APPLE INC.

REPORT OF THE

SPECIAL LITIGATION COMMITTEE OF THE BOARD

REGARDING DIRECTOR DEFENDANTS AND SETTLEMENT

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I. EXECUTIVE SUMMARY

This is the second of two reports by the Special Litigation Committee (the "SLC") of the Apple Board of Directors addressing claims asserted in the Second Consolidated Amended Shareholder Derivative Complaint for Breach of Fiduciary Duty filed March 2, 2016 (the "SCAC") in the action titled *In Re Apple Inc. E-Book Derivative Litigation* (the "Derivative Action"). The SLC's first report regarding Eduardo Cue (the "Cue Report"), dated January 19, 2017, summarized the basis for the SLC's conclusion that the derivative claim against defendant Eduardo Cue lacks merit and that dismissal of the claim is in Apple's best interests. This second report summarizes the SLC's conclusion that the derivative claim against the director defendants lacks merit and sets forth the basis for the SLC's conclusion that settlement of claims against all defendants is in Apple's best interests. This report should be read in conjunction with the Cue Report, which includes more extensive discussion of some of the facts included in this report.

The Derivative Action is based on litigation against Apple for violating Section 1 of the Sherman Antitrust Act brought by the United States Department of Justice ("DOJ"), 33 states and territories, and private litigants. That antitrust litigation concerned agreements reached in January 2010 between Apple and five of the six largest book publishers in the United States to sell electronic books ("ebooks") in Apple's iBookstore (the "Publisher Agreements"). After a bench trial, on July 10, 2013, Judge Denise Cote of the United States District Court for the Southern District of New York held Apple liable for a per se violation of the Sherman Antitrust Act (the "Antitrust Action"). Ultimately, the District Court imposed an external compliance monitor for an initial two year term to oversee the development of a comprehensive antitrust compliance program at Apple (the "Monitor" and "Monitorship") and Apple paid $450 million in settlement. By the end of the two year Monitorship, Apple had "entirely revamped" its antitrust compliance program and, with the approval of the DOJ, the District Court dismissed the Monitor on October 13, 2015.

On August 15, 2014, prior to the Monitor's discharge, the Derivative Action was filed in the Superior Court in Santa Clara, California, asserting a claim of breach of fiduciary duty

against Mr. Cue and eight current and former directors of Apple (the "Director Defendants"). The derivative plaintiffs' (the "Derivative Plaintiffs" or "Plaintiffs") allegations are currently set forth in the SCAC.

The SCAC alleges that Mr. Cue's conduct in negotiating and entering into the Publisher Agreements was a breach of fiduciary duty, that the directors at the time failed to establish compliance practices at Apple that would have prevented the antitrust violation, and that the directors themselves should have known about and stopped the transactions. The SCAC further alleges that following the initiation of action by the DOJ, Apple's directors failed to put in place an appropriate antitrust compliance program by the time of the final judgment. Finally, the SCAC alleges that Apple's directors affirmatively interfered with the Monitor's efforts to assure the establishment of a high quality antitrust compliance program and exposed Apple to the risk of contempt in the District Court.

In response to the Derivative Action, on April 26, 2016, Apple's Board of Directors formed the SLC, and granted it the authority to investigate and evaluate all claims made on behalf of the corporation in the Derivative Action and to determine whether and to what extent it would be in Apple's best interests to pursue, litigate, settle or otherwise dispose of the claim against Mr. Cue (who was not an officer or director at the time of the ebook negotiations) and the Director Defendants. Two Apple Board members were appointed to the SLC: James Bell and Susan Wagner. Mr. Bell became a director on October 1, 2015, more than one year after the Derivative Action was filed and twelve days before the Monitor was discharged. Ms. Wagner became a director on July 17, 2014, one month before the Derivative Action was filed, at the end of the period covered by the second of four semi-annual Monitor reports.

The SLC has spent eleven months independently investigating and evaluating the claim made on behalf of Apple in the Derivative Action against the Director Defendants. The SLC has determined that, at all times, all Director Defendants properly discharged their fiduciary duties to Apple and its shareholders. Based on the evidence obtained and reviewed by the SLC, had this case not settled, the SLC would have sought dismissal of the Derivative Action against each of

the Director Defendants.

In November 2016, the parties to the Derivative Action commenced a mediation with the Honorable Layn Phillips, a retired federal district court judge and well-respected mediator. The SLC conducted the negotiation on behalf of Apple. The individual defendants were represented by counsel separate from the SLC's counsel. While the SLC determined that Apple fully complied with the final judgment by developing an exceptional antitrust compliance program with appropriate Board oversight, in order to settle the case the SLC agreed to institute further enhancements to Apple's antitrust compliance program. For the reasons explained in this report, the SLC has determined that settlement of the Derivative Action is in Apple's and its shareholders' best interest.

II. APPLE'S ENTRY INTO THE EBOOKS MARKET AND THE TRANSACTIONS THAT GAVE RISE TO THE ANTITRUST JUDGMENT

To provide background, below is a brief summary of the events surrounding Apple's entry into the ebooks market. A more detailed discussion of these events can be found in the Cue Report.

A. Background Of The Ebook Industry

In late 2009, Apple CEO Steve Jobs was preparing to launch Apple's first iPad in early 2010, and was considering whether to include with it an ebook reader application. Amazon's Kindle had been launched in 2007, and Amazon quickly became the market leader in the sale of ebooks and ebook readers, selling nearly 90% of all ebooks. At that time, book publishers distributed print and digital books through a wholesale pricing model, in which the publishers sold books and ebooks to a retailer, such as Amazon, at wholesale prices. The retailer then offered the print book and ebook to consumers at whatever prices it chose. Amazon was selling new release ebooks at $9.99, which was lower than the wholesale price it paid for these ebooks. The publishers' attempts to combat Amazon's below cost pricing, and in particular the publishers' practice of delaying the release of ebooks because of that pricing, was widely publicized in articles in the Wall Street Journal, the New York Times, and other publications.

B. Apple's Negotiations With Publishers

Apple negotiated the Publisher Agreements during a six-week period in December 2009 and January 2010. The negotiations took place between the quarterly Apple Board meetings that occurred on November 10, 2009 and February 25, 2010. No Board member, other than Steve Jobs, was involved with the negotiations. At the time, the total size of the ebook market was estimated to be $150 million in annual sales, while Apple had more than $35 billion in annual revenue.

In mid-November 2009, Jobs directed Apple employee Eduardo Cue, Vice President, Internet Services, to "pursue an ebookstore," with the goal to announce the "iBookstore" together with the iPad at the iPad's launch on January 27, 2010. With this schedule, Cue had basically two months to acquire enough content to create a viable Apple ebookstore. Cue had been with Apple since 1989, and had been the lead negotiator for Apple's previous content stores: the Apple Online Store in 1998, the iTunes Store in 2003, and the App Store in 2008, as well as movies and television within the iTunes store. Since 2004, Cue had been responsible for running all of Apple's digital content stores.

Cue's negotiating team included Keith Moerer, Director of TV, Books & Podcasting for iTunes, and Kevin Saul, Associate General Counsel. Saul reported to Apple's General Counsel, Bruce Sewell. Saul had worked as an attorney on most of Cue's content store negotiations since 2002, and Cue had a high opinion of Saul's legal ability. As counsel, Saul was responsible for advising Cue on legal matters, drafting and negotiating agreements and resolving legal issues as they arose during negotiations.

Cue and Jobs discussed the publishing industry and developed a strategy for approaching publishers to provide content for Apple's new ebookstore. With Jobs' input and approval, Cue developed objectives and goals for Apple's entry into the ebook market, which Cue summarized as "selection, price, and profitability." As to "selection," Apple's ebook store had to have the maximum number of ebooks possible. This meant that Apple had to enter into contracts with most of the six largest publishers and had to release a book as an ebook at the same time it was

released in hardcover. As to "price," because an ebook was less expensive to produce than a hardcover book, Apple wanted most of the cost savings to be passed on to consumers. As to "profitability," Apple was unwilling to sell ebooks below cost like Amazon. In addition, Apple would not agree to sell ebooks at higher prices than they could be purchased from another source. Cue explained Apple's approach and concerns to each of the publishers during the negotiations.

Between December 15 and January 27, Cue negotiated separately with representatives of the six largest book publishers in the United States. Ultimately, he entered into substantially similar agreements with five of the six publishers. The major similar terms were: (1) Apple and the publisher would enter into an agency agreement, whereby Apple was the selling agent of the publisher and the publisher would establish the retail price for each ebook sold by Apple; (2) Apple would receive a 30 percent commission on each sale; (3) Apple's price would be subject to a most favored nation ("MFN") clause, which meant that the publishers had to allow Apple to sell at the lowest retail price available for each book; and (4) the retail pricing would be subject to pricing caps. As Apple completed negotiation of the separate contracts, Cue advised publishers how many agreements had been reached with other publishers.

Throughout the ebook negotiations Cue relied on legal advice provided by Saul, who was consulting with a team of Apple in-house lawyers and with outside counsel to resolve legal issues, including potential antitrust issues. Cue also kept Jobs informed about key issues and contract terms.

C. The Launch Of The iPad And iBookstore

On January 27, 2010, Jobs introduced the highly anticipated iPad at a presentation in San Francisco, California. Jobs announced that iPads would include a new Apple-designed application, iBooks, that ebooks published by Penguin, HarperCollins, Simon & Schuster, MacMillan, and Hachette (the "Publishers") would be available for purchase from Apple's iBookstore, and that Apple was "going to open the floodgates for the rest of the publishers in the world starting this afternoon."

During his presentation of the iBookstore, Jobs demonstrated purchasing an ebook, Ted Kennedy's "True Compass" memoir, for $14.99. Jobs was asked by a reporter after his presentation why people would pay $14.99 in the iBookstore to purchase an ebook that was selling at Amazon for $9.99. Jobs responded, "Well, that won't be the case. … The price will be the same," and explained that "Publishers are actually withholding their books from Amazon because they are not happy." The day after the iPad launch, Jobs explained to his biographer, Walter Isaacson:

> Amazon screwed it up. It paid the wholesale price for some books, but started selling them below cost at $9.99. The publishers hated that -- they thought it would trash their ability to sell hardcover books at $28. So before Apple even got on the scene, some booksellers were starting to withhold books from Amazon. So we told the publishers, "We'll go to the agency model, where you set the price, and we get our 30%, and yes, the customer pays a little more, but that's what you want anyway." But we also asked for a guarantee that if anybody else is selling the books cheaper than we are, then we can sell them at the lower price too. So they went to Amazon and said, "You're going to sign an agency contract or we're not going to give you the books."

Within months of signing the Publisher Agreements with Apple, the five Publishers changed Amazon from a wholesale model to an agency model, which allowed the Publishers to control Amazon's pricing. Thereafter, with Amazon no longer able to set below-cost prices, retail prices of ebooks rose. As the District Court found:

> [A]fter the iBookstore opened in April 2010, the price caps in the Agreements became the new retail prices for the Publisher Defendants' e-books. In the five months that followed, the Publisher Defendants collectively priced 85.7% of their New Release titles sold through Amazon and 92.1% of their New Release titles sold through Apple within 1% of the price caps. This was also true for 99.4% of the NYT Bestseller titles on Apple's iBookstore, and 96.8% of NYT Bestsellers sold through Amazon. The increases at Amazon within roughly two weeks of moving to agency amounted to an average per unit e-book retail price increase of 14.2% for their New Releases, 42.7% for their NYT Bestsellers, and 18.6% across all of the Publisher Defendants' e-books.

United States v. Apple Inc., 952 F. Supp. 2d 638, 682 (S.D.N.Y. 2013).

III. THE ANTITRUST TRIAL, JUDGMENT AND SETTLEMENT

A. Antitrust Judgment

The DOJ began investigating Apple's entry into the ebooks market and the negotiation of the Publisher Agreements in or around May 2010. The DOJ filed suit against Apple and the Publishers in April 2012, alleging violation of Section 1 of the Sherman Act. All of the Publishers settled before trial.

On July 10, 2013, after a three-week bench trial of the Antitrust Action before United States District Judge Denise Cote, the Court held that:

> The Plaintiffs have shown through compelling evidence that Apple violated Section 1 of the Sherman Act by conspiring with the Publisher Defendants to eliminate retail price competition and to raise e-book prices. … Apple not only willingly joined the conspiracy, but also forcefully facilitated it. ... This price-fixing conspiracy would not have succeeded without the active facilitation and encouragement of Apple.

Apple, 952 F. Supp. 2d at 691 (also referred to herein as the "Antitrust Order").

The Court found that "[i]n negotiating the caps for its pricing tiers, Apple understood that it was setting the new retail prices at which e-books would be sold." *Id.* at 692. The Court also found that "Apple included the MFN … both to protect itself against any retail price competition and to ensure that it had no retail price competition. Apple fully understood and intended that the MFN would lead the Publisher Defendants inexorably to demand that Amazon switch to an agency relationship with each of them." *Id.*

The Court determined that Apple's participation in the conspiracy was "essential" in that Apple "assured each Publisher Defendant that it would only move forward if a critical mass of the major publishing houses agreed to its agency terms. It promised each Publisher Defendant that it was getting identical terms in its Agreement in every material way. It kept each Publisher Defendant apprised of how many others had agreed to execute Apple's Agreements." *Id.*

The District Court examined the Publisher Agreements "in the context of the entire record" and determined that "the caps for the price tiers were the fiercely negotiated new retail prices for e-books and that the MFN was the term that effectively forced the Publisher

Defendants to eliminate retail price competition and place all of their e-tailers on the agency model." *Id*. at 699. "The issue is not whether an entity executed an agency agreement or used an MFN, but whether it conspired to raise prices." *Id*. While the District Court found that alone none of the provisions of the Publisher Agreements were illegal, it concluded that a combination of factors, including the contract provisions, the coordination among publishers, and Apple's facilitation of and participation in that coordination, rendered the conduct a per se violation of the Sherman Act. *Id.* at 698.

The District Court stated that: "The record at trial demonstrated a blatant and aggressive disregard at Apple for the requirements of the law. Apple executives used their considerable skills to orchestrate a price-fixing scheme that significantly raised the prices of E-books. This conduct included Apple lawyers and its highest level executives." August 27, 2013 Antitrust Action Hearing Transcript at 17. However, the DOJ did not institute any criminal or civil investigation or proceedings against any individual and no individual was found to be personally liable for any antitrust violations.

On September 5, 2013, the District Court entered final judgment and a permanent injunction (the "Final Judgment"). The Court found that Apple had not instituted an effective antitrust compliance program, so as part of the Final Judgment the Court appointed a Monitor with "the power and authority to review and evaluate Apple's existing internal antitrust compliance policies and procedures and the training program required by … this Final Judgment, and to recommend to Apple changes to address any perceived deficiencies in those policies, procedures, and training." Final Judgment at 11. The DOJ requested a ten year Monitor appointment, but the District Court appointed the Monitor for two years, subject to extension.

B. Monetary Settlement

On July 16, 2014, Apple agreed to pay $450 million to the Plaintiff States and to consumer class plaintiffs to settle claims conditioned on the outcome of its appeal of the District Court's liability finding.

C. Appellate Proceedings

On June 30, 2015, the United States Court of Appeals for the Second Circuit rejected Apple's appeal, with one extensive dissent. The majority opinion found:

> Apple wanted quick and successful entry into the ebook market and to eliminate retail price competition with Amazon. In exchange, it offered the publishers an opportunity to confront Amazon as one of an organized group … united in an effort to eradicate the $9.99 price point. Both sides needed a critical mass of publishers to achieve their goals. The MFN played a pivotal role in this *quid pro quo* by stiffen[ing] the spines of the [publishers] to ensure that they would demand new terms from Amazon, and protecting Apple from retail price competition.

United States v. Apple Inc., 791 F.3d 290, 305 (2nd Cir. 2015) (internal citations omitted). The dissent noted the unique nature of the case:

> [A]s the government conceded at oral argument, no court has previously considered a restraint of this kind. Several features make it sui generis: (a) a vertical relationship (b) facilitating a horizontal conspiracy (c) to overcome barriers to entry in a market dominated by a single firm (d) in an industry created by an emergent technology.

Id. at 348 (dissenting opinion, underline in original). The liability finding and injunction were upheld on appeal, causing Apple to pay the previously agreed $450 million settlement.

IV. THE DERIVATIVE ACTION

A. Procedural History

The initial derivative shareholder complaint was filed in August, 2014, less than one year into the Monitorship. The Amended Consolidated Complaint ("ACC") was filed on June 8, 2015. The SCAC was filed on March 2, 2016, after the Monitor was discharged.

The Derivative Plaintiffs allege wrongful conduct by Mr. Cue and nine former or current directors over three distinct time periods: (1) the period from November 2009 to April 2010, during which the Publisher Agreements were negotiated and signed; (2) the period from April 2010 to September 4, 2013, the day before the Final Judgment; and (3) the period from the Final Judgment on September 5, 2013, through the end of the Monitorship, on October 13, 2015. For the first period, the SCAC alleges that Mr. Cue's conduct as an Apple "officer" (which he was

not) in negotiating and entering into the agreements was a breach of fiduciary duty, that the directors at the time failed to establish and oversee compliance practices at Apple that would have prevented the antitrust violation, and that the directors themselves should have known about and stopped the transactions. For the second period, Plaintiffs allege that following the initiation of the action by the DOJ, the directors failed to institute an appropriate antitrust compliance program by the time of the Final Judgment. For the third period, Plaintiffs allege that the directors affirmatively interfered with the Monitor's efforts to establish a high quality antitrust compliance program and exposed Apple to the risk of contempt in the District Court.

Plaintiffs allege a single claim for breach of fiduciary duty derivatively on behalf of Apple against its Chief Executive Officer and director, Timothy D. Cook (claims are alleged against Mr. Cook solely based on his role as a director), Senior Vice President of Internet Software and Services, Eduardo Cue, Chairman of the Board, Arthur D. Levinson, current directors Albert A. Gore, Jr., Robert A. Iger, Andrea Jung, Ronald D. Sugar, and Susan L. Wagner, and former directors Millard S. Drexler and William V. Campbell. The Apple Directors have different board tenures. Accordingly the three periods of the Derivative Action apply to them as follows:

First Period (ebook negotiations)	Levinson, Gore, Drexler, Jung, Campbell
Second Period (iPad Launch through Final Judgment)	Levinson, Gore, Cook, Iger, Jung, Sugar, Drexler and Campbell
Third Period (Final Judgment/ Monitorship)	Levinson, Gore, Cook, Iger, Jung, Sugar, Drexler, Campbell and Wagner

Apple and the individual defendants demurred to the ACC. The Superior Court issued its ruling on that demurrer on December 21, 2015 (the "Order Re Demurrer"). The Court found that as to the first two periods, Plaintiffs had not sufficiently alleged that demand on the Board to undertake the derivative claim was futile. The Court found that Plaintiffs had sufficiently alleged demand futility only "with respect to the alleged non-compliance with the Final

Judgment," which is the third period identified by the Court. Order Re Demurrer at 21. Even though the ACC was deficient as to the first two time periods, the Court denied the demurrer as to the directors because Plaintiffs pleaded a single cause of action.

The Superior Court, however, sustained the demurrer as to Mr. Cue, finding that "Plaintiffs have not stated a viable cause of action … because [Cue] acted with advice from counsel while negotiating the [publisher] agreements and Plaintiffs do not allege that he acted without good faith." *Id.* at 21-22. The Superior Court granted Plaintiffs leave to amend the ACC. On March 2, 2016, Plaintiffs filed the SCAC.

On April 26, 2016, Apple's Board of Directors formed the SLC to investigate the derivative claim. On June 22, 2016, the SLC sought to stay the Derivative Action pending the results of its investigation. The Superior Court denied the motion to stay on August 1, 2016. Plaintiffs thereafter sought extensive discovery from Apple and the individual defendants at the same time that the SLC investigated the claims.

On November 15, 2016, the SLC and the Plaintiffs engaged in mediation with the Honorable Layn Philips, a retired federal district court judge, and one of the pre-eminent mediators in the United States. After the initial in-person mediation, the parties continued to mediate through Judge Philips.

On December 8, 2016, the Director Defendants (not including Ms. Wagner) filed a motion to strike certain allegations in the SCAC "on the ground that in those portions [covering the first two periods], Plaintiffs seek to assert claims based on conduct with respect to which the Court has previously found that Plaintiffs have failed to satisfy the demand requirement," and Mr. Cue filed a demurrer to the SCAC.

On January 20, 2017, the SLC distributed to Apple's Board and Plaintiffs the Cue Report, which summarizes the basis for the SLC's conclusion that dismissal of the claim against Cue is in Apple's and its shareholders' best interest. On March 3, 3017, as a result of mediation, the parties agreed upon settlement terms for the entire Derivative Action, and all motions and discovery ceased.

B. The Individual Defendants

In addition to Mr. Cue, the Derivative Plaintiffs named as defendants the following nine current and former members Apple's Board listed here in the order each joined the Board:

1. Defendant William V. Campbell

Mr. Campbell earned a bachelor's and master's degree from Columbia University. He joined Apple in July 1983 as Vice President of Marketing, was named Vice President of Sales in January 1984, and became Group Executive of the United States in June 1985. Mr. Campbell then became President and Chief Executive Officer of Claris Corp., which was purchased by Apple in 1990. He served as Intuit's President and Chief Executive Officer from 1994 to 1998. In 1998 he became Chairman of the Board of Directors of Intuit.

Mr. Campbell was a member of Apple's Board of Directors from 1997 to 2014. From at least February 2012 through May 2014 Mr. Campbell served on the Nominating and Corporate Governance Committee. In 2009 and part of 2012 Mr. Campbell served on the Compensation Committee. From at least January 2009 through May 2014 he served on the Audit & Finance Committee ("AFC"). Mr. Campbell passed away in April, 2016.

2. Defendant Millard S. Drexler

Mr. Drexler earned a bachelor's degree from the University of Buffalo and an MBA from Boston University. He was President and Chief Executive Officer of The Gap, Inc. from 1995 to September 2002, and also as its President from 1987 and as a director from November 1983 to October 2002. Mr. Drexler has been Chairman and Chief Executive Officer of J.Crew Group, Inc. since 2003. He also has served on the board of Warby Parker since September 2013 and on the board of Teach for America, Inc. since October 2011.

Mr. Drexler joined Apple's Board in 1999 and left the board in January 2015. From at least February 2008 through his departure, he was on both the Compensation Committee and the Nominating and Corporate Governance Committee.

3. Defendant Arthur D. Levinson

Dr. Levinson earned a Bachelor of Science degree from the University of Washington

and a doctorate in biochemical sciences from Princeton University. He served as Chief Executive Officer of Genentech, Inc. from July 1995 to April 2009, Chairman of Genentech from September 1999 to September 2014, and director of Google from 2004 to 2009. Dr. Levinson currently serves as Chief Executive Officer of Calico.

Dr. Levinson joined the Apple board in 2000 and served as Co-Lead Director from 2005 through November 2011. Since November 2011 he has served as Chairman of the Board. Since at least February 2008 Dr. Levinson has served as a member of the AFC. Dr. Levinson was on the Nominating and Corporate Governance Committee since at least February 2008 through November 2011. He was on the Compensation Committee in 2015.

4. Defendant Albert A. Gore, Jr.

Former Vice President Gore earned a bachelor's degree with high honors in government from Harvard University. He was elected to the U.S. House of Representatives in 1976, 1978, 1980 and 1982 and the U.S. Senate in 1984 and 1990. He was inaugurated as the 45th Vice President of the United States on January 20, 1993, and served for eight years.

Former Vice President Gore is the author of several bestselling books and the subject of an Oscar-winning documentary on climate change, as well as co-recipient of the 2007 Nobel Peace Prize for "informing the world of the dangers posed by climate change." He has served as chairman of Generation Investment Management, an investment management firm, since 2004, as a senior partner at Kleiner Perkins Caufield & Byers, a venture capital firm, since 2007, and is chairman of The Climate Reality Project, a non-profit devoted to solving the climate crisis.

Former Vice President Gore joined the Apple board in 2003. Since at least February 2008 he has been a member of both the Compensation Committee and the Nominating and Corporate Governance Committee.

5. Defendant Andrea Jung

Ms. Jung earned a bachelor's degree in English literature, magna cum laude, from Princeton University. She is the former Chair and Chief Executive Officer of Avon Products, Inc., serving as Chief Executive Officer from 1999 through April 2012, and as Chair of the

Board of Directors from 2001 through December 2012. She has been a member of the Board of Directors of the General Electric Company since 1998 and a member of the Supervisory Board of Daimler AG since 2013. She also serves on the Committee for Economic Development, an independent, nonprofit, nonpartisan American think-tank.

Ms. Jung joined the Apple board in 2008 and served as Co-Lead Director from at least February 2009 through February 2011. In 2010, she served on the Audit and Finance Committee. Since May, 2009, Ms. Jung has served on the Compensation Committee and has been its chair since February 2010. Since August 2014 Ms. Jung has served on the Nominating and Corporate Governance Committee.

6. Defendant Dr. Ronald D. Sugar

Dr. Sugar earned his bachelor's degree in electrical engineering, summa cum laude, from the University of California, Los Angeles, where he also received master's and doctorate degrees in the same field. He subsequently completed executive programs at Stanford University, The Wharton School of the University of Pennsylvania, and Harvard University. Dr. Sugar served as Chairman and Chief Executive Officer at Northrop Grumman Corporation from 2003 until his retirement in 2010. Before Northrop, he held executive positions at Litton Industries and TRW Inc., where he served as Chief Financial Officer. He is a member of the National Academy of Engineering, a fellow of both the American Institute of Aeronautics and Astronautics and the Royal Aeronautical Society, a director of Chevron Corporation, Amgen Inc. and Air Lease Corporation, and serves as a senior advisor to the private investment firm Ares Management LLC.

Dr. Sugar joined Apple's Board in 2010. He has been Chair of the AFC since November 2010.

7. Defendant Timothy D. Cook

Mr. Cook earned a Bachelor of Science degree in Industrial Engineering from Auburn University and an M.B.A. from Duke University, where he was a Fuqua Scholar. Prior to joining Apple, he served as vice president of Corporate Materials for Compaq, Chief Operating

Officer of the Reseller Division at Intelligent Electronics, and a director of North American Fulfillment at IBM.

Mr. Cook joined Apple in 1998 as Senior Vice President of Worldwide Operations. He became Apple's Chief Operating Officer in 2007. In 2011, Cook was named Apple's Chief Executive Officer and became a member of the Apple Board of Directors, positions he holds today.

8. Defendant Robert A. Iger

Mr. Iger earned a bachelor's degree in television-radio from Ithaca College. He was named President and Chief Operating Officer of ABC's corporate parent, Capital Cities/ABC, in 1994. In 2000, Mr. Iger was named President and Chief Operating Officer of The Walt Disney Company and became a member of Disney's board of directors. He assumed the title of President and Chief Executive Officer of Disney in 2005, and is currently Disney's Chairman and Chief Executive Officer. In 2010, President Barack Obama appointed him to the President's Export Council, which advises the President on how to promote U.S. exports, jobs, and growth.

Mr. Iger joined the Apple board in November 2011. From 2012 through 2015, Mr. Iger served on the AFC. Since August 2014, Mr. Iger has served on the Nominating and Corporate Governance Committee, and he has served on the Compensation Committee since 2016.

9. Defendant Susan Wagner

Ms. Wagner graduated with honors from Wellesley College with degrees in English and Economics, and earned an MBA in Finance from the University of Chicago, where she has received the Distinguished Alumni Award. After obtaining her MBA, Ms. Wagner worked at Lehman Brothers in New York City where she became a vice president, supporting investment banking and capital markets activities of mortgage and savings institutions. She left Lehman Brothers in 1988 to co-found BlackRock. BlackRock is currently the largest asset management firm in the world, managing over $4.3 trillion. At BlackRock she served as Vice Chair from 2006 to 2012. She also served as a member of BlackRock's Global Executive Committee and Global Operating Committee, as Chief Operating Officer, and as head of Corporate Strategy,

Corporate Development, Investor Relations, Marketing and Communications, Alternative Investments and International client businesses. She also served as Global Executive Sponsor of, and as a Director continues to support, BlackRock's Women's Initiative Network. Ms. Wagner retired in 2012 but continues to serve on the boards of BlackRock and DSP BlackRock (India). Ms. Wagner also serves on the Board of Directors of Swiss Re, Color Genomics, Wellesley College, and the Hackley School. She was named as one of Fortune Magazine's "50 Most Powerful Women in Business," included on similar lists published by the Financial Times and Crain's New York, and honored by the National Council for Research on Women.

Ms. Wagner joined Apple's Board in July, 2014, one month before the derivative action was instituted and at the time the Monitor was preparing his second of four reports. Ms. Wagner has served on Apple's AFC since August, 2014.

C. The Cause Of Action Against The Director Defendants

Plaintiffs' breach of fiduciary duty claim against the Director Defendants seeks "to hold them responsible for the harm they have caused and continue to cause to Apple, as a result of their reckless and/or conscious disregard of their duties in light of known inadequacies in their antitrust and other monitoring policies, their unexcused pattern of inattention amounting to an abdication of their duties to Apple and its shareholders; and their conscious inaction in light of the Final Judgment." SCAC, ¶ 36. Plaintiffs allege that the Director Defendants "violated and breached their fiduciary duties of care and loyalty." *Id.* at ¶ 328. Specifically, the Director Defendants are alleged to have "breached their duty of loyalty by failing to exercise reasonable oversight of Apple by: (i) failing to implement a reasonable system of internal controls and reporting systems designed to detect and prevent violations of antitrust laws and/or consciously disregarded the fact that the one policy in place was inadequate, notwithstanding red flags of the Company's penchant for engaging in antitrust violations; or (ii) consciously disregarding that Apple executives were causing or allowing Apple to facilitate an unlawful price-fixing conspiracy with the Publisher Defendants; by (iii) affirmatively refusing to comply with the Final Judgment." *Id.* at ¶ 329.

Plaintiffs' detailed allegations include the following:

- "Throughout the relevant period each of the Director Defendants, as former and current members of Apple's Board, had the duty and obligation to take steps such that neither the CEO nor Apple's senior management, including defendant Cue, engaged in illegal conduct, and to ensure that proper reporting procedures were in place such that they were kept sufficiently abreast and informed as to the CEO's and senior managements' activities." *Id*. at ¶ 106.

- "Apple's internal reporting systems and procedures were inadequate to enable the Board to detect or prevent the underlying misconduct, to monitor its senior managers, and most particularly Jobs and his executive team, thereby causing the Company to be liable for violating antitrust laws." *Id*. at ¶ 222.

- "Apple's entry into the billion dollar e-book market … should have been reviewed and evaluated by the entire Board because it involved a new industry that had the potential to generate substantial revenue for the Company. … But the Board, including defendants Cook, Levinson, Drexler, Gore, Jung, and Campbell, failed to conduct any review or evaluation whatsoever of Apple's strategy for selling e-books in connection with the launch of the iPad."[1] *Id*. at ¶ 224.

- "[T]he Board failed to consider whether the Company's internal reporting systems and controls were adequate to detect and prevent potential violations of antitrust laws on even one occasion in 2009 or 2010. Minutes from the meetings of Apple's Board and its committees show that defendants Cook, Levinson, Drexler, Gore, Jung, and Campbell failed to discuss or evaluate Apple's antitrust compliance controls at a single Board or committee meeting in 2009 or 2010." *Id*. at ¶ 226.

- "The Board members ignored red flags of the underlying misconduct, despite knowing that the Company, and particularly Jobs, had a penchant for engaging in actions in the high technology field to fix prices and restrain trade." *Id*. at ¶ 227.

- "[A]fter the Order, the Director Defendants on the Board knew that Apple has [sic] refused to comply fully with the Order and the Final Judgment and resisted and refused to cooperate with the Monitor appointed by the District Court." *Id*. at ¶ 233.

- "As a direct and proximate result of the Individual Defendants' actions (and conscious inactions), Apple has expended, and will continue to expend, significant sums of money associated with its unlawful anticompetitive agreements. Such expenditures include, but are not limited to, costs associated with defending, settling, and satisfying the Final Judgment entered in the Antitrust Action." *Id.* at ¶ 290.

V. THE SPECIAL LITIGATION COMMITTEE

A. The Law Governing Special Litigation Committees

Because the corporation is "a legal entity separate from its shareholders … when a corporation has suffered an injury to its property the corporation is the party that possesses the

[1] Cook was not on Apple's Board during the ebook negotiations in 2009-2010

right to sue for redress." *Desaigoudar v. Meyercord,* 108 Cal. App. 4th 173, 183 (2003). *See also Patrick v. Alacer Corp*., 167 Cal. App. 4th 995, 1003 (2008) ("[T]he particular stockholder who brings the [derivative] suit is merely a nominal party plaintiff. It is the corporation that is the ultimate beneficiary of such a derivative suit. Thus, [t]he corporation [is] the real party plaintiff in the action.") (brackets original, internal citations omitted).

When shareholders allege corporate wrongdoing, as is the case here, "the common practice is for the board to appoint a special litigation committee of independent directors to investigate the challenged transaction." *Desaigoudar*, 108 Cal. App. 4th at 185; *see also Will v. Engebretson & Co.,* 213 Cal. App. 3d 1033, 1040 (1989) ("The business judgment rule has been held … to permit a corporation to appoint a special litigation committee to decide whether the maintenance of a shareholder's derivative suit is in the corporation's best interests"). The special litigation committee concept furthers "the fundamental principle that those best suited to make decisions for a corporation—including the decision to file suit on its behalf—are its directors, not its stockholders or the courts." *Finley v. Superior Court,* 80 Cal. App. 4th 1152, 1163 (2000). Even where a shareholder's demand on a board of directors is excused, the board of directors may appoint a special litigation committee to determine whether pursuing the derivative litigation is in the best interest of the company. *Zapata Corp. v. Maldonado*, 430 A.2d 779, 786 (Del. 1981). As a duly appointed committee of the board, a special litigation committee has "all the authority of the board." Cal. Corp. Code § 311.

The fundamental business judgment issue for a special litigation committee is to determine whether it is in the corporation's best interests to pursue the claims alleged in the derivative lawsuit.

> [T]he decision whether and to what extent to explore and prosecute such claims lies within the judgment and control of the corporation's board of directors. Necessarily such decision must be predicated on the weighing and balancing of a variety of disparate considerations to reach a considered conclusion as to what course of action or inaction is best calculated to protect and advance the interests of the corporation.

Desaigoudar, 108 Cal. App. 4th at 187-88.

In considering the decision of the SLC, under California law the court does not substitute its judgment for the SLC's business judgment.[2] *Desaigoudar*, 108 Cal. App. 4th at 189. Rather, a court defers to the special litigation committee's business judgment if it determines (1) the "members of a special litigation committee were independent," *i.e.,* "whether each member was in a position to base his decision on the merits of the issue rather than being governed by extraneous considerations or influences"; and (2) the "committee employed proper procedures," which "involves an analysis of the committee's good faith" including "the procedures employed." *Id.* (citations omitted).

An SLC may determine in its business judgment that termination of a derivative action through settlement is in the corporation's best interests. *See e.g., In re Oracle Sec. Litig*., 852 F. Supp. 1437, 1440 (N.D. Cal. 1994) (approving settlement of derivative action "[o]n the basis of the report of Oracle's special litigation committee"). In *Oracle,* the Court applied Delaware law and approved a derivative settlement recommended by an SLC because the SLC exhibited independent judgment and acted in good faith in its investigation, and the SLC properly exercised its business judgment. *Id.* (applying *Zapata* approach to review independence, good faith, and reasonableness of SLC's decision). *See also, Carlton Invs. v. Tlc Beatrice Int'l Holdings,* 1997 Del. Ch. LEXIS 86, at *5 (Ch. May 30, 1997) (approving settlement negotiated by an SLC, applying Delaware law); *In re UnitedHealth Group Inc. Derivative Litig.*, 2009 Minn. Dist. LEXIS 121, *20 (Minn. Dist. Ct. 2009) (approving settlement negotiated by an SLC, applying Minnesota law). As explained below, the SLC was specifically empowered to settle the Derivative Action, and has determined that settlement is in Apple's and its shareholders' best interest.

B. Establishment Of The SLC

On April 26, 2016, Apple's Board of Directors formed the SLC by unanimous vote, and gave it full responsibility for the claims asserted in the SCAC. The resolution forming the SLC

[2] In contrast, under Delaware law the court reviews the business judgment of the SLC. *Zapata*, 430 A.2d at 789.

states:

> [T]o the fullest extent permitted by the Bylaws and applicable law, the Special Litigation Committee shall have the authority to investigate and evaluate any and all claims and allegations asserted in the Actions and to pursue, litigate, settle, or otherwise dispose of any and all claims and allegations asserted in the Actions, in whatever manner the Special Litigation Committee deems reasonable and necessary to enable it to discharge its responsibilities.

On July 17, 2016, Apple's Board approved a resolution confirming the SLC's full and exclusive authority over the Actions. The SLC is composed of two Apple directors, Susan L. Wagner and James A. Bell. Ms. Wagner's background is described above, in Section IV.B.9.

Mr. Bell joined Apple's Board in October, 2015, the same month the Monitor was discharged. Mr. Bell has served on Apple's AFC since January, 2016. Mr. Bell received his bachelor's degree in accounting from California State University, Los Angeles. In 1972, Mr. Bell began working at Rockwell International and ultimately became Manager of General and Cost Accounting. In 1996, Mr. Bell became Vice President of Contracts and Pricing at The Boeing Company. In that position, he oversaw policy direction, acquisition reform, new business opportunities and program performance. In 2004, he became Chief Financial Officer of Boeing, at that time a $52 billion, 157,000-person commercial airplane and defense company. From 2008 through 2011, he served as CFO and Corporate President of The Boeing Company. As CFO, Mr. Bell was responsible for the company's overall financial management, reporting, and transparency. He also oversaw multiple corporate functions, including Controller, Treasury, investor relations, corporate and strategic development, and customer-financing activities. Mr. Bell oversaw Boeing Capital Corporation and Boeing Shared Services during his 38-year career at Boeing, and was interim CEO of The Boeing Company in 2005. Mr. Bell retired from The Boeing Company in 2012.

Mr. Bell has served since 2005 as a director of Dow Chemical Company. In 2011 Mr. Bell joined the Board of Directors and Audit Committee of JP Morgan Chase. He has served since March, 2015, as a director of CDW Corporation, a Fortune 500 company that provides

technology solutions to business, government, education, and healthcare. He is a member of the Board of Trustees at Rush University Medical Center. In 2004 Mr. Bell was honored as a Distinguished Alumnus of the College of Business and Economics by California State University, Los Angeles.

C. Retention Of Counsel

Shortly after the SLC was formed, its members interviewed several counsel and ultimately retained the law firm of Shartsis Friese LLP ("Shartsis") to assist in conducting its investigation and evaluation. Shartsis had no role in the ebook negotiations or the antitrust litigation, and has never represented any of the individual defendants. Other than a Shartsis real estate partner who worked on two small real estate transactions for Apple between July 2012 and September 2013 (totaling approximately 45 hours of work), Shartsis has never represented Apple in any matters.

Counsel provided the SLC members guidance regarding the legal standards governing SLCs generally, legal standards regarding the claim alleged, and assisted the SLC in conducting its investigation, negotiating the settlement, preparing the Cue Report and this Report. Shartsis Partners Arthur Shartsis, Jahan Raissi, Frank Cialone, Larisa Meisenheimer, and Associate (now Partner) Kajsa Minor have had primary responsibility for assisting the SLC as necessary.

Arthur Shartsis received a bachelor's degree in 1967 from the University of California at Berkeley where he was valedictorian. He pursued graduate studies at Oxford University in 1968, and obtained a juris doctor in 1971 from Berkeley Law (Boalt Hall). In 1975, he co-founded Shartsis Friese LLP. He specializes in complex litigation, including fiduciary, financial, antitrust, and securities litigation. He has represented major corporations, global law firms, federal and state court judges, public entities, a number of California Constitutional Officers, including the Governor, and the States of California and Hawaii. He has tried cases in state and federal courts and in arbitration forums and argued cases in state and federal appellate courts, including the California Supreme Court, and he successfully opposed a petition for a writ of certiorari to the United States Supreme Court. He has been listed in *Best Lawyers in America*

since 1991. The Los Angeles and San Francisco Daily Journal identified Mr. Shartsis in its special American Bar Association Convention Edition as one of the top 14 litigators in California. He is the founding President of the Association of Business Trial Lawyers of Northern California. He was elected to, and served as President of, the BART Board of Directors.

Jahan Raissi is the Chair of Shartsis' Securities Enforcement Defense Group. He obtained his juris doctor from the University of California, Hastings College of the Law *cum laude* in 1993. He was a Senior Counsel in the Division of Enforcement of the Securities and Exchange Commission in Washington D.C., where he handled investigations and litigation involving, among other things, internal corporate controls, public company disclosures and periodic reports, and insider trading. He represents boards, officers, directors and entities before federal and state securities regulators, before self-regulatory organizations and in private litigation. He has represented individuals and corporations with regard to derivative claims. His principal areas of practice are SEC enforcement matters, DOJ/US Attorney investigations, securities litigation, internal investigations, and regulatory compliance.

Frank Cialone co-chairs Shartsis' Litigation Department. He obtained a bachelor's degree from Brown University in 1987 and a juris doctor from the University of California at Berkeley in 1994. His practice focuses on fiduciary litigation matters, including disputes involving the duties of directors and officers. He counsels clients at all stages of disputes, from pre-filing negotiations to litigation through arbitration or trial.

Larisa Meisenheimer co-chairs Shartsis' Litigation Department. She obtained a bachelor's degree *cum laude* from Pomona College in 1999 and a juris doctor from Stanford Law School in 2003, where she graduated Order of the Coif. She was a Deputy District Attorney in Multnomah County (Portland), Oregon, where she tried more than 20 cases, and regularly argued constitutional motions and civil commitment hearings. She has extensive experience counseling clients on antitrust and unfair competition law and representing clients in antitrust and unfair competition litigation.

D. SLC Independence

A properly formed special litigation committee is comprised of board members capable of independently and objectively investigating the underlying claims and making a determination of the company's best interests with regard to those claims. "In considering … whether the members of a special litigation committee were independent—the court must determine whether each member was 'in a position to base his decision on the merits of the issue rather than being governed by extraneous considerations or influences.'" *Desaigoudar*, 108 Cal. App. 4th at 189 (*citing Katz v. Chevron Corp*., 22 Cal. App. 4th 1352, 1367 (1994) and *quoting Kaplan v. Wyatt*, 499 A.2d 1184, 1189 (Del. Oct. 9, 1985)). Where a director is subject to "direct and substantial" liability for the claims investigated by a special litigation committee, that director may lack the requisite independence to serve on the committee. *Johnson v. Hui*, 811 F. Supp. 479, 486 (N.D. Cal. 1991).

Ms. Wagner and Mr. Bell are independent board members as to the claims against the Director Defendants. Ms. Wagner joined Apple's Board in July 2014, which was more than one year after the District Court's Antitrust Order was issued. Mr. Bell joined the Board later, in October, 2015. Prior to joining Apple's Board, neither SLC member had any personal or professional relationship with any of the defendants or with Apple. Their evaluation of the claims asserted in the SCAC is untainted by extraneous influences. Both SLC members are independent and capable of objectively analyzing the derivative claims and determining the course of action that is in Apple's best interests.

In opposing the SLC's request for a stay of the Derivative Action, the Derivative Plaintiffs asserted that Ms. Wagner may not be independent because she is a defendant and she demurred to their claim. Simply being a named defendant in a derivative action does not render a director interested for purposes of serving as a member of a special litigation committee, as uniform case law holds. *Moradi v. Adelson*, 2012 U.S. Dist. LEXIS 121092, at *12 (D. Nev. Aug. 27, 2012) ("[M]erely being named as defendants does not establish that [special litigation committee members] are not independent."); *Johnson,* 811 F. Supp. at 487 (Finding that SLC

member's "nominal appearance as a defendant does not undermine his ability to operate as an independent and unbiased member of the SLC."); *Spiegel v. Buntrock*, 571 A.2d 767, 774 n.14 (Del. 1990) ("[T]he fact that all directors are named as defendants in a derivative complaint is not determinative of their lack of independence."). If a derivative plaintiff could disqualify every director by merely suing them, derivative plaintiffs could easily disqualify entire boards, or force boards to change or add directors in order to maintain control over the company's claims. Here, in fact, the Plaintiffs named every Apple director other than Mr. Bell, who joined the Board after all events alleged in the SCAC.

The fact that Ms. Wagner demurred to Plaintiffs' ACC does not compromise her independence. Once sued, a director—particularly a director who has no liability and about whom no specific facts are alleged—is entitled to defend herself, and does not have to choose between losing independence or defending herself. *See e.g., Strougo ex rel. Brazil Fund v. Padegs*, 986 F. Supp. 812, 815 (S.D.N.Y. 1997) (rejecting plaintiff's argument that an SLC member who was a defendant lacked independence because he moved to dismiss the claims).

In evaluating the SLC's independence, the court looks not at the allegations of the complaint but at the facts and evidence. *Gaines v. Haughton*, 645 F.2d 761, 772 (9th Cir. 1981) (affirming dismissal of derivative suit because plaintiff "has not raised a triable issue of fact" as to independence). There are no actionable facts, acts or omissions alleged against Ms. Wagner in the SCAC for the period that Ms. Wagner has served on Apple's Board. Plaintiffs allege only the dates of Ms. Wagner's board service and her compensation. *See* SCAC, ¶¶ 99, 295. Plaintiffs' only claim that could arguably apply to Ms. Wagner is that the entire Board interfered with the Monitor and failed to comply with the Final Judgment after July of 2014, which created a risk that Apple would be held in contempt of court. *Id.* at ¶¶ 268-89. Since the Monitor was discharged by the District Court after the minimum two year period, without Apple ever being found in contempt of any Court order, there is no possibility of contempt as alleged by Plaintiffs and therefore no basis for a claim against Ms. Wagner.

Ms. Wagner fully cooperated with the Monitor and has consistently supported Apple's

efforts to institute a comprehensive antitrust compliance program. The Monitor confirmed in his interview with the SLC that, contrary to the allegations in the SCAC regarding the Director Defendants, Ms. Wagner was fully cooperative with the Monitorship. The Monitor reported to the SLC that Ms. Wagner "was the best director at Apple" who he dealt with, and that Ms. Wagner gave him "no trouble whatsoever." He further reported that he had no reason to believe that any Apple director did anything to interfere with the Monitorship. He said he had no reason to doubt that the directors were supportive of Apple developing a quality Antitrust compliance program: "I never got the sense that any member of the Board of Directors was opposed to having Apple either have a best in class program or improve its Antitrust Compliance Program." Accordingly, Ms. Wagner faces no risk of liability that could impact her independence.

The SLC's counsel is also independent. "'[I]ndependent' counsel" for purposes of a special litigation committee, "means counsel that was not associated with the challenged transactions." *Desaigoudar*, 108 Cal. App. 4th at 195. Shartsis Friese had no role whatsoever in, or related to, the ebook negotiations, the related Antitrust Action, or the Monitorship.

VI. THE SLC'S INVESTIGATION

The SLC's investigation had the benefit of a voluminous trial record from the Antitrust Action. The SLC also obtained company and Board documents from Apple and interviewed relevant witnesses including the Monitor, Apple personnel, and defendants. Mr. Jobs and Mr. Saul were not interviewed because they both passed away before the SLC was created. Below is a summary of the SLC's investigative work.

A. Documents Reviewed

The SLC and its counsel obtained a large volume of documents from Apple and publically available sources relevant to the claim asserted in the SCAC. In total, the SLC's counsel reviewed more than 17,000 documents. The SLC and its counsel's review included the following documents:

- Documents regarding Apple's antitrust compliance policies from 2009 to the present

- All documents and emails produced by Apple in the Antitrust Action authored by or sent to Steve Jobs between 11/1/09 and 4/1/10
- All documents and emails produced by Apple in the Antitrust Action authored by or sent to Eduardo Cue between 11/1/09 and 4/1/10
- All documents and emails produced by Apple in the Antitrust Action authored by or sent to Kevin Saul between 11/1/09 and 4/1/10
- All documents and emails produced by Apple in the Antitrust Action authored by or sent to Keith Moerer between 11/1/09 and 4/1/10
- Contracts with the Publishers concerning ebooks
- Deposition transcripts and exhibits for Apple employees in the Antitrust Action:
  - Alcorn, Peter
  - Cook, Tim
  - Cue, Eddy
  - Fortstall, Scott
  - Gray, Eric
  - Kellermann, Beth
  - Lilie, Barbara
  - McDonald, Robert
  - Moerer, Keith
  - Robbin, Jeffrey
  - Saul, Kevin
  - Schiller, Phil
  - Tchao, Michael
- Deposition transcripts and exhibits for Publishers in the Antitrust Action:
  - Dohle, Markus
  - Eulau, Dennis
  - Foy, Fritz
  - Gigante, Alexander
  - Heffernan, Richard

  - Hely-Hutchinson, Timothy
  - Hirschhorn, Elinor
  - Hulse, Leslie
  - Kennedy, Susan
  - Lazarus, Alison
  - Makinson, John
  - McCall, Tim
  - McIntosh, Madeline
  - Murray, Brian
  - Napack, Brian
  - Nourry, Arnaud
  - Protti, Casey
  - Reidy, Carolyn
  - Salat, Rudiger
  - Sargent, John
  - Shanks, David
  - Shore, Genevieve
  - Stroh, Jane
  - Thomas, Maja
  - Williams, Coram
  - Young, David
- Pre-trial submissions in the Antitrust Action
- Opening statements and closing arguments in Antitrust Action
- Trial testimony and exhibits (excluding certain third-party internal documents) for all fact witnesses in the Antitrust Action:
  - Cue, Eddy
  - Grandinetti, Russell
  - Horner, Theresa

- McDonald, Robert
- Moerer, Keith
- Murray, Brian
- Naggar, David
- Porco, Laura
- Reidy, Carolyn
- Sargent, John
- Saul, Kevin
- Shanks, David
- Turvey, Thomas
- Young, David

- Briefing and Circuit Court opinion related to Apple's appeal of Judge Cote's Final Judgment
  - 7/14/2014 Appellant Apple's Opening Brief
  - 7/14/2014 Appellant Apple's Reply Brief
  - 7/15/2014 Appellees United States and Plaintiff-States Joint Brief
  - 6/30/2015 Second Circuit Opinion

- Briefing, orders, and hearing transcripts relating to the injunction issued by Judge Cote and the appointment of the Monitor
  - 8/2/2013 Plaintiffs' Memorandum of Law ISO Proposed Injunction
  - 8/2/2013 Apple's Memorandum of Law in Response to Proposed Injunction
  - 8/7/2013 Settling Defendants' Memorandum of Law in Opposition to Proposed Injunction
  - 8/8/2013 Letter from Department of Justice
  - 8/23/2013 Plaintiffs' Memorandum of Law In Support of Revised Proposed Injunction
  - 8/23/2013 Declaration of L. Buterman In Support of Plaintiffs' Revised Proposed Injunction
  - 8/26/2013 Letter from Apple
  - 8/27/2013 Transcript of Proceedings Held 8/27/2013

- 9/5/2013 Letter from Department of Justice
- 9/5/2013 Judge Cote Order re Injunction and Final Judgment
- 10/16/2013 Judge Cote Order re Appointing Monitor

- Briefing, orders, and hearing transcripts related to Apple's challenges to the Monitor and efforts to stay the Monitorship
  - 10/16/2013 Order
  - 11/21/2013 Order
  - 11/27/2013 Objections Re Order
  - 11/27/2013 Declaration of Theodore J. Boutrous In Support of Objection to Order
  - 12/2/2013 Order
  - 12/13/2013 Order
  - 12/14/2013 Defendant Apple's Memorandum Of Law In Support Of Its Motion By Order To Show Cause For A Stay Of The Injunction Pending Appeal
  - 12/14/2013 Declaration of G. Levoff
  - 12/14/2013 Declaration of T. Boutrous
  - 12/14/2013 Letter Addressed To Judge Denise L. Cote From Lawrence Buterman Re: Apple's Proposed Order To Show Cause
  - 12/23/2013 Transcript for Hearing on Dec. 13, 2013
  - 12/30/2013 Plaintiffs' Memorandum of Law in Opposition to Apple Inc.'s Motion to Show Cause for a Stay of the Injunction Pending Appeal
  - 12/30/2014 Declaration of Michael R. Bromwich in Opposition to Apple Inc.'s Motion to Show Cause for a Stay of the Injunction Pending Appeal
  - 1/7/2014 Letter Addressed To Judge Denise L. Cote From Theodore J. Boutros Jr. Re: Objections To The External Compliance Monitor
  - 1/7/2014 Declaration of C. Richman
  - 1/7/2014 Reply Memorandum In Support of Apple's Motion By Order To Show Cause For A Stay Of The Injunction Pending Appeal
  - 1/7/2014 Declaration of K. Andeer
  - 1/7/2014 Declaration of M. Reilly
  - 1/7/2014 Declaration of T. Boutrous

- 1/8/2014 Letter Addressed To Judge Denise L. Cote From Lawrence E. Buterman Re: Apple's Reply Memorandum

- 1/10/2014 Plaintiffs' Sur-Reply in Opposition to Apple Inc.'s Motion to Show Cause for a Stay of the Injunction Pending Appeal

- 1/10/2014 Supplemental Declaration of Michael Bromwich

- 1/16/2014 Order

- 2/19/2014 Order

- 2/20/2014 Letter Addressed To Judge Denise L. Cote From Theodore J. Boutrous, Jr. Re: Monitorship Issues

- 2/20/2014 Order

- Unredacted versions of the four Monitor Reports, including all exhibits
  - April 14, 2014 - First Monitor Report
  - October 14, 2014 - Second Monitor Report and Exhibits A - F
  - April 14, 2015 - Third Monitor Report and Exhibits A - G
  - October 5, 2015 - Fourth Monitor Report and Exhibits A - Q

- Briefing and orders relating to the discharge of the Monitor
  - 10/5/2015 - Order - Discharge Order
  - 10/6/2015 - Letter Addressed To Judge Denise L. Cote From Michael R. Bromwich In Response To The Court's October 5, 2015 Order Concerning, Among Other Matters, The Fourth Report Of The External Compliance Monitor
  - 10/12/2015 - Letter Addressed To Judge Denise L. Cote From Plaintiffs And Apple Re: October 5, 2015 Order Instructing The Parties To Provide Positions In Writing On Whether The Monitorship Should Be Extended
  - 10/13/2015 - Order

- All correspondence between the Monitor and Apple or Apple's counsel

- Published articles regarding the Monitorship

- Board resolutions regarding the SLC

- Apple's Bylaws in effect since 2009

- Relevant Board and Board Committee packages, agendas, and minutes from January 2009 to August 2016

- Relevant Audit and Finance Committee agendas, packages, and minutes from January 2009 to May 1, 2016

- Reports presented by Apple's Antitrust Compliance Officer and her communications with the Board from November 2013 to August 2016
- Reports presented by Apple's Chief Compliance Officer to the Board from January 2009 to August 2016
- Reports presented by Apple's VP of Internal Audit to the Board from January 2009 to May 1, 2016
- Apple Form DEF 14A Annual Proxy Statements filed with the SEC
- PricewaterhouseCooper LLP's Report regarding Apple's antitrust policies
- Apple's Indemnity Agreements with its officers and directors
- *Steve Jobs,* Walter Isaacson (Simon & Schuster 2011) (quoted extensively in the SCAC)

B. Interviews

The SLC, with and through counsel, conducted fifteen formal interviews. The SLC members participated in interviews of Eduardo Cue, Apple directors[3] and key employees, and the Monitor. In addition to those interviews, counsel conducted a number of interviews with Apple's outside counsel and other Apple employees with relevant information. The following individuals were formally interviewed in connection with the SLC's investigation:

- Andeer, Kyle - Apple Senior Director, Sales & Retail/Competition Law & Policy
- Bromwich, Michael - Court Appointed Monitor
- Cue, Eduardo - Apple Senior Vice President, Internet Software and Services
- Drexler, Millard S. - former Apple Board Member
- Gore Jr., Albert - Apple Board Member
- Jung, Andrea - Apple Board Member, Chair of Compensation Committee

[3] The SLC did not interview directors Iger and Cook because the case settled before those interviews were conducted. The allegations against Mr. Iger and Mr. Cook relate only to the second period between the iPad launch and the Final Judgment, and the third period regarding the Final Judgment, since neither director was on the Board during the ebook negotiations. As noted in this report, the allegations against all Director Defendants are contrary to the evidence, including what the SLC learned directly from the Monitor. The SLC is satisfied that its conclusions are fully supported by extensive evidence regarding the claims against all of the Director Defendants. Accordingly, under the circumstances, interviews of directors Cook and Iger were viewed as unnecessary in order to complete this report in support of the settlement of the Derivative Action.

- Levinson, Dr. Arthur D. - Apple Board Member, Board Chair
- Moerer, Keith - Apple Director, iBooks
- Moyer, Tom - Apple Chief Compliance Officer, Head of Global Security
- Putnam, Sara - PricewaterhouseCoopers LLP Partner
- Reilly, Matthew - Former Simpson Thacher & Bartlett LLP Partner
- Richman, Cynthia - Gibson Dunn & Crutcher LLP Partner
- Said, Deena - Apple Antitrust Compliance Officer
- Sugar, Dr. Ronald D. - Apple Board Member, Chair of Audit and Finance Committee
- Vetter, Doug - Apple Vice President, Associate General Counsel, Assistant Secretary

The SLC requested but was denied meetings with the attorneys at the Department of Justice who prosecuted the Antitrust Action, with counsel for the class action plaintiffs, and with counsel for the Derivative Plaintiffs.

C. SLC Meetings

In addition to phone calls and emails, the SLC formally met twenty (20) times, and maintained minutes of those meetings.

VII. APPLE'S ANTITRUST COMPLIANCE PROGRAM BEFORE THE MONITORSHIP

Below is a summary of Apple's antitrust compliance program and Board oversight of that program before, during and after the ebook negotiations, which is based on the SLC's extensive review of documents and witness interviews.

A. Apple's Antitrust Compliance Program Before and During the Ebook Negotiations

Prior to the ebook negotiations, which took place in late 2009 and early 2010, Apple had a written Antitrust and Competition Law Policy and Business Conduct Policy that was available to its employees as of March 2009, and had been presented to and discussed with the Board. Those policies were developed and instituted as part of Apple's corporate compliance efforts, led by Eric Pressler, who served as the head of compliance from March 2006 to September 2009.

Prior to working at Apple, Mr. Pressler was the Chief Compliance Officer of Pacific Gas & Electric. Apple's Business Conduct Policy included a handbook, a helpline, training programs, and identification of areas of regulatory risk. Thus, as of March 2009, Apple's antitrust-related compliance policies included: (1) a stand-alone Antitrust and Competition Law Policy (the "Antitrust Policy"); and (2) a section of Apple's Business Conduct handbook dedicated to "Competition and Trade Practices" (the "Business Conduct Policy").

The Antitrust Policy expressed Apple's commitment "to conducting business ethically, honestly, and in full compliance with applicable laws and regulations, including U.S. and international antitrust and competition laws." It further provided that "[v]iolations of this Antitrust and Competition Law Policy or related legal requirements may result in disciplinary action up to and including termination of employment." The Antitrust Policy contained the following detailed description of conduct prohibited by the antitrust laws:

- **Price-Fixing Agreements**. Price-fixing, which is illegal in addition to being against Apple policy, involves competitors agreeing among themselves on the prices they will charge. This includes any agreement on 1) final price to customers, 2) components of price, 3) a process to set price, or 4) whether to bid or not bid in a competitive market. Avoid any discussions with a competitor involving price, price setting, or bidding.

- **No Market Allocation Agreements**. Agreements among competitors not to compete, based on the allocation of certain markets or market segments, are illegal. These illegal agreements may include the allocation of customers, territories or product markets. A good example is an understanding that one company will only sell in the northern half of a country, state or city, and the other company will only sell in the southern half. Avoid any discussions with competitors that could be perceived as an attempt to allocate markets and reduce competition.

- **No Group Boycotts**. Group boycotts involve two or more competitors deciding that they will not deal with (boycott) a particular customer, reseller, or supplier in order to affect price or competition. Avoid any discussions with competitors related to restrictions on doing business with specific customers, resellers or suppliers unless you have cleared the matter with the Legal Department in advance.

- **Communications with Competitors**. Avoid any unnecessary contact or communications with competitors. When there are interactions with competitors, such as at a trade association or standards body meeting, be extremely careful in what you say and never participate in even casual discussions regarding matters such as price, terms of sale, bids, discounts, promotions, costs, inventories, product plans, marketing plans, resellers, suppliers, or any confidential information.

- **Comments Regarding Competitors**. When selling Apple products and services,

Apple employees may comment accurately on the advantages of Apple's offerings relative to those of competitors. False or misleading remarks about competitors or their products must not be made. Make sure all comments of this nature are accurate, honest, fair, factual and defensible.

- **Additional Restrictions Based on Large Market Share**. A company that has a significant share of the market for a product or service in a particular geographic region may be viewed as having a monopoly or a dominant market position. Those with a dominant market position may be subject to additional scrutiny by government officials to ensure that illegal predatory or exclusionary conduct, such as excessively high prices, below-cost discounting or a refusal to supply, is not taking place. Any sales or marketing activities that could potentially be viewed as predatory or exclusionary must be reviewed with the Legal Department in advance if the activities related to matters where Apple has a significant share of the relevant market.

- **Additional Geographic Considerations**. Within the U.S., various states may impose their own additional competition rules. Outside the U.S., there may be country- or region-specific competition requirements or restrictions. Contact the Legal Department to determine how these requirements or restrictions might impact Apple's activities.

The Antitrust Policy also prohibited anticompetitive conduct when interacting with channel members (defined as "third-party companies and individuals involved in the authorized sale and distribution of Apple products and services."). In addition to educating Apple employees regarding prohibited practices, the Antitrust Policy warned employees that antitrust law is complex and fact-specific and encouraged Apple employees to seek advice from Apple's legal department to ensure compliance with antitrust laws.

The Business Conduct Policy proscribed engaging in potentially anticompetitive conduct. Specifically, it informed employees that they should not:

- Agree with competitors or exchange information with competitors on prices, policies, contract terms, costs, inventories, marketing plans, or capacity plans.

- Agree with a competitor that the competitor will sell goods and services to customer A (and you will not), and that you will sell goods and services to Customer B (and your competitor will not).

- Agree with resellers on the resale pricing of Apple products without Legal Department approval.

- Require vendors to purchase Apple products in order to sell products or services to Apple.

- Describe the products or services of competitors inaccurately to promote Apple products or services.

- Engage in any pricing or other practices that could defraud a supplier or others.
- Violate fair bidding practices, including bidding quiet periods.

Apple employees had access to both the Antitrust Policy and the Business Conduct Policy through Apple's internal employee website, where they were posted in March 2009.

Prior to the ebook negotiations, Apple's Board was informed of the updated Antitrust Policy and Business Conduct Policy. The directors on the Board at the time, including defendants Campbell, Drexler, Gore, Jung, and Levinson, discussed the updated policies with Apple's General Counsel. The availability of the policies to employees was also reported to the Board. Consequently, at the time of the ebook negotiations, Apple had in place an updated Antitrust Policy instituted by Apple's top compliance personnel under the Board's oversight.

In addition to Apple's compliance policies described above, from 2009 to the present, Apple has had a reporting system that enables Apple's Board to supervise Apple's compliance programs and risk management. The Board's Audit and Finance Committee ("AFC"), which is comprised of at least three Apple Board members and meets at least quarterly, is charged with oversight and monitoring of, among other things, Apple's "systems of internal controls," and is charged with reviewing and discussing "with management the program that management has established to monitor compliance with the Corporation's Business Conduct Policy." In the years preceding and following the ebook negotiations, the AFC received quarterly business conduct and compliance reports directly from compliance personnel. The AFC also received internal audit updates and reporting from the Vice President, Internal Audit, Christopher Keller. Mr. Keller's presentations included analysis of various business risks, including antitrust. The AFC reported to the full Board regarding compliance at the Board's quarterly meetings. There were no indications that Apple's antitrust compliance programs were deficient in any way or that Apple had any imminent risk of an antitrust violation.

B. Apple's Antitrust Compliance Program from 2010-2013

During the period between the conclusion of the ebook negotiations in early 2010 and the Final Judgment in the Antitrust Action in September, 2013, Apple was actively reviewing, and

where appropriate, enhancing its compliance policies in all areas of the Company, including antitrust compliance. Prior to the ebook negotiations, in September 2009, Apple's Director of Employment Law, Tom Moyer, became its Chief Compliance Officer ("CCO"). Upon becoming CCO, Mr. Moyer conducted a review of Apple's compliance policies, and worked with compliance personnel to update and enhance those policies. Nothing came to Mr. Moyer's attention at this time, or at any time, that indicated a significant antitrust risk for Apple, or that indicated any antitrust risk related to the ebook negotiations.

In mid-2010, Apple created a Risk Oversight Committee ("ROC") that reported directly to the AFC. The ROC was led by Apple's VP Internal Audit, Christopher Keller, and was charged with assisting the AFC in fulfilling its oversight responsibilities regarding (a) risks inherent to the business of the Corporation, (b) the identification, assessment, management, and monitoring of those risks, and (c) risk management decisions, practices, and activities of the Corporation. In early 2011, the ROC commenced an internal audit of Apple's business risks, including antitrust risk, which culminated in a presentation to the Board. Thereafter, Mr. Keller regularly presented the Board quarterly updates of the activities of the ROC, which included the ROC's assessment of antitrust risk and ongoing mitigation projects.

In November 2010, Apple created the position of Director of Competition Law and Policy to enhance its antitrust compliance efforts and hired Kyle Andeer, an attorney with extensive antitrust law expertise. Prior to joining Apple, Mr. Andeer worked at the Department of Justice's Antitrust Division in Washington D.C., where he prosecuted antitrust violations for five years, and at the San Francisco office of the Federal Trade Commission's ("FTC") litigation department working on antitrust issues. Mr. Andeer reported directly to Bruce Sewell, Apple's General Counsel.

Mr. Andeer focused on building the competition law group at Apple. Mr. Andeer immediately reviewed Apple's antitrust compliance policies. He met with Apple CCO Tom Moyer and the legal department to understand the current training, policies and practices. He also met with Apple's senior executives, particularly those in areas with potential exposure to

antitrust violations. Mr. Andeer then focused on updating the Antitrust Policy, the Business Conduct Policy, and Apple's employee training programs, including both online and in-person training. Mr. Andeer also worked closely with Mr. Moyer to evaluate enterprise risk across the company, including competition law risks. After Mr. Andeer arrived at Apple, he recruited to Apple's Competition Law Group Sean Dillon in November, 2011, and Brendan McNamara in February, 2014, both of whom are former deputy assistant directors at the FTC.

Throughout the time period from 2010 through 2013, the AFC received quarterly risk oversight updates from Mr. Keller, Business Conduct and Compliance updates from Mr. Moyer and legal updates from Mr. Sewell, including updates about antitrust compliance. Dr. Ronald Sugar, head of the AFC starting in November 2010, was actively involved, and communicated with compliance personnel regularly outside of scheduled AFC meetings. The AFC, in turn, presented updates concerning the reports it received to the full Board at its quarterly meetings.

VIII. APPLE'S RESPONSE TO THE FINAL JUDGMENT

As a part of the Final Judgment, the District Court ordered Apple to hire a full-time Antitrust Compliance Officer and ordered the appointment of a Monitor to oversee the development of improved antitrust compliance programs at Apple. This section summarizes Apple's response to the Final Judgment.

A. Apple's Antitrust Compliance Officer

The District Court ordered Apple to hire a new employee to serve as an Antitrust Compliance Officer, "who shall report to the Audit Committee or equivalent committee of Apple's Board of Directors and shall be responsible, on a full-time basis until the expiration of this Final Judgment, for supervising Apple's antitrust compliance efforts…." Final Judgment at 8. Apple hired Ms. Deena Said, an attorney with compliance experience at Hitachi Data Systems, to be its Antitrust compliance Officer ("ACO"). With Board approval, she was hired in November 2013, to develop and implement improved antitrust compliance policies pursuant to the Final Judgment. She met with the AFC on her first day at Apple, and reported directly to the

AFC and its committee chair, Dr. Sugar.

B. The Monitorship

The Monitor was charged with assessing "whether Apple's internal antitrust compliance policies and procedures, as they exist 90 days after his or her appointment, are reasonably designed to detect and prevent violations of the antitrust laws," and "whether Apple's training program … as it exists 90 days after his or her appointment, is sufficiently comprehensive and effective." Final Judgment at 11. The court authorized the Monitor to make "recommendations reasonably designed to improve Apple's policies, procedures, and training for ensuring antitrust compliance," and ordered that, if Apple objected to any such recommendation, Apple would have to reach agreement with the Monitor on "an alternative policy, procedure, or system designed to achieve the same result" or apply to the District Court for relief. *Id.* at 12.

The relationship between Apple and the Monitor was contentious from the beginning. There were disputes over the Monitor's initial billing rate ($1100 per hour) and the billing rates of his team, the scope of his requests for information and interviews, and the Monitor's view that his investigation should commence immediately upon his appointment, while Apple believed he should wait 90 days so that Apple could institute the programs that the Monitor would evaluate. Apple unsuccessfully moved to stay the Monitorship and disqualify the Monitor, and sought to limit the scope of his investigation.

When it became apparent that there would be areas of contention with the Monitor, Apple bifurcated responsibilities at Apple between a group of people who did the substantive work of developing an improved compliance program under his supervision, and a different group of people who addressed procedural disagreements with the Monitor. The latter group included attorneys at Gibson, Dunn & Crutcher and Apple in-house attorneys who were responsible for reviewing the Monitor's bills, ensuring that Apple's confidential information was not disclosed in the Monitor's reports, and other areas that resulted in much of the friction with the Monitor that is reflected in his reports.

The substantive work with the Monitor was handled primarily by CCO Tom Moyer,

Director of Competition Law, Kyle Andeer, and Apple's newly hired Antitrust Compliance Officer, Deena Said. Apple also retained Matt Reilly of Simpson Thacher & Bartlett LLP ("STB"), who had been at the Federal Trade Commission for many years, to assist Apple in complying with the Monitorship. By bifurcating the relationship with the Monitor in this way, Apple was able to cooperate with the Monitor on substance and develop a quality antitrust compliance program, unimpeded by contentious issues.

C. The Monitor's Reports

The Final Judgment required the Monitor, within 180 days of his appointment, to "provide a written report to Apple, the United States, the Representative Plaintiff States, and the Court setting forth his … assessment of Apple's internal antitrust compliance policies, procedures, and training and, if appropriate, making recommendations reasonably designed to improve Apple's policies, procedures, and training for ensuring antitrust compliance." Final Judgment at 12. The Monitor issued four reports—one every six months—which are summarized below.

1. First Monitor Report

The Monitor's First Report covered the period from the appointment of the Monitor in October 2013 to March 2014, and was issued on April 14, 2014. The Monitor stated that the "monitoring team has experienced extended and unexpected delays in its efforts to evaluate Apple's antitrust compliance policies, procedures, and training ('Apple's Compliance Program')." First Report at ii.

The Monitor also expressed frustration that his access to the Board had, in his view, been inappropriately limited. The Monitor described several of his requests to meet with directors, including a letter he sent to the Board wherein he expressed disappointment with Apple's lack of cooperation and failure to produce Apple employees for interviews. *Id.* at 13, 19, 20-21. Apple's counsel responded that such interviews should occur after the 90-day window that the Final Judgment provided for updating Apple's policies. During the first period, the Monitor

interviewed one member of the Board, Dr. Ronald Sugar, the chair of the AFC, and Apple proposed that the Monitor interview several Apple employees including Mr. Moyer, Ms. Said, and Mr. Andeer.

The Monitor acknowledged that after the Second Circuit decision denying Apple's motion to stay the Monitorship in early February, "the relationship between Apple and the monitoring team has significantly improved … and has become more focused on achieving the goal of enhancing Apple's Antitrust Compliance Program pursuant to the Final Judgment." *Id.*, at ii. The Monitor described Apple's revisions to date to its Antitrust and Competition Law Policy and Business Conduct Policy, its Business Conduct Policy E-Book, and its online and live antitrust compliance training courses and presentations. *Id.* at 37-41. The Monitor noted that, "[a]lthough Apple is appealing the [district] Court's findings, it has been working to enhance its Antitrust Compliance Program." *Id.* at 42. The Monitor concluded that, "Apple has made a promising start in enhancing its Antitrust Compliance Program … but … still has much work to do." *Id.* at 43.

2. Second Monitor Report

The Monitor's Second Report (for the period March 2014 through August 2014), issued on October 14, 2014, noted that the positive "shift in tone" continued, but the Monitor criticized Apple for not developing adequate procedures in a number of areas. The Monitor identified two "main weaknesses in Apple's Program." First, "the Program lacks clear procedures for its full implementation." Second, the Monitor had "not yet seen evidence that Apple's Program is adequately overseen by the Board or the Board's Audit and Finance Committee." Second Report at 73-74. The Monitor said that he needed further information to "determine whether the company's Board or the Board's Audit and Finance Committee adequately oversees Apple's Antitrust Compliance Program." *Id.* at ix & 55-56. The Monitor planned "to devote significant attention to learning about Apple's Board and Audit and Finance Committee during the next reporting period." *Id.* at 56.

3. Third Monitor Report

In his Third Report (for the period September 2014 through February 2015), issued on April 14, 2015, the Monitor noted Apple's progress in developing the compliance program but criticized its lack of cooperation. Third Report at 90-91. The Monitor commented favorably on the antitrust training that David Boies had provided to the Board in August of 2014. By the end of January 2015, the Monitor had interviewed all members of Apple's Board of Directors. The Monitor observed that "Board oversight has undeniably increased since the Second Report. We are aware of increased communications between company personal and the Board [regarding antitrust compliance]." *Id.*at ix. However, the Monitor recommended that "Apple's Board must do more to rigorously oversee the Program" and stated that he "lack[ed] critical information on which to base our assessment of the Board's engagement regarding, and active oversight of, the Program…." *Id.* at ix and 89.

4. Fourth Monitor Report

The Fourth Report (for the period March 1, 2015 to September 4, 2015), issued on October 5, 2015, described each of the Monitor's recommendations and Apple's response, showing that Apple accepted and instituted the vast majority of those recommendations. In some instances, Apple objected and provided the reasons for those objections; for example, Apple objected to the Monitor's recommendation that it disclose its risk assessment report to the court on the ground of attorney-client privilege, and the Monitor agreed to hold that recommendation in abeyance. The Monitor indicated that "[o]ur overall assessment is that Apple's antitrust compliance program is much stronger and more complete than it was when the Court issued the Final Judgment, although there remain some gaps in our information." Fourth Report at 2.

The Monitor specifically described his recommendations concerning the role of the Board. Although the Monitor noted that he and Apple had disagreed about the Board's role in day-to-day oversight of the antitrust compliance program, he concluded that:

> Based on all of the information we gathered during this reporting period—including detailed interviews of Board members and ET members, and monitoring of Board antitrust training—we have

> seen significant improvement in the Board's oversight of the Antitrust Compliance Program. Its interest in these issues needs to be sustained, especially as Apple enters new markets and develops new products and services.

Id. at 100. The Monitor specifically noted that "both the AFC and full Board have actively questioned Apple management about potential antitrust issues related to new initiatives," and at training sessions "Board members asked numerous questions that suggested they were engaged and interested in Apple's antitrust compliance." *Id.* at 99-100. The Monitor recommended that "going forward, the Board [should] exercise rigorous oversight regarding antitrust-related issues." *Id.*

The Monitor concluded with an expression of frustration at the tone of the relationship with Apple, but recognized that Apple's programs had substantially improved. The Monitor noted that Apple's "lack of cooperation has cast an unnecessary shadow over meaningful progress in developing a comprehensive and effective antitrust compliance program." *Id.* at 108. The Monitor concluded that "Apple made substantial progress in developing and improving its Antitrust Compliance program and in implementing the numerous recommendations we made in our previous reports," and noted a "significant improvement in the engagement and involvement of Apple's [executive team] in antitrust issues." *Id.* at 107-08.

D. Board Oversight of Apple's Response to the Final Judgment

The Board exercised oversight over Apple's development of an updated Antitrust Compliance Program during the Monitorship. All of the Monitor's recommendations were presented to the AFC, and the AFC asked questions regarding Apple's response, the status of implementation, and the reasons why management had objected to any recommendation. The AFC was actively involved in determining Apple's final position on all recommendations, and reported them to the Board.

Throughout the Monitorship, Mr. Moyer reported directly to the AFC at its quarterly meetings. Mr. Moyer reported to the SLC that the members of the AFC consistently pushed the compliance department to have a "best-in-class" antitrust compliance program. At no time did any Board member state or indicate that Apple should not comply with any aspect of the Final

Judgment; to the contrary, Board members insisted that Apple cooperate with the Monitor and comply with the Final Judgment. Mr. Moyer particularly noted that Dr. Sugar spoke to him, early in the Monitorship, about Dr. Sugar's experience with the Department of Defense, and said that the Monitor would provide a "gold standard" for compliance, that Mr. Moyer's job was to implement that standard at Apple, and that Apple needed to comply with the Monitor. To Mr. Moyer's knowledge, no director resisted the Monitor's requests for information or interviews. The Monitor confirmed to the SLC that the Board did not interfere with his work.

Ms. Said also reported directly to the AFC quarterly regarding Apple's antitrust compliance program, the Monitorship, and Apple's compliance with the Final Judgment. Dr. Sugar spoke with Ms. Said each month outside of AFC meetings and reviewed the Monitor's reports with Ms. Said in order to more closely monitor Apple's efforts to comply with the Final Judgment. All Board members also reviewed the Monitor's second, third and fourth reports (the substance of the first report was summarized at length in the second report). The Director Defendants expressed to the SLC that the information they received gave them confidence in Ms. Said and the other compliance personnel at Apple, and confidence that Apple was building an exceptional program and fully complying with the Final Judgment.

The Board also actively participated in antitrust trainings in 2014 and 2015. In the 2014 training, renowned antitrust attorney David Boies, of Boies, Schiller & Flexner LLP led an in depth antitrust compliance training for Apple's Board members. Directors Cook, Drexler, Gore, Iger, Jung, Levinson, Sugar, and Wagner were all present for that training. Dr. Sugar and Dr. Levinson also both took the employee antitrust training program, at their own initiative, to provide feedback regarding its content and delivery.

In summary, the SLC found that during the Monitorship the Board exercised oversight over the development of the updated antitrust compliance program on at least three levels: (1) Dr. Sugar, the chair of the AFC, had monthly contact with Ms. Said between AFC meetings, personally reviewed and asked questions about Apple's responses to each of the recommendations by the Monitor, and took both the Board training and at his own initiative the

employee training; (2) the AFC received quarterly updates from Ms. Said and Mr. Moyer regarding the substantive work being done to improve Apple's compliance functions and was involved in developing Apple's proposed responses to the Monitor's recommendations; and (3) the full Board received quarterly reports from the AFC that included detailed information about Apple's compliance program and the Monitorship. During this time, Mr. Keller also continued to provide presentations to the AFC regarding risk oversight, which in turn were reported to the Board.

E. Apple's Development of an Updated Antitrust Compliance Program

The SLC has confirmed that during the course of the two-year Monitorship Apple engaged in an extensive company-wide effort to overhaul its antitrust compliance programs. Apple developed new live and online training materials; created a new suite of antitrust compliance procedures covering all aspects of the antitrust compliance program; worked to integrate its antitrust compliance programs with existing Business Conduct and Compliance resources; established more formal processes around risk assessments and audits; added resources to Apple's intranet page and the antitrust compliance webpage; and took additional steps to ensure compliance with the Final Judgment, compliance with the antitrust laws, and the effective monitoring and reporting of any antitrust allegations, questions, and concerns.

The Monitor made 100 recommendations, and Apple accepted 94 of them. CCO Tom Moyer summarized to the SLC the Monitor's recommendations, and Apple's responses, as follows:

- The Monitor made 12 recommendations regarding antitrust compliance policies, of which Apple adopted 11. Apple did not adopt the recommendation that the antitrust policy be presented differently for different business groups at the company, because they wanted to have a uniform policy that would be presented to everyone. The Monitor ultimately determined that Apple's antitrust policy was effective and useful.

- The Monitor made 20 recommendations regarding antitrust compliance training, and Apple adopted all 20. The Monitor referred to Apple's program as an appropriate mechanism for training, and noted that employees remembered the training program long after participating in it.

- The Monitor made 25 recommendations regarding antitrust compliance procedures, and Apple adopted 23 of them. The two that they did not adopt related to how

employees would report antitrust issues. Apple wanted to encourage employees to report such issues to any person that they felt appropriate, rather than being limited to reporting through a single channel.

- The Monitor's remaining 43 recommendations, in Mr. Moyer's view, were outside the areas of policies, training, and procedures that were defined in the Final Judgment. Nevertheless, Apple adopted all but three of these recommendations. Those three (and Apple's view, as indicated by Mr. Moyer) were (1) that Apple provide a written antitrust risk assessment to the Monitor (which would risk a waiver of attorney-client privilege and create risk for the company in future litigation), (2) that the Antitrust Compliance Officer have access to information regarding all business areas and products under development (Apple wanted to limit the scope of this, especially to exclude products in the early development phase), and (3) that Apple set a threshold of risk magnitude that would require a report to the Board (the Board wanted to be informed of all antitrust issues).

Near the end of the Monitoring period, in the fall of 2015, Ms. Said determined that an independent third-party review of Apple's Antitrust Compliance Program would be beneficial to Apple's efforts to develop an enhanced program. Apple engaged PricewaterhouseCoopers LLP ("PwC") to perform the review. PwC used its proprietary Compliance Program Effectiveness Framework to assess Apple's Antitrust compliance program, and summarized its findings in a report issued to Apple and the District Court. PwC concluded, among other things, that all individuals interviewed expressed that Apple's Senior Management, AFC, and Board emphasized the importance of compliance with antitrust laws, and that antitrust compliance was an organizational priority in which the AFC, the Board, General Counsel and Chief Compliance Officer were actively engaged. PwC confirmed to the SLC that Apple's Antitrust Compliance Program is of the highest quality.

F. Apple's Reports to The District Court

The Final Judgment required Apple's ACO to submit annually a "written statement as to the fact and manner of Apple's compliance with Sections III., IV., and V." of the Final Judgment. Apple filed Statements of Compliance with the Final Judgment with the District Court on October 6, 2014 and October 6, 2015.

In Apple's 2014 Statement of Compliance, Apple detailed its efforts "to (1) comply with the Final Judgment, (2) enhance its Antitrust Compliance Program and accompanying materials,

and (3) facilitate the monitorship and cooperate with the [Monitor]." The report to the District Court included the following:

- "Ms. Said has been intimately involved in, and has provided strategic direction on, the steps Apple has taken to ensure compliance with the Final Judgment."

- "Apple has distributed the Final Judgment to the Board, Mr. Cook, and its Senior Vice Presidents and to all employees engaged in whole or in part in activities relating to the iBooks Store, and each of those individuals certified his or her understanding of the judgment."

- "Apple provided live training to all relevant iBooks Store, App Store and iTunes employees, led by members of Apple's in-house antitrust and competition group – primarily by the group's Senior Director, Kyle Andeer. Experienced antitrust practitioners, such as Mr. Andeer and members of his team, as well as renowned antitrust attorney David Boies, have conducted several live trainings for hundreds of Apple employees, including all Board and Executive Team members."

- "Apple distributed both the Final Judgment and a summary thereof to the Board and obtained certifications from its Directors on November 19, 2013. Apple likewise distributed these materials to the Executive Team, as well as all other covered employees, and obtained all necessary certifications by December 5, 2013."

- "Apple began to develop improvements to its antitrust compliance program even before the entry of the Final Judgment. These improvements were designed to be both comprehensive and innovative. Apple committed hundreds of person-hours to create a new antitrust online course, new live training materials, and other written and electronic resources…"

- "Apple retained Simpson Thacher & Bartlett ("STB") specifically to assist in identifying potential risks and to assist in improving its Antitrust Compliance Program."

- "On September 23, 2013, Mr. Andeer presented a live training to Apple's U.S. iBooks Store group, covering everything from the specific requirements of the Final Judgment to Apple's new training program, and the role of the ECM, and Apple's compliance efforts moving forward. On December 5, 2014, Mr. Andeer provided a second live training to worldwide iBooks Store employees, and, in January and February 2014, he conducted broad trainings to a diverse group of employees that went far beyond the specific terms of the Final Judgment."

- "In addition to the training, Apple rolled out a major update to its Antitrust Compliance Program on June 30, 2014. This rollout included a revised Business Conduct eBook containing a new chapter specifically on antitrust and competition; a revised antitrust and competition policy; assignment of online training to more than 5,000 employees; deployment of a new internal website focusing on antitrust and competition issues; and communications from key executives to Apple employees supporting the program."

- "Mr. Andeer has received information regarding Apple's unannounced products, thereby providing an opportunity to identify early on any risks presented by new products or offerings, and became chief sales counsel at Apple roughly a year ago.

With one of Apple's most senior antitrust experts embedded in the sales group, that critical business unit now receives daily guidance on any antitrust issues or concerns that may arise, and Mr. Andeer is well informed of the most nuanced antitrust business risks."

- "In addition to the work done by Apple, STB has spent months analyzing Apple's antitrust risks in order to help ensure it has a relevant and focused compliance program. Specifically, antitrust experts at STB studied Apple's products, business, and typical interactions with competitors, resellers, customers, and suppliers in order to provide an outside assessment of potential risks."

- "Apple's new antitrust policy begins with a statement from Bruce Sewell, Apple's General Counsel, detailing Apple's commitment to compliance with the antitrust laws and to preventing and reporting any potential violations. It also highlights Apple's in-house competition law team, ACO, and Apple's helpline. The policy provides several pages of detailed substantive content covering topics such as interactions with competitors; prohibitions on price-fixing, market allocation, group boycotts, and bid-rigging; and interactions with resellers and suppliers, concluding with a further reminder to contact the legal department with any questions or concerns regarding antitrust compliance and a reminder of Apple's strict anti-reprisal policy."

- Apple has made more than 40 "high-level employees and Board members available for interviews by the [Monitor]."

In Apple's 2015 Statement of Compliance, Ms. Said provided an overview and update of Apple's efforts since the Final Judgment, including the following:

- "I am confident that I have the resources, and support from Apple's Board of Directors ("Board") and senior leadership, to further develop an already effective and comprehensive Program."

- "I report directly to the Audit and Finance Committee ("AFC") in my capacity as ACO—my employment, performance, compensation, and budget are all approved by the head of the AFC, Dr. Ronald Sugar, with whom I have regular and substantial communications. I provide a quarterly report to the Board, and I make a formal presentation regarding updates to the Program, the status of our compliance efforts, and our ongoing work with the [Monitor] at every other meeting of the AFC."

- "In November 2014, I met individually with each member of the Board and presented a lengthy update regarding the status of the Program and Apple's compliance with the Final Judgment. I am preparing a similar update to be shared with the individual members of the Board in November 2015. I have found Apple's Board members to be involved, engaged, and committed to the Program and compliance overall."

- "I have direct and unfettered access to every member of the Board and [Apple's Executive Team], including the ability to raise any concerns I may have regarding the progress of the Program, any antitrust issues or risks of which I become aware, and compliance with the Final Judgment."

- "In 2015, Apple conducted 13 separate live training sessions, including sessions for

Apple's Board, [Executive Team], and all relevant iBooks Store, App Store, and iTunes employees. The trainings were led by members of Apple's Competition Law Team, such as Mr. Kyle Andeer, Mr. Sean Dillon, and Mr. Brendan McNamara."

- "I created an audit procedure in July 2015 and updated it in August 2015. I drafted the new procedure based on extensive personal research regarding compliance audits, customized to Apple's Program and the audit requirements of the Final Judgment."

- "I independently retained PwC to conduct a third-party audit of Apple's Program. PwC completed its initial audit in 2015, reporting its findings to me in September."

- "I have prominently disseminated to Apple employees information regarding a number of mechanisms for reporting suspected Final Judgment or antitrust violations. These include, inter alia, the Helpline; a separate third-party whistleblower line; an email address to which employees can submit complaints; contact information for the Competition Law Team; my own contact information; and messages contained in the Business Conduct Policy and other."

- "I meet on a quarterly basis with Apple executives and with senior in-house Apple attorneys in the Internet Software and Services, Sales, Marketing, Product, Hardware, and Software groups to inquire about any actual or potential violations of the Final Judgment or allegations that Apple has violated the antitrust laws, as well as any questions, issues, or concerns that those employees may have. I also confirm with the Helpline employees that they have not received a report of any actual or potential violations of the Final Judgment or allegations that Apple has violated the antitrust laws. I conduct these quarterly interviews to ensure that any actual or potential violations of the Final Judgment or allegations of antitrust issues have been reported appropriately and that no allegations or complaints have slipped through the cracks."

- "In 2015, I extensively revised Apple's investigation procedure, which sets forth the manner in which Apple receives, investigates, and, where appropriate, imposes discipline for alleged violations of the antitrust laws or of the Final Judgment. The procedure also covers the ways in which Apple employees may report any actual or potential antitrust violations or concerns, the procedures used by me and other legal and compliance personnel to seek out and obtain information about potential violations, and Apple's strict non-reprisal policy. In 2015, I added content to the investigation procedure to address issues such as the logging and systematic recordkeeping of alleged violations, additional steps to mitigate potential conflicts of interest, and the involvement of independent third parties where appropriate."

IX. DISCHARGE OF THE MONITOR BY THE DISTRICT COURT

Before the Monitorship ended, Mr. Moyer and others from Apple (including in-house and outside counsel) met with Justice Department attorneys in Washington, D.C. The Monitor was not present for that meeting. Apple made a presentation about its antitrust compliance program, including how it had been developed, the number of recommendations from the Monitor that

Apple had adopted, the reasons for not adopting other recommendations, and the fact that PwC had been retained to review the program.

Although the DOJ had originally sought a ten-year monitorship, the DOJ recommended to the District Court that the Monitorship not be extended beyond the initial two-year period. In a joint letter submitted to Judge Cote on October 12, 2015, the DOJ stated:

> Although the Monitor faced a challenging relationship with Apple, that did not prevent him from fulfilling the fundamental purpose of the Monitorship: ensuring that Apple implemented a significantly strengthened antitrust compliance program. … In spite of the challenges he encountered, the Monitor was not deterred from evaluating Apple's antitrust compliance program, recommending improvements, and seeing his recommendations implemented. The Monitor observes that Apple has now implemented meaningful antitrust policies, procedures, and training programs that were obviously lacking at the time Apple participated in and facilitated the horizontal price-fixing conspiracy found by this Court. Apple's failure to adopt a more constructive working relationship with the Monitor regrettably required the Monitor to expend considerably more time and resources than otherwise would have been necessary to carry out his duties, but ultimately did not prevent the Monitor from satisfying his responsibilities or Apple from greatly improving its antitrust policies, procedures, and training.

The DOJ further stated, "In arriving at our conclusion not to recommend an extension of the Monitor's term, we ultimately give greater weight to the Monitor's assessment that Apple has put in place a meaningful antitrust compliance program than to the difficult path it took to achieve this result." The District Court concurred and terminated the Monitorship on October 13, 2015, finding that "Apple has entirely revamped its antitrust compliance program."

X. APPLE'S CURRENT ANTITRUST COMPLIANCE PROGRAM

Since the termination of the Monitorship in 2015, Apple has continued to update and improve its antitrust compliance policies and practices. As a result, Apple's antitrust compliance program includes the following elements:

- Apple employs a full time Antitrust Compliance Officer dedicated to ensuring Apple's compliance with the antitrust laws, Ms. Said, who is charged with overseeing and executing Apple's Antitrust Compliance Program.
- Apple has a detailed Antitrust and Competition Law Policy. This policy is maintained and updated by the ACO, in consultation with the head of the Competition Law Team, and the Chief Compliance Officer ("CCO").

- Apple has a Business Conduct Policy with a dedicated Antitrust and Competition section. This policy is maintained and updated by the Business Conduct and Global Compliance Team. The ACO, in consultation with the head of the Competition Law Team, works with the Business Conduct and Global Compliance Team to update the Antitrust and Competition Law section of the Policy.

- Apple regularly takes steps to ensure that the Antitrust and Competition Law Policy is disseminated, understood, and used.

- Apple has an Antitrust Compliance Program review procedure that provides the timing, substantive, and logistical guidelines for revising Apple's antitrust policies and procedures. This procedure is maintained and updated by the ACO.

- Apple has a live and online training procedure to address the manner in which the ACO determines the audience, number of sessions, substantive materials, and logistical considerations in planning each of the annual live and online training sessions. This procedure is maintained and updated by the ACO.

- The Competition Law Team provides live training to employees not subject to the terms of the Final Judgment, but who they have determined would benefit from live training.

- To the extent possible, the ACO attends every live antitrust training provided by the Competition Law Team.

- Since the Final Judgment in July of 2013, Apple has provided antitrust training to more than 10,000 employees.

- Apple has a feedback procedure addressing the steps the ACO takes to solicit employee feedback for Apple's live and online antitrust trainings. This procedure is maintained and updated by the ACO. The ACO uses feedback obtained from employees to inform updates to the Antitrust Compliance Program.

- Apple maintains records of feedback regarding the antitrust live and online training. Apple also electronically tracks training attendance.

- Apple has a procedure setting forth the methods that Apple uses to detect, investigate, and, if necessary, impose discipline for violations of the antitrust laws. This procedure is maintained and updated by the ACO, in consultation with the CCO and the head of the Competition Law Team.

- The ACO disseminates to Apple employees information regarding a number of mechanisms for reporting suspected antitrust violations. This includes content in the live and online trainings reiterating this obligation.

- Apple has an escalation procedure for addressing how information about antitrust issues should be escalated to the appropriate people within Apple. This procedure is maintained and updated by the ACO.

- Apple disseminates its own non-reprisal policy throughout the company and sets clear expectations that its employees not engage in retaliatory behavior against third parties. The following materials contain anti-reprisal language to help encourage questions and reporting of issues: Antitrust and Competition Law Policy, online training, live training, Business Conduct eBook chapter, Summary of the Final

Judgment, logging certifications, and intranet site.

- The ACO communicates annually to Apple's employees that they may disclose to the ACO, without reprisal, information concerning any potential violation of the antitrust laws.
- Apple has an audit procedure customized to Apple's Antitrust Compliance Program. This procedure is maintained and updated by the ACO.
- The ACO conducts a quarterly audit of new eBooks contracts.
- In addition to its real-time risk analysis, Apple conducts a more formal comprehensive antitrust risk assessment. This risk assessment is used, among other purposes, to inform and modify the Antitrust Compliance Program.
- All categories of employees identified in the Final Judgment are required to certify that they have read and understand the Antitrust and Competition Law Policy.
- Apple maintains a Business Conduct Helpline and an antitrust/competition law mailbox that are available to Apple employees for questions related to antitrust.
- The ACO audits the Business Conduct Helpline specific to antitrust issues to ensure that matters are promptly brought to her attention.
- The ACO tracks questions and responses from the competitionlaw@apple.com mailbox.
- Apple maintains a dedicated intranet page with information about its Antitrust Compliance Program, including links to antitrust compliance training materials and contact information for the ACO and Competition Law Team.
- Antitrust Compliance Program Updates are provided to the Board of Directors on a quarterly basis.
- The Chair of the AFC reviews the performance evaluation and compensation of the ACO in concert with Apple's management.
- The ACO provides a quarterly update to the AFC concerning the Antitrust Compliance Program.
- The Chair of the AFC and the ACO participate in a monthly phone call to discuss issues related to the Antitrust Compliance Program.
- On a quarterly basis, the ACO meets with key executives and senior lawyers to ensure that any questions or allegations concerning antitrust issues have been addressed.
- The head of the Competition Law Team meets with business and legal stakeholders on a regular basis to keep apprised of antitrust related matters.

Apple continues regularly to review and update this program to ensure full compliance with antitrust and competition laws.

XI. LEGAL STANDARDS APPLICABLE TO THE CLAIM AGAINST THE DIRECTOR DEFENDANTS

Plaintiffs' single claim for breach of fiduciary duty requires the existence of a fiduciary duty, its breach, and damages. *City of Atascadero v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 68 Cal. App. 4th 445, 483 (1998). Below is a non-exhaustive summary of legal standards that are applicable to the Derivative Plaintiffs' claims against the Director Defendants. In Section XII below, these standards are applied to Plaintiffs' specific allegations and the facts determined by the SLC.

A. Duty Of Care

Under California law, corporate directors owe a legal duty to the corporation and its shareholders to serve "in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances." Cal. Corp. Code § 309(a).

"The duty of due care requires that a director gathers and considers material information with 'reasonable diligence.'" 1-3 Liability of Corporate Officers and Directors § 3.01 (2015). "Directors are not merely bound to be honest; they must also be diligent and careful in performing the duties they have undertaken." *Burt v. Irvine Co.,* 237 Cal. App. 2d 828, 852 (1965) (citation omitted). Thus, the duty of care refers to a duty to "make reasonably informed decisions." 1-3 Liability of Corporate Officers and Directors § 3.01 (2015).

To act on an informed basis, "California allows non-officer directors to rely upon company employees and advisors without a duty of further inquiry absent special circumstances." *FDIC v. Castetter,* 184 F.3d 1040, 1045 (1999) (*citing Gaillard v. Natomas Co.*, 208 Cal. App. 3d 1250, 1264-5 (1989)). "[T]he function of the board of directors is to determine the general business policy of the corporation and … the directors are entitled to rely upon the officers and employees of the corporation, both in carrying out that policy and in receiving reports and information upon which to base that policy." *Briano v. Rubio*, 46 Cal. App. 4th

1167, 1179 (1996) (*citing* 2 Marsh, Cal. Corporation Law (3d ed. 1996) § 11.4, p. 804). Directors are also entitled to rely upon the recommendation of board committees and are "not required to initiate their own independent investigation." *Gaillard,* 208 Cal. App. 3d at 1271. However, "the duty of 'reasonable inquiry' … constitutes a condition to the right of reliance, such that directors may not close their eyes to what is going on about them in corporate business, and must in appropriate circumstances make such reasonable inquiry as an ordinarily prudent person under similar circumstances." *Id.* at 1264-65.

Normally, one who breaches a duty of care through ordinary negligence is liable for the damages that are proximately caused thereby, but corporate directors are not subject to an ordinary negligence standard. Instead, they are protected by the business judgment rule. *In re AWTR Liquidation Inc.,* 548 B.R. 300, 314 (C.D. Cal. 2016). "The business judgment rule sets up a *presumption* that directors' decisions are made in good faith and are based upon sound and informed business judgment." *Lee v. Interinsurance Exchange,* 50 Cal. App. 4th 694, 715 (1996) (emphasis in original); *see also Katz v. Chevron Corp*., 22 Cal. App. 4th 1352, 1366 (1994). Pursuant to the business judgment rule, in making business decisions, "a director is not liable for a mistake in business judgment which is made in good faith and in what he or she believes to be the best interests of the corporation, where no conflict of interest exists." *Gaillard*, 208 Cal. App. 3d at 1263. While the business judgment rule protects directors from liability for ordinary negligence, it does not apply in instances of "fraud, bad faith, overreaching or an unreasonable failure to investigate material facts." *Lee*, 50 Cal. App. 4th at 715.

The business judgment rule is codified in California Corporations Code section 309(a), which "immunizes corporate directors from personal liability if they act in accordance with certain conditions." *Scheenstra v. California Dairies, Inc*., 213 Cal. App. 4th 370, 386 (2013). "[I]t is the very essence of the business judgment rule that, where a reasonable business purpose is asserted, the motives of directors will not be scrutinized, absent a basis for overcoming the presumption of good faith embodied by the business judgment rule." *Id.* at 717. *See also Furman v. Walton*, 2007 U.S. Dist. LEXIS 39618, at *7 (N.D. Cal. May 16, 2007) ("Under the

business judgment rule, a court will not substitute its judgment for that of the board, and the board's decision will be upheld unless it cannot be attributed to any rational business purpose.") (*aff'd Furman v. Walton,* 2009 U.S. App. LEXIS 6136 (9th Cir. Cal. Mar. 26, 2009)).

B. Duty Of Oversight

A director's fiduciary duties include the duty to monitor and oversee the corporation's affairs. A board of directors has a duty to "exercise a good faith judgment that the corporation's information and reporting system is in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations, so that it may satisfy its responsibility." *In re Caremark Int'l,* 698 A.2d 959, 970 (Del. Ch. 1996).

A claim that directors have violated their duty to monitor the corporation's affairs "is possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment." *Id.* at 967. "[O]nly a sustained or systematic failure of the board to exercise oversight—such as an utter failure to attempt to assure a reasonable information and reporting system [exists]—will establish the lack of good faith that is a necessary condition to liability." *Id.* at 971. Directors cannot be held liable on an oversight claim unless "(a) the directors utterly failed to implement any reporting or information system or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention." *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (emphasis in original). *See also, In re Verifone Holdings, Inc.,* 2009 U.S. Dist. LEXIS 44138, at *17 (N.D. Cal. May 26, 2009) ("there must be a showing that the directors breached their fiduciary duty by failing to attend to their duties in good faith, or put otherwise, that the directors were conscious of the fact that they were not doing their jobs").

Therefore, director liability for failure of oversight requires intentional conduct, *i.e.,* evidence that directors "acted with a state of mind consistent with a conscious decision to breach their duty of care." *Desimone v. Barrows,* 924 A.2d 908, 935 (Del. Ch. 2007). "[D]irector liability for failure to monitor require[s] a finding that the directors acted with the state of mind

… of a disloyal director - bad faith - because their indolence was so persistent that it could not be ascribed to anything other than a knowing decision not to even try to make sure the corporation's officers had developed and were implementing a prudent approach to ensuring law compliance." *Id.* "[A] showing of bad faith is a *necessary condition* to director oversight liability." *In re Citigroup Inc. S'holder Derivative Litig*. 964 A.2d 106, 123 (Del. Ch. 2009) (emphasis original). "[M]ere negligent failure to monitor problems and control risks is insufficient to ascribe bad faith to the directors." *Leyte-Vidal v. Semel*, 220 Cal. App. 4th 1001, 1014 (2013). "[E]ven gross negligence is insufficient to constitute bad faith in what amounts to an oversight challenge." *Id.*

The Superior Court, in ruling on the Director Defendants' demurrer, described the standard for a lack of oversight claims as follows: "[A]llegations of lack of oversight require a showing of lack of good faith. ... Lack of good faith requires a showing of bad faith, that is, a conscious or deliberate failure to fulfill the duty of oversight with actual or constructive knowledge of their failure to act as the law requires." Order Re Demurrer, at 14 (*citing In re SAIC Inc.*, 948 F. Supp. 2d 366, 382 (S.D.N.Y. 2013)).

C. Duty Of Loyalty

A director's duty of loyalty requires the director always to put the interests of the corporation above his or her own personal interest. The majority of case law involving the duty of loyalty concerns allegations of self-dealing. The duty of loyalty also includes a duty to act in good faith. *See e.g., Brown v. Brewer,* 2010 U.S. Dist. LEXIS 60863, at *13-14 (C.D. Cal. June 17, 2010) ("the requirement to act in good faith is a subsidiary element, *i.e.,* a condition, of the fundamental duty of loyalty.") (internal quotation marks omitted) (*citing Stone*, 911 A.2d at 369-70). Some courts therefore characterize a director's breach of the duty of oversight as a breach of the duty of loyalty. *See e.g., Stone*, 911 A.2d at 369-70 ("Where directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith."). *See also*, *Brown*, 2010 U.S. Dist. LEXIS 60863, at **16-17 ("The obligation to act in good faith, which is a necessary component of satisfying the duty of loyalty, requires

directors to act for the purpose of advancing corporate well-being. Therefore, any 'intentional dereliction of duty, a conscious disregard for one's responsibilities[,]' constitutes bad faith, or the failure to act in good faith.") (citation omitted).

XII. ANALYSIS OF THE CLAIM AGAINST THE DIRECTOR DEFENDANTS

A. Allegations Relating to the Ebook Negotiations

Plaintiffs allege that the Director Defendants breached their fiduciary duties by failing to implement proper procedures to detect violations of antitrust laws and, as a result, Apple was found liable for antitrust violations related to the ebook negotiations that occurred between December 2009 and April 2010. SCAC, ¶¶ 222-236; Order Re Demurrer at 8. Five of the Director Defendants—Levinson, Gore, Drexler, Jung, and Campbell—were serving on Apple's Board between December 2009 and April 2010. No director is alleged to have been involved in or known about the ebook negotiations as they were occurring, which is consistent with the SLC's investigation. Plaintiffs allege that those five directors are liable for failing to institute adequate internal reporting and controls to ensure compliance with the antitrust laws, exercise reasonable oversight of Apple's compliance in light of "red flags," and to be involved in the ebook negotiations themselves to ensure compliance with antitrust laws. SCAC, ¶¶ 138-226. The SLC has determined that these allegations are contrary to the facts and unsupported by law.

1. Allegations That The Board Failed To Institute A System To Ensure Compliance With Antitrust Laws And Exercise Oversight Prior To The Ebook Negotiations

As described above, directors cannot be held liable on an oversight claim unless "(a) the directors utterly failed to implement any reporting or information system or controls; <u>or</u> (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention." *Stone*, 911 A.2d at 370 (Del. 2006) (emphasis in original). As Plaintiffs' recognize, at the time of the ebook negotiations, Apple had an antitrust compliance program in place, and that program was presented to and discussed with the Board. *See* SCAC, ¶ 222; *see* Section

VII.A., *supra*. However, Plaintiffs allege that "Apple's internal reporting systems and procedures were inadequate to enable the Board to detect or prevent the underlying misconduct, to monitor its senior managers, and most particularly Jobs and his executive team, thereby causing the Company to be liable for violating antitrust laws." SCAC, ¶ 222. In other words, although Apple had an antitrust compliance program and a reporting system in place, Plaintiffs assert that the program and system were so deficient that they are a basis for oversight liability.

Plaintiffs cannot succeed on an oversight claim by arguing, in hindsight, that the system in place was inadequate to detect the ultimate violation that occurred; rather, Plaintiffs would have to prove that the directors acted in bad faith. *Stone*, 911 A.2d at 370; *see also In re Citigroup Inc. S'holder Derivative Litig*., 964 A.2d at 123 ("[A] showing of bad faith is a *necessary condition* to director oversight liability.") (emphasis original). *See also,* Order Re Demurrer at 12 ("To state a claim under *Caremark* based on the failure to oversight [sic] when a policy is in place, 'a plaintiff must plead the existence of facts suggesting that the board knew that internal controls were inadequate, that the inadequacies could leave room for illegal or materially harmful behavior, and that the board chose to do nothing about the control deficiencies that it knew existed.") (*quoting Desimone*, 924 A.2d 908, 940 (Del. Ch. 2007); *see Caremark,* 698 A.2d at 971 ("Such a test of liability—lack of good faith as evidenced by sustained or systematic failure of a director to exercise reasonable oversight—is quite high."). There are no allegations, and the SLC has found no evidence, that meet the "quite high" standard for oversight liability.

The SLC determined that the directors oversaw the antitrust compliance program in good faith. Apple's Board properly delegated compliance oversight, including antitrust compliance, to the AFC. The AFC met ten times in 2009 and eight times in 2010 (twice as many times as called for by the AFC's charter), and received quarterly reports directly from Apple's compliance personnel. The full Board also received compliance updates quarterly in 2009 and 2010. Materials were provided to directors in advance of AFC and Board meetings. The directors were informed by Apple employees of areas of risk, of risk mitigating projects, of compliance

initiatives, and of management's plans to address and implement them.

Apple's directors were entitled to rely on Apple's employees, including its General Counsel, Mr. Pressler, and Mr. Moyer, all experienced and competent professionals, to develop, update, and implement the antitrust compliance program, and the directors exercised oversight by receiving regular reporting. *In re Citigroup Inc. S'holder Derivative Litig*., 964 A.2d 106, 131 (Del. Ch. 2009) ("Director oversight duties are designed to ensure reasonable reporting and information systems exist …"); *Briano*, 46 Cal. App. 4th at 1179 ("directors are entitled to rely upon the officers and employees of the corporation"); *see also* Cal. Corp. Code § 309(b)(3) (directors "shall be entitled to rely on" information in good faith that is presented by board committee). There is no evidence that any director acted in bad faith.

Moreover, there is no evidence that any Apple director consciously disregarded his or her responsibilities. Apple's directors were active and engaged during this time (and continuously thereafter). Mr. Levinson missed only one AFC meeting in each of 2009 and 2010, and attended all Board meetings those years. He reviewed the materials for the meeting he did not attend. Ms. Jung attended all but one AFC meeting during her tenure on the AFC in 2010 (she reviewed the materials for the meeting she missed), and attended all Board meetings in 2009 and 2010. Mr. Campbell attended all but one AFC meeting in 2009, all AFC meetings in 2010, and all Board meetings in 2009 and 2010. Mr. Gore and Mr. Drexler attended all Board meetings in 2009 and 2010 (neither director served on the AFC). The SLC determined that each of the directors interviewed by the SLC (Levinson, Gore, Drexler, and Jung), consistently reviewed Board materials in advance of meetings and were actively engaged on Board issues.

Mr. Moyer reported to the SLC that the AFC members asked him focused questions about his compliance program development. He described Apple's Board as "incredibly encouraging" and consistently pushing for a world-class compliance program. The directors were unrestrained in questioning Apple executives who presented information to them, and were satisfied with the responses they received.

Each director interviewed by the SLC expressed a high level of confidence in Apple's

senior executives, including compliance personnel. The directors indicated to the SLC that they had no reason to question the competence of those involved in compliance at Apple. Mr. Levinson received periodic reports about compliance prior to 2009. He described Apple's compliance employees as reliable, skillful, and competent. Mr. Drexler described the reporting to the Board from compliance employees as "honest and comprehensive." Ms. Jung described Apple's senior executives as "highly qualified" and responsive to Board questions and input. Mr. Gore found the leadership of Apple to be "exceptional" and the compliance staff's efforts to develop and implement compliance policies to be "outstanding." According to Mr. Gore, the Board consistently conveyed to Apple's compliance employees the importance of maintaining high standards.

The SLC has not found any evidence that any director, prior to the ebook negotiations, had notice of deficiencies in the antitrust compliance program or of potential antitrust violations. The basis for oversight liability on which Plaintiffs rely—a "conscious failure to monitor"—has been held to require a showing that there were "red flags" that put directors on notice of the ultimate liability, which the directors consciously disregarded. *Stone*, 911 A. 2d at 373. A claim for failure of oversight in the face of red flags "requires the plaintiff to demonstrate: (1) that the alleged red flags actually constitute red flags, i.e., that they could plausibly have served as warnings about the problems at issue; (2) that defendants were aware of the red flags; and (3) that defendants acted in bad faith in failing to take appropriate action in light of those red flags." Order Re Demurrer at 12 (*citing In re Capital One Derivative S'holder Litig.*, 952 F. Supp. 2d 770, 786 (E.D. Va. 2013). The Superior Court in ruling on the Director Defendants' demurrer found that the "red flags" alleged in the ACC (and again in the SCAC) do not raise the inference that the Board knew that its policies were inadequate or that antitrust violations were occurring at Apple prior to 2010 or at any time thereafter.[4] *See* Order Re Demurrer at 13 ("Allegations of

[4] The Superior Court's analysis of the alleged red flags was in the context of the second time period, between the iPad Launch and the Final Judgment. The Court's analysis of those alleged red flags being insufficient to put the directors on notice included events that predated the ebook negotiations. Conduct in early 2009 that is insufficient to constitute a red flag in 2010-2013 is also insufficient to constitute a red flag in late 2009-2010.

knowledge of an unrelated violation of the law are too attenuated to support a *Caremark* claim") (*citing In re SAIC Inc. Derivative Litig.,* 948 F. Supp. 2d at 387); *see also id. (citing In re Citigroup Inc. S'holder Derivative Litig*., 964 A.2d at 129 (finding alleged "red flags" about prior unrelated wrongdoing insufficient to put director on a heightened alert)). The SLC found that there is no evidence that any of the directors were aware of any facts that should have put them on notice that the ebook antitrust violation would occur. *See Stone*, 911 A.2d at 373 ("In the absence of red flags, good faith in the context of oversight must be measured by the directors' actions to assure a reasonable information and reporting system exists and not by second-guessing after the occurrence of employee conduct that results in an unintended adverse outcome.").

That Apple's antitrust compliance policy did not prevent the ebook antitrust violation from occurring does not subject the directors to liability. The directors' good faith belief that the compliance policy in place was appropriate, and reliance on competent and experienced professionals and board committees involved in establishing the compliance program, is protected by the business judgment rule. Cal. Corp. Code § 309(b). Directors are not guarantors of corporate policies or conduct. *See e.g., Caremark,* 698 A.2d at 971-972 (Where "the corporation's information systems appear to have represented a good faith attempt to be informed of relevant facts, [i]f the directors did not know the specifics of the activities that lead to the indictments, they cannot be faulted."); *Stone*, 911 A.2d at 373 ("the directors' good faith exercise of oversight responsibility may not invariably prevent employees from violating criminal laws, or from causing the corporation to incur significant financial liability, or both"); *Desimone,* 924 A.2d at 940 ("Delaware courts routinely reject the conclusory allegation that because illegal behavior occurred, internal controls must have been deficient, and the board must have known so."). "Good faith, not a good result, is what is required of the board." *Reiter v. Fairbank*, 2016 Del. Ch. LEXIS 158, at **42-43 (Del. Ch. Oct. 18, 2016) (finding allegations of oversight liability insufficient where "reasonable minds [could] argue" whether directors' oversight over compliance program was "sufficiently robust or flawed" but allegations failed to

support any reasonable inference that directors "consciously allowed" the company to violate the law "so as to sustain a finding they acted in bad faith.").

2. Allegations That The Board Should Have Been Involved In The Ebook Negotiations

Plaintiffs allege that Apple's directors should have been involved in, directly overseen, and intervened in the ebook negotiations (SCAC, ¶ 224), but that claim is unsupported by law. The ebook negotiations were commenced and substantially concluded between board meetings during a six-week period in December, 2009 and January, 2010. At the time of Apple's entry into the ebooks market, the market was very small, with the total market for all ebooks estimated at below $150 million per year (the entire market therefore representing less than 0.41% of Apple's total revenue in 2009). Directors are not charged with knowing the intricacies of every contract or business arrangement of a corporation, especially one as large as Apple. *Caremark*, 698 A.2d at 971 ("of course, the duty to act in good faith to be informed cannot be thought to require directors to possess detailed information about all aspects of the operation of the enterprise.").

The Board was entitled to rely on Apple's executives to do their jobs without direct Board involvement in the ebook negotiations. Without any reason to suspect otherwise, the directors are not subject to liability for relying on the Apple officers and employees who engaged in the negotiations to obey the law. *Id*. at 969 ("neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf."); *see also Graham v. Allis-Chalmers Mfg. Co.,* 41 Del. Ch. 78, 85 (1963) ("absent cause for suspicion there is no duty upon the directors to install and operate a corporate system of espionage to ferret out wrongdoing which they have no reason to suspect exists."); *Rosenblatt v. Getty Oil Co.,* 493 A.2d 929, 943 (Del. 1985) ("An informed decision to delegate a task is as much an exercise of business judgment as any other. The realities of modern corporate life are such that directors cannot be expected to manage the day-to-day activities of a company.") (*citing Aronson v. Lewis*, 473 A.2d 805, 813 (Del. 1984)).

There is no evidence that if Apple's Board had contemporaneously known about the ebook negotiations that the outcome would have been any different, *i.e.,* that the Board could or should have recognized that a violation of any antitrust laws was occurring, when Apple's legal counsel and business executives did not. The antitrust analysis by the District Court in 2013 that a vertical price fix was a per se violation was described as "sui generis" by the Court of Appeal; the Justice Department acknowledged that "no court has previously considered a restraint of this kind." *United States v. Apple Inc.,* 791 F.3d 290, 348 (2nd Cir. 2015) (dissent). In terms of the directors relying on employee conduct, the SLC determined that in negotiating the Publisher Agreements, Mr. Cue complied with Apple's antitrust policy, consulted and relied on Apple's legal counsel, and acted with the authority and approval of Apple's CEO, Steve Jobs. *See* Cue Report at 50-63. The SLC found no evidence that Mr. Cue believed that the Publisher Agreements were illegal or violated antitrust laws. Therefore, the Director Defendants are not subject to liability for an alleged failure to intervene in the ebook negotiations.

In summary, the SLC has found no basis to assert that directors Levinson, Gore, Drexler, Jung, or Campbell are liable for breach of fiduciary duties during the period of the ebook negotiations in January 2009 through April 2010.

B. Allegations Relating To The Period Between The iPad Launch And The Final Judgment

Plaintiffs allege that the Director Defendants breached their fiduciary duties by failing to institute a sufficient antitrust compliance program at Apple from the time of the iPad launch in January 2010, to the date of the Antitrust Judgment on September 5, 2013, resulting in imposition of the Monitor (Plaintiffs do not allege that any antitrust violations occurred during or after this time period). *See* SCAC, ¶¶ 304, 308; Order Re Demurrer at 8, 12-15. Other than Susan Wagner, who did not join Apple's Board until late July 2014, all of the Director Defendants were on the Board for at least some part of this period. Plaintiffs allege that the Director Defendants ignored red flags that should have alerted them that the antitrust compliance program was deficient. SCAC, ¶ 228.

As explained above, a claim for failure of oversight in the face of red flags "requires the plaintiff to demonstrate: (1) that the alleged red flags actually constitute red flags, i.e., that they could plausibly have served as warnings about the problems at issue; (2) that defendants were aware of the red flags; and (3) that defendants acted in bad faith in failing to take appropriate action in light of those red flags." Order Re Demurrer at 12 (*citing In re Capital One Derivative S'holder Litig.*, 952 F. Supp. 2d at 786). In ruling on the demurrer to the ACC, the Superior Court found that Plaintiffs did not sufficiently allege "red flags" to show that the Board knew its internal controls were inadequate during this period. Order Re Demurrer at 12-15. The SLC's investigation confirms that during the period of 2010 to 2013, the directors acted in good faith and did not have reason to know that Apple's antitrust compliance program was in any way deficient, *i.e.*, there were no red flags that should have notified the Board that the program needed to be changed.

To the contrary, during the period between the iPad Launch and the Final Judgment, the directors could and did properly rely on Apple officers and employees to create and maintain an adequate compliance program. The Board knew that under the guidance of CCO Tom Moyer and the new Director of Competition Law, Kyle Andeer, and others, Apple was continuing to improve its existing compliance programs. Thus, even had there been red flags, which there were not, the directors knew that Apple was affirmatively taking steps to improve antitrust compliance, and did not ignore red flags in bad faith.

The potential damages arising from these alleged failures after the Publisher Agreements were entered into are too speculative and small to justify the costs and risks of Apple suing its own indemnified directors, even if there was a claim. At most, the damages would be the costs associated with imposition of the Monitorship. The Monitor costs were an immaterial amount to a company with approximately $150 billion in annual revenue at the time, and infinitely less than the possible injury Apple's shareholders would suffer if Apple (with a stock value of more than $600 billion) sued its own Board and CEO. Moreover, as discussed below, while the Monitorship imposed a burden on Apple, it also brought the benefit that Apple built a higher

quality antitrust compliance program.

Therefore, the breach of fiduciary duty claim based on allegations of lack of director oversight between the iPad Launch and the Final Judgment is unsupported and contradicted by the facts, and lacks a viable theory of damages.

C. Allegations Relating To The Final Judgment And Monitorship

Finally, Plaintiffs allege that the Director Defendants breached their fiduciary duties by consciously failing to comply with the Final Judgment, issued on September 5, 2013, thereby exposing Apple to risk of contempt. SCAC, ¶¶ 253-289; Order Re Demurrer at 8. The District Court that entered the Final Judgment, however, never found Apple violated the Final Judgment, never found Apple in contempt (nor did any party request that Apple be held in contempt), and dismissed the Monitor after the minimum term of two years, with the DOJ's support. The DOJ concluded that Apple's disputes with the Monitor did "not prevent the Monitor from satisfying his responsibilities or Apple from greatly improving its antitrust policies, procedures, and training." Thus, no liability exposure arose for Apple, or any director, as a result of any director or Board conduct during the Monitorship.

In the SLC's interview, the Monitor confirmed that he does not believe—and has no reason to believe—that any Apple director was responsible for the negative issues that he discussed in his Reports. Plaintiffs erroneously allege that the Monitor reported that "the Board failed to make itself available to the monitoring team by 'consistently resist[ing] and [being] unresponsive' to repeated requests for interviews and/or information," and that "the Board 'unnecessarily complicated [] monitoring efforts by making unilateral decisions that [] affected [the Monitor's] ability to discharge [its] responsibilities.'" SACC, ¶ 268, citing and (selectively) quoting Second Report at 22, 56 (brackets in original). These quotes are inaccurate. The Monitor's Reports made these statements about "Apple," not "the Board." The Monitor confirmed to the SLC that these allegations by Plaintiffs about his reports were not accurate.

In PwC's independent review of Apple's antitrust compliance program, conducted at the end of the Monitorship, PwC confirmed that Apple's Board and AFC expressed its commitment

to compliance to Apple's Senior Management. PwC further confirmed in its interview with the SLC that by the end of the Monitorship, Apple had developed one of the most comprehensive antitrust compliance programs in the United States, which includes a dedicated Antitrust Compliance Officer, and detailed policies for educating employees, detecting issues, reporting possible violations and addressing antitrust risks.

The SLC has determined that the Director Defendants complied with the Final Judgment, and has found no evidence that any Director Defendant engaged in any wrongdoing or intentionally did anything to interfere with the Monitorship. Each Director Defendant interviewed by the SLC, including the members of the AFC, confirmed that he or she believed Apple should work cooperatively with the Monitor to ensure that Apple fully complied with the Final Judgment. The Director Defendants conveyed their views to management that they wanted Apple to comply with the Final Judgment. The Director Defendants fully supported Apple's compliance with the Final Judgment and cooperation with the Monitor, and supported Apple's development and implementation of a first rate antitrust compliance program.

Board members, and particularly the AFC, actively reviewed the substantive compliance materials prepared by Mr. Moyer, Ms. Said, Mr. Andeer, and others. The AFC reviewed all of the Monitor's recommendations and Apple's proposed responses to them to determine if Apple was adequately complying with the Monitor's recommendations, if Apple's objections to any recommendation were warranted and appropriate, and if Apple was building a strong compliance program. These facts are substantiated by the materials provided to the AFC, by the Monitor's Reports, by PwC's report, and by the SLC's interviews with the Monitor, PwC, directors, and employees at Apple.

Plaintiffs also plead that Apple's responses to the Monitor's substantive recommendations were deficient, that such responses constitute a breach of fiduciary duty by the directors, and even that the directors placed Apple in violation of the Final Judgment. As an initial matter, the directors were entitled to rely on Apple's employees and executives to work directly with the Monitor on those issues. *See Briano*, 46 Cal. App. 4th at 1179 ("directors are

entitled to rely upon the officers and employees of the corporation."). Those allegations are also demonstrably wrong. Apple objected to only a handful of the Monitor's one hundred recommendations. In each instance, Apple provided clear and specific reasons for its position in writing (which writings were attached to the non-public version of the Monitor's Reports). In every instance, the Monitor and Apple agreed either to forgo or modify the recommendation. The Monitor, who was specifically directed in the Final Judgment to report any violation of the Judgment to the DOJ, never made any such report. The District Court's dismissal of the Monitor after two years with the consent of the DOJ conclusively proves that Apple complied with the Final Judgment.

Finally, Plaintiffs have no viable theory of damages based on the allegations regarding the Monitorship, which lasted the minimum period of the Monitor's appointment. The District Court did not issue contempt sanctions against Apple as a result of the difficulties with the Monitor (difficulties the Board did not cause or authorize, and for which the directors are not personally liable in any event), and the de minimis costs incurred do not justify the costs of Apple suing its own indemnified directors and officers. Moreover, any damage analysis would have to take into account Apple's benefit from the Monitorship, which includes the benefit of having "revamped" its antitrust compliance program. There is no factual or legal basis on which to pursue a claim against any Director Defendant for conduct related to the Monitorship.

XIII. INDEMNIFICATION OF DIRECTORS

As part of its investigation, the SLC reviewed the indemnity agreements that Apple entered into with each director (the "Indemnity Agreement"). The Indemnity Agreement provides that Apple will indemnify each director to the maximum extent permitted by law and states that it "shall apply to acts or omissions of [the director] which occurred prior [the execution] date if [the director] was serving in any Corporate Status at the time such act or omission occurred." *Indemnity Agreement*, § 12. Corporate Status is defined to include a person who was acting as an employee or agent of Apple. *Id.*, § 13(a). The Indemnity Agreement therefore applies to all derivative claims against the Director Defendants.

For claims brought by or on behalf of Apple (the "Company") against any director (the "Indemnitee"), the Indemnity Agreement provides that:

> [T]he Company shall indemnify Indemnitee against any and all Expenses and, to the fullest extent permitted by law, amounts paid in settlement … unless the Company shall establish, in accordance with the procedures described in Section 3 of this Agreement, that Indemnitee did not act in good faith and in a manner Indemnitee reasonably believed to be in the best interests of the Company and its shareholders, except that no indemnification shall be made in respect of any claim, issue or matter as to which Indemnitee shall have been adjudged to be liable to the Company … unless and only to the extent that the court in which such Proceeding is or was pending shall determine … Indemnitee is fairly and reasonably entitled to indemnity for Expenses or amounts paid in settlement….

Id., § 2(b). The Indemnity Agreement also requires Apple to advance expenses incurred by directors in defending against the claim:

> The Company shall advance all Expenses incurred by Indemnitee in connection with [a claim brought by Apple] (but not amounts actually paid in settlement of any such Proceeding). Indemnitee hereby undertakes to repay such amounts advanced only if, and to the extent that, it shall ultimately be determined that Indemnitee is not entitled to be indemnified by the Company as authorized hereby. … Advances shall be unsecured and interest free. Advances shall be made without regard to Indemnitee's ability to repay such amounts and without regard to Indemnitee's ultimate entitlement to indemnification under the other provisions of this Agreement. Advances shall include any and all Expenses incurred pursuing an action to enforce this right of advancement ….

Id., § 3(a). *See also* Cal. Corp. Code § 317(c).

In short, pursuant to the Indemnity Agreement and applicable California law, if Apple were to bring a claim against a director, then Apple must advance all expenses incurred by them in defending against Apple's claim. If Apple were to prevail on its claim against a director, then the director would not be indemnified for the amount of the judgment, and the director would have to repay the expenses advanced unless a court determines that the repayment of expenses was not warranted based on the totality of the circumstances. If Apple were to lose a claim asserted against a director, Apple would not be reimbursed for the expenses it advanced to defend against the claim.

XIV. CONSIDERATIONS OF THE SLC

Below is a non-exhaustive list of factors considered by the SLC in reaching its conclusion that settlement of the Derivative Action is in Apple's best interests:

- whether each Director Defendant engaged in any conduct that gives rise to a cause of action by Apple;
- Management's reports to the AFC and Board regarding compliance and risk assessments;
- the competence and engagement of Apple's compliance management;
- the rights of directors to reasonably rely on the information and opinions of others, including employees, attorneys, officers, other directors, and committees of the board;
- the high level of participation of directors in committee and board meetings;
- the applicability of the business judgment rule protecting reasonably prudent good faith business decisions by directors;
- Mr. Cue's reliance on, and the involvement of, Apple legal counsel during the ebook negotiations, consistent with Apple's antitrust compliance policy;
- the unique nature of the antitrust violation found by the District Court;
- the history of Apple's compliance programs prior to the ebook negotiations;
- the Director Defendants' support for Apple establishing a best-in-class antitrust compliance program;
- the Monitor's statements to the SLC regarding the Director Defendants;
- the Monitor's assessment of Apple's antitrust compliance program at the end of the Monitorship;
- Apple's performance of the Monitor's recommendations;
- the quality of Apple's antitrust compliance program developed during the Monitorship;
- PricewaterhouseCoopers' independent evaluation of Apple's antitrust compliance program at the end of the Monitorship;
- the DOJ's assessment of Apple's antitrust compliance program and resulting recommendation to the District Court to discharge the Monitor;
- the District Court's Order concluding the Monitorship;
- Apple's continued efforts to maintain Antitrust compliance policies and procedures;
- the existence of current audit procedures designed to test and evaluate Apple's

exposure to compliance risk;

- the likelihood that asserting any claim against any defendant would yield no financial recovery for Apple;
- the cost to Apple in resources of time and money of pursuing any claim against any defendant;
- the existence of defendants' exculpation and indemnity rights;
- the effect that pursuit of the claims would have on Apple's reputation, standing in its industry, and morale among its employees; and
- the potential harm to Apple and its shareholders from protracted litigation with its directors;
- The costs and advantages of settlement compared to the costs and business interruption of continued litigation.

XV. THE SLC'S DECISION REGARDING SETTLEMENT

As a result of its comprehensive review of the materials and facts summarized in this Report and the Cue Report, the SLC has determined settlement of the Derivative Action is in Apple's best interests.

The Derivative Action has been expensive and distracting for the company, including for management. *See In re Oracle Sec. Litig.*, 852 F. Supp. 1437, 1443 (N.D. Cal. 1994) ("Derivative litigation is unavoidably distracting to corporate officials whose efforts might more profitably be devoted to the company's business."). Plaintiffs have sought extensive discovery, including detailed interrogatories for each of the defendants as well as a deposition schedule that would occupy the time of Apple directors, officers and employees. The litigation has required separate counsel for a number of parties, including for Mr. Cue, Ms. Wagner, the Director Defendants, and Apple. The cost for all of these counsel is borne by the corporation.

With the backdrop of all of the activity and cost of the litigation, and months after its investigation began, the SLC engaged in mediation to determine if a prompt and reasonable resolution of the matter could be achieved, and thereby avoid further costs and business interference that would result from ongoing litigation.

For the reasons explained herein and in the Cue Report, the SLC determined that the claims against Mr. Cue and the Director Defendants lack merit and that pursuing litigation

against any defendant was not likely to be successful and would not yield any recovery for the company, let alone any significant recovery warranting such costs and distraction. The SLC concluded that termination of the entire action against all defendants is in Apple's and its shareholders' best interest. The SLC recognized that seeking to terminate the Derivative Action through motion practice after completion of its reports always has inherent risk and lacks the benefit of immediate termination of the lawsuit that settlement provides. In addition, once the SLC seeks termination by dismissal, the Plaintiffs are also entitled to seek discovery about the SLC's extensive investigation and independence, thereby delaying resolution and increasing costs.

The parties mediated the claims in the SCAC before the Honorable Layn Phillips. Both members of the SLC attended and participated in an entire day of mediation on November 15, 2017. Thereafter, negotiations with Plaintiffs were conducted through the mediator from the date of the live mediation through March 3, 3017, when the terms of settlement were agreed upon and, as a result, active litigation ceased. Both SLC members were actively involved in the negotiations.

Based on the SLC's conclusion regarding the lack of merit of the claims asserted in the SCAC, no monetary damages will be paid to the company by or on behalf of any defendant. However, as part of the settlement, the SLC agreed to entertain in good faith specific enhancements to Apple's existing antitrust compliance program, which will benefit Apple and its shareholders more than continued protracted litigation. The SLC consulted with appropriate Apple personnel who confirmed that the agreed upon enhancements would be feasible and beneficial. The settlement agreement regarding enhancements is as follows:

> As a part of a settlement of the claims asserted in the Second Amended Consolidated Complaint, the following Board resolutions shall be adopted and remain in place until at least December 2022:
>
> 1. Apple's Antitrust Compliance Program described in Exhibit A[5] is hereby formally adopted.

[5] The Antitrust Compliance Program is described in Section X.

2. The Audit and Finance Committee (AFC) shall meet at least quarterly, and in any event shall meet within four weeks of notice of the formal institution of any state or federal antitrust investigation.

3. Apple's Antitrust Compliance Officer (ACO) shall attend the quarterly in-person AFC meetings and advise the AFC regarding significant antitrust issues and legal developments relevant to the Corporation's business.

4. The ACO shall provide the AFC with a quarterly written report regarding Apple's compliance with the Final Judgment, including updates concerning:

(i) the status of the Implementation Plan;

(ii) the status and results of any risk assessment or risk audit performed by the ACO or any employee or third party consultant engaged by the ACO to perform or provide assistance to the ACO in performing the risk assessment or audit;

(iii) an evaluation of Apple's internal controls, reporting procedures, systems, and policies, including recommendations based upon that evaluation; and

(iv) any complaints or violations of the antitrust laws, or the compliance measures in place at Apple to detect and prevent violations of the antitrust laws.

5. The AFC shall conduct an annual review (Annual Review) to consider any antitrust matters that may impact the Corporation and to determine whether the Corporation's corporate governance is providing adequate protection with respect to antitrust matters. The Annual Review shall include:

(i) reviewing an antitrust risk assessment report prepared by the Corporation's management and/or any other committee or employee group dedicated to antitrust compliance, respecting all aspects of the Corporation and all product lines, such that the AFC can properly evaluate the Corporation's antitrust risk both at the enterprise level and on a product line basis;

(ii) receiving a written report from the Corporation's management or a third party consultant regarding the current status of any practices implemented because of the Final Judgment and Order Entering Permanent Injunction, or a result of a recommendation from the monitor appointed through that process; and

(iii) reviewing any recommendations made by the monitor, but not adopted by the Corporation, to determine whether they should be adopted at that time, or whether a similar provision may be beneficial to the Corporation.

6. Based on the Annual Review, the AFC shall determine whether the policies and practices of the Corporation with respect to antitrust compliance are appropriate and sufficient, and whether any new policies need to be adopted, or whether modifications to existing policies need to be made.

7. The AFC shall provide a report to the Board regarding the results of its Annual Review.

8. The AFC shall meet at least annually with the top executives it deems critical to the success of the Corporation's antitrust compliance policies to discuss the current state of such policies.

9. Quarterly Board meetings shall include discussion of any material litigation or material potential litigation involving alleged antitrust violations.

10. The ACO shall:

(i) meet with members of any division at Apple responsible for a new product launch to discuss and evaluate any antitrust concerns relating to that new product; and

(ii) provide a report for the Board and the Chief Executive Officer on a regular basis, addressing any antitrust concerns respecting the launch of any new product and indicating the means that the Corporation intends to take to address such concerns.

11. The ACO shall continue to have access to all Corporation documents and personnel she/he requires to carry out her/his duties.

12. The Chair of the AFC shall meet with the ACO on a quarterly basis, and review with the ACO the efficacy of any antitrust compliance measures.

13. The Chair of the AFC shall review and provide guidance regarding compensation, hiring and firing related to the ACO, and the AFC shall review and provide guidance regarding the scope of the ACO's duties and responsibilities.

14. The Board and the other Apple employees listed in Sections V.A and V.B of the Final Judgment issued by Judge Cote on September 5, 2013, shall receive annual training in antitrust compliance.

15. The Corporation shall make its antitrust and competition law and policy available to the public on its corporate governance website.

16. On an annual basis, the ACO shall retain an independent consultant to update the antitrust compliance program review conducted by PricewaterhouseCoopers in 2015. The independent consultant shall identify material deficiencies, if any, in the Corporation's antitrust compliance program. The independent consultant shall provide a report to the AFC, which shall consider the recommendations in the report.

17. The Corporation shall add language to its proxy statement indicating that antitrust compliance experience will be one of the factors considered by the Nominating & Corporate Governance Committee in identifying candidates for the next open position for director.

18. The Chief Compliance Officer shall meet annually with the AFC to discuss the performance of the ACO.

19. The ACO shall meet quarterly with the head of the Competition Law Team to discuss significant antitrust issues and legal developments relevant to the Corporation's business.

Once the above enhancements were negotiated and agreed upon in final form, the parties negotiated a fee for Plaintiffs' counsel. The fee negotiations, also conducted through Judge Philips, took into account the then-current state of the litigation, the interests of Apple in terminating the litigation before incurring further costs and business interference, the value of the enhancements, and a general sense of the amount of work performed by Plaintiffs. Based on these considerations, the SLC agreed to a fee of $2.75 million, which Plaintiffs will present for approval to the Superior Court.

XVI. CONCLUSION

The claims asserted in the Derivative Action lack merit, but Apple's best interests are served by eliminating the risk, costs, delay and distraction associated with continued protracted litigation. Apple will benefit from the negotiated enhancements to Apple's already high quality antitrust compliance program. The SLC has been granted plenary authority by the Apple Board of Directors to settle this litigation, and will seek to do so on the terms that were negotiated.

The Special Litigation Committee of the Board of Directors of Apple Inc.

Date: May __, 2017

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SUSAN L. WAGNER

Date: May __, 2017

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JAMES A. BELL

SHARTSIS FRIESE LLP

Date: May __, 2017

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ARTHUR J. SHARTSIS

Attorneys for the Special Litigation Committee of the Board of Directors of Apple Inc.