

Alert 10-195

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Delaware Supreme Court Rejects Investor's Books and Records Access Appeal – ***City of Westland Police & Fire Retirement Sys. v. Axcelis Tech., Inc.***

On August 11, 2010, the Delaware Supreme Court, in *City of Westland Police & Fire Retirement Sys. v. Axcelis Tech., Inc.*, Del., No. 594, 2009, affirmed the Delaware Court of Chancery's dismissal of a stockholder's lawsuit brought under 8 *Del. C.* § 220 to compel Axcelis Technologies, Inc. ("Axcelis") to provide access to its books and records to a plaintiff-stockholder after Axcelis' board rejected a \$630 million merger offer from Sumitomo Heavy Industries, Ltd. ("SHI").

The SHI Merger Offer. In 1983, Axcelis and SHI entered into a joint venture relationship, pursuant to which the joint venture would develop, manufacture and sell semiconductor equipment and would license technology from Axcelis. In February 2008, SHI offered to acquire Axcelis for \$5.20 per share (a premium of nearly \$1.00 over the prior closing price). The Axcelis board rejected SHI's proposal and concluded that the SHI bid did not reflect Axcelis' true worth.

In March 2008, SHI raised its bid to \$6 per share. The Axcelis board again rejected this premium bid and concluded that a transaction with SHI would not be in the stockholders' best interests and that there would need to be a confidential exchange of information for serious negotiations to occur.

In May 2008, Axcelis held its annual stockholders' meeting at which the terms for three directors were expiring. Although the three directors ran unopposed for reelection, they all received less than a majority of the votes in their reelection bids. Axcelis employs plurality voting under Delaware law; accordingly, a director may be elected without receiving a majority of the votes cast.

The Axcelis board, however, also adopted a plurality plus governance policy, pursuant to which directors who do not receive a majority of the stockholder vote must submit their resignations to the board's nominating and corporate governance committee, who must then consider and recommend to the board whether such resignations should be accepted or rejected. The plurality plus governance policy was triggered by the May 2008 election results, and the three directors submitted their resignations. However, the board decided not to accept their resignations citing as a reason the knowledge and experience of the three directors, as well as their importance in furthering negotiations with SHI.

In June 2008, Axcelis and SHI entered into a confidentiality agreement and SHI gained access to additional Axcelis information. SHI then put further acquisition discussions on hold and ultimately did not make a revised offer for Axcelis. After Axcelis publicly announced this development, Axcelis stock price had dropped to \$1.43 per share.

The Demand For Inspection. In December 2008, City of Westland Police & Fire Retirement System ("Westland") sent a demand letter to Axcelis pursuant to 8 *Del. C.* § 220 seeking, among other things, documents relating to the negotiations with SHI. 8 *Del. C.* § 220(b) provides, in relevant part, as follows: "Any stockholder . . . shall, upon written demand under oath stating the purpose thereof, have the right . . . to inspect for any proper purpose, and to make copies and extracts from . . . [t]he corporation's stock ledger, a list of its stockholders, and its other books and records . . ." 8 *Del. C.* § 220(c) then provides, in relevant part, as follows: "If the corporation . . . refuses to permit an inspection sought by a stockholder . . . or does not reply to the demand within 5 business days after the demand has been made, the stockholder may apply to the Court of Chancery for an order to compel such inspection."

Axcelis rejected the demand for inspection on the basis that Westland had failed to satisfy the standards of 8 *Del. C.* § 220 and Delaware case law.

Westland filed suit. The Court of Chancery dismissed Westland's complaint and held that Westland failed to prove a "proper purpose" for its request. Westland appealed to the Delaware Supreme Court.

The Appeal. Westland raised two issues on appeal.

First, Westland argued that the Court of Chancery misapplied the standard which requires a plaintiff seeking inspection of books and records to present some credible evidence of corporate wrongdoing in connection with books and records requests seeking such information. Westland argued that the Court of Chancery improperly required it to present affirmative evidence of wrongdoing. **The Court of Chancery held, and the Supreme Court affirmed, that Westland failed to establish a credible basis to infer wrongdoing. Specifically, these Delaware courts rejected Westland's cursory allegation that SHI's acquisition proposal was a threat to the Axcelis board and, as a result, there must have been some wrongdoing on the part of the Axcelis board.** The Supreme Court noted that although Westland disagreed with the inferences drawn by the Court of Chancery from the undisputed factual record, the record provided no credible basis to infer that the Axcelis board's rejections of SHI's proposals and refusal to extend the deadline for SHI to submit a revised bid were anything other than good faith business decisions.

Second, Westland argued that the Court of Chancery should adopt the *Blasius* standard when reviewing a board of directors' decision to reject director resignations when a plurality plus governance policy is triggered resulting in the mandatory tender of resignations. In *Blasius Indus. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988), the Court of Chancery held that a corporation's board is required to demonstrate a compelling justification for board-adopted measures which interfere with, or frustrate, a stockholder vote.

The Supreme Court rejected Westland's *Blasius* argument, in part because the burden remained on Westland to establish a proper purpose for a books and records demand. The Supreme Court clarified that the making of a books and records demand, or filing a books and records complaint, for purposes of investigating the suitability of directors whose tendered resignations were rejected, will not automatically entitle the plaintiff-stockholder to relief.

However, if enough stockholders withheld their votes to trigger the plurality plus governance policy, this alone may satisfy the requirement that a stockholder must establish a credible basis to infer that the director is unsuitable. **Nevertheless, the stockholder-plaintiff must still make the additional showing that the information sought by the stockholder is necessary and essential to assessing whether a director is unsuitable to stand for reelection.** Also, access to board documents may be limited or restricted by the need to protect confidential board communications. As explained by the Supreme Court, this strikes the appropriate balance between a stockholder's entitlement to information and the directors' entitlement to make decision in the corporation's best interests free from abusive litigation.

Conclusion. The business judgment rule is alive and well in Delaware. The mere fact that a board rejected an acquisition proposal, absent some credible evidence of wrongdoing, will not automatically trigger a right to inspect. However, the failure to attain a plurality plus may establish a credible basis to infer that the subject director is unsuitable. Nevertheless, a stockholder must still make the additional showing that the information sought is necessary when assessing whether a director is unsuitable to stand for reelection. Furthermore, even if the corporation is required to produce some information to a stockholder, such information may be restricted to protect confidential material.

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