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Case No. 5795-VCL

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

LOUISIANA MUNICIPAL POLICE EMPLOYEES' RETIREMENT SYSTEM and U.F.C.W. LOCAL 1776 & PARTICIPATING EMPLOYERS PENSION FUND, Plaintiffs, v. DAVID PYOTT, HERBERT W. BOYER, LOUIS J. LAVIGNE, GAVIN S. HERBERT, STEPHEN J. RYAN, LEONARD D. SCHAEFFER, MICHAEL R. GALLAGHER, ROBERT ALEXANDER INGRAM, TREVOR M. JONES, DAWN E. HUDSON, RUSSELL T. RAY, and DEBORAH DUNSIRE, Defendants, and ALLERGAN, INC., Nominal Defendant.	:	C.A. No. 5795-VCL

PLAINTIFFS' BRIEF IN OPPOSITION TO DEFENDANTS' APPLICATION FOR CERTIFICATION OF INTERLOCUTORY APPEAL

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Plaintiffs, Louisiana Municipal Police Employees' Retirement System ("LAMPERS") and U.F.C.W. Local 1776 & Participating Employers Pension Fund ("Local 1776") (together, "Plaintiffs"), respectfully submit this Brief in opposition to the Application For Certification Of Interlocutory Appeal ("Application") filed by Defendants, David E.I. Pyott, Herbert W. Boyer, Ph.D., Louis J. Lavigne, Jr., Gavin S. Herbert, Stephen J. Ryan, M.D., Leonard D. Schaeffer, Michael R. Gallagher, Robert A. Ingram, Trevor M. Jones, Ph.D., Dawn E. Hudson, Russell T. Ray, and Deborah Dunsire, M.D. (collectively, the "Individual Defendants"), and Nominal Defendant, Allergan, Inc. (collectively, with the Individual Defendants, the "Defendants"), on June 21, 2012.

INTRODUCTION AND PRELIMINARY STATEMENT

In a decision fully supported by the relevant Delaware authority, the Court of Chancery denied Defendants' motions to dismiss in this action, finding demand to be excused as futile, and further holding that Plaintiffs stated viable claims against the Individual Defendants. *See* June 11, 2012 Opinion (the "Opinion"). The Court also concluded, as a predicate to its determination on the merits of Defendants' motions to dismiss, that a five-page opinion issued by a California federal district court granting motions to dismiss in a separate, albeit related action did not preclude this Court from consideration of the sufficiency of Plaintiffs' complaint against Defendants' motions to dismiss.

Defendants now seek interlocutory review of the Court of Chancery's conclusion that the California district court's opinion should not be given preclusive effect in this action. The Court of Chancery based this decision on its ruling that, in the context of

derivative litigation, shareholders of a corporation are not in privity with one another for collateral estoppel purposes until one of them is found to have the authority to pursue claims derivatively on behalf of the corporation by a showing of demand futility or wrongful refusal. *See* Opinion at pp. 14-36. The Court thereafter described an alternative basis upon which it would have reached the same conclusion, that is, that Plaintiffs in the present action are not collaterally estopped from asserting derivative claims in this case because the California plaintiffs were not adequate representatives for purposes of invoking the collateral estoppel doctrine. *Id*. at pp. 37-65.

Defendants argue that the Opinion should be certified for interlocutory appeal because, among other things, portions of the Opinion addressing collateral estoppel and issue preclusion, as well as inadequacy of representation, raise issues of first impression and conflict with the decisions of other courts. Defendants further seek review of the "merits" holdings of the Opinion, *i.e.*, that Plaintiffs sufficiently pled facts demonstrating demand futility and stated viable claims against the Individual Defendants, asserting that this Court misapplied Delaware law and interpreted Plaintiffs' allegations and the documents underlying those allegations too favorably to Plaintiffs and not within the "context" that Defendants would have liked the allegations and evidence to be viewed.

Defendants' Application should be denied because the Opinion does not meet the requirements for certification under Supreme Court Rule 42.

First, the Court of Chancery's rulings as to collateral estoppel and privity are in line with Delaware Supreme Court precedent. In deciding that the question of whether a stockholder in a Delaware corporation can sue derivatively after another stockholder

attempted to plead demand futility is a matter of substantive Delaware law implicating the internal affairs doctrine, the Court of Chancery relied on relevant U.S. Supreme Court and Delaware Supreme Court decisions. *See* Opinion at pp. 19-22. Moreover, in holding that an earlier Rule 23.1 dismissal does not have a preclusive effect on a subsequent derivative action because the earlier plaintiff was not in privity with the corporation or its stockholders, the Court of Chancery relied on Delaware Supreme Court and Court of Chancery precedent that is directly in line with that conclusion. Notably, the Opinion relies on *Rales v. Blasband*, 634 A.2d 927 (Del. 1993), and *Kaplan v. Peat, Marwick, Mitchell & Co.*, 540 A.2d 726 (Del. 1988), in support of the proposition that as a matter of Delaware law, a stockholder whose litigation efforts are opposed by the corporation does not have authority to sue on behalf of the corporation until there has been a finding of demand excusal or wrongful refusal. *See* Opinion at p. 23.

In this regard, the Court of Chancery further analyzed the two-fold nature of a derivative suit, as stated in a seminal decision of the Delaware Supreme Court, *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984), as follows: "First, it is the equivalent of a suit by the shareholders to compel the corporation to sue. Second, it is a suit by the corporation, asserted by the shareholders on its behalf, against those liable to it." Opinion at pp. 24-25 (also citing prior and subsequent Delaware Supreme Court and Court of Chancery decisions). Thus, the Court's ruling that "until a derivative action passes the Rule 23.1 stage, the stockholder does not have authority to assert the corporation's claims and is not suing in the name of the corporation," *see* Opinion at 26,

is not only correct but well-supported by controlling Delaware precedents.[1] And the Court's conclusion is further supported by its analysis of *Kohls v. Kenetch Corp.*, 791 A.2d 763 (Del. Ch. 2000), upon which it relies for the proposition that the adjudication of one stockholder's individual claim does not have preclusive effect on another stockholder's ability to assert that claim. *See* Opinion at pp. 29-32.

It is on the basis of these controlling and fundamental tenets of Delaware law that the Court of Chancery concluded that, when a stockholder attempts to plead demand excusal, an earlier Rule 23.1 dismissal of a complaint filed by a different stockholder should not have preclusive effect, because privity does not exist. Thus, the Court of Chancery's conclusion in this regard is grounded in well-settled Delaware law and should not be certified for an interlocutory appeal.

Contrary to Defendants' assertions, this Court's collateral estoppel and privity rulings do not conflict directly with decisions of other courts. While the Opinion cites various cases that have held differently, these decisions are easily distinguishable from the present case in that they are based on different factual patterns and/or have a different procedural posture. For instance, in *In re Career Education Corp. Derivative Litig.*, 2007

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[1] Contrary to Defendants' assertion in the Application, ¶ 5 (pp. 3-4), *Aronson v. Lewis* does not stand for the proposition that any time the Court of Chancery denies a motion to dismiss under Rule 23.1, it has determined a substantial issue or established a legal right. To the contrary, *Aronson* specifically states that the Supreme Court accepted the interlocutory appeal in that case to address a crucial issue left unanswered by the Supreme Court's opinion in *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981), "when is a stockholder's demand upon a board of directors, to redress an alleged wrong to the corporation, excused as futile prior to the filing of a derivative suit?" *Id.* at 807. Since *Aronson* now serves as the seminal case for demand futility, the Court of Chancery's denial of a 23.1 motion to dismiss under *Aronson* does not determine a substantial issue or establish a legal right.

WL 2875203 (Del. Ch. Sept. 28, 2007), after conducting a comparison of the complaints and the arguments in both the Delaware action and an earlier filed derivative lawsuit pending in Illinois federal court, the Court of Chancery decided that the Delaware plaintiffs were precluded from re-litigating the issue of demand futility based on the Illinois court's previous determination of that issue in the context of essentially the same allegations and claims. That is quite unlike the situation here, where, among other things, the Court of Chancery was provided with only a heavily redacted version of the California complaint, it was not provided with the briefing submitted to the California court, the Plaintiffs here set forth a *Caremark* claim that the California plaintiffs were not pursuing, and the opinion of the California district court failed to reference numerous allegations and underlying documents that form the basis of Plaintiffs' claims here.

Defendants further assert that a Rule 23.1 dismissal for failing to plead demand futility precludes successive shareholders from re-litigating demand futility when the two actions are based ***on the same facts***. *See* Application, ¶ 7 at pp. 4-5 (emphasis added). Critically, however, Defendants never made that type of showing here. Defendants did not provide the Court or Plaintiffs with the actual complaint filed in California (providing only a heavily redacted version of the complaint). Nor did they provide the Court of Chancery with the briefs submitted on the dismissal motions in the California case. Thus, Defendants failed to show that the facts alleged in the case at bar were merely duplicative of the facts alleged in the California court. And the California court's decision certainly did not provide a basis for such a conclusion, given not only its brevity but also the paucity of references to the complaint or underlying documents in that case. While this

Court undertook an extensive investigation of the facts underlying the Complaint here, citing not only to allegations in Plaintiffs' Complaint but also to certain documents provided by Defendants in support of their motions to dismiss (*see* Opinion at pp. 2-10 & 69-81), there was no indication whatsoever that any such documents were presented to, or considered by, the California court. Thus, even under the standard they themselves advocated, Defendants failed to show that the two cases were based on the same facts.

Second, the Court of Chancery's alternate basis for declining to give preclusive effect to the California decision, *i.e.*, that the California plaintiffs did not adequately represent Allergan, similarly does not warrant interlocutory review by the Supreme Court. As an initial matter, whether the Court of Chancery is correct in so holding is not a matter that needs to be reached now, since the Opinion makes clear that this is an "independent basis" for declining to give collateral estoppel effect to the California decision. *See* Opinion at p. 37. Moreover, while the Court of Chancery's formulation of the issue may be characterized as ground-breaking, the analysis cites numerous Delaware opinions suggesting that a fast-filing plaintiff who does not first conduct a meaningful investigation has not provided adequate representation. *See* Opinion at pp. 37-38 (*citing, e.g., King v. Verifone Hldgs., Inc.*, 994 A.2d 354 (Del. Ch. 2010); *Baca v. Insight Enters., Inc.*, 2010 WL 2219715 (Del. Ch. June 3, 2010)). Thus, interlocutory review is not warranted on this basis either.

As more fully set forth herein, there is no need or occasion for immediate review by the Delaware Supreme Court of the Opinion issued by this Court. Rather, now that the Opinion has been issued, and especially given the broad coverage the decision

received (which Defendants tout in their Application), this Court and the Delaware Supreme Court should allow derivative litigation practices to evolve in light of the holdings in the Opinion. While Defendants contend that the Opinion will have "widespread ramifications," at this point the holdings at issue are limited to the present case and its specific fact pattern. Moreover, as the Court chronicled, Delaware courts have "long exhorted potential derivative plaintiffs to use Section 220 to investigate their claims and obtain corporate books and records *before* filing derivative litigation," further noting many derivative complaints not based on Section 220 documents that were dismissed, and some cases that were initially dismissed but ultimately upheld after the plaintiff utilized a Section 220 demand to plead a more particularized complaint. *See* Opinion at p. 51; *see also id.* at pp. 51-53 & notes 22-25. Thereafter, appropriately applying Delaware law with respect to the sufficiency of a complaint, this Court allowed this case to proceed in light of the well-reasoned conclusions that it reached, after a full investigation of Plaintiffs' Complaint, full briefing by the parties, and oral argument (which the California district court did not allow).

Since the Court's conclusions were based on well-settled law, and the inadequate representation finding was cited in the Opinion as an "independent basis" for declining to give collateral estoppel effect to the California decision, the Opinion should not be certified for interlocutory appeal pursuant to Supreme Court Rule 42.

ARGUMENT

A. Defendants' Application For Interlocutory Appeal Fails To Satisfy Rule 42

An application for certification of interlocutory appeal will be granted "only in extraordinary circumstances." *O'Neill v. Eden,* 941 A.2d 1019 (Del. 2008). The applicant must show that the interlocutory order: (i) determined a substantial issue; (ii) established a legal right; and (iii) meets one or more of the five enumerated criteria under Rule 42(b). Donald J. Wolfe and Michael A. Pittenger, *Corporate & Commercial Practice In the Delaware Court of Chancery* §14-4 at 14-6 (2008). All three prongs must be met. Here, of the five criteria under Rule 42(b), Defendants invoke two: (1) they assert that certification is appropriate pursuant to Rule 41 because the questions raised in their Application are "of the first instance" in Delaware and are the subject of conflicting trial court decisions; and (2) they claim that resolution of the appeal will terminate the litigation and serve justice.

As shown below, Defendants are wrong on both parts of their Rule 42(b) analysis.

As a preliminary matter, however, Defendants are also wrong in arguing that the denial of a motion to dismiss on the ground that a plaintiff has demonstrated demand futility is immediately appealable because such a ruling (i) determined a substantial issue, and (ii) established a legal right. The case cited by Defendants for this proposition, *Aronson v. Lewis,* as shown above at pp. 3-4 & n.1, certainly does not establish such a right of appeal. Moreover, the Court of Chancery, in *Stepak v. Pioneer Texas Corp.*, 1982 WL 8775 (Del. Ch. July 7, 1982), held firmly that no such immediate appeal is warranted. In *Stepak,* the Court stated the "sole issue presented is whether or not a

holding that a demand need not be made on the corporate defendant in a derivative suit is an appealable interlocutory order." *Id.* at *1. After noting the requirements of Rule 42, the Court continued:

> For the following three reasons I am of the opinion that the Court's ruling is not appealable as an interlocutory order.
>
> First of all, the order did not establish a legal right. Thus, the order is analogous to a ruling on whether or not a cause of action is barred by the statute of limitations. In *Levinson v. Conlon,* Del. Supr., 385 A.2d 717 (1978), the Delaware Supreme Court held that an adverse ruling on whether the statute of limitations barred the plaintiffs' cause of action did not establish a legal right. Rather, the Court determined that an affirmative defense was not available, and the consequence of the decision was that the parties must proceed to trial, a ruling which our cases have held is not the basis for an interlocutory appeal. See, e.g., *Brunswick Corporation v. Bowl-Mor Company, Inc.,* Del. Supr., 297 A.2d 67 (1972); *Hoofe v. Keane Corp.,* Del. Supr., 269 A.2d 276 (1971); *Cross v. Hair.*, Del. Supr., 258 A.2d 277 (1969). Indeed, the rights of the parties as they go to trial remain unchanged.
>
> Similarly, in the case at bar, the Court has merely determined that an affirmative defense was not available. The Court did not determine an issue essential to the position of the parties regarding the merits of the case. Moreover, as in *Levinson*, either party may yet prevail at the trial level. Hence, the instant order does not establish a legal right.
>
> Secondly, the question of whether a demand is necessary, as are other questions concerning derivative actions, is a matter addressed to the sound discretion of the Court of Chancery, invoking as it does, important policy considerations. *See* Chancery Rule 23.1. As such, the instant order is a discretionary and routine matter better left for final disposition by the trial court.
>
> Lastly, because the instant order is procedural and discretionary, finding it appealable as an interlocutory order would tend to exacerbate two highly undesirable problems inherent in them, namely, the fragmentation of a case and a delay in its final disposition. *Levinson v. Conlon,* supra.

> For the foregoing reasons, I deny the defendant's motion for certification of an interlocutory appeal pursuant to Rule 42, and it is SO ORDERED.

Id.

Here, the Court's ruling that Plaintiffs are entitled to continue this action on behalf of Allergan notwithstanding that Plaintiffs did not make a demand on the Board to prosecute the case is similarly not an appealable order. The Opinion did not "determine an issue essential to the position of the parties regarding the merits of the case." This Court's rejection of the Defendants' position that the California court ruling collaterally estops Plaintiffs from continuing with their action was, similarly, an interlocutory ruling that did not establish any legal rights and will not be a substantial issue on the merits of the case. To the contrary, the right of a shareholder to bring a derivative case is well-established under Delaware law, as are the legal standards by which allegations of demand futility in a complaint are to be judged. Thus, while the Opinion applied well-settled legal standards to the facts alleged in the Complaint, the Opinion did not establish Plaintiffs' legal right – which was established by the Delaware legislature – to bring this action.

Because the Opinion did not establish a legal right or determine a substantial issue related to the merits of this action, the Opinion should not be certified for interlocutory review.

B. There Is No Novelty Or Conflict On The Issue Of Privity

Defendants' Application does not establish that this Court's Opinion presents the type of "extraordinary circumstance" sufficient to warrant certification of an interlocutory appeal. As explained below, the question of privity for collateral estoppel purposes is

neither a question of law of the first instance in Delaware, nor truly a source of conflicting trial court decisions. Absent such a showing, Defendants have failed to satisfy Rule 42.

1. Delaware Law Is Well-Settled On The Question Of Privity

In ruling that the collateral estoppel doctrine does not bar the instant suit, the Court found the absence of privity between Plaintiffs here and the California plaintiffs to be dispositive. The Court's decision rests soundly on longstanding and established Delaware law. *See* Opinion at pp. 14-36.

To begin with, citing exhaustively to Delaware law, the Court reasoned that a finding of demand excusal or wrongful refusal is a necessary predicate to a stockholder's authority to sue on the corporation's behalf and, thus, to the determination of privity:

> . . . [A]s a matter of Delaware law, a stockholder whose litigation efforts are opposed by the corporation does not have authority to sue on behalf of the corporation until there has been a finding of demand excusal or wrongful refusal. In *Rales v. Blasband*, the Delaware Supreme Court addressed this issue:
>
> > Because directors are empowered to manage, or direct the management of, the business and affairs of the corporation, the right of a stockholder to prosecute a derivative suit is limited to situations where the stockholder has demanded that the directors pursue the corporate claim and they have wrongfully refused to do so or where demand is excused because the directors are incapable of making an impartial decision regarding such litigation.
>
> 634 A.2d 927, 932 (Del. 1993) (citation omitted). In *Kaplan v. Peat, Marwick, Mitchell & Co*., the Delaware Supreme Court was equally clear:
>
> > [P]re-suit demand under Chancery Court Rule 23.1 is an objective burden which must be met in order for the shareholder to have capacity to sue on behalf of the corporation. *The right to bring a derivative action does not*

> *come into existence until the plaintiff shareholder has made a demand on the corporation to institute such an action or until the shareholder has demonstrated that demand would be futile*.
>
> 540 A.2d 726, 730 (Del. 1988) (emphasis added). Delaware Court of Chancery decisions have long expressed these same principles. *See, e.g.*, *Ainscow*, 180 A. at 615 ("[A] stockholder has no right to file a bill in the corporation's behalf unless he has first made demand on the corporation that it bring the suit and the demand has been answered by a refusal, or unless the circumstances are such that because of the relation of the responsible officers of the corporation to the alleged wrongs, a demand would be obviously futile . . . ."); *accord Maldonado v. Flynn*, 413 A.2d 1251, 1262 (Del. Ch. 1980) ("The stockholder's individual right to bring the action does not ripen, however, until he has made a demand on the corporation which has been met with a refusal by the corporation to assert its cause of action or unless he can show a demand to be futile."), *rev'd on other grounds*, *Zapata Corp. v. Maldonado*, 430 A.2d 779, 784 (Del. 1981) ("[W]here demand is properly excused, the stockholder does possess the ability to initiate the action on his corporation's behalf.").

See Opinion at pp. 23-24. Absent authority to sue in the corporation's name, the Court concluded that privity cannot exist between shareholders of the corporation and, consequently, "a decision *granting* a Rule 23.1 dismissal cannot have preclusive effect." *Id*. at pp. 14-15.

This holding is not novel to Delaware law. As the Court went to great lengths to explain, a shareholder's authority to sue on behalf of the corporation only upon a finding of demand excusal or wrongful refusal "flows from the two-fold nature of the derivative suit" announced nearly three decades ago by the Delaware Supreme Court in *Aronson v. Lewis*, and eight decades earlier by the Chancery Court in *Cantor v. Sachs*, 162 A. 73, 76 (Del. Ch. 1932). *See* Opinion at pp. 24-26. From this precedent, the Court reasoned that "[u]ntil a Rule 23.1 motion is denied or the board decides not to oppose the derivative

action, the stockholder plaintiff is only suing to 'compel the corporation to sue.'" *Id*. at p. 26 (citing *Aronson*).

Indeed, citing to *Kohls v. Kenetech Corp*., 791 A.2d 763 (Del. Ch. 2000), yet another Delaware case, the Court noted that, even in the context of individual stockholder claims, the notion that one stockholder's suit does not have preclusive effect against another stockholder's suit for the same claim is hardly non-precedential. *See* Opinion at pp. 29-32. Rather, it is rooted in the principle that "'[a] person who is not a party to an action is not bound by the judgment in that action.'" *Id*. at p. 29 (citing *Kohls*) (quoting Restatement (Second) of Judgments § 62 cmt. c (1982)). As the Court duly noted, an exception to this "no preclusion" principle, as set forth in *Kohls*, is a "properly commenced and maintained representative action," that is, where the stockholder has authority to sue on behalf of the corporation or a class of other stockholders. *Id*. at pp. 31-32.

Finally, further citing to *West Coast Management & Capital, LLC v. Carrier Access Corp*., 914 A.2d 636, 642 (Del. Ch. 2006), and Rule 15(aaa), both established Delaware authorities, the Court explained that "dismissal pursuant to Rule 23.1 is 'with prejudice *to the named plaintiffs only*.'" *See* Opinion at pp. 34-35 (emphasis added). Thus, "when a different stockholder attempts to plead demand excusal [or wrongful refusal], an earlier Rule 23.1 dismissal should not have a preclusive effect." *Id*. at p. 34. Here, of course, the California plaintiffs were never authorized to assert their derivative claims on behalf of Allergan, and it is undisputed that the California plaintiffs (all of whom are individual investors) are separate from, and not in privity with, Plaintiffs

pursuing this case in Delaware (both of which are institutional investors). It follows, then, that the California decision may not be given preclusive effect to terminate the claims being asserted by Plaintiffs in this Court.

Against this powerful recitation of longstanding and well-settled Delaware law and principles, Defendants' depiction of the privity question as one of "first impression" is legally unsupportable and unpersuasive. Delaware Law is abundantly clear that, until a Rule 23.1 motion is denied or the board assents to the derivative action, a stockholder does not have the authority to sue on the corporation's behalf and, therefore, lacks privity with other stockholders.

2. There Is No Conflict Of Decisions On The Privity Question

That certain federal and state courts have decided the question of privity differently than the Court here is of no moment. As the Court explained, while these cases are premised on the "legal truism that a derivative plaintiff sues in the name of the corporation" (*see* Opinion at p. 23), Delaware law goes much further. Rather: "These cases miss that *as a matter of Delaware law*, a stockholder whose litigation efforts are opposed by the corporation does not have authority to sue on behalf of the corporation until there has been a finding of demand excusal or wrongful refusal." *Id*. at p. 23 (emphasis added).[2]

[2] The Opinion further notes, in this regard, that Defendants should be estopped from asserting a collateral estoppel argument against the Delaware Plaintiffs after the same Defendants argued successfully in the California case that the California plaintiffs lacked the authority to assert claims *derivatively* on behalf of Allergan. *See* Opinion at p. 27 & n.10 (emphasis in original).

Significantly, the Court of Chancery in *West Coast Management*, 914 A.2d at 643, n.22, rejected the so-called "conflicting" decisions upon which Defendants rely, finding them of "dubious" authority. There, the Court of Chancery explained why "equitable considerations" rendered them so: "While a prior suit by another plaintiff with similar allegations of demand futility may bar a second plaintiff from filing the same suit, if the second plaintiff makes substantially different allegations of demand futility based on additional information, issue preclusion, from both a logic and fairness standpoint, would not apply." *Id*. Clearly, the Court here abided by Delaware law in refusing to follow the other decisions.[3]

Moreover, these other decisions are materially distinguishable from the instant case. *See, e.g*., *In re Sonus Networks, Inc. S'holder Deriv. Litig*., 499 F.3d 47, 56 (1st Cir. 2007) (privity not analyzed under Delaware law); *Arduini ex rel. Int'l Game Tech. v. Hart*, 2012 WL 893874, at *1, *3 (D. Nev. Mar. 14, 2012) (same); *In re Bed Bath & Beyond Inc. Deriv. Litig*., 2007 WL 4165389, *3, *7-8 (D.N.J. Nov. 19, 2007) (same); *Hanson v. Odyssey Healthcare, Inc*., 2007 WL 5186795, *1, *5 (N.D. Tex. Sept. 21, 2007) (same); *LeBoyer v. Greenspan*, 2007 WL 4287646, *1, *3 (C.D. Cal. June 13, 2007) (same); *Henik ex rel. LaBranche & Co. v. LaBranche*, 433 F. Supp. 2d. 372, 376, 379-80 (S.D.N.Y. 2006) (same); *Kaplan v. Bennett*, 465 F. Supp. 555, 560 (S.D.N.Y. 1979) (same); *Carroll ex rel. Pfizer, Inc. v. McKinnell*, 2008 WL 731834 (N.Y. Sup. Ct. 2008) (although the earlier action pled demand futility and the subsequent action pled

[3] As noted above, not only did Defendants fail to show that the allegations in the Complaint at bar were duplicative of the allegations in the California action, but the California decision makes it clear that the plaintiffs in that case were not pursuing a *Caremark* claim, which Plaintiffs here are pursuing.

demand refusal, both actions pled the same allegations of lack of disinterest and independence of the board). Clearly, these cases do not present a conflict of Delaware law on the question of privity.

Nor does *In re Career Educ. Corp. Deriv. Litig.*, 2007 WL 2875203 (Del. Ch. Sept. 28, 2007), the lone Delaware decision upon which Defendants rely for this point, create a conflict. The Court of Chancery here carefully analyzed *Career Education* and rightly distinguished it on factual and legal grounds, as follows:

> Notably, the plaintiffs in *Career Education* "concede[d] that collateral estoppel or issue preclusion applie[d] to their Rule 23.1 arguments" and contended only that they should not be precluded from raising issues not addressed in the prior action. *Id*. at *7. The *Career Education* Court therefore accepted that a Rule 23.1 dismissal would have preclusive effect, did not grapple with the authority issue, and analyzed only whether (i) the plaintiffs in the prior proceeding provided adequate representation and (ii) the two cases involved different issues.

Opinion at pp. 35-36. As to the latter point, as explained above, the Court in *Career Education* undertook a comparison of the allegations and claims in the Delaware action and the earlier-filed federal action, and only after doing so did the Court of Chancery decide that the Delaware plaintiffs were precluded from re-litigating the issue of demand futility. 2007 WL 2875203 at * 11-14. Here, no such comparison was or could be undertaken because, among other things, Defendants provided the Court and Plaintiffs with a heavily redacted version of the California complaint, thereby rendering any such comparison impossible to conduct. Indeed, the California dismissal order itself precluded any meaningful comparison of allegations, as it failed to refer to many of the allegations contained in the operative complaint here. *Career Education* is patently inapposite, and the Court of Chancery need not have followed it.

C. The Court's Ruling On Inadequate Representation Does Not Conflict And Is Supported By Delaware Precedent

The primary basis for the Court finding that collateral estoppel did not apply was a lack of privity between Plaintiffs here and the unrelated, individual plaintiffs in the California federal court case. As the Court makes clear, the inadequate representation of the California plaintiffs was a separate and independent finding that also rendered collateral estoppel inapplicable. *See* Opinion at pp. 37, 82.

The Court's ruling that the California plaintiffs were inadequate representatives does not conflict with previous decisions of the Supreme Court and does not present an issue of first impression. The Supreme Court has given the Court of Chancery discretion in addressing a derivative plaintiff's failure to conduct a books and records demand prior to filing a plenary action. *See, e.g., King v. Verifone Holdings, Inc.*, 12 A.3d 1140, 1151 (Del. 2011); *Grimes v. Donald*, 673 A.2d 1207, 1216 n. 11 (Del. 1996) (*citing Rales v. Blasband*, 634 A.2d at 934-35 n.10) ("[n]othing requires the Court of Chancery or any other court having appropriate jurisdiction to countenance this process by penalizing diligent counsel who has employed these methods, including Section 220, in a deliberate and thorough manner in preparing a complaint that meets the demand excused test of *Aronson*."). In *King*, the Supreme Court acknowledged "[t]o the extent that the premature filing of a plenary derivative action may be a potential abuse," remedies are available to the Court of Chancery. 12 A.3d at 1151. The Supreme Court further suggested that certain remedies are available to the Court of Chancery, including denying lead plaintiff status to "fast-filers," dismissing the derivative complaint with prejudice and without leave to amend as to the named plaintiff, and granting leave to amend

conditioned on the plaintiff paying defendants' attorneys' fees incurred on the initial motion to dismiss. *Id*. at 1151-52. Notably, the Supreme Court explicitly stated that these examples were "intended only as illustrative" and "that such remedies are for the plenary court to fashion and impose in the plenary action." *Id*. at 1152.

Moreover, contrary to Defendants' argument, the Opinion does not duplicate or go beyond the actions taken by the Court of Chancery in *White v. Panic*, 783 A. 2d 543 (Del. 2001) and *King II*, 12 A.3d 1140. In *White v. Panic*, the Court of Chancery refused to "give a broad reading to the facts alleged" in a derivative complaint at the motion to dismiss stage or "infer from them the existence of other facts that would have been proven or disproven by a farther pre-suit investigation at the motion stage because the Plaintiff failed to conduct a books and records demand prior to filing." 783 A.2d at 549. Rejecting the Court of Chancery's new standard, the Supreme Court stated:

> a perceived deficiency in the plaintiff's pre-suit investigation would not permit the Court of Chancery, or this Court on appeal, to limit its reading of the complaint or to deny the plaintiff the benefit of reasonable inferences from well-pleaded factual allegations. If the plaintiff fails to undertake appropriate investigation before filing suit, the plaintiff will simply have fewer "particularized facts" from which the court may draw reasonable inferences.

Id. at 549-50.

Likewise, in *King II*, the Court of Chancery found that a shareholder lacked a proper purpose under 8 Del. C. § 220 because the shareholder had filed a derivative action in a California federal court and was dismissed without prejudice by the California court before making a books and records demand. 12 A.3d 1140, 1144-45. The Supreme Court reversed the Court of Chancery's finding, holding that long-standing Delaware

precedent recognizes as a proper purpose the inspection of books and records to aid a plaintiff in pleading demand futility where a previously filed plenary action was dismissed without prejudice and with leave to amend. *Id*. at 1150. The Supreme Court went on to caution, however, that filing a plenary derivative action without having first resorted to the inspection process afforded by 8 Del. C. § 220 may well prove imprudent and cost-ineffective. *Id*.

Here, the Court's finding that the California plaintiffs were inadequate representatives did not impose "a new judicially created demand requirement," as Defendants argue. Rather, the finding of the California plaintiffs' inadequacy merely served as an alternative basis for the Court's decision that Plaintiffs here are not and should not be bound by a decision reached by the California federal court in a case brought by other plaintiffs who had not sought documents through a Section 220 books and records demand. This finding falls squarely within the Court's discretionary powers to fashion a remedy in the plenary action, in accord with the Supreme Court and Court of Chancery decisions cited above.[4]

[4] Defendants assert that not only should this Court certify for interlocutory review the Court's ruling on whether the California decision collaterally estopped Plaintiffs from proceeding with this action, but that it should certify the entire decision, including its findings on the merits of the Defendants' motions to dismiss. Plaintiffs believe the Court's analysis of the Complaint as a whole and the documents underlying certain allegations in the Complaint that Defendants appended to the briefs they submitted in support of their dismissal motions, are prototypical interlocutory rulings that are not subject to immediate appeal. If the Court would like any further briefing on this issue, Plaintiffs would be pleased to supply it. However, Plaintiffs believe that Defendants' suggestion in this regard is so far beyond the bounds of Rule 42 and does not require any response to show its lack of merit.

CONCLUSION

Defendants' Application falls short of Rule 42's requirements for certification of an interlocutory appeal. The Court carefully considered the issues of collateral estoppel, privity, and inadequate representation, and its conclusions on these issues, as well as the merits of Defendants' motions to dismiss, rest unequivocally on established Delaware law. For these reasons, and for all of the reasons set forth above, Plaintiffs respectfully submit that the Court should deny Defendants' Application in its entirety.

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