IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

IN RE CAREER EDUCATION CORPORATION DERIVATIVE LITIGATION	)))	CONSOLIDATED C.A. No. 1398-VCP

MEMORANDUM OPINION

Submitted: July 11, 2007
Decided: September 28, 2007

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PARSONS, Vice Chancellor.

I.

This action constitutes one of a series of derivative action in this and other courts challenging the oversight of the board of directors of Career Education Corporation and accusing a majority of its directors of improper insider trading. Defendants moved to dismiss or stay this action in favor of an earlier filed derivative action then pending in federal court in Chicago, captioned *McSparran v. Larson*, and for failure to make the requisite demand on the board of the Company. During the pendency of Defendants' motion, the court in *McSparran* dismissed that action with prejudice for failure of the plaintiffs to satisfy the demand requirements of Court of Chancery Rule 23.1. Defendants in this action supplemented their motion to seek dismissal on the additional ground that Plaintiffs' demand futility contention was barred under the doctrine of issue preclusion.

For the reasons discussed in this memorandum opinion, the Court will deny the motion to dismiss or stay this action based on the earlier filed federal court action as moot. In addition, the Court will grant Defendants' motion and dismiss all of the claims in this action with prejudice to the named derivative Plaintiffs, because Plaintiffs are precluded from relitigating the issue of demand futility based on the *McSparran* court's previous determination of that issue in the context of essentially the same allegations and claims.

A. Parties[1]

The plaintiffs in this consolidated derivative action are Diane Romero and Robert Neel ("Plaintiffs"). Romero alleges she has continuously been a shareholder in Career Education Corporation ("CEC" or the "Company"), the nominal defendant, since November 25, 2003. Neel alleges that he purchased stock in CEC on March 25, 2003 and that he has continued to hold his shares since that date. CEC is a Delaware corporation with its principal place of business in Illinois.

The individual defendants in this action all serve or served on the board of directors of CEC (collectively, "Defendants"). Defendant John M. Larson has served as President, Chief Executive Officer, and a director of CEC since its inception in 1994 and as Chairman of the Board since 2000. Defendant Patrick K. Pesch has been a director since 1995 and served as the Company's Chief Financial Officer and Treasurer since 1999. Defendant Robert E. Dowdell has been on the board of directors since 1994 and serves as chairman of the board's compensation committee. Defendant Thomas B. Lally has served on the board of directors of CEC and been a member of the audit committee since 1998. Defendant Wallace O. Laub has served as a director of CEC since 1994. Defendant Keith K. Ogata has served as a director of CEC and as a member of the audit committee since 1998. Defendant Dennis H. Chookaszian has served as a director of CEC since October 2002.

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[1] The facts described in this opinion are taken from the well pleaded allegations of the complaint. I assume those allegations to be true, as I must, for purposes of the pending motion to dismiss. *Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988).

B. The Facts

CEC provides private, for profit post-secondary education. The Company operates colleges, schools, and universities with an enrolled student body of roughly 90,000. CEC has physical campuses throughout the United States, Canada, France, the United Kingdom, and the United Arab Emirates. The Company also maintains an online presence through its subsidiaries American InterContinental University Online and Colorado Technical University Online.

This litigation, and several others, arose from two public disclosures the Company made in late 2003. The first announcement, made on November 17, reported that a former director of career services at Gibbs College in Montclair, New Jersey ("Gibbs") had filed a *qui tam* action against CEC alleging that employees at Gibbs falsified student records to boost enrollment, student retention, and graduation rates. The former employee also alleged that she had been wrongfully terminated for refusing to participate in doctoring records.

On December 3, 2003 the Company made a second announcement that revealed an additional *qui tam* lawsuit filed against CEC by a former registrar at Brooks Institute of Photography in Santa Barbara, California ("Brooks Institute"). The market reacted negatively to each of these reports and CEC stock declined precipitously, suffering a 13.4% drop on November 17 and a further 33.3% loss through December 3rd and 4th.

The problems at CEC did not end there. The Securities and Exchange Commission ("SEC") notified the Company on January 7, 2004 that they had launched an

investigation into CEC's accounting treatment of "doubtful accounts."[2] This investigation escalated into a formal inquiry by June 22, 2004. The Company further revealed in a Form 10-Q filed on November 4, 2004 that the United States Department of Justice commenced an investigation into the two lawsuits filed by the former employees of Gibbs and Brooks Institute and the purported misconduct by the Company. Additional regulatory problems surfaced in the Company's Form 10-K for fiscal year 2004 filed on March 16, 2005. The 10-K disclosed that several schools were in danger of losing accreditation, a critical credential for a school seeking to enable enrolled students to qualify for favorable government loans.

Defendants, other than Chookaszian, sold large blocks of stock at various times before these disclosures. The sales identified by Plaintiffs in the Complaint occurred at varying times with respect to each Defendant, but generally took place from April of 2003 through July, August, and September of the same year.[3] Plaintiffs further allege

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[2] Consol. Compl., filed July 18, 2006 ("Complaint" or "Compl.") at 22.

[3] The breakdown of the sales by the director defendants during this period is as follows:

- Larson sold 300,000 shares from April 25 to August 19, 2003 disposing of approximately 39% of his total holdings. His last stock sale before that period was in September 2002.
- Pesch sold 146,000 shares from April 25 to August 14, 2003 disposing of approximately 69% of his total holdings. His last stock sale was in May 2002.
- Dowdell sold 61,900 shares from May 1 to September 18, 2003 disposing of approximately 32% of his total holdings. His last stock sale was in December of 2001.

that these sales totaled, in the aggregate, approximately $47 million and were unusual when compared to Defendants' prior trading history.

C. Procedural History

On January 6, 2004 Romero sought inspection of CEC's books and records under Section 220 of the Delaware General Corporation Law ("DGCL").[4] The important information Romero gleaned from these documents consisted of relevant minutes from audit committee meetings that discussed the accusations of malfeasance at Gibbs. Romero relied heavily on this information in the derivative complaint she filed on June 3, 2005 and the amended derivative complaint she filed on October 12, 2005. Romero did not make a pre-suit demand upon CEC and her Complaint contains a number of averments in support of demand excusal. Romero alleged that Defendants, except for Chookaszian, sold over $46 million worth of CEC stock in mid-2003 based on material non-public information in breach of their fiduciary duties. She also asserted that

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- Lally sold 48,000 shares from April 25 to July 25, 2003 disposing of approximately 49% of his total holdings. His last stock sale was in March of 2002.
- Laub sold 40,000 shares from April 30 to July 25, 2003 disposing of approximately 74% of his total holdings. His last stock sale was in September of 2002.
- Ogata sold 28,500 shares from April 25 to August 19, 2003 disposing of approximately 44% of his total holdings. His last stock sale was in September of 2002.

[4] 8 *Del. C.* § 220. Pls.' Opening Supp. Submission ("POSB") at 1. Defendants required Romero to sign a confidentiality agreement before they would release the pertinent records. Due to this agreement, Romero filed her derivative complaint and amended derivative complaint under seal. Defendants also filed their opening brief under seal.

Defendants breached their fiduciary duties by failing to properly address "obvious and pervasive problems with CEC's accounting and internal control practices and procedures."[5]

On July 5, 2005, Defendants responded with a motion to dismiss pursuant to Court of Chancery Rule 12(b)(6) or alternatively for failure to make a demand on the Company as required under Rule 23.1.[6] In their opening brief submitted on August 19, 2005, Defendants sought to have the Romero lawsuit dismissed, or alternatively stayed, in favor of an earlier filed lawsuit pending in the United States District Court for the Northern District of Illinois, captioned *McSparran v. Larson*, that included similar factual allegations and claims.[7] On October 26, 2005, Defendants filed a third motion to dismiss that reiterated the arguments made in their July 5 motion and added an assertion that Romero lacked standing because she did not hold stock in CEC at the time of the challenged insider stock sales.

After Defendants raised the standing issue, Neel filed his complaint on May 15, 2006. Because Neel acquired his stock before the sales in question, he clearly had standing. To strengthen Neel's allegations, Romero sought to share with him the

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5 Deriv. Compl., filed June 3, 2005, at 39.

6 Based on my decision to grant Defendants' motion to dismiss under Rule 23.1, I do not address Defendants' motion to dismiss under 12(b)(6). *See Rattner v. Bidzos*, 2003 WL 22284323, at *6 (Del. Ch. 2003) (declining to consider defendants' motion to dismiss based on Rule 12(b)(6) given the disposition of the defendants' motion to dismiss based on Rule 23.1).

7 *See McSparran ex rel. Career Educ. Corp. v. Larson*, 2007 WL 684123 (N.D. Ill. Feb. 28, 2007) (hereinafter *McSparran*).

information she received from her Section 220 inspection. The Company opposed this request citing the same confidentiality concerns it previously raised with Romero. On April 28, 2006, I granted Romero's request to unseal her amended derivative complaint. Thereafter, Neel amended his complaint to incorporate the same operative facts as those alleged in Romero's complaint. Neel also named the same Defendants as Romero, except for Chookaszian.[8]

On July 17, 2006, I granted a motion by Romero and Neel to consolidate their derivative actions. Plaintiffs filed their consolidated derivative complaint (the "Complaint") on July 18, 2006, and after further extensive briefing by the parties, the Court heard argument on Defendants' motion to dismiss on March 8, 2007. At argument the Court invited supplemental briefs on the effect of the district court's February 28, 2007 dismissal with prejudice of the *McSparran* litigation. Thereafter, the parties submitted both opening and answering supplemental briefs on that issue.

D. Other Proceedings in Illinois and Delaware

In light of the accusations and regulatory investigations against CEC, a number of lawsuits were filed in state and federal court alleging similar facts and asserting similar claims. Based on the common issues in these suits, several of them were consolidated or stayed in the interest of judicial economy.

First, several federal securities class actions were filed against CEC in the U.S. District Court for the Northern District of Illinois. These actions were consolidated and

[8] This departure from Romero's pleadings apparently stems from the fact that Neel focused his allegations on the insider trading claims. Neither Plaintiff challenged any of Chookaszian's stock sales.

captioned as *In re Career Education Corp. Securities Litigation* (the "Federal Securities Litigation").[9] The plaintiffs in the Federal Securities Litigation did not seek an inspection of CEC's books and records; instead, they relied primarily on interviews with current and former employees to form their complaint. The putative class alleged that CEC made false and materially misleading statements and omissions in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5.[10] These statements and omissions primarily pertained to student starts, student populations, job placements, and accounting disclosures.[11] The plaintiffs asserted that the defendants made the challenged representations on the Company website, as well as in press releases, SEC filings, and conference calls.[12]

On February 11, 2005, the district court granted CEC's motion to dismiss the complaint in the Federal Securities Litigation without prejudice and permitted the plaintiffs to file an amended complaint by May 11, 2005. The plaintiffs filed an amended complaint, but the court again ruled that the plaintiffs did not meet their burden under Rule 23.1. While the court gave the plaintiffs an opportunity to file a third amended complaint, they did not do so.

In addition to the Federal Securities Litigation, the plaintiffs in *McSparran*, as referenced earlier, filed a derivative action on behalf of CEC in the Northern District of

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9 2006 WL 999988 (N.D. Ill. Mar. 28, 2006).

10 *Id*. at *1.

11 *Id*.

12 *Id*.

Illinois.[13] After the court granted a motion to dismiss on May 3, 2006, the plaintiffs in *McSparran* responded by filing an amended complaint. The defendants again moved to dismiss, however, and the court dismissed the claims in *McSparran* with prejudice on February 28, 2007.[14]

A short discussion of *McSparran* is appropriate, because Defendants in this case urge the Court to give preclusive effect to the dismissal of that action. *McSparran* involved substantially similar factual allegations and claims to those before this Court. The plaintiffs in *McSparran* named all of the Defendants implicated in this lawsuit.[15] While the plaintiffs in *McSparran* asserted eight separate claims for relief, not all of them are relevant to this case.[16] The plaintiffs in *McSparran* averred that the defendants breached their fiduciary duties by actively fabricating critical internal performance metrics, such as enrollment figures and accounting numbers, and then sold their stock at an inflated price.[17] In addition, the plaintiffs claimed that the defendants breached their fiduciary duties by failing to properly monitor the Company.[18] The latter claim asserted

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13 *McSparran v. Larson*, 2006 WL 250698 (N.D. Ill. Jan. 27, 2006). The *McSparran* action was consolidated with another derivative action, *Ulrich v. Larson*, No. 04 Civ. 4778 (N.D. Ill. filed July 20, 2004).

14 *McSparran v. Larson*, 2007 WL 684123 (N.D. Ill. Feb. 28, 2007).

15 Verified S'holders' Am. Deriv. Compl. at 14-19, *McSparran v. Larson*, No. 04 C 0041 (N.D. Ill. filed June 8, 2006) ("*McSparran* Complaint") attached as Ex. A to Ralston Aff.

16 *Id*. at 129-34.

17 *McSparran*, 2007 WL 684123, at *1.

18 *Id*.

that the defendants violated their obligations to the Company as articulated in the *Caremark* case by failing to respond to legitimate indications of wrongdoing.[19]

The plaintiffs in *McSparran* argued that demand was futile under two alternative theories: (1) because the board of directors were beholden to Larson, the President and CEO; and (2) because a majority of the directors faced a substantial likelihood of liability, and therefore were interested. The district court summarily dismissed the first argument, noting that the plaintiffs had not pled any particularized facts that the directors were financially or personally dependent on the CEO.[20]

In support of their second argument, the plaintiffs emphasized that the defendants faced a substantial likelihood of liability from their purportedly improper stock sales, as well as their failure to properly address wrongdoing that came to their attention. As to the first allegation the plaintiffs claimed that the directors perpetrated a scheme to inflate CEC's stock price by falsifying enrollment and accounting figures so they could sell their stock at a higher price.[21] The court again cited the inadequacy of the pleadings in ruling that the plaintiffs could not show the directors were interested on this basis.

Citing the extensive factual allegations in the *McSparran* Complaint, which include the key facts alleged in this case and more, the court focused on the aspect of the plaintiffs' argument challenging the board's oversight of CEC. The plaintiffs argued that the defendants knew of impropriety taking place and breached their fiduciary duties by

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19 *Id*.; *see In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959 (Del. Ch. 1996).

20 *McSparran*, 2007 WL 684123, at *4.

21 *Id*.

failing to take corrective steps to rectify it. The court found that the plaintiffs failed to plead particularized facts that a majority of the board faced a substantial likelihood of liability due to their oversight of the Company. Noting the difficulty that plaintiffs have experienced in attempting to succeed on a fiduciary duty claim based on *Caremark*, the court found that the directors did not face the requisite threat of liability.

In addition, the *McSparran* court held that the plaintiffs had not made a sufficient showing of a threat of liability based on the insider trading claims, although its discussion of this issue is rather abbreviated. The court described the plaintiffs' allegations as follows:

> Defendants were allegedly . . . active participants in a scheme to report false accounting of revenues and enrollment figures so that they could sell their holdings of CEC stock at inflated prices . . . . Either of these . . . scenarios could result in personal liability for defendants. However, [it is not] established with the requisite level of particularity in the [a]mended [c]omplaint.[22]

The court's opinion indicates that it understood that plaintiffs had asserted claims for insider trading.[23] Nevertheless, the court dismissed all of the plaintiffs' claims for failure to establish demand futility under Rule 23.1.

The plaintiffs appealed the district court's ruling. On May 30, 2007, however, the Court of Appeals for the Seventh Circuit granted a motion by the *McSparran* plaintiffs-appellants to dismiss their appeal. Thus, the dismissal of the *McSparran* case is final.

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[22] *Id*. at *6.

[23] *See id*. at *2, 5-6.

The termination of *McSparran* influenced the disposition of at least one state court action that had been stayed pending the outcome of that litigation. In *Xiao-Qiong Huang v. Larson*, pending in Illinois state court,[24] the Illinois court gave the plaintiffs 21 days to voluntarily dismiss their complaint or explain why their case should not be dismissed, based on the final determination in *McSparran* on the same issues. The plaintiffs assented to the dismissal of their complaint with prejudice on June 27, 2007.[25]

E. Plaintiffs' Allegations

The core of Romero and Neel's Complaint derives from alleged falsification of records at three of CEC's eighty-two schools and regulatory reviews of those allegations and the Company's treatment of its allowance for doubtful accounts. Relying on this factual background, Plaintiffs assert that Defendants breached their duty of loyalty by engaging in insider selling based on material non-public information. Plaintiffs also assert a *Caremark* claim that Defendants breached their fiduciary duties by willfully ignoring pervasive problems with CEC's accounting and internal controls procedures, when they had a duty to take corrective steps to alleviate those problems.[26] Plaintiffs

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24 No. 04 Civ. 10579 (Ill. App. Ct. filed July 2, 2004).

25 *Nicholas v. Dowdell*, another derivative action which was filed in this court on November 10, 2004, no further activity has occurred since this court stayed that case on March 17, 2005. No. 819-N (Del. Ch. filed Nov. 10, 2004).

26 Plaintiffs' third and final claim is for unjust enrichment. Defendants ignored this claim, and Plaintiffs did not mention it at argument or in their subsequent briefs. The Court therefore assumes that any and all arguments regarding demand futility as to Plaintiffs' unjust enrichment claim are subsumed in Plaintiffs' arguments as to the insider trading claim.

made no pre-suit demand on the CEC board as required under Rule 23.1; instead, they put forth three independent grounds for excusing demand.

1. Insider trading claim

Plaintiffs allege that Defendants sold their stock when they learned of possible falsification of records at Brooks College in Sunnyvale and Long Beach, California ("Brooks College"), as well as Brooks Institute.[27]

Plaintiffs specifically allege that Defendants, with the exception of Dowdell, became aware of the allegations of widespread records tampering at Brooks College in a meeting on April 13, 2003.[28] Following this initial revelation, Plaintiffs maintain that the same group of Defendants participated in another meeting on April 14, 2003, where they engaged their legal advisor to investigate the allegations regarding Brooks College.[29] According to the Complaint, Defendants, with the exception of Dowdell, reviewed the results of this investigation on May 19, 2003 at an audit committee meeting, and Ogata made suggestions to address the problems. The audit committee agreed with Ogata's

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[27] The disclosure on November 17, 2003 concerned Gibbs. The April and May, 2003 audit committee meetings concerned falsification at Brooks College. The September 8, 2003 letter and the subsequent disclosure on December 3 concerned Brooks Institute.

[28] Plaintiffs allege that Defendants Larson, Pesch, Laub, Ogata, and Chookaszian participated in a teleconference on April 13, 2003 where they discussed phone calls made on April 11, 2003 from the controller of Brooks College, Kenny Sader, to Chookaszian, Lally and Ogata. In these phone calls, Sader allegedly reported to Chookaszian, Lally and Ogata that he had become aware of "widespread falsification of records at Brooks College." Compl. at 8.

[29] Defendants engaged the law firm of Kattin Muchin Zavis Rosenman to conduct the investigation.

recommendations and concluded that no action beyond those was necessary. Roughly two weeks later Defendants, other than Chookaszian, began selling large portions of their holdings, which did not comport with their prior dispositions. Plaintiffs accuse Defendants of engaging in this seemingly irregular trading activity to liquidate much of their stock before the allegations regarding fabrications of records became public and depressed the CEC stock price.[30]

2. Oversight/*Caremark* claim

Plaintiffs' *Caremark* claim asserts that Defendants failed to fulfill their oversight responsibilities by not properly addressing the problems that later were exposed by former employees and regulators. These problems included not only the allegations regarding Brooks College and Brooks Institute, but also the reported activity at Gibbs. Plaintiffs allege that despite numerous warning signs Defendants failed to address CEC's problems decisively with remedial action, as they were required to do so as fiduciaries.

3. Demand futility allegations

Plaintiffs in this derivative action aver that they did not make a demand upon the Company under Rule 23.1 because doing so would have been futile. Plaintiffs base this contention on three separate arguments: (1) that the directors are not independent due to their history of business relationships with one another; (2) that each of the Defendants

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[30] Plaintiffs also contend that on September 8, 2003 all Defendants received a letter from a former registrar at a separate school, Brooks Institute, that contained allegations of employees manipulating student records and improper regulatory compliance. All the challenged stock sales occurred well before September 8, except for the sale of 2,603.3 shares on September 18, 2003 by Dowdell. Compl. at 13.

faces a substantial likelihood of liability based on their failure to address red flags in the Company's accounting and internal controls; and (3) that five of the nine directors face a substantial likelihood of liability for having made improper stock sales.

4. Claim and issue preclusion

Despite the final dismissal with prejudice in *McSparran*, Plaintiffs defended the viability of their claims going forward in their supplemental briefs. Plaintiffs contend, and Defendants agree, that under principles of *res judicata* or claim preclusion the ruling in *McSparran* only applies to their demand futility arguments and not their substantive claims, because the *McSparran* court based its decision solely on Rule 23.1.[31]

On the other hand, Plaintiffs concede that collateral estoppel or issue preclusion applies to their Rule 23.1 arguments. Furthermore, in Plaintiffs' supplemental briefs and oral argument, they essentially acknowledge that the dismissal in *McSparran* precludes further litigation of their demand futility arguments, except to the extent they relate to their insider trading claims.[32] Plaintiffs contend that their insider trading claims remain viable, because the *McSparran* decision only addressed demand futility in terms of the independence of the directors and their continued disinterestedness in the face of the *McSparran* plaintiffs' *Caremark* claim. According to Plaintiffs, *McSparran* did not address whether the defendants would face a substantial likelihood of liability from their

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[31] POSB at 4 (citing *Nussbacher v. Continental Ill. Bank & Trust Co.*, 61 F.R.D. 399, 405 (N.D. Ill. 1973)).

[32] Tr. of Oral Argument ("Tr.") at 53-54.

stock sales, and thus does not collaterally estop Romero and Neel from pursuing that issue in this case.

During argument, Plaintiffs' counsel accentuated the fact that Romero, unlike the plaintiffs in *McSparran*, sought an inspection under Section 220 of the DGCL, and that the facts garnered from the documents produced differentiated Plaintiffs' Complaint from that in *McSparran*.[33] Specifically, they point to the minutes from the April 13 and 14 audit committee meetings.[34] Plaintiffs also emphasized that their claim for demand futility rests on insider trading, whereas the plaintiffs in *McSparran* did not put forth a substantially similar claim because they did not have access to the same information.[35]

Perhaps most importantly, Plaintiffs argue that their insider trading claims differ fundamentally from those in *McSparran*. In *McSparran*, the allegations suggested a collusive, top-down fraud intended to inflate the stock price to allow the defendants to sell their shares at a higher price. Plaintiffs here do not aver that Defendants were involved in masterminding a sweeping fraud, but rather that they received material inside information and then improperly sold their stock. The details of this portion of Plaintiffs' argument are addressed later in this opinion.

F. Defendants' Contentions

Defendants moved to dismiss Romero from this action for lack of standing and to dismiss the Complaint in general on several other grounds. They seek dismissal based on

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[33] Tr. at 44-45.

[34] Tr. at 57-58.

[35] Tr. at 45-46.

(1) the *McWane* doctrine, (2) the doctrine of *forum non conveniens*, (3) Plaintiffs' failure to plead demand, and (4) issue preclusion or collateral estoppel.

Defendants challenge Romero's standing because she failed to allege that she acquired and continuously held stock from the time of the challenged stock sales, citing Section 327 of the DGCL. Based on the earlier-filed *McSparran* litigation then pending in federal court in Illinois, Defendants moved to dismiss or stay Romero and Neel's Complaint under the *McWane* doctrine regarding first-filed actions or, alternatively on doctrine of *forum non conveniens* grounds. In addition, Defendants seek dismissal based on their contention that Plaintiffs failed to make a demand upon the Company or demonstrate demand futility with the requisite factual particularity required under the heightened pleading standard of Rule 23.1.

In support of their argument under Rule 23.1, Defendants made several different arguments. First, they assert that mere allegations that several of the CEC directors worked together in the past are insufficient to demonstrate the inability of a majority of directors to consider a demand.[36] Next, Defendants argue that Plaintiffs' allegations that a majority of the CEC directors face a substantial likelihood of liability do not show demand futility.

Concerning the likelihood of liability on Plaintiffs' oversight claims, Defendants argue that those claims should fail on the merits based on the standard described in

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[36] Defendants rely on Delaware case law holding that "social and business ties alone do not give rise to a lack of independence." Defs.' Op. Supp. Br. ("DOSB") at 14-15 (citing *Apple Computer, Inc. v. Exponential Tech.*, 1999 WL 39547, at *12 (Del. Ch. 1999)).

Caremark. Under that standard, Plaintiffs must show that Defendants "knew or should have known the alleged pervasive, imprudent and illegal activity was occurring or had occurred; and made no good faith effort to remedy such misconduct."[37] Noting the difficulty of meeting this standard, Defendants argue, among other things, that the relatively few claims of misfeasance the directors became aware of were not sufficiently material to create a substantial risk of liability under *Caremark*.[38]

Defendants also contend that Plaintiffs' demand futility argument based on the insider trading claim fails in three respects: (1) there are no particularized facts that the alleged wrongdoing at Brooks College, Brooks Institute, and Gibbs actually occurred; (2) there are no particularized facts that any of the alleged improprieties had a material effect on CEC's finances or operations; and (3) there are insufficient pleadings to demonstrate that Defendants knew about the alleged problems, besides those at Brooks College, when they sold their stock.

Defendants assert that Plaintiffs' allegations regarding Brooks College lack particularity because they disclose nothing about the nature and extent of the falsifications and, in any event, that the non-public information was not material. The first mention of the Brooks Institute claims appeared in the September 8, 2003 letter. Because only one director traded stock after that date, Defendants further argue that a

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[37] Defs.' Op. Br. ("DOB") at 17. *See In re Caremark Int'l Deriv. Litig.*, 698 A.2d 959, 971 (Del. Ch. 1996).

[38] *See* Tr. at 49.

majority of the board still could independently and disinterestedly exercise its business judgment in responding to a demand on those claims.[39]

Finally, Defendants contend that the ruling in *McSparran* precludes Plaintiffs from presenting any of their demand futility arguments. Based on Plaintiffs' briefs, Defendants argue that the only claims Plaintiffs have advanced after *McSparran* are the insider trading claims. The plaintiffs in *McSparran*, according to Defendants in this action, made the same insider trading claims based on the same facts as Plaintiffs in this action, including the references to the minutes from the April and May 2003 audit committee meetings. Defendants therefore contend that the federal courts' dismissal of all of the plaintiffs' claims in *McSparran* for lack of demand precludes Plaintiffs here from relitigating the demand futility issue.

II.

Generally when considering a motion to dismiss for failure to plead demand the court is limited to the allegations in the complaint. The court must accept the well-plead allegations in the complaint as true and draw all reasonable inferences in favor of the plaintiffs.[40] When considering a motion to dismiss, the court also may take judicial notice of publicly filed documents,[41] such as documents publicly filed in litigation pending in other jurisdictions.

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39 DOB at 21.

40 *Guttman v. Huang*, 823 A.2d 492, 499 (Del. Ch. 2003).

41 *In re Wheelabrator Techs., Inc. S'holders Litig*., 1992 WL 212595, at *12 (Del. Ch. 1992); *see also Diceon Elec., Inc. v. Calvary Partners, L.P.*, 772 F. Supp. 859, 861 (D. Del. 1991).

1. Standing

The primary purpose of standing is to ensure the plaintiff has "suffered a redressable injury."[42] In the context of a derivative claim, this principle, embodied in Section 327 of the DGCL, requires the plaintiff to have held shares in the corporation at the time of the transaction in question and to continuously hold shares throughout the litigation.[43] Romero does not allege that she held CEC stock until after the challenged stock sales. Thus, she has no standing as to any of the insider trading claims.[44] The only Plaintiff in this action who has standing to pursue the asserted insider trading claims is Neel.

2. McWane doctrine

Defendants moved to dismiss this litigation under the *McWane* doctrine based on the first-filed *McSparran* litigation.[45] Under *McWane*,[46] this Court has the discretion to stay or dismiss a proceeding "in favor of a first-filed action in another jurisdiction."[47]

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42 *Leboyer v. Greenspan*, 2006 WL 2987705, at *3 (Del. Ch. 2006).

43 8 *Del. C.* § 327.

44 Because Romero's allegations in support of her *Caremark* claim include the period of time after she acquired her stock, she does appear to have standing to pursue that claim.

45 Plaintiffs attempt to claim the date of their Section 220 demand as the imputed date of their later filed derivative action. Vice Chancellor Lamb, however, recently rejected this argument as a matter of law. *See Kaufman v. Kumar*, 2007 WL 1765617, at *2 (Del. Ch. 2007).

46 *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng. Co.*, 263 A.2d 281 (Del. 1970).

47 *Chadwick v. Metro Corp.*, 2004 WL 1874652, at *2 (Del. 2004).

The Court may invoke this doctrine when "(1) a first-filed prior pending action exists in another jurisdiction, (2) that action involves similar parties and issues, and (3) the court in the other jurisdiction is capable of rendering prompt and complete justice."[48]

Defendants argue that because the plaintiffs in *McSparran* filed their derivative complaint involving similar parties and issues, on January 5, 2004, approximately 18 months before Romero filed her complaint in June of 2005, involving similar parties and issues, *McWane* supports entering a stay or dismissal of this litigation. I need not address Defendants' argument, however, because the district court dismissed the *McSparran* Complaint with prejudice on February 28, 2007 and on May 30, 2007, the Seventh Circuit granted the plaintiffs' motion to dismiss their appeal of that decision. Thus, there no longer is any first-filed action pending elsewhere, and *McWane* does not apply.[49]

3. *Forum non conveniens*

Defendants also argue that, even if *McWane* does not apply, this litigation should be dismissed pursuant to the doctrine of *forum non conveniens*. The analysis under *forum non conveniens* requires this Court to review six factors when deciding whether to stay or dismiss an action. These factors are: "(1) the applicability of Delaware law, (2) the relative ease of access of proof, (3) the availability of compulsory process for witnesses,

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[48] *Kaufman*, 2007 WL 1765617, at *2.

[49] There is a similar, earlier-filed action pending in this Court, namely *Nicholas v. Dowdell*. *See supra* note 25. Defendants, however, based the aspects of their *McWane* and *forum non conveniens* arguments related to the existence of co-pending litigation elsewhere solely on the *McSparran* case. Moreover, the *Nicholas* action has been stayed and has not progressed to the same extent that this action has. Therefore, that case provides no basis for dismissing or staying this action.

(4) the pendency or non-pendency of a similar action or actions in another jurisdiction, (5) the possibility of a need to view the premises; and (6) all other practical considerations that would make the trial easy, expeditious, and inexpensive."[50] Defendants must show that litigating in Delaware would impose an "overwhelming hardship" on them, not simply an inconvenience.[51]

Defendants based their *forum non conveniens* argument primarily on the pendency of the *McSparran* litigation in what they contended was a much more convenient forum. As with their *McWane* argument, the termination of *McSparran* effectively mooted Defendants' *forum non conveniens* argument. I therefore deny that portion of Defendants' motion to dismiss.

4. Issue preclusion of demand futility allegations

Next, I consider the potential issue preclusive effect of the decision in *McSparran* on this litigation. This court recently addressed the preclusive effect of a judgment in a derivative action in federal court on a plaintiff's demand futility allegations in *West Coast Management & Capital, LLC v. Carrier Access Corp*.[52] In that case, the court followed the full faith and credit requirements "constitutionally mandated" in federal court. The court also observed that, "when the original decision is in federal court, federal issue

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50 *Ryan v. Gifford*, 918 A.2d 341, 351 (Del. Ch. 2007) (citing *In re Chambers Dev. Co. S'holder Litig.*, 1993 WL 179335, at *6 (Del. Ch. 1993)).

51 *Id.* (citing *Berger v. Intelident Solutions, Inc.*, 906 A.2d 134 (Del. 2006)).

52 914 A.2d 636 (Del. Ch. 2006).

preclusion law likely applies."[53] The *West Coast* case did not determine, however, the extent to which issue preclusion applies to a subsequent action, such as this case, commenced by a different derivative plaintiff.[54]

West Coast noted the trend in recent federal case law extending collateral estoppel to different plaintiffs in a second derivative suit.[55] Those cases justified the extension of the doctrine based on the unique position of the parties in derivative suits. Because the corporation is the true party in interest in a derivative suit, courts have precluded different derivative plaintiffs in subsequent suits.[56] This commonality lends itself to the application of collateral estoppel or issue preclusion. It also raises legitimate concerns, however, as to the adequacy of the representation in the prior proceeding. Where a plaintiff alleges that the interests of the corporation were not suitably represented in the prior proceeding collateral estoppel may not apply.[57]

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53 *Id*. at 643.

54 In *West Coast*, the court stated, "While a prior suit by another plaintiff with similar allegations of demand futility may bar a second plaintiff from filing the same suit, if the second plaintiff makes substantially different allegations of demand futility based on additional information, issue preclusion from both a logic and fairness standpoint would not apply." *Id*. at 643 n.22.

55 *Id*. (citing *Leboyer v. Greenspan*, 2006 WL 2987705 (C.D. Cal. Oct. 16, 2006); *Henik ex rel. LaBranche & Co. v. LaBranche*, 433 F. Supp. 2d 372 (S.D.N.Y. 2006); *In re Sonus Networks, Inc. S'holder Deriv. Litig.*, 422 F. Supp. 2d 281 (D. Mass. 2006). *But see Ji v. Van Heyningen*, 2006 WL 2521440 (D.R.I. Aug. 29, 2006)).

56 *Henik*, 433 F. Supp. 2d at 380; *Leboyer*, 2006 WL 2987705, at *3 ("differing groups of shareholders who can potentially stand in the corporation's stead are in privity for purposes of issue preclusion").

57 *Henik*, 433 F. Supp. 2d at 381.

Romero and Neel's Complaint does not challenge the adequacy of the representation in *McSparran*. In arguing against the application of issue preclusion here, the only criticism Plaintiffs leveled against the plaintiffs in *McSparran* was that their allegations were less compelling because they did not have the benefit of facts garnered from a Section 220 demand. Thus, Romero and Neel did not directly challenge the adequacy of the plaintiffs' representation in *McSparran*. Moreover, while the plaintiffs in *McSparran* did not pursue a Section 220 action, the amended complaint they filed on June 8, 2006 contained the same information Plaintiffs rely on to distinguish their allegations in this case. Undoubtedly, the *McSparran* plaintiffs took these allegations from Romero's complaint after this Court unsealed it on April 28, 2006.[58]

Consistent with recent federal cases and the dictum in *West Coast*, Romero and Neel may be precluded from relitigating the issue of demand futility based on the final judgment in *McSparran*. To bar litigation on a specific issue on grounds of issue preclusion, the moving party must demonstrate the following elements:

> (1) the issue sought to be precluded must be the same as that involved in the prior litigation, (2) the issue must have been actually litigated, (3) the determination of the issue must have been essential to the final judgment, and (4) the party against

[58] Plaintiffs argue that the "efficacy" of the Section 220 device would be hindered if this Court precludes issues proffered by Plaintiffs based on prior litigation that did not include a Section 220 demand. While the Delaware courts have encouraged prospective plaintiffs to make a Section 220 demand before filing a derivative suit, there is no risk in this case that the application of issue preclusion will undercut that principle. The reason is simple: even though the plaintiffs in *McSparran* did not pursue a Section 220 demand, the *McSparran* Complaint contained all of the key factual allegations that Plaintiffs rely on in this action.

> whom estoppel is invoked must be fully represented in the prior action.[59]

Resolution of the question of issue preclusion may render it unnecessary to address the merits of Plaintiffs' demand futility arguments. Accordingly, I begin by analyzing whether any of those arguments remains viable in the wake of the *McSparran* decision.

a. Potential *Caremark* liability and lack of board independence

Plaintiffs did not dispute, at argument or in their supplemental briefs, Defendants' claims that the decision in *McSparran* precludes them from continuing to litigate the issues of demand futility based on either an alleged lack of director independence or exposure to potential liability based on Plaintiffs' *Caremark* claims. Indeed, at argument Plaintiffs specifically acknowledged that the *Caremark* issue likely would be precluded in light of the final determination in *McSparran*.[60]

The record on Defendants' motion to dismiss indicates that all of the elements for application of issue preclusion exist as to Plaintiffs' arguments of demand futility based on Defendants' independence and potential liability for their oversight of the Company. The federal court in Illinois had before it the same factual allegations and claims presented in this case. Those issues were actually litigated and determined by a final judgment.[61] Count III of the Consolidated Complaint in this action asserts a *Caremark*

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59 *La Preferida, Inc. v. Cerveceria Modelo, S.A. de C.V.*, 914 F.2d 900, 906 (7th Cir. 1990).

60 Tr. at 52-53.

61 Generally, for an issue to be "actually litigated," the parties must have had notice, opportunity, and an incentive to pursue the same issues in the prior proceeding. *Leboyer v. Greenspan*, 2006 WL 2987705, at *2 (C.D. Cal. Oct. 16, 2006).

claim for breach of fiduciary duties based on Plaintiffs' accusations that the director Defendants "willfully ignored the obvious, pervasive and material problems with CEC's accounting practices and procedures, internal controls, and legal and regulatory compliance and failed to make a good faith effort to correct the problems or prevent their occurrence."[62] Count I of the operative complaint in *McSparran* makes a similar lack of oversight claim.[63] The defendants in that action moved to dismiss the *Caremark* claim for failing to plead demand or demand futility with the requisite particularity. The district court granted that motion after being fully apprised of McSparran's arguments to excuse demand on the grounds that a majority of the Board lacked independence or were interested because they faced a substantial likelihood of liability for the wrongs alleged by McSparran. In granting the defendants' motion to dismiss, the court necessarily decided both of those issues in the defendants favor. Lastly, the ruling in *McSparran* satisfies the finality requirement in that it resulted in a dismissal with prejudice in the district court and the plaintiffs ultimately abandoned their appeal of that ruling.

For these reasons, I conclude under principles of issue preclusion that the dismissal with prejudice of the derivative complaint on behalf of CEC in *McSparran* bars Plaintiffs in this action from relitigating the issue of whether a demand would be futile because the directors lacked independence or because they were subject to a claim for breach of fiduciary duty under *Caremark*.

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62 Compl. ¶ 62.

63 *McSparran* Compl. at 129-30.

b. Insider trading

Plaintiffs deny that the *McSparran* decision provides any basis to preclude their litigating the issue of demand futility based on the directors' potential liability as a result of the insider trading claims in this case. According to Plaintiffs, "McSparran contains absolutely no 'finding' on whether a majority of the Board faces a substantial likelihood of liability by reason of their stock sales."[64] Further, Plaintiffs contend that Defendants bear the burden of proving that the *McSparran* court previously decided the same issue related to insider trading.

The underlying issue presented here and, according to Defendants, in *McSparran* is whether Plaintiffs have pled particularized facts sufficient to excuse demand under the heightened pleading standard of Rule 23.1. It is well settled that a derivative action must first be presented to the board of directors to allow them to decide whether they should pursue the claim. This requirement recognizes the directors inherent power to manage the affairs of the corporation under Section 141(a) of the DGCL.[65] Plaintiffs will only be relieved of this obligation when they meet the exceptions defined by the Supreme Court of Delaware in the seminal cases of *Aronson v. Lewis*[66] and *Rales v. Blasband*.[67]

In *Aronson*, the court deemed demand futile where "under the particularized facts alleged, a reasonable doubt is created that (1) the directors are disinterested and

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64 Pls.' Ans. Supp. Br. ("PASB") at 3.

65 8 *Del. C.* § 141(a).

66 473 A.2d 805 (Del. 1984).

67 634 A.2d 927 (Del. 1993).

independent and (2) the challenged transaction was otherwise the product of a valid exercise of business judgment."[68] The plaintiff need only satisfy one prong to meet the standard.[69] The court in *Rales* outlined three situations where *Aronson* would not apply. Those are: "(1) where the board made a business decision but a majority of the directors who made the decision have since been replaced; (2) where the claim at issue does not arise from a business decision of the board; and (3) when a board of a different company made the challenged business decision."[70] In this case, Plaintiffs challenge insider stock sales made by various directors. Because this is not a specific action taken by the entire board, *Rales* is the proper standard.[71] That standard requires this Court to determine whether, "the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could have properly exercised its independent and disinterested business judgment in

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68 *Aronson*, 473 A.2d at 814-15.

69 *Brehm v. Eisner*, 746 A.2d 244, 256 (Del. 2000).

70 *Rales*, 634 A.2d at 933-34.

71 *Rattner v. Bidzos*, 2003 WL 22284323, at *8 (Del. Ch. 2003). *See also Guttman v. Huang*, 823 A.2d 492, 503 (Del Ch. 2003) (applying *Rales* when determining whether directors who allegedly sold stock on inside information were interested for purposes of demand futility). The court in *McSparran* applied the *Aronson* test for determining whether demand should be excused. *McSparran*, 2007 WL 684123, at *3. For purposes of the issues currently before me, however, the *Aronson* and *Rales* standards are essentially the same. *See Khanna v. McMinn*, 2006 WL 1388744, at *12 (Del. Ch. May 9, 2006) (where particularized facts created a reasonable doubt that a majority of the directors are independent and disinterested, demand futility under *Rales* or the first prong of *Aronson* will be met).

responding to a demand."[72] Where a director faces a substantial threat of liability from the challenged transaction, that director will be interested under *Rales.*[73]

For the reasons stated below, I conclude that, contrary to Plaintiffs' assertions, the plaintiffs in *McSparran* presented, among other things, the same insider trading claims as Romero and Neel and the same facts pertaining to insider trading and demand excusal. I also find that the court in *McSparran* necessarily resolved the same demand issue presented here as part of its decision to dismiss with prejudice all of the pending claims in that action.

In reaching these conclusions, I begin with a comparison of the operative pleadings: Romero and Neel's Consolidated Complaint, filed July 18, 2006, and the Amended Derivative Complaint in *McSparran*, dated June 8, 2006. Both documents include the expanded allegations that Plaintiffs say they developed from the results of Romero's Section 220 demand. This information encompasses everything Romero and Neel pled regarding their insider trading claims and their allegations of demand futility.[74] In addition, the operative complaints in *McSparran* and this case contain very similar claims for insider trading.

The Eighth Claim for Relief in *McSparran* is entitled, "Against the Insider Selling Defendants for Breach of Fiduciary Duty for Insider Selling and Misappropriation of

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72 *Rales*, 634 A.2d at 934.

73 *Id*. at 936.

74 *Compare* Compl. ¶¶ 19-26 *with McSparran* Compl. ¶¶ 125-128, 289.

Information."[75] This claim asserts that when they sold their stock the Insider Selling Defendants[76] knew or had reason to know:

> [P]roprietary non-public information concerning the Company's operations and financial condition. It was a proprietary asset belonging to the Company, which the Insider Selling Defendants used for their own benefit when they sold their holdings in Career Education stock at prices higher than they could have obtained had the market been aware, as they were, of the true state of the Company's operations and financial condition.
>
> At the time of their stock sales, the Insider Selling Defendants knew that the Company's financial condition was materially overstated and did not reflect the Company's substantial liability arising from its involvement in the manipulative financial aid and enrollment practices and other improper schemes described herein which, when reported, would cause the price of the Company's common stock to dramatically decrease. The Insider Selling Defendants' sale of Career Education common stock while in possession and control of this material adverse non-public information was a breach of their fiduciary duties.[77]

That claim closely corresponds to Count I of the Consolidated Complaint in this action. Count I, entitled, "Against the Individual Defendants other than Chookaszian for Breach of Fiduciary Duties (Insider Trading)," asserts that:

> At the time of each of the stock sales set forth herein, each of the Individual Defendants knew, but did not disclose publicly, the material information set forth in paragraphs 19-26. Each

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75 *McSparran* Compl. at 133.

76 As defined in the *McSparran* Complaint, the Insider Selling Defendants include all of the named individual Defendants in this action, except Chookaszian -- *i.e.*, Larson, Pesch, Dowdell, Lally, Laub, and Ogata - - and the following persons named as defendants in the *McSparran* action only: Todd H. Steele, Jacob P. Gruver, and Nick Fluge.

77 *McSparran* Compl. ¶¶ 315-316.

> of the Individual Defendants made each of their aforementioned stock sales on the basis of and because of this material non-public information.
>
> The Individual Defendants' sales of CEC common stock based on their knowledge of material non-public information was a breach of their fiduciary duties of loyalty and good faith.[78]

Plaintiffs' contention that Romero and Neel's insider trading claims differ substantially from those at issue in *McSparran* is not persuasive. The insider trading allegations in *McSparran* included not only the same allegations made in this case, but also additional allegations, as well. For example, the *McSparran* complaint also alleged that the director defendants made public disclosures denying the allegations of wrongdoing in order to boost the stock price of the shares they sold. The Complaint in this action did not include those allegations. As Plaintiffs here assert, the *McSparran* court did characterize the insider trading claim somewhat differently, stating: "the essence of the plaintiffs' [a]mended [c]omplaint is that defendants artificially inflated CEC's stock price so that they could sell their holdings of CEC's stock at a higher price than the true value of the company would warrant."[79] The insider trading claims in this case cover a shorter time period subsumed within the broader period at issue in *McSparran*.[80] Further, Plaintiffs in this action emphasize that the accused director

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78 Compl. ¶¶ 54-55.

79 *McSparran*, 2007 WL 684123, at *2.

80 The *McSparran* plaintiffs alleged that the same six director defendants implicated in this suit sold over $70 million in stock. According to the *McSparran* Complaint, these transactions generally occurred from April of 2003 to May of 2004. In addition to these sales, the plaintiffs in *McSparran* challenged $68 million in stock sales made by CEC officers. *McSparran* Compl. ¶¶ 121-22.

defendants traded with knowledge of adverse non-public information. For purposes of issue preclusion, however, I do not consider these differences material.

Although the *McSparran* court in its demand futility analysis specifically discussed the aspect of the plaintiffs' insider trading claims related to the defendants' having improperly *inflated* CEC's stock price, the language of the actual claims asserted in *McSparran* makes clear that they also included allegations that the insider defendants traded on material adverse, non-public information about CEC. Thus, I conclude that the similarities between the insider trading claims in *McSparran* and this action support application of the doctrine of issue preclusion.

Plaintiffs further argue that the *McSparran* court "declined to adjudicate the issue of whether a majority of the Board faced a substantial likelihood of liability for their allegedly improper stock sales."[81] Thus, the court, in Plaintiffs' view, did not address the key issue raised by their argument to excuse demand in the circumstances of this case. Plaintiffs rely heavily on the following statement in the opinion of the district court dismissing the *McSparran* action:

> The Amended Complaint pleads that the defendants improperly overvalued the company in order to raise the stock price and then sold their stock for a large profit. Although it is alleged that all but one of the defendants sold their stock, plaintiffs still fail to plead with particularity that a majority of CEC's Board of Directors face a substantial likelihood of personal liability *for reasons other than their stock sale* or generalized inferences about their roles as directors.[82]

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81 PASB at 4.

82 *McSparran*, 2007 WL 684123, at *5 (emphasis added).

Plaintiffs read this statement to mean that the *McSparran* court ignored the allegations of insider trading. I do not read the statement that way.

I understand the above-quoted statement to mean that the court recognized that mere allegations of stock sales by directors at a time when they possessed insider information generally are not sufficient to excuse a demand under Rule 23.1.[83] The *McSparran* court did focus most of its discussion of the demand futility issue on the allegations related to the *Caremark* claims, but not to the complete exclusion of the plaintiffs' other claims. One example is the court's conclusion regarding the alleged interestedness of the directors:

> Finally, as noted previously, even if plaintiffs pled with particularity certain allegations about a minority of the directors, the court need not consider the allegations because demand futility arises only when a majority of the directors are interested in the outcome of the litigation. Because the Amended Complaint fails to establish that a majority of CEC's directors face a substantial likelihood of personal

[83] *Guttman v. Huang*, 823 A.2d 492, 505 (Del. Ch. 2003) (refusing to excuse demand because plaintiffs failed to plead particularized facts that at the time the defendants made material stock sales they knew material non-public inside information) (cited in Defs.' Reply Br. at 11); *Stepak v. Ross*, 1985 WL 21137, at *5 (Del. Ch. Sept. 5, 1985)). I do not mean to suggest by this statement that the allegations regarding the stock sales of the director defendants in this case and in *McSparran* are not troubling. The magnitude and timing of those sales arguably do raise suspicion. The *McSparran* court, however, had those allegations before it in the context of a similar claim for insider trading, and appears, at least implicitly, to have considered them. Thus, this case does not fit the hypothetical scenario posited in *West Coast Mgmt. & Capital, LLC v. Carrier Access Corp.*, 914 A.2d 636, 643 n.22 (Del. Ch. 2006), in which a derivative plaintiff in a second case "makes substantially different allegations of demand futility based on additional information," and thereby potentially avoids the application of issue preclusion.

> liability, the plaintiffs cannot show demand futility, and the Amended Complaint must be dismissed.[84]

In sum, I conclude that the *McSparran* court did consider demand excusal in relation to all of the plaintiffs' claims, including those for insider trading, based on all the allegations in the *McSparran* Complaint, which included everything averred in this case. Thus, the doctrine of issue preclusion bars Plaintiffs from litigating its contention of demand futility in this case.[85]

III. CONCLUSION

For the reasons stated, the Court denies as moot Defendants' motion to dismiss or stay this action based on the pendency of an earlier filed action elsewhere or *forum non conveniens*, but grants Defendants' motion to dismiss Plaintiffs' Complaint for failure to satisfy the demand requirements of Court of Chancery Rule 23.1 based on the previous judgment to the same effect in the *McSparran* case. Accordingly, the derivative claims asserted in this action are dismissed with prejudice as to each of the named Plaintiffs.

IT IS SO ORDERED.

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84 *McSparran*, 2007 WL 684123, at *6.

85 Based on this conclusion, the Court need not address the merits of Plaintiffs' various demand futility arguments in this case.