IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

IN RE CAREMARK INTERNATIONAL,)
INC. DERIVATIVE LITIGATION) Cons. C.A. No. 13670
)

DEFENDANTS' OPENING BRIEF IN SUPPORT OF THEIR MOTION TO DISMISS PLAINTIFFS' SECOND AMENDED COMPLAINT

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NATURE AND STAGE OF THE PROCEEDINGS

The original complaint (the "Original Complaint") in this derivative action was filed on August 5, 1994 against nominal defendant Caremark International Inc. ("Caremark" or the "Company") and all of the thirteen directors who constitute the current board of directors of Caremark (the "Board" or the "Director Defendants"). (Dkt. 1). Five similar derivative complaints subsequently were filed against the defendants. The Court has consolidated the six actions for all purposes. (Dkt. 10, 17).

On September 14, 1994, defendants filed a motion and opening brief to dismiss the Original Complaint for failing to state a claim upon which relief can be granted and for failing to comply with the pleading requirements of Chancery Court Rule 23.1. (Dkt. 8, 9). Rather than file an answering brief, plaintiffs filed an amended complaint on October 28, 1994. (Dkt. 12; the "Amended Complaint").

On November 18, 1994, defendants filed a motion to dismiss the Amended Complaint for failing to state a claim upon which relief can be granted and for failing to comply with the pleading requirements of Chancery Court Rule 23.1. (Dkt. 13). As defendants were finalizing their opening brief in support of their motion to dismiss the Amended Complaint, defendants were informed by plaintiffs in early-December 1994 of their intention to once again amend their complaint. Plaintiffs filed their second amended complaint on December 30, 1994. (Dkt. 14; the "Second Amended Complaint").[1]

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[1]For the convenience of the Court, a copy of the Second Amended Complaint is attached hereto as Exhibit A. All references herein to the paragraphs of the Second Amended Complaint are identified as "2d Amend. Comp. ¶ __." Copies of all unreported opinions cited herein are included in alphabetical order in the compendium filed contemporaneously herewith.

On January 13, 1995, the defendants moved for the third time to dismiss the pending complaint on the grounds that plaintiffs have failed to state a claim upon which relief can be granted and failed to comply with the pleading requirements of Chancery Court Rule 23.1. (Dkt. 15). This is defendants' opening brief in support of their motion to dismiss the Second Amended Complaint.

PRELIMINARY STATEMENT

In their earlier opening brief to dismiss the Original Complaint, defendants demonstrated that plaintiffs had failed to justify their failure to make a pre-suit demand regarding the plaintiffs' central contention that the Director Defendants failed to oversee certain payment practices by Caremark. (Dkt. 8). Plaintiffs responded to defendants' dismissal arguments by making a host of conclusory allegations in the Amended Complaint, which are repeated in the Second Amended Complaint, to the effect that the Director Defendants "consciously direct[ed], encourag[ed] and/or conceal[ed] the unlawful kickback scheme and other illegal practices of Caremark ...." (2d Amend. Comp. ¶ 78(a)). Despite the filing of three complaints, plaintiffs have yet to state a valid cause of action or to provide any particularized factual support for their allegations against the Director Defendants. As discussed below, the Second Amended Complaint is subject to dismissal on two grounds.

First, in seeking solely to recover money damages from the Director Defendants, plaintiffs charge the Caremark directors with failing to exercise due care in overseeing the Company's payment practices. Plaintiffs, however, continuously fail to acknowledge the provision in the Caremark certificate of incorporation which, as authorized by 8 Del. C. § 102(b)(7), immunizes the Director Defendants, to the fullest extent permitted under Delaware law, from liability for monetary damages arising out of alleged breaches of fiduciary duty. Since the Caremark charter bars any recovery by plaintiffs against the Director Defendants in this action, the Second Amended Complaint should be dismissed in its entirety, pursuant to Chancery Court Rule 12(b)(6), for failure to state a claim upon which relief can be granted.

Second, the Second Amended Complaint also is subject to dismissal due to plaintiffs' failure to allege with the requisite particularity, as required by Chancery Court Rule 23.1, that a pre-suit demand is excused. Because plaintiffs do not identify or challenge any specific decision by the Board, the Supreme Court's decision in Rales v. Blasband, Del. Supr., 634 A.2d 927 (1993), dictates that the two-part Aronson test does not apply to plaintiffs' claim that a pre-suit demand would have been futile. Instead, Rales requires plaintiffs to meet the more demanding standard of demonstrating, through particularized allegations of fact, that a majority of the Director Defendants have a conflict of interest which precludes them from independently considering a demand by plaintiffs for corrective action. As demonstrated below, plaintiffs fail to meet this standard.

The allegations in the Second Amended Complaint are derived primarily from several magazine and newspaper articles addressing (i) a recent indictment of Caremark, three of its employees and two other individuals for allegedly violating federal Medicaid and Medicare rules governing payments to doctors; (ii) a separate indictment of a doctor who allegedly received illegal payments from an unnamed company; (iii) other federal investigative activity regarding payments to doctors by Caremark; and (iv) two civil suits involving Caremark. The Second Amended Complaint, however, concedes that not one of the thirteen members of the Board is even under investigation for any of the alleged wrongdoing. Moreover, the Second Amended Complaint omits any particularized factual basis for plaintiffs' repeated assertion that the Director Defendants "consciously" or "affirmatively" participated in the alleged wrongdoing. (2d Amend. Comp. ¶¶ 43, 66, 69(a), 75, 78(a), 79(a)). Nevertheless, without making a pre-suit demand upon the Board for remedial action, plaintiffs have sued the entire Board and asserted that the Director Defendants are completely disabled from managing Caremark's response to the alleged wrongs.

At best, the Second Amended Complaint asserts in conclusory terms three legally insufficient demand futility claims: (i) the Director Defendants participated in or approved of the alleged wrongs; (ii) the Director Defendants acquiesced to or failed to rectify the alleged wrongs, and (iii) the Director Defendants cannot be expected to sue themselves. These vague contentions clearly are inadequate under Delaware law to impute to any -- much less a majority -- of the Director Defendants a disqualifying personal interest or lack of independence. Since plaintiffs' demand futility contentions are insufficient under Rales to deprive the Board of its managerial function to control Caremark's response to the alleged wrongdoing, the Second Amended Complaint should be dismissed for failure to comply with the pleading requirements of Chancery Court Rule 23.1. Furthermore, since plaintiffs have failed in three efforts to state a claim which could withstand a motion to dismiss, the Second Amended Complaint should be dismissed with prejudice.

STATEMENT OF FACTS[2]

A. The Parties.

Plaintiffs allegedly are stockholders of Caremark. (2d Amend. Comp. ¶ 6).

Nominal defendant Caremark is a Delaware corporation based in Northbrook, Illinois. (2d Amend. Comp. ¶ 7). Following the incorporation of Caremark in August 1992 as a wholly owned subsidiary of Baxter International, Inc. ("Baxter"), Caremark became a public company on November 30, 1992 as the result of a spin-off from Baxter. (2d Amend. Comp. ¶ 11). In 1993, Caremark had revenues of approximately $1.78 billion based upon two principal business activities throughout the United States and overseas: (i) the provision of alternative site health care services (including home infusion therapy), and (ii) the provision of managed care services for prescription drug benefit programs and multi-physician group practices. (2d Amend. Comp. ¶¶ 7-10, 12). Approximately 14% of the Company's 1993 revenues were attributable to Medicare and Medicaid patients. (2d Amend. Comp. ¶¶ 5, 12).

The Director Defendants are the thirteen current members of Caremark's Board. (2d Amend. Comp. ¶¶ 13-14). Ten of the Director Defendants are outside directors who are not employees of Caremark. (See 2d Amend. Comp. ¶ 14). Defendant C.A. Lance Piccolo has been Chairman of the Board, Chief Executive Officer and a director of

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[2]For purposes of defendants' motion to dismiss, "all facts of the pleadings and reasonable inferences to be drawn therefrom are accepted as true, but neither inferences nor conclusions of fact unsupported by allegations of specific facts upon which the inferences for conclusions rest are accepted as true." Grobow v. Perot, Del. Supr., 539 A.2d 180, 187 n.6 (1988). For the record, defendants dispute vigorously the factual contentions and legal conclusions set forth in the Second Amended Complaint.

Caremark since 1992. (2d Amend. Comp. ¶ 13). Defendant James G. Connelly, III, has been President, Chief Operating Officer and a director of Caremark since 1992. (Id.). Defendant Thomas W. Hodson has been a Senior Vice President and Chief Financial Officer of Caremark since 1992. (Id.). (Defendants Piccolo, Connelly and Hodson collectively are referred to herein as the "Inside Directors"). Prior to the spin-off of Caremark from Baxter, the Inside Directors were senior employees of Baxter. (2d Amend. Comp. ¶ 13).

Defendants Raymond D. Oddi, Peter Whitington, Blaine J. Yarrington, J. Ira Harris, Ralph W. Muller, Kenneth N. Pontikes, Nancy G. Brinker, Vincent A. Calarco, Roger L. Headrick and Phillip B. Rooney (collectively, the "Outside Directors") are all directors of Caremark who are not employees of the Company. (2d Amend. Comp. ¶ 14). Although the Second Amended Complaint refers to Caremark's 1994 proxy statement (2d Amend. Comp. ¶ 16), plaintiffs conspicuously fail to identify the distinguished records of the ten Outside Directors:

J. Ira Harris: Senior Partner of Lazard Freres & Co. and a director of Manpower, Inc. and Brinker International, Inc.

Roger L. Headrick: President of Minnesota Viking Football Club, Inc. and a director of Crompton & Knowles Corporation; previously executive vice president and chief financial officer of The Pillsbury Company.

Ralph W. Muller: President of University of Chicago Hospital.

Raymond D. Oddi: Director of the First Prairie Series of Money Market and Mutual Funds; former senior vice president and chief financial officer of Baxter.

Kenneth N.Pontikes: Chairman of the board and president of Comdisco, Inc. and a director of Richardson Electronics, Ltd. and Pier 1 Imports, Inc.

Nancy G. Brinker: Chairman of Susan G. Komen Breast Cancer Foundation.

Vincent A. Calarco: Chairman of the board and president of Crompton & Knowles Corporation and a director of J.M. Huber Corporation.

Phillip B. Rooney: Chairman of the board and chief executive officer of Wheelabrator Technologies, Inc. and a director of numerous public companies.

Dr. Peter F. Whitington: Professor of Medicine at the University of Chicago School of Medicine.

Blaine J. Yarrington: Former executive vice president of Amoco Corporation.

(See Caremark 1994 proxy statement at 2-3, attached as Ex. B).[3] With the exception of Nancy G. Brinker, who has been a Caremark director since 1993, all of the Outside Directors have been directors of Caremark since 1992. (2d Amend. Comp. ¶ 14).

B. Plaintiffs' Allegations of Wrongdoing.

The Second Amended Complaint describes purported wrongdoing by Caremark, certain of its employees and several third parties. Notably, plaintiffs fail to allege with particularity that any of the Director Defendants were involved in, approved of or acquiesced to any of the alleged misconduct. Instead, as discussed below, plaintiffs rely solely upon conclusory and unsupported allegations in an attempt to impute to the

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[3]By referring to various documents in the Second Amended Complaint, plaintiffs have incorporated those documents into their pleading. Accordingly, the Director Defendants are entitled to support their motion to dismiss by referring to the contents of such documents without converting their application into a motion for summary judgment. See Ch. Ct. R. 10(c); Lewis v. Straetz, Del. Ch., C.A. No. 7859, Hartnett, V.C. (Feb. 12, 1986); In re Wheelabrator Technologies, Inc. Sh. Litig., Del. Ch., Cons. C.A. No. 11495, slip op. at 21-22, Jacobs, V.C. (Sept. 1, 1992); Cortec Indus., Inc. v. Sum Holding, L.P., 949 F.2d 42, 47-48 (2d Cir. 1991), cert. denied, Cortec Indus., Inc. v. Westinghouse Credit Corp., 112 S. Ct. 1561 (1992) (documents, particularly those which are publicly filed, may be considered by the court on a motion to dismiss if there was notice to the plaintiff of their contents and they were integral to the plaintiff's claim).

Director Defendants the alleged wrongdoing which, if it occurred at all, was carried out by various persons who are not members of the Caremark Board.

1. Allegations Of Wrongdoing By Caremark, Its Employees And Third Parties.

Plaintiffs allege that Caremark and certain of its employees violated federal laws by paying illegal kickbacks to physicians and hospitals to induce the referral of patients for services supplied by Caremark. (See 2d Amend. Comp. ¶¶ 27, 35-39, 42, 44-47, 54, 57-61, 65, 66, 68-71). Plaintiffs cite seven examples of such supposedly illegal conduct which are the predicates for their derivative claims against the Director Defendants. (2d Amend. Comp. ¶¶ 35-73).

a. The OIG Investigation.

Caremark was notified in August 1991 that the Office of the Inspector General of the U.S. Department of Health and Human Services ("OIG") and the U.S. Department of Justice had commenced an "investigation" to determine whether the Company's fee-for-service and other arrangements with physicians and hospitals violated federal laws prohibiting payment of remuneration to induce the prescription of the Company's infusion therapy services to Medicare and Medicaid beneficiaries (the "OIG Investigation"). (2d Amend. Comp. ¶¶ 21-22). Based upon the commencement of the OIG Investigation, plaintiffs allege that "at least as early as 1991, Caremark's senior management knew "that the Company's fees-for-services arrangements were likely illegal...." (2d Amend. Comp. ¶ 26); Plaintiffs further assert, on the basis of a Wall Street Journal article published on August 4, 1994 (the "August WSJ Article"), the day before plaintiffs filed their Original Complaint, that investigations are ongoing as to Caremark's alleged illegal practice of paying doctors throughout the United States to refer Medicare or Medicaid beneficiaries to the Company's home infusion program. (2d Amend. Comp. ¶¶ 49-50).

b. **<u>The Minneapolis Indictment</u>.**

Plaintiffs' principal allegations of wrongdoing center around an August 4, 1994 indictment by a federal grand jury in Minneapolis of Caremark, two Caremark vice presidents, a general manager of Caremark, a vice president of Genentech, Inc. and a physician (the "Minneapolis Indictment"). (2d Amend. Comp. ¶ 44). Plaintiffs assert that the Minneapolis Indictment was the result of an expansion of the OIG Investigation to determine whether Caremark was making improper payments to physicians for prescribing a human growth hormone manufactured by Genentech and distributed by the Company. (2d Amend. Comp. ¶ 42). The Minneapolis Indictment charges that, between 1986 and 1994, Caremark, three of its employees and the Genentech employee conspired to cause Caremark to pay $1.1 million in "kickbacks" to the physician to induce him to prescribe the growth hormone produced by Genentech. (2d Amend. Comp. ¶¶ 44, 46-48).

Plaintiffs also assert that the Minneapolis Indictment "implicates" the former president of Caremark, who is not named as a defendant in the Minneapolis Indictment, and that documents alleged to be "critical" to the payments were sent from Caremark's headquarters in Chicago. (2d Amend. Comp. ¶ 45). Although plaintiffs allege that the Minneapolis Indictment refers to two documents purportedly linking the alleged Caremark payments to patient referrals, the Second Amended Complaint does not assert that any of the Director Defendants authored, received or knew about the documents. (2d Amend.

Comp. ¶ 46). Plaintiffs also allege that in November 1994 the indictment against the physician was expanded and a user of the Genetech growth hormone filed a class action lawsuit against unidentified defendants based upon the contention that comparable treatments were less expensive than the Caremark program. (2d Amend. Comp. ¶ 52).

Based upon the statement in the Minneapolis Indictment that unidentified Caremark employees questioned the payments to the defendant doctor, plaintiffs conclude that unidentified members of Caremark's "senior management" supposedly were aware of the improper payments and refused to act. (2d Amend. Comp. ¶ 48). However, plaintiffs concede in the Second Amended Complaint that none of the Director Defendants were named as defendants or otherwise implicated in the Minneapolis Indictment. (See 2d Amend. Comp. ¶¶ 42-53). Nor do plaintiffs contend that any of the Director Defendants had any relationship with the doctor, the Genentech employee or the Caremark employees named in the Minneapolis Indictment. (Id.). Furthermore, plaintiffs do not contend that any of the Director Defendants are implicated in the ongoing investigations into Caremark's payment practices. (See 2d Amend. Comp. ¶ 49).

c. **The Ohio Investigation And Indictment.**

Again relying on the August WSJ Article, plaintiffs allege that federal authorities are investigating purported "payments" by Caremark to unidentified physicians in Columbus, Ohio (the "Ohio Investigation"). (See 2d Amend. Comp. ¶ 54).[4] The

[4]For purposes of this motion, the court may accept as true that the August WSJ Article contained a report on the Ohio Investigation and the investigation of the Minnesota Joint Venture, which is discussed below. However, as with the other articles cited by plaintiffs, the Court should not accept, even for purposes of this motion, the content of (continued...)

August WSJ Article refers to an asserted plan by investigators to interview 100-120 doctors who allegedly received large payments from Caremark, and to the prospect that federal authorities will pursue possible civil restitution claims. (Id.).

Plaintiffs also allege that, on September 20, 1994, a federal grand jury in Columbus, Ohio indicted a doctor on charges that he accepted $134,600 in kickbacks from a "home infusion company" for the referral of patients from 1991 through September 1994. (the "Ohio Indictment"; 2d Amend. Comp. ¶ 55). The Ohio Indictment does not name the company that allegedly paid the kickbacks. (2d Amend. Comp. ¶ 55). Nonetheless, based on articles in the Wall Street Journal and Financial World, plaintiffs allege that Caremark is the unnamed (and unindicted) company in the Ohio Indictment. (2d Amend. Comp. ¶¶ 55-57). Plaintiffs do not allege that any of the Director Defendants have been linked to the Ohio Investigation, were named as defendants in the Ohio Indictment or were even referred to in the Ohio Indictment. (See 2d Amend. Comp. ¶¶ 54-57).

d. The Minnesota Joint Venture Investigation.

Plaintiffs also refer, somewhat obliquely, to a reported "investigation" of a joint venture involving Caremark and the University of Minnesota Hospital (the "Minnesota Joint Venture") which resulted in the supposedly improper payment of $3 million over 2-1/2 years by Caremark to a non-profit corporation formed by doctors in the departments

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[4](...continued)
the newspaper report as true. For example, the Court should not accept as true the information unidentified "federal authorities" purportedly told a Wall Street Journal reporter regarding the Ohio Investigation. (See 2d Amend. Comp. ¶ 54). This double and triple hearsay does not constitute "well-pleaded factual allegations."

of surgery, medicine and pediatrics at the hospital. (See 2d Amend. Comp. ¶¶ 35-41, 50). Plaintiffs' allegations regarding the Minnesota Joint Venture are little more than a selective recitation of portions of two articles, published on October 18, 1993 in the Minneapolis Star Tribune, which raise questions about the legality of the payments. (2d Amend. Comp. ¶¶ 37-39). In any event, plaintiffs nowhere allege in the Second Amended Complaint that the Director Defendants were in any way involved in or even aware of the purported "scheme" involving the Minnesota Joint Venture. (See 2d Amend. Comp. ¶¶ 35-41). Moreover, despite the passage of more than one year between the publication of the articles and the filing of the Second Amended Complaint, plaintiffs do not assert that Caremark or its employees have been charged with wrongdoing in connection with the Minnesota Joint Venture.

e. **The Atlanta Lawsuit.**

Another of plaintiffs' allegations of wrongdoing by Caremark relates to certain allegedly improper practices by Caremark and several additional parties in Atlanta. Without referring to the source of their information, plaintiffs allege that physicians in the Atlanta area received improper fees for prescribing Caremark's services or medication to their patients. (2d Amend. Comp. ¶ 58). Plaintiffs allege that Caremark paid two of these doctors at least 25% of Caremark's billings to the patients. (2d Amend. Comp. ¶¶ 58-59). Plaintiffs further allege that Caremark had an arrangement with a pharmacy in Atlanta whereby the Company would bill directly the patients' insurance carriers. (2d Amend. Comp. ¶ 60). Plaintiffs accuse Caremark of overbilling the insurance carriers and making payments to the pharmacy and to the physicians who prescribed the medication. (Id.).

The Second Amended Complaint further alleges that an individual with AIDS filed a lawsuit in Atlanta asserting that Caremark and additional defendants improperly depleted his health insurance benefits (the "Atlanta Lawsuit"). (2d Amend. Comp. ¶ 61). The plaintiff in the Atlanta Lawsuit charged Caremark with developing a fraudulent scheme that it has implemented nationwide for illegal payments to physicians. (Id.). Plaintiffs in this case acknowledge that the Atlanta Lawsuit was settled on November 29, 1994. (2d Amend. Comp. ¶ 62). Plaintiffs allege that the plaintiff in the Atlanta Lawsuit is cooperating with the FBI and "other federal agencies," who allegedly are "looking into Caremark's payments to doctors in over a dozen states." (2d Amend. Comp. ¶ 63). Consistent with their other allegations, plaintiffs do not assert in the Second Amended Complaint that the Director Defendants participated in, approved of or had knowledge of any of the alleged wrongdoing in Atlanta or in any other location. (See 2d Amend. Comp. ¶¶ 58-63).

f. The Detroit Investigation.

Based upon an article appearing on November 11, 1994 in the Wall Street Journal (the "November WSJ Article"), plaintiffs refer to a federal investigation (the "Detroit Investigation") of Dr. Bruce A. Margulis ("Margulis"), who allegedly earned $11.5 million between 1988 and 1992 in a joint venture with Caremark with headquarters in Detroit. (2d Amend. Comp. ¶¶ 65-72). According to the article, the federal government is investigating whether Margulis authorized the payment by the joint venture of improper fees to doctors for patient referrals. (2d Amend. Comp. ¶¶ 65, 68, 71). Plaintiffs assert that "Caremark's senior management [were] well aware of Margulis' activities." (2d Amend. Comp. ¶ 67). Plaintiffs base this allegation on alleged social ties between Margulis and a former Caremark executive vice president, Sheldon A. Asher, and the comment of a former Caremark employee as to her "impression" that Asher approved of Margulis' activities. (Id.).

g. The FTC Investigation.

Finally, plaintiffs allege in a single paragraph that the Federal Trade Commission ("FTC") is expanding its inquiry into Caremark's contractual alliances with drug companies (the "FTC Investigation"). (2d Amend. Comp. ¶ 73). The FTC apparently is seeking to determine whether drug manufacturers (including Pfizer, Bristol-Myers, Squibb and Rhone-Poulenc Rorer) and managed care companies (such as Caremark) are engaged in anti-competitive practices. (Id.). Plaintiffs do not identify any alleged wrongdoing by Caremark which pertains to the FTC Investigation. Understandably, therefore, the Second Amended Complaint fails to assert any supposed involvement, knowledge, approval or acquiescence of any of the Director Defendants in any matter relating to the FTC Investigation. (See 2d Amend. Comp. ¶ 73).

2. Allegations Of Wrongdoing By The Director Defendants.

Having alleged wrongdoing by a small number of Caremark employees and third parties, plaintiffs unsuccessfully attempt to connect the Director Defendants to these actions by making three conclusory allegations: (i) that the Director Defendants had actual knowledge of the illegal practices, (ii) that the Director Defendants made "affirmative" decisions to approve the challenged practices or to decline to pursue remedial measures, and (iii) that the Director Defendants acquiesced to the illegal practices and otherwise failed to comply with their duty to oversee the Company's activities. As discussed below, all of these charges are based on totally unsupported conclusions or factual assumptions.

Plaintiffs initially assert that, in view of the August 1991 notification to Caremark of the OIG Investigation, subsequent public statements by the Company's officers regarding the OIG Investigation, and the Company's public filings with the SEC during 1992-1994 regarding the potentially adverse effect of a possible finding that the Company violated federal regulations regarding payments for patient referrals (2d Amend. Comp. ¶¶ 21-32), the Director Defendants were "fully aware" of Caremark's "illegal activities." (2d Amend. Comp. ¶ 33; <u>see</u> <u>also</u> 2d Amend. Comp. ¶¶ 27, 79(a)-(b)). However, there are no particularized facts in the Second Amended Complaint to support plaintiffs' conclusory charge. Instead, plaintiffs merely have <u>assumed</u> that the Director Defendants knew that Caremark's practices were illegal. This assumption is unsubstantiated by the conclusory factual allegations in the Second Amended Complaint.

Plaintiffs' second charge is that the Director Defendants "consciously permitted the waste of corporate assets and consciously failed to take action to recover corporate assets diverted to the kickback scheme" in order to inflate Caremark's revenues and market share for home infusion services. (2d Amend. Comp. ¶ 75; <u>see</u> <u>also</u> 2d Amend. Comp. ¶¶ 2, 78(a), (c)-(f), 79(a)-(d)). While these assertions insinuate some type of affirmative participation in the alleged wrongdoing by the Director Defendants, the

Second Amended Complaint does not identify any specific decisions or actions by any of the Director Defendants to support these allegations. Despite the considerable attention by the media to the investigations, indictments and lawsuits relating to Caremark, plaintiffs have failed to identify in the Second Amended Complaint even a single decision by the Board regarding any of the supposed misconduct.

Plaintiffs' third attack on the Director Defendants is that, in view of the Ohio Indictment, the Minneapolis Indictment, the Atlanta Lawsuit and the reports of government investigations into Caremark's payment practices, the Director Defendants supposedly "allowed" Caremark to violate certain laws, failed to initiate corrective procedures, failed to adequately supervise Caremark's employees and failed to take action against the individuals responsible for the wrongdoing. (2d Amend. Comp. ¶¶ 34, 43; see also 2d Amend. Comp. ¶¶ 2, 75, 78(c)-(g), 79(a)-(b), (d)). In making these "lack of oversight" charges, plaintiffs ignore the undeniable fact that none of the proceedings set forth in the Second Amended Complaint have resulted in a finding of improper conduct by Caremark or any of its directors, officers or employees. Plaintiffs simply have not set forth the requisite particularized allegations of fact which support the bare assertion that the Director Defendants acquiesced in illegal activities.

Plaintiffs assert that the acts and omissions of the Director Defendants have resulted in the waste of Caremark assets, caused the risk of significant losses to Caremark, diminished the Company's goodwill and business opportunities, and caused Caremark to suffer an indeterminable amount of damages due to potential legal costs, criminal penalties, civil restitution claims and lost business. (2d Amend. Comp. ¶¶ 4-5, 80-88).

Plaintiffs concede that their claims against the Director Defendants are derivative in nature. (2d Amend. Comp. ¶¶ 1, 2, 79). Nevertheless, plaintiffs commenced this action without making a pre-litigation demand on the Caremark board. (2d Amend. Comp. ¶ 79). For the reasons set forth below, plaintiffs' allegations are insufficient to: state a claim upon which relief can be granted under Chancery Court Rule 12(b)(6) or to excuse a pre-suit demand under Chancery Court Rule 23.1. Therefore, the Second Amended Complaint should be dismissed.

ARGUMENT

I. BECAUSE THE CAREMARK CHARTER IMMUNIZES THE DIRECTOR DEFENDANTS FROM LIABILITY FOR DUE CARE CLAIMS, THE SECOND AMENDED COMPLAINT MUST BE DISMISSED.

Since Caremark's incorporation on August 7, 1992, Article EIGHTH of the Company's certificate of incorporation has provided, in pertinent part, as follows:

> To the fullest extent permitted by the General Corporation Law of Delaware as the same exists or may hereafter be amended, a director of the corporation shall not be liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director.

(the "Charter Provision"; attached as Ex. C).[5] Therefore, during the entire period in which the Director Defendants have served as directors of Caremark, the Charter Provision has afforded them the protections authorized by 8 Del. C. § 102(b)(7) ("Section 102(b)(7)").[6] A charter provision adopted pursuant to Section 102(b)(7) eliminates the monetary liability of directors for all breaches of fiduciary duty not expressly excepted

[5]The Court may properly take judicial notice of Caremark's certificate of incorporation without defendants' motion to dismiss being converted into a motion for summary judgment. Wheelabrator, slip op. at 21-22.

[6]Section 102(b)(7) provides that a corporation may include in its certificate of incorporation:

> A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under §174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit.

for coverage, including the duties of care and disclosure. Arnold v. Society for Savings Bancorp, Del. Supr., No. 473, 1993, slip op. at 44, Veasey, C.J. (Dec. 28, 1994). Accord John Hancock Capital Growth Management, Inc. v. Aris Corp., Del. Ch., C.A. No. 9920, slip op. at 4, Jacobs, V.C. (Aug. 24, 1990) (Section 102(b)(7) charter provision forecloses due care claims against directors); Wheelabrator, slip op. at 22 (Section 102(b)(7) charter provision bars plaintiffs' due care claims for money damages); Rothenberg v. Santa Fe Pacific Corp., Del. Ch., C.A. No. 11749, slip op. at 7-10, Jacobs, V.C. (May 18, 1992) (due care claims barred by Section 102(b)(7) charter provision); Leslie v. Telephonics Office Technologies, Inc., Del. Ch., C.A. No. 13045, slip op. at 23, Allen, C. (Dec. 30, 1993) ("As a theoretical matter, any claim for compensatory damages stemming from a duty of care violation by the defendants would be barred by the § 102(b)(7) provision").

Since plaintiffs plead, at best, violations of the Director Defendants' duty of care and seek as relief only money damages from the Director Defendants, the two causes of action set forth in the Second Amended Complaint must be dismissed in view of the claim preclusive effect of the Charter Provision. (See 2d Amend. Comp. ¶¶ 80-88). Plaintiffs' second cause of action expressly asserts a claim that the Director Defendants were grossly negligent and purportedly breached their duties of care. (2d Amend. Comp. ¶ 86). Recovery on plaintiffs' second cause of action clearly is barred by the Charter Provision.

Perhaps recognizing the bar of the Charter Provision, plaintiffs' first cause of action asserts, albeit in a vague and conclusory way, that the Director Defendants failed "to exercise due care and loyalty in the performance of their duties". (2d Amend. Comp.

¶ 82). The core allegations of plaintiffs' first cause of action involve acts or omissions which constitute waste of corporate assets, mismanagement and gross negligence (2d Amend. Comp. ¶ 81) -- all of which are barred by the Charter Provision. By words alone, however, plaintiffs attempt to recharacterize their duty of care/oversight claims as amounting to violations of the Director Defendants' fiduciary duty "to act in the best interest of the Corporation and its shareholders." (2d Amend. Comp. ¶ 81). Plaintiffs' single conclusory incantation of the word "loyalty" and their feeble suggestion as to the Director Defendants' improper "interests," like their unsubstantiated claims of "affirmative" and "knowing" conduct, are insufficient to circumvent the bar of the Charter Provision.

While all well-pleaded allegations are accepted as true on a motion to dismiss, "such a motion does not concede pleaded conclusions of law or fact where there are no allegations of specific facts which would support such conclusion." Weinberger v. UOP, Inc., Del. Ch., 409 A.2d 1262, 1264 (1979). No particularized allegation in the Second Amended Complaint suggests that the Director Defendants breached their duty of loyalty by securing an improper personal profit, engaging in a self-dealing transaction, or pursuing their own interests or some other objective which is inconsistent with the well-being of Caremark or its stockholders.[7] Moreover, plaintiffs' bare statement at the end of the Second Amended Complaint that the Director Defendants supposedly acted in a

[7]Indeed, plaintiffs' only specific statement regarding the Director Defendants' motivation -- the desire to maintain Caremark's market share in the infusion business (2d Amend. Comp. ¶ 43) -- contradicts the notion that the Director Defendants acted with conflicting loyalties.

self-interested or disloyal fashion is fundamentally inconsistent with their central allegation that the Director Defendants negligently failed to oversee the activities of certain Caremark employees. (See 2d Amend. Comp. ¶ 78(c)).

In similar circumstances, this Court has affirmed the bar afforded by a Section 102(b)(7) charter provision. In In re Dataproducts Corp. Sh. Litig., Del. Ch., C.A. No. 11164, Jacobs, V.C. (Aug. 22, 1991), plaintiffs attempted to evade the Section 102(b)(7) provision in the Dataproducts charter by alleging that the directors' alleged abdication of their oversight function and acquiescence to supposed misconduct by management involved acts or omissions which were not in good faith and constituted intentional misconduct. Slip op. at 10-11. The Court found that plaintiffs' "abdication" claims were "equally consistent with director gross negligence as with conduct that was intentional or in bad faith...." Slip op. at 11. Since the Section 102(b)(7) provision in the Dataproducts charter barred director liability for due care claims, the Court granted defendants' motion to dismiss the "abdication" and "acquiescence" claims against the director defendants. Slip op. at 11-12.

Similarly, in Boeing Co. v. Shrontz, Del. Ch., C.A. No. 11273, Berger, V.C. (Apr. 20, 1992), plaintiffs alleged that Boeing's directors failed to prevent and/or correct a pattern of misconduct by officers and employees in connection with various government contracts. The misconduct by Boeing and its employees involved criminal conduct to evade government security regulations, overcharging on numerous defense contracts and deliberately submitting a low bid on a contract which would cause the company to lose $385 million on the deal. The Court found that plaintiffs' "failure of oversight" claims could be asserted, if at all, only as to the wrongs alleged to have occurred prior to Boeing's adoption a Section 102(b)(7) charter provision. Slip op. at 12. Accord Bell Atlantic Corp. v. Bolger, 2 F.3d 1304, 1312-13 (3d Cir. 1993) (Section 102(b)(7) charter provision bars director liability for failure to exercise proper oversight of sales personnel whose actions resulted in $40 million settlement of consumer fraud claims).

As in Dataproducts, Boeing and Bell Atlantic, plaintiffs' "lack of oversight" allegations in the Second Amended Complaint are barred by Caremark's Charter Provision. The Second Amended Complaint asserts, at most, breaches of the duty of care based on the purported failure of the Director Defendants to oversee the actions of certain Caremark employees. Although plaintiffs charge the Director Defendants with "consciously directing, encouraging and/or concealing the unlawful kickback scheme and other illegal practices of Caremark ...." (2d Amend. Comp. ¶ 78(a)), there simply are no allegations of specific fact in the Second Amended Complaint which support their conclusions. See, supra, pp. 9-18. Since plaintiffs only seek money damages in this case, the Charter Provision dictates that none of their due care claims are cognizable as a matter of law and, therefore, the Second Amended Complaint should be dismissed in its entirety.

II. THE SECOND AMENDED COMPLAINT MUST BE DISMISSED FOR FAILURE TO COMPLY WITH RULE 23.1.

A. Plaintiffs' Demand Excusal Allegations Must Be Evaluated Under Rales.

In recognition of the "cardinal precept of the General Corporation Law of the State of Delaware ... that directors, rather than shareholders, manage the business and affairs of the corporation," Aronson v. Lewis, Del. Supr., 473 A.2d 805, 811 (1984), Chancery Court Rule 23.1 requires plaintiffs to allege in a derivative complaint, with particularity, either that they have demanded that the board of directors pursue the corporate claim and the demand has been wrongfully refused, or that the making of such a demand is excused because the directors are incapable of making an impartial decision regarding the litigation. Ch. Ct. R. 23.1. As our Supreme Court has noted:

> The purpose of pre-suit demand is to assure that the stockholder affords the corporation the opportunity to address an alleged wrong without litigation, to decide whether to invest the resources of the corporation in litigation, and to control any litigation which does occur.

Spiegel v. Buntrock, Del. Supr., 571 A.2d 767, 773 (1990); accord Kaplan v. Peat, Marwick, Mitchell & Co., Del. Supr., 540 A.2d 726, 730 (1988). Thus, "the demand requirement ... exists at the threshold, first to insure that a stockholder exhausts his intracorporate remedies, and then to provide a safeguard against strike suits." Aronson, 473 A.2d at 811-12 (citations and footnotes omitted).[8]

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[8] As this Court is well aware, "[t]he demand requirement is not a 'mere formalit[y] of litigation,' but rather an important 'stricture[] of substantive law.'" Levine v. Smith, Del. Supr., 591 A.2d 194, 207 (1991) (citation omitted). By filing the Second Amended Complaint without making a pre-suit demand, plaintiffs are attempting to deprive the corporation (and its directors) of the right and option to redress alleged wrongs. See (continued...)

In a traditional derivative action challenging the propriety of an affirmative decision by directors, a pre-suit demand will be excused if the plaintiff alleges particularized facts creating a reasonable doubt that (i) the directors are disinterested or independent; or (ii) the challenged transaction was otherwise the product of a valid exercise of business judgment. Aronson, 473 A.2d at 814.[9] Although Aronson correctly stresses the importance of the demand requirement (and deference to board decisions regarding the conduct of derivative litigation), the Supreme Court has held that the two-part test for demand excusal articulated in Aronson does not apply in a case where, as here, the derivative complaint does not challenge a specific business decision. Rales, 634 A.2d at 933-34. The second prong of the Aronson demand futility test addresses whether

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[8](...continued)
Pogostin v. Rice, Del. Supr., 480 A.2d 619, 624 (1984). Decisions whether to take action to assert corporate rights and, if so, what action to take are the responsibility of the board of directors, which governs the corporation on behalf of all the shareholders. See, e.g., Levine, 591 A.2d at 203. The demand requirement, as a fundamental element of this system of corporate governance, is imposed to ensure that in the first instance the board of directors, rather than an individual shareholder or his counsel, makes such decisions after having been given a full and fair opportunity to investigate and to decide what, if any, action should be taken. See, e.g., Daily Income Fund, Inc. v. Fox, 464 U.S. 523, 530 (1984) (the derivative action "could, if unrestrained, undermine the basic principle of corporate governance that the decisions of a corporation -- including the decision to initiate litigation -- should be made by the board of directors").

[9]For purposes of their motion to dismiss the Second Amended Complaint under Chancery Court Rule 23.1, defendants acknowledge that the Court must accept as true the well-pleaded factual allegations of the Second Amended Complaint. See, e.g., Rales, 634 A.2d at 931. Conclusory factual and legal allegations, however, are not accepted as true. Id. As the Supreme Court confirmed in Grobow, 539 A.2d at 187, "[a] trial court need not blindly accept as true all allegations, nor must it draw all inferences from them in plaintiffs' favor unless they are reasonable inferences." Thus, the pleading requirement of Chancery Court Rule 23.1 is "an exception to the general notice pleading standard" and a plaintiff's pleading burden is "more onerous than that required to withstand" an ordinary motion to dismiss. Levine, 591 A.2d at 207.

directors have acted in conformity with the business judgment rule in approving a challenged transaction. Rales, 634 A.2d at 933. Accordingly, the analysis under the second-prong of Aronson logically is inapplicable in situations "where the board that would be considering the demand did not make a business decision which is being challenged in the derivative suit." Id. at 933-34.

In Rales, the Supreme Court described three principal scenarios in which the Aronson test is inapplicable to determine whether a pre-suit demand would be futile:

> (1) where a business decision was made by the board of a company, but a majority of the directors making the decision have been replaced; (2) where the subject of the derivative suit is not a business decision of the board; and (3) where, as here, the decision being challenged was made by the board of a different corporation.

Rales, 634 A.2d at 934 (emphasis supplied; footnotes omitted).

The eighty-eight paragraphs of the Second Amended Complaint fail to identify even a single decision by the Caremark Board. The only allegations even remotely approaching any claim of a business decision are plaintiffs' opaque suggestions that the Director Defendants "affirmatively facilitated" the alleged wrongdoing. (2d Amend. Comp. ¶ 79(a)). Plaintiffs plead no factual support (particularized or otherwise) for these conclusory assertions. See, supra, pp. 9-18. Putting aside plaintiffs' conclusory and ineffective attempts to create a business decision where none exists, the Second Amended Complaint asserts only that the Defendant Directors knew of the alleged wrongs and failed to take corrective actions. (See, e.g., 2d Amend. Comp. ¶¶ 33, 43, 75, 79(a)-(b), 79(d)). Accordingly, the demand excusal allegations of the Second Amended Complaint are not subject to the two-part inquiry under Aronson and, instead, must be reviewed under the narrower test set forth in Rales. See Rales, 634 A.2d at 934 n. 9 (confirming that Aronson does not apply to an action alleging that the directors failed to oversee subordinates).

When plaintiffs in a derivative action assert director liability due to the failure to make a decision or to take some action, Rales dictates that a pre-suit demand will be excused as futile only if "the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand." Rales, 634 A.2d at 934. The Supreme Court emphasized in Rales that:

> where directors are sued derivatively because they have failed to do something (such as a failure to oversee subordinates), demand should not be excused automatically in the absence of allegations demonstrating why the Board is incapable of considering a demand. Indeed, requiring demand in such circumstances is consistent with the board's managerial prerogatives because it permits the board to have the opportunity to take action where it has not previously considered doing so.

Id. at 934 n. 9. Thus, in order to excuse demand in this case, plaintiffs bear the burden of alleging particularized facts showing that a majority of the Director Defendants have a disqualifying personal interest or lack of independence. Id. at 937. See also Pogostin, 480 A.2d at 624, 626 (the first part of the Aronson test for demand futility requires plaintiff to demonstrate the disqualifying interests or lack of independence of a majority of the directors "at the time the complaint was filed").[10]

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[10]The Rales test essentially requires the application of the first prong of the Aronson test to determine whether the board "could have considered a [pre-suit] demand without (continued...)

As demonstrated below, plaintiffs' conclusory and generalized allegations of demand futility in the Second Amended Complaint fail to satisfy the particularized pleading requirements of Chancery Court Rule 23.1, and cannot serve to deprive the Caremark Board of its fundamental prerogative to manage the Company's response to the legal proceedings set forth in the Second Amended Complaint.

B. Plaintiffs Fail To Allege Particularized Facts Creating A Reasonable Doubt That The Director Defendants Have A Disqualifying Interest Regarding The Matters Alleged In The Second Amended Complaint.

Plaintiffs devote only four subparagraphs in the Second Amended Complaint to explain the three reasons for their failure to make a pre-suit demand on the Caremark Board. (See 2d Amend. Comp. ¶ 79(a)-(d)). These allegations fail to create any doubt that the Caremark Board could consider the allegations in the Second Amended Complaint "free of personal financial interest and improper extraneous influences." Rales, 634 A.2d at 935 (footnote omitted).

1. Plaintiffs Allege That The Director Defendants "Affirmatively Facilitated" Or Approved Of The Alleged Wrongs.

In the Second Amended Complaint, plaintiffs assert in two subparagraphs essentially the same excuse for failing to make a pre-suit demand:

> (a) The Director Defendants, since the Company's spin-off as a public company in November 1992, have known of the wrongs forming the basis for the claims alleged herein and the materiality of such wrongs

[10](...continued)
being affected by improper influences." See Rales, 634 A.2d at 935 n. 12 (citing Aronson). Accordingly, as in Rales, opinions applying the first prong of the Aronson test to a particular set of facts are cited herein as instructive precedent. See Rales, 634 A.2d at 936-37.

> to the Company's financial well-being and reputation. The Director Defendants have affirmatively facilitated the continuation of the misconduct detailed herein, unreasonably and recklessly choosing to put at risk Caremark's resources and ability to conduct its business rather than discontinue the unlawful practices and schemes which have led to the numerous investigations, criminal indictments and civil lawsuits described herein.
>
> * * *
>
> (d) The Director Defendants were intimately and personally involved in approving, fostering and/or countenancing the kickback and overbilling schemes which are the subject of the investigations, criminal indictments and civil lawsuits described herein. As a consequence, the Director Defendants are personally and acutely interested in suppressing full disclosure of their wrongs and are thereby disabled from addressing a pre-suit demand with impartiality and independence.

(2d Amend. Comp. ¶ 79(a) & (d); emphasis added).

Stripped of its excess language, plaintiffs here assert as a justification for excusing demand that the Director Defendants should be disabled from considering allegedly improper patient referral payments to doctors by Caremark because they "affirmatively facilitated" or "approv[ed], foster[ed] and/or countenanc[ed]" the supposedly illegal activities. (Id.). This is nothing more than an artful reformulation of the shopworn assertion that directors are "interested" when they approve of or participate in the challenged activity. As the Supreme Court, this Court and several other courts have held repeatedly, such generalized and conclusory allegations of director approval or participation are wholly insufficient to excuse demand.[11]

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[11]See, e.g., Aronson, 473 A.2d at 817 ("mere directorial approval of a transaction, absent particularized facts supporting a breach of fiduciary duty claim, or otherwise establishing the lack of independence or disinterestedness of a majority of the directors, is insufficient to excuse demand"); Levine, 591 A.2d at 207-208; Pogostin, 480 A.2d at (continued...)

Similar allegations of demand futility were addressed in Richardson v. Graves, Del. Ch., C.A. No. 6617, Longobardi, V.C. (June 17, 1983), where the corporation, three of its directors and a vice president had been indicted by a federal grand jury and pled nolo contendere to antitrust violations, wire fraud and racketeering. Richardson, slip op. at 1-2. Plaintiff argued that demand was futile because the balance of the directors "'authorized, acquiesced in and/or ratified'" the unlawful conduct. Slip op. at 2. In a holding squarely applicable here, the Court rejected that argument on the ground that a majority of the board was not implicated in the indictments or the lawsuits filed in reaction to the indictments. Slip op. at 7-8. The Court also questioned "the use of the

[11](...continued)
625 ("we note that plaintiffs' bootstrap allegations of futility, based on claims of directorial participation in and liability for the wrongs alleged, coupled with a reluctance by directors to sue themselves, were laid to rest in Aronson"); Grobow v. Perot, Del. Ch., 526 A.2d 914, 924 (1987), aff'd, Del. Supr., 539 A.2d 180 (1988) ("It is now well-settled that an allegation that a majority of directors approved, participated, or acquiesced in a challenged transaction will not, in and of itself, establish demand futility"); Emerald Partners v. Berlin, Del. Ch., C.A. No. 9700, slip op. at 15, Hartnett, V.C. (Dec. 23, 1993) ("mere allegation of participation in the approval of a challenged transaction is insufficient to excuse a pre-suit demand"); Haber v. Bell, Del. Ch., 465 A.2d 353, 359 (1983) ("[a]llegations that the members of a Board of Directors 'approved or acquiesced in' the action which plaintiffs attack are ... not sufficient to excuse a demand for redress before suit"); Kaufman v. Beal, Del. Ch., Cons. C.A. Nos. 6485, 6526, slip op. at 9, Hartnett, V.C. (Feb. 25, 1983) ("mere allegations of approval of a challenged transaction or participation by directors in alleged wrongful conduct, absent a showing of self interest or bias by a majority of the Board, have been held to be insufficient to excuse a demand"); Good v. Getty Oil Co., Del. Ch., 514 A.2d 1104, 1107-09 (1986) (rejecting an allegation that "the Texaco directors knowingly participated in and knew of the violations of the law" as insufficient to excuse demand because "the manner of participation and the nature and extent of the knowledge possessed by the members of the Board of Directors are not particularized"); Kaufman v. Belmont, Del. Ch., 479 A.2d 282, 288 (1984).

terms 'authorized, acquiesced in and ratified,'" stating that such terms "are obviously conclusory." Slip op. at 8. As the Court stated, in order to excuse demand:

> [N]otice pleading is not enough. Generalities, artistically ambiguous, all-encompassing conclusory allegations are not enough. What is required are pleadings that are specific and, if conclusory, supported by sufficient factual allegations that corroborate the conclusion and support the proposition that demand is futile.

Slip op. at 6 (citation omitted).

Plaintiffs' artistically ambiguous "affirmative facilitation" allegation also is similar to allegations rejected in Allison v. General Motors Corp., 604 F. Supp. 1106 (D. Del.), aff'd, 782 F.2d 1026 (3d Cir. 1985) (applying Delaware law). Plaintiff argued in Allison that a pre-suit demand was excused because the individual defendants, "as members of the GM Board, participated in the underlying wrongs, i.e., the decision to manufacture and sell X-cars with a known brake deficiency and ... to submit false and incorrect information to the government and the public." Allison, 604 F. Supp at 1114. In rejecting this allegation, the District Court stated:

> [U]nless a plaintiff makes sufficiently particular allegations of participation, self-dealing, bias, bad faith, or corrupt motive, failure to make a demand will not be excused. Plaintiff has not made particular allegations of this nature. The mere fact that plaintiff names members of the Board of Directors as defendants or even makes conclusory allegations of director wrongdoing does not suffice to excuse demand.

Id. (citations omitted).

As in Richardson and Allison, the Second Amended Complaint is completely devoid of any specific factual allegation which substantiates plaintiffs' conclusions that the Director Defendants "affirmatively facilitated" or "approv[ed], foster[ed] and/or countenanc[ed]" the illegal activities by Caremark. See, supra, pp. 9-18. In fact, as in

Richardson, plaintiffs' descriptions of the OIG Investigation, the Minneapolis Indictment, the Ohio, Detroit and FTC Investigations, the Atlanta Lawsuit and the Minnesota Joint Venture concede that none of the Director Defendants has been named, implicated, charged, indicted or even investigated. Plaintiffs' allegations that the Director Defendants approved of or participated in the alleged wrongdoing are completely conclusory and, therefore, insufficient to excuse demand.[12]

2. Plaintiffs Assert That The Director Defendants Permitted The Underlying Wrongs To Continue And Failed To Take Remedial Actions.

Plaintiffs next allege that demand should be excused because:

> (b) The Director Defendants recklessly disregarded their fiduciary obligations in failing to exercise skill, diligence and prudent business judgment. They have permitted the systemic wrongs alleged herein to continue unchecked although they have long had knowledge of those wrongs and, in fact, at least since the 1992 Form 10-K, have admitted their knowledge of these wrongs and have represented through the Company's officers that the misconduct would be corrected.

(2d Amend. Comp. ¶ 79(b); emphasis added). Unfortunately for plaintiffs, numerous cases confirm that such allegations of knowledge and failure to take remedial action do not excuse pre-suit demand.

[12]Plaintiffs also state in conclusory fashion that the Director Defendants cannot be expected to act with "independence" in respect to a demand regarding the alleged underlying wrongs. (2d Amend. Comp. ¶ 79(d); emphasis added). To establish lack of independence, plaintiffs must show that the Director Defendants are beholden to another person or so under that person's influence that the directors' discretion would be sterilized. Rales, 634 A.2d at 936. The Second Amended Complaint, however, does not even begin to suggest that any member of the Caremark Board -- much less a majority of the Director Defendants -- is incapable of acting independently of any third party.

In Allison, plaintiff similarly contended that demand was excused because of defendants' "[f]ailure to bring suit despite knowing for four years of the alleged underlying wrongs." Allison, 604 F. Supp. at 1113. The district court squarely rejected this argument:

> [T]he GM Board's knowledge of wrongs and failure to institute suit, without more, is inadequate to excuse demand. A general allegation that the Board acquiesced, as signified by its failure to file remedial litigation, is not sufficiently particular to demonstrate demand futility.

Id. (citations omitted). The plaintiff in Allison failed to establish demand futility because his complaint (like the Second Amended Complaint) failed to "offer some particularized legally cognizable reason why the ... Board is unable to redress the alleged wrong." Id.

This Court also has rejected repeatedly similar "failure to take action" claims. See, e.g., Lewis v. Fites, Del. Ch., C.A. No. 12,566, slip op. at 5-6, Berger, V.C. (Feb. 18, 1993) ("The complaint alleges that Caterpillar's directors have been aware of the alleged wrongs for more than two years but have taken no action because they participated in and approved the alleged wrongs and would have to sue themselves. Allegations of this sort offered as an excuse for failure to make demand have been rejected repeatedly"); Richardson, slip op. at 8-9 (rejecting the claim that "the corporation's inaction in seeking redress against [four employees found guilty of illegal activities] is proof that a demand would have been futile" because "[s]uch conclusions have no basis in fact and in law"); Stotland v. GAF Corp., Del. Ch., C.A. No. 6876, slip op. at 14, Longobardi, V.C. (Sept. 1, 1983) (rejecting plaintiffs' claim that the "board's failure to seek redress itself prior to the filing of this suit is proof that any demand on the board would have been futile"). Thus, plaintiffs' claim that demand is excused because the

Director Defendants had knowledge of the alleged wrongs but failed to take action must be rejected.

In asserting that the Director Defendants allowed certain of Caremark's payment practices "to continue unchecked" (2d Amend. Comp. ¶ 79(b)), plaintiffs are only stating that the Director Defendants supposedly failed to carry out their oversight obligations.[13] Mirror image allegations that directors failed in their oversight duties or otherwise failed to stop wrongdoing by the corporation repeatedly have been held to be insufficient to excuse demand. For example, in Shields v. Erickson, 710 F. Supp. 686, 687 (N.D. Ill. 1989), plaintiffs alleged that demand was excused because the directors failed to maintain a system of internal financial controls which would have prevented the corporation from incurring $127.3 million in fines and from being suspended from receiving new defense contracts as a result of fraudulently overcharging the federal government, paying bribes to government personnel and taking improper tax write-offs. The district court determined that plaintiffs had not alleged sufficiently that a pre-suit demand would have been futile:

> All the directors are accused of the same kind of participation in the wrongdoing: approving or acquiescing in the alleged misdeeds and permitting the corporation to operate with insufficient accounting controls. There are no specific allegations of self-dealing as to any directors, or that the directors have personally benefitted from the illegal activities, or that

[13]Despite the sprinkling of verbs and adverbs in the Second Amended Complaint such as "consciously directing," "permitting" and "facilitating," plaintiffs essentially allege a failure of oversight. (See, e.g., 2d Amend. Comp. ¶ 78). In fact, when plaintiffs outlined what they perceived to be the duties of the Director Defendants in this case, they almost exclusively described an oversight function. (See 2d Amend. Comp. ¶ 77). As discussed above, such conclusory failure of oversight allegations will not suffice to excuse demand.

> any director is criminally culpable. At most, the directors are accused of negligence. This is insufficient to subject any director to criminal liability or to demonstrate that the directors would not consider a claim for relief.

Id. at 692 (emphasis added). Accord Citron v. Daniell, 796 F. Supp. 649 (D. Conn. 1992) (finding allegations of the directors' failure to maintain adequate internal financial controls insufficient to excuse demand despite allegations that United Technologies engaged in bribery and other illegal practices to procure defense contracts).

Contrary to the foregoing authorities, plaintiffs' argument in this case effectively would impose a per se rule that whenever corporate employees engage in alleged wrongdoing which results in an indictment or similar action against a company, board members cannot be allowed to address a pre-suit demand because they potentially could be liable for failure to "adequately supervise" those employees. Because such a rule would obviate the demand requirement altogether, the courts repeatedly have declined to excuse demand in this context. See Levine v. Prudential Bache Properties, Inc., 855 F. Supp. 924, 941 (N.D. Ill. 1994) (applying Delaware law) ("Such a vague allegation [of defendant involvement in wrongdoing] invites the court to hold that demand would be futile whenever the corporation ... is the subject of even a routine regulatory or criminal investigation"); Mozes v. Welch, 638 F. Supp. 215, 219-23 (D. Conn. 1986) (refusing to excuse demand despite guilty plea by General Electric to defrauding the federal government); In re E. F. Hutton Banking Practices Litig., 634 F. Supp. 265, 270-73 (S.D.N.Y. 1986) (refusing to excuse demand despite the company's guilty plea to 2,000 charges of mail and wire fraud resulting in the company incurring fines and costs of approximately $11 million).

Furthermore, plaintiffs' "lack of oversight" allegations fail to excuse demand because the directors of a multinational corporation cannot automatically be deemed to be "interested" in the allegations of a derivative action arising out of the government's investigative activities. Under plaintiffs' standard, even if (as in this case) none of the directors are implicated in the wrongdoing, the board would be disabled from addressing a demand for corrective action any time the government launches an investigation or commences a lawsuit. Since Delaware law is to the contrary, as confirmed in Richardson, Allison and the other decisions cited above, plaintiffs' "failure of oversight" allegations are insufficient to excuse a pre-suit demand.[14]

Plaintiffs must plead particularized facts to support their contention that the Director Defendants -- who are not accused by anyone other than plaintiffs of knowledge of or acquiescence in illegal activities -- are nonetheless disabled from determining what,

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[14]Plaintiffs' factual allegations in the Second Amended Complaint also do not support the weak assertion in the first sentence of ¶ 79(b) of the Second Amended Complaint that the Board made a business decision relating to alleged wrongdoing. (See 2d Amend. Comp. ¶ 79(b)). In view of defendants' demonstration that the Original Complaint should have been dismissed under the Rales test, plaintiffs attempt in the Second Amended Complaint to state allegations regarding affirmative decisions which would allow plaintiffs to plead demand excusal under the second prong of the Aronson test. If the mere insertion of the phrase "failing to exercise skill, diligence and prudent business judgment" is sufficient, in the absence of any particularized factual support whatsoever, to raise a presumption that a business decision was in fact made, all plaintiffs would avoid the demanding test for demand excusal under Rales by simply making such a conclusory allegation. However, numerous decisions confirm that, in view of plaintiffs' continuing inability to connect the alleged illegal conduct to any specific acts or decisions by the Caremark Board, plaintiffs' unsupported allegations must be disregarded in determining whether pre-suit demand is excused. See, e.g., Grobow, 539 A.2d at 187; Stotland, slip op. at 16-17 ("As this Court has stated before, stockholders bringing claims on behalf of a corporation must realize that futility cannot be evidenced by boilerplate allegations devoid of pertinent factual support").

if any, remedial action should be taken by the Company. Because plaintiffs' allegations in the Second Amended Complaint fail to demonstrate that any of the Director Defendants have any disqualifying personal interest pertinent to the government investigations and lawsuits, plaintiffs' "lack of oversight" allegations fail to excuse pre-suit demand.

3. Plaintiffs Allege That The Director Defendants Would Be Required To Sue Themselves.

In a third effort to excuse their failure to make a pre-suit demand, plaintiffs allege that:

> (c) The long-term continuing course of corporate misconduct and mismanagement, alleged in detail herein, is the product of the Director Defendants' breach of their fiduciary duties and is so egregious that there is a substantial likelihood that each of the Director Defendants will be found personally liable to Caremark for the substantial damages which it has suffered and will continue to suffer as a result thereof. Accordingly, each of the Director Defendants suffers from an irreconcilable conflict of interest regarding the prosecution of this action. The Director Defendants cannot exercise the requisite disinterested to make good faith business judgments with respect to the matters complained of herein without being influenced by the adverse personal consequences, financially and to their reputations, which they would suffer in pursuing the claims asserted herein.

(2d Amend. Comp. ¶ 79(c); emphasis added).

This allegation is simply an iteration of the discredited contention that Director Defendants have a disqualifying interest because they would have to sue themselves. As the Supreme Court made clear in Aronson, this type of generalized pleading will not excuse demand:

> Plaintiff's final argument is the incantation that demand is excused because the directors otherwise would have to sue themselves, thereby placing the conduct of the litigation in hostile hands and preventing its effective prosecution. This bootstrap argument has been made to and

> dismissed by other courts. Its acceptance would effectively abrogate Rule 23.1 and weaken the managerial power of directors.

Aronson, 473 A.2d at 818 (citations omitted). Accord Rales, 634 A.2d at 936 ("Normally, 'the mere threat of personal liability for approving a questioned transaction, standing alone, is insufficient to challenge either the independence or disinterestedness of directors....'") (quoting Aronson, 473 A.2d at 815); Pogostin, 480 A.2d at 625 ("we note that the plaintiffs' bootstrap allegations of futility, based on claims of directorial participation in and liability for the wrongs alleged, coupled with a reluctance by directors to sue themselves, were laid to rest in Aronson") (citation omitted); Grobow, 526 A.2d at 924 ("The claim that the directors would be required to sue themselves, or that any action brought would be in hostile hands and not diligently prosecuted, has ... been rejected by the Delaware Supreme Court and this Court"); Lewis v. Fites, slip op. at 6 (alleged heightened threat of personal liability insufficient to create reasonable doubt directors were disinterested, thereby excusing demand).

Plaintiffs apparently are attempting to draw support for their conclusory claims of demand futility from the Supreme Court's pronouncement in Rales that:

> Directorial interest also exists where a corporate decision will have a materially detrimental impact on a director, but not on the corporation and the stockholders. In such circumstances, a director cannot be expected to exercise his or her independent business judgment without being influenced by the adverse personal consequences resulting from the decision.

Rales, 634 A.2d at 936 (emphasis added). Although plaintiffs have included the emphasized portion of this language verbatim in paragraph 79(c) of the Second Amended Complaint, plaintiffs' reformulation of their conflict of interest claim fails for at least two reasons.

First, plaintiffs have not described at all (much less with the requisite particularity mandated by Rule 23.1) how a decision as to the alleged underlying wrongs would have "adverse personal consequences" on any of the Director Defendants. (2d Amend. Comp. ¶ 79(c)). The Second Amended Complaint acknowledges that none of the thirteen Director Defendants has been indicted or is under investigation in connection with the alleged payment of illegal kickbacks. Thus, a suit to recover damages on behalf of Caremark against those responsible for any such improprieties would not be detrimental to the Director Defendants.

Second, the finding of director interest in Rales was predicated on the Supreme Court's acceptance of a Third Circuit finding that plaintiff had raised a reasonable doubt as to the applicability of the business judgment rule to the approval of the challenged transaction by certain of the director defendants. Rales, 634 A.2d at 936. Based solely upon that binding determination, the Supreme Court concluded that pre-suit demand was excused because the liability of certain of the director defendants in that case was more than a "mere threat" and might be a "substantial likelihood." Id. Here, unlike in Rales, there has been no preliminary (let alone binding) assessment of the Director Defendants' potential liability.

Indeed, the allegations against the Director Defendants in the Second Amended Complaint pale in comparison to the allegations in Lewis v. Fites that the Caterpillar directors faced the risk of personal liability due to the entry of an SEC consent order establishing federal securities law violations by the corporation. Lewis v. Fites, slip op. at 6. Since the SEC consent order did not contain any findings as to the Caterpillar directors, then-Vice Chancellor Berger found that the Caterpillar directors did not face the "substantial likelihood" of liability required to excuse demand. Id. Of course, since the Director Defendants have not even been named in connection with any of the government investigations, the Director Defendants cannot be deemed to be "interested" due to any purported risk of personal liability.

III. PLAINTIFFS' REPEATED FAILURE TO CURE THE DEFICIENCIES IN THEIR PLEADINGS WARRANTS THE DISMISSAL OF THE SECOND AMENDED COMPLAINT WITH PREJUDICE.

The Second Amended Complaint represents plaintiffs' third futile attempt to circumvent the Charter Provision and the demand requirement of Rule 23.1. As with all prior attempts, the Second Amended Complaint relies on factual allegations which are plainly insufficient to excuse demand. The substance of plaintiffs' deficient demand-excusal allegations has remained constant in the three complaints: (i) that the Director Defendants had knowledge of the alleged wrongs; (ii) that the Director Defendants approved of or failed to rectify the alleged wrongs; and (iii) that the Director Defendants cannot be expected to sue themselves. In fact, the Second Amended Complaint omits the allegation asserted in the two previous complaints that the Director Defendants had a conflicting financial interest by virtue of their stock options. For the alternative reasons set forth above, the Charter Provision and the plaintiffs' continuing failure to comply with Rule 23.1 dictate that the Second Amended Complaint must be dismissed.

Under Chancery Court Rule 15(a), the allowance of any amendment, after the first, is discretionary. Mergenthaler, Inc. v. Jefferson, Del. Supr., 332 A.2d 396, 398 (1975). While leave to amend generally is given freely under Rule 15(a), a further amendment may be denied where, as in this case, "there is evidence of undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies, prejudice, futility, or the like." Hess v. Carmine, Del. Super. Ct., 396 A.2d 173, 177 (1978) (citing Foman v. Davis, 371 U.S. 178 (1962) (emphasis added)). The denial of leave to amend is justified where "[i]n substance the amended complaint realleges in more detail the original complaint ...." Denkla v. Independence Found., Del. Supr., 193 A.2d 538, 544 (1963); see also Mullen v. Alarmguard, Del. Supr., 625 A.2d 258, 263 (1993) (repeated attempts at amendment warrant the denial of further leave to amend); Laird v. Buckley, Del. Supr., 539 A.2d 1076, 1079 (1988) (denial of leave to amend justified where plaintiff had been permitted to amend complaint twice and only sought to allege additional factual bases for gross negligence claim); Rabkin v. Philip A. Hunt Chem. Corp., Del. Ch., 480 A.2d 655, 662 (1984), rev'd on other grounds, Del. Supr., 498 A.2d 1099 (1985). H&H Poultry Co. v. Whaley, Del. Supr., 408 A.2d 289, 291 (1979). Plaintiffs have already been given three bites at the apple. Each of the three complaints has asserted the same legal theories for excusing demand, and each amendment has merely added additional facts which do not alter the legal theories upon which plaintiffs rely. The repeated failure of plaintiffs to cure the deficiencies in their pleadings justifies the denial of further leave to amend.

Moreover, Caremark and its stockholders are being injured by the deflection of the Director Defendants' attention to focus on the plaintiffs' repeatedly futile claims in this litigation. Plaintiffs' maneuvering also has resulted in hardship to Caremark and the Director Defendants in the form of mounting legal bills. In view of the mandatory advancement and indemnification provisions in the Caremark charter (see Ex. C), and in light of the indemnification for expenses which is available under 8 Del. C. § 145(b) and (c), the legal fees of the Director Defendants ultimately are being borne by the Company and its shareholders. Thus, not only are the Director Defendants being burdened, but the interests of Caremark's stockholders, who plaintiffs purportedly represent, ultimately are being prejudiced. Plaintiffs have made three futile efforts -- at the substantial expense of the Company and its stockholders -- to state a claim. Because plaintiffs repeatedly have failed to comply with the pleading requirements of Chancery Court Rules 12(b)(6) and 23.1, the Second Amended Complaint should be dismissed with prejudice.

CONCLUSION

For all of the foregoing reasons, defendants respectfully request that their motion to dismiss plaintiffs' Second Amended Complaint pursuant to Chancery Court Rules 12(b)(6) and 23.1 be granted in all respects, and the Second Amended Complaint be dismissed with prejudice.

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Dated: January 25, 1995

EXHIBIT A

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

IN RE CAREMARK INTERNATIONAL INC. DERIVATIVE LITIGATION	Civil Action No. 13670

SECOND AMENDED DERIVATIVE COMPLAINT

Plaintiffs, by their attorneys, allege upon information and belief, except as to the allegations which pertain to plaintiffs, which are alleged upon knowledge, as follows:

INTRODUCTION

1. This is a shareholder derivative action brought on behalf and in the right of Caremark International Inc. ("Caremark" or the "Company") for injuries suffered by Caremark and its shareholders as a result of breaches of the fiduciary and other duties owed to it and its shareholders by the individual defendants, who constitute its Board of Directors (the term "defendants" shall refer to the individual defendants unless otherwise indicated).

2. The derivative claims arise out of a pervasive and systemic course of business dealings in which the defendants wrongfully allowed Caremark to engage in violations of Federal and State anti-kickback laws for Medicaid and Medicare patients, which has resulted in a massive federal investigation, the indictment of Caremark and certain officers of the Company, several federal and state law suits and an ongoing investigation of Caremark's practice

of paying doctors throughout the Country for patient referrals since at least 1991.

3. The defendants have specifically acknowledged since 1992 in publicly filed reports of Caremark (a) the existence of these long-term investigations by, among other agencies, the U.S. Department of Justice and the Office of the Inspector General of the Department of Health and Human Services (the "HHS-OIG"), and (b) the material adverse effect criminal indictments or other penalties could have on Caremark's business. They have also acknowledged publicly on several occasions that they would take steps to terminate such illegal conduct.

4. Nonetheless, in reckless disregard of their obligation to act in the best interest of the Company and its stockholders the defendants caused, countenanced or allowed Caremark to continue to engage in such misconduct to Caremark's detriment and damage.

5. As a result of the indictments, investigations and lawsuits arising from Caremark's continued illegal conduct, Caremark faces the loss of millions of dollars from legal defense costs, criminal penalties, civil restitution (including treble damages) and lost business resulting from possible exclusion from Medicare and Medicaid programs, which accounted for 14% of the Company's 1993 revenues. In this action, plaintiffs seek relief on behalf of Caremark requiring defendants to account to it for all damages arising from defendants' wrongdoing.

THE PARTIES

6. Plaintiffs Carole Friedman, Claire Blum, Peroje Tejani, Kenneth Steiner, Paul C. Hagan and Elaine Drage were at the time of the transactions and events complained of and are still shareholders of Caremark.

7. Caremark is a Delaware corporation with its executive offices located in Northbrook, Illinois. Caremark provides the following services throughout the United States and overseas: (1) alternative site health care services, including infusion therapy, growth hormone therapy, and hemophilia therapy, and (2) managed care services for prescription drug benefit programs and multi-physician group practices.

8. A significant part of Caremark's health care services consists of infusion therapies, which include: (1) total parenteral nutrition therapy ("TPN"), which is the intravenous feeding for patients unable to ingest or absorb nutrients due to gastrointestinal illnesses or conditions; (2) enteral nutrition therapy, which is nutritional therapy administered to patients with at least partial digestive tract function; (3) antibiotics, antiviral and antifungal therapies, which are used to treat various infections and diseases, including bone infractions and infections related to HIV/AIDS; (4) chemotherapy, which involves the infusion of cancer fighting drugs, blood product therapies and certain biotechnology drugs for cancer patients; and (5) pain management therapy, which involves the administration of pain-controlling drugs to terminally or chronically ill patients. In addition to

its alternative site infusion therapies, Caremark also offers other alternate site patient care services, including pharmaceutical service alliance programs, hemophilia therapy, immune deficiency therapy and rehabilitation services.

9. Caremark's managed care segment consists of (1) prescription drug benefit administration; (2) a preferred provider network; and (3) a business initiative in multi-specialty physician group practice management, which includes administrative services such as billing, accounting and personnel services to large multi-specialty medical group practices.

10. Caremark derives most of its patient care revenues from third party payors, including private insurers, Medicare, Medicaid and workers compensation programs. Approximately 25 percent of Caremark's patient care revenues have historically been attributable to Medicare and Medicaid patients. Caremark also provides services as a subcontractor to hospitals, physicians or other alternate site providers, including joint ventures formed by Caremark with hospitals, physicians, nursing agencies and other healthcare providers, that receive the assignment of benefits or reimbursement from the patient and pay Caremark a negotiated fee.

11. Caremark was incorporated in August 1992 as a wholly-owned subsidiary of Baxter International, Inc. ("Baxter"). On November 30, 1992, Baxter distributed to holders of its common stock all of the outstanding shares of common stock of Caremark, together with preferred stock purchase rights.

12. In fiscal 1993, Caremark's total revenues were approximately $1.78 billion. According to the Company's Form 10-K for the fiscal year ended December 31, 1993, approximately 14% of the Company's revenues were directly attributable to Medicare and Medicaid patients.

13. Defendants C.A. Lance Piccolo, James G. Connelly, III, and Thomas W. Hodson are collectively referred to as the "Officer/Director Defendants." Defendant Piccolo has been Chairman of the Board and Chief Executive Officer of Caremark since August 1992. Defendant Connelly has been President and Chief Operating Officer of Caremark since August 1992. Defendant Hodson has been a Senior Vice President and Chief Financial Officer of Caremark since August 1992. Defendant Piccolo was an executive vice president of Baxter and from 1988 to 1992 served as a director of Baxter. Defendant Connolly was a group and corporate vice president at Baxter prior to 1992. Defendant Hodson was a group, corporate and senior vice president at Baxter and was responsible for Baxter's financial relations, strategic planning and acquisition/divestitures.

14. Defendants Raymond D. Oddi, Peter F. Whitington, Blaime J. Yarrington, Ira J. Harris, Ralph W. Muller, Kenneth N. Pontikes, Vincent A. Calarco, Roger L. Headrick and Philip B. Rooney are and have been directors of Caremark since 1992. Defendant Nancy G. Brinker has been a director since 1993. Defendant Oddi had previously been a senior vice president and chief financial officer at Baxter. Defendant Yarrington served on the Baxter board of

directors from 1988 to 1992. Defendants Oddi, Whitington, Yarrington, Harris, Muller, Pontikes, Calarco, Headrick, Rooney, and Brinker are collectively referred to as the Non-Officer Director Defendants.

15. The Officer/Director Defendants and the Non-Officer Director Defendants are jointly referred to as the Director Defendants.

16. Caremark's "pay philosophy" for executives, as explained in its Proxy Statement dated March 22, 1994, emphasized "pay-for-performance" incentives with compensation based on part upon pre-tax earnings growth. Each of the Officer/Director Defendants holds options to purchase Caremark stock and restricted performance stock subject to, among other factors, annual performance-based vesting conditions.

OPERATIVE FACTS

17. Caremark is the leading provider of home-infusion services in the United States with about a 30% market share. The Company's business is subject to extensive state and federal regulation governing reimbursement under federal and state medical assistance programs and the financial relationships between healthcare providers and potential referral sources, in particular, physicians and hospitals.

18. In November 1987, Congress enacted the Omnibus Budget Reconciliation Act of 1987 which contains a section entitled "Physician Ownership of, and Referral to, Health Care Entities." This section commonly known as the "Stark Legislation" requires a

provider seeking payment from the Medicare program to disclose the provider's referral sources and any ownership interest by physician investors.

19. Under this legislation, it is unlawful for physicians to receive a direct or indirect fee i.e., a kickback, in return for referring patients to health care providers or for prescribing drugs to patients.

20. Likewise, many of the States have adopted statutes, rules and regulations prohibiting the direct or indirect payment of fees primarily for the referral of patients or the prescription of drugs.

21. In August of 1991, shortly after "safe-harbor" regulations were issued identifying appropriate business relationships between physicians and health care providers, and prior to the Company's spin-off from Baxter, Caremark was notified that the HHS-OIG, in conjunction with the U.S. Department of Justice, had begun an investigation of Caremark's fee for services arrangements.

22. As part of the investigation, the HHS-OIG initially issued subpoenas to Caremark on August 9, 1991 for 800 contracts between Caremark and physicians who were paid fees by Caremark for the so-called monitoring of home-care patients. At issue was whether the fees paid by Caremark were for legitimate services or disguised fees for referrals of Medicare patients. Subsequently, a federal grand jury was empaneled to determine whether the Company's fee-for-service and other arrangements with physicians and hospitals in connection with infusion therapy services violated

federal laws which prohibit the payment of remuneration to induce the referral of Medicare and Medicaid beneficiaries.

23. The HHS-OIG investigation was highly publicized. In the September 16, 1991 edition of Modern Healthcare, it was reported that Caremark's practice of paying doctors for "monitoring" patients was widespread. In total, the federal government had paid approximately $130 million in 1991 to Caremark for home-care services provided to Medicare and Medicaid patients.

24. Caremark's top management publicly responded to the new "safe harbor" guidelines and their potential impact upon Caremark. On September 9, 1991, Caremark's spokesman Les Jacobson, as reported in the Chicago Tribune, represented that Caremark would discontinue consulting arrangements with doctors for Medicare and Medicaid home-care patients as of October 1, 1991, the same day new federal regulations went into effect. Carmark's then president and Chief Executive Officer Charles H. Blanchard ("Blanchard") stated:

> The safe-harbor regulations were created to determine what is beyond reproach regarding provider and physician practices with Medicare and Medicaid.
>
> The regulations are drawn very narrowly, and do not address physician involvement in home care. As a result, Caremark is taking the conservative position of discontinuing this service to Medicare and Medicaid patients, effective Oct. 1, until the issue is resolved.

25. Blanchard also told Business Week (October 7, 1991) that the Company knew that the payments to physicians described above fell into a "gray area" in that they were neither prohibited by the Federal anti-kickback law nor expressly permitted. However,

Blanchard also confirmed that beginning October 1, 1991, Caremark had stopped paying physicians and hospitals who referred Medicare and Medicaid patients to its facilities.

26. Thus, at least as early as 1991, Caremark's senior management knew that the Company's fees-for-services arrangements were likely illegal and could subject the Company to significant penalties. Further, the Company's upper-level management had publicly committed to cease such conduct by Caremark. Caremark's upper-level management also publicly admitted that Caremark was already at risk for such conduct resulting from a Federal indictment. As Caremark publicly reported in its Form 10-Q for June 30, 1992, just months before the spin-off of Caremark from Baxter:

> The Office of the Inspector General of the U.S. Department of Health and Human Services and the U.S. Department of Justice are investigating Caremark to determine whether Caremark's fee-for-service and other arrangements with physicians and hospitals, violate federal laws prohibiting payments to induce the referral of Medicare or Medicaid beneficiaries. <u>Penalties for violating these laws could include exclusion from participation on the Medicare and Medicaid programs and civil and criminal fines and penalties. If imposed, these penalties could have a material adverse effect on Caremark's business</u>.

27. On November 30, 1992, Caremark became a public company. At the time, the Company's Board of Directors was fully informed about Caremark's exceedingly risky and potentially criminal practices. The directors' knowledge was derived, at a minimum, from existence of the HHS-OIG investigation, the public filings

relating to the HHS-OIG investigation of Caremark, the public statements made by Caremark's senior management, including CEO Blanchard, that they would stop Caremark from engaging in its likely illegal practices, together with reports from Caremark's management and advisors that (1) Caremark's wide-spread practice of making direct and indirect payments (e.g., consulting, monitoring, marketing, and research fees) to physicians who refer patients to Caremark was potentially illegal and violative of Medicaid and Medicare laws; (2) the investigation by the HHS-OIG and the U.S. Department of Justice could result in the loss of millions of dollars in revenue for Caremark; and (3) the Company had publicly committed to stop paying physicians for "monitoring" Medicare patients.

28. The Director Defendants also admitted that they were well aware of the material adverse effect that the HHS-OIG investigation and resulting indictments could have on the Company's business operations (and thus the materially adverse effect the continuation of Caremark's practices could have on its financial condition). For example, the Director Defendants (except Brinker) made detailed disclosures in Caremark's Form 10-K for fiscal year ended December 31, 1992, soon after the spin-off, that:

> The OIG and the Department of Justice are investigating Caremark to determine whether Caremark's fee-for-service and other arrangements with physicians and hospitals violate the Medicare Referral Payments Law (the federal law prohibiting the payment of remuneration to induce the referral of Medicare and Medicaid patients). Caremark has received several document requests from the OIG and the Department of Justice. Civil

> penalties for violating the Medicare Referral Payments Law include exclusion from participation in the Medicare and Medicaid program. Criminal penalties could include fines of up to $25,000 per violation or up to five years imprisonment, or both, subject to increases under the Federal Organizational Sentencing Guidelines. <u>If imposed, such penalties could have a material adverse effect on Caremark's business</u>. The outcome of this investigation is not presently determinable. Growth in sales slowed following initial publicity related to this investigation as well as reported investigations of others. Based on these changes and discussions with customers, Caremark believes that this publicity had adversely affected revenues from certain patient care services and may continue to do so. (Emphasis added).

29. The Caremark Directors also reviewed and approved similar disclosures regarding the HHS-OIG Investigation which were made in Caremark's quarterly reports on Form 10-Q for the periods ending March 31, June 30, and September 30, 1993.

30. The Director Defendants also made similar disclosures in Caremark's Form 10-K for fiscal year ended December 31, 1993, as follows:

> <u>OIG Investigation</u>
>
> Caremark was notified in August 1991 that the OIG and the U.S. Department of Justice, with subsequent grand jury participation, are investigating Caremark to determine whether Caremark's fee-for-service and other arrangements with physicians and hospitals in connection with infusion therapy services violate federal laws prohibiting payment of remuneration to induce the referral of Medicare and Medicaid beneficiaries. Caremark has provided and continues to provide information and documents. The nature, scope timing and outcome of the investigation are not currently determinable. Civil penalties for violating this law could include exclusion

> from participation in the Medicare and Medicaid programs. Criminal penalties could include exclusion from participation in the Medicare and Medicaid programs. Criminal penalties could include fines of up to $25,000 per violation or up to five years imprisonment, or both, subject to increases under the Federal Organizational Sentencing Guidelines. In 1993, approximately 14% of Caremark's revenues were directly attributable to Medicare and Medicaid patients. <u>Although such revenues do not directly generate a material percentage of Caremark's profits, there can be no assurance that exclusion from these programs would not adversely affect Caremark's ability to attract and retain non-Medicare and Medicaid business. As such, if imposed, such penalties, although not estimable at this time, could have a material adverse effect on Caremark's business.</u> Growth in revenues slowed following initial publicity related to this investigation as well as reported investigations of other companies. Based on these changes and discussions with customers, Caremark believes that this publicity has adversely affected revenues, however not materially, from certain patient care services and may adversely affect revenues in the future. (emphasis added)

31. Caremark also disclosed in the 1993 Form 10-K that both the exclusion from Medicare or Medicaid programs and/or an indictment which has not been dismissed within a 90-day period constituted events of default under the Company's $150 million bank credit agreement (although no borrowings were then outstanding). If the Company were to default on the terms of its credit facility, it would be unable to obtain any borrowing from conventional bank sources to redirect its business efforts -- a necessary high-cost venture once Medicare and Medicaid revenues terminated. Thus, default on a credit facility would severely affect Caremark's

business and the value of plaintiffs' investments regardless of the Company's actual borrowings.

32. At an international health care conference run by First Boston in early October 1993, Caremark's new Chairman and Chief Executive Officer, Lance Piccolo ("Piccolo"), publicly reaffirmed that the HHS-OIG investigation was still in progress, but that no charges had yet been brought.

33. Based upon the foregoing, there is little doubt that the Director Defendants were fully aware of (a) Caremark's widespread practices of indirectly paying doctors who referred patients to Caremark, among other illegal activities; (b) the significant adverse consequences of such conduct; and (c) the public commitment of Caremark's directors and senior management that it would terminate its "fee for services" practices.

34. Nonetheless, two recent indictments against Caremark and/or doctors with whom the Company was associated, a recently filed state court case captioned Booth v. Rankin, a class action on behalf of Protropin users, and other public disclosures reveal that, in fact, the Director Defendants have acted in reckless disregard of their fiduciary obligations in permitting Caremark to continue its illegal activities on a nationwide basis after the November 1992 spin-off until the present.

A. The University of Minnesota Scheme

35. In October 1993, it was publicly disclosed that Caremark had paid doctors in the University of Minnesota's (the

"University") home infusion program about $3 million over a 2-1/2 year period for referring patients to Caremark.

36. Doctors in the University's surgery, medicine and pediatrics departments formed a nonprofit corporation called Physician Managed Care ("PMC"). PMC formed a partnership with Caremark called Managed Care Incentives. The contract between Caremark and PMC provided that the doctors were to receive 18% of all patient revenues.

37. The Minneapolis Star Tribune reported on October 18, 1993, that, as a consequence of the illegal referral arrangement, in less than three years Caremark had pulled in a profit of $17 million while the University doctors had received about $3 million from the PMC/Caremark venture.

38. The Star Tribune also reported that the payments to the doctors would be considered a "kickback" by governmental authorities regardless of whether the payments went to University research and education, rather than into the doctors' own pockets.

39. The Star Tribune further reported that Caremark has had special access to University patients that other local home-infusion companies do not. The Star Tribune reported that although the University doctors said they do not keep figures on total referrals, they conceded that almost half of home-infusion patients have gone to Caremark.

40. Caremark has such close ties to the University that company nurses are stationed in the hospital and help plan patient discharges to Caremark's home-care program. In contrast, an

official of a competitor said that his nurses were turned away at the same hospital.

41. Notably, Dr. Randall Moore, who negotiated the Caremark deal, quit the University to become a medical director at Caremark's headquarters in Illinois.

B. <u>The Minnesota Indictment</u>

42. In 1993, the HHS-OIG investigation against Caremark was expanded to include Caremark's nationwide scheme of illegal kickbacks to physicians who prescribed a human growth hormone called Protropin, manufactured by Genentech, Inc. Caremark was then the largest distributor of Protropin, accounting for about 75% of the $217 million in 1993 revenues.

43. Despite their knowledge of: (i) the expansion of the HHS-OIG investigation to include prescription drugs particularly Protropin, (ii) the highly-publicized Minnesota kickback scheme, (iii) the "consulting," "marketing" and "research" relationships with physicians who provided millions of dollars in patient referrals to Caremark, (iv) and the dire consequences to Caremark's business which could result if these indirect payments were not stopped, defendants consciously allowed and facilitated the continuation of these wide-spread illegal practices regarding Protropin in order to maintain Caremark's market share.

44. On August 4, 1994, the United States Attorney for the District of Minnesota issued a press release reporting that a federal grand jury in Minneapolis had indicted Caremark and Caremark vice presidents James R. Mieszala and Joseph L. Herring,

and a former general manager, Judy F. Giel. United States v. Brown et al., Wo. Cr. 4-94-95 (D. Minn.) (the "Minneapolis Indictment"). The fifty-one count indictment charged Caremark, Mieszala, Herring, Giel and Edmon E. Jennings of Genentech, Inc. with conspiring to pay over $1.1 million in kickbacks to Dr. David A. Brown to induce him to prescribe the growth hormone Protropin produced by Genentech and marketed by Caremark. The kickbacks were alleged to have been disguised as payments for a fictitious medical study and other purported services. The indictment was based on conduct beginning as early as 1986 and continuing into 1994, a period which includes the period of the Director Defendants' stewardship of Caremark.

45. The Minnesota Indictment implicates Caremark's prior president, and describes memoranda and other documents critical to the scheme which originated at Caremark's Chicago headquarters as late as 1993.

46. Among the documents in Caremark's files which serve as a basis of the indictment is a document entitled "Return on the Investment in Research Grants -- An Analysis of Caremark Inc." This document analyzes the return which Caremark enjoys for every dollar invested in research, and calculated that Caremark obtained $6.55 for each research dollar. The report further states that Dr. Brown was paid $100,000 by Caremark for research from January 1989 through April 1, 1990 while Caremark received $4,372,000 in patient referral revenues from Brown. In another document a Mr. Herring, identified in the indictment, stated that Caremark would approve a

$50,000 research grant so long as there were 150 patient referrals in return.

47. The Minneapolis Indictment recites numerous payments, in cash and in kind, to Brown for patient or drug referrals made to Caremark, including

(a) a $75,000 "consulting fee" paid in 1993 to one of Brown's companies, Applied Biomedical Consultants ("ABC"), notwithstanding that Brown was relatively inexperienced in home infusion therapies and related issues;

(b) periodic payments of $15,000 each beginning October 1, 1992 until February 1994 which were disguised as a "marketing fee"; and

(c) creating, at Brown's request, a Protropin sales and marketing position in Caremark's Minneapolis branch, and hiring, in late 1992, a non-college graduate female friend of Brown to fill the position.

48. The Minnesota Indictment further states that Caremark officers had specifically questioned the payments to Brown in writing indicating that senior management was aware of this arrangement but refused to act. For instance, one business manager in the Chicago office wrote that Brown had been paid $409,000 from 1988 until 1992, and he still had not published any research results.

49. The announcement of the Minneapolis Indictment was the first public disclosure of the Justice Department's three-year investigation of Caremark. As reported by <u>The Wall Street Journal</u>

on August 4, 1994, the investigation is ongoing into Carema illegal practice of paying doctors throughout the United States to refer patients to its home infusion programs.

50. The August 4, 1994 Wall Street Journal article also notes that the Minneapolis Indictment is separate from another investigation involving a Caremark joint venture at the University of Minnesota Hospital, which is previously described.

51. On August 31, 1994, while in possession of undisclosed material information regarding the breadth of the federal inquiries, Defendant Brinker sold 3,000 shares of Caremark stock.

52. On November 24, 1994, the federal indictment against Dr. Brown was expanded to include charges of defrauding Medicaid, Medicare, John Hancock Insurance Co., and Aetna Insurance Co. of $391,152. Additionally, it was disclosed that the family of a young patient who paid $150,000 for the Genentech growth hormone treatment had filed a class action lawsuit alleging, inter alia, that comparable treatments cost 30% less than Caremark's program.

53. Caremark's potential liability relating to the Minneapolis Indictment alone is reported to be $12 million. As other indictments and civil actions are commenced, Caremark's legal liability will escalate.

C. The Ohio Indictment

54. The August 4, 1994 Wall Street Journal article disclosed that a federal investigation was scrutinizing other aspects of Caremark's modus operandi, namely, payments to doctors located in Columbus, Ohio, and that an additional indictment could come within

the next few weeks. The article further noted that investigators were planning to interview between 100 and 120 additional doctors who allegedly received large payments from Caremark. The article also stated that Federal authorities were considering pursuing possible civil restitution.

55. On September 20, 1994, a federal grand jury in Columbus Ohio, indicted a doctor on charges that he accepted $134,600 in kickbacks from a "home infusion company" for the referral of patients from 1991 through September 1994. United States v. Neufeld, P.O., No. CR-2-94-144 (S.D. Ohio) (the "Ohio Indictment"). The unnamed company has been uniformly reported by media sources such as The Wall Street Journal and Financial World to be Caremark.

56. The Ohio doctor was charged with one count of conspiracy to solicit and accept kickbacks, 24 counts of acceptance and solicitation of kickbacks and three counts of mail fraud. The Ohio Indictment alleged that, among other indirect benefits, the home-infusion company (i.e., Caremark), had supplied the physician with a facsimile machine, a computer, and nurses to staff his office, all at no cost. Federal law makes illegal any payments in return for referral of Medicare or Medicaid patients, including staffing and equipment purchases.

57. On September 21, 1994, The Wall Street Journal reported that Caremark was the Company that had paid kickbacks to the physician in the Ohio Indictment and that "[g]overnment officials said this is one of multiple federal criminal cases being pursued related to Caremark."

D. <u>**The Atlanta Overbilling and Kickback Scheme**</u>

58. Caremark has also paid kickbacks to physicians in the Atlanta area in return for referrals to Caremark for prescribing medication which Caremark distributes. This fee was usually a flat percentage (generally 25%) of whatever Caremark billed to the patient's insurance carriers.

59. At least two of the Atlanta physicians who participated in this scheme, Michael D. Rankin and Mark L. Tanner, practiced together at the Atlanta Family Practice. In order to control the scheme, these physicians would use Dr. Rankin's taxpayer identification number for all non-Caremark business and Dr. Tanner's taxpayer identification number for all of their Caremark business. Caremark paid these physicians at least 25% of Caremark's billings to the patients they referred for Caremark's services or medication. Rankin and Tanner have received from Caremark several million dollars in referral fees, while Caremark has made tens of millions of dollars from just this facet of the scheme.

60. As part of this scheme, when participating physicians signed up a patient, they would send that patient to the Howell Mill Pharmacy in Atlanta to have prescriptions filled. This pharmacy had an arrangement with Caremark whereby Caremark would bill the patients's insurance carrier for the medications rather than have the pharmacy bill the carrier itself. In doing so, Caremark would inflate the price of the medications sometimes by up to 500% when billing the insurance carrier. Caremark would then

pay a kickback not only to the physician who prescribed medications but also to the pharmacy.

61. In April 1994, Caremark, along with others, was named as a defendant in a federal civil action brought under RICO for "plunder[ing] one million dollars in insurance benefits" from an Atlanta AIDS patient. Booth v. Rankin, et. al., Civ. No. E-2758 (Sup. Ct. Fulton County) (the "Atlanta Lawsuit"). The Complaint alleged that "Caremark has developed a fraudulent scheme that it has implemented on a nationwide basis whereby it pays criminal kickbacks to physicians . . . for unwarranted patient referrals for unconscionable fees and charges." The Complaint stated that Caremark paid kickbacks of as much as 33% of billings to physicians.

62. This lawsuit was settled on November 29, 1994. In return for signing an exculpatory affidavit, the AIDS victim was given lifetime home care services which includes nursing, patient assistance with claims processing and coordination of care, 24-hour care delivery and emergency services. Additionally, Caremark agreed to pay an undisclosed amount covering the AIDS victims legal costs and fees.

63. The plaintiffs' lawyer said that he was cooperating with the Federal Bureau of Investigation and other federal agencies, which are looking into Caremark's payments to doctors in over a dozen states.

64. In an October 25, 1994 Financial World article, defendant Piccolo admitted that he was not concerned with the possibility

that Caremark could lose its Medicaid and Medicare busines Federal violations since government reimbursement was or fraction of Caremark's sales and produced "scant profits."

E. <u>The Detroit "Dollars For Docs" Scheme</u>

65. On November 11, 1994, <u>The Wall Street Journal</u> reported that the Federal government was investigating Dr. Bruce A. Margolis, President of Caremark's Detroit office, for making kickbacks of up to $100,000 to doctors in return for patient referrals, in the guise of fees for services rendered. The practice was openly called "dollars for docs" in Caremark's Detroit office.

66. Dr. Margolis' scheme started with his joint venture with Caremark Physician Health Resources to provide home infusion therapy, employing Dr. Margolis' private company, Physician Care P.C., to make the kickbacks. The joint venture in 1989 split $4.7 million before taxes. Altogether, Dr. Margolis' scheme brought him $11.5 million between 1988 and 1992.

67. Caremark's senior management was well aware of Margolis' activities. Caremark's Executive Vice President Sheldon D. Asher was a frequent house guest, attended Detroit Piston games with Margolis and shared an active rivalry with Margolis regarding exotic sports cars. In 1990, Asher was instrumental in inducing Margolis to continue with Caremark after he received a "sweetened deal" to stay with Caremark. Margolis later became President of Caremark's Detroit branch. As Pat Moorhatch, a former Caremark Operations Manager explained:

> There was upper-management support for what Bruce was doing. . . . My impression was that Shelly [Asher] approved what Bruce was doing.

68. Reportedly, a Michigan doctor enlisted by Margolis, Joseph Natale, generated Caremark sales of over $2 million a year by placing hundreds of people on a home antibiotic therapy for Lyme Disease at a time when very few cases of Lyme Disease were reported in Michigan. A 1992 Caremark internal document describes Natole as producing "good and growing volume" of some $866,000 per year. In one year, Natole and Caremark split $600,000 in profits. Philip I. Frame, a state assistant attorney general, has concluded that "the overdiagnosis and the Caremark issue are intertwined. The more you overdiagnose, the more you made. Ninety-five percent of [Dr. Natole's] cases are misdiagnosed."

F. Kickbacks -- A Widespread Caremark Policy

69. Recent disclosures confirm that Caremark's illegal practices, including its kickback scheme, were an integral and accepted part of the Company's business practices. For instance, Mark Deponio ("Deponio"), Caremark's Grand Rapids General Manager in 1991, confirmed that kickbacks were part of the sales pitch given to Caremark employees and managers, and was an integral component of Caremark's business practice. Deponio said that he found the payments to doctors so repugnant that he quit after a few months. He related that "[w]hat came through at a sales meeting was that the intent of these payments was to steer business" to

Caremark. "The clear intent of the payments was to influence patient referrals."

70. Barbara Petroff, a former Caremark pharmacist in Detroit confirmed that illegal kickbacks were rampant at Caremark and a widespread Caremark policy, stating that "[p]robably two-thirds of the payments were just paying off doctors."

71. Another Margolis enlistee was Dr. Jay Collins, a surgeon in West Branch, Michigan. In 1992, he received kickbacks of between $1,300 and $1,900 a month in return for prescribing intravenous nutrients known as TPN. The hospital Collins is affiliated with, as well as Federal law enforcement officials and Blue Cross/Blue Shield of Michigan are currently investigating Collins' "treatment" strategy and his relationship with Caremark.

72. On November 18, 1994, The New York Times and Chicago Tribune reported that the three year old investigation of kickbacks by Caremark had expanded to Caremark's Detroit area office.

G. The Federal Trade Commission Inquiry into Improper Influencing of Doctor Services

73. On November 26, 1994, it was disclosed that the Federal Trade Commission ("FTC") was expanding its inquiry into Caremark's contractual alliances with drug companies, including "such matters as competition, pricing, restrictions on the availability of drugs and efforts to influence what doctors prescribe." The investigation is centered on the role of Caremark's prescription drug benefit management services which had previously announced that its managed-care unit had arranged special relationships with several

drug makers, including Pfizer Inc., Bristol-Myers, Squibb and Rhone-Poulenc Rorer.

H. <u>The Civil and Criminal Lawsuits</u>

74. The Federal indictments have caused the Company to increase its expenditures for legal counsel and retain a high profile, high cost former United States prosecutor to assist in defending itself against the Department of Justice lawsuit. Additionally, Caremark faces at least 13 shareholder lawsuits, criminal and civil penalties and the loss of millions of dollars in Medicaid and Medicare revenues.

75. The Director Defendants have failed to sue any of the Company officers for wasting corporate assets by having entered into the illegal kickback schemes. The Director Defendants have consciously permitted the waste of corporate assets and consciously failed to take action to recover corporate assets diverted to the kickback scheme, in the misguided hope that by doing so they would be able to continue to inflate Caremark's revenues and its market share in the home infusion market, among others.

DEFENDANTS' BREACH OF THEIR FIDUCIARY DUTIES

76. Each Director Defendant owed and owes to the Company and to its shareholders fiduciary duties to act in good faith and exercise due care and diligence in the management and administration of the affairs of Caremark and in the use and preservation of its property and assets.

77. To discharge their fiduciary duties, the Director Defendants were and are required to exercise reasonable and prudent judgment as to the management, policies, practices, controls and financial affairs of Caremark, and to insure that the Company seeks recompense from those responsible for prior and current wrongs done to it, and to exercise proper business judgment. Defendants were and are required to assure that Caremark was not involved in illegal conduct. By virtue of this obligation, defendants were required:

(a) To set and carry-out policies, manage and supervise the conduct of Caremark's employees, business, and affairs in accordance with State and federal laws and regulations, and the charters, regulations, rules, and by-laws of the Company;

(b) To exercise reasonable and prudent judgment and control and supervision over the officers, employees and agents of Caremark;

(c) To remain informed as to how Caremark conducted its operations;

(d) To ensure the prudence and soundness of the policies and practices undertaken or proposed to be undertaken by Caremark;

(e) To make a reasonable investigation upon receiving notice or information of an imprudent or unsound decision, condition, or practice, and to take steps to correct any imprudent or unsound decision, condition, or practice; and

(f) To conduct the affairs of the Company in an efficient business-like manner so as to make it possible to provide the highest quality performance of its business and to thereby maximize the profits to the stockholders.

78. The Director Defendants breached their fiduciary duties by, among other things:

(a) consciously directing, encouraging and/or concealing the unlawful kickback scheme and other illegal practices of Caremark described herein;

(b) falsely representing to the public that corrective action was being taken to stop illegal payments to physicians when it was not -- resulting in, among other problems -- federal securities lawsuits;

(c) permitting the illegal business practices to continue notwithstanding that the federal investigations could likely lead (and did lead) to indictments against Caremark and its employees, criminal and civil fines, penalties and judgment and loss of business, in the unreasonable hope and expectation that the financial rewards from Caremark's illegal kickback and overbilling scheme and their remunerations would outweigh the risks and any punishment attendant thereto;

(d) deciding not to implement adequate corrective procedures after they were informed of the federal investigation;

(e) facilitating the activities of the employees, managers and upper level executives of Caremark who were directly involved in the illegal schemes, by <u>inter alia</u>, deciding not to direct them to act with honesty and integrity in order to preserve and enhance Caremark's reputation in the business community and its assets;

(f) recklessly exposing Caremark to millions of dollars of losses, including the loss of future business opportunities as a result of their conscious decision to allow Caremark and its employees to operate in violation of federal and state laws and their encouragement of the Company's improper practices; and

(g) taking no steps to remove or institute legal action against those officers, directors and employees responsible for permitting Caremark to engage in the improper and illegal practices described in detail above, thereby exposing the Company to financial injury.

ALLEGATIONS REGARDING DEMAND

79. Under the circumstances, pre-suit demand by plaintiffs is excused and is futile for at least the following reasons:

(a) The Director Defendants, since the Company's spin-off as a public company in November 1992, have known of the wrongs forming the basis for the claims alleged herein and the materiality of such wrongs to the Company's financial well-being and reputation. The Director Defendants have affirmatively facilitated the continuation of the misconduct detailed herein, unreasonably and recklessly choosing to put at risk Caremark's resources and ability to conduct its business rather than discontinue the unlawful practices and schemes which have led to the numerous investigations, criminal indictments and civil lawsuits described herein.

(b) The Director Defendants recklessly disregarded their fiduciary obligations in failing to exercise skill, diligence and prudent business judgment. They have permitted the systemic wrongs alleged herein to continue unchecked although they have long had knowledge of those wrongs and, in fact, at least since the 1992 Form 10-K, have admitted their knowledge of these wrongs and have represented through the Company's officers that the misconduct would be corrected.

(c) The long-term continuing course of corporate misconduct and mismanagement, alleged in detail herein, is the product of the Director Defendants' breach of their fiduciary duties and is so egregious that there is a substantial likelihood that each of the Director Defendants will be found personally liable to Caremark for the substantial damages which it has suffered and will continue to suffer as a result thereof. Accordingly, each of the Director Defendants suffers from an irreconcilable conflict of interest regarding the prosecution of this action. The Director Defendants cannot exercise the requisite disinterestedness to make good faith business judgments with respect to the matters complained of herein without being influenced by the adverse personal consequences, financially and to their reputations, which they would suffer in pursuing the claims asserted herein.

(d) The Director Defendants were intimately and personally involved in approving, fostering and/or countenancing the kickback and overbilling schemes which are the subject of the investigations, criminal indictments and civil lawsuits described herein. As a consequence, the Director Defendants are personally and acutely interested in suppressing full disclosure of their wrongs and are thereby disabled from addressing a pre-suit demand with impartiality and independence.

AS AND FOR A FIRST CAUSE OF ACTION FOR
BREACH OF FIDUCIARY DUTY AGAINST ALL DEFENDANTS

80. Plaintiffs hereby incorporate by reference paragraphs 1 though 79, supra, as if fully set forth herein.

81. Each of the defendants, individually or jointly, as herein alleged, committed one or more of the acts or omissions to act, which constituted waste of corporate assets, mismanagement, gross negligence and violations of their fiduciary duties and their duty to act in the best interests of the Corporation and its shareholders.

82. As a direct and proximate result of defendants' failures to exercise due care and loyalty in the performance of their duties, as alleged herein, and their failure to exercise reasonable business judgment, Caremark has engaged in imprudent and unlawful activities, all of which have caused and will cause significant losses to Caremark.

83. The Company has been further injured by the waste of valuable corporate assets and loss of goodwill and business opportunities that were proximately caused by the defendants' misconduct.

84. By reason of defendants' misconduct as set forth above, Caremark has suffered and will continue to suffer damages amounting to many millions of dollars.

AS AND FOR A SECOND CAUSE OF ACTION FOR GROSS NEGLIGENCE AGAINST ALL DEFENDANTS

85. Plaintiffs hereby incorporate by reference paragraphs 1 through 84, supra as if fully set forth herein.

86. Each of the defendants committed one or more acts of gross negligence in the conduct of the Company's business. Defendants, as officers and/or directors of Caremark, owed to Caremark duties of care in the performance of their duties. Each defendant breached his or her duty of care to Caremark by acting in a grossly negligent fashion in the performance of such duty, and by failing to act in the best interests of the corporation and its shareholders.

87. Caremark has been seriously damaged by the wrongs alleged herein.

88. As to both causes of action, plaintiffs have no adequate remedy at law.

WHEREFORE, plaintiffs demand judgment as follows:

A. Directing defendants, jointly and severally, to account to the Company for all damages sustained and to be sustained by the Company as a result of the breaches of fiduciary duty and gross negligence of defendants;

B. Awarding to plaintiffs the costs and disbursements of the action, including reasonable attorneys' fees, accountants' and experts' fees, costs and expenses; and

C. Granting such other and further relief as the Court may deem just and proper.

ROSENTHAL, MONHAIT, GROSS
& GODDESS, P.A.

By ______________________
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CERTIFICATE OF SERVICE

I, Joseph A. Rosenthal, do hereby certify that on December 30, 1994, I caused copies of the foregoing Notice and Motion for Leave to File Second Amended Derivative Complaint to be served on defendants as follows:

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Richards, Layton & Finger
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Wilmington, DE 19801

Kenneth J. Nachbar, Esquire
Morris, Nichols, Arsht & Tunnell
1201 N. Market Street
Wilmington, DE 19801

Joseph A. Rosenthal

EXHIBIT B

CAREMARK INTERNATIONAL INC.
2215 SANDERS ROAD
NORTHBROOK, ILLINOIS 60062

PROXY STATEMENT

The enclosed proxy is solicited on behalf of the Board of Directors of the Company for use at the Annual Meeting of Stockholders of the Company to be held on April 19, 1994, and any adjournments thereof. This proxy statement and accompanying proxy are first being sent to stockholders on or about March 22, 1994.

Shares represented by an effective proxy given by a stockholder will be voted as directed by the stockholder. If a properly signed proxy form is returned to the Company and is not marked, it will be voted in accordance with the recommendation of the Board of Directors on all proposals. A stockholder giving a proxy may revoke it at any time prior to the voting of the proxy by giving written notice to the secretary of the Company, by executing a later dated proxy or by attending the meeting and voting in person.

The Company's common stock, $1.00 par value (the "Common Stock"), is the only issued and outstanding class of stock. Only stockholders of record at the close of business on March 2, 1994 are entitled to notice of and to vote at the meeting. At the close of business on March 2, 1994, the Company had 71,607,615 shares of Common Stock outstanding and entitled to vote. Each share of Common Stock of the Company is entitled to one vote. A list of stockholders entitled to vote at the meeting will be kept at the stock transfer department of The First National Bank of Chicago for a period of 10 days prior to the meeting.

ELECTION OF DIRECTORS

The Board of Directors of the Company consists of three classes, as nearly equal in number as possible. One of the three classes, comprising approximately one-third of the directors, is elected each year to succeed the directors whose terms are expiring. The number of directors of the Company, as determined by the Board under Article Fifth of the Company's Certificate of Incorporation, is currently thirteen. Directors hold office until the annual meeting for the year in which their terms expire and until their successors are elected and qualified unless, prior to that time, they have resigned, retired, or otherwise left office.

The nominees for whom the enclosed proxy is intended to be voted are set forth below. It is not contemplated that any of these nominees will be unavailable for election, but if such a situation should arise, the proxy will be voted in accordance with the best judgment of the proxyholder unless a stockholder has directed otherwise. Under the Company's bylaws, directors are elected by a plurality of the voting power of the shares of capital stock of the Company present in person or represented by proxy at the meeting and entitled to vote for the election of directors. Shares represented at the meeting in person or by proxy but withheld or otherwise not cast for the election of directors will have no effect on the outcome of the election.

Each of the Directors of the Company has been a Director since 1992, except Nancy G. Brinker, who was appointed in 1993.

Nominees for Election as Directors to be Elected for a Term of Three Years Ending at the Annual Meeting of Stockholders in 1997

Name	Age	Business Experience During the Past Five Years and Other Information
James G. Connelly III	48	Mr. Connelly has been the president and chief operating officer of the Company since August 1992. Mr. Connelly was the president of a subsidiary of the Company from April 1992 to November 30, 1992. From May 1990 to November 30, 1992, Mr. Connelly was a group vice president of Baxter International Inc. ("Baxter"), a manufacturer and marketer of health care products. Prior to 1990, he was a corporate vice president of Baxter, responsible for its hospital supply business group.
Raymond D. Oddi	66	For the past five years, Mr. Oddi has served as a consultant for the Alcar Group, Inc., a privately held business consulting firm, and Baxter. Mr. Oddi is a former senior vice president and chief financial officer of Baxter. Mr. Oddi also serves as a director of the First Prairie Series of Money Market and Mutual Funds.
Peter F. Whitington, M.D.	46	Dr. Whitington is, and since 1987 has been, the director of the section of pediatric gastroenterology, hepatology and nutrition, and is a professor of pediatrics and medicine at the University of Chicago Pritzker School of Medicine.
Blaine J. Yarrington	75	Mr. Yarrington is a former executive vice president and director of Amoco Corporation, a diversified energy company. From before 1988 until April 1992, Mr. Yarrington served as a director of Baxter.

The Board of Directors recommends a vote FOR the election of each nominee for director named above.

DIRECTORS WHOSE TERMS OF OFFICE CONTINUE

Terms Expiring at 1995 Annual Meeting of Stockholders

Name	Age	Business Experience During the Past Five Years and Other Information
J. Ira Harris	55	Mr. Harris has been a senior partner with Lazard Frères & Co., an international investment banking firm, since 1988. Mr. Harris also serves as a director of Manpower Inc. and Brinker International, Inc.
Ralph W. Muller	48	Mr. Muller is, and since 1986 has been, the president of the University of Chicago Hospitals, a health care institution located in Chicago, Illinois.
C.A. Lance Piccolo	53	Mr. Piccolo has been chairman of the board and chief executive officer of the Company since August 1992. From 1987 until November 30, 1992, Mr. Piccolo was an executive vice president of Baxter and from 1988 until November 30, 1992, he served as a director of Baxter. Mr. Piccolo also serves as a director of Crompton & Knowles Corporation and Orthomet, Inc.
Kenneth N. Pontikes	53	Mr. Pontikes is, and since 1969 has been, the chairman of the board and president of Comdisco, Inc., an independent computer and high technology leasing company. Mr. Pontikes also serves as a director of Richardson Electronics, Ltd. and Pier 1 Imports, Inc.

Terms Expiring at 1996 Annual Meeting of Stockholders

Name	Age	Business Experience During the Past Five Years and Other Information
Nancy G. Brinker	47	Ms. Brinker is, and since 1982 has been, the founding chairman of the board of The Susan G. Komen Breast Cancer Foundation.
Vincent A. Calarco	51	Mr. Calarco is, and since 1985 has been, president and chief executive officer of and since 1986 has been chairman of the board of, Crompton & Knowles Corporation, a multinational specialty chemicals and special industry machinery manufacturer. Mr. Calarco also serves as a director of J.M. Huber Corporation.
Roger L. Headrick	57	Mr. Headrick has been president and chief executive officer of the Minnesota Vikings Football Club since 1991. Additionally, since June 1989, Mr. Headrick has been president and chief executive officer of ProtaTek International, Inc., a bio-process and biotechnology company that develops and manufactures animal vaccines. Prior to 1989, he was executive vice president and chief financial officer of The Pillsbury Company, a food manufacturing and processing company. Mr. Headrick also serves as a director of Crompton & Knowles Corporation.
Thomas W. Hodson	47	Mr. Hodson has been the senior vice president and chief financial officer of the Company since August 1992. Mr. Hodson was a group vice president of Baxter from April 1992 to November 30, 1992. From 1988 to 1990, Mr. Hodson was a corporate vice president of Baxter, and from 1990 to 1992, he was a senior vice president of Baxter responsible for financial relations, strategic planning, acquisitions and divestitures and corporate communications.
Phillip B. Rooney	49	Mr. Rooney is a director of, and since 1984 has been president and chief operating officer of, WMX Technologies, Inc., an environmental services company. Mr. Rooney is a director of, and the chairman of the board and chief executive officer of, Wheelabrator Technologies Inc., an affiliate of WMX Technologies, Inc. in the waste-to-energy and pollution control industry. Mr. Rooney also serves as a director and chairman of the board of Rust International Inc. which provides engineering, construction, environmental and infrastructure consulting, environment restoration and on site industrial services. Mr. Rooney also serves as a director of Chemical Waste Management, Inc., Illinois Tool Works Inc., ServiceMaster Management Corporation, Urban Shopping Centers, Inc. and Waste Management International plc.

EXHIBIT C

STATE OF DELAWARE
SECRETARY OF STATE
DIVISION OF CORPORATIONS
FILED 10:00 AM 08/07/1992
732220035 - 2306130

CERTIFICATE OF INCORPORATION
of
CAREMARK INTERNATIONAL INC.

* * * * *

Caremark International Inc., a Delaware corporation, hereby adopts this certificate of incorporation as contemplated by the provisions of Section 102 of the General Corporation Law of Delaware.

FIRST: The name of the corporation is Caremark International Inc.

SECOND: The registered office of the corporation in the State of Delaware is located at 1209 Orange Street in the City of Wilmington, County of New Castle. The name of the registered agent of the corporation is The Corporation Trust Company.

THIRD: The purpose of the corporation is to engage in any lawful act or activity for which a corporation may be organized under the General Corporation Law of the State of Delaware as set forth in Title 8 of the Delaware Code.

FOURTH: The total number of shares of stock which the corporation shall have authority to issue is Two Hundred Twenty Million (220,000,000) shares, of which Twenty Million (20,000,000) shares, par value $.01 per share, shall be preferred stock (the "Preferred Stock") and of which Two Hundred Million (200,000,000) shares, par value $1.00 per share, shall be common stock (the "Common Stock").

Authority is hereby expressly granted to and vested in the board of directors of the corporation to issue Preferred Stock in one or more series and in connection therewith to fix by resolutions providing for the issue of such series the number of shares to be included in such series and the designations and such voting powers, full or limited, or no voting powers, and such of the preferences and relative, participating, optional or other special rights, and the qualifications, limitations or restrictions thereof, of such series of the Preferred Stock which are not fixed by the certificate of incorporation, to the full extent now or hereafter permitted by the laws of the State of Delaware. Without limiting the generality of the grant of authority contained in the preceding sentence, the board of directors is authorized to determine any or all of the following, and the shares of each series may vary from the shares of any other series in any or all of the following respects:

1. The number of shares of such series (which may subsequently be increased, except as otherwise provided by the resolutions of the board of directors providing for the issue of such series, or decreased to a number not less than the number of shares then outstanding) and the distinctive designation thereof;

SIXTH: The board of directors shall be divided into three classes. The term of office for one class of directors will expire each year at the annual meeting of stockholders, or thereafter in each case until the directors' respective successors are elected and qualified. The directors chosen to succeed those whose terms are expiring shall be identified as being of the same class as the directors whom they succeed and shall be elected for a term expiring at the third succeeding annual meeting of stockholders or thereafter in each case until their respective successors are elected and qualified, subject to death, resignation, retirement or removal from office.

Any new positions created as a result of the increase in the number of directors shall be allocated to make the classes of directors as nearly equal as possible. Any director elected to fill a term resulting from an increase in the number of directors shall have the same term as the other members of his class. A director elected to fill any other vacancy shall have the same remaining term as that of his predecessor.

Notwithstanding the foregoing, whenever the holders of any one or more classes or series of Preferred Stock issued by the corporation shall have the right, voting separately by class or series, to elect directors at an annual or special meeting of stockholders, the election, term of office, filling of vacancies and other features of such directorships shall be governed by the terms of the certificate of incorporation applicable thereto, and such directors so elected shall not be divided into classes pursuant to this Article SIXTH unless expressly provided by such terms.

This Article SIXTH may not be amended or repealed without the affirmative vote of at least two-thirds of the holders of all the securities of the corporation then entitled to vote on such change.

SEVENTH: The board of directors shall have such powers as are permitted by the General Corporation Law of Delaware, including, without limitation, without the assent or vote of the stockholders, to make, alter, amend, change, add to, or repeal the by-laws of the corporation; to fix and vary the amount to be reserved as working capital; to authorize and cause to be executed mortgages and liens upon all the property of the corporation, or any part thereof, to determine the use and disposition of any surplus or net profits over and above the capital stock paid in, and to fix the times for the declaration and payment of dividends.

EIGHTH: To the fullest extent permitted by the General Corporation Law of Delaware as the same exists or may hereafter be amended, a director of the corporation shall not be liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director.

NINTH: The corporation shall indemnify and advance expenses to each person who serves as an officer or director of the corporation or a subsidiary of the corporation and each person who serves or may have served at the request of the

CERTIFICATE OF SERVICE

It is hereby certified that two copies of the foregoing Defendants' Opening Brief In Support Of Their Motion To Dismiss Plaintiffs' Second Amended Complaint were served this 25th day of January, 1995, by hand delivery on local counsel as follows:

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Kevin G. Abrams