IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

H. ALLEN LITT, Trustee of the H. ALLEN LITT, ESQ., P.C. PENSION FUND, Dated September 1, 1984, Derivatively on Behalf of Nominal Defendant, PROGRESS FINANCIAL CORPORATION,

Plaintiff,

v. **C.A. No. 19083-NC**

W. KIRK WYCOFF, STEPHEN T. ZARRILLI, JOSEPH R. KLINGER CHARLES J. TORNETTA, A. JOHN MAY, KEVIN J. SILVERANG, WILLIAM 0. DAGGETT, WILLIAM L. MUELLER, PAUL M. LANOCE, G. DANIEL JONES, and JOHN E. F. CORSON,

Defendants,

and

PROGRESS FINANCIAL CORPORATION, a Delaware corporation,

Nominal Defendant.

MEMORANDUM OPINION

Date Submitted: April 24,2002
Date Decided: March 28, 2003

Norman M. Monhait, Esquire of Rosenthal, Monhait, Gross & Goddess, P.A., Wilmington, Delaware, Sherrie R. Savett, Esquire, Carole A. Broderick, Esquire, Michael T. Fantini, Esquire and Christopher L. Nelson, Esquire, of Berger & Montague, P.C., Philadelphia, Pennsylvania, Attorneys for Plaintiff

Kenneth J. Nachbar, Esquire and William M. Lafferty, Esquire of Morris, Nichols, Arsht & Tunnell, Wilmington, Delaware, Attorneys for Defendants W. Kirk Wycoff, Stephen T. Zarrilli, Joseph R. Klinger, Charles J. Tometta, A. John May, Kevin J. Silverang, William 0. Daggett, William L. Mueller, Paul M. Lanoce, G. Daniel Jones, and John E. F. Corson

NOBLE, Vice Chancellor

I. INTRODUCTION

Plaintiff H. Allen Litt brings this derivative action, in his capacity as trustee of the H. Allen Litt, Esq. P.C. Pension Fund,' on behalf of nominal defendant, Progress Financial Corporation, a Delaware corporation and thrift holding company ("Progress Financial" or the "Company"). Progress Financial, in turn, is the sole shareholder of Progress Bank, a federally chartered savings bank (the "Bank").[2] The boards of directors of the Company and the Bank are identical in composition. The Plaintiff alleges that the directors of Progress Financial breached their fiduciary duties to the Company and its shareholders by conducting lending activities, which the Plaintiff contends were inappropriate for a thrift entity, through the TechBanc division:[3] by paying bonuses to officers, in the form of warrants received from lending customers, for securing business for the

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[1] The caption lists Mr. Litt as the trustee of the pension fund. The Complaint alleges that "Plaintiff H. Allen Litt is, and was at all relevant times, a shareholder of nominal defendant Progress Financial." Compl. ¶ 2. Throughout this opinion, I presume standing of the Plaintiff, either personally or as trustee of the pension fund, on the basis of this allegation.

[2] The Complaint is often ambiguous about which entity, the Company or the Bank, took specific actions. For the purposes of this Memorandum Opinion, however, the differences are not material to my analysis. Therefore, I refer to the entities nonspecifically throughout this opinion as "Progress" wherever distinction is unnecessary or impossible.

[3] It is unclear whether TechBanc is a division of the Company or of the Bank. The Complaint refers to TechBanc as "the Bank's soon to be defunct division," Compl. ¶ 4(e), and as "the Company's 'Special Lending Division.'" Id. ¶ 19.

TechBanc division (the "Incentive Compensation Plan"); and by paying certain other fees and commissions to officers and directors.

The Defendants have moved to dismiss the action because the Plaintiff failed to make demand upon Progress' board of directors as required by Court of Chancery Rule 23.1. For reasons discussed below, the motion to dismiss is granted.

II. FACTUAL BACKGROUND[4]

The Defendants, who are directors of Progress Financial and the Bank, are W. Kirk Wycoff ("Wycoff'), Joseph R. Klinger ("Klinger"), Stephen T. Zarrilli ("Zarrilli"), Charles J. Tometta ("Tometta"), A. John May[5] ("May"), Kevin J. Silverang[6] ("Silverang"), William 0. Daggett, Jr. ("Daggett"), William L. Mueller ("Mueller"), Paul M. LaNoce ("LaNoce"), G. Daniel Jones ("Jones"), and John E. F. Corson ("Corson"). Wycoff is, in addition, the President and Chief Executive Officer of both the Company and the Bank and is the Chairman of the

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[4] The facts upon which I base this decision and, unless otherwise specified, all facts discussed in this opinion are taken from the well-pled allegations of the Complaint and any documents incorporated by reference. ***See White v. Panic, 783*** A.2d 543, 547-48 n.5 (Del. 2001).

[5] May is a partner at the law firm of Pepper, Hamilton LLP, which provides legal services to the Company.

[6] Silverang is a partner at the law firm of Buchanan Ingersoll, which provides legal services to the Company.

Board of the Company. Klinger also serves as Executive Vice President of the Bank.[7]

Tornetta's family members are partners in 436 Plymouth Road Associates, L.P. ("Plymouth Road"). Progress Financial has a fifteen-year lease on property owned by Plymouth Road on which Progress Financial makes lease payments totaling $85,000 annually.

Zarrilli was Chief Executive Officer and Chief Financial Officer of U.S. Interactive, Inc. ("USIT"). USIT, under Zarrilli's leadership, was a significant borrower from Progress. During that time, Wycoff and Zarrilli developed a "significant and longstanding relationship."[8] Zanilli became a director of Progress in June 2000 and left his position at USIT on September 15, 2000. USIT filed for bankruptcy in January 2001. Zarrilli is a major shareholder of USIT; USIT's May 1, 2000, proxy statement disclosed that Zarrilli owned nearly 600,000 shares of USIT common stock.

The Complaint is primarily focused on the TechBanc division's business. Over time, the lending activities conducted through the TechBanc division had the

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[7] Klinger may be an officer of the Company as well. See Compl. ¶ 28 (discussing the Company's award of compensation to its executive officers, including Klinger).
[8] *Id.* ¶ 5.

effect of changing the allocation of Progress' lending and leasing portfolio by increasing the percentage of Progress' assets allocated to commercial loans.' TechBanc specialized in lending to start-up Internet and technology companies. Following a review and examination of the Bank, the Office of Thrift Supervision ("OTS") issued a directive requiring the Bank to:

> "(i) reduce its lending to early stage companies; (ii) increase its leverage capital ratio . . .; and (iii) increase its valuation allowance and implement improved credit review and monitoring programs."[10]

Progress issued a press release announcing that the directors had approved a resolution to bring the Bank into compliance with the directive. In addition, Progress announced its intention to "wind down [its] technology-based portfolio of loans to pre-profit clients,"" apparently a decision to discontinue or to change radically the lending activities of the TechBanc division.

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[9] This impact on the portfolio allocation is alleged to have caused the Bank to violate the Home Owners' Loan Act's ("HOLA") qualified thrift lender test, which requires thrift institutions, such as the Bank, to maintain a certain percentage of their portfolio in housing, small business and consumer-related assets. See 12 U.S.C. § 1467a(m) (codifying the qualified thrift lender test). The Complaint also asserts that the TechBanc lending activities have resulted in large losses to the Bank. The only specifics given are that as a result of making more loans with higher risks, Progress was required to increase its loss reserves, which resulted in the Company reporting a loss of $1.4 million in the second quarter of 2001. This allegation, however, is amplified by the allegation that the losses reported in 2001 were caused by the need to reverse a $2.6 million gain (reported in 2000) on USIT warrants which had subsequently declined in value.

[10] Compl. ¶ 35 (quoting Progress Financial Corp. Press Release of July 12, 2001).

[11] *Id.*

Progress received warrants from borrowers on loans made through TechBanc. In 1999, Progress initiated the Incentive Compensation Plan through which officers and employees received a portion of the warrants that were issued to Progress. The grant of warrants was tied to the making of the loan and was not based on the repayment performance of the borrower. The employees to whom these warrants were transferred could liquidate them 180 days after receipt either in the open market or by having Progress cash out the warrants. Through this plan, Wycoff received warrants to acquire shares in five companies in 1999.[12] In 2000, Progress cashed out Wycoff s warrants in three companies for $78,255. The Complaint states, in addition, that it is believed that Klinger also received warrants through the Incentive Compensation Plan.

USIT was a lending customer of the TechBanc division and Progress received USIT warrants in conjunction with the loans.[13] In 2000 Progress Financial reported a gain of $2.6 million due to a market value adjustment on these warrants. Then, after USIT filed for bankruptcy in January 2001, the Company had to reverse the adjustment and report a loss in the first quarter of 2001. As a

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[12] See *infra* note 14.

[13] Some of these warrants were transferred to Wycoff through the Incentive Compensation Plan. The Complaint specifically states that in 1999 Wycoff received warrants to acquire 7,000 shares of USIT at $3.50 per share. The August 1999 initial public offering price of USIT was made at $10.00 per share.

result, the financial picture of Progress Financial, as reflected in the 2000 financial statement, was somewhat rosier than would prove to be true. Both Klinger and Wycoff received bonuses and the Compensation Committee determined executive compensation based on the inflated 2000 financial statement.[14]

Progress also utilized bonuses to reward employees and, in one case, an outside director for their efforts to accomplish certain goals of the business in areas

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[14] The Complaint sets forth Wycoff s compensation in some detail. "For the period 19982000, Wycoff received base salary from the Company of $1,098.035. In 2000, Wycoff received options to purchase 42,000 shares of Progress Financial stock as part of his compensation . . . . These options . . . have a potential realizable value of almost $800,000. Wycoff further received for the period 1998-2000 . . . incentive payments and bonuses totaling $831,040. All of the above does not include the warrants he received personally for making high risk loans to pre-profit companies as set forth in ¶ 19." Compl. ¶ 4(a). Wycoff also "receive[d] from the Company perquisites worth $50,000 per year." Id. ¶ 4(e).

Wycoff was also rewarded with ten percent of any warrants that were received by the Bank as part of the loan transaction. The warrants Wycoff received in 1999 are described by the Plaintiff as follows:

> (a) 12,490 shares-of VerticalNet, Inc. at $2.79 per share, which had the first public offering of its stock in February 1999 at a price of $8.00 per share;
>
> (b) 6,001 shares of IQEplc at $4.16 per share, which had the first public offering of its stock in May 1999 at a price of $12.50 per share;
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> (c) 3,400 shares of Internet Capital Group, Inc. at $5.00 per share, which had the first public offering in August 1999 at a price of $6.00 per share;
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> (d) 6,250 shares of Ravisent Technologies, Inc. at $3.56 per share, which had the first public offering of its stock in July, 1999 at a price of $12.00 per share;
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> (e) 7,000 shares of US Interactive, Inc. at $3.50 per share, which had the first public offering of its stock in August of 1999 at a price of $10.00 per share.

Id. ¶ 19.

outside the scope of the Incentive Compensation Plan. For example, Progress paid Wycoff bonuses for efforts to raise capital for limited partnerships-Ben Franklin/Progress Capital Fund, L.P. and NewSpring Ventures, L.P.[15]—as well as an incentive payment of over $150,000 on the sale of Procall Teleservices, Inc. ("Procall"), a teleservices subsidiary of the Company. Daggett, a director who is not alleged to have been an employee of Progress, also received a payment of more than $150,000 in connection with the sale of Procall. In addition to bonuses and incentive payments, Progress made loans to executive officers, directors, and their affiliates.[16]

III. ANALYSIS

Defendants have moved to dismiss the Complaint under Court of Chancery Rule 23.1 for the Plaintiffs failure to make demand on Progress Financial's board of directors (the "Board") or to plead demand futility sufficiently. The Plaintiff admits that demand was not made and instead argues that demand should be

[15] The Complaint alleges that Wycoff is a partner of both limited partnerships but does not give any more information regarding the nature, extent, or origin of the interest.

[16] The Company's 2001 proxy materials disclosed that such loans totaled $4.2 million. The 1999 proxy materials disclosed that such loans totaled $6.2 million. The 2000 proxy materials disclosed loans to directors at preferred rates, noting that no individual director had received more than $60,000 in preferred-rate loans. Compl. ¶ 34.

excused as futile. Under the two-pronged *Aronson* test,[17] demand will be excused as futile where the "particularized facts alleged in the complaint create a reasonable doubt *(i.e.,* reason to doubt) that (1) the directors upon whom the demand would be made were disinterested and independent or (2) the challenged transaction was otherwise the product of a valid exercise of business judgment."'* Therefore, the Court must determine whether the Complaint includes allegations of "particularized facts creating a reasonable doubt that the actions of the defendants were protected by the business judgment rule."[19] The Plaintiff is entitled to the benefit of reasonable inferences that may be drawn from the particularized facts alleged but may not rely upon conclusory allegations."

The Board, as comprised on August 29, 2001, the date the Complaint was filed, is the board for purposes of evaluating whether demand is required or excused.[21] The Complaint names eleven directors as defendants. It is not clear whether these eleven constitute the entire Progress Financial board. For purposes

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[17] *Aronson v. Lewis, 473* A.2d *805,* 814 (Del. 1984); *see Brehm v. Eisner, 746* A.2d 244, 256 (Del. 2000).
[18] *Zupnick v. Goizueta, 698* A.2d *384,386* (Del. Ch. 1997); *see also Aronson, 473* A.2d at 814.
[19] *Brehm, 746* A.2d at 255.
[20] *Id.*
[21] *See, e.g., Haseotes v. Bentas,* 2002 Del. Ch. LEXIS 106, at *14 (Del. Ch.); *Needham v. Cruver,* 1993 Del. Ch. LEXIS 76, at *8-9 (Del. Ch.); *Harris v. Carter, 582* A.2d 222, 229-32 (Del. Ch. 1990).

of evaluating the demand requirement, I draw the inference that the eleven individual defendants named in the Complaint were the only directors of Progress Financial as of August 29,200 1.

A. *Disinterest and Independence: First Prong of the* Aronson *Test*

In order to excuse demand under the first prong of *Aronson,* a plaintiff must plead particularized facts that raise a reasonable doubt whether a majority of the board upon which demand would be made was disinterested in the challenged transaction or was able to exercise independent business judgment with respect to it.[22] A director is "interested" when he or she appears on both sides of the challenged transaction or expects to derive a personal benefit from it, such as in a self-dealing transaction.[23] Where self-dealing is not alleged, the benefit accruing to the allegedly interested director must be shown to be material to that director.[24] A benefit is material when its importance to the director, in the opinion of the Court, is such that the director probably could not fulfill his or her fiduciary duties to the corporation "without being influenced by [an] overriding personal

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[22] *Aronson, 473* A.2d, at 814.

[23] *Id.* at *812; Orman v. Cullman, 794* A.2d 5, 23 (Del. Ch. 2002). See *also Cede & Co. v. Technicolor, Inc., 634* A.2d 345,362 (Del. 1993).

[24] *Or-man, 794* A.2d at 23, 25 n.50.

interest."[25] A director is considered "independent" unless the complaint alleges particularized facts to show that the director is unable to base his or her decisions on the corporate merits of the issue before the board.[26] For example, the complaint may demonstrate a "direction of corporate conduct in such a way as to comport with the wishes or interests of" the controlling person" or may plead facts that indicate the director is so "beholden to" or influenced by the controlling person that the director is unable to exercise discretion with respect to corporate decisions.[28]

The Complaint makes no allegation that Mueller, Jones, Corson, or LaNoce are unable to consider demand disinterestedly and independently. On the other hand, the Defendants concede that Wycoff and Klinger may be considered interested for the purposes of evaluating the Rule 23.1 demand requirement. Thus, demand would not be excused under the first prong of *Aronson* unless the allegations of the Complaint raise a reasonable doubt about the disinterest or

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[25] *In re GM Class H S'holders Litig., 734* A.2d 611,617 (Del. Ch. 1999).
[26] *Aronson, 473* A.2d at 816.
[27] *Kaplan v. Centex Corp., 284* A.2d 119, 123 (Del. Ch. 1971); *see also Aronson, 473* A.2d at 816; *Orman, 794* A.2d at 24.
[28] *Rales v. Blasband, 634* A.2d 927,936 (Del. 1993); *see also Aronson, 473* A.2d at *8 15; Orman,* 794 A.2d at 24.

independence of at least four of the remaining five directors (Zarrilli, Tometta, Daggett, May, or Silverang).[29]

1. Stephen T. Zarrilli

Zarrilli was the Chief Executive Officer of USIT until September 15, 2000. He left that position approximately three months after becoming a member of Progress' board in June 2000. While Zarrilli was CEO of USIT, but apparently prior to his service as a director of Progress, USIT received loans from Progress. After Zarrilli left USIT, it filed for bankruptcy-necessitating, for purposes of Progress' financial statement, a readjustment of the valuation of the USIT warrants received in connection with the loans. Zarrilli holds nearly 600,000 shares of USIT common stock. While Zarrilli was at USIT, he developed a "significant" relationship with Wycoff because Zarrilli controlled USIT's decision to become a lending customer of Progress.

Construing these facts in the light most favorable to the Plaintiff, Zarrilli, in his capacity as an officer of USIT, caused USIT to apply for loans-loans that the Plaintiff alleges turned out to be detrimental to Progress. The Complaint notes ominously that Zarrilli's service on the Board overlapped his employment at USIT

[29] The Plaintiff has not attempted to allege that anyone other than Wycoff dominated the other directors' independent judgment regarding Progress' affairs.

for about three months. The pertinent question is not whether a director has been employed by a customer of the corporation. The critical issue, instead, is whether the director was conflicted in his loyalties with respect to challenged board actions. The Complaint contains no allegations of this sort. Significantly missing is any indication that Zarrilli had conflicting loyalties or made any decision based upon conflicting loyalties-that after Zarrilli became a director, for example, Progress made any loans to USIT or that USIT received any preferential treatment in the servicing of its loans. Furthermore, there is no suggestion that any of the actions taken after he became a director of Progress benefited Zarrilli directly or benefited USIT, thereby assisting Zarrilli indirectly as a USIT shareholder. Thus, the Complaint fails to plead particularized facts that raise a reasonable doubt of Zarrilli's disinterest in the challenged transactions.

In addition, the allegation that Zarrilli and Wycoff developed a "relationship" while Zarrilli was at USIT is insufficient to raise a reasonable doubt as to Zarrilli's independence from Wycoff. Neither mere personal friendship alone,[30] nor mere outside business relationships alone,[31] are sufficient to raise a

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[30] *See, e.g., Crescent/Mach I Partners, L.P. v. Turner,* 2000 Del. Ch. LEXIS 145, at *40–41 (Del. Ch.).

[31] *See, e.g., Goldman* v. *Pogo.com, Inc.,* 2002 Del. Ch. LEXIS 71, at *\ 14* (Del. Ch.); *Orman, 794* A.2d at *26-27; Crescent/Mach I Partners, L.P., 2000* Del. Ch. LEXIS 145, at *40–41.

reasonable doubt regarding a director's independence. Also, the Plaintiff has not made any cognizable allegation that Zarrilli developed a sense of "owingness" to Wycoff as the result of the loans that Progress may have made to USIT before Zarrilli joined the Board.

Thus, I find that the Complaint fails to raise a reasonable doubt that Zarrilli is disinterested in the challenged transactions or capable of exercising business judgment independently of Wycoff.

2. Charles J. Tometta

The Complaint alleges that Progress leases property from a limited partnership and that Tometta's "family members" are the partners. The lease is for fifteen years and the lease payments amount to slightly over $7,000 per month to the limited partnership. The particularized factual allegations end there. From this, the Plaintiff would have the Court infer that Tometta is beholden to Wycoff who may be in a position at the end of the lease to elect not to renew it.[32] Again, the factual allegations fall far short of providing a basis for the Court to do so.

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[32] The Plaintiff may also be suggesting somewhat obliquely that Wycoff would be in a position to cause Progress to breach the lease prior to its expiration and, consequently, Tometta must stay in Wycoff s good graces to ensure the uninterrupted income to the partnership. When stated directly, the implausibility of the suggestion-that for this reason Tometta has no choice but to keep Wycoff happy-becomes obvious since the limited partnership would doubtless have a remedy at law for breach of the lease.

First, the relationship between Tornetta and the "family members" who are partners of the limited partnership is unspecified. Second, there are no facts supplied from which the Court may infer that the amount of the lease payment represents a significant departure from fair market value or is material to Tometta or to any of Tometta's family members. In some circumstances, this Court has determined that material financial interests of close family members may factor into the disinterest and independence analysis under the *Aronson* test.[33] Here, however, the failure to allege with particularity both close familial relationship and materiality amounts to a failure to raise a reasonable doubt regarding Tometta's disinterest and independence.[34]

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[33] See, e.g., *Cal. Pub. Employees' Ret. Sys.* v. *Coder,* 2002 Del. Ch. LEXIS 144, at *28-29 (Del. Ch. 2002) (considering a director's son's primary employment with the corporation as one of several factors supporting a reasonable doubt whether the director could consider demand impartially where such demand was adverse to the interests of the corporate CEO); *Mizel v. Connelly,* 1999 Del. Ch. LEXIS 157, at *ll-14 (Del. Ch.) (discussing why one of the directors may be unable to consider demand impartially where such demand was adverse to his grandfather's interests).

[34] The Complaint does not support any contention that Wycoff, as Chief Executive Officer, is vested with unilateral non-reviewable authority to breach contracts on behalf of Progress, was the unilateral decision-maker for leasing the property in question, or could be expected to be the unilateral decision-maker with respect to renewal of the fifteen-year lease upon its expiration.

I also question whether the renewal or non-renewal of a single fifteen-year lease of property, which is not alleged to be at a rate substantially above market value, could suffice to raise a reasonable doubt of a director's independence or disinterest even if the quantum of income derived from the lease were material to Tometta or his close family members.

Finally, the Complaint alleges that "Tometta and his family own substantial tracts of real estate that Defendant Wycoff has caused and will continue to cause to be leased by Progress Financial, in exchange for Tometta's acquiescence to Wycoff s decisions." Compl. ¶ 7. This allegation, especially when contrasted with the allegations regarding the Plymouth Road lease,

3. William 0. Daggett

The Complaint alleges only one fact with regard to the disinterest or independence of Daggett: that Progress paid Daggett and Wycoff over $150,000 each as a commission for their respective roles in the sale of Procall. The payments are described as "excessive" by the Plaintiff, but there are no allegations related to the value or sale price of Procall or to how Wycoff and Daggett participated in its sale. It is therefore impossible to determine whether the payments were excessive, and it would be unreasonable to infer that they were. Furthermore, there are no allegations that either Wycoff or Daggett stood on both sides of the transaction or that either the Procall transaction as a whole or the commission payments specifically were unfair to Progress Financial or its shareholders. I cannot, therefore, ascertain how this single commission earned on a one-time sale of a subsidiary would render Daggett beholden to anyone and thus unable to exercise his independent business judgment. Moreover, this allegation does not call into question Daggett's disinterest in any of the other challenged transactions.

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lacks the particularity required by Rule 23.1.

Nonetheless, it is clear that Daggett does have a personal financial interest in this sizeable fee that he received from Progress. In addition, I accept that a single fee of $150,000 for unspecified services may be material to Daggett. Thus, I conclude that the Plaintiff has raised a reasonable doubt as to whether Daggett was disinterested in the commissions paid in connection with the sale of Procall. For all other challenged transactions, however, the Plaintiff has failed to raise a reasonable doubt that Daggett is disinterested and independent.

Thus, I have determined that the Complaint does not raise a reasonable doubt as to the independence or disinterest of Zarrilli, Tometta, or, for all transactions other than the bonuses paid on the sale of Procall, Daggett. I need not consider, therefore, whether the other directors, May or Silverang, are disinterested and independent. For the reasons stated above, I find that, under the first prong of *Aronson,* demand would not be excused under Court of Chancery Rule 23.1 because at least six of the eleven directors (Zarrilli, Tometta, Mueller, LaNoce, Jones, and Corson and, for all but one transaction, Daggett, as well) are disinterested and independent and, thus, able to review fairly any demand made pursuant to Rule 23.1.

B. *Valid Exercise of Business Judgment: Second Prong of the* Aronson *Test*

Even though a majority of the board is determined to be disinterested and independent, demand may be excused under the second prong of the *Aronson* test.

In order for demand to be so excused, the plaintiff must allege particularized facts that give rise to a reasonable doubt whether the challenged transaction is entitled to the protection of the business judgment rule.[35] A plaintiff may rebut the presumption that the board's decision is entitled to deference by raising a reasonable doubt whether the action was taken on an informed basis or whether the directors honestly and in good faith believed that the action was in the best interests of the corpotation.[36] Thus, in order to excuse demand when a majority of the board at the time of demand is found to be disinterested and independent, the plaintiff must plead particularized facts sufficient to raise a reasonable doubt that the action was taken in good faith or a reasonable doubt that the board was adequately informed in making the decision. The Complaint fails to do so.

The Complaint does not allege any particularized facts regarding the process by which the Board initiated or approved the challenged actions, notably approval of the Incentive Compensation Plan. Similarly, the Complaint does not allege that the Board failed to obtain appropriate legal advice or other professional guidance before implementing either the TechBanc program or the Incentive Compensation Plan.

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[35] *Aronson*, *473* A.2d at 814-15.
[36] *Id.* at 812.

The decision to offer bonuses to employees who bring in business that a company is seeking to attract would normally be within the ambit of a board's business judgment. Indeed, the Complaint fails to allege any specific reasons, except for the possible violation of state and federal banking requirements, why the Board should have been concerned about the propriety of the Incentive Compensation Plan[37]-no warnings from banking regulators and no investigation or enforcement activity conducted or contemplated. The Court will not infer that the Board acted recklessly or in bad faith, absent specific particularized allegations of fact giving rise to such an inference.[38] Here, read in the light most favorable to the Plaintiffs position, the allegations are that the directors approved an incentive compensation program by which certain officers and employees would receive bonuses for procuring new business in a market niche in which the Board had decided to seek to expand Progress' participation-loans to fledgling technology

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[37] The Complaint does allege that the changes to the Bank's loan and lease portfolio structure, due to the loans made through the TechBanc division, caused banking regulators to issue a directive that Progress reduce lending through the TechBanc division, increase loss reserves, and take various other actions. This, however, does not call into question the Board's exercise of business judgment and does not help the Plaintiffs case for excusing demand because the Complaint also alleges that the Board cooperated and fully complied with the only negative response received from banking regulators with regard to the challenged actions. I refrain, however, from relying upon this allegation to draw an inference that the OTS reviewed and did not find fault with the Incentive Compensation Plan.

[38] *See Aronson, 473* A.2d at 814.

companies. As it has turned out, this may have been a poor (or poorly timed) decision, but employee compensation decisions made by a fully informed, disinterested, and independent board of directors are usually entitled to the protection of the business judgment rule.[39]

In his brief opposing the motion to dismiss, the Plaintiff defends his failure to allege particularized facts in the Complaint on the basis that the corporate records of Progress Financial, which could provide factual detail for particularized allegations, are in the exclusive possession and control of the Defendants. Because 8 ***Del. C.*** § 220 provides shareholders reasonable access to corporate records, this argument is both inaccurate and unavailing. Both this Court and the Supreme

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[39] See 8 ***Del. C.*** § 122(5) (officer and agent compensation); *id.* § 141(h) (director compensation); ***White,*** 783 A.2d at 553 n.35 (noting the board's discretion in setting executive compensation); ***Brehm,*** 746 A.2d at 262 & n.56 (indicating that when setting executive compensation, the outer limit of the discretion of the board is defined by unconscionable conduct, waste, or fraud); ***Grimes*** v. *Donald,* 673 A.2d 1207, 1215 (Del. 1996) (observing that when "an independent and informed board, acting in good faith, determines that the services of a particular individual warrant large amounts of money, whether in the form of current salary or severance provisions, the board has made a business judgment. That judgment normally will receive the protection of the business judgment rule unless the facts show that such amounts, compared with the services to be received in exchange, constitute waste or could not otherwise be the product of a valid exercise of business judgment."); *Lewis v. Hirsch,* 1994 Del. Ch. LEXIS 68, at *10–11 (Del. Ch.) (stating that executive compensation is "ordinarily left to the business judgment of a company's board of directors"); *Tate & Lyle PLC v. Staley Cont'l, Inc.,* 1988 Del. Ch. LEXIS 61, at * 19-22 (Del. Ch.) (finding business judgment rule did protect disinterested directors' approval of compensation packages for other directors); *see also Telxon Corp. v. Meyerson, 802* A.2d 257, *265-66* (Del. *2002); In re Nat'l Auto Credit, Inc. S'holders Litig.,* 2003 Del. Ch. LEXIS 5, at *50–55 (Del. Ch.).

Court have admonished plaintiffs to make use of the "tools at hand" on many occasions.[40] Plaintiffs who fail to do so act at their own hazard.[41]

The allegation that the Board's decision to implement the compensation program was illegal and, thus, not entitled to the benefits of the presumptions of the business judgment rule, is more troubling. The Complaint alleges that the Incentive Compensation Plan violated the banking laws of the United States, 18 U.S.C. § 215, and the Commonwealth of Pennsylvania, 7 P.S. § 1413. In addition, it is alleged that the Incentive Compensation Plan transgressed federal banking regulations, specifically 12 C.F.R. § 570 and OTS Regulatory Bulletin 27b. Defendants' alleged violation of these statutory and regulatory provisions, according to the Plaintiff, requires application of a per se rule that illegal conduct authorized by the Board excuses the Plaintiff from any duty to make pre-suit demand upon the Board.

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[40] Specifically, plaintiffs are encouraged to invoke 8 *Del.* C. § 220 in order to establish whether the records of the corporation support or refute the suspicion of wrongdoing prior to filing a derivative action. *See, e.g., White, 783* A.2d at *549* n.15; *Brehm, 746* A.2d at 262 n.57, 266; *Rules,* 634 A.2d at 934-35 n.lO; *Ash* v. ***McCall,*** 2000 Del. Ch. LEXIS 144, at *56 n.56 (Del. Ch.).

[41] See *White,* 783 A.2d at 555-57 & n.54; ***Mizel,*** 2000 Del. Ch. LEXIS 157, at *16 n.5

1. Bribery Statutes: 18 U.S.C. § 215 and 7 P.S. § 1413

In order to plead that demand is excused because the challenged corporate act was illegal and not within the scope of the business judgment rule, the Plaintiff must at least plead particularized facts that raise a reasonable doubt about the legality of the corporate act in question.[42] However, the allegations in the Complaint fail to support a reasonable inference that adoption of the Incentive Compensation Plan constituted criminal conduct.[43]

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[42] For examples of the use of the criminal law to support fiduciary duty claims against corporate directors, see *In re Caremark Int'l Derivative Litig.*, 698 A.2d 959, 970–72 (Del. Ch. 1996); *In re Baxter Int'l, Inc. S'holders Litig.*, 654 A.2d 1268, 1270-71 (Del. Ch. 1995). Both of these cases address a board's supervisory responsibilities; they do not directly address the directors' liability for their own actions as directors. In *Gagliardi v. Trifoods Int'l, Inc.*, 1996 Del. Ch. LEXIS 87 (Del. Ch.), *published in part*, 683 A.2d 1049 (Del. Ch. 1996), this Court observed that "[t]he business outcome of an investment project that is unaffected by director self-interest or bad faith cannot itself be an occasion for director liability. That is the hard core of the business judgment doctrine." *Id.* at **10–11 (footnote omitted). The Court further explained:

> "By 'bad faith' is meant a transaction that is authorized for some purpose other than a genuine attempt to advance corporate welfare *or is known to constitute a violation of applicable positive law.* There can be no personal liability of a director for losses arising from 'illegal' transactions if a director were financially disinterested, acted in good faith, and relied on advice of counsel reasonably selected in authorizing a transaction."

Id. at **11 n.2 (citation omitted) (emphasis added). The Complaint does not allege whether the Board had the benefit of advice of counsel when it approved the Incentive Compensation Plan.

[43] For purposes of ruling on this motion to dismiss, I consider the text of the pertinent statutes, regulations, and OTS Regulatory Bulletin 27b, which are integral to the Complaint and incorporated by reference therein. *See In re Santa Fe Pac. Corp. S'holders Litig.*, 669 A.2d 59, 69-70 (Del. 1995).

Violation of either 18 U.S.C. § 215 or 7 P.S. § 1413 constitutes criminal conduct? The plain language of these statutes is designed to prohibit bribery of banking personnel.[45] It does not appear to apply in the situation where a bank pays either salary or bonuses to its own employees for doing their jobs. In fact, 18 U.S.C. § 215(c) reads, "This section shall not apply to bona fide salary, wages, fees, or other compensation paid, or expenses paid or reimbursed, in the usual course of business." Furthermore, the Plaintiff fails to direct the Court to any

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[44] 18 U.S.C. § 215(a) provides in pertinent part:

> Whoever (1) corruptly gives, offers, or promises anything of value to any person, with intent to influence or reward an officer, director, employee, agent, or attorney of a financial institution in connection with any business or transaction of such institution; or (2) as an officer, director, employee, agent, or attorney of a financial institution, corruptly solicits or demands for the benefit of any person, or corruptly accepts or agrees to accept, anything of value from any person, intending to be influenced or rewarded in connection with any business or transaction of such institution; shall be [punished in accordance with the statute].

Violation of 18 U.S.C. § 215 is a felony punishable by a fine of up to $1 million or three times the value of the consideration offered and up to thirty years in prison, unless the amount offered is less than $1,000. 18 U.S.C. § 215(a).

7 P.S. $1413(a) provides in pertinent part:

> No director, trustee, officer, employee or attorney of an institution or of an affiliate of the institution shall: (i) receive anything of value for procuring or attempting to procure any loan from or investment by the institution.

Violation of 7 P.S. § 1413 is a misdemeanor punishable by a tine of not more than $1,000 plus the amount received and no more than one-year imprisonment. 7 P.S. § 2102(a) (specifying penalty for violation of 7 P.S. § 1413 and other provisions of the Commonwealth's banking code).

[45] Violation of § 215 is commonly referred to *as* "bank bribery." See, e.g., *United States v. Kenrick,* 221 F.3d 19, *26* (1st Cir. 2000); *United States v. Haese,* 162 F.3d 359, 363 (5th Cir. 1998); *United States v. Jennings,* 160 F.3d 1006, 1015 (4th Cir. 1998); *United States v. Cohen,* 152 F.3d 321,323 (4th Cir. 1998).

precedent for enforcing either statute in the context of bonuses paid by a bank to its own employees, nor to any past, present, or contemplated enforcement actions or investigations of Progress on the basis that the Incentive Compensation Plan violated any applicable law. Thus, the Complaint fails to raise a reasonable doubt that the directors, by adopting and implementing the Incentive Compensation Plan, violated (or facilitated the violation of) either statute and, therefore, does not raise a reasonable doubt whether the decision to implement the plan was not illegal?

2. Banking Regulations and Guidelines: 12 C.F.R. § 570 and OTS Regulatory Bulletin 27b

In order for the Plaintiff to demonstrate that demand should be excused under the second prong of *Aronson,* he must demonstrate that the decision to adopt the Incentive Compensation Plan was not entitled to the protection of the business judgment rule at the time the board made the decision. Although it is possible that

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[46] In this case, there is no allegation that any criminal prosecution or regulatory enforcement action has ever been initiated under either of these statutory provisions. I note that when a plaintiff seeks to invoke a statute, regulation, or regulatory guidance to define the standard against which a corporate board's actions are to be measured and when those actions, in the absence of such a statute, regulation, or guideline, would not otherwise implicate fiduciary duty considerations, there are two factors which, while not precluding judicial intervention here, counsel for caution. First, the absence of any enforcement action, particularly where the regulators are alleged to have been aware of the conduct, suggests that the regulators, who are presumed to have expertise in their particular field, did not consider the conduct worthy of further enforcement proceedings. Second, the Court is being asked to construe statutes and regulations of the federal government and a statute of another state in ways that the Plaintiff does not allege they have ever been interpreted or applied in the past.

the Incentive Compensation Plan (or other programs approved by the Board) may have ultimately run afoul of the banking regulations cited by the Plaintiff, the particularized allegations of the Complaint fail to provide a basis for doubting whether the Board's actions, when measured against the relevant regulatory requirements as of the time of the actions, were the product of a valid exercise of business judgment.

Through 12 C.F.R. Part 570, the OTS has adopted safety and soundness standards for savings associations.[47] When a thrift institution fails to meet these standards, OTS may require the development and implementation of a compliance plan to address its concerns. The OTS' concerns for excessive executive compensation are addressed, first, in the context of "Operational and Managerial Standards," which, ***inter alia***, require thrift institutions to "maintain safeguards to prevent the payment of compensation, fees, and benefits that are excessive or that could lead to material financial loss to the institution."[48] Second, and somewhat more specifically, the safety and soundness standards contain a "Prohibition on Compensation That Constitutes an Unsafe and Unsound Practice" which provides:

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[47] OTS promulgated the regulations under the authority of the Federal Deposit Insurance Act, as amended, 12 U.S.C. § 1831p-1. The Interagency Guidelines Establishing Standards for Safety and Soundness are set forth in Appendix A to 12 C.F.R. Part 570.

[48] 12 C.F.R. § 570, app. A.II.I.

> Excessive compensation is prohibited as an unsafe and unsound practice. Compensation shall be considered excessive when amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal shareholder considering the following:
>
> 1. The combined value of all cash and non-cash benefits provided to the individual;
>
> 2. The compensation history of the individual and other individuals with comparable expertise at the institution;
>
> 3. The financial condition of the institution;
>
> 4. Comparable compensation practices at comparable institutions, based on factors such as asset size, geographic location, and the complexity of the loan portfolio or other assets;
>
> * * *
>
> 6. Any connection between the individual and any fraudulent act or omission, breach of trust or fiduciary duty, or inside or abuse with regard to the institution; and
>
> 7. Any other factors the agencies determine to be relevant.[49]

Furthermore, "[c]ompensation that could lead to material financial loss to an institution is prohibited as an unsafe and unsound practice."[50]

By Regulatory Bulletin 27b, the OTS provides guidance to its examiners regarding reasonable compensation arrangements and to the directors of thrift

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[49] **12 C.F.R. § 570**, app. A.III.A.
[50] **12 C.F.R. § 570** app. A.III.B.

institutions regarding the performance of their responsibilities in overseeing executive compensation. OTS has specifically addressed the issue of incentive pay for thrift executives:

> An increasing number of businesses today rely on incentive pay to motivate managers and employees to excel. OTS encourages incentive-based compensation but prohibits arrangements that provide incentives contrary to the safe and sound operation of the association. For example, compensation based primarily on short-term operating results may encourage unreasonable risk-taking to achieve short-term profits. The board of directors should closely monitor compensation tied to current operating results.[51]

The Board's decision to pursue an aggressive plan for making loans to startup technology companies through TechBanc did not turn out well. The problems arising from Progress' loans to pre-profit companies resulted in a directive from OTS which required Progress, *inter alia*, to:

> (i) reduce its lending to early stage technology companies; (ii) increase its leverage capital ratio . . . and its total risk-based capital ratio . . . ; and (iii) increase its valuation allowance and implement approved credit review and monitoring programs.'*

The Board approved a resolution in July 2001, that implemented the terms of the OTS directive. At that time, Progress announced that it had suspended payment of its quarterly dividend and that it would "exit the business of lending to pre-profit

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[51] Regulatory Bulletin 27(b).

[52] Compl. ¶ 35 (quoting Progress Financial Corp. Press Release of July 12, 2001).

companies and . . . wind down [its] technology-based portfolio of loans to pre-profit clients."[53] The Plaintiff does not allege that OTS then, or at any other time, either questioned or challenged the Incentive Compensation Plan.[54]

Determining whether the Board's adoption of the Incentive Compensation Plan to stimulate TechBanc loans to pre-profit technology companies was the result of the exercise of its business judgment requires an evaluation of the Board's actions as of the time of that decision. The Plaintiff frames the Complaint as a challenge to the Incentive Compensation Plan and not as a direct attack on the TechBanc lending program. According to the Plaintiff, the Incentive Compensation Plan was imprudent, in part, because it was too successful in achieving its goals: it resulted in too many loans having been made by TechBanc to pre-profit companies. The Plaintiff has not alleged with particularity facts evidencing that the compensation received by Progress executives was "excessive" when the amount is measured in the context of an enterprise of the Progress' scope.

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[53] *Id.*

[54] The OTS directive that resulted in the July 2001 resolution restricted the granting of "[h]igh risk loans," which were defined to include "certain commercial business loans and other credit relationships that (i) the Bank originates through its Tech-Bar&Specialized Lending Division, (ii) involve the receipt by the Bank or an affiliate of warrants [or] other equity interest, (iii) are made to a pre-profit company or a company reliant on venture capital funding, or (iv) are otherwise determined by the OTS to have a higher than ordinary degree of credit risk." Compl. ¶ 36.

Instead, he alleges that the Incentive Compensation Plan created too great an incentive to make the loans that the Board wanted Progress to make. As a result, these loans ultimately turned out to have been unduly risky and, therefore, caused financial harm to Progress. The Plaintiff argues that the Incentive Compensation Plan, which induced Progress executives to make these loans, violated the regulatory prohibition upon excessive compensation because it "[led] to material financial loss."[55] In substance, the Plaintiff asks that the conduct of the Board be measured by the results of the TechBanc pre-profit loan program.

The exercise of business judgment cannot be evaluated, as the Plaintiff seems to suggest, merely by looking at the results of that business judgment. While challenges are seldom, if ever, made to business judgments that turn out well, the simple fact that the business decision caused significant loss does not dictate how that decision should be classified or evaluated. The Plaintiffs allegations regarding the Board's authorization of the Incentive Compensation Plan

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[55] See 12 C.F.R. § 570 app. A.II.I.; *id.* $570 app. A.III.B. It is not altogether clear that the Plaintiff has successfully alleged that the TechBanc program, in fact, resulted in "material financial loss." Part of the Plaintiffs criticism is that warrants which resulted in a paper profit in one year had to be reversed as an accounting matter when their value plunged. While that caused a loss in the second year, the cumulative effect on income over the two-year period does not appear to have been material. Furthermore, that OTS required Progress to increase its loss reserves because of the TechBanc operations does not necessarily mean that losses, in fact, resulted. It may be that the increase in reserves resulted from perceived risk instead of actual loss. Nevertheless, for purposes of this Memorandum Opinion, the Court will accept the Plaintiffs allegation that the TechBanc program caused "material financial loss."

(or the TechBanc loan program) are paltry. There are, for example, no particularized allegations about "comparable compensation at comparable institutions" or that Wycoff's compensation (or the compensation of other executives) was "disproportionate to the services rendered?

It may be fair to charge the Board with knowledge that the TechBanc loan program ***could*** have resulted in material financial loss to Progress because, in the most simplistic sense, any new major venture entails risk and that risk carries potential adverse consequences.[57] The decision to run the risks of that loan

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[56] Furthermore, if the focus is on financial losses attributable to the TechBanc loan program, there are few objective factors set forth in the Complaint by which the conduct of the Board, at the time of decision, can be measured. Loans were made to pre-profit technology companies, a concept which, with the hindsight of 2003, may be easy to criticize. At the time of the loans, however, the eventual failure of many of those ventures was not as apparent. In addition, one may wonder, particularly in light of the policies reflected in HOLA, whether it was a wise decision for the directors of a savings institution to view the start-up technology sector as a promising target for new business. Nonetheless, these factors do not support the argument that the decision to implement the TechBanc loan program was beyond the scope of the Board's business judgment.

[57] The Plaintiff also focuses on the "short-term" nature of the incentive compensation program because the warrants were awarded to the executives responsible for making the loans without any assurance that the loans would, in fact, turn out to be "profitable." Although I accept for purposes of this motion to dismiss that the Incentive Compensation Plan awarded "compensation based on short-term operating results," that conclusion is not as self-evident as the Plaintiff argues. First, one can read "operating results" to refer to short-term profits, thus reflecting a concern that accounting judgments might be affected by the potential for additional compensation. The Plaintiff alludes to this possibility when he questions the profits resulting from the increase in value (during USIT's better times) of the USIT warrants. Compl. ¶ 28. Second, warrants, or their value to Progress' executives, have a time-delayed aspect: not only must Progress' executives wait 180 days to cash out but also the value must be sustained for that period. In theory, at least, warrants may be viewed as a means of affording the opportunity to participate in long-term appreciation in value. Moreover, the guidelines set forth in Regulatory Bulletin 27(b) direct boards to "closely monitor compensation tied to current operating results."

program, when evaluated as of the time of the Board's decision, was not such an improvident decision as to deny the directors the presumption of the business judgment rule. Thus, the decision of the Board to pay Progress executives incentive compensation to implement the TechBanc loan program does not, even though the incentive pay may have encouraged the executives to make the loans that caused material financial loss to Progress, constitute conduct beyond the scope of the business judgment rule.[58]

Significantly, Regulatory Bulletin 27(b) does not expressly to bar compensation tied to short-term results.

[58] The Plaintiff relies on several cases from other jurisdictions in support of his claim. None, however, is helpful to his cause. For example, in *Reilly Mortgage Group, Inc. v. Mount Vernon Savings & Loan Ass'n*, 568 F. Supp. 1067 (E.D. Va. 1983), demand on a bank's board of directors was excused because of the cumulative effect of many shortcomings in the directors' conduct including the allegation that the board approved a course of conduct in violation of federal and state regulations, continued to approve the allegedly illegal practices after repeated warnings from state and federal regulators, failed to hold stockholder meetings, and personally profited from the allegedly wrongful conduct. In this case, the TechBanc loan program was halted promptly after regulatory concern was expressed and a large majority of directors has not been alleged with particularity to have personal or financial interest in the Incentive Compensation Program or the TechBanc loan program. Other cases relied upon by the Plaintiff, such as *Amerifirst Bank v. Bomar,* 757 F. Supp. 1365 (S.D. Fla. 1991), emphasize that the analysis was under a Rule 12(b)(6) standard and did not reflect a requirement that allegations be made with particularity. *In Federal Deposit Ins. Corp. v. Schreiner, 892* F. Supp. 869 (W.D. Tex. 1995), alleged violations of a federal banking regulation were evaluated in the context of specific examples of objective violations of the regulation as of when the bank's board made the challenged decision (e.g., loans to insiders made on terms not substantially similar to loans to persons not associated with the bank; loans violated bank's own loan policy).

The Plaintiff also cites *Joy v. North,* 692 F.2d 880 (2d Cir.1982), *cert. denied, 460* U.S. 105 1 (1983), as providing a yardstick for measuring the Board's conduct. In *Joy,* however, the challenged loan put the bank in "a classic 'no win' situation." *Id.* at 896. Here, the Board was focused, as it appeared possible at the time, on the significant upside potential of loans to startup technology companies. Moreover, the Complaint does not allege that the Board could not reasonably have concluded that these loans (or the portfolio of these loan evaluated as a whole)

The Plaintiffs theory ultimately proves too much. He looks to the unhappy results of the TechBanc program approved by the directors and implemented with the inducements provided through the Incentive Compensation Plan. With his allegation of material financial harm, he then invokes federal banking regulations which require directors to avoid executive compensation plans that result in "material financial loss." Because the TechBanc program resulted in material financial loss, the directors, in the view of the Plaintiff, are personally liable; that is, in this instance, they are the functional equivalent of guarantors. That, however, is not the province of corporate directors. To adopt the Plaintiffs analytical methodology would discourage risk-taking and would unduly restrict the exercise of the business decision-making process which is contemplated by Section 14 1 of

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would be profitable or that the Board did not consider the potential risks that could be recognized at the time. While it is apparent with the benefit of hindsight that the Board did not give sufficient weight to the risks associated with the TechBanc loan portfolio, the decision to implement the TechBanc loan program, with the aid of the Incentive Compensation Plan, does not allow a challenge by the Plaintiff to the Board's conduct without a prior demand under *Aronson's* second prong.

The Complaint may also be read as seeking to allege that the Board failed to exercise appropriate supervision over the TechBanc loan program and the Incentive Compensation Program as they were implemented. Compl. ¶ 55(ii). The particularized facts of the Complaint demonstrate that promptly following the directive issued by the OTS which required that the TechBanc loan program be modified (a directive with no alleged mention of the Incentive Compensation Plan), the Board called off the TechBanc loan program and commenced efforts to reduce Progress' exposure to the adverse affects of that program. Thus, there are no particularized allegations that the directors failed to exercise supervision over the TechBanc loan program or the Incentive Compensation Plan (as opposed to their authorization of those programs) that would implicate the standards of *In re Caremark Int'l Deriv. Litig.*, or *In re Baxter Int'l, Inc. S'holders Litig.*

the Delaware General Corporation Law. Indeed, the Plaintiffs analysis turns on whether the business decision was successful, but such a post-hoc analysis of director conduct is not sponsored by the second prong of *Aronson*.[59] In sum, the Plaintiffs allegations about the Incentive Compensation Plan do not excuse demand under *Aronson 's* second prong.[60]

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[59] As explained in *Gagliardi*:

> But directors will tend to deviate from [the] rational acceptance of corporate risk *if* in authorizing the corporation to undertake a risky investment, the directors must assume some degree of personal risk relating to ***ex post facto*** claims of derivative liability for any resulting corporate loss.
>
> Corporate directors of public companies typically have a very small proportionate ownership interest in their corporations and little or no incentive compensation. Thus, they enjoy (as residual owners) only a very small proportion of any "upside" gains earned by the corporation on risky investment projects. If, however, corporate directors were to be found liable for a corporate loss from a risky project on the ground that the investment was too risky (foolishly risky! stupidly risky! egregiously risky!-you supply the adverb), their liability would be joint and several for the whole loss (with I suppose a right of contribution). Given the scale of operation of modem public corporations, this stupefying disjunction between risk and reward for corporate directors threatens undesirable effects.

683 A.2d at 1052.

Moreover, although the Plaintiff argues that "the Board knowingly approved corporate action in violation of law," Pl.'s Opp'n to Defs.' Opening Br. in Supp. of Their Mot. to Dismiss the Compl. at 26, the Complaint does not allege with particularity that the Board, when it approved the Incentive Compensation Plan or the TechBanc loan program, knew that its actions were illegal.

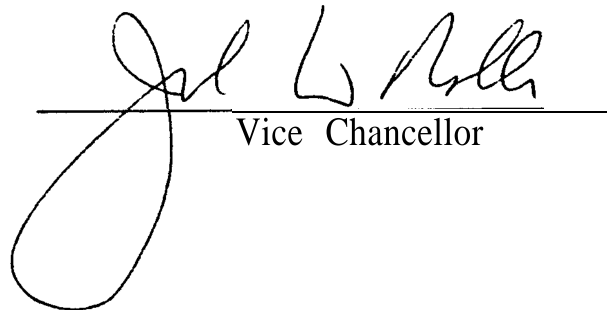
[60] It is not clear that the Plaintiff relies upon an alleged violation of HOLA to excuse demand under the second prong of Aronson. According to the Plaintiff, the Board failed to meet the "qualified thrift leader" test when it failed to maintain 65% of its "portfolio assets" in housing, small business, and consumer related assets. Compl. ¶¶ 3, 33. The Plaintiff alleges that Progress failed that test when only 62.35% of its assets were invested in "qualified thrift investments." ***Id.*** ¶ 33. There is, however, no allegation that the Board was aware that its lending practices would lead to this result; moreover, there is no allegation that the Board failed to take remedial measures when it learned of the status of the Bank's portfolio.

The Plaintiff does not allege that demand is excused because of other challenged conduct,

IV. CONCLUSION

The Complaint, when read in the light most favorable to the Plaintiff's position, has failed to allege with particularity facts sufficient to raise a reasonable doubt whether a majority of the board was disinterested and independent or whether the challenged actions were the product of the exercise of the board's business judgment. Demand is therefore not excused and, because demand was not made, the Complaint is dismissed.

IT IS SO ORDERED.



Vice Chancellor

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such as the commissions paid in the Procall sale or the participation in the limited partnerships with which Wycoff was affiliated.