No. 12-1208

In the Supreme Court of the United States

UBS FINANCIAL SERVICES INCORPORATED OF PUERTO RICO, ET AL.,
Petitioners,

v.

UNIÓN DE EMPLEADOS DE MUELLES DE PUERTO RICO PRSSA WELFARE PLAN, ET AL.,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the First Circuit

REPLY BRIEF FOR PETITIONERS

JAY B. KASNER
SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP
Four Times Square
New York, New York 10036
Phone: (212) 735-3000

SALVADOR J. ANTONETTI-STUTTS
UBALDO M. FERNÁNDEZ
MAURICIO O. MUÑIZ-LUCIANO
O'NEILL & BORGES LLC
250 Muñoz Rivera Avenue
Suite 800
San Juan, Puerto Rico 00918
Phone: (787) 764-8181

PAUL J. LOCKWOOD
Counsel of Record
NICOLE A. DISALVO
SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP
One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899
paul.lockwood@skadden.com
Phone: (302) 651-3000

Counsel for Petitioners UBS Financial Services Incorporated of Puerto Rico, UBS Trust Company of Puerto Rico, Miguel A. Ferrer, Carlos V. Ubiñas, Stephen C. Roussin and Leslie Highley, Jr.

Additional counsel listed on inside cover

JOSÉ C. SÁNCHEZ-CASTRO
JOSÉ LUIS BARRIOS-RAMOS
LOPEZ SÁNCHEZ PIRILLO &
HYMOVITZ LLC
P.O. Box 11917
San Juan, Puerto Rico 00922
Phone: (787) 522-6776

Counsel for Petitioners Puerto Rico Fixed Income Fund II, Inc., Puerto Rico Fixed Income Fund III, Inc., Puerto Rico Fixed Income Fund IV, Inc., and Tax-Free Puerto Rico Fund II, Inc.

RAFAEL ESCALERA-RODRÍGUEZ
PEDRO SANTIAGO-RIVERA
REICHARD & ESCALERA
P.O. Box 364148
San Juan, Puerto Rico 00936
Phone: (787) 777-8888

Counsel for Petitioners Mario S. Belaval, Agustín Cabrer-Roig, Gabriel Dolagaray-Balado, Carlos Nido, Luis M. Pellot-González, Vicente J. León and Clotilde Pérez

STATEMENT PURSUANT TO RULE 29.6

Petitioners' Rule 29.6 Statement was set forth at page iii of its Petition for Writ of Certiorari, and there are no amendments to that Statement.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

CASES

Page

STATUTES AND RULES

I. Introduction

Contrary to the contentions of Respondents, [1] (i) Petitioners have not "exaggerated" the split among the circuits – there is an undisputed circuit split regarding the standard of review to be applied to appeals from dismissals pursuant to Rule 23.1 (*see* pp. 3-4, *infra*); (ii) this circuit split will not be resolved on its own – even Respondents concede that the First Circuit decision is the minority position (*see* pp. 5-6, *infra*); (iii) the standard of review for Rule 23.1 dismissals is not an obscure legal issue but a recurring issue of national importance – the issue is currently being argued in appeals pending in four different circuits (*see* pp. 6-7, *infra*); and (iv) applying the abuse of discretion standard would have made a difference here – the district court's dismissal of Respondents' complaint would have been affirmed under the deferential abuse of discretion standard (*see* pp. 9-12, *infra*). For these reasons, explained more fully below, Respondents have failed to rebut Petitioners' showing that a writ of certiorari should be granted.

First, Respondents *concede that there is a split among the circuits* on which standard of review to apply to an appeal from a dismissal of a shareholder derivative suit for failure to comply with the demand requirements of Rule 23.1. Respondents merely disagree with the scope of the split; as they describe it, the First, Sixth and Eighth Circuits apply a supposedly "modern" *de novo* standard while the

---

[1] Undefined capitalized terms have the same meaning as in the petition for writ of certiorari ("Petition").

Second, Third, Seventh, Ninth, Tenth, Eleventh and D.C. Circuits apply the traditional abuse of discretion standard. This quibbling about the extent of the split does not in any way lessen the need for this Court to resolve this clear circuit split.[2]

Second, this is not a novel issue that the circuits need time to resolve on their own – federal courts have been hearing appeals from dismissals of derivative suits on demand grounds for more than a century. Furthermore, Respondents' assertion that there is purportedly a trend toward a "modern" *de novo* review standard is belied by the fact that, even by Respondents' count of the split, the circuits prefer the traditional abuse of discretion standard by a two-to-one margin.

Third, the standard of review for Rule 23.1 appeals is an issue of recurring national importance. Rule 23.1 is the federal courts' procedural mechanism for implementing an important issue of state corporate governance – the relative authority of the board of directors and shareholders over a corporation's litigation rights. *See Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 98-99 (1991).

Fourth, under the abuse of discretion standard, Petitioners would have prevailed on appeal. Notably, the First Circuit did not state that the outcome would have been the same under either standard, which courts typically do when the standard is disputed but immaterial to the outcome.

---

[2] Respondents' contention that the Sixth Circuit has adopted a *de novo* standard of review for Rule 23.1 appeals is itself an exaggeration. *See* pp. 3-4, *infra*.

II. The Circuit Split Calls For Certiorari To Be Granted.

A. Respondents Concede That A Split Among The Circuit Courts Exists.

The parties agree that the First Circuit's decision to review *de novo* a district court's dismissal pursuant to Rule 23.1 for failure to plead demand futility conflicts with decisions by the Second, Third, Seventh, Ninth, Tenth, Eleventh and D.C. Circuits, which each apply an abuse of discretion standard in such appeals. (Opp. Br. at 10 n.5) The parties part ways only in that Respondents contend that the Sixth and Eighth Circuits have sided with the First Circuit. (Opp. Br. at 10) But even if the Court includes the Sixth and Eighth Circuits on the side of the First Circuit, that does not lessen the need for the Court to resolve a clear circuit split. Whether the decision below is on the short side of a 7 to 1 split or a 7 to 3 split is irrelevant to the question whether the Petition should be granted.

In any case, Petitioners submit that the accurate count as of the filing of this reply brief is a 7 to 2 split among the circuits. Petitioners agree with Respondents that an Eighth Circuit decision issued just a few days before Petitioners filed the Petition, *Gomes v. American Century Companies,* 710 F.3d 811, 815 (8th Cir. 2013), appears to adopt a *de novo* standard for Rule 23.1 appeals.[3] In affirming a dismissal of a derivative suit for failure to plead demand futility, the *Gomes* opinion includes a

[3] Petitioners were unaware of this newly issued case when the Petition was filed.

cursory statement that the standard of review is *de novo*. *See id.* ("We review *de novo* a district court's decision to grant a motion to dismiss, accepting the complaint's allegations as true."). In employing a *de novo* standard, the Eighth Circuit did not discuss the traditional abuse of discretion standard or the First Circuit's recent decision to switch to the *de novo* standard. *See id.*

The parties disagree, however, on whether the Sixth Circuit has adopted a *de novo* standard for review of Rule 23.1 dismissals. The two cases cited by Respondents describe a standard of review for *Rule 12(b)(6)*, not Rule 23.1. *See In re Ferro Corp. Derivative Litig.*, 511 F.3d 611, 617 (6th Cir. 2008) ("We review *de novo* the district court's dismissal of a complaint for failure to state a claim under Rule 12(b)(6)."); *McCall v. Scott,* 239 F.3d 808, 815 (6th Cir. 2001) ("A district court's decision to dismiss under Fed. R. Civ. P. 12(b)(6) is reviewed *de novo*."). Indeed, the First Circuit presumably shared Petitioners' view that these holdings shed no light on the Rule 23.1 standard because the First Circuit's opinion does not discuss *Ferro* or *McCall* as endorsing a *de novo* standard for Rule 23.1 appeals.[4]

The parties' disagreement about *Ferro* and *McCall*, however, is beside the point. Regardless of whether the circuit split is 7 to 3 or 7 to 2, it requires the attention of this Court.

---

[4] In an appeal pending before the Sixth Circuit, *Lukas v. McPeak,* No. 12-6285 (6th Cir. 2013), the parties have briefed the question of the appropriate standard to apply to the review of Rule 23.1 dismissals. Thus, *Lukas* may definitively resolve the issue in that circuit.

B. The Circuit Split Will Not Resolve Itself.

Respondents next contend that the Court need not resolve the circuit split because it will purportedly resolve itself over time without the intervention of this Court. (Opp. Br. at 11-12) Respondents' assertion that only a little more patience is needed does not square with the fact that appeals from dismissals of derivative suits for failure to plead demand futility go back over a century. (*See* Pet. at 22)

Respondents contend that there is a recent "trend" toward *de novo* review, but a review of the cases cited by Respondents shows no trend that is likely to create uniformity in the circuits. Respondents argue that the Second and Ninth Circuits "appear inclined to discard that [abuse of discretion] standard" (Opp. Br. at 11), but the most recent opinions from those courts show otherwise. Nine years ago, in *Scalisi v. Fund Asset Management, L.P.*, 380 F.3d 133, 137 n.6 (2d Cir. 2004), one Second Circuit panel questioned whether the abuse of discretion standard for Rule 23.1 dismissals should be abandoned, but recent decisions from the Second Circuit continue to apply the abuse of discretion standard. *See, e.g., Lambrecht v. O'Neal*, Nos. 11-1285, 11-1589, 2012 WL 6013440, at *1 (2d Cir. 2012); *Stein v. Immelt*, 472 F. App'x 64 (2d Cir. 2012); *Halebian v. Berv*, 590 F.3d 195, 203 (2d Cir. 2009). Likewise, four years ago, a panel of the Ninth Circuit questioned whether abuse of discretion is the appropriate standard of review for Rule 23.1 appeals, *see Laborers International Union of North America v. Bailey*, 310 F. App'x 128, 130 (9th Cir. 2009), but subsequent Ninth Circuit cases have applied the

traditional abuse of discretion standard. *See Israni v. Bittman*, 473 F. App'x 548, 550 (9th Cir. 2012); *Baca v. Crown*, 458 F. App'x 694, 696 (9th Cir. 2011); *Lynch v. Rawls*, 429 F. App'x 641, 643 (9th Cir. 2011); *Simmonds v. Credit Suisse Sec. LLC*, 638 F.3d 1072, 1087 (9th Cir. 2011), *vacated on other grounds*, 132 S. Ct. 1414 (2012); *Indiana Elec. Workers Pension Trust Fund, IBEW v. Dunn*, 352 F. App'x 157, 159 (9th Cir. 2009).

Respondents contend that the Delaware Supreme Court's opinion in *Brehm v. Eisner,* 746 A.2d 244 (Del. 2000), has touched off a widespread reconsideration of the standard of review for Rule 23.1 appeals, but the only circuit to change its standard of review based on the reasoning of *Brehm* is the First Circuit in the opinion below. The Second, Third, Ninth, Tenth and Eleventh Circuits have each applied the traditional abuse of discretion standard of review post-*Brehm*. *See, e.g., Lambrecht*, 2012 WL 6013440, at *1; *Israni*, 473 F. App'x at 550; *Staehr v. Alm*, 269 F. App'x 888, 891 (11th Cir. 2008); *Cadle v. Hicks*, 272 F. App'x 676, 677 (10th Cir. 2008); *In re Merck & Co. Sec., Derivative & ERISA Litig.*, 493 F.3d 393, 399 (3d Cir. 2007); *Fagin v. Gilmartin*, 432 F.3d 276, 281 (3d Cir. 2005).

C. The Standard Of Review Of Rule 23.1 Dismissals Is An Important Aspect Of Corporate Jurisprudence.

The issue raised in the Petition is important to corporations, their directors and their shareholders because the difference in abuse of discretion review versus plenary review may often be determinative to Rule 23.1 appeals. (Pet. at 18-20) Furthermore, a Rule 23.1 determination by a trial court is not merely

a preliminary pleading matter, but decides who has the legal right to litigate on behalf of the corporation – the board of directors or the shareholder plaintiff.

Respondents argue (Opp. Br. at 13-14) that this issue is unimportant because, even if the split remains, there would be little likelihood of divergent outcomes across the federal appellate courts due to different standards of review. On the contrary, this Court has noted the stark difference between abuse of discretion and *de novo* review. *Salve Regina Coll. v. Russell*, 499 U.S. 225, 238 (1991) (holding that "the difference between a rule of deference and the duty to exercise independent review is 'much more than a matter of degree'").

The proliferation of challenges to the traditional abuse of discretion standard of review for Rule 23.1 dismissals in just the few months since the First Circuit's decision below belies Respondents' assertion that the question presented addresses an "obscure legal issue." (Opp. Br. at 13) After the decision below, appellants in the Second, Sixth, Seventh and Ninth Circuits have urged those courts to follow the First Circuit and adopt *de novo* review. Reply Brief for Plaintiff-Appellant Patrick P. Lukas, *Lukas v. McPeak*, No. 12-6285, 2013 WL 1721512, at *9 (6th Cir. Apr. 8, 2013); Reply Brief of Plaintiff-Appellant, *Westmoreland Cnty. Emps. Ret. Sys. v. Parkinson, Jr.*, No. 12-3342, 2013 WL 1752618, at *6 (7th Cir. Apr. 8, 2013); Brief of Plaintiff-Appellant, *St. of Mich. Emps. Ret. Sys. v. Bear Stearns Cos.,* No. 11-4177-cv, 2013 WL 1494945, at *16-17 (2d Cir. Apr. 5, 2013); Reply Brief for Plaintiff-Appellant, *Saginaw Police & Fire Pension Fund v. Andreessen*, No. 12-16473, 2013 WL 874897, at *4-5 (9th Cir. Feb. 28, 2013).

III. Abuse Of Discretion Is The Appropriate Standard Of Review For A Dismissal Pursuant To Rule 23.1.

Respondents contend that the First Circuit properly applied *de novo* review to the District Court's dismissal for failure to allege particularized facts sufficient to excuse their failure to make a pre-suit demand on the boards of the Funds. According to Respondents, a dismissal pursuant to Rule 23.1 is no different from a dismissal pursuant to Rule 12(b)(6) and should get the same standard of review on appeal. (Opp. Br. at 7-8) This argument conflicts with (1) the fact-specific analysis required under Rule 23.1 and (2) the historic purpose and development of the Rule. (Pet. at 21-22)

Indeed, one important difference between Rule 23.1 and Rule 12(b)(6) is that the trial court's factual determinations regarding demand futility, although based on allegations of particularized fact instead of evidence, are never further considered at a final factual hearing. There will be no trial on the demand question. The Rule 23.1 motion is, in essence, a threshold equitable proceeding within the derivative suit in which the trial court, sitting in equity, resolves a factual dispute (based on particularized allegations) regarding whether demand was excused (or, if a demand was made, whether it was wrongfully refused). Under such circumstances, deference to the traditional equitable discretion of the trial court is appropriate. (*See id.*)

IV. Petitioners Would Have Prevailed Under The Abuse Of Discretion Standard.

Respondents contend that this case is not appropriate for review by this Court because the outcome in the First Circuit would have been the same under the abuse of discretion standard. (Opp. Br. at 14-21) Respondents' arguments in support of this assertion are unconvincing for three reasons.

First, the First Circuit did *not* state that it would have reached its decision under the traditional abuse of discretion standard instead of its newly adopted *de novo* standard. Where the standard of review is disputed by the parties, but is irrelevant to the outcome of an appeal, courts usually say so. *See Israni*, 473 F. App'x at 550 n.1 ("a *de novo* standard of review would not change the outcome of this case"); *Kautz v. Sugarman*, 456 F. App'x 16, 18 (2d Cir. 2011) ("our ruling today would be required under either standard"). *See also Lambrecht*, 2012 WL 6013440, at *1 n.1; *Laborers Int'l Union of N. Am.*, 310 F. App'x at 130 n.1. Thus, the absence of such a statement in the First Circuit's decision strongly implies that the standard *did* matter to the First Circuit.

Second, Respondents contend that, regardless of which standard was applied, the First Circuit's review would have been plenary because the District Court's decision "rest[ed] on a question of law *or* mixed question of law and fact that involve[d] legal principles." (Opp. Br. at 15) But the First Circuit disagreed with the District Court's analysis *of the facts*, not the law. For example, in considering Petitioner Belaval's independence, the First Circuit reiterated the facts alleged in the complaint and

concluded that the District Court "failed to make reasonable, common sense inferences" from them. (App. 23a-26a) Similarly, when reviewing the District Court's decision with respect to Petitioner León, the First Circuit admittedly engaged in a new examination of the facts. (*Id.* at 26a ("we examine the facts alleged"); *see also* Pet. at 26) Even Respondents admit that the First Circuit's reversal was based on its conclusion that the District Court failed to "'analyze more broadly the facts alleged,'" "'focused too narrowly on whether plaintiffs had pled'" sufficient facts, and "'declined to make reasonable inferences of materiality from the facts alleged by plaintiffs.'" (Opp. Br. at 15) The First Circuit's disagreement with the District Court's assessment of the facts was inconsistent with the abuse of discretion standard. *See, e.g.*, *Scalisi*, 380 F.3d at 137 (abuse of discretion applies "where 'determination of the sufficiency of allegations of futility depends on the circumstances of the individual case'") (quoting *Kaster v. Modification Sys., Inc.*, 731 F.2d 1014, 1018 (2d Cir. 1984)). *See also Hutchinson ex rel. Julien v. Patrick*, 636 F.3d 1, 15 (1st Cir. 2011) (district court did not abuse its discretion by deciding an issue over "which reasonable minds could disagree").[5]

---

[5] Respondents point to *Lynch v. Rawls* to show that the abuse of discretion standard would not have changed the outcome here. 429 F. App'x 641, 643 (9th Cir. 2011). *Lynch* is inapposite. In *Lynch*, the Ninth Circuit held that the district court abused its discretion by dismissing a derivative action for failure to plead demand futility because the facts alleged regarding the directors' participation in a stock option backdating scheme were nearly identical to facts alleged in *(cont'd)*

Respondents next argue that abuse of discretion review would have reached the same result because the District Court made an errant conclusion of law in holding that two directors who were UBS Puerto Rico employees, Ubiñas and Roussin, were independent from UBS Puerto Rico. (Opp. Br. at 19) Respondents contend that the District Court abused its discretion because "defendants had conceded that [Ubiñas and Roussin] were not independent for futility purposes." (*Id.*) Respondents' assertion that Petitioners conceded this point is incorrect. Petitioners did not argue this point because it was irrelevant to the outcome of the Rule 23.1 analysis, which requires the District Court to determine whether a *majority* of the board lacked independence. (App. 14a; *see also id.* at 18a (acknowledging that at least six directors had to be interested or lack independence to find demand futility)) Thus, even if the District Court's conclusion with respect to the independence of Ubiñas and Roussin was an "errant conclusion of law," it would not have been material to the District Court's ultimate calculus of the majority of the Board's independence because the unaffiliated outside directors made up a majority of the Board. In other words, Respondents' arguments regarding

---

(cont'd from previous page)
Delaware cases that had found demand to be excused. *See id.* In particular, the Ninth Circuit held that the district court erred by "engag[ing] in an extensive, fact-based examination and criticism of [p]laintiffs' proffered statistical analysis" when similar statistical analyses regarding options backdating had been found to be sufficient by the Delaware courts. *See id.* at 644. Here, unlike *Lynch*, Respondents point to no closely analogous Puerto Rico or Delaware case that the District Court ignored.

Ubiñas and Roussin would not cause the appeal to come out the same way under the abuse of discretion standard.

CONCLUSION

For the foregoing reasons and those articulated in the Petition, Petitioners respectfully request that this Court grant certiorari to review the judgment of the First Circuit.

Respectfully submitted,

PAUL J. LOCKWOOD
Counsel of Record
NICOLE A. DISALVO
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899
paul.lockwood@skadden.com
Phone: (302) 651-3000

JAY B. KASNER
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
Four Times Square
New York, New York 10036
Phone: (212) 735-3000

SALVADOR J. ANTONETTI-STUTTS
UBALDO M. FERNÁNDEZ
MAURICIO O. MUÑIZ-LUCIANO
O'NEILL & BORGES LLC
250 Muñoz Rivera Avenue
Suite 800
San Juan, Puerto Rico 00918
Phone: (787) 764-8181

Counsel for Petitioners
UBS Financial Services
Incorporated of Puerto Rico,
UBS Trust Company of Puerto
Rico, Miguel A. Ferrer,
Carlos V. Ubiñas, Stephen C.
Roussin and Leslie Highley, Jr.

JOSÉ C. SÁNCHEZ-CASTRO
JOSÉ LUIS BARRIOS-RAMOS
LOPEZ SANCHEZ PIRILLO & HYMOVITZ LLC
P.O. Box 11917
San Juan, Puerto Rico 00922
Phone: (787) 522-6776

Counsel for Petitioners
Puerto Rico Fixed Income Fund II, Inc.,
Puerto Rico Fixed Income Fund III, Inc.,
Puerto Rico Fixed Income Fund IV, Inc., and
Tax-Free Puerto Rico Fund II, Inc.

RAFAEL ESCALERA-RODRÍGUEZ
PEDRO SANTIAGO-RIVERA
REICHARD & ESCALERA
P.O. Box 364148
San Juan, Puerto Rico 00936
Phone: (787) 777-8888

Counsel for Petitioners Mario S. Belaval, Agustín Cabrer-Roig, Gabriel Dolagaray-Balado, Carlos Nido, Luis M. Pellot-González, Vicente J. León and Clotilde Pérez

DATED: May 17, 2013