

IN RE ORACLE CORP. DERIVATIVE LITIGATION

824 A.2d 917 (Del. Ch. 2003)

In this opinion, I address the motion of the special litigation committee ("SLC") of Oracle Corporation to terminate this action, "the Delaware Derivative Action," and other such actions pending in the name of Oracle against certain Oracle directors and officers. These actions allege that these Oracle directors engaged in insider trading while in possession of material, non-public information showing that Oracle would not meet the earnings guidance it gave to the market for the third quarter of Oracle's fiscal year 2001. The SLC bears the burden of persuasion on this motion and must convince me that there is no material issue of fact calling into doubt its independence. This requirement is set forth in *Zapata Corp. v. Maldonado* and its progeny.

The question of independence "turns on whether a director is, *for any substantial reason*, incapable of making a decision with only the best interests of the corporation in mind." That is, the independence test ultimately "focus[es] on impartiality and objectivity." In this case, the SLC has failed to demonstrate that no material factual question exists regarding its independence.

During discovery, it emerged that the two SLC members – both of whom are professors at Stanford University – are being asked to investigate fellow Oracle directors who have important ties to Stanford, too. Among the directors who are accused by the derivative plaintiffs of insider trading are: (1) another Stanford professor, who taught one of the SLC members when the SLC member was a Ph.D. candidate and who serves as a senior fellow and a steering committee member alongside that SLC member at the Stanford Institute for Economic Policy Research or "SIEPR"; (2) a Stanford alumnus who has directed millions of dollars of contributions to Stanford during recent years, serves as Chair of SIEPR's Advisory Board and has a conference center named for him at SIEPR's facility, and has contributed nearly \$600,000 to SIEPR and the Stanford Law School, both parts of Stanford with which one of the SLC members is closely affiliated; and (3) Oracle's CEO, who has made millions of dollars in donations to Stanford through a personal foundation and large donations indirectly through Oracle, and who was considering making donations of his \$100 million house and \$170 million for a scholarship program as late as August 2001, at around the same time period the SLC members were added to the Oracle board. Taken together, these and other facts cause me to harbor a reasonable doubt about the impartiality of the SLC.

It is no easy task to decide whether to accuse a fellow director of insider trading. For Oracle to compound that difficulty by requiring SLC members to consider accusing a fellow professor and two large benefactors of their university of conduct that is rightly considered a violation of criminal law was unnecessary and inconsistent with the concept of independence recognized by our law. The possibility that these extraneous considerations biased the inquiry of the SLC is too substantial for this court to ignore. I therefore deny the SLC's motion to terminate.

I. *Factual Background*

A. *Summary of the Plaintiffs' Allegations*

The Delaware Derivative Complaint centers on alleged insider trading by four members of Oracle's board of directors – Lawrence Ellison, Jeffrey Henley, Donald Lucas, and Michael Boskin (collectively, the "Trading Defendants"). Each of the Trading Defendants had a very different role at Oracle.

Ellison is Oracle's Chairman, Chief Executive Officer, and its largest stockholder, owning nearly twenty-five percent of Oracle's voting shares. By virtue of his ownership position, Ellison is one of the wealthiest men in America. By virtue of his managerial position, Ellison has regular access to a great deal of information about how Oracle is performing on a week-to-week basis.

Henley is Oracle's Chief Financial Officer, Executive Vice President, and a director of the corporation. Like Ellison, Henley has his finger on the pulse of Oracle's performance constantly.

Lucas is a director who chairs Oracle's Executive Committee and its Finance and Audit Committee [...] Boskin is a director, Chairman of the Compensation Committee, and a member of the Finance and Audit Committee. [...]

According to the plaintiffs, each of these Trading Defendants possessed material, non-public information demonstrating that Oracle would fail to meet the earnings and revenue guidance it had provided to the market in December 2000 [regarding Oracle's expected performance in the third quarter of Financial Year 2001 ("3Q FY 2001"), which ran from December 1, 2000 to February 28, 2001]. [...]

[The court describes the alleged negative information that was revealed to the Oracle management between December 2000 and February 2001]

During the time when these disturbing signals were allegedly being sent, the Trading Defendants engaged in the following trades:

- On January 3, 2001, Lucas sold 150,000 shares of Oracle common stock at \$30 per share, reaping proceeds of over \$4.6 million. These sales constituted 17% of Lucas's Oracle holdings.
- On January 4, 2001, Henley sold one million shares of Oracle stock at approximately \$32 per share, yielding over \$32.3 million. These sales represented 7% of Henley's Oracle holdings.
- On January 17, 2001, Boskin sold 150,000 shares of Oracle stock at over \$33 per share, generating in excess of \$5 million. These sales were 16% of Boskin's Oracle holdings.
- From January 22 to January 31, 2001, Ellison sold over 29 million shares at prices above \$30 per share, producing over \$894 million. Despite the huge proceeds generated by these sales, they constituted the sale of only 2% of Ellison's Oracle holdings.

Into early to mid-February, Oracle allegedly continued to assure the market that it would meet its December guidance. Then, on March 1, 2001, the company announced that rather than posting 12 cents per share in quarterly earnings and 25% license revenue growth as projected, the company's earnings for the quarter would be 10 cents per share and license revenue growth only 6%. The stock market reacted swiftly and negatively to this news, with Oracle's share price dropping as low as \$15.75 before closing at \$16.88—a 21% decline in one day. These prices were well below the above \$30 per share prices at which the Trading Defendants sold in January 2001. [...]

B. The Plaintiffs' Claims in the Delaware Derivative Action

The plaintiffs make two central claims in their amended complaint in the Delaware Derivative Action. First, the plaintiffs allege that the Trading Defendants breached their duty of loyalty by misappropriating inside information and using it as the basis for trading decisions. [...]

Second, as to the other defendants—who are the members of the Oracle board who did not trade — the plaintiffs allege a *Caremark* violation, in the sense that the board's indifference to the deviation between the company's December guidance and reality was so extreme as to constitute subjective bad faith.

C. The Various Litigations

Oracle's failure to meet its earnings and revenue guidance, and the sales by the Trading Defendants, inevitably generated a spate of lawsuits. [...]

D. The Formation of the Special Litigation Committee

On February 1, 2002, Oracle formed the SLC in order to investigate the Delaware Derivative Action and to determine whether Oracle should press the claims raised by the plaintiffs, settle the case, or terminate it. Soon after its formation, the SLC's charge was broadened to give it the same mandate as to all the pending derivative actions, wherever they were filed.

The SLC was granted full authority to decide these matters without the need for approval by the other members of the Oracle board.

E. The Members of the Special Litigation Committee

Two Oracle board members were named to the SLC. Both of them joined the Oracle board on October 15, 2001, more than a half a year after Oracle's 3Q FY 2001 closed. The SLC members also share something else: both are tenured professors at Stanford University.

Professor Hector Garcia-Molina is Chairman of the Computer Science Department at Stanford [...] Garcia-Molina's appointment at Stanford represented a homecoming of some sort, because he obtained both his undergraduate and graduate degrees from Stanford.

The other SLC member, Professor Joseph Grundfest, is the W.A. Franke Professor of Law and Business at Stanford University. He directs the University's well-known Directors' College and the Roberts Program in Law, Business, and Corporate Governance at the Stanford Law School. [...] Immediately before coming to Stanford, Grundfest served for five years as a Commissioner of the Securities and Exchange Commission. Like Garcia-Molina, Grundfest's appointment at Stanford was a homecoming, because he obtained his law degree and performed significant post-graduate work in economics at Stanford.

As will be discussed more specifically later, Grundfest also serves as a steering committee member and a senior fellow of the Stanford Institute for Economic Policy Research, and releases working papers under the "SIEPR" banner.

For their services, the SLC members were paid \$250 an hour, a rate below that which they could command for other activities, such as consulting or expert witness testimony. Nonetheless, during the course of their work, the SLC members became concerned that (arguably scandal-driven) developments in the evolving area of corporate governance as well as the decision in *Telxon v. Meyerson*, might render the amount of their compensation so high as to be an argument against their independence. Therefore, Garcia-Molina and Grundfest agreed to give up any SLC-related compensation if their compensation was deemed by this court to impair their impartiality.

F. The SLC Members Are Recruited to the Board

The SLC members were recruited to the board primarily by defendant Lucas, with help from defendant Boskin. The wooing of them began in the summer of 2001. Before deciding to join the Oracle board, Grundfest, in particular, did a good deal of due diligence. His review included reading publicly available information, among other things, the then-current complaint in the Federal Class Action.

Grundfest then met with defendants Ellison and Henley, among others, and asked them some questions about the Federal Class Action. The claims in the Federal Class Action are predicated on facts that are substantively identical to those on which the claims in the Delaware Derivative Action are based. Grundfest received answers that were consistent enough with what he called the "exogenous" information about the case to form sufficient confidence to at least join the Oracle board. Grundfest testified that this did not mean that he had concluded that the claims in the

Federal Class Action had no merit, only that Ellison's and Henley's explanations of their conduct were plausible. Grundfest did, however, conclude that these were reputable businessmen with whom he felt comfortable serving as a fellow director, and that Henley had given very impressive answers to difficult questions regarding the way Oracle conducted its financial reporting operations.¹¹

G. *The SLC's Advisors*

The most important advisors retained by the SLC were its counsel from Simpson Thacher & Bartlett LLP. Simpson Thacher had not performed material amounts of legal work for Oracle or any of the individual defendants before its engagement, and the plaintiffs have not challenged its independence.

National Economic Research Advisors ("NERA") was retained by the SLC to perform some analytical work. The plaintiffs have not challenged NERA's independence.

H. *The SLC's Investigation and Report*

The SLC's investigation was, by any objective measure, extensive. The SLC reviewed an enormous amount of paper and electronic records. SLC counsel interviewed seventy witnesses, some of them twice. SLC members participated in several key interviews, including the interviews of the Trading Defendants.

Importantly, the interviewees included all the senior members of Oracle's management most involved in its projection and monitoring of the company's financial performance, including its sales and revenue growth. These interviews combined with a special focus on the documents at the company bearing on these subjects, including e-mail communications.

The SLC also asked the plaintiffs in the various actions to identify witnesses the Committee should interview. The Federal Class Action plaintiffs identified ten such persons and the Committee interviewed all but one, who refused to cooperate. The Delaware Derivative Action plaintiffs and the other derivative plaintiffs declined to provide the SLC with any witness list or to meet with the SLC.

During the course of the investigation, the SLC met with its counsel thirty-five times for a total of eighty hours. In addition to that, the SLC members, particularly Professor Grundfest, devoted many more hours to the investigation.

In the end, the SLC produced an extremely lengthy Report totaling 1,110 pages (excluding appendices and exhibits) that concluded that Oracle should not pursue the plaintiffs' claims against the Trading Defendants or any of the other Oracle directors serving during the 3Q FY 2001.

[...]

¹¹ The plaintiffs claim that Grundfest prejudged the Trading Defendants' culpability in a manner equivalent to that of the Chairman of the HealthSouth special litigation committee, as discussed in the recent *Biondi v. Scrushy* decision. The two situations are not reasonably comparable. In *Biondi*, the HealthSouth SLC Chairman publicly announced his conclusion that the HealthSouth CEO, who was the target of the SLC's investigation, had not acted with the required *scienter*. He did so in a company press release in advance of the SLC's own investigation. Here, Grundfest simply made a judgment that Ellison and Henley had given a plausible accounting for themselves and were, in general, reputable businessmen with whom he was comfortable serving as a fellow director. I find credible Grundfest's contention that he took their statements for what they were, statements by persons with a self-interest in exculpation. That said, it would have been a better practice for the Report to have identified that Grundfest had inquired about the Federal Class Action in determining whether to join Oracle's board. Cf. Report at VII-1 ("The interviews commenced in April 2002 and were completed by early November 2002.").

II. *The SLC Moves to Terminate*

Consistent with its Report, the SLC moved to terminate this litigation. The plaintiffs were granted discovery focusing on three primary topics: the independence of the SLC, the good faith of its investigative efforts, and the reasonableness of the bases for its conclusion that the lawsuit should be terminated. Additionally, the plaintiffs received a large volume of documents comprising the materials that the SLC relied upon in preparing its Report.

III. *The Applicable Procedural Standard*

In order to prevail on its motion to terminate the Delaware Derivative Action, the SLC must persuade me that: (1) its members were independent; (2) that they acted in good faith; and (3) that they had reasonable bases for their recommendations. If the SLC meets that burden, I am free to grant its motion or may, in my discretion, undertake my own examination of whether Oracle should terminate and permit the suit to proceed if I, in my oxymoronic judicial “business judgment,” conclude that procession is in the best interests of the company. This two-step analysis comes, of course, from *Zapata*.

[...]

As I understand it, this standard requires me to determine whether, on the basis of the undisputed factual record, I am convinced that the SLC was independent, acted in good faith, and had a reasonable basis for its recommendation. If there is a material factual question about these issues causing doubt about any of these grounds, I read *Zapata* and its progeny as requiring a denial of the SLC's motion to terminate.²⁰

In this case, the plaintiffs principally challenge the SLC's independence and the reasonableness of its recommendation. For reasons I next explain, I need examine only the more difficult question, which relates to the SLC's independence.

IV. *Is the SLC Independent?* A. *The Facts Disclosed in the Report*

In its Report, the SLC took the position that its members were independent. In support of that position, the Report noted several factors including:

- the fact that neither Grundfest nor Garcia-Molina received compensation from Oracle other than as directors;
- the fact that neither Grundfest nor Garcia-Molina were on the Oracle board at the time of the alleged wrongdoing;
- the fact that both Grundfest and Garcia-Molina were willing to return their compensation as SLC members if necessary to preserve their status as independent;
- the absence of any other material ties between Oracle, the Trading Defendants, and any of the other defendants, on the one hand, and Grundfest and Garcia-Molina, on the other; and
- the absence of any material ties between Oracle, the Trading Defendants, and any of the other defendants, on the one hand, and the SLC's advisors, on the other.

Noticeably absent from the SLC Report was any disclosure of several significant ties between Oracle or the Trading Defendants and Stanford University, the university that employs both members of the SLC. In the Report, it was only disclosed that:

²⁰ [...] Importantly, the granting of the SLC's motion [...] does not mean that the court has made a determination that the claims the SLC wants dismissed would be subject to termination on a summary judgment motion, only that the court is satisfied that there is no material factual dispute that the SLC had a reasonable basis for its decision to seek termination.

- defendant Boskin was a Stanford professor;
- the SLC members were aware that Lucas had made certain donations to Stanford; and
- among the contributions was a donation of \$50,000 worth of stock that Lucas donated to Stanford Law School after Grundfest delivered a speech to a venture capital fund meeting in response to Lucas's request. It happens that Lucas's son is a partner in the fund and that approximately half the donation was allocated for use by Grundfest in his personal research.

B. *The "Stanford" Facts that Emerged During Discovery*

In view of the modesty of these disclosed ties, it was with some shock that a series of other ties among Stanford, Oracle, and the Trading Defendants emerged during discovery. Although the plaintiffs have embellished these ties considerably beyond what is reasonable, the plain facts are a striking departure from the picture presented in the Report.

Before discussing these facts, I begin with certain features of the record – as I read it – that are favorable to the SLC. Initially, I am satisfied that neither of the SLC members is compromised by a fear that support for the prosecution of this suit would endanger his ability to make a nice living. Both of the SLC members are distinguished in their fields and highly respected. Both have tenure, which could not have been stripped from them for making a determination that this lawsuit should proceed.

Nor have the plaintiffs developed evidence that either Grundfest or Garcia-Molina have fundraising responsibilities at Stanford. Although Garcia-Molina is a department chairman, the record is devoid of any indication that he is required to generate contributions. And even though Grundfest heads up Stanford's Directors' College, the plaintiffs have not argued that he has a fundraising role in that regard. For this reason, it is important to acknowledge up front that the SLC members occupy positions within the Stanford community different from that of the University's President, deans, and development professionals, all of whom, it can be reasonably assumed, are required to engage heavily in the pursuit of contributions to the University.

This is an important point of departure for discussing the multitude of ties that have emerged among the Trading Defendants, Oracle, and Stanford during discovery in this case. In evaluating these ties, the court is not faced with the relatively easier call of considering whether these ties would call into question the impartiality of an SLC member who was a key fundraiser at Stanford²¹ or who was an untenured faculty member subject to removal without cause. Instead, one must acknowledge that the question is whether the ties I am about to identify would be of a material concern to two distinguished, tenured faculty members whose current jobs would not be threatened by whatever good faith decision they made as SLC members.

With this question in mind, I begin to discuss the specific ties that allegedly compromise the SLC's independence, beginning with those involving Professor Boskin.

1. *Boskin*

Defendant Michael J. Boskin is the T.M. Friedman Professor of Economics at Stanford University.

²¹ Compare *In re The Limited, Inc. S'holders Litig.* (concluding that a university president who had solicited a \$25 million contribution from a corporation's President, Chairman, and CEO was not independent of that corporate official in light of the sense of "owingness" that the university president might harbor with respect to the corporate official), and *Lewis v. Fuqua* (finding that a special litigation committee member was not independent where the committee member was also the president of a university that received a \$10 million charitable pledge from the corporation's CEO and the CEO was a trustee of the university), with *In re Walt Disney Co. Derivative Litig.* (deciding that the plaintiffs had not created reasonable doubt as to a director's independence where a corporation's Chairman and CEO had given over \$1 million in donations to the university at which the director was the university president and from which one of the CEO's sons had graduated).

During the Administration of President George H.W. Bush, Boskin occupied the coveted and important position of Chairman of the President's Council of Economic Advisors. He returned to Stanford after this government service, continuing a teaching career there that had begun many years earlier.

During the 1970s, Boskin taught Grundfest when Grundfest was a Ph.D. candidate. Although Boskin was not Grundfest's advisor and although they do not socialize, the two have remained in contact over the years, speaking occasionally about matters of public policy.

Furthermore, both Boskin and Grundfest are senior fellows and steering committee members at the Stanford Institute for Economic Policy Research, which was previously defined as "SIEPR." According to the SLC, the title of senior fellow is largely an honorary one. According to SIEPR's own web site, however, "[s]enior fellows actively participate in SIEPR research and participate in its governance."

Likewise, the SLC contends that Grundfest went MIA as a steering committee member, having failed to attend a meeting since 1997. The SIEPR web site, however, identifies its steering committee as having the role of "advising the director [of SIEPR] and guiding [SIEPR] on matters pertaining to research and academics." Because Grundfest allegedly did not attend to these duties, his service alongside Boskin in that capacity is, the SLC contends, not relevant to his independence.

That said, the SLC does not deny that both Boskin and Grundfest publish working papers under the SIEPR rubric and that SIEPR helps to publicize their respective works. Indeed, as I will note later in this opinion, Grundfest, in the same month the SLC was formed, addressed a meeting of some of SIEPR's largest benefactors-the so-called "SIEPR Associates." The SLC just claims that the SIEPR affiliation is one in which SIEPR basks in the glow of Boskin and Grundfest, not the other way around, and that the mutual service of the two as senior fellows and steering committee members is not a collegial tie of any significance.

With these facts in mind, I now set forth the ties that defendant Lucas has to Stanford.

2. Lucas

[...] Lucas's ties with Stanford are far, far richer than the SLC Report lets on. To begin, Lucas is a Stanford alumnus, having obtained both his undergraduate and graduate degrees there. By any measure, he has been a very loyal alumnus.

[The court describes significant donations made by Lucas and an affiliated family foundation]

From these undisputed facts, it is inarguable that Lucas is a very important alumnus of Stanford and a generous contributor to not one, but two, parts of Stanford important to Grundfest: the Law School and SIEPR.

With these facts in mind, it remains to enrich the factual stew further, by considering defendant Ellison's ties to Stanford.

3. Ellison

There can be little doubt that Ellison is a major figure in the community in which Stanford is located. The so-called Silicon Valley has generated many success stories, among the greatest of which is that of Oracle and its leader, Ellison. One of the wealthiest men in America, Ellison is a major figure in the nation's increasingly important information technology industry. Given his

wealth, Ellison is also in a position to make - and, in fact, he has made – major charitable contributions.

[The court describes significant donations made by Ellison and Oracle to Stanford (or under Stanford's control)]

Taken together, these facts suggest that Ellison (when considered as an individual and as the key executive and major stockholder of Oracle) had, at the very least, been involved in several endeavors of value to Stanford.

[...]

In order to buttress the argument that Stanford did not feel beholden to him, Ellison shared with the court the (otherwise private) fact that one of his children had applied to Stanford in October 2000 and was not admitted. If Stanford felt comfortable rejecting Ellison's child, the SLC contends, why should the SLC members hesitate before recommending that Oracle press insider trading-based fiduciary duty claims against Ellison?

But the fact remains that Ellison was still talking very publicly and seriously about the possibility of endowing a graduate interdisciplinary studies program at Stanford during the summer *after* his child was rejected from Stanford's undergraduate program.

C. *The SLC's Argument*

The SLC contends that even together, these facts regarding the ties among Oracle, the Trading Defendants, Stanford, and the SLC members do not impair the SLC's independence. In so arguing, the SLC places great weight on the fact that none of the Trading Defendants have the practical ability to deprive either Grundfest or Garcia-Molina of their current positions at Stanford. Nor, given their tenure, does Stanford itself have any practical ability to punish them for taking action adverse to Boskin, Lucas, or Ellison – each of whom, as we have seen, has contributed (in one way or another) great value to Stanford as an institution. As important, neither Garcia-Molina nor Grundfest are part of the official fundraising apparatus at Stanford; thus, it is not their on-the-job duty to be solicitous of contributors, and fundraising success does not factor into their treatment as professors.

In so arguing, the SLC focuses on the language of previous opinions of this court and the Delaware Supreme Court that indicates that a director is not independent only if he is dominated and controlled by an interested party, such as a Trading Defendant. The SLC also emphasizes that much of our jurisprudence on independence focuses on economically consequential relationships between the allegedly interested party and the directors who allegedly cannot act independently of that director. Put another way, much of our law focuses the bias inquiry on whether there are economically material ties between the interested party and the director whose impartiality is questioned, treating the possible effect on one's personal wealth as the key to the independence inquiry. Putting a point on this, the SLC cites certain decisions of Delaware courts concluding that directors who are personal friends of an interested party were not, by virtue of those personal ties, to be labeled non-independent.⁴⁴

More subtly, the SLC argues that university professors simply are not inhibited types, unwilling to

⁴⁴ See, e.g., *Crescent/Mach I Partners, L.P. v. Turner* (stating that an allegation of a fifteen-year professional and personal relationship between a CEO and a director does not, in itself, raise a reasonable doubt about the director's independence); *In re Walt Disney Co. Derivative Litig.* ("Demand is not excused, however, just because directors would have to sue 'their family, friends and business associates.' " (quoting *Abrams v. Koether*)).

make tough decisions even as to fellow professors and large contributors. What is tenure about if not to provide professors with intellectual freedom, even in non-traditional roles such as special litigation committee members? No less ardently – but with no record evidence that reliably supports its ultimate point – the SLC contends that Garcia-Molina and Grundfest are extremely distinguished in their fields and were not, in fact, influenced by the facts identified heretofore. Indeed, the SLC argues, how could they have been influenced by many of these facts when they did not learn them until the post-Report discovery process? If it boils down to the simple fact that both share with Boskin the status of a Stanford professor, how material can this be when there are 1,700 others who also occupy the same position?

[...]

E. *The Court's Analysis of the SLC's Independence*

[...] According to the SLC, its members are independent unless they are essentially subservient to the Trading Defendants-*i.e.*, they are under the “domination and control” of the interested parties. If the SLC is correct and this is the central inquiry in the independence determination, they would win. Nothing in the record suggests to me that either Garcia-Molina or Grundfest are dominated and controlled by any of the Trading Defendants, by Oracle, or even by Stanford.⁴⁶

But, in my view, an emphasis on “domination and control” would serve only to fetishize much-parroted language, at the cost of denuding the independence inquiry of its intellectual integrity. Take an easy example. Imagine if two brothers were on a corporate board, each successful in different businesses and not dependent in any way on the other's beneficence in order to be wealthy. The brothers are brothers, they stay in touch and consider each other family, but each is opinionated and strong-willed. A derivative action is filed targeting a transaction involving one of the brothers. The other brother is put on a special litigation committee to investigate the case. If the test is domination and control, then one brother could investigate the other. Does any sensible person think that is our law? I do not think it is.

And it should not be our law. Delaware law should not be based on a reductionist view of human nature that simplifies human motivations on the lines of the least sophisticated notions of the law and economics movement. *Homo sapiens* is not merely *homo economicus*. We may be thankful that an array of other motivations exist that influence human behavior; not all are any better than greed or avarice, think of envy, to name just one. But also think of motives like love, friendship, and collegiality, think of those among us who direct their behavior as best they can on a guiding creed or set of moral values.

Nor should our law ignore the social nature of humans. To be direct, corporate directors are generally the sort of people deeply enmeshed in social institutions. Such institutions have norms, expectations that, explicitly and implicitly, influence and channel the behavior of those who participate in their operation. Some things are “just not done,” or only at a cost, which might not be so severe as a loss of position, but may involve a loss of standing in the institution. In being appropriately sensitive to this factor, our law also cannot assume – absent some proof of the point – that corporate directors are, as a general matter, persons of unusual social bravery, who operate heedless to the inhibitions that social norms generate for ordinary folk.

For all these reasons, this court has previously held that the Delaware Supreme Court's teachings

⁴⁶ This is not to say that the facts could not be simply read as providing a basis for a professor interested in promotion within the University to be less than aggressive as an SLC member. Even tenured professors and department chairs sometimes seek different chairs, duties, or even to climb to positions like Provost, which chart the path towards a university presidency. I do not consider this factor to be of weight here, however, but note it.

on independence can be summarized thusly:

At bottom, the question of independence turns on whether a director is, *for any substantial reason*, incapable of making a decision with only the best interests of the corporation in mind. That is, the Supreme Court cases ultimately focus on impartiality and objectivity.

[...]

In examining whether the SLC has met its burden to demonstrate that there is no material dispute of fact regarding its independence, the court must bear in mind the function of special litigation committees under our jurisprudence. Under Delaware law, the primary means by which corporate defendants may obtain a dismissal of a derivative suit is by showing that the plaintiffs have not met their pleading burden under the test of *Aronson v. Lewis*, or the related standard set forth in *Rales v. Blasband*. In simple terms, these tests permit a corporation to terminate a derivative suit if its board is comprised of directors who can impartially consider a demand.

Special litigation committees are permitted as a last chance for a corporation to control a derivative claim in circumstances when a majority of its directors cannot impartially consider a demand. By vesting the power of the board to determine what to do with the suit in a committee of independent directors, a corporation may retain control over whether the suit will proceed, so long as the committee meets the standard set forth in *Zapata*.

In evaluating the independence of a special litigation committee, this court must take into account the extraordinary importance and difficulty of such a committee's responsibility. It is, I daresay, easier to say no to a friend, relative, colleague, or boss who seeks assent for an act (*e.g.*, a transaction) that has not yet occurred than it would be to cause a corporation to sue that person. [...] Denying a fellow director the ability to proceed on a matter important to him may not be easy, but it must, as a general matter, be less difficult than finding that there is reason to believe that the fellow director has committed serious wrongdoing and that a derivative suit should proceed against him.

The difficulty of making this decision is compounded in the special litigation committee context because the weight of making the moral judgment necessarily falls on less than the full board. A small number of directors feels the moral gravity – and social pressures – of this duty alone.

For all these reasons, the independence inquiry is critically important if the special litigation committee process is to retain its integrity, a quality that is, in turn, essential to the utility of that process. [...]

The importance and special sensitivity of the SLC's task is also relevant for another obvious reason: investigations do not follow a scientific process like an old-fashioned assembly line. The investigators' mindset and talent influence, for good or ill, the course of an investigation. Just as there are obvious dangers from investigators suffering from too much zeal, so too are dangers posed by investigators who harbor reasons not to pursue the investigation's targets with full vigor.

[...]

2. *The SLC Has Not Met Its Burden to Demonstrate the Absence of a Material Dispute of Fact About Its Independence*

[...] I conclude that the SLC has not met its burden to show the absence of a material factual question about its independence. I find this to be the case because the ties among the SLC, the Trading Defendants, and Stanford are so substantial that they cause reasonable doubt about the SLC's ability to impartially consider whether the Trading Defendants should face suit. The concern that arises from these ties can be stated fairly simply, focusing on defendants Boskin, Lucas, and

Ellison in that order, and then collectively.

As SLC members, Grundfest and Garcia-Molina were already being asked to consider whether the company should level extremely serious accusations of wrongdoing against fellow board members. As to Boskin, both SLC members faced another layer of complexity: the determination of whether to have Oracle press insider trading claims against a fellow professor at their university. Even though Boskin was in a different academic department from either SLC member, it is reasonable to assume that the fact that Boskin was also on faculty would – to persons possessing typical sensibilities and institutional loyalty – be a matter of more than trivial concern. Universities are obviously places of at-times intense debate, but they also see themselves as communities. In fact, Stanford refers to itself as a “community of scholars.” To accuse a fellow professor – whom one might see at the faculty club or at inter-disciplinary presentations of academic papers – of insider trading cannot be a small thing – even for the most callous of academics.

As to Boskin, Grundfest faced an even more complex challenge than Garcia-Molina. Boskin was a professor who had taught him and with whom he had maintained contact over the years. Their areas of academic interest intersected, putting Grundfest in contact if not directly with Boskin, then regularly with Boskin's colleagues. Moreover, although I am told by the SLC that the title of senior fellow at SIEPR is an honorary one, the fact remains that Grundfest willingly accepted it and was one of a select number of faculty who attained that status. And, they both just happened to also be steering committee members. Having these ties, Grundfest (I infer) would have more difficulty objectively determining whether Boskin engaged in improper insider trading than would a person who was not a fellow professor, had not been a student of Boskin, had not kept in touch with Boskin over the years, and who was not a senior fellow and steering committee member at SIEPR.

In so concluding, I necessarily draw on a general sense of human nature. It may be that Grundfest is a very special person who is capable of putting these kinds of things totally aside. But the SLC has not provided evidence that that is the case. In this respect, it is critical to note that I do not infer that Grundfest would be less likely to recommend suit against Boskin than someone without these ties. Human nature being what it is, it is entirely possible that Grundfest would in fact be tougher on Boskin than he would on someone with whom he did not have such connections. The inference I draw is subtly, but importantly, different. What I infer is that a person in Grundfest's position would find it difficult to assess Boskin's conduct without pondering his own association with Boskin and their mutual affiliations. Although these connections might produce bias in either a tougher or laxer direction, the key inference is that these connections would be on the mind of a person in Grundfest's position, putting him in the position of either causing serious legal action to be brought against a person with whom he shares several connections (an awkward thing) or not doing so (and risking being seen as having engaged in favoritism toward his old professor and SIEPR colleague).

The same concerns also exist as to Lucas. For Grundfest to vote to accuse Lucas of insider trading would require him to accuse SIEPR's Advisory Board Chair and major benefactor of serious wrongdoing-of conduct that violates federal securities laws. Such action would also require Grundfest to make charges against a man who recently donated \$50,000 to Stanford Law School after Grundfest made a speech at his request.⁶⁵

And, for both Grundfest and Garcia-Molina, service on the SLC demanded that they consider whether an extremely generous and influential Stanford alumnus should be sued by Oracle for insider trading. Although they were not responsible for fundraising, as sophisticated professors they undoubtedly are aware of how important large contributors are to Stanford, and they share in

⁶⁵ [...] Lucas has contributed \$149,000 to the Law School, \$424,000 to SIEPR, and millions more to other Stanford institutions.

the benefits that come from serving at a university with a rich endowment. A reasonable professor giving any thought to the matter would obviously consider the effect his decision might have on the University's relationship with Lucas, it being (one hopes) sensible to infer that a professor of reasonable collegiality and loyalty cares about the well-being of the institution he serves.

In so concluding, I give little weight to the SLC's argument that it was unaware of just how substantial Lucas's beneficence to Stanford has been. I do so for two key reasons. Initially, it undermines, rather than inspires, confidence that the SLC did not examine the Trading Defendants' ties to Stanford more closely in preparing its Report. The Report's failure to identify these ties is important because it is the SLC's burden to show independence. In forming the SLC, the Oracle board should have undertaken a thorough consideration of the facts bearing on the independence of the proposed SLC members from the key objects of the investigation.

The purported ignorance of the SLC members about all of Lucas's donations to Stanford is not helpful to them for another reason: there were too many visible manifestations of Lucas's status as a major contributor for me to conclude that Grundfest, at the very least, did not understand Lucas to be an extremely generous benefactor of Stanford. [...]

Garcia-Molina is in a somewhat better position to disclaim knowledge of how generous an alumnus Lucas had been. Even so, the scope of Lucas's activities and their easy discoverability gives me doubt that he did not know of the relative magnitude of Lucas's generosity to Stanford. Furthermore, Grundfest comprised half of the SLC and was its most active member. His non-independence is sufficient alone to require a denial of the SLC's motion.⁶⁹

[...]

In view of the ties involving Boskin and Lucas alone, I would conclude that the SLC has failed to meet its burden on the independence question. The tantalizing facts about Ellison merely reinforce this conclusion. The SLC, of course, argues that Ellison is not a large benefactor of Stanford personally, that Stanford has demonstrated its independence of him by rejecting his child for admission, and that, in any event, the SLC was ignorant of any negotiations between Ellison and Stanford about a large contribution. For these reasons, the SLC says, its ability to act independently of Ellison is clear.

I find differently. The notion that anyone in Palo Alto can accuse Ellison of insider trading without harboring some fear of social awkwardness seems a stretch. That being said, I do not mean to imply that the mere fact that Ellison is worth tens of billions of dollars and is the key force behind a very important social institution in Silicon Valley disqualifies all persons who live there from being independent of him. Rather, it is merely an acknowledgement of the simple fact that accusing such a significant person in that community of such serious wrongdoing is no small thing.

Given that general context, Ellison's relationship to Stanford itself contributes to my overall doubt, when heaped on top of the ties involving Boskin and Lucas. During the period when Grundfest and Garcia-Molina were being added to the Oracle board, Ellison was publicly considering making extremely large contributions to Stanford. [...]

Of course, the SLC says these facts are meaningless because Stanford rejected Ellison's child for

⁶⁹ See *In re Walt Disney Co. Derivative Litig.* (“[U]nder Aronson’s first prong—director independence—for demand to be futile, the Plaintiffs must show a reasonable doubt as to the disinterest of at least half of the directors.”); *Beneville v. York* (concluding that “[w]hen one member of a two-member board of directors cannot impartially consider a stockholder litigation demand” demand is excused); *In re The Limited, Inc. S’holders Litig.* (“[W]here the challenged actions are those of a board consisting of an even number of directors, plaintiffs meet their burden of demonstrating the futility of making demand on the board by showing that half of the board was either interested or not independent.”).

admission. I am not sure what to make of this fact, but it surely cannot bear the heavy weight the SLC gives it. The aftermath of denying Ellison's child admission might, after all, as likely manifest itself in a desire on the part of the Stanford community never to offend Ellison again, lest he permanently write off Stanford as a possible object of his charitable aims [...].

Taken in isolation, the facts about Ellison might well not be enough to compromise the SLC's independence. But that is not the relevant inquiry. The pertinent question is whether, given *all* the facts, the SLC has met its independence burden.

When viewed in that manner, the facts about Ellison buttress the conclusion that the SLC has not met its burden. Whether the SLC members had precise knowledge of all the facts that have emerged is not essential, what is important is that by any measure this was a social atmosphere painted in too much vivid Stanford Cardinal red for the SLC members to have reasonably ignored it. Summarized fairly, two Stanford professors were recruited to the Oracle board in summer 2001 and soon asked to investigate a fellow professor and two benefactors of the University. On Grundfest's part, the facts are more substantial, because his connections – through his personal experiences, SIEPR, and the Law School – to Boskin and to Lucas run deeper.

It seems to me that the connections outlined in this opinion would weigh on the mind of a reasonable special litigation committee member deciding whether to level the serious charge of insider trading against the Trading Defendants. As indicated before, this does not mean that the SLC would be less inclined to find such charges meritorious, only that the connections identified would be on the mind of the SLC members in a way that generates an unacceptable risk of bias. That is, these connections generate a reasonable doubt about the SLC's impartiality because they suggest that material considerations other than the best interests of Oracle could have influenced the SLC's inquiry and judgments.

[...]

Rather than form an SLC whose membership was free from bias-creating relationships, Oracle formed a committee fraught with them. As a result, the SLC has failed to meet its *Zapata* burden, and its motion to terminate must be denied. Because of this reality, I do not burden the reader with an examination of the other *Zapata* factors. In the absence of a finding that the SLC was independent, its subjective good faith and the reasonableness of its conclusions would not be sufficient to justify termination. Without confidence that the SLC was impartial, its findings do not provide the assurance our law requires for the dismissal of a derivative suit without a merits inquiry.

[...]