

Chancery Tosses Class Suit Over \$3B Zimmer Biomet Cashout

By **Jeff Montgomery**

Law360 (August 26, 2021, 2:42 PM EDT) -- Delaware's Chancery Court has dismissed a derivative suit for damages from Zimmer Biomet Holdings Inc. directors, top officers and private equity investors related to a \$3 billion private equity cash-out and stock dive in 2016, finding that stockholders unjustifiably skipped an initial demand for action by the medical device maker's directors.

Vice Chancellor Lori W. Will concluded in dismissing the suit with prejudice Wednesday that the stockholders' failure to first put the allegations to the board — or show why it would have been futile — doomed claims that included breach of fiduciary duty, insider trading, unjust enrichment and breach of contract.

"There are no specific facts pleaded to support a reasonable inference that the directors acted in bad faith, intentionally concealed material information, knowingly facilitated insider trading, or deliberately ignored 'red flags,'" Vice Chancellor Will wrote. She said the company's charter protects board members against all but bad faith and intentional dereliction of fiduciary duties.

"In terms of disclosures, the plaintiffs cannot link what the Zimmer board knew before late 2016 to any material misstatements or omissions that the board was directly involved in issuing," the vice chancellor wrote.

The suit had leveled counts alleging breaches of fiduciary duty and unjust enrichment against two officers and 11 current or former directors of Zimmer Biomet, insider trading against two directors who held private equity seats on the board, aiding and abetting against the individual defendants and the private equity funds, and breach of contract against the funds.

A separate federal securities class suit that focused on some of the same allegedly undisclosed problems was settled in 2020 for \$50 million in Indiana federal court.

Much of the suit focused on compliance issues and purported company disclosure failures at a key Indiana plant where strong growth had been projected after a \$13.4 billion, mid-2015 merger between Zimmer Holdings and medical device maker Biomet Inc.

The suit claimed that ZBH's former and current directors and officers failed to disclose manufacturing quality and control problems at the Indiana site, despite internal audits launched after the U.S. Food and Drug Administration turned up "systemic" issues at other ZBH sites in the spring of 2016.

Absent from the complaint, Vice Chancellor Will found, was support for claims that two directors with ties to private equity investors tipped the private equity firms off to negative developments, or that the private equity interests exerted control over their board designates.

The PE companies involved — The Blackstone Group, Goldman Sachs Capital Partners, Kohlberg Kravis Roberts & Co. LP and TPG Global LLC — all sold off their investments in Zimmer Biomet for a total of \$3.3 billion between February and August 2016.

The final PE offering took place a month before the start of a critical FDA inspection that led to a hold on shipments from the Indiana site and three months before the agency's most critical report in November 2016.

"Despite having access to the relevant board minutes and materials," Vice Chancellor Will wrote, "the plaintiffs cannot link what the directors learned about continuing FDA compliance challenges with any materially misleading statements they were responsible for making."

A third-quarter report below expectations on Oct. 31, 2016, was followed by a 14% drop in the company's stock price, with the hold on shipments going unmentioned during an earnings call with investors, the vice chancellor said.

"The difficulty for the plaintiffs is an absence of pleaded facts implying bad faith on the part of the director defendants" in presentations on internal audits and FDA activities, the vice chancellor said. "The first time that the plaintiffs allege with particularity that the full board learned of the fallout from the North Campus inspection is at a December 16, 2016 board meeting, well after the exit of the PE investors and the stock drop."

ZBH's shares fell from \$122.55 on Oct. 30, 2016, to \$97.99. Most of the decline, however, took place weeks before the market was told of the Indiana plant troubles and holds on product shipments.

Much of the drop took place after the Oct. 31 earnings report that ZBH said revealed problems to the market.

"It is difficult to square these allegations with the plaintiffs' contention that the directors were engaging 'in a scheme to defraud Zimmer investors,'" the vice chancellor wrote.

Neither Zimmer Biomet nor a representative for the stockholders immediately replied to a request for comment.

The investors are represented by P. Bradford deLeeuw of deLeeuw Law LLC, Ricard A. Speirs and Christopher Lometti of Cohen Milstein Sellers & Toll PLLC, Robert C. Schubert and Willem F. Jonckheer of Schubert Jonckheer & Kolbe LLP and Kip B. Shuman, Rusty E. Glenn and Brett D. Stecker of Shuman Glenn & Stecker.

Zimmer Biomet and the current and former officers and directors are represented by John C. Barillare, Troy S. Brown and Laura Hughes McNally of Morgan Lewis & Bockius LLP.

KKR Biomet LLC, TPG Partners et al., Michael W. Michelson and Jeffrey K. Rhodes are represented by William M. Lafferty, Ryan D. Stottmann and Sabrina M. Hendershot of Morris Nichols Arshat & Tunnell LLP, Peter E. Kazanoff, Sara A. Ricciardi and Courtney G. Skarupski of Simpson Thacher & Bartlett LLP and

Daniel V. McCaughey, Erin Macgowan and Christian Reigstad of Ropes & Gray LLP.

The Goldman Sachs private equity affiliates are represented by Kevin G. Abrams and J. Peter Shindel Jr. of Abrams & Baylis LLP and Paul Vizcarrondo and John F. Lynch of Wachtell Lipton Rosen & Katz.

The Blackstone Capital Partners private equity affiliates are represented by Daniel A. Mason, Matthew D. Stachel, Andrew J. Ehrlich and Brette Tannenbaum of Paul Weiss Rifkind Wharton & Garrison LLP.

The case is In re: Zimmer Biomet Holdings Inc. Derivative Litigation, case number 2019-0455, in the Court of Chancery of the State of Delaware.

--Additional reporting by Rose Krebs, Emilie Ruscoe and Reenat Sinay. Editing by Alyssa Miller.

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