Chancery Addresses Director Compensation Under 'Investors Bancorp' in 'Stein'

In *Stein v. Blankfein*, the Delaware Court of Chancery issued one of its first opinions addressing director compensation following the Delaware Supreme Court's ruling in *In re Investors Bancorp Stockholder Litigation*.

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In *Stein v. Blankfein*, C.A. No. 2017-0354-SG (Del. Ch. May 31), the Delaware Court of Chancery issued one of its first opinions addressing director compensation following the Delaware Supreme Court's ruling in *In re Investors Bancorp Stockholder Litigation*, 177 A.3d 1208 (Del. 2017), that stockholder approval of a compensation plan may only "ratify" future director awards if the board is left with no further discretion in awarding grants under the plan. Applying *Investors Bancorp*, the court in *Stein* declined to dismiss a challenge to discretionary director awards. The court nevertheless dismissed related disclosure claims, including those seeking to invalidate past equity grants, in accordance with the Delaware courts' preference for disclosure claims to be pressed pre-closing.

Stein involved challenges to the fairness of the compensation of The Goldman Sachs Group Inc.'s nonemployee directors and the past approval of its stock incentive plans. With respect to the former, the plaintiff alleged that the nonemployee directors fixed their own compensation, subjecting these decisions to the entire fairness standard. Despite acknowledging that stockholder approval of the plan did not "ratify" future discretionary awards, the defendants moved to dismiss, arguing that the terms of the plan—which purported to absolve the directors of liability for future breaches of duty in administering the plan absent bad faith—caused the stockholders to have waived their right to bring such claims by approving the plan. The court rejected this argument, explaining that waivers only relinquish known rights and that additional detailed disclosures would have been necessary for the stockholders to have waived their right to challenge discretionary decisions under the plan. The court then cast doubt on the viability of such a waiver even with these disclosures, citing, inter alia, the difference between Delaware's statutes governing corporations, which do not permit modifications of fiduciary duties or exculpation for breaches of the duty of loyalty, and those governing alternative entities, which give parties the contractual freedom to modify fiduciary duties and provide such exculpation.

The defendants separately claimed that the plaintiff failed to adequately plead that the awards were unfair. They argued that the complaint failed to raise any problems with the compensation process, that an outside consultant had advised with respect to the compensation decisions, and that the awards had not affected Goldman's performance. The plaintiff, however, alleged that the directors were paid nearly twice as much as directors in Goldman's identified peer group, that the directors in that peer group had attended more meetings than the defendants, and that the peer group companies had similar or better performance than Goldman over the relevant period. In assessing these arguments, the court observed that, "in light of the power the DGCL confers on directors to self-compensate," a plaintiff's pleading "burden in the self-compensation area cannot be simply conclusory." The court further stated that "above-average" compensation did not necessarily evidence "unfairness," noting that, if it did, "half of all companies would be overcompensating their directors." Given the low pleading standard applied on a motion to dismiss, the court nevertheless found the plaintiff's allegations sufficient to survive a motion to dismiss.

By contrast, the court dismissed on the pleadings the plaintiff's claims alleging that disclosures required by a treasury regulation were not provided in connection with the stockholders' 2013 and 2015 approval of Goldman's incentive plans. The plaintiff alleged that those plans were never duly approved due to these purported disclosure deficiencies and were therefore void ab initio, resulting in the directors having breached their fiduciary duties by granting awards thereunder. The court dismissed the claim as to the 2013 stockholder vote on standing grounds, as the plaintiff had only been a stockholder since 2014. Although the claim as to the 2015 stockholder vote was brought in 2017-—and was therefore within the three-year statute of limitations period—the court found it was barred by laches. Citing the preference for disclosure claims to be brought pre-closing, the court stated: "Laches is apt in disclosure cases where the plaintiff eschews pre-vote relief, then, significantly after the fact, seeks rescission." As the relevant regulation was referenced in the proxy statement, the court found that any deficiency would have been obvious on its face. The court then dismissed a final disclosure claim regarding the tax deductibility of certain cash-based compensation, finding Goldman's disclosures on the matter sufficient.

Takeaways

Stein illustrates the difficulty, post *Investors Bancorp*, of dispensing with challenges to discretionary director compensation awards on a motion to dismiss. As the court recognized, proceeding past this stage "does give a plaintiff significant leverage." But as the court further observed, *Investors Bancorp* and its progeny should not "encourage a massive filing of strike suits." First, "the amount at issue will not be large" in most cases, and even if claims survive, plaintiffs are then faced with the prospect of incurring "significant expense developing a record which may well lead to a determination that the compensation was fair." Second, as outlined in *Investors Bancorp*, both past and future director compensation may be ratified if specific awards are approved by stockholders or made under self-executing stockholder-approved plans. Notwithstanding its acknowledgment of the difficulties of dismissing entire fairness claims on the pleadings, the court's discussion did provide some support for the possibility of dismissing other claims failing to adequately allege unfairness. Specifically, the court noted that the pleadings regarding the fairness of director compensation need to be more than conclusory and that facts indicating that compensation was above-average do not alone establish unfairness. Notably, in one other case, the Court of Chancery dismissed on the pleadings a plaintiff's challenge to director equity awards valued at up to $120,000, finding it inconceivable that compensation to directors of a public company at that level would fail to meet the entire fairness standard under the circumstances alleged, see *Oldfather v. Ells*, C.A. No. 12118-VCL (Del. Ch. Dec. 7, 2016) (transcript).

Stein further illustrates the difficulty in bringing post-closing disclosure claims seeking to invalidate corporate action, which claims stockholder plaintiffs have been making with greater frequency after *Corwin*. In addition to the existing Supreme Court precedent standing for the proposition that disclosure deficiencies in past votes do not void corporate action (but, at most, render it voidable), *Arnold v. Society for Savings Bancorp.*, 678 A.3d 533, 536–37 (Del. 1996), *Stein* suggests that disclosure claims seeking to unwind past corporate action may be barred by laches, even if those claims are brought within the three-year statute of limitations period.

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