IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

FRANK DAVID SEINFELD,	:	
	:	
Plaintiff,	:	
	:	
vs.	:	Civil Action
	:	No. 6462-VCG
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.	:	

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Chancery Courtroom No. 12D
New Castle County Courthouse
500 North King Street
Wilmington, Delaware
Thursday, March 29, 2012
1:00 p.m.

- - -

BEFORE: HON. SAM GLASSCOCK, III, Vice Chancellor.

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ORAL ARGUMENT

APPEARANCES:

ROBERT D. GOLDBERG, ESQ.
Biggs & Battaglia
-and-
ALEXANDER ARNOLD GERSHON, ESQ.
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for Plaintiff

ANDRE G. BOUCHARD, ESQ.
Bouchard, Margules & Friedlander, P.A.
-and-
MICHELE ODORIZZI, ESQ.
of the Illinois Bar
Mayer Brown LLP
for Defendant Republic Services, Inc.

DANIEL A. DREISBACH, ESQ.
Richards, Layton & Finger, P.A.
for the Individual Defendants

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THE COURT: Good afternoon.

MR. BOUCHARD: Good afternoon, Your Honor. Andy Bouchard for Republic Services, Inc. I wanted to introduce to the Court my co-counsel, Michele Odorizzi, who will be making the argument for the company, and Mr. Dreisbach will be making the argument for the individual defendants.

THE COURT: Welcome.

MR. GOLDBERG: Good afternoon, Your Honor. Robert Goldberg for the plaintiff, Seinfeld. With me at counsel table is Arnold Gershon, who has been admitted pro hac vice, and will make the argument.

THE COURT: Welcome, Mr. Gershon.

MR. GOLDBERG: And Michael Toomey, his associate.

THE COURT: Welcome.

Are you going to begin then, Miss Odorizzi?

MS. ODORIZZI: Yes, Your Honor. Thank you.

As Mr. Bouchard said, I am going to be arguing on behalf of the company. So I am going to argue the demand futility arguments with respect to

three of plaintiff's claims. Mr. Dreisbach will be arguing the 12(b)(6) motion on behalf of the directors on the claim that they overpaid themselves.

THE COURT: Very well. Thank you.

MS. ODORIZZI: If it please the Court, what I would like to do is just march through the various claims and start with them in the order that they appeared in the reply brief.

The first one is the synergy bonus. And as a point of information, because it's not in the briefs, the synergy bonuses were, in fact, paid.

THE COURT: They have now been paid?

MS. ODORIZZI: They have now been paid. The compensation committee determined that the $150 million target had been exceeded and that it was $180 million of run rate cost savings annually. So they approved the maximum amount of the bonus, which is about $69 million, and that has been paid in February.

Now, plaintiff concedes that the compensation committee and the outside directors, who make up the overwhelming majority of the board here, were not interested at all with respect to the synergy bonuses. They don't receive the bonuses, and there is

no allegation that they are dominated or controlled by anyone who did receive the bonuses. So plaintiff has to rely on the second Aronson prong and show that the decision to pay the bonuses was not a valid business judgment. And plaintiff says that he meets that requirement because the directors misinterpreted the synergy plan. He says that the synergy plan allowed the bonus to be paid only if earnings before incoming taxes, EBIT, was greater after the merger than it had been before the merger.

Now, under Ryan v. Gifford to show a demand futility on the theory that you misinterpreted the provisions of a shareholder approved plan, plaintiff has to show, or allege, particularized facts that would show that the directors knowingly and intentionally violated an expressed provision of the contract. And he can't meet that standard. Because under the synergy plan, under its plain language, you don't look to see whether EBIT was larger after the merger than it had been before the merger. Instead what you are trying to get at is whether, because of these synergy initiatives, your cost savings were such that EBIT is larger than it would have been absent those synergies. So the comparator, the measuring

stick, is not what we didn't pass. It's what you would have done absent those initiatives. And that's not only the plain language of the plan, it's also common sense.

If you look at the plan, it doesn't say that you have these improvements based on other things. It has to be very targeted. It has to be because, for example, you were able to save on head count or you were able to consolidate roots or you were able to consolidate landfills. If you can do that and save money because of that, then it counts. If revenues go down and your top-line revenues go down, and therefore your EBIT goes down because there is a recession in the country and your business goes down, you don't lose the opportunity to get your bonus, if, in fact, you've achieved those cost improvements. By the same token if your top line had gone up because economic conditions had improved, you wouldn't get the bonus just because your top line improved, and you said, "Well, you know, we don't have to do those initiatives anymore." So it's targeted to these things.

Now, in order to meet his burden, I think plaintiff has to show, at a minimum, that his

interpretation is the only interpretation that's reasonable. And his interpretation, we submit, is not even one that is reasonable. The plan isn't ambiguous, but if it had been ambiguous, the plan specifically provides that the compensation committee gets to interpret it in its sole and absolute discretion. So it's the comp committee that ultimately has to make the decision on whether the synergy bonus is payable, not a court. And, therefore, we would say to Your Honor that they just haven't come close to meeting the demand futility standard.

THE COURT: Now, are you saying that no matter how clear it might be that the committee misread the plan, that I am precluded from going beyond the motion-to-dismiss stage by the prescription that they have the sole discretion to interpret it?

MS. ODORIZZI: No.

THE COURT: They can't make a completely nonsensical determination.

MS. ODORIZZI: No, Your Honor.

THE COURT: It has to be one of a number of reasonable alternatives then they can. That's your position.

MS. ODORIZZI: Right. If it's reasonably susceptible to their interpretation, then they are out of court on demand futility action.

THE COURT: If it's ambiguous, then they get to resolve it?

MS. ODORIZZI: They get to resolve it. If they were actually violating the clear and unambiguous terms, then you are into Ryan v. Gifford.

THE COURT: Got it.

MS. ODORIZZI: So that's the synergy bonus.

And the second one, the second claim that plaintiffs have, is a claim that the directors committed waste and breached their fiduciary duties by granting awards of restricted stock to executives that vested over time rather than vesting based on performance, and everyone agrees that when they vest over time that they don't fall within the 162(m) exception. So that if you pay them to a covered employee who makes more than $1 million in non-performance based compensation, they are not tax deductible.

THE COURT: And the board understood that.

MS. ODORIZZI: The board understood that. Absolutely. It's disclosed in the proxy statements. The board has said it has no policy of having all compensation be tax deductible, and this is one element that its chosen not to do that.

Now, on this claim the plaintiff says he meets Aronson's first prong because he says the directors are interested. And he gets to that because these grants were given under the stock plan, and the directors are eligible participants under the stock plan. Now, the cases he cites in support of his notion that they are interested are in opposite here because those cases involve the situation where the plaintiff was challenging the validity of the plan so that the directors' compensation would have been affected had the plaintiffs won. In this case, they're not challenging the validity of the stock plan. Instead, they're challenging one decision that was made under that plan. And that decision was made only with respect to executive compensation.

THE COURT: Did the directors award themselves any time-based bonus?

MS. ODORIZZI: Not under this plan because the directors they did award themselves

restricted stock, and that's what Mr. Dreisbach is going to talk about.

THE COURT: Right. I am talking about under this plan.

MS. ODORIZZI: Yes, it is under this same plan but not when they made this particular decision.

THE COURT: All right. I understand.

MS. ODORIZZI: The decision that is being challenged here on time based versus performance based all goes with respect to executives. And, of course, for directors they are not subject to 162(m) anyway, so for them it doesn't really matter.

Now, plaintiff says in his brief that they have also violated the terms of the stock plan. And what he does is he takes the purpose of the stock plan, which is to incentivize people to maximize the benefits for the company, and he says that only works if you have performance-based compensation. So he says, again, they're violating the terms of the plan by doing time-based vesting. But the problem with that argument is Section 9(b) of the plan specifically says that, again in their sole and absolute discretion, the compensation committee can decide on

what terms and conditions these restricted stock grants can be made and including but not limited to vesting based on time or performance. So I don't think you can say that they acted knowingly and intentionally against the expressed terms of the contract when the expressed terms of the contract permit them to do what they did. So I think that part of it goes off.

And then plaintiff says, "Well, they're not tax deductible, and that's a reason for claiming a breach of fiduciary duty." But that assumes that there is a fiduciary duty to ensure that every payment is deductible, and there is just not. Deductibility is, we absolutely concede, an issue that a compensation committee should take into account when they are making a business judgment, but it's only one of many factors that they have to decide. And they have to balance the question of performance-based vesting versus do you want to give your executives a certain known compensation level that they can count on no matter how the company does, which may or may not be, you know, after all how it does may not be all attributable to their efforts. Some of it may be attributable to simply hard times. So that's a

delicate balance that they have to make, and it's a business judgment.

Here, plaintiff doesn't allege that there was anything wrong with the process. As Your Honor said, they knew this wasn't deductible. There is no claim that they didn't think about it, consider it, take all the factors into account. Instead, plaintiff says, "I don't like the conclusion you came to." He is challenging the merits of the business judgment, and that is something, as Your Honor said in the Goldman Sachs case, that a shareholder can't do through a derivative action. And it doesn't make a difference that he cited three of the 12 peer firms that Republic says in its proxy statement it looks to on executive comp, and he says, "Well, they use mostly performance based." First, it's only three of 12, but even if it was 12 of 12, it's still a business judgment for the board to make, and he hasn't shown demand futility on that issue.

And the third issue that -- his third claim that he has is Mr. O'Connor's retirement agreement. And, again, on that retirement agreement, there is no allegation that the directors -- the outside directors -- are dominated and controlled by

Mr. O'Connor or that they had any personal interest in overpaying him when he retired. So they have to go to the second Aronson prong and say that it wasn't a valid business judgment. Of course, we have two issues here on the retirement agreement. One of them is the payment of his long-term incentive plan award, the LTIP award at target, and there's been a lot of ink spilled in the brief about that. And I think it should be clear from the briefs until 2008 there was a lot of uncertainty over what retirement provisions you could have with respect to somebody who retired in the middle of a performance period and still comply with 182, the IRS Code. And there were two alternatives. One is you could say, "If you retire, you just get the award at target, full amount."

THE COURT: That was the initial position of the IRS.

MS. ODORIZZI: That was the initial position of the IRS. That was okay. That didn't alter the nature of the award as being performance based, and then later on the IRS said, "No, you can't do that. You have to basically wait until the performance period is over, and then you can take -- if it's earned, you can take a pro rata share." So if

you have a three-year period, you retire one year in, you wait until the three years is over. If it's earned, you get one third.

And the IRS in 2008 said, "We are going forward. We are going to go on the pro rata approach. That's the way you have to do it, but we are going to have transition roles, and for award periods that begin on or before January 1, 2009, you can use the old approach. You can pay a target. It's fine. For everything after that, you have to do it on the pro rata approach." That's exactly what Republic did in Mr. O'Connor's 2009 employment agreement, and that carries over into the retirement agreement. And you can see it. He has the 2009 to 2011 paid to target. The 2010 to 2012 paid pro rata. So plaintiff doesn't dispute that it follows the IRS guidelines. What he says is the IRS is wrong. It did something it had no power to do. It's void. He says, "Sooner or later the IRS is going to figure out that it was wrong, and it's going to deny these deductions." Now, it's been four years, and the IRS hasn't changed its mind yet. So we think the likelihood it's going to change its mind is probably slim and none.

But this is not a tax case. It's a

shareholder derivative action, and in a shareholder derivative action, the question is not was the IRS right or wrong, but rather was the board acting rationally to rely on the IRS's guidance. And I think to even ask that question is to answer it. It can't be a violation of a business judgment rule in a tax matter to rely on the guidance the IRS has given through a formal revenue. It just can't.

Now, plaintiff says that this payment of the retirement actually blows the deductibility for the entire executive incentive plan. And that's not -- his theory isn't in his complaint. It's in his brief. But the theory, as I understand it from the brief, is that in some way by paying Mr. O'Connor at target, the comp committee was amending the executive incentive plan, and because they didn't get shareholder approval for the amendment, then he says that blows your treatment under 162 out because you have to have a shareholder approval.

Now, we think that is absolutely wrong because the comp committee never said it was amending the plan. All they did was interpret the plan. And we have gone through in our brief all the steps as to why the interpretation is entirely reasonable giving

the terms of the plan, which specifically allow you to apply different retirement provisions if you have an employment agreement, which they had with Mr. O'Connor. So we don't see any misinterpretation of the plan.

And again, if there is an ambiguity, they have the right to interpret it. But even if it were a misinterpretation of the plan, that wouldn't be an amendment of the plan. It would simply be a mistake with respect to one award. So I don't know -- he can't get from here to there to say that what they've done has caused a cataclysm where you are never going to be able to deduct anything. So, again, on that claim there is just no basis for a shareholder to come in here and challenge the decisions the board has made that have been made based on the IRS's guidance.

THE COURT: To what extent on the motion to dismiss do I need to assume that the cataclysmic result will occur?

MS. ODORIZZI: Well, Your Honor, I don't think you have to assume that it will occur at all. They've not alleged -- again, we are not in a high bleeding standard particularized facts. There is

absolutely nothing alleged to suggest to Your Honor that this is a possible scenario at all, that the IRS has questioned this. The IRS has indicated that if you interpret a plan in a particular way, you have to go tell the shareholders and get new approval. He cited nothing to indicate that the IRS agrees with this interpretation. It's really a figment of the plaintiffs own imagination, and, you know, what is Republic supposed to do now, not claim a deduction? If Republic didn't claim the deductions, some other shareholder will come in and say you are wasting money because you are not claiming deductions that you are entitled to. So I think it's highly unlikely, remote even, but if, at the end of the day it did happen, that still doesn't mean you get to challenge the decision the compensation committee made because the compensation committee made that decision based on the information before it at the time and the question is: Is whether what they did is so irrational that it wasn't a valid business judgment. That's an extremely difficult standard to meet that he just hasn't come close to.

That brings us to the last claim, which is the $1.8 million award, additional award that

Mr. O'Connor was given in his retirement agreement. Now, plaintiff says there is no consideration for that award and that it's waste. In terms of consideration, we think there is consideration for the award and that it shows on the face of the contract because the contract gave him a bundle of rights in return for an agreement that had him retiring on mutually acceptable terms.

THE COURT: But doesn't the same agreement cut out the $1.8 million bonus as apart from that bundle and specifically ascribe to it the rational that it's for past performance?

MS. ODORIZZI: It does say -- it does have a sentence that says we will give you $1.8 million for past services to the company. It does. I don't think that is carving it out or if there is consideration generally for the agreement, it means that it can't be for anything else. I mean, that was the way it was described in the agreement. But still, the entire agreement has consideration, and this is a part of the agreement. Plaintiff doesn't allege, for example, that Mr. O'Connor would have agreed to retire had he not gotten the entire package and retire at the time that everybody wanted him to

retire because he did have leverage. He had an evergreen provision in his employment agreement that enabled him to basically pick when he retired.

THE COURT: What if, instead of saying here is $1.8 million and this is for past performance, he said here is $1.8 million and this is a gift? Would that get them past a motion to dismiss on a waste claim?

MS. ODORIZZI: And they had specifically characterized it as a gift, I think that would get them by the consideration part of it if it was really carved out and said this is a gift.

THE COURT: Even though it discussed earlier in the agreement a bundle of compensation that was being given for the agreement in total?

MS. ODORIZZI: If it was really designated as a gift, I think so.

THE COURT: Well, then why was this any different?

MS. ODORIZZI: Well, I think it's just -- you know, this is in recognition of your long services, which is not -- it's not contrary to the notion that it's also part of the compensation for retiring. I mean those two concepts rub together very

well.

THE COURT: Let's assume that we are going to analyze it on its own.

MS. ODORIZZI: Right.

THE COURT: It said past compensation, the compensation for past service or your long years of service.

MS. ODORIZZI: Right.

THE COURT: How do I evaluate whether that is sufficiently sized and related to the past service to survive a waste claim?

MS. ODORIZZI: Well, I think --

THE COURT: -- at this stage.

MS. ODORIZZI: Right. First of all, you don't look at it through the 12(b)(6) lens of a waste claim. You look at it through the demand futility, where that puts the burden on the plaintiff to allege particularized facts showing that this was not a valid business judgment.

THE COURT: Right. But if you have pled particularized facts sufficient to survive on a motion to dismiss on a waste claim, you are pretty close to the same standard, are you not, to show that the board wasn't using its business judgment in

approving the gift?

MS. ODORIZZI: Except that I think on this one the standard, as Your Honor knows, is that it's not unreasonable given his prior service. So I think they have to allege something to show that it was not unreasonable given his prior service. And that there is, at least, a basis for challenge in the reasonableness of it in light of his prior service. They haven't done that. The complaint is devoid of any allegations about that except to say in a conclusory manner it's not unreasonable given his -- or it is unreasonable in light of what he had been paid before.

I think they have to come up with something where it's their burden at this stage to show that, again, going back to the fact that these directors had no incentive to overpay Mr. O'Connor as he is going out the door. They don't allege that they had any, and it's inconceivable that they had any. So in that situation and given that it's not on its face, it's not the $69 million in the City Group case, for example. It's not huge in the context of the overall compensation. It's their burden to come up with some basis for explaining to Your Honor why there is a

reasonable doubt about whether it was proportional to his past service.

THE COURT: I understand. Anything else?

MS. ODORIZZI: That's all I had, Your Honor.

THE COURT: Before I turn to Mr. Dreisbach, I think I would like to hear from the plaintiffs on those issues that involve the demand futility rule.

MR. GERSHON: Good afternoon, Your Honor.

THE COURT: Good afternoon, Mr. Gershon.

MR. GERSHON: May it please the Court. My name is Arnold Gershon from Barrack, Rodos & Bacine. I represent the plaintiff in this action.

Initially, Your Honor, we had two main points that we wanted to make today. One was that the board action in approving the O'Connor retirement agreement rendered the entire executive incentive plan non-tax deductible, as our complaint alleges, in Paragraph 23, and in addition, it also renders the synergy plan non-tax deductible because the synergy

plan is indeed part of the executive incentive plan.

The other main point we had hoped to present was that under the synergy plan, the management did not achieve its performance goals, and therefore, it was wrong to pay any synergy bonuses under that plan. I gather, however, Your Honor would like to address -- me to address a couple of other points in addition to that.

THE COURT: Well, I am happy to hear whatever presentation you make.

MR. GERSHON: On June 25th, 2010, defendant O'Connor and Republic Services signed his retirement agreement under which the company agreed to pay him a target amount of one and a quarter million dollars that pertained to his three-year performance period beginning at the beginning of January '09 continuing through December 31st, 2011. Now by its terms, that payment under his employment agreement was not earned and not determined to have been earned as an amount of compensation. The company justified this payment by saying, "Well, under Section 5.2 of the executive incentive plan, he would get a pro rata share of that bonus, but under 5.3(ii) of the executive incentive plan, we can make an exception if

there's an employment contract that provides for a different result."

First, there is a footnote to all of this, the concept of paying a pro rata share is not something that comes from the Internal Revenue Service. It is nowhere stated in the Rev. Rul. 2008-13 that an employee who retires in the middle of a performance period is entitled to a pro rata share of what would have been earned if he had stayed the entire period. This is invented by -- it wasn't even invented by Republic Service. I think it comes from a law review article in the Appalachian Law Journal or something like that where it's proposed that this is a way to get through Revenue Rule 2008-13. It does not come through the Internal Revenue Service. It is not in the statute. It is not in the regulation. It is not in the Revenue Rule.

THE COURT: But your argument doesn't depend, at least on the point you are making now, on whether that payment is tax deductible, does it? Your argument depends on whether it has amended the plan with that shareholder approval.

MR. GERSHON: That's correct. That's absolutely right, Your Honor.

THE COURT: So it really doesn't -- I understand there is another argument that does depend on that.

MR. GERSHON: This is just a footnote because I understood my learned friend to say that the Internal Revenue Service proposed that this pro rata rule that appears in the executive incentive plan. I don't think that's where it comes from. What they said was there is an exception under the terms of the plan itself, and that exception is found in Section or Article 5.3(ii) of the executive incentive plan, but that 5.3 only allows changes to Article 5.1 and 5.2 of the executive incentive plan which covers a number of things. It covers, for example, retirement because of disability. It covers termination for cause. Under this 5.3(ii) the committee can make exceptions to the terms of 5.1 and 5.2. What it cannot do is make an exception for Article 4.2 of the executive incentive plan which requires that no bonus be paid unless the performance goals are achieved and the bonus is earned by its terms. Under the terms of his employment agreement, this target amount is unearned. And so to make that change is to make a change in the plan that is not contemplated by 5.3.

Now, it's true that in Article 6.1 of the executive incentive plan, the committee has almost unlimited discretion as to what they can do. And in Part V of 6.1, it can correct any defect; it can supply any omission; and it can reconcile any inconsistency that otherwise exists in the executive incentive plan. And that's what they did here. They have the power to do that. They can indeed provide that there is an omission.

In 5.3, it doesn't cover 4.2, but we can supply that omission now, and that's what they did. The problem with doing it that way for the plan is: That it requires a vote of the stockholders to approve it under -- not only under Section 162(m) but under the terms of the synergy plan itself because the synergy plan provides that it must comply with 162(m) of the Internal Revenue Code. So having taken on this burden, it would be wrong for the committee to make such a substantial change in the terms of the plan without getting stockholder approval. They could have done it because while the agreement provided -- the retirement agreement was signed in June 2010 provided that Mr. O'Connor would retire as of June 1st, 2011. It also provided that they were not going to pay him

until some time between six months after he retired, which would be July 1st, 2011 and December 31, 2011. They had a stockholders meeting in 2011. They could have run that by the stockholders then. There was no reason not to do it.

THE COURT: But you are assuming that is the action the board took and that it decided to amend the EIP by utilizing its power to fill gaps. Why isn't it just the case that it made a mistake about its authority and that it only applies to this one decision and not to void the entire tax deductibility of the shareholder plan through an amendment?

MR. GERSHON: Because now they have done it. The plan is changed forever. They now have a decision that 5.3 can supersede 4.2. It ought to be -- it's something nobody saw -- none of the stockholders saw it, for example, when they approved the plan. It was invisible to everybody what was going to happen here. Nobody knew that Mr. O'Connor was going to retire when they approved the plan. In fact, it looked like he was in for the long pull. All of a sudden, he decides to retire. Why not get that change approved? If this is the way they mean for the

plan to work, why not get it approved? Otherwise, the plan is changed forever. They can't go back -- well, I suppose they could go back and change it again and say, "This time no more changing of 4.2." But they've done it. They've paid compensation under the executive incentive plan.

The harm is done. And the way to fix that harm is either to get -- the best way to fix that harm is to get a stockholder vote approval. They haven't done it. That's what they ought to do. And this is what's happened, whether or not that one and a quarter million dollars is a tax deductible payment, there is some discussion in the briefs as to whether it was tax deductible based among other things whether he was a covered employee at the relevant time. However you come out on that, the plan itself is changed.

The other point I wanted to address was the synergy plan. The synergy plan, when we first addressed it in the federal action, we argued that the synergy plan was so complicated that nobody could understand it, much less would it comply with Section 126(m). Not only does it have a laundry list of possible things to consider, it has a phrase to catch

everything and any other thing we may think of that may help here. So it's an open-ended opaque plan that nobody could understand. What our learned friend said about that in their reply brief in the federal action was that there is only one synergy goal, measurable earnings improvement over baseline through cost improvement.

THE COURT: Why should I care about what they represented unless you are claiming that they're estopped from arguing something else here?

MR. GERSHON: This is the history of how we got where we were. We said, "The plan is complicated, and nobody can understand it." They said, "Oh, it's very simple."

THE COURT: All right.

MR. GERSHON: Earnings.

THE COURT: But what is it? Is it simple or is it complicated?

MR. GERSHON: It's really complicated.

THE COURT: If it's really complicated, how can it be waste to hand out bonuses under the plan? Isn't that within their -- the boards business judgment to try to exercise its business judgment to apply the plan?

MR. GERSHON: Well, first of all, the plan has to be objective and definite.

THE COURT: You are talking about for tax purposes?

MR. GERSHON: I am talking about for plan purposes too. Because the plan itself says that the plan must comply with Section 162(m). That's a term of the synergy plan. It's in Article 1.

THE COURT: I am just trying to see what the breach of duty is that you are claiming with respect to this very complicated plan and the boards administration of it.

MR. GERSHON: Well, if we take the statements that -- the judicial statements of the defendants that it's based on earnings improvement, it fails. If we take their second statement that it's not based on earnings, it's based on earnings before income and taxes, it fails there too. From everything that appears in the public record and from everything that the company has said about this synergy plan, which is not much, there is no way to assume that there was any synergy improvement at all here.

THE COURT: How do I know that?

MR. GERSHON: Because they don't show

it.

THE COURT: How is it their burden to show it?

MR. GERSHON: Because they foisted this plan onto the stockholders, and they say, "Don't you worry about a thing. This money has been earned." And they can't explain it. They can't explain it. They couldn't explain it in the Federal Court. They couldn't explain it here. There is no way to know what they are paying -- we know what they are paying, but there is no reason to know why they are paying it.

THE COURT: Mr. Gershon, was there a books and records request to get the board minutes to explain why the board decided that these bonuses had been earned under the synergy plan?

MR. GERSHON: No, there was not.

THE COURT: I am struggling to know why I would assume that they've made a mistake in computing the bonuses under the synergy plan.

MR. GERSHON: Because they cannot explain what they have done. If it were a simple matter to explain it, you would see it.

THE COURT: It's not their burden to explain it, is it?

MR. GERSHON: I think it is.

THE COURT: How is that? Explain that to me.

MR. GERSHON: That's because they have a plan and they say we have achieved earnings -- we have achieved EBIT improvement here without saying how they've done it. Having said just enough, they should be required to say something about what they have done here, and the fact that they are unable to say what they have done or unable to explain what this amount is, the presumption should arise. It is the goals have not been achieved.

THE COURT: Just so I am clear. I want to make sure I understand you. An independent unconflicted board, administering a plan that makes a decision that goals have been met in connection with their plan in connection with a derivative suit brought to challenge that determination, has the burden at this stage of the proceedings to show that they have not made an error and that they are -- in fact, those bonuses were earned.

MR. GERSHON: Let's go back to what Your Honor has just said. It's true that there is a committee that administers this plan. The committee

itself does not sit down with numbers and decide what's in and what's out. In fact, what happens is people working at the company who report to the people who are going to get bonuses sit down and do the actual calculations, if calculations are done at all. And they present a report that says the bonuses have been earned. In fact, they have been more than earned. In fact, we were only looking to get $150 million in synergies and we have $180 or $190 -- whatever the correct number is -- million. If there were a report that provided those numbers so that the committee could actually make a judgment, we'd see that report now. Because right now the company is in a position of having tried to explain this plan three different ways, none of which works. It's true we could sit down and spend a year on a books and records case to get it, but it shouldn't be required under these circumstances where you have a plan that on its face nobody can understand.

THE COURT: All right. I understand the argument.

MR. GERSHON: Okay. One or two other points to make. The stock plan provides, as a purpose of the plan, that it is to encourage maximum effort by

whoever participates in the plan. Now, who participates in the plan, employees and non-employee directors, and if an employee is also a director, he participates in the stock plan too. As the defendants opening brief says, time-based restricted stock does not provide as good an incentive as performance-based restrictive stock.

THE COURT: Isn't that a decision quintessentially for the board of directors to determine whether it's better to have a plan which will incentivize employees to stay and give their efforts in a down turn in the economy or whether it's better to have it tied to performance so that they strive to meet them? Isn't that the kind of decision the board has to make? Why would I make that decision?

MR. GERSHON: Because they didn't rank any performance-based stock at all here.

THE COURT: They made a decision that time based was more appropriate based on their analysis. Why do I go beyond that?

MR. GERSHON: Well because they, themselves, say in their brief that time based is not as powerful an incentive as performance based. Now,

you can have a performance-based stock.

THE COURT: Why do you think they did it then? Why would they do -- why would they pick a bonus plan that was less effective than another one that was available and tax deductible when they clearly knew those facts?

MR. GERSHON: They treat themselves the same way. The directors are participants in the stock plan. They're subject to the same constraints as everybody else. They didn't treat the employees under the more onerous standard of a performance-based plan, performance-based stock because they didn't treat themselves that way. They were treating themselves exactly the way they are treating the officers.

THE COURT: So is the theory that to mask the fact that they weren't holding themselves to this standard and the inappropriateness of that, they bestowed the same inappropriate standard on the employees?

MR. GERSHON: That's pretty good, Your Honor.

THE COURT: I am struggling a little bit.

MR. GERSHON: I see, but I think that's the explanation. They pass a plan seeking maximum effort among other things. They don't give any performance-based stock, none at all. Something is wrong.

THE COURT: But they could, if they wished, give themselves, and we will talk about this later about whether they have a burden to show that it's entirely fair, but they could give themselves time-based bonuses and give the employees performance-based bonuses, could they not? They could have done that. So what's the theory for why they had to give the employees time-based bonuses in order to give themselves time-based bonuses?

MR. GERSHON: This is what they did. There is only so far we can go with guessing with their motivation of doing stuff.

THE COURT: Right. But you have to plead facts that allow me to draw an inference.

MR. GERSHON: The fact is that there peers give a lot of performance-based stock. Now, they say we cherrypicked three companies, but we didn't cherrypick them all by ourselves. We picked them from their list of peers, and we didn't.

THE COURT: What did the other nine do?

MR. GERSHON: Don't know.

THE COURT: You didn't check those?

MR. GERSHON: No.

THE COURT: All right. That's fair enough.

MR. GERSHON: We picked three, and they seemed to be giving a lot of performance-based stock. Now, this plan, the stock plan, is a little unusual from all the stock plans that I have looked at in that it requires as a purpose maximum effort. You don't see that very often in incentive plans. You say they have language, like, well stock plan -- the purpose of this bonus plan, the stock plan is to incentivize or to attract able personnel or to give participants an ownership interest in the company. This goes farther. This plan goes to the point of saying we want maximum effort from our people and that means us to, the directors. We include ourselves in that. Under those particularized facts, it's our position that indeed some amount of performance-based stock should be granted here instead of resorting entirely to the less incentivizing time-based stock.

THE COURT: Thank you, Mr. Gershon. I understand.

MR. GERSHON: One more point about the $1.8 million. It's clearly from past consideration in the cases that have addressed this. I think it may be in the Coca-Cola case. I think this Court analogized or maybe expressly stated that a payment for past services for which compensation has been paid is, in essence, a gift and for that reason is presumptively wrong. And while there are two exceptions to it, our position is that in a normal course of events when there is a rule followed by exceptions, we allege the breach of the rule, and it's a defense not an affirmative burden to plead that the exceptions haven't been met either is our position on that.

THE COURT: All right. I understand that. Thank you for your argument, Mr. Gershon.

Miss Odorizzi, if you wish to make a brief rebuttal, then I will turn to Mr. Dreisbach.

MS. ODORIZZI: Just a couple of things --

THE COURT: Am I pronouncing your name correctly?

MS. ODORIZZI: Odorizzi; Odorizzi;

it's all good.

THE COURT: I will do my best. I am not sure I can pick one or the other. I don't seem to have the capability to learn it, but I apologize.

MS. ODORIZZI: One of the things about the compensation hearing is that there is plenty of performance-based compensation for Republic's executive officers. There is the EIP. There's the synergy plan, which was a one-time deal. Under the stock plan, they're also granted stock options at fair market value. Those are performance based by definition. And, yes, we said that there's, you know, in our brief that if you have a time based, there is a little less tie to the immediate performance, but there is certainly long-term performance tie of giving anyone stock.

THE COURT: I think I understand that.

MS. ODORIZZI: Yes. And I think the only other thing I would say is Mr. Gershon said that it was invisible to everybody, the interpretation of the retirement provisions of the plan. But when the plan was approved in 2009, the very same proxy statement had a description of Mr. O'Connor's employment agreement and specifically explained how

the retirement provisions worked. So the interpretation at that time was already in place. That that was appropriate. It's not when they paid that is the relevant fact. It's when they entered into the agreement that had a retirement provision that enabled him to get a payment at target before -- for periods that began 2009 or earlier.

THE COURT: All right.

MS. ODORIZZI: Thank you, Your Honor.

THE COURT: Before you step down, what do you make of Mr. Gershon's argument, and he hasn't capsuled it as an estoppel argument or judicial estoppel, but that the company and the board in the District Court action made a representation that the synergy plan would award bonuses based on revenue solely?

MS. ODORIZZI: Based on -- what we said is based on earnings as impacted by the costs. I don't think what we said in that case was any different than what we are saying here that you look at the impact on EBIT -- earnings, EBIT, whatever you want to call them -- but you look at the impact due to the cost savings. We never said that we had to have more today than we had before the merger. We never

said that.

THE COURT: I understand that. Thank you.

MS. ODORIZZI: Thank you.

THE COURT: Mr. Dreisbach, did you wish to make your argument now? You have been very patient with us.

MR. DREISBACH: I would. Good afternoon, Your Honor.

THE COURT: Good afternoon.

MR. DREISBACH: Dan Dreisbach from Richards, Layton & Finger on behalf of the individual defendants. I rise solely to address our claim to dismiss under Rule 12(b)(6) the claim asserted against the non-director -- I'm sorry -- non-employee directors for excessive fees paid to them, which is accused by my dear friend of being waste. These claims are found solely in Paragraphs 34 to 37 of the amended derivative complaint. I pause to note that this is the amended complaint, and under 15(aaa) this means this is their best shot. The allegations are slight with respect to this claim contained in the half-page of the complaint.

THE COURT: I don't mean to interrupt

you, but they really turn, do they not, on whether the entire fairness analysis applies? If that applies, that's enough to get by a motion to dismiss. If it doesn't apply, then they're, I think, in some significant difficulty here.

MR. DREISBACH: Your Honor, I think that is certainly where they are going. And I can turn to that immediately. The entire fairness is alleged to be the standard to be applied based upon one case, National Auto Credit. In that case, Vice Chancellor Noble decided that entire fairness applied. It was a very different circumstance than here. There, there was a bunch of back scratching going on. There was an approval of an agreement called the zoomlot agreement, which provided the Chairman and chief executive officer, Mr. McNamara, with shelter for his stock and also consolidated his control of NAC. In exchange for the agreement of the directors to approve that agreement, the directors received large fees, both for past services and for future services. Based upon that scenario, the Court said this is different. It wasn't pursuant to a plan or anything like that. This was something different where there was this back scratching going on.

THE COURT: What if the plan simply said the board in its discretion shall set it's own compensation bonuses, and they exercise that discretion and give themselves bonuses, is that a self-dealing transaction that requires entire fairness?

MR. DREISBACH: I think it's a little different, Your Honor, because it wasn't a shareholder approved plan in that circumstance.

THE COURT: Well, there is. It simply says apply your discretion. Is that a situation where, despite the shareholder approved plan, the board would have to demonstrate entire fairness because it's engaged in self-dealing?

MR. DREISBACH: I don't believe so, Your Honor, because the stockholders set parameters of the plan and said to the directors, "You may set your own compensation based upon your own discretion."

THE COURT: So in that point, they have no duty to the shareholders other than, I suppose, to be informed as to what they're doing and what impact it will have. There's no more duty in that self-dealing transaction simply because the shareholders have said use your discretion.

MR. DREISBACH: I am not sure it's unlimited, Your Honor.

THE COURT: It seems to me -- I don't mean to interrupt you. It seems to me for a shareholder plan that allows the board to act in a self-dealing way or to benefit itself, it has to provide some guidance to the board in order for it to escape entire fairness, does it not? It can't be just do whatever you like.

MR. DREISBACH: Well, that's not the plan that we --

THE COURT: Why don't you describe for me what limits on the boards action there were in this particular plan, that would be helpful I think?

I'm sorry, Mr. Dreisbach. I will certainly let you conduct your argument. I don't mean to be quite so bossy, but I am interested in this particular point. It will be helpful to me.

MR. DREISBACH: Yes, sir. I may need to dig that up. I thought I had it clipped, but there are certainly limits on the board's ability to grant options. As you might suspect, they're not within a very narrow range or fairly broad range. I believe it was up the dollar value of $4 million or something

like that. Obviously, these don't reach anywhere near that level.

THE COURT: But they were given limits on what they could do?

MR. DREISBACH: They certainly were, Your Honor. There is no challenge either to the adoption of the plan itself or that these awards were outside the terms of the plan. I think the then-Vice Chancellor Steele's decision in 3Com tells us that if there is a plan that's not challenged and the awards are within the plan, it's business judgment subject to the waste standard. And I think it's a very difficult burden to meet. They don't even attempt to do that in their complaint. In the four or five paragraphs, there is no allegation of gift. There is no allegation that Republic did not receive any consideration for the services, nothing of the kind. Perhaps, the limit is judicially a shocking disparity between the services provided and the payment rendered. We are not even close to that. The only thing that they allege is they allege that Waste Management, one of the 12 peer companies -- paid its directors in 2010 compensation which I believe maxed out at $405,000.

THE COURT: Just so we are clear -- I am sorry to interrupt you.

MR. DREISBACH: Sure.

THE COURT: I think I understand pretty well the waste standard. What I am struggling with a little bit is how I apply Vice Chancellor Steele's decision and what discretion the shareholders can provide to the board and still avoid a self-dealing transaction or the effects of a self-dealing transaction. As I've said, at least as I preliminarily view it, if the plan says, "Just use your discretion. The sky is the limit, board." That's probably not going to get you out of a self-dealing transaction. If the stock price exceeds $10, you get a million dollars. That's obviously mechanical. So where are we on that spectrum, if indeed you believe there is a spectrum. You may believe that the sky is the limit is sufficient, but I would have trouble with that standard.

MR. DREISBACH: Your Honor, I am not here advocating that standard is appropriate. Although, it may be in the certain case where the stockholders are fully informed, are told, "Hey, listen. What you are doing is giving the directors

unlimited authority to provide compensation for themselves." Here, there again was no challenge to the disclosures in connection with the approval of the plan. What the limits are of that, I can't tell you. Perhaps the courts will tell us one day, but as far as we know from what the courts decisions have told us to date, that if there is an approved plan, there is no challenge to the terms of the plan. It's business judgment subject to the waste standard which is a very onerous burden to meet.

THE COURT: I am sorry. I have interrupted you.

MR. DREISBACH: No. No. It's quite all right.

THE COURT: In this plan, you told me there is a financial cap, and the board is below the financial cap. Are there other -- I probably should know this already. I apologize, Mr. Dreisbach. But if you could help me out, are there other limitations on the boards freedom of acts in setting its own bonuses?

MR. DREISBACH: Your Honor, I closed the book on the plan. My understanding is there is a dollar limit and a share limit imposed in the plan for

the awards the directors get.

THE COURT: That's very helpful. I appreciate that.

MR. DREISBACH: I can get you the cite in just a minute.

THE COURT: All right. Anything else?

MR. DREISBACH: No, Your Honor, unless Your Honor has anymore questions.

THE COURT: No, you've addressed my questions. I appreciate it. I am sorry to have interrupted you so many times. It was very helpful to me.

MR. DREISBACH: I would rather have it that way.

THE COURT: Thank you.

Did you wish to give a presentation on that issue, Mr. Gershon?

MR. GERSHON: Thank you, Your Honor.

The stock plan provides that there is a limit to the amount of stock that can be granted as performance shares restricted stock and awards of common stock to any eligible individual during any one fiscal year, and that appears on Page A-7 of the stock plan, which is Exhibit D to the defendants motion to

dismiss, and in Article 6(a)(iii), it says that limit is 1,250,000 shares. Now the price of Republic stock during that period was, I think, in the mid 20s or something like that. So what we are talking about is the directors, according to their argument, under Vice Chancellor Steele's decision would be giving themselves perhaps $30 million a year. That's pretty high. It's not as high as the $90 million maximum in Chief Judge Sleet's decision in Resnik against Woertz last year. But it's pretty high. And in fact, our argument is that it's so high that it's shocking that they should be allowed to give themselves that much and to have such a maximum apply even if they're only giving themselves $800,000 worth of stock in a year that that grant ought to be subject to an entire fairness analysis because this maximum is so high that it doesn't function as a maximum at all.

THE COURT: I understand the argument.

MR. GERSHON: Okay.

THE COURT: Anything else?

MR. GERSHON: No, Your Honor.

THE COURT: I appreciate, counsel, the concise way you have presented things. The briefing was very complete. And it didn't need to be

completely repeated here, and I appreciate you not doing that and sticking to the points that you thought were important. I also appreciate your forbearance with me and your willingness to engage in those areas that were helpful to me. Particularly, Mr. Dreisbach, whom I'm afraid I was a little rude, and I apologize if I was. I didn't mean to be. Some very interesting issues. I appreciate the presentations, and I will try to get you something promptly.

Is there anything else we can profitably do this afternoon?

MR. DREISBACH: No, Your Honor.

MR. GERSHON: No, Your Honor.

THE COURT: Thank you. I enjoyed the argument.

MS. ODORIZZI: Thank you, Your Honor.

(Hearing adjourned at 2:05 p.m.)

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CERTIFICATE

I, CHRISTINE L. QUINN, Official Court Reporter for the Court of Chancery of the State of Delaware, do hereby certify that the foregoing pages numbered 3 through 50 contain a true and correct transcription of the proceedings as stenographically reported by me at the hearing in the above cause before the Vice Chancellor of the State of Delaware, on the date therein indicated.

IN WITNESS WHEREOF I have hereunto set my hand this 11th day of April, 2012.

/s/ Christine L. Quinn

Official Court Reporter
of the Chancery Court
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