EFiled: Aug 25 2011 5:29PM EDT
Transaction ID 39493936
Case No. 6462-VCG

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

FRANK DAVID SEINFELD, Plaintiff, v. DONALD W. SLAGER, JAMES E. O'CONNOR, JOHN W. CROGHAN, TOD C. HOLMES, DAVID I. FOLEY, RAMON A. RODRIGUEZ, MICHAEL W. WICKHAM, JAMES W. CROWNOVER, NOLAN LEHMANN, ALLAN C. SORENSEN, WILLIAM J. FLYNN, W. LEE NUTTER, JOHN M. TRANI, MICHAEL LARSON, and REPUBLIC SERVICES, INC., Defendants,	CIVIL ACTION NO. 6462-VCG

<u>AMENDED STOCKHOLDER'S DERIVATIVE COMPLAINT</u>

Plaintiff, by and through his attorneys, alleges as follows:

1. The plaintiff is a stockholder of defendant Republic Services, Inc. ("Republic" or the "Company") and was a stockholder at the time of the transactions complained of herein and has been such continuously since then.

2. Defendants James E. O'Connor, Tod C. Holmes, and Donald W. Slager (the "Officer Defendants" or "Covered Employees") are three of the Company's Covered Employees and three of the non-resident officers of the Company, as defined in 10 Del. C. § 3114(b).

3. Defendants James E. O'Connor, Donald W. Slager, John W. Croghan, James W. Crownover, William J. Flynn, David I. Foley, Michael Larson, Nolan Lehmann, W. Lee Nutter, Ramon A. Rodriguez, Allan Sorensen, John M. Trani, and Michael W. Wickham, (sometimes the

"Director Defendants"), thirteen in number, are all the members of the Company's board of directors.

4. Defendants Flynn, Wickham, Foley, Larson, and Sorensen, five in number, are all the members of the compensation committee of the Company's board of directors. Previously, defendants Lehmann and Rodriguez were members of the compensation committee.

5. Republic's fiscal year ends December 31. On February 10, 2011, it had outstanding 384,060,682 shares of common stock, which are traded on the New York Stock Exchange.

6. This is a stockholder's derivative action on behalf of Republic to recover from the Director Defendants for committing waste by paying non-tax-deductible compensation to the Officer Defendants. In addition, the Director Defendants paid defendant O'Connor for past services for which he had already been paid. O'Connor was unjustly enriched thereby. This is also an action on behalf of Republic to recover against the Officer Defendants for unjust enrichment at the Company's expense for receiving and accepting compensation that the Director Defendants wrongfully caused the Company to pay to them in the form of non-tax-deductible annual cash incentives under the Company's Executive Incentive Plan (the "EIP") and restricted stock and restricted stock units under the Company's 2007 Stock Incentive Plan. This is an action on behalf of Republic to recover the excessive compensation that the directors paid themselves as members of the board. Finally, this is an action on behalf of Republic to prevent the payment of incentive awards under the Company's Synergy Incentive Plan.

7. This action follows an action in the United States District Court for the District of Delaware entitled *Seinfeld v. O'Connor*, 09-cv-887 (LPS), where Judge Stark dismissed the direct (not derivative) federal claims for failure to state a claim for relief. *Seinfeld v. O'Connor,* 774 F. Supp. 2d 660 (D. Del. March 30, 2011). But Judge Stark held that the stockholder's derivative

claims were all based on Delaware state law and dismissed them for lack of federal jurisdiction, prefacing that disposition to say, "The Court notes that Seinfeld also arguably raises theories of waste and unjust enrichment in his derivative action." *Id.* at p. 12 fn. 12.

8. The Internal Revenue Code ("IRC") § 162(m) subjects the Company to special treatment with respect to its compensation of the Covered Employees. Whereas IRC § 162 (a)(1) allows the Company an income tax deduction for "a reasonable allowance for salaries or other compensation for personal services actually rendered," IRC § 162(m) imposes restrictions on that deduction for the compensation of the Company's Covered Employees. The Covered Employees are the CEO and the "four highest compensated officers." Treas. Reg. § 1.162-27(c)(2)(i)(B). Defendant O'Connor was the CEO from 2009 and earlier until January 1, 2011, when his retirement became effective. Defendant Slager then succeeded him as CEO.

9. Specifically, IRC § 162(m) provides that annual compensation of covered employees in excess of $1 million is not tax-deductible unless the compensation is performance-based, pursuant to a plan containing pre-established, objective criteria that the stockholders have approved. The Joint Committee on Taxation specifically addressed the relevance of this provision of the Code in a report that expressly recognizes its role as a tool of corporate governance: **"The $1 million deduction limitation reflects corporate governance issues regarding excessive compensation, rather than issues of tax policy."** JOINT COMMITTEE OF TAXATION, REPORT OF INVESTIGATION OF ENRON CORPORATION AND RELATED ENTITIES REGARDING FEDERAL TAX AND COMPENSATION ISSUES AND POLICY RECOMMENDATIONS, 2003 WL 25599037 n.2211 and accompanying text (2003). The Treasury has promulgated regulations concerning IRC § 162(m) at Treas. Reg. § 1.162-27.

10. It is the public policy of the United States that corporate senior executive compensation must be reasonable, performance based, objectively determined, and pre-approved by

stockholders. The purpose of the IRC § 162(m) is to align the performance incentive with the interests of shareholders. *See* Internal Revenue Service Chief counsel Attorney Memorandum, IRS AM 2009-006, 2009 WL 2138881 (July 17, 2009). In furtherance of this public policy, another purpose of IRC § 162(m) is to give stockholders a say on corporate executive compensation. H.R. Conf. Rep. 103-213, 1993 WL 302291 at *587 ("the compensation must be approved by a majority of shares voting in a separate vote"). More recently, the United States has increased the voice of stockholders on corporate executive compensation with the advisory say-on-pay provisions of the Dodd-Frank Act. PL 111-203, July 21, 2010, 15 U.S.C. § 78n-1.

11. The EIP is the Company's cash incentive plan that pays the participant a cash bonus for meeting or exceeding performance goals measured by the Company's financial results. Defendant O'Connor was a participant in the EIP in 2009 and 2010.

12. The EIP provides for annual bonuses for meeting performance goals in one year and for long term bonuses for meeting performance goals in periods longer than one year. In 2009 and 2010, defendant O'Connor participated in the EIP for annual bonuses and for three year bonuses, i.e., for the periods January 1, 2009, through December 31, 2011, and for January 1, 2010, through December 31, 2012.

13. On June 24, 2010, Republic's board of directors accepted defendant O'Connor's retirement as CEO, effective January 1, 2011.

14. Section 5.2 of the EIP provides that, if a participant retires during a period in which his performance is in progress and not yet completed, the Company will pay him a fractional amount of what he would have received had he continued working until the end of the period. The fraction is the number of completed calendar months over the total number of months in the period. For defendant O'Connor the fraction under the EIP for the 2009-2011 period was 24/36.

15. But § 5.2 of the EIP is expressly subject to § 5.3 of the EIP, which provides that § 5.2 is inapplicable to the extent provided in any employment agreement between a participant and the Company.

16. There was an employment contract effective February 21, 2007, between the Company and O'Connor, which provided that upon his retirement the Company would pay O'Connor an amount equal to the "full target amount" for each performance award in which he was then participating as to which the award had "not been determined to have been earned." The target amount is the amount that O'Connor would get if he met his goal. If he exceeded his target goal he would get more. If he met less than his target goal, he would get less, and if he met it enough less, he would get zero. So, if the February 21, 2007, contract had been in place when he retired on June 24, 2010, under § 5.3 of the EIP the Company would have paid him targets rather than pro-rated incentive awards, and the contract did not require that the performance goals be met for the Company to pay the full target amounts.

17. But on February 21, 2008, the Internal Revenue Service (the "IRS" or the "Service") released Rev. Rul. 2008-13, 2008-10 I.R.B. 518, 2008 WL 451876 (IRS Feb. 21, 2008). There, the Service ruled that compensation is not performance-based if the Covered Employee would receive all or even part of the compensation ***regardless*** of whether the performance goal is met, citing Treas. Reg. § 1.162-27(e)(2)(v). The Service went on to note that the regulation provided an exception if the plan allows unearned compensation to be paid upon death, disability, or change of ownership or control, but not upon retirement. Accordingly, the IRS ruled that a plan that paid "performance-based" compensation upon retirement during the performance period was not a performance-based plan, so that no compensation paid under such a plan would be tax-deductible.

18. The Service was aware, however, that there were plans in existence that had provisions similar to the retirement provision in the February 21, 2007, employment contract and that it would be unfair to deny tax deductions to companies that were bound by such agreements made before the release of Rev. Rul. 2008-13. Accordingly, the IRS stated that Rev. Rul. 2008-13 would not be applied to disallow a deduction paid pursuant to an employment contract in effect on February 21, 2008. The IRS acted thus under IRC § 7805(b)(8) and specifically cited that statute, which provides:

> The Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect.

But the IRS went further and also stated that Rev. Rul. 2008-13 would not be applied to disallow a deduction if the performance period for such compensation begins on or before January 1, 2009. In so stating the Service exceeded the authority delegated to it under IRC § 7805(b), and to that extent the January 1, 2009 provision is ineffective. An administrative rule out of harmony with the statute is void.

19. The IRS's administrative rulings have both prospective and retroactive effect. But the IRS may limit the retroactive effect of a ruling under IRC § 7805(b)(8). Allowing the IRS to apply rulings only prospectively, and not retroactively, was to avoid the inequity for persons who had completed transactions in reliance upon pre-existing practices.

20. The Company and O'Connor entered into new employment contracts twice in 2009, on February 21, and May 4, which they entitled, respectively, the Second Amended and Restated Employment Agreement and the Amended and Restated Agreement. In both contracts they limited O'Connor's right, upon retirement, to be paid the "full target amount" for each performance award

in which he was then participating as to which the award had “not been determined to have been earned,” to those award periods beginning on or before January 1, 2009. But for award periods beginning after January 1, 2009, both contracts limited O’Connor’s payment to a pro-rata share of the actual result, as provided in 5.2 of the EIP in which O’Connor was then a participant. The January 1, 2009, “full target amount” is what O’Connor would have been paid under the February 21, 2007, employment contract, but that 2007 contract was no longer in effect.

21. As part of O’Connor’s retirement the Company agreed to pay him the “full target amount” of his incentive award for 2009-2011, i.e., $1,250,000. This payment was in contravention of Treas. Reg. §1.162(e)(2)(v) because it was paid even though O’Connor had not met his performance goal. That payment was also in contravention of the substance of Rev. Rul. 2008-13.

22. To the extent that Rev. Rul. 2008-13 states that it will not be applied to performance periods beginning as late as January 1, 2009, it is inconsistent with IRC §7805(b)(8) because such non-applicability is prospective and not retroactive, and it is inconsistent with Treas. Reg. § 1.162-27(e)(2)(v) because it treats as deductible a payment even though a Covered Employee did not meet his performance goal.

23. Section 5.3 of the EIP, requiring the payment to defendant O’Connor of a bonus that is unearned because of his retirement, renders the entire EIP non-tax-deductible, and all payments under it constitute waste. Defendants O’Connor, Slager, and Holmes were or are participants in the EIP.

24. The language concerning the payment to O’Connor of the “full target amount” in the 2009 employment contracts was hidden. When the Company’s board solicited the stockholders to approve the EIP, the 2009 proxy statement and the supplement to it made representations concerning the February 21, 2009, O’Connor employment contract and the May 4, 2009, O’Connor employment

contract, but they both omitted to disclose the requirement to pay him the "full target amount" upon his retirement. In the federal court, Seinfeld argued that the EIP contravened IRC § 162(m) because it paid compensation regardless of whether performance goals were met, but the Company's reply brief stated that under § 5.2 of the EIP, a participant would only receive a pro-rata share of his bonus if he retired before the end of the performance period, and the federal court accepted that as a fact. *Seinfeld v. O'Connor,* 774 F. Supp. 2d 660 at P.8. The Company's reply brief omitted to disclose the "full target amount" payment even though that brief was filed on August 2, 2011, shortly after O'Connor and the Company's general counsel signed the retirement contract containing the target payment language. The federal court went on to say, "Seinfeld might have a point if the EIP provided for payments based solely on retirement, but . . . it does not." But it does. The federal court was misinformed.

25. On June 24, 2010, when the Company's board accepted O'Connor's retirement, he had been the Company's CEO and a member of its board of directors for ten years. During that time the Company compensated defendant O'Connor for his work. From 2006, for which the annual proxy statement first disclosed defendant O'Connor's total annual compensation, through 2010, the Company paid O'Connor total annual compensation of between $5 million and $10 million.

26. At the time that the board accepted his retirement, O'Connor had an employment agreement with the Company that became effective May 14, 2009, and which contained provisions concerning his retirement. In addition to continuing various health benefits, stock options, and other retirement benefits, the agreement provided for the payment to O'Connor of $10 million.

27. But on or about June 25, 2010, the Company's board resolved to give O'Connor an additional lump sum cash retirement payment of $1,800,000. The express purpose of this payment was "to reward you for your long service to the Company." This payment was not authorized by the

May 14, 2009, employment agreement. The Company had paid O'Connor for his long service to the Company, and there is nothing in the expressed purpose of this payment to show that is was based on an implied contract or that the amount is not unreasonable in view of the services rendered, especially in light of the other payments by the Company to O'Connor. This payment was for no consideration and was a gift or waste.

28. The $1,800,000 payment from the Company to O'Connor is recited in a retirement agreement dated June 25, 2010. That agreement recites that the consideration from O'Connor for the $1,800,000 and other benefits to him is a general release of all claims, of any nature arising from the employment relationship between O'Connor and the Company. The retirement agreement omits to state any facts to support such released claims or even the existence of any claims O'Connor has against the Company or that there is a dispute between O'Connor and the Company. The releases given by O'Connor for non-existing claims have no value and do not constitute consideration. The $1,800,000 payment by the Company to O'Connor is not allowed under Delaware law, which looks to whether or not there is consideration for the contract.

29. Under the Company's 2007 Stock Incentive Plan (the "Stock Plan"), the Company can grant restricted stock and restricted stock units. The Stock Plan defines restricted stock as Republic common stock, $.01 par value per share, subject to certain restrictions, as determined by the compensation committee, granted pursuant to section 9 of the Stock Plan. The Stock Plan defines restricted stock units as the right to receive a fixed number of shares of Republic common stock, $.01 par value per share, or the cash equivalent, granted pursuant to section 9 of the Stock Plan.

30. Pursuant to section 9(b) of the Stock Plan, restricted stock and restricted stock units can have time based vesting restrictions, i.e., they vest after the mere passage of time and are not

tax-deductible compensation under IRC § 162(m), or performance based restrictions, i.e., they vest upon the attainment of performance goals, so that they may qualify as tax-deductible compensation under IRC § 162(m). The Company reports that it has only granted time based, non-tax-deductible restricted stock and restricted stock units to its Covered Employees under the Stock Plan. These grants have been in amounts ranging from $1 million to $5 million per year to each Covered Employee and have constituted between 25% and 65% of their total compensation.

31. The Stock Plan by its terms invites the award of some performance based restricted stock and restricted stock units, but the Republic board makes no awards at all of such tax deductible stock-based compensation. It contravenes the Stock Plan to award so much time-based restricted stock and restricted stock units instead of performance-based stock to Covered Employees because the purpose of the Stock Plan is to align the interests of Covered Employees with those of the Company's stockholders and to incentivize the Covered Employees to expend the maximum effort for the growth and success of the Company. Granting so much time-based restricted stock defeats those purposes.

32. It is highly unusual for Republic to pay so much non-tax-deductible compensation to Covered Employees. For example, Waste Management, Inc., a Delaware corporation, is one of Republic's peer group companies, which Republic uses as a meaningful comparison for senior executive compensation. Waste Management has a stock plan, but when it grants stock compensation to its covered employees almost all of it is performance based, not time based. The same is true of Norfolk Southern Corporation, a Virginia corporation, also in Republic's peer group, which granted Covered Employees five times as much performance based stock as time based stock. The same is also true of CSX Corporation, a Virginia corporation, also in Republic's peer group, which granted covered employees three times as much performance based stock as time based stock.

33. Defendants O’Connor, Slager, and Holmes were or are participants in the Stock Plan.

34. The Director Defendants are all participants in the Stock Plan, and they award themselves as directors, except in past years O’Connor and now Slager, time-based restricted stock units from it.

35. In 2010, the board awarded the Director Defendants, except O’Connor, $215,000 each in restricted stock units, which brought their annual compensation to between $320,000 and $345,000 each. In 2009, the board awarded the Director Defendants, except O’Connor, $743,700 each in restricted stock units, which brought their annual compensation to between $843,000 and $891,000 each. The annual compensation of the Republic directors far exceeds the annual compensation of the Waste Management directors of between $205,000 and $240,000, except for the non-executive chairman of the board, who was paid $422,000 in 2010. The Director Defendants have paid themselves excessive compensation, which constitutes waste and unjust enrichment and is unreasonable and non-tax-deductible under IRC § 162(a)(1).

36. As the result of the acts of the Individual Defendants, the Company has faced and will continue to face substantial and avoidable income tax liabilities.

37. The Director Defendants have committed waste, and they and the Individual Defendants have enjoyed unjust enrichment.

38. The Company’s stockholders approved the Synergy Incentive Plan (the “Synergy Plan”) at their 2009 annual meeting. The Synergy Plan was to pay incentive awards to officers and employees if the merger of the Company and Allied Waste Industries, Inc., a Delaware corporation (“Allied”), on December 5, 2008, were to achieve synergies of between $100 million and $150 million. As to the performance goal under the Synergy Plan, the Company stated, “There is only one goal: measurable earnings improvement over baseline through cost improvements as a result of the

integration of the two predecessor companies." If the synergies were to amount to $150 million the maximum incentives were to be $15 million for O'Connor, $10 million for Slager, $8 million for Holmes, and $36 million for additional executives and managers, or a total of $69 million. If the synergies were $100 million, the incentive amounts would be 25% of the maximum amounts.

39. The Company has stated that the synergies achieved were $190 million and that it has accrued liabilities of $68.1 million under the Synergy Plan to be paid during the first quarter of 2012.

40. In 2007, the last full year before the merger, Allied had earnings of $309.8 million, and Republic had earnings of $290.2 million, for a total of $600.0 million. In the first nine months of 2008, Allied had earnings of $296.5 million, and Republic had earnings of $205.5 million, for a total of $502.0 million. The Company had earnings of $495.0 million in 2009 and $506.5 million in 2010. There has been no "measurable earnings improvement" at all. The Company should not pay anything under the Synergy Plan.

41. One of the purposes of the annual meeting on May 12, 2011, was a solicitation by the Company's board for the stockholders to approve the covered employees' compensation. Such a resolution was required by 15 U.S.C. § 78n-1. Such stockholder vote is not binding on the Company. 15 U.S.C. § 78n-1(c).

42. The stockholder vote to approve or reject executive compensation is popularly known as say-on-pay. A report from the corporate governance firm Laurel Hill Advisory Group for the week ended January 7, 2011, stated, "The 50% plus of companies surveyed on the question believe a vote of 80% or more in favor of their pay plan is a positive." There was substantial opposition by the Company's stockholders to the say-on-pay proposal. The stockholders submitted proxies well in advance of the meeting and only, approximately, 63% of the votes were being cast in favor. The result of the say-on-pay vote should weigh in favor of the relief that the plaintiff seeks.

43. The plaintiff has not made any demand upon Republic's board of directors to institute this action because demand is excused as futile. Eleven members of the board, a majority, are interested in their own excessive compensation as directors. In addition, all the members of the board are interested because they participate in and are unjustly enriched by the Stock Plan which is unreasonable and non-tax-deductible under IRC § 162(a)(1).

44. Defendant O'Connor is interested in the payment to him of unearned long-term incentive compensation in the amount of $1,250,000 for the period January 1, 2009, through December 31, 2011. Defendant O'Connor is also interested in the payment to him of $1,800,000 for past services for which he has already been fully compensated.

45. The board has made gifts and committed waste in the payments to O'Connor of $1,250,000 and $1,800,000. Those acts are not the product of business judgment.

46. Defendants Slager and O'Connor are interested in the payments to them under the EIP and the awards to them of restricted stock and restricted stock units.

47. A majority of the board has made awards to the Covered Employees of non-tax-deductible restricted stock and restricted stock units. Those awards constitute waste, and they are highly unusual. It would be a simple matter to make awards where the restrictions were performance-based because the Stock Plan already contains provisions for such awards. The board majority's waste and highly unusual conduct excuses demand because they are not the product of business judgment.

48. The proposed payments of incentives under the Synergy Plan contravenes that Plan because the goal of "measurable earnings improvement" was not met. Such payment is not protected by the business judgment rule. Defendants O'Connor and Slager are interested in those payments.

49. Waste and unjust enrichment are not the products of business judgment.

50. Based on substantially similar allegations, the federal court held that the plaintiff raised arguable theories of waste and unjust enrichment in his derivative action. *Seinfeld v. O'Connor*, 774 F. Supp. 2d 660 at p.12 fn.12. The defendants were all parties there, and they are precluded from denying it.

WHEREFORE, plaintiff prays for the following relief:

A. An equitable accounting for the losses sustained by the Company;

B. A mandatory injunction requiring the directors to issue restricted stock and award restricted stock units where the restrictions are performance-based;

C. An injunction against further excessive payments of non-tax-deductible compensation;

D. An injunction against the payment to defendant O'Connor of his full target amount of $1,250,000 and his reward for past services of $1,800,000.

E. An injunction against the payment of "incentives" under the Synergy Plan;

F. Awarding plaintiff the costs and disbursements of this action, including reasonable accountants', experts' and attorneys' fees; and

G. Granting such other, further relief, whether similar or different, as by this Court may be deemed just and proper.

Dated: August 25, 2011

BIGGS and BATTAGLIA

By:/s/Robert Goldberg
Robert D. Goldberg (I.D. No. 631)
921 North Orange Street
Wilmington DE 19899
Tel: 302.655.9677
goldberg@batlaw.com
Attorneys for Plaintiff

Of Counsel
BARRACK, RODOS & BACINE
Alexander Arnold Gershon
Michael A. Toomey

425 Park Avenue – Suite 3100
New York, NY 10022
(212) 688-0782

BARRACK, RODOS & BACINE
Daniel E. Bacine
3300 Two Commerce Square
2001 Market Street
Philadelphia, Pennsylvania 19103
Telephone (215) 963-0600