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Re: *Central Laborers Pension Fund v. News Corporation*
C.A. No. 6287-VCN
Date Submitted: August 11, 2011

Dear Counsel:

Plaintiff Central Laborers Pension Fund (“Central Laborers”) brought this action to inspect certain books and records of Defendant News Corporation (“News Corp.”) under 8 *Del. C.* § 220 (the “220 Action”). News Corp. had announced that it would acquire Shine Group Ltd. (the “Proposed Transaction”). Central Laborers, a News Corp. stockholder, set forth in a demand letter that its purposes for making demand to inspect those books and records were to investigate potential breaches of fiduciary duty in connection with the Proposed

Transaction and to determine whether making a demand on the News Corp. board was necessary before commencing a derivative action on behalf of News Corp. to challenge the Proposed Transaction.

Central Laborers, joined by another plaintiff, filed a derivative action against News Corp., as a nominal defendant, and News Corp.'s directors claiming that the Proposed Transaction is the outcome of an unfair process and at an unfair price (the "Derivative Action").¹ Shortly after filing the Derivative Action, Central Laborers commenced the 220 Action.

News Corp. has moved to dismiss the 220 Action under Court of Chancery Rule 12(b)(6) because the simultaneous filing of the Derivative Action refutes any claim of a proper purpose for its inspection demand.² As a general matter, by

¹ *Amalgamated Bank & Central Laborers Pension Fund v. News Corp.*, C.A. No. 6285-CC (Del. Ch.). This action was later consolidated with a related action; the current consolidated derivative action is styled *In re News Corp. S'holder Deriv. Litig.*, C.A. No. 6285-VCN (Del. Ch.).

² When considering a motion to dismiss under Court of Chancery Rule 12(b)(6), the Court "should accept all well-pleaded factual allegations in the Complaint as true, accept even vague allegations in the Complaint as 'well-pleaded' if they provide the defendant notice of the claim, draw all reasonable inferences in favor of the plaintiff, and deny the motion unless the plaintiff could not recover under any reasonably conceivable set of circumstances susceptible of proof." *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings LLC*, 27 A.3d 531, 536 (Del. 2011). The facts are not in dispute, and, despite Central Laborers' argument that a hearing would be appropriate, it is difficult to discern any benefit from such an effort.

filing its derivative complaint, Central Laborers acknowledged—if, for no other reason than to satisfy its lawyers’ Rule 11 obligations—that it had sufficient information to support its substantive allegations and its allegations of demand futility that would excuse prior demand on the News Corp. board—both necessary to go down the path chosen by it to challenge the Proposed Transaction. In short, the stockholder plaintiff who files a Section 220 action immediately after its derivative action is acting inconsistently.³

At stake, however, is more than inconsistent pleading. This Court routinely stays discovery in derivative actions while non-frivolous motions to dismiss are resolved.⁴ Derivative actions impinge upon the ability of directors to manage the affairs of the corporation; they also impose substantial compliance costs on the

Under Section 220, in order to gain access to a corporation’s books and records, a stockholder must establish a proper purpose for the inspection, 8 *Del. C.* § 220(c), and a proper purpose is defined as “a purpose reasonably related to such person’s interest as a stockholder.” 8 *Del. C.* § 220(b).

³ See, e.g., *Baca v. Insight Enters., Inc.*, 2010 WL 2219715, at *4 (Del. Ch. June 3, 2010) (“[T]he stockholder who serves a post-plenary action Section 220 demand contradicts his own certification that he already possessed sufficient information to file a complaint.”).

⁴ See, e.g., *Brehm v. Eisner*, 746 A.2d 244, 266 (Del. 2000); Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* § 9.02[b][3], at 9-69 (2010) (“[T]he Court of Chancery should routinely grant a motion to stay discovery pending resolution of the defendant’s motion to dismiss the complaint for failure to make a demand under Court of Chancery Rule 23.1.”).

corporation. Section 220 was not adopted as a substitute for litigation discovery; instead, in this context, it serves to enable potential derivative plaintiffs to obtain the necessary information in advance of filing their derivative action.⁵ Although there may be special circumstances that would warrant the pursuit of a books and records action at the same time as the related derivative action,⁶ those circumstances do not exist here, and Central Laborers does not point out any unusual conditions that would support a deviation from the general rule.

Central Laborers, however, invokes a recent decision of the Delaware Supreme Court, *King v. Verifone Holdings, Inc.*,⁷ to support the filing of the 220 Action immediately after the filing of the Derivative Action. The Supreme Court held that a derivative plaintiff whose complaint had been dismissed for failure to plead demand futility successfully was not, on account of the mere fact

⁵ See, e.g., *King v. Verifone Holdings, Inc.*, 12 A.3d 1140, 1146-47 (Del. 2011) (“Delaware courts have strongly encouraged stockholder-plaintiffs to utilize Section 220 before filing a derivative action, in order to satisfy the heightened demand futility pleading requirements of Court of Chancery Rule 23.1. . . . By first prosecuting a Section 220 action to inspect books and records, the stockholder-plaintiff may be able to uncover particularized facts that would establish demand excusal in a subsequent derivative suit.”).

⁶ Cf. *Khanna v. Covad Commc’ns Grp., Inc.*, 2004 WL 187274, at *4 (Del. Ch. Jan. 23, 2004) (filing driven by time limitations).

⁷ 12 A.3d 1140 (Del. 2011).

that a derivative action had been filed, “legally precluded from prosecuting a later-filed Section 220 proceeding.”⁸ That case arose out of circumstances materially different from those associated with the 220 Action and the Derivative Action. The Derivative Action has not been dismissed; no judicial action has occurred that would suggest a need or a reason for further pleadings or efforts to gather important facts to support a cognizable purpose for an inspection of News Corp.’s books and records. It was, in *Verifone*, the judicial determination that the allegations were not sufficient coupled with the judicially-granted leave to amend that eliminated the inconsistency that one may find in the simultaneous filing of two related actions, as happened here.

Verifone cannot fairly be read as manifesting the Supreme Court’s approval of a stockholder’s simultaneous filing of both a derivative action and a Section 220 action. To the contrary, the Supreme Court clearly expressed its view that dismissal of a Section 220 action is proper when the “stockholder-plaintiffs plenary derivative complaint [is] still pending and the plenary court ha[s] not granted the

⁸ *Id.* at 1141.

plaintiff leave to amend.”⁹ In short, once the derivative action is filed, and until the judicial processing of the dismissal motion reaches the point where a recasting of the allegations has been authorized, the stockholder may not, as a general matter, demonstrate a proper purpose for invoking Section 220.

The Supreme Court summarized the substance of its holding:

The result we reach here affirms long-standing Delaware precedent which recognizes that it is a proper purpose under Section 220 to inspect books and records that would aid the plaintiff in pleading demand futility in a to-be-amended complaint in a plenary derivative action, where the earlier-filed plenary complaint was dismissed on demand futility-related grounds without prejudice and with leave to amend. That holding should not be read as an endorsement by this Court of proceeding in that way.¹⁰

Nothing in Central Laborers’ complaint brings it within the harbors mapped by the Supreme Court. Nothing in *Verifone* would authorize it to use the tools of Section 220 while actively pursuing a simultaneously-filed plenary derivative action at its early stages.¹¹

⁹ *Verifone*, 12 A.3d at 1148. See also *Beiser v. PMC-Sierra, Inc.*, 2009 WL 483321 (Del. Ch. Feb. 26, 2009).

¹⁰ *Verifone*, 12 A.3d at 1150.

¹¹ One of the concerns expressed by the Supreme Court in *Verifone* was this Court’s imposing restrictions that find no support in the text of Section 220. *Verifone*, 12 A.3d at 1151. In *Verifone*, the Supreme Court concluded that the opportunity given to the shareholder to amend

Because Central Laborers' currently-pending derivative action necessarily reflects its view that it had sufficient grounds for alleging both demand futility and its substantive claims without the need for the assistance afforded by Section 220, it is, at this time, unable to tender a proper purpose for pursuing its efforts to inspect the books and records of News Corp.¹² Accordingly, the 220 Action is dismissed.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-K

the complaint in the derivative action in the face of dismissal satisfied the statutory proper purpose standard. In contrast, it is the proper purpose standard that limits Central Laborers in the 220 Action. Until its implicit representation that it has sufficient facts for its pleadings in the Derivative Action is rejected (or, perhaps, seriously called into question) by the Court handling the Derivative Action, it simply cannot identify that proper purpose that is consistent with the statutory standard.

¹² With this conclusion, it is not necessary to address the additional grounds for dismissal posited by News Corp.