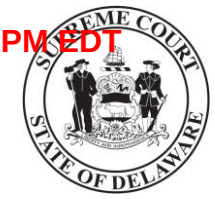

IN THE SUPREME COURT OF THE STATE OF DELAWARE

SOUTHEASTERN PENNSYLVANIA TRANSPORTATION AUTHORITY,	:	
Plaintiff Below, Appellant,	:	No. 239, 2015
v.	:	Court Below: Court of Chancery of the State of Delaware
ABBVIE, INC., a Delaware Corporation,	:	C.A. No. 10374-VCG
Defendant Below, Appellee,	:	

APPELLANT'S OPENING BRIEF

CHIMICLES & TIKELLIS LLP
Pamela S. Tikellis (Del. I.D. #2172)
Robert J. Kriner, Jr. (Del. I.D. #2546)
Scott M. Tucker (Del. I.D. #4925)
Matthew T. Arvizu (Del. I.D. #6010)
222 Delaware Ave., Suite 1100
Wilmington, Delaware 19801
Tel: (302) 656-2500

Attorneys for Southeastern Pennsylvania Transportation Authority

Dated: June 29, 2015

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NATURE AND STAGE OF PROCEEDINGS

Appellant Southeastern Pennsylvania Transportation Authority ("SEPTA" or "Plaintiff") is a stockholder of AbbVie Inc. ("AbbVie" or the "Company"). On November 3, 2014, SEPTA served a demand letter pursuant to 8 *Del. C.* § 220 ("Section 220") on AbbVie (the "Demand") to inspect certain books and records of the Company to determine whether members of AbbVie's board of directors (the "Board") and officers breached their fiduciary duties or engaged in mismanagement in approving and/or terminating the acquisition of Shire Plc ("Shire"), a company incorporated in the Republic of Ireland (the "Transaction").

AbbVie rejected the Demand and, on November 19, 2014, SEPTA initiated this action. After a trial on a stipulated record, the Court of Chancery held that SEPTA lacked a "proper purpose" for inspection because it had not demonstrated a credible basis to show that AbbVie's directors or officers engaged in non-exculpated conduct. *Southeastern Pennsylvania Transportation Authority v. AbbVie Inc*, C.A. No. 10374- VCG, slip opinion at 43 (Del. Ch. April 15, 2015).[1] This new, heightened standard is contrary to this Court's precedent that in order to have a proper purpose a stockholder need only seek to investigate possible wrongdoing or mismanagement. Accordingly, SEPTA appeals the judgment of the Court of Chancery.

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[1] The Memorandum Opinion is attached to this Brief as Exhibit A ("Ex. A at __").

SUMMARY OF ARGUMENT

1. The Court of Chancery erred in holding that a stockholder that pursues a Section 220 demand to investigate potential corporate wrongdoing by fiduciaries of companies with an 8 *Del. C.* § 102(b)(7) ("Section 102(b)(7)") charter provision has a proper purpose only to the extent he seeks to investigate loyalty breaches or illegal conduct. The Court of Chancery's new "proper purpose" articulation is contrary to the precedent of this Court which holds that investigating possible corporate wrongdoing or mismanagement is a "proper purpose." *Seinfeld v. Verizon Communs., Inc.*, 909 A.2d 117, 121 (Del. 2006). The Court of Chancery's ruling requires a stockholder to establish the very facts for which the Section 220 inspection is necessary.

2. The Court of Chancery also erred in applying the newly articulated "proper purpose" to the evidence produced at trial and determining that SEPTA had not established a credible basis to infer possible wrongdoing. Viewed under the correct Delaware law, the record fully supports a finding that SEPTA established a credible basis to infer possible wrongdoing or mismanagement. The Court of Chancery acknowledged a credible basis to infer a significant failure by the Board but arbitrarily characterized the failure as mere negligence, when the failure may have just as conceivably been intentional. The Section 220 inspection is necessary to determine the nature of the failure.

3. Lastly, the Court of Chancery erred in requiring SEPTA to identify specific wrongdoing by specific officers in order to show a credible basis to infer possible wrongdoing by AbbVie's officers whose conduct is not covered by the Section 102(b)(7) charter provision. The Court of Chancery's holding is not supported by Delaware law and is contrary to the repeated admonishments of Delaware Courts that plaintiffs use Section 220 to uncover facts concerning wrongdoing by specific fiduciaries.

STATEMENT OF FACTS

I. Background

AbbVie is a Delaware corporation with a principal place of business in North Chicago, Illinois. A524; Ex. A at 3.

Shire is a publicly-traded "global specialty biopharmaceutical company" registered in the island of Jersey, a Crown Dependency of the United Kingdom with its principal place of business in Dublin, Republic of Ireland. *Id.*

AbbVie's senior management targeted Shire for a possible acquisition in October 2013. A129; Ex. A at 3-4. AbbVie's pursuit of Shire was part of a trend where U.S. companies pursued corporate "inversion" deals to reduce their tax burdens on income. A129-130, 245, 294.[2]

AbbVie's pursuit of an inversion with Shire was in the midst of imminent federal regulation to eliminate the tax benefit of inversions to U.S. corporations. The efforts of regulators included both potential legislative and executive action, including a fiscal year 2015 budget proposal by President Obama, to limit the U.S. companies from engaging in inversion deals.[3] A130, 294-297.

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[2] This is a strategy by which a United States company acquires a foreign subsidiary in a country that has lower tax rates and less stringent corporate governance requirements. A130. The surviving company is then re-domiciled to the foreign country. *Id.*

[3] On April 30, 2014, *Bloomberg* noted that an official with the Treasury Department had stated that "cracking down" on inversion deals was "a priority for the Obama administration" and that the Treasury Department had not "said whether it will curtail the deals with new regulations, which it could advance without Congress". A821.

II. AbbVie Agrees To Acquire Shire

AbbVie's CEO, Richard Gonzalez ("Gonzalez"), began negotiating an acquisition of Shire with Shire's Non-Executive Chairman in May 2014. A564-568; Ex. A. at 6-8. Before starting the negotiations, Gonzalez "came to believe that even without the [tax] benefits of an inversion, acquiring Shire made sense." A790. AbbVie's senior management, including Gonzalez, were involved in the negotiations with Shire and updated the Board regarding the "legal, financial and other considerations" for the Transaction. A564-568. As AbbVie's senior management negotiated the acquisition, the drum-beat of imminent inversion regulation continued.[4] The prospect of regulation was so obvious, deal makers included clauses in merger agreements for many inversions that could allow the buyer to terminate or restructure the transaction if the tax laws were to change. A792, 826.

On July 18, 2014, the Board agreed to acquire Shire pursuant to a Co-

[4] On May 20, 2014, legislation was introduced before both chambers of Congress, which largely mirrored President Obama's budget proposal and was designed to stop corporate inversions ("Inversion Legislation"). A130, 294-304, 546. The Inversion Legislation would treat newly-merged companies as domestic corporations if 50% of the combined company was held by former shareholders of the U.S.-based company or if the executive officers and senior management and 25% of the combined company's employees, sales or assets are located in the United States. *Id.* The Inversion Legislation would be **retroactive**, applying to any inversion completed after May 8, 2014. A130, 296, 299. Treasury Secretary Lew also publicly advocated for immediate retroactive changes to the U.S. tax system to deter inversions. A825-826. Secretary Lew sent a letter to the U.S. Senate advocating immediate, **retroactive** action to curb Inversions and further stated that if he sought a way to use administrative action to address inversion, he would. *Id.*

Operation Agreement (the "Co-Operation Agreement"). A221, 305-306. The Co-Operation Agreement included a $1.635 billion "Break Fee" payable to Shire if the Board changed its recommendation and a meeting of AbbVie's shareholders did not occur within 60 days of the change in recommendation or the AbbVie stockholders did not approve the Transaction; or in certain circumstances where the Transaction did not receive all regulatory approvals. A221, 318-319. The Break Fee amount equated to nearly 40% of AbbVie's net earnings for the year ended December 31, 2013 and approximately 79% of its net earnings for the six month period ended June 30, 2104. A221; 551. The Co-Operation Agreement also included a "Cost Reimbursement Payment" of $500 million that, according to reports, was the sticking point between AbbVie and Shire and was specifically requested by Shire to protect against the AbbVie stockholders voting against the Transaction if the government eliminated the tax benefits.[5] A362, 790.

AbbVie and Shire agreed that two closing conditions relating to regulatory events occurring after December 31, 2013 would not apply to any change of tax laws or regulations that could cause the new company to be treated as a United States corporation for federal tax purposes. A587. Though other companies had protected against the obvious prospect of a change of tax laws or regulations, no

[5] There is no indication in the public filings or public reports that Shire demanded the Break Fee.

fiduciary-out or other protective provision was included in the Transaction.[6] A729, 792, 826.

When asked by investors and analysts in a conference call held on July 18, 2014, Gonzalez downplayed the importance of the tax benefit, stating "[t]ax is clearly a benefit, but it's not the primary rationale for [the Proposed Inversion];" and that the Transaction "has excellent strategic fit and has a compelling financial impact well beyond the tax impact;" and that AbbVie "would not be doing it if it was just the tax impact." A800, 801; Ex. A at 15.

The Shire acquisition was subject to approval by the AbbVie stockholders. A514. Thus, the Board was required to provide its recommendation to the AbbVie stockholders together with all material information relating to the decision whether to vote for the acquisition.

AbbVie filed a preliminary Form S-4 concerning the Shire acquisition on August 21, 2014. A501-572. According to the S-4, the Board identified numerous benefits of the Transaction including,[7] "the potential realization of tax and

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[6] Shortly after AbbVie announced the Transaction, the Treasury reiterated that it was "reviewing a broad range of authorities for possible administrative actions to limit inversions 'as well as approaches that could meaningfully reduce the tax benefits after inversions take place.'" A835. Further, during remarks before the Urban Institute, Secretary Lew stated:

> [t]he Treasury Department is completing an evaluation of what we can do to make these deals less economically appealing, and we plan to make a decision in the very near future.

A838.

[7] In addition to the tax benefits, the Transaction purportedly created numerous "significant strategic and financial benefits" including: the creation of a global market leader with unique characteristics [...] by combining two companies with leadership positions in specialty

operational synergies...as a result of the Combination;" "against a number of uncertainties, risks and potentially negative factors" including "the risk that a change in applicable [tax] laws..., or official interpretations thereof, could cause New AbbVie to be treated as a US domestic corporation for US federal income tax purposes...or otherwise adversely affect New AbbVie or its affiliates." A222, 546, 569, 570. AbbVie acknowledged that not only did the Inversion Legislation pose a risk to the tax benefit, but the U.S. Congress, the Organization for Economic Co-Operation and Development, and other government agencies were focused on "issues relating to 'base erosion and profit shifting,' including situations where payments are made between affiliates from a jurisdiction with high tax rates to a jurisdiction with low tax rates." A546, 785, 786. Nevertheless, the Board gave an unqualified approval and recommendation of the Transaction as "in the best interest of AbbVie stockholders." A568.

The Board "did not attribute any particular weight to any factors considered by it and did not form an opinion as to whether any individual factor (positive or negative), considered in isolation, supported or failed to support its recommendation. Rather, the Board considered the totality of the factors." A569, 570. The S-4 further stated "[i]n view of the wide variety of factors considered by

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pharmaceuticals; the strong complementary fit of Shire's platform with AbbVie's existing specialty focus; and the combined financial strength and R&D experience of New AbbVie. A222, 223, 318,319, 568-570. In addition, a combination with Shire could allow AbbVie to reduce its dependence on Humira, diversify its product line, and add to its revenue due to Shire's projected 2014 revenue of $5.8 billion. A 222, 812-820.

the Board in connection with its evaluation of the Combination, the Board did not consider it practical to, and did not quantify, rank or otherwise assign specific weights to the factors that it considered in reaching its determination and recommendation." A571.

III. Termination of the Transaction Based on Inversion Regulations

On September 22, 2014, the U.S. Treasury enacted regulations which eliminated the tax benefit of the Transaction ("Inversion Regulations"). A107, 246, 247, 292, 293, 464-477. The Inversion Regulations: (i) prevented inverted companies from accessing a foreign subsidiary's earnings while deferring U.S. tax through the use of creative loans; (ii) prevented inverted companies from restructuring a foreign subsidiary in order to access the subsidiary's earnings tax-free; (iii) closed a loophole to prevent inverted companies from transferring cash or property from a controlled foreign corporation to the new parent to completely avoid U.S. tax; and (iv) made it more difficult for U.S. entities to invert by strengthening the requirement that the former owners of the U.S. entity own less than 80 percent of the new combined entity. A247, 292, 293, 464-477. These changes were foreseeable by the Board when it approved the Transaction as several governmental entities were considering similar provisions that would apply retroactively to inversions. A546. In fact, the S-4 acknowledges that the Inversion Legislation was focused on decreasing the percentage former stockholders of the

U.S. entity could own in the new combined company below 80% and that multiple governmental agencies were focused on limiting the ability of inverted companies to move funds between the entities in order to avoid taxes in higher tax jurisdictions. *Id.*

On October, 15, 2014, AbbVie publicly announced that the Board changed its recommendation and urged AbbVie stockholders to reject the Transaction ("Change in Recommendation"). A809. AbbVie's officers and directors decided that the regulations "fundamentally changed the implied value of Shire to AbbVie in a significant manner" and constituted a "deal breaker" warranting a change of the Board's recommendation of the Transaction. *Id.* The Company stated that the determination was made "following a detailed consideration of the impact of the...changes to the tax rules." *Id.*

On October 20, 2014, AbbVie and Shire publicly announced that they had mutually agreed to terminate the Transaction. A495. In the announcement, AbbVie stated that in response to the Inversion Regulations, "the company conducted a thorough review" of the Inversion Regulations and as a result AbbVie's executive management concluded that pursuing the Transaction "was no longer in the best interests of AbbVie and its shareholders." A201, 495. The Board "supported [management's] conclusion" and made the Change in Recommendation and entered into a Termination Agreement, requiring AbbVie to

pay the $1.635 Billion Break Fee. A495.[8]

IV. SEPTA's Section 220 Demand

On November 3, 2014, SEPTA made its Demand on AbbVie, seeking inspection of AbbVie's books and records. A110, 285-291. The stated purposes of the Demand were:

> (1) to investigate possible breaches of fiduciary duties and mismanagement by the Board and officers of AbbVie in connection with approving the Break Fee;
> (2) to investigate possible breaches of fiduciary duties and mismanagement by the Board and officers of AbbVie in connection with the Board's Change in Recommendation announced on October 15, 2014; and
> (3) to investigate possible breaches of fiduciary duties and mismanagement by the Board and officers of AbbVie in connection with AbbVie's entry into the Termination Agreement;
> (4) to investigate possible waste of corporate assets and breaches of fiduciary duties by the Board and officers of AbbVie in connection with AbbVie's payment of the $1.64 billion Break Fee; and
> (5) to investigate the ability of the Board to consider a demand to initiate and maintain litigation related to any breaches of fiduciary duty prior to commencing any derivative litigation.

A110-111, 250-251.

On November 11, 2014, AbbVie asserted multiple objections to the Demand and refused to produce the demanded records. A498-500. AbbVie asserted that the Demand did not state a proper purpose because it ". . . does not provide any

[8] Given the Change in Recommendation, AbbVie did not schedule a stockholder meeting to vote on the Transaction. *Id.*

credible basis for an inference that AbbVie's directors acted in bad faith or breached their duty of loyalty either when they approved the Shire agreement, including the 3% break-up fee, or when they determined to change their recommendation and terminate the transaction." A113-114, 498-500.

V. SEPTA Established A Proper Purpose And Scope At Trial

Plaintiff commenced this action on November 19, 2014. Trial proceeded on a stipulated record on February 11, 2015.

At trial, SEPTA established a credible basis to infer that the AbbVie directors and officers may have failed properly to discharge their fiduciary duties in approving and/or terminating the Transaction. SEPTA established a credible basis to infer that the AbbVie directors and officers may have failed to identify and consider, or disregarded, the "deal breaker" financial impact which would be caused by the loss of the tax benefit due to new tax regulations; or that the AbbVie directors and officers asserted the new tax regulations as a false pretext to terminate the acquisition which had been touted as having numerous benefits other than tax. A221-227, 17-25

SEPTA showed that the prospect of imminent regulations which could eliminate the tax benefit was self-evident at the time the officers recommended and the directors approved the Transaction. A21-26, 130, 221-222, 225, 231-233. SEPTA showed that, according to the S-4, the Board gave no particular weight to

the particular benefits or risks, including the tax benefit and the risks such benefit would be eliminated by government action, and did not form an opinion or identify any specific risk as a deal breaker in isolation. A19, 21, 25, 225. Further, the "Background" discussion in the S-4 indicated that the AbbVie officers and directors discussed the benefits and risks, but included no indication of any discussion of the deal-breaker impact of losing the tax benefit. A19, 21, 25, 589-570. No analysis or estimate of the economic impact of the loss of the tax benefit was included in the S-4. A19, 21, 25, 569-581.

Despite being aware of the methods the government was considering to deter inversions, it apparently was not until after the Inversion Regulations were announced, that AbbVie's management conducted an analysis of the effect a change to the tax laws, or interpretations thereof, would have on the Transaction and determined that such changes substantially changed the value of the Transaction to AbbVie and constituted a "deal breaker." A201, 495. No explanation was provided nor is it apparent why the potential "deal breaker" conclusion could not have been reached prior to approval of the Transaction through the same "detailed consideration." As acknowledged by the S-4, the Board was on notice that the government was looking to take action similar to the Inversion Regulations when it approved the Transaction. A546. This is not a case where an unforeseeable event with an unquantifiable impact occurred after Board

approval. A20.

The facts detailed support more than an inference that AbbVie's directors and officers may have engaged in mismanagement, waste or wrongdoing in approving and/or terminating the Transaction.

SEPTA also established at trial that the nine categories of records it seeks are "necessary and essential" to its purposes. A27-31, 146-153, 239-243. Specifically, SEPTA demonstrated that the records requested were narrowly tailored to investigate the proper purposes of the Demand, focusing on the documents and communications that the directors and officers considered and reviewed in approving and terminating the Transaction and the ability of the Board to consider a demand to institute derivative litigation if necessary. *Id.*

ARGUMENT

I. THE COURT OF CHANCERY ERRED BY HOLDING SEPTA FAILED TO ESTABLISH A PROPER PURPOSE UNDER SECTION 220

A. QUESTION PRESENTED

Is SEPTA's stated purpose for exercising its Section 220 investigation rights -- to investigate possible breaches of fiduciary duty, mismanagement and waste -- proper under Delaware law? A14-17, 137-144, 220-237.

B. SCOPE OF REVIEW

Under Section 220, whether a stockholder has a "proper purpose" is an issue of law and equity which the Court reviews *de novo*. *Security First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 567 (Del. 1997), *citing Thomas & Betts Corp. v. Leviton Manufacturing Co.*, 681 A.2d 1026, 1030 (Del. 1996). The Court reviews *de novo* whether the Court below correctly formulated the applicable legal standard. *Brehm v. Eisner*, 906 A.2d 27, 48 (Del. 2006).

C. MERITS OF THE ARGUMENT

This Court has stated: "[i]t is well established that a stockholder's desire to investigate wrongdoing or mismanagement is a 'proper purpose.'" *Seinfeld,* 909 A.2d at 121; *See also Thomas & Betts Corp. v. Leviton Mfg. Co.*, 685 A.2d 702, 710 (Del. Ch. 1995) ("investigating possible waste and mismanagement is a proper purpose under 8 *Del. C.* §220").

Contrary to this Court's precedent that investigation of wrongdoing or mismanagement is a "proper purpose" under Section 220, the Court of Chancery determined that only a stockholder providing a basis to infer a breach of the duty of loyalty or other non-exculpated wrongdoing may inspect corporate books and records, warping the underlying law and policy for this Court's prior decisions.

Below, the Court concluded that the Court of Chancery "has not squarely addressed the issue of whether, when a stockholder seeks to investigate corporate wrongdoing *solely* for the purpose of evaluating whether to bring a derivative action, the 'proper purpose' requirement under Section 220 is limited to investigating non-exculpated corporate wrongdoing." Ex. A at 31 (emphasis in original). In holding that such a limitation "should exist," the Court reasoned that: a "proper purpose" requires the stockholder to establish a "credible basis" for a "justiciable" claim and where, as here, the corporation has an exculpatory provision under Section 102(b)(7), a stockholder can only state a proper purpose if the stockholder articulates non-exculpated corporate wrongdoing. *Id.* at 32-34.[9]

The new articulation by the Court of Chancery limits a stockholder to investigating potential loyalty breaches or illegal conduct by fiduciaries of companies with a Section 102(b)(7) provision. Under this new ruling, fiduciary conduct that, from the publicly available information, is not obviously a breach of

[9] As discussed in Sections II and III, *infra.*, absent the erroneously narrowed interpretation of the proper purpose requirement, SEPTA indeed established a credible basis to infer possible corporate wrongdoing and mismanagement.

the duty loyalty, cannot be investigated. In effect, a stockholder that has, as the law requires, established a credible basis to infer possible corporate wrongdoing and mismanagement may, nevertheless, be denied its inspection rights. This rigid requirement would apply despite the fact that the inspection may reveal that the corporate wrongdoing arose from a breach of loyalty. *See e.g.*, *Brehm*, 906 A.2d at 67 (Del. 2006) (positing that an example of disloyal, bad faith conduct would be intentional failure "to act in the face of a known duty to act, demonstrating a conscious disregard for his duties.").

This cannot be the result this Court intended when it stated that investigating wrongdoing and mismanagement is a proper purpose. By narrowly interpreting the proper purpose of investigation of wrongdoing or mismanagement, the Court of Chancery expected SEPTA to establish the very facts for which the Section 220 inspection is necessary. Delaware Courts have rejected the notion that stockholders must do so. *See Security First*, 687 A.2d at 568 (footnotes omitted).

In *Marmon v. Arbinet-Thexchange, Inc.*, 2004 Del. Ch. LEXIS 44, *18-19 (Apr. 28, 2004), the company attempted to prove at the Section 220 trial that the conduct the stockholder claimed may constitute mismanagement was in fact lawful and in no sense improper. The Court concluded:

> This gambit, if allowed, would turn on its head both §220 and the case law upholding a books and records inspection for the purpose of investigating mismanagement. In such a case, the issue is whether the evidentiary showing is sufficient to justify a court-ordered books and

> records inspection to uncover evidence (if any exists) of mismanagement. Under Arbinet's view of the law, a demanding shareholder under §220 would first have to prove actual mismanagement in order to become entitled to conduct the predicate books and records inspection that would uncover (if it exists) evidence of such mismanagement. Besides, being circular and conceptually wrong, that litigation approach is inequitable and subversive of §220.

Id. at 18-19. *Accord. La. Mun. Police Emples. Ret. Sys. v. Countrywide Fin. Corp.*, 2007 Del. Ch. LEXIS 138, *43-44 (Del. Ch. Oct. 2, 2007) (litigating the merits of a derivative suit in the context of a Section 220 action would "completely undermine the purpose of Section 220 proceedings."); *Sutherland v. Dardanelle Timber Co.*, 2006 Del. Ch. LEXIS 88 (Del. Ch. May 16, 2006) (the credible basis standard is not equivalent to that of Court of Chancery Rule 12(b)(6)); *Khanna v. Covad Communs. Group*, 2004 Del. Ch. LEXIS 11, *21 (Del. Ch. Jan. 23, 2004) ("A Section 220 action is not the proper forum for litigating a breach of fiduciary duty case.").

Moreover, the new standard, if upheld, will require the stockholder seeking inspection, and the Court, to speculate as to what relief, *i.e.* monetary or equitable, could be available for plenary claims that have not been, nor may never be, asserted. *See Arnold v. Soc'y for Sav. Bancorp., Inc.*, 678 A.2d 533, 535 n.2 (Del. 1996) ("Under 8 *Del. C.* §102(b)(7), directors are not exempt from equitable relief."); *Cal. Pub. Emp. Ret. Sys. v. Coulter*, 2002 Del. Ch. LEXIS 144, *59 (Del. Ch. Dec. 18, 2002) (refusing to dismiss claims based on Section 102(b)(7) where

"the remedy sought is not limited to damages"); *see also Chaffin v. GNI Group, Inc.*, 1999 Del. Ch. LEXIS 182, *21 (Del. Ch. Sept. 3, 1999) (holding the exculpatory clause would not bar the plaintiffs from recovering money damages for the plaintiffs' duty of care claims). Because the Court of Chancery has broad discretion in plenary cases to fashion any remedy which may be appropriate, including injunctive or monetary relief, stockholders and the Court cannot determine what form of relief, if any, would be appropriate without first investigating and concluding that wrongdoing did in fact occur and identifying the nature of the wrong. *Int'l Telecharge Inc. v. Bomorko, Inc.*, 766 A.2d 437, 440 (Del. 2000).

The Court of Chancery further erred in concluding that several "*analogous*" decisions by it "support the conclusion" that the new, narrowed interpretation of the proper purpose of investigating wrongdoing or mismanagement "should exist."[10] Ex. A at 31. The cited cases all differ from this one because, in the cited cases, regardless of what the books and records might yield, the plaintiff could never pursue an action to redress the corporate mismanagement and wrongdoing.

For example, the Court of Chancery cited *Graulich v. Dell, Inc.* 2011 Del. Ch. LEXIS 76 (Del. Ch. May 16, 2011), as support. There, the Court concluded

[10] The Court of Chancery acknowledged existing contrary authority citing *Amalgamated Bank v. UICI*, 2005 Del. Ch. LEXIS 82, *6-7 (Del. Ch. June 2, 2005) (concluding that fact-based affirmative defenses to potential plenary actions were not proper defenses to a Section 220 inspection.).

that the indisputable facts showed: the plaintiff lacked standing to bring derivative claims related to the possible wrongdoing; the claims were time-barred; and the claims were barred by claim preclusion. *Id.* at 21. Thus, the *Dell* plaintiff did not state a proper purpose even though facts uncovered during a books and records inspection might show wrongdoing or mismanagement.

The Court of Chancery also relied on *West Coast Mgmt. & Capital LLC v. Carrier Access Corp.*, 914 A.2d 636 (Del. Ch. Nov. 14, 2006), in crafting its new standard, for the proposition that a Section 220 inspection "must be to some end." Ex. A at 29. The Court in *West Coast*, however, made the "some end" statement in the context of an explanation that the stockholder could not re-litigate derivative claims that had been previously brought by the same stockholder and dismissed by a federal court, regardless of the facts found in the inspection. *Id.* at 646-647. The Court stated that the stockholder's "clear...sole purpose and end [was] to pursue a second derivative suit - an end barred by issue preclusion," and that a mere fishing expedition or inspection for pure curiosity does not constitute a "proper purpose" under Section 220. *Id.*

The Court of Chancery's citation of *La. Mun. Police Emps.' Ret. Sys. v. Lennar Corp.*, 2012 Del. Ch. LEXIS 230 (Del. Ch. Oct. 5, 2012), likewise does not support a new limitation of the proper purpose of investigating corporate mismanagement or wrongdoing. Ex. A at 32 n. 107. In *dicta*, the Court in *Lennar*

stated, without citation, that a stockholder seeking "to investigate wrongdoing for which there is no remedy...has not stated a proper purpose." 2012 Del. Ch. LEXIS 230 at *6. *Lennar* provides no support to require a stockholder to establish, in its demand, a non-exculpated breach of duty in order to have a proper purpose under Section 220.[11]

The Court of Chancery also justifies the new, limiting interpretation of proper purpose based on "the necessity of proper balance of benefits and burdens of proof under section 220." Ex. A at 32. The new interpretation, however, undermines the legal and policy considerations concerning the relative "benefits and burdens" under Section 220. The Court of Chancery's ruling effectively heightens the "credible basis" standard, requiring stockholders to overcome what is akin to rule 12(b)(6) or 23.1 standards in order to obtain books and records. This requires evidence of a breach of duty and evidence that the breach constituted non-exculpated conduct, *i.e.* a breach of loyalty.

This Court and the Court of Chancery have recognized access to corporate records is necessary to determine the contextual facts concerning directors' and officers' action or inaction and whether the action or inaction implicates wrongdoing or mismanagement. *Amalgamated,* 2005 Del. Ch. LEXIS 82, *13-14

[11] The Court in *Lennar* ultimately held that two news articles and old settled lawsuits were inadequate to "constitute 'some evidence' of misconduct sufficient to support a *Section 220* demand." *Id.* at 14. The Court concluded that "Plaintiff...presented only a chain of inferences that never amount to more than speculation." *Id.* at 14.

("[b]ecause director independence is a 'contextual inquiry,' potential shareholder plaintiffs have been admonished to employ the *Section 220* process"), citing *Beam v. Stewart*, 845 A.2d 1040, 1056 (Del. 2004). Delaware Courts have urged the use of stockholder investigation rights to avoid needless plenary litigation. The decades-long catalogue of admonitions concerning stockholders' failure to use Section 220 to investigate potential derivative claims involved cases where the stockholder brought plenary claims alleging misconduct without having first obtained records concerning the contextual facts. *See Beam*, 845 A.2d at 1057 (observing that a Section 220 investigation might have uncovered facts to support the allegations that a majority of directors lacked independence); *Desimone v. Barrows*, 924 A.2d 908, 951 (Del. Ch. 2007) (noting that a Section 220 investigation may have uncovered facts about a board's investigation, process, discussion, conclusions and rationale); *Ash v. McCall*, 2000 Del. Ch. LEXIS 144, *55-56 (Del. Ch. Sept. 15, 2000) (Section 220 investigation may have uncovered facts demonstrating that directors possessed knowledge of potential accounting improprieties and took no action to respond to them, failing to act in good faith).

The Court of Chancery's limitation of the proper purpose requirement eviscerates and undermines the policy of and admonitions by this Court, that stockholders use Section 220 to determine if actionable claims exist. The new onerous requirement will only serve to discourage stockholders from using the

"tools at hand."

In sum, Delaware law provides that a stockholder, with a credible basis to infer possible corporate wrongdoing or mismanagement has a proper purpose to inspect corporate books and records. The Court of Chancery improperly limited that right by holding that the stockholder only has a proper purpose if he can establish – at the Section 220 demand stage – that the corporate wrongdoing or mismanagement was the result of some, non-exculpable conduct.

II. THE COURT OF CHANCERY ERRED BY CONCLUDING SEPTA DID NOT ESTABLISH A CREDIBLE BASIS TO INFER POSSIBLE WRONGDOING BY THE DIRECTORS

A. QUESTION PRESENTED

Did SEPTA establish a credible basis from which to infer possible corporate wrongdoing or mismanagement by the directors under Delaware law? A15-28, 138-144, 220-237.

B. SCOPE OF REVIEW

The question of whether a shareholder has demonstrated a credible basis to infer wrongdoing is a mixed issue of law and fact. *City of Westland Police & Fire Ret. Sys. v. Axcelis Techs., Inc.*, 1 A.3d 281, 287 (Del. 2010), *citing Security First,* 687 A.2d at 565. On a mixed question of law and fact, the trial Court's "factual findings will be reviewed for 'clear error' and its legal determinations...will be reviewed by [the Supreme] Court *de novo.*" *DV Realty Advisors LLC v. Policemen's Annuity and Benefit Fund of Chi., Ill.*,75 A.3d 101, 109 (Del. 2013).

C. MERITS OF THE ARGUMENT

The Court of Chancery erroneously considered the evidence of "credible basis" against an improperly narrow interpretation of SEPTA's proper purpose. Once the legal error discussed in Section I, *supra.*, is corrected, the record establishes that SEPTA has made a sufficient showing.

This Court has repeatedly reaffirmed that "the 'credible basis' standard

...strik[es] the appropriate balance between (on the one hand) affording shareholders access to corporate records that may provide some evidence of possible wrongdoing and (on the other) safeguarding the corporation's right to deny requests for inspection based solely upon suspicion or curiosity." *City of Westland*, 1 A.3d at 287, citing *Seinfeld*, 909 A. 2d 117. The "credible basis" standard is the lowest possible standard. *Id.* The stockholder's burden under this standard does not require the stockholder to prove fiduciary wrongdoing actually occurred. *Seinfeld*, 909 A.2d at 122.

> Stockholders need only show, by a preponderance of the evidence, a credible basis from which the Court...can infer there is possible mismanagement that would warrant further investigation - a showing that 'may ultimately fall well short of demonstrating that anything wrong occurred.' That 'threshold may be satisfied by a credible showing, through documents, logic, testimony or otherwise, that there are legitimate issues of wrongdoing.'

Id. at 122-123 (citations omitted). This Court has stated that the "credible-basis-from-some-evidence" standard is settled law and should be "overruled only 'for urgent reasons and upon clear manifestation of error.'" *Id.* at 123-124.

The Court of Chancery concluded that SEPTA established "at most, that AbbVie's directors were aware of the risk that the government would act to eliminate the tax benefits of inversions; that the directors intentionally took that risk and bet a tremendous amount of the stockholders' money on the chance that the risk would not come to pass; and that the risk ultimately did come to pass,

leading to a spectacular failure of the [Transaction] and a huge loss to the stockholders. These facts fail to show a credible basis that the Company's directors have breached their duty of loyalty, and are not sufficient to sustain a Section 220 inspection under the circumstances." Ex. A at 43.

The Court of Chancery recognized the existence of a reasonable inference that the Board "failed to take into account the effect of...the loss of the tax benefit... on the viability of the deal as a whole" but arbitrarily characterized the failure as negligence.[12] *Id.* at 39 n.122. The Board's failure regarding such an important aspect of the Transaction, however, may just as conceivably constitute a breach of loyalty, depending on the facts concerning where director action and/or inaction falls on the spectrum of mere inattention to intentional bad faith disregard. *See Brehm*, 906 A.2d at 64-67 (nature of fiduciary misconduct and breach on spectrum depends on the facts and state of mind). In fact, the Court of Chancery's arbitrary characterization of the nature of the Board's failure demonstrates the utility and necessity of Section 220 to obtain the contextual facts concerning possible wrongdoing.

As discussed *supra*, the Court of Chancery's conclusion that Plaintiff did not establish a credible basis was based on the newly articulated requirement rather than the correct proper purpose requirement. Had the Court of Chancery viewed

[12] The Court of Chancery recognized at trial that a stockholder does not need to prove a specific breach of duty in order to have a credible basis, when it noted: "the statement 'director wrongdoing' would seem to encompass even exculpated breaches of duty. A59:2-4.

the evidence under the correct requirement, the record fully supports a finding that SEPTA established a credible basis to infer possible wrongdoing or mismanagement.

The "credible basis" standard does not require proof that any breach of duty actually occurred or that the wrongdoing constituted a breach of the duty of loyalty. The "credible basis" standard requires a showing only of "*possible* wrongdoing," or that a breach "may have occurred." *Seinfeld*, 909 A.2d at 118 (emphasis in original).

At trial, SEPTA provided sufficient evidence to support the longstanding "credible basis" standard. When the AbbVie directors and officers approved and recommended the Transaction, they touted numerous strategic and financial benefits that supported the Transaction. Yet, despite the overt efforts to eliminate the tax benefits of inversion deals, the Board made no effort to form an opinion whether the Transaction was still in the best interests of the stockholders if the tax benefits were eliminated. Moreover, in discussing these benefits, AbbVie and Gonzalez downplayed the import of the tax benefits for the Transaction, noting that the Transaction had a strategic and financial impact beyond the tax benefit. Ex. A at 15; A569-570, 790, 800-801. Even though directors and officers in other similar deals were protecting their shareholders from potential changes to the tax laws or interpretations thereof by negotiating fiduciary out provisions in merger

agreements in the event such a change eliminated the advisability of the deals, the AbbVie officers and directors failed to include such a provision in the Co-Operation Agreement.[13]

However, shortly after approving the Transaction and within weeks of the announcement of the Inversion Regulations, AbbVie management concluded and the Board agreed that the acquisition was not in the best interests of the stockholders, notwithstanding the numerous other benefits stated and purportedly given equal weight by the Board. The Company gave no indication that the analysis and calculation could not have been undertaken prior to the acquisition agreement. There is no indication in the S-4 that any such analysis or consideration to evaluate the potential impact was undertaken prior to the Co-Operation Agreement. Surely, such an analysis would have been material to stockholders voting whether to approve the acquisition.

As the Court of Chancery noted, the record establishes a credible basis to infer a failure by the Board, but arbitrarily characterized the failure as mere negligence. Ex. A at 39 n.122. The failure may just as conceivably have been

[13] In approving and recommending the Transaction, the AbbVie directors had an affirmative duty to determine whether the Transaction was advisable and in the best interests of the Company and its stockholders and to do so in accordance with their continuing fiduciary duties of care and loyalty. *Smith v. Van Gorkom*, 488 A.2d 858, 872-873 (Del. 1985). Merely recognizing a risk of new regulations does not necessarily satisfy the directors' duties where, as here, the risk relates to a "deal breaker" financial impact. Further, when a director intentionally fails to act on an informed basis or consciously disregards a risk, it constitutes a breach of the duty of loyalty in a failure to act in good faith. *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006). "[T]he need for adequate information is central to the enlightened evaluation of a transaction that a board must make." *Barkan v. Amstead Indus., Inc.*, 567 A.2d 1279, 1286 (Del. 1989).

intentional. AbbVie's books and records are necessary for SEPTA and the Court to determine whether the directors and officers considered, ignored and/or consciously disregarded the deal-breaker impact of a change to the tax law or regulations on the Transaction and whether the Transaction would be in the best interest of the AbbVie stockholders if a change to the tax law, or interpretations thereof (particularly retroactive) were enacted (the prospect of which was obviously likely) and the tax benefit lost. Similarly, the books and records are necessary to determine whether the analysis performed by management after the Inversion Regulations were announced supports the termination or was a pretext, given the numerous other benefits touted and unqualified original recommendation by the directors and officers.

The Court of Chancery further erred when it determined SEPTA had not provided a "credible basis" to infer waste because it was "inappropriate" for the Court "to judge whether including the Break Fee was appropriate given the risk that government action might sink the deal, or to judge whether paying the Break Fee was better for the Company" than closing the Transaction. Ex. A at 40. First, the Court of Chancery's finding required SEPTA to demonstrate that the AbbVie directors and officers in fact engaged in waste. That is not the standard; SEPTA need only provide facts inferring that waste may have occurred. Second, the Court of Chancery's finding that the Break Fee was a necessary cog for Shire to agree to

the Transaction was contrary to the evidence. The evidence presented by SEPTA demonstrates that Shire demanded the $500 million Cost Reimbursement Payment, not the $1.635 billion Break Fee, to protect against the risk the tax benefits were eliminated. As such, the approval of the Break Fee may constitute waste or a breach of fiduciary duty if it was not required by Shire to enter into the Transaction or the AbbVie directors and officers approved it without considering the need for it or how it would benefit AbbVie's shareholders.[14]

Given that SEPTA has shown a proper purpose for its investigation and, as discussed *supra*, established the books and records sought as "necessary and essential" before the Court of Chancery, the summary nature of a Section 220 action favors this Court determining the scope of books and records that SEPTA is entitled to inspect. *Cent. Laborers Pension Fund v. News Corp.*, 45 A.3d 139, 141 (Del. 2011) (In an appeal of a 220 action, the "Court may rest its appellate decision on any issue that was fairly presented to the Court of Chancery, even if that issue was not addressed."); *Unitrin Inc. v. Am. Gen. Corp. (In re Unitrin, Inc.)*, 651 A.2d 1361, 1390 (Del. 1995) (The Delaware Supreme Court may "rule on an issue fairly presented to the trial court, even if it was not addressed by the trial court.")

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[14] The propriety of a termination fee turns on an examination of a number of factors, including: the overall size of the termination fee, the absolute size of the transaction, the benefit to shareholders and the degree to which a counterparty found the termination fee to be crucial. *La. Mun. Police Emples. Ret. Sys. v. Crawford*, 918 A.2d 1172, 1182 n.10 (Del. Ch. Feb. 27, 2007) *citing In re Toys "R" Us, Inc., S'holder Litig.*, 877 A.2d 975, 1016 (Del. Ch. June 22, 2005).

III. THE COURT OF CHANCERY ERRED BY CONCLUDING THAT THERE WAS NO CREDIBLE BASIS TO INFER WRONGDOING BY OFFICERS

A. QUESTION PRESENTED

Does Section 220 require SEPTA to establish specific wrongdoing by specific officers to show a credible basis to infer wrongdoing? A14-20, 218-227.

B. SCOPE OF REVIEW

The Scope of Review is the same as that articulated in Section II.B, *supra*.

C. MERITS OF THE ARGUMENT

SEPTA produced credible evidence at trial that AbbVie's senior management had a significant role in identifying Shire as an acquisition target, continually advising the Board on the "legal, financial and other considerations" for the Transaction and negotiating the Transaction. A564-568. Notably, Gonzalez negotiated the Transaction in his capacity of CEO. A564. SEPTA also showed that in response to the Inversion Regulations, AbbVie's senior management team made the initial determination that the Transaction "was no longer in the best interests of stockholders at the agreed upon valuation, and the Board fully supported that conclusion." A223, 495. The senior management's significant role with respect to the negotiation of the Transaction, the Change in Recommendation and the termination of the Transaction provide a credible basis to infer that just as the directors, the officers may have engaged in mismanagement

and wrongdoing.

The Court of Chancery, however, required SEPTA to articulate specific wrongdoing by specific AbbVie officers in order to demonstrate a credible basis to infer wrongdoing by AbbVie's officers. Specifically, the Court of Chancery found that the only officer specifically mentioned was Gonzalez,[15] who also serves as the Chairman of the Board, and consequently he is protected by AbbVie's exculpatory provision for acts in his capacity as a director. Ex. A at 33-34 n. 108.

The Court of Chancery cited no authority requiring a shareholder seeking inspection under Section 220 to allege evidence of specific wrongdoing by specific fiduciaries. In fact, Delaware Courts have repeatedly admonished plaintiffs to use a Section 220 investigation to uncover facts sufficient to demonstrate wrongdoing by specific fiduciaries. *In re Sanchez Energy*, 2014 Del. Ch. LEXIS 239, *34 (Del. Ch. Nov. 25, 2014) (admonishing plaintiffs for not using Section 220 to uncover documents evidencing the involvement of officers and directors in a negotiation process); *In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 808, 819-820 (Del. Ch. 2005) (noting plaintiffs should have used Section 220 to investigate wrongdoing by specific individuals).

As discussed in Section I *supra*, the Court of Chancery erred in treating a Section 220 proceeding as a plenary proceeding and invoking Section 102(b)(7).

[15] Other than Gonzalez no other senior officer was identified in the S-4 as participating in the negotiation of the Transaction. The "tools at hand" are necessary for SEPTA to make such an identification.

The Court of Chancery acknowledged that Section 102(b)(7) does not apply to officers, even in its newly articulated requirement. Nonetheless, the Court of Chancery wrongly concluded that because Gonzalez was the Chairman of the Board, his actions were protected by AbbVie's Section 102(b)(7) provision.[16] Ex. A at 33-34 n.108. This finding completely ignores that AbbVie's senior management identified Shire as an acquisition target, the Board vested management with the authority to negotiate the Transaction and that Gonzalez, in his role as Chief Executive Officer, was the primary negotiator on behalf of AbbVie. A564-568. In fact, in discussing Gonzalez's role in the negotiations, the S-4 refers to him solely in his capacity as "Chief Executive Officer," not Chairman of the Board. A564. In addition, senior management made the determination in the first instance to terminate the Transaction. As such, even under the Court of Chancery's new articulation, SEPTA provided a credible basis to infer that Gonzalez's actions were taken in his capacity as an officer and thus not protected under AbbVie's Section 102(b)(7) provision in any plenary action.

For all these reasons, SEPTA established a credible basis to infer possible wrongdoing by AbbVie officers.

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[16] *McPadden v. Sidhu*, 964 A.2d 1262, 1275 (Del. Ch. Aug. 29, 2008) ("an officer does not benefit from the protections of [an] exculpatory provision, which are only available to directors."); *In re Celera Corp. S'holder Litig.*, 2012 Del. Ch. LEXIS 66, *104 n. 191 (Del. Ch. March 23, 2012) *citing Gantler v. Stephens*, 965 A.2d 695, 709 n. 37 (Del. 2009). ("Unlike with directors, "there currently is no statutory provision [like §102(b)(7)] authorizing comparable exculpation of corporate officers.").

CONCLUSION

For the foregoing reasons, the Court of Chancery's judgment should be reversed in its entirety.

Respectfully submitted,

CHIMICLES & TIKELLIS LLP

/s/ Pamela S. Tikellis

Pamela S. Tikellis (Del. I.D. #2172)
Robert J. Kriner, Jr. (Del. I.D. #2546)
Scott M. Tucker (Del. I.D. #4925)
Matthew T. Arvizu (Del. I.D. #6010)
222 Delaware Ave., Suite 1100
Wilmington, Delaware 19801
Tel: (302) 656-2500

Attorneys for Southeastern Pennsylvania Transportation Authority