SUPREME COURT OF DELAWARE

In re Walt Disney Co. Derivative Litigation

906 A.2d 27 (Del. 2006) · No. No. 411, 2005 · Decided June 8, 2006

SUMMARY

The Delaware Supreme Court affirmed the Court of Chancery’s judgment for the defendants in a derivative action arising from Michael Ovitz’s hiring and termination as president of The Walt Disney Company. The court upheld findings that the Disney directors did not breach their fiduciary duties or commit waste, and that Ovitz’s approximately $130 million severance payment was required under his employment agreement.

CASE DETAILS

COURT	Supreme Court of Delaware
WRITING FOR THE COURT	Jacobs, Justice; Steele, Chief Justice; Holland, Justice; Berger, Justice; Ridgely, Justice
JURISDICTION	Delaware
DECIDED	June 8, 2006
DOCKET	No. 411, 2005
DISPOSITION	affirmed
PROCEDURAL POSTURE	Shareholders brought derivative actions challenging Michael Ovitz's employment agreement, his non-fault termination payment, and the conduct of Disney's directors and officers. After a trial in the Court of Chancery, judgment was entered for all defendants. The plaintiffs appealed.
STANDARD OF REVIEW	Legal rulings are reviewed de novo or plenary; factual findings based on witness credibility are upheld unless clearly wrong; non-credibility factual findings are accepted if supported by the evidence and an orderly and logical reasoning process. Summary-judgment review examines the entire record under the same framework.
PRECEDENTIAL VALUE	published precedential opinion
PARTIES	William Brehm and Geraldine Brehm, as Trustees and Custodians, Michael Grening, Richard Kaplan and David Kaplan, as Trustees, Thomas M. Malloy, Richard J. Kager and Carol R. Kager, as Joint Tenants, Michael Caesar, as Trustee for Howard Gunty, Inc. Profit

Sharing Plan, Robert S. Goldberg, I.R.A., Michael Shore, Michele DeBendictis, Peter Lawrence, I.R.A., Melvin Zupnick, Judith B. Wohl, I.R.A., James C. Hays, Barnett Stepak v. Michael D. Eisner, Michael S. Ovitz, Stephen F. Bollenbach, Sanford M. Litvack, Irwin Russell, Roy E. Disney, Stanley P. Gold, Richard A. Nunis, Sidney Poitier, Robert A.M. Stern, E. Cardon Walker, Raymond L. Watson, Gary L. Wilson, Reveta F. Bowers, Ignacio E. Lozano Jr., George J. Mitchell, Leo J. O'Donovan, Thomas S. Murphy, The Walt Disney Company

TOPICS

fiduciary duty | business judgment rule | corporate governance | appellate procedure

PRACTICE AREAS

corporate law | fiduciary duty | appellate procedure | commercial litigation | contracts

QUESTIONS PRESENTED

1. Whether Ovitz owed fiduciary duties during the negotiation of the employment agreement before formally assuming office.
2. Whether Ovitz breached fiduciary duties by receiving the non-fault termination payment or by failing to convene a board meeting to consider termination for cause.
3. Whether Disney's compensation committee and directors breached fiduciary duties of care or good faith in approving the employment agreement and electing Ovitz as President.
4. Whether gross negligence, without more, constitutes bad faith and defeats business-judgment-rule protection.
5. Whether the Disney board or compensation committee was required to approve Ovitz's termination and the resulting severance payment.
6. Whether Disney's directors acted improperly in concluding that Ovitz could not be terminated for cause.
7. Whether the non-fault termination provisions or the severance payment constituted corporate waste.

HOLDINGS

1. Ovitz was not a fiduciary during the material pre-October 1, 1995 negotiation of the employment agreement because he had not assumed or purported to assume the duties of Disney's presidency, and the material terms at issue had already been agreed upon before he became an officer.
2. Ovitz did not breach fiduciary duties by receiving the non-fault termination payment because he did not participate in the decisions to terminate him or to terminate him without cause, and the corporation imposed the contractual transaction upon him.
3. Grossly negligent conduct, including a failure to inform oneself of available material facts, does not by itself constitute bad faith or breach the fiduciary duty to act in good faith.

4. The compensation committee and Disney directors did not breach their duties of care or good faith in approving the employment agreement, including its non-fault termination provisions, or in electing Ovitz as President.
5. Neither the new board nor the compensation committee was required to act on Ovitz's termination or the resulting non-fault payment because Disney's governing instruments gave the Chairman/CEO concurrent authority to remove a lesser officer, and the compensation committee had already approved the contractual termination provisions.
6. The non-fault termination provisions and the resulting payment did not constitute corporate waste because they served a rational business purpose and the payment was contractually required.

KEY QUOTATIONS

> *"The answer is clearly no. From a broad philosophical standpoint, that question is more complex than would appear, if only because (as the Chancellor and others have observed) "issues of good faith are (to a certain degree) inseparably and necessarily intertwined with the duties of care and loyalty...." But, in the pragmatic, conduct-regulating legal realm which calls for more precise conceptual line drawing, the answer is that grossly negligent conduct, without more, does not and cannot constitute a breach of the fiduciary duty to act in good faith."* (65)

> *"In our view it must be, for at least two reasons. First, the universe of fiduciary misconduct is not limited to either disloyalty in the classic sense (i.e., preferring the adverse self-interest of the fiduciary or of a related person to the interest of the corporation) or gross negligence."* (67)

> *"To recover on a claim of corporate waste, the plaintiffs must shoulder the burden of proving that the exchange was "so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration.""* (74)

FACTUAL BACKGROUND

Disney hired Michael Ovitz as President under a five-year employment agreement containing substantial compensation and non-fault termination provisions. Ovitz was terminated without cause after approximately fourteen months, resulting in a severance payment valued at roughly $130 million, including cash and accelerated stock options. Disney shareholders alleged that Ovitz and the Disney directors breached fiduciary duties, that the directors acted in bad faith or with gross negligence, and that the severance payment constituted corporate waste. The Court of Chancery found that the compensation committee and directors were adequately informed, acted in good faith, and made rational business decisions.

PROCEDURAL HISTORY

The Court of Chancery dismissed the original complaint, and the Delaware Supreme Court affirmed in part and reversed in part in Brehm v. Eisner, allowing the plaintiffs to replead. After the second amended complaint survived a motion to dismiss and Ovitz obtained partial summary judgment, the case was tried over 37 days. The Court of Chancery entered judgment for the defendants, finding no fiduciary-duty breach or corporate waste. The Supreme Court of Delaware affirmed.

DISPOSITION

affirmed

CASES CITED

- Brehm v. Eisner, 746 A.2d 244 (Del. 2000)
- In re The Walt Disney Co. Derivative Litig., 731 A.2d 342 (Del. Ch. 1998)
- In re The Walt Disney Co. Derivative Litig., 825 A.2d 275 (Del. Ch. 2003)
- In re Walt Disney Co. Derivative Litig., 2004 WL 2050138 (Del. Ch. Sept. 10, 2004)
- Emerald Partners v. Berlin
- Levitt v. Bouvier, 287 A.2d 671 (Del. 1972)
- Alabama By-Products v. Neal, 588 A.2d 255 (Del. 1991)