



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

**CITY OF WESTLAND POLICE &
FIRE RETIREMENT SYSTEM,**

Plaintiff,

v.

AXCELIS TECHNOLOGIES, INC.,

Defendant.

C. A. No. 4473-VCN

DEFENDANT'S ANSWERING PRE-TRIAL BRIEF

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PRELIMINARY STATEMENT¹

Upon review of Plaintiff's Opening Brief, a couple of things are now immediately clear: Plaintiff's so-called evidence of wrongdoing consists of unremarkable things, such as (i) the Board's rejection of the SHI Proposals and a subsequent decline in Axcelis' stock price, and (ii) the Board's decision, in accordance with Axcelis' Governance Policies, not to accept the resignations of directors who were validly elected at the Company's 2008 Annual Meeting. Other than these facts, Plaintiff's "evidence" can be reduce to wholly conclusory allegations, without even a suggestion of cognizable self-interest, that outside directors not employed by Axcelis sought to entrench themselves to preserve their directorships. The factual background set out in Defendant's Opening Brief fully and accurately describes the events underpinning this action. Neither the entirety of those facts, nor a restatement of Plaintiff's factual recitation, will be undertaken here. Rather, Axcelis discusses facts only as needed in the course of countering Plaintiff's legal arguments.

Plaintiff's Opening Brief espouses legal theories that are not supported by the facts. Surprisingly, Plaintiff contends that the Board's decision not to accept the resignations of Directors Hardis, Thompson, and Fletcher was motivated by entrenchment and thwarted the will of Axcelis' stockholders, thus triggering *Blasius* review. However, simply saying it does not make it so. Nothing in the record supports the bald assertion of entrenchment motivation. Moreover, nothing of substance supports Plaintiff's claim that *Blasius* applies when reviewing the Board's post-election decision not to accept resignations of the three Directors validly elected by Axcelis' stockholders in an uncontested election. Plaintiff

¹ Unless otherwise indicated, defined terms herein shall have the meaning ascribed to them in Defendant's Opening Brief.

seems to suggest, without authority, that the Company's Governance Policies (despite expressly providing for the Board's exercise of discretion) gave stockholders the *right* to remove directors by withholding majority support. Not only is this argument legally infirm, it is illogical. The Governance Policies easily could have stated that directors who do not receive majority support *shall resign*. They do not. Alternatively, Plaintiff and/or other Axcelis stockholders could have exercised their franchise by seeking to seat directors of their choice in a contested election. They did not.

Plaintiff also argues that *Unocal* review should apply because the Board's decision not to immediately engage in discussions with SHI to sell the Company, and its later decision to sell its stake in SEN, were "defensive" measures motivated by entrenchment. True to pattern, however, Plaintiff fails to provide any analysis of what cognizable self-interest might possibly be motivating outside independent directors to say "no" to SHI's Proposals. More importantly, *Unocal* is not implicated here because no defensive measures were implemented in response to a perceived threat to Axcelis. The case law is clear that a board's exercise of its Section 251 power to say "no" to a merger proposal is subject to business judgment review. Plaintiff has offered no evidence of disloyalty that would tend to rebut that presumption.

As for the sale of Axcelis' stake in SEN, that was not defensive because at the time of the sale no overtures or proposals from SHI were present or even threatened. By the time of the sale, the First and Second Proposals were a year in the past, and the discussions in June and July of 2008 that Axcelis *agreed to engage in* (after SHI finally agreed to a routine confidentiality agreement) were also concluded. Indeed, SHI itself announced that those discussions were over after it declined to make a revised proposal to acquire Axcelis.

Axcelis' sale of its 50% interest in SEN should be seen for what it actually was. It was a means by which the Company, after an attempt at refinancing, was able to generate cash to pay down overdue debt and thereby avoid the entry of an adverse judgment in pending litigation regarding that debt.

For all its sound and fury, Plaintiff's Opening Brief signifies nothing. What is at issue here are business decisions of the Board with which Plaintiff disagrees. Of course, that is not evidence of wrongdoing. Boards of directors govern the affairs of Delaware corporations in accordance with their independent exercise of fiduciary duty. They are not reflexive bodies charged with the obligation to affect the disparate and fluctuating objectives of stockholders. As this Court has recognized, the board room is not a New England town hall. Plaintiff simply has not offered credible evidence of probable corporate wrongdoing such that it should be entitled to bypass the Board's judgment and use its Section 220 Demand to mine the Company's books and records in the hopes of unearthing a claim.

ARGUMENT

I. DISAGREEMENT WITH A BOARD'S BUSINESS DECISION, SPECULATION, AND A PLAINTIFF'S OWN SELF-SERVING AND CONCLUSORY ALLEGATIONS DO NOT CONSTITUTE EVIDENCE OF PROBABLE CORPORATE WRONGDOING

Although Plaintiff acknowledges that it bears the burden to present credible evidence of probable corporate wrongdoing before it can investigate purported breaches of fiduciary duty (*see* POB at p. 12), Plaintiff continues to rely on mere speculation, disagreements with the Board's business decisions, and its own conclusory allegations. None of these constitute credible evidence in a Section 220 case. *See Seinfeld v. Verizon*, 909 A.2d 117, 120 (Del. 2006) (holding that "a disagreement with the business judgment of [the board]...is not evidence of wrongdoing"); *Mattes v. Checkers Drive-In Restaurants, Inc.*, 2002 WL 337865, at *5 (Del. Ch. Mar. 28, 2001) (holding that "[m]ere curiosity or a desire for a fishing expedition will not suffice") (internal citation omitted); *Weiland v. Central & South West Corp.*, 1989 WL 48740, at *2 (Del. Ch. May 9, 1989) (dismissing Section 220 action where facts failed to evidence that board members were interested rather than independent or that they failed to exercise due care); *Everett v. Hollywood Park, Inc.*, 1996 WL 32171, at *5-6 (Del. Ch. Jan. 19, 1996) (declining Section 220 demand with respect to transactions for which plaintiff did not establish credible evidence of self-dealing).

Recognizing that its Demand actually hinges on its own conclusory allegations -- as opposed to "evidence" -- Plaintiff cites a decision of this Court for the proposition that its own allegations satisfy the "credible evidence" standard in a Section 220 case. (POB at p. 12.) It should come as no surprise that the cited case, *Deephaven Risk ARB Trading Ltd. v. Unitedglobalcom, Inc.*, 2005 WL 1713067 (Del. Ch. July 13, 2005), stands for no such

proposition. In *Deephaven*, an investment fund sought books and records to investigate possible mismanagement in connection with significant discrepancies in the disclosed results of an issuer's rights offering. Pursuant to the offering, a total of 83 million rights were distributed to the issuer's class A stockholders. The offering allowed the stockholders to subscribe to purchase one share of class A stock at a discount for each right held. The offering also included an oversubscription privilege pursuant to which rightholders who exercised their basic subscription privilege in full could purchase additional stock on a pro rata basis until the issuer sold all 83 million shares.

Following an initial tabulation by the issuer's rights agent, the issuer disclosed that it received subscriptions for approximately 64 million shares and an oversubscription for approximately 67 million shares. Based on these numbers, the plaintiff investment fund was eligible for the entire 1 million shares it sought to purchase in accordance with its oversubscription privilege. A week later, the issuer disclosed substantially different results. In that press release, the issuer stated that it had received subscriptions for 82 million of the 83 million rights. This left only 1 million shares available for oversubscriptions, which drastically reduced the number of shares that plaintiff could purchase based on its oversubscription privilege.

Ultimately, the Court determined that there was credible evidence of wrongdoing, but the potential wrongdoing was not premised on plaintiff's own allegations. Rather, the Court was persuaded by the following "facts":

- The substantial discrepancy in the number of subscriptions disclosed in the issuer's press releases;
- The fact that there were seven days between the press releases, but yet the rights offering deadline was on the eve of the first press release, which should have allowed the issuer and its right agent to determine the actual

subscription numbers in a more timely fashion;

- Conversations between representatives of plaintiff, the issuer, and its rights agent in which plaintiff was told that the first press release accounted for subscriptions from rightholders who were unable to deliver their rights certificates, but complied by providing notices of guaranteed delivery. This was inconsistent with the second press release, which specifically stated that the figures in the first press release excluded shares unsubscribed pursuant to guaranteed delivery procedures; and
- Conversations between representatives of plaintiff and the rights agent in which plaintiff was led to believe that the initial undersubscription likely was due to the inability of foreign holders to comply with complicated exercise procedures. In light of other inconsistencies, this suggested the possibility that the issuer and/or its rights agent had, subsequent to the closing of the offering, made exceptions for certain foreign issuers and allowed them to exercise despite noncompliance with the procedures in the prospectus.

See Deephaven, 2005 WL 1713067, at *22-25. This type of evidence -- substantial discrepancies in press releases disclosing discreet calculations and conflicting testimony from defendant and its agent -- is a far cry from the speculations offered by Plaintiff here. As shown below, Plaintiff's disagreement with the Board's business decisions and its speculation based on selective quotations and flawed logic does not constitute credible evidence of probable corporate wrongdoing.

II. AXCELIS' RETENTION OF DIRECTORS VALIDLY ELECTED BY A PLURALITY, IN ACCORDANCE WITH THE COMPANY'S BY-LAWS AND IN ACCORDANCE WITH DELAWARE LAW, IS NOT CREDIBLE EVIDENCE OF PROBABLE CORPORATE WRONGDOING

A. Plaintiff's Conclusory Allegations Of Entrenchment Are Contradicted By The Record And Do Not Implicate *Unocal*

At the outset, any consideration of the Board's decision to reject the tendered resignations of Directors Hardis, Thompson, and Fletcher must start from the premise that the Company's By-Laws provide, in accordance with Delaware law, for director elections based on plurality voting. (*See* By-Laws of Axcelis Technologies, Inc., effective August 8,

2007, § 1.9, attached hereto as Exhibit “1” (“Any election by stockholders shall be determined by a plurality of the votes cast by the stockholders entitled to vote at the election.”); 8 *Del. C.* § 216 (providing that, unless otherwise specified in a company’s certificate of incorporation or bylaws, “[d]irectors shall be elected by a plurality of the votes of shares present in person or represented by proxy at the meeting and entitled to vote on the election of directors”). Each of Directors Hardis, Thompson, and Fletcher received a plurality of the votes cast at the Company’s 2008 Annual Meeting, although they did not receive majority stockholder support. (Stip., ¶¶ 25-27; Press Release dated May 1, 2008, filed as Ex. 99.1 to the Company’s Form 8-K, filed with the SEC on May 1, 2008, Stip., Ex. “O.”) Accordingly, Directors Hardis, Thompson, and Fletcher were elected to the Board.

What Plaintiff complains about is how the Board implemented its Governance Policies in response to the election results. The Company’s Governance Policies provide that in an uncontested election such as the one at issue here, directors who receive less than majority stockholder support must offer to resign their directorships. (Stip., Ex. “P”) Thereafter, the Nominating and Governance Committee shall recommend to the Board what action should be taken in response to any offer of resignation. (*Id.*) The remaining members of the Board are then free to exercise their business judgment in determining whether to accept those resignations. Here, these steps were followed and the Board determined that it was not in the stockholders’ best interests to accept the tendered resignations. (*See* Stip., Ex. “Q.”)

Plaintiff's argument that the Board's decision not to accept the resignations of Directors Hardis, Thompson, and Fletcher creates a credible basis of probable corporate wrongdoing is doomed from the outset because that entire argument hinges on an unfounded premise. Plaintiff states in its Opening Brief: "As Plaintiff alleges in its Complaint, Axcelis retained these rejected directors for the principal purpose of entrenching those directors in office." (POB at p. 13.) Plaintiff appears to suggest that its own self-serving and conclusory allegations are sufficient to constitute credible evidence. They are not. Moreover, and as demonstrated in Axcelis's Opening Pretrial Brief (*see* DOB at pp. 28-31), Plaintiff has not and cannot show any cognizable entrenchment motives. Six of Axcelis' seven directors are outside directors not employed by the Company. (Axcelis Proxy Statement on Schedule 14A, filed with SEC on March 27, 2008 at p. 28-29, attached hereto as Exhibit "2.") In addition, those outside directors are all "independent" for purposes of the NASDAQ rules. (*Id.*) Plaintiff does not contest either of these facts.

In the absence of any evidence of actionable self-interest, Plaintiff's bald assertion of entrenchment motives cannot be countenanced:

A claim of this kind must be viewed with caution, because to argue that directors have an entrenchment motive solely because they could lose their positions following an acquisition is, to an extent, tautological. By its very nature, a board decision to reject a merger proposal could always enable a plaintiff to assert that a majority of the directors had an entrenchment motive. For that reason, the plaintiffs must plead, in addition to a motive to retain corporate control, other facts sufficient to state a cognizable claim that the Director Defendants acted disloyally.

Gantler v. Stephens, 965 A.2d 695, 707 (Del. 2009). There is yet another curiosity in Plaintiff's argument. Plaintiff contends that the Directors other than Hardis, Thompson,

and Fletcher sought to entrench Hardis, Thompson, and Fletcher. (*See* POB at p. 21) (arguing that “Axcelis retained these rejected directors for the principal purpose of entrenching those directors in office”)) Plaintiff does not even hazard an explanation as to why it is that the Directors other than Hardis, Thompson, and Fletcher would seek to entrench Directors *other than themselves*. No possible motive for such an occurrence is even suggested. That is not surprising because an entrenchment analysis seeks to determine what motivates a director to perpetuate *him or herself* in office. A director is “interested” in a transaction when *he or she sits on both sides of the transaction* or expects to derive a *personal financial benefit* that is not also shared by other shareholders generally or the corporation as a whole. *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000); *see also Nebenzahl v. Miller*, 1993 WL 488284, at *3 (Del. Ch. Nov. 8, 1993). No such facts exist here.

Plaintiff’s selective quotations from the record do not even provide factual support for the already faulty legal premise upon which its entrenchment argument is based. To start, Plaintiff points to a portion of an Axcelis press release in which it lists the Board’s reasons for rejecting the resignations of Hardis, Thompson, and Fletcher. (DOB at p. 13.) One of those reasons was the desire to keep these key knowledgeable directors in place for purposes of continuing talks with SHI. (Stip., Ex. “Q.”) According to Plaintiff, this does not pass “the laugh test” because SHI claims that it continually has been “rebuffed.” (DOB at p. 13.) Contrary to Plaintiff’s invective, what is laughable is its desperate attempt at stitching together sound bites in order to pass off that patchwork as “evidence” of some corporate wrongdoing.

First, there were several disclosed reasons supporting the Board's determination not to accept the resignations of Hardis, Thompson, and Fletcher. Those reasons included:

- Those three directors are experienced and knowledgeable about the Company;
- If their resignations were accepted, the Board would be left with only four remaining directors;
- One or more of the three directors serves on each of the key committees of the Company;
- Mr. Hardis serves as lead director;
- The Board believed that losing this experience and knowledge would harm the Company; and
- The Board also noted that retention of these directors is particularly important if Axcelis is able to move forward on discussions with SHI following finalization of an appropriate non-disclosure agreement.

(Stip., Ex. "Q.") What the Company actually disclosed, then, is six independent reasons why the Board made the decision it did. As to the one particular reason Plaintiff attacks, there is nothing in the record to suggest that it is false. That SHI indicated publicly that it was "repeatedly rebuffed" is not surprising. The statement was made in the midst of SHI's unsolicited merger proposals to Axcelis and its press campaign in support thereof. Plaintiff simply cannot take this posturing statement by SHI and purport by the fiat of draftsmanship to make it into a fact. The record is replete with references to the multiple meetings that representatives of Axcelis and SHI had over the years. (Press Release dated March 17, 2008, filed as Exhibit 99.2 to the Company's Form 8-K filed with the SEC March 12, 2008, Stip., Ex. "L"; Press Release dated September 15, 2008, filed as Exhibit 99.1 to the Company's Form 8-K, filed with the SEC on September 15, 2008, Stip., Ex. "S.") It is also undisputed that Axcelis was willing to have private talks with SHI after

execution of an appropriate and customary non-disclosure agreement. (*Id.*) Indeed, that very thing happened, and, as a result thereof, SHI was provided with due diligence materials and numerous meetings with Axcelis management. (Press Release dated September 15, 2008, filed as Exhibit 99.1 to the Company's Form 8-K, filed with the SEC on September 15, 2008, Stip., Ex. "S.") The fact that Axcelis said "no" to SHI's first two acquisition proposals, as it was entitled to do, and the fact that SHI never submitted a revised proposal after due diligence by no means constitutes evidence that the Board did not believe that Thompson, Hardis, and Fletcher were important to discussions with SHI. Neither is it evidence of entrenchment.

Above and beyond the fact that Plaintiff has failed to make any showing of an entrenchment motive that merits further discovery through a books and records inspection, its citation to *Unocal* for the unremarkable proposition that "directors may not have acted solely or primarily out of a desire to perpetuate themselves in office" (DOB at p. 13), has no application here. *Unocal v. Mesa Petroleum*, 493 A.2d 946, 955 (Del. 1985). As discussed more fully later, *Unocal* is not implicated where, as here, (i) the Board does not implement any defensive measures in response to a threat to the Company, and (ii) the Board must exercise its Section 251 power in response to a merger proposal.

B. Plaintiff's Conclusory Allegations of Entrenchment Are Contradicted By The Record And Do Not Implicate *Blasius*

Starting again from the unfounded premise that the Directors declined to immediately engage in talks with SHI to sell the Company out of some unidentified interest to entrench themselves, Plaintiff states that "a board may not act to entrench itself at the expense of the shareholder franchise." (DOB at p. 13.) From there, Plaintiff goes on to argue that when a board acts for the primary purpose of interfering with the stockholder

franchise, the directors must establish a “compelling justification” for that action. (DOB at pp. 13-14) (citing *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 661 (Del. Ch. 1988.)) Plaintiff has the legal principles right, it just has no facts to implicate them. So what does Plaintiff do? It ignores its problem and simply jumps to a conclusion by maintaining that the Directors cannot offer a “compelling justification” for interfering with the stockholder franchise based on the decision not to accept the resignations of Directors Hardis, Thompson, and Fletcher. (DOB at p. 14.)

This lame argument suffers from at least two fundamental and fatal flaws. To the extent the argument is premised on suspicions of entrenchment, Plaintiff has failed to offer one iota of evidence (credible or not) from which it reasonably could be concluded that the Directors had a cognizable entrenchment motive. As already discussed, it is never enough to state simply that outside independent directors are motivated by a desire to retain their directorships.² Moreover, in a classic case of putting the cart before the horse, Plaintiff assumes that *Blasius* review is the appropriate standard and then purports to apply it without offering any evidence or argument as to why that onerous and rarely applied standard of review is appropriate here. *See Williams v. Geir*, 671 A.2d 1368, 1376 (Del. 1996) (holding that the burden of satisfying the “compelling justification” standard under *Blasius* “is quite onerous, and is therefore rarely applied”). Sophistry is no substitute for analysis.

² While Puma is the only “inside” director employed by the Company, there are no allegations that she was motivated by any self-interest in connection with the Board’s decision not to accept the resignations of Hardis, Thompson, and Fletcher. Even if there were such allegations, there are no allegations suggesting that any (much less a majority) of the remaining Directors are beholden to her.

There is simply no evidence to support the conclusion that the Directors acted for the sole or primary purpose of interfering with the stockholder franchise. As made clear by the Delaware Supreme Court, the *Blasius* test is “appropriate only where the ‘primary purpose’ of the board’s action [is] to interfere with or impede exercise of the shareholder franchise and the stockholders are not given a ‘full and fair opportunity to vote.’” *Williams*, 671 A.2d at 1376 (quoting *Stroud v. Grace*, 606 A.2d 75, 92 (Del. 1992)) (emphasis added). Plaintiff’s “evidence” of purported disloyalty is that the Directors supposedly overruled a lawful stockholder vote. (*See* DOB at pp. 14-18.)³ As discussed above, no vote was interfered with. Indeed, there was a vote for election of directors at the Company’s 2008 Annual Meeting, and, in accordance with Delaware law and the Company’s By-Laws, Directors Hardis, Thompson, and Fletcher were elected. Additionally, the Company’s plurality voting regime for director elections was fully disclosed in a Proxy Statement disseminated to stockholders in anticipation of the 2008 Annual Meeting. (Axcelis Preliminary Proxy Statement, on Schedule 14D filed with the SEC on February 28, 2008 at p. 2, attached hereto as Exhibit “3.”)

³ Plaintiff also suggests that the Board must have thwarted the will of Axcelis’ stockholders because a 12% stockholder wrote to the Board to opine that the failure of Hardis, Thompson and Fletcher to receive majority stockholder support was an expression of the stockholders’ frustration over the purported unresponsiveness of these directors to SHI’s overtures. (*See* POB at pp. 7-8.) This cannot possibly constitute evidence of a breach of the duty of loyalty. It is the opinion of one minority stockholder who is not speaking on behalf of other Axcelis stockholders. Even if that were the case, it is irrelevant. As explained herein, the Governance Policies do not give Axcelis stockholders who withhold their votes the right to thereby remove directors. In fact, the Governance Policies clearly provide that accepting resignations is a matter for the Board’s discretion -- it is not a stockholder decision to make.

Here, there is no doubt that Axcelis' stockholders were entitled to, and did, exercise their franchise to elect directors at the 2008 Annual Meeting. There is also no doubt that neither Plaintiff, nor any other stockholder, opted to run a proxy contest in support of an alternative slate of directors. That, however, is the way in which Delaware law, and Axcelis' governing documents, contemplate the stockholders exercising their franchise to change the constitution of the Board.⁴ Indeed, this is no doubt why the Delaware Supreme Court has clarified that *Blasius* review is implicated in contested director elections. *MM Companies, Inc. v. Liquid Audio, Inc.*, 813 A.2d 1118, 1131 (Del. 2003). Plaintiff nevertheless suggests that the Governance Policies create some right to, or protected interest in, the removal of directors Hardis, Thompson, and Fletcher. Plaintiff points to no authority for its ill-considered proposition that stockholders have some type of right to create vacancies as a consequence of withholding majority stockholder support.⁵ If that is what Axcelis intended, which it did not, the Governance Policies easily could have provided that directors receiving less than majority stockholder support in an uncontested election shall resign. They do not. Rather, the Policies require an offer of resignation, followed by a recommendation from the Nominating and Governance Committee, and finally a decision by the Board as to whether the resignations should be accepted. That is precisely what happened here (*see* Stip., Ex. "P"), and it happened in conformity with

⁴ Stockholders have no right to create vacancies, but they may run a proxy contest or seek to remove directors for cause. (*See* Stip. Ex. "A" at Article THIRD, § 6.4)

⁵ Even if vacancies were created, they would be filled by the Board. (Stip. Ex. "A" at Article THIRD, § 6.3; Ex. "1" at § 2.4.)

Delaware law and the Company's governing documents.⁶ Clearly, Plaintiff is not pleased with the outcome. That displeasure, however, does not mean that the outcome must have been achieved via a breach of loyalty. Plaintiff's only "evidence" that it was is its bald assertion that the Directors were motivated by their desire to entrench themselves and, as a result, acted with the primary purpose of interfering with the stockholder franchise in an uncontested election for directors. While it is true that Delaware's Section 220 jurisprudence does not necessitate actual proof of corporate wrongdoing, it does require credible evidence. Plaintiff's strained arguments and selective quoting from the record do not meet that "not insubstantial" burden.

Plaintiff's fallback position -- that *Unocal* applies -- fares no better. For the reasons explained below, *Unocal* does not apply. Not surprisingly, though, Plaintiff proceeds from an assumed conclusion that *Unocal* applies and then confidently goes on to show how the Directors cannot satisfy the reasonableness analysis required by *Unocal/Unitrin*. While it is easy to show how a defendant cannot live up to an inapplicable standard, it is not so easy to establish how the standard applies in the first instance. Perhaps due to this difficulty, Plaintiff never undertakes the exercise. *Axcelis* does so below.

⁶ Plaintiff's characterize this as a "loophole" that allowed the Board to "overturn" election results. (POB at p. 15) As already explained, that position is contrary to law and contrary to the facts. In support of its argument that it had some type of right to create vacancies that was frustrated by the Board's application of the Governance Policies, Plaintiff cites *Scnell v. Chris-Craft Indus. Inc.*, 285 A.2d 437 (Del. 1971). (*Id.*) *Schnell* does not help Plaintiff. The Delaware Supreme Court has held that *Schnell* "should be reserved for those instances that threaten the fabric of the law, or which by an improper manipulation of the law, would deprive a person of a clear right." *Alabama By-Products Corp. v. Neal*, 588 A.2d 255, 258 n.1 (Del. 1991). Here, Plaintiff had no right to create vacancies on the Board, much less a "clear right" that implicates the fabric of Delaware corporate law.

III. BECAUSE THE BOARD TOOK NO “DEFENSIVE” ACTION, *UNOCAL* DOES NOT APPLY

A. Saying “No” To An Unsolicited Merger Proposal, Which Implicates The Board’s Section 251 Power, Is Subject To Business Judgment Review And Is Not Defensive

Unocal review does not apply in this case. “Enhanced judicial scrutiny of *Unocal* applies ‘whenever the record reflects that a board of directors took defensive measures in response to a perceived threat to corporate policy and effectiveness which touches upon issues of control.’” *In re Santa Fe Pac. Corp. S’holder Litig.*, 669 A.2d 59, 71 (Del. 1995) (quoting *Unitrin, Inc. v. Gen. Corp.*, 651 A.2d 1361, 1372 n.9 (Del. 1995)); *see also Unocal v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985). *Unocal* does not apply to the present case for the simple reasons that SHI has not initiated a tender offer and the Board did not adopt defensive measures to thwart an offer.⁷ *Unocal* “starts from the premise that the transaction at issue was defensive.” *Shamrock Holdings, Inc. v. Polaroid Corp.*, 559 A.2d 257, 271 (Del. Ch. 1989). That premise simply does not apply here.

Rather, the issue here is Plaintiff’s contention that there is evidence of breaches of fiduciary duty sounding in loyalty, and not a complaint about implementation of defensive measures in response to a threatened change in control. In the Delaware Supreme Court’s recent *Gantler* decision, the Court rejected plaintiffs’ argument that *Unocal* review applied to a board’s decision to reject a value-maximizing transaction in favor of an allegedly self-interested transaction. According to the Court:

⁷ “In order for the board’s *defensive actions* to survive this enhanced judicial scrutiny, the board must establish: (1) that it had reasonable ground to believe that the hostile bid for control threatened corporate policy and effectiveness; and (2) that the defensive measures adopted were reasonable in relation to the threat posed.” *Chesapeake Corp. v. Shore*, 771 A.2d 293, 330 (Del. Ch. 2000) (quoting *Unocal*, 493 A.2d at 955; *Unitrin*, 651 A.2d at 1373).

Plaintiffs argue that Count I, fairly read, alleges that the defendants stood to lose the benefits of corporate control if the Company were sold, and that they therefore took defensive action by sabotaging the due diligence process, rejecting the First Place offer, and terminating the Sale Process.

The Court of Chancery properly refused to apply *Unocal* in this fashion. The premise of *Unocal* is “that the transaction was defensive.” Count I sounds in disloyalty, not improper defensive conduct. Count I does not allege any hostile takeover attempt or similar threatened external action from which it could reasonably be inferred that the defendants acted “defensively.”

Gantler, 965 A.2d at 705; *see id.* at n.23 (“Rejecting an acquisition offer, without more, is not ‘defensive action’ under *Unocal*.”). As in *Gantler*, Axcelis is not subject to a hostile tender offer, or any threatening action that could cause the Court reasonably to consider the Company’s action as “defensive.” SHI simply made unsolicited offers to acquire the Company, which the Company rejected.

In *TW Services, Inc. v. SWT Acquisition Corp.*, 1989 WL 20290 (Del. Ch. March 2, 1989), this Court held that *Unocal*’s proportionality test did not apply to the “board’s decision not to divert [a company] from its long term business plan in order to facilitate or propose an extraordinary transaction designed to maximize current shareholder value.” 1989 WL 20290, at *1.⁸ The *SWT* Court reasoned:

⁸ Even in the context of a tender offer, Delaware law places great power in the hands of a board to “just say no.” As recognized by the Delaware Supreme Court in *Paramount Communications, Inc. v. Time Inc.* (“*Time-Warner*”), 571 A.2d 1140 (Del. 1989):

Delaware confers the management of the corporate enterprise to the stockholders’ duly elected board representatives. The fiduciary duty to manage a corporate enterprise includes the selection of a time frame for achievement of corporate goals. That duty may not be delegated to the stockholders. Directors are not obligated

Should a court be required to review a decision not to pursue a merger, it would, in my opinion, ask itself two fundamental questions that the business judgment form of judicial review requires: did the board reach that decision in good faith pursuit of legitimate corporate interests, and did it do so advisedly? Supposing that the plaintiff failed to persuade the court that the answer to either question was in the negative, the court would not go on to exercise even the restrained level of substantive review that *Unocal* contemplates. It would not ask whether the decision could be justified as “reasonable” in relation to anything else, as it is to do when the decision is to preclude a tender offer.

The offer of SWT involves *both* a proposal to negotiate a merger and a conditional tender offer precluded by a poison pill. Insofar as it constitutes a proposal to negotiate a merger, I understand the law to permit the board to decline it, with no threat of judicial sanction providing it functions on the question in good faith pursuit of legitimate corporate interests and advisedly.

SWT, 1989 WL 20290, at *10) (emphasis added). Significantly, the Court’s conclusion that *Unocal* did not apply was also premised on the fact that the proposed transaction was subject to the execution of a merger agreement. Under Section 251 of the DGCL, a necessary prerequisite to a merger agreement is a resolution of the target board declaring the advisability of the proposed merger. See 8 Del. C. § 251(b) (“The board of directors of each corporation which desires to merge or consolidate shall adopt a resolution approving an agreement of merger or consolidation and declaring its advisability.”) As observed in *SWT*, when a merger proposal is subject to a target board’s Section 251 power, it is subject to traditional business judgment review and not heightened scrutiny under *Unocal*:

to abandon a deliberately conceived corporate plan for a short-term shareholder profit unless there is clearly no basis to sustain the corporate strategy.

Id. at 1154. See also *In re Pure Resources, Inc., Shareholders Lit.*, 808 A.2d 421, 440 (Del. Ch. 2002) (discussing potential reach of *Time-Warner*).

By conditioning the closing of its tender offer upon the execution of a merger agreement, SWT has implicated not simply the self-conferred power arising from the Stock Rights Plan, but the board's Section 251 power. I do not accept that SWT has waived the Agreement Condition. It has not done so. For whatever perceived advantage it sought, it has left that Condition in place in a modified form. By doing so, it continues to call upon the board to act under Section 251. The exercise of a board's power under that Section is, where there is no interested merger involved, subject to a traditional business judgment review, not the proportionality review of Unocal. Since SWT has chosen to proceed in a way that does require exercise of the TW board's Section 251 power, it cannot complain if the board's decision with respect to it is reviewed under the traditional business judgment approach.

SWT, 1989 WL 20290, at *11 (emphasis added). That is the case here.

Notwithstanding this well settled body of law, Plaintiff continues its desperate attempt to force the application of *Unocal* review. As if its argument somehow becomes meritorious by virtue of repetition, Plaintiff asserts yet again, in conclusory fashion: "Undoubtedly, the Board at least considered SHI's acquisition proposal as a threat to the Board member's positions on the Board." (POB at p. 17.) To reiterate, Plaintiff offers no evidence of any entrenchment motive. Plaintiff's argument is a non-starter because, as mentioned above and in Axcelis' Opening Brief (DOB at pp. 28-31), absent evidence of actionable self-interest, allegations of entrenchment motive based on the mere rejection of a merger proposal do not suggest any wrongdoing.

If Plaintiff's *Unocal* argument is further indulged (which it need not be), an additional fatal flaw is revealed. Plaintiff argues that the Directors could not reasonably have perceived a threat to Axcelis' corporate policy and effectiveness because "Axcelis shareholders considered a merger to be necessary to Axcelis' long-term success and SHI to be the 'most logical' acquirer." (POB at p. 17.) This reveals a misunderstanding of one of

the most basic tenets of Delaware corporate law -- the business and affairs of the corporation are run by its directors. Directors' discharge of this duty is dictated by their independent exercise of their fiduciary duties; directors are not merely agents obliged to effect the wishes of stockholders. As explained by this Court:

Directors are not thermometers, existing to register the ever-changing sentiments of stockholders. Directors are expected to use their own business judgment to advance the interests of the corporation and its stockholders. During their term in office, directors may take good faith actions that they believe will benefit stockholders, even if they realize stockholders do not agree with them.

In re Lear Corp. S'holder Litig., 967 A.2d 640, 655 (Del. Ch. 2008). *See id.* at 655-56 (explaining the irrelevance of the opinions of proxy advisory firms to directors' discharge of their fiduciary duties).

Because the business judgment rule applies to the Board's decision to reject the SHI Proposals, there is no need to engage in any type of proportionality analysis. Rather, it is incumbent on Plaintiff to show credible evidence of probable corporate wrongdoing of the type that would rebut the presumption of business judgment. A substantial majority of Axcelis' Opening Brief was dedicated to that analysis, and it will not be repeated here. Suffice it to say that nothing offered up by Plaintiff in its Opening Brief changes the conclusions compelled by Axcelis' Opening Brief. Plaintiff has failed to show any credible evidence of disloyalty that would suggest that the Board was not protected in its decision to decline the SHI Proposals. In the absence of such evidence, there is no basis to allow the fishing expedition sought by way of the Demand.

B. The Sale Of Axcelis' Stake In SEN Is Irrelevant And Is Not Defensive

1. The Record Demonstrates Clearly That The True, And Fully Disclosed, Purpose Of The SEN Sale Was To Satisfy Debt Obligations And To Obtain Dismissal Of A Lawsuit Regarding Nonpayment Of Those Debt Obligations

Axcelis' sale of its 50% interest in SEN to SHI is irrelevant. That transaction took place in March 2009, months after the Demand. It follows, of necessity, that the SEN sale had no bearing on the Demand or the relief sought therein. Regardless, the SEN sale constitutes no evidence of wrongdoing.

First and foremost, the SEN sale was not "defensive" because it was not implemented in response to a takeover threat. The record demonstrates this conclusively. Second, the record additionally demonstrates the true purpose of the sale -- to raise funds to satisfy overdue debt obligations and to secure the dismissal of pending litigation regarding that default. Consider the history laid out below.

SHI made the First Proposal on February 4, 2008. (*See* Stip., ¶ 9; Axcelis Press Release dated February 11, 2008, Stip., Ex. "E."). On February 25, 2008, the Company announced that the Board had rejected the First Proposal. (Stip., ¶ 13.) The Company also disclosed an investor presentation regarding the First Proposal and the reasons it was rejected. (Company Presentation dated February 25, 2008, filed as Ex. 99.1 to the Company's Form 8-K, filed with the SEC on February 25, 2008, Stip., Ex. "H.") The Company's February 25, 2008 press release also discussed the Board's rejection of the First Proposal and how it failed to recognize the Company's true value. (Stip., ¶ 13; *see* Press Release dated February 25, 2008, filed as Ex. 99.3 to the Company's Form 8-K, filed with the SEC on February 25, 2008, Stip., Ex. "H.")

SHI made the Second Proposal on March 10, 2008. (Stip., ¶ 15) On March 17, 2008, the Company announced that the Board had rejected the Second Proposal (Stip., ¶ 17), disclosed the reasons for that rejection (Press release dated March 17, 2008, filed as Ex. 99.2 to the Company's Form 8-K, filed with the SEC on March 17, 2008 at p. 1, Stip., Ex. "L"), and even further elaborated on those reasons in a subsequent letter to its stockholders. (Letter to Shareholders dated April 14, 2008, filed as Ex. 99.2 to the Company's Form 8-K, filed with the SEC on April 14, 2008 at pp. 2-3, Stip., Ex. "M.")

Months later, in June 2008, Axcelis and SHI commenced talks regarding SHI's bid to acquire Axcelis. (See Axcelis Press Release, dated June 6, 2008, Stip., Ex. "R.") In connection therewith, the parties entered into a confidentiality agreement with respect to such discussions. (*Id.*)

In June 2008, after entering into the above-referenced confidentiality agreement, representatives of Axcelis management provided data in response to SHI's due diligence requests and met several times in June and July with representatives from SHI to discuss SHI's due diligence requests. (Stip., ¶ 33.) After the above-referenced June and July 2008 meetings between representatives from Axcelis and SHI, SHI requested additional information from Axcelis in order to perform due diligence in formulating an acquisition proposal. (*Id.* at ¶ 34.) Axcelis agreed to provide additional information to SHI, and agreed to further meetings with SHI, in exchange for SHI agreeing to commit to a specific written schedule for submitting a revised acquisition proposal, which proposal was to include an indication of value and a draft acquisition agreement. (*Id.* at ¶ 35.) SHI agreed to submit a revised acquisition proposal to Axcelis by August 1, 2008. (*Id.* at ¶ 36.)

Thereafter, SHI requested from Axcelis an extension of the August 1, 2008 deadline. (*Id.* at ¶ 37.) Specifically, SHI requested an additional seven weeks to perform due diligence before deciding whether to submit a revised acquisition proposal and a five week period of confirmatory due diligence thereafter. (*Id.*) Based on a determination by the Board, Axcelis informed SHI that it could not agree to the extended deadline due to SHI's repeated failure to deliver a new acquisition proposal (despite its ability to have made two prior proposals) and the uncertainty that any bona fide proposal was forthcoming. (*Id.* at ¶ 38; Press Release dated September 15, 2008, filed as Ex. 99.1 to the Company's Form 8-K, filed with the SEC on September 15, 2008, Stip., Ex. "S".)

Instead, Axcelis granted SHI until the end of August 2008 to submit a revised acquisition proposal. (Stip., ¶ 39.) Axcelis also made an alternative proposal to SHI that SEN and Axcelis could become one company by SHI exchanging its SEN shares for Axcelis shares. (*Id.*) SHI decided not to submit a revised acquisition proposal to Axcelis. In a September 15, 2008 press release, Axcelis announced that on September 4, 2008, SHI informed Axcelis that it was placing discussions regarding the acquisition of Axcelis on "hold." (*Id.* at ¶ 40.)

Subsequent to the Demand and Axcelis' response thereto (*see* Stip., Exs. "V" and "W"), Axcelis sold its 50% stake in SEN to SHI in a transaction that closed on March 30, 2009. (Press Release dated March 30, 2009, filed as Exhibit 99.1 to the Company's Form 8-K, filed with the SEC on April 3, 2009, Stip., Exs. "Z" and "AA.") After fees and expenses, Axcelis received net proceeds from the sale of approximately \$122.3 million, a majority of which were needed to service overdue debt. (*Id.*) Indeed, in the months leading up to the date on which interest payments on that debt was due, the Company

disclosed that it was considering refinancing options. (See Press Release dated September 15, 2008, filed as Ex. 99.1 to the Company's Form 8-K, filed with the SEC on September 15, 2008, Stip., Ex. "S.") As explained more fully in its Annual Report for the year ended December 31, 2008, Axcelis' sale of its stake in SEN not only allowed the Company to discharge its debt, but also secured the obligee's agreement to dismiss pending litigation regarding non-payment of that debt. (Stip., Ex. "B" at p. 20) ("In February 2009, as an inducement to enter into the Share Purchase Agreement dated February 26, 2009...with [SHI] and [SEN], ... the Trustee confirmed in writing that judgment will not be entered in this litigation until after April 13, 2009, during which time it was contemplated that the closing under the Share Purchase Agreement would occur...A portion of the net proceeds was used in the direct repayment of all amounts due under the Indenture. As a result of the payment, the trustee for the Notes will withdraw litigation filed in connection with Axcelis' default on the Notes.")

Viewed in this factual context, it is clear that Axcelis' sale of its stake in SEN to SHI simply was not in response to the SHI Proposals. By the time of the sale in March 2009, the Proposals had long since been rejected, and no other proposals or "threats" from SHI were present (or even alleged to be present). Indeed, by the time the February 26, 2009 Share Purchase Agreement pursuant to which Axcelis would sell its interest in SEN to SHI was executed (see Stip., Ex. "Z"), the SHI Proposals had been off the table for approximately one year. While there was potential for a revised proposal based on Axcelis' agreement to engage in discussions with SHI, such a proposal never came to pass, and SHI announced that negotiations were over. (See Stip., ¶ 40.)

Axcelis was not defending against a threat of the type implicated by *Unocal* when it sold its stake in SEN to SHI. To the extent that Axcelis was defending itself against anything, it was defending itself from the consequences of a default under the Notes and the related action commenced by the Trustee. Axcelis sold its 50% interest in SEN to SHI in order to raise money to satisfy debt obligations and obtain the Trustee's dismissal of a pending lawsuit. This was fully disclosed, as was the fact that the SEN sale was agreed to only after ACLS had explored refinancing options in the third quarter of 2008.

2. Plaintiff's Remaining Arguments Are Factually And Legally Deficient

Because Axcelis' sale of its 50% interest in SEN to SHI was not a "defensive" action subject to *Unocal* review, Plaintiff's remaining arguments need not be addressed. They are nevertheless disposed of briefly.

First, as in its Complaint, Plaintiff suggests that the \$122 million received by Axcelis for its 50% interest in SEN was a "relatively paltry sum." (POB at p. 19.) Of course, Plaintiff neglects to indicate in relation to what this sum is purportedly paltry. In its Complaint, Plaintiff contended that \$122 constituted a fire sale price in relation to the implied equity value of SHI's Second Proposal. (Stip., Ex. "CC" at ¶ 33.) As pointed out in Axcelis' Opening Brief, Plaintiff offers no explanation as to the relationship that the value of Axcelis' interest in SEN bears to the value of Axcelis as a whole. (DOB at p. 35-36.) If, however, the relationship between \$122 million and the implied equity value of the Company is an appropriate measuring stick by which to gauge the appropriateness of what Axcelis received in exchange for its interest in SEN, then a different calculation must be considered. If one compares \$122 million to the implied equity value of Axcelis based on the Company's stock price as of the date of the Share Purchase Agreement, the \$122

million received by Axcelis for its share of SEN is anything but “paltry.” On the date of the Share Purchase Agreement, February 26, 2009, Axcelis’ closing stock price was \$0.35 per share of common stock. (Axcelis Historical Stock Price Report, attached hereto as Exhibit “4.”) As of December 31, 2008, Axcelis had 103,280,000 shares of common stock outstanding. (Stip., Ex. “B” at p. F-3.) This yields an implied equity value of \$36,148,000.⁹

Second, Plaintiff repeats its mantra that the Directors acted to entrench themselves when they rejected the SHI Proposals. (POB at p. 19.) Yet again, Plaintiff offers no explanation for what supposedly motivated the Directors to reject the SHI Proposals in favor of retaining their directorships. *See Pogostin v. Rice*, 480 A.2d 619, 627 (Del. 1984), overruled on other grounds by *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) (holding that mere allegation of desire to retain directorship is not evidence of entrenchment); *see also In re Paxson Comm’n. Corp. S’holders. Litig.*, 2001 WL 812028, at *8-9 (Del. Ch. July 12, 2001). The most Plaintiff does is offer the factually inaccurate statement that the sale of Axcelis’ stake in SEN, as opposed to a merger, would allow the Directors to keep their “jobs.” (POB at p. 19.) Six of the seven Axcelis Directors are outside directors not employed by the Company. (Ex. “2” at pp. 27-28.) They have no interest in retaining their “jobs.”

⁹ Despite these mathematical exercises, on the present record one cannot conclude anything about whether the SEN sale price was “paltry” or not by looking at either the SHI \$6.00 proposal in 2008 or the market value of Axcelis in February 2009. All anyone can say is that the value of 50% of SEN is obviously included in the total value of Axcelis at both those dates, so by definition the value of 50% of SEN is less than the value of Axcelis prior to the sale. What remains clear, though, is that Plaintiff has not offered any credible evidence to suggest that the sale price of Axcelis’ interest in SEN was so insufficient so as to suggest a breach of fiduciary duty. The only competent evidence in the record compels the conclusion that the Board complied with its fiduciary duties when it decided to sell the Company’s stake in SEN for the price, and at the time, it did.

Third, as to Plaintiff's accusation that the Directors were unwilling to negotiate in response to the SHI Proposals (POB at p. 19), that is contradicted by the record. While the Board did decline to engage in discussions to immediately sell Axcelis in response to the SHI Proposals, the Board was willing to engage SHI in private discussions upon the execution of a customary non-disclosure agreement. (See Press Release dated March 12, 2008 filed as Exhibit 99.2 to the Company's Form 8-K, filed with the SEC on March 17, 2008, Stip., Ex. "L.") In June 2008 that very thing happened and the parties engaged in numerous management meetings and Axcelis provided documents in response to SHI's due diligence requests. (Press Release dated September 15, 2008, filed as Exhibit 99.1 to the Company's Form 8-K, filed with the SEC on September 15, 2008, as Stip., Ex. "S.") Both of these facts belie Plaintiff's contention that Axcelis was unwilling to negotiate. Even prior to the First Proposal, representatives of SHI and Axcelis met regularly for years to discuss how to maximize the value of SEN. (See Press Release dated March 12, 2008 filed as Exhibit 99.2 to the Company's Form 8-K, filed with the SEC on March 17, 2008, Stip., Ex. "L.") During that same time period, Axcelis agreed to discuss the Company's market value to SHI subject to the execution of a non-disclosure agreement. (*Id.*) Of course, that is legally irrelevant because the Board was free to decline to negotiate a merger with SHI. See *Gantler*, 965 A.2d at 706; *SWT*, 1989 WL 20290, at * 10-12; *Kahn v. MSB Bancorp, Inc.*, 1998 WL 409355, at * 3 (Del. Ch. July 16, 2008).

Lastly, Plaintiff's contention that Axcelis did not give SHI sufficient time to formulate a revised proposal, like its contention that Axcelis was unwilling to negotiate, is contradicted by the record. Plaintiff's contentions are at best characterizations of fact, not facts themselves. What the record does reveal is that SHI had no difficulty making

proposals for Axcelis. It made the First Proposal in February 2008 (Stip., ¶ 9) and the Second Proposal in March 2008. (Stip., ¶ 15.) After SHI finally agreed to enter into a non-disclosure agreement and have some private discussions with Axcelis in June and July of 2008, it received even more information. (Stip., ¶ 33.) Still, SHI failed to come forward with a revised acquisition proposal, even after being given until the end of August 2008 to do so. (Stip., ¶¶ 35-40.) Against this backdrop, the fact that Axcelis would not give SHI almost another three months to deliver a revised written proposal -- SHI requested seven more weeks to decide whether it would make a proposal, and another five weeks of confirmatory due diligence after that -- can hardly be characterized as an unwillingness to negotiate.

CONCLUSION

For the foregoing reasons, Defendant respectfully requests that the Court conclude that Plaintiff has failed to show any credible evidence of probable wrongdoing to warrant an inspection of the Company's books and records for the purported purpose of investigating possible mismanagement or breach of fiduciary duty.

DATED: June 29, 2009

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CERTIFICATE OF SERVICE

I, John L. Reed, do hereby certify that on this 29th day of June 2009, a copy of the foregoing **DEFENDANT'S ANSWERING PRE-TRIAL BRIEF** was served on the following in the manner indicated:

LEXIS NEXIS FILE AND SERVE

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