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Securities Regulation Daily Wrap Up, TOP STORY—N.C. Super.: Duke Energy board did not breach fiduciary duties by granting CEO a $44 million severance for one day's work, (May 1, 2014)

Securities Regulation Daily Wrap Up

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By John M. Jascob, J.D.

The North Carolina Business Court has dismissed a shareholder derivative suit alleging that the board of **Duke Energy** Corporation (Duke) committed waste and breached its fiduciary duties by granting William Johnson up to $44 million in severance payments after Johnson served only one day as the company's CEO. The court held that the existence of an employment contract barred a claim against Johnson for unjust enrichment, while the plaintiff lacked standing to bring corporate waste and fiduciary duty claims on behalf of Duke because he failed to make a pre-suit demand on the board of directors. Accordingly, the claims were dismissed (*Krieger v. Johnson*, April 30, 2014, Jolly, Jr., J.).

Background. The action arose out of the 2011-2012 merger between **Duke Energy** and Progress Energy, Inc. Following completion of the merger, Progress Energy became a wholly owned subsidiary of Duke, thereby creating one of the country's largest electric utility companies. The complaint alleged that representations were made to shareholders that Johnson, who had been Progress Energy's CEO, would serve as the new CEO of the combined company, with Duke's former CEO, James Rogers, becoming the executive chairman of the board of directors.

After the merger was approved by shareholders but before completion of the transaction, Johnson entered into a new three-year employment agreement with Duke. Under the contract, Johnson was to receive significant severance payments if Duke terminated his employment without cause, or if Johnson voluntarily resigned for good reason prior to the second anniversary of the closing of the transaction. Only hours after the merger was finalized, however, the Duke board removed Johnson as CEO, replacing him with Rogers. Johnson and Duke then entered into the separation agreement, with Johnson's removal triggering payments to him that could reach as much as $44.4 million.

Unjust enrichment claim. The court rejected the plaintiff's claim that Johnson's severance payment represented unjust enrichment in the form of excessive compensation. The court noted that an unjust enrichment claim cannot be maintained where an explicit contract exists between the parties, and the complaint revealed that Johnson's severance payments arose out of his employment agreement with Duke. Even assuming the truth of the plaintiff's contention that the payment was excessive in light of Johnson's "scant hours of service," the existence of a contract concerning the subject matter of the claim was dispositive. Accordingly, the court dismissed the claim.

Directors' disinterest or independence. As to the plaintiff's claims that Duke's directors breached their fiduciary duties, the plaintiff failed to establish that his failure to make a pre-suit demand on the board was excused under the law of Delaware, Duke's state of incorporation. The plaintiff argued that demand would have been futile because the directors faced a substantial likelihood of personal liability for committing waste and violating Duke's compensation mandates by approving Johnson's severance payment. Although noting that the relative timing of Johnson's employment agreement and his departure presented some "troublesome details," the court ruled that the plaintiff's conclusory allegations were inadequate to demonstrate a substantial likelihood of liability on the part of the defendants. Moreover, Duke's statements in the proxy materials emphasizing the importance of performance-based executive compensation were plainly aspirational on their face and should not be contorted into affirmative mandates or representations that could give rise to a substantial likelihood of liability for the directors under the circumstances, the court reasoned.

Directors' business judgment. Next, the court held that the plaintiff failed to raise a reasonable doubt as to whether the merger was the product of a valid exercise of business judgment. Apart from a conclusory allegation that the board was in a "hurry to pay Johnson off," the complaint contained no particularized allegations that the directors were not adequately informed in making the decision to terminate Johnson's employment agreement and approve the severance payments to him.

Although the plaintiff contended that the board's unanimous decision to pay Johnson $44 million "for only a few hours of work" constituted clear waste of company assets under Delaware law, the complaint failed to account for the fact that in the event of merger, Johnson was entitled to receive substantial severance benefits under Progress Energy's management change-in-control plan, even if his subsequent employment agreement with Duke had never been formalized. Moreover, in further consideration of his severance payments, Johnson provided: (1) a release of claims against Duke; (2) an agreement to cooperate with Duke in respect to transition matters; and (3) non-competition, non-solicitation, non-disparagement and confidentiality covenants. Accordingly, the allegations failed to support a finding that what Duke received in consideration for the severance payments to Johnson was so inadequate that no person of ordinary, sound business judgment would deem it worth the amount paid.

The case is No. 12 CVS 13727.

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Companies: **Duke Energy** Corporation

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