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Case No. 2019-0808-



**IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE**

BARBARA KAILAS, derivatively  
on Behalf of KRAFT HEINZ  
COMPANY,

Plaintiff,

vs.

3G CAPITAL INC., 3G GLOBAL  
FOOD HOLDINGS, LP, 3G  
GLOBAL FOOD HOLDINGS GP,  
LP, 3G CAPITAL PARTNERS, LP,  
3G CAPITAL PARTNERS III LP,  
3G CAPITAL PARTNERS, LTD.,  
HK 318 LP,

Defendants,

and

KRAFT HEINZ COMPANY,

Nominal Defendant.

C.A. No.:

**VERIFIED STOCKHOLDER DERIVATIVE COMPLAINT**

Plaintiff Barbara Kailas, derivatively, on behalf of Kraft Heinz Company (“Kraft Heinz” or the “Company”), alleges the following based upon information and belief as to the investigation conducted by her counsel, which included, among other things, a review of U.S. Securities and Exchange Commission (“SEC”) filings by Kraft Heinz and defendants, securities analyst reports, press releases, and other public statements issued by, or about, the Company. Plaintiff believes that

substantial additional evidentiary support will exist for the allegations set forth herein after a reasonable opportunity for discovery.

**I.**

**NATURE OF THE ACTION**

1. This is a shareholder derivative action brought on behalf of Kraft Heinz seeking to recover insider trading profits rightfully belonging to Kraft Heinz. Defendants (hereafter sometimes referred to as “3G” or the “Controlling Shareholder”) misused and misappropriated material non-public information about Kraft Heinz business operations and the value of its assets to sell \$1.2 billion of Kraft Heinz stock at an average price of \$59.47 per share in August 2018 and thereby avoid losses of over \$30 per share when Kraft Heinz revealed the extent to which its businesses and assets had been rapidly deteriorating.

2. The Controlling Shareholder has known since 2017, if not sooner, that the publicly reported values of Kraft Heinz goodwill and intangible assets were impaired and/or at risk for a near term material impairment charge and were thus overstated throughout 2018 and as a result Kraft Heinz stock price was artificially inflated during 2018.

3. As of December 2017, the Company showed \$44.8 billion in goodwill on its balance sheet, and approximately \$53.65 billion of “intangible assets” much of which was added as a result of the Kraft Heinz merger in 2015. By contrast, the

aggregate market value of Kraft Heinz's approximately 1.2 billion common shares outstanding, based on its average price in the fourth calendar quarter of 2017 of approximately 78 per share, was approximately \$93 billion. Goodwill and intangible assets together represented 87% of the Company assets in 2018. However, as early as May 2017, analysts were questioning the stated amount of goodwill and intangible assets the Company was reporting on its financial statements. Defendants knew that Kraft Heinz's declining results throughout 2017 and 2018 were the result of recognized trends in retail food consumer's preference and buying habits. Moreover, the Controlling Shareholder's relentless cost cutting since it acquired control of Kraft Heinz had caused a material underinvestment in the Kraft Heinz brand, which left Company's products at a competitive disadvantage versus better positioned competitors and niche brands and changing trends in consumer preferences. The foregoing led to permanent impairment of the Kraft Heinz brand value that should have been recognized earlier with write downs or other public disclosures.

4. Company officers, directors, and the Controlling Shareholder have known since at least early 2017 that powerful trends in the retail food and beverage business which were leading customers towards private label brands such as those offered by Amazon, Walmart and Costco. Those trends were (i) undermining sales growth of Company products; (ii) materially weakening the Company's leverage

over retailers for shelf space and promotional support; (iii) continuously weakening the Company's products pricing power in a materially changed competitive landscape for the Company's products in a permanent way, all of which posed an immediate and future threat to the Company's sales, margins and cash flows from units/products. This state of affairs, which continued unabated through 2017 and 2018, presented a material risk to Kraft Heinz earnings and cash flow and indicated that its goodwill and intangible assets had become permanently impaired and thus its valuations of those assets were materially overstated and would need to be materially written down.

5. The 3G Defendants, whose founders, partners and owners were key executive officers and directors of Kraft Heinz, took advantage of the artificially inflated price of Kraft Heinz in August 2018 and sold material amounts of Kraft Heinz stock based on material adverse non-public information. By selling, 3G avoided approximately \$600 million in losses realized when Kraft Heinz disclosed the permanent impairment of assets that occurred in 2018.

6. On February 21, 2019, after the stock market closed, Kraft Heinz announced that it had to write off almost 20% of its \$44 billion dollars in goodwill through an impairment charge and an additional impairment write down of close to 20% of the carrying amounts of certain intangible assets pertaining to its brands. At that time, the total impairment charges resulted in a reported net loss attributable

to common shareholders of \$12.6 billion and diluted loss per share of \$10.34 for the annual period ended December 31, 2018. The loss, and Kraft Heinz's excessive debt load relative to assets and earnings potential, pressured Kraft Heinz into a 36% reduction of its quarterly dividend to \$.04 per share from its \$0.0625 quarterly dividend. The decrease was designed to save the company \$1 billion a year.

7. This sudden and massive public disclosure of the asset impairment that had been occurring throughout 2018 was the inevitable result of Kraft Heinz declining results and was or should have been anticipated and disclosed by the Controlling Shareholder and its board designees.

8. At the same time, in February 2019, the Company publicly disclosed for the first time that Kraft Heinz had received a subpoena from the SEC in October 2018 in relation to accounting associated with the Company's procurement function. As a result of the SEC investigation, the Company conducted its own internal investigation, which resulted in the Company recording a \$25 million increase to costs of products sold, damaging the Company's credibility and provoking fears of future accounting adjustments.

9. As a result of the February 19, 2019 disclosures, the price of Kraft Heinz common stock declined over 27% from \$48.18 per share on the day before the announcement to \$34.95 per share, erasing more than \$16 billion of the Company's market capitalization. Since February 19, 2019 it has traded down

below \$30 per share.

10. In March 2019, Kraft Heinz also disclosed the SEC was investigating Kraft Heinz goodwill and intangible asset valuations and impairments.

11. This shareholder derivative action seeks to recover for the Company the insider trading profits earned by 3G.

12. Demand is excused in this action because a majority of the members of the Company's Board are not now disinterested (even after announced changes to its Board took place in June and July 2019), and cannot act with the requisite independence because they are employed by, associated with, or beholden to, Kraft Heinz and/or 3G Capital (which has control of Kraft Heinz through its ownership stake and representation on Kraft Heinz board of directors and has exercised its control power). Non 3G-affiliated directors employed by Kraft Heinz (Cahill and Zoghbi) cannot exercise independent judgment. The Berkshire Hathaway designated directors on the Kraft Heinz board (Abel and Cool) cannot exercise independent judgment on whether to sue 3G to recover for Kraft Heinz over \$600 million of ill-gotten insider profits because Warren Buffett has committed Berkshire Hathaway to several large co-investments with 3G Capital and has publicly stated his desire for Berkshire Hathaway to do more investments with 3G Capital even after 3G's flawed, selfish stewardship of 3G was revealed in February 2019. The other directors (Pope, Jackson, Dewan) cannot exercise independent

judgment because they face a substantial likelihood of liability in other pending or potential shareholder class actions and/or derivative actions involving, or which would involve, some of the same issues raised herein.

## II.

### JURISDICTION AND VENUE

13. Nominal Defendant Kraft Heinz is a Delaware corporation and governed by the laws of the State of Delaware and the decisional laws of this Court. This Court has jurisdiction over Kraft Heinz under 10 Del. C. § 3111.

14. The Defendants have consented to jurisdiction in this Court. Nominal Defendant has a venue provision in its By-Laws which requires its shareholders to bring suits on behalf of the Company in Delaware Chancery Court. The action is not a collusive one to confer jurisdiction that the Court would otherwise lack. As alleged herein, demand would have been futile.

## III.

### PARTIES

#### A. Plaintiff

15. As set forth in the verification accompanying this complaint, Plaintiff is and was a beneficial owner of Kraft Heinz continuously from at least throughout 2017 through the present. Plaintiff will fairly and adequately represent the interests of the shareholders who are similarly situated in enforcing the right of the

corporation.

**B. Nominal Defendant**

16. Nominal Defendant Kraft Heinz is one of the largest food and beverage companies worldwide. The Company was formed in 2015 when Kraft Foods Group, Inc. (“Kraft”) merged with H.J. Heinz Holding Corporation (“Heinz”). The Company maintains its principal executive offices in Pittsburgh, Pennsylvania and its common stock is listed and trades on the NASDAQ under the ticker symbol “KHC.” As of 2015 and through the present, it was/is controlled by Defendants through their stock ownership, and shareholder agreements with Berkshire Hathaway and through their control of the Company’s Board.

**C. Defendants**

17. Defendant 3G Global Food Holding, LP (“3G Global”) is a private equity firm specializing in buyout investments in brands and businesses in the retail and consumer sectors. During the relevant time period of 2017 - 2019, 3G Global, together with its affiliates the other named Defendants - - had access to material adverse non-public information about Kraft Heinz.

18. Defendants 3G Capital, Inc., 3G Capital Partners II, LP, 3G Capital Partner, Ltd., 3G Capital Partners LP, 3G Global Food Holdings GP, LP and HK 318 LP are all affiliates of Defendant 3G Global Food Holdings, LP (collectively, “3G” or “3G Defendants”).

19. The 3G Defendants sold \$1.2 billion in Kraft Heinz stock (over 13% of its investment in Kraft Heinz expressed in dollars), and thereby avoided over \$600 million in losses when Kraft Heinz stock price collapsed upon the February 2019 announcement of the permanent impairment of Kraft Heinz assets and the need to restate prior financial statements.

#### IV.

#### DEMAND FUTILITY

20. At present, the Company's Board of Directors consists of eleven members.

21. Demand would be futile in this action because at least majority of the members of the Board cannot exercise independent or disinterested business judgment in responding to a demand to sue for the reasons set forth herein.

22. A majority (at least seven of eleven) of the Company's board is employed by Kraft Heinz (Zoghbi, Cahill) or 3G Capital (Behring, Lemann, Castro Neves) or Berkshire Hathaway (Abel, Cool) and thus incapable of rendering independent or disinterested judgment with respect to a suit against 3G.

#### **A. A Majority Of The Current Directors Cannot Objectively Consider A Demand To Sue 3G For Insider Trading**

##### **1. The Current Board**

23. Alexandre Behring ("Behring") was appointed Chairman of the Kraft Heinz board of directors effective July 2015 and previously served as Chairman of

the Heinz board from June 2013 to July 2015. Mr. Behring is a co-founder of 3G Capital, a global investment firm, and has been its managing partner and a director since 2004. Since 2014 he has served as the Executive Chairman of the Board of Restaurant Brands International, Inc. a major food service conglomerate owned by Defendants. He is also director of Anheuser-Busch Inbev SA/NV, a global brewer wherein Defendants own, directly or indirectly, approximately 40% of the shares since April 2014. 3G maintains significant investments in, and controls, both Restaurant Brands International and InBev.

24. Jorge Paulo Lemann (“Lemann”) was appointed to the Kraft Heinz board of directors effective July 2015 and previously served on the Heinz board from June 2013 to July 2015. Mr. Lemann is a co-founder of 3G Capital. Mr. Lemann was formerly a director of Anheuser-Busch InBev. He is a member of both the Compensation Committee and Nominating and Corporate Governance Committee.

25. Alexandre Van Damme (“Van Damme”) has been a Kraft Heinz director since April 2018 and has served as a member of the board of Restaurant Brands International since December 2014 which is controlled by 3G. Van Damme has been publicly described as “close” to 3G’s founders. He previously served on the board of Burger King Worldwide, Inc. (now part of Restaurant Brands) and its predecessor from December 2011 to December 2014. Van Damme has served as

a member of the board of directors of Anheuser-Busch InBev since 1992 which 3G also controls as described above.

26. George Zoghbi (“Zoghbi”) is a director and has been since April 2018 and has been a full-time paid “Special Advisor” to the Company working with the Kraft Heinz directors and the 3G partners who are Kraft Heinz Executive Officers since October 2017. In its 2018 Notice of Annual Meeting of Shareholders, Kraft Heinz admitted that Zoghbi is not “independent.”

27. John T. Cahill (“Cahill”) was appointed Vice Chairman of the Kraft Heinz board of directors effective July 2015. Cahill was until July 1, 2019 a paid “consultant” to Kraft Heinz since 2017 and was paid approximately \$700,000 per year by Kraft Heinz. In its 2018 Notice of Annual Meeting of Shareholders, Kraft Heinz admitted that Cahill is not “independent.”

28. Gregory Abel (“Abel”) was appointed to the Kraft Heinz board of directors effective July 2015 and previously served on the Heinz board from June 2013 to July 2015. He is the CEO of Berkshire Hathaway Energy. In January 2018, Mr. Abel was elected to the Board of Directors of Berkshire Hathaway, a diversified holding company, and appointed as its Vice Chairman, Non-Insurance Business Operations. Abel is Berkshire Hathaway’s and Warren Buffet’s employee.

29. Tracy Britt Cool (“Cool”) was appointed to the Kraft Heinz board of directors effective July 2015 and previously served on the Heinz board from June 2013 to July 2015. Ms. Cool started her career at Berkshire Hathaway as Mr. Buffet’s financial assistant. Five years later at age 30, she was named the Chief Executive Officer of The Pampered Chef (a Berkshire Hathaway company), a direct seller of high-quality cooking tools. Ms. Cool is currently is a director of three Berkshire Hathaway Companies: Benjamin Moore & Co., a leading manufacturer and retailer of paints and architectural coatings (since June 2012), Larson-Juhl, a manufacturer and distributor of wood and metal framing products (since January 2012), and Oriental Trading Company, a direct merchant of party suppliers, arts and crafts, toys and novelties (since November 2012).

30. Feroz Dewan (“Dewan”) was appointed to the Kraft Heinz board of directors effective October 2016 and is a member of the Audit Committee. He is the CEO of Arena Holdings Management LLC, an investment holding company.

31. Jeanne P. Jackson (“Jackson”) was appointed to the Kraft Heinz board of directors effective July 2015 and previously served on the Kraft board from October 2012 to July 2015. She is currently a member of both the Compensation and Nominating and Corporate Governance Committee. Ms. Jackson is Founder and Chief Executive Officer of MSP Capital, a private equity and investment

company. She currently serves as a director of Delta Airlines, Inc. and McDonald's Corporation and was formerly a director of Motorola Mobility Holdings, Inc.

32. John C. Pope ("Pope") was appointed to the Kraft Heinz board of directors effective July 2015 and previously served on the Kraft board from August 2012 to July 2015. He is the Chair of the Audit Committee and a member of the Nominating and Corporate Governance Committee. Mr. Pope has served as Chairman of PFI Group, LLC, a financial management firm, since 1994. Mr. Pope also serves as Chairman of the Board of R.R. Donnelley and Sons Co., a printing company, since May 2014; and as a director of Talgo S.A., a railcar manufacturer, since March 2015; and as a director of Waste Management, Inc., a provider of comprehensive waste management services, since 1997.

33. Joao M. Castro-Neves was appointed director of Kraft Heinz in June 2019. He has been a partner with 3G Capital since July 2018. Prior thereto he has served in executive officer positions at other 3G controlled companies since at least 2015.

## **2. 3G Dominates Kraft Heinz' Board**

34. 3G has dominated and controlled Kraft Heinz and its board and continues to do so. In May 2013, the New York Times, in an article on Kraft Heinz discussing the operation of the company noted "3G is closely held and their partner – including Kraft Heinz's chief executive officer, Bernardo Hees – takes a hands-

on approach to managing their investments.” “Bernando Hees of Kraft Heinz: New Mistakes Are Welcome,” The New York Times, May 3, 2018, David Gilles. It was reported in 2015 that Lemann, then 75, had “handed over daily operations of 3G to a handful of associates, including Behring.”

35. Since the merger, 3G has exercised a high degree of control over Kraft Heinz at executive levels and through the ranks. According to New York Times reporters, Julie Creswell and David Yaffee-Bellany:

Kraft personnel, including some with decades of experience, were replaced by 3G leadership, some of whom had virtually no experience in the consumer packaged goods industry. . .

The New York Times, “How 2 Great Brands Merged Into A Mess” September 24, 2019, B, P 1 (“NYT Article”).

36. 3G’s domination is further demonstrated by the executive level personnel changes that have occurred since the collapse of the Company’s stock price in February 2019, whereby 3G partners were installed in executive positions usually subject to board approval.

37. In February 2019, director Telles announced he would not stand for re-election as a director in 2019. The Board immediately announced that Daniel Schutz, a 3G partner since 2008, would be nominated for Telles’ board seat.

38. In April 2019, KHC's Board announced the appointment of Miguel Patricio as CEO to replace Bernardo Hees. Patricio had been Chief Marketing Officer at 3G controlled Anheuser-Busch InBev since 2012.

39. In June 2019, Castro-Neves was appointed to KHC's board. Castro-Neves had been a partner at 3G since July 2018 was a director of Restaurant Brands International controlled by 3G and was an officer at InBev since 1996.

40. In August 2019, 3G partner David Knopf was removed as KHC's CFO and was replaced by Paulo Basilio, a 3G partner since July 2012.

**3. The Berkshire Hathaway Designated Directors, Abel And Cool, Cannot Exercise Objective Judgment Whether To Sue 3G For Insider Trading**

41. The connections among 3G and Berkshire Hathaway and 3G founder and Warren Buffet are significant and demonstrate why the Berkshire Hathaway directors cannot objectively consider a demand to sue 3G.

(a) In 2013, 3G and Berkshire Hathaway teamed up to take Heinz private in a \$23 billion deal. In SEC filings, Kraft Heinz has admitted that Berkshire Hathaway and 3G have "substantial control" of Kraft Heinz and "may have conflicts of interests" between them and Kraft Heinz.

(b) In 2014 Berkshire Hathaway loaned 3G \$3 billion to finance Burger King's acquisition of Canadian restaurant chain Tim Horton's.

(c) In 2015, The New York Times quoted Warren Buffett about his 3G partners: “I knew they were wonderful going into the Heinz deal.” “In terms of ability, in terms of integrity, every aspect of it. 3G has been a perfect partner.” (See, “3G Capital, Warren Buffett’s Favorite Partner in Deals worth Billions.”) The author of the article noted that Berkshire Hathaway’s Warren Buffett and 3G’s founder, Jorge Paulo Lemann, have known each other for “decades” and “the two men have grown close.”

(d) Berkshire Hathaway Chairman Buffett has repeatedly expressed a desire and willingness to partner with 3G on more investments. That public posture, asserted repeatedly, compels the conclusion that Berkshire Hathaway affiliated Kraft Heinz directors will not take any action against 3G or its designated directors.

(1) On February 27, 2015, in his annual letter to shareholders Warren Buffett wrote about 3G:

Two years ago my friend, Jorge Paulo Lemann, asked Berkshire to join his 3G Capital group in the acquisition of Heinz. My affirmative response was a no brainer. I knew immediately that this partnership would work well from both a personal and financial standpoint. And it most definitely has.

....

We expect to partner with 3G in more activities . . . Our favored arrangement, however, will usually be to link up as a permanent equity partner (who in some cases, contributes to the financing

of the deal as well). Whatever the structure, we feel good when working with Jorge Paulo.

(2) In his 2016 letter to shareholders Mr. Buffett wrote about 3G and the Kraft Heinz mergers:

Jorge Paulo and his associates could not be better partners.

. . . We will also look for opportunities to partner with Jorge Paulo, either as a financing partner, as was the case when his group purchased Tim Horton's, or as a combined equity-and-financing partner, as at Heinz.

(e) On March 7, 2017, The New York times quoted Warren Buffett praising 3G: "Jorge Paulo and his associates could not be better partners." The New York Times, Deal Professor, "Can 3G Capital Keep Thriving On Acquisitions and Cost Cutting?" Steven David Solomon.

(f) Even after Kraft Heinz stock price fell to approximately \$30 per share after the February 2019 disclosures of material brand value erosion and internal control issues and SEC subpoenas, Buffett defended 3G founder Lemann publicly, calling him an "outstanding human being" and saying he would "absolutely continue doing business with him."

42. Further, notwithstanding that Berkshire Hathaway itself did not sell any stock along with 3G in August 2010, Berkshire Hathaway nonetheless is exposed to a substantial likelihood of liability. As a result of the relationships between and among Berkshire Hathaway and 3G, evidence which could be

adduced in this case may establish that Berkshire Hathaway and 3G may be deemed to be a “group” for the purpose of Section 13(d) of the Exchange Act. If Berkshire Hathaway and 3G were deemed a “group” (because of their agreement to acquire, hold and/or dispose of Kraft Heinz stock), Berkshire Hathaway could be liable for some or all the insider profits owed to Kraft Heinz. Accordingly, The Berkshire Hathaway affiliated directors on the board, namely, Abel and Cool, are incapable of rendering independent judgment with respect to a suit against 3G.

**4. Directors Cahill And Zoghbi Are, As Admitted By The Company, “Not Independent”**

43. Directors Cahill and Zoghbi are paid consultants to Kraft Heinz whom the Company admitted in Proxy Statements are not “independent.”

**5. Directors Not Affiliated With 3G, Kraft or Berkshire Hathaway Face Substantial Likelihood Of Personal Liability**

44. Demand is further excused because all Directors face a substantial likelihood of liability in other derivative actions arising out of non-disclosure of the impairment of assets. Furthermore, Kraft Heinz directors Pope, Devan, Jackson and Van Damme and other directors serving in June 2018 potentially face substantial liability under Section 11 of the Securities Act of 1933 for signing materially misleading and false Registration Statements with respect Kraft Heinz’ June 2018 billion dollar bond offering. Under that statute, the Kraft Heinz directors upon whom demand would be made here have limited defenses to potential

liability. Accordingly, these directors would not authorize a suit that could uncover facts exposing them to Section 11 liability potentially for hundreds of millions of dollars.

**B. Duties Owed By 3G To Kraft Heinz**

45. Under long established Delaware law, controlling shareholders such as 3G are company fiduciaries who stand in a trustee-like position vis a vis the Company. As such and for the reasons set forth below, 3G was under a duty to abstain from trading in Kraft Heinz stock while it was in possession of material, non-public adverse information about the Company.

46. 3G is an entity which operates through its partners and employees. 3G's "knowledge" is the sum total of its partners knowledge. 3G had access to adverse material non-public information through the officers and directors who are affiliated with 3G. The 3G partners who were/are Kraft Heinz director and/or executive officers are/were:

(a) Bernardo Hees ("Hees") is a 3G partner, and was at all relevant times, Kraft Heinz's Chief Executive Officer.

(b) Paulo Basilio ("Basilio"), a 3G partner, served as Kraft Heinz's Executive Vice President ("EVP") and Chief Financial Officer ("CFO") from its formation in July 2015 until October 1, 2017, when he was appointed as the Company's Zone President of U.S business.

(c) David Knopf (“Knopf”) a 3G partner joined Kraft Heinz upon its formation in July 2015, initially serving as Vice President of Finance, Head of Global Budget & Business Planning, Zero-Based Budgeting, and Financial & Strategic Planning. On October 1, 2017, Knopf assumed Defendant Basilio’s CFO responsibilities when Basilio was appointed as the Company’s EVP and CFO.

(d) Directors Telles, Behring and Lemann were partners of 3G at all relevant times.

47. The Kraft Heinz Employee Code of Conduct (“Code of Conduct”) contains prohibitions, restrictions and guidelines on insider trading that are applicable to all directors:

Never buy or sell Company securities . . . when you possess inside information or during trading blackout periods.

....

Don’t disclose inside information to anyone outside the Company (including family members of friends) for any reason. If that person uses this information to trade in the stock market, you are legally responsible for tipping that person.

48. The Code of Conduct specifically addressed “directors” and “waivers” of compliance with the Code:

#### WAIVERS

While all of us are expected to uphold our Code at all times, the Company understands that, in rare circumstances, a waiver of the Code might be necessary. Such waivers are granted on a case by case basis and are only appropriate when strict

adherence to the Code could cause significant hardship.

Any waiver or amendment of this Code for the Chief Executive Officer, General Counsel, Chief Financial Officer, Global Controller, other senior financial or executive officers or directors must be approved by the Board of Directors.

49. All 3G's designated directors were expected to adhere to the Code of Conduct which they were required to sign and affirm, and which included, in part the following provisions:

**Conflicts of Interest**

Maintaining its loyalty to the Company, avoiding any situations that create or appear to create a conflict of interest and providing notice to the Chair of any actual or apparent conflict of interest.

....

**Corporate Opportunity**

Refraining from using the Company's property, information or position for personal gain.

....

**Proprietary Information**

Maintaining the confidentiality of the Company's proprietary information, except when the Company authorizes disclosures or as required by laws, regulations, or legal proceedings.

50. Defendant 3G would have known of the Company's Code of Conduct and policies about use of inside information as it related to 3G's sale of Company stock because 3G partners (and Company directors) Telles, Behring and Lemann

were members of the Company's Governance Committee in 2015, 2016 and/or 2017. One of the areas of responsibility of the Governance Committee was advising the full board about "related person transactions" and monitoring directors' compliance with Kraft Heinz stock ownership guidelines.

V.

**SUBSTANTIVE ALLEGATIONS**

**A. Background**

51. In February 2013, the public company, H. J. Heinz Company, was acquired by 3G for \$23 billion. At that time, Heinz was controlled by Berkshire Hathaway Inc. and 3G Capital, who together beneficially owned approximately 50% of Heinz.

52. 3G Capital is a Brazilian-American, private equity firm known for achieving significant cost reduction in companies under its management by, among other things, implementing zero-based budgeting at its portfolio companies. Zero-based budgeting is a process whereby budgets are determined only after all anticipated expenses in a given period have been justified as being necessary, irrespective of what the budget may have been in a prior period.

53. On March 25, 2015, Kraft announced a \$35 billion merger with Heinz, arranged by Berkshire Hathaway and 3G Capital. The companies heralded the "significant synergy opportunities" that would result from "combining Kraft's

brands with Heinz's international platform" while promising to be "fully committed to maintaining an investment grade rating." The resulting company was expected to have a market value of over \$80 billion.

54. Kraft Heinz became one of the largest food and beverage companies in the world with a portfolio of mature brands that include *Heinz, Kraft, ABC, Oscar Mayer, Philadelphia, Classico, Planters, Velveeta, Jell-O, Lunchables, Kool Aid, Maxwell House, Capri Sun, Smart-Ones and Ore-Ida*. The Kraft businesses manufacture and market food and beverage products, including cheese, meats, refreshment beverages, coffee, packaged dinners, refrigerated meals, snack nuts, dressings, and other grocery products, primarily in the U.S. and Canada. The Heinz businesses manufacture and market an extensive line of food products, including ketchup, condiments and sauces, frozen food, soups, beans and pasta meals, infant nutrition and other food products.

55. After the Merger, Kraft Heinz was led by 3G executives and partners. Hees, a partner at 3G Capital since July 2010, became CEO of Kraft Heinz upon the closing of the Merger after serving as CEO of Heinz since its formation in June 2013. Likewise, Basilio, a partner of 3G Capital since July 2012, became EVP and CFO of Kraft Heinz upon the closing of the Merger after previously serving as CFO of Heinz since its formation in June 2013 and then became U.S. zone President in 2017. On October 1, 2017, Knopf, then only 29 years of age, assumed

Defendant Basilio's responsibilities and became EVP and CFO of Kraft Heinz. Knopf has been a partner of 3G Capital since July 2012 and held various roles at 3G Capital from 2013 to 2015.

**B. 3G's Access to Insider Company Financial Information**

56. 3G had access to and reviewed voluminous financial data about the Company. According to a NYT Article: "Managers and employees inside Kraft said they spend long hours and weekends after the deal closing gathering data on everything . . . those figures were stuffed into voluminous spreadsheets and given to 3G." *See* NYT September 24, 2019, Section B, Page 1 "How 2 Great Brands Merged Into A Mess."

57. 3G had access to Kraft Heinz financial information that showed declining metrics of Kraft Heinz assets such that Defendants could discern the near-certainty that a write down of asset values would be required to recognize the impairment in value these assets experienced over the previous 18 months. In 2018, 3G principals occupied nearly all of the Company's executive officer positions:

(a) Bernardo Hees, a 3G partner since July 2010 was the Company's CEO from 2015 to May 2018;

(b) Paulo Basilio, a 3G partner since June 2013 was the Company's CFO from 2015 through October 2017;

(c) David Knopf, a partner at 3G since 2015 was the Company's "Vice President of Finance, Head of Global Budget & Business Planning, Zero Based Budgeting and Financial and Strategic Planning from July 2015 until August 2016, and the Company's "Vice President, Category Head of Planters' Business" from August 2016 until September 2017.

58. 3G's access to the Company's most granular and sensitive inside information was also assured by the fact that from 2015 through 2016, a 3G partner and KHC director Behring was a member of KHC's board level "Operations and Strategy Committee." According to Kraft Heinz's 2016 and 2017 proxy statements, that Committee was described as follows:

The Board formed the Operations and Strategy Committee to assist it in overseeing and facilitating the development and implementation of our ongoing operations and corporate strategy. The Operations and Strategy Committee's responsibilities also include, among others, reviewing and making recommendations to the Board regarding

- our corporate strategy, integration plans, performance, and annual capital plan, as well as certain individual capital projects;
- the impact of external developments and factors, such as the changes in economic and market conditions, competition in the industry, environmental and safety regulations, federal, state and local regulations and technology, on our corporate strategy and its execution;
- identification of prospects and opportunities for corporate developments and growth initiatives, including

acquisitions, divestitures, joint ventures and strategic alliances; and

- implementation of our corporate strategy through corporate developments and growth initiatives, including acquisitions, divestitures, joint ventures and strategic alliances

**C. 3G's Cost Cutting Exacerbated Consumer Trends Undermining The Company's Asset Values**

59. Consistent with 3G's philosophy, Kraft Heinz adopted a series of cost reduction initiatives after the merger when integrating the operations of Kraft and Heinz. These cost-cutting initiatives initially helped lower costs and drive increases in highly leveraged Kraft Heinz's profitability even though the Company's sales were declining.

60. From the start in 2015, the Kraft Heinz strategy centered on harsh cost-cutting to create earnings growth. Defendants knew, or should have known, that, as a result of their cost cutting obsession, company products were being starved of marketing and promotion and research and development funds. In addition, powerful consumer trends were weakening the Company's pricing power and competitive position relative to competitors Costco, Walmart and Amazon products.

61. Despite the Company's positive public statements, behind the scenes, this high-profile merger with expectations to create long term shareholder value failed to deliver. Kraft Heinz's operational results have been faltering since late

2016. Sales grew only .3% in 2016 and, through the third quarter of 2017, were down 1.8%. Beginning in the first quarter of 2017, Kraft Heinz net (organic) sales began a steady decline, in that quarter they declined 2.7%. In the 2<sup>nd</sup> quarter 2017, organic net sales declined 0.9%. In the 3<sup>rd</sup> quarter 2017 net organic sales increased .3%. In the 4<sup>th</sup> quarter of 2017, organic net sales declined .6%. “Organic” sales are defined by Kraft Heinz as “net sales excluding, when they occur, the impact of acquisitions, currency, divestitures and a 53<sup>rd</sup> week of shipments”. Over the preceding two years, Kraft Heinz’s cash on hand fell from \$3.9 billion to \$1.4 billion even as debt increased, including a \$1 billion increase in debt through the first three quarters of 2018. These trends were the result of declining cash flow generated by sales of its products caused by the trends identified here.

62. By mid-2017, Defendants knew that 3G’s belt-tightening measures had run their course, depleted the Company of valuable resources, marginalized its internal controls, and left Kraft Heinz’s iconic brands badly damaged. The consumer shift from Kraft Heinz legacy brands to organic or private label offerings impaired the Company’s pricing power and commoditized its product categories.

63. In February 2018, Warren Buffet retired from Kraft Heinz Board of Directors, reportedly to “decrease his travel commitments”.

64. In the first quarter of 2018, organic net sales decreased 1.5%; in the 2<sup>nd</sup> quarter of 2018 organic net sales declined by .4%.

65. Kraft Heinz's sales declines and brand impairment were the predictable result of 3G's extreme cost cutting and reduction in advertising and marketing budgets. Kraft Heinz has been spending only 2-3% of annual sales revenues on advertising and marketing its brands compared to the industry average of 5% to 10%. According to published analysis, Kraft Heinz cut advertising by 11% to \$629 million in 2017 to 2.4% of sales compared to the 3.5% to 5.5% of sales at competitors Kellogg, Mondalez and Conagra. At Kraft Heinz, research and development dropped 22% in 2017 to \$120 million or 0.3% of sales versus industry peers' expenditures of approximately 1% of sales. Kraft, in the year before its merger with Heinz, spent \$149 million on research and development.

66. By April 2018, director Lemann (a 3G partner) was publicly admitting that Kraft Heinz's business was "being disrupted" (as reported in Forbes Editor's Pick, April 30, 2018, Jorge Paulo Lemann Says Era of Disruption In Consumer Brands Caught 3G Capital By Surprise," Antoine Gara.).

67. Further admissions by Lemann were reported in April 2018 in The Wall Street Journal, where the 3G co-founder, Kraft director and controlling person was quoted:

I'm a terrified dinosaur. I've been living in this cozy world of old brands [and] big volumes. You could just focus on being very efficient and you'd be ok all of a sudden we are being disrupted in all ways. If you go to a supermarket, you see hundreds of new brands. In beer, we had the new kinds of beer coming in from all over. We are running to adjust.

68. The effects of adverse conditions upon Kraft Heinz in 2017 and 2018 were only publicly revealed in 2019 in a CNBC interview (as reported in a February 25, 2019 Dow Jones News Report), when Warren Buffett acknowledged what afflicted KHC in 2017 and 2018:

KHC was losing its bargaining power with retailers due to competition with private label brands such as Costco's "Kirkland." [Mr. Buffett noted how fast and how far KHC had fallen behind Costco]: "So here they are, 100 years plus tons of advertising, built into people's habits and everything else and now Kirkland, a private label brand comes along with only 750 outlets does 50% more business." Mr. Buffett also noted that consumer brands' "ability to price has changed."

69. Further admissions about previously concealed adverse conditions at Kraft Heinz appeared in a Reuters February 25, 2019 interview where Mr. Buffett acknowledged that Amazon.com Inc., Walmart, Inc. brands were pressuring KHC and said "the ability to price has changed, and that's huge."

70. The impairment charges pertain to reported valuation estimates of good will and intangible assets. Kraft Heinz has represented that it makes value estimates for goodwill and intangible assets based on *inter alia* "estimated future annual net cash flows for each reporting unit (including net sales, costs of products sold, SG&A, working capital and capital expenditures)." The inputs of those estimates are not publicly known, nor calculable by non-insiders, accordingly only an insider would/could have such knowledge.

71. Kraft Heinz supposedly had an established formula for calculating both “fair value” of goodwill and intangible assets and any impairment thereof. As stated in its 1Q 2018 10-Q, (and repeated in pertinent part in prior and subsequent periodic financial reports) the Company was carrying \$44.8 billion in goodwill and \$53.8 billion in intangible assets, stating, in pertinent part, the following:

We test goodwill for impairment at least annually in the second quarter or when a triggering event occurs. We performed our 2017 annual impairment test as of April 2, 2017. As a result of our 2017 annual impairment test, there was no impairment of goodwill. Each of our goodwill reporting units had excess fair value over its carrying value of at least 10% as of April 2, 2017.

Our goodwill balance consists of 20 reporting units and had an aggregate carrying value of \$44.8 billion as of March 31, 2018. As a majority of our goodwill was recently recorded in connection with business combinations that occurred in 2015 and 2013, representing fair values as of the respective transaction dates, there was not a significant excess of fair values over carrying values as of April 2, 2017. We have a risk of future impairment to the extent that individual reporting unit performance does not meet our projections. Additionally, if our current assumptions and estimates, including projected revenues and income growth rates, terminal growth rates, competitive and consumer trends, market-based discount rates, and other market factors, are not met, or if valuation factors outside of our control change unfavorably, the estimated fair value of our goodwill could be adversely affected, leading to a potential impairment in the future. No events occurred during the period ended March 31, 2018 that indicated it was more likely than not that our goodwill was impaired. There were no accumulated impairment losses to goodwill as of March 31, 2018.

\* \* \*

We test indefinite-lived intangible assets for impairment at least annually in the second quarter or when a triggering event occurs. We performed our 2017 annual impairment test as of April 2, 2017. As a result of our 2017 annual impairment test, we recognized a non-cash impairment loss of \$49 million in SG&A in the second quarter of 2017. This loss was due to continued declines in nutritional beverages in India. The loss was recorded in our EMEA segment as the related trademark is owned by our Italian subsidiary. Each of our other brands had excess fair value over its carrying value of at least 10% as of April 2, 2017.

Our indefinite-lived intangible assets primarily consist of a large number of individual brands and had an aggregate carrying value of \$53.8 billion as of March 31, 2018. As a majority of our indefinite-lived intangible assets were recently recorded in connection with business combinations that occurred in 2015 and 2013, representing fair values as of the respective transaction dates, there was not a significant excess of fair values over carrying values as of April 2, 2017. We have a risk of future impairment to the extent individual brand performance does not meet our projections. Additionally, if our current assumptions and estimates, including projected revenues and income growth rates, terminal growth rates, competitive and consumer trends, market-based discount rates, and other market factors, are not met, or if valuation factors outside of our control change unfavorably, the estimated fair values of our indefinite-lived intangible assets could be adversely affected, leading to potential impairments in the future. No events occurred during the period ended March 31, 2018 that indicated it was more likely than not that our indefinite-lived intangible assets were impaired.

72. 3G's partners who were Kraft Heinz officers and/or directors were also privy to the material adverse information of decline in asset value because SEC reporting requirements forced Kraft Heinz to analyze the relevant issues. Only insiders, and not public investors, could discern the increasing impairment in

the value of these assets because Kraft Heinz's financial reports were notoriously lacking in detail as noted by Wells Fargo analyst John Baumgartner's reported reaction to poor third quarter financial results in November 2018 that Kraft isn't known for "copious financial detail." The investing public could not discern or even estimate the ongoing impairment in value because Kraft Heinz, as reported, made the calculations based on "estimated future annual net cash flows for each reporting unit (including net sales, costs of products sold, SG&A, working capital and capital expenditures)" none of which were provided to public investors with the necessary details.

73. Several days after the report of the results 2nd quarter 2018, Defendants sold 20 million shares of Kraft Heinz stock at approximately \$59.50 per share.

74. When the Kraft Heinz deal closed, Mr. Buffett was reported to have said in an interview: "We [Berkshire Hathaway] may increase our ownership if any members of the 3G Group ultimately want to sell out later." However, Berkshire Hathaway did not acquire any of the shares sold by 3G and has not acquired any additional shares of Kraft Heinz since its initial purchase.

75. Further evidence that Defendants as insiders had access to material adverse information may be inferred from the fact that SEC reporting requirements mandated that Kraft Heinz perform the analysis of trends and uncertainties that

would lead to the asset write down. Throughout 2017 and 2018, Kraft Heinz filed an Annual Report on Form 10-K and three Quarterly Reports on Form 10-Q for each of the quarterly periods in 2017 and 2018. Each of the filings and their respective contents were governed by SEC rules and regulations, including but not limited to “Regulation S-K: Item 303 Requirements” (management’s discussion and analysis of financial condition and results of operations).

(a) **Item 303 Requirements Regulations S-K** : Item 303 imposes an affirmative duty on issuers to disclose “events” or “uncertainties” that will have a material or unfavorable impact on the registrant's future revenue.<sup>1</sup>

(b) Specifically, Item 303 requires issuers to disclose in the registration statement any “trend, demand, commitment, event or uncertainty” that is “both presently known to management and reasonably likely to have material effects on the registrant's financial condition or results of operations.”<sup>2</sup>

Pursuant to Item 303(a), for a fiscal year, a registrant has an affirmative duty to:  
(i) describe any unusual or infrequent events or transactions or any significant economic changes that materially affected the amount of reported income from

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<sup>1</sup> See 17 C.F.R. § 229.303(a)(3)(i) & (ii); Mgmt’s Discussion and Analysis of Fin. Condition and Results of Operation, Exchange Act Release No. 6835 (“S.E.C. Release No. 6835”), 1989 WL 1092885, at \*4 (May 18, 1989).

<sup>2</sup> See *id.*; 17 C.F.R. § 229.303(a)(3)(ii).

continuing operations and, in each case, indicate the extent to which the income was so affected; (ii) describe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations. If the registrant knows of events that will cause a material change in the relationship between costs and revenues (such as known future increases in costs of labor or materials or price increases or inventory adjustments), the change in the relationship shall be disclosed.<sup>3</sup>

(c) Thus, even a one-time event, if “reasonably expect[ed]” to have a material impact of results, must be disclosed. Examples of such required disclosures include: “[a] reduction in the registrant’s product prices; erosion in the registrant’s market share; changes in insurance coverage; or the likely non-renewal of a material contract.”<sup>4</sup> Accordingly, as the SEC has repeatedly emphasized, the “specific provisions in Item 303 [as set forth above] require disclosure of forward-looking information.”<sup>5</sup> Indeed, the SEC has stated that

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<sup>3</sup> See 17 C.F.R. § 229.303(a)(3)(i)-(ii); see also S.E.C. Release No. 6835,1989 WL 1092885, at \*8 (May 18, 1989) (“Other non-recurring items should be discussed as unusual or infrequent events or transactions that materially affected the amount of reported income from continuing operations.”) (citation and quotation omitted).

<sup>4</sup> S.E.C. Release No. 6835, 1989 WL 1092885, at \*4.

<sup>5</sup> *Id.* at \*3.

disclosure requirements under Item 303 are “intended to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long-term analysis of the business of the company” and “a historical and prospective analysis of the registrant's financial condition ... with particular emphasis on the registrant's prospects for the future.”<sup>6</sup> Thus, “material forward-looking information regarding known material trends and uncertainties is required to be disclosed as part of the required discussion of those matters and the analysis of their effects.”<sup>7</sup>

76. The 3G Defendants knew that as of the latest at June 30, 2018, the Company had five reporting units whose fair value exceeded the carrying value by less than 10% and therefore the goodwill those units were carrying were at risk of write down.

77. The impairment in Kraft Heinz assets was only unveiled to the public when, on February 21, 2019, Kraft Heinz announced its earnings for the fourth quarter of 2018 and disclosed that the Company took an impairment charge of \$15.4 billion to lower the carrying amount of goodwill in its U.S. Refrigerated

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<sup>6</sup> *Id.*; see also *id.* at \*17.

<sup>7</sup> See Comm’n Guidance Regarding Mgmt’s Discussion and Analysis of Fin. Condition and Results of Operations, S.E.C. Release No. 8350, 2003 WL 22996757, at \*11 (December 19, 2003).

and Canada Retail reporting units and the carrying amount of certain intangible assets, including the Kraft and Oscar Mayer trademarks. The impairment charge resulted in a net loss attributable to common shareholders of \$12.6 billion and diluted loss per share of \$10.34. The impairment charges were approximately 13% and 15% of the amount of goodwill and intangible assets respectively which Kraft Heinz represented to public investors.

78. The magnitude of the impairment changes is even more dramatic because a Kraft Heinz spokesman ruled out interest rate increases in 2018 as a meaningful driver of the impairment charge.

79. The Company's write down was the largest in U.S. consumer staples industry in at least a decade according to a published report citing *Duff & Phelps LLC*, a valuation firm. According to Duff & Phelps, the sector experienced 88 write downs from 2013 through 2017 for a total of \$9.6 billion.

80. The Company further publicly disclosed, for the first time on February 21, 2019, that Kraft Heinz had received a subpoena from the SEC in October 2018 in relation to the Company's procurement function. As a result of the SEC investigation, the Company conducted its own internal investigation, which resulted in the Company recording a \$25 million increase to costs of products sold, damaging the Company's credibility and provoking fears of future accounting adjustments. On the same day, the Company announced a quarterly dividend of

\$0.40 per share, which represents a 36% reduction from the \$0.625 quarterly dividend Kraft Heinz had been paying. This reduction was designed to save the company \$1 billion a year to help reduce long-term debt of \$30.9 billion.

81. As a result of these disclosures, the price of Kraft Heinz common stock plummeted over 27% from \$48.18 per share to \$34.95 per share, erasing more than \$16 billion of the Company's market capitalization on extremely heavy trading volume. 3G however avoided these losses by selling 20,000,000 shares at approximately \$59.50 per share.

82. In 2019, Kraft Heinz disclosed information further indicating that insiders were aware of the material risk of material asset impairment and that such impairment charges were anticipated.

83. Kraft Heinz stated it tests its asset valuations for goodwill and intangible assets on the first day of the second calendar quarter of each year. In 2018 that would have been April 1, 2018, over four months before 3G sold 20 million shares of Company stock. Kraft Heinz also represented that it may perform such tests at other times as well depending on circumstances such as:

- a sustained decrease in market cap of Kraft Heinz;
- Increased competition or unexpected loss of market share;
- Unexpected significant declines in operating results; and
- Significant adverse changes in markets.

All of these triggering events occurred in 2017 through 2018 and thus insiders had non-public knowledge of the risk of material asset write-downs.

84. In an interview reported by Reuters on February 25, 2019 “Warren Buffett Says Berkshire Overpaid For Kraft Heinz,” Mr. Buffett observed the market reacted “probably quite properly” to the news. In an interview reported on Dow Jones News on February 25, 2019 Mr. Buffett said he wouldn’t buy more Kraft Heinz for Berkshire Hathaway “because it isn’t worth as much.”

85. On March 1, 2019, the SEC subpoenaed Kraft Heinz for documents related to assessment of goodwill and intangible asset impairments.

86. On June 7, 2019, Kraft Heinz finally issued its overdue Annual Report on Form 10-K for the annual period ended December 31, 2017. In it, Kraft Heinz revealed an “impairment loss” of \$7 billion reducing its goodwill asset value from \$44.8 billion to \$36.50 billion at the end of 2018. Similarly, Kraft Heinz reported an impairment loss of \$8.925 billion to intangible assets reducing the value of that asset from \$53.65 billion at the end of 2017 to \$43.97 billion at the end of 2018.

## **CAUSE OF ACTION**

### **BREACH OF FIDUCIARY DUTY FOR INSIDER SELLING AND MISAPPROPRIATION OF MATERIAL, NON-PUBLIC INFORMATION AGAINST 3G DEFENDANTS**

87. Plaintiff incorporates by reference and realleges every allegation contained above as through fully set forth herein.

88. Defendants 3G (the “Selling Defendants”) sold Kraft Heinz stock, while they knew the material adverse non-public information described herein, and sold Kraft Heinz stock on the basis of such information.

89. 3G’s sale of \$1.2 billion of Kraft Heinz stock was significant because it represented approximately 13% of 3G’s original investment in Kraft Heinz. In 2013, 3G invested \$4 billion of its cash in the Heinz takeover and then an additional \$5 billion. The sale at issue here was 3G’s first sale of Kraft Heinz securities since the merger. Traditionally, 3G has not sold any portion of its major holdings in many years; 3G’s last sale of Restaurant Brands International stock occurred in 2015.

90. The material information described above was proprietary, non-public information concerning the Company’s business and financial condition. It was a proprietary asset belonging to the Company, which 3G used for their own benefit when they sold Kraft Heinz stock.

91. Because using the Company’s proprietary information for their own gain constitutes a breach of 3G’s fiduciary duties, and/or an unlawful misappropriation of inside information, the Company is entitled to the imposition of a constructive trust on any profits they obtained thereby and subsequent return thereof.

**RELIEF REQUESTED**

WHEREFORE, Plaintiff demands judgment as follows:

- (a) Determining that this action is a proper derivative action maintainable under law and demand is excused;
- (b) Awarding to Kraft Heinz restitution from 3G, and ordering disgorgement of all profits, obtained by 3G from its insider trading;
- (c) Awarding to Plaintiff the costs and disbursements of the action, including reasonable attorneys' fees, accountants' and experts' fees, costs, and expenses; and
- (d) Granting such other and further relief as the Court deems just and proper.

DATED: October 9, 2019

**COOCH AND TAYLOR, P.A.**

/s/ Blake A. Bennett  
Blake A. Bennett (#5133)  
The Nemours Building  
1007 N. Orange Street, Suite 1120  
Wilmington, DE 19801  
(302) 984-3800  
*Attorney for Plaintiff*

**OF COUNSEL**

Kenneth A. Wexler  
Kara A. Elgersma  
WEXLER WALLACE LLP  
55 West Monroe, Suite 3300  
Chicago, Illinois 60603  
(312) 346-2222  
[kaw@wexlerwallace.com](mailto:kaw@wexlerwallace.com)  
[kae@wexlerwallace.com](mailto:kae@wexlerwallace.com)  
*Attorneys for Plaintiff*