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Case Number 390,2013

IN THE SUPREME COURT OF THE STATE OF DELAWARE

HAROLD GRILL 2 IRA,

Plaintiff Below, Appellant,

v.

LOUIS R. CHÊNEVERT, JOHN V. FARACI, JEAN-PIERRE GARNIER, JAMIE S. GORELICK, EDWARD A. KANGAS, ELLEN J. KULLMAN, MARSHALL O. LARSEN, RICHARD D. MCCORMICK, HAROLD MCGRAW III, RICHARD B. MYERS, H. PATRICK SWYGERT, ANDRE VILLENEUVE, CHRISTINE TODD WHITMAN, and GEORGE DAVID,

Defendants Below, Appellees,

and

UNITED TECHNOLOGIES CORP.,

Nominal Defendant Below, Appellee

No. 390, 2013

COURT BELOW:

COURT OF CHANCERY OF THE STATE OF DELAWARE
C.A. NO. 7999-CS

APPELLEES' ANSWERING BRIEF

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NATURE OF PROCEEDINGS

In June 2012, United Technologies Corporation ("UTC"), a Delaware corporation, entered into a deferred prosecution agreement ("DPA") with the U.S. Department of Justice and into a consent agreement with the U.S. Department of State. UTC entered into the agreements to resolve charges that (1) one of its subsidiaries exported software in 2002 and 2003 to the Chinese government for use in a military helicopter, without authorization by the State Department, and (2) in 2006, UTC and two of its subsidiaries made false statements in voluntary disclosures to the State Department about the unauthorized exports. Both agreements require UTC to implement remedial measures and pay monetary penalties.

Plaintiff Howard Grill 2 IRA filed this derivative action on October 24, 2012. The complaint names as defendants all thirteen incumbent UTC directors, as well as one former director. The complaint seeks to hold the defendant directors responsible for the liability UTC incurred in resolving the software export control violations and related disclosure violations.

On February 8, 2013, defendants moved to dismiss the complaint, arguing, among other things, that the complaint failed to satisfy the stringent pleading standard of Court of Chancery Rule 23.1. In opposition, plaintiff argued that demand was excused because a majority of the incumbent directors faced a substantial likelihood of liability under the complaint and accordingly could not impartially consider a demand. Specifically, plaintiff argued that the complaint alleged with sufficient particularity that the defendant directors had "caus[ed] the

corporation to violate the positive laws it is obliged to obey," either by deliberately causing UTC to include the false statements in the 2006 disclosures or by failing to correct those false statements until July 2010, or both.

On June 18, 2013, the Court of Chancery (Strine, C.) dismissed the complaint for failure to satisfy Rule 23.1. The court ruled that the complaint did not "plead with particularity that a majority of the board faces a substantial risk of liability," A 13, because "the complaint does not allege that the directors caused any legal breach, in the first instance, or even that they were aware before the end of 2011 that UTC had broken the law," A 12. This is plaintiff's appeal of that dismissal.

SUMMARY OF ARGUMENT

1. Denied. Plaintiff argues that demand is excused because the complaint alleges with particularity that at least a majority of UTC's incumbent directors face a substantial likelihood of liability for the asserted claims. In particular, plaintiff argues that the directors face a substantial likelihood of liability for deliberately failing to correct until 2010 false statements that UTC made in voluntary disclosures to the State Department in 2006 regarding export control violations. According to plaintiff, the directors' deliberate failure to correct the false statements led to criminal charges against UTC and its subsidiaries and ultimately to UTC's entry into a DPA and consent agreement with the government.

As the Court of Chancery correctly concluded, the complaint is subject to dismissal under Rule 23.1 because it does not allege with particularity that any of the defendant directors faces a substantial likelihood of liability. Judicially noticeable court records conclusively show that UTC was never charged with failing to correct the false statements made in the 2006 disclosures, and so never incurred any liability for any failure to correct those disclosures. Moreover, the complaint does not allege any facts that could plausibly support an inference that the defendant directors knew that UTC intended to submit the 2006 disclosures, much less that they knew the planned disclosures contained false statements. And even assuming, contrary to judicially noticeable fact, that UTC incurred liability for failing to correct the false statements in the 2006 disclosures until 2010, there is no basis in the complaint to infer that the directors learned of any false statements in the disclosures before 2010. Therefore, the complaint cannot support an

inference that the defendant directors knowingly concealed the falsity of those statements from the government until 2010.

2. Denied. Plaintiff argues that the complaint alleges with sufficient particularity that the defendant directors learned of the false statements in the 2006 disclosures before 2010 because the complaint alleges that the board discussed the export control violations and the previously submitted 2006 disclosures at meetings between December 2006 and September 2008. But the allegation that the board discussed the 2006 disclosures does not by itself support a reasonable inference that the board knew those disclosures contained false statements. In addition, the complaint does not allege that anyone who briefed the board was aware of the false statements, or that any director learned of the false statements in communications outside of board meetings. Accordingly, as the Court of Chancery correctly concluded, the complaint does not plead with sufficient particularity that any of the defendant directors learned of the false statements in the 2006 disclosures before July 2010, when the directors' alleged concealment of the false statements ended.

COUNTERSTATEMENT OF FACTS

The background below assumes the truth of the allegations in the complaint and is provided for purposes of this appeal only. The facts are drawn from the complaint and, except where noted, all citations are of the complaint.

A. United Technologies Corporation, its subsidiaries, and its directors

Nominal defendant UTC is a Delaware corporation headquartered in Hartford, Connecticut. A 21 (¶ 13). It provides high technology products and services to the building systems and aerospace industries and is a major military contractor to the U.S. and foreign governments. A 18 (¶ 4), A 21 (¶ 13). Pratt & Whitney Canada ("P&W Canada" or "PWC") is a Canadian subsidiary of UTC that supplies aircraft engines for commercial, military, business, and general aviation markets. A 21 (¶ 13). Hamilton Sundstrand Corp. ("HSC") is a U.S. subsidiary of UTC that supplies aerospace products such as flight and engine control systems. A 21 (¶ 13), A 38 (¶ 69). P&W Canada and HSC, together with UTC, are referred to as the "UTC entities."

UTC has thirteen directors, A 21-23 (¶¶ 15-27), all of whom are exculpated by the company's charter from liability for duty of care violations, *see* Restated Certificate of Incorporation, A 171 (TENTH).[1] Louis Chênevert, the company's president and chief executive officer, is currently the chairman of the board. A 21 (¶ 15). The other twelve directors, none of whom is alleged to have ever been employed by UTC, are John V. Faraci, Jean-Pierre Garnier, Jamie S. Gorelick,

[1] The court takes judicial notice of a corporate charter in resolving a motion to dismiss under Court of Chancery Rule 23.1. *In re Baxter Int'l, Inc. S'holders Litig.*, 654 A.2d 1268, 1270 (Del. Ch. 1995).

Edward A. Kangas, Ellen J. Kullman, Marshall O. Larsen, Richard D. McCormick, Harold McGraw III, Richard B. Myers, H. Patrick Swygert, Andrew Villeneuve, and Christine Todd Whitman. A 21-23 (¶¶ 16-27). The complaint names as defendants all of UTC's present directors, A 21-23 (¶¶ 16-27), as well as George David, who retired as the company's chairman and chief executive officer in 2009, A 23 (¶ 28).

The UTC board has an Audit Committee, composed entirely of outside directors, A 21-23 (¶¶ 16, 19, 22, 24, 25, 26), that is responsible for overseeing "the adequacy of processes to assure compliance with UTC's policies and procedures, financial controls, code of ethics and applicable laws and regulations, and policies with respect to risk assessment and management," A 26 (¶ 36).

The UTC entities are subject to the Arms Export Control Act (the "AECA"), 22 U.S.C. §§ 2278-2780, and the International Traffic in Arms Regulations (the "ITAR"), 22 C.F.R. §§ 120-130. A 18 (¶ 4). The AECA restricts U.S. defense contractors from selling sensitive technologies to certain foreign countries. A 18 (¶ 4). The ITAR implement the provisions of the AECA and are interpreted and enforced by the Department of State Directorate of Defense Trade Controls. A 18 (¶ 4). As relevant here, the ITAR provide that information and material related to U.S. military technologies may not be transferred to any foreign state unless authorized by the State Department. A 18 (¶ 4). ITAR-restricted material includes civilian technologies modified with ITAR-controlled technologies. A 18 (¶ 4).

B. P&W Canada unlawfully exports engine control software to China

In early 2000, the Chinese government approached P&W Canada about supplying PT6C-67C engines for a new twin engine, 5.5-ton helicopter called the Chinese Medium Helicopter ("CMH"). A 29 (¶ 38). The Chinese government presented the CMH as a dual-use helicopter, with a military version to be developed first and a civil version to follow. A 29 (¶ 38). The Chinese government told P&W Canada that it intended to use the 67C engines in development models of the military version and production models of the civil version, but that it planned to use Chinese-made engines in production models of the military version. A 29-30 (¶ 38). P&W Canada shipped ten 67C engines to China between November 2001 and October 2002. A 33 (¶ 50). The export of the engines did not violate U.S. export controls because the 67C engines were federally certified as "dual use"—military and civil—items under the ITAR. A 19 (¶ 7), A 33 (¶ 50).

In January 2002, P&W Canada issued a purchase order to HSC for electronic engine control software for the 67C engines sent to China. A 33 (¶ 51). P&W Canada told HSC that the software was for a commercial dual-use helicopter. A 33 (¶ 51). Between January 2002 and October 2003, HSC exported modified engine control software to P&W Canada, which in turn exported the software to China. A 33 (¶ 52). Although the software, unlike the engines themselves, was a controlled technology subject to American export restrictions, no export authorization was sought or obtained. A 19 (¶ 7), A 33 (¶ 52).

In early 2004, HSC sent inquiries to P&W Canada regarding the "end-use" of the modified software. A 37 (¶ 68). When HSC learned that P&W Canada was exporting the software to China for use in a military helicopter without State Department authorization, it refused to continue supplying the software. A 39 (¶¶ 71-72).

P&W Canada had initially hoped that it would secure a position as the exclusive provider of engines for the civil version of the CMH by providing engines for the development of the military version. A 31 (¶ 45). But by 2006, P&W Canada had obtained no such commitment and it declined to continue supporting the CMH program. A 31 (¶ 45), A 43 (¶ 87). P&W Canada ultimately did not ship any engines to China for the CMH other than the ten development engines. A 43 (¶ 88).

C. UTC voluntarily but inaccurately discloses P&W Canada's unlawful software exports

On February 15, 2006, an investor advisory group sent an e-mail to UTC's investor relations department inquiring about UTC's alleged involvement in the manufacture of a Chinese combat helicopter in violation of U.S. and European Union arms embargoes. A 43-44 (¶ 89). The inquiry and other general information related to the CMH program were included in briefing materials prepared for "relevant personnel" by UTC before the April 2006 annual shareholders meeting. A 44 (¶ 89). The complaint alleges that the relevant personnel "apparently include[ed] UTC's Chairman of the Board and/or other directors in attendance at the meeting." A 44 (¶ 89). At the time, UTC's chairman

and chief executive officer was George David. A 23 (¶ 28). David retired as a director of UTC in 2009. A 23 (¶ 28). The complaint does not allege which or how many other directors might have seen the briefing materials.

In April and May 2006, lawyers from UTC and P&W Canada met to discuss the briefing materials and P&W Canada's China programs and resolved to determine whether UTC had to disclose the export of the engine control software to China. A 44 (¶ 90). On May 8, 2006, UTC decided that the export violated regulations and should be disclosed to the State Department. A 44 (¶ 91).

On July 17, 2006, UTC sent a letter disclosing the violation to the Department of State Directorate of Defense Trade Controls. A 44 (¶ 92). UTC sent two follow-up submissions to the State Department on August 11, 2006 and September 6, 2006. A 45 (¶ 93). The submissions stated that P&W Canada understood at the outset of its engagement with the Chinese government that the CMH was intended to be a dual-use platform, with civil and military versions to be developed contemporaneously, A 45 (¶ 94), and that P&W Canada did not know the lead version would be military until 2003 or 2004, A 44-45 (¶¶ 92-93). These statements were inaccurate because at least some P&W Canada employees had known in 2000 that the Chinese government intended to develop a military version before a civil version and that the Chinese government had only later proposed a contemporaneous development schedule. A 29 (¶ 38), A 31 (¶¶ 43, 45).

Some unnamed UTC employees realized before the submissions were sent that the planned disclosure regarding when P&W Canada became aware of the lead military version was inaccurate. A 46 (¶ 98). They communicated their concerns

about the inaccuracy of the planned disclosure to an unnamed UTC executive, but the executive declined to alter the disclosure. A 46 (¶ 98). The complaint does not allege that the executive shared the concerns with anyone else.

In addition to describing the circumstances surrounding the unlicensed software exports, UTC's submissions to the State Department also stated that UTC had promptly taken remedial action upon learning of the export violations. A 45 (¶ 93). In July 2010, UTC acknowledged that HSC had failed to implement all the corrective measures as disclosed. A 48 (¶ 108).

D. The UTC Board of Directors and Audit Committee are briefed on the violation of export controls

The complaint alleges that the UTC Board of Directors and Audit Committee were briefed on and discussed the violation of export controls in connection with the CMH program at six meetings between December 2006 and September 2008. With respect to these meetings, the complaint alleges only that:

- A board presentation dated December 12, 2006 and titled "Business Practices" refers to the violation of export controls in connection with the CMH program, A 46 (¶ 99);

- A board presentation dated December 2007 and titled "Litigation" contains the heading "Z-10 Investigation Update," A 47 (¶ 101);

- Minutes from a December 11, 2007 Audit Committee meeting state that the committee was briefed on UTC's disclosures of export control violations to the State Department, A 47 (¶ 102);

- Minutes from a December 12, 2007 board meeting show that the export control violations were again discussed, A 47 (¶ 103);

- Minutes from a September 10, 2008 Audit Committee meeting state that the committee discussed the "Z-10 export matter," A 47 (¶ 105);

- Minutes from a September 10, 2008 board meeting show that the board was given an update on the "Z-10 Investigation," A 47 (¶ 106).

The complaint does not allege that any export control violation related to the CMH program occurred after the board was first briefed on the matter.

E. UTC and two of its subsidiaries enter into agreements with the U.S. government to resolve charges that they committed and failed to properly disclose export control violations

In November 2011, the State Department informed UTC that it considered the disclosures UTC made in 2006 concerning the CMH program to be deficient and to warrant penalties or sanctions. A 49 (¶ 111). UTC publicly disclosed this fact in a February 2012 10-K filing and further disclosed that it was in discussions with the State Department regarding a consent agreement that it anticipated would provide for a payment by the company. A 49-50 (¶ 112). In the same filing, UTC disclosed that it was also in discussions with the Justice Department, which had separately conducted a criminal investigation of the export of the HSC software to China and the accuracy of the company's 2006 disclosures to the State Department. A 50 (¶ 112).

On June 28, 2012, the Justice Department filed in the U.S. District Court for the District of Connecticut a three-count information (the "Information") charging the UTC entities with violations related to the unauthorized software exports. A 50 (¶ 113); *see also* A 17 (¶ 1) (identifying the case as *United States* v. *United Technologies Corp.*, Cr. No. 12-146 (D. Conn.)). The first count charged that from

approximately January 2002 to October 2003, P&W Canada knowingly caused HSC to export software for use in the military CMH without authorization from the State Department. A 50 (¶ 114): Information, A 228-29 (¶¶ 30-31). The second count charged that the UTC entities knowingly made materially false statements in the disclosures submitted to the State Department on July 17, 2006 and September 6, 2006. A 51 (¶ 114); Information, A 229-30 (¶¶ 32-33). In particular, the second count charged that the UTC entities had falsely asserted that the Chinese government initially described the CMH program as a dual-use platform that would support parallel development of civil and military versions and that P&W Canada employees only later learned that the lead version would be military. A 51 (¶ 114); Information, A 229-30 (¶ 33). The third count charged that P&W Canada, from at least July 2002 to July 2006, and HSC, from at least 2004 to July 2006, knowingly failed to inform the State Department of the export of HSC software to China, despite knowing or having reason to know that the export was unlawful. A 51 (¶ 114); Information, A 230-31 (¶¶ 34-35).

On the same day, UTC, P&W Canada, and HSC each filed a waiver of indictment, and the government filed the DPA and a plea agreement. A 50 (¶ 113); Plea Agreement, A 233-43. The DPA contained a "Statement of Facts" describing the factual basis for the charged violations. *See* DPA, A 193-213. The government did not ascribe any blame to the UTC board or any individual director in that statement, elsewhere in the DPA, or in the Information.

Under the plea agreement, only P&W Canada pleaded guilty and only to the first and second counts of the Information. *See* Plea Agreement, A 233-34.

Pursuant to the DPA, the government recommended to the court that prosecution of all remaining charges be deferred for two years.[2] *See* DPA, A 175. Upon the government's motion, the court entered judgment pursuant to the DPA and the plea agreement. A 50 (¶ 113); Judgment, A 244-46.

In addition to entering into the DPA, UTC also entered into a consent agreement with the State Department. A 51 (¶ 115). The consent agreement provided that the company would implement various remedial measures with respect to its AECA and ITAR compliance programs. A 51 (¶ 115). The agreement also provided for an aggregate civil penalty of $55 million, A 51 (¶ 115), $20 million of which would be suspended if UTC applied at least that amount to remedial measures, *see* DPA, A 182 (¶ 10(d)).

F. The Court of Chancery dismisses the complaint for failure to satisfy Rule 23.1

Plaintiff Howard Grill 2 IRA has held UTC stock since July 2006. A 20 (¶ 12). In July 2012, plaintiff made a books-and-records demand on UTC pursuant to 8 Del. Code § 220. A 20-21 (¶ 12). Plaintiff filed this derivative complaint on October 24, 2012, naming as defendants all thirteen incumbent UTC directors and George David, UTC's chairman and chief executive officer until 2009. The complaint alleges two claims against the director defendants, one for breach of fiduciary duty (Count I), A 62-64 (¶¶ 138-144), and one for waste (Count II),

[2] The complaint erroneously alleges that UTC, P&W Canada, and HSC each pleaded guilty to all three counts of the Information. A 50-51 (¶ 114). But, as the Court of Chancery recognized, the judicially noticeable court records show otherwise. A 5. Plaintiff does not contest that aspect of the Court of Chancery's decision in its appeal.

A 64-65 (¶¶ 145-151), but plaintiff abandoned its waste claim after defendants filed their motion to dismiss.

As the Court of Chancery observed, "[t]he complaint is written like a *Caremark* complaint." A 11. The complaint alleges that the Director Defendants breached their fiduciary duties by failing to properly discharge their oversight duties: "By subjecting UTC to the unreasonable risk of substantial losses due to their failure to monitor, prevent and/or report the many acts of UTC managers and controlling persons that directly and knowingly violated ITAR and the Arms Export Control Act, the Director Defendants failed responsibly and with due care to oversee and implement proper business practices . . . ." A 64-65 (¶ 148). The complaint thus seeks to hold the director defendants responsible for the export control violations related to the CMH program committed by UTC or its subsidiaries.

In their motion to dismiss, defendants argued that (1) the complaint failed to state a *Caremark* claim, and (2) plaintiff did not have standing to pursue derivative claims for much of the charged misconduct, such as the unlawful software exports and the failure to disclose those exports until July 2006, because that conduct preceded plaintiff's ownership of UTC stock. In response, plaintiff argued that the complaint neither asserted a *Caremark* claim nor sought to hold the director defendants responsible for corporate misconduct before July 2006. Rather, plaintiff argued, the complaint's extensive allegations concerning pre-2006 misconduct were just "background." According to plaintiff, the complaint alleged that the director defendants breached their duty of loyalty by deliberately causing

UTC to submit false statements to the government in 2006 and by refusing to acknowledge the falsity of those statements until July 2010, all in violation of 18 U.S.C. § 1001, as charged in Count Two of the Information.

The Court of Chancery ruled that the complaint failed to satisfy the stringent pleading standard of Rule 23.1. "Of course," the court recognized, "it is a breach of the duty of loyalty for the directors of a corporation to knowingly cause that corporation to break the law." A 12. "[B]ut the complaint does not even plead any facts in an attempt to support a pleading stage inference that any particular director should have known that the disclosures were false, much less plead facts supporting a pleading stage inference of actual knowledge." A 12.

ARGUMENT

I. The Court of Chancery's dismissal of the complaint under Rule 23.1 should be affirmed

A. Question Presented

Plaintiff seeks to hold the defendant directors liable for deliberately waiting until 2010 to correct false statements that UTC made to the federal government in 2006. Is the plaintiff excused from making demand notwithstanding the complaint's failure to allege that any present UTC director knew, before 2010, that UTC made false statements to the government in 2006?

B. Scope of Review

This Court reviews *de novo* the dismissal of a derivative action under Court of Chancery Rule 23.1. *See Stone* v. *Ritter*, 911 A.2d 362, 371 (Del. 2006).

C. Merits of Argument

Under Delaware law, the decision whether to pursue litigation on behalf of a corporation is normally entrusted to the board of directors, which is generally charged with managing the business and affairs of the corporation. *Id.* at 366. Court of Chancery Rule 23.1 thus requires that the complaint in a derivative action "allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors . . . and the reasons for the plaintiff's failure to obtain the action or for not making the effort." A plaintiff who chooses not to make demand upon the board satisfies the requirement of Rule 23.1 by alleging with particularity that demand is excused because the directors cannot

impartially decide whether to bring the claims the plaintiff seeks to assert on behalf of the corporation. *See Aronson* v. *Lewis*, 473 A.2d 805, 814-15 (Del. 1984).

Rule 23.1's "stringent requirements of factual particularity . . . differ substantially from the permissive notice pleadings governed solely by Chancery Rule 8(a)" and are "not satisfied by conclusory statements or mere notice pleading." *Brehm* v. *Eisner*, 746 A.2d 244, 254 (Del. 2000). A derivative complaint that fails to allege particularized facts showing why the board should be deprived of its right to control corporate litigation will be dismissed. *See Aronson*, 473 A.2d at 814-15.

Plaintiff here asserts that the incumbent defendant directors cannot impartially consider a demand because "each faces a substantial likelihood of liability," Pl's Br. at 10, for "causing the corporation to violate the positive laws it is obliged to obey," *id.* at 30 (quoting *Guttman* v. *Huang*, 823 A.2d 492, 506 n.34 (Del. Ch. 2003)). Specifically, plaintiff accuses the directors of causing UTC to violate 18 U.S.C. § 1001 between 2006 and July 2010 by deliberately failing to correct false statements made in the disclosures UTC submitted to the State Department in 2006. *See, e.g.*, Pl.'s Br. at 1 ("The Board's misconduct involved their complicity in misrepresentation to federal agencies by failing to correct prior false disclosures to the government . . . ."); *id.* at 11-12 ("[I]n July 2006, UTC submitted a misleading description of the export violations to the Department of State, and for four years thereafter, [the Director Defendants] continued to mislead the government until in July 2010 UTC acknowledged the misrepresentations." (internal citations omitted)); *id.* at 30 ("The positive law violated was . . . 18

U.S.C. § 1001.”). This misconduct harmed UTC, plaintiff asserts, because it led the federal government to charge UTC with violating § 1001 in Count Two of the Information, and ultimately to UTC’s entry into the DPA and consent agreement. *See id.* at 3-4, 30.

This grave accusation appears nowhere in the complaint. The complaint does not plead a single fact suggesting that the directors knowingly caused UTC to violate 18 U.S.C. § 1001 by deliberately failing to correct false statements in disclosures already submitted to the State Department. The complaint does not even plead the *conclusion* that the directors engaged in such a fraud or cover-up. It is telling that plaintiff does not cite the complaint when it asserts in its brief that the directors caused UTC to violate § 1001. *See, e.g.*, Pl.’s Br. at 33 (asserting, without citing the complaint, that “the Board’s conduct at issue caused the Company to violate the law, namely, 18 U.S.C. § 1001”). Contrary to plaintiff’s suggestion, the complaint is devoid of particularized allegations suggesting that UTC’s directors knowingly sanctioned the company’s violation of § 1001 or any other law.

To begin with, the government did not charge UTC with violating 18 U.S.C. § 1001 by failing to correct false statements over a four-year period ending in July 2010. Count Two of the Information (the only count in which the government charged UTC or any of its subsidiaries with a violation of § 1001) charged that UTC, P&W Canada, and HSC violated § 1001 by knowingly including false statements in disclosures submitted to the State Department “on July 17, 2006 and September 6, 2006.” *See* Information, A 229-30 (¶ 33). That is all. The

government did not charge UTC or any of its subsidiaries with making any false statements after September 6, 2006. And it did not charge UTC or any of its subsidiaries with failing to correct false statements in previously submitted disclosures.

Nor does the DPA fault UTC for submitting false disclosures after September 6, 2006 or for failing to correct previously submitted disclosures. Even plaintiff's own complaint does not allege that UTC made any false statements to the State Department after September 6, 2006, or that the government ever faulted UTC for failing to correct previously submitted disclosures. Plaintiff's assertion that UTC was charged with violating § 1001 between 2006 and July 2010 by deliberately failing to correct false statements in disclosures to the State Department is thus not only disproven by the judicially noticeable Information and DPA, but also inconsistent with its own complaint.

1. The complaint does not and cannot plead that the directors knowingly caused UTC to submit false disclosures to the government

Because there is no pleaded basis to infer that UTC incurred any liability for deliberately failing to correct the false statements made in the 2006 disclosures, plaintiff's argument that the director defendants themselves face a substantial likelihood of liability for that alleged misconduct necessarily fails. Furthermore, the complaint does not contain particularized allegations that the defendant directors face a substantial likelihood of liability even for the charged misconduct—that is, the false statements made in the 2006 disclosures.

The complaint includes no allegations suggesting that the defendant directors knowingly authorized the submission of the false statements in 2006. Not a single fact is alleged to show that any director had input of any kind into the contents of the July and September 2006 disclosures, or knew the contents of those disclosures before they were submitted, or knew even that those disclosures were being made. Plaintiff identifies only one communication to any director regarding the Chinese helicopter program before the first of the 2006 disclosures was submitted: the briefing materials relating to the February 2006 investor inquiry that were prepared before the April 2006 annual shareholders' meeting. *See* Compl., A 43-44 (¶ 89); Pl.'s Br. at 11. The complaint, however, nowhere alleges that those briefing materials indicated that the company intended to disclose export violations in connection with the program, much less that the briefing materials contained any basis to suspect that any disclosures would contain false statements. To the contrary, the complaint alleges that UTC did not even determine that any export control violations had occurred until May 2006—after the briefing materials were distributed. *See* Compl., A 43-44 (¶¶ 89-91).

In any event, the complaint does not allege that the briefing materials were sent to even a single incumbent director. The complaint alleges only that the briefing materials were distributed to "UTC's Chairman . . . and/or other directors in attendance at the [April 2006 annual shareholders] meeting." Compl., A 44 (¶89). In 2006, George David was UTC's chairman and chief executive officer, but he retired in 2009 and is not presently a director of UTC. Compl., A 23 (¶ 28). No other directors are alleged to have seen the briefing materials, and the

complaint's cagey "and/or" allegation confirms that plaintiff cannot plead that any other director did see them.[3] Lacking entirely are particularized allegations showing that a specific director (let alone a majority of incumbent directors) saw the briefing materials. There is thus no pleaded basis to accuse any director of authorizing the false statements in the July and September 2006 disclosures—the only false statements charged by the government as violations of § 1001.

2. The complaint does not and cannot plead that the directors knowingly failed to correct false disclosures previously submitted to the government

There is similarly no pleaded basis to accuse any director of knowingly failing to correct the false statements in the July and September 2006 disclosures that were charged as violations of § 1001—even assuming, contrary to the complaint, the Information, and the DPA, that UTC incurred any liability for such a failure. Plaintiff's theory is that UTC's directors learned of the false statements at board meetings held between December 2006 and September 2008 but failed to acknowledge to the government the falsity of those statements until July 2010. *See, e.g.*, Pl.'s Br. at 18, 22-23. The allegations of the complaint do not support any part of this theory. Plaintiff does not plead facts showing when the directors learned of the false statements (let alone that they learned of them in board meetings beginning in December 2006). And plaintiff does not plead facts showing that UTC failed to acknowledge the falsity of those statements to the

[3] Moreover, the complaint's allegation that the briefing materials might have been prepared for and distributed to any director other than David is not supported by the DPA, which says that the briefing materials were prepared for "UTC senior management"—not the directors. *See* DPA, A 210.

government until July 2010. Both sets of factual allegations are necessary to support an inference that the directors improperly delayed alerting the government to the false statements after learning of the false statements themselves.

Plaintiff argues that the complaint pleads with sufficient particularity that the directors learned of the false statements at board meetings held between December 2006 and September 2008. *See* Pl.'s Br. at 27. But, as the Court of Chancery explained, the complaint's allegations, taken as true, establish only "that the board discussed the export violations in those meetings, *not* that the board was made aware that the company had made false disclosures and knowingly failed to cause UTC to correct them." A 12-13 (emphasis in original). In their entirety, the allegations concerning those board meetings consist of the following:

- "A largely redacted UTC internal presentation apparently intended for the Board, titled 'Business Practices' and dated December 12, 2006, references the violation of the export control regulations on the CMH project." Compl., A 46 (¶ 99).

- "A largely redacted internal UTC presentation apparently intended for the Board, titled 'Litigation' and dated '12/07,' contains the heading 'Z-10 Investigation Update.'" Compl., A 47 (¶ 101).

- "Minutes from a December 11, 2007 Audit Committee meeting state that the committee was briefed on UTC's disclosures of export violations to the State Department." Compl., A 47 (¶ 102).

- "Minutes from a December 12, 2007 Board meeting demonstrate that the export control violations were discussed." Compl., A 47 (¶ 103).

- "Minutes from a September 10, 2008 Audit Committee meeting state that the committee discussed the 'Z-10 export matter.'" Compl., A 47 (¶ 105).

- "Minutes from a September 10, 2008 Board meeting demonstrate that the Board was given an update on the 'Z-10 Investigation.'" Compl., A 47 (¶ 106).

None of these pleadings indicates that the false statements in the July and September 2006 disclosures were discussed or revealed at the board meetings. Nor do the minutes of the meetings, which were produced to plaintiff for inspection and which plaintiff attached as exhibits to its opposition brief below, show otherwise. *See* A 93-161. The complaint does not allege that the directors were informed of the false statements in any communications other than briefings at the specified board meetings. Plaintiff nevertheless insists that the directors' knowledge of the false statements can be inferred from the allegations that the directors were informed of the 2006 voluntary disclosures. But that inference is not reasonable, even under a lax notice pleading standard, because the complaint does not allege any facts suggesting that anyone who briefed the board knew of the false statements. Rather, the complaint alleges only that unnamed employees of UTC suspected that the disclosures contained false statements, but does not allege any facts that could support an inference that these concerns were directly or indirectly communicated to any director.

Plaintiff's concealment theory thus fails because the complaint does not allege when the directors learned of the false statements, much less that they learned of them before July 2010, when the period of their alleged concealment of the false statements ended. That defect precludes an inference that the directors

knew of inaccuracies in the disclosures before the government did, and thus also an inference that they deliberately concealed any inaccuracies from the government.

Plaintiff's concealment theory fails for yet another reason. Even assuming that the complaint sufficiently pleads that the directors learned of the false statements at the first alleged board meeting in which the board was briefed on the export violations—the December 2006 meeting—the complaint would still fail to support an inference that the directors concealed anything. That is because the complaint does not include any well-pleaded allegations as to when UTC acknowledged to the government the falsity of the statements that were ultimately charged as violations of § 1001. The complaint thus cannot support an inference that the directors improperly delayed notifying the government of the false statements.

Plaintiff tries to cure this defect by sleight of hand. Quoting a paragraph from the DPA's Statement of Facts not included in the complaint, plaintiff tells the Court that UTC did not acknowledge the falsity of the statements ultimately charged as violations of § 1001 until July 2010. Pl.'s Br. at 22. This is not what the DPA says. The paragraph from the DPA on which plaintiff relies states:

> The UTC Entities' disclosures also stated: "P&W/UTC . . . will continue to maintain and implement [certain] corrective actions . . . to avoid any future occurrences of this type of violation." During the course of the investigation, the UTC Entities were asked to report on the status of the corrective actions they had identified in the Z10 disclosure letters. In a July 2010 response, UTC acknowledged that HSC had neglected to follow through on, and had overstated several of the corrective actions—

> corrective actions that were presented to [the State Department] as mitigating factors to consider in their review of the conduct.

Pl.'s Br. at 22 (quoting DPA , A 212).

Plaintiff erroneously concludes from this paragraph that UTC did not acknowledge having made false statements until July 2010. The paragraph does not say that. It refers only to an acknowledgment of inaccurate statements concerning "corrective actions" that UTC and its subsidiaries had pledged to take in the 2006 disclosures in an effort to prevent export control violations of the type reported—the unlicensed export of engine control software to China. The inaccurate statements concerning "corrective actions," however, were not charged as violations of § 1001. The false statements charged as violations of § 1001 concerned when and how P&W Canada learned that the Chinese government intended to develop a military helicopter before a related civil model. *See* Information, A 229-30 (¶ 33). The Information specifies the charged false statements as:

> (1) that the Chinese Z10 helicopter program was first represented to PWC as a dual-use helicopter platform where civil and military applications would be developed in parallel, but as it unfolded, the Chinese Medium Helicopter became a military attack helicopter platform with a civil helicopter platform to follow;
>
> (2) that from the inception of the Z10 program in 2000, representatives from the China Aviation Industry Corporation II ("AVIC II") and the China National Aero-Technology Import & Export Corporation ("CATIC") in the People's Republic of China advised PWC that the Z10 program was a common helicopter program from

> which both civil and military variants would be developed in parallel utilizing a common platform; and
>
> (3) that PWC only learned several years into the project that the military version of the helicopter was the lead version, which they learned for the first time, by happenstance, in March 2003, when certain PWC engineers walked through a hangar in China and saw the Z10 military attack helicopter prototype for the first time;

Information, A 229-30 (¶ 33).[4]

The complaint does not allege (nor does plaintiff identify in its brief) when UTC first acknowledged the falsity of *those* statements. The complaint thus does not (and could not consistent with Court of Chancery Rule 11) allege that UTC waited until July 2010 to acknowledge to the government the falsity of those statements. And without such an allegation, the complaint cannot support an inference that the directors did not direct UTC to notify the government of the false statements immediately after they learned of them—even if that was, as plaintiff assumes (without any pleaded support), in December 2006.[5]

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[4] Plaintiff asserts in its brief that the director defendants finally acknowledged the false statements in July 2010 because it did not become clear until 2009 that the UTC entities would not be selected as contractors for the production models of the military CMH. *See* Pl.'s Br. at 29 ("With the Z10 [military attack helicopter] in production, the Director Defendants knew the UTC Entities could no longer hope to obtain CMH contracts and UTC could now come clean with the State Department"). But plaintiff's own complaint alleges that the Chinese government informed P&W Canada in 2000 that "it planned to use Chinese-made engines in production models of the military version." Compl., A 29-30 (¶ 38).

[5] The full DPA, which plaintiff quotes only selectively, discredits plaintiff's theory that UTC's directors deliberately concealed the false statements in the 2006 disclosures from the government. In the DPA, the government expressly recognizes that UTC "cooperated" with its investigation, A 186 (¶ 22), undertook "extensive reforms and remedial actions" in response to the investigated misconduct, A 176 (¶ 7), and "devoted significant resources" to identifying and disclosing past export control violations, A 177. None of these corporate actions, which plaintiff omits from the complaint and its brief, are consistent with a four-year scheme by the directors to

* * *

The Court of Chancery's dismissal of the complaint with prejudice should be affirmed for all these reasons. Plaintiff's theory of liability can fairly be characterized as outrageous. Plaintiff accuses UTC's overwhelmingly independent board of lying to the State Department over many years and perpetrating an extensive criminal fraud against the federal government. Plaintiff makes these grave accusations in a brief but conspicuously fails to utter a word of these charges—not a single supporting fact, not even the conclusory charge—in a verified pleading. This is not a coincidence. Plaintiff's accusations could not be made in a verified complaint consistent with law.

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conceal false statements in two disclosures regarding export control violations committed in connection with one program.

CONCLUSION

For the foregoing reasons, this Court should affirm the Court of Chancery's dismissal of the complaint with prejudice pursuant to Rule 15(aaa).

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