UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF OHIO

NECA-IBEW PENSION FUND (THE DECATUR PLAN), Derivatively on Behalf of CINCINNATI BELL INC. Plaintiff, vs. PHILLIP R. COX, et al., Defendants, – and – CINCINNATI BELL INC., an Ohio corporation, Nominal Party.	No. 1:11-cv-00451-SSB-JGW

NOTICE OF MOTION AND MOTION AND MEMORANDUM FOR PRELIMINARY INJUNCTION FREEZING THE 2010 EXECUTIVE PAY INCREASES

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Plaintiffs move for a preliminary injunction to maintain the status quo pending a final resolution on the merits. A preliminary injunction should issue because plaintiffs have shown a likelihood of success on the merits and the balance of hardships weighs in its favor. This motion is supported by the following Memorandum.

I. INTRODUCTION

This is a shareholders derivative action on behalf of Cincinnati Bell Inc., against the majority of its board of directors for breaching their fiduciary duty of loyalty by paying excessive compensation that was not in the shareholders' best interests. This motion requests an injunction – to maintain the *status quo* – and freeze certain pay increases that were not in Cincinnati Bell shareholders best interest. As detailed below, plaintiffs have demonstrated a likelihood of success on the merits and that the balance of hardships weigh in their favor.

In 2010, Cincinnati Bell suffered a 68.4% decline in net income and a negative 18.8% annual shareholder return. Its earnings per share also declined 75.7%. But Cincinnati Bell's top executives received pay raises between 54.3% and 80.3%. The Cincinnati Bell board professed to follow a strict pay-for-performance executive compensation policy, designed to reward Cincinnati Bell's executives for superior performance and to have consequences for underperformance. Thus, the 2010 executive compensation approved by the Cincinnati Bell board – rewarding corporate managers for underperformance – was in direct violation of the Cincinnati Bell board's internal pay-for-performance executive compensation policy. Making the Board's decision even more egregious was the fact that the majority of Cincinnati Bell voting shareholders voted against the Board's recommendation to financially reward Company executives whose stewardship in 2010 contributed to such a poor year for the Company.

To maintain the *status quo* in light of the Board's decision to grant Cincinnati Bell executives outrageous pay raises for 2010 – despite the Company's undeniably poor financial performance in

2010 – plaintiffs request the Court enter a preliminary injunction: (1) enjoining the Cincinnati Bell Board from effectuating the 2010 executive compensation plan; and (2) placing the amount of increased compensation into a constructive, interest-bearing trust.

II. FACTUAL BACKGROUND

This is a failed-say-on-pay shareholders' derivative suit on behalf of nominal party Cincinnati Bell Engineering Group Inc. ("Cincinnati Bell" or the "Company") against the majority of the Cincinnati Bell Board of Directors, namely defendants Phillip R. Cox, Bruce L. Byrnes, Jakki L. Haussler, Craig F. Maier, Alex Shumate, Lynn A. Wentworth and John M. Zrno (together, "Cincinnati Bell Board"); Cincinnati Bell's top executives, namely defendants John F. Cassidy (Cincinnati Bell's President and Chief Executive Officer ("CEO")), Gary J. Wojtaszek and Christopher J. Wilson; and Cincinnati Bell's compensation consultant, defendant Towers Watson & Co.

The factual allegations of the Complaint are straightforward, and unlike in most lawsuits, largely admitted or otherwise uncontestable. Stated as concisely as possible, the Cincinnati Bell Board told shareholders that it approved executive compensation on a pay-for-performance basis, but, in fact, did not. As a result, Cincinnati Bell's top executives received pay increases between 54.3% and 80.3% – including a 71.7% raise for Cincinnati Bell's CEO – despite the Company's dismal financial results. ¶¶2; 27-31.[1] In 2010, Cincinnati Bell' business declined and the Company posted some of its worst financial results in recent years. ¶¶28-29. For example, in 2010, Cincinnati Bell posted a $61.3 million decline in net income and a negative 18.8% annual shareholder return. *Id*. And, the Company's 2010 net income applicable to common shareowners, earnings per share

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[1] All references to "¶__" herein are to the Verified Shareholder Derivative Complaint filed July 5, 2011.

("EPS"), and total shareholders' equity also all materially declined. *Id*. Thus, under any commonly understood definition of pay-for-performance, the Cincinnati Bell Board clearly departed from their own internal pay-for-performance executive compensation policy by approving substantial pay raises for Cincinnati Bell's CEO and top executives in 2010.

Whether the 2010 executive compensation is in the best interest of Cincinnati Bell shareholders is ***not*** a disputed issue in this case. The Cincinnati Bell shareholders have already voted upon whether they think, in their own independent business judgment, the 2010 CEO and top executive pay hikes are in their best interest as shareholders, owners, and resoundingly concluded that the answer is "no." More specifically, in the Company's first-ever say-on-pay advisory vote on May 3, 2011, 66% of voting Cincinnati Bell shareholders rejected the 2010 executive compensation as not serving the best interest of shareholders. ¶35.

The say-on-pay vote under the newly enacted Dodd-Frank law did not alter the fiduciary duties of corporate directors relative to the payment of executive compensation, and plaintiffs do not contend otherwise. But the Dodd-Frank Act did provide a mechanism for courts (and litigants alike) to objectively evaluate whether executive compensation is, in fact, in the best interest of shareholders. And, this is precisely what Congress intended when it enacted the say-on-pay provisions of the Dodd-Frank Act, *i.e.*, that the say-on-pay advisory votes serve as a referendum on whether executive compensation is in the best interest of shareholders. *See* S. Rep. No. 111-176, at 133-34 (2010). Thus, the adverse Cincinnati Bell say-on-pay vote is probative, if not the best evidence, of the fact that, in the view of Cincinnati Bell shareholders, the 2010 CEO and top executives pay hikes are not in their best interest as Cincinnati Bell shareholders.

It is axiomatic under Ohio law, Cincinnati Bell's state of incorporation, that directors owe the corporation an unremitting duty of loyalty that requires them to at all times put the best interests of shareholders ahead of their own interest and the interests of third parties, including corporate

managers. Directors who failed to act in the best interest of shareholders are not eligible for business judgment protection, because to qualify for such protection the directors' decision must serve the best interest of shareholders. Here, the adverse Cincinnati Bell say-on-pay vote is direct evidence that the Cincinnati Bell Board's 2010 executive compensation is not in the best interest of Cincinnati Bell shareholders. Accordingly, plaintiffs have stated an actionable claim for breach of loyalty against the Cincinnati Bell Board for which they are not entitled to business judgment protection, at least not at the pleading and/or summary judgment stage. *See In re Nat'l Century Fin. Enters., Inv. Litig.*, 504 F. Supp. 2d 287, 312 (S.D. Ohio 2007); *see also Ryan v. Gifford*, 918 A.2d 341, 357 (Del. Ch. 2007).[2]

Taken as true, the factual allegations of the Complaint demonstrate not only that plaintiffs have pleaded facts that successfully rebut the presumption of business judgment associated with the Cincinnati Bell Board's 2010 executive compensation decisions, but also that the Cincinnati Bell Board is *prima facie* liable for breach of loyalty. Directors who are *prima facie* liable also face a substantial likelihood of liability under Ohio law; and therefore, a pre-suit demand upon the Cincinnati Bell Board is excused as futile. *Ferro*, 511 F.3d at 617-18 ("'Ohio courts have found a demand presumptively futile "where the directors are antagonistic, adversely interested, or involved in the transactions attacked."'").

As previously mentioned, the vast majority of the operative facts in this litigation are admitted, *i.e.*, come directly from Cincinnati Bell's SEC filings, and/or are not legitimately contestable. These most relevant facts include:

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[2] Even when the derivative claims are brought under federal law, the Court applies the substantive law of the state of incorporation, here Ohio. *See, e.g.*, *In re Ferro Corp. Derivative Litig.*, 511 F.3d 611, 617 (6th Cir. 2008). "Ohio courts routinely look to Delaware case law for guidance in deciding corporate law issues generally, and demand futility issues specifically." *In re Keithley Instruments, Inc.*, 599 F. Supp. 2d 875, 888 n.10 (N.D. Ohio 2008)

1. Cincinnati Bell is an Ohio corporation and therefore its internal affairs, including whether the Cincinnati Bell Board acted in the best interest of shareholders when increasing CEO and top executive pay in 2010, despite the fact that in 2010 Cincinnati Bell suffered a 68.4% decline in net income, are governed by Ohio law. ¶37.

2. The Cincinnati Bell Board voluntarily adopted pay-for-performance for its executive compensation philosophy, and represented to Cincinnati Bell shareholders that it's executive compensation system is designed to link executive pay with corporate performance by rewarding executives for superior performance and having consequences for underperformance. ¶27.

3. Cincinnati Bell's shareholder base consists primarily of sophisticated institutional investors, such as Peninsula Capital Advisors LLC, Wells Capital Management Inc., and the Government Pension Fund of Norway that own millions of Cincinnati Bell's shares worth tens of millions of dollars. ¶34.[3] These types of sophisticated institutional interests have experience in and the resources to independently evaluate whether executive compensation is in their best interests as shareholders, owners of Cincinnati Bell.

4. Cincinnati Bell's institutional shareholders have financial interests in Cincinnati Bell that typically are significantly larger than the individual and/or collective financial interests of the Cincinnati Bell Board and/or its corporate managers.

5. In connection with Cincinnati Bell's say-on-pay advisory vote, the Cincinnati Bell Board unanimously recommended shareholder approval of the 2010 executive compensation in the Proxy Statement, dated December 17, 2010. ¶32.

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[3] *See also* http://investors.morningstar.com/ownership/shareholders-major.html?t=CBB (listing Cincinnati Bell's largest shareholders).

6. In connection with Cincinnati Bell's say-on-pay advisory vote, the Cincinnati Bell Board set forth all of the material factors that it considered and led it to conclude that increasing CEO and top executive pay in 2010 was consistent with Cincinnati Bell's pay-for-performance executive compensation policy, and, most importantly, in the best interests of Cincinnati Bell shareholders. ¶¶32-33.

7. On May 3, 2011, Cincinnati Bell conducted its annual shareholder meeting and during that meeting shareholders voted upon the Cincinnati Bell Board's 2010 executive compensation in the Company's first-ever say-on-pay advisory vote. ¶35.

8. On May 9, 2011, Cincinnati Bell reported the final results of the say-on-pay advisory vote in a Form 8-K filed with the SEC, and that Form 8-K reported that 96,939,788 shares voted against the Cincinnati Bell Board's 2010 executive compensation proposal, or approximately 66%. *See* Cincinnati Bell Form 8-K (May 9, 2011).

9. Since the adverse Cincinnati Bell say-on-pay vote, the Cincinnati Bell Board has not publicly reported in a filing with the SEC that the 2010 executive compensation has been or will be rescinded or otherwise modified.

Taken as true, as they must be at this stage of the pleadings, plaintiffs have presented facts that demonstrate they have a strong likelihood of success on the merits. Not only do the particularized facts pleaded in the complaint excuse a pre-suit demand upon the Cincinnati Bell Board because such a demand is a useless and futile act as a matter of law, the particularized facts pleaded in the complaint also state an actionable claim against the Cincinnati Bell Board for breach of loyalty by pleading direct evidence, *i.e.*, ***the conclusion of Cincinnati Bell shareholders, that the Cincinnati Bell Board's 2010 executive compensation is not in the best interest of Cincinnati Bell shareholders***, and therefore not eligible for business judgment protection.

But, if defendants are permitted to dissipate the fruits of their misconduct and unjust enrichment, Cincinnati Bell's ability to be fully compensated for the harm to its business and shareholder democracy will be irreparably harmed. Therefore, plaintiffs respectfully request that their motion for a preliminary injunction, to maintain the *status quo* by placing a freeze order upon the excessive 2010 executive compensation for the duration of this litigation be granted in full.

III. RELIEF SOUGHT

This motion is necessitated in order to maintain the *status quo* and avoid an unwarranted depletion of Company assets. Accordingly, plaintiffs respectfully move this Court for an order: (1) placing a freeze order upon the excessive 2010 executive compensation for the duration of this litigation; and (2) placing the amount of increased compensation into a constructive, interest-bearing trust. Immediate equitable relief is necessary to protect Cincinnati Bell shareholders because the executives' excessive compensation will be extremely difficult – if not impossible – for Cincinnati Bell to recover should the executives act to hide and/or dissipate the excessive compensation they have received and continue to receive.

IV. ARGUMENT

A. The Legal Standards Applicable to the Issuance of a Preliminary Injunction

A court may issue a preliminary injunction to preserve the status quo pending a determination of the action on its merits. *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 290 (1940) (upholding preliminary injunction in order to maintain status quo); *Stenberg v. Cheker Oil Co.*, 573 F.2d 921, 925 (6th Cir. 1978) ("'[T]he purpose of a preliminary injunction is to preserve the status quo.'"). When considering a motion for preliminary injunctive relief, courts consider: (1) whether the movant has a strong likelihood of success on the merits; (2) whether the movant would suffer irreparable injury without the injunction; (3) whether issuance of the injunction would cause substantial harm to others; and (4) whether the public interest would be served by issuance of the

injunction. *Hunter v. Hamilton Cnty. Bd. of Elections*, 635 F.3d 219, 233 (6th Cir. 2011). These four considerations are factors the court should balance, not prerequisites that the moving party must meet. *Certified Restoration Dry Cleaning Network, L.L.C. v. Tenke Corp.*, 511 F.3d 535, 542 (6th Cir. 2007) (reversing decision not to grant preliminary injunction). A district court need not make findings as to each of the four factors if fewer factors determine the issue. *Id.*

As the Supreme Court has stated, "'[t]he purpose of a preliminary injunction is merely to preserve the relative positions of the parties until a trial on the merits can be held.'" *Six Clinics Holding Corp., II v. Cafcomp Sys.*, 119 F.3d 393, 400 (6th Cir. 1997) (quoting *Univ. of Tex. v. Camenisch*, 451 U.S. 390, 395 (1981)). Given this limited purpose, a preliminary injunction is customarily granted on the basis of procedures less formal and evidence less complete than a trial on the merits. *Id.* Thus, a party is not required to prove his case in full at a preliminary-injunction hearing. *Id.*

B. The Court Should Issue a Preliminary Injunction

1. There Is a Substantial Likelihood that Plaintiffs Will Succeed on the Merits

a. Overview of Plaintiffs' Claim and the Relevant Law

To demonstrate a likelihood of success on the merits, plaintiffs need only show that a pre-suit demand upon the Cincinnati Bell Board would have been futile and that the Cincinnati Bell Board breached its duty of loyalty by approving the 2010 executive pay hikes. *Grobow v. Perot*, 539 A.2d 180, 186 (Del. 1988); *Aronson v. Lewis*, 473 A.2d 805, 814 (Del. 1984).[4] Whether plaintiffs have

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[4] As previously noted, "Ohio courts routinely look to Delaware case law for guidance in deciding corporate law issues generally, and demand futility issues specifically. . . . Accordingly, the Court refers often to such authorities, and treats those cases as highly persuasive." *Keithley*, 599 F. Supp. 2d at 888 n.10. *See also In re Gen. Tire & Rubber Co. Sec. Litig.*, 726 F.2d 1075, 1082 (6th Cir. 1984) ("The inapplicability of federal law and the paucity of controlling Ohio law on the scope

satisfied both of these conditions, in turn, depends solely upon whether the particularized facts pleaded in the Complaint are sufficient to rebut the rebuttable presumption of business judgment traditionally afforded by courts to the pay decisions of boards of directors. *See In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27 (Del. 2006).

Under Ohio (and Delaware) law the business judgment rule protects directors from second-guessing by courts, ***but only if the directors acted in the best interest of shareholders***. *See, e.g.*, *Marsalis v. Wilson*, 149 Ohio App. 3d 637, 641 (Ohio Ct. App. 2002); *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 36-37 (2010). Therefore, to qualify for business judgment protection, it is essential that directors at all times put the best interests of shareholders ahead of their own interests and the interests of third parties, including corporate managers. *See, e.g.*, *Cede & Co. v. Technicolor, Inc*., 634 A.2d 345, 360 (Del. 1993) ("In exercising [business judgment], directors are charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders."); *Crescent/Mach I Partners, L.P. v. Turner*, 846 A.2d 963, 982-83 (Del. Ch. 2000).

Here, the short answer to the critical business judgment question before the Court is simply "yes." In this case, plaintiffs have rebutted the rebuttable presumption of business judgment by pleading, with particularity, the conclusion of Cincinnati Bell shareholders that the 2010 executive compensation was not in their best interests. In that vote, and as intended by Congress, Cincinnati Bell shareholders voted upon whether the 2010 executive compensation was in their best interest as shareholders, owners of the corporation. S. Rep. No. 111-176, at 133 (2010) ("[S]hareholders, as the owners of the corporation, have a right to express their opinion collectively on the appropriateness of

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of the business judgment rule, therefore, requires that we search to other states for guidance on how the Ohio courts would apply that rule to the facts before us.").

executive pay.").[5] Resoundingly, 66% of voting Cincinnati Bell shareholders determined, in their own independent business judgment, that the Cincinnati Bell Board's 2010 CEO and top executive pay hikes are not in the best interest of shareholders.

The directors of an Ohio corporation who do not act in the interests of shareholders breach their duty of loyalty and may be held liable for damages. *Flarey v. Youngstown Osteopathic Hosp*., 151 Ohio App. 3d 92, 96 (2002); *see also Ryan*, 918 A.2d at 357. Disloyal directors also face a substantial risk of liability, thereby excusing a pre-suit demand upon the board of directors as a useless and futile act. *Ferro*, 511 F.3d at 617-18 ("Ohio courts have found a demand presumptively futile 'where the directors are antagonistic, adversely interested, or involved in the transactions attacked.'"); *Carlin v. Brownfiel*d, No. 84AP-345, 1985 WL 10327, *4-*5 (Ohio Ct. App. June 18, 1985) (reversing grant of summary judgment on demand futility).

Accordingly, the likelihood of success on the merits decidedly tips in favor of plaintiffs and against defendants, and therefore the requested preliminary injunction should issue.

b. Breach of Duty of Loyalty

Under well-settled corporate law, business judgment protection for executive compensation decisions extends only to directors who act in the best interests of shareholders. *See, e.g*., *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 138 (Del. Ch. 2009) (holding business judgment presumption did not protect "disproportionately large" executive compensation package); *In re infoUSA, Inc. S'holders Litig.*, 953 A.2d 963, 1000 (Del. Ch. 2007) (finding allegations of extravagant executive compensation and insider transactions sufficient to state a claim for fiduciary breach). As the court in *infoUSA* held, "The [business judgment rule] does not require the Court to

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[5] *See also* S. Rep. No. 111-176 at 134 ("an annual, advisory shareowner vote on executive compensation would efficiently and effectively provide boards with useful information about whether investors view the company's compensation practices to be in shareowners' best interests").

bless the conclusion of a director that is self-evidently nonsense on stilts, nor does it protect a board that looks into the sun and names it the moon." *Id.*

Here, the Cincinnati Bell Board said that its executive compensation policy is designed to link executive compensation and corporate performance, and thereby reward executives for superior performance and have consequences for underperformance. Most recently, in Cincinnati Bell's 2011 Proxy Statement, dated March 21, 2011, the Cincinnati Bell Board represented that it had developed a compensation program designed not only to retain outstanding executives, but also to incentivize and reward them for achieving superior performance in the pursuit of Cincinnati Bell' business and financial term objectives, stating:

> The guiding principles of the Company's compensation policies and decisions include aligning each executive's compensation with the Company's business strategy and the interests of our shareholders and providing incentives needed to attract, motivate and retain key executives who are important to our long-term success. Consistent with this philosophy, ***a significant portion of the total compensation for each of our executives is directly related to the Company's earnings and revenues and other performance factors*** that measure our progress against the goals of our strategic plan as well as performance against our peer companies.

See Cincinnati Bell 2011 Proxy Statement (Mar. 21, 2011) at 20 ("Proxy Statement").

Importantly, no one forced the Cincinnati Bell Board to adopt a pay-for-performance executive compensation model. In fact, there is no evidence of any sort suggesting that anyone bullied the Cincinnati Bell Board into committing itself to compensate Cincinnati Bell's CEO and top executives – who are their business allies and friends – on a pay-for-performance basis. Instead, the Cincinnati Bell Board voluntarily adopted pay-for-performance as the touchstone for the payment of executive compensation, and then represented to Cincinnati Bell shareholders that the Cincinnati Bell's executive compensation is firmly rooted in a pay-for-performance philosophy that directly ties corporate pay to corporate performance.

Whenever directors adopt a particular executive compensation policy, whether for payment of bonuses, cash, stock awards and/or stock options, the directors must strictly adhere to the terms of their executive compensation policy.[6] The directors of an Ohio corporation who deviate from their internal executive compensation policy breach their fiduciary duty of loyalty, and that is exactly the situation here.

On May 3, 2011, the Cincinnati Bell Board put their 2010 executive compensation up for vote by Cincinnati Bell shareholders in the Company's first ever say-on-pay vote. In support of their pay proposal, the Cincinnati Bell Board tried to explain why increasing CEO and top executive pay in 2010, despite the Company's large 68.4% decline in 2010 net income, was consistent with the Board's pay-for-performance executive compensation policy and, in fact, in the best interest of Cincinnati Bell shareholders. Proxy Statement at 20. The Cincinnati Bell Board concluded the statement in support of the 2010 executive compensation with a unanimous recommendation to shareholders that the 2010 compensation be approved as in the best interest of shareholders. Specifically, the Cincinnati Bell Board stated:

> The say-on-pay vote is advisory and, therefore, not binding on the Company, the Compensation Committee or the Board of Directors. Our Board of Directors and our Compensation Committee value the opinions of our shareholders and to the extent there is any significant vote against the named executive officer compensation as disclosed in this Proxy Statement, ***we will consider our shareholders' concerns*** and the Compensation Committee will evaluate whether any actions are necessary to address those concerns.
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> * * *
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> **Our Recommendation**

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[6] *See Ryan*, 918 A.2d at 357 (finding directors acted disloyally by retroactively selecting the price for options when their option granting policy required the price to be set on the date of grant); *Provenz v. Miller*, 102 F.3d 1478 (1996) (holding directors violations of their own internal policies shows falsity and scienter in a fraud case).

> ***The Board recommends that shareholders vote "FOR" the approval, on an advisory basis, of the compensation of its named executive officers as disclosed in this Proxy Statement.***

Id.

After considering what the Cincinnati Bell Board had said about the 2010 executive compensation being pay-for-performance and in their best interest, on May 3, 2011, the majority of voting Cincinnati Bell shareholder roundly rejected the 2010 executive compensation. According to Cincinnati Bell's May 9, 2011 Form 8-K, 96,939,788 shares voted against the 2010 executive compensation, or 66% of voting Cincinnati Bell shareholders. This was a landslide defeat for the Cincinnati Bell Board's 2010 executive compensation, and, because the result of a vote, whether advisory or not, reflects the will of the voters, is direct evidence that the 2010 CEO and top executive pay hikes, between 54.3% and 80.3%, are not in the best interest of Cincinnati Bell shareholders. *See Gantler v. Stephens*, 965 A.2d 695, 713 (Del. 2009) (stating that even non-legally binding shareholder votes can have dispositive effect).[7]

Cincinnati Bell shareholders made a sophisticated business decision in rejecting the 2010 executive compensation. This is not surprising, however, since Cincinnati Bell's largest shareholders are primarily sophisticated institutional investors. ¶34 These types of institutional shareholders own millions of Cincinnati Bell shares worth tens of millions of dollars. They possess vast experience with and expertise in evaluating whether executive compensation is in their best interest as shareholders, and, to the extent necessary, possess the resources to retain consultants

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[7] According to the Senate Banking Report, the purpose of the advisory say on pay vote is to provide an efficient means for shareholders, as the owners of the corporation, to collectively express whether the corporation's executive compensation is in their best interest as shareholders. S. Rep. No. 111-176, at 133 (2010) ("The Committee believes that shareholders, as the owners of the corporation, have a right to express their opinion collectively on the appropriateness of executive pay.").

and/or experts to assist them in determining whether executive compensation is in their best interest as shareholders, owners, of Cincinnati Bell.

In short, the result of the adverse Cincinnati Bell say-on-pay vote reflects the determination of Cincinnati Bell shareholders, as owners, that the 2010 executive compensation is not in their best interest. This is as Congress intended: for say-on-pay advisory votes to function as a referendum on whether the executive compensation voted upon is in the best interest of shareholders. *See* S. Rep. No. 111-176, at 134 ("Nonbinding shareowner votes on pay [were meant to] serve as a direct referendum on the decisions of the compensation committee and [] offer a more targeted way to signal shareowner discontent than withholding votes from committee members.").

The adverse Cincinnati Bell say-on-pay vote also has significant implication for this Court's application of the business judgment rule, which provides the standard for judicial review in excessive compensation cases. In a nutshell, although Dodd-Frank did not alter the fiduciary obligations of corporate directors, it did provide a mechanism for courts to objectively test whether executive compensation is in the best interest of shareholders. Courts need no longer rely heavily on process-oriented factors to divine whether executive compensation serves the best interest of shareholders.[8] Now, courts may simply examine the publicly reported results of the advisory say-on-pay votes to determine whether shareholders, in their own business judgment, think the executive compensation is in their best interests as owners.

Thus, after Dodd-Frank, an objective means for testing whether executive compensation is, in fact, in the best interest of shareholders exists, *i.e.*, the result of an advisory say-on-pay vote. The advisory votes under Dodd-Frank are not binding, and plaintiffs do not contend otherwise. But that

[8] *See Walt Disney*, 906 A.2d 27 (recognizing that under modern principles of corporate governance the Disney Board's decision to pay Ovitz millions might not withstand scrutiny under Delaware's business judgment rule).

misses the point, the result of an advisory say-on-pay vote is direct evidence of whether executive compensation is, in fact, in the best interest of shareholders, and may be considered by the court when called upon to assess whether directors acted in the best interest of shareholders when making executive pay decisions. *Gantler*, 965 A.2d 713 (stating that even non-legally binding shareholder votes can have dispositive effect).

Under Ohio law, business judgment protection extends only to directors who act in the best interests of shareholders. *See, e.g.*, *Marsalis*, 149 Ohio App. 3d at 641-42; *see also Ryan*, 918 A.2d at 357. But in this case the evidence shows that the Cincinnati Bell Board did not act in the best interest of Cincinnati Bell shareholders when it approved the 2010 executive compensation. Notwithstanding its advisory nature, the evidence arising from Cincinnati Bell's adverse say-on-pay vote is probative evidence, if not the best evidence, of the fact that Cincinnati Bell shareholders, in their independent business judgment, have concluded that the 2010 executive compensation is not in their best interest. *See Gantler*, 965 A.2d at 713; *Sample*, 914 A.2d at 666 (considering effect of shareholder ratification on wasteful executive compensation).[9] Therefore, plaintiffs have successfully rebutted the presumption of business judgment that would typically be afforded the Cincinnati Bell Board's executive pay decisions and stated an actionable claim against defendants for breach of loyalty, by presenting evidence, which if taken as true, as it must be on this motion, demonstrates that the Cincinnati Bell Board's 2010 executive compensation is not in the best interest

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[9] Moreover, as the beneficiaries of the directors' fiduciary trust, the Cincinnati Bell shareholders vote rejecting the Cincinnati Bell Board's 2010 executive compensation is presumptive evidence that the 2010 executive compensation is not in the best interest of Cincinnati Bell shareholders, as owners of the corporation. *See Sample*, 914 A.2d at 675 (denying motion to dismiss because plaintiffs successfully rebutted the business judgment rule presumption at the pleadings stage).

of Cincinnati Bell shareholders. *Ryan*, 918 A.2d at 358 (holding that breach of loyalty claim stated where complaint alleged directors are not entitled to business judgment protection).

Under established precedent and procedure, defendants must now be afforded an opportunity to carry their burden of proof and persuasion with respect to convincing the jury that the 2010 executive compensation did not breach their duty of loyalty and, in fact, was independent, in good faith and reasonable under the circumstances. *Marsalis*, 149 Ohio App. 3d at 642; *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1162 (Del. 1995) (once business judgment rule rebutted burden shifts to defendants to prove entire fairness); *Nat'l Century*, 504 F. Supp. 2d at 312 (Under Ohio law, "the business judgment rule imposes a burden of proof, not a burden of pleading."). At summary judgment and trial, however, defendants' affirmative defense will likely fail, because the result of the adverse Cincinnati Bell say-on-pay vote cannot be undone. The adverse say-on-pay vote will always reflect the fact that Cincinnati Bell shareholders determined, in their own independent business judgment, that the 2010 executive compensation is not in their best interest as shareholder, owners of the corporation. This is powerful evidence that the 2010 executive compensation is not in the best interest of shareholders and, consequently, that the Cincinnati Bell Board breached its fiduciary duty of loyalty by failing to act in the best interest of Cincinnati Bell shareholders when approving the 2010 CEO and top executive pay hikes challenged herein. *Nagy v. Bistricer*, 770 A.2d 43, 64 (Del. Ch. 2000) (holding directors liable for breach of loyalty for failing to act in shareholders' best interest).

Therefore, based upon the facts of this case, the likelihood of success on the merits with respect to defendant's breach of loyalty strongly tips in favor of plaintiffs and against defendants.

c. Futility of Demand

The likelihood of success on the merits as to futility of demand also strongly favors plaintiffs. In *Aronson*, the Delaware Supreme Court concluded that a pre-suit demand upon a board of directors

is not necessary under two circumstances: (i) when there is reason to doubt that the board of directors is independent; and/or (ii) when there is reason to doubt that the challenged decision is the product of a valid exercise of business judgment. *Aronson*, 473 A.2d 805, 814-15.[10]

Here, a pre-suit demand upon the Cincinnati Bell Board was unnecessary under the second prong of *Aronson v. Lewis*. This is because Cincinnati Bell Board's 2010 executive compensation was not a valid exercise of business judgment. *See supra* §IV.B.1.b. Under *Aronson* and its progeny, directors who are *prima facie* liable for a breach of loyalty face a substantial likelihood of liability sufficient to excuse a pre-suit demand upon the board of directors. *Aronson*, 473 A.2d at 814-15; *Carmody v. Toll Bros*., 723 A.2d 1180, 1189 (Del. Ch. 1998).

Toll Brothers is instructive. There, as here, the plaintiff presented facts that raised a reason to doubt that the decision of the board of directors was a valid exercise of business judgment. *See id.* at 1189. In response to the complaint, the board of directors moved to dismiss for failure to plead futility of demand. Ruling for the plaintiff, the Delaware Chancery Court determined that because the board of directors had been determined to be *prima facie* liable for making false statement to shareholders, the directors faced a substantial likelihood of liability, thereby excusing a pre-suit demand. Specifically, the *Toll Brothers* Court held: "***A demand is deemed excused if the complaint's particularized factual allegations create a reason to doubt that the board would consider the demand in a disinterested, impartial manner***." *Id.* (emphasis added). Similarly, "'Ohio courts have found a demand presumptively futile' 'where the directors are antagonistic, adversely interested, or involved in the transactions attacked.'" *Keithley*, 599 F. Supp. 2d at 890.

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[10] As discussed previously, "Ohio courts routinely look to Delaware case law for guidance in deciding corporate law issues generally, and demand futility issues specifically." *Keithley*, 599 F. Supp. 2d at 888 n.10 (analyzing demand futility in connection with an Ohio corporation and discussing *Aronson*).

The same result should attain here. Directors who do not act at all times in the best interest of shareholders breach their duty of loyalty, and that is exactly what happened here when the Cincinnati Bell Board approved the 2010 executive compensation. *See* §IV.B.1.b. *supra*. Therefore, the Cincinnati Bell Board is disabled from considering any pre-suit demand for action that plaintiffs may have made. Accordingly, the likelihood of success on the merits with respect to futility of demand also strongly tips in favor of plaintiffs, and further supports issuance of the requested preliminary injunction against defendants.

2. The Balance of Hardships Strongly Favors Plaintiffs

Plaintiffs will suffer irreparable harm without the issuance of the requested injunction. Specifically, immediate equitable relief is necessary to protect Cincinnati Bell shareholders because the executives' excessive compensation is resulting in the depletion of corporate funds. Many courts have entered injunctions in cases involving executive compensation – finding that depletion of corporate funds resulted in irreparable harm. *See, e.g.*, *Stanton v. Couturier*, 661 F. Supp. 2d 1141, 1148 (E.D. Cal. 2009) (granting preliminary injunction prohibiting director from engaging in arbitration as it would result in irreparable harm from depletion of corporate funds where compensation package likely violated law); *Johnson v. Couturier*, 572 F.3d 1067, 1086 (9th Cir. 2009) (affirming trial court's order enjoining advancement of fees to directors where plaintiffs showed probable success on merits of underlying claim based on grossly disproportionate compensation). Moreover, it will be extremely difficult – if not impossible – for Cincinnati Bell to recover the executives' excessive compensation should the executives act to hide and/or dissipate the excessive compensation they have received and continue to receive. While defendants will likely argue that they are extremely rich individuals able to pay a judgment after a verdict and have no motive to hide and/or dissipate the excessive compensation, the fact is that they could take such action. And, the possibility of irreparable harm justifies issuance of an injunction. *See, e.g.*,

Walczak v. EPL Prolong, Inc., 198 F.3d 725, 733 (9th Cir. 1999) (upholding preliminary injunction to freeze corporation's assets where breach of fiduciary duty would result in "possibility of irreparable harm").

In contrast to the irreparable harm that would result from denial of plaintiffs' motion – the Company's permanent loss of the excessive compensation – the order plaintiffs seek will not cause the defendants any real hardship. An order that simply freezes the excessive 2010 executive compensation will allow the executives to retain this compensation pending a final resolution on the merits. Those defendants that remain employed at Cincinnati Bell will continue to receive compensation from the Company. Defendants' remaining assets will remain free and unencumbered to use as they see fit and there is certainly not an argument that the 2010 excessive compensation is necessary for defendants' short-term well-being.

It is difficult to conceive how defendants could be harmed by an injunction freezing the excessive compensation. Any inconvenience to defendants resulting from this injunction is *de minimus* and insufficient to constitute a hardship that would defeat Cincinnati Bell's right to preserve plaintiffs equitable remedies and prevent further harm to the Company. In any event, any such inconvenience is significantly outweighed by the damage that will ensue if the Company is permitted to continue paying the 2010 excessive executive compensation – the permanent loss of these Company assets.

Finally, it has been held that in striking this balance, "the injury a defendant might suffer if an injunction were imposed may be discounted by the fact that the ***defendant brought that injury upon itself***." *Novartis Consumer Health, Inc. v. Johnson & Johnson-Merck Consumer Pharms. Co.*, 290 F.3d 578, 596 (3d Cir. 2002) (emphasis added). This is particularly relevant in the present case, as it was Defendants' conduct and/or abdication of their fiduciary duties that caused the excessive executive compensation to be approved.

In short, plaintiff would suffer irreparable harm without the injunction while defendants will not suffer any harm by issuance of the injunction.

3. The Public Interest Favors Granting an Injunction.

The democratic principle of majority rule is not limited to our form of government – it also applies to public corporations. Indeed, the Supreme Court has long emphasized the importance of "'the procedures of corporate democracy.'" *Citizens United v. FEC*, ___ U.S. ___, 130 S. Ct. 876, 911 (2010). As this Court has observed:

> As Directors, the [] Board has a fiduciary duty to the shareholders. While that duty does not necessarily mandate that the Board follow every directive of the majority of shareholders, it surely includes some obligation to at least ensure that principals of corporate democracy are not unduly submerged in an attempt by management to entrench itself.

NCR Corp. v. Am. Tel. & Tel. Co., 761 F. Supp. 475, 494-95 (S.D. Ohio 1991) (granting an injunction). It is in the public interest to ensure that principals of corporate democracy – here the shareholder vote overwhelmingly rejecting the 2010 executive compensation – are not unduly submerged. By granting this motion for a preliminary injunction – and maintaining the status quo – the Court can ensure that the principal of corporate democracy is not unduly submerged pending a trial on the merits.

V. CONCLUSION

Plaintiffs respectfully request that this Court grant the preliminary injunction in its entirety.

DATED: August 1, 2011

Respectfully submitted,

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s/Jack Landskroner

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CERTIFICATE OF SERVICE

I hereby certify that on August 1, 2011, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the e-mail addresses denoted on the attached Electronic Mail Notice List, and I hereby certify that I have mailed the foregoing document or paper via the United States Postal Service to the non-CM/ECF participants indicated on the attached Manual Notice List.

I certify under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed on August 1, 2011.

s/Jack Landskroner

JACK LANDSKRONER

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Manual Notice List

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¿ (No manual recipients)