IN THE SUPREME COURT OF THE STATE OF DELAWARE

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

APPELLEE'S ANSWERING BRIEF

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Dated: July 29, 2015

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NATURE OF PROCEEDINGS

This appeal arose from the denial of the demand of Appellant Southeastern Pennsylvania Transportation Authority ("SEPTA"), pursuant to 8 Del. C. § 220, to inspect the books and records of AbbVie Inc. SEPTA contended it was entitled to inspection to evaluate a derivative action against AbbVie's officers and directors for breach of fiduciary duties and waste in connection with AbbVie's potential acquisition of Shire plc. AbbVie refused SEPTA's demand for inspection because SEPTA failed to state a proper purpose or provide a credible basis for inferring fiduciary misconduct in connection with that transaction.

Based on a stipulated record, on April 15, 2015, the Court of Chancery issued a Memorandum Opinion denying SEPTA's demand for inspection. Judgment was entered on April 22, 2015, and SEPTA's appeal followed.

AbbVie files this Answering Brief in response to SEPTA's appeal of the Court of Chancery's rulings that (1) SEPTA did not state a proper purpose to investigate any breach of fiduciary duty other than the duty of loyalty, because any other alleged wrongdoing was exculpated and therefore could not be the basis for a shareholder derivative action, the sole end for which SEPTA sought inspection; (2) SEPTA failed to establish a credible basis to infer that AbbVie's directors breached their fiduciary duty of loyalty or committed waste; and (3) SEPTA failed to establish a credible basis to infer any wrongdoing by AbbVie's officers.

SUMMARY OF ARGUMENT

1. Denied. The Court of Chancery correctly held that SEPTA did not state a proper purpose to investigate any breach of fiduciary duty other than the duty of loyalty, since any other alleged wrongdoing is exculpated by the Section 102(b)(7) clause in AbbVie's Certificate of Incorporation. The Court of Chancery properly premised this holding on the principle that "if a stockholder seeks inspection solely to evaluate whether to bring derivative litigation, the corporate wrongdoing which he seeks to investigate must necessarily be justiciable." (Pl. Ex. A[1] at 32)

2. Denied. The Court of Chancery correctly held that SEPTA failed to establish a credible basis to infer a breach of loyalty or other corporate misconduct by AbbVie's directors. Properly applying this Court's long-standing rule that a plaintiff seeking inspection pursuant to Section 220 must show some evidence supporting a credible basis to infer legitimate issues of wrongdoing, the Court of Chancery found no evidence supporting a credible basis that the AbbVie board's decisions were anything other than informed business judgments or that they constituted a breach of fiduciary duty or corporate waste.

[1] SEPTA attached the Court of Chancery's April 15, 2015 opinion to its opening brief as Exhibit A. Citations to "Pl. Ex. A" throughout this Brief are citations to that opinion.

3. Denied. The Court of Chancery correctly held that SEPTA did not establish a credible basis to infer corporate wrongdoing by AbbVie's officers. The Court found that SEPTA had made *no* concrete allegations against AbbVie's non-director officers, and held that generalized, unsupported allegations failed to meet SEPTA's burden of establishing a credible basis. Because SEPTA made no specific arguments about officer wrongdoing at the trial court, any such arguments have been waived here. And even were SEPTA's allegations against AbbVie's directors to apply to AbbVie's officers, those allegations are equally insufficient to establish a credible basis to infer wrongdoing by the officers.

STATEMENT OF FACTS

Defendant AbbVie is a research-based biopharmaceutical company headquartered in North Chicago, Illinois. (A524) AbbVie develops, manufactures, and sells innovative pharmaceutical products. (*See id.*) Shire plc is a biopharmaceutical company registered in the island of Jersey (in the U.K.) and headquartered in Ireland. (A524–25) Shire develops products related to rare diseases, neuroscience, and gastrointestinal conditions. (A524)

A. Late 2013 And Early 2014: AbbVie Contemplates A Merger With Shire And Begins Negotiations.

In October 2013, AbbVie identified Shire as a potential strategic partner. AbbVie was interested in Shire for many reasons, including its compatible and profitable product platform, attractive financial profile, and research and development potential. (A564; A318–19) In the seven months before approaching Shire with a proposal, AbbVie worked with a team of U.S. and U.K. legal, tax, and financial experts to study a potential business combination. (A533, A536, A564, A735)

On February 20, 2014, senior management presented the AbbVie board of directors with an overview of a potential transaction with Shire. (A564) AbbVie formally engaged J.P. Morgan as financial advisor on April 7, 2014. (*Id.*) On April 30, 2014, AbbVie's senior management reviewed with the board the legal, financial, and other considerations in connection with a potential transaction. (*Id.*)

The board authorized AbbVie's Chairman and CEO, Richard Gonzalez, to initiate discussions with Shire with a preliminary proposal. (*Id.*) Gonzalez met with Susan Kilsby, Shire's board chairman, on May 2.

From the first meeting, it was apparent that Shire was, at best, a reluctant partner. Indeed, Shire repeatedly rebuffed AbbVie's proposals before finally agreeing to engage in negotiations:

- **AbbVie's First Bid:** Following his May 2 meeting with Kilsby, on May 6, Gonzalez sent a non-binding cash and stock proposal to Shire with an indicative value of £39.50 per Shire ordinary share. (*Id.*) Shire rejected the proposal within three days. (A565)

- **AbbVie's Second Bid:** Following a May 9 board meeting, at which senior management, legal advisors, and J.P. Morgan reviewed a potential transaction with Shire, AbbVie sent a second bid to Shire at £40.97 per share. (*Id.*) Kilsby rejected both the proposal and Gonzalez's invitation to meet to discuss it. (*Id.*)

- **AbbVie's Third Bid:** At a special meeting of the AbbVie board on May 28, 2014, during which it reviewed the legal, financial, and business implications of the potential transaction, the board authorized a further increased proposal. (*Id.*) On May 30, Gonzalez submitted a proposal to Shire at £46.26 per share and again offered to meet with Kilsby to discuss terms. (*Id.*) Shire again rejected the increased proposal, and Kilsby explicitly discouraged Gonzalez from making any further proposals. (A565–66)

- **AbbVie's Fourth Bid:** Following a meeting on June 19, 2014, at which the board reviewed the status of the proposed Shire transaction with senior management, legal advisors, and J.P. Morgan, AbbVie increased its offer to £51.15 per share on July 8, 2014. (A566–67) Shire rejected the offer, but agreed to meet with AbbVie and to provide AbbVie with due diligence materials. (*Id.*)

- **AbbVie's Fifth Bid:** On July 9, 2014, the AbbVie board reviewed developments in the potential transaction with Shire, including the increased proposal made on July 8. (*Id.*) Following that review, AbbVie increased its offer to £52.25 per share. (*Id.*) Shire did not accept this offer, but Kilsby finally discussed proposed terms of the transaction with Gonzalez. (*Id.*)

- **AbbVie's Sixth Bid:** The executive committee of AbbVie's board met on July 13, 2014, to review developments, including recent discussions between Gonzalez and Kilsby, and authorized another increased proposal. (*Id.*) AbbVie then increased its offer to £53.20 per share. (*Id.*) Kilsby stated her belief that the Shire board would be willing to recommend the transaction at that price, subject to satisfactory resolution of other deal terms. (*Id.*)

As reflected by this summary of the record evidence, AbbVie's board was advised and consulted at each step of the effort to engage in discussions with Shire.

B. July 2014: AbbVie And Shire Reach An Agreement.

Following Kilsby's positive indication on July 13 of the Shire board's willingness to consider a transaction at the offered price, AbbVie and Shire engaged in negotiations over deal terms. Shire and AbbVie agreed to structure their combination as a so-called "inversion" transaction in which New AbbVie, the combined entity's new parent, would be a U.K.-based corporation. (A310) Reaching agreement on termination provisions, including on what terms Shire would be willing to allow AbbVie to withdraw from the transaction, was the "final sticking point" for Shire in the negotiations. (*See* A568; A787–90) Shire ultimately agreed that AbbVie's board, consistent with its fiduciary duties, could withdraw or modify its recommendation "in a manner adverse to the consummation of the Combination," and, if that resulted in the transaction being terminated, then AbbVie would pay a termination fee reflecting 3% of the total deal value. (A530–32) AbbVie secured Shire's agreement that this termination fee would be Shire's sole remedy in the event of termination on this basis. (A532)

On July 17, 2014, the AbbVie board held a special meeting with its legal and financial advisors to consider the specific terms of the proposed transaction. (A568) The board voted to approve the combination of AbbVie and Shire on the proposed terms. (*Id.*) On July 18, AbbVie and Shire executed the Co-operation Agreement and announced the proposed transaction. (*Id.*) In announcing the deal, AbbVie explained that it was motivated by the strategic advantages of combining its pharmaceutical business with Shire's as well as the transaction's tax benefits that would allow AbbVie to reduce its effective tax rate and gain flexible access to global cash flows. (A310–11; A504; A612–14)

C. The Legislative And Regulatory Backdrop Of The Transaction.

As AbbVie negotiated with Shire, certain members of Congress were advocating tax legislation to inhibit or foreclose inversion transactions. Consensus among those observing and participating in Washington's debate, however, was that any such legislative reform would be slow in coming. Analysts agreed that the near-term risk of legislation addressing or limiting inversion transactions was low:

- **April 29, 2014:** "Although President Obama has proposed rules that would almost eliminate inversions, his proposal stands little chance of becoming law. ***Congress is also unlikely to act during this election year***." (B8 (emphasis added))

- **July 16, 2014:** "Lawmakers say they want to stop United States companies from reincorporating overseas to lower their tax bills, but the Obama administration and ***Congress appear unlikely to take any action to stem the tide of such deals anytime soon***." (A791–95 (emphasis added))
- **July 25, 2014:** "Despite the heated rhetoric coming out of Washington, we continue to believe that ***legislation targeting tax inversions remains unlikely in the near term***, given the current political landscape. Tax inversion is more likely to be addressed as part of comprehensive tax reform rather than a piecemeal provision, and the earliest that could likely happen is 2015. AbbVie expects to close the deal in 4Q14, and the consensus seems to be that such legislation would not be retroactive." (B9 (emphasis added))

Consistent with this commentary, to this day, Congress has taken no action.

Statements by key government officials indicated that potential ***administrative*** reform to inhibit inversion transactions was even less likely than legislative action. In April 2014, Internal Revenue Service commissioner John Koskinen stated, "We've done, I think, probably all we can within the statute [on tax inversions]." (A821–22) One analyst noted, "Koskinen's remarks show the limits of the government's ability to respond without Congress and suggest that the Obama administration won't make a regulatory move to stop or limit so-called corporate inversions." (*Id.*) Further driving home this point, Secretary of the Treasury Jack Lew confirmed on July 16, 2014, that Treasury did not have the authority to effect tax inversion reform and that Congress, which would need to enact any such reforms, "might not get it done quickly." (A826) Secretary Lew elaborated:

> "[W]e [at Treasury] have looked at the tax code. . . . ***We do not believe we have the authority to address this inversion question through administrative action.*** If we did, we would be doing more. That's why legislation is needed."

(*Id.* (emphasis added))

D. September 2014: The Treasury Department Does An About-Face.

After AbbVie and Shire reached and announced their deal, reports began to emerge in August 2014 that the U.S. Treasury was considering unspecified measures to address inversion transactions. (*See* B15) Despite having disavowed its authority to take action to address tax inversions, on September 22, 2014, Treasury issued a Notice of its intention to issue wide-reaching tax inversion rules. (*See* A464–77) These rules would apply retroactively to inversions completed on or after the date of the Notice and would "re-interpret[] longstanding tax principles in a uniquely selective manner designed specifically to destroy the financial benefits of these types of transactions." (A495) For example, the new rules would prevent inverted companies from taking actions that were previously permissible, including accessing a foreign subsidiary's earnings while deferring U.S. tax through the use of "hopscotch" loans, restructuring a foreign subsidiary to access its earnings tax-free, and transferring cash or property from a foreign subsidiary to the new parent without incurring U.S. tax. (A464–77; A292–93) Treasury further indicated that additional new, unspecified regulations would likely follow. (A477)

AbbVie analyzed the proposed Shire transaction in light of the new Treasury rules and threat of future additional unidentified rules and explored whether options existed to keep the transaction viable at the agreed-upon price. (A809; A478–97) Its analysis included the advice of external tax, legal, and financial advisors in both the U.S. and the U.K. (A478–97) AbbVie's executive management team ultimately concluded that pursuing the transaction at the agreed upon valuation was no longer in the best interests of stockholders. (*Id.*) As AbbVie explained, the new Treasury rules "eliminated certain of the financial benefits of the transaction, most notably the ability to access current and future global cash flows in a tax efficient manner as originally contemplated in the transaction. This fundamentally changed the implied value of Shire to AbbVie in a significant manner." (A809) Further, Treasury's notice "introduced an unacceptable level of risk and uncertainty given the magnitude of the proposed changes and the stated intention of the Department of Treasury to continue to revise tax principles to further impact such transactions." (A495)

E. October 2014: AbbVie And Shire Terminate The Agreement.

Based on the analysis of AbbVie's management and advisors, the board decided to withdraw its recommendation of the proposed transaction. (*Id.*) AbbVie and Shire subsequently entered into an agreement terminating the transaction, and AbbVie paid Shire the agreed-upon termination fee (approximately 3% of the value of the deal, or about $1.635 billion). (A479)

F. The Proceedings Under 8 Del. C. § 220.

On November 3, 2014, SEPTA sent a demand letter seeking to inspect AbbVie's books and records. (A245–91) AbbVie denied the requested inspection because SEPTA failed to establish a proper purpose for its demand. (A498–500) SEPTA filed its Complaint on November 19, 2014. The Chancery Court heard oral argument on February 11, 2015, based on a stipulated record.

On April 15, 2015, the Court of Chancery issued an opinion denying SEPTA's Section 220 demand.[2] The Court held SEPTA (1) did not have a proper purpose to investigate any breach of fiduciary duty other than the duty of loyalty, when SEPTA's sole reason for inspection was to evaluate whether to bring a shareholder derivative claim (Pl. Ex. A at 27–33); (2) failed to establish a credible basis to infer a breach of a fiduciary duty or waste by AbbVie's directors (Pl. Ex. A at 34–43); and (3) failed to establish a credible basis to infer a breach of a fiduciary duty or waste by AbbVie's officers (Pl. Ex. A at 33–34 n.108).

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[2] In the same opinion, the Court of Chancery also denied the substantially similar Section 220 demand of a second plaintiff, James Rizzolo. Rizzolo did not appeal.

ARGUMENT

I. THE COURT OF CHANCERY PROPERLY HELD SEPTA DID NOT STATE A PROPER PURPOSE TO INVESTIGATE ANY BREACH OF FIDUCIARY DUTY OTHER THAN THE DUTY OF LOYALTY.

A. Question Presented

Did the Court of Chancery correctly hold that SEPTA failed to state a proper purpose to investigate any breach of fiduciary duty other than the duty of loyalty in order to bring a derivative action, when any other alleged wrongdoing was exculpated by AbbVie's Certificate of Incorporation? (A182–84)

B. Scope Of Review

"This Court reviews *de novo* whether or not a party's stated purpose for seeking inspection . . . is a 'proper purpose.'" *City of Westland Police & Fire Ret. Sys. v. Axcelis Techs., Inc.*, 1 A.3d 281, 287 (Del. 2010).

C. Merits Of The Argument

A "mere statement" of a purpose to investigate possible corporate wrongdoing does not entitle a shareholder to Section 220 inspection relief. *Axcelis Techs., Inc.*, 1 A.3d at 287. The Court of Chancery has repeatedly held that "a stockholder 'must do more than state, in a conclusory manner, a generally acceptable proper purpose'—the investigation of corporate mismanagement 'must be to some end.'" *Graulich v. Dell Inc.*, 2011 WL 1843813, at *5 (Del. Ch. May 16, 2011) (quoting *W. Coast Mgmt. & Capital, LLC v. Carrier Access Corp.*, 914 A.2d 636, 646 (Del. Ch. 2006)); *see also Beiser v. PMC-Sierra, Inc.*, 2009 WL

483321, at *3 (Del. Ch. Feb. 26, 2009) (in addition to stating a proper purpose, a plaintiff "must state a reason for the purpose, *i.e.*, what it will do with the information, or an end to which that investigation may lead").

Where the stated end of a Section 220 inspection is to bring a shareholder derivative claim, the Court of Chancery has repeatedly held that the claim must be one for which the shareholder has a remedy—otherwise, the shareholder does not have a proper purpose for the inspection. *See, e.g.*, *La. Mun. Police Emps.' Ret. Sys. v. Lennar Corp.*, 2012 WL 4760881, at *2 (Del. Ch. Oct. 5, 2012) ("[I]f a stockholder seeks to use Section 220 to investigate corporate wrongdoing for which there is no remedy . . . then that stockholder has not stated a proper purpose."); *Graulich*, 2011 WL 1843813, at *6 (holding that a stockholder's effort to establish a proper purpose is "eviscerate[d]" when the stockholder has articulated no purpose other than to investigate wrongdoing for which there would be no remedy).

Here, the Court of Chancery concluded—and SEPTA does not dispute—that "future derivative litigation" was "the sole motivation for the Plaintiffs' investigations into corporate wrongdoing among AbbVie's directors and officers." (Pl. Ex. A at 30) Accordingly, consistent with prior precedent, the Court of Chancery held that whether SEPTA had stated a proper purpose depended on that purpose being to investigate a breach of fiduciary duty for which SEPTA had an available remedy. (Pl. Ex. A at 32–33) SEPTA, however, has no potential derivative claim against AbbVie's directors for breach of the duty of care, due to the Section 102(b)(7) exculpatory clause in AbbVie's Certificate of Incorporation. (B5) That clause bars stockholders from recovering damages in a derivative suit against the corporation's directors for a breach of fiduciary duty other than breach of the duty of loyalty.[3] *See* 8 Del. C. § 102(b)(7); *Stone v. Ritter*, 911 A.2d 362, 369–70 (Del. 2006). Thus, the Court of Chancery properly held SEPTA did not state a "proper purpose" to investigate any breach of fiduciary duty other than the duty of loyalty.[4] (Pl. Ex. A at 33)

Both the Court of Chancery's and this Court's "proper purpose" precedent refute SEPTA's assertion that the Court of Chancery created a new rule that improperly limits stockholders' ability to use Section 220 for a proper purpose.

First, the Court of Chancery did not create a "new rule." Rather, it applied a principle articulated in prior Court of Chancery decisions to the particular context of this claim. SEPTA points to the Court of Chancery's statement that the court previously "has not squarely addressed the issue of whether, when a stockholder

[3] While Section 102(b)(7) does not preclude claims for injunctive relief based on breaches of the duty of care, SEPTA has never suggested it sought to pursue injunctive relief. Nor could it. This case arises out of a failed transaction, and there is nothing for a court to enjoin.

[4] The Court of Chancery found that SEPTA's other stated purpose, investigating demand futility, was moot, noting that SEPTA admitted at trial that "investigating demand futility is a proper purpose only if the plaintiff has established a credible basis to investigate corporate wrongdoing that ultimately could form the basis of a derivative suit." (Pl. Ex. A. at 27 n.92)

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 wrongdoing." (Pl. Br. 16 (quoting Pl. Ex. A at 31)) But the Court of Chancery went on to find that "analogous decisions interpreting Section 220 support the conclusion that such a limitation should exist." (Pl. Ex. A at 31) For example, the Court of Chancery has denied Section 220 requests to investigate potential wrongdoing when a future derivative action would be time-barred. *Wolst v. Monster Beverage Corp.*, 2014 WL 4966139, at *2 (Del. Ch. Oct. 3, 2014); *Graulich*, 2011 WL 1843813, at *6. Similarly, the Court of Chancery has held that a plaintiff did not state a proper purpose to inspect records to pursue derivative claims barred by issue preclusion. *W. Coast Mgmt.*, 914 A.2d at 646–47.

Like alleged wrongdoing that is time-barred or barred by issue preclusion, alleged wrongdoing that is exculpated is "wrongdoing for which there is no remedy" where (as here) the plaintiff's stated intention is to bring a derivative action. *Lennar Corp.*, 2012 WL 4760881, at *2. Like the plaintiffs in *Wolst*, *Graulich*, and *West Coast Management*, who had not stated a proper purpose because they sought to investigate alleged wrongdoing that was not actionable, SEPTA did not state a proper purpose insofar as it sought to investigate exculpated breaches of fiduciary duty. The Court of Chancery properly applied the same principle as numerous Court of Chancery decisions when it held that SEPTA did not state a "proper purpose" to investigate any breach of fiduciary duty other than the duty of loyalty for the purpose of bringing a shareholder derivative action.

Second, the Court of Chancery's ruling is fully consistent with this Court's decisions applying the "proper purpose" requirement. The holding is in keeping with the rule that "a mere statement of a purpose to investigate possible general mismanagement, *without more*, will not entitle a shareholder to broad § 220 inspection relief." *Axcelis Techs., Inc.*, 1 A.3d at 287 (emphasis in original)*; see also Seinfeld v. Verizon Commc'ns, Inc.,* 909 A.2d 117, 122–23 (Del. 2006) (noting that Seinfeld's disagreement with the business judgment of Verizon's board of directors did not constitute a proper purpose for inspection under section 220). SEPTA is therefore incorrect when it asserts that a desire to investigate *any* alleged wrongdoing or mismanagement is a proper purpose under Section 220. (Pl. Br. 16) Here, the Court of Chancery properly considered both the specific end for which SEPTA sought inspection and AbbVie's Section 102(b)(7) exculpatory clause in determining whether SEPTA stated a proper purpose.

SEPTA also asserts that the Court of Chancery's holding alters "proper purpose" doctrine because it "limits a stockholder to investigating potential loyalty breaches or illegal conduct by fiduciaries of companies with a Section 102(b)(7) provision." (Pl. Br. 16) Yet this "limitation" applies only where, as here, a stockholder's stated purpose is to investigate a possible breach of duty for which it would have no remedy. (*See* Pl. Ex. A at 29–30) As this Court stated in *Seinfeld*, the rationale for Section 220 investigation of potential director wrongdoing is that "where the allegations of mismanagement prove meritorious, investigation furthers the interest of all stockholders and should increase stockholder return." 909 A. 2d at 121. Investigation of exculpated conduct for the sole purpose of bringing a potential derivative action would not further the interests of stockholders and increase stockholder returns; it would only do the opposite by imposing needless costs on the corporation.[5]

For these reasons, the Court of Chancery's holding that SEPTA did not state a proper purpose for investigating any alleged breach of fiduciary duty other than the duty of loyalty is a correct statement of Delaware law and should be affirmed.

[5] The Court of Chancery's decision is also fully consistent with *Grimes v. Donald*, 673 A.2d 1207 (Del. 1996), in which this Court urged stockholders to utilize Section 220 before filing derivative suits. Nothing in *Grimes* suggests that investigating a potential derivative claim for an exculpated breach of fiduciary duty is a proper purpose. *See Seinfeld*, 909 A.2d at 122 (noting that *Grimes* did not suggest its reference to using the "tools at hand" modified the need for a stockholder to show a proper purpose).

II. THE COURT OF CHANCERY PROPERLY RULED THAT SEPTA DID NOT STATE A CREDIBLE BASIS FOR INVESTIGATING A POSSIBLE BREACH OF FIDUCIARY DUTY OR OTHER WRONGDOING BY ABBVIE'S DIRECTORS.

A. Question Presented

Did the Court of Chancery properly conclude that SEPTA failed to establish a credible basis to infer any breach of fiduciary duty or other wrongdoing by AbbVie's directors? (A181–203)

B. Scope Of Review

"A trial judge's determination that a credible basis does (or does not) exist to infer managerial wrongdoing is a mixed finding of fact and law that is entitled to considerable deference." *Axcelis Techs.*, 1 A.3d at 287. "[F]actual findings are entitled to a high level of deference." *United Techs. Corp. v. Treppel*, 109 A.3d 553, 557 (Del. 2014) (citation omitted).

C. Merits Of The Argument

Where the stated purpose of a Section 220 demand is to investigate possible breaches of fiduciary duty or waste, plaintiffs have the burden of showing, "by a preponderance of the evidence," a credible basis from which the Court of Chancery can reasonably infer such wrongdoing may have occurred. *Seinfeld*, 909 A.2d at 122–23 ("There must be some evidence of possible mismanagement as would warrant further investigation of the matter"); *Thomas & Betts Corp. v. Leviton Mfg. Co.*, 681 A.2d 1026, 1031 (Del. 1996). Although the burden of proof for credible basis is low, it "is not insubstantial." *Seinfeld*, 909 A.2d at 122, 123, 125 (affirming denial of Section 220 inspection); *Axcelis Techs.*, 1 A.3d at 287 (same).[6] As the Court of Chancery held after considering the record before it: "[n]otwithstanding this low standard . . . [SEPTA] failed to meet it here," because SEPTA showed "only that the directors took a risky decision that failed at substantial cost to the stockholders. Evaluating risk is the *raison d'être* of a corporate director." (Pl. Ex. A at 2)

The Court of Chancery correctly ruled that SEPTA failed to establish a credible basis to investigate wrongdoing by AbbVie's directors. SEPTA submitted no evidence supporting a credible basis to infer that the AbbVie board's decisions regarding the proposed Shire transaction were anything other than informed business judgments the directors believed to be in AbbVie's best interest. SEPTA provided no credible basis to infer that AbbVie's directors breached their duty of loyalty, acted in bad faith, or committed waste. And even if AbbVie's exculpatory

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6 SEPTA attempts to conflate the credible basis and proper purpose requirements, claiming that the Court of Chancery's credible basis analysis was "effectively heighten[ed]" by a "newly articulated" proper purpose requirement. (Pl. Br. 21, 26, 32–33) As explained above in Section I, the Court of Chancery did *not* articulate a new version of the proper purpose requirement. Nor did the Court conflate the credible basis and proper purpose requirements. Rather, after addressing whether SEPTA had stated a proper purpose to investigate potential wrongdoing, the Court of Chancery separately evaluated whether SEPTA had met its burden to submit evidence to establish a credible basis for an inference such wrongdoing occurred. (Pl. Ex. A at 34)

provision did not preclude SEPTA from investigating a breach of the duty of care, SEPTA provided no evidentiary basis to infer any breach of that duty either.

1. SEPTA Offered No Evidence To Support A Credible Basis To Believe That AbbVie's Directors May Have Breached Their Duty Of Loyalty Or Acted In Bad Faith.

In a transactional context like this, "an extreme set of facts" is required to support a claim of disloyalty premised on the directors intentionally disregarding their duties. *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 243 (Del. 2009). To establish a credible basis for a breach of the duty of loyalty, SEPTA was required to show some evidence to support a reasonable inference of "not only an intent to harm but also intentional dereliction of duty" and "conscious disregard for . . . responsibilities" amounting to bad faith. *Id.* at 240.

SEPTA's brief cites no evidence establishing a credible basis to suspect that AbbVie's directors consciously or intentionally acted in disregard of their fiduciary duties to AbbVie. SEPTA challenges both the board's decision to agree to the terms of the transaction and the board's change of recommendation and termination of the transaction after the tax benefits of the deal were eliminated. (Pl. Br. 27–28) But SEPTA does not identify any facts in the record providing a credible basis to reasonably infer that in making these decisions the AbbVie board consciously failed to act on an informed basis or otherwise acted in bad faith.

Quite the opposite, the undisputed record upon which the Court of Chancery relied showed that AbbVie's directors carefully evaluated the proposed Shire transaction over the course of seven board meetings and were assisted throughout the process by a team of legal, tax, and financial experts. (A564–68; Pl. Ex. A at 38–39) After the September Treasury Notice, informed by a thorough review of the effects of the Notice by the executive management team and its expert advisors, the board determined that completing the transaction at the agreed price was no longer in the best interest of AbbVie's shareholders. (A479) There is no plausible basis to suggest the board made either decision in bad faith.

Contrary to SEPTA's argument, the Court of Chancery did not conclude that the board failed to take into account the loss of the tax benefit on the deal's viability, nor did it "arbitrarily" conclude that such a failure was "mere negligence." (*See* Pl. Br. 26, 28) Rather, the court rejected SEPTA's argument that "the Company's failure to identify the tax benefit as a 'deal breaker' in the preliminary proxy statement indicates that the Company ignored or was not cognizant of the repercussions of the tax benefit on the deal as a whole." (Pl. Ex. A at 39 n.122) Stating that it did not find SEPTA's argument persuasive, the court concluded that "*the most*" it could reasonably infer from the factual record before it was that the directors' actions were negligent, and that even if this were true, it would "fail[] to prove a credible basis to demonstrate a breach of care, let alone loyalty." (*Id.*) As in *Axcelis*, SEPTA's disagreement with the inferences the Court of Chancery drew from the undisputed facts is insufficient to challenge the court's conclusions. 1 A.3d at 288 ("Essentially, Westland disagrees with the Vice Chancellor's inferences from the undisputed facts. Westland's disagreement, without any further affirmative showing, is insufficient.").

Finally, SEPTA argues that "[t]he Board's failure . . . may just as conceivably constitute a breach of the duty of loyalty" and that an inspection of AbbVie's books and records might turn up evidence that could "conceivably constitute a breach of loyalty." (Pl. Br. 26) This argument relies on the "mere suspicion" standard this Court has repeatedly rejected. *See Seinfeld*, 909 A.2d at 123 & n.41 (collecting cases). The mere hope that an investigation "may reveal" some actionable misconduct is not sufficient to establish a proper purpose. Indeed, that is precisely the kind of fishing expedition this Court has held to be inappropriate under Section 220. *See Sec. First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 568 (Del. 1997) (stating that to demonstrate a proper purpose, "[m]ere curiosity or a desire for a fishing expedition will not suffice"). Rather, a shareholder invoking Section 220 must establish a credible basis to believe wrongdoing has occurred *before* it is entitled to inspection.

Ultimately, SEPTA's argument amounts to nothing more than subjective disagreements with the board's business decisions. But such disagreements do not establish a credible basis for wrongdoing sufficient to support a Section 220 demand. *See Seinfeld*, 909 A.2d at 120 (affirming conclusion that disagreement with business judgment of defendant's board "is not evidence of wrongdoing"); *Axcelis Techs.*, 1 A.3d at 287 (affirming decision that plaintiff failed to establish a credible basis to infer wrongdoing "because the record provides no credible basis to infer that the board's [actions] were other than good faith business decisions"). The Court of Chancery carefully reviewed the stipulated factual record and concluded that SEPTA's disagreements are not evidence of bad faith or a breach of the duty of loyalty sufficient to support its Section 220 demand. This conclusion, which is entitled to considerable deference, is fully consistent with this Court's jurisprudence denying Section 220 demands based on similar arguments.

2. SEPTA Provided No Evidence To Support A Credible Basis To Believe AbbVie's Directors Breached The Duty Of Care.

Even if investigating a breach of the duty of care were a proper purpose here, which it is not, SEPTA provides no evidence to infer that AbbVie's directors breached their duty of care.[7] Directors are presumed to have "acted on an informed basis." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984). To deprive a

[7] AbbVie fully briefed this issue in the Court of Chancery. (A190–202) Although its decision was based principally on SEPTA's failure to establish a credible basis for a possible breach of the duty of loyalty, the Court of Chancery did address, albeit briefly, SEPTA's failure to show a credible basis for breach of the duty of care. (Pl. Ex. A at 39 n.122) In any event, "this 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 by that court." *Cent. Laborers Pension Fund v. News Corp.*, 45 A.3d 139, 141 (Del. 2012).

board's decision of the protection of the business judgment rule, a plaintiff must prove the directors acted so far without information that they can be said to have passed an "unintelligent and unadvised judgment." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985) (citation omitted). That is, their conduct must rise to the level of gross negligence. *E.g.*, *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 66 (Del. 1989). SEPTA failed to present any evidence establishing a credible basis to infer a breach of the duty of care.

- **Entering Into The Shire Agreement And Evaluating Tax Risks.**

SEPTA suggests, with no evidentiary support, that AbbVie's directors breached their duty of care by approving the Shire transaction without proper evaluation, claiming that "the Board made no effort to form an opinion whether the Transaction was still in the best interest of the stockholders if the tax benefits were eliminated." (Pl. Br. 27) SEPTA does not dispute that the proposed transaction would have resulted in significant synergies, or that Shire was a desirable target. Nor does it contend that the bundle of expected benefits, including tax benefits, failed to justify the agreed-upon price. Rather, SEPTA takes issue with the board's failure to predict and evaluate in advance the impact of broad, novel, and unexpected actions by Treasury after AbbVie and Shire entered the Co-operation Agreement. (Pl. Br. 27–28)

As disclosed in the preliminary Form S-4, AbbVie's board met many times regarding the Shire transaction, received detailed advice from management and advisors, and thoroughly considered the risk of adverse changes to tax laws. (A536, A546–47, A564–68) Armed with knowledge of the risks, but with no ability to predict how or whether those risks might materialize, the AbbVie board made an informed, deliberate decision to move forward with the transaction. (Pl. Ex. A at 43 ("AbbVie's directors were aware of the risk that the government would act to eliminate the tax benefits of inversions," but took a chance "that the risk would not come to pass."))

As the Court of Chancery recognized, the fact that a risk the board assessed and decided to take materialized does not support an inference that the directors breached their fiduciary duties. (Pl. Ex. A at 38–39, 43) *See In re Citigroup, Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 131 (Del. Ch. 2009) (noting that directors' oversight duties are not designed to hold directors liable "for failure to predict the future and to properly evaluate business risk"). Indeed, that is the very essence of the business judgment rule: to protect directors who take good faith business risks. (Pl. Ex. A at 2) *See In re Lear Corp. S'holder Litig.*, 967 A.2d 640, 651 (Del. Ch. 2008). SEPTA's counsel conceded at trial that "taking on business risk is a matter within the board's judgment" (A18) and "misapprehension of risk alone is not actionable conduct." (Pl. Ex. A at 39 n.122)

SEPTA argues that AbbVie's board should have assessed the value of the transaction on the assumption there would be no tax benefits and that a failure to do so could "conceivably constitute a breach of loyalty." (*See* Pl. Br. 26) In making this argument, SEPTA ignores the undisputed facts of record. AbbVie planned to close the Shire deal in the fourth quarter of 2014. (A306) Analysts, however, were reporting that "the earliest [tax reform] could likely happen is 2015." (B9) As the Court of Chancery found, "the record illustrates that through the date AbbVie executed the Co-Operation Agreement, the opinion of a number of commentators, analysts, and even government officials themselves was that the legislative branch would not, and the administrative branch could not, act to deter inversion in the short term." (Pl. Ex. A at 38 n.121) Additionally, the consensus view was that any legislation, if eventually passed, ***"would not be retroactive,"*** and thus would not have an effect on the value of the by-then-closed Shire deal. (B9)

Thus, the Court of Chancery properly found that SEPTA did not establish a credible basis to infer that the AbbVie board's decision to move forward with the Shire deal was anything but a reasonably calculated, informed determination entrusted to the business judgment of the board. *See Axcelis Techs.*, 1 A.3d at 287.

- **Lack Of A Cost-Free Fiduciary Out Clause.**

SEPTA also argues that the absence of a cost-free "fiduciary out" provision is a credible basis for suspecting that the directors breached their duty of care. (Pl.

Br. 27–28) Judicial scrutiny of board action—particularly contract terms—is not a hindsight-driven evaluation of whether the board's decision was a good one; rather, "what matters is whether the board acted reasonably based on the circumstances then facing it." *In re Toys "R" Us, Inc. S'holder Litig*., 877 A.2d 975, 1016 (Del. Ch. 2005).

Here, SEPTA offered no evidence at trial, and points to no evidence on appeal, permitting an inference that AbbVie had bargaining leverage to negotiate the ancillary terms of the deal, and the record suggests just the opposite. As the Court of Chancery found, negotiations with Shire were quasi-hostile, requiring AbbVie to increase its proposal multiple times before Shire would even engage in discussions. (Pl. Ex. A at 39) Nor did SEPTA offer any evidence that AbbVie failed to seek a cost-free termination provision, or that it would have been possible to obtain one given Shire's resistance to entering into a deal. In short, there was no basis to support an inference that the board did not exercise valid business judgment in deciding to enter into an agreement with a 3% termination fee that did not include a free "out" for adverse tax action by the government. SEPTA's second-guessing of the merits of the board's decision is "precisely the kind of inquiry that the business judgment rule prohibits." *See In re Dow Chem. Co. Deriv. Litig.*, 2010 WL 66769, at *9 (Del. Ch. Jan. 11, 2010) (dismissing fiduciary duty claims where a board approved a deal without a financing "out" rather than risking that its merger partner "would walk away").

- **Statements By AbbVie And CEO About The Agreement.**

SEPTA makes the conclusory assertion that statements by AbbVie and its CEO about the tax benefits of the proposed transaction "downplayed the import of the tax benefits for the Transaction." (Pl. Br. 27) However, SEPTA does not explain how any of these statements was false or violated a fiduciary duty.

AbbVie repeatedly made clear in its public statements before and after signing the Co-operation Agreement with Shire that it was pursuing the transaction for a number of strategic and financial reasons, including Shire's complementary product platform and specialty focus, enhanced research and development potential, strong access to European markets, a lower tax rate, and the ability to use funds outside the U.S. in a tax efficient manner. (A504, 516) AbbVie said it was not pursuing the transaction *solely* for the tax benefits—an assertion SEPTA did not challenge—*not* that tax benefits were nonexistent or unimportant. AbbVie's statements about the legitimate strategic and financial impact of the transaction do not establish any credible basis to infer wrongdoing.

- **Change Of Recommendation And Termination Of Transaction.**

SEPTA also claims it is entitled to examine AbbVie's books and records to determine if the analysis performed by management after the Treasury Notice supports the board's decision to change its recommendation or "was a pretext."

(Pl. Br. 29) SEPTA offered no evidence at trial, and cites none in its brief, that raises this theory above pure speculation. Nor does SEPTA explain what the decision could have been a pretext for. There is no basis to believe that the board's decision to abandon the transaction was anything other than an informed business judgment that the transaction was no longer in the shareholders' interest based on subsequent developments. As the Court of Chancery recognized: "there was a material change in circumstances following AbbVie entering into the Co-Operation Agreement—the loss of the tax benefits attending the Treasure notice—that led the Company's board to terminate the Proposed Inversion." (Pl. Ex. A at 42)[8]

SEPTA does not dispute that the new Treasury rules eliminated certain financial benefits of the Shire transaction and introduced a new level of uncertainty. (A495) AbbVie and a team of experts spent nearly a month analyzing the proposed transaction in light of the new rules and attempting to find a viable path to complete the transaction. AbbVie's management ultimately concluded, however, that pursuing the deal at the agreed price was no longer in the best interest of AbbVie and its shareholders. (*Id.*) AbbVie's board agreed and determined, in the exercise of its business judgment, that AbbVie should no longer

[8] The Court of Chancery has repeatedly held that when conditions relating to a proposed transaction materially change, directors have a fiduciary duty to reconsider their recommendation to approve the transaction. *In re Primedia, Inc. S'holders Litig.*, 67 A.3d 455, 491 (Del. Ch. 2013); *Frontier Oil Corp. v. Holly Corp.*, 2005 WL 1039027, at *28 (Del. Ch. Apr. 29, 2005). That is precisely what the AbbVie directors did here.

pursue the proposed transaction. This is a classic example of a decision protected by the business judgment rule. *Aronson*, 473 A.2d at 812. As the Court of Chancery recognized, SEPTA did not identify any facts suggesting that the presumption of the business judgment rule would not apply to this decision. (*See* Pl. Ex. A at 2)

In sum, the Court of Chancery properly found that SEPTA failed to show a credible basis to infer any possible breach of the AbbVie board's fiduciary duties.

3. SEPTA Provided No Evidence To Support A Credible Basis For A Claim Of Waste.

The Court of Chancery properly found that SEPTA provided no credible basis to infer that AbbVie's decisions to agree to the termination fee, and later to terminate the Co-operation Agreement and pay the fee, constituted waste. (Pl. Br. 29–30) "[W]aste entails an exchange of corporate assets for consideration so disproportionately small as to lie beyond the range at which any reasonable person might be willing to trade. . . . Such a transfer is in effect a gift." *Brehm v. Eisner*, 746 A.2d 244, 263 (Del. 2000). "[A] claim of waste will arise only in the rare 'unconscionable case where directors irrationally squander or give away corporate assets,'" and "the board's decision will be upheld unless it cannot be 'attributed to any rational business purpose.'" *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 74 (Del. 2006) (quoting *Brehm*, 746 A.2d at 263).

SEPTA attempts to obscure this standard, arguing that the Court of Chancery's ruling improperly "required SEPTA to demonstrate that the AbbVie directors and officers in fact engaged in waste." (Pl. Br. 29) Not so. The Court of Chancery merely required SEPTA to point to some evidence establishing a credible basis from which it could infer that AbbVie may have engaged in waste. It properly refused to evaluate in hindsight the board's decisions with regard to the break fee "under the guise of the waste standard." (Pl. Ex. A at 40)

SEPTA identified no evidence at trial, and cites none on appeal, supporting a plausible inference that it might be able to satisfy the "onerous standard for waste." *Disney*, 906 A.2d at 74. Rather, "the record suggests that the $1.635 billion Break Fee was an actively negotiated provision by a reluctant merger target." (Pl. Ex. A at 39)[9] Representatives of the two companies negotiated terms including "whether a break fee or other compensation payment would apply if the [Transaction] were not to be completed under various scenarios (*including the AbbVie Board changing its recommendation* or the AbbVie shareholders failing to approve the [Transaction])." (A568; Pl. Ex. A at 8–9 (emphasis added))

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9 On appeal, SEPTA asserts for the first time 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." (Pl. Br. 30) SEPTA does not cite the record for this assertion and, indeed, never presented such evidence. Based on the record evidence, the Cost Reimbursement Payment was required by Shire to protect it in the event AbbVie's shareholders voted not to approve the transaction for any reason. (A568; A790) The Break Fee was required by Shire to protect it against AbbVie's board withdrawing its recommendation, which is exactly what happened here. (A568; *see* A479)

SEPTA presented no evidence that the $1.635 billion Break Fee was an attempt by AbbVie's directors to "give away corporate assets." *See Brehm*, 746 A.2d at 265; *Disney*, 906 A.2d at 74. While the gross dollar amount of the fee was large, the Court of Chancery noted that "it was a commonplace 3% of total value of that target." (Pl. Ex. A at 39) The Court of Chancery properly found no credible basis to infer that the board's decisions to agree to the break fee, and later to pay it when contractually required, constituted an irrational squandering of corporate assets. *See Disney*, 906 A.2d at 74.

* * *

With "considerable deference" due to the Court of Chancery's decision that SEPTA did not establish a credible basis to reasonably infer a breach of fiduciary duty or waste by AbbVie's directors, this Court should uphold its ruling.

III. THE COURT OF CHANCERY PROPERLY RULED THAT SEPTA DID NOT STATE A CREDIBLE BASIS TO INFER WRONGDOING BY ABBVIE'S OFFICERS.

A. Question Presented

Did the Court of Chancery properly conclude that SEPTA failed to establish a credible basis to infer any breach of fiduciary duty or other wrongdoing by AbbVie's officers?[10]

B. Scope Of Review

"A trial judge's determination that a credible basis does (or does not) exist to infer managerial wrongdoing is a mixed finding of fact and law that is entitled to considerable deference." *Axcelis Techs.*, 1 A.3d at 287. "[F]actual findings are entitled to a high level of deference." *Treppel*, 109 A.3d at 557 (citation omitted).

C. Merits Of The Argument

The Court of Chancery properly found that SEPTA failed to establish a credible basis that AbbVie's officers engaged in corporate wrongdoing. Although SEPTA now attempts to argue that senior management's "significant role" in the transaction "provide[s] a credible basis to infer that just as the directors, the officers may have engaged in mismanagement and wrongdoing" (Pl. Br. 31–32), SEPTA submitted no evidence at trial to support this claim. Rather, the Complaint referred to AbbVie's officers "in name only," an afterthought to allegations against

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10 As SEPTA did not raise this issue in the trial court, AbbVie did not address the issue in its trial court filings.

the directors. (*See* Pl. Ex. A at 33 n.108) Contrary to SEPTA's assertion that the Court of Chancery "required SEPTA to articulate specific wrongdoing by specific AbbVie officers in order to demonstrate a credible basis to infer wrongdoing by AbbVie's officers" (Pl. Br. 32), the Court of Chancery noted that SEPTA had made *no* concrete allegations against *any* of AbbVie's officers except Gonzalez, who was also a director. (Pl. Ex. A at 33–34 n.108) The court properly concluded that SEPTA's generalized and conclusory allegations against AbbVie's officers, unsupported by any evidence at trial, were insufficient.

Because SEPTA raised no substantial claims against the officers at trial, they are barred from attempting to do so on appeal. *See Disney*, 906 A.2d at 48 (citing Del. Supr. Ct. R. 8) ("Only questions fairly presented to the trial court are properly before this Court for review."). Even if this Court assumes that all of SEPTA's allegations against AbbVie's directors apply in equal force to AbbVie's officers, however, SEPTA's arguments fail for the same reasons explained above in Section II.C. Although AbbVie's exculpatory clause would not apply to officers, SEPTA did not establish a credible basis that AbbVie's directors or officers breached their duty of care, much less committed a breach of loyalty or corporate waste. This Court should accord the considerable deference due to the Court of Chancery's decision and affirm its ruling.

CONCLUSION

The Court of Chancery's rulings were well-founded based on the relevant evidence presented at trial and established law. Those rulings should be affirmed.

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Dated: July 29, 2015