IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

NATALIE GORDON, Derivatively on Behalf of NAVIGANT CONSULTING, INC.,	)	
Plaintiff,	)	Case No. 12-cv-00369
v.	)	Honorable Amy J. St. Eve
WILLIAM M. GOODYEAR, JULIE M. HOWARD, THOMAS A. NARDI, MONICA M. WEED, THOMAS A. GILDEHAUS, CYNTHIA A. GLASSMAN, STEPHAN A. JAMES, PETER B. POND, SAMUEL K. SKINNER, JAMES R. THOMPSON and MICHAEL L. TIPSORD,	)	
Defendants,	)	
and	)	
NAVIGANT CONSULTING, INC.,	)	
Nominal Defendant.	)	

DEFENDANTS' MEMORANDUM IN SUPPORT OF THEIR MOTION TO DISMISS

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INTRODUCTION

This case is one of a series of shareholder derivative lawsuits unsuccessfully advancing a novel legal theory—that the "say-on-pay" provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") somehow alters the legal protections afforded by the business judgment rule to compensation decisions by boards of directors. Dodd-Frank's "say-on-pay" provision requires companies to subject their executive compensation to an advisory shareholder vote on a periodic basis. As Plaintiff's theory goes, if a simple majority of a company's shareholders expresses displeasure with compensation that *already* has been awarded and paid to executives, the directors of that company can be presumed to have breached their fiduciary duties by earlier having authorized that compensation. This theory is directly contradicted by the plain language of Dodd-Frank, which expressly states that "say-on-pay" votes are *non-binding* and do *not* alter the fiduciary duties of directors. It is thus no surprise that numerous courts already have rejected Plaintiff's theory out of hand and dismissed similar shareholder derivative actions at the outset.

Plaintiff Natalie Gordon[1] purports to bring this derivative action on behalf of Navigant Consulting, Inc. ("Navigant" or the "Company") against its directors and officers because, on April 25, 2011, Navigant's shareholders narrowly voted to express their disapproval of the compensation paid to Navigant's Named Executive Officers (the "NEOs") for 2010, as disclosed in Navigant's March 16, 2011 proxy statement (the "Proxy") (Ex. B). The Complaint, however, does not come close to meeting the exacting pleading requirements for maintaining a derivative claim. Under Delaware law, the board of directors—not individual shareholders—manages the

[1] Ms. Gordon is no stranger to shareholder litigation. She appears to have brought at least 11 shareholder lawsuits since 2005, including several with the assistance of Plaintiff's counsel in this case. *See*, *e.g.*, *Gordon v. McAfee*, CA5752 (Del. Ch. 2010); *Gordon v. Coca-Cola*, 10-CV-182500 (Fulton Cty, Ga. 2010); *Gordon v. Royal Bank of Scotland*, 09-CV-704 (S.D.N.Y. 2009); *Gordon v. Mayo Shattuck*, C-08-5915 (Baltimore City Cir. Ct., Md. 2010).

affairs of a corporation. Thus, in a derivative action, the threshold question is whether a single shareholder may usurp the prerogatives of a duly elected board of directors to decide what is in a company's best interest—including whether the company should bring a lawsuit. Where, as here, the shareholder has not first made a demand upon the board of directors to take the requested action, she may not bring a derivative action unless she makes a *particularized* showing that demand on the board is "excused." Plaintiff has utterly failed to make this required showing here, and the Complaint must therefore be dismissed in its entirety pursuant to Federal Rule of Civil Procedure 23.1.[2]

FACTUAL BACKGROUND

I. The Company

Navigant is a Delaware[3] corporation that provides consulting services. (Compl. ¶ 11). At all relevant times, Navigant had eight directors, only one of whom, Mr. Goodyear, was also a Company officer. (*Id.* ¶ 12.) The remaining seven directors, Mr. Gildehaus, Ms. Glassman, Mr. James, Mr. Pond, Mr. Skinner, Mr. Thompson, and Mr. Tipsord (collectively, the "Outside Directors"), are not alleged to have been either officers or employees of Navigant. During 2010, Navigant had four NEOs: Mr. Goodyear, the CEO; Ms. Howard, the COO; Mr. Nardi, the CFO; and Ms. Weed, the General Counsel. (*Id.* ¶¶ 12-15.)

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[2] As explained below (*infra* at 10 n.9), in the alternative certain individual defendants should also be dismissed from Count I pursuant to Federal Rule of Civil Procedure 12(b)(6).

[3] Plaintiff inaccurately asserts that Navigant is incorporated in Illinois. (*See* Compl. ¶ 11.) The Proxy (attached as Ex. B and cited in Compl. ¶¶ 31-32, 34-36), as well as the Company's other securities filings, disclose that, in fact, Navigant is incorporated in Delaware. On a motion to dismiss, a court may take judicial notice of matters of public record and documents referred to in the Complaint. *See, e.g., Hecker v. Deere & Co.*, 556 F.3d 575, 582-83 (7th Cir. 2009); *Hickman v. Wells Fargo Bank N.A.*, 683 F. Supp. 2d 779, 784 (N.D. Ill. 2010). Moreover, the attached Amended and Restated Certificate of Incorporation, issued by the Secretary of State of the State of Delaware ("Certificate of Incorporation"), further demonstrates that Navigant is a Delaware corporation. (*See* Ex. A.) The Court may take judicial notice of this Certificate of Incorporation. *See Bronstein v. Austin*, 2008 WL 4735230, at *4 n.3 (N.D. Ill. May 30, 2008) (taking judicial notice of certificate of incorporation on motion to dismiss) (Ex. G).

The Complaint alleges that the Compensation Committee (the "Compensation Committee") of Navigant's Board of Directors (the "Board") decides the compensation for the NEOs. (*Id.* ¶¶ 28-30.)[4] For 2010, the Company's executive compensation program approved by the Compensation Committee had three primary components: salary, annual cash bonus, and long-term equity-based incentive compensation ("equity"). The NEOs' 2010 salary was determined near the beginning of 2010, but cash bonuses and equity for 2010 performance were awarded in early 2011, based, in part, on individual and Company performance for 2010, as well as peer benchmarks. (*See* Compl. ¶¶ 30-33; Proxy at 12-18.)

Plaintiff's claim rests on assertions that, in her view, the NEOs' compensation was too high and not justified by Navigant's 2010 performance. (Compl. ¶¶ 42-44.) As an example, Plaintiff singles out that two of the four NEOs purportedly received "pay raises of $220,000 and $148,000 … respectively." (*Id.* ¶ 42.) Not only is this incorrect, and inconsistent with what the Proxy itself discloses (Proxy at 18-20, 23), but the Proxy also reveals that compensation for 2010 performance for *all four* of the NEOs meaningfully *declined* compared to their compensation for 2009 performance: Mr. Goodyear's by more than 10%; Mr. Nardi's by more than 18%; Ms. Howard's by more than 6%; and Ms. Weed's by more than 20%.

The following charts compare the executive compensation received by each Named Executive Officer for 2010 performance versus 2009 performance.[5]

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[4] According to the Complaint, during the relevant period the Compensation Committee consisted of four outside directors, *i.e.*, Mr. Gildehaus, Ms. Glassman, Mr. James, and Mr. Tipsord. (Compl. ¶ 28.)

[5] The figures presented in the following charts are based on tables included in the Company's 2011 proxy materials. (*See* Proxy at 18-20, 23; April 15, 2011 Supplemental Proxy Statement ("Supplemental Proxy") at 1 (Ex. C).) They substantively differ from the 2010 Summary Compensation Table that appears in the Proxy in their treatment of equity awards granted after the end of the calendar year but based on performance for the prior year. This is fully consistent with the Complaint itself, which recognizes and alleges that the cash bonuses paid and equity awards granted in early 2011 were compensation for 2010. (*See, e.g.,* Compl. ¶ 50.) Pursuant to SEC rules, the Summary Compensation Table requires the Company to report equity awards in the year they are granted, even if the grants are

Mr. Goodyear

Year	Salary	Cash Bonus	Equity	Total	Change
2010	$850,000	$275,000	$300,000	$1,425,000	-10.9%
2009	$850,000	$0	$750,000	$1,600,000	***

Mr. Nardi

Year	Salary	Cash Bonus	Equity	Total	Change
2010	$450,000	$150,000	$135,000	$735,000	-18.3%
2009	$450,000	$150,000	$300,000	$900,000	***

Ms. Howard

Year	Salary	Cash Bonus	Equity	Total	Change
2010	$600,000	$200,000	$225,000	$1,025,000	-6.8%
2009	$600,000	$0	$500,000	$1,100,000	***

Ms. Weed

Year	Salary	Cash Bonus	Equity	Total	Change
2010	$400,000	$100,000	$115,000	$615,000	-20.6%
2009	$400,000	$125,000	$250,000	$775,000	***

Total

Year	Salary	Cash Bonus	Equity	Total	Change
2010	$2,300,000	$725,000	$775,000	$3,800,000	-13.1%
2009	$2,300,000	$275,000	$1,800,000	$4,375,000	***

As these charts reflect, and as stated clearly in the Proxy, the NEOs received no salary increases at all in 2010. And although the cash bonuses paid in early 2011 to two of the NEOs for 2010 performance increased by a total of $450,000, the equity awards granted at the same time to those same NEOs *decreased* by a larger amount. Indeed, the total compensation awarded to the NEOs with respect to 2010 performance declined more than 13% from the compensation awarded a year earlier for 2009 performance.

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intended as compensation for the prior year's performance. Thus, the 2010 Summary Compensation Table includes equity awards granted at the beginning of 2010, but intended as compensation for 2009 performance, in the row labeled "2010." The charts above list those equity awards in the row labeled "2009," to reflect that those awards were granted based on 2009 performance. In the row labeled "2010," the charts in this table likewise include equity awards granted in early 2011 as compensation for 2010 performance. (*See* further discussion in Proxy at 17-18; Supplemental Proxy at 1.)

II. The "Say-on-Pay" Vote

In 2010, Congress enacted Dodd-Frank, which included a new provision requiring "say-on-pay" shareholder votes. Specifically, Section 951 of Dodd-Frank, 15 U.S.C. § 78n-1(a), provides that, at least once every three years, a company's proxy statement must contain a resolution asking shareholders to approve, on a non-binding, advisory basis, the compensation of the company's named executive officers as described in the proxy statement.

Although the Complaint cites random excerpts of Dodd-Frank's legislative history (Compl. ¶¶ 45-49), it barely acknowledges that the "say-on-pay" vote is "non-binding" (*id.* ¶ 46). In fact, Dodd-Frank specifically provides that the "say-on-pay" vote "shall not be binding on the issuer or the board of directors of an issuer." *See* 15 U.S.C. § 78n-1(c). Moreover, the statute explicitly states that the "say-on-pay" vote "may not be construed—(1) as overruling a decision by [the company] or board of directors; (2) to create or imply any change to the fiduciary duties of [the company] or board of directors; (3) to create or imply any additional fiduciary duties for [the company] or its board of directors; or (4) to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation." *Id.*

Dodd-Frank's legislative history further underscores that while the "say-on-pay" provision was intended to allow the shareholders "to express their opinion collectively on the appropriateness of executive pay," "the result [of the vote] is not binding on the board or management." S. Rep. No. 111-176, at 133 (2010); *see also* H.R. Rep. No. 111-236, at 25 (2009) (the proposed "say-on-pay" vote is advisory); H.R. Conf. Rep. No. 111-517, at 872 (2010) (same). In explaining Dodd-Frank, the SEC noted (emphasis added):

> The Say-on-Pay, frequency, and golden parachute votes ***are advisory rather than binding***. The Dodd-Frank Act specifies that the shareholder vote to approve executive compensation 'shall not be binding on the issuer or the board of directors of an issuer.' . . .

> ***It is up to the company's board of directors to determine what it considers to be the best compensation policies and practices for the company. Unlike a binding vote, advisory votes do not require the company or its board of directors to take a specific action.*** The company's board of directors may consider advisory votes and may follow up with other communications or dialogue with shareholders as part of its deliberative process in making policy decisions.

SEC Investor Bulletin, "Say-on-Pay and Golden Parachute Votes" at 3-4 (March 2011).

Pursuant to the Dodd-Frank "say-on-pay" provision, Navigant's Proxy included a non-binding resolution approving the 2010 executive compensation paid to the Company's NEOs, as disclosed in the Proxy. (Compl. ¶ 50.) At the Company's annual shareholders' meeting on April 25, 2011, the shareholders voted against the advisory "say-on-pay" resolution, albeit by a narrow margin: 51% of shares voted against the resolution, with 41.6% voting for it and 7.2% being broker non-votes. (*See* Navigant 4/26/11 Form 8-K at 2 (Ex. D).)[6]

Almost nine months after this "say-on-pay" vote, Plaintiff brought this suit. In Count I, Plaintiff alleges that each of the individual defendants breached a fiduciary duty of loyalty by virtue of the 2010 executive compensation decisions having been "excessive," and should be liable to the Company for unspecified amounts. (Compl. ¶¶ 67-69). In Count II, Plaintiff claims that the NEOs were "unjustly enriched" by the compensation they received, and should repay some unspecified amounts. (*Id*. ¶¶ 74-75.)

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[6] Although not necessary to resolve this motion, it bears noting that Plaintiff's assertion that the "Navigant Board has failed to rescind or amend the 2010 executive compensation, despite the shareholders' say-on-pay vote" is, once again, simply wrong. (Compl. ¶ 58.) The Company's public filings disclose that, after the negative say-on-pay vote (but well before this suit), the Compensation Committee modified the terms of the restricted stock awards granted in early 2011 (for 2010 performance) to include performance-based vesting conditions for a portion of those awards. Certain tranches of these awards now vest if and only to the extent certain future performance criteria are met. (*See* Navigant 9/1/11 Form 8-K at 2 (Ex. E).)

ARGUMENT

I. THE DEMAND REQUIREMENT.

A "cardinal precept" of Delaware law is that "directors, rather than shareholders, manage the business and affairs of the corporation."[7] *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984). A shareholder derivative action, in which a shareholder brings suit in the name of the corporation, "[b]y its very nature . . . impinges on the managerial freedom of directors." *Id.*; *White v. Panic*, 783 A.2d 543, 550 n.18 (Del. 2001) ("The directors of a corporation and not its shareholders manage the business and affairs of the corporation . . . and, accordingly the directors are responsible for deciding whether to engage in derivative litigation."). As a result, a shareholder's ability to bring a derivative action is limited in the first instance by a demand requirement imposed by Delaware law, pursuant to which "shareholders seeking to assert a claim on behalf of the corporation must first . . . mak[e] a demand on the directors to obtain the action desired." *Spiegel v. Buntrock*, 571 A.2d 767, 773 (Del. 1990); *Oakland County Employees' Ret. Sys. v. Massaro*, 772 F. Supp. 2d 973, 976 (N.D. Ill. 2011).

The demand requirement is incorporated in Federal Rule of Civil Procedure 23.1, which requires that a complaint in a derivative action allege with particularity the efforts, if any, the plaintiff made to obtain the desired action and the reason for the plaintiff's failure to make a demand. *Starrels*, 870 F.2d at 1170. Moreover, Delaware's demand requirement "is more than a mere pleading requirement; it is a substantive right," *id.* at 1171, and thus "Delaware law governs whether the facts alleged in the complaint are sufficient to excuse demand," *Oakland County Employees' Ret. Sys. v. Massaro*, 736 F. Supp. 2d 1181, 1189 (N.D. Ill. 2010). Under

[7] Because Navigant is a Delaware corporation (*supra* at 2 n.3), Delaware law governs whether demand is excused, as well as the substantive issues pertaining to Plaintiff's putative derivative claims against the Defendants. *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 108-09 (1991); *Starrels v. First Nat'l Bank of Chicago*, 870 F.2d 1168, 1170 (7th Cir. 1989).

both federal and Delaware law, such allegations must meet "stringent requirements of factual particularity," which cannot be satisfied "by conclusory statements or mere notice pleading." *Brehm v. Eisner*, 746 A.2d 244, 254-55 (Del. 2000); *see also Garza v. Belton*, 2010 WL 3324881, at *4 (N.D. Ill. Aug. 13, 2010) (Ex. I); *Zurich Capital Markets Inc. v. Coglianese*, 332 F. Supp. 2d 1087, 1115 (N.D. Ill. 2004). These heightened substantive standards for determining whether demand is "excused" exist because it otherwise would be all too easy for a single shareholder to usurp the authority to manage corporate affairs that Delaware vests in directors.

Plaintiff concedes that she has not made a demand on Navigant's Board here. (Compl. ¶ 61.) Therefore, the Complaint must be dismissed unless Plaintiff has alleged particularized facts establishing that making such a demand would be futile. *Aronson*, 473 A.2d at 808; Fed. R. Civ. P. 23.1. Because Plaintiff challenges a specific business decision—the executive compensation decisions for 2010 reflected in the Proxy—the two-part *Aronson* test applies. *See Garza*, 2010 WL 3324881, at *5. Under *Aronson*, demand is excused only if "under the particularized facts alleged, a reasonable doubt is created that: (1) the directors are disinterested and independent and (2) the challenged transaction was otherwise the product of a valid exercise of business judgment." 437 A.2d at 814; *see also Starrels*, 870 F.2d at 1171. Plaintiff's Complaint falls far short under either prong of *Aronson*.

II. PLAINTIFF FAILS TO PLEAD DEMAND FUTILITY ADEQUATELY.

A. Plaintiff Fails to Allege Particularized Facts Sufficient to Create a Legitimate Issue Regarding the Independence and Disinterest of a Majority of the Directors.

To show that demand is excused under the first prong of *Aronson*, Plaintiff bears the burden of pleading particularized facts indicating that a majority of the Board is not independent of some interested party or is otherwise not itself disinterested. *Beam ex rel. Martha Stewart*

Living Omnimedia, Inc. v. Steward, 845 A.2d 1040, 1048-49 (Del. 2004); *Aronson*, 437 A.2d at 814. The Complaint here fails in its attempts to do so.

1. Plaintiff Does Not Challenge the Independence of a Majority of the Directors.

To show that a director lacks independence, a complaint must show that the director is so "dominated by" or "beholden to" another person who is self-interested with respect to the matter in question that the director's "discretion would be sterilized" by virtue of this relationship. *Beam*, 845 A.2d at 1050; *Levine v. Smith*, 511 A.2d 194, 205 (Del. 1991). The Complaint makes no attempt to allege, even in conclusory fashion, that the Outside Directors (seven of the eight members of the Board) were controlled or dominated by the NEOs or anyone else. Accordingly, there is no issue of "independence" present here.

2. Plaintiff Fails to Allege Particularized Facts Sufficient to Create a Reasonable Doubt Regarding the Disinterest of a Majority of the Directors.

Of the eight directors, the Complaint alleges that only one of them, Mr. Goodyear, Navigant's CEO at the time, received any personal benefit from the Board's decision (*i.e.*, his 2010 compensation). (Compl. ¶ 64.)[8] The Complaint does not assert that any of the Outside Directors reaped any personal benefits, financial or otherwise, from the 2010 executive compensation decisions or stood on both sides of the transaction. Instead, Plaintiff's sole apparent theory for excusing demand is that the Outside Directors approved the 2010 executive compensation decisions and therefore "face[] a substantial likelihood of liability for breach of

[8] The Complaint does not allege that Mr. Goodyear was a member of the Compensation Committee. Nor does it contain any allegation that Mr. Goodyear participated in the decision regarding his own compensation. In any event, as the Delaware Supreme Court has made clear, "[t]his Court has never held that one director's colorable interest in a challenged transaction is sufficient, without more, to deprive a *board* of the protection of the business judgment rule presumption of loyalty." *Cede & Co. v. Technicolor, Inc*., 634 A.2d 345, 363 (Del. 1993).

loyalty for authorizing the 2010 executive compensation." (*Id.* ¶¶ 62-63.)[9]

Essentially, Plaintiff asserts that the Board is disqualified from considering a demand *because Plaintiff has sued all of its members*. Delaware courts, however, have flatly and consistently rejected the notion that demand is excused merely because directors are themselves named as defendants, recognizing that such an argument would eviscerate the demand requirement in every case:

> Plaintiff's final argument is the incantation that demand is excused because the directors otherwise would have to sue themselves, thereby placing the conduct of the litigation in hostile hands and preventing its effective prosecution. This bootstrap argument has been made to and dismissed by other courts. Its acceptance would effectively abrogate Rule 23.1 and weaken the managerial power of directors. Unless facts are alleged with particularity to overcome the presumptions of independence and a proper exercise of business judgment, in which case the directors could not be expected to sue themselves, a bare claim of this sort raises no legally cognizable issue under Delaware corporate law.

Aronson, 472 A.2d at 818. The law is clear that "the 'mere threat' of personal liability does not excuse demand." *Oakland County*, 772 F. Supp. 2d at 977; *see also Brehm*, 746 A.2d at 257 n.34. Instead, as the Complaint itself recognizes (¶ 62), a heightened "substantial likelihood" showing is required under Delaware law: demand is excused only in the "rare case" in which a plaintiff has alleged particularized facts demonstrating "director conduct that is 'so egregious on its face that board approval cannot meet the test of business judgment, and a substantial likelihood of director liability therefore exists.'" *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 121 (Del. Ch. 2009) (quoting *Aronson*, 473 A.2d at 815); *see also Wood v. Baum*, 953 A.2d 136, 141 (Del. 2008) (affirming dismissal of derivative claim where plaintiffs did not plead

[9] Although the Complaint also names the NEOs as defendants to Count I, it does not allege that any of the NEOs participated in the decisions regarding their 2010 compensation. Accordingly, quite apart from the insufficiency of the Complaint under Rule 23.1, the allegations in Count I against defendants Goodyear, Howard, Nardi and Weed are patently insufficient and, pursuant to Rule12(b)(6) should not be permitted to proceed in any event.

with particularity facts showing that the directors faced "a substantial risk of personal liability").

The Complaint alleges only one claim against the Board members, *i.e.*, that the 2010 executive compensation decisions constituted a breach of the fiduciary duty of loyalty. (*See* Compl. ¶¶ 65-72.)[10] A duty of loyalty claim can be pled in one of two ways: (1) by demonstrating a "financial or other cognizable fiduciary conflict of interest," by the director in the challenged decision, or (2) by demonstrating a failure of the directors to "act[] in the good faith belief that [their] actions are in the corporation's best interest." *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006). Here, there are no allegations that the Outside Directors had any financial or other conflict of interest, and thus Plaintiff's only avenue is to allege that they acted in bad faith.

The showing necessary to create a substantial likelihood of liability for bad faith is particularly high. Bad faith may be established only "where the fiduciary *intentionally* acts with a purpose other than that of advancing the best interests of the corporation, where the fiduciary acts *with the intent* to violate applicable positive law, or where the fiduciary *intentionally* fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties." *Id*. at 369 (emphasis added). This is a subjective determination; bad faith requires "conduct motivated to do harm" or "intentional dereliction of duty, a conscious disregard for one's responsibilities." *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 64-68 (Del. 2006).

Plaintiff does not come close to providing particularized allegations that meet this test and which demonstrate a "substantial likelihood" of director liability on this theory. To begin with, although Plaintiff attempts to suggest that the compensation decisions were "not in the best interests" of Navigant (Compl. ¶ 56), that confuses the relevant inquiry. The subjective bad faith

[10] Indeed, this theory of liability is the only one open to Plaintiff, because Navigant's Certificate of Incorporation insulates the Board from liability for breach of the duty of care. (*See* Certificate of Incorporation, Art. XIII.B; *see also* 8 Del. C. § 102(b)(7); *Wood*, 953 A.2d at 141, 144 (relying on exculpatory charter provision to dismiss a shareholder derivative suit alleging a breach of the duty of care).)

required for a breach of the duty of loyalty is not remotely the same as Plaintiff's attempt to second-guess the advisability of decisions; only the former suffices for a duty of loyalty claim. And, in that regard, the Complaint contains no non-conclusory, factual allegations demonstrating a "substantial likelihood" that any of the Board members acted in a way that was intentionally designed to damage the Company or with conscious disregard for its interests—as opposed to acting with the genuine belief (whether correct or not) that they were acting in the best interests of the Company. The Complaint does not even attempt to provide a plausible explanation, much less a factual basis, as to why the directors would try to damage the Company.

Instead, the Complaint relies primarily on the negative say-on-pay vote to rebut the presumption that directors acted in good faith. But other courts faced with similar adverse shareholder votes have rejected attempts to infer a substantial likelihood of director bad faith. *See, e.g., Laborers' Local v. Intersil*, 2012 WL 762319, at *5 (N.D. Cal. Mar. 7, 2012) (Ex. N); *Plumbers Local No. 137 Pension Fund v. Davis*, 2012 WL 104776, at *5 (D. Or. Jan. 11, 2012) (Ex. S), *adopted as the district court's opinion*, 2012 WL 602391 (D. Or. Feb. 23, 2012) (Ex. T); *Teamsters Local 237 Add'l Sec. Benefit Fund v. McCarthy*, No. 2011-cv-197841, slip op. at 14-16 (Ga. Super. Ct. Sept. 16, 2011) (Ex. U). Indeed, the fact that 41.6% of Navigant's shareholders *approved* of the executive compensation decisions alone demonstrates that this is a matter as to which reasonable persons could reach different conclusions, without any inference of "bad faith" arising. There is no more reason to believe that these shareholders sought intentionally to damage Navigant in their decisions than to believe that Board members sought to do so. Rather, the executive compensation decisions at issue are protected by the business judgment rule, and neither a negative say-on-pay vote nor Plaintiff's attempts at second-guessing alter the standards for evaluating such decisions. (*See* Section II.B.)

B. Plaintiff Fails to Allege Particularized Facts Sufficient to Create a Reasonable Doubt that the Compensation Decisions are Protected by the Business Judgment Rule.

The business judgment rule is a presumption that, among other things, the directors of a corporation acted "in good faith and in the honest belief that the action taken was in the best interests of the company."[11] *Spiegel*, 571 A.2d at 774. For demand to be excused under the second prong of the *Aronson* test, a plaintiff must plead particularized facts creating a "reasonable doubt" that "the challenged transaction was otherwise the product of a valid exercise of business judgment." 437 A.2d at 814. This pleading requirement imposes on Plaintiff "a substantial burden, as the second prong of the *Aronson* test is directed to extreme cases in which despite the appearance of independence and disinterest a decision is so extreme or curious as to itself raise a legitimate ground to justify further inquiry and judicial review"—*i.e.*, the decision is so obviously lacking in any conceivable justification that by itself it creates an inference of wrongdoing. *Highland Legacy Ltd. v. Singer*, 2006 WL 741939, at *7 (Del. Ch. Mar. 17, 2006) (internal quotation marks omitted) (Ex. K).

Plaintiff's arguments against application of the business judgment rule are essentially two-fold: (1) the Board's decision must have been made in bad faith because executive compensation was awarded despite a decline in the Company's stock price, and (2) the negative say-on-pay vote removes the presumptions otherwise afforded by the business judgment rule.

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[11] The business judgment rule also creates a presumption that directors acted "on an informed basis," *i.e.,* with due care. *Spiegel*, 571 A.2d at 774. Here, as noted previously (*supra* at 11), Plaintiff alleges a breach of the duty of loyalty, not of the duty of care. Moreover, the Complaint contains no allegations suggesting that the members of the Board were not adequately informed. To the contrary, the Complaint admits that the Company had a Compensation Committee specifically tasked with evaluating and determining executive compensation, and that the Compensation Committee set compensation after evaluating "peer group benchmarks, as well as individual and company performance assessments" (Compl. ¶¶ 28-34, 43, 50), allegations which "indicate that the board adequately informed itself before making a decision on compensation." *See In re Goldman Sachs Group, Inc. S'holder Litig.*, 2011 WL 4826104, at *15 (Del. Ch. Oct. 12, 2011) (Ex. J).

The first argument is merely impermissible second-guessing of the Board's business judgment, and the second is contrary to both Delaware law and Dodd-Frank.

1. Executive Compensation Decisions are Protected by the Business Judgment Rule.

Long-established Delaware law makes clear that executive compensation decisions are not only matters that rest within a board's business judgment, but are decisions with respect to which a board is particularly "entitled to great deference" because it is "the essence of business judgment for a board to determine if a particular individual warrants large amounts of money." *Brehm*, 746 A.2d at 263.[12] Indeed, the Delaware Supreme Court in *Brehm* affirmed dismissal of a shareholder derivative suit challenging a $140 million severance package made to a single executive terminated after only 14 months of employment, holding that plaintiffs had not pled facts sufficient to give rise to a reasonable doubt that the board's compensation decision was protected by the business judgment rule. *Id*. at 253, 263, 266. The Complaint's allegations of "excessive" compensation here pale by comparison. (*See* Compl. ¶¶ 42, 43.)

Plaintiff nonetheless seeks to challenge the Board's 2010 executive compensation decisions on the grounds that the compensation was "excessive" in light of declines in the Company's stock price in 2010, negative shareholder return in previous years, and an alleged "underperformance" compared to the "Business Services" industry in general. (*See* Compl. ¶¶ 2-3, 5, 35-41.) But these allegations do not remotely describe a situation so extreme on its face as to give rise to an inference that Board members must have acted in bad faith or without an honest

[12] *See also Pirelli Armstrong Tire Corp. Retiree Med. Benefits Trust v. Raines*, 534 F.3d 779, 791 (D.C. Cir. 2008) (applying Delaware law) ("[C]ourts rarely second-guess directors' compensation and severance decisions because the size and structure of executive compensation are inherently matters of judgment."); *Lewis v. Hirsch*, 1994 WL 263551, at *3 (Del. Ch. June 1, 1994) ("[E]xecutive compensation is a matter ordinarily left to the business judgment of a company's board of directors.") (Ex. O); *Haber v. Bell*, 465 A.2d 353, 359 (Del. Ch. 1983) ("[G]enerally directors have the sole authority to determine compensation levels and this determination is protected by the presumption of the business judgment rule.").

belief in what they were approving. Indeed, as noted earlier, shareholders holding more than 41% of the shares present voted *in favor* of the resolution. (*See* Navigant 4/26/11 Form 8-K at 2.) And mere disagreement about the philosophies underlying a board's compensation decisions (or their implementation) is simply insufficient to rebut the presumption of the business judgment rule. *See Goldman Sachs Group*, 2011 WL 4826104, at *14 ("The Plaintiffs' allegations mainly propose that the compensation scheme implemented by the board does not perfectly align [employee and stockholder] interests; and that, in fact, it may encourage employee behavior incongruent with the stockholders' interest. This may be correct, but it is irrelevant. The fact that the Plaintiffs may desire a different compensation scheme does not indicate that equitable relief is warranted.").

Moreover, Plaintiff's attempt to single out a very few self-selected factors for purposes of arguing that the compensation was "excessive" is tendentious in its omissions and distortive in its inclusions. For example, nowhere does Plaintiff allege that Navigant's executive compensation, or, for that matter, its shareholder return, was out of line with that of its industry peers.[13] Yet setting executive compensation at competitive levels, so as to retain and attract needed talent, is a core consideration, which is why Navigant's Compensation Committee Charter makes shareholder return only one factor in the executive compensation decisions—while also emphasizing that compensation remain "competitive."[14] (Tellingly, Plaintiff nowhere

[13] While the Complaint refers to a generic "Business Services" industry, Navigant is in a specific segment involving certain types of consulting services.

[14] The Complaint cites Navigant's Compensation Committee Charter, which provides that the Compensation Committee should consider "the Company's performance and relative shareholder return" as one of "a number of factors," including "the value of similar incentive awards to chief executive officers at comparable companies, and the awards given to the Company's Chief Executive Officer in past years." (Compl. ¶ 30.) Similarly, the Proxy also makes clear that while "the company's financial and strategic performance" is a significant factor in the NEOs' compensation, other factors include ensuring that compensation remains "competitive" relative to the Company's peer group and commensurate with each NEO's "individual performance objectives." (*Id.* ¶ 31.)

alleges what an appropriate level of compensation should have been.) Similarly, the Compensation Committee Charter recognizes that an executive's "performance" is also to be measured against "individual performance objectives"—as to which the Complaint is likewise entirely silent.[15]

Plaintiff cannot create an inference that the 2010 compensation decisions must have been the product of deliberate bad faith simply by ignoring the myriad of factors that go into such decisions and creating her own reductionist calculus. At bottom, Plaintiff is engaged in little more than an exercise in second-guessing, which is precisely what the business judgment rule prohibits and particularly so in the quintessentially discretionary realm of compensation.

2. The Say-on-Pay Vote Does Not Rebut the Business Judgment Rule.

Despite the presumption of propriety that attaches to the Board's compensation decisions, Plaintiff nonetheless alleges that the shareholder vote "is direct and probative evidence rebutting the presumption that the Navigant Board's 2010 executive compensation decisions were in the best interests of the Navigant shareholders." (*See* Compl. ¶ 56.) As discussed *supra* at 11-12, this confuses the relevant inquiry—which, for purposes of a duty of loyalty claim, is one of s*ubjective* "bad faith," not a mere dispute about what constitutes objective "best interests." Moreover, this argument is directly contrary to settled Delaware law, which makes clear that directors—not shareholders—manage the corporation. *In re Lear Corp. S'holder Litig.*, 967 A.2d 640, 655 (Del. Ch. 2008) ("[D]irectors may take good faith actions that they believe will benefit stockholders, even if they realize that the stockholders do not agree with them."); *Paramount*

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[15] Plaintiff also asserts that the "absurdity" of the 2010 executive compensation is apparent because the Company awarded no cash bonuses after a smaller drop in the stock price between 2008 and 2009, whereas the Company awarded bonuses after a larger stock price drop between 2009 and 2010. (Compl. ¶ 44.) Although this assertion, even if true, would not remotely give rise to an inference that Board members acted with bad faith in their 2010 compensation determinations, the assertion distorts the compensation picture. By focusing only on cash bonuses, Plaintiff ignores that, as discussed *supra* at 3-4, each of the NEO's total compensation for 2010 performance was significantly lower than his or her total compensation for 2009 performance. And the assertion that the Company awarded no cash bonuses in 2009 is also incorrect as to Mr. Nardi and Ms. Weed. (*See* Proxy at 23.)

Comm. Inc. v. Time Inc., 1989 WL 79880, at *30 (Del. Ch. July 14, 1989) ("The corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares. In fact, directors, not shareholders, are charged with the duty to manage the firm.") (Ex. R); *In re TW Services, Inc. S'holders Litig.*, 1989 WL 20290, at *8 n.14 (Del. Ch. Mar. 2, 1989) ("[A] corporation is not a New England town meeting; directors, not shareholders, have responsibilities to manage the business and affairs of the corporation, subject however to a fiduciary obligation.") (Ex. V). Indeed, Delaware law recognizes that a board not only has the *right*, but also the *responsibility*, to make decisions in the exercise of its own best business judgment, regardless what the body of shareholders may prefer or how they may vote. *See Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985).

Given this well-settled law, Plaintiff's only remaining avenue is to assert that Dodd-Frank changed the landscape, altering legal presumptions of compliance with fiduciary duties when shareholders disagree after-the-fact with board compensation decisions. But as discussed previously (*supra* at 5-6), Dodd-Frank makes clear that "say-on-pay" votes are advisory and non-binding, and that Dodd-Frank does *not* alter a board's fiduciary duties. *See* 15 U.S.C. § 78n-1(c). Thus, the statute cannot be read to erase the protections afforded by the business judgment rule.

Numerous courts around the country already have rejected the exact argument set forth by Plaintiff, holding that a negative say-on-pay vote is *not* a basis for a claim for breach of fiduciary duty or a reason to hold that a shareholder demand is excused. For example, two federal district courts recently applied Delaware law to dismiss shareholder derivative suits in which, as here, plaintiffs sought to assert claims of breach of fiduciary duty and unjust enrichment based on negative say-on-pay votes. *See Intersil*, 2012 WL 762319; *Davis*, 2012 WL 104776. In dismissing the complaints for failure adequately to plead that demand was excused,

both courts held that plaintiffs failed to overcome the presumption that a board's compensation decision is protected by the business judgment rule. *Intersil*, 2012 WL 762319, at *8; *Davis*, 2012 WL 104776, at *7-8. Both courts rejected arguments by plaintiffs that a negative say-on-pay vote was "prima facie evidence that the board's action was not in the corporation or shareholders' best interest and that this vote shifts the presumption in Plaintiffs' favor," finding that the mere fact of a negative say-on-pay vote does not rebut the business judgment presumption. *Davis*, 2012 WL 104776, at *7; *Intersil*, 2012 WL 762319, at *8. Moreover, both courts rejected plaintiffs' allegations that the decisions were contrary to the ethos of the company's "pay for performance" policy. *Davis*, 2012 WL 104776, at *7; *Intersil*, 2012 WL 762319, at *6. Finally, both courts held that the board did not face a substantial likelihood of liability for having allegedly awarded excessive compensation. *Davis*, 2012 WL 104776, at *5; *Intersil*, 2012 WL 762319, at *5.[16]

Several of the courts dismissing "say-on-pay" cases have relied on the fact that Dodd-Frank explicitly did not alter the standard by which compensation decisions are judged. *See Davis*, 2012 WL 104776, at *7-8; *Jacobs Engineering II*, slip op. at 8 ("By its explicit terms, the Dodd-Frank Act creates no binding effect on a shareholder compensation vote when construing a board's fiduciary duties in approving such compensation."); *Assad v. Hart*, 2012 WL 33220, at *4 (S.D. Cal. Jan. 6, 2012) (dismissing a claim for breach of fiduciary duty based on a board's alleged failure to alter 2010 executive compensation after a negative say-on-pay vote, holding that "[t]he Dodd-Frank Wall Street Reform Act did not create a private right of action or create

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[16] Several courts applying the law of other states also have dismissed shareholder derivative suits based on negative say-on-pay votes. *See, e.g., Weinberg ex rel. BioMed Realty Trust, Inc. v. Gold*, 2012 WL 812348, at *6 (D. Md. Mar. 12, 2012) (Ex. W) (applying Maryland law); *In re Jacobs Engineering Group, Inc. Consolidated S'holder Deriv. Litig*. (*Jacobs Engineering II*), No. BC454543, slip op. at 13-14 (Cal. Super. Ct. Mar. 6, 2012) (Ex. M) (applying California law); *In re Jacobs Engineering Group, Inc. Consolidated S'holder Deriv. Litig*. (*Jacobs Engineering I*), No. BC454543, slip op. at 2-3 (Cal. Super. Ct. Nov. 10, 2011) (Ex. L) (same).

new fiduciary duties") (Ex. F); *see also Dennis v. Hart*, 2012 WL 33199, *3 (S.D. Cal. Jan. 6, 2012) (rejecting shareholder's contention that an adverse say-on-pay vote rebutted business judgment presumptions) (Ex. H). As explained by a Georgia state trial court, which was applying Delaware law, and which dismissed a shareholder derivative suit asserting similar claims, the board's compensation decisions were protected by the business judgment rule, and Dodd-Frank did not alter that calculus:

> Plaintiffs' contention that the 'independent business judgment of Beazer's shareholders suffices to rebut the presumption of the business judgment protection finds no support either in governing Delaware law or in the Dodd-Frank Act's new say on pay provisions. The Dodd-Frank Act expressly and unambiguously states that shareholder say on pay votes are advisory and "*shall not be binding on the issuer or the board of directors* of an issuer, and *may not be construed* (1) *as overruling a decision by such issuer or board of directors*; (2) *to create or imply any change to the fiduciary duties of such issuer or board of directors*; [or] (3) *to create or imply any additional fiduciary duties for such issuer or board of directors*." *See* Dodd-Frank Act, 124 Stat. 1376, 1900 (emphasis added); 15 U.S.C. § 78n-1(c). Thus, the Dodd-Frank Act expressly preserved the pre-existing fiduciary duty framework concerning directors' executive compensation decisions.

McCarthy, slip op. at 11 (applying Delaware law). The court also explained that, as in this case, the framework for 2010 executive compensation had been approved prior to the "say-on-pay" vote, and characterized plaintiffs' argument that the subsequent "say-on-pay" vote rebutted the presumption that the earlier compensation decisions reflected valid business judgment as "wholly unpersuasive both factually and legally." *Id*. at 10.

There is, to our knowledge, only one court that has permitted a derivative suit based on a say-on-pay vote to survive a motion to dismiss. *See NECA-IBEW Pension Fund ex rel. Cincinnati Bell, Inc. v. Co*x, 2011 WL 4383368 (S.D. Ohio Sept. 20, 2011) (Ex. P). However, the *Cincinnati Bell* decision was based on Ohio law, which differs significantly from Delaware law in that Ohio law does not require a derivative plaintiff to allege facts in a complaint to

overcome the application of the business judgment rule. Instead, unlike under Delaware law, Ohio law only considers the business judgment rule to be an affirmative defense, as the *Cincinnati Bell* court noted.[17] Other courts have relied on this difference in declining to follow *Cincinnati Bell* and dismissing similar claims. *See Davis*, 2012 WL 104776, at *8; *see also BioMed Realty Trust*, 2012 WL 812348, at *6 (applying Maryland law and declining to follow *Cincinnati Bell* as unpersuasive); *Jacobs Engineering I*, slip op. at 2-3 (applying California law and declining to follow *Cincinnati Bell* as unpersuasive). And less than a week after its motion to dismiss decision, the same court denied plaintiff's request for a preliminary injunction, holding that plaintiff had not established a strong likelihood of success on the merits given the business judgment affirmative defense under Ohio law. *NECA-IBEW Pension Fund v. Co*x, No. 11-cv-451, slip. op. at 3 (S.D. Ohio Sept. 26, 2011) (Ex. Q).

Finally, it is worth noting that the facts here are even less favorable for Plaintiff than they were in the other cases rejecting Plaintiff's theory. Here, total compensation for each of the NEOs actually *declined* for the year at issue (*see supra* at 3-4). In many of the other "say-on-pay" cases discussed above, officer compensation had increased, and sometimes by very substantial amounts. *See, e.g., Intersil*, 2012 WL 762319, at *8 (increased by average of 41.7%); *Assad*, 2012 WL 33220, at *1 (increase of $2.4 million).

This Court should do exactly what every other court to address a Dodd-Frank "say-on-pay" case under Delaware law has done—find that demand is not excused and dismiss the case.

CONCLUSION

For all of the above reasons, this action should be dismissed.

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[17] *Compare Cede & Co.*, 634 A.2d at 360-61 (explaining that, under Delaware law, "a shareholder plaintiff challenging a board decision has the burden at the outset to rebut the rule's presumption"), *with Marsalis v. Wilson*, 778 N.E.2d 612, 616 (Ohio Ct. App. 2002) (holding that plaintiffs are not "obligated to plead operative facts in their complaint that would rebut the presumption.").

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Respectfully submitted,

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