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Case Number 594,2009

IN THE SUPREME COURT OF THE STATE OF DELAWARE

CITY OF WESTLAND POLICE & FIRE RETIREMENT SYSTEM,	:	No. 594,2009
Appellant,	:	ON APPEAL FROM THE OPINION DATED SEPTEMBER 28, 2009 AND ORDER DATED SEPTEMBER 28, 2009 OF THE COURT OF CHANCERY OF THE STATE OF DELAWARE IN C.A. NO. 4473-VCN
v.	:	
AXCELIS TECHNOLOGIES, INC.,	:	
Appellee.	:	

APPELLANT'S REPLY BRIEF

DATED: February 18, 2010

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COUNTERSTATEMENT OF FACTS

Defendant's counterstatement of the facts quotes myriad statements from the Board of Directors of Axcelis Technologies, Inc. ("Axcelis" or the "Company") through which the directors attempted to justify their decisions (1) to reject the acquisition proposals presented by Sumitomo Heavy Industries ("SHI"), (2) to reject the resignations of the three directors who failed to receive the support of a majority of shareholders at Axcelis's 2008 annual meeting, (3) to decline SHI's request for additional time to formulate an acquisition proposal, and (4) ultimately to sell the Company's 50% stake in SEN Corporation ("SEN") to SHI. Axcelis's Answering Brief at 7-16. ("Def. Br."). Axcelis also cites certain statements from Sterling Capital Management ("Sterling"), arguing that such statements suggest that Sterling thought that SHI's original proposals undervalued the Company. (Def. Br. at 11). Axcelis's arguments, and its characterization of the facts, however, are largely irrelevant.

Whether Axcelis's directors can articulate a justification for their actions is hardly dispositive for purposes of evaluating Plaintiff's right to inspection under Section 220 of the DGCL. Simply because those directors gave an explanation does not mean that such an explanation is logical, reasonable, or pertinently, that shareholders must accept it. In fact, the entire point of even having books and records inspections is that shareholders are not required to accept management's explanations at face value. Shareholders are entitled – and indeed encouraged – to inspect books and records when, as here,

management's explanations simply don't add up. And that is what Plaintiff is attempting to do here.

Axcelis also summarily concludes that, besides Plaintiff, no other stockholders believed that the Board's decision to retain the rejected directors was unlawful, wrongful, or contrary to the stockholders' wishes. (Def. Br. at 15). Axcelis's argument in this regard is not only irrelevant, but it certainly begs the question of why over half of the Company's stockholders who cast their votes at the 2008 annual meeting withheld their votes from those directors in the first place. Axcelis's voting policy *required* directors who did not receive the support of a majority of the shareholders who cast their votes at the 2008 annual meeting to resign. (A321). The existence of this resignation requirement, at the very least, provides a "credible basis" to infer that those shareholders who made the affirmative decision to withhold their votes for Messrs. Hardis, Fletcher, and Thompson did so in order to cause those directors to resign and no longer serve on the Company's Board of Directors.

Axcelis's extensive citation to the self-serving statements of the Company's directors, more importantly, demonstrates the underlying problem with the Court of Chancery's application of the "credible basis" standard articulated by this Court in *Seinfeld.* If corporate directors can defeat a shareholders' Section 220 request simply by denying wrongdoing and providing an explanation (however truthful, or not) for their conduct (which is the clear implication of the Court of Chancery's holding), then Section 220 would be rendered essentially worthless as a viable tool for investigating corporate wrongdoing.

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN FAILING TO APPLY THE "CREDIBLE BASIS" STANDARD TO WESTLAND P&F'S BOOKS AND RECORDS ACTION

Axcelis misconstrues the first issue on appeal as one involving only "findings of fact." (Def. Br. at 19). Axcelis is mistaken. Because Plaintiff challenges the Court of Chancery's application of law – specifically the "credible basis" standard – the correct standard of review is *de novo*. *Chavous v. State*, 953 A.2d 282, 286 n.15 (Del. 2008). But even if an abuse of discretion standard applies, the Court of Chancery abused its discretion here.

A. As Even Axcelis's Brief Shows, The Court of Chancery Incorrectly Applied the "Credible Basis" Standard Formulated by this Court

In *Seinfeld v. Verizon*, 909 A.2d 117 (Del. 2006), this Court held that that a shareholder requesting books and records under Section 220 must "present '*some evidence*' to *suggest* a 'credible basis' from which a court *can* infer that mismanagement, waste, or wrongdoing *may* have occurred." 909 A.2d at 118 (emphasis added). Axcelis attempts to heighten Plaintiff's burden by reformulating the standard set forth by this Court from one that requires shareholders to present some evidence that suggests a credible basis from which a court "*can*" infer wrongdoing "*may*" have occurred, into one that requires shareholders to supply a credible basis from which a court must find "*probable* wrongdoing" before granting inspection rights. (Def. Br. at 20). This not-so subtle distinction exposes the flaw in Axcelis's argument – and in the Court of Chancery's holding.

In determining whether a shareholder has satisfied its burden in a Section 220 proceeding, the question is *not* whether the existence of

corporate wrongdoing is "probable" or even "more likely than not." Indeed, in *Seinfeld*, this Court explained that "[a] stockholder is 'not required to prove by a preponderance of the evidence that waste and [mis]management are actually occurring.'" 909 A.2d at 123 (quoting *Thomas & Betts Corp. v. Leviton Mfg. Co. Inc.*, 681 A.2d 1026, 1031 (Del. 1996)). Rather, the question is whether, based on the record presented by the shareholder "through documents, logic, testimony or otherwise, that there are legitimate issues of wrongdoing." *Id.*

The fundamental error of the Court of Chancery here was its holding that Plaintiff failed satisfy its burden under Section 220 because it did not present sufficient evidence to justify an inference "that the Board's decision to retain the Three Directors was either motivated by entrenchment or was defensive in nature." (Mem. Op. at 12). But for purposes of Section 220, the question was *not* whether the Board's conduct "*was* either motivated by entrenchment or *was* defensive in nature" (emphasis added), but whether the Board's conduct *may have been* improperly motivated or defensive. In its brief, Axcelis ignores this point entirely. Instead, Axcelis defends the Court of Chancery's holding by pointing out that Delaware courts historically have rejected "structural bias" as a basis for inferring an improper motive of entrenchment of corporate directors. (Def. Br. at 27). Yet the cases Axcelis cites in support of this point, *Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart* 845 A.2d 1040 (Del. 2004), and *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), were decided in the context of motions to dismiss, and not in the context

of a Section 220 proceeding where the question is not whether a plaintiff alleged sufficient facts to demonstrate that the directors were actually improperly motivated, but whether the shareholder should be entitled to investigate the directors' motivations.

Nevertheless, Plaintiff did not rely on the existence of any "structural bias" to justify its Section 220 demands, but presented evidence which, viewed in its entirety, raised some question regarding the motivation of the Axcelis directors in responding to SHI's acquisition proposals and in rejecting the resignations of Messrs. Hardis, Fletcher, and Thompson.

1. A Threat to Corporate Control Existed

According to Axcelis, there was no legitimate basis to even question the motivations of the Company's directors because no threat to their control over the Company ever existed. Thus, Axcelis argues, *Unocal* could not possibly apply. (Def. Br. at 22); *see also* (Mem. Op. at 16). Axcelis's arguments, and the Court of Chancery's holding in this regard, are simply incorrect.

The fact that as of the time of Axcelis's 2008 annual meeting SHI had not launched a hostile tender offer or engaged in a contested proxy fight most certainly ***does not*** preclude the application of *Unocal*. This Court repeatedly has held that a board's actions may be subject to enhanced scrutiny under *Unocal* even in the absence of a hostile bidder. In *Moran v. Household Int'l, Inc.*, 500 A.2d 1346 (Del. 1985), for example, this Court applied *Unocal* to a preemptive defensive measure taken by a board where no bidder even existed. *Id.* at 1350-53. Similarly, in *Stroud v. Grace*, 606 A.2d 75 (Del. 1992),

this Court explained that even a "perceived" threat to corporate control is sufficient to implicate enhanced scrutiny under *Unocal*. *Id*. at 82.

For this reason, Axcelis's attempt to distinguish *Black v. Hollinger, Int'l Inc.*, 872 A.2d 559 (Del. 2005), and *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361 (Del. 1995), misses its mark. The holdings in those cases do not, as Axcelis suggests, apply only to situations where "boards enacted poison pills in response to hostile tender offers." (Def. Br. at 22 n.11). Rather, they both, and in particular *Unitrin*, stand for the much broader proposition that where, as here, a board responds to a threat to corporate control, enhanced judicial scrutiny applies. *Unitrin*, 651 A.2d at 1388 ("Proper and proportionate defensive responses ... are permitted to thwart perceived threats.").

Here, at the time of Axcelis's 2008 annual meeting, SHI had tried for over two years to engage the Axcelis Board in discussions regarding a possible sale of the Company and had gone public with its offer and its frustration with the Axcelis Board's refusal to negotiate. (A255-A258). Further, the class of Axcelis directors up for election at the 2008 annual meeting faced an organized "vote no" campaign by shareholders (supported by proxy advisory firms) specifically designed to trigger the Company's voting policy and force those directors to resign from the Board. (A319). With the prospect of SHI making public offers to acquire the Company, and shareholders making a concerted effort to vote three directors out of office, it simply cannot be said that the Axcelis directors could not have

"perceived" a threat to their control over the Company. That the remaining directors would have had the ability to consider the resignations under the Company's voting policy, or the ability to appoint new directors to fill vacancies under Delaware law *see* (Def. Br. at 25) impacts only the scope and extent of the threat (which may be relevant in weighing the "reasonableness" of any response under *Unocal*), but it does not mean that a threat to control could not exist at any level.

Axcelis's attempt to refute this point does not make any sense. Axcelis argues that simply because the Company's Board rejected SHI's second acquisition proposal *before* shareholders launched their "vote no" campaign and before the Company's annual meeting, this somehow means that SHI's proposal could not be deemed a threat to corporate control implicating *Unocal.* (Def. Br. at 24). Axcelis's argument is illogical. The anger of Axcelis's shareholders did not "transmute" SHI's acquisition proposals into a threat to corporate control. The fact that SHI was actively pursuing an acquisition of the Company itself constituted a "threat," regardless of the level of the shareholders' anger. *See AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 112 (Del. Ch. 1986) (finding that a "non-coercive" and "concededly fair" offer that did not "threaten[] injury to shareholders" nevertheless constituted a threat to corporate control). That shareholders were actively seeking to vote a class of directors off of the Axcelis Board for failing to talk to SHI demonstrates the seriousness of this threat, and itself constituted a threat to the

ability of the Axcelis Board to maintain its unified opposition to SHI's efforts.

2. The Axcelis Board Responded to a Threat to Corporate Control

Axcelis goes to great lengths to argue that the Company's Board had an absolute right to simply "just say no" to SHI's offers. (Def. Br. at 23-24) (citing *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009) and *TW Services, Inc. v. SWT Acquisition Corp.*, 1989 WL 20290 (Del. Ch. March 2, 1989)). In *Gantler*, this Court explained that "[r]ejecting an acquisition offer, *without more*, is not 'defensive action' under *Unocal*." 965 A.2d at 705, n.23 (emphasis added). But, as explained in Plaintiff's opening brief, and unlike *Gantler*, the Axcelis Board did more than simply "say no." Specifically, as even Axcelis's brief acknowledges, the Axcelis Board affirmatively responded to SHI's proposals by: (1) rejecting the resignations of Messrs. Hardis, Fletcher, and Thompson; (2) rejecting SHI's request for a modest extension of time; and thereafter (3) selling the Company's 50% interest in SEN to SHI, in direct contradiction of Axcelis's previous justifications for rejecting SHI's offers. So whether the Axcelis Board could "just say no" is really beside the point. The fact that Axcelis and the Court of Chancery *deny* that the Axcelis directors took these actions as part of a concerted effort to defend against SHI and to entrench themselves in control over the Company does not mean that it is patently unreasonable to infer that the directors' actions in this regard may, in fact, have been improperly motivated. Indeed, such denials merely demonstrate the

need for Plaintiff to use the Section 220 mechanism to investigate these claims. The Court of Chancery erred, therefore, in holding that Plaintiff failed to present a "credible basis" from which that court *could infer* that corporate wrongdoing *may have occurred* because Plaintiff did not present "evidence that the Board disloyally desired to fend off SHI's advances." (Mem. Op. at 16); *see Khanna v. Covad Commc'ns Group, Inc.*, 2004 WL 187274, at *6 (Del. Ch. Jan. 23, 2004) ("A Section 220 action is not the proper forum for litigating a breach of fiduciary duty case. All that the Section 220 plaintiff must show is a credible basis for claiming that 'there are legitimate issues of wrongdoing.'")

At the very least, the evidence presented to the Court of Chancery demonstrated that the Axcelis Board, in fact, attempted to fend off SHI's advances. (*See, e.g.*, A435-A441, A980-A985, A988-A990). Whether they did so "disloyally," *i.e.*, with an improper motive of entrenchment, is a factual question that warrants investigation. *See Goodwin v. Live Entertainment, Inc.*, 1999 WL 64265, at *25 (Del. Ch. Jan. 25, 1999) (explaining that whether a defendant acts with an "entrenchment motive" is a "necessarily 'fact-dominated question[.]'") (quoting *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 364 (Del. 1993)). But more importantly, under *Unocal*, if any of the Axcelis Board's conduct was designed or intended to respond to SHI's acquisition efforts, there was a "credible basis" to believe that the Axcelis directors would have had the burden to demonstrate the reasonableness of their conduct and the proportionality of their

response. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

Axcelis argues that the Court of Chancery properly rejected Plaintiff's 220 requests because the directors' conduct cannot be characterized as "defensive." For example, Axcelis now claims that the Board's decision to retain the rejected directors was not a response to SHI's acquisition proposals. (Def. Br. at 25). But this contradicts the Board's previous position that it retained these directors precisely because they were necessary for dealing with SHI. (A43). But even accepting Axcelis's spin that the rejected directors were necessary for "mov[ing] forward" in discussions with SHI (A324), it is undisputed that the Board's decision was motivated, at least in part, by the acquisition proposals made by SHI. *Id.*

More importantly, however, Axcelis's arguments that the Board's conduct cannot be characterized as defensive hinges entirely on the veracity of the directors' own statements. For example, Axcelis argues that, rather than being defensive, the rejection of the resignations of Messrs. Hardis, Fletcher, and Thompson was necessary because the directors claimed that their presence was necessary to "move forward on discussions with SHI." (Def. Br. at 15). Similarly, Axcelis claims that the Board's refusal to grant SHI a reasonable extension to formulate a formal demand was not defensive by repeating verbatim language from the Company's September 15, 2008 Form 8-K, in which the Axcelis's Chairperson Mary Puma purported to explain why SHI determined to walk away. (Def. Br. at 16, citing A-333). This again puts shareholders in the untenable position of being forced to accept

management's claims without being afforded any method to verify those claims. To hold that a corporate board's simple denial of wrongdoing precludes a shareholder from arguing that a "credible basis" exists to suspect that corporate wrongdoing occurred by questioning the veracity of those same directors would render Section 220 meaningless as a tool for investigating claims that hinge on the directors' motives and subjective intent. At the very least, shareholders should be entitled to access corporate records to test the veracity of directors' statements where, in the absence of denials of wrongdoing or potentially concocted explanations, there is reason to suspect that they behaved improperly. *See Grimes v. Donald*, 673 A.2d 1207, 1218 (Del. 1996) ("A stockholder ... has the right to use the 'tools at hand' to obtain the relevant corporate records.").

Finally, Axcelis argues that the fact that the Axcelis Board ultimately did engage in discussions with SHI absolutely refutes any suggestion that the directors behaved improperly, and their decision to sell Axcelis's 50% interest in SEN to SHI is completely irrelevant and justified for reasons unrelated to SHI's previous acquisition efforts. (Def. Br. at 25-27). Neither argument holds water. First, the fact that the Axcelis Board purported to meet with SHI proves nothing. *Unocal* applies if the directors adopted defensive measures *even if* those directors purport to engage in discussions with an unwelcome suitor. *See Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 184 (Del. 1986) (holding that a *Unocal* analysis applied to considering defensive measures adopted by a target corporation even though it engaged in discussions with the hostile

suitor). Second, the fact that Axcelis can articulate a justification for selling the Company's interest in SEN to SHI does not necessarily mean that the decision to sell the central asset that originally had prompted SHI's interest in acquiring the Company was not, at bottom, a defensive measure. Indeed, the directors could have used the Company's holdings in SEN as leverage to bring SHI back to the bargaining table after they caused SHI to walk away in November of 2008. *See, e.g.*, *City Capital Assoc. Ltd. P'ship v. Interco Inc.*, 551 A.2d 787, 801 (Del. Ch. 1988) (finding that the sale of a key corporate asset was "clearly defensive," requiring enhanced scrutiny under *Unocal*) (dismissed for mootness on appeal). Thus, even assuming *arguendo* that ultimately Axcelis's directors could show that they did not act defensively in agreeing to sell the Company's interest in SEN, that is beside the point. There exists now and at the time Plaintiff made its inspection demands a credible basis to infer such a sale may have been a defensive response to SHI. This is particularly true in light of the fact that after Axcelis sold SEN to SHI, SHI no longer expressed any interest in acquiring Axcelis.

3. A Credible Basis Exists To Infer That Wrongdoing May Have Occurred

As this Court held in *Unitrin*, where a target company's defensive actions are related to one another, the principles of *Unocal* require those actions to be evaluated collectively. 651 A.2d at 1387. Here, the conduct of the Axcelis Board in rejecting the directors' resignations, refusing to give SHI an extension of time to make an offer, and selling the Company's 50% interest in SEN to SHI appeared

to have been part of an ongoing – and ultimately successful - effort to ward off SHI's unwanted proposals to acquire the Company. If the Board's conduct in this regard in fact was designed and intended to fend off SHI, then *Unocal* applies and the directors would be required to demonstrate the reasonableness of their conduct. *Unitrin*, 651 A.2d at 1387. But for purposes of evaluating Plaintiff's Section 220 requests, whether *Unocal* in fact applies is not the relevant inquiry. Rather, the relevant inquiry is whether there is a "credible basis" to believe that the Axcelis directors' conduct *may have* been improperly motivated. *See Seinfeld*, 909 A.2d at 118 ("We reaffirm the well-established law of Delaware that stockholders seeking inspection under section 220 must present 'some evidence' to *suggest* a 'credible basis' from which a court *can* infer that mismanagement, waste or wrongdoing may have occurred.") (emphasis added). Here, but for the Axcelis directors' own self-serving explanations and denials of wrongdoing, the record before the Court of Chancery gave rise to a credible basis to believe that the directors intended to fend off SHI's acquisition proposals in behaving as they did. By holding that the Plaintiff failed to carry its burden under Section 220 because it did not provide definitive "evidence" of the directors' wrongful intent (Mem. Op. at 16-17), the Court of Chancery improperly conflated this Court's "credible basis" standard as articulated in *Seinfeld* with the pleading standard applicable in the context of a motion to dismiss.

II. A CREDIBLE BASIS EXISTS TO SUSPECT THAT THE AXCELIS BOARD REJECTED THE RESIGNATIONS OF THE DIRECTORS TO REVERSE THE INTENDED OUTCOME OF A SHAREHOLDER VOTE, THUS TRIGGERING ENHANCED SCRUTINY UNDER BLASIUS.

Axcelis insists that this Court should apply an abuse of discretion standard in reviewing the Court of Chancery's holding that *Blasius* did not require any enhanced scrutiny of the Axcelis Board's conduct here. (Def. Br. at 28). But again, whether a shareholder complied with the requirements of Section 220 is, as the case cited by Axcelis shows, a question of law entitled to *de novo* review. *See Sec. First Corp. v. U.S. Die Casting and Dev. Co.*, 687 A.2d 563, 567 (Del. 1997) ("This Court reviews *de novo* the question of a 'proper purpose' under Section 220(b)."). And whether *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988) applies is also a question of law subject to *de novo* review by this Court. *See Unitrin*, 651 A.2d at 1385 (reviewing *de novo* the Court of Chancery's legal conclusions regarding whether the court should apply enhanced scrutiny).

Merits

Even aside from the possible application of *Unocal* to the Axcelis Board's dealings with SHI, the fact that the directors rejected resignations submitted pursuant to a voting policy that *required* directors to resign if they did not receive majority support for their reelection gives rise to a reasonable inference that the incumbent directors intended to reject the outcome of the shareholder vote by doing so. The fact that the rejection of these resignations had the direct impact of reversing the intended outcome of a corporate election itself gives rise to a "credible basis" to suspect that *Blasius* applies.

Axcelis advances three main arguments for why the Board's retention of directors rejected by a majority of the Company's shareholders could not implicate any heightened standard of review: (1) Plaintiff did not demonstrate that the Axcelis Board acted "primarily" to disenfranchise shareholders (Def. Br. at 29); (2) the Axcelis directors merely acted in accordance with a company policy, and thus their decision cannot be subjected to enhanced scrutiny (*id.* at 31); and (3) shareholders cannot complain that the directors rejected the resignations because the voting policy at issue was a "policy" and not a "bylaw," and thus cannot be "enforced" by the shareholders. (*Id.* at 30). Axcelis's arguments are misplaced.

First, to satisfy its burden under *Seinfeld*, Plaintiff need not prove that *Blasius* necessarily applies to the Axcelis directors' rejection of the resignations. Rather, Plaintiff need only show that *Blasius* <u>*might*</u> apply. Even accepting Axcelis's (false) premise that *Blasius* is not implicated because Plaintiff cannot show that the directors acted "primarily" to interfere with the shareholder franchise, that does not mean that a court could not infer that they *may have* unlawfully intended to interfere with the outcome a shareholder vote, thus requiring *Blasius'* application in a trial on the merits. As this Court explained in *Security First*, "[t]he actual wrongdoing itself need not be proved in a Section 220 proceeding[.]" 687 A.2d at 567.

Second, the fact that the Axcelis directors "fully complied with" the Company's voting policy (Def. Br. at 31) does not automatically shield their conduct from meaningful judicial review. *See, e.g. Stroud*

v. Grace, 606 A.2d 75, 96 (Del. 1992) ("It is not an overstatement to suggest that every valid by-law is always susceptible to potential misuse."); *Lerman v. Diagnostic Data, Inc.*, 421 A.2d 906 (Del. Ch. 1980) (invalidating a board's otherwise lawful bylaw amendment where the directors exploited the new bylaw to "thwart[] shareholder opposition and perpetuat[e] management in office"); *Datapoint Corp. v. Plaza Sec. Co.*, 496 A.2d 1031, 1036 (Del. 1985)(issuing a preliminary injunction preventing a board from enforcing a bylaw that intruded on "fundamental stockholder rights"). Even if a board enacts a lawful policy, if it chooses to act under that policy, it must do so in compliance – not only with the policy itself – but with Delaware law. In other words, there is no circumstance where directors may be excused from adhering to their fiduciary obligations. *See Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914 (Del. 2003) ("The stockholders of a Delaware corporation are entitled to rely upon the board to discharge its fiduciary duties at all times.")

Third, Axcelis argues that there is no reason to question the directors' conduct here because "a 'plurality plus' voting 'policy' – as opposed to a charter or bylaw provision – generally cannot be enforced by stockholders." (Def. Br. at 30). But the fact that the voting scheme at Axcelis is embodied in a "policy" as opposed to a "bylaw" is a distinction without a difference. The question is not, as Axcelis suggests, whether shareholders can "enforce" this "policy," but whether *if* a corporate board determines to reject a resignation that was the intended result of a concerted effort by shareholders to withhold their votes for the proposed reelection of a corporate

director, there is a "credible basis" to believe that Delaware law would apply some level of enhanced scrutiny to the board's decision in this regard. *See Aprahamian v. HBO & Co.*, 531 A.2d 1204, 1206-07 (Del. Ch. 1987) ("When the election machinery appears, at least facially, to have been manipulated, those in charge of the election have the burden of persuasion to justify their actions.").

Axcelis argues that the standard of review to be applied by this Court should be determined by how the Board drafted the voting policy itself, rather than established principles of Delaware law. *See* Del. Br. at 31 (comparing Axcelis's voting policy with voting schemes at other corporations). Axcelis is mistaken. Indeed, in *MM Companies, Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118 (Del. 2003), this Court acknowledged that the board in that case certainly acted within its authority in that case, but explained that the scope board's authority was beside the point. Where a corporate board exercised "otherwise valid powers" for the "inequitable purposes" of frustrating a shareholder vote, this Court explained, the board's decision was not entitled to the deference afforded under the business judgment rule, but rather that the enhanced standard of review required by *Blasius* applies. *Id.* at 1132.[1] Axcelis's directors, therefore, do not get to

[1] Axcelis's attempt to distinguish *Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437 (Del. 1971), fails. In this Section 220 proceeding, the question is not whether Axcelis's shareholders had a "clear right" to demand that the Company's directors satisfy the rigors of *Blasius* and prove that they were justified in rejecting the resignations. Rather, the question is whether there was a credible basis to believe that the directors' decision in this regard, which clearly impacted and related to a corporate election, was not necessarily entitled to the kind of absolute deference normally afforded under the business judgment rule. In fact, Axcelis's argument that "*Schnell* applies only where a board's action has a *subjective inequitable motivation* akin to

define for themselves the standard of review that applies to their decision to reject resignations submitted pursuant a voting scheme that triggered the affirmative requirement that directors resign if their reelection was opposed by a majority of shareholders.

Finally, Axcelis's attempts to downplay the legitimate questions raised by Court of Chancery's decision by challenging Plaintiff's citation to Prof. Hammermesh's observations and disparaging those whose writings may be critical of certain aspects of Delaware law. But again, Axcelis misses the point. Prof. Hammermesh's discussion did not focus on any supposed distinction between a bylaw and a corporate policy, as Axcelis argues. (Def. Br. at 32). To the contrary, Prof. Hammermesh noted that "there is little in the opinion to suggest that the question of wrongdoing, and the choice of standard of judicial review of the rejection of the resignation, would be treated any differently if the rejection followed a failure to achieve a majority vote required bylaw, under which the director would nonetheless continue in office as a holdover director, rather than under a Pfizer type policy, under which the director is actually formally elected."[2] Instead, Prof. Hammermesh focused on the nature of the rights and interests at issue, and recognized that some level of

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bad faith" (Def. Br. at 34, emphasis added), actually demonstrates why Plaintiff's 220 requests were appropriate here. Before filing an action that affirmatively alleges that a director acted with a "subjective inequitable motivation," is it not reasonable for the shareholder at least to investigate the basis upon which the director made his or her decision?

[2] Lawrence A. Hamermesh, Court of Chancery Deals a Blow to Use of "Pfizer Type" Majority Voting Policies as a Mechanism for Shareholder Activism, The Institute of Delaware Corporate & Business Law, http://blogs.law.widener.edu/delcorp/de-corporate-law-news/%E2%80%9Cpfizer-type%E2%80%9D-majority-voting-policies/

heightened accountability to shareholders was appropriate because issues concerning who will represent the shareholders on a corporate board is a "matter … at least partly within the domain of the stockholders' legal power."[3] Indeed, the very articles that Axcelis cites in support of its assertion that the academic literature uniformly "anticipated" that "plurality-plus" voting policies would "not be subject to heightened scrutiny" (Def. Br. at 33), acknowledge that the level of scrutiny applicable to such policies has been and still is an unsettled question.[4]

What *is* clear, however, is the Court of Chancery's holding eliminates the possibility of judicial oversight on a novel and developing area of corporate law. By holding that a board's rejection of director resignations submitted under a "plurality plus" or "Pfizer style" voting scheme cannot satisfy even the minimal "credible basis" standard to justify a Section 220 demand, the Court of Chancery has rendered shareholders powerless to even question directors' conduct in

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[3] *Id.*

[4] *See,* Vincent Falcone, *Majority Voting In Director Elections: A Simple, Direct, and Swift Solution?*, 2007 COLUM. BUS. L. REV. 844, 876 (2007) ("the reviewing court may focus on the board's interference with the shareholder franchise. ... The board's refusal to oust a director who has received less than a majority of the votes cast in an election could easily be viewed as an 'instance in which an incumbent board seeks to thwart a shareholder majority.'"); William K. Sjorstom, Jr. and Young Sang Kim, *Majority Voting For The Election of Directors*, 40 CONN. L. REV. 459, 486-87 (2007) (opining without citing to any authority that "presumably" an exercise of the board's discretion under a Pfizer-style voting policy would be subject to business judgment review); *see also* Joshua R. Mourning, *The Majority-Voting Movement: Curtailing Shareholder Disenfranchisement In Corporate Elections*, 85 WASH. U. L. REV. 1143, 1194 n.284 (2007) ("it is not entirely clear that the business judgment rule would automatically apply" where a board rejects directors resignations under a Pfizer-style voting policy).

this regard. Regardless of how Axcelis characterizes the merits (or lack thereof) of arguments advanced by those critical of certain substantive aspects of Delaware law (such as Prof. Brown), what is important is that by rejecting Plaintiff's Section 220 requests here, the Court of Chancery effectively removed the Delaware judiciary from the ability to form policy and develop law in an area involving the central issue of corporate democracy – director elections.[5] The Court of Chancery's decision here should be reversed.

CONCLUSION

For the foregoing reasons, the Court of Chancery's September 28, 2009 Memorandum Opinion and Order should be REVERSED.

Respectfully submitted,

/s/ Michael J. Barry

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[5] *See, e.g.*, Faith Stevelman, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law*, 34 DEL. J. CORP. L. 57 (2009) ("the state's legislators and jurists are becoming sensitive to increased threats to [Delaware corporate] law's sustained preeminence"); Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 612 (2003) (explaining that the federal government has already preempted state law regarding the proxy solicitation process because states did "'virtually nothing to cope with the problem' of managerial abuses in soliciting proxies" and that federal preemption remains a threat to Delaware corporate law).

CERTIFICATE OF SERVICE

I hereby certify that the foregoing Appellant's Reply Brief was caused to be served on the 18th day of February, 2010 on the following parties in the manner indicated below:

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