

IN THE SUPERIOR COURT OF FULTON COUNTY

STATE OF GEORGIA

CITY OF PONTIAC GENERAL
EMPLOYEES' RETIREMENT SYSTEM,
STEVEN STARK, NICHOLAS WEIL and
ARNOLD WANDEL, Derivatively on Behalf
of THE HOME DEPOT, INC.,

Plaintiffs,

vs.

KENNETH G. LANGONE, ROBERT L.
NARDELLI, CAROL B. TOMÉ, LABAN P.
JACKSON, JR., DENNIS M. DONOVAN,
FRANK L. FERNANDEZ, THOMAS V.
TAYLOR, JOHN L. CLENDENIN,
CLAUDIO X. GONZÁLEZ, BONNIE G.
HILL, GREGORY D. BRENNEMAN,
MILLEDGE A. HART, III, ANGELO R.
MOZILO, THOMAS J. RIDGE, LAWRENCE
R. JOHNSTON, BERRY R. COX, RICHARD
H. BROWN and RICHARD A. GRASSO,

Defendants,

- and -

THE HOME DEPOT, INC., a Delaware
corporation,

Nominal Defendant.

Civil Action No. 2006-cv-122302

PLAINTIFFS' MEMORANDUM OF LAW
IN SUPPORT OF MOTION FOR
PRELIMINARY APPROVAL OF
PROPOSED DERIVATIVE SETTLEMENT

NOW COME plaintiffs the City of Pontiac General Employees' Retirement System, Steven Stark, Nicholas Weil, and Arnold Wandel, and, pursuant to O.C.G.A. §14-2-745, respectfully submit their memorandum of law in support of the parties' Motion for Preliminary Approval of Proposed Derivative Settlement ("Motion for Preliminary Approval"). The terms of the proposed derivative settlement (the "Settlement") are enumerated in the Stipulation of Settlement (the "Stipulation"), which is attached as Exhibit 1 to the concurrently-filed Motion for Preliminary Approval. Plaintiffs submit that the proposed Settlement warrants notifying by publication shareholders of The Home Depot, Inc. ("Home Depot" or the "Company") of their rights in connection therewith.¹ A proposed order preliminarily approving the Settlement ("Preliminary Approval Order") is attached to the Stipulation as Exhibit B, and is submitted separately herewith for the Court's convenience.

I. INTRODUCTION

A. Procedural History and the Settlement

This case is a consolidated action of six separate shareholder derivative actions filed on behalf of individual shareholders of Home Depot in Fulton County Superior Court in mid-2006. The claims before the Court allege three related areas of wrongdoing: stock option backdating, improper payments to former CEO Robert Nardelli, and return-to-vendor ("RTV") accounting manipulations. Plaintiffs alleged that, as a result of these activities, defendants caused Home Depot to report false and misleading financial results in Home Depot's SEC filings and other documents distributed to shareholders. Joint Amended Complaint at ¶¶100-151.

On June 16, 2006, Home Depot issued a press release admitting that at least five option grants had been backdated. *Id.* ¶¶6, 74. Defendants attempted to downplay the extent of any wrongdoing, stating that the total financial impact of their conduct would be limited to \$10 million.

¹ A copy of the proposed notice (the "Notice") is attached to the Stipulation as Exhibit B-1.

Id. at ¶6. In December 2006, Home Depot acknowledged that defendants had mispriced options over a multi-year period. *Id.* Plaintiffs assert that the Company's prior financial reporting had been false and misleading because Home Depot had been accounting for stock options as if it had not been granting backdated options, which are treated differently under accounting rules than options with exercise prices equal to the stock price on the date of the grant. *Id.* at ¶7.

As noted above, plaintiffs further alleged that defendants caused Home Depot to engage in improper RTV chargeback practices, which, also contributed to the Company's release and filing of false financial results over a period of years. *Id.* at ¶¶78-90, 100-151.

The parties have engaged in substantial discovery. Defendants have produced, and counsel for plaintiffs have reviewed, tens of thousands of pages of documents. Plaintiffs have taken numerous depositions, including the depositions of five of the named defendants, including Robert Nardelli. Plaintiffs have also taken a Rule 30(b)(6) deposition of the Company. Plaintiffs and defendants have briefed and filed numerous motions to compel, including motions on complex issues such as metadata production. (Plaintiffs note that the Court appointed a Special Master to assist with discovery disputes and that the Special Master ably and professionally enabled the parties to resolve many of these disputes). Finally, the parties briefed several motions with the Court, including a motion for preliminary injunction by plaintiffs and multiple motions to dismiss by defendants.

Following all of this discovery, as well as the various motions and rulings by the Court, the parties entered into a lengthy and complicated series of settlement discussions. These discussions included multiple days of mediation conducted over the course of several months, numerous follow-up conference calls with the mediator, confirmatory discovery, and a multi-month, laborious drafting of mutually-agreeable settlement papers. Based on all of these efforts to date, the parties now respectfully request that this Court grant preliminary approval to the proposed Settlement, as set

forth in the Preliminary Approval Order. The parties also request that this Court set a hearing (the "Settlement Hearing") to consider final approval of the proposed Settlement. In connection therewith, the parties additionally request that this Court direct that notice of the proposed Settlement, in the form attached as Exhibit B-1 to the Stipulation, be disseminated via publication within five days of the entry of the Preliminary Approval Order and that Home Depot shareholders of record as of March 28, 2008 shall, in the event they have any objection to the Settlement, file with the Court for its consideration and deliver to counsel for plaintiffs and the Company a written notice of objection consistent with the manner and procedure set forth in the Notice.

B. The Settlement Confers Substantial Benefits Upon the Company

The Settlement confers substantial benefits upon the Company and its shareholders in the form of significant corporate governance enhancements. For instance, the Settlement requires that Home Depot, among other things, shall: (i) adopt multiple changes to the structure of the Board of Directors of Home Depot, (ii) require two-thirds of its directors to be independent, (iii) require the Audit, Nominating and Corporate Governance, and Leadership Development and Compensation Committees to consist entirely of independent directors, (iv) adopt director independence standards, (v) require certain directors to receive compensation in the form of equity grants, (vi) permit shareholders to ask questions at annual meetings, (vii) adopt certain compensation policies and procedural safeguards for officers and directors, (viii) implement voting standards for uncontested director elections that require director nominees to receive a majority of votes cast in order to be elected to the board; (ix) impose safeguards on the removal procedures for directors, (x) adopt safeguards and notice requirements on stock option plans to lower the risk of backdating, (xi) permit large shareholders or groups of shareholders to nominate directors, (xii) ensure compliance with the Company's Return to Vendor Policy, and (xiii) adopt a Best Value Contracting Policy. The

Stipulation also provides for an attorneys' fee – negotiated between the parties – of approximately \$8.5 million in Home Depot common stock and \$6 million in cash for fees and expenses.

II. ARGUMENT

A. The Discontinuance or Settlement of Derivative Claims Requires Court Approval

O.C.G.A. §14-2-745 provides that “[a] derivative proceeding may not be discontinued or settled without the court’s approval.” The *Manual for Complex Litigation* (3d ed. 1995) (“*Manual*”) suggests that approval of settlements in complex litigations, such as class actions and derivative actions, involve a two-step process. *Id.* at §30.41.² In the first step, “counsel submit the proposed terms of settlement and the court makes a preliminary fairness evaluation.” *Id.* at 236. As long as the initial evaluation of the proposed settlement “does not disclose grounds to doubt its fairness or other obvious deficiencies” and “appears to fall within the range of possible approval,” a court should then, as its second step, direct that notice pursuant to the rules be given to shareholders informing them that a formal hearing will be held at which time arguments and evidence may be presented in support and opposition to the settlement. *Id.* at 237; *see also* O.C.G.A. §14-2-745.

B. Preliminary Approval of the Settlement Is Proper and Notice of the Settlement Should Be Ordered

The settlement of litigation is favored; indeed, there is a strong policy favoring compromises which resolve litigation. *Williams v. First Nat’l Bank*, 216 U.S. 582 (1910); *see also Leary v. Julian*, 225 Ga. App. 472, 474, 484 S.E. 2d 75, 77 (1997) (settlement agreements are highly favored under Georgia law). This policy is especially true in derivative litigation, where settlements are

² Courts consider the same factors in analyzing a derivative settlement as those considered in analyzing a class action settlement since the same concerns are present in the class and derivative action contexts - protecting the interests of absent shareholders. *Treasurer of Conn. v. Ballard, Spahr, Andrews & Ingersoll LLP*, 866 A.2d 479 (Pa. Commw. 2005).

particularly favored because such litigation “is notoriously difficult and unpredictable.” *In re Xcel Energy, Inc. Sec., Derivative & “ERISA” Litig.*, 364 F. Supp. 2d 980, 1003 (D. Minn. 2005) (citation omitted); *Maher v. Zapata*, 714 F.2d 436, 455 (5th Cir. 1983).³ As a result of the complexity of such cases, as well as the corresponding burden on judicial resources, there is a strong public policy favoring the settlement of complex litigation. *Zapata*, 714 F.2d at 455; *see also Cotton v. Hinton*, 559 F.2d 1326, 1331 (5th Cir. 1977).

As noted above, the Court should make a preliminary fairness evaluation of the proposed Settlement. *Manual* at §30.41. During this preliminary fairness evaluation, the Court should examine only whether the Settlement is within the range of possible approval, or, in other words, whether there is probable cause to notify shareholders of the proposed Settlement. *Horton v. Merrill Lynch, Pierce, Fenner & Smith*, 855 F. Supp. 825, 827 (E.D.N.C. 1994); *Manual* at §30.41. Preliminary approval “is not tantamount to a finding that the settlement is fair and reasonable. It is at most a determination that there is what might be termed ‘probable cause’ to submit the proposal to class members and to hold a full-scale hearing as to the fairness.” *In re Traffic Executive Ass'n E.R.R.*, 627 F.2d 631, 634 (2d Cir. 1980).

As outlined above, and as demonstrated more fully in the Stipulation, plaintiffs submit that the proposed Settlement is an excellent result for Home Depot and its shareholders. Plaintiffs, by and through experienced counsel, have confirmed, through extensive discovery, that the proposed Settlement is fair, reasonable, and adequate. There is nothing in the record to suggest any grounds to

³ Because there are few definitive holdings by Georgia courts with respect to the matters here at issue, it is appropriate for the Court to look to relevant federal cases for guidance. *See, e.g., Dee v. Sweet*, 218 Ga. App. 18, 20, 460 S.E. 2d 110, 113 (1995); *S. R. Co. v. Malone Freight Lines, Inc.*, 174 Ga. App. 405, 408, 330 S.E. 2d 371, 376 (1985); *Sta-Power Indus., Inc. v. Avant*, 134 Ga. App. 952, 953, 216 S.E. 2d 897, 900 (1975) (“Since there are only a few definitive holdings in Georgia on [the class action] section of the Civil Practice Act, we also look to federal cases to aid us.”).

doubt the Settlement’s fairness. Thus, the Settlement falls well within the range of possible approval. Accordingly, the parties request that the Court preliminarily approve the Settlement and order that Notice be disseminated to shareholders consistent with the terms of the Stipulation, via publication in *Investor’s Business Daily*, in the form attached to the Stipulation as Exhibit B-1.

III. PROPOSED SCHEDULE OF EVENTS

In connection with preliminary approval of the Settlement, the parties request that the Court (1) establish dates by which notice of the Settlement will be published and by which holders of Home Depot stock may object to the Settlement, and (2) set the Settlement Hearing date. The following schedule is proposed:

Notice published (“Notice Date”)	no later than 5 business days after entry of the Preliminary Approval Order
Date by which papers in support of the Settlement are to be filed	21 calendar days prior to Settlement Hearing
Last day for Home Depot shareholders to object to the Settlement	14 calendar days prior to Settlement Hearing
Date by which any reply papers in support of the Settlement are to be filed	7 calendar days prior to Settlement Hearing
Settlement Hearing	approximately 55 to 60 days from entry of the Preliminary Approval Order, at Court’s convenience

This schedule is similar to those used in other derivative settlements and provides due process to current holders of Home Depot common stock with respect to their rights concerning the Settlement.

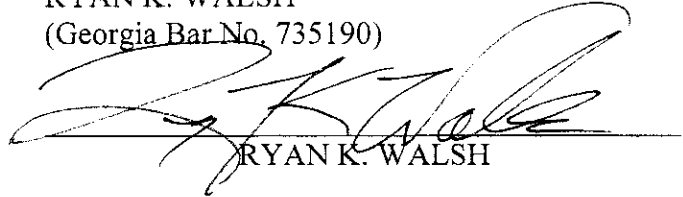
IV. CONCLUSION

In light of the foregoing, plaintiffs respectfully request that this Court grant the Motion for Preliminary Approval and enter the proposed Preliminary Approval Order, which is attached to the Stipulation as Exhibit B and is submitted separately herewith.

DATED: April ^{2nd}, 2008

Respectfully submitted,

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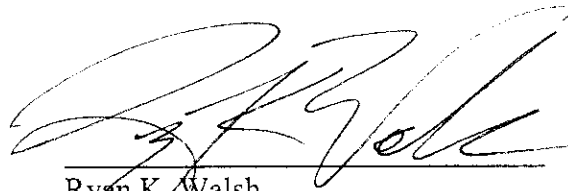
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CERTIFICATE OF SERVICE

This certifies that I have this day served a true and correct copy of the foregoing PLAINTIFFS' MEORANDUM OF LAW IN SUPPORT OF MOTION FOR PRELIMINARY APPROVAL OF PROPOSED DERIVATIVE SETTLEMENT upon all parties of record by electronic mail and United States mail, postage prepaid, addressed to counsel of record, as listed on the attached service list.

This 3rd day of April, 2008.

A handwritten signature in black ink, appearing to read 'Ryan K. Walsh', written over a horizontal line.

Ryan K. Walsh
(Georgia Bar No. 735190)

HOME DEPOT DERIVATIVE

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