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Case No. 4521-CC

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

MCG CAPITAL CORPORATION, for itself and in the right and for the benefit of Jenzabar, Inc., Plaintiff, v. ROBERT A. MAGINN, JR., LING CHAI, JAMISON BARR, JOSEPH SAN MIGUEL, DANIEL QUINN MILLS, JENZABAR, INC., Defendants, and JENZABAR, INC., Nominal Defendant.	C.A. No. 4521-CC

DEFENDANTS ROBERT A. MAGINN, JR.'S AND LING CHAI'S
OPENING BRIEF IN SUPPORT OF THEIR MOTION TO DISMISS

OF COUNSEL:

Stephen D. Poss
Kevin P. Martin
GOODWIN PROCTER LLP
Exchange Place
53 State Street
Boston, MA 02109
(617) 570-1000

POTTER ANDERSON & CORROON LLP
Peter J. Walsh, Jr. (DSB. No. 2437)
Abigail M. Legrow (DSB No. 4673)
Daniel A. Mason (DSB No. 5206)
1313 N. Market Street
Hercules Plaza, 6th Floor
P.O. Box 951
Wilmington, Delaware 19899
(302) 984-6000

Attorneys for Defendants Robert A. Maginn, Jr. and Ling Chai

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PRELIMINARY STATEMENT

Defendants Robert A. Maginn, Jr. and Ling Chai join in the arguments in support of the Motion to Dismiss presented by the remaining defendants – Jenzabar, Inc., Jamison Barr, Joseph San Miguel, and Daniel Quinn Mills – in their separate memorandum of law (the "Jenzabar Opening Brief"). Maginn and Chai submit this memorandum to present arguments particular to their own defense, and to provide additional arguments relating to some common defenses.

As an initial matter, a count-by-count review of each of the 12 counts in the Complaint and the documents cited therein demonstrates that plaintiff MCG Capital Corporation ("MCG") has failed to state any claims against Maginn or Chai. Indeed, several of the Counts brought against Maginn and Chai make absolutely no sense, and the only explanation can be that MCG did not care what claims it asserted against which defendants, but was only concerned with exerting pressure on all of the defendants.

First, it is clear that Maginn and Chai cannot possibly be proper defendants with respect to Count 1 ("Breach of Contract" with respect to the Preferred Stock and Warrant Purchase Agreement ("PSWPA")) and Count 2 ("Breach of Charter") because they are not parties to the PSWPA or the Charter, nor under the terms of these agreements can they "approv[e] compensation increases," the alleged basis for liability in these Counts. It was thus completely irresponsible and frivolous for MCG to name "all Defendants" as the subjects of Counts 1 and 2. For the same reasons, Maginn and Chai cannot be proper defendants with respect to Counts 9, 10, and 11, all of which seek declaratory judgments concerning the interpretation of the PSWPA and Charter. These counts therefore must be dismissed for failure to state a claim against these two defendants.

Second, Counts 7, 8, and 12, all of which seek an "accounting" or "rescission" of salary and bonus payments made to Maginn and Chai, must be dismissed because they do not even

state a claim – an "accounting" and "rescission" are remedies, not separate causes of action.

Third, Counts 1, 2, 3, 4, 5 (in part), 6, 7, 8, 9, 10, and 12, all of which concern the payment of compensation to Maginn and Chai by Jenzabar,[1] must all be dismissed for the separate and independently sufficient reason that, as explained in the Jenzabar Opening Brief, the documents upon which MCG relies in its Complaint clearly permit the Jenzabar Board of Directors (or the Compensation Committee thereof) to consider and grant increases in base salary and bonus to Maginn and Chai, with or without MCG's approval. Indeed, contrary to MCG's theory that the payment of salary and bonuses to Maginn and Chai is a "transaction, contract, agreement or arrangement with an Affiliate" within the meaning of the PSWPA, the PSWPA explicitly acknowledges the existence of Maginn's agreement as a "Material Contract" **and** states, in a provision entitled "Transactions with Affiliates," that "No affiliate of the Company and no officer or director of the Company … is a party to any material Contract or transaction with the Company." This makes clear what common sense already suggests, that the payment of compensation to a corporate officer is not a transaction with a corporate affiliate for purposes of the PSWPA.

Fourth, Counts 3 and 4, which accuse Maginn and Chai of aiding and abetting the breaches of contract that are the subject of Counts 1 and 2, must be dismissed because (as further explained in the Jenzabar Opening Brief) there is no applicable cause of action under Delaware law against an officer or director of a corporation for aiding and abetting a breach of contract by

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[1] Jenzabar's Compensation Committee approved the salary increases and bonuses about which MCG now complains in late 2008. (*See* Compl. ¶¶ 40-47). MCG alleges that the Compensation Committee's approval of such compensation "violated MCG's consent and voting rights." (*Id.* ¶ 40). The Complaint fails to explain why – if such rights were violated – MCG took no action with respect to such compensation issues for months. Tellingly, MCG challenged these compensation payments only ***after*** receiving notice from Jenzabar in late March 2009 of its intention to repurchase MCG's stock. (*Id.*).

the corporation. Moreover, MCG's theory that Maginn and Chai could aid and abet a breach of contract merely by asking for a raise runs afoul of the express provisions in their employment contracts requiring the Board of Directors to consider increasing their base salary and bonuses.

Fifth, Count 6, which brings a claim of "unjust enrichment" against Maginn and Chai, must be dismissed because, among other reasons, MCG's Complaint itself alleges that the compensation paid to Maginn and Chai is the subject of numerous contracts – including, among others, their employment contracts – and it is black letter law that an unjust enrichment claim will not lie where express contracts govern the subject matter at hand. Furthermore, MCG's unjust enrichment claim alleges that the salary and bonuses paid to Maginn and Chai are "over and above amounts permitted under the terms of their respective Employment Agreements," but those agreements contain no limits on compensation and explicitly contemplate increases in compensation for Maginn and Chai. Indeed, MCG's Complaint does not even allege, as a necessary element for an unjust enrichment claim, that the compensation paid to Maginn and Chai is more than fair compensation for their efforts on Jenzabar's behalf. Count 6 is clearly another claim that simply does not make sense on its face, and can only have been brought to increase litigation expenses and risks for the Defendants.

Finally, even the Complaint makes clear that many of the alleged breaches of fiduciary duty which are the subject of Count 5 cannot have been committed by Maginn or Chai. In particular (and yet again), they have no ability to "approv[e] bonus payments and salary increases" to themselves, and the Complaint does not allege that they made any assertions in their individual capacity to MCG concerning MCG's rights and duties under the Jenzabar Charter. Maginn and Chai join in the arguments, made in the Jenzabar Opening Brief, that MCG cannot bring a breach of fiduciary duty claim against anyone with respect to the remaining

aspects of Count 5. Furthermore, Count 5 must be dismissed because it alleges a breach of Defendants' fiduciary duties as directors of Jenzabar, and the Jenzabar Charter explicitly exculpates the company's directors with respect to such claims.

In addition to these reasons why no claim is stated against Maginn and Chai, Maginn and Chai also join in, and expressly incorporate herein by reference, the arguments made in the Jenzabar Opening Brief that the entire Complaint must be dismissed (except Count 11 as to defendant Jenzabar). These arguments include, *inter alia*, MCG's failure to state a claim with respect to each of the counts in its Complaint, failure to make demand on the Board of Directors, and failure to satisfy the necessary criteria to represent Jenzabar's shareholders in a derivative action.

In summary, for the reasons given herein and in the Jenzabar Opening Brief, each of the counts in MCG's Complaint must be dismissed as against defendants Maginn and Chai.

NATURE AND STAGE OF THE PROCEEDINGS

Plaintiff MCG filed this action on April 21, 2009 against Jenzabar and four (4) of the five (5) members of its Board of Directors, including defendants Maginn and Chai.[2] Also named as a defendant is Jamison Barr ("Barr"), Jenzabar's Vice President and General Counsel. The Verified Complaint ("Complaint" or "Compl.") purports to bring direct claims against the Defendants on MCG's behalf, as well as derivative claims on behalf of Jenzabar.

On May 18, 2009, defendants jointly moved to dismiss all of MCG's claims, except for a portion of Count 11 (relating to the repurchase of MCG's Senior Preferred Stock). This is defendants Maginn's and Chai's Opening Brief in support of their motion to dismiss the claims asserted against them. Defendants Jenzabar, Barr, San Miguel and Mills are filing a brief

[2] MCG did not name as a defendant its designee to the Board, Peter Malekian.

contemporaneously herewith, which Maginn and Chai join and expressly adopt (hereinafter "Jenzabar Opening Brief").

STATEMENT OF FACTS[3]

Defendants Maginn and Chai hereby adopt the Statement of Facts set forth in the Opening Brief of Jenzabar and the other defendants. For purposes of their motion to dismiss, the pertinent allegations of the Complaint are as follows:

I. Robert A. Maginn, Jr.

Maginn is a member of the Board of Directors of Jenzabar, and has served as the Chairman of the Board since 1998 and as the Company's Chief Executive Officer since 2001. (Compl. ¶ 3). Mr. Maginn led Jenzabar's transformation from a dot-com start-up to an enterprise solution provider. Mr. Maginn brings to Jenzabar decades of expertise in business strategy from his nearly twenty years as a Senior Partner and Director at Bain & Company prior to joining Jenzabar. Pursuant to the terms of an Employment Agreement between Maginn and Jenzabar, approved by MCG at the time of its investment in Jenzabar in June 2004 (*see* Transmittal Affidavit of Geoffrey G. Grivner, Esq. ("Grivner Aff.") at Exh. A),[4] Maginn has (since June 2004) received from Jenzabar a base salary of $400,000 per year, plus bonuses totaling approximately $3.7 million, for an average annual compensation of approximately $1.14 million. (*See* Compl. ¶¶ 27-28).[5]

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[3] The "facts" recited herein are derived from the allegations of the Verified Complaint and documents incorporated by reference therein, and may be assumed to be true solely for purposes of this motion, and only to the extent they are non-conclusory and do not contradict those documents cognizable by the Court on this Motion.

[4] As set forth in Jenzabar's Opening Brief, the Employment Agreements of Maginn and Chai are integral to MCG's claims and incorporated into the Complaint, and therefore, may be considered on a motion to dismiss. Jenzabar Opening Brief, at 6 n.5.

[5] Maginn also holds a considerable equity stake in Jenzabar, including options and common stock, which align his interests with the interests of the Company. (Compl. ¶ 30).

Maginn's Employment Agreement twice refers to the Board of Directors possessing authority to increase Maginn's compensation. First, with respect to Maginn's base salary, the Employment Agreement states:

> The Board shall periodically review Executive's Base Salary consistent with the compensation practices and guidelines of the Company, <u>but</u> the Board shall have no obligation or requirement to increase such Base Salary at any time during the Term. … If Executive's Base Salary is increased by the Board during the Term, <u>then</u> such increased Base Salary shall then constitute the Base Salary for all purposes of this Agreement.

(Grivner Aff., Exh. A, § 5(a)). Second, Section 5(b)(ii) of the Employment Agreement, governing quarterly bonuses, states:

> The Board shall periodically review Executive's Quarterly Bonus for increase (but not decrease below 54% of the Executive Bonus Pool), consistent with the compensation practices and guidelines of the Company.

(*Id.* § 5(b)(ii)). Thus, through use of the word "shall" Maginn's Employment Agreement not only permits, but explicitly requires "the Board" to review Maginn's base salary and bonus for potential "increase" and empowers the Board to grant such increases.

II. <u>Ling Chai</u>

Chai founded Jenzabar in 1998. She is a member of the Board of Directors, and since March 2001 has served as the Company's President and Chief Operating Officer. She is married to Maginn. (Compl. ¶4). Pursuant to the terms of an Employment Agreement between Chai and Jenzabar, approved by MCG at the time of its investment in Jenzabar in June 2004 (*see* Grivner Aff., Exh. B), since June 2004 Chai has received from Jenzabar a base salary of $340,000 per year, plus bonuses totaling approximately $972,000, for an average annual compensation of $534,000. (*See* Compl. ¶¶ 27, 29; Grivner Aff., Exh. B, § 5(a)).[6]

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[6] Chai also holds a considerable equity stake in Jenzabar, including options and common stock,

As with Maginn's Employment Agreement, Chai's Employment Agreement explicitly requires the Board of Directors to consider whether to raise Chai's base salary and bonus. It identically states that

> The Board of Directors of the Company ("Board") shall periodically review Executive's Base Salary consistent with the compensation practices and guidelines of the Company, <u>but</u> the Board shall have no obligation or requirement to increase such Base Salary at any time during the Term. … If Executive's Base Salary is increased by the Board during the Term, <u>then</u> such increased Base Salary shall then constitute the Base Salary for all purposes of this Agreement.

(Grivner Aff., Exh. B, § 5(a)). And it identically states that

> The Board shall periodically review Executive's Quarterly Bonus for increase (but not decrease below 22% of the Executive Bonus Pool), consistent with the compensation practices and guidelines of the Company.

(*Id*. § 5(b)(2)).

III. <u>The December 2008 Compensation Committee Approvals</u>

On December 18, 2008, the Compensation Committee of the Board of Directors, consisting of Defendants San Miguel, Mills and MCG's designee, Malekian, approved a salary increase for Maginn from $400,000 to $450,000. (Compl. ¶ 44). The Committee further approved a bonus to Maginn for fiscal years 2007 and 2008. (*Id*. ¶ 47). MCG's designee to the Board, Malekian, opposed the salary increase and bonuses. (*Id*. ¶ 44). At the same meeting, the Committee approved a salary increase for Chai from $340,000 to $380,000. (*Id*. ¶ 44). The raises were the first time that Maginn's and Chai's salaries had increased since execution of the Employment Agreements in June 2004. The Committee further approved a bonus to Chai for fiscal years 2007 and 2008. (*Id*. ¶ 44). The Complaint does not specify the amount of Chai's

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which align her interests with the interests of the Company. (Compl. ¶ 30).

bonus, but alleges that the Committee approved a total of $794,000 collectively for Maginn and Chai for 2007 and 2008. (*Id.* ¶ 47).

On December 23, 2008, the Compensation Committee approved a $750,000 bonus to Maginn that had been authorized in 2002 by the Jenzabar Board of Directors, but which, as a result of an oversight, had never been paid. (Compl. ¶ 50). This bonus was also approved and paid over the objection of MCG's director designee, Malekian. (*Id.* ¶¶ 51, 54). MCG claims that Maginn also requested an "additional retroactive bonus of $3.5 million," but does not allege that such bonus was ever considered or approved by the Compensation Committee, or ever paid. (*See id.* ¶ 56).

IV. MCG's Claimed Right To Consent To Salary Increases And Bonuses

MCG invested in Jenzabar by way of term loans on June 30, 2004 in exchange for Senior Preferred Stock, Subordinated Preferred Stock and warrants to purchase shares of Jenzabar common stock. (Compl. ¶¶ 11, 20). Jenzabar repaid the loans in March 2006. (*Id.* ¶ 21). According to the Complaint, on March 31, 2009, Jenzabar sent MCG a notice indicating its intent to repurchase MCG's Preferred Stock. (*Id.* ¶ 71).[7] Pursuant to the Charter, if the Preferred Stock is repurchased, MCG may lose a right of consent or approval as to certain corporate actions, such as the issuance or redemption of stock, the payment of dividends, mergers and acquisitions, and reconstituting the Board. (*Id.* ¶ 74).

According to the Complaint, the sources of MCG's alleged "consent and voting rights" are Section 5.12(h) of the Preferred Stock and Warrant Purchase Agreement (the "PSWPA") and Article V of Jenzabar's Fifth Amended and Restated Certificate of Incorporation (the "Charter"). (Compl. ¶¶ 36, 38). In fact, the PSWPA and Charter only prohibit Jenzabar from entering into certain extraordinary transactions, including any "transaction, contract, agreement or

[7] While not pertinent to the Motion to Dismiss, the notice was actually sent on March 30.

arrangement with an affiliate," including with a "shareholder, officer, or director," without the consent or approval of MCG. (Charter (Compl. Exh. 1), art V, § 1(a); PSWPA (Compl. Exh. 2), § 5.12). Neither the PSWPA nor the Charter anywhere purports to restrict Jenzabar's or its Compensation Committee's ability to make compensation decisions, particularly those authorized by Maginn's and Chai's Employment Agreements, which were approved by MCG and executed contemporaneously with the PSWPA and Charter. (*See* Compl. Exh. 1, 2). Further, Section 3.24 of the PSWPA expressly excludes the Employment Agreements from the scope of "affiliate transactions" subject to Section 5.12's restrictions. *Compare* PSWPA (Compl. Exh. 2), § 3.24 ("No affiliate of the Company, and no officer or director of the Company … is a party to any material Contract or transaction with the company"), *with id.*, § 3.10 and Schedule 3.10 (listing the Maginn Employment Agreement as a "material contract" of Jenzabar). MCG's Complaint fails to explain or justify MCG's extraordinary reading of the PSWPA and Charter.

ARGUMENT

Under Court of Chancery Rule 12(b)(6), a claim will be dismissed "where it appears with 'reasonable certainty' that the plaintiff could not prevail on any set of facts that can be inferred from the pleadings." *In re Paxson Commc'n Corp. S'holders Litig.*, 2001 Del. Ch. LEXIS 95, at *7 (Del. Ch.) (citation omitted).[8] When considering a complaint's sufficiency, all well-pleaded allegations of fact and reasonable inferences to be drawn therefrom are accepted as true, but neither inferences nor conclusions of law or fact are accepted as "true without specific allegations of fact which support the conclusion." *Haber v. Bell*, 465 A.2d 353, 357 (Del. Ch. 1983) (citation omitted); *see Zoren v. Genesis Energy, L.P.*, 836 A.2d 521, 527 (Del. Ch. 2003); *Steinman v. Levine*, 2002 Del. Ch. LEXIS 132, at *26 (Del. Ch.), *aff'd*, 822 A.2d 397 (Del. 2003) (TABLE). This Court may also consider in conjunction with a motion to dismiss "documents

[8] A compendium of unreported decisions is being filed simultaneously herewith.

outside the pleadings … as long as [they] are integral to the plaintiff's claim." *Sanders v. Devine*, 1997 Del. Ch. LEXIS 131, at *14 (Del. Ch.) (citations omitted).

Upon an examination of the pleadings in the Complaint and the documents referenced therein, it is clear that MCG has failed to state any claims against Maginn or Chai. Indeed, many of the Counts in the Complaint make absolutely no sense as asserted against Maginn and Chai.

I. Counts 1, 2, 9, 10, and 11 Cannot Be Brought Against Maginn and Chai

Counts 1, 2, 9, 10, and 11 must be dismissed for the reasons given in the Jenzabar Opening Brief, and also for the additional reasons particular to Maginn and Chai provided herein.

As an initial matter, Counts 1 and 2, for "Breach of Contract" and "Breach of Charter," both allege that the "Defendants" breached the PSWPA and Charter by "approving compensation for Maginn and Chai without the consent of, and over the objection of, MCG." Compl. ¶¶ 89, 93. But the Complaint does not allege that Maginn and Chai approved their own compensation – it alleges that two members of the Compensation Committee of the board, of which Maginn and Chai are not members, did so. *See id.* ¶¶ 40-47. Thus, as applied to Maginn and Chai Counts 1 and 2 on their face make absolutely no sense, and are frivolous and irresponsible, because the Complaint itself makes clear that they did not take the actions that are the subject of those Counts. For this reason alone these Counts must be dismissed against Maginn and Chai.

In addition, Count 1 must be dismissed against Maginn and Chai for the additional and independently sufficient reason that they are not parties to the PSWPA, and directors and officers of a corporation are not parties to, or liable on, corporate contracts, as long as they do not purport to bind themselves individually, *Wallace v. Wood*, 752 A.2d 1175, 1180 (Del. Ch. 1999), and as long as they act within their roles, *Shearin v. E.F. Hutton Group, Inc.*, 652 A.2d 578, 590 (Del. Ch. 1994). Here, the Complaint has not alleged that Maginn and Chai are parties to the PSWPA

or acted outside their roles as directors and officers of the Company, and the face of the documents demonstrates that neither Maginn nor Chai executed them in his or her individual capacity.

Similarly, Count 2 must be dismissed against Maginn and Chai because corporate officers and directors are not proper defendants in an action brought by preferred shareholders alleging breach of the corporate charter. As explained in the Jenzabar Opening Brief at 32-35, a corporate charter is in substance a contract between the corporation and the preferred shareholders. Because the Maginn and Chai are not parties to that contract, they cannot be defendants in an action alleging breach of the Charter.

Likewise, with respect to Claims 9, 10, and 11, these claims must be dismissed against Maginn and Chai because they seek declaratory judgments with respect to a contract to which Maginn and Chai are not parties, and concern conduct which Maginn and Chai are not alleged to have undertaken.

In particular, in Count 9 MCG alleges that "[a]n actual and justiciable controversy has arisen and now exists between MCG and Defendants with respect to 5.12(h) of the PSWPA," which relates to the Compensation Committee's approval of Maginn and Chai's salary and bonus. *See* Compl. ¶ 128. Maginn and Chai are not parties to the PSWPA and as discussed above they played no role in approving their own compensation in supposed breach of the PSWPA. The controversy that is the subject of Count 9 is between Jenzabar and MCG, not Maginn and Chai and MCG.

In Count 10 MCG alleges that "[a]n actual and justiciable controversy has arisen and now exists between MCG and Defendants with respect to Article V, Section A.1.(b)(x) of the Jenzabar Charter," concerning approval of Affiliate transactions. *See* Compl. ¶ 132. Again, as

discussed above, Maginn and Chai are not parties to the contract between Jenzabar and MCG found in the Charter, and they are not accused of the conduct – approving their compensation – that is the subject of this controversy. This controversy is between Jenzabar and MCG, not Maginn and Chai and MCG.

Finally, in Count 11 MCG alleges that "[a]n actual and justiciable controversy has arisen and now exists between MCG and Defendants with respect to Article V, Sections A.4 and A.5 of the Jenzabar Charter," concerning the procedures for Jenzabar's repurchase of preferred stock held by MCG. *See* Compl. ¶ 137. But once more Maginn and Chai are not parties to the Charter, and there are no allegations in the Complaint that Maginn and Chai in their personal capacities have anything to do with Jenzabar's repurchase of preferred shares from MCG. Once again, this controversy is only between Jenzabar and MCG.

In summary, Maginn and Chai are not parties to the PSWPA or the Charter, they are not accused of undertaking the conduct that allegedly breached those contracts (Counts 1 and 2), and they are not parties to the controversies with respect to which MCG seeks declaratory relief (Counts 9, 10, and 11). Counts 1, 2, 9, 10, and 11 therefore must be dismissed as against Maginn and Chai for failure to state a claim.

II. <u>Counts 7, 8, and 12 Present Remedies, Not Causes of Action</u>

In Counts 7, 8, and 12, MCG presents as "causes of action" what are actually two *remedies*: an accounting and rescission. As explained in the Jenzabar Opening Brief, counts consisting of claims for remedies must be dismissed. *See* Jenzabar Opening Brief at 43; *see generally Addy v. Piedmonte*, 2009 Del. Ch. LEXIS 38, at *79 (Del. Ch.) (holding that requests for equitable relief "are not claims in and of themselves, but types of remedies dependent on the viability and outcome of the underlying causes of action...."); *Rhodes v. Silkroad Equity, LLC*, 2007 Del. Ch. LEXIS 96, at *43 (Del. Ch.); *see also Empire Fin. Servs., Inc. v. Bank of N.Y.*,

2003 Del. Super. LEXIS 372, at *3 (Del. Super. Ct.) ("An accounting is a form of relief, not a cause of action.").

III. **<u>Counts 1, 2, 3, 4, 5 (in Part), 6, 7, 8, 9, 10, and 12 Must Be Dismissed Because MCG's Theory of Liability is Contradicted by the Operative Documents</u>**

The vast majority of the counts listed in the Complaint – Counts 1, 2, 3, 4, 5 (in part), 6, 7, 8, 9, 10 and 12 – concern the decision by Jenzabar to increase the base salary and bonus compensation of Maginn and Chai, and to pay a previously authorized (but never paid) bonus to Maginn. Each of these counts must be dismissed against Maginn and Chai for one or more of the reasons discussed elsewhere in this brief, and also for the reasons given in the Jenzabar Opening Brief, which are incorporated herein.

Maginn and Chai write separately to emphasize two points.

As an initial matter, the fact that executives are paid more than a particular shareholder believes is justified is not sufficient to state a claim under Delaware law. Compensation decisions are firmly within the business judgment of the board. *Grimes v. Donald*, 673 A.2d 1207, 1215 (Del. 1996), *overruled in part on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000); *Nelson v. Emerson*, 2008 Del. Ch. LEXIS 56, at *48 (Del. Ch.) (claim that fails to cast "a legitimate shadow over the exercise of business judgment reflected in compensation decisions" must be dismissed) (*quoting Gagliardi v. TriFoods Int'l, Inc*., 683 A.2d 1049, 1051 (Del. Ch. 1996)). MCG's Complaint fails to allege that the compensation was not reasonable in return for the services that Maginn and Chai provided, and therefore must be dismissed. In determining whether compensation is excessive, a Court considers whether it was reasonable for a company to pay the particular individual in question the amount that it did. *See Grimes*, 673 A.2d at 1215 (observing that it is the essence of business judgment for a board to "determine[] that the services of a particular individual warrant large amounts of money, whether in the form

of current salary or severance provisions"); *Nelson*, 2008 Del. Ch. LEXIS 56, at *48 (dismissing complaint where allegations contain no support for an inference that compensation exceeded what was "rational and proper"); *see also Meiselman v. Eberstadt*, 170 A.2d 720 (Del. Ch. 1961) (compensation should be considered in light of the responsibilities involved and the duties performed by the executives in question). The Complaint contains no allegations that would support any inference that Maginn and Chai's compensation is unreasonable.

Moreover, the Compensation Committee of the Board's approval of their increased base salaries and bonuses is not a breach of either the PSWPA or the Charter. There are at least three independently sufficient reasons for this. First, as explained above, the existing Employment Agreements between Jenzabar and Maginn and Chai – which were approved by MCG as part of the PSWPA – both explicitly vest authority in the Board to increase Maginn and Chai's base salary and bonuses. *See supra* at 6, 7. MCG's repeated allegations that the Employment Agreements somehow limit the compensation that can be paid to Maginn and Chai, Compl. at 2 & ¶¶ 25-26, 47-48, 111, 119, 121-22, is directly contrary to this explicitly open-ended authority expressly provided to the Board.

Second, the Employment Agreements are not "affiliate" transactions with respect to which MCG has any special voting rights under the PSWPA or Charter. In fact, the PSWPA explicitly acknowledges the existence of Maginn's Employment Agreement as a "Material Contract," *see* PSWPA § 3.10 and schedule 3.10, **and** states, in a provision entitled "Transactions with Affiliates," that "No affiliate of the Company and no officer or director of the Company … is a party to any material Contract or transaction with the Company." PSWPA (Compl. Exh. 2), § 3.24. In other words, Maginn's material Employment Agreement is *not* an affiliated-party transaction within the meaning of the PSWPA. This is clear evidence in the

PSWPA itself that the PSWPA's grant of special voting rights to MCG with respect to affiliate transactions, and the Charter's substantively identical grant, do not apply to Jenzabar's payment of compensation to its officers.

Third, even if the Employment Agreements were "affiliate" transactions, the Compensation Committee of the Board's decision to pay increased base salaries and bonuses to Maginn and Chai did not trigger MCG's special voting rights because it did not require the Company to "enter into … any transaction, contract, agreement or arrangement with a shareholder, officer, or director of the Corporation," Charter (Compl. Exh. 1), art. V, § 1.A.1(b)(x) (emphasis added); PSWPA (Compl. Exh. 2), § 5.12(h) (same). The relevant "agreements" under which the increased compensation was paid – the Employment Agreements – have existed since June 30, 2004, and the Compensation Committee was merely exercising its authority under those existing agreements.

IV. Counts 3 and 4 Must Be Dismissed Because There Is No Aiding and Abetting a Breach of Contract or Charter

Counts 3 and 4 of the Complaint accuse Maginn and Chai of "aiding and abetting" San Miguel and Mills to "breach" the PSWPA and Charter by "encourag[ing]" them to increase Maginn and Chai's salaries and bonuses. In other words, MCG seeks to hold Maginn and Chai personally liable because they asked for a raise and the Compensation Committee said yes.

This baseless cause of action fails for all the reasons given elsewhere in this brief and in the Jenzabar Opening Brief. Among others, as explained in the Jenzabar Opening Brief there is no cause of action for aiding and abetting a breach of contract. *See* Jenzabar Opening Br. at 35-36. Only the actual party to a contract may breach it, and historically the law has only held third parties liable for the breach under rare circumstances, requiring proof of *tortious* interference with the contract. In that regard, MCG does not attempt to plead tortious interference, its

Complaint contains no allegations that would support such a theory against Maginn and Chai, and no such allegations could be pled in any event.

Moreover, as noted Maginn's and Chai's Employment Agreements expressly require Jenzabar to consider whether to increase Maginn and Chai's base salaries and bonuses. *See supra* at 6, 7. Thus, Counts 3 and 4 ask the Court to hold Maginn and Chai liable for "encouraging" Jenzabar to do something that Jenzabar is explicitly required to do under the terms of the Employment Agreements, agreements that have been in place since June 2004 and that were explicitly referenced in the PSWPA between Jenzabar and MCG and approved by MCG.

V. Count 6 Must Be Dismissed For Failure to State a Claim of Unjust Enrichment

Unjust enrichment is "the unjust retention of a benefit to the loss of another, or the retention of money or property of another against the fundamental principles of justice or equity and good conscience." *Fleer Corp. v. Topps Chewing Gum, Inc.*, 539 A.2d 1060, 1062 (Del. 1988) (quotation marks and citation omitted). The elements of unjust enrichment are (i) an enrichment, (ii) an impoverishment, (iii) a relation between the enrichment and impoverishment, (iv) the absence of justification, and (v) the absence of a remedy provided by law. *Cantor Fitzgerald, L.P. v. Cantor*, 724 A.2d 571, 585 (Del. Ch. 1998). Further, to obtain restitution in relation to alleged unjust enrichment, a plaintiff is "required to show that the defendants were unjustly enriched, that the defendants secured a benefit, and that it would be unconscionable to allow them to retain that benefit." *Schock v. Nash*, 732 A.2d 217, 232 (Del. 1999) (citation omitted).

Here, MCG's claim for unjust enrichment fails on two independent and legally sufficient grounds. First, as a matter of law, a claim for unjust enrichment cannot stand where, as here, express, enforceable contracts, *i.e.*, the Employment Agreements, control the relationship

between Maginn and Chai and the Company. Second, the unjust enrichment claim is deficiently plead in that the Complaint fails to establish, or even allege, that the salary and bonus payments allotted to Maginn and Chai exceeded the value of the services rendered as CEO and President and COO, respectively.

A. An Express Contract Defeats a Claim for Unjust Enrichment

Courts developed unjust enrichment as a theory of recovery to remedy the absence of a formal contract. *Bakerman v. Sidney Frank Importing Co., Inc.*, 2006 Del. Ch. LEXIS 180, at *66 (Del. Ch.) (granting motion to dismiss claim of unjust enrichment) (citations omitted). Therefore, it is well-settled that unjust enrichment claims will be dismissed whenever the Court determines that an express contract controls the dispute at issue:

> Therefore, claims of unjust enrichment may survive a motion to dismiss when the validity of the contract is in doubt or uncertain. When the complaint alleges an express, enforceable contract that controls the parties' relationship, however, a claim for unjust enrichment will be dismissed. This is the case even when the enforceable contract gives rise to a fiduciary relationship between the parties.

Id. (citations omitted); *see also Rossdeutscher v. Viacom, Inc*., 768 A.2d 8, 23-24 (Del. 2001) ("Courts generally dismiss claims for *quantum meruit* on the pleadings . . . when it is clear from the face of the complaint that there exists an express contract that clearly controls") (quotation marks and citations omitted); *ID Biomedical Corp. v. TM Techs*., 1995 Del. Ch. LEXIS 34, at *39 (Del. Ch.) ("A party cannot seek recovery under an unjust enrichment theory if a contract is the measure of [the] plaintiff's right") (quotation marks and citations omitted); *CIT Commc'ns Fin., Corp. v. Level 3 Commc'ns, LLC*, 2008 Del. Super. LEXIS 225, at *14 (Del. Super. Ct.) ("The existence of an express contract governing the relationship of the parties precludes a claim of unjust enrichment arising from the same relationship") (citation omitted).

Here, Jenzabar's existing Employment Agreements with Maginn and Chai, which were

approved by MCG at the time of its investment in Jenzabar, explicitly provide the Board with discretion and authority to increase their salaries or bonuses. The Employment Agreements provide for base salaries of *not less than* $400,000 and $340,000 to be paid to Maginn and Chai, respectively. (*See* Grivner Aff., Exhs. A & B, § 5). As set forth above, *see supra* at 6, 7, the Employment Agreements explicitly require the Board to consider increasing Maginn and Chai's base salaries and bonuses, and provide explicit authority to the Board to approve such increases. Thus, the Board's decision to increase Maginn's and Chai's salaries, and to pay bonuses to them, was made pursuant to and within the express authority delegated to it by an existing contract. Because the contract governs the relationship between Maginn, Chai, Jenzabar and MCG, the claims for unjust enrichment should be dismissed.

B. MCG Fails To Plead Or Establish Enrichment Or Impoverishment

MCG repeatedly makes the conclusory allegation that the salary and bonus payments made to Maginn and Chai were "not authorized" (Compl. ¶¶ 33, 144), were "above what was permitted" (*id.* ¶ 121), were "unlawful" (*id.* ¶¶ 49, 85, 97, 102, 113, 116) and were "invalid" (*id.* ¶¶ 91, 95). MCG does not, however, plead or allege that the bonus and salary payments exceeded the actual value of the services rendered by Maginn and Chai and key officers of the Company. Nor do the Employment Agreements contain any limit on what salary or bonus increases "were permitted."

Beyond a passing reference to the payments being "unwarranted and unlawful," (Compl. ¶ 49), the Complaint fails entirely to plead that the compensation to Maginn and Chai exceeded the value of their service and performance. Accordingly, as the Complaint fails to plead or present any predicate for concluding that the payments constituted an enrichment to Maginn or Chai or an impoverishment to Jenzabar, the claim for unjust enrichment must fail as a matter of law. *See Triton Constr. Co. v. E. Shore Elec. Servs.*, 2009 Del. Ch. LEXIS 88, at *83 (Del. Ch.)

(holding that where a former employee's "salary and benefits constituted fair compensation" for his efforts, the former employer "has not proved that it is entitled to relief based on a claim of unjust enrichment"). Indeed, Jenzabar would be unjustly enriched if Maginn and Chai were required to forfeit "compensation for services they legitimately performed during their administration." *Technicorp Int'l II, Inc. v. Johnston*, 2000 Del. Ch. LEXIS 81, at *196 and *199 (Del. Ch.) (generally recognizing "an entitlement to reasonable compensation," lest the entity "be unjustly enriched at the defendants' expense"), *aff'd*, 720 A.2d 542 (Del. 1998).

VI. Count 5 Does Not State Any Breaches of Fiduciary Duty Against Maginn or Chai

In Count 5, MCG alleges that Maginn, Chai and the other individual defendants breached fiduciary duties owed to the company in a laundry list of ways. Again, Maginn and Chai incorporate by reference the arguments why Count 5 must be dismissed made in the Jenzabar Opening Brief, and write separately to provide some additional reasons why the count should be dismissed as against them.

First, MCG's Complaint fails to tie its laundry list of accusations in Count 5 to Maginn and Chai. Two of those allegations – both of which relate to "approving bonus payments and salary increases to Defendants Maginn and Chai," *see* Compl. ¶ 108 – cannot be breaches of fiduciary duty by Maginn and Chai for all the reasons given above, *see supra* at 10-12, 13-16, starting with the fact that it is nowhere alleged that Maginn and Chai approved their own bonuses and salaries. To the contrary, MCG alleges specifically that the Compensation Committee, on which Maginn and Chai do not sit, approved the salaries and bonuses. *See supra* at 7-8.

MCG next complains about Defendants' supposed failure to "keep Board members properly informed with timely information"; "failing to provide adequate notice of the agendas of Board meetings"; "failing to circulate minutes of the Board meetings in time for meaningful comment"; and "failing to incorporate Malekian's comments, changes, and additions to the

Board minutes." Compl., ¶ 108. Maginn and Chai incorporate by reference the arguments made in the Jenzabar Opening Brief concerning MCG's lack of standing with respect to these allegations. Even if MCG had standing – and it does not – MCG has utterly failed to allege any harm to itself from these alleged procedural defects. When did the alleged failure to "keep Board members properly informed with timely information" cause any damage to Jenzabar or MCG? When did the alleged "failing to provide adequate notice of the agendas of Board meetings" cause harm? Have the shareholders been harmed by the alleged failure to circulate minutes of Board meetings quickly enough, or the alleged failure to adopt all of Malekian's proposed revisions? There is simply no precedent for permitting a shareholder such as MCG to bring suit alleging breach of fiduciary duty based on its dissatisfaction with the alleged inefficiency of the Board's internal procedures, particularly where the shareholder fails to allege any direct harm to the corporation or shareholder that thereby resulted.

Finally, MCG asserts that Maginn, Chai, and the other individual defendants breached their fiduciary duties by "asserting to MCG that it must give its Warrant Put Notice by April 29, 2009 or lose its special voting rights." Maginn and Chai incorporate by reference the arguments in favor of dismissing this piece of Count 5 made in the Jenzabar Opening Brief.

Additionally, to the extent that Count 5 alleges any breaches of fiduciary duty (*see* Compl. ¶ 108 (alleging generally that that the defendants "breach[ed] their duties of care, loyalty, and good faith")), any such claim must be dismissed, as Jenzabar's Fifth Amended and Restated Certificate of Incorporation contains a exculpatory provision authorized by 8 *Del. C.* § 102(b)(7) eliminating personal liability for directors for any breach of fiduciary duty "[t]o the fullest extent permitted by law." *See* 8 *Del. C.* § 102(b)(7); Compl. Exh. 1, art. VIII ("To the fullest extent permitted by law, a director of the Corporation shall not be personally liable to the Corporation

or its stockholders for monetary damages for breach of fiduciary duty as a director."). As Article VIII of the Charter exculpates the directors from personal liability for any alleged breach of the duty of care, any claim alleging breach of the duty of care must be dismissed. *See, e.g., Am. Int'l Group, Inc. v. Greenberg*, 965 A.2d 763, 776 (Del. Ch. 2009) (holding that where plaintiffs "bring a breach of the duty of care claim seeking monetary damages" against directors, notwithstanding a § 102(b)(7) exculpatory provision, "[t]he due care claim cannot be a source of recovery . . . and must be dismissed"); *Hokanson v. Petty*, 2008 Del. Ch. LEXIS 182, at *15 (Del. Ch.) (holding that, in light of the company's § 102(b)(7) exculpatory provision, "a fiduciary duty claim in this case premised on a duty of care violation cannot be sustained," and therefore dismissing plaintiffs' duty of care claims); *In re Lear Corp. S'holder Litig.*, 967 A.2d 640, 648 (Del. Ch. 2008) ("[B]ecause the [company's] charter contains an exculpatory provision authorized by § 102(b)(7), the plaintiffs cannot sustain their complaint even by pleading facts supporting an inference of gross negligence; they must plead a non-exculpated claim.") (citations omitted); *McMillan v. Intercargo Corp.*, 768 A.2d 492, 501 (Del. Ch. 2000) (recognizing that the company's certificate of incorporation contains an exculpatory provision, and dismissing the plaintiffs' claims "to the extent that those claims are premised upon allegations that the defendant directors failed to meet the requisite standard of care").

CONCLUSION

WHEREFORE, for the reasons given herein and in the Jenzabar Opening Brief, Robert A. Maginn, Jr. and Ling Chai respectfully request that the Court grant their motion to dismiss.

POTTER ANDERSON & CORROON LLP

By: ___*/s/ Peter J. Walsh, Jr.*______________
Peter J. Walsh, Jr. (DSB. No. 2437)
Abigail M. Legrow (DSB No. 4673)
Daniel A. Mason (DSB No. 5206)
1313 N. Market Street
Hercules Plaza, 6th Floor
P.O. Box 951
Wilmington, Delaware 19899
(302) 984-6000

Attorneys for Defendants Robert A. Maginn, Jr. and Ling Chai

OF COUNSEL:

Stephen D. Poss
Kevin P. Martin
GOODWIN PROCTER LLP
Exchange Place
53 State Street
Boston, MA 02109
(617) 570-1000

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923399

CERTIFICATE OF SERVICE

I hereby certify that on July 2, 2009, a copy of the foregoing was served via *Lexis-Nexis File and Serve* on the following counsel:

David C. McBride, Esquire
Matin Lessner, Esquire
Emily Burton, Esquire
Young Conaway Stargatt & Taylor, LLP
The Brandywine Building
1000 West Street, 17th Floor
Wilmington, DE 19801

Catherine G. Dearlove, Esquire
Thomas A. Uebler, Esquire
RICHARDS, LAYTON & FINGER, P.A.
One Rodney Square
920 North King Street
Wilmington, DE 19801

___*/s/ Peter J. Walsh, Jr.*__________
Peter J. Walsh, Jr. (I.D. No. 2437)