

NO. A08-114

State of Minnesota
In Supreme Court

In re UnitedHealth Group Incorporated
Shareholder Derivative Litigation

and

In re UnitedHealth Group Incorporated
PSLRA Litigation

**RESPONDING BRIEF OF LEAD PLAINTIFFS IN THE
FEDERAL SHAREHOLDER DERIVATIVE LITIGATION**

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INTRODUCTION

Lead Plaintiffs submit this responding brief to answer arguments made in the opening briefs of the UnitedHealth Group Incorporated (UnitedHealth) Board of Directors (the Board), Defendant William McGuire and Defendant David J. Lubben (collectively Defendants).¹

The settlement of any derivative action is always subject to court approval. In federal court, the relevant rule is Federal Rule of Civil Procedure 23.1. In Minnesota state courts, the relevant rule is Minnesota Rule of Civil Procedure 23.09. In either forum, however, the rule is essentially the same: In considering any motion to approve the settlement of a derivative claim, the court is required to exercise independent judgment to determine whether the proposed settlement is fair, reasonable and adequate.

In their opening briefs, Defendants ignore this requirement. Instead, they argue that because the Special Litigation Committee (the SLC) established by UnitedHealth's Board approved certain financial agreements with various Individual Defendants as part of an anticipated

¹ Lead Plaintiffs refer to Defendants' opening briefs respectively as "Bd. Br.," "McGuire Br.," and "Lubben Br."

settlement, Minnesota law requires the federal court to defer absolutely and blindly to the “business judgment” of the SLC, and that any judicial review is limited to considering whether the SLC was independent and acted in good faith.² Defendants are wrong for several reasons.

First, Defendants’ argument puts the proverbial cart before the horse. Because the SLC has not intervened to take over the action and realign the parties, this case remains a derivative action. And because this is a derivative case, Fed. R. Civ. P. 23.1 applies and *requires* the district court to exercise its own independent judgment in considering any settlement that may be presented for approval, just as Minn. R. Civ. P. 23.09 applies in state court.³ As a result, the *Auerbach-Zapata* question is not implicated.

² *See, e.g.*, Bd. Br. at 8 (“If deference is given to a special litigation committee’s decision to sue or not sue, it is natural to extend the same deference to a decision not to pursue a lawsuit where settlements have been reached.”); McGuire Br. at 10 (“There is no principled basis for concluding that the decision to *settle* such claims on specific terms should be subject to any less deference [than an SLC decision not to sue].”) (emphasis in original); Lubben Br. at 8 (arguing that the court should defer to the SLC even though “the method of ending a derivative claim involves a settlement of some claims rather than a determination that the corporation should not pursue those claims.”).

³ In fact, no settlement has yet been submitted for court approval. Rather, the parties have agreed to certain financial terms with certain

Second, to the extent this Court deems it appropriate to address the level of judicial deference applicable to decisions of special litigation committees that impact ongoing litigation—and it should not—Defendants are wrong to equate a settlement with a decision not to pursue a derivative action. A settlement is fundamentally different from a mere dismissal of a lawsuit in that the settlement involves obligations and releases of rights that should be reviewed independently by a court. The Minnesota Supreme Court precedent on which Defendants primarily rely does not require the narrow interpretation of Minnesota’s business judgment rule that Defendants advocate, and the fact that the financial agreements approved by the Lead Plaintiffs and the SLC in this case expressly contemplate court approval suggests that far greater scrutiny be applied to any special litigation committee decision.

Finally, Defendants’ argument that courts should defer to the decision of a special litigation committee because courts are “ill-equipped”

Defendants and are still in discussions regarding other material terms, including corporate governance reforms. It is anticipated that the financial terms agreed to and others will be incorporated into a global settlement that will then be submitted for court approval in accordance with Fed. R. Civ. P. 23.1.

to evaluate derivative settlements is patently meritless and contrary to procedural and case law.

REPLY ARGUMENT

I. In this Derivative Suit, the Federal Court Must Apply Fed. R. Civ. P. 23.1.

Rule 23.1(c) of the Federal Rules of Civil Procedure governs the settlement of derivative actions in federal court and provides that, “[a] derivative action may be settled, voluntarily dismissed, or compromised *only* with the court’s approval.” (Emphasis added.) In short, so long as this remains a derivative case, Fed. R. Civ. P. 23.1 applies and the federal court must independently assess the fairness of any agreed settlement. *See, e.g., Seigal v. Merrick*, 590 F.2d 35, 37 (2d Cir. 1978) (in a shareholder derivative action “because of the vicarious representation involved, the court has a duty to perform before an action can be ‘settled’”); *Greenspun v. Bogan*, 492 F.2d 375, 378 (1st Cir. 1974) (in shareholder derivative action “[a] court . . . must exercise judgment sufficiently independent and objective to safeguard the interests of shareholders not directly involved in the action”).

In this regard, the Federal Rules of Civil Procedure are no different from Minnesota's rules. Both require court approval when a derivative action is settled. So long as this case remains a derivative action, Fed. R. Civ. P. 23.1 or Minn. R. Civ. P. 23.09 would govern any settlement that may be presented.

The SLC's "business judgment" would *only* come into play *if* the SLC had intervened to realign the case and make UnitedHealth a plaintiff rather than a nominal defendant, thus eliminating the derivative nature of the case and rendering derivative action civil procedure rules inapplicable.

A special litigation committee's decision to assume control over a lawsuit through an intervention motion, if approved by a court, fundamentally changes the nature of the case. No longer would the lawsuit be prosecuted by a shareholder derivatively on behalf of a corporation, but by the corporation itself, realigned as the plaintiff through the authority of the board as vested in the special committee. *See, e.g., Valeant Pharms. Int'l v. Jerney*, 921 A.2d 732, 735 (Del. Ch. 2007) (observing that "[t]he litigation was initiated as a stockholder derivative action but, following a change in control of the board, a special litigation committee of the board of directors chose to realign the corporation as a plaintiff" so that

“the company took over control of the litigation”). If that happens, the case is no longer a derivative case, but a direct action by the corporation itself. See *Telxon Corp. v. Bogomolny*, 792 A.2d 964, 968 (Del. Ch. 2001) (corporation named in the stockholder derivative action was acquired by a company that “realigned itself as plaintiff and filed an Amended Complaint converting the derivative action to a direct action”).

Only *after* a special litigation committee assumes such control and thereafter takes some action to impact that litigation is a court called upon to determine the appropriate standard of review to be applied to the committee’s decision. In other words, unless the special litigation committee actually assumes a role in the case and makes a motion, the question of which standard of review is appropriate—whether it be the standard applied by Delaware courts under *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981) or that applied by New York courts under *Auerbach v. Bennett*, 393 N.E. 2d 994 (1979)—is not implicated.

This was precisely the point recognized by the court in *In re Par Pharmaceutical, Inc. Derivative Litigation*, 750 F. Supp. 641 (S.D.N.Y. 1990), in which a special litigation committee made certain recommendations regarding what claims the corporation should pursue or should dismiss,

but did *not* intervene to take over a case. “Allowing the corporation to take over the derivative action pursuant to Rule 23.1,” the court observed, “offers numerous practical advantages including the possibility of alternative remedies, recognition and termination of meritless actions and the ability to utilize the corporation’s oft-superior financial resources and knowledge of the challenged transactions.” *Id.* at 645. Indeed, the very purpose of the “demand” requirement embodied in Rule 23.1 is “to give the derivative corporation itself the opportunity to take over a suit which was brought on its behalf in the first place, and thus to allow the directors the chance to occupy their normal status as conductors of the corporation’s affairs.” *Id.* at 645 (quoting *Brody v. Chemical Bank*, 517 F.2d 932, 934 (2d Cir. 1975)).

However, because the special litigation committee in *Par Pharmaceutical* did not “take over” the litigation, the court determined that the issue of the appropriate deference the court should apply to the committee’s recommendation regarding the litigation was not implicated. *Id.* at 645 (noting that “[t]he question of whether the business judgment rule applies to the decision of a . . . special litigation committee to terminate the derivative action is not raised by the present motion”). And

thus the parties' dispute regarding whether *Auerbach* or *Zapata* applied was "largely irrelevant." *Id.* at 645-46 n.8; see also *Greenfield v. Hamilton Oil Corp.*, 760 P.2d 664, 668 (Colo. Ct. App. 1988) (holding that where a special litigation committee did not move to dismiss claims, it was "unnecessary" to resolve the parties' dispute between whether the court should apply *Auerbach* or *Zapata*). Facts sufficiently analogous to *Par Pharmaceutical* are involved here, and the same result should occur.

Since this case remains a derivative case and further because the agreements reached between Lead Plaintiffs, the SLC, and various Defendants are expressly subject to court approval, the federal court must independently evaluate the settlement pursuant to Fed. R. Civ. P. 23.1, and the SLC is not entitled to the deference Defendants advocate. Significantly, neither the Board, nor McGuire, nor Lubben has cited a federal case, a Minnesota case, or a case from any other state, in which a court was presented with a derivative or class action settlement and abdicated its duty under Fed. R. Civ. P. 23.1 to independently evaluate the terms of that settlement.

Derivative or class action settlements require judicial approval because *the court itself* has a responsibility when approving such

settlements to ensure that the settlement is fair, reasonable, and adequate to the shareholders or class members involved. *See, e.g., Seigal*, 590 F.2d at 37; *Greenspun*, 492 F.2d at 378; *see also In re Coordinated Pretrial Proceedings in Antibiotic Antitrust Actions*, 410 F. Supp. 659, 664 (D. Minn. 1974) (observing that “[a]lthough there is a public policy encouraging settlement of legal disputes, the court supervising a class action has the responsibility to protect members of the class who are not before the Court from a collusive or improvident settlement”). A special litigation committee is not entitled to deference that would defeat the reviewing court’s fundamental obligation to protect absent shareholders. Therefore, where a derivative action involving a Minnesota corporation is resolved through settlement, a reviewing court must independently determine that the settlement is fair, reasonable and adequate.⁴

⁴ The language of the UnitedHealth Board resolution creating the SLC provides that the SLC is established to “analyze the legal rights and remedies of the company and determine whether those remedies should be pursued.” (ALP 157-59.) It did not permit the SLC to negotiate or enter into a settlement. Defendants have not argued that a settlement was either authorized or contemplated when the SLC was constituted and appointed. Furthermore, the SLC is not acting to settle this case independent of Lead Plaintiffs. The settlement discussions and the agreement on financial terms (*see supra* n.3) are tripartite discussions involving Lead Plaintiffs, Defendants and the SLC.

II. Assuming *Arguendo* that the Federal Court Must Consider the Recommendation of the SLC, the Court Must Still Evaluate the Settlement Independently.

A. The Court should Evaluate Any Settlement Independently Because a Decision to Settle is Fundamentally Different from a Decision not to Pursue an Action.

Defendants' argument for deferring to the decision of a special litigation committee in the context of a settlement also misses the mark because a settlement is fundamentally different from a decision not to pursue litigation. Unlike a special litigation committee's decision not to pursue litigation, a decision to accept a settlement involves a complicated and binding release of rights and exchange of obligations. In this case, for example, the terms of the anticipated settlement will require hundreds of millions of dollars to change hands, agreed-upon corporate governance changes will fundamentally alter the way UnitedHealth is managed, and most importantly, UnitedHealth and its shareholders will release forever their rights to pursue these claims again.

Complete and total deference to the will of a special litigation committee would amount to an improper "rubber stamp" of the terms of a derivative settlement and would be a violation of a court's responsibility to protect the rights of absent shareholders of UnitedHealth. *See, e.g., Seigal,*

590 F.2d at 37-38 (observing that court approval of shareholder derivative action “cannot be a rubber stamp of what the parties alone agree is fair and equitable”); *Greenspun*, 492 F.2d at 378 (noting that it is “well-established that a court should not merely rubber stamp whatever settlement is proposed by the parties to a shareholder derivative action”). In direct contrast to a settlement, when a special litigation committee refuses to pursue litigation, shareholders do not permanently release any rights and the company does not incur any affirmative obligations that may affect the absent shareholders.

B. *Janssen* does not Preclude Independent Judicial Scrutiny of Derivative Settlements.

Defendants fundamentally misconstrue the Minnesota Supreme Court’s holding in *Janssen v. Best & Flanagan*, 662 N.W. 2d 876 (Minn. 2003), and then ask the Court to extend Defendants’ interpretation to a special litigation committee’s decision concerning settlement.⁵ Defendants are

⁵ The Board argues that “this Court has previously recognized in *Janssen* . . . that a decision by a corporation through a duly authorized special litigation committee to pursue or not to pursue derivative claims is generally protected by the business judgment rule so long as the special litigation committee was independent and acted in good faith.” Bd. Br. at 8. Similarly, McGuire argues that Minnesota courts “have held that the business judgment rule precludes judicial review of a good-faith decision

wrong. This Court in *Janssen* never addressed, and expressly declined to resolve, the issue of whether a court should independently review the merits of a special litigation committee's decision not to bring suit.

Moreover, unlike the situation here, *Janssen* did not involve a settlement, voluntary dismissal or compromise, and never addressed the impact of Fed. R. Civ. P. 23.1 or Minn. R. Civ. P. 23.09 in the context of a settlement.⁶

Contrary to Defendants' argument, the Minnesota Supreme Court in *Janssen* did not hold that the business judgment rule precludes any judicial review of a good-faith decision by an independent special litigation committee. The Court in *Janssen* never stated the exact standard for judicial review of a special litigation committee's decision not to bring an action, either in the context of a for-profit or nonprofit corporation. The

of a duly-constituted and independent SLC" and that this case law "culminated" with *Janssen*. McGuire Br. at 8.

⁶ To the extent Defendants argue or imply that a special litigation committee's refusal to join a derivative suit is the equivalent to a voluntary dismissal or compromise, Defendants are mistaken. There is nothing "voluntary" about a special litigation committee's decision to seek dismissal of a derivative plaintiff's lawsuit. *See, e.g. Burks v. Lasker*, 441 U.S. 471, 485 n.16 (1979) (the words "shall not be dismissed or compromised without approval of the court" apply "only to voluntary settlements between derivative plaintiffs and defendants, and were intended to prevent plaintiffs from selling out their fellow shareholders. They do not apply where the plaintiffs' action is involuntarily dismissed by a court . . .").

Court only concluded that a committee that is not independent cannot possibly meet *any* business judgment rule standard. The *Janssen* Court stated:

[b]ecause we hold that [the committee's] investigation failed the most minimal version of a business judgment rule, requiring that a litigation committee act in good faith, with independence, we need not reach the question of whether a more exacting standard of judicial review may be appropriate for nonprofit corporations than in the case of for-profit corporations.

Id. at 888 n.5.

Also contrary to Defendants' position, commentators have interpreted *Janssen* to be an invitation to Minnesota district courts to subject the decisions of special litigation committees to independent judicial scrutiny. See Eric J. Moutz, *Janssen v. Best and Flanagan: At Long Last The Beginning Of The End For The Auerbach Approach In Minnesota?* 30 Wm. Mitchell L. Rev. 489, 511 (2003) (noting in adopting the one-strike rule that the *Janssen* court refused to allow a board to bolster its business and that it "would be wholly consistent with *Janssen* for a court to apply this same methodology and 'balancing test' in other circumstances where the facts suggest a meritorious suit is being suppressed").

As discussed above, this Court need not defer to the decision of the SLC here because this is a derivative case, and any settlement is thus subject to Rule 23.1. However, assuming *arguendo* that this Court determines that some deference is appropriate, and further assuming that this Court decides to apply or clarify its ruling in *Janssen*, Lead Plaintiffs respectfully submit that this case is fundamentally different from *Janssen*. Independent judicial scrutiny is even more appropriate under the facts at bar than in *Janssen* precisely because, as discussed above, this case involves a derivative settlement that requires judicial approval under Fed. R. Civ. P. 23.1. This demonstrates further the appropriateness of the more flexible approach to the business judgment rule embodied in *Zapata Corp. v. Maldonado*, 430 A.2d 779, 788 (Del. 1981), which requires a determination of reasonableness through a court's exercise of its own business judgment. See Lead Pls.' Opening Br. at 18.

C. Courts are Well-Equipped to Evaluate Settlements.

Defendants make the specious argument that courts are ill-equipped to evaluate settlements. See, e.g. McGuire Br. at 11 (stating that "courts are ill-equipped" to determine "whether or on what terms to pursue, dismiss, settle or compromise a litigation"); see also Bd. Br. at 20 (arguing that

“courts are not well-equipped to scrutinize the decisions of a corporation,” citing *Janssen*, 662 N.W. 2d at 883). In arguing for a “more ‘deferential’ approach to the application of the business judgment rule,” see Bd. Br. at 17, Defendants cite *Drilling v. Berman*, 589 N.W. 2d 503, 507 (Minn. Ct. App. 1999), in which the Minnesota Court of Appeals limited its review of a special litigation committee’s decision that shareholder derivative claims not be pursued to whether the SLC was independent and acted in good faith. *Drilling*, 589 N.W. at 511. The Board argues that the Minnesota Court of Appeals in *Drilling* refused to independently evaluate the special litigation committee’s decision not to pursue a derivative claim *because* that court determined that courts are “ill-equipped” to evaluate business judgments as to *whether* a derivative action should be pursued. Bd. Br. at 17.⁷

Even if the *Drilling* court was right, and Lead Plaintiffs submit that it was not, this rationale is simply not applicable in the context of a

⁷ The Board states: “The *Drilling* court explained that it adopted this deferential standard *because* ‘courts are ill-equipped to evaluate business judgments while corporate directors [are] particularly qualified to discharge that responsibility.’ . . . Applying this standard, the court concluded that the committee was independent and had conducted its investigation in good faith, and affirmed the district court’s dismissal of the action.” Bd. Br. at 17 (citations omitted) (emphasis added).

settlement. The idea that courts are unable to evaluate proposed settlements cannot be further from the truth and cannot be defended on any legitimate grounds. Initially, assuming this case were to proceed to trial, the court would be required to weigh evidence, decide motions, and make numerous determinations as to the merits of Lead Plaintiffs' claims. It is nonsensical to assume that courts are equipped for these tasks, but "ill-equipped" to evaluate a settlement, particularly where, as here, the action has been proceeding before the court for over two years. An evaluation of settlement terms is unlike a business decision not to pursue a derivative claim because it involves issues related to litigation, such as the release of rights or the merits of claims in an action that is already proceeding.

Courts are eminently qualified, capable, and well-seasoned in evaluating settlements. *See, e.g., Grunin v. Int'l House of Pancakes*, 513 F.2d 114, 123 (8th Cir. 1975) (holding that when a trial judge, who acts as a fiduciary, evaluates a settlement, "[g]reat weight is accorded his views because he is exposed to the litigants, and their strategies, positions and proofs" because the judge "is aware of the expense and possible legal bars to success . . . [and] is on the firing line and can evaluate the action

accordingly"); *SST, Inc. v. City of Minneapolis*, 288 N.W. 2d 225, 231 (Minn. 1979) (noting that in evaluating a settlement, the court is trusted to compare the settlement terms with the result the plaintiffs were likely to obtain at trial).

Courts routinely evaluate derivative and class action settlements, and in fact are *required* to do so under both Minnesota and federal law. *See* Fed. R. Civ. P. 23(e) (requiring court approval for class actions); Fed. R. Civ. P. 23.1(c) (requiring court approval for derivative actions); Minn. R. Civ. P. 23.05(a) (requiring court approval for class action settlements); Minn. R. Civ. P. 23.09 (specifically providing that a derivative action "shall not be dismissed or compromised without the approval of the court"). Since courts routinely evaluate settlements of this type, there can be no legitimate argument that a court must apply a highly deferential standard to a special litigation committee decision to settle a derivative action because the court is "ill-equipped" to evaluate a derivative settlement.

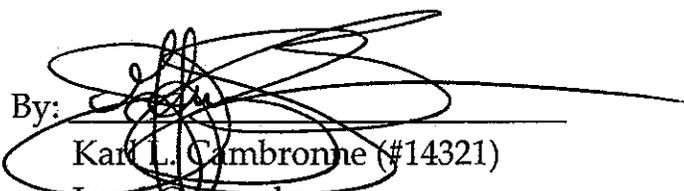
CONCLUSION

Lead Plaintiffs respectfully request that the Minnesota Supreme Court answer the certified question as described in Lead Plaintiffs' Opening Brief, namely that when a shareholder derivative action

involving a Minnesota corporation is resolved through settlement, either negotiated with or subsequently approved by a properly appointed special litigation committee, the district court must review and only approve a derivative settlement if it is fair, reasonable, and adequate under Fed. R. Civ. P. 23.1 or Minn. R. Civ. P. 23.09.

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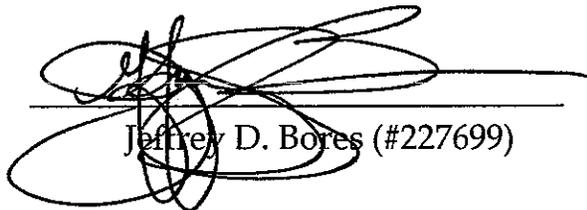
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WORD COUNT CERTIFICATION

The undersigned certifies that the Opening Brief of Lead Plaintiffs in the Federal Shareholder Derivative Action contains 3,098 words and 303 lines, and that it therefore complies with the requirements of Minn. R. Civ. App. P. 132.01. This brief was prepared using Microsoft Word 2003 and the word and line counts were determined by that word processing program. The font used is Palatino Linotype 13 pt, a proportional spaced font.



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