IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

ALEXANDER GARBER, Plaintiff,	)	
v.	)	Civil Action No. 91-2112
PAUL E. LEGO, et al., Defendant.	)	

R E P O R T

GARY L. LANCASTER,
United States Magistrate Judge

This is a shareholder's derivative suit brought on behalf of Westinghouse Electric Corporation ("Westinghouse"). By this action, plaintiff challenges certain incentive compensation awards granted to Westinghouse executives pursuant to an Annual Performance Plan. The eleven individual defendants were directors of Westinghouse at the time awards were granted.

Defendants have filed a Motion to Dismiss or in the Alternative for Partial Summary Judgment. By this motion, defendants contend that this action should be dismissed because plaintiff has failed either to make a pre-litigation demand upon Westinghouse's Board of Directors or shareholders, or to plead facts with the particularity required by Federal Rule of Civil Procedure 23.1 to excuse such demand. We agree and the Motion to Dismiss should be granted.

I. <u>FACTUAL BACKGROUND</u>

Westinghouse has an Annual Performance Plan ("Plan") that provides for incentive compensation for Westinghouse employees who have "materially contributed to the success of Westinghouse." The incentive compensation is in addition to the employees' regular salaries. The Plan limited incentive compensation available for distribution to five percent of Westinghouse's consolidated net income for a particular year before deducting income taxes and any provision for such incentive compensation. Additionally, unused incentive fund amounts from previous years may be carried forward.

The Plan is administered by a committee of five Westinghouse directors who determine who are to be awarded incentive compensation and in what amounts. The Plan provides that "the Committee's determination will be conclusive and binding on all parties." At all material time, the Committee was composed of defendants Campbell, Carter, McLaughlin, McPherson, and Pivirotto. These five members of the board were non-employee, non-management directors. Plaintiff does not allege that any of these defendants received incentive compensation awards.

On January 29, 1991, the Committee awarded $28 million in Annual Performance Plan awards to 292 Westinghouse employees, two of whom are defendants here, Lego and Stern. At the time the awards were approved, Westinghouse had reported a net income for 1990 of more than $1 billion.

Plaintiff alleges, however, that at the time the incentive awards were approved, the defendants knew that a major economic reversal was imminent which would eliminate or substantially reduce Westinghouse's reported net income for 1990. Specifically, defendants knew and Westinghouse did in February, 1991 report a major "write down."[1] The effect of this write down was to reduce Westinghouse's 1990 consolidated net income before taxes to $428 million. Plaintiff alleges that under the circumstance, the individual defendants acted intentionally and recklessly by approving or acquiescing in the awards. Further, after the write down, they did nothing to cancel or recover the incentive compensation awards that had been granted. Plaintiffs seek to hold the individual defendants liable, jointly and severally, for the damages that their misconduct in respect of the awards has caused Westinghouse.

II. STANDARD OF REVIEW

When considering a 12(b)(6) motion to dismiss, the complaint must be read in the light most favorable to the plaintiff

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1. A write down is an accounting method by which Westinghouse restated its consolidated net income in order to reflect a valuation provision with respect to certain Westinghouse Credit Corporation assets.

and all well-pleaded material allegations must be taken as true. Estelle v. Gamble, 429 U.S. 97 (1976); Hochman v. Board of Education of Newark, 534 F.2d 1094 (3d Cir. 1976). The Court must also accept reasonable inferences from the facts in plaintiff's favor. See Murray v. City of Milford, 380 F.2d 468, 470 (2d Cir. 1967).

The issue is not whether the plaintiff will prevail in the end, or whether recovery appears to be unlikely or even remote, but only whether the plaintiff is entitled to offer evidence in support of the claims. Scheuer v. Rhodes, 416 U.S. 232, 236 (1974). Before dismissing a complaint, the Court must be satisfied "beyond a doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Paolino v. Channel Home Centers, 668 F.2d 721, 722 (3d Cir. 1981) (quoting Conley v. Gibson, 355 U.S. 41, 45-46 (1957)).

III. DISCUSSION

In a shareholders derivative action, Federal Rule of Civil Procedure 23.1 requires that

> [t]he complaint shall allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority, . . . and the reasons for his failure to obtain the action or for not making the effort.

Thus, Rule 23.1 expressly requires that a shareholder's derivative complaint allege either that a demand was made or that demand should be excused since demand would have been futile. _Lewis v. Curtis_, 671 F.2d 779, 784 (3d Cir.), _cert_. _denied_, 459 U.S. 880 (1982). Where a plaintiff seeks to be excused from the demand requirements of Rule 23.1, the Court looks solely to the complaint to determine whether the plaintiff has met this burden. _Id_.

The demand requirement prevents the court from interfering with the internal affairs of a corporation until all intracorporate remedies have been exhausted. It furthers a basic principle of corporate organization--that the management of the corporation is entrusted to its board of directors. _Cramer v. General Tel. & Electronics Corp._, 582 F.2d 259, 274-75 (3d Cir. 1978), _cert_. _denied_, 439 U.S. 1129 (1979). At the same time, Rule 23.1 and case law recognize that it is sometimes necessary to have shareholders enforce or assume the directors' duties of corporate governance. However, the demand requirement is a way to maintain control over such suits by shareholders who attempt to usurp the traditional role and duties of the directors. _See_ _Daily Income Fund, Inc. v. Fox_, 464 U.S. 523 (1984).

In _Lewis v. Curtis_, the Court of Appeals recognized that the derivative plaintiff will be excused from the demand requirement when his complaint alleges that a majority of the directors have participated in the underlying wrongdoing or that the board is controlled by the alleged wrongdoers. 671 F.2d at 784. The court explained though that the mere approval of an allegedly injurious corporate act, absent self-interest or bias by a majority of the board, is insufficient to excuse demand. Id. See also Greenspun, 634 F.2d at 1210[.] The blanket allegation that demand upon the directors would be futile because the directors "would be suing themselves" is alone not sufficient to excuse demand. In Lewis, the court explained.

> To preserve the vitality of rule 23.1, however, courts have refused to excuse demand simply because a majority of the directors are named in the complaint and have cautioned that mere conclusory allegations of director wrongdoing will not suffice to excuse demand. See Greenspun v. Del E. Webb Corp., 634 F.2d 1204, 1209-10 (9th Cir. 1980); Heit v. Baird, 567 F.2d 1157, 1162 (1st Cir. 1977)[.]

671 F.2d at 785. Thus, the court concluded, "the interestedness of the directors in the transaction is more relevant than the character of the alleged wrong." Id. at 786.

A fair reading of Lewis leads us to the conclusion that the fact that a plaintiff/shareholder challenges a decision by members of a board, alone, does not establish a self-interested transaction sufficient to excuse demand. "Participation by the directors in the challenged transaction absent self-interest or bias should not excuse [demand]." Lewis v. Curtis, 671 F.2d at 787 (quoting Note, The Demand and Standing Requirement in Stockholder Derivative Actions, 44 U.Chi.L.Rev. 168, 181-82 (1976)).

Instantly, there is no dispute that plaintiff made no demand. Plaintiff contends, however, that demand should be excused because demand would have been futile in that all of the board had knowledge of, participated in, and/or approved of the awards. Yet, plaintiff here neither alleges collusion among the directors, nor that the directors, other than the two who were also corporate officers, financially or otherwise benefitted from their action, or inaction. Simply put, plaintiff alleges that the five board members who also served on the Committee are "self-interested" only because this suit is a direct challenge to their decision to grant incentive awards. This is a classic
example of a challenge to a Board's business judgment and, thus, plaintiff will not be excused from the demand requirement.

Accordingly, defendants' Motion to Dismiss should be granted.

United States Magistrate Judge

Dated: July 10, 1992

cc: All Counsel of Record

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