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.	:	Civil Action No. 5795-VCL
DAVID PYOTT, HERBERT W. BOYER, LOUIS J. LAVINGNE, 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.	:	

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Chancery Court Chambers
New Castle County Courthouse
Wilmington, Delaware
Friday, July 6, 2012
12:05 p.m.

- - -

BEFORE: HON. J. TRAVIS LASTER, VICE CHANCELLOR

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ORAL ARGUMENT-MOTION TO STAY, APPLICATION FOR CERTIFICATION OF INTERLOCUTORY APPEAL
RULING OF THE COURT

APPEARANCES:
(By telephone):

PAMELA S. TIKELLIS, ESQ.
SCOTT M. TUCKER, ESQ.
Chimicles & Tikellis LLP
-and-
SCOTT R. SHEPHERD, ESQ.
of the Pennsylvania bar
Shepherd, Finkelman, Miller & Shah, LLP
-and-
JEFFREY W. GOLAN, ESQ.
of the Pennsylvania bar
Barrack, Rodos & Bacine
for Plaintiffs

KENNETH J. NACHBAR, ESQ.
SHANNON E. GERMAN, ESQ.
Morris, Nichols, Arsht & Tunnell LLP
-and-
WAYNE W. SMITH, ESQ.
of the California bar
Gibson, Dunn & Crutcher LLP
for Individual Defendants

CATHY L. REESE, ESQ.
JEREMY D. ANDERSON, ESQ.
Fish & Richardson P.C.
for Nominal Defendant Allergan, Inc.

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THE COURT: I have one clock that says I'm three minutes late and one clock that says I'm three minutes early, so I'm not sure which it is, but I'm happy to join you.

MS. TIKELLIS: Your Honor is right on time.

THE COURT: Ms. Tikellis, I think this is the first time you've joined us in this case. It's good to have you here.

MS. TIKELLIS: Thank you very much, Your Honor. I'm here obviously on behalf of the plaintiffs, and with me is my associate, Scott Tucker and my colleagues Jeff Golan and Scott Shepherd whom I think Your Honor is familiar with.

To the extent Your Honor wants to hear from counsel for the plaintiffs, with Your Honor's permission, Mr. Shepherd will speak on our behalf.

THE COURT: That's fine.

Whom else do we have?

MR. NACHBAR: Your Honor, Ken Nachbar and Shannon German here on behalf of the individual defendants and Wayne Smith and perhaps others at his shop are also on the phone.

MR. SMITH: I think it's just me.

MS. REESE: Good afternoon, Your Honor. Cathy Reese and Jeremy Anderson of Fish & Richardson on behalf of the nominal defendant, Allergan.

THE COURT: Great. Well, welcome everyone. I'm happy to proceed however you wish.

Mr. Nachbar, I think it's your application.

MR. NACHBAR: It is.

Thank you, Your Honor, for hearing us on a quick basis. As Your Honor knows, Supreme Court Rule 42 governs this application, and that rule has three requirements; that the ruling determine a substantial issue, that the ruling establish legal rights and that the ruling meet one of the other requirements of Rule 42.

I think that the first two requirements here are pretty easily met. The opinion determined a substantial issue, whether a pre-suit demand under Rule 23.1 was required, and it established a legal right, the right of the plaintiffs to prosecute this action on behalf of Allergan.

This same issue was certified for an interlocutory appeal in Aronson which is, at least as

to this aspect of the case -- I'm not talking about the third prong yet, but on the first two prongs, factually indistinguishable.

Like the present case, it was a denial of a Rule 23.1 motion and 12(b)(6) motion. And it determined the same issue that this case determined and established the same legal right that this case established.

THE COURT: Mr. Nachbar, let me ask you a question and interrupt. How would you go about distinguishing when Rule 23.1 denials should go up and when they shouldn't?

MR. NACHBAR: Well, I think the third prong is the distinguishing prong. So that's what I'll get to in a minute. I think that unless you have facts that I can't think of as I'm sitting here right now, I think the first two prongs are always going to be met and you really look to the third prong.

Look, the rule obviously is discretionary, and I think the prongs are all guidance for the Court's discretion in the end. And I don't think the Court has ever been literalistic or really formulistic in its application. It's really discretionary.

But they do lay out the criteria to guide discretion, so I think the third prong -- at the time of Aronson, you could understand why the Court took that because it was, at the time, a novel issue. It was, as Your Honor may recall, a majority stockholder who was awarded allegedly excessive compensation by a financially disinterested independent board.

And the question was in the shadow of a controlling stockholder, in a transaction in which the controlling stockholder was getting I think it was paid compensation in that case, was a demand required. The Supreme Court had never addressed that issue. The Chancery Court said demand was excused. The Supreme Court took the case, and as we all know, reversed.

The next case that came up that was identical to Aronson, you wouldn't have an interlocutory appeal, I would think, or something that was similar along the same lines because it wouldn't be a novel issue.

Now, if it came out differently, then maybe you would have an interlocutory appeal because of an inconsistency in precedents, but the point is that that case was taken, I think, because it was a

novel issue, it was an important issue for the State of Delaware. The Supreme Court took it.

Now, plaintiffs' only attempt to deal with Aronson, as far as I can tell, is to quote Chancellor Marvel's opinion from 1982 in Stepak, but Stepak, of course, predates Aronson. It's possible that Aronson was expressly -- that Stepak was expressly overruled in Aronson.

The Supreme Court's holding accepting the interlocutory appeal in Aronson is not available, so I don't know precisely what it says, but if it didn't explicitly overrule Aronson about the first two prongs, it certainly implicitly -- Aronson implicitly overruled Stepak because it came out differently on facts that I think are really indistinguishable.

THE COURT: I think we're also in a different world because at the time of Stepak, and really for a long time after Stepak, you could legitimately argue that a Rule 23.1 determination was fact-specific and carried elements of discretion, and it was something (because it involved necessarily some degree of judgment) that the Court of Chancery was going to be developing expertise in, and therefore, there would be an appropriate role for Supreme Court

deference on a Rule 23.1 review.

We all know now that post-Brehm, it's matter-of-law review. So that's another, I think, bullet against the Stepak cite because it seemed to rely, at least in some significant part, on the discretionary nature of the determination.

MR. NACHBAR: We agree with that. So that really brings us to the important prong I think for today's exercise, which is the third prong.

And, there, there are several categories that we think are implicated; does the ruling at issue conflict with prior decisions, does it decide issues of first impression, does it involve a case dispositive issue, would review serve the interests of justice.

Now, those are fairly elastic, at least the last two of them, criteria. The first two are probably a little bit less elastic. The important thing, from our perspective, Your Honor, is that the opinion was quite candid, we thought, in recognizing that it conflicted with prior similar cases.

Now, remarkably, plaintiffs base their opposition to this application on disagreeing with Your Honor about that. But as the opinion recognizes,

a growing body of precedents, and I think that's Your Honor's word, six cases cited in the opinion, have held that a Section 23.1 dismissal collaterally estops other stockholders from claiming demand futility on similar grounds.

I think the opinion is, again, quite forthright in not trying to reconcile those cases, not trying to factually distinguish them, but rather to come out differently on the law and say that those cases aren't really well reasoned and didn't consider the issue carefully enough.

What plaintiffs essentially argue is that Your Honor's opinion is correct and it better comports with precedents concerning privity that underlie the six other opinions and Your Honor's opinion.

Now, the Supreme Court may or may not ultimately agree, but that is not today's question. Today's question is whether the opinion conflicts with precedent. The opinion, I think, quite squarely says that it does, and I don't think that plaintiffs arguments to the contrary are convincing.

Really, the only case that they discuss in any detail is Career Education, and what

they say about that case is that, well, the Court had the entire complaint in that case, and the complaint here was redacted, so Your Honor couldn't really tell if the claims in California were similar to the claims here and the demand futility allegations were similar.

I think that's, frankly, absurd. Plaintiffs have not pointed to any claim in this case that wasn't within the ambit of what was alleged in California, and while there are some redactions to the complaint, you can tell from the complaint and also from the Court's opinions, which was not just one opinion, but actually three opinions, because there was an initial dismissal, there was a dismissal of the amended complaint and there was a motion for reargument on the amended complaint, the grounds for alleging demand futility in that case are pretty clear, and they're not materially different in any respect from the grounds for alleging demand futility in this case.

So Career Education, I don't think, can be fairly distinguished on the grounds that there were some redactions to the complaint here.

All that the plaintiffs say about the other cases is they didn't apply Delaware law, which

really brings us to, I think, the second point of where the opinion conflicts with, we think, precedent. Notably, the Thompson case and the West Coast Management case rather squarely hold that if the rendering court would apply collateral estoppel against a subsequent shareholder plaintiff in a derivative case, this Court must preclude a subsequent plaintiff from relitigating the issue that was determine by the rendering court.

Now, here, the rendering court, the Central District of California, would have applied collateral estoppel to preclude a new stockholder from relitigating demand futility. We know that because the LeBoyer case squarely so holds.

Now, the opinion, I think, fairly read, says that the LeBoyer case was wrongfully decided. That may or may not be correct, but again, that's not today's question. Today's question is whether there's a conflict, and we think that there surely is.

The Thompson court, the West Coast Management court, wouldn't have looked beyond the superficial holding of LeBoyer. It would have applied collateral estoppel simply because LeBoyer applied

collateral estoppel.

This court reached a different result. I think an appeal, whether it's taken now or taken later, will determine whether the Court was proper in reaching the result that it did. But clearly we think the opinion reaches a different result than those prior courts would have reached, and that is a conflict in precedent.

It is absolutely a ground for satisfying the third prong of Rule 42, and frankly, we think that everybody, including the plaintiffs, would be better off if an interlocutory appeal were permitted so that we can get these threshold issues determined by the Supreme Court now.

The Court also had, of course, the alternate ground for its holding, and that was that the California representatives were inadequate representatives. Now, the plaintiffs say, well, adequacy of representation is something that has a long history in the Delaware Court of Chancery; there's nothing novel, nothing conflicting with other precedent in the Court's holding.

We disagree. We understand the holding to be that one who fails to obtain books and

records prior to filing a derivative case, even if that plaintiff has significant other sources of information, such as some of the criminal papers that were publicly available here, is automatically an inadequate representative.

Moreover, the inadequacy holding was applied to plaintiffs who weren't before the Court. Typically when you have inadequacy of representation, it's somebody who is before the Court, has notice and opportunity to be heard. They explain why they really are an adequate representative, and the Court determines that.

Here, the holding was applied to California plaintiffs who weren't before the Court and weren't heard on the issue, and the basis for the holding was simply that they hadn't made a 220 demand.

I think that is novel because there certainly are a lot of derivative cases that have proceeded in the absence of a 220 demand. Some have resulted in demand ultimately being excused, some have resulted in motions to dismiss being granted.

Finally, I would submit that these are very, very important issues. Your Honor issued an innovative ruling. It has important effects. We've

cited in our papers some of the authorities that have already been discussed the case. There are no doubt others that we haven't attached.

The case will have important effects on not only the litigants in this case, but all derivative litigations going forward. And we believe that it's clearly in the interests of justice that an interlocutory appeal be certified.

We have an important ruling. Let's get the Supreme Court's view on it. It may well be that it's affirmed; it may well be that it's reversed, but I think the litigants to this case, and really the corporate bar generally, will be best served if the Supreme Court is permitted to express its view on that sooner rather than later.

Unless Your Honor has questions, we also have a stay of proceedings, but I'm wondering if addressing the interlocutory appeal first and hearing from the other side on that might be preferable.

THE COURT: You ought to address them both together. It dovetails and affects both because of the question of "an important issue of law" and also because of "the likelihood of preliminary view of the merits on appeal."

Why was my Allergan ruling akin to legislation or regulation?

MR. NACHBAR: I'm not sure that it is.

THE COURT: Well, you said in note four of your paper that it was.

MR. NACHBAR: I'm trying to locate exactly what we said. I apologize. I have the other side's papers.

THE COURT: That's all right. It's footnote four on page 20.

MR. NACHBAR: I'm sorry, could you tell me one more time, legislation or --

THE COURT: Regulation.

MR. NACHBAR: Well, it certainly, we think, can be seen as regulation and in some sense legislation in the sense that it's reaching a different result.

THE COURT: That it's a novel ruling.

MR. NACHBAR: Because it's a novel ruling and certainly --

THE COURT: Is it true that whenever a court addresses a question of first impression it's legislating?

MR. NACHBAR: I think one has a better

argument that it's legislating when the Court reaches a different result from prior courts. I'm not sure that it's necessarily a first -- I think if it's a case of first impression and you say legislating, that's overly rhetorical at best, because obviously a court -- if it's an issue that's never been presented before, a court has a duty to decide it. That's its obligation.

So if you want to say, well, it's legislating, then no matter how it came out, I guess you could always say it's legislating. I think that's probably a little bit overly rhetorical.

MR. SMITH: I think Gibson Dunn takes the credit or the fall for that footnote. The reason it's a footnote is it wasn't a major point. But our thought, Your Honor, related to the creation of the presuming of an inadequate plaintiff --

THE COURT: Let me ask you something, Mr. Smith. Is what bothers you about that -- what is it about that that bothers you? Is it that it's a presumption?

MR. SMITH: Well, it's a presumption that was applied here without an analysis of any other factors. So it kind of changes, in our view, the

dynamics, rightly or wrongly. And I understand the desire to end the fast filers, but the thought is it greatly changes the existing dynamic under the statutory scheme where plaintiffs routinely file derivative cases prior to going through a 220 procedure.

THE COURT: It certainly does that. But why is that "legislation or regulation"?

MR. SMITH: Well --

THE COURT: Which is not something I think the courts do.

MR. SMITH: Because it potentially changes the regulatory scheme where access to 23.1 proceedings can effectively be barred until there is a requirement to go through the 220 proceeding if that presumption is applied rigorously and in the absence of the analysis of other factors.

Then it becomes almost an irrebuttable presumption, and it changes the statutory scheme where you have two different procedures, and now the process is that you must go through a 220 before you get to the 23.1.

That was our thought, Your Honor. It's in a footnote because it was not one of our main

points.

THE COURT: Right, and I know that, but this is important because you don't get to throw things in footnotes without thinking about them. You have to have a real reason for putting things in footnotes.

What I'm not clear about is there's a lot of presumptions out there in our law. There are business judgment rule presumptions which you all embrace and rely on quite heavily. There's pleading presumptions. Like Rule 23.1 has presumptions that you have to overcome by non-conclusory allegations.

Now, are those legislative? I think you'll actually find that they're deeply entrenched in the common law. You want to label those legislative and regulatory and hence improper?

MR. SMITH: Your Honor, I didn't necessarily say -- I guess if it's regulatory or statutory, it maybe becomes improper for the Court to do it, but the point was that it greatly changes the statutory scheme of the dynamics between a 220 demand and a 23.1 proceeding if that presumption is applied without the analysis of any other factors.

We may be wrong in how we looked at

how you applied it, but we saw you called it a presumption, but we didn't see the weighing of any other factors, so that the presumption becomes an almost irrebuttable presumption, which in that context, in our view, does change the statutory dynamic or the relationship because it creates a new requirement to file a 23.1 proceeding. One must go through 220 before one can file a 23.1.

THE COURT: All right. Let me come up with a question for Mr. Smith, although I'm happy to have either of you answer it.

Could you elaborate on your Commerce Clause theory that appears on page 17 of the application?

MR. SMITH: The Commerce Clause issue is one that -- I apologize because I'm not a constitutional law scholar. One of our lawyers who is an appellate specialist in the constitutional arena felt that the collateral estoppel and the effect on the full faith and credit judgments implicates the commerce clause.

THE COURT: Well, that's actually not what you said. What you actually said was that it raises a Commerce Clause issue that's "a question of

first impression whether Delaware may constitutionally regulate the economic incentives of out-of-state actors, especially out-of-state attorneys."

So this Commerce Clause argument was apparently some type of argument that it is, in fact, economic legislation that seeks to regulate out-of-state actors. It doesn't say much more than that.

So I was hoping you could spell it out a little bit more.

MR. SMITH: Well, we discussed several of this gentleman's theories, and that one relates to the fact that it makes it virtually -- I shouldn't say impossible, but a lawyer that wants to litigate these claims in another state cannot reach finality of a judgment.

None of the litigants to an out-of-state proceeding can reach finality in their litigation if they have not proceeded through 220, because that judgment is always subject to being rejected on the basis of inadequate representation.

THE COURT: Is it your position that that's true as to the actual plaintiff who sues in the other litigation?

MR. SMITH: I don't know.

THE COURT: Didn't I specifically say in the decision that collateral estoppel and preclusion principles clearly apply to the actual plaintiff who sues in the other case, because there is no question about the same party requirement?

Thus, to the extent this gentleman is suggesting that the actual parties to the other litigation can never get finality, that's dead wrong. The actual parties to the other litigation are the suing stockholder and the defendants. They get finality as to themselves.

The question is to what degree they can then apply that judgment, which is final as to themselves, to others. That's where you get the relationship issue.

But what I was trying to understand now is parsing this commerce clause issue. His theory was that the decision regulates out-of-state attorneys because out-of-state attorneys have this trouble achieving finality? Is that right?

MR. SMITH: Well, yes, attorneys and even in the party context. While the privity is satisfied, there have been cases in various jurisdictions that have looked at the preclusive

effect of even judgments where the allegation was that the representation of counsel in the prior case was inadequate.

THE COURT: As to other parties, not as to the individual stockholder plaintiff who sues.

MR. SMITH: That's correct, Your Honor.

THE COURT: So on your colleague's point, the parties to the original case are the stockholder who sued and the defendant. It may be a nominal defendant. The parties to that case get finality. There is no ability to relitigate anything as to that original plaintiff.

The question posed by your arguments is to what degree that decision, which is final as to the parties in the first case, can be applied to others who were not parties to that case.

Let me ask you something else.

MR. NACHBAR: Your Honor, before we leave that one, what I understood is that, sure, if you have a dismissal where you don't get by the first prong of Aronson or you don't get by 23.1, yes, that's correct.

What if you do get by 23.1, or what if

you settle the case and the plaintiff goes ahead and sues in California and loses, or settles the case and then there's a collateral attack because the plaintiff wasn't an adequate representative, he didn't seek a 220 paper before he filed his complaint. There's just questions.

THE COURT: Mr. Nachbar, I can answer that for you right now. I don't have the page in front of me, but I actually specifically addressed that in the decision where I talked about cases in which, under the general hornbook rule, preclusion principles clearly apply. One of those is where a settlement has been approved by a court in compliance with the requirements of 23.1. Why? Because to approve such a settlement, the Court has to make an adequacy of representation determination.

So it's in there. It specifically discussed where I talk about the reliance out of context by these other courts on the principle that the judgment is in the name of the corporation, without considering whether the person who is the stockholder as yet has authority to sue on behalf of the corporation.

I cite specific instances where it

applies, one of which is when a settlement has been approved consistent with the requirements of 23.1.

So, look, let me ask another question, because part of what I have to do is assess your chances on appeal. There's also a reference on page 17 of the application to a Due Process Clause theory. It's not spelled out at all. What is your Due Process Clause theory?

MR. SMITH: I think the due process clause is potentially two-fold, Your Honor. One, the litigant to the California proceeding, some of the litigants to the California proceeding, have been deemed to be inadequate representatives without having an opportunity to appear and be heard.

And the second is that the defendants are required to litigate repeatedly in various jurisdictions without being able to reach finality.

THE COURT: Did you all actually look at collateral estoppel cases as opposed to settlement cases to see how the adequacy of representation analysis was conducted in those cases?

MR. SMITH: We did look at a number of adequacy of representation cases, yes, Your Honor.

THE COURT: In the collateral estoppel

context?

MR. SMITH: In a variety of contexts, yes.

THE COURT: Look, now, I actually have your papers. All the citations that you cited in your papers were not in the collateral estoppel context.

MR. SMITH: That's because it's hard to find them in the collateral estoppel context, Your Honor.

THE COURT: Which ones would you point me to in the collateral estoppel context?

MR. SMITH: I don't remember. I think we cited the best cases that we found that laid out the requirements for an adequate representation. If we had some in the collateral estoppel context, I think we would have cited them.

THE COURT: All right.

Do you have anything else to say?

MR. SHEPHERD: Briefly, Your Honor, as most of these issues have been addressed at some length.

The defendants focus in their papers on what I'll call the noise that has been created in the legal press by Your Honor's articulation of some

of the factors involved in the fast filing problem. But there's nothing new about that.

Your articulation is different than maybe other courts have set out, but it's a problem that's been discussed for years, as has the injunction of the Delaware courts to use the 220 process. So there's nothing new about that.

Really, the only issue is whether or not there was sufficient privity between the Delaware plaintiffs and the California plaintiffs such that collateral estoppel would apply.

And what the defendants say is that under the Full Faith and Credit Clause, the California court, if the situation were reversed, would be required to find that collateral estoppel precluded the California case from proceeding, which is incorrect as a matter of Delaware law.

If there had been a dismissal in Delaware, Delaware rules, Chancery rules make clear, Rule 15(aaa), that the dismissal would be only as to the named plaintiffs.

So the defendant -- the theory that defendants have that makes this subject for interlocutory appeal is simply wrong. Whatever the

cases hold for a California court to hold that a Delaware dismissal was anything more than a dismissal of the individual plaintiffs claims would simply be incorrect.

As to all of the -- I don't think I have anything to say other than what the papers say as to the inadequacy of representation. It's an alternate theory. It's a formulation of what courts have said for many years, but it's not central to the Court's holding, and I don't think there's much I could add to what we've said unless Your Honor has questions.

THE COURT: I don't. Thank you.

I'm ready to give you all my ruling.

The defendants seek certification of an interlocutory appeal from my opinion dated June 11, 2012. They also seek a stay of proceedings pending the outcome of the appeal. As I will discuss, there are important issues raised by the opinion that I believe the Delaware Supreme Court should address. There's also a lot of fear-mongering and rhetoric in the application that is, frankly, disappointing. The defendants seem to be taking a kitchen sink approach. Just because the United States Supreme Court has

recently been talking about the Commerce Clause doesn't mean everybody should throw it into their briefs. For the reasons that follow, I will grant both motions.

First let's discuss certification. Certifying an interlocutory appeal is not something that any member of this Court does lightly. As Chief Justice Steele noted when he served on this Court, "There can be no mystery about the relative weight the Supreme Court places on its policy against piecemeal appeals and the possibility of avoiding judicial inefficiency in the Court below." That's from Emerald Partners, 1996 WL 361510 at page three.

In my almost three years, I guess two and a half on the Court, I have certified only one case - CNX. I thought that case was a poster child for interlocutory appeal. The Supreme Court declined to accept it. That's perfectly fine. It's their docket. They have complete discretion about whether to take an appeal.

What that discretion shows though is that although the Supreme Court sometimes speaks of "affirming" a trial court's certification decision, the certification itself is merely a recommendation.

It's like an employee who goes to his boss and says, "You know what, Boss, I really think you ought to take a look at this. This is important." The boss gets to decide to look or not. The employee is simply telling the boss that in the employee's view this is something they ought to think about looking at.

Like any good boss, the Supreme Court has given lower courts guidance about the types of things that warrant bringing cases to their attention. That guidance appears in Supreme Court Rule 42.

Rule 42(b) states: "No interlocutory appeal will be certified by the trial court or accepted by" [the Supreme Court], "unless the order of the trial court determines a substantial issue, establishes a legal right, and meets one or more of the following criteria."

Under Rule 42(b(i), one of the criteria is "any of the criteria applicable to proceedings for certification of questions of law set forth in Rule 41."

Rule 41(b) states that, "without limiting [the Supreme Court's] discretion to hear proceedings on certification, the following illustrate reasons for accepting certification." There are

three. One is an original question of law. The second is conflicting decisions, and the third is an unsettled question of law relating to constitutionality, construction, or application of a statute.

At the said at the outset, this is one of those rare cases where I recommend that the Supreme Court accept an interlocutory appeal.

As the defendants correctly observe, the Delaware Supreme Court's precedent recognizes that the denial of a Rule 23.1 motion can satisfy the first two requirements of Rule 42. The denial of a Rule 23.1 motion determines a substantial issue by deciding whether a stockholder plaintiff can displace the board of directors' authority to control a cause of action belonging to the corporation. The legal right established by the denial of a Rule 23.1 motion is the right of the plaintiff to litigate the corporation's cause of action, subject to the board's ability to re-assert itself through a special litigation committee. The granting of interlocutory appeals in Aronson and Zapata show that those two threshold requirements can be met.

Pause to note the irony in the

defendants arguing that a Rule 23.1 denial establishes a legal right; namely, and I quote, that "plaintiffs therefore have the legal right to assert claims derivatively on behalf of Allergan." That's from page four of their motion. This correct statement of the law necessarily recognizes that until a Rule 23.1 motion has been denied, the plaintiffs did not have the legal right to assert claims derivatively on behalf of Allergan. They, therefore, were not in privity with the corporation, precisely as I held in the Opinion. The defendants are thus now contending, correctly, that my opinion determined a legal right so that they can argue on appeal that it effectively did not determine a legal right. Put differently, they plan to argue on appeal that any derivative plaintiff, just by filing suit, has the right to sue on behalf of and is in privity with Allergan. If that's true, then my decision didn't determine a legal right. But for present purposes, the defendants benefit from accepting what Delaware law actually says; namely, that only the denial of a Rule 23.1 decision gives a stockholder authority to sue. Ironic.

There's an even bigger irony in the defendants' position. According to the defendants, my

decision established a legal right by letting a stockholder plaintiff sue, whereas, in their words on page six, "they prevailed after a full and fair opportunity to litigate in California, twice securing a federal judgment holding that under 8 Del. C. Section 141(b), the board of directors, not individual stockholders, should control whether, and how, the company should pursue any of the claims that the California and Delaware plaintiffs were asserting simultaneously."

That is precisely not what happens if the first dismissal is preclusion. The LeBoyer decision holds that a Rule 23.1 dismissal is "on the merits." The privity analysis is the same for collateral estoppel (issue preclusion) as it is for res judicata (claim preclusion). The concept of preclusion based on a Rule 23.1 dismissal started with a 2006 decision in the Southern District of New York, Henik v. LaBranche. All of the later decisions, including LeBoyer, cite or can be traced through intermediate citations to Henik. There, the Court held that a Rule 23.1 dismissal was preclusive under the doctrines of both collateral estoppel and res judicata.

Now, pause and think about what that means. The dismissal was on the merits. The corporation is in privity, allegedly, with the stockholder whose claims were dismissed on the merits. Res judicata applies. The implication is fairly simple: Preclusion operates against the corporation as well. I'll say that again. If I'm wrong about privity, then under the Henik-LeBoyer preclusion analysis, if the corporation wants to assert claims against any of the individual defendants, those individual defendants can invoke and be protected by the preclusion doctrine. Far from preserving the corporation's opportunity to assert its claims, preclusion destroys it.

This can be a real issue. I recently had a derivative action in which a fast-filer here in Delaware sued on behalf of Berkshire Hathaway to assert derivatively the corporation's claims for insider trading against David Sokol. The insider trading allegations clearly survived a Rule 12(b)(6) motion, but the fast-filing plaintiff had no non-conclusory basis to assert that the board was disabled under Rule 23.1. Berkshire argued that it was still considering what to do about Sokol and might

well sue. I dismissed under Rule 23.1, but I did so without prejudice precisely to avoid any possible argument by Sokol that Henik and other preclusion precedents that have relied on res judicata would allegedly block the corporation's suit.

This is a serious legal problem, because I only see two parts to the collateral estoppel analysis that turn on Delaware law: Privity and adequacy of representation. Both of those are internal affairs issues in this context, where you're talking about a stockholder plaintiff and a Delaware corporation. Once you get beyond those elements, everything else is necessarily the law of the originating forum. At that point, it becomes impossible for a second court to distinguish between an initial complaint filed without Section 220, a later complaint filed with Section 220, or most problematically, a suit by the corporation itself. The law of the originating forum determines those issues. That problem is what makes impossible the approach that Vice Chancellor Lamb tried to suggest in West Coast, and which Vice Chancellor Parsons tried to apply in Career Education, in which the first dismissal is not preclusive against a later complaint

that added a lot of additional facts. The scope of preclusion is controlled by the first court's judgment, and as the cases cited in footnotes three through six show, other jurisdictions do not follow these fine distinctions about whether you have added more facts. They rather look at whether the same issue was litigated, and they define "issue" broadly. It's only if you address the two Delaware law issues in the analysis; namely, the privity issue and the adequacy of representation issue, that there is an ability for the Delaware corporation to retain control of its own cause of action.

This is a major policy issue raised by the federal approach. This is also a point, I'm afraid, that the plaintiffs in this action still aren't getting. In your opposition, you try to say that I said the same thing as Career Education, and you embrace the idea of factual distinctions between the complaints. That doesn't work under LeBoyer because of the way LeBoyer defines "same issue." At most, it would only work if you had an originating jurisdiction that defines the litigated issue based on the facts alleged in the first complaint rather than the legal issue.

Now, this adds even more irony to the defendant claiming that they preserved the board of director's ability to determine whether the corporation should assert its claims. What their preclusion analysis does is take that decision out of the hands of the directors and put it under the control of the non-corporate law of the jurisdiction in which the first stockholder happens to file suit. Under their approach, it is thus the fast-filing stockholder who determines, simply by picking a jurisdiction, whether the corporation gets to preserve its claims or whether they're barred by preclusion doctrine and res judicata. That result is contrary to Delaware law, which says that the board controls the derivative action until a Rule 23.1 motion has been denied.

The Rule 23.1 decision therefore meets the first two Rule 42(b) criteria by determining a substantial issue and deciding a legal right. The decision also meets the requirements of Rule 41(b)(ii) because decisions of the trial court conflict. As I explained in the opinion, Career Education followed Henik and other federal courts on this issue. The Career Education decision did not address the choice

of law issue raised by the privity analysis. The Career Education decision did not, therefore, apply Delaware law to the privity issue. The Career Education court, therefore, did not address the controlling Delaware Supreme Court cases that hold squarely that until a Rule 23.1 motion is denied, a stockholder is only asserting an individual claim to have the corporation sue and does not yet have the right to sue in the name of the corporation.

Now, I have explained why and what are good reasons to certify, or what I believe are good reasons to certify, and why I think this is an important issue that the Delaware Supreme Court should take a look at it. They don't have to. I'm not telling them to do it. All I'm saying is this is a big one, and I think they ought to think about it.

Next let's talk about what are some not good reasons. The first is the assertion that a federal court ruling on Delaware law should be regarded as a "trial court" ruling for purposes of conflict. As support for this proposition, the application notes that a federal district court can certify a question of law to our Supreme Court. That's a very different issue than viewing the federal

district courts as co-equals with Delaware courts for purposes of conflicts over Delaware law.

As members of this court have often said, and I have often said, Delaware judges get good at corporation law because we see a lot of it. It's not because we're smarter. It's not because we're wiser. It's not because we're better looking. Whenever you do something a lot, you develop a competitive advantage. Federal courts don't see anything close to the number of Delaware corporate law issues this court sees.

As I already noted, the Rule 23.1 preclusion concept trend started with Henik in 2006. That, frankly, was the surprise. You can sense the surprise in Vice Chancellor Lamb's opinion in West Coast. I was in practice at the time. I remember it coming out of the blue. I would be surprised if any Delaware lawyer, in light of Grimes, Rule 15(aaa) and Delaware case law, thought that a Rule 23.1 dismissal would be preclusive against a different stockholder plaintiff. Against the same stockholder plaintiff on a redo, absolutely. It's the same party. But not against a different one.

Candidly, I think Henik is a good

example of the problems that arise for rational development of the law when specialized plaintiffs firms are forced to brief nuanced corporate issues. In Delaware, you have some corporate specialists on the plaintiffs side. The Prickett Jones lawyers are very good at statutory issues. So is Ms. Tikellis. I'm very glad that she's now going to take an active role in the case. Mr. Monhait have has served for years on the Corporate Laws Council. Outside of Delaware, I can't think of a specialized plaintiffs firm with a technical Delaware law person. It doesn't mean they don't do a lot of Delaware work, but it means what they focus on are the bad-facts cases as opposed to nuances of the statute or the case law. Plus, their business model doesn't lead to detailed and thorough legal research. It's a hit-and-hope model. Detailed and thorough research takes time and money, which is not something worth investing when you're in a volume business. Yet arrayed against the specialized plaintiffs' firms are top defense firms who are paid by corporate D&O policies to make every argument possible on behalf of their clients. And the defense firms often hire Delaware firms on a consulting basis.

The matchup in Henik illustrates this imbalance. For the plaintiffs, you had Faruqi & Faruqi, a firm that has an established track record as a frequent filer and fast settler. According to a Bloomberg article that appeared on February 16, 2012, the Faruqi firm had a lead or co-lead role in 10 of the 57 class action merger suits that went forward in Delaware in 2010 or 2011. Not one of Faruqi's cases generated a return for its clients. Among firms settling five or more cases, only the Faruqi firm got zero in every case. On the other side of the "v" in Henik, for the defendants, you had Weil Gotshal and a team led by Irwin Warren, a highly experienced litigator, and Steve Radin, the author of a multi-volume treatise called "The Business Judgment Rule." I'd call that a mismatch.

Let's put another fact on the table as well. Defense counsel don't have an obligation to make sure the law works in the long run, or makes sense, or is balanced and efficient. As was argued strenuously to me during the Nighthawk proceeding, defense lawyers are ethically obligated to do whatever they can to get their clients out of the immediate case. As the defendants have shown in this case, you

can plausibly argue, consistent with Rule 11, that the Supreme Court decisions from Delaware that specifically address when a stockholder plaintiff has authority to sue are not rendered in the collateral estoppel context. You, therefore, can conclude that those would not need to be brought to a Court's attention on a collateral estoppel issue.

It is not at all surprising to me that the excellent defense attorneys in Henik argued preclusion as strongly as possible. Nor is it at all surprising to me that the Delaware Supreme Court decisions made no appearance in the opinion.

Once Henik went in the direction of preclusiveness, it's hardly surprising that other courts followed and produced what I called, and the defendants like to quote me on this, "a growing body of precedent." As Chancellor Strine has frequently observed, one of the adjectives most commonly ascribed to the federal court system by the federal courts themselves is "overburdened." Henik offers an easy way of getting rid of whole swathes of cases. Later cases just followed Henik. When you read them in a series, as I have, and as I commend everyone to do, you can tell that the later decisions are largely

parroting Henik. I, therefore, don't believe that much weight, if any at all, should be given to the non-Delaware cases that address the collateral estoppel issue. Nor do I believe that the existence of those decisions supports certification.

A second reason that I reject as a basis for certification is the defendants' contention that the opinion has "stirred significant controversy." As evidence of the existence of "significant controversy," they cite three internet postings; two by the media and one by a practitioner. Rules 41 and 42 don't mention controversy as a factor, and with good reason. In the current media and practitioner environment in which every decision and transcript from the Delaware courts is scrutinized and commented on, it's very easy to find commentary that might be described as "stirring controversy" for purposes of an appeal. This is a good example of how controversy can be misleading, because two of the articles that the defendants cite, frankly, miss the boat on the decision.

The first misleading piece is an article by David Marcus cited on page three of the application. It has the unfortunate title "Laster

Issues Cross-Country Bench Slap." Mr. Marcus erroneously suggests that I treated the California ruling "almost contemptuously." I have known Mr. Marcus for years. He covers the Delaware courts closely. He has a law degree from a very prestigious institution. Indeed, some might say that he attended the ideal combination of law and undergraduate institutions. He's an excellent reporter. He usually does a very good job at getting to the substance of a ruling. But here, the article opted for controversy and a sensationalistic headline.

It baffles me how Mr. Marcus could have read my opinion as attempting to be anything but respectful to Judge Carter. Throughout the course of the case, Judge Carter and I have tried not to interfere with each other's jurisdiction and to be respectful of each other. There are lengthy exchanges in earlier transcript rulings expressing these sentiments. My decision continued that practice. I noted my respectful disagreement with the California Federal Court, but I did not attack the Court or its decision, nor demean it.

Mr. Marcus highlights a passage in which I stated that "for reasons that are not clear to

me, briefing on the motions to dismiss moved forward more quickly in California than in Delaware." For some reason he views that as criticism of Judge Carter. Not at all. It was a factual statement. I did not know why the California case went faster, giving rise to an unnecessary collateral estoppel issue. Usually this Court moves faster than the federal courts, which have much larger and more varied dockets than we do. To the extent anyone should have felt there was an implied question in this comment, it was the Delaware lawyers, and particularly the plaintiffs, for not moving the case here. Or perhaps the defendants, because we all know that one of the tactics defendants like to use -- I'm not saying it's illegitimate; it's just a tactic defendants like to use -- is to give procedural and scheduling advantages to the plaintiffs whom they view as weaker, and correspondingly slow down the plaintiffs they view as stronger. In this situation, the Delaware plaintiffs were the ones who were actually working the case, pursuing 220, and putting in the real effort. So it wouldn't have been surprising for the defendants to have tried to move slower in Delaware and faster in California. I don't know if that happened, but if

there was any type of pregnant question, it was directed to counsel. The comment by no means was directed at Judge Carter.

It's also disappointing that Mr. Marcus views this as a decision about where derivative litigation should be filed. This wasn't a "where" decision. It was a "how" decision. Yes, the Chancellor and other members of the Court, including I, have spoken a lot about the comparative advantage that Delaware courts gain because we do a lot of Delaware work. Mr. Marcus has written a lot about those issues. But this case isn't part of that discussion.

I would never suggest, and I don't think any member of this Court would suggest, that other courts cannot deal quite competently with Delaware law. Of course they can. They especially can in non-expedited cases where you don't have time pressure limiting the amount of research and thinking you can do. Mr. Marcus quotes Professor Kahan in his article saying that "Had the situation been the reverse -- Delaware judges rejecting a suit and the California judges saying we are not bound by the dismissal -- I am not sure whether Laster would have

been happy." If the fast-filer was in Delaware and the diligent filer in California, the fast-filer should be dismissed for inadequate representation and the California case should go forward. Period. Stop. This isn't a "where" decision. It's a "how" decision.

Diligent plaintiffs should get to litigate. Where they litigate is a different question. If corporations want to solve the "where" problem, they can adopt forum-specific charter provisions. If they want to pick California, they can pick California. If they want to pick Delaware, they can pick Delaware.

The second misleading piece was written by Keith Paul Bishop and is also cited on page three of the application. Mr. Bishop appears to be the author of a treatise on Nevada corporation law, a writer on California corporation and securities law issues, and he appears generally skeptical, from what I've been able to find, of Delaware's leadership position in the corporate area. He makes four points in his post. Each of the four might sound good if you said it fast and your audience didn't know a lot about corporate law. But each has a rather obvious and critical flaw.

First, Mr. Bishop notes that my decision disagrees with recent federal precedent on the question of privity. He doesn't mention that the whole point of my lengthy privity analysis was to explain that Henik, again the real first-mover and surprise decision in this area, missed a rather fundamental point of Delaware corporate law about when a stockholder has a right to sue in the name of the corporation. The privity point is not something where I made new law. There are multiple Delaware Supreme Court decisions directly on point that address the internal allocation of authority over a derivative action before a Rule 23.1 determination.

The Delaware Supreme Court is the only court in the land constitutionally empowered to determine the parameters of Delaware law. The relationship between a stockholder and the corporation is governed by Delaware law. The federal cases missed the Delaware Supreme Court precedent. It might help to generate "controversy" to suggest that my decision went against the list of federal cases, but what I really did was follow controlling Delaware Supreme Court precedent.

Mr. Bishop's second complaint is that

my opinion "presumes to tell a California federal court how it should rule." He cites my observation that "if the collateral estoppel issue were properly presented to the California Federal Court, that court should decline to follow LeBoyer and hold instead that collateral estoppel does not bar a later derivative action by a different stockholder." The defendants have embraced this idea in their application.

This is an odd comment on two levels. At the litigation level, it misses the quite basic point that the purpose of a collateral estoppel analysis is to predict how the issuing court would treat its own judgment. The second court is supposed to "presume," to use Mr. Bishop's word, to say what the first court would do. But this isn't presuming. It's doing what collateral estoppel requires.

What Mr. Bishop really seems bothered about is the linguistic use of the word "should." This is even more odd, because he seems to be a transactional lawyer who, one would think, has rendered legal opinions. Opiners have three choices when rendering an opinion: Would, could, and should. To say when a court "would" do is to make an absolute statement and invite opinion liability. There's

always some minimal possibility that a court could come out differently. To say what a court "could" do doesn't offer much of an opinion. Again, there's usually some argument in favor of positions to support "could."

This leaves "should." That word does not carry any maternally moralistic overtones. It predicts, as it does when used in a legal opinion, what the writer believes is the most likely outcome under the circumstances. Saying "the Eagles should win" does not carry any of the moralistic connotations of "you really should apologize." So it is with "if the collateral estoppel issue were properly presented to the California Federal Court, that court should decline to follow LeBoyer." That is what I predict is most likely under the circumstances if the controlling Delaware Supreme Court precedents on privity were presented to the California Federal Court. That is precisely what I'm supposed to do -- predict -- when applying collateral estoppel.

Third, Mr. Bishop criticizes me for holding that "collateral estoppel is governed by the internal affairs doctrine." This is rather obviously wrong. I didn't hold that collateral estoppel is

governed by the internal affairs doctrine. I looked to California law for the elements of collateral estoppel. One of those elements is privity. Privity refers to the parameters of the relationship between the parties to the judgment and the party against whom the judgment is attempted at being applied. To analyze privity, you therefore have to analyze the law that governs the relationship between those parties.

This is, or should be, a basic point. For example, assume that a New York court appoints a guardian for the property of a disabled person. The guardian brings an action in California that results in a judgment. Relying on collateral estoppel, the defendants seek to use the judgment in a different action involving the person, not the property, of the disabled person. Where would the California court look to determine whether the guardian had authority such that collateral estoppel would apply? The California court would look to the order appointing the guardian and what it said about the scope of the guardian's authority. That issue would be governed by the law of the jurisdiction creating the relationship -- New York -- not the law of the court issuing the judgment.

Take another example. Assume that a real estate agent signed a listing agreement for the client that was expressly governed by New York law. The plaintiff obtains a California judgment against the real estate agent. The plaintiff seeks to use the judgment offensively, relying on collateral estoppel, in an action against the real estate agent's client. Where would a court look to determine if the real estate agent had actual authority sufficient to bind the client? The court, in the first instance, would look to the listing agreement, which would be governed by New York law. Perhaps there would be other issues, like apparent authority, that would be governed by the law of other jurisdictions. But the Court enforcing the original judgment would have to consider the law governing the relationship of the parties to analyze the issue of privity.

One could easily think of other examples. Consider a receiver appointed under New York law for a New York corporation. The receiver sues in California. What law determines the scope of the receiver's authority for purposes of privity? It should be New York. Or consider various family relationships, such as common law spouses or adult

adoptions. What law would determine whether those individuals were in privity? The law creating and governing the underlying relationship.

Here, the issue of privity is governed by Delaware law. Importantly, I am not the only one who says this. In In re Sonus Networks, the leading federal case on collateral estoppel and the only federal court of appeals decision, the United States Court of Appeals for the First Circuit holds that privity is governed by the internal affairs doctrine. That's Sonus Networks 499 F.3d at 64.

Mr. Bishop points out that collateral estoppel is not a corporate law doctrine. Obviously. No one, including me, claims that it is. One element of collateral estoppel is privity. Privity requires that you look at the relationship between the party to the first judgment and the party to the second judgment. The First Circuit held in Sonus Networks, and I held for the reasons stated in my opinion, that the relationship between a stockholder and the corporation is governed by the internal affairs doctrine, such that for purposes of privity, a court considering a derivative action involving a Delaware corporation must look to Delaware law. I didn't say

the internal affairs doctrine applies to collateral estoppel.

Finally, Mr. Bishop objects that I ruled on adequacy of representation in a case in another jurisdiction. This is another issue that the defendants embrace. According to Mr. Bishop, this is a problem because it requires the second court "to judge the work of the plaintiffs in a case that is not before it."

Again, this is not something I came up with. This is an inherent part of preclusion analysis. All of the cases cited in my opinion, and the Restatement of Judgments, recognize that adequacy of representation is always a requirement. Adequacy of representation always will be judged by the second court in a collateral estoppel context. That's how it works. The second court determines whether collateral estoppel applies. The second court necessarily is judging adequacy of representation in a case that wasn't before it. That's what collateral estoppel does. It's an analysis in which the second court looks at the first court's judgment. To cite a California example, you can go to the Ninth Circuit case of Epstein v. MCA, although that decision was

withdrawn on other grounds. That is 126 F. 3d 1235 out of the Ninth Circuit. For other California cases judging adequacy of representation in an earlier action as part of a collateral estoppel analysis, you can look at Harriss v. Pan American World Airlines, Frazier v. City of Richmond and cases cited therein. There's also a number of unreported California decisions that are identified on Westlaw as "non-citable," so I won't mention them by name.

Now, I spent a lot of time going through the Marcus and Bishop articles for two reasons. First, the defendants rely on them. They put them in their papers as suggesting that this decision created controversy. Well, unfortunately, Mr. Marcus made an uncharacteristic mistake or uncharacteristic misjudgment. He's certainly entitled to his own opinion about what happened, but I think wrongly so in this case. Mr. Bishop went zero for four. To the extent that the defendants have relied on and somewhat parroted Mr. Bishop's arguments, it's even more important for me to have addressed them. Regardless, I don't think controversy is an issue that warrants certification because, as I said, the controversy in this case is not well founded.

So, for those reasons, I am going to certify the appeal.

Now, I turn to the stay pending appeal. Under Supreme Court Rule 32(a), "A stay pending appeal may be granted or denied in the discretion of the trial court." In deciding whether or not to grant a stay pending appeal, the Court of Chancery applies the Kirpat factors, so named after Kirpat v. Delaware Alcoholic Beverage Control Commission, 741 A.2d 356 (Del. 1998). The four factors are:

First, a preliminary assessment of the likelihood of success on the merits of the appeal;

Second, whether the petitioner will suffer irreparable injury if the stay is not granted;

Third, whether any other interested party will suffer irreparable injury if a stay a granted, and,

Fourth, whether the public interests will be harmed if a stay is granted.

No one factor is dispositive. They must be balanced with "all of the equities involved in the case together." That's Kirpat 741 A.2d at 358.

I'll start with the preliminary

assessment of the merits of the appeal. My decision rested on two separate and independent grounds. The Delaware Supreme Court could affirm on either and not reach the other. I will discuss each.

First, privity. Because I believe the privity analysis is governed by controlling Delaware Supreme Court precedent, I do not believe that the defendants have a meaningful chance of appeal on this issue. For the defendants to prevail, the Delaware Supreme Court would have to overrule many long-standing precedents on two core issues: First, the point at which a stockholder has authority to assert a corporate claim, and second, the two-phase nature of the derivative action, in which before a Rule 23.1 motion is denied, the stockholder is only asserting an individual claim. I regard the long list of Delaware Supreme Court cases on which I relied as established and dispositive.

For their main grounds for appeal, the defendants again follow Mr. Bishop and try to claim that I didn't follow California law on collateral estoppel. Again, that's a mischaracterization of the opinion. I followed the elements of LeBoyer precisely. One of the elements under LeBoyer is

privity. To analyze privity, you have to analyze the law that governs the relationship between the parties. As the First Circuit recognized in Sonus Networks, privity is governed by the internal affairs doctrine and Delaware law.

Once we get to Delaware law, the defendants' only response to the numerous Delaware Supreme Court cases on which I relied, including Rales and Peat Marwick, is to say that I took them out of context and that those decisions didn't address collateral estoppel. That concept appears on page five, where the defendants say my analysis "dramatically extends the Delaware Supreme Court's observations on the nature of derivative litigation to an issue that has not previously been considered by the Delaware Supreme Court." The same idea appears on page 18.

To the contrary, the question raised by the privity analysis is precisely the same question raised by the Delaware Supreme Court's Rule 23.1 jurisprudence. The question is this: Does the stockholder have authority to bring the claim prior to the denial of a Rule 23.1 motion? Rales and Peat Marwick say no. That's precisely the issue raised by

the privity analysis. The authority to sue is authority to sue. Whether it's raised and addressed directly in a Rule 23.1 decision or indirectly via privity as part of collateral estoppel, it's the same authority question.

Indeed, it's because the authority question is the same that I find it "inequitable" for defendants to argue that a stockholder plaintiff lacks authority to sue for purposes of Rule 23.1, then turn around and say the exact opposite for purposes of collateral estoppel. On page seven of their application, the defendants go to great lengths to describe the procedural history of the litigation in an effort to show that they did not act "inequitably." The "inequity" point turns solely on the reversal of position and the judicial estoppel implications. It has nothing to do with procedural history of the case.

The defendants also say that I misapplied Kohls. In footnote five, they argue that Kohls v. Kennetech involved individual claims, but this case involves derivative claims. In the opinion, you will see citations to five Delaware Supreme Court cases and three Court of Chancery cases saying that until the denial of a Rule 23.1 motion, a stockholder

asserts an individual claim against the corporation for permission to sue. That's an individual claim, just like Kohls.

Because there is clear Delaware Supreme Court case law on these points, I do not agree that I "declined to give an order of the federal court the same preclusive effect that the order would receive in that same court." That's on page four of the stay motion and paragraph seven of the application for certification. Again, I believe that if the California Federal Court were presented with the privity analysis as I explained it, the Court would agree with Sonus Networks, the only Court of Appeals decision to address this, and treat privity as an issue governed by the internal affairs doctrine. The California Federal Court then would follow Rales and Peat Marwick and hold that preclusion does not apply.

I disagree fundamentally with the defendants' contention that absent preclusion, corporations will be forced to relitigate demand futility ad infinitum. That comment appeared out of the blue in Henik. It simply gets repeated by other courts. There are multiple reasons why this won't happen.

First, in most cases, the initial Rule 23.1 decision will be persuasive. If only I could have followed Judge Carter's opinion. I would have corrected the preclusion mistake, then found his analysis persuasive. That would have ended the case and shown everyone that following the correct principles of Delaware law laid down by the Supreme Court doesn't open a can of worms. Unfortunately, after going through the documents the plaintiffs supplied, I concluded that the California Judgment treated this case as if the complaint had only made bare allegations unsupported by internal documents. That's not surprising, because the vast majority of Rule 23.1 decisions have addressed precisely that type of complaint. As my decision explains, when all the plaintiff advances is unsupported allegations, the business judgment rule presumption means you don't credit them. But when a plaintiff cites internal documents from which different interpretations can be drawn, the Supreme Court decisions on the Rule 23.1 pleading standard say that the plaintiff gets the reasonable inference. So although I had to differ with the California court in this case, that outcome will not be common.

What my decision should mean at most is that defendants might have to litigate the Rule 23.1 issue twice: Once against the fast-filer who sued without books and records, and once against the stockholder who got them. You know what? That's exactly what defendants already are doing. In fact, it's currently worse. Because many cases are fast-filed in parallel, defendants currently brief multiple Rule 23.1 motions simultaneously. Because federal courts routinely dismiss without prejudice, plaintiffs are currently able to replead and relitigate demand futility seriatim. Moreover, under King II, plaintiffs can take a free shot, then use Section 220 and litigate demand futility at least twice.

Rather than creating a worse system, Allergan helps correct this. Going forward, defendants can move to dismiss or stay complaints filed by fast filers on the grounds that the plaintiff is an inadequate representative. The plaintiff, because this is a rebuttable presumption as I will get to, the plaintiff will have to come forward with a reason why they should be allowed to go forward. But because it's a presumption, this means defendants won't have to litigate multiple rounds of Rule 23.1

motions. They should win most of the stay or dismissal motions on inadequacy. In fact, they shouldn't have to litigate Rule 23.1 motions on bare bones fast-filed complaints at all. Defendants should be able to avoid reaching the Rule 23.1 issue entirely by moving to stay. The defendants also, of course, retain the ultimate fallback. Defendants never lose control of a derivative action. Boards always retain the ability to take control of the derivative suit via special litigation committee. They can always put a stop to whatever circus they're confronted with.

So, because my privity analysis rests on established Delaware Supreme Court precedent, I believe that the defendants do not have a meaningful likelihood of success on appeal. I have tried to follow binding Supreme Court precedents faithfully. The Supreme Court can change the law. That's their prerogative.

Now the fast-filer presumption. It's, frankly, difficult to predict how the Supreme Court will regard the presumption. As I hope I explained sufficiently in the opinion, the problem of multi-jurisdictional litigation involving fast-filing plaintiffs is a real one, and the Court of Chancery

has tried to address it repeatedly. I trust that the Delaware Supreme Court understands that we keep trying because it's a real and very serious problem. There are only two sovereigns with the ability to bring rationality to this situation. One is the state of incorporation. The other is the federal government. Because corporate law has long been the domain of the states, the states of incorporation have the first crack. But if the states of incorporation don't take steps to craft a rational system, the federal government eventually does step in. PSLRA, SLUSA and CAFA all show that the federal government is more than capable of intervening massively with an effort to solve multi-jurisdictional issues through sweeping measures.

There is also a major policy issue lurking here involving institutional credibility. Ever since Rales, the Delaware courts have been telling stockholders to use Section 220 to craft meaningful complaints. Not surprisingly, we have been dismissing complaints where stockholders couldn't plead with particularity because they didn't use Section 220. But under the current system, a stockholder effectively can't use Section 220 because

the current legal regime favors fast-filers and penalizes stockholders who try to follow the rules. As I discussed at length in my opinion, Chancery decisions have tried to craft a more rational system. In my view, if we mean what we say about Section 220, then we need to have a legal system that not just tells stockholders to use Section 220, but also protects stockholders who do it right. If our law does not address derivative actions in a way that makes using Section 220 and crafting meaningful complaints viable, then we justifiably can be accused of hypocrisy.

Hypocrisy isn't a nice word. I don't think the Delaware courts are hypocrites. Look at how we've approached rights plans. In Moran, our Supreme Court upheld the pill in part because of the ability of stockholders to replace the board. As a corollary, Delaware courts have been assiduous in protecting the stockholder franchise. It would have been manifestly unfair -- indeed arguably hypocritical -- if we had validated the pill because of the ability of stockholders to replace the board, but then allowed incumbent management to shut down the ability of stockholders to wage a proxy contest. The same is

true with derivative actions and Section 220.

The defendants say a lot of things about the fast-filer presumption that are simply wrong. First they say on page 12 that I adopt a per se rule that someone who doesn't use Section 220 is always an inadequate plaintiff. That's incorrect. I adopted what Chancellor Strine suggested in King I, which is a rebuttable presumption that a fast-filing plaintiff with a minimal stake who files hastily is not an adequate plaintiff. It's not a per se rule.

Next, the defendants are wrong to say on page 13 of their application that I based the presumption on two Chancery decisions, citing King I and White v. Panic. I drew the presumption from King I, but the primary authority for it comes from two Delaware Supreme Court decisions. The first is Rales, where the Delaware Supreme Court made clear that "nothing requires the Court of Chancery, or any other court having appropriate jurisdiction, to countenance [fast-filing] by penalizing diligent counsel who has employed investigative methods, including Section 220, in a deliberate and thorough manner in preparing a complaint that meets the demand excused test of Aronson." That's 634 A 2d. at 934, note 10.

The second authority is King II, not King I. In King II, the Delaware Supreme Court suggests the denial of lead plaintiff status as remedy for fast-filed derivative actions. That's page 1151 of that decision. Additional authority for the presumption came from the decisions I cited in Part II.A.3 of my opinion, including King I and White v. Panic. But to say I relied only on King I and White v. Panic is not correct.

Particularly glaringly, along similar lines, the defendants said on page 17 that I based my conclusions "on academic and economic theory rather than precedents or law." I would encourage the defendants to count up the number of decisions I have cited in the fast-filer section of the opinion.

It's also not the case, as the defendants assert on page 13, that under the fast-filer presumption "the corporate defendant is prevented from relying on the preclusive effect of a Rule 23.1 dismissal in another forum in order to penalize the presumptively inadequate plaintiff." As I have already discussed, it is the existing preclusion approach that penalizes the corporation by operating equally on the entity as a party in privity

with the original stockholder. Moreover, it is the existing preclusion system that penalizes the corporation, and indirectly all of its stockholders, by foreclosing potential recovery from individual defendants by giving preclusive effect to an inadequate pleading. The principal beneficiaries of the current system are those rare corporate defendants against whom a meritorious Rule 23.1 claim could be pled using Section 220. The other beneficiaries of the current system are, frankly, defense lawyers, who get to litigate easy Rule 23.1 motions over and over again. I say easy because when a complaint is filed basically without using Section 220, the Rule 23.1 motion will almost inevitably be granted.

It's also not the case that a fast-filer can be rehabilitated by reaching agreement with an adequate plaintiff, as the defendant suggests on page 13. I have never been asked to determine whether LAMPERS is an adequate plaintiff. No one ever made the motion. Given that they were a fast-filer, you can predict how it might come out.

The defendants are also wrong to assert on page 17 that issues like a fast-filer presumption in a derivative action should be "reserved

exclusively for the Delaware General Assembly." In Schoon v. Smith, the Delaware Supreme Court rejected explicitly the argument that derivative actions are exclusively the province for legislation by the General Assembly. As Justice Ridgley explained in Schoon, the derivative action was invented in equity. "Accordingly," the Schoon court held that decisions over the scope of derivative actions are ones that "the judiciary is empowered to make as well." That's page 204 of that decision. Justice Ridgley explained at length that the judiciary has the power "to overturn judicially-created doctrine so long as that doctrine has not been codified in statute" as well as to extend judicially created equitable doctrines so long as the extension is consistent with principles of equity. That's page 205. He also cited the principle that "The law should be an ever developing body of doctrines, precepts, and rules designed to meet the evolving needs of society." It is always possible that the Delaware Supreme Court decides going forward to defer to the General Assembly on corporate derivative actions, but that is not how historically these issues have been addressed.

In saying this, I recognize that the

Delaware Supreme Court has said recently on occasion that corporate issues should be addressed by the General Assembly rather than the courts. The basic principle of having a legislature craft laws forms the democratic foundation of our republic. But it is, frankly, simplistic to think that only the legislature can or should create law, or that the conversation is a one-way street in which the legislature creates law and the court simply applies it. The law-making function is a two-way conversation between the legislature and the court. Although more and more of the law in this country is statutory, thereby approaching the Napoleonic, continental model of an all-encompassing civil code, the bulk of our law, particularly in Delaware, remains true to the Anglo-Saxon tradition of the common law. Across vast areas of the legal landscape, particularly in Delaware, governing law is judge-made common law.

This is particularly true in Delaware, where all our fiduciary duty law is judge-made. Part of what others have call the "genius" of Delaware law has been the tradition of courts of equity addressing fiduciary and corporate law issues on a case-by-case basis. The annual commentaries on amendments to the

Delaware General Corporation Law are full of instances in which the Council and the General Assembly have left an issue for the courts. Given the long tradition of judge-made law in the corporate arena, and given the deference that the Corporate Laws Council and the General Assembly have shown to the courts, it should take more than a perfunctory statement by counsel about something being better left to the General Assembly to explain why the judiciary should not address a properly presented corporate law issue.

At the risk of offending my superiors on the Supreme Court, this is one of the aspects of King II that could readily be debated. On page 1151 of the decision that appears in Volume 12 of Atlantic Third, the King II opinion stated, "If relief under Section 220 is to be restricted in the manner adjudicated by the Court of Chancery, any such restriction should be imposed expressly by the General Assembly, not decreed by judicial common law decision-making."

Frankly, given the history at Section 220, this was an odd statement. Stockholder inspection rights were not originally created by the

General Assembly. The right was recognized by the King's Bench in the form of a writ of mandamus to the corporation. The practice crossed the Atlantic and became part of the law of Delaware. That is why originally the writ of mandamus inspection cases were heard in Superior Court.

The requirement of a proper purpose was part of the common law remedy. The earliest decision I could find referring to the question of a stockholder's purpose is a Delaware Supreme Court decision from 1910, State v. Jessup & Moore Paper Company. The purpose in the case asserted was a familiar one -- valuing shares. The Delaware Supreme Court stated the law as follows: "The principle of law has long been established in this state that a stockholder of a corporation has a right to inspect and make extracts from the books of the corporation at a proper time and for proper purposes." The Delaware Supreme Court held in that case, as a matter of common law, that valuing shares is a proper purpose.

In the century since, what purposes qualify as "proper" versus "improper" has always been determined as a matter of common law by the Delaware courts. It has never been statutory. Even after the

adoption of Section 220, the proper purpose element was left to the development by the judiciary. There is no list of proper purposes in Section 220. There is no list of improper purposes in Section 220. What purposes are or aren't proper has always been determined by the courts based on the facts of the case.

In King I, Chancellor Strine followed the common law tradition and determined under the facts of the case that the stockholder plaintiff had an improper purpose for seeking books and records. No one, including I, could question the authority of the Delaware Supreme Court in disagreeing with Chancellor Strine's conclusion. Nor can anyone question the authority of the Delaware Supreme Court to say that the subject will no longer be within the purview of the common law but rather left to the General Assembly. I do think it's a fair question to ask, however, why a subject that always has been the purview of the common law should now be left to the General Assembly. For those familiar with the history of inspection rights, their common law origins, and the longstanding manner in which proper purpose has been determined, it was an odd move for the Delaware

courts to abandon the field.

I offer these comments respectfully and not in an effort to reargue King II, but rather to illustrate that in the area of corporate law, where courts of equity -- and in that category I include the Delaware Supreme Court -- have long been leaders in the law-making function, deference to the legislature can be a judicially radical, rather than a judicially conservative move. When counsel in the corporate arena says something ought to be left to the legislature, there should be an analysis of the history of the policy and issues involved and an explanation of why that's true. Here, in this instance, given that the Delaware Supreme Court has already held in Schoon v. Smith that derivative actions are an area where courts have authority, I submit that the showing should be all the greater.

I do agree with the defendants that the application of a fast-filer presumption will need to be developed in future cases. Unlike the defendants, I do not view that as a fatal flaw on which to take an appeal, but rather as the heart of the common law method. Traditionally, Delaware has regarded the common law method as a foundation of its

legal system. Judicial decisions flesh out the law on a case-by-case basis. Historically, that has been viewed as a strength of Delaware's jurisprudence and preferrable to legislative enactment because, among other things, it allows tailored decisions and, if necessary, mid-course direction.

Now, as additional grounds for appeal, the defendants mention an assortment of constitutional arguments. They strike me as rather sophomoric, as if someone were attempting to use new words they found in the thesaurus but without really getting the context right. For a decision making short work of similar out-of-context constitutional arguments, you can see Burton v. American Cyanamid 775 F. Supp. 2d 1093 from the Eastern District of Wisconsin.

The first is the pejorative label of "judicial legislation or regulation." The defendants didn't explain in their papers where that came from, and I'm still, frankly, not sure. In some circles, saying a decision is "judicial legislation" waves the same bloody shirt as the cry of "activist judges." I have a hard time discerning what is legislative or regulatory about a presumption. That's a common law technique that courts have always used. There are the

presumptions created by the business judgment rule. There's the res ipsa loquitur presumption of negligence. There is also the problem, unconfronted by the defendants, that there are already default common law legal rules in place. If the fast- filer presumption is akin to "legislation or regulation," creating a constitutional problem, then so too is the first-to-file rule. If one is regulation, then so is the other, which would create a paradox where there could be no rule at all. What the defendants are engaged in is labeling, not argument.

The next is the Commerce Clause theory. I could not find a court that had applied the Commerce Clause to a judicial decision. A series of opinions, of which Burton is one, regard it as unlikely that the Commerce Clause even applies to judicial decisions. According to the defendants, the Commerce Clause issue arises because apparently I have tried to "regulate the economic incentives of out-of-state actors, especially out-of-state attorneys." This is quite good, except as legal analysis.

First, the decision did not regulate out-of-state attorneys. It addressed a stockholder

plaintiff in a Delaware corporation. A Delaware corporation is a creature of Delaware law. The stock is a creation of Delaware law. The stock is sitused in Delaware. Could there really be a constitutional issue with a Delaware court addressing the rights conveyed by a property interest created under Delaware law and governed by Delaware law? The regulation of a stockholder derivative plaintiff is as core a matter of internal affairs as one can have.

Second, if the defendants are correct, Delaware has big problems. Virtually every corporate decision that this Court renders, or which the Delaware Supreme Court renders, affects the economic interests of out-of-state actors.

How about a little decision called Moran? Did the validation of the pill affect the economic incentives of out-of-state actors such that it was a Commerce Clause violation? Or Unocal. Did the intermediate standard of review affect the economic incentives of out-of-state factors like bidders? Or Revlon. That was as clear an economically oriented rule, or at least it was perceived to be at the time, as there could be. Under the defendants' view, apparently each created a

constitutional problem. I'm not sure what the Delaware courts have been doing all these years.

Third, if the defendants are correct, let's stipulate that the DGCL is unconstitutional. Section 327 certainly is. It regulates stockholder plaintiffs who wish to bring derivative actions, just like my decision. So is Section 151, which addresses the rights, powers and privileges of stockholders in a Delaware corporation. Section 211 requires a Delaware corporation have annual stockholder meetings and gives a right of action if a meeting isn't held in 13 months. Sounds to me like all the Delaware lawyers on this call better start brushing up on medical malpractice and slip and fall.

Now let's talk about the Due Process theory. That appears to be non-existent. It's not spelled out at all in the papers. None of the defendants were denied due process. All of the defendants had notice and an opportunity to be heard. This was the peak of Matthews v. Eldrege process rights. Perhaps what the defendants are thinking here is the idea that Allergan has some type of vested right in the existing state of common law. That argument depends in the first instance on the

correctness of the regulatory notion I already discussed. It depends in the second instance on the idea that an entity has a protected interest in decisions that misconstrue controlling Supreme Court precedent.

Most significantly, and this is critical because the defendants often do this, it creates a false unity between Allergan, which may well benefit from the derivative action, and the individual defendants who clearly benefit and only benefit from the preclusion rule. One can't now say whether Allergan would or wouldn't benefit from the derivative action. One can say that the defendants benefit from preclusion.

Lastly, there's a criticism that I erred by going beyond the briefing of the parties at oral argument and by addressing issues that were waived because they were not briefed. These objections appear on page 17 and 26. In my view, a court can treat the issue not briefed as waived, but a court is not required to do so. Some of the United States Supreme Court's landmark cases were decided on grounds that were never raised by the parties, including Erie Railroad v. Tompkins and Mapp v. Ohio.

So were Unocal and Revlon, and more recently, the clarification of ratification doctrine in Gantler.

Judges are assigned the task of settling the meaning of disputed questions of law, not just for the present parties, but for all who must comply with it. Because judges operate within a common law system in which a decision in one case sets a precedent for others, making accurate statements about the law is essential. As the United States Supreme Court observed in Kamen, "when an issue or claim is properly before the court, the Court is not limited to the particular legal theories advanced by the parties, but rather retains the independent power to identify and apply the proper construction of governing law." A similar observation appears in the National Bank case, 508 U.S. 448 (1993). I should say Kamen is the case cited in my decision.

To limit judges solely to the arguments raised by the parties, particularly in representative litigation where the court has an oversight role, would be to hamper and stunt and ultimately skew the development of the law.

I also reject the argument in footnote six that the presumption of good faith created by the

business judgment rule is effectively unrebuttable because a court can never draw an inference of illegality. If that's the case, then the Supreme Court needn't have bothered saying, in Brehm, "Plaintiffs are entitled to all reasonable factual inferences that logically flow from the particularized facts alleged." Nor that a plaintiff need not "plead particularized facts sufficient to sustain a 'judicial finding' either of director interest or lack of director independence," nor that a plaintiff does not have to demonstrate a reasonable probability of success on the claims.

Each of those statements recognizes that there are circumstances when the business judgment rule presumption can be rebutted. It's rare. One such situation is when a plaintiff does plead evidence, such as internal documents, from which competing factual inferences can be drawn.

So as my all-too-lengthy discussion of the defendants' arguments today suggests, we have a situation where the individual defendants have thrown in the kitchen sink. Despite my skepticism about their arguments, I will grant the stay. I do so because of a core principle of Delaware law. That

core principle is that until a Rule 23.1 motion is denied, a plaintiff is not entitled to discovery.

Because of the nature of a derivative action, many issues that initially appear procedural and potentially governed by the law of the adjudicating forum, in fact, implicate the substantive law of the chartering jurisdiction and are governed by the internal affairs doctrine. One of those is pre Rule 23.1 discovery in a derivative action. Whether a putative derivative plaintiff can obtain discovery before a ruling on a Rule 23.1 dismissal seems like a quintessential procedural issue governed by the law of the adjudicating forum, but as a matter of substantive Delaware law, a putative derivative plaintiff is "not entitled to discovery to assist their compliance with Rule 23.1." That's from Rales v. Blasband. In Beam v. Martha Stewart, "Derivative plaintiffs are not entitled to discovery in order to demonstrate demand futility." In Brehm v. Eisner, "Rule 23.1 does not permit a stockholder to cause the corporation to expend money and resources in discovery and trial based solely on conclusions, opinions or speculation." In Kaplan v. Peat Marwick: "When deciding a motion to dismiss for failure to make a demand under Chancery

Rule 23.1, the record before the court must be restricted to the allegations of the complaint."

This substantive rule of law reflects Section 141(a)'s allocation of authority between the board of directors and the stockholders. Until the Rule 23.1 motion has been denied or the corporation otherwise permits the stockholder to go forward, the stockholder lacks substantive authority to conduct the derivative litigation, including deploying litigation mechanisms like discovery on the corporation's behalf.

This is another area where, candidly, the King II decision went in an odd direction. The Supreme Court there intimated that the ability of a plaintiff to obtain discovery before a Rule 23.1 denial was a function of the PSLRA stay and the degree to which the stay spilled over into a derivative action based on securities law violation. In footnote 13 of that decision, it was stated, "Under the current state of the federal case law, the availability of discovery in a derivative federal action appeared unsettled. It is unclear whether the Private Securities Litigation Reform Act, which stays discovery in private class actions arising under federal securities law, also applies to derivative

actions." It then discussed the cases applying the stay and others not applying the stay.

The extent to which the PSLRA stay spills over to related litigation is certainly a live and debatable issue. It has been raised in a series of Section 220 cases. In my view, however, in a derivative action involving a Delaware corporation, it is a second-level issue that need not be reached. That is because, as a substantive matter of Delaware corporate law, under controlling Delaware Supreme Court precedent, a stockholder plaintiff in a Delaware action doesn't have authority to seek discovery pending the denial of a Rule 23.1 motion. That rule applies regardless of the law giving rise to the underlying claim or prompting the derivative suit.

In this case, were I to allow discovery to go forward in a case where I have recommended that the Supreme Court accept an interlocutory appeal, there is a risk that this core principle of Delaware law would be violated. I am far from infallible. I have done my best in Allergan. I really did. But the Supreme Court doesn't have to agree with me. They may disagree with my reasoning. If they do, then it would violate Section 141(a) and

the allocation of authority within a Delaware corporation for the plaintiffs to have pursued discovery on claims they don't have authority to control. For that reason, I am granting the stay. I am not requiring bond or any other security.

I'm sorry for the overly lengthy nature of these comments. It was, in my view, necessitated because of the number of arguments that were raised in the papers, some of which were rather extreme, and the need, therefore, to address them in the context of evaluating the likelihood of success on appeal as well as whether an interlocutory appeal should be certified.

I appreciate your patience with my ruling. I will now get on Lexis Nexis and grant both the order certifying the opinion for interlocutory appeal and also the order granting the stay penning appeal.

Thank you, counsel, for your time.

(The teleconference concluded at 1:50 p.m.)

CERTIFICATE

I, MAUREEN M. McCAFFERY, Official Court Reporter of the Chancery Court, State of Delaware, do hereby certify that the foregoing pages numbered 3 through 84 contain a true and correct transcription of the proceedings as stenographically reported by me at the teleconference in the above cause before the Vice Chancellor of the State of Delaware, on the date therein indicated.

IN WITNESS WHEREOF, I have hereunto set my hand at Dover, this 10th day of July, 2012.

/s/Maureen M. McCaffery

Maureen M. McCaffery
Official Court Reporter
of the Chancery Court
State of Delaware