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Delaware Federal Court Dismisses Say-on-Pay Case

Reaffirming that the advisory “say-on-pay” vote required by the Dodd-Frank Act cannot be used to attack directors’ executive compensation decisions, the United States District Court for the District of Delaware recently dismissed a derivative complaint brought after a negative say-on-pay vote. The court, applying Delaware law, found that the plaintiff had not pleaded facts sufficient to show that demand would have been futile, or to state a claim upon which relief could be granted. [*Raul v. Rynd*, C.A. No. 11-560-LPS](#) (D. Del. March 14, 2013).

The complaint was filed in 2011, and was one of a number of similar lawsuits filed after Dodd-Frank’s requirement for advisory votes on compensation came into effect. The plaintiff challenged the board’s compensation decisions, alleging that increased compensation in a year when the company posted a net operating loss and negative shareholder return violated the company’s pay-for-performance philosophy and rendered the company’s compensation disclosures in its proxy statement misleading. The plaintiff asserted that the negative shareholder advisory vote rebutted the presumption of business judgment surrounding the board’s compensation decisions.

In dismissing the complaint, the court found that the plaintiff “misconstrue[d] the effect of the shareholder vote” and “mischaracterize[d]” the compensation plan, holding that the plaintiff’s allegations based on the advisory vote “fail to recognize the[] realities of Dodd-Frank” — namely, that the Act “explicitly prohibits construing the shareholder vote as ‘overruling’ the Board’s compensation decision” or altering directors’ fiduciary duties. The court further noted that the plaintiff’s “selective” characterization of the company’s compensation philosophy as “pay for performance” excluded the other goals discussed in the company’s proxy statement.

The *Raul* decision reinforces the Dodd-Frank Act’s bar on attempts to use the advisory shareholder vote to overrule directors’ business judgment on matters of executive compensation. The decision recognizes that directors should be permitted to determine appropriate compensation for executives in accordance with their company’s overall compensation philosophy — including such motivations as attracting, retaining, and incentivizing executives — without fear that they will be subject to liability should shareholders express disagreement with those judgments through an advisory say-on-pay vote.

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