the third parties, allowing third parties to collect any data without monitoring, not reviewing third party terms and conditions, or in any way monitoring the use of Facebook's data or enforcing Facebook's written policies for third parties).

Moreover, in 2015, Officer Defendants learned about Cambridge Analytica, which served as yet another warning of how Facebook's practices were not complying with its legal obligations. Instead of addressing the problem, Facebook employees took steps to concealing the Cambridge Analytica debacle. For

example, a Facebook in-house lawyer was ordered to obtain non-disclosure agreements from the Cambridge Analytica parties, ¶¶201; a Facebook employee threatened a reporter and newspaper to bury the story, ¶¶220; a top Facebook executive lied to the British Parliament, 214-215, 219-223; and Zuckerberg himself misled the U.S. Congress about the extent of Facebook's data sharing practice. ¶¶240-244, 247. Specifically, when Congress questioned Zuckerberg about data sharing with third party app developers, he claimed that the practice stopped in 2014 though it had continued well beyond that time. ¶¶241, 247, 256. When Congress questioned Zuckerberg about sharing data with device makers, Zuckerberg feigned ignorance. ¶255. Facebook finally admitted to Facebook's data sharing practices with third parties in June 2018 without notice to or consent from its users. ¶¶248-254.

Officer Defendants exposed Facebook to legal liability for fines, ¶¶27, 35, 116, 143, 144, 345, 361; legal actions, ¶¶27, 116, 345, 350; ruining its relationship with users, ¶¶263-264; ruining its relationships with regulators and governments, ¶¶27, 35, 45; damaging its reputation, ¶¶45, 341, 347, 348, 400; causing a $120 billion market loss, ¶¶348; and the loss of senior executives. ¶¶27, 341-52. Koum resigned from the Board effective April 30, 2018, ¶¶60; Facebook's General Counsel recently resigned; and the co-founders running Instagram recently

resigned citing differences in philosophies on data sharing and privacy as the reason.[15] Officer Defendants have steadfastly refused to change their culture or their ideology that privacy is passé.[16] *See, e.g.*, 117-121, 123, 192-198. Their mismanagement of Facebook's most precious asset, user data, is beyond gross negligence and, rather, reflects bad faith and the conscious disregard of law. ¶¶263-264.

Facebook Defendants argue that Officer Defendants did not breach their fiduciary duties because they do not owe *Caremark* obligations. MTD at n.10. But here the Officer Defendants did not fail to prevent an illegal act, they caused the illegal act. Whether or not officers owe *Caremark* obligations is semantic at best. The Amended Complaint alleges that they failed to manage Facebook with loyalty and care, making informed judgments to consciously allow and not intervene in

[15] *See* Weaver Aff. at 2, Kurt Wagner, "Instagram's Co-Founders, Kevin Systrom and Mike Krieger, Are Leaving Amid Frustrations With Parent Company Facebook," *Recode*, available at https://www.recode.net/2018/9/24/17899342/instagram-cofounders-depart-kevin-systrom-mike-krieger. The Court may take judicial notice of the resignations because there were numerous media reports after Mr. Systrom and Mr. Krieger departed from Facebook and the fact of their departures is not reasonably subject to dispute. D.R.E. 201(b)(2).

[16] On the contrary, just last year, the United States Supreme Court ruled that the government could not obtain cell phone location data without a warrant, enforcing the view that even in a digital world, U.S. citizens are still entitled to control over their digitally stored personal data. *Carpenter v. United States*, 138 S.Ct. 2206 (2018).

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ongoing violations of the law. This is not protected under the business judgment rule. Both law and logic support this rule. *See Desimone v. Barrows*, 924 A.2d 908, 934-35 (Del. Ch. 2007) ("Delaware corporate law has long been clear on this rather obvious notion; namely, that it is utterly inconsistent with one's duty of fidelity to the corporation to consciously cause the corporation to act unlawfully" and "the knowing use of illegal means to pursue profit for the corporation is director misconduct."); *Metro Commc'n Corp. BVI v. Advanced Mobilecomm Techs., Inc*., 854 A.2d 121, 131 (Del. Ch. 2004) ("Under Delaware law, a fiduciary may not choose to manage an entity in an illegal fashion, even if the fiduciary believes that the illegal activity will result in profits for the entity."); *Kahn v. Roberts*, 679 A.2d 460, 465 (Del. 1996) ("The business judgment rule normally protects all lawful actions of the board, provided they were taken in good faith.").

In any case, the Delaware Supreme Court in *Gantler v. Stephens* expressly held that corporate officers owe fiduciary duties that are *identical* to those owed by corporate directors, and thus officers, like directors, do owe oversight duties. 965 A.2d 695, 708-09 & n.37 (Del. 2009).

Finally, Facebook Defendants contend that the Amended Complaint does not allege duty of care violations against the Officer Defendants or which conduct Zuckerberg took in his capacity as an officer versus a director. MTD at 20 & n.11.

[redacted]

On the contrary, in mostly every instance Zuckerberg is referenced in the Amended Complaint it is in his capacity as the most senior executive of Facebook. *Chen v. Howard-Anderson*, 87 A.3d 648, 686 (Del. Ch. 2014) ("Because the plaintiffs have assembled evidence sufficient to support claims against [the CEO] and [the CFO] in their capacity as officers, the Exculpatory Provision does not protect them."). The Amended Complaint also alleges in several places that as an officer he violated his duty of care. ¶¶30, 62, 394-95, 408. Since Delaware law does not exculpate corporate officers for violating their duty of care, which Facebook Defendants admit, MTD at 20, n.11, Officer Defendants face an even higher likelihood of liability for their misconduct than that of the other Director Defendants. *Gantler*, 965 A.2d at 709 n.37 (noting there is no statutory provision authorizing exculpation of corporate officers).

2. Director Defendants Violated Their Duty of Oversight When They Utterly Failed To Monitor Facebook's Sharing of Data With Third Parties

As set forth above, Facebook was bound by the Terms of Use and U.S. privacy and consumer laws and regulations, EU's General Data Protection Regulation ("GDPR"), and various Privacy Shield Frameworks, ¶¶109-10, to give users ***notice*** of Facebook's data sharing, obtain users' ***informed consent*** for how their data is used, and protect users' data, including personal identifiable

information (PII). ¶¶110-11. The Amended Complaint alleges that Director Defendants knew from various sources and indicators that Facebook was sharing data with third parties in violation of these laws.

Director Defendants failed to exercise "business judgment" when they consciously allowed companywide illegal conduct by utterly failing to implement a system by which to monitor third parties access to, collection and use of data. *AmSouth*, 911 A.2d at 370 (director oversight liability arises if "the directors utterly failed to implement any reporting or information system or controls").

[redacted] But these two together do not amount to a system or controls over third parties' access to, collection and use of data. The allegations relating to Parakilas' testimony provide a sufficient basis for this Court to reasonably infer that Director Defendants utterly failed to adopt a reporting and compliance system over Facebook's data sharing with third parties. Indeed, Facebook Defendants implicitly concede they had no system in place for monitoring third parties as they have asserted in the past and continue to assert that

[redacted]

they owed no duty to oversee third parties. MTD at 24-25. On its face, Facebook's data sharing practice of giving third parties unfettered access to users' data does not comply with Facebook's legal obligations to provide users notice and obtain users' consent. ¶¶97-101, 145, 150, 151, 152, 153.

Facebook Defendants rely on *In re Gen. Motors Co. Derivative Litig*., No. CV 9627-VCG, 2015 WL 3958724, at *14 (Del. Ch. June 26, 2015), *aff'd sub nom. In re Gen. Motors Co. Derivative Litig*., 133 A.3d 971 (Del. 2016), but there the plaintiff claimed that the company "lacked procedures to comply with its NHTSA reporting requirements" while simultaneously conceding that the company adopted and maintained a database to report quarterly to NHTSA.

Director Defendants, therefore, face a substantial likelihood of liability under the first prong of *Caremark.*

3. Director Defendants Failed to Act When They Learned About Cambridge Analytica in 2015

Delaware law is clear that directors may not "consciously disregard" their duty to act when the corporation is suffering harm from the illegal or imprudent activity of its employees. *AmSouth*, 911 A.2d at 369 (*quoting In re Walt Disney Co. Deriv. Litig*., 906 A.2d at 67).

When a board is on notice of illegal conduct, it has a duty to act. *Massey*, 2011 WL 2176479, at *21 ("For fiduciaries of Delaware corporations, there is no

room to flout the law governing the corporation's affairs. If the fiduciaries of a Delaware corporation do not like the applicable law, they can lobby to get it changed. But until it is changed, they must act in good faith to ensure that the corporation tries to comply with its legal duties"). A board does not get to stick its head in the sand and feign "ignorance" of "liability creating activities within the corporation." *AmSouth*, 911 A.2d at 369.

The Amended Complaint alleges that the Board knew Facebook's legal obligations before sharing data with a third party, knew that Facebook had previously violated these obligations by improperly sharing data with third parties (*namely,* the Canadian Regulatory Settlement and FTC Order delivered to the Board), and they knew data was Facebook's most precious asset. Yet, in 2015, when the Board learned about Cambridge Analytica through the *Guardian* article and allegations that a third party had received access to tens of millions of Facebook users' private data without users' consent, it took no action. Failure of a board take action in the face of a "known duty to act" constitutes bad faith. *Walt Disney*, 906 A.2d at 67.

At that moment, the Board had a duty to initiate an investigation or engage in some reasonable process to review the serious allegations being made given the affirmative obligations in the FTC Order. [redacted]

[redacted]

[redacted] Meanwhile, the Board signed off on public filings reassuring investors of Facebook's compliance with the above listed laws. Delaware law is clear that directors may not "consciously disregard" their duty to act when the corporation is suffering harm from the illegal or imprudent activity of its employees. *AmSouth*, 911 A.2d at 369 (quoting *Walt Disney*, 906 A.2d at 67).

4. Director Defendants Adequately Alleged That Director Defendants Knew of and Ignored Control Deficiencies

Facebook Defendants next contend that the Amended Complaint fails to allege that Facebook Defendants knew based on a series of "red flags" that Facebook was not complying with privacy laws. (MTD at 17-24).

First, Facebook Defendants misstate the standard. Plaintiffs need only show that the directors knew "*or should have known"* that the company was violating the law. *Melbourne Mun. Firefighters Pension Tr. Find on behalf of Qualcomm, Inc. v. Jacobs*, 2016 WL 4076369, at *8 (Del Ch. Aug. 1, 2016) (explaining that plaintiffs must show that the directors "knew or should have known" that the corporation was violating the law).

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Second, Facebook Defendants rely on a series of inapposite cases. For example, they cite to *Melbourne*, 2016 WL 4076369, at *8, but in that case the Court found that the board considered and disagreed that it was running afoul of antitrust laws. *Id.* at *10. Director Defendants, by contrast, did not conduct any analysis whatsoever. Facebook Defendants also rely heavily on *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106 (Del. Ch. 2009), but in that case the Court found that the company's directors did not have a duty to protect the company against exposure to subprime lending market - no illegal conduct was even implicated there. *Id.* at 131.

Cases with comparable facts illustrate the clear rule of law that a board's conscious abandonment of duty evinces bad faith and is not protected by the business judgment rule, excusing demand. The decisions in *AIG*, *Massey*, *In re Abbott Laboratories Derivative Shareholders Litigation*, 325 F.3d 795 (7th Cir. 2003) ("*Abbott Labs*"), and *In re Veeco Instruments, Inc. Sec. Litig*., 434 F. Supp. 2d 267 (S.D.N.Y. 2006), are all instructive.

Applying the *Caremark* standard, this Court in *AIG* sustained breach of duty of loyalty claims where directors turned a blind eye to systemic illegal conduct. The Court held that *AIG* involved "pervasive, diverse and substantial fraud" that "permeated AIG's way of doing business." *AIG* at 776-777. AIG's directors were,

[redacted].

at a minimum, "aware of the schemes and knowingly failed to stop them." *Id.* at 799. Applying the *Caremark* standard, the Court sustained the breach of duty of loyalty claims against the Director Defendants for knowing about operational weaknesses and allowing employees to exploit them. *Id.* at 798-99.

In *Massey*, management "fostered a business strategy expressly designed to put coal production and higher profits over compliance with the law" and caused the Company to "take an openly aggressive attitude" with regulators." 2011 WL 2176479, at *19. Plaintiffs alleged that the directors "did not make a good faith effort to ensure that Massey complied with its legal obligations" and did not "respond to numerous red and yellow flags by aggressively correcting the management culture at Massey that allegedly put profits ahead of safety." *Id.* "[I]nstead of using their supervisory authority over management to make sure that Massey genuinely changed it culture and made mine safety a genuine priority, the independent directors are alleged to have done nothing of actual substance to change the direction of the company's real policy." *Id*. Reviewing these allegations, then-Vice-Chancellor Strine found that "there seems little doubt that a faithful application of the plaintiff-friendly pleading standard would preclude dismissal… at the pleading stage." *Id.* at *20.

[redacted]

In *Abbott Labs*, derivative plaintiffs alleged that the directors ignored red flags raised by the FDA about violations of healthcare regulations over a six year period, and consciously took no action to remedy those problems or exercise reasonable oversight. *Abbot Labs*, at 802-803. Plaintiffs argued that the board "knew of the continuing pattern of noncompliance with FDA regulation and knew that the continued failure to comply with FDA regulations would result in severe penalties and yet ignored repeated red flags raised by the FDA and in media reports and chose not to bring a prompt halt to the improper conduct causing the noncompliance, nor to reprimand those persons involved, nor to seek redress for Abbott for the serious damages it has sustained."

The Seventh Circuit, in reversing the district court's dismissal, held that the "facts support a reasonable assumption that there was a 'sustained and systematic failure of the board to exercise oversight', in this case intentional in that the directors knew of the violations of law, took no steps in an effort to prevent or remedy the situation, and that failure to take any action for such an inordinate amount of time resulted in substantial corporate losses. . . . " *Id.* at 809. *See also In re Pfizer Inc. S'holder Deriv. Litig.*, 722 F.Supp.2d 453, 462 (S.D.N.Y. 2010) (finding demand is excused because board "deliberately disregarded reports of the illegal marketing practices eventually resulting in the 2009 settlement"); *In re*

SFBC Int'l, Inc. Sec. & Deriv. Litig., 495 F. Supp. 2d 477, 486 (D.N.J. 2007) (excusing demand because "the alleged misconduct related to the core of PDG's business" and the directors ignored "particularly flagrant and reprehensible wrongdoing….").

In *Veeco,* derivative plaintiffs alleged that board members were aware of a pattern of violations of the federal export laws due to, among other things, multiple internal reports of these violations. 434 F. Supp. 2d at 272. The plaintiffs asserted that pre-suit demand upon the members of the board's audit committee would have been futile because, *inter alia*, it "abdicated its responsibility to monitor legal compliance and investigate whistleblower claims relating to the Company's allegedly flagrant, systematic and repeated violations of export control laws." *Id.* at 277-78. The Court agreed because Veeco was "not a case where the directors had 'no grounds for suspicion' or 'were blamelessly unaware of the conduct leading to the corporate liability,'" but rather a situation where the complaint adequately alleged that "the director-committee members 'conscientiously permitted a known violation of law by the corporation to occur.'" *Id.* at 278 (citation omitted). The same is true here. The Board was regularly informed of red flags indicating Company-wide violations of privacy regulations around the globe. ¶¶124, 129, 131-136, 138-142, 143, 144-164.

[redacted]

As in *AIG*, *Massey*, *Abbott Labs*, *Veeco* and the other cases cited herein, this was a well-documented, well-known, cultural disregard for privacy in furtherance of growth and profit over an extended ten-year period. Facebook Defendants contend that the red flags were not clear enough and that the Amended Complaint does not sufficiently set forth knowledge or bad faith on the part of the Director Defendants. MTD at 18-23.

However, at this stage of the proceeding, prior to obtaining any discovery, it is reasonable for this Court to infer that all of the Director Defendants had knowledge of the illegal data sharing practices for the following allegations: (a) Facebook's open and notorious indifference towards privacy, ¶¶117-121; (b) the relentless pursuit of growth at any cost, ¶123; (c) the known, systemic and prolonged sharing of data in violation of privacy laws, including with over a million unvetted app developers and device makers, ¶¶83, 84; (d) the direct violation of the 2010 Canadian Regulatory Settlement by failing to change the platform and continuing to share data with app developers, ¶¶129-130; (e) the violations of the 2011 FTC Order by sharing user data with app developers and device makers without users' knowledge or express consent for a prolonged seven year period, ¶143; (f) the litany of lawsuits, bad press, settlements, and multiple public apologies by Zuckerberg and Sandberg that spanned the entire relevant

period over Facebook's data sharing practices and violations of users' privacy, ¶¶131, 140, 143, 185-187; (g) the 2011-2012 warnings from Facebook's operations manager Sandy Parakilas, ¶¶144-164; (h) Facebook's and Palantir's involvement in 2014 with Cambridge Analytica, ¶¶165-180; (i) the December 11, 2015 *Guardian* article that Cambridge Analytica may have been misusing Facebook data for political manipulation, ¶¶181-183; (j) the decision to hire one of the co-founders of GSR, Joseph Chancellor, in November 2015, ¶180; (k) the interference with Facebook's news feed in 2016 and warnings of McNamee to Zuckerberg and Sandberg, ¶¶192-198; (l) [redacted]; (m) [redacted]; (n) [redacted]; (o) the rewriting of Stamos's White Paper in April 2017, ¶207; (p) the leaked Stamos memorandum criticizing Facebook's data and security practices, ¶208; (q) the dismissal of Stamos due to friction with Zuckerberg and Sandberg [redacted]

[redacted]

[redacted], ¶212; (r) the false testimony of Milner during a February 2018 hearing before the British Parliament, ¶¶214-15; (s) the April 2018 resignation of defendant director Koum's over privacy concerns, ¶60; (t) Desmond-Hellmann's decision to step down from the Audit Committee in or around May 2018, ¶58; (u) the legal threats by Facebook to *The Guardian* for its March 2018 expose on Cambridge Analytica, ¶220; (v) the steadfast refusal of Zuckerberg to appear before the British Parliament, ¶¶224-27; and, most recently (w) the abrupt resignations of Instagram co-founders Kevin Systrom and Michael Krieger on September 25, 2018 due to Zuckerberg's relentless push for more Instagram data sharing as the means to drive profits and growth. Weaver Aff. at 2.

The holdings in *AIG*, *Massey*, *Abbott Labs*, and *Veeco*, excusing demand strongly support excusing demand here, especially in light of the requirements of the FTC Order, and the more pervasive and prolonged wrongdoing alleged in the Complaint. The Court should reject Facebook Defendants' contention that these "red flags" were not sufficiently connected to the corporate trauma – as red flags need only give directors reasonable notice of a problem. *Melbourne Mun. Firefighters*, 2016 WL 4076369, at *8 (plaintiffs must show that directors "knew or should have known" that the corporation was violating the law). Moreover, it is reasonable to infer from the allegations that it was impossible for Director

[redacted]

Defendants not to know given the ample warnings by regulators, media and the information known to Zuckerberg, Sandberg, and the Audit Committee Members (which constitutes a Board majority). Thus, Facebook Defendants cannot contend that the Director Defendants were blamelessly unaware of ongoing violations. The allegations show that the "corporation's information systems" did not reflect "a good faith attempt to be informed of relevant facts." *Caremark*, 698 A.2d at 972. Rather the allegations support a finding that this was a "sustained or systematic failure of the board to exercise oversight"– based on multiple employee and witness accounts. *Caremark*, 698 A.2d at 971.

5. Zuckerberg, Sandberg And Koum Face Substantial Likelihood Of Liability For Insider Trading

A *Brophy*[17] claim requires a plaintiff to plead sufficient particularized facts to support a "reasonable inference" that: "(1) the corporate fiduciary possessed material, nonpublic company information; and (2) the corporate fiduciary used that information improperly by making trades because she was motivated, in whole or in part, by the substance of that information." *Am. Int'l Grp., Inc., Consol. Deriv. Litig.*, 965 A.2d 763, 800 (Del. Ch. 2009), *aff'd sub nom.* 11 A.3d 228 (Del.

[17] *See Brophy v. Cities Serv. Co.*, 70 A.2d 5 (1949).

[redacted]

2011).[18] As explained below, the Complaint pleads sufficient particularized facts to reasonably infer that Insider-Trading Plaintiffs breached their fiduciary duty of loyalty to the Company by trading Facebook stock on confidential information.

a. Insider-Trading Defendants Possessed Material, Non-Public Information Concerning Third Parties' Access to Private User Data.

The Guardian's December 2015 Cambridge Analytica article did *not* disclose the vast majority of the confidential information that Insider-Trading Defendants' possessed, and that information was "material." Following full disclosure of all confidential information, Facebook stock plummeted by nearly $120 billion.

i. *Insider-Trading Defendants Possessed Confidential, Non-Public Information*

Plaintiffs' pleadings go well beyond "general knowledge [stated] in a conclusory fashion. . . [and] explained solely by virtue of their service in their various capacity." *Rattner v. Bidzos*, 2003 WL 22284323, at *11 (Del. Ch. Sept. 30, 2003). Indeed if, as Facebook Defendants contend, the market was fully aware of all relevant facts following the 2015 disclosure, then there would have be no

[18] Delaware officers and directors who "misuse[d] company information to profit at the expense of innocent buyers of their stock [must] disgorge their profits." *Kahn v. Kolberg Kravis Roberts & Co., L.P.*, 23 A.3d 831, 840 (Del. 2011). "This doctrine is not designed to punish inadvertence, but to police intentional misconduct." *Guttman v. Huang*, 823 A.2d 492, 505 (Del. Ch. 2003).

[redacted]

need for state, federal, and foreign governments (and their agencies) to open investigations in 2018 to understand "what Facebook knew [in December 2015] and why the company didn't reveal [pertinent information] at the time to its users or investors, as well as any discrepancies in more recent accounts, among other issues." ¶27. Yet, in the spring of 2018 no less than six U.S. federal government agencies opened investigations. ¶¶27, 342.

For instance, it was revealed that Facebook: may have "aided Kogan" in misappropriating user data, ¶189; and in any event, failed to ensure the misappropriated data was deleted until at least April 3, 2017. ¶200-204. Then, on June 8, 2018, following an internal investigation into each app on the Platform, Facebook admitted it suspended an additional 214 third-party apps on suspicion of misappropriation of private user data. ¶¶20, 41. The reason these apps operated subversively prior to June 2018 was because Facebook Defendants lacked sufficient oversight controls, declined to enforce their data security policies, or otherwise ignored infrastructure vulnerabilities despite repeated warnings from numerous high-level Facebook employees and officials dating back at least to 2011. ¶¶145-64, 197-98, 206-08, 212, 245-49, 389.

Perhaps the most damning disclosure of previously confidential information was that Facebook affirmatively entered into agreements with "whitelist"

companies[19] and "integration partners"[20] to exploit personal user information and the personal information of their friends. ¶¶250-52. According to the *New York Times*, "integration partners" had access to "user ID, name, photograph, 'about' information, location, email, and mobile number", as well as "private Facebook messages and friends' responses, along with the friends' names and Facebook user IDs." ¶254. By engaging a single Facebook user, an "integration partner" could "retrieve identifying information for nearly 295,000 Facebook users, including more than 50 types of information about [each of the users'] 'friends' . . . and their 'friends.'" *Id*.

The "whitelist" and "integration partner" agreements are directly at odds with Facebook's public positions on data sharing and user privacy. ¶¶266-72. For example, Zuckerberg represented to Congress on April 9-10, 2018 that third-party access to "friends of friends" data was totally "walled off" in 2015. ¶275. One week later, on April 18, 2018, Facebook surreptitiously updated its data sharing and user privacy policies (which among other things instruct users to hold Facebook "accountable" for any violations thereof) by removing the clause that

[19] The 60 "whitelist" companies, included "dating apps Hinge and Coffee Meets Bagel, Royal Bank of Canada, and Nissan Motor Co." ¶259, 281.

[20] The 52 companies with which Facebook had "integration partnerships" primarily included "device makers and operating systems, [such as] Amazon, Apple, AT&T, Microsoft Samsung, BlackBerry, and Chinese telecommunications company Huawei." ¶250.

[redacted]

"data and information shared with Facebook's advertisers, measurement, and analytics partners did not include users' PII." ¶¶97-99. Then, in June 2018, Defendant Zuckerberg submitted written testimony to Congress that it had entered into "whitelist" and "integration partner" agreements, which shared user PII.

This was not the first time that Facebook Defendants deceived the public to obfuscate or prevent the disclosure of previously confidential facts. Indeed, when Facebook Defendants found out about *The Guardian's* March 17, 2018 exposé, they threatened legal action if it was published and then lied about it. ¶220. Facebook Defendants also affirmatively mislead British Parliament on February 8, 2018, unequivocally stating Cambridge Analytic never accessed Facebook user data. ¶16. Parliament later obtained Company records that proved "Facebook was aware of the data harvesting. . . prior to December 2015." ¶188. Parliament subsequently fined the Company "the highest allowable fine of £500,00 for "fail[ing] to be transparent. . . ." ¶351.

As the Amended Complaint specifies, at the time of trading Facebook's securities, each Insider-Trading Defendant was aware of the non-public, confidential facts alleged herein. *See* ¶¶9, 10, 12-13, 19-20, 26, 35, 40, 44, 75, 81, 93, 142, 188, 191, 198, 207, 212, 215, 231, 233-34, 236, 249, 255, 257, 264, 271, 296, 383, 384-85 (concerning Zuckerberg's knowledge); ¶¶10, 35, 44, 75, 121,

[redacted]

142, 191, 198, 207, 212, 236, 300, 338, 383, and 384 (concerning Sandberg's knowledge); and ¶¶10, 35, 44, 60, 142, 188, 191, 236, 384 (concerning Koum's knowledge). Consequently, Plaintiffs have satisfied the "access to confidential information" prong. *See, e.g.*, *Triton Const. Co. v. E. Shore Elec. Servs., Inc.*, 2009 WL 1387115, at *11 (Del. Ch. May 18, 2009), *aff'd,* 988 A.2d 938 (Del. 2010) (holding an insider has access to confidential information simply by being present in meetings where the confidential information was discussed).

Facebook Defendants suggest it is "nonsensical" that Defendant Sandberg possessed material, non-public information in February 2016 when she gave the public "assurances that [Facebook] had a policy against granting access to user data to third parties" because Facebook "did have such a policy." MTD at 35 n.13. Facebook Defendants' argument however proves Plaintiffs' point. As previously discussed, Defendant Sandberg knew the Company was violating its user privacy and user data agreements when authorizing "whitelist" companies and "integration partners" to access user PII.

Facebook Defendants also argue there are insufficient facts pled concerning Defendant Koum's trades because Plaintiffs fail to identify "which of Mr. Koum's trades are at issue in this case; explain what material, non-public information Mr. Koum possessed at the time of the trades; or allege that the trades were suspicious

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in timing or amount." MTD at 38-39. As the citations herein demonstrate, Plaintiffs clearly articulated the material, non-public information that Defendant Koum possessed. The Complaint also clearly specifies the trades at issue for Defendant Koum, ¶¶293, 303, 304 (citing Ex. Q), and that the trades were suspicious in timing or amount. ¶¶305-07.

ii. *The Inside Information Was Material*

Facebook Defendants also make a perfunctory argument that even if Insider-Trading Defendants possessed non-public information that information was not material. MTD at 35-36. This argument is simply not credible.

Information is "material" if there is a "substantial likelihood that the nonpublic fact would have assumed actual significance in the deliberations of a person deciding whether to buy, sell, vote, or tender stock." *Silverberg on Behalf of Dendreon Corp. v. Gold*, 2013 WL 6859282, at *10 (Del. Ch. Dec. 31, 2013). Here, "[w]hen the Company finally revealed the full impact of the Directors' breaches on earnings on July 25, 2018, Facebook shareholders lost $119 billion in a single day — ***the largest single-day destruction of shareholder value in history***." ¶265 (emphasis in original). For context, the loss "exceeded the entire market capitalization of General Electric, Goldman Sachs or IBM" and was "larger than the gross domestic product of 153 nations." *Id*. The mammoth drop in price

was not caused by the Company missing soft projection and estimates as to value. Rather, it was caused by Facebook Defendants' failure to protect the corporation's key assets — *e.g.*, the largest repository of confidential personal data in the world. ¶¶263-65. When the information possessed by Insider-Trading Defendants was disclosed, the mix of the information in the market was "significantly altered."

b. Insider-Trading Defendants Traded on the Basis of Material, Non-Public Information

Facebook Defendants argue that the trades were executed pursuant to a Rule 10b5-1 trading plan, but this argument fails for several reasons. This argument is an affirmative defense not properly considered on motion to dismiss. *In re Able Labs. Sec. Litig.*, 2008 WL 1967509, at *27 n.40 (D.N.J. Mar. 24, 2008); *see also Elec. Workers Pension Tr. Fund of IBEW Local Union No. 58 v. CommScope, Inc.*, 2013 WL 4014978, at *7 (W.D.N.C. Aug. 6, 2013); *Freudenberg v. E*Trade Fin. Corp.*, 712 F. Supp. 2d 171, 200–01 (S.D.N.Y. 2010); *Malin v. XL Cap. Ltd.*, 499 F.Supp.2d 117, 156 (D. Conn. 2007); *In re Cardinal Health Inc. Sec. Litig.*, 426 F. Supp. 2d 688, 734 (S.D. Ohio 2006); *see also Reid v. Spazio*, 970 A.2d 176, 183 (Del. 2009) (explaining, "affirmative defenses . . . are not ordinarily well-suited for treatment on [motion to dismiss].").

In asserting a valid 10b5-1 plan defense, Facebook Defendants must submit evidence that the plan was made in good faith prior to possessing material, non-

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public information. *In re Able Labs. Sec. Litig.*, 2008 WL 1967509, at *27; *see also* Rule 10b5-1 Trading Plans — The Safe Harbor Provided by Rule 10b5-1 Trading Plans, 4 Law Sec. Reg. § 12:163. The sale of the securities must have also occurred in accordance with the plan, and the plan cannot be modified while the insider possessed the material, non-public information at issue. *City of Roseville Employees' Ret. Sys. v. Horizon Lines, Inc.*, 686 F. Supp. 2d 404, 425 (D. Del. 2009). Finally, a 10b5-1 plan safe harbor is presumptively rebutted if the pleading specifies the trading pattern at issue was "unusual."[21] *City of Roseville*, 686 F. Supp. 2d at 425.

Trading plans can be modified or violated, or it is entirely possible that the Insider-Trading Defendants constructed these plans to take maximum advantage of insider knowledge while securing a defense for themselves. These are triable issues of fact that require discovery. Certainly, the timing and size of the trades (especially compared to the prior year's trades) demonstrate that there is reason to infer that "at least in part they consciously acted to exploit the fact that they possessed material, nonpublic information." *Silverberg*, 2013 WL 6859282, at *14;

[21] A recent study that reviewed more than 100,000 trades by more than 3,000 executives using 10b5-1 trading plans found that trading under these plans beat the market by more than 6% during a six-month period while trading without these plans beat the market by only 1.9%. Alan D. Jagolinzer, *Do Insiders Trade Strategically within the SEC Rule 10b5-1 Safe Harbor?* (Dec. 6, 2006), *available at* http://ssrn.com/abstract=541052.

[redacted]

see also Am. Int'l Grp., 965 A.2d at 801. Specifically, beginning on February 17, 2018, as Facebook representatives misled British Parliament, ¶¶213-18, Zuckerberg ramped up his sales, shedding approximately 23.93 million shares (netting approximately, $4.43 billion) after selling only 4.1 million shares the entire prior year. ¶¶298-99. Sandberg similarly accelerated her sales on the eve of public disclosure, selling only 107,766 shares in 2015 before selling 4 million shares in 2016 and 2017 combined (netting $385.6 million) and then 548,000 shares in the early part of 2018 (netting $100 in profits). ¶¶300-02. Koum meanwhile sold the most shares during this time-period, netting more than $7.9 billion. ¶303. Soon after, Koum resigned from the Board on April 30, 2018. The Insider Trading Defendants ramped up their sales, even if by a trading plan, because they knew that full disclosure of their improper data sharing practices was imminent. ¶¶293-303.

At the appropriate time, Facebook Defendants will need to prove their defense, including that the Insider-Trading Defendants executed all trades of Facebook stock pursuant to their trading plans, and that they executed their respective trading plans prior to acquiring insider-knowledge alleged here. Facebook Defendants will also need to prove that the plans were entered in good

faith and were not later amended. Finally, Facebook Defendants will need to explain why certain unusually large trades were "accelerated". ¶¶298, 300-01.

For these reasons, Plaintiffs have stated a valid *Brophy* claim and Zuckerberg, Sandberg and Koum face a substantial risk of personal liability (including disgorgement of *millions* of dollars in ill-gotten gains), rendering them unable to consider demand on the insider trading claim.

6. Director Defendants Face A Substantial Likelihood of Liability For Violating Disclosure Duties

Any time corporate directors in Delaware voluntarily communicate with shareholders, "they must do so with honesty and fairness, recognizing that they owe a duty of loyalty. . . regardless of the absence of a request for action required pursuant to a statute, the corporation's certificate of incorporation or any bylaw provision." *Jackson Nat. Life Ins. Co. v. Kennedy*, 741 A.2d 377, 381 (Del. Ch. 1999). When requesting shareholder action, directors must supply shareholders with all information material to the shareholders' decision, as well as sufficient context to "provide a balanced, truthful account of all matters disclosed in the communications with shareholders." *Malone v. Brincat*, 722 A.2d 5, 12 (Del. 1998) (citing *Zirn v. VLI Corp.*, 681 A.2d 1050, 1056 (Del. 1996)). Directors violate their duty of disclosure if they are "alleged to have deliberately issued an intentionally false communication to the stockholders" even when no shareholder

action is being sought. *Id.* Omissions and misleading partial disclosures also violate Delaware directors' fiduciary duty of disclosure. *Appel v. Berkman*, 180 A.3d 1055 (Del. 2018) (citing *In re Walt Disney Co. Derivative Litig.*, 731 A.2d 342, 376 (Del. Ch. 1998)); *Zirn*, 681 A.2d at 1057 ("Directors have an obligation not to omit facts in a manner that renders partially disclosed information materially misleading"); *In re Orchard Enterprises Inc. Stockholder Litig.*, 88 A.3d 1, 22 (Del. Ch. 2014) (internal quotation marks and citations omitted) ("Once directors begin to speak on a subject, they assume an obligation to provide the stockholders with an accurate, full, and fair characterization.").

In *In re Hansen Med., Inc. S'holders Litig*., the Court held that the plaintiffs stated "a reasonably conceivable non-exculpated claim for breach of fiduciary duties against the Director Defendants due to material misstatements and omissions in the Proxy" when those plaintiffs alleged that the directors failed to fully and fairly disclose "all material information." 2018 WL 3030808, at *10 (Del. Ch. June 18, 2018) (internal citations and quotations omitted) (finding "[p]laintiffs have stated a reasonably conceivable claim that the Merger should be considered under the entire fairness standard of review because it was a conflicted transaction involving [a control group]."). Under Delaware law, "when a board chooses to disclose a course of events or to discuss a specific subject, it has long been

understood that it cannot do so in a materially misleading way, by disclosing only part of the story, and leaving the reader with a distorted impression. . . Partial disclosure, in which some material facts are not disclosed or are presented in an ambiguous, incomplete, or misleading manner, is not sufficient to meet a fiduciary's disclosure obligations." *Id.* at *10.

Facebook Defendants rely on *Steinberg v. Bearden*, No. 2017-0286, 2018 WL 2434558 (Del. Ch. May 30, 2018) and *Ellis v. Gonzalez*, 2018 WL 3360816 (Del. Ch. Jul. 10, 2018) to argue that Plaintiffs' allegations are insufficient to show that the Director Defendants knew the Company's disclosures to its shareholders were misleading. The courts in *Steinberg* and *Ellis* held that demand may not be excused on an independent, disinterested, and exculpated board of directors based on disclosure violations. Those cases have no bearing here where the Amended Complaint sufficiently demonstrates that the Director Defendants are *not* independent and disinterested, and where Plaintiffs' disclosure claims implicate the duty of loyalty and thus are not exculpated under Section 102(b)(7).

Far from merely "allowing" the company to mislead its shareholders, the detailed facts demonstrate that Facebook Defendants knew that Facebook's data sharing practice and security protocols were inadequate to protect users' data, and yet critical disclosures and warnings are omitted from Facebook's public

statements. ¶¶117-23. The Amended Complaint describes a culture of indifference to users' privacy that permeated Facebook. *Id.* Facebook's Board openly discussed the "[o]ngoing attacks on our privacy practices," "prescribing formalities notice and consent obligations and rigid restrictions on data use that will continually challenge our vision and philosophy," and "scrutiny of Facebook and our practices has significantly increased which has created the risk of regulatory delay for launches of some sensitive initiatives." ¶119. When the Board was faced with reports from a top-level executive of lax controls over data security, comparing the multi-billion-dollar company to a "college campus" in terms of online security, that executive was relieved of his duties. ¶120. The Amended Complaint describes "numerous red flags – including lawsuits, internal and external reports, and [Facebook Defendants'] own admissions through repeated apologies – that Facebook was not securing users' private information." ¶124. As set forth above, there were multiple red flags, including the CIPPIC action and Canadian Regulatory Settlement in 2010, the FTC investigation and resulting FTC Order in 2011, the class action lawsuit over privacy violations settled in 2011, the paper revealing Facebook's psychological testing on nearly 700,000 users without permission in 2014, multiple maximum fines assessed by European regulators, warnings from Parakilas in 2011 and 2012, warnings from Stamos in 2016 and

[redacted]

2017. ¶¶143, 145-60. Parakilas described the "typical reaction" at Facebook as "try[ing] to put any negative press coverage to bed as quickly as possible, with no sincere efforts to put safeguards in place or to identify and stop abusive developers." ¶161. There are ample facts in the Amended Complaint to infer that Facebook Defendants knew Facebook had major data sharing and security problems. The omissions of discussions about their data sharing practices, Cambridge Analytica, and virtually non-existent system or controls over third parties, falsely reassured shareholders that Facebook had everything under control.

Facebook's communications to its investors were ambiguous, incomplete, and misleading. The public statements made following the revelation of the Cambridge Analytica scandal in December 2015, including the 2017 and 2018 Proxy Statements and the Form 10-Ks filed with the SEC in 2016, 2017, and 2018, reassured investors that Facebook's user data was secure and under control, while in reality Facebook was illegally sharing data with third parties, as it did with Cambridge Analytica in 2014. Director Defendants failed to disclose in Facebook's filings that:

- even after the Cambridge Analytica breach, Facebook continued to share private user data with sixty additional third-party app developers, ¶281;
- the size, scope, and details of the Cambridge Analytica in the 2017 and 2018 Proxy Statements, ¶284;

[redacted]

- Facebook waited six months to secure a promise from Kogan and GSR that the misappropriated data had been deleted without any verification, ¶¶201-202;

- SCL did not confirm it deleted Facebook users' data and derivative data until September 6, 2016, and the company did not sign a certification that the data was destroyed until April 3, 2017, ¶204; or

- the existence of "integration partnerships" with 52 companies through which Facebook shared the exactly types of data that were exploited and misused by Cambridge Analytica, including the personal data of Facebook users' "friends" who did not consent to having their data disclosed, ¶252.

Facebook Defendants contend that information about Cambridge Analytica was in the "public domain" in 2015 through the *Guardian* article (MTD at 31) and therefore Plaintiffs cannot allege that they did not know about this breach. Yet, they simultaneously argue that the Amended Complaints fails to allege "what the directors knew and when." MTD at 29. Based on Facebook Defendants' logic, it is reasonable for the Court to infer that the Director Defendants were on notice of Cambridge Analytica in 2015. Zuckerberg admitted this in his testimony to Congress. ¶¶241, 247.

Despite having knowledge of a potentially material breach involving Cambridge Analytica in 2015 and knowledge of a Company investigation, which was also publicly announced, Director Defendants continued reviewing, signing, and/or approving misleading, incomplete statements about Facebook's data sharing practices and Cambridge Analytica in its 2017 and 2018 Proxy Statements and

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From 10-Ks. ¶¶277, 284. Each of those actions alone or in combination is sufficient to hold Facebook Defendants personally liable for any failure to disclose material information within. *O'Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 920 n.34 (Del. 1999) ("[C]orporate fiduciaries have an obligation to confirm that statements in communications contemplating stockholder action are true before disseminating the communications to the stockholders."). And indeed, the Director Defendants "were able to and did, directly and indirectly, exercise control over the content of the various public statements issued by Facebook that were false and misleading." ¶76. They falsely assured investors in public filings that they were in compliance with privacy laws, when they knew that an investigation into the actions of Cambridge Analytica and Facebook's role was underway. Making reassuring statements to investors while omitting details about the potentially massive data breach revealed in 2015 demonstrates bad faith. *See Doppelt v. Windstream Holdings, Inc.*, 2016 WL 612929, at *6 n. 70 (Del. Ch. Feb. 5, 2016) (complaint alleges sufficient facts to infer alleged omissions in proxy statement were made knowingly and in bad faith, even where director conflicts not alleged: "Why an independent board would engage in bad faith is. . . a question the Court need not address at this stage in the proceeding; Plaintiffs need only plead facts from which the Court can reasonably infer that the Board conceivably acted

in bad faith"); *Chen v. Howard-Anderson*, 87 A.3d 648 (Del. Ch. 2014) (denying defendants' motion for summary judgment on failure to disclose claims because there was evidence that defendants knew about "disclosure problems" before approving proxy statement); *Crescent/Mach I Partners, L.P. v. Turner*, 846 A.d 963, 987, 989 (Del. Ch. 2000) (shareholders stated claim for breach of duty to disclose where they alleged that directors "effected the merger in bad faith which they disguised in a misleading proxy statement"). Directors Defendant' bad faith is further demonstrated by the allegations showing that Facebook employees were directed to cover-up the breach by securing NDAs from Kogan, Cambridge Analytica, GSR and other employees and entities involved in the breach and failing to verify the destruction of the data. ¶¶201-204.

[redacted]

Moreover, Director Defendants were highly motivated to conceal the Cambridge Analytica breach because it would have revealed the bigger problem-that Facebook was engaged in illegal third-party data sharing practices. Parakilas explained:

> At a company that was deeply concerned about protecting its users, this situation would have been met with a robust effort to cut off developers who were making questionable use of data. But when I was at Facebook, the typical reaction I recall looked like this: try to put any negative press coverage to bed as quickly as possible, with no sincere efforts to put safeguards in place or to identify and stop abusive developers. . . .

¶161. Parakilas later testified: "[I]t was known and understood. . . that there was risk with respect to the way that Facebook Platform was handling data" but "it was a risk that they were willing to take." ¶163.

[redacted]

Director Defendants understood why omissions about Cambridge Analytica and these other third party data sharing practices were material as they issued warnings to investors that "improper access to or disclosure of our data or user data . . . could harm our reputation and adversely affect our business." ¶270. *See also, supra*, Section I.C.5.ii. Given what they knew in 2015 and what they failed to disclose in 2016, 2017, and 2018, coupled with Facebook's attempts to conceal the details of Cambridge Analytica, the Court has a reasonably conceivable basis to infer that Director Defendants violated their duty of disclosure in bad faith.

Facebook Defendants argue that the only information the public learned in March 2018 was that Cambridge Analytica lied about destroying the Facebook data it misappropriated. MTD at 32. On the contrary, the Amended Complaint alleges that Facebook's shareholders learned for the first time the scope and details of the Cambridge Analytica breach, including Facebook's role in transferring the data to Cambridge Analytica and the sordid details of the data misuse. Shareholders also learned about management's indifference when they waited six months after the 2015 *Guardian* article to contact Cambridge Analytica about destroying the data and failed to verify the destruction of the data, and the subsequent actions to conceal the breach and Facebook's role. Shareholders learned that despite 87 million users being impacted, Facebook never notified a

single one and that PII was obtained by an unauthorized party with extreme ease and with Facebook's assistance. The "total mix" of information available to Facebook's Director Defendants differed substantially from the information they disclosed to shareholders. Given Facebook's repeated public statements regarding the importance of users believing that their data was secure and protective, the directors' failure to disclose that the data still existed in the hands of a third part alters the mix of information available to shareholders.

Finally, the Amended Complaint establishes that Director Defendants' misleading disclosures caused harm to its shareholders, which is sufficient for Plaintiffs' disclosure claim to survive a 12(b)(6) motion. The injury that resulted from their conduct is not "shareholder outrage," but harm to Plaintiffs' economic and voting rights. Failure to disclose information *always* "impinge[s] upon the stockholder franchise and stockholders' right to make an informed decision on corporate affairs," and thus harm always results from corporate directors' breach of the duty to disclose. *O'Reilly*, 745 A.2d at 916-17. Moreover, "so long as the plaintiff pleads sufficiently the other specific elements of a breach of the fiduciary duty of disclosure arising from a false statement, omission or partial disclosure, a plaintiff may request nominal damages without pleading causation or actual quantifiable damages." *Id.* at 917. As detailed above, the allegations in the

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Amended Complaint are more than sufficient to demonstrate not only the harm imposed on Plaintiffs' rights, but that the harm resulted directly from Facebook Defendants' conduct. Facebook Defendants rely on *Glinert v. Wickes Companies, Inc.*, but that case was an order denying a post-trial motion for relief from final judgment which required the plaintiff to prove by clear and convincing evidence that newly discovered evidence of Facebook Defendants' misleading disclosures would have changed the outcome of the litigation. *Glinert*, 1992 WL 165513 (Del. Ch. Jul. 14, 1992). In *Virginia Bankshares, Inc. v. Sandberg*, cited by Facebook Defendants, the U.S. Supreme Court rejected a theory of recovery – that causation is established where directors issued a misleading proxy statement to avoid the ill will of minority shareholders – that is not alleged in the Amended Complaint. Neither case is instructive for deciding a motion to dismiss, or the elements of any claims alleged here. Facebook Defendants cannot impose a heightened pleading standard by arguing that, whether shareholders were permitted to exercise their rights or not, the result would have been the same.

The totality of the well-pled allegations in the Amended Complaint provide a substantial basis upon which this Court can conceivably infer that the Director Defendants knew that they were misleading investors about Facebook's data sharing practices and Cambridge Analytica, or at a minimum, that Zuckerberg,

Sandberg, and Audit Committee members Andreessen, Bowles, and Desmond-Hellmann, knew that Facebook's public statements were misleading. Since these individuals comprise the majority of the Board, and face a substantial likelihood of liability, the Board cannot impartially assess demand as to Count V.

Having successfully pled claims for breach of the fiduciary duties of loyalty and care against Facebook Defendants under the heightened pleading standard of Rule 23.1, *supra*, based on allegations of their direct knowledge of, participation in and/or failure to correct, numerous aspects of the wrongdoing taking place at Facebook, the Amended Complaint satisfies the more plaintiff-friendly standard of Rule 12(b)(6). *In re Am. Int'l Grp., Inc.*, 965 A.2d 763, 799 (Del. Ch. 2009), *aff'd sub nom. Teachers' Ret. Sys. of Louisiana v. PricewaterhouseCoopers LLP*, 11 A.3d 228 (Del. 2011).

D. PwC Cannot Rely On Pre-suit Demand

Since demand is excused because the Board is "incapable of making an impartial decision" on the merits of this litigation, so too is any demand made to pursue aider-and-abettor PwC for liability arising from the same misconduct. *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 102 (1991) (holding aiders and abettors cannot rely on demand futility as a defense where a court finds that

demand is futile when a majority of the directors have participated in or approved the alleged wrongdoing).

Filing an aiding-and-abetting claim against PwC required the majority of Facebook Board's to acknowledge their own disloyalty and mismanagement in failing to adequately protect the Company's principal asset, user data. This is because the Officer and Director Defendants needed PwC's audits to conclude Facebook's controls were "sufficiently effective." ¶¶192-96. The Amended Complaint alleges that PwC's audits reached the "proper" conclusion because PwC implement sub-standard auditing procedures and methodologies, and by selectively ignoring material facts.[22] ¶¶327-37. Through PwC's aid, Facebook Defendants concealed their third party data sharing practices and lack of a system or controls over third parties invited onto the platform.

Courts have excused demand as futile in analogous circumstances. *In re eBay, Inc. S'holder Litig.*, 2004 WL 253521, at *5; *In re Trump Hotels S'holder Deriv. Litig.*, 2000 WL 1371317, at *11 (S.D.N.Y. Sept. 21, 2000). In *Trump Hotels*, the Southern District of New York applied Delaware law to hold demand

[22] PwC argues that the lack of "affiliation" between PwC and Facebook Defendants is "fatal" to Plaintiffs' demand futility argument without citing a single authority in support. PwC MTD at 8. Under *Kaplan*, the only consideration that matters is whether the Director Defendants were able to make an impartial decision with respect to the underlying misconduct, not whether an aider and abettor is "affiliated" with a corporate board.

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was futile as to the third-party (financial advisor) defendants "because the Board could not have been expected to exercise independent business judgment with respect to the [underlying] Transaction, it follows that the Board would also be unable to consider impartially the merits of a demand against a third party [financial advisory] . . . whose Fairness Opinion was critical to the success of the Transaction." *In re Trump Hotels S'holder Deriv. Litig.*, 2000 WL 1371317, at *11. In that case, the director defendants sold a hotel and casino to "dispose of a losing business and escape all the attendant risks of default on the large debt held by the casino's parent company." *Id*. at *2. As part of the scheme, defendants issued a proxy statement in August 1996 that included a statement from the board's financial advisors that they reviewed the transaction and concluded it was "fair, from a financial point of view to [the Company]." *Id*. at *4. The financial advisor defendants' statement, however, was made in bad faith because they relied on improper evaluation "methodologies" and "materially false and misleading" information that was "contradicted or unsupported by the actual facts." *Id*. Since there was no "reasonable basis" for the third party to reach their conclusion on valuation, the court found that demand was excused as futile. *Id*.

Similarly here, Facebook Defendants retained PwC as an "independent" auditor, following the FTC's finding that Facebook had "overrid[den] the users'

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privacy settings to reveal personal information and to disclose, for commercial benefit, user data — and the personal data of friends and family members — to third parties without [user] knowledge or affirmative consent." ¶321; *see also* ¶¶32, 323, 327. Like *Trump Hotels*, where the advisor Facebook Defendants' evaluation relied on "materially false" information "contradicted or unsupported by the actual facts," PwC's audits were misleading because they failed to include or discuss known material facts.[23] Specifically that: (a) Cambridge Analytica improperly accessed user data in December 2015 and retained possession of that data until at least April 3, 2017, ¶¶204, 337; (b) Facebook entered into "whitelist" agreements and "integration partnerships" to share user data and the data of their friends without express user consent, ¶¶249-60; and (c) even after Facebook purportedly updating its entire platform in 2014 to "dramatically limit" the information third-party apps accessed without express user consent, private user

[23] PwC's audit, covering the two-year period between February 2015 and February 2017, "incurr[ed] over 4,500 hours" of fieldwork, primarily at Facebook's Menlo Park, CA headquarters, PwC 2017 Audit at 16, whereby PwC claims to have "use[d] a combination of inquiry, observation and/or inspection for testing of the controls," which demanded PwC interview numerous individuals in various Facebook departments to ensure the controls in place worked as intended. *Id*. at 17. PwC was further required to "evaluat[e] and adjust[] [Facebook's] privacy program in light of the results of the testing and monitoring. . . [and] any material changes to [Facebook's] operations or business arrangement, or any other circumstances that [Facebook] knows or has reason to know may have a material impact on the effectiveness of its privacy program." *Id*. at 20.

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data was still susceptible to misappropriation and misuse. ¶¶19-20. Thus, the Board cannot assess demand against its aider-and-abettor PwC. *See Rales*, 634 A.2d at 934 (Del. 1993) (explaining demand is futile where directors are incapable of "impartially consider[ing] its merits without being influenced by improper considerations").

II. DIRECTOR DEFENDANTS CANNOT CLAIM THE PROTECTION OF THE EXCULPATORY PROVISION OF SECTION 102(b)(7)

Facebook Defendants seek to rely on the exculpatory provision in Facebook's Certificate of Incorporation in seeking dismissal. MTD at 29. Setting aside the fact that Plaintiffs have rebutted the business judgment presumption and, as demonstrated above, Director Defendants have violated their duty of loyalty, an exculpation provision such as that authorized by § 102(b)(7) is "in the nature of an affirmative defense." *Emerald Partners v. Berlin*, 787 A.2d 85, 91-92 (Del. 2001).

As a result, "it is the burden of the defendants to demonstrate that they are entitled to the protections" of this provision. *Id.* at 98; *In re Emerging Communications, Inc. S'holders Litig.*, 2004 Del. Ch. LEXIS 70, **145-46 (Del. Ch. 2004). Where, as here, a complaint implicates duty of loyalty claims, a § 102(b)(7) provision will not operate as a bar to duty of care claims on a motion to dismiss. *Alidina v. Internetcom Corp.*, 2002 WL 31584292, at *8 (Del. Ch. Nov. 6, 2002). Even if Facebook's § 102(b)(7) provision was implicated here (which it is

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not), it still would not be a ground to dismiss the duty of care claims against Director Defendants to the extent that Plaintiffs seek non-monetary relief. *California Public Employees' Retirement Sys. v. Coulter*, 2002 WL 31888343, at *17 (Del. Ch. Dec. 18, 2002) (denying motion to dismiss on § 102(b)(7) grounds where complaint did not solely assert duty of care claims, nor solely seek monetary damages). As such, Facebook Defendants' motion on the grounds of its exculpatory provision should be denied.

III. THE INDEMNIFICATION AND CONTRIBUTION CLAIMS ARE RIPE

Facebook Defendants' ripeness challenge to Plaintiffs' contribution and indemnification claims is also unavailing. Under Delaware law, a claim for contribution or indemnification accrues for statute of limitations purposes when the claimant "'suffers loss or damage through payment of a claim after judgment or settlement.'" *Certainteed Corp. v. Celotex Corp.*, 2005 WL 217032 at * 3, n. 2 (Del. Ch. Jan. 24, 2005). However, the question of ripeness is different from the question of accrual of a claim for statute of limitations purposes. Indeed, the Delaware courts have acknowledged that judicial efficiency often favors litigation of contribution and indemnification claims simultaneously with the underlying predicate actions – *i.e.*, before the statute of limitations has begun to run. *See, e.g.*, *Daystar Constr. Mgmt., Inc. v. Mitchell*, 2006 WL 2053649, at *11 (Del. Super.

July 12, 2006) ("if contribution or indemnification claims are brought as derivative cross or third-party claims, *i.e.*, the claimant's right to indemnification or contribution is contingent upon the success of the plaintiff's direct claim against him, then the court may adjudicate all claims together in the interest of judicial economy") (citation omitted); *McMichael v. Delaware Motor Coach Co.*, 107 A.2d 895, 896 (Del. Super. 1954) (contribution or indemnification claims may be brought where the claimant's right to indemnification or contribution is still contingent upon the success of the plaintiff's direct claim because adjudicating all of the claims together is in the interest of judicial economy). Plaintiffs' claims are indisputably ripe for adjudication as to the fines levied on Facebook to date. The fact that other actions, such as the securities and consumer actions, have not yet been reduced to judgment or settled does not negate the fact that the claims are ripe as to the regulatory investigations resolved to date.

Finally, it would be inefficient and a waste of this Court's resources to require Plaintiffs to bring a separate action after the consumer and securities actions are fully adjudicated. *See Schick, Inc. v. Amalgamated Clothing & Textile Workers Union*, 533 A.2d 1235, 1239 (Del. Ch. 1987) (in deciding whether a matter is ripe for judicial determination, relevant considerations include "the need to conserve scarce resources"). Judicial efficiency favors litigation of the

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contribution and indemnification claims simultaneously with the predicate litigations. Elements of the underlying misconduct by Facebook Defendants that serve as the basis of the indemnification and contribution claims will be litigated in this action.

IV. THE COMPLAINT STATES A CLAIM AGAINST PWC FOR AIDING-AND-ABETTING

A claim for aiding-and-abetting is assessed under Chancery Rule 12(b), *not* the heightened standard of Chancery Rule 23.1. Under Rule 12(b), "[a] party is entitled to dismissal of the complaint only where it is clear from its allegations that the plaintiff would not be entitled to relief under any set of facts that could be proven to support the claim." *In re Walt Disney Co. Deriv. Litig.*, 825 A.2d 275, 285 (Del. Ch. 2003). Rule 12(b) further "accept[s] all of plaintiff's well-pleaded factual allegations as true and give plaintiff the benefit of all inferences that may be drawn from the facts." *Id*.

The elements of an aiding-and-abetting claim are: "(1) the existence of a fiduciary relationship, (2) a breach of a fiduciary duty, (3) defendant's knowing participation in that breach and (4) damages proximately caused by the breach." *Cumming on behalf of New Senior Inv. Grp., Inc. v. Edens*, 2018 WL 992877, at *26 (Del. Ch. Feb. 20, 2018) (Slights, V.C.) (citing *Malpiede v. Townson*, 780 A.2d 1075, 1096 (Del. 2001). PwC challenges only the third prong of this test,

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asserting– incorrectly– that Plaintiffs have failed to plead PwC's "knowing participation." PwC MTD at 9-13.

"Knowing participation requires that a third party act with the knowledge that the conduct advocated or assisted constitutes a breach of the board's fiduciary duty." *In re Transkaryotic Therapies, Inc.*, 2008 WL 2699442, at *16 (Del. Ch. June 19, 2008 revised June 24, 2008). Even if a plaintiff does not plead actual knowledge, a court may infer a non-fiduciary's knowing participation "if a fiduciary breaches its duty in an inherently wrongful manner, and the plaintiff alleges specific facts from which that court could reasonably infer knowledge of the breach." *Crescent/Mach I Partners, L.P.*, 846 A.2d at 990; *Edens*, 2018 WL 992877, at *26 (finding that an aider-and-abettor "knowingly participated" in the underlying fiduciary breach if they "had actual or constructive knowledge that their conduct was legally improper."). Plaintiffs' Amended Complaint succeeds under either standard.

A. PwC Learned About Cambridge Analytica in 2015, Failed to Investigate, and Continued Falsely Certifying to the FTC That Facebook was Not Illegally Sharing Data With Third Parties

PwC argues that Plaintiffs failed to sufficiently allege "knowing participation" because there is no evidence that PwC was "aware of any action by Facebook's Board when PwC determined what testing procedures to apply."

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"Awareness" or "knowledge" does not demand, as PwC contends, allegations that PwC attended Facebook board meetings where "privacy incidents and system weaknesses were discussed." PwC MTD at 12. Rather, PwC need only have been aware that Facebook Defendants had a fiduciary responsibility to protect user privacy at the time PwC facilitated the breach of that duty. *See In re eBay, Inc. S'holder Litig.*, 2004 WL 253521, at *1.

There is no question PwC was aware of Facebook Defendants' duty. Facebook Defendants hired PwC to audit Facebook's privacy program following the FTC's 2011 Consent Order. ¶32. PwC, at the time of submitting the audits, knew or should have known: the importance of privacy and data security to Facebook's business model, ¶¶308-40; that the Consent Order prohibited Facebook from, among other things, "making misrepresentations about the privacy or security of consumers' personal information", ¶323; that Facebook was required to "obtain consumers' affirmative express consent before enacting changes that override their privacy preferences", and "establish and maintain a comprehensive privacy program designed to address privacy risks. . . and to protect the privacy

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and confidentiality of consumers' information", ¶323; and that a violation of the Consent Order subjected Facebook to "steep penalties of $40,000 per violation per day." ¶14. Indeed, PwC's Independent Assessor's Report even specifies that "given that Facebook protects the data of over 1.7 billion people, security is critical to [Facebook's] operations and success. . . [therefore] part of PwC's independent assessment [is to] verify that technical, physical, and administrative security controls [are] designed to protect covered information from unauthorized access, as well as those designed to prevent, detect, and respond to security threats and vulnerabilities. . . ."[24]

Consequently, the court may reasonably infer that PwC was aware that Facebook Defendants owed a duty to the Company to protect its most valuable asset — the private user data within its possession — and that Facebook "fear[ed] FTC fines or lost advertising revenue." PwC MTD at 12; *see RCS Creditor Tr. v. Schorsch*, 2018 WL 1640169, at *6 (Del. Ch. Apr. 5, 2018) (finding liability where it was "reasonably conceivable that each of the [third-party Facebook Defendants] understand that his assistance in [the scheme] contributed to a breach of fiduciary duty"); *Guttman*, 823 A.2d at 506 (explaining, "one cannot act loyally as a corporate director by causing the corporation to violate the positive laws it is

[24] Am. Compl., Ex. J at 11-12.

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obliged to obey"); *Penn Mart Realty Co. v. Becker*, 298 A.2d 349, 351 (Del. Ch. 1972) (explaining, "[f]raud and self-dealing are not the only ways in which corporate directors may breach their fiduciary duty; they may also breach that duty by being grossly negligent or by wasting corporate assets").

B. PwC's Conduct Contributed to and Aided Facebook Defendants' Breach of Their Fiduciary Duties

The Court may reasonably infer from the facts pled that PwC's actions contributed to and aided Facebook Defendants' breach of their fiduciary duties.

PwC's audit of Facebook's privacy practices was ***government-mandated.*** ¶¶325-326. PwC's essential role was to serve as the FTC's gatekeeper in detecting and revealing corporate misconduct on the part of Facebook and, specifically, to advise the FTC of any illegal data sharing by Facebook with third parties. ¶325. The FTC, in turn, served as the public's gatekeeper. Thus, while PwC did not directly report to the public, as it argues, PwC understood that its function was to protect the public by alerting the FTC of any illegal data sharing by Facebook with third parties.

The Amended Complaint alleges that PwC knew, or at least constructively knew, about the allegations made in the 2015 *Guardian* article that Facebook may have improperly shared the private data of tens of millions of Facebook users without users' notice or consent. ¶337. Yet, on April 2017, PwC provided

Facebook a clean certification concluding that Facebook was in compliance with the FTC Order from February 11, 2015 February 10, 2017. There was no indication in PwC's audit report that it conducted any investigation into the Cambridge Analytica allegations (nor did Facebook's Board request one). PwC's April 2017 audit report stated:

> In our opinion, Facebook's privacy controls were operating with sufficient effectiveness to provide ***reasonable assurance to protect the privacy of covered information*** and that the controls have so operated throughout the Reporting Period, ***in all material respects for the two years ended February 11, 2017***, based upon the Facebook Privacy Program set forth in Management's Assertion.

PwC certified Facebook's compliance with the Consent Order, by almost exclusively relying on "Management's Assertions" while knowing that Facebook may have illegally shared voluminous amounts of private data with third party Cambridge Analytica. The *Guardian's* 2015 article gave PwC every conceivable reason to increase its testing or conduct a more directed investigation.

PwC claimed in its audit report that its examination was conducted in "accordance with attestation standards established by the American Institute of Certified Public Accountants," but PwC neglected to investigate a known red flag or apply the most effective test procedure. PwC claims that it did not intentionally "omit[] re-performance testing. . . to assist the Individual Facebook Defendants in

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their alleged breach of fiduciary duties," but that presents a factual issue not appropriately decided at this stage of the proceeding without discovery. PwC MTD at 11-13.

PwC's report was misleading and it provided false certifications to the FTC (and therefore the public) about Facebook's third party data sharing practices. PwC aided and abetted the continue cover-up of Cambridge Analytica being orchestrated by Officer and Director Defendants. *RBC Capital Markets, LLC v. Jervis*, 129 A.3d 816, 863 (Del. 2015) (finding an aiding and abetting claim stated where plaintiffs alleged the advisors submitted "fragmentary and misleading information" to the board).

PwC argues that Plaintiffs failed to assert that it knew "a single piece of non-public information about any privacy incident." PwC MTD at 12. However, even if that were true, the allegations *still* sufficient allege an aiding and abetting claim.[25] PwC was the government-mandated privacy gatekeeper, PwC knew about the 2015

[25] PwC ignores the allegations in the Amended Complaint that PwC spent nearly 4,500 hours at Facebook's Menlo Park, CA headquarters, had access to confidential information, including access to Facebook employees in of Facebook's privacy and data control operations, and had access to confidential information concerning "privacy incident[s]" at Facebook. ¶327 (citing to Exhibit R, S, J). PwC's auditing responsibilities also coincided with: the 2014-2015 transition of Facebook's platform and the timing of when Facebook entered into improper data sharing agreements with whitelist companies and "integration partners". ¶251, 281. PwC's reports did not discuss any of these material events squarely relevant to Facebook's data sharing practices with third parties.

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Cambridge Analytica breach, PwC agreed to use "the [GAPP] framework . . . to define company-specific criteria for the foundation of the Facebook Privacy Program" rather than design its own "rigorous and independent" audit program, ¶329, PwC omitted significant testing procedures, and when its gatekeeping functions mattered most – during the 2016 Presidential elections – it knowingly turned a blind eye to Facebook's data sharing practices with third parties such as Cambridge Analytica. PwC continued to certify Facebook's compliance with the FTC Order while having reason to doubt its truth. PwC's reports created an information vacuum, which Facebook Defendants used to breach their fiduciary duties to the Company and its shareholders. *Jervis*, 129 A.3d at 863; *accord In re Rural Metro Corp.*, 88 A.3d at 97.

[redacted] or the lack of communication between "anyone at Facebook and PwC," but this *completely ignores* "Management's Assertions" in PwC's Reports. PwC's own reports confirm that the auditor had access and communicated with management, its own reports confirm that. Only with discovery will Plaintiffs know the extent of these communications and how they colored PwC's perspective or created PwC's willingness to prepare false and misleading audit reports. Notably, PwC is

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currently cooperating with the FTC and has compiled and produced documents in connection with the FTC's investigation which are the subject of Plaintiffs' Motion to Compel. [D.I. # 66.]

The Amended Complaint raises a sufficient inference based on the factual allegations (including its knowledge of the assertions in the 2015 article and use of sub-standard auditing methodologies) to conceal the Company's controls over privacy were inadequate.[26] Based on the well-pled allegations in the Amended Complaint against PwC, it is at least conceivable for this Court to infer that PwC was knowingly complicit in the concealment of Facebook's illegal data sharing. Thus, Plaintiffs have stated a viable aiding-and-abetting claim.

V. PLAINTIFFS' ACTION SHOULD PROCEED TO DISCOVERY

Upon the denial of their motion to dismiss, Facebook Defendants seek to stay this action for an unlimited number of years until the FTC investigation, federal securities and consumer cases are all resolved because Count VI in the

[26] Had PwC's audit included all "integral component[s]," Facebook Defendants would have been forced to explain the ongoing misappropriation of the information of 87 million users, ¶170, and why certain whitelist companies and "integration partners" were permitted to circumvent the Company's privacy and data policies to collect private user information, ¶¶250-60. Perhaps this is why Terrell McSweeney, a former commissioner at the FTC, explained that "it's a struggle to make sure third-party assessments are truly independent." ¶337 n.160.

Amended Complaint seeks contribution and indemnification. MTD at 53. The Court should reject this request.

Courts have the discretion to grant a stay where the moving party has shown overwhelming hardship or inconvenience would result absent a stay. *In re Molycorp, Inc. S'holder Deriv. Litig.*, 2014 WL 1891384, at *4 (Del. Ch. May 12, 2014) (citing *Adirondack GP, Inc. v. Am. Power Corp.*, 1996 WL 684376, at *6 (Del. Ch. Nov. 13, 1996)); *see Ryan v. Gifford*, 918 A.2d at 349. Such a showing has not been made here.

A. STAYING THIS LITIGATION WOULD UNDERMINE DELAWARE'S STRONG INTERESTS IN ADJUDICATING CORPORATE GOVERNANCE MATTERS AND SEVERELY PREJUDICE SHAREHOLDERS

Delaware courts have a "strong interest in promptly, uniformly, and authoritatively deciding corporate governance disputes of Delaware corporations . . . ." *Molycorp*, 2014 WL 1891384, at *5; *Brandin v. Deason*, 941 A.2d 1020, 1024 (Del. Ch. 2007) (explaining, "Delaware courts have a sizable interest in resolving [] novel issues to promote uniformity and clarity in the law that governs a great number of corporations"). This is because corporate governance disputes often raise Delaware interests that are "so compelling" that the court must "rationally conclude" against the stay. *Id*. Delaware's "strong interest" is diminished only if

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the *primary* corporate governance claim is for indemnification of a purported securities law violation. *Id.*

The thrust of the Amended Complaint is not indemnification, but rather to address the mismanagement and corporate governance of a controlled company that has no independent oversight. *In re Citigroup Inc.*, 964 A.2d at 118 (acknowledging "important issues regarding the standards governing directors and officers of Delaware corporations" and that Delaware "has an ongoing interest in applying [its] law to director conduct").

Plaintiffs will be litigating the duties of officers and directors of data companies and privacy, and seeking to make changes to Facebook's corporate governance, changes that are needed as soon as practicable. As such, corporate governance and the improvements needed are not the focus of, nor will they conflict with decisions made or relief sought in the securities or consumer actions.

Nor will the resolution of the corporate governance issues in this case hinge on a finding that federal securities laws were violated. The Amended Complaint does not directly seek indemnification for violations of federal or state securities laws, but even if it did, adjudication of this portion of the indemnification claim will not resolve Plaintiffs' corporate governance claims which are novel in several

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respects.[27] Plaintiffs seek to ensure that the mismanagement at issue is not repeated. Thus, this action will continue even if the contribution and indemnification claim disappear.[28] *Id*.

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[27] *See, e.g.*, *Molycorp*, 2014 WL 1891384, at *6-7 (lifting the stay even though the facts alleged "partially overlapped with those of the Federal Securities Action, [because] the allegations at the heart of the Proposed Amended Complaint . . . implicate an evolving and important question of Delaware corporate law . . ."); *In re China Agritech, Inc. S'holder Deriv. Litig.,* 2013 WL 2181514, at *27 (Del. Ch. May 21, 2013*)* (denying stay because the derivative action was not "primarily an indemnification-oriented action"); *Dias v. Purches*, 2012 WL 689160, at *2 (Del. Ch. Mar. 5, 2012) (denying stay in a stockholder action due to "the interest of this state in the behavior of fiduciaries for its corporate citizens. . . ."); *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 117 (Del. Ch. 2009) (denying stay even though there was "some overlap" between the two actions because the derivative Delaware case "raises important issues regarding the standards governing directors and officers of Delaware corporations, and Delaware has an ongoing interest in applying our law to director conduct in the context of current market conditions—conditions which change rapidly and pose new challenges for directors and officers of Delaware corporations"); *Ryan*, 918 A.2d at 351 (denying stay because the California action would *not* render the Delaware action moot, and Delaware courts have a substantial interest in determining issues pertaining to the scope of "Delaware's common law fiduciary duties"); *Biondi v. Scrushy*, 820 A.2d 1148, 1150 (Del. Ch. 2003) (denying stay because the derivative complaint implicated duty of loyalty allegations not presented in the securities litigation) *aff'd sub nom. In re HealthSouth Corp. S'holder Litig.*, 847 A.2d 1121 (Del. 2004).

[28] All the cases to which Facebook Defendants cite confirm this point. *See e.g.*, *In re Twitter, Inc. S'holder Deriv. Litig.*, 2018 WL 3536085, at *4 (D. Del. July 23, 2018) (granting stay where "Plaintiffs generally [sought] to shift potential corporate losses in the Securities Action to individual directors and officers in the Derivative Action") *rep't and rec. adopted sub nom.* 2018 WL 4326986 (D. Del. Sept. 10, 2018); *In re Insys Therapeutics Inc. Deriv. Litig.*, 2017 WL 5953515, at *3 (Del. Ch. Nov. 30, 2017) (granting the stay where the harm from the class action settlements would not be fully known until the security class actions were resolved); *In re Duke Energy Corp. Coal Ash Deriv. Litig.*, 2015 WL 5135066, at

Defending "simultaneous lawsuits with closely related factual underpinnings but where neither the claims nor the theories of liabilities overlap cannot be said to be unfairly prejudicial; to a certain extent, it may be an inherent risk of being a director of a publicly traded Delaware corporation." *Molycorp,* 2014 WL 1891384, at *7. Plaintiffs allegations "for breaches of fiduciary duty" do not "implicate the same practical considerations in the Court's calculus of whether to grant a stay," *Molycorp,* 2014 WL 1891384, at *5, because the claims will exist even if the related litigations are dismissed and because the issues raised in this action are novel and not covered in the other actions. *Ryan,* 918 A.2d at 350-51.

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*2 (Del. Ch. Aug. 31, 2015) (granting the stay because the determination of corporate liability in the related action would "facilitate processing of the derivative action," but limiting the stay to three months because a longer stay is unfair and prejudicial); Trans. of Oral Arg., *Hays v. Dvorak,* 2014 WL 7640981 (Del. Ch. Dec. 15, 2014) (granting stay pending Federal Circuit appeal where "the central issue of damages turns on the existence and the amount of the judgment [defendant] may have to pay"); Tran. of Oral Arg., *In re Molycorp, Inc. S'holder Deriv. Litig.*, 2013 WL 3818576 (Del. Ch. May 14, 2013) (granting stay where the outcome depended on "the Colorado action", *but see Molycorp,* 2014 WL 1891384, at *6, lifting the stay after plaintiff filed an amended complaint that raised independent breach of fiduciary duty claims); *In re Diamond Foods, Inc. Deriv. Litig.*, 2013 WL 755673, at *2 (Del. Ch. Feb. 28, 2013) (granting stay where plaintiff sought indemnification pending the outcome of related securities litigation); *see also In re STEC, Inc. Deriv. Litig.*, 2012 WL 8978155, at *8 (C.D. Cal. Jan. 11, 2012) (granting stay because the relief requested depended on the outcome of the federal securities class action); *In re Groupon Deriv. Litig.*, 882 F. Supp. 2d 1043, 1049 (N.D. Ill. 2012) (granting stay pending resolution of the motion to dismiss in the securities action because doing so would "significantly simplify the central issue in the derivative case" and the short stay would not be unduly prejudicial to plaintiffs).

There are many governance issues in this case, including whether one person should have so much power and control over a Company that can do so much harm to people and societies globally. Also at issue is whether the Facebook Defendants violated their fiduciary duties in how they conducted themselves. This case may also determine important contours of how officers and directors should manage and oversee privacy compliance when it comes to big data. ¶263. The claims are inextricably intertwined with the rise of the "information economy," which has forced courts, shareholders, and corporations to address novel questions about the duties of officers and directors to protect digital information and assets. Thus, in this case, the court must assess both corporate governance issues pertaining to affirmative corporate actions– here, Facebook Defendants' authorization of "whitelist" companies and "integration partners" to access user PII without user consent and in direct violation of the Company's data use and user privacy policies– as well as corporate inaction, such as allegations of inadequate oversight, reporting, and controls. ¶¶67-77. The case also uniquely raises more traditional issues of corporate governance, such as proxy disclosure requirements, ¶¶417-22, and claims of insider-trading, ¶¶423-28.

The fact that the FTC investigation and related cases rely on or pertain to similar underlying facts does not mean that there are sufficient practical

considerations favoring a stay. *Molycorp,* 2014 WL 1891384, at *5. Unlike the FTC investigation and related actions, only this case seeks an "extraordinary injunction ordering [] emergency measures" that require Facebook to adopt policies and amend the bylaws to "require the Chair of the Board to be an independent member of the Board and the roles of Chair and CEO be split," and "initiat[e] and adopt[] a recapitalization plan for all outstanding stock to have one vote per share. . . for the common good of all shareholders. . . ." ¶3. Such relief is needed now, and a limitless stay, like the one requested by Facebook Defendants, will cause harm to shareholders who want changes to the corporate governance of Facebook immediately. Just recently a coalition of four States sent Facebook's Board another proposal "to make the role of Board Chair an independent position . . . [given] Facebook missing, or mishandling a number of severe controversies" in advance of the 2019 annual shareholder meeting. The Amended Complaint seeks this and other needed equitable relief. Am. Compl. at 174-176. Therefore a limitless stay will delay needed change and improvements. Because these unique and novel allegations and the relief sought may only be raised and obtained in a Delaware derivative action, the outcome of which is not dependent upon the amount of the FTC fine or consumer case, "the current action is the dog, not the tail" and the stay should be rejected. *China Agritech*, 2013 WL 2181514, at *27.

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The stay will be especially prejudicial since in reaching the analysis, the Court will have concluded either that the Board is dominated and controlled by Zuckerberg and/or faces a substantial likelihood of personal liability for their wrongdoing. Since the majority of directors are the same (and officers), a stay would effectively endorse the wrongdoers continued control of Facebook. *Cf. In re Insys Therapeutics Inc.*, 2017 WL 5953515, at *3 (prejudice minimal where the board's "size and composition have changed significantly since the filing of the Complaint, and both the CEO and CFO have been replaced").

B. STAY WILL POSTPONE THE USE OF, NOT PRESERVE, JUDICIAL RESOURCES AND SOME REASONABLE COORDINATION WILL ADDRESS CONCERNS OF DUPLICATION

Facebook Defendants assert that a stay is needed to "preserve judicial resources and reduce the litigation burden on the parties and the court" and avoid duplication of efforts and a risk of inconsistent findings between this Court and the courts adjudicating the federal securities and consumer cases. MTD at 55.

A stay is not appropriate where, as here, liability under Delaware law will be adjudicated entirely "separate from, and not contingent on, a finding of liability" in the federal securities and consumer actions. *Molycorp*, 2014 WL 1891384, at *7. *Cf. Brudno*, 2003 WL 1874750, at *5 (explaining, judicial efficiency favors a stay where "the overwhelming thrust of the Delaware Action complaint is a demand for

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indemnification largely for harm to be incurred by [Facebook Defendants] in the Federal Securities Action.").

Since Plaintiffs raise significant corporate governance issues — that are not being adjudicated in other matters — the final adjudication of the federal securities and consumer actions will not resolve, or even help to resolve, many issues raised in the Amended Complaint. It may to some extent resolve some damages questions or assist in certain findings of fact, but a limitless stay will not save judicial resources, it will simply postpone the use of those resources. The fact that there will be "some overlap" with other actions that "arise[] out of the same nucleus of operative fact" does not justify the unreasonable delay sought here. *In re Citigroup Inc.*, 964 A.2d at 118; *see also Molycorp*, 2014 WL 1891384, at *5-7.

Moreover, if the mere risk of a conflicting decision or the mere existence of a securities or consumer proceeding were enough to warrant a stay, then nearly every case in Delaware would be stayed as there are often related and parallel cases proceeding in other jurisdictions. As discussed above, this action is principally concerned with novel and critical issues of Delaware corporate governance not raised or related to the outcome of either the federal securities or consumer actions. Given the distinct issues presented, neither related action is likely to cause conflicting decisions with any order of this Court. *Ryan*, 918 A.2d at 350; *see also*

In re Citigroup Inc., 964 A.2d at 119. Should either case be dismissed, the impact on this litigation would be *de minimis*. *Ryan*, 918 A.2d at 351. However, even in cases where overlapping factual issue exist– such as whether false and misleading statements were made, parties can limit inconsistencies under principles of judicial deference, full faith and credit, preclusion and similar assertions and defenses.

Finally, appreciating the burdens of discovery, Delaware courts have prudently ordered that, "in lieu of a stay, the better course is to require coordinated discovery on overlapping issues." *China Agritech*, 2013 WL 2181514, at *27. Plaintiffs would be willing to agree to some discovery coordination on an overlapping issue where doing so would be efficient and result in no unfairness or prejudice.

C. PROCEEDING WITH THIS LITIGATION WILL NOT RESULT IN *OVERWHELMING* HARDSHIP AND INCONVENIENCE

Facebook Defendants must show that absent a stay, *overwhelming* hardship and inconvenience would result. *Ryan*, 918 A.2d at 351. Their entire hardship argument boils down to this: if the case proceeds, Plaintiffs, on behalf of the Company, would seek to prove that the Board violated securities laws, consumer protection laws, and the FTC Consent Decree, while, simultaneously, Facebook will be seeking to contest that in related litigation and in the FTC regulatory investigation. However, this is a distinction without a difference.

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Facebook Defendants will be asserting that Facebook did not mislead the FTC or the United States government, their users, and investors in this action as well as the FTC investigation, and the consumer and federal securities suits. In other words, Facebook will not be forced to take a conflicting position as a result of its posture in the derivative suit. Nor will a finding that the Directors Defendants and Officer Defendants breached their duty of candor and disclosure necessarily translate into securities fraud. The claims are different, the standards are different, and many factual and legal issues that matter in one case, matter little in the other.

There is simply nothing particularly hard, unusual or overwhelming about litigating this derivative action simultaneously with the other actions or while the FTC investigation is pending. Delaware courts routinely recognize that, "[a]s the circumstances here demonstrate, it is conceivable that the directors and stockholders of a corporation may be defendants in two simultaneous lawsuits with closely related factual underpinnings but where neither the claims nor the theories of liabilities overlap." *Molycorp*, 2014 WL 1891384, at *7. In those situations, "[d]efending these two actions at the same time cannot be said to be unfairly prejudicial; to a certain extent, it may be an inherent risk of being a director of a publicly traded Delaware corporation." *Id.* This is because in a "representative

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lawsuit" the court's "paramount interest" is "ensuring that a corporation's stockholders receive 'fair and consistent enforcement of their rights under the laws governing the corporation.'" *Brandin v. Deason*, 941 A.2d at 1023–24 (quoting *In re Topps Co. S'holder Litig.*, 924 A.2d 951, 953 (Del. Ch. 2007)). *See also China Agritech*, 2013 WL 2181514, at *27 (denying stay as "prejudicial" where the litigation is not "primarily an indemnification-oriented action" and "the securities actions do[es] not appear to be moving forward actively"). *Cf. In re Duke Energy Corp.*, 2015 WL 5135066, at *1 (granting the stay but limiting it to three months because "it would be unfair to the Plaintiffs, and the Company's shareholders . . . to wait [longer].").

Finally, Facebook Defendants seek to stay the momentum in this action given Plaintiffs' history of vigorous prosecution. Plaintiff Sbriglio moved to intervene in the parallel federal derivative suit filed in California federal court when Facebook Defendants were being unclear about their position on whether they intended to waive Delaware as the proper forum under Facebook's Certificate of Incorporation. Plaintiffs were zealous in securing discovery from Facebook a mere three weeks into the case, after which Plaintiffs propounded party and non-party discovery and moved to compel Facebook Defendants and PwC when they refused to reproduce a set of the FTC that were already reviewed, compiled and

previously produced. Having shown their intent to vigorously pursue all aspects of this litigation, Facebook Defendants seek to stay such discovery and progress because it is their clear intention here to seek the advantages of the defendant-friendly procedures of the Private Securities Litigation Reform Act (the "PSLRA")– specifically, the heightened pleading requirements and initial discovery stay contained in 15 U.S.C § 78u-4(b)– onto purely state law claims that would otherwise not be subject to those provisions. Facebook Defendants should not be permitted to obstruct discovery, in the guise of a stay. "PSLRA and SLUSA were not intended to protect corporate management from shareholder derivative claims. Those are left to state law." *Romero v. Career Educ. Corp*., 2005 WL 1798042 at *3, n.16 (Del. Ch.) (quoting *City of Austin Police Ret. Sys. v. ITT Educ. Serves., Inc*., 2005 WL 280345 (S.D. Ind. Feb. 2, 2005)).

CONCLUSION

Plaintiffs respectfully move for an order denying Facebook Defendants' motion to dismiss or, in the alternative, stay this action (Dkt. #56) and PwC's motion to dismiss (Dkt. #55 and 57).

Respectfully Submitted,

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