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8 RYAN OSWALD,

9 Plaintiff,

10 v.

11 IDENTIV, INC., et al.,

12 Defendants.

Case No. [16-cv-00241-CRB](#)**ORDER DENYING MOTION TO  
DISMISS**

Ryan Oswald brings this shareholder derivative lawsuit on behalf of Identiv, Inc., claiming that Defendants, Identiv's Board of Directors and an executive,<sup>1</sup> breached their fiduciary duties and committed waste. See generally Second Amended Complaint ("SAC") (dkt. 38-3). Before Oswald can proceed on behalf of Identiv, he must plead particularized facts demonstrating that a demand upon the Identiv Directors would have been futile. This Court previously granted without prejudice Defendants' Motion to Dismiss Oswald's Amended Complaint for failure to adequately allege demand futility, and stayed the case to allow Oswald to investigate further and amend his complaint. Order (dkt. 34). Oswald has now amended, and Defendants again move to dismiss. See SAC; MTD (dkt. 43). As discussed below, Oswald's Second Amended Complaint includes new

<sup>1</sup> Identiv is the nominal defendant in a derivative capacity. The defendants in this action are: current Identiv directors Steven Humphreys, Gary Kremen, and James E. Ousley; former directors Jason Hart, Saad Alazem, and Daniel S. Wenzel; and Identiv's former Chief Financial Officer, Brian Nelson.

1 particularized facts sufficient to show demand futility. The Court therefore DENIES the  
2 Motion to Dismiss.

3 **I. BACKGROUND**

4 Identiv is a security technology company incorporated under the laws of the State of  
5 Delaware. SAC ¶ 16. Jason Hart was its CEO, and Ana Ruggiero was Hart's executive  
6 assistant until she was fired. See id. ¶¶ 18, 44–51. In April 2015, Ruggiero brought suit in  
7 Alameda Superior Court alleging a number of employment-related causes of action. Id.;  
8 see also Ruggiero v. Identiv, Inc., No. HG15764795 (Cal. Super. Ct. Alameda County.,  
9 filed Apr. 2, 2015). In her complaint, Ruggiero alleged that Hart had improperly charged  
10 Identiv for numerous personal expenses. SAC ¶¶ 45–50.

11 About a month after Ruggiero filed her complaint, Identiv disclosed that it would be  
12 unable to timely file certain executive compensation information with the U.S. Securities  
13 and Exchange Commission (SEC). Id. ¶ 2. Identiv's Board of Directors—  
14 then composed of Humphreys, Hart, Ousley, Kremen, Alazem, and Wenzel—formed a  
15 Special Committee to investigate the allegations in Ruggiero's lawsuit and any similar or  
16 related facts. Id. ¶¶ 53, 96. In November 2015, Identiv publicly disclosed that its  
17 independent auditor, BDO, had resigned because it was “unwilling to be associated with  
18 the consolidated financial statements prepared by management for any of the fiscal periods  
19 within 2015.” Id. ¶ 4.

20 Oswald then brought this shareholder derivative lawsuit against Identiv's Board of  
21 Directors, alleging that the Identiv Directors breached their fiduciary duty and wasted  
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1 corporate assets.<sup>2</sup> See Complaint (dkt. 1); FAC (dkt. 21). In November 2016, this Court  
2 granted without prejudice Defendants' Motion to Dismiss Oswald's Amended Complaint  
3 for failure to allege demand futility with particularity, and stayed the case "so that Oswald  
4 can exercise his rights under [Delaware law] to inspect Identiv's books and records."  
5 Order at 8. Oswald's Second Amended Complaint includes new facts and details obtained  
6 through this inspection.

7       Oswald's Second Amended Complaint alleges that the Board allowed Hart to  
8 systematically misuse and misappropriate Identiv's funds for his own personal indulgence.  
9       Oswald alleges that Hart spent tens of thousands of dollars on two parties in Las Vegas,  
10 then submitted the charges to Identiv for reimbursement.<sup>3</sup> SAC ¶¶ 48, 50. Board members  
11 Kremen and Humphreys attended these parties. Id. One party in early July 2014 included  
12 \$8,700 in "champagne showers,"<sup>4</sup> \$1,900 in massages for Kremen, \$5,000 in vodka, and  
13 \$5,000 at a restaurant. Id. ¶ 48. In September 2014, Hart, Nelson, Humphreys, Kremen,  
14 and five other people spent \$28,959 in Las Vegas, including \$14,500 at a nightclub and  
15 \$8,000 on upgraded hotel accommodations. Id. ¶ 50. Oswald alleges that Hart routinely  
16 submitted business expense reimbursement requests for other non-business purchases,  
17 including two drones, for approximately \$5,000, six computer servers for his home, for  
18 \$18,000 each, and \$3,000 in American Express gift cards. Id. ¶ 46.

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24       <sup>2</sup> This Court also handled the related securities class action, which involved the same facts as  
25 those in Oswald's original Complaint. See generally *Rok v. Identiv*, No. 15-cv-5775 CRB, 2017  
26 WL 35496 (N.D. Cal. Jan. 4, 2017). The Court dismissed the securities case, observing that the  
"allegations might support a derivative shareholder suit, . . . but they do not provide the necessary  
scienter in a securities fraud case." Id., 2017 WL 35496, at \*13.

27       <sup>3</sup> The documents Identiv produced in response to Oswald's books and records demand  
28 corroborate these expenses, originally described in the Ruggiero Complaint. See *id.* ¶ 56.

<sup>4</sup> A champagne shower involves shaking a champagne bottle in celebration and spraying it on  
oneself and one's friends. See, e.g., <https://www.youtube.com/watch?v=Dj-O9Dr1kSA>.

Oswald further alleges that, as detailed in the Ruggiero Complaint, Ruggiero raised her concerns about Hart's charges with the CFO, defendant Nelson, but Nelson took no action. Id. ¶ 48. In addition, Nelson gave Hart a personal loan of \$26,000, after which the Compensation Committee "suddenly" awarded Nelson equity compensation worth \$902,850. Id. ¶ 49. Identiv's public filings and Board materials corroborate the timing and amount of this award. Id. ¶ 49 n.2. Oswald alleges that Hart orchestrated the award as repayment for the loan and "in exchange for [Nelson's] silence" about Hart's misuse of corporate funds. Id. ¶ 6.

In May 2015, the Board established a Special Committee, composed of Board members Ousley and Wenzel, in response to the allegations in the Ruggiero Complaint. Id. ¶ 53. The Special Committee was to "consider, investigate, review, evaluate and analyze the facts, allegations and circumstances" of the Ruggiero Complaint, and "any similar or related facts . . . relating to expense reimbursements or payments on behalf of executive officers of the company." Id.; McGrath Decl. (dkt. 43-1), Ex. 15. The Special Committee was not empowered to make a final decision regarding its investigation or take any final action, only to "report its findings to the full Board and . . . recommend to the full Board what action to take, if any, in response to its findings." SAC ¶ 53. The Special Committee retained independent counsel<sup>5</sup> and the accounting firm, Deloitte, to assist in its investigation. Id. ¶¶ 54, 56.

Deloitte reviewed 1,987 expense reimbursement submissions, totaling

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<sup>5</sup> The source for this allegation, the BDO resignation letter discussed below, defines independent counsel as the "independent law firm" retained by the Special Committee together with a "forensic consultant hired by the law firm." See id. ¶ 78.

\$1,011,185.02.<sup>6</sup> See id. ¶ 62; McGrath Decl. Ex. 17 (“Deloitte Spreadsheet”).<sup>7</sup> Deloitte raised concerns about charges from one of the Las Vegas parties attended by defendants Hart, Kremen, and a “U.S. Marshals Contact,” John Bailey, repeatedly flagging the trip in its report as involving “potential bribery issues.” SAC ¶¶ 57, 58. Bailey was a federal employee “believed to have been subsequently influential in assisting Identiv obtain certain government contracts worth millions of dollars.” Id. ¶ 48. According to the Ruggiero Complaint, Hart initially labelled the expenses as “customer event – senior exec and Board plus customers including us marshall [sic].” Id. In the course of the Special Committee’s investigation, Hart reclassified the charges for Bailey’s lodging as “100% personal,” but maintained that his own lodging for the trip was “100% business.” Id. ¶ 58. Deloitte noted the inconsistency in its review: “How can Jason Hart’s lodging be 100% business when Mr. Bailey’s lodging is listed as 100% personal. Either Mr. Hart took Mr. Bailey to Las Vegas as a personal friend with no business intent or he took Mr. Bailey to Las Vegas with a business intent.” Id.

Deloitte identified many other red flags in addition to the bribery issue. In the Deloitte Report, it repeatedly observed that billing many of the challenged charges as business expenses might “not be acceptable for IRS purposes.” Id. ¶ 59. In connection with a \$14,500 dinner in Las Vegas at which defendants Hart and Kremen were present, Deloitte wrote: “This is not a ‘closing celebration dinner.’” Id. ¶ 60. Regarding the same trip to Las Vegas, Deloitte noted, “[t]o assist the Board of Directors in carrying out its

<sup>6</sup> Identiv produced the Deloitte Report to Oswald in response to his books and records demand. See Opp'n (dkt. 44-2) at 2 n.4.

<sup>7</sup> The Court requested and reviewed an electronic searchable version of the Deloitte Spreadsheet. See Order Directing Filing (dkt. 50).

1 fiduciary duties, Deloitte is prepared to provide the Board in excess of 1,000 pictures  
2 documenting this trip.” Id. Deloitte also flagged multiple expenses with the note,  
3 “Deloitte believes that the lack of support [for the charge] represents a business and  
4 potentially a tax issue,” and “Identiv should consult its tax attorneys on these matters.”  
5  
6 See, e.g., Deloitte Spreadsheet, ID# 1591, 1715 at Column L.

7 According to Identiv’s books and records production to Oswald, Deloitte discussed  
8 these issues with the independent counsel and the Board. SAC ¶¶ 57, 59. In its report,  
9 Deloitte stated that the reasons Hart gave for expenses associated with the Las Vegas  
10 parties (and many other expenses) were not sufficient to support a business purpose. Id.  
11 The Board “[noted] Deloitte’s position,” then made a “policy decision” to allocate the  
12 challenged charges, in whole or in part, as business expenses anyway. Id. The Board  
13 decided to treat the expenses associated with the U.S. Marshal contact, Mr. Bailey, as  
14 personal expenses. Id.

15 Deloitte concluded that \$518,601.36 of the charges it reviewed were non-business  
16 personal expenses, expenses that violated Company policy and could not be supported as  
17 business expenses, or possible business expenses that were incurred in violation of  
18 Company policy. See id. ¶ 62. The Board approved classification of an additional  
19 \$257,260.85 in expenses as business expenses, in many instances overriding Deloitte’s  
20 conclusion that the purpose provided was not sufficient to support a business purpose. See  
21 id.; compare Deloitte Spreadsheet column Q (“no”) with id. column S (amount approved  
22 by Board as business expense).

23 Oswald alleges that independent counsel asked the Special Committee to allow  
24 further investigation. See SAC ¶ 78 (“multiple requests by . . . the Independent Counsel. .

1 . . . Independent Counsel has communicated various other limitations in the scope of the  
2 Independent Investigation, including that the Independent Investigation was halted before  
3 Independent Counsel completed its planned investigative procedures. . . . limited advice  
4 provided by Independent Counsel”); id. ¶ 99 (“Special Committee’s counsel believed that  
5 additional investigation should be conducted”); id. ¶ 102 (same).  
6

7 There was no further investigation. On August 28, 2015, the Special Committee  
8 reported its findings and presented recommendations to the Board.<sup>8</sup> Id. ¶ 70. Hart was not  
9 present. Id. The Special Committee members, Ousley and Wenzel, expressed their view  
10 that the investigation “had been very extensive and thorough,” but “noted input from  
11 independent counsel to the Committee with respect to possible additional investigative  
12 work on certain items.” Id. ¶ 71. The non-committee board members present—  
13 Humphreys, Kremen, and Alazem—“unanimously accepted the recommendation of the  
14 [Special] Committee” to conclude the investigative phase of the Special Committee. Id.  
15

16 Identiv’s independent auditor, BDO, requested on multiple occasions that the Board  
17 investigate further, and resigned on November 23, 2015, essentially because the Board  
18 refused. Id. ¶ 78. BDO’s resignation letter<sup>9</sup> to the Board states that after it became aware  
19 of Hart’s “improper expenses, including relating to the entertainment of an employee of  
20 the US Marshals Service,” “in accordance with the requirements of Section 10A [of the  
21 Securities Exchange Act of 1934,] . . . BDO has sought to determine whether it is likely  
22 that an illegal act has occurred; and if so, the possible effect of each illegal act on the  
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27 <sup>8</sup> Identiv produced the Special Committee Report to Oswald in response to his books and records  
28 demand. See Opp’n at 2 n.5.

<sup>9</sup> Identiv produced the BDO letter to Oswald in response to his books and records demand. See  
Opp’n at 3 n.6.

1 financial statements of the Company.” Id. Despite “multiple requests by BDO,” the  
2 Special Committee refused to seek any legal advice from independent counsel regarding  
3 whether an illegal act had occurred, and halted the investigation “before Independent  
4 Counsel completed its planned investigative procedures.” Id. BDO determined that “the  
5 Company ha[d] not taken timely and appropriate remedial actions because of, at a  
6 minimum, the limitations on the scope of the Independent Investigation, the limited advice  
7 provided by Independent Counsel, and the limited actions taken regarding the on-going  
8 role and involvement of Mr. Hart with the Company.” Id. BDO advised that it was  
9 “unwilling to be associated with the consolidated financial statements prepared by  
10 management for the quarterly and annual financial reporting periods for the fiscal year  
11 ending December 31, 2015,” and resigned effective immediately. Id.

14 In addition to the allegations concerning Identiv’s investigation of the claims in the  
15 Ruggiero Complaint, Oswald also alleges that the Board gave Hart a golden parachute. In  
16 September 2015, Humphreys replaced Hart as the CEO of Identiv, but—despite the  
17 Special Committee’s conclusion that “Mr. Hart’s entertainment of a U.S. government  
18 employee in 2014 violated the Company’s Code of Conduct and Ethics,” id. ¶ 70—Hart  
19 continued to serve as President, id. ¶ 74. Identiv entered into a new compensation  
20 agreement with Hart, worth up to \$875,000 per year, including commissions and bonuses,  
21 plus valuable non-cash benefits. Id. After this action was filed, Hart resigned for reasons  
22 purportedly unrelated to the wrongdoing. Id. ¶ 86. Because Hart was not fired for cause,  
23 he received full severance. Id. ¶¶ 86, 107. Although Identiv’s amended Form 10-K for the  
24 year 2014 indicates that Hart was improperly reimbursed for \$111,015 in non-business  
25 expenses, he only repaid \$35,784 upon leaving Identiv. Id. ¶¶ 81, 89. Oswald alleges that  
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1 the true amount of company funds that Hart diverted is significantly higher than the  
2 \$111,015 that Defendants admit to in Identiv's 10-K filings. Id. ¶ 8.

3 Since this action was filed, Hart, Alazem, and Wenzel left the Board, and non-  
4 defendant director Nina B. Shapiro joined it. SAC ¶ 96. The current Board is Humphreys,  
5 Kremen, Ousley, and Shapiro. Id.

## 7 **II. LEGAL STANDARD**

8 “The derivative form of action permits an individual shareholder to bring suit to  
9 enforce a corporate cause of action against officers, directors, and third parties.”

10 Rosenbloom v. Pyott, 765 F.3d 1137, 1147 (9th Cir. 2014) (quoting Kamen v. Kemper Fin.  
11 Servs., Inc., 500 U.S. 90, 95 (1991)). “A shareholder seeking to vindicate the interests of a  
12 corporation through a derivative suit must first demand action from the corporation’s  
13 directors or plead with particularity the reasons why such demand would have been futile.”  
14 Id. at 1148 (citing Fed. R. Civ. P. 23.1). “The purpose of this demand requirement in a  
15 derivative suit is to implement ‘the basic principle of corporate governance that the  
16 decisions of a corporation—including the decision to initiate litigation—should be made  
17 by the board of directors or the majority of shareholders.’” Id. (quoting In re Pfizer Inc.  
18 S’holder Derivative Litig., 722 F. Supp. 2d 453, 458 (S.D.N.Y. 2010)).

22 Rule 23.1 requires a plaintiff to “allege with particularity . . . the reasons for the  
23 plaintiff’s failure to” make a demand. Fed. R. Civ. P. 23.1(b)(3). However, “[t]he  
24 substantive law which determines whether demand is, in fact, futile is provided by the state  
25 of incorporation of the entity on whose behalf the plaintiff is seeking relief.” Rosenbloom,  
26 765 F.3d at 1148 (citation omitted). Identiv is a Delaware corporation and Delaware law  
27 therefore applies.

1           In the context of pre-suit demand, the directors of a corporation enjoy the benefit of  
2 the business judgment rule, which “is a presumption that in making a business decision,  
3 the directors . . . acted on an informed basis, in good faith and in the honest belief that the  
4 action taken was in the best interests of the company.” Aronson v. Lewis, 473 A.2d 805,  
5 812 (Del. 1984). Demand is excused as futile where the plaintiff creates a reasonable  
6 doubt that the directors’ action was entitled to the protections of the business judgment  
7 rule. Id. at 808. “Plaintiffs are entitled to all reasonable factual inferences that logically  
8 flow from the particularized facts alleged, but conclusory allegations are not considered as  
9 expressly pleaded facts or factual inferences.” Rosenbloom, 765 F.3d at 1148 (quoting  
10 Brehm v. Eisner, 746 A.2d 244, 255 (Del. 2000)).

### 13           **III. DISCUSSION**

14           Defendants move to dismiss Oswald’s Second Amended Complaint on the grounds  
15 that (A) Oswald lacks standing because some of the alleged wrongdoing occurred before  
16 he was an Identiv shareholder, and (B) Oswald has not alleged particularized facts to  
17 demonstrate demand futility. As discussed below, both of Defendants’ arguments fail.

#### 19           **A. Standing**

20           A derivative plaintiff has no standing to sue unless he meets Rule 23.1’s  
21 requirements, Kona Enters., Inc. v. Estate of Bishop, 179 F.3d 767, 769 (9th Cir. 1999),  
22 and Rule 23.1 requires that a derivative plaintiff be a shareholder at the time of the alleged  
23 wrongful acts, Fed. R. Civ. P. 23.1(b)(1). Defendants argue that Oswald does not have  
24 standing to bring derivative shareholder claims because some of the alleged misconduct  
25 occurred before he became a shareholder. MTD at 2.

26           Oswald has been a shareholder of Identiv since September 24, 2014. SAC ¶ 15. He

1 therefore has standing to bring claims for alleged breaches of fiduciary duty or waste that  
2 occurred after September 24, 2014, but not before. See Kona, F.3d at 769. To the extent  
3 that Defendants allowed Hart to misuse corporate funds prior to September 2014, Oswald  
4 does not have standing to challenge this conduct.<sup>4</sup> However, even conduct that occurred  
5 before an individual was a shareholder may be relevant to the extent that it demonstrates a  
6 pattern of wrongful conduct. See In re MRV Commons., Inc., No. 08-cv-3800-GAF, 2010  
7 WL 1891717, at \*2 (C.D. Cal. May 10, 2010) (citing In re Zoran Corp. Derivative Litig.,  
8 511 F. Supp. 2d 986, 1010 (N.D. Cal. 2007))). Therefore, even though Oswald lacks  
9 standing to bring claims arising out of pre-September 2014 conduct, such conduct is still  
10 relevant for this limited purpose.

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13 Oswald also has standing to bring claims based on the Board's failing to conduct a  
14 legitimate investigation into Hart's wrongdoing, failing to hold Hart and Nelson to  
15 account, allowing Hart to repay substantially less than the total amount of money he  
16 diverted, and awarding Hart severance, because all of this conduct occurred after  
17 September 2014. See SAC ¶¶ 8, 44, 53. The Board took these actions in response to the  
18 Ruggiero Complaint, which was not filed until April 2015. Id.  
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## B. Demand Futility

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22 There are two tests for demand futility under Delaware law: (1) the test articulated  
23 in Aronson, 473 A.2d at 814, and (2) the test articulated in Rales v. Blasband, 634 A.2d  
24 927, 934 (Del. 1993). The Aronson test applies where a majority of the board of directors  
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27 <sup>4</sup> Hart incurred many charges between 2013 and September 2014 for which he allegedly received  
28 improper reimbursement. See SAC ¶¶ 45–50. It is not clear when the reimbursements were  
granted or when the Board allowed the misuse.

1 who would consider a shareholder demand also made the challenged decision. See 473  
2 A.2d at 814; see also *Ryan v. Gifford*, 918 A.2d 341, 353 (Del. Ch. 2007). The Rales test  
3 applies where the board on which demand would be made did not make the business  
4 decision challenged in the litigation (e.g., where a majority of the directors who made the  
5 decision have since been replaced, or where the challenged conduct is inaction by the  
6 board). 634 A.2d at 934. Here, because Oswald alleges that a majority of the current  
7 Board made the challenged business decisions, the Aronson test applies.

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9 To demonstrate demand futility under Aronson, a shareholder plaintiff must create a  
10 reasonable doubt that either: “(1) the directors are disinterested and independent [or]  
11 (2) the challenged transaction was otherwise the product of a valid exercise of business  
12 judgement.” Aronson, 473 A.2d at 814. The test is disjunctive—a reasonable doubt as to  
13 either prong will establish demand futility. See id. at 815.

14  
15 The parties are at odds regarding whether Oswald must plead demand futility as to a  
16 majority of the original six-member Board, or as to the current four-member Board. See  
17 SAC ¶¶ 96–109 (alleging demand futility as to six original directors); but see id. ¶ 96 n.4  
18 (asserting that “[a]lthough plaintiff believes that demand futility is assessed as to the board  
19 in place when this action was commenced, demand would also be excused if demand  
20 futility were evaluated against the current Board. . . .”); MTD at iv (arguing that Oswald is  
21 incorrect to allege demand futility as to six original directors). However, because  
22 Defendants do not dispute that Hart is interested, Oswald can reach a majority of either  
23 Board by successfully challenging any two of Humphreys, Kremen, and Ousley.<sup>10</sup>  
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28 <sup>10</sup> No one suggests that there is any basis to challenge current Board member Shapiro.

1                   Oswald argues that demand is futile based on both Aronson prongs.

2                   **1.        Aronson Prong 1: Interest**

3                   Under the first prong of Aronson, a plaintiff can displace the protection of the  
4 business judgement rule by alleging particularized facts that raise a reasonable doubt that a  
5 majority of the directors are either independent or disinterested. Aronson, 473 A.2d at  
6 814–15. Directors are considered to lack independence if they are “under an influence  
7 which sterilizes their discretion,” or beholden to and controlled by an interested party. Id.  
8 at 815. Directors are considered interested if they either “appear on both sides of a  
9 transaction [or] expect to derive any personal financial benefit from it in the sense of self-  
10 dealing, as opposed to a benefit which devolves upon the corporation or all stockholders  
11 generally.” Id. at 814. A plaintiff can also show interest if a director faces a “substantial  
12 likelihood” of personal liability for approving the questioned transaction. See id. at 815  
13 (noting that this is rare, and that a “mere threat” of liability alone is insufficient).  
14

15                   Here, Oswald attempts to satisfy the first Aronson prong by showing that  
16 Humphreys and Kremen are not disinterested, either because (a) they personally  
17 participated in Hart’s misuse of corporate funds, or (b) they voted to prematurely end the  
18 Special Committee investigation. Neither argument succeeds.  
19

20                   **a.        Kremen’s and Humphreys’ participation in the misuse of  
21                   Identiv’s funds in Las Vegas**

22                   Oswald argues that Kremen and Humphreys are complicit in Hart’s improper  
23 business expense reimbursements because they participated in the parties, enjoyed the  
24 benefits of the company’s funds, and themselves submitted improper expenses related to  
25 the Las Vegas trips. See SAC ¶¶ 98, 101. Oswald argues that this behavior (i) exposes  
26

1 Kremen and Humphreys to a substantial likelihood of liability, and (ii) amounts to self-  
2 dealing, making both directors interested. *Id.* ¶¶ 99, 102.<sup>11</sup>

3 **i. Likelihood of Liability**

4 Defendants argue that Kremen and Humphreys do not face any likelihood of  
5 liability in connection with improper expenses because they are both exculpated by their  
6 corporation's certificate of incorporation for alleged breaches of their duty of care  
7 consistent with tit. 8 Del. Code § 102(b)(7). See McGrath Decl. Ex. 1 at 2. But Oswald  
8 alleges that Defendants breached their fiduciary duty of loyalty, see SAC ¶ 115, and  
9 Defendants are not exculpated for a breach of loyalty, see McGrath Decl. Ex. 1 at 2 ("A  
10 director of the Corporation shall not be personally liable . . . for breaches of fiduciary duty  
11 as a director, except for liability (i) for any breach of the director's duty of loyalty . . .").  
12

13 Defendants next argue that Humphreys and Kremen do not face a substantial  
14 likelihood of liability for improper expenses because Oswald has not pled that either knew  
15 that Hart was expensing the Las Vegas trips to Identiv. MTD at 5. But Oswald pled that  
16 Humphreys and Kremen themselves submitted reimbursement requests for expenses  
17 incurred at the parties. SAC ¶¶ 98, 101. At this stage, Oswald is entitled to the reasonable  
18 inference that if the directors submitted their own reimbursement requests (and thereby  
19 demonstrated a belief that the trip was a business trip), they knew that Hart would expense  
20 charges as well. See Rosenbloom, 765 F.3d at 1148. As Oswald remarks: "How  
21 Humphreys and Kremen could think they were attending a business event . . . and  
22 simultaneously not know the Company was paying the bill is a mystery." See Opp'n at 8  
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25 <sup>11</sup> In its Order dismissing Oswald's Amended Complaint, the Court noted that "[t]he Las Vegas  
26 trips raise questions about the independence and disinterest of both Kremen and Humphreys," but  
27 held that Oswald had not pled interest with particularity. Order at 3.

(citing MTD at 5 (arguing in one breath that the trip might have had a legitimate business purpose and in the next that Humphreys and Kremen did not know that Hart submitted any expenses)).<sup>12</sup>

Still, Oswald has not shown that the threat of liability that Humphreys and Kremen faced on this subject was substantial, or more than a “mere threat” of liability, as required by Aronson. The Delaware Supreme Court in Aronson noted that there will only be a substantial threat of liability “in rare cases [where] a transaction may be so egregious on its face that Board approval cannot meet the test of business judgment.” 473 A.2d at 815. The allegations that Kremen received massages costings \$1,900, or that Humphreys submitted nearly \$1,000 in expenses for reimbursement in connection with a Las Vegas party, standing alone, are not “so egregious on [their] face” that the two directors face a substantial likelihood of liability. See id.

## ii. Self-Dealing

Similarly, Oswald’s claims of self-dealing on the basis of these expenses fails, because Oswald has not shown that the benefits that Humphreys and Kremen gained from their participation in Hart’s wrongdoing were material to them.

“[W]hen a party challenges a director’s action based on . . . self-interest, that party

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<sup>12</sup> Defendants argue that “[t]his case is on all fours with In re Polycom, Inc. Deriv. Litig., 78 F. Supp. 3d 1006 (N.D. Cal. 2015).” MTD at 6. Not quite. In re Polycom sounds similar, as it involved allegations that a CEO “claimed reimbursements for numerous inappropriate personal expenses.” Id. at 1011. In that case, the plaintiffs argued that demand should be excused because the board faced substantial liability for failing to adequately oversee the company’s auditing and accounting controls. Id. at 1014. The court held that absent any evidence that the board knew that violations were occurring, it could not “simply infer the board knew or should have known of the problems with [the CEO’s] expense reports.” Id. at 1015–16. In this case, Oswald does not contend that the Board “must have known” of Hart’s misconduct due to some vague “duty to be informed,” see id. at 1016, but points to Humphreys’ and Kremen’s own conduct alongside Hart’s. See Opp’n at 8 (“Kremen and Humphreys were both present, received personal luxuries paid for by Identiv, and submitted for reimbursement expenses incurred at those parties.”).

must allege that the director's interest is material to that director." Solomon v. Armstrong, 747 A.2d 1098, 1118 (Del. Ch. 1999), aff'd, 746 A.2d 277 (Del. 2000); see also Cinerama, Inc. v. Technicolor, 663 A.2d 1156, 1167 (Del. 1995) (courts must consider whether the benefit is material to the "actual person," not use an objective "reasonable person" standard). "Materiality means that the alleged benefit was significant enough 'in the context of the director's economic circumstances, as to have made it improbable that the director could perform her fiduciary duties to the . . . shareholders without being influenced by her overriding personal interest.'" Orman v. Cullman, 794 A.2d 5, 23 (Del. Ch. 2002). Establishing that a director "expect[s] to derive [a] personal financial benefit from [a transaction]" that is not enjoyed by the corporation or all stockholders generally, Aronson, 473 A.2d at 814, does not alone establish that the director is interested—the benefit must also be material to that director. Cinerama, 663 A.2d at 1167.

However, materiality is not required for classic self-dealing, where the director "appear[s] on both sides of a transaction." Orman, 794 A.2d at 25 n.50. Oswald's argument that the benefits Kremen and Humphreys received need not be material relies on such cases. See Opp'n at 9 (citing Calma v. Templeton, 114 A.3d 563, 576 (Del. Ch. 2015) (challenging directors' award of restricted stock units to themselves); Cambridge Ret. Sys. v. Bosnjak, No. 9178-CB, 2014 Del. Ch. LEXIS 107, at \*11 (Ch. June 26, 2014) (challenging directors' payment of compensation to themselves); London v. Tyrrell, Civil Action No. 3321-CC, 2008 Del. Ch. LEXIS 75, at \*14–15 (Ch. June 24, 2008) (challenging directors' grant of stock options to themselves); In re Investors Bancorp, Inc. Stockholder Litig., No. 12327-VCS, 2017 Del. Ch. LEXIS 53, at \*16 n.9 (Ch. Apr. 5, 2017) (challenging directors' grant of equity awards to themselves)). These cases stand for

1 the proposition that when directors decide matters of their own compensation, they stand  
2 on both sides of a transaction with the company, and so materiality is not required. Id.

3 Here, there is no allegation that Kremen and Humphreys approved their own  
4 expenses, set their own salaries, or awarded themselves stock options. They did not stand  
5 on both sides of that kind of transaction. Thus, in order to show their interest, Oswald  
6 must show that the benefits that Kremen and Humphreys received by participating in  
7 Hart's Las Vegas parties were material. See Cede & Co. v. Technicolor, Inc., 634 A.2d  
8 345, 364 (Del. 1993). Oswald has not pled with particularity that these benefits (Kremen's  
9 \$1,900 in massages and Humphreys' nearly \$1,000 in reimbursed expenses) were material.  
10 Oswald has not raised a reasonable doubt that Kremen and Humphreys are disinterested on  
11 the basis of their receiving benefits from Hart's misuse of corporate funds.

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13 **b. The Board's vote to end the Special Committee's  
14 investigation prematurely**

15 Oswald also argues that Humphreys and Kremen were interested in any demand  
16 regarding their vote to end the Special Committee investigation because they participated  
17 in the conduct that was under investigation.<sup>13</sup>

18 Defendants argue that Humphreys and Kremen could not have been interested  
19 because the scope of the Special Committee's investigation was so narrow that it only  
20 included Hart's improper expenses and conduct. See MTD at 13. In fact, the Board

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25 <sup>13</sup> In its Order dismissing Oswald's Amended Complaint, the Court held that Oswald had not pled  
26 interest with particularity, noting that "the procedures, findings, conclusions, and  
27 recommendations of the Special Committee remain unknown." Order at 4. Although the  
28 Amended Complaint vaguely referred to a "sham Special Committee investigation," see, e.g.,  
FAC ¶¶ 83–84, the Second Amended Complaint includes more extensive allegations about the  
circumstances of the Board's "premature conclusion" of the investigation, see, e.g., SAC  
¶¶ 70, 71, 78, 79, 106.

1 directed the Special Committee to investigate “the facts, allegations and circumstances” of  
2 the Ruggiero Complaint, and “any similar or related facts.” SAC ¶ 53; McGrath Decl. Ex.  
3 15. Kremen and Humphreys were named in the Ruggiero Complaint, and the Deloitte  
4 Report shows inspection of expenses that Kremen and Humphreys enjoyed and possibly  
5 incurred. See id. ¶¶ 99, 102; see generally Deloitte Spreadsheet. At this stage, Oswald is  
6 entitled to a broad reading of the scope of the investigation, because it is a reasonable  
7 inference that investigators considered the conduct of Kremen and Humphreys to be  
8 similar or related to that of Hart. See Rosenbloom, 765 F.3d at 1148.  
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10       Oswald argues that Humphreys and Kremen “stood on both sides” here because  
11 they voted to end an investigation into their own conduct. Opp’n at 11. Although  
12 intuitively it seems correct that Humphreys and Kremen would be “interested” in an  
13 investigation into their participation in alleged wrongdoing, it is not clear that voting to  
14 end an internal investigation falls within the definition of a “self-dealing transaction” as  
15 contemplated by Delaware law. Oswald has not cited any precedent for the assertion that  
16 transactions bestowing non-financial benefits qualify as self-dealing.<sup>14</sup> Every case that  
17 Oswald cites in his brief involves self-dealing in the context of financial transactions. See,  
18 e.g., Opp’n at 11 (citing In re Brocade, 615 F. Supp. 2d at 1047 (evaluating interest where  
19 “Defendants received and exercised failed options”); Calma, 114 A.3d 563, 575  
20 (evaluating interest where defendants awarded themselves restricted stock units as  
21 compensation)). It does not appear that any court has applied the self-dealing doctrine in  
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27       <sup>14</sup> Defendants incorrectly cite Cinerama, 663 A.2d at 1169, for the proposition that self-dealing  
28 only occurs “when a director deals directly with the corporation, or has a stake in or is an officer  
or director of a firm that deals with the corporation.” See MTD at 7–8. In fact, Cinerama cites  
these as “example[s]” of self-dealing. 663 A.2d at 1169.

1 this way yet.

2       Oswald does cite to one Delaware case which evaluated a non-financial transaction  
3 similar to the one here, but the court in that case seems to have excused demand under the  
4 second prong of Aronson, not the first. See Opp'n at 11 (citing In re China Agritech, Inc.,  
5 No. 7163-VCL, 2013 Del. Ch. LEXIS 132, at \*68 (May 21, 2013)); In re China Agritech,  
6 Inc., 2013 Del. Ch. LEXIS 132, at \*65 ("The members of the Audit Committee could not  
7 properly consider a litigation demand regarding the termination of the Company's outside  
8 auditors because the allegations of the Complaint support a reasonable inference that they  
9 failed to act in good faith.") (emphasis added); id., at \*68 ("The actions of four of the  
10 seven members of the Demand Board were at issue in the Special Committee investigation.  
11 . . . these directors could not properly consider a demand under Aronson that asked them to  
12 assert litigation relating to the Audit Committee's termination of the outside auditors or  
13 management's related activities." ).<sup>15</sup>

14       Rather than rely on a novel interpretation of self-dealing, the Court will follow In re  
15 China Agritech. Analysis of the Board's decision to end the investigation prematurely and  
16 without investigating the potential bribery issue fits squarely in the good faith analysis of  
17 the second prong of Aronson.

18           **2.       Aronson Prong 2: Valid Exercise of Business Judgment**

19       Under the second prong of Aronson, demand is excused as futile where a plaintiff

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25       <sup>15</sup> In re China Agritech did recognize that a CEO risked liability in connection with his company's  
26 terminating its outside auditors, see id., at \*65 ("Chang could not properly consider a litigation  
27 demand regarding the termination of the Company's outside auditors because his role in  
28 management as the Company's CEO gives rise to a reasonable inference that he would face  
personal and professional risk in any litigation over the dispute, making him interested in the  
outcome."), arguably invoking the first Aronson prong, but it did not characterize such conduct  
(much less the rest of the board's conduct) as "self-dealing."

1 can raise a reasonable doubt that the challenged transaction was a valid exercise of  
2 business judgement. Aronson, 473 A.2d at 814. A showing that directors were grossly  
3 negligent or acted in bad faith directly rebuts the business judgement presumption. In re  
4 Walt Disney Co. Deriv. Litig., 906 A.2d 27, 52 (Del. 2006). Aronson explained that “to  
5 invoke the rule’s protection directors have a duty to inform themselves, prior to making a  
6 business decision, of all material information reasonably available to them,” and they  
7 “must then act with requisite care<sup>16</sup> in the discharge of their duties.” 473 A.2d at 812.

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9 Here, Oswald attempts to satisfy the second Aronson prong by showing that  
10 Humphreys and Kremen (a) acted in bad faith when they voted to prematurely end the  
11 Special Committee investigation, and (b) committed waste by awarding Hart severance  
12 and permitting him to only repay a portion of the funds that he diverted for personal use.  
13 The Court agrees that Oswald has raised a reasonable doubt that Humphreys and Kremen  
14 acted in good faith.

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17 **a. Bad Faith**

18 Under Delaware law, bad faith exists where a director acts with “intentional  
19 dereliction of duty” or “conscious disregard for [his or her] responsibilities.” In re Walt  
20 Disney, 906 A.2d at 66. It is also bad faith where a fiduciary “acts with the intent to  
21 violate applicable positive law” or “intentionally acts with a purpose other than that of  
22 advancing the best interests of the corporation.” Id. at 67.

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24 Oswald urges the Court to infer that the Board knowingly decided not to find out if  
25 a crime had been committed. See Opp’n at 13. This is a reasonable inference to make at  
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28<sup>16</sup> Under Delaware law, director liability is predicated upon concepts of gross negligence. Id.

1 this stage, and it is based entirely on information that is newly alleged in the Second  
2 Amended Complaint. Because Deloitte discussed its review of the challenged expenses  
3 with the Board, see SAC ¶¶ 57, 59, it is reasonable to infer that before the Board voted to  
4 end the investigation, Humphreys and Kremen knew that their participation and expenses  
5 had turned up as improper in the Deloitte Report, and that the entire Board knew that  
6 Deloitte believed that there was a “potential bribery issue” during one of the Las Vegas  
7 parties. Id. The Court can also reasonably infer that Humphreys, Kremen, and Ousley  
8 knew of BDO’s position that further investigation was vital, as described in BDO’s  
9 November 23, 2015 letter addressed to the entire Board. See id. ¶ 78 (describing “multiple  
10 requests by BDO” to investigate further “[s]ince October 17, 2015”).

13 With this knowledge, the Board nonetheless chose to terminate the Special  
14 Committee’s investigation, and to keep it closed. The “knowing and intentional” approval  
15 of wrongdoing to the benefit of insiders “cannot be an exercise of business judgment.” See  
16 Ryan, 918 A.2d at 354; see also In re Atmel Deriv. Litig., No. 06-4592 JF (HRL), 2008  
17 U.S. Dist. LEXIS 91909, at \*22 (N.D. Cal. June 25, 2008). Where a Board “intentionally  
18 conceals the nature of its earlier actions, it is reasonable for a court to infer that the act  
19 concealed was itself one of disloyalty that could not have arisen from a good faith business  
20 judgment.” In re Tyson Foods, Inc. Consol. S’holder Litig., No. 1106-CC, 2007 Del. Ch.  
21 LEXIS 120, at \*12–13 (Ch. Aug. 15, 2007).

24 Defendants argue that rather than adequately alleging bad faith, Oswald is  
25 improperly second-guessing the Board’s actions. See MTD at 10 (citing In re Autodesk,  
26 Inc., S’holder Deriv. Litig., No. 06-cv-7185-PJH, 2008 U.S. Dist. LEXIS 101015, at \*21  
27 (N.D. Cal. Dec. 15, 2008) (“an attack on a Board’s internal investigation is improper in the

1 context of a demand futility argument, because such an argument depends on the premise  
2 that the plaintiff has necessarily abandoned the Board as a vehicle for righting the wrongs  
3 complained of"). But Oswald does not second-guess the decision to end the investigation;  
4 he alleges that it was not made in good faith. See Opp'n at 13. Additionally, in In re  
5 Autodesk, the court was evaluating interest under the Rales test, not good faith under  
6 Aronson's second prong (which is not available as a path to establish demand futility under  
7 the Rales test), and "the actions being investigated (options backdating) were not actions  
8 of the Audit Committee or the Board." In re Autodesk, 2008 U.S. Dist. LEXIS 101015, at  
9 \*25. In contrast, here half the current Board participated in the conduct being  
10 investigated.<sup>17</sup>

11 Defendants also rely on In re Am. Apparel, Inc., 2014 Deriv. S'holder Litig., 2015  
12 WL 12724070, at \*19–20 (C.D. Cal. April 28, 2015), which held that "disputes" about the  
13 "appropriate response" to misconduct were subject to "difference[]s in interpretation" and  
14 were, in that case, "insufficient to establish the [board] acted in bad faith." See MTD at 10  
15 n.18. As in In re Autodesk, the misconduct at issue in In re American Apparel was entirely  
16 that of the CEO, not the board itself. See id. at \*2 ("[t]his action emerges out of the  
17 behavior of American Apparel founder . . . Charney, and the Company's decision to  
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<sup>17</sup> Defendants argue that it is irrelevant whether Humphreys and Kremen were under investigation, because "at the time the Special Committee's recommendations were approved, the Board consisted of five outside directors (Humphreys, Kremen, Alazem, Ousley, and Wenzel), and so "even without Humphreys' and Kremen's votes, there was still a majority and quorum on the Board to approve concluding the investigation." MTD at 13. There are at least two problems with that assertion. First, it is problematic that Humphreys and Kremen even participated in the discussion and decision of whether to end the Special Committee's work, rather than recusing as Hart presumably did. Second, the SAC alleges that it was only "the non-committee board members" who "unanimously accepted the recommendation of the Committee," suggesting that Humphreys and Kremen were two of three Board members who made the decision, rather than two of five. See SAC ¶ 71. This is a reasonable inference to draw at this stage of the litigation.

1 terminate him as CEO in June 2014.”). Moreover, the plaintiffs in that case had alleged  
2 that the board breached its duty “by not acting earlier,” and therefore had to allege with  
3 specificity “why the Board’s delay in suspending and ultimately terminating Charney was  
4 a breach of their duties.” Id. at \*19. Plaintiffs failed to allege “the point at which the  
5 Board was acting in bad faith by retaining Charney.” Id. Here, Oswald has not alleged  
6 that the Board should have taken action against Hart at some earlier point. The issue is  
7 instead the Board’s decision to conclude the Special Committee investigation, where that  
8 investigation involved Humphreys’ and Kremen’s own expenses along with Hart’s, and a  
9 “potential bribery issue,” despite being urged not to do so by Deloitte, independent  
10 counsel, and BDO. See SAC ¶¶ 57, 59, 71, 78.<sup>18</sup>

13 Defendants’ further argument that the Board must have acted in good faith because  
14 the company spent “nearly \$3 million” on the investigation only to recover “pennies” also  
15 falls flat. See MTD at 12. “[D]irectors [are] entitled to a presumption that they can and  
16 should be allowed to manage the business affairs of a corporation, including the decision  
17 of whether and how to investigate errors.” In re Comput. Scis. Corp. Derivative Litig., 244  
18 F.R.D. 580, 591 (C.D. Cal. 2007). But this presumption is rebutted if a plaintiff pleads  
19 “particularized allegations showing the Board is unworthy of this deference.” Id.  
20 Defendants argue that Deloitte’s investigation only identified approximately \$164,000  
21 worth of expenses that had insufficient documentation submitted to support a business  
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25 <sup>18</sup> Defendants also cite to In re FalconStor Software, Inc., 966 N.Y.S.2d 642, 655 (N.Y. Sup. Ct.  
26 2013) for the proposition that “conduct[ing] its internal investigation [is] exactly the kind of  
27 action[] that [is] entrusted to a board of directors and which the Delaware courts state they are  
28 reluctant to question.” MTD at 10 n.18. But the court in that case, a New York Supreme Court,  
prefaced that observation by stating that “not a single one of the current members of the board of  
directors was implicated [in the litigation],” or “knew or indeed had reason to know that they were  
violating the shareholder plan.” Id. at 654–55. That makes In re FalconStor distinguishable.

1 expense or that “appear[ed] to be non-business, personal” expenses. MTD at 12. This  
2 figure does not include the \$354,528.36 in charges that Deloitte classified as possible  
3 business expenses incurred in violation of Company policy. See SAC ¶ 62. It also does  
4 not account for the items that the Board approved classifying as business expenses,  
5 overriding Deloitte’s conclusion that the purpose provided was not sufficient to support  
6 business purpose. See id. According to the Deloitte Spreadsheet, many of Hart’s Las  
7 Vegas expenses fall into this category. See generally Deloitte Spreadsheet; compare id.  
8 column Q (“no”) with id. column S (amount approved by Board as business expense).  
9 Even if \$164,000 is the proper figure, Identiv only recovered \$35,784 from Hart. SAC  
10 ¶ 89. These figures, combined with the inference that the Board knowingly chose not to  
11 investigate whether a crime had been committed, raise a reasonable doubt that the Board’s  
12 “decision of whether and how to investigate errors” is worthy of deference. See In re  
13 Comput. Scis., 244 F.R.D. at 591.

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Oswald has raised a reasonable doubt that the Board acted in good faith when it  
voted to end the investigation. Oswald has pled particularized facts raising an inference  
that the Board knowingly decided—contrary to the advice of independent counsel,  
Deloitte, and BDO—not to get to the bottom of its executives’ expenses or find out if a  
crime had been committed. This amounts to a “conscious disregard for [their]  
responsibilities,” which is bad faith. See In re Walt Disney, 906 A.2d at 66.

Because Oswald has raised a reasonable doubt that the challenged action was made  
in good faith, demand on the Board is excused as futile. See Aronson, 473 A.2d at 814.  
The Court therefore DENIES the Motion to Dismiss.

## b. Waste

Because Oswald prevails on his argument about bad faith, he need not also prevail on his argument about waste. Indeed, the Court holds that Oswald has not established demand futility on this ground.

To state a claim for corporate waste, a plaintiff must show that “the Board’s decision was so egregious or irrational that it could not have been based on a valid assessment of the corporation’s bests interests.” White v. Panic, 783 A.2d 543, 554 n.36 (Del. 2001). This requires the plaintiff to demonstrate that “an exchange was so one-sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration.” In re Walt Disney, 906 A.2d at 74. Waste often entails “a transfer of corporate assets that serves no corporate purpose, or for which no consideration at all is received.” Brehm, 746 A.2d at 263. A “mere disagreement cannot serve as grounds for imposing liability based on alleged . . . waste.” Id. at 266. Thus, a corporate waste claim fails “if there is any substantial consideration received by the corporation, and . . . there is a good faith judgment” that under the circumstances the transaction was worthwhile. White, 783 A.2d at 554.

Oswald argues that the Board committed waste because it chose not to fire Hart for cause, allowed him to receive severance under his employment agreement, and allowed him to repay only a fraction of the funds he allegedly diverted for personal use. Opp'n at 15. These allegations do not overcome the “high hurdle” necessary to challenge the “great deference” the Board is granted in this area. See Brehm, 746 A.2d at 262–63. Oswald has not pled that Hart was of zero value to Identiv. Thus, the Court cannot assume that his severance was in exchange for nothing. Furthermore, whether to terminate Hart for cause

1 and risk litigation is left to the sound discretion of the Board. See White, 783 A.2d at 554.

2 Because Identiv's decision not to fire Hart for cause could "have been based on a  
3 valid assessment of the corporation's bests interests," it cannot be considered wasteful for  
4 purposes of demand futility. See White, 783 A.2d at 554 n.36

5 **IV. CONCLUSION**

6 For the foregoing reasons, Oswald has pled sufficient particularized facts to  
7 demonstrate demand futility under the second prong of Aronson. Oswald has created a  
8 reasonable doubt that the Board acted in good faith in its decision to end the Special  
9 Committee investigation. Thus Oswald has met his burden under Rule 23.1. The Court  
10 DENIES Defendant's Motion to Dismiss the Second Amended Complaint.

11 **IT IS SO ORDERED.**

12 Dated: October 27, 2017



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13 CHARLES R. BREYER  
14 United States District Judge