NO. 17-375

IN THE

Supreme Court of the United States

CHARLOTTE KOKOCINSKI, DERIVATIVELY ON BEHALF OF MEDTRONIC, INC., *Petitioner*,

v.

ARTHUR D. COLLINS, JR., ET AL., *Respondents*.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

REPLY BRIEF FOR PETITIONER

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Federal Cases

TABLE OF AUTHORITIES—Continued

Page(s)

State Cases

Rules

Other Authorities

INTRODUCTION

Respondents have a curious understanding of what constitutes a circuit split. Opp. 1. Respondents do not contest that, in reviewing a district-court order dismissing a shareholder derivative action based on a special litigation committee's recommendation, two circuits apply an abuse-of-discretion standard, and five a *de novo* standard. That is a mature, decades-old conflict requiring immediate resolution, regardless whether the courts on one side of the split have specifically rejected the reasoning of the other side. What matters is that litigation outcomes are diverging based solely on the circuit where a case is filed. Respondents implicitly concede that if this case was pending in the First, Second, Fifth, Sixth, or Ninth Circuits, the district-court decision would receive *de novo* rather than deferential review.

Alternatively, Respondents suggest this is a poor vehicle to resolve the split because the Eighth Circuit would have reached the same result even if it had applied a *de novo* standard. Opp. 2–3. But that is not what the Eighth Circuit said; with respect to both parts of its merits analysis, the Eighth Circuit ruled by stating that the district court had not abused its discretion. Pet. App. 14a, 20a. This Court assumes that there "is some practical difference in outcome depending upon which standard is used." *Dickinson* v. *Zurko*, 527 U.S. 150, 162 (1999). And under a *de novo* standard, it is hard to say the committee used adequate methodologies to determine that Kokocinski's claims were not worth pursuing when Medtronic entered into a $40 million whistleblower settlement and an $85 million class-action settlement for securities fraud based on some of the same conduct alleged here. Certiorari is warranted.

ARGUMENT

I. This case irrefutably involves a circuit split.

Regarding the first question presented, there is undeniably a split in circuit authority. Notably, Respondents concede that the Eighth Circuit held that an order dismissing a derivate action based on a special litigation committee's recommendation must "be reviewed for an abuse of discretion." Opp. 1. In so holding, the court relied on *Peller* v. *Southern Co.*, 911 F.2d 1532, 1536 (11th Cir. 1990). Pet. App. 6a–10a. *Peller* involved not only dismissal for failure to adequately plead demand futility, but *also* a motion to dismiss based on a special litigation committee's recommendation, where the Eleventh Circuit applied Rule 23.1 and reviewed under an abuse-of-discretion standard. 911 F.2d at 1539; *contra* Opp. 15.

Likewise, Respondents concede that the First, Fifth, Sixth, and Ninth Circuits have—since as early as 1981—applied a *de novo* standard of review in identical contexts. Opp. 14–15 (discussing *Sarnacki* v. *Golden*, 778 F.3d 217, 222 (1st Cir. 2015), *Bach* v. *Nat'l W. Life Ins. Co.*, 810 F.2d 509, 510 (5th Cir. 1987), *Booth Family Trust* v. *Jeffries*, 640 F.3d 134, 139 (6th Cir. 2011), and *Gaines* v. *Haughton*, 645 F.2d 761, 768 n.13 (9th Cir. 1981)). And while Respondents say the Second Circuit in *Halebian* v. *Berv*, 644 F.3d 122 (2d Cir. 2011), "did not comment on the standard of review" and did "not mention Rule 23.1," Opp. 15, the Second Circuit *did* reference the defendants' reliance on Rule 23.1 for the standard of review, 644 F.3d 125, and it *rejected* that argument, remanding with instructions for the district court to apply a summary-judgment (*de novo*) standard to the motion to dismiss. *Id.* at 132.

Analyzing these same cases, the Eighth Circuit rejected the majority approach and sided with the Eleventh Circuit. That is the definition of a circuit split. Wex Legal Dictionary, "Circuit Split" ("When two or more circuits in the United States court of appeals reach opposite interpretations of federal law.").[1] Yet, attempting to sidestep this Court's review, Respondents insist this is "not a 'split' at all." Opp. 1. Why? Because the Eighth Circuit's *reasoning* (reliance on Rule 23.1) was not expressly rejected by the circuits applying *de novo* review. *Id.* at 2, 13–23.

That argument is inaccurate, see *Halebian*, 644 F.3d at 125, 132, and irrelevant. The problem with a circuit split is not that one court directly criticizes another's reasoning. It is that litigants in identical cases experience different outcomes simply due to the geography where the suit is pending. And here, it cannot be disputed that if this case was pending in the First, Second, Fifth, Sixth, or Ninth Circuits, Kokocinski would have received the benefit of a *de novo* rather than deferential judicial review.

In any event, Respondents misapprehend the Eighth Circuit's ruling. In shoehorning the special litigation committee's motion into Rule 23.1(c)'s rubric of "settlement, voluntary dismissal, or compromise," Fed. R. Civ. P. 23(c), the Eighth Circuit cited the Ninth Circuit's contrary decision in *Gaines* and explicitly rejected the approach of treating the motion "as one for summary judgment brought under Rule 56." Pet. App. 43a. Again, that is a split.

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[1] https://www.law.cornell.edu/wex/circuit_split (last visited Nov. 27, 2017).

Respondents conclude by insisting that a deferential standard of review is superior to *de novo* review. Opp. 16–17. Respondents are wrong for the reasons stated in the petition. Pet. 18–21. Moreover, Respondents conflate the equitable aspect of a derivative action with the proper standard of review of a trial court's decision—in equity or at law—based on the same record before an appellate court. Opp. 18–19. Contrary to Respondents' citations to *Ross*, *eBay*, *Farmer*, and *Hecht*,[2] the mere fact that derivative standing is an equitable issue is not determinative of the proper standard of review of a decision regarding derivative standing. See, *e.g.*, *Dodge* v. *Knowles*, 114 U.S. 430, 434 (1885) (reviewing *de novo* "an appeal in equity"). Rather, as held in *Brehm* v. *Eisner*, Delaware's seminal decision on the standard of review for a trial court's decision on derivative standing, this equity issue must be reviewed *de novo* because "[t]he nature of [the appellate court's] analysis of a complaint in a derivative suit is the same as that applied by the Court of Chancery in making its decision in the first instance." 746 A.2d 244, 253 (Del. 2000).

More important, no matter which side has the better end of the split, the Court should grant the petition and resolve it. It is untenable that the conflict be allowed to percolate and grow, Opp. 21–22, given that the justice system is already producing divergent results for similarly-situated litigants.

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[2] *Ross* v. *Bernard*, 396 U.S. 531 (1970); *eBay Inc.* v. *MercExchange, L.L.C.*, 547 U.S. 388 (2006); *Farmer* v. *Brennan*, 511 U.S. 825 (1994); *Hecht* v. *Bowles*, 321 U.S. 321 (1944).

On this point, the Nevada Supreme Court's recent decision in *In re DISH Network Derivative Litigation*, 401 P.3d 1081 (Nev. 2017), highlights the need for granting certiorari. There, a divided court similarly affirmed a trial court's decision to adopt a special litigation committee's recommendation to dismiss a derivative action. *Id.* at 1085, 1094. Citing the Eighth Circuit's decision here, a majority of the Nevada justices—over a forceful dissent—applied an abuse-of-discretion standard of review. *Id.* at 1088 n.2. The justices did so even though the trial court treated the special litigation committee's motion as one for summary judgment and granted discovery regarding the committee's independence and the thoroughness of its investigation. *Id.* at 1087.

To justify their use of an abuse-of-discretion standard, the justices in the majority latched onto the fact that the trial court "assess[ed] the weight and credibility of the evidence." *Id.* at 1088 n.2. The same procedural choice by the trial court—*i.e.*, the summary-judgment nature of the trial court's dismissal order— caused the dissent to favor a *de novo* review, identifying the same circuit split advanced by Kokocinski here. *Id.* at 1096–97. The competing views amongst the members of the Nevada Supreme Court—even in a case where they agreed on the summary-judgment procedure—reflect the urgent need for this Court's authoritative pronouncement on the proper standard of review as well as the appropriate procedural vehicle to resolve special-litigation-committee recommendations in shareholder derivative actions brought in federal court.

II. This is a proper vehicle to resolve the circuit split.

Having failed to alter the reality of the circuit split, Respondents pivot and say this case is a poor vehicle for deciding the first question presented because the Eighth Circuit would have reached the same result even if it had applied a *de novo* standard of review. Opp. 2–3, 23–25. Not so.

In reviewing a special litigation committee's recommendation, courts consider whether the committee members (1) "possessed a disinterested independence" and (2) used "investigative procedures and methodologies [that] were adequate, appropriate and pursued in good faith." Pet. App. 14a (citation omitted). With respect to the first factor, the Eighth Circuit rejected Kokocinski's argument because the "district court did not abuse its discretion." Pet. App. 18a. Likewise, the court rejected Kokocinski's argument with regard to the second factor because the court found "no abuse of discretion." Pet. App. 20a.

Perhaps Respondents believe that the standard of review makes no difference. But this Court has definitively rejected that assumption. *Dickinson*, 527 U.S. at 162 (there "is some practical difference in outcome depending upon which standard [of review] is used"). And it is difficult to see how, applying a *de novo* standard, a court could say as a matter of law that the special litigation committee's recommendation was based on a methodology that was adequate and appropriate. To reach that outcome, the committee necessarily had to conclude that there was very little financial benefit for the company to obtain by pursuing a cause of action against the defendant officers and directors.

That lawsuit is based on many of the same facts that resulted in multiple government investigations conducted by the United States Department of Justice (DOJ) and the United States Senate Finance Committee, with Medtronic agreeing to a whistle-blower settlement with the DOJ for $40 million. Those same facts forced Medtronic to enter into a class-action settlement for securities fraud for another $85 million. Those same facts resulted in an artificially inflated share price at a time the defendant officers and directors authorized a stock-repurchase program that cost Medtronic $2.8 *billion*. And the massive settlement amounts were not even considered by the defendant officers and directors when awarding executive compensation. A lawsuit against those officers and directors is likely to generate more than a nominal judgment. And that is before factoring in the news that broke while the appeal was pending in this case: that the defendants violated Food and Drug Administration requirements by failing to report patient deaths caused by Infuse. In all, Kokocinski reasonably claims damage to the company totaling hundreds of millions of dollars, an amount—supported by known facts, unrefuted by Respondents—that cannot seriously be characterized as so insignificant that it is not in the company's best interests to pursue recovery of those losses.

In sum, the first question presented raises a deep and mature circuit split that must be resolved, and this case is an ideal vehicle for this Court to do so. Certiorari is warranted.

III. If the Court rules against Kokocinski on the first question presented, this case also raises a second circuit split.

The second question presented by the petition assumes that the Eighth and Eleventh Circuits are correct that Rule 23.1—rather than Rule 12(b)(6) or Rule 56—governs an order granting dismissal of a derivative action based on the recommendation of a special litigation committee. With respect to this question, Respondents do not even attempt to argue there is no split; the First, Second, Sixth, and Seventh Circuits are plainly on one side, with the Third, Ninth, Tenth, Eleventh, and D.C. Circuits on the other. Pet. 21–24. Instead, Respondents argue that the mature and established split is over the standard of review for orders resolving motions to dismiss under Rule 23.1(b), whereas *this* case involves Rule 23.1(c). Opp. 25–28.

The flaw in that argument is that even if Rule 23.1 is relevant, Rule 23.1(c) is the worst possible sub-section to apply to dismissal motions based on special-litigation-committee recommendations. As explained in the petition, Rule 23.1(c) only addresses court approval when a derivative action is to "be settled, *voluntarily* dismissed, or compromised." Fed. R. Civ. P. 23.1(c) (emphasis added). The present action is certainly not a settlement or compromise. And it is not remotely close to being a "voluntary" dismissal. Kokocinski vehemently contests the motion to dismiss, and if the district court's decision granting the motion is ultimately affirmed, it will mean the end of this litigation.

Respondents criticize Petitioner for not explaining adequately why a motion to dismiss is more akin to a proceeding under Rule 23.1(b) than a voluntary dismissal or settlement under Rule 23.1(c). Opp. 27–28. But that point is self-evident. Rule 23.1(b) governs motions that seek to dismiss a derivative action based on the inadequacy of the plaintiff's complaint. The proceeding at issue here was also a motion that sought to dismiss Kokocinski's derivative action based on the purported inadequacy of her complaint (lack of proof that the committee's recommendation should be rejected). Conversely, Respondents proffer no rational explanation why a dispositive motion to dismiss based on special-litigation-committee documents subjected to no discovery would be controlled by a sub-rule that applies only when there is a *joint* agreement to settle the action or when the plaintiff has *voluntarily* decided simply to walk away.

In a last-ditch effort to evade review of the second question presented, Respondents argue that there is no circuit conflict "with regard to whether Rule 23.1*(b)* is a proper analog for a motion to terminate." Opp. 27. That contention misses the point altogether. The circuit conflict is over the proper standard of review to apply when reviewing a motion to dismiss. And whether this Court ultimately holds that the review framework is governed by Rule 23.1(b), Rule 23.1(c), Rule 12(b)(6), Rule 56, or something else entirely, the conflict described in the petition remains. Again, Respondents resort to merits arguments, failing to respond in a meaningful way to the disarray among the circuits over how to review orders that terminate derivative actions based on special-litigation-committee recommendations.

IV. The Court should provide the lower courts with direction about discovery in the context of a motion to dismiss a derivative action.

The petition's final question asks whether a plaintiff in a derivative action has a right to discovery before a district court rules on a special litigation committee's motion to dismiss. As the petition explains, Kokocinski desired to show the committee was biased because of the extraordinary amount of compensation it received, but she was not entitled to know what the committee members were actually paid. Kokocinski desired to show the members' selection was biased, but she was not entitled to know how the committee was formed or members chosen. Kokocinski desired to show the committee's methodology was unsound, but she was not entitled to know the process for making the investigation. And Kokocinski desired to argue that Medtronic's adoption of the committee's recommendation was made in bad faith, but she was not entitled to any information about that adoption process, including the extent to which the defendants in this case participated in that decisions. Pet. 25.

Respondents try to discredit Kokocinski by accusing her of mischaracterizing the Eighth Circuit as holding that she was entitled to *no* discovery, on any topic. Opp. 28. Kokocinski's actual position is more modest. Kokocinski's argument is that the district court and Eighth Circuit left her powerless to challenge the special litigation committee's recommendation by denying her basic discovery "regarding the special litigation committee's independence and the validity of its methodology." Pet. 12.

Respondents then defend the Eighth Circuit's decision, and deny any conflict with other circuits, by framing the situation as one where the Eighth Circuit simply deferred to the district court's discretion. Opp. 28–31. But the Eighth Circuit went further than that. It placed the burden on Kokocinski to show that "further discovery may be fruitful" and not merely a "fishing expedition." Pet. App. 22a. That is a particularly high hurdle given that all the information that would allow a derivative plaintiff to show "fruitfulness" is in the hands of the company and its officers and directors. And this is exactly the rationale adopted in *Parkoff* v. *General Telephone & Electric Corp.*, 53 N.Y.2d 412 (1981), by the New York high court, whose decision in *Auerbach* v. *Bennett*, 47 N.Y.2d 619 (N.Y. 1979), is controlling. See *Parkoff*, 53 N.Y.2d at 417–18 (noting that "almost all possible evidentiary data with respect to the areas of permissible inquiry were within the exclusive possession of defendants.").[3]

Regardless, the conflict with the Second Circuit's decision in *Halebian* is apparent. There, too, a district court granted a motion to dismiss a derivative action based on a belief that it should defer to the discretion of the special litigation committee.

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[3] Notably, in *DISH Network*—a case cited by Respondents—the trial court, in applying the *Auerbach* approach to a special litigation committee's recommendation, granted plaintiff discovery under the Nevada counterpart of Rule 56(d) regarding the committee's independence and the thoroughness of the committee's investigation. 401 P.3d at 1087.

Though holding that whether to allow discovery in the context of a Rule 56 motion for summary judgment rests within the district court's discretion, 644 F.3d at 133, the Second Circuit concluded that the district court's erroneous application of an abuse-of-discretion standard warranted a remand so that the district court could reevaluate the discovery request "in light of Rule 56 case law and procedures." *Id.* That is the same relief that Kokocinski seeks here, not an order simply directing that discovery be granted. Pet. 29 ("Kokocinski respectfully submits that the most appropriate way to deal with this record defect is to remand to the district court for reconsideration, as the Second Circuit did in *Halebian*."). This is a reasonable request, one that should be granted alongside the first two questions presented regarding the appropriate standard of review.

CONCLUSION

For the foregoing reasons, and those stated in the petition for a writ of certiorari, the petition should be granted.

Respectfully submitted,

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