

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.

**BRIEF OF WILLIAM W. MCGUIRE
ON CERTIFIED QUESTION**

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ISSUE ON APPEAL

The United States District Court for the District of Minnesota certified a question to this Court, reformulated by Order of this Court as follows:

To what extent does the business judgment rule as recognized in Minnesota law require a court, in deciding whether to approve a proposed settlement of a shareholder derivative action, to defer to the decision of a Special Litigation Committee duly constituted under Minn. Stat. § 302A.241, subd. 1 (2006), that the derivative action should be settled on specific terms?

Janssen v. Best & Flanagan, 662 N.W.2d 876 (Minn. 2003)

Skoglund v. Brady, 541 N.W.2d 17 (Minn. Ct. App. 1995)

Drilling v. Berman, 589 N.W.2d 503 (Minn. Ct. App. 1999)

Black v. NuAire, Inc., 426 N.W.2d 203 (Minn. Ct. App. 1988)

Minn. Stat. § 302A.241, subdiv. 1 (2006)

INTRODUCTION

Because a corporation is a legal entity separate from its shareholders, when a corporation has suffered an injury, *the corporation*, not its shareholders, possesses the right to sue for redress. Shareholders may sue derivatively but generally first must give the

corporation, through its board, the opportunity to bring (or assume) an action itself to remedy harm to the corporation. *See Winter v. Farmers Educ. & Coop. Union*, 107 N.W.2d 226, 233 (Minn. 1961). Under Minnesota law, the board's decision whether to pursue the action is protected by the business judgment rule, absent a conflict of interest. *Janssen v. Best & Flanagan*, 662 N.W.2d 876, 888 (Minn. 2003). Minnesota law, like the laws of many other states, authorizes a corporate board to delegate to an independent Special Litigation Committee ("SLC") comprised of disinterested members the authority to decide whether pursuit of the derivative claims is in the "best interests" of the corporate body. *See* Minn. Stat. § 302A.241, subdiv. 1 (2006).

The certified question asks this Court to decide to what extent Minnesota's business judgment rule requires a reviewing court to defer to the decision of a duly-constituted SLC that settlement of derivative claims is in the best interests of the corporation. This Court should confirm the precedent it set in *Janssen* by holding that decisions to settle such claims, and the terms thereof, are due the same deference as the decisions of a disinterested board of directors to sue or not to sue, so

long as the Committee is independent and conducted its investigation in good faith.

STATEMENT OF THE CASE

In April 2006, shareholders of UnitedHealth Group (“UHG” or “the Company”), demanded that the Company pursue state and federal claims against certain of its present and former directors and officers, including Dr. William W. McGuire, in connection with the Company’s past stock-option grants. On June 26, 2006, in response to the demand, the UHG Board of Directors (“the Board”) appointed an SLC to investigate the merits of those claims and determine whether and to what extent the Company should pursue them. Nearly eighteen months later, on December 6, 2007, the SLC issued its Report, concluding that it was in the best interests of the Company not to pursue the derivative claims. As a part of that decision, the SLC concluded it should agree to settle with Dr. McGuire, UHG’s former CEO, David Lubben, its former General Counsel, and William Spears, the former chairman of the compensation committee of the Company’s board of directors, and also seek further remediation from Steven Hemsley, UHG’s current CEO. That same day, the state and federal

derivative plaintiffs agreed to the terms of the SLC's proposed settlements.

On December 26, 2007, in an order granting a motion by plaintiffs in a related securities class action suit for an injunction against Dr. McGuire, the United States District Court for the District of Minnesota (Rosenbaum, C.J.) certified the question whether Minnesota's business judgment rule requires judicial deference to the SLC's derivative settlement. This Court accepted the district court's certified question, as reformulated above, on February 1, 2008.

STATEMENT OF FACTS

On March 18, 2006, *The Wall Street Journal* published an article questioning whether executives at certain public companies, including UnitedHealth, were awarded so-called "backdated" stock options. (Ex. 1¹, WSJ Article.) Shortly thereafter, the Board of Directors appointed a committee of independent directors to review the Company's historical and current stock option practices .

In April 2006, the Board received a letter from counsel representing a putative derivative plaintiff, demanding that the

¹ "Ex. __" refers to exhibits contained in the accompanying appendix.

Company pursue state and federal claims against certain present and former directors and officers.²

On June 26, 2006, in response to the demand letter, the Board adopted a resolution appointing an SLC pursuant to Minnesota Statutes § 302A.241, subdiv. 1 (2006), and investing it with “ ‘complete power and authority to investigate the Derivative Claim[s] and analyze the legal rights or remedies of the Company and determine whether those rights or remedies should be pursued.’ ” (Ex. 2, SLC Report at 14 (quoting Board’s June 26, 2006 resolution).)

The SLC is composed of two retired justices of this Court, Honorable Kathleen A. Blatz (formerly Chief Justice of this Court) and Honorable Edward C. Stringer, both of whom have served as members of corporate Boards of Directors, and neither of whom has ever served on UHG’s Board. (*Id.* at 15-17.) The district court that certified the question here noted that “[t]he SLC’s members are two retired Minnesota Supreme Court justices” whom the court knows “to be persons of unquestioned integrity and probity.” (Ex. 3, Op. 3.)

² On May 5, 2006, the first of several securities class actions was also filed against former and present members of the Board (and the

The SLC retained independent counsel and other professionals to assist in its investigation. (*Id.* at 17-22.) Over a period of fifteen months, the SLC investigated a wide array of issues relating to the Company's stock option granting practices. (*Id.* at 32.) The SLC investigated the roles of each of the present and former officers named in the putative derivative actions in the stock option granting practices generally and in connection with specific grants. (*Id.*) It collected six million documents, and each member of the SLC personally reviewed thousands of documents and prepared for and conducted fifty witness interviews. (*Id.*)

After the SLC completed its investigation, it "deliberated and considered the claims against each defendant and whether the pursuit of those claims would be in the best interests of the Company in light of all the facts and circumstances." (*Id.*)

On December 6, 2007, at the conclusion of a thorough, 15-month-long investigation and deliberation, the SLC issued its final report. The SLC Report concluded that claims should not be pursued against the

Company). Both the class action lawsuits and the putative federal derivative actions were assigned to Chief Judge Rosenbaum.

Company's officers and directors, including the claims that were to be settled, as noted above.

The SLC Report includes detailed legal analysis of the potential derivative claims, as well as the defendants' likely defenses. (*Id.* at 39-57.) In determining what course would best serve the Company, the SLC "considered the legal and factual strengths and weaknesses" of the derivative claims and also considered the various "costs and risks" associated with pursuing them. (*Id.* at 57.) Among those considerations were "the significant financial expenditures required to litigate the claims"; "potential disruption and dislocation to the business of the Company"; the Company's indemnification and defense costs obligations; the exculpatory clause of the Company's charter, limiting viable claims against directors; insurance coverage; "potential effects on the Company's current and future business relationships"; and "possible effects on the Company's other litigation risks." (*Id.* at 57-58.)

On December 26, 2007, in connection with an order granting a preliminary injunction motion by the plaintiffs in the federal class action suit, the district court certified a question to this Court regarding

the appropriate deference to be paid to the SLC's judgment. This Court accepted and reformulated the question as set forth above.

ARGUMENT

In the two decades that SLCs have existed in Minnesota, the courts of this state have held that the business judgment rule precludes judicial review of a good-faith decision of a duly-constituted and independent SLC. This case law, the culmination of which was *Janssen v. Best & Flanagan*, 662 N.W.2d 876 (Minn. 2003), has developed for good reason. Deference to SLCs is consistent with the policies behind the Minnesota statute authorizing their use: to encourage independent directors to exercise the same sound business judgment in the matter of litigation claims against officers as they do with respect to other key business decisions—without the fear that they will be second-guessed by shareholders. A number of other jurisdictions have similarly recognized that judicial deference to good-faith decisions of an independent SLC is consistent with the policies underlying the business judgment rule. There is no sound reason to reject that precedent and adopt a new approach.

I. FOR TWO DECADES, THE COURTS OF MINNESOTA HAVE DEFERRED TO THE GOOD-FAITH DETERMINATIONS OF INDEPENDENT SPECIAL LITIGATION COMMITTEES UNDER MINNESOTA'S BUSINESS JUDGMENT RULE

A. As This Court Has Recognized, The Business Judgment Rule Mandates Deference To A Corporate Body's Litigation Decisions

“The business judgment rule is a presumption protecting conduct by directors that can be attributed to any rational business purpose.”

Janssen v. Best & Flanagan, 662 N.W.2d 876, 882 (Minn. 2003)

(citation omitted). The “rule was developed by state and federal courts to protect boards of directors [from] shareholder claims that the board made unprofitable business decisions.” *Id.* Under the business judgment rule, courts will defer to the business judgment of disinterested corporate directors so long as that judgment was informed and made in good faith. *Id.* The rule is based on the rationale that “courts are ill-equipped to judge the wisdom of business ventures” and should be “reticent to replace a well-meaning decision by a corporate board with their own.” *Id.* (citing *Auerbach v. Bennett*, 393 N.E.2d 994, 1000 (N.Y. 1979)).

The business judgment rule has long been applied to a disinterested corporate body's decisions to pursue or not to pursue

litigation against officers or directors. *United Copper Sec. Co. v. Amalgamated Copper Co.*, 244 U.S. 261, 263, 264 (1917). As this Court has cogently explained, the decision whether to pursue shareholders' derivative claims "involves 'the weighing and balancing of legal, ethical, commercial, promotional, public relations, fiscal and other factors familiar to the resolution of many if not most corporate problems,'" a calculus "best done by the board of directors." *Janssen*, 662 N.W.2d at 884 (quoting *Auerbach*, 393 N.E.2d at 1002)).

There is no principled basis for concluding that the decision to *settle* such claims on specific terms should be subject to any less deference. First, a settlement is a decision not to pursue a claim in court in exchange for some kind of consideration. Ultimately, settlement is a business judgment that requires the same calculus as a decision not to pursue a claim. Indeed, if the trial courts are going to start second-guessing business judgments, an SLC's abandoning a claim against an officer or director without requiring payment or other remediation from him should require closer scrutiny than its decision not to pursue a claim after getting the company something in exchange. Second, Minnesota Rule of Civil Procedure 23.09 and Federal Rule of

Civil Procedure 23.1(c) require court approval of settlements, voluntary dismissals, or compromises of derivative actions. *See* Minn. R. Civ. Proc. 23.09; Fed. R. Civ. Proc. 23.1(c). But neither rule makes a distinction among those three options, implying that the standard for approval should be the same. If an SLC is involved, a voluntary dismissal, compromise, or settlement should be evaluated under the *Janssen* standard: Was the SLC that decided to dismiss, settle, or compromise the company's claim independent and did it act in good faith? If so, under *Janssen*, the courts should defer to the business judgment of the body most likely to act in the company's overall best interest—the SLC. Courts are well-equipped to evaluate the legal aspects of pursuing a case, but are ill-equipped to engage in the complex calculus involving ethical, commercial, promotional, public relations, fiscal and other factors involved in making a business decision about whether or on what terms to pursue, dismiss, settle, or compromise a claim. Performing that calculus is precisely what SLCs are created to do. Courts should therefore defer to them, subject only to independence and good faith.

B. The Minnesota Courts Have Repeatedly Held The Business Judgment Rule Forecloses Substantive Review Of The Decision Of A Special Litigation Committee To Forego Derivative Litigation

That Courts should defer to independent SLC's acting in good faith is not a novel idea. Like the courts of many other states, Minnesota courts have consistently held that the business judgment rule precludes a court from second-guessing the decision of an independent special litigation committee—no less than that of a board of directors—not to pursue derivative claims. *See Janssen*, 662 N.W.2d at 884.

Following what has become known as the “*Auerbach* approach,” or “the traditional rule,” the Minnesota Court of Appeals consistently deferred to the decision of a special litigation committee to dismiss a derivative suit, provided the committee was independent and made its decision in good faith. *See Drilling v. Berman*, 589 N.W.2d 503, 507, 510-11 (Minn. Ct. App. 1999) (citing *Auerbach*, 393 N.E.2d at 1000) (“we limit our inquiry to whether the committee was independent and conducted its investigation in good faith”; “information regarding the committee’s reasoning is not relevant”), review denied (Minn. May 18, 1999); *Skoglund v. Brady*, 541 N.W.2d 17, 21 (Minn. Ct. App. 1995)

(district court “properly limited its review to determining whether the special litigation committee was independent and conducted its review in good faith”), review denied (Minn. Feb. 27, 1996); *see also Black v. NuAire, Inc.*, 426 N.W.2d 203, 209-10 (Minn. App. 1988) (adopting the *Auerbach* approach), review denied (Minn. Aug. 24, 1988)). In 2003, the Supreme Court confirmed that jurisprudence in *Janssen*.

An SLC is independent if its members are “disinterested” and “the board properly delegates its authority to act” to the SLC. *Janssen*, 662 N.W.2d at 884. As this Court has explained, the “key element is that the board delegates to a committee of disinterested persons the board’s power to control the litigation.” *Id.* “If the board properly delegates its authority to act . . . , the court will extend deference to the committee’s decision under the business judgment rule.” *Id.* (citing *Drilling*, 589 N.W.2d at 510); *Skoglund*, 541 N.W.2d at 21; *Black*, 426 N.W.2d at 209-10. In determining whether an investigation was conducted in good faith, Minnesota courts have considered four factors: “(1) the length and scope of the investigation, (2) the committee’s use of independent counsel or experts, (3) the corporation’s or the defendants’ involvement,

if any, in the investigation, and (4) the adequacy and reliability of the information supplied to the committee.” *Drilling*, 589 N.W.2d at 509.

Minnesota is in good company in according deference to the good-faith decisions of an SLC under the business judgment rule. As the courts of many other jurisdictions have recognized, courts are “ill-equipped to evaluate business judgments,” whereas corporate directors and their chosen representatives are “peculiarly qualified to discharge that responsibility.” *Black*, 426 N.W.2d at 210 (citing *Auerbach*, 393 N.E.2d at 1000); *see also, e.g., Atkins v. Hibernia Corp.*, 182 F.3d 320, 325 (5th Cir. 1999) (following *Auerbach*, as “best *Erie* guess” of approach Louisiana Supreme Court would adopt); *Hirsch v. Jones Intercable, Inc.*, 984 P.2d 629, 637-38 (Colo. 1999) (adopting *Auerbach* approach); *Roberts v. Alabama Power Co.*, 404 So.2d 629, 632-33 (Ala. 1981) (same); *Desaigoudar v. Meyercord*, 108 Cal. App. 4th 173, 189-90 (Cal. Ct. App. 2003) (following *Auerbach*); *Miller v. Bargaheiser*, 591 N.E.2d 1339, 1343 (Ohio Ct. App. 1990) (extending *Auerbach* to SLC of nonprofit corporation).

Janssen presented the question whether a *nonprofit* board of directors that is not sufficiently independent may establish a special

litigation committee with authority to make the decision. Early in its opinion, this Court cited *Skoglund* and *Drilling*, with approval, as setting forth “the principles by which we apply the business judgment rule to a for-profit corporate board’s decision whether to join a derivative lawsuit.” 662 N.W.2d at 883.

The *Janssen* Court concluded that nonprofit corporations were permitted to appoint SLCs. *Id.* at 884. It further held, however, that the SLC did not qualify for deference under the business judgment rule, because the SLC did not act “in good faith, with independence.” *Id.* at 888 n.5. Because the SLC had not acted in good faith, this Court noted that it “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.* (emphasis added). In reserving the question whether the business judgment rule as applied in *Skoglund* and *Drilling* can be applied uncritically to nonprofit corporations, however, this Court did not create any doubt as to the rule it would apply to SLCs *generally*. On the contrary, its reference to the possibility of a “more exacting standard of judicial

review” for non-profits confirms that the standard of *Skoglund* and *Drilling* continues to apply to for-profit corporations.

C. Deference To The Good Faith Decisions Of A Special Litigation Committee Is Consistent With The Purposes Of The Minnesota Business Corporation Act

The Minnesota statute authorizing the use of SLCs does not address judicial review of SLC decisions. The history of the statute, however, indicates that the Minnesota legislature fully expected that review would be limited to the issues of independence and good faith.

As originally enacted, the Minnesota Business Corporation Act (“MBCA”) contained a provision devoted exclusively to SLCs. That provision, former § 302A.243, authorized the board to delegate its authority to an SLC and provided that “[t]he good faith determinations of the committee are binding upon the corporation and its directors, officers, and shareholders.” 1982 Minn. Laws ch. 497, § 28. Relying in part this language, the Minnesota Court of Appeals concluded that those decisions were not subject to substantive review by a court. *Black*, 426 N.W.2d at 209-10.

Recognizing that Minnesota was one of only a few states with legislation governing judicial review of special litigation committees, the

Minnesota legislature repealed Section 302A.243 in 1989. *Drilling*, 589 N.W.2d at 506 (citing *Hearing on S.F. No. 190 Before the Senate Comm. on the Judiciary* (Apr. 11, 1989) (statement of Sen. Luther)). But far from questioning the *Black* court's adoption of the *Auerbach* rule, the Minnesota legislature took the highly unusual step of stating in its repealer that "the repeal of Minnesota Statutes section 302A.243 *does not imply that the legislature has accepted or rejected the substance of the repealed section* but must be interpreted in the same manner as if Section 302A.243 had not been enacted." 1989 Minn. Laws ch. 172, § 12 (emphasis added). The legislature thus made it crystal clear that this development did not signal legislative disapproval of the *Auerbach* approach as adopted in *Black*. See *Skoglund*, 541 N.W.2d at 21 (rejecting plaintiff's argument that "courts should apply stricter scrutiny to the independence of a special committee and should conduct a substantive review of a special committee's decisions" in light of the repeal of Section 302A.243). As in most other jurisdictions, the question of judicial review would simply be left to the courts. See *Drilling*, 589 N.W.2d at 506 (citing *Hearing of S.F. No. 190 Before the Senate Comm.*

on the Judiciary, Civil Law Div. (Mar. 17, 1989) (statement of Sen. Luther)).

At the same time, the legislature amended § 302A.241, which governs board committees generally, to authorize special litigation committees. Before it was amended, § 302A.241 provided that “[c]ommittees are subject at all times to the direction and control of the board.” 1982 Minn. Laws ch. 497, § 26. Once this provision was amended to authorize SLCs, however, it was revised to read: “*Committees other than special litigation committees . . .* are subject at all times to the direction and control of the board.” Minn. Stat. § 302A.241, subdiv. 1 (emphasis added).

This revision makes perfect sense against the background of the Court of Appeals’ decision in *Black* and the law of a majority of jurisdictions to have then-addressed the question of judicial review of SLC determinations. If Minnesota courts were to defer to the good-faith decision of an SLC, the SLC could not be beholden to the board. As this Court has recognized, the “key element is that the board delegates . . . [its] power to control the litigation.” *Janssen*, 662 N.W.2d at 884. “If the board properly delegates its authority to act . . . , the court will

extend deference to the committee's decision under the business judgment rule." *Id.*

II. THERE IS NO SOUND POLICY REASON TO REJECT TWO DECADES OF CASE LAW APPLYING THE BUSINESS JUDGMENT RULE TO DECISIONS OF A SPECIAL LITIGATION COMMITTEE

Some states have adopted, either judicially or legislatively, a standard of judicial review less deferential than the *Janssen* approach. In these jurisdictions, a reviewing court will defer to the decision of an SLC if the SLC is independent and acted in good faith, *and* there is a "reasonable" basis for that decision. *See, e.g., Houle v. Low*, 556 N.E.2d 51, 59 (Mass. 1990). A few states have gone further, authorizing a reviewing court, "in its discretion", to exercise its own judgment as to whether a derivative action should proceed. *See, e.g., Zapata Corp. v. Maldonado*, 430 A.2d 779, 789 (Del. 1981). There is no sound policy reason to reject twenty years of Minnesota law and embrace any of these alternative approaches.

In *Zapata*, the Delaware Supreme Court noted the competing considerations of the derivative suit as a means of policing boards of directors, on the one hand, and allowing the corporation to rid itself of

meritless or otherwise harmful litigation, on the other. The court therefore sought to find “a balancing point where bona fide stockholder power to bring corporate causes of action cannot be unfairly trampled on by the board of directors, but the corporation can rid itself of detrimental litigation.” 430 A.2d at 786-87. But the *Zapata* court’s approach to this balancing—to allow a reviewing court to conduct essentially de novo review—is completely at odds with the business judgment rule.³

Similarly, the district court’s suggestion that the SLC in this case should have disclosed all of its factual findings (Ex. 6, Op. 9) further illustrates that a more searching judicial inquiry would undermine the purpose of the business judgment rule. It is not the role of an SLC,

³ Even courts applying Delaware law have been reticent to engage in the review envisioned under *Zapata*’s second step. *See, e.g., Carlton Investments v. TLC Beatrice Int’l Holdings, Inc.*, No. CIV.A.13950, 1997 WL 305829, at *2 (Del.Ch. May 30, 1997) (“As to the conceptually difficult second step of the *Zapata* technique, it is difficult to rationalize in principle; but it must have been designed to offer protection for cases in which, while the court could not consciously determine on the first leg of the analysis that there was no want of independence or good faith, it nevertheless ‘felt’ that the result reached was ‘irrational’ or ‘egregious’ or some other such extreme word.”).

standing in the shoes of the Board of Directors, to function like a legislative committee or a government prosecutor charged with informing the public of a wrong committed against it. And, as the SLC candidly explained, “it would be contrary to the Company’s best interests to set forth detailed factual findings regarding the claims asserted in the Derivative Actions, as the Company is subject to ongoing federal securities fraud actions involving similar allegations.” (Ex. 2, SLC Report at 59.)

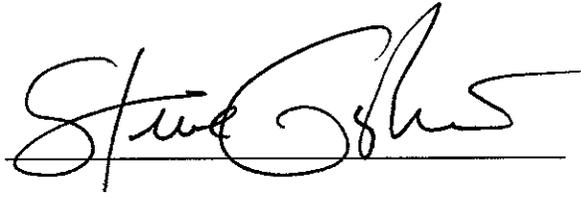
Moreover, diligent application of the *Janssen* approach strikes the balance that *Zapata* sought, while remaining consistent with the rule. Even under the deferential *Janssen* approach, a trial court must find, as a factual matter, that the SLC is truly disinterested and that it conducted its investigation in good faith. Once the court has satisfied itself in that regard, however, that is the end of its inquiry. It is equally inappropriate for a court to substitute its judgment for an SLC’s judgment about whether to pursue a claim as it would be to substitute its judgment for the business judgment of a disinterested board of directors making a decision within its province.

CONCLUSION

For the reasons stated above, this Court should hold that the decision of a Special Litigation Committee to dismiss or settle a derivative action is due the same deference as the decisions of a disinterested board of directors to commence or not commence litigation, so long as the Committee is independent and made its decision in good faith.

Respectfully submitted,

February 28, 2008

A handwritten signature in black ink, appearing to read "Steve Gaskins", written over a horizontal line.

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I hereby certify that on February 29, 2008, I caused two (2) copies of the foregoing BRIEF OF WILLIAM W. McGUIRE ON CERTIFIED QUESTION to be served upon the following via First Class Mail Postage Prepaid:

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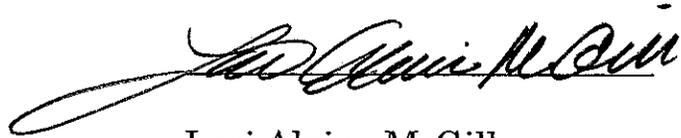
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A handwritten signature in cursive script, appearing to read "Lori Alvino McGill". The signature is written in black ink and is positioned above the printed name.

Lori Alvino McGill