with the full and complete disclosure requirement imposed on a fiduciary. Therefore, the effectuation of the tender offer was held in abeyance until further disclosure was made.

1. Corporations ⟹ 316(1)

Where defendants stand on both sides of a transaction, they are under fiducairy duty to the minority shareholders of the corporation subject to the transaction.

2. Injunction ⟹ 151

Where an application for preliminary injunction is before the court, the plaintiff has the burden of showing that there is a reasonable probability that he would prevail on the merits if a trial were held.

3. Injunctions ⟹ 132,135

Preliminary injunction constitutes extraordinary relief and is addressed to the sound discretion of the court, to be guided according to the particular circumstances in each case.

4. Corporations ⟹ 187

Although the fiduciary duty of a majority shareholder in making a tender offer is limited to full disclosure, there is an exception when the maker of the tender offer, owing the fiduciary duty, structures the offer in such a way as to result in an unfair price being offered and the disclosures are unlikely to call the unwary shareholders attention to the unfairness.

5. Corporations ⟹ 187

Majority shareholders have a duty to exercise complete candor when approaching minority shareholders with a tender offer. Therefore, failure to disclose that an appraiser was not given access to data necessary to completely evaluate the value of stock and failure to fully disclose recent discoveries, regardless of defendants's claim that they were too recent, are factors in violation of the full disclosure requiremetn of Delaware law.

6. Corporation ⟹ 187

Majority shareholders have a duty to exercise complete candor in approaching minority shareholders for a tender offer of their shares and have a duty to make a full disclosure of all the facts and circumstances surrounding the offer. Although no one factor standing alone would constitute a breach of a majority shareholder's duty, all factors considered together in light of the surrounding circumstances

can make it clear that the tender offeror has not met his duty of disclosure under Delaware Law.

7. Corporations ⟹ 182.4(5)

Failure to negotiate at arms-length does not ipso facto indicate an unfair price for tender offer of shares of stock, but is merely one factor to be considered in determining the fairness of the offer.

8. Injunction ⟹ 151

Where plaintiffs have shown a reasonable probability of success, the court must then determine if there is a probability of irreparable harm to justify a preliminary injunction. To permit minority shareholders to tender their shares without full disclosure by defendants might forever deny their tendering shareholders their right to be treated fairly and would therefore constitute irreparable harm.

9. Equity ⟹ 39(1)
Injunction ⟹ 137(2), 137(4)

In acting upon applications for preliminary injunctions, a court of equity has broad discretionary powers and is to structure a remedy which is fair to all competing interests.

Morris and Rosenthal, P.A., Wilmington, Delaware; Abbey & Ellis, New York, New York; Lowery, Dannenberg & Knapp, P.C., New York, New York; Wolf Popper Ross Wolf & Jones, New York, New York; Harvey Greenfield, Esquire, New York, New York; Milberg Weiss Bershad Specthrie & Lerach, New York, New York; Wolf Haldenstein Adler Freeman & Herz, New York, New York, for plaintiffs.

Richards, Layton & Finger, Wilmington, Delaware, for defendant, Shell Oil Company

Morris, Nichols, Arsht & Tunnell, Wilmington, Delaware; and Cravath, Swaine & Moore, New York, New York, for defendant, SPNV Holdings, Inc.

HARTNETT, *Vice-Chancellor*

I

This action is a consolidation of six actions brought as class actions on behalf of the shareholders of defendant Shell Oil Company ("Shell"), a Delaware corporation. The suit attacks a tender offer made by defendant SPNV Holdings, Inc. ("SPNV"), a Delaware corpora-

tion, which was formed for the purpose of obtaining the shares of stock of Shell owned by minority shareholders. The majority of Shell's outstanding common stock is controlled by defendant Royal Dutch Petroleum Company ("Royal Dutch"). The tender offer commenced on April 4, 1984, and will expire—unless extended—on May 9, 1984. The withdrawal date for the tender offer was April 24, 1984, and SPNV has commenced to purchase shares which have already been tendered.

Plaintiffs requested a preliminary injunction to enjoin the completion of the tender offer. It was heard by the Court on a expedited basis on Friday, May 4, 1984.

After considering all the facts and circumstances of this most unusual tender offer, I find that plaintiffs have shown the reasonable probability that the Court would find, after trial, that some of the defendants stand on both sides of the transaction and therefore have a fiduciary duty to the minority shareholders of Shell but that they have failed to meet the high standard of conduct imposed by Delaware law on fiduciaries and therefore, in the interests of the minority shareholders, the tender offer must be held in abeyance until the defendant SPNV makes further disclosures to the tender offerees and cures certain deficiencies.

II

The underlying facts are not in dispute. Defendant Royal Dutch has, for over 60 years, controlled through various subsidiaries a majority of the stock of Shell. Royal Dutch now, through subsidiaries, controls 69.5 % of the outstanding common shares of Shell. Shell is a corporation which is a major explorer for, producer and marketer of oil and oil products. It has 309 million shares of outstanding common stock held by more than 38,000 stockholders other than Royal Dutch. Its stock is traded on the New York Stock Exchange and elsewhere. Its assets consist of valuable oil reserves—some of which are considered as "proven reserves" and are therefore publicly disclosed on Shell's financial statements and some of which are considered as "probable reserves" and are therefore not disclosed publicly in Shell's public financial statements.

Shell has always been operated independently of Royal Dutch, but Royal Dutch has always selected Shell's directors and two directors are direct employees of Royal Dutch. The Chairman of the Board has always been a "Royal Dutch director". A majority of the directors (six) of Shell are outside directors with considerable background and experience as executives with other corporations.

Commencing in 1982 the Royal Dutch group began considering the acquisition of the common shares of stock of Shell held by others—

either by making a tender offer for the minority shares or through a freeze-out merger. In 1982 the Royal Dutch group retained Morgan Stanley & Co., Incorporated. ("Morgan Stanley"), a New York investment banker, to prepare an estimate of the value of the minority shares of Shell. No effort to acquire the minority shares took place at the time however.

Early in 1984 the Royal Dutch group again decided to attempt to acquire the minority shares of Shell and on January 16, 1984, Morgan Stanley was asked to update it valuation. This it did eight days later on January 24, 1984, and advised that the value of the minority shares, in its opinion, was $53 per share. The report of Morgan Stanley stated that its opinion of value was based only on publicly available information and Morgan Stanley was not furnished with any detailed information on the probable reserves except for general information as to their existence.

One of the subsidiaries used by the Royal Dutch group to control Shell is Shell Petroleum Company Limited ("Dutch Shell"), a Netherlands corporation. On January 24, 1984, Dutch Shell announced its intention to merge Shell into SPNV. Under the proposed merger the minority shares of Shell were to be cashed-out for $55 per share. Two days after the merger intention announcement, on January 26, 1984, Shell's fourth quarter earnings were reported which increased $1.42 per share (a 25% gain) over the same period of year previously. On January 23, 1984, the day preceding the Dutch Shell merger intention announcement, Shell announced that it had made an important major oil strike in the Beaufort Sea off of the share of Alaska.

The Board of Directors of Shell, immediately after learning of the January 24, 1984, merger offer, created a special committee consisting of the six outside directors of Shell to evaluate the merger proposal. The committee undertook its work with vigor and retained Godman-Sachs & Co. ("Goldman-Sachs"), a New York investment banker, to prepare an estimate of the value of the minority shares. The committee also retained several other consultants to assist it in evaluating the merger proposal and especially the value of the probable reserves. Goldman-Sachs was retained on the basis of a fixed fee plus a bonus to be based on any additional sums eventually paid for the minority shares. Goldman-Sachs arrived at a figure of $80-$85 per share as its estimate of the value of Shell's outstanding common stock.

The special committee met on March 26, 27, and 28, 1984, to consider the report of Goldman-Sachs and the other experts retained by the committee. On March 28, 1984, the committee considered the opinion of Goldman-Sachs that the liquidation value of the Shell shares was in the $80-$85 per share range.

Mr. Bookout, the President of Shell, opined in effect that, in his opinion, the shares might have a value of as much as $91 per shae if Shell were sold as a going concern to a purchaser on an open auction basis and if all the possible contingencies upon which value is based were favorable to Shell.

The committee then unanimously rejected the $55 merger offer of Dutch Shell as being unacceptable and indicated that it would entertain a $75 per share offer. Goldman-Sachs also then expressed that $75 per share was in the lower range of what would be, in its opinion, a fair merger price offer. On March 29, 1984, the full Board of Directors of Shell approved the recommendation of the special committee.

The action of the committee and the Board was communicated to Royal Dutch. (Two members of the Shell Board are direct representatives of Royal Dutch.)

What transpired then is somewhat disputed. Plaintiffs claim that Royal Dutch flatly rejected any negotiations as to price. Royal Dutch claims that it was willing to negotiate as to price but the spread between the parties was too great to conduct meaningful negotiations. In any event, no arms-length negotiations as to price ever took place.

On March 29, 1984, Royal Dutch announced that it had withdrawn its merger proposal and would commence a tender offer to the minority shareholders at $55 per share. On April 4, 1984, the offering circular for the tender offer raised the tender offer price to $58 per share. Shortly after the tender offer announcement the shares of Shell traded at $60 per share. Shortly before the tender offer the shares had traded at $57-$59 per share. Prior to the merger offer in January of 1984, the Shell stock had been selling for about $44 per share.

Dutch Shell also publicly announced that it would not make another public tender offer for 18 months and that it intended to eventually obtain all the shares of Shell. It disclosed that if it obtained 90% or more of the minority shares as a result of the tender offer, it would effectuate a short form merger to obtain the remainder of the shares. In such an eventuality, any dissenting shareholders, of course, would be relegated to relying on the Delaware appraisal statute for redress.

In the event that 90% of the shares of Shell were not tendered, Dutch Shell announced it might buy sufficient shares on the open market to reach the 90% figure needed to effectuate a short form merger. Dutch Shell also commenced to solicit acceptance of the tender offer by a telephone campaign. As part of this campaign, it has advised some Shell stockholders that after the tender offer is terminated,

the Shell stock may well drop to its previous price of about $40 per share.

Plaintiffs view this scenario as being coercive to the minority stockholders of Shell. They further claim that defendants have a fiduciary duty to the minority stockholders and that this duty has been breached because the defendants have been guilty of unfair dealing with the minority and of offering an unfair price.

Defendants, however, maintain that they have been scrupulously fair and have not breached any fiduciary duty to the minority stockholders—either by unfair dealing or by offering an unfair price. In any event, they claim that under Delaware law they have no legal duty to offer a fair price and that they have complied with their acknowledged duty of fair dealing by making a full and complete disclosure of all the facts to the minority shareholders.

III

[1] It is elementary that defendants, because they stand on both sides of the transaction, are under a fiduciary duty to the minority stockholders of Shell. *Sterling v. Mayflower Hotel Corp.*, Del. Supr., 93 A.2d 107 (1952); *Guth v. Loft, Inc.*, Del. Supr., 5 A.2d 503 (1939); *Weinberger v. UOP, Inc.*, Del. Supr., 457 A.2d 701 (1983); *Singer v. Magnavox Co.*, Del. Supr., 380 A.2d 969 (1977). At trial, therefore, the burden of persuasion would fall upon the defendants. *Schreiber v. Bryan*, Del. Ch., 396 A.2d 512 (1978).

[2,3] The present matter is before the Court, however, upon an application for a preliminary injunction and therefore plaintiffs have the burden of showing that there is a reasonable probability of their prevailing on the merits if a trial were held. *Gimbel v. Signal Companies*, Del. Ch., 316 A.2d 599 (1974).

From the evidence adduced by the discovery and affidavits I am convinced that the plaintiffs have met their burden of showing that there is a reasonable probability that the defendants have not offered a fair price for the shares of Shell held by the minority stockholders and that defendants have not made a full and complete disclosure of all pertinent facts with complete candor.

The question remains, however, whether these oversights are sufficient to justify the extraordinary remedy of a preliminary injunction.

IV

[4] Defendants vigorously argue that they have no legal duty to offer a fair price (although they also maintain that the price offered

is fair). They argue that their only fiduciary duty as a majority stockholder making a tender offer is one of full disclosure. They cite the unreported case of *Lewis v. Fuqua Industries*, Del. Ch., C.A. No. 6534, Hartnett, V.C., 7 Del. J. Corp. L. 478 (1982) and *Lynch v. Vickers Energy Corp.*, Del. Ch., 351 A.2d 570 (1976), *rev'd. on other gronds*, Del. Supr., 383 A.2d 278 (1977), and *American Medicorp, Inc. v. Humana, Inc.*, Del. Ch., 381 A.2d 571 (1977), none of which cases, however, involved the unusual factual situation present here.

The rationale of the cases cited is that a stockholder is under no compulsion to accept a tender offer and can determine for himself if the offer is fair to him. The stockholder's option to accept or reject a tender offer is, of course, necessarily based on whether he has before him all the facts necessary to make an informed decision. *Lynch v. Vickers Energy Corp., supra.*

While I agree with the general rule that a stockholder, if there has been a complete disclosure to him of all germane facts with complete candor, should be left free to make his own decision as to whether to tender or keep his shares, there are exceptions. One such exception is when the maker of a tender offer, who has a fiduciary duty to the offeree, structures the offer in such a way as to result in an unfair price being offered and the disclosures are unlikely to call the unwary stockholder's attention to the unfairness.

Here the tender offeror retained Morgan Stanley to render an opinion as to the fairness of the price to be offered. Obviously a primary purpose of the fairness opinion of Morgan Stanley was to convince the stockholders to whom the tender offer was to be made that the price offered was fair. To believe otherwise is unrealistic. The maker of the tender offer, however, withheld from Morgan Stanley essential facts necessary for Morgan Stanley to arrive at a fair and accurate opinion as to the value. The essential information withheld was any non-public information about the value of the probable oil reserves. It would defy reason to find that an oil exploration company such as Shell could be valued without any in depth inquiry into the estimated value of the probable oil reserves. Indeed, it is possible—although not probable—that the probable reserves may be the single most valuable asset of Shell.

Reasonable men can differ as to opinions as to value. Indeed, the Court is well aware that expert appraisers usually express different opinions as to value even when they use the same data for arriving at their opinion. And it is not unusual that an expert appraiser will express a higher value if he has been hired by the plaintiff than if he has been hired by the defendant.

The problem here is not that the value opinion of Goldman-Sachs is higher than the value opinion of Morgan Stanley—that is expected by sophisticated investors—but rather that Morgan Stanley was not even given the opportunity to examine and evaluate the data relating to the value of the probable reserves. This conduct falls short of the fiduciary duty owed to the stockholders of Shell by the maker of the tender offer. It shows a failure to make available to the appraiser hired by the offeror the essential information needed by the appraiser if his appraisal was to have any meaning. This would appear to be a breach of fiduciary duty aside from any issue of failure to make full disclosure.

[5] In addition, the disclosures made to the stockholders failed to clearly and unequivocally disclose that essential and necessary information had been withheld from the appraiser. A disclosure to the effect that "Morgan Stanley based its opinion of value on publicly disclosed information" falls far short of the full and complete disclosure with absolute candor required by Delaware law. *Lynch v. Vickers Energy Corp., supra.*

This alone constitutes a breach of fiduciary duty and is probably adequate reason to impose sanctions upon some of the defendants. There are, however, other failures of full disclosure which appear in the record.

V

A careful review of the tender offer materials shows that they do not satisfy the requirement of disclosure of all germane facts with complete candor as is required by Delaware law. *Lynch v. Vickers Energy Corp., supra.* In *Vickers*, the Delaware Supreme Court held that a tender offer failed to disclose fully two critical facts, each of which fell short of the standard which requires a complete disclosure of all germane facts. The Court found that it was not disclosed that a "highly qualified" petroleum engineer, who was a member of the target company's management had calculated the net asset value to be worth significantly more than the minimum amount disclosed in the offer. Furthermore, the Court held that there was a failure to state that the offeror's management had authorized open market purchase of the target's stock during the period preceding the $12 per share tender offer for bids up to $15 per share.

The failure to disclose with complete candor that Morgan Stanley was not given access to the data necessary to fully and completely evaluate the value of the probable oil reserves has been discussed previously. Defendants claim that there was an adequate disclosure of the valuation of the probable reserves by Morgan Stanley because Morgan Stanley did assign a value to the probable reserves. It is clear,

however, that Morgan Stanley did not explicitly state a value for the probable reserves and it is unlikely that they ascribed very much value to them. It certainly did not expressly state that it did not have available to it all the data necessary to make an informed judgment as to the value of the probable reserves. The fact that Shell in its 14-D-9 Schedule filed with the SEC did reveal certain data concerning the value of the probable reserves does not relieve the tender offeror from meeting its duty of full disclosure.

There also has been no disclosure of the fact that some of Shell's management made estimates of value based on a going concern basis of $91 per share. I find this to be a germane fact that a stockholder would deem relevant in making his decision. SPNV cannot meet its duty by claiming that the plaintiffs cannot prove that SPNV knew about the $91 figure. Two of the directors of Shell are employees of Royal Dutch and they most certainly knew, of should have known, of the management's opinion as to value. SPNV and its investment advisor never made a request for Shell management's in-house evaluation when it is clear that they should have made inquiry. As evidenced by the comment of Mr. Van Wachem of the Royal Dutch group:

> ". . . we find it difficult to believe that any outsider, no matter how competent, could improve upon the evaluation of oil and gas reserves made by the professional Shell Oil staff over a substantial period of time in the regular course of their business."

Defendants argue that Shell's 14-D-9 Schedule as filed with the SEC, which reflected that there had been expressions of values ranging from $77 to $152 should be considered a part of the materials available to the stockholders concerning this tender offer and those disclosures therefore cure the failure of the tender offer materials to disclose the existence of the $91 per share valuation opinion. This argument also falls short. The $91 figure, calculated in response to a request from the special committee, is surely a relevant figure. The duty to disclose it cannot be fulfilled by mere reliance on a general expression of value. A similar argument was made and rejected in *Lynch v. Vickers, supra.* In that case, the defendants asserted that they discharged a duty to disclose specific estimates by disclosing that the target company's net asset value was "not less than $200,000,000 . . . and could be more." Justice Duffy replied to that argument by stating, "Technically speaking, the language may be accurate; but that kind of generality is hardly a substitute for hard facts when the law requires complete candor."

The failure to fully disclose the recent discoveries in the Beaufort Sea is also troublesome. The deposition testimony of Mr. Fiedorek of Morgan Stanley stated that Morgan Stanley did not include the value of that discovery in connection with the fairness opinion of April 3, 1984. Basically, it was his opinion that the discovery was too recent, the equity market had not had time to react, and it had not yet been proven that the discovery was significant. He concluded that, "Based on these factors and discussions with Mr. Good, who is the Morgan Stanley oil and gas reserves analyst and is extremely knowledgeable in the industry generally, and specifically in the area where the Beaufort Sea discovery is located, we were of the view that it did not have present material effect on the value of Shell, and hence, the Beaufort Sea discovery was among those factors considered and was included in the subsequent fairness opinions of March 29 and April 3." Hence, he stated, no amount of value was added because of the Beaufort Sea discovery. However, from a review of an exhibit placed in evidence by the plaintiffs, it is apparent that Mr. Good, Morgan Stanley's own expert analyst, did ascribe a value to the discovery in what appears to be an inter-office memorandum to a F. B. Whittemore (copy to B. D. Fiedorek) on January 23, 1984. His estimate was that Shell's incremental increase per share because of the discovery would be $3.90. Although this is an estimate, it is certainly relevant and material to an indecisive shareholder. While the testing at the Beaufort Sea is incomplete, the prsence of oil has been confirmed. Furthermore, there was enough time to include the estimate from Shell's specialist in the Beaufort Sea area in the tender offer circular or to at least have mentioned the potential value the discovery had.

[6] Lastly, the failure of the tender offer materials to completely and with utmost candor make clear that the initial valuation opinion of Morgan Stanley was arrived at after only eight days of scrutiny violates the rule set forth in *Weinberger v. UOP, Inc.*, Del. Supr., 457 A.2d 701 (1983). The fact that Morgan Stanley had prepared a similar preliminary report in 1982 does not relieve the tender offeror from fully disclosing the circumstances surrounding the presentation of Morgan Stanley's fairness opinion.

In summary, it may be that each of the failures to disclose, as discussed above, standing alone might not be of great importance to a stockholder asked to decide whether to tender or hold his shares. When, however, they are all considered together and are also considered against the factual background of this transaction, it is clear that the tender offeror has not met its duty of disclosure under Delaware law.

VI

[7]I reject plaintiffs' argument that the tender offeror's failure to negotiate the price in an arms-length manner violates the rule of law announced in *Weinberger v UOP, Inc., supra. Weinberger* involved a freeze-out merger—not a tender offer. In *Weinberger* the Court merely indicated that an arms-length negotiation was desirable. Of course, if arms-length negotiations took place it would be powerful evidence that the price arrived at was fair. Cf. *Getty Oil Co. v. Skelly Oil Co.*, Del. Supr., 267 A.2d 883 (1970). But the failure to arrive at the price by arms-length negotiations does not *ipso facto* indicate an unfair price. It is but one factor to be considered.

VII

[8]Having found that the plaintiffs have shown the reasonable probability that some of the defendants have breached a fiduciary duty, it is now necessary to consider whether there exists the reasonable probability of irreparable harm. *Gimbel v. Signal Companies, Inc.*, Del. Ch., 316 A.2d 599 (1974).

To permit the minority stockholders of Shell to decide to tender their shares without the omissions of the defendants being cured might forever deny to those tendering stockholders their right to be treated fairly. This would constitute such harm as could not easily be unscrambled and is therefore irreparable.

VIII

In my holdings I have not substituted my judgment of the fairness of the tender offer price for the opinion of the ultimate finder—the stockholder. It is likely that both the opinions of Morgan Stanley and of Goldman-Sachs leave something to be desired. Morgan Stanley's inability to judge the value of the probable reserves because of the lack of information, the shortness of time in the preparation of its update report, its quick and cursory reaffirmation of its opinion as to value after the fourth quarter earnings were announced, and after the announcement of the Alaskan oil discovery, all tend to diminish the impact of its opinion.

Likewise, the over-reliance by Goldman-Sachs on a liquidation analysis, its questionable methodology, and the uncertainty of its opinion, also leave something to be desired.

And as in all appraisals, the impartiality of the appraiser is always open to evaluation.

What I have found is that Morgan Stanley was prevented from doing the job for which it was hired because of the failure of the tender offeror to make available to it the data which it needed to prepare a valid fairness opinion. I have also found that certain germane facts were not disclosed to the minority stockholders which they should have been given, considering all the facts and circumstances present here, if they are to have a fair opportunity to make an informed judgment as to the fairness of the tender offer.

IX

[9]Finally to be considered is the remedy to be granted. Only defendants Shell and SPNV are presently before the Court. Plaintiffs have not shown any basis for a preliminary injunction to be entered against Shell and therefore any relief granted must be as to SPNV.

This Court, as the court of equity, has broad discretionary powers to grant or withhold a preliminary injunction, *Bayard v. Martin*, Del. Supr., 101 A.2d 329 (1953), and to structure a remedy which will be as fair as possible to all the competing interests. *Guarantee Bank v. Magness Construction Co.*, Del. Supr., 462 A.2d 405 (1983).

In fashioning an appropriate remedy for this stage of the proceeding, I must balance several considerations. The plaintiffs have convinced me that it is reasonably probable that the tender price is too low because it probably does not reflect the full value of the probable reserves. The record also shows that Goldman-Sachs found that the value of these reserves, when examined in depth, would only add—at a maximum—an additional $4 per share to the value of Shell's shares.

On the other hand the record also shows that Morgan Stanley did ascribe a value to the probable oil reserves, although it did so without an indepth analysis of their potential and did not ascribe an explicit value.

Although the tender offer price is probably below the true value of the shares and is certainly below the liquidation value of the shares if all the stock of the company were offered for sale on an open bid basis, the facts are that all the shares will never be so offered. Obviously the fact as to the ownership of the majority of the outstanding shares by the Royal Dutch group precludes that a value equal to the liquidation value will ever be reached in the market place. The liquidation value—whatever it may be—must therefore be discounted by a stockholder who is considering whether to tender. How much of a discount is for each investor to decide for himself—but only after he has been given all the facts.

The Court is mindful that some stockholders of Shell have probably considered selling their shares at $44—or even $40—per share and the tender offer price of $58 is considered to be a windfall. Their rights must be considered.

Other stockholders, who may believe that the value of Shell stock is more than the $58 per share offered, may desire to weigh this against the fact that it may be many years before a higher price is available to them and they may desire to consider that it is not unlikely that upon termination of the tender offer the stock will drop to near its pre-tender offer price.

Other stockholders may believe that the tender offer price is greater than the fair value of stock because the tender offer does represent a 32% premium over the reputed closing price on the day before the public announcement of the initial proposal of SPNV to acquire the minority shares and because they, with some justification, must discount the opinion of Goldman-Sachs which has a stake in the outcome and is most certainly not impartial.

Plaintiffs seek to permanently enjoin what they term to be the freeze-out of the minority stockholders. To grant such relief would be overbroad, might not be consistent with investment desires of many stockholders, and would prohibit a tender offer being made by the majority stockholder which is permitted under Delaware law if done properly.

It would be impossible to imagine all the different reasons a particular stockholder might have for deciding to tender or not to tender shares in response to the tender offer. The best way to attempt to reconcile and at least partially protect the many different interests and investment desires of the minority stockholders and still maintain the duty of the Court to prevent breaches of fiduciary duty is to hold the completion of the tender offer in abeyance, to require Morgan Stanley to review in good faith the date developed by the independent committee and to again express their opinion as to value after such review and to disclose by supplemental notices the information which I have found should have been disclosed. Those stockholders who have tendered must be given an opportunity to withdraw their shares, if they desire, after the supplemental disclosure is made.

The need to promptly comply with this ruling is obvious. Counsel shall be expected to promptly confer and submit a proposed order.

Needless to say, I have not commented on all the many arguments made by the parties, some of which are obviously not relevant. I also have had to summarize or only briefly touch on other allegations or arguments but the constraints of time permitted no more.

I also note that the mere compliance with the mandate of this opinion will not end this matter. The other remedies for the defendants' apparent breach of their fiduciary duties, however, must await another day.

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## KAPLAN v. WYATT

No. 6361

*Court of Chancery of the State of Delaware, New Castle*

January 18, 1984

Following a report by the Special Litigation Committee formed by Coastal Corporation to investigate plaintiffs' claims in a shareholders derivative suit, the committee moved for dismissal of the action. Plaintiffs moved for limited discovery in order to make a record on the motion, requesting, among other things, each and every document reviewed or relied upon by the committee in formulating its report. The court of chancery, per Chancellor Brown, denied all but a limited portion of the discovery request, as the court considered the request overly broad and unwarranted since the plaintiffs could allege no specific facts to support the general allegations of wrongdoing set forth in their complaint. The court found this void of particulars in the plaintiffs' case most damaging to their motion in light of the Litigation Committee's lengthy and detailed report setting forth numerous findings, as well as the factual basis it relied upon in reaching its conclusion.

In addition, plaintiffs sought to revoke the *pro hac vice* admission of Texas counsel for the defendant, based on the attorney's conduct in secretly tape recording a conversation with the New York counsel for the plaintiffs, during a previous derivative action on the same facts tried in the federal courts in New York.

1. Corporations ⟹ 213

When ruling on a motion to dismiss a derivative action filed by a Special Litigation Committee, the court will inquire into the independence and good faith of the committee and reasonableness of the bases for its conclusions. Limited discovery may be permitted at the court's discretion to facilitate this inquiry. However, the purpose

of any discovery at this stage is to aid the court in evaluating the motion to dismiss more so than to aid the plaintiff in developing facts to support the merits of his case.

2. Corporations ⟹ 212

Where a Special Litigation Committee, in moving for dismissal of a stockholders derivative suit, files a lengthy and detailed report setting forth numerous findings as well as the factual basis relied upon in reaching its conslusion, the total production of all documents reviewed and relied upon by the committee in compiling its report is not necessary to the stockholder's right to challenge the good faith of the committee or reasonableness of the basis for its conclusions; particularly when the stockholders have set forth no particulars in their complaint of any specific misconduct by the defendants in support of their general charges of wrongdoing.

3. Corporations ⟹ 212

A plaintiff seeking limited discovery in order to oppose a motion by a Special Litigation Committee to dismiss a stockholder's derivative suit should have the opportunity to depose the committee members concerning the good faith of its efforts and reasonableness of its conclusions. When the committee files a lengthy and detailed report setting forth its findings and the factual basis for its conclusion, the report itself, together with any knowledge the plaintiff may have supporting the allegations of the complaint, provides a reasonable basis to enable plaintiff to proceed with those depositions.

4. Attorney and Client ⟹ 38

It is unethical for an attorney in the course of his practice to record a conversation without informing all parties to that conversation.

5. Attorney and Client ⟹ 38

When a meeting of counsel is directed to be held by a federal judge with regard to a case pending before him, it is reprehensible for one attorney to secretly tape record another in the course of each representing his respective client, regardless of the circumstances which are said to justify it.

6. Attorney and Client ⟹ 36(1)

Where a party seeks a motion to revoke the admission *pro hac vice* of opposing counsel based on conduct engaged by him in another jurisdiction and in another case, the court will grant such a motion

only where the acts of the attorney are contemptuous of the court or where they adversely affect the conduct of the trial. Otherwise, the matter should be left to the disciplinary machinery of the home state of the attorney.

7. Attorney and Client ⟹ 10

In ruling on a motion to revoke the admission of counsel to a proceeding *pro hac vice* based on the allegation of unethical conduct, the court will balance the need of the litigants to be represented by the counsel of their choice against the inherent right of the court to assure the ethical conduct of the attorneys who appear before it. In such deliberations, it would be inappropriate for a court to take such action against an attorney when his professional record is otherwise unblemished, the conduct complained of took place in another jurisdiction, and when the results of his conduct can be handled so as not to adversely affect the further course of the present proceedings.

8. Evidence ⟹ 359(5)

Where an attorney secretly tapes his conversations with opposing counsel, in the course of each representing his respective client, any transcript made therefrom shall not be used or relied on by any party for any purpose connected to the proceedings.

Irving Morris, Esquire, of Morris and Rosenthal, Wilmington, Delaware, and Melvyn Weiss, Esquire, of Milberg, Weiss, Bershad, Specthrie & Lerach, New York, New York, for plaintiff.

Henry N. Herndon, Jr., Esquire, and Clark W. Furlow, Esquire, of Morris, James, Hitchens & Williams, Wilmington, Delaware, for the Special Litigation Committee.

Roderick R. McKelvie, Esquire, of Ashby, McKelvie & Geddes, Wilmington, Delaware, and Robert E. Walls, Esquire, Houston, Texas, for defendant The Coastal Corporation.

BROWN, *Chancellor*

Two motions are pending in this matter. First, pursuant to the format created by *Zapata Corp. v. Maldonado*, Del.Supr., 430 A.2d 779 (1981) this derivative action has advanced to the phase wherein the Special Litigation Committee (hereafter "the Committee") has investigated plaintiffs's claims, filed its report and moved for dismissal of the action, thus prompting the plaintiff to move for limited discovery

so as to make his record on the motion. This motion for limited discovery is before the Court for decision.

Secondly, plaintiff has moved to revoke the *pro hac vice* admissions of Texas counsel for the defendant, The Coastal Corporation (hereafter "Coastal"), the basis being that the attorney, Robert E. Walls, concealed a tape recorder on his person and secretly taped a conversation with Melvyn I. Weiss and his partner, New York counsel for the plaintiff in this action. I deal with these motions as follows.

I

Predictably, the plaintiff's motion for "limited" discovery with regard to the Committee's motion to dismiss actually seeks production of documents which would appear to cover all aspects of the plaintiff's case, and then some. He seeks the production of each and every document reviewed or relied upon by the Committee in formulating its report and, in addition, he seeks all documents relating to any business relations between Coastal and any company or business with which either of the two members of the Committee were ever affiliated. Moreover, he wants all documents bearing upon the manner in which the law firm and the accounting firm which assisted the Committee were selected, plus documents showing the fees paid to these firms and the time expended by them. In all, plaintiff seeks the production of documents in 54 separate categories. Once this production is completed, plaintiff would propose to take the depositions of the members of the Committee as well as the depositions of all members of the law firm retained by the Committee who assisted in the investigation.

The breadth of this "limited" discovery sought by the plaintiff is no doubt influenced by the fact that the Committee, assisted by the New York law firm of Brown, Wood, Ivey, Mitchell & Petty ("Brown,Wood") and the accounting firm of Ernst & Whinney, is said to have investigated the allegations of the complaint over a period of seven months during which time either its members or its attorneys interviewed 140 people, examined hundreds or perhaps thousands of documents and traveled to London, Bermuda and various cities in the United States. Moreover, the Committee went on to investigate related matters beyond those alleged in the complaint. The result of its investigation is a 156-page report, supplemented by appendixes and affadavits, in which the Committee finds the charges in the complaint to be wholly without foundation.

Plaintiff contends that his production demands are narrowly drawn and addressed in the main to specific aspects of the report. And indeed,

this may be true as far as it goes. But the fact is that because the report is so comprehensive in its coverage of the things alleged and of matters related to things alleged in the complaint, the discovery sought by the plaintiff necessarily covers the entire spectrum of the plaintiff's case, and perhaps more.

[1]The decision in *Zapata* makes clear that the function of the Court in addressing a motion to dismiss a derivative action brought on by a special litigation committee is to inquire into the independence and good faith of the committee and reasonableness of the bases for its conclusion that the derivative action should be dismissed. Limited discovery may be permitted by the Court, in its discretion, to facilitate its inquiries into this limited area. *Zapata Corp. v. Maldonado, supra,* at 430 A.2d 788. Thus, the purpose of any discovery at this stage is to aid the Court in evaluating the motion to dismiss under the aforesaid guidelines more so than to aid the plaintiff in developing facts which would support the merits of his case. It is within the scope of these confines that the plaintiff, through limited discovery, is to be given "the opportunity to make a record on the motion." Thus sayeth *Zapata* as I read it.

Measured against this standard I agree with the defendants that what the plaintiff is seeking by his discovery request is not so much an opportunity to assist the Court in its inquiries into the independence, good faith and reasonableness of the Committee as it is an opportunity to assist the plaintiff in his effort to find something—anything—to which he can point in support of his complaint. I say this because to date plaintiff has neither alleged any specific facts in his complaint nor came forward with any specific fact to support the general allegations of wrongdoing set forth in the complaint. Nor, with the exception of the inferences contained in one document, has the plaintiff given the Committee any indication of any specific acts of wrongdoing which he feels it should have investigated despite the repeated requests of the Committee that he do so.

In short, the Committee, in a rather staggering expenditure of time and money, has purported to investigate any and all things even remotely connected with the general allegations of wrongdoing set forth in the complaint without the benefit of any meaningful input from the plaintiff along the way as to any specific instances into which it should have been looking, and it has found nothing which would appear to support a derivative action on behalf of the corporation. Now, the plaintiff would like to have full discovery of everything which the Committee has done and found, he says, in order to test whether the Committee has acted independently, reasonably and in good faith in

reaching its conclusions. Plaintiff, from his perspective, may well feel that he needs all of this. For my part, however, I do not.

Plaintiff argues first of all that there are seven serious impediments to the acceptance of the asserted good faith and independence of the Committee. Among these is the charge that neither the Brown, Wood firm nor Ernst & Whinney are independent since they have both been sued as defendants in prior litigation brought by the present counsel for the plaintiff. Thus, the implication is that the law firm and the accounting firm are out to get revenge on plaintiff's lawyers and, accordingly, their advice to the Committee is probably tainted by this bias.

Plaintiff also charges that one of the two Committee members is not independent because of previous business dealings with Coastal. He also attacks the credibility of certain persons interviewed by the Committee for various stated reasons. And he attributes bad faith to the Committee because it failed to disclose that it had received a transcript of the surreptitious tape recording made of plaintiff's counsel by Walls.

I note that the common thread which ties all of plaintiff's "seven impediments" together is that they all constitute arguments as to why the Committee's motion to dismiss the suit should be denied and, in the process, they all rely in the main on facts which are already known to the plaintiff. As such, none of these contentions serve to justify the wide-ranging document production and discovery that the plaintiff seeks concerning everything that the Committee did over its seven-month investigation.

Turning then to what I feel is relevant discovery given the stage of the proceedings and the circumstances of the case, I think it sufficient that plaintiff's requests for production Nos. 2 through 5 be granted. These seek documentary information concerning the nomination of Mr. Holliday and Mr. Marshall (the two persons who comprised the Committee) as directors of Coastal as well as all documents indicating the existence of any business organizations with which Holliday and Marshall are said to have been affiliated. I think that this is fair documentary discovery with regard to the independence of the Committee.

[2]On the other hand, I do not feel that the total production of all other documents reviewed and relied upon the Committee in compiling its report is necessary to the plaintiff's right to challenge the good faith of the Committee or the reasonableness of the bases for its conclusion that the derivative action should be dismissed. Nor do I feel it warranted. In this regard I am particularly mindful of the

fact that the plaintiff has set forth no particulars in his complaint of any specific misconduct by the defendant Oscar S. Wyatt or by the defendant WJS Shipping Associates, Inc. to support his general charges of wrongdoing by these defendants. Contrasted with this, the Committee has filed a lengthy and detailed report setting forth numerous findings as well as the factual basis relied upon by it in reaching each such conclusion.

The report itself discloses in detail the breadth of the Committee's investigation and the reasons for its recommendation. Plaintiff has the Committee's position and its bases therefore. There is no doubt as to where it stands on the plaintiff's charges, or why. If the plaintiff has evidentiary matter which tends to contradict the facts relied upon and disclosed by the Committee in reaching its conclusions, or facts which would tend to indicate that the Committee did not conduct its investigation in good faith, then I think that the time has come for the plaintiff to bring them forth and develop them on his own as opposed to culling through hundreds or thousands of documents previously reviewed by the Committee on the pretense of attempting to satisfy himself that the Committee has done a good faith job and that its report and recommendation are warranted based upon that which it had before it.

[3]It is my feeling that the report itself, together with any knowledge the plaintiff may have supporting the allegations of the complaint, provides a reasonable basis to enable the plaintiff to depose the members of the Committee concerning the good faith of its effort and the reasonableness of its conclusions. And I feel that the plaintiff should have the opportunity to depose the Committee. But under the circumstances of this case I think that this is sufficient for my purposes with regard to the pending motion of the Committee to dismiss the suit pursuant to the procedure established by *Zapata*.

In this regard, it has been brought to my attention that Raymond Holliday, one of the two Committee members, has died since the presentation of the plaintiff's motion. In view of this unfortunate development, I shall grant leave to the plaintiff to depose Mr. Marshall and also to depose the member of the Brown, Wood firm, to be designated by the Committee, who is the most knowledgeable of the facts of its investigation and the manner in which it was conducted. Absent the death of Mr. Holliday I would not have done this and would have limited the depositions to those of Holliday and Marshall. In view of the scope of the report and the length of the Committee's investigation, however, I do not think it would be fair to limit the plaintiff to the deposition of only one person who participated in the enterprise.

Counsel for the Committee may submit a form of order reflecting the result reached herein.

II

The motion to revoke the *pro hac vice* admission of Robert E. Walls as Texas counsel for Coastal presents an awkward problem. The facts applicable to the motion are these.

Prior to this action being filed in Delaware, the plaintiff first filed his derivative action in the Federal courts in New York. The defendents responded by attempting to take the deposition of both the plaintiff and his counsel, it being their feeling that the suit had been filed in the absence of any knowledge by the plaintiff and his counsel of any real facts of substance to back it up. The Federal judge refused to permit the deposition of plaintiff's counsel to be taken, but he did direct that counsel for the parties meet with each other to discuss the case.

Such a meeting was held in New York on November 20, 1980. It was attended by Mr. Weiss and his partner, Richard M. Meyer, on behalf of the plaintiff, and by Michael Lesch, counsel for the defendant Oscar S. Wyatt, and by Mr. Walls as counsel for Coastal. Without disclosing it to his fellow attorneys, Walls secretly tape recorded this meeting. He later caused a transcript of the meeting to be prepared for use by Coastal in the defense of the matter.

Subsequently, the New York action was voluntarily dismissed and this suit was filed in Delaware. At an early proceeding Mr. Walls was admitted "*pro hac vice*. Also during previous proceedings in this case Walls filed an affidavit in which he relied on statements made by Weiss during the New York meeting between counsel. That affidavit was offered to contradict statements being made by Weiss to this Court. It was not until other proceedings in this case during June 1983 that Weiss and his local associate counsel first learned that Walls had taped the November 20, 1980 meeting. At that time Walls candidly admitted to the Court that he had taped the meeting without the consent or knowledge of the others present, but he took the position that it was perfectly legal to do so both under the law of Texas, where he was admitted to practice, and under the law of New York, where the taping actually occurred. (This is based upon what to me is a rather tenuous rule of law generally applicable to criminal matters that where at least one party to a conversation consents to it being recorded, i.e., the person making the recording, it is lawful to do so even though the other parties to the conversation are unaware that the recording

is taking place.) Walls also indicated at the time that such recording of a conversation by an attorney was expressly permitted under a ruling of the Texas Bar Association.

[4]What we have all learned since June, however, is that there is a 1974 ruling of the American Bar Association (Formal Opinion 337) and a 1974 ruling of the New York State Bar Association which denounce the practice of a lawyer recording a conversation without the consent of the other persons present. Moreover, in 1978 the Ethics Committee of the Texas Bar Association reversed its previous position and specifically ruled that it was unethical for an attorney in the course of his practice to record a conversation without informing all parties to the conversation.

Mr. Walls now states by affidavit that he was unaware of these rulings when he made the secret recording of his meeting with Weiss, Meyer and Lesch. He further indicates that he will refrain from any similar activity in this case in the future. Nonetheless, while his mistake may have been an honest one, the fact remains that to the extent that he was acting as an attorney for Coastal at the time his conduct would appear to have been improper under the rulings of both the Texas and New York State Bar Associations as well as under the formal ruling of the American Bar Association.

[5]Personally, I have a strong aversion to any such tactics. For one attorney to secretly tape record another in the course of each representing his respective client is, to me, reprehensible regardless of the circumstances which are said to justify it. This is particularly true when it is done at a meeting of counsel directed to be held by a Federal judge with regard to a case pending before him. Were this done in a case pending before me I would not hesitate to remove out-of-state counsel on the spot. This, however, highlights the problem.

The improper conduct of Mr. Walls in secretly taping his fellow members of the Bar did not occur in this case. Rather, it occurred in the context of the New York action prior to the time that this case was ever filed. Thus, the basis for the motion to revoke Mr. Wall's admission *pro hac vice* is conduct engaged by him in another juridiction and in another case, albeit one between the same parties and with same basic issues. The extent to which he has done anything in this case consists of the filing of an affadavit to put before this Court factual matter which he obtained as a result of the secretly recorded conversation and, as I understand it, this was done at a time when Walls believed that he had done nothing improper by making the recording.

Coastal, through its local counsel, asks that Walls be permitted to remain in the case. He is said to be the member of Coastal's house counsel staff who has the most knowledge of the matter since he has been actively involved in the proceedings for some three years now. Coastal contends that it would work an unfair hardship upon it as the client if Walls were now to be disqualified from further participation in the case. It says that this is a factor to be considered before the *pro hac vice* admission of an attorney is revoked. See *Hallman v. Sturm Ruger & Co., Inc.*, Wash.App., 639 P.2d 805 (1982); *Johnson v. Trueblood*, 629 F.2d 302 (3rd Cir.1980).

Moreover, Coastal argues that this Court has no authority to disqualify Walls under the present circumstances. It points out that he was in good standing as a member of the Bar in his home state of Texas at the time that he was admitted in this case, and that he remains so at present. It argues that whether or not his conduct in recording the meeting is deserving of disciplinary action is a matter to be determined by the Texas Bar Association and its highest Court, if necessary, and not by this Court, just as it would be the function of the Delaware Bar Association and the Delaware Supreme Court, and not the function of this Court, to pass upon the propriety of conduct by a Delaware lawyer committed outside of the presence of this Court.

[6]Indeed, in the absence of any Delaware precedent on the subject, Coastal asks that this Court be guided by the decision in *Hahn v. Boeing Company*, Wash.Supr., 621 P.2d 1263 (1980) in which it was held that a trial court lacks the authority to conduct what, in effect, are attorney disciplinary proceedings even though it has the authority to disqualify an attorney for unethical conduct committed in proceedings before it. In *Hahn v. Boeing Company* it was indicated that a trial court should disqualify counsel from appearing *pro hac vice* only where the acts of the attorney are contemptuous of the court or where they adversely affect the conduct of the trial. Otherwise, the decision indicates that the matter should be left to the disciplinary machinery of the home state of the attorney.

[7]Having reflected upon the problem, and balancing the need of Coastal to be represented by counsel of its choice against the inherent right of the Court to assure the ethical conduct of the attorneys who appear before it, I am persuaded to accept the argument of Coastal and to deny the motion to disqualify Walls. Since his professional record is said to be otherwise unblemished, since the conduct complained of took place in another jurisdiction prior to the filing of this case, and

since I feel that the tainted product of his effort can be handled in a manner so as not to adversely affect the further course of these proceedings, I feel that it would be inappropriate for this Court to take action against Walls which might be equated by others with a finding that he had violated the Code of Professional Responsibility. That question can be passed upon by the appropriate authorities elsewhere, if necessary.

[8]At the same time, and so as to dispel any thought that the Court, by denying the motion, is putting its seal of approval upon the type of activity engaged in by Walls, it is further my conclusion that the statements made by Weiss, Meyer and Lesch at the November 20, 1980 meeting, as reduced to transcript form by Walls, shall not be used or relied upon by Coastal, or by any other party to this proceeding, for any purpose connected with this proceeding. Nor do I intend to pay any attention to excerpts from the transcript. To the extent that the right to free expression and confidentiality between counsel that should have prevailed at the aforesaid meeting can be honored and protected after the fact, it is my intention to do so, at least within the confines of the litigation in this Court.

On this basis the motion of the plaintiff to rescind and revoke the *pro hac vice* admission of Mr. Walls is denied. Plaintiff may submit an appropriate form of order reflecting this decision.

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## PELMAR CO. v. MORGAS, INC.

No. 7519

*Court of Chancery of the State of Delaware, New Castle*

April 16, 1984

Plaintiff, a partner, sought (1) to preliminarily enjoin the partners of his partners of his partnership from entering into arbitration regarding a contract between the partnership and a corporate aligned with the plaintiff and (2) to be made privy to legal advice given to the other partners regarding the arbitration. The decision to seek arbitration had been properly made under the terms of the partnership agreement.

The court of chancery, per Chancellor Brown, conditionally denied the injunction on the ground that the plaintiff, under the partnership

agreement, could call a meeting of the partnership to attempt to persuade the other partners to call off the arbitration but had waited one month to call a meeting, and, when he did so, failed to set forth his position on the merits. In addition, the plaintiff waited two months to bring suit. Nonetheless, the court could not justify the withholding of legal advice regarding the arbitration even though the opposing party was aligned with the plaintiff. Therefore, the court conditioned the denial of the preliminary injunction on the disclosure of the legal advice.

1. Partnership ⟹ 70

Partners owe a fiduciary duty to other partners at common law.

2. Partnership ⟹ 14

All partners have equal rights in the management and conduct of the partnership business.

3. Partnership ⟹ 1

A partner is not entitled to withhold legal advice given to the partnership from another partner even if that advice is in regard to contracts with entities related to the partner from whom the information is sought to be withheld. DEL. CODE ANN. tit. 6, § 1520 (1953).

4. Partnership ⟹ 118

A partner who has failed to pursue promptly his remedies under the partnership agreement may not seek to enjoin his partners from taking actions authorized by the partnership agreement.

R. Franklin Balotti, Esquire, of Richards, Layton & Finger, Wilmington, Delaware, for plaintiff.

H. James Conaway, Jr., Esquire, of Young, Conaway, Stargatt & Taylor, Wilmington, Delaware, for defendants.

BROWN, *Chancellor*

This is a decision on the application of the plaintiff for a preliminary injunction. The application arises out of the demand of one partner to a partnership that it be made privy to certain legal advice provided to the other two partners, and that the partnership be enjoined from seeking arbitration of a commercial contract dispute until such time as it has been properly authorized to do so by the partners at a meeting called pursuant to the notice required under the partnership agreement.

The partnership is the defendant Lachmar. It was formed under Delaware law. The three partners are the plaintiff Pelmar Company ("Pelmar") and the defendants Morgas, Inc. ("Morgas") and Pantheon, Inc. ("Pantheon"). Pelmar is a subsidiary of Panhandle Eastern Corporation ("Panhandle") and it owns 40% of Lachmar. Morgas is a subsidiary of Moore McCormick Resources and Pantheon is a subsidiary of General Dynamics Corporation. Morgas and Pantheon own the remaining 60% of Lachmar.

Two other players in the scenario are Trunkline LNG Company ("TLC") and Trunkline Gas Company ("Trunkline"). Both TLC and Trunkline are subsidiaries of Panhandle, and thus they are sister companies of the plaintiff Pelmar.

Lachmar was formed for the purpose of owning and operating two transoceanic supertankers which were to transport liquified natural gas from Algeria to Louisiana under a separate agreement ("the Transportation Agreement") between Lachmar and TLC. In another agreement ("the Trunkline Agreement") with Lachmar, Trunkline agreed to take all action necessary to enable TLC to perform its obligation to Lachmar under the Transportation Agreement. The Transportation Agreement contains a "ship or pay" provision which requires TLC to make certain minimum freight payments each year to Lachmar whether or not liquified natural gas is actually shipped during that year.

Lachmar made the first regular delivery of liquified natural gas on December 1, 1982. It continued to make deliveries until April, 1983. At that time TLC ceased transporting liquified natural gas on the two Lachmar tankers. The tankers have been idle since that time.

On December 14, 1983, at a Lachmar management meeting, Pelmar's representative (who is also connected in his employment with Panhandle and TLC) delivered a letter from TLC purporting to "suspend" TLC's obligations to Lachmar under the Transportation Agreement due to adverse economic and market conditions. By another letter Trunkline purported to suspend its obligations to Lachmar under the Trunkline Agreement. As a result, Morgas and Pantheon voted at that meeting for Lachmar to retain legal counsel to advise and represent Lachmar with regard to any options it had as a result of the communication received from TLC and Trunkline. Pelmar's representative abstained from voting on this proposal.

On January 13, 1984, the minimum "ship-or-pay" freight payment—it being in the sum of $87 million—was due from TLC to Lachmar. Apparently, between December 14, 1983 and January 13, 1984 Morgan and Pantheon—presumably after having received

legal advice on Lachmar's behalf—concluded that Lachmar should invoke the arbitration provisions of its agreements with TLC and Trunkline. Lachmar apparently has, among other things, an annual obligation of $30 million which must be paid toward the cost of the two tankers. Income from the Transportation Agreement with TLC is apparently Lachmar's only source of income. If the Transportation Agreement could be suspended indefinitely, and if Lachmar was entitled to no payments under it during its suspension, Lachmar would be financially crippled. Thus, apparently, the decision by Morgas and Pantheon to have Lachmar seek arbitration.

At the same time, Morgas and Panteon were apparently fearful that if Lachmar was caused to take such action prior to January 13, 1984, the $87 million payment due from TLC would, in all probability, not be made. Thus, they adopted a wait-and-see approach.

On January 13, 1984 TLC made the $87 million payment to Lachmar. With this payment safe in hand, Morgas and Pantheon felt that Lachmar was then in a position to assert its rights under the Transportation Agreement. Accordingly, on the theory that Lachmar was facing an emergency situation, Morgas and Pantheon caused an emergency meeting of Lachmar to be convened by telephone on January 16, 1984 without advance notice to Pelmar, and at that telephone meeting they cast their combined 60% vote to authorize Lachmar to seek arbitration. Pelmar voted against the proposal. On the same day, Lachmar's demand for arbitration was served on TLC and Trunkline.

On February 13, 1984 Pelmar requested that a meeting of Lachmar be held on March 1, 1984 to, among other things, discuss the procedures that had been used to initiate the arbitration. At that meeting Pelmar apparently for the first time voiced its objection to the manner in which the demand for arbitration by Lachmar had been authorized. Pelmar complained of the fact that it had not been privy to the legal advice given to Lachmar, that the January 16 telephone meeting did not comply with the partnership procedure for calling meetings, and that the question of having Lachmar demand arbitration had not been adequately discussed prior to the decision being made. Prior to the close of the meeting, Morgas and Pantheon voted to ratify the action taken at the January 16 meeting. Pelmar followed bringing this suit.

[1,2]Pelmar relies on the proposition that partners owe a fiduciary duty to other partners at common law, *Boxer v. Husky Oil Co.*, Del. Ch., 429 A.2d 995 (1981), and that all partners have equal rights in the management and conduct of the partnership business. *Chaiken v. Employment Security Commission*, Del. Super., 274 A.2d 707 (1971).

Pelmar charges that Morgas and Pantheon have violated these standards.

[3]Concerning the legal advice received by Morgas and Pantheon on behalf of Lachmar prior to the initiation of arbitration, Pelmar contends that the refusal of Morgas and Pantheon to disclose such advice to Pelmar violates that portion of 6 *Del.C.* §1520 which states that "[p]artners shall render on demand true and full information of all things affecting the partnership to any partner." As to the January 16 emergency meeting of the partnership management committee at which the decision was made for Lachmar to seek arbitration, Pelmar argues that there was no emergency confronting Lachmar at the time and that as a consequence the meeting should have been convened only after 10 days notice and after an agenda had been established as called for by the partnership agreement.

On this latter point Pelmar argues that with the receipt of the $87 million payment from TLC on January 13, 1984 Lachmar was in a position to cover its financial obligations for the balance of the calendar year. Since another payment was not due from TLC until January, 1985, Pelmar contends that Lachmar could hardly have been in an emergency situation three days after the receipt of the payment when the purported emergency meeting was called by its other two partners. It argues that there certainly was adequate time to give 10 days notice and permit all three partners to discuss the wisdom of initiating arbitration against TLC and Trunkline at that time.

Pelmar points out that Morgas and Pantheon all but concede that the manner in which the arbitration demand was authorized constituted litigation strategy by Morgas and Pantheon designed for a "quick strike"so as to accomplish their desired goal on behalf of Lachmar before Pelmar had an opportunity to participate in the decision-making process. This, argues Pelmar, amounted to a breach of the fiduciary duty owed to it by Morgas and Pelmar, and deprived it of an equal opportunity to participate in the management of the partnership.

Accordingly, Pelmar asks that Lachmar, Morgas and Pantheon be preliminarily enjoined from going forward with the arbitration and from taking any other steps to carry out the action approved at the January 16 telephone meeting until such time as Pelmar is provided with knowledge of the legal advice received on behalf of Lachmar by Morgas and Pantheon and a meeting of all three partners is held after 10 days notice at which Pelmar will have an opportunity to persuade its fellow partners that seeking arbitration at this time is not in the best interests of Lachmar.

Morgas and Pantheon take the position that this is so much procedural maneuvering intended by Pelmar to frustrate and delay Lachmar in seeking a determination of its rights under its contracts with TLC and Trunkline. They point to the obvious fact that Pelmar is a sister corporation to TLC and Trunkline, all three of which are owned and controlled by Panhandle. Since TLC and Trunkline are opposed to the arbitration, Morgas and Pantheon view the technical demands of Pelmar to be nothing more than a thinly-veiled attempt to further the interests of TLC and Trunkline by putting off the arbitration as long as possible.

Morgas and Pantheon take the position that an emergency did exist for Lachmar on January 16 when the emergency meeting was called. In fact, they say that an emergency was created on December 14, 1983 when Lachmar was given notice that TLC and Trunkline were unilaterally "suspending" their contractual obligations to Lachmar. They say that they were forced by practical considerations to wait until January 13 to see if the $87 million payment would be made to Lachmar by TLC, and that they invoked the emergency meeting procedure almost immediately after that date. They point to the fact that arbitration proceedings on a matter of this magnitude take time and that it will be difficult enough as it is for the arbitration procedure to run its course within a year. In short, they take the position that time was of the essence since the ultimate survival of Lachmar was at stake and that their action in calling the emergency meeting was thus in keeping with the understanding of the partnership agreement.

Morgas and Pantheon point out also that as a practical matter notice to Pelmar is notice to TLC and Trunkline. The same is true with regard to the legal advice rendered to Lachmar concerning the wisdom and its chances in seeking arbitration. To provide this information to Pelmar is, they say, to disclose Lachmar's legal position and strategy to TLC and Trunkline.

Moreover, Morgas and Pantheon contend that to the extent that there could have been any deficiency with regard to the January 16 emergency meeting it was cured by the March 1 meeting, convened on 10 days notice at Pelmar's request, as a result of which the action taken at the January 16 meeting was discussed by all three partners and ratified thereafter by the combined 60% vote of Morgas and Pantheon.

In essence, Morgas and Pantheon take the position that a prompt determination by arbitration as to whether TLC can unilaterally sus-

pend its payment obligations to Lachmar because of economic conditions is vital to the future course and existence of Lachmar. They say that the vote will be the same anyway if the preliminary injunction is granted and a new meeting on 10 days notice is required. Thus, they point out that Pelmar is threatened with no immediate irreparable injury since the outcome will be the same, and for the same reason, whether the arbitration in process is permitted to go forward or whether the commencement of arbitration is required to be started anew, thus recycling the matter for no useful reason after a waste of three months time. Thus, they would have the application denied.

The circumstances outlined by the foregoing creates an awkward situation. It would seem that Pelmar could likely prove upon a final hearing that its fellow partners purposely met and formulated business strategy for the partnership to the deliberate exclusion of Pelmar. As a general principle, it would seem that a partner in Pelmar's position should be able to participate in the decision-making process and offer its reasons in opposition to the action sought to be taken even though there was a basis to believe in advance that it would be outvoted by its fellow partners. It would be difficult indeed for this Court to put its seal of approval on conduct which deliberately deprived a minority partner of its contractual and statutory right to be heard and to participate in partnership management decisions simply because that partner was aligned with business interests which the other partners perceived for their own reasons to be in conflict with the best interests of the partnership. By this decision I do not purpose to do so.

At the same time, a court of equity will not close its eyes to the practicalities of a situation, nor will it place form ahead of substance. Here, while I have no serious doubt that Morgas and Pantheon purposely set up the situation so that they could take action swiftly on behalf of Lachmar with virtually no advance notice to Pelmar, I cannot conclude overall that Pelmar has demonstrated an entitlement to preliminary injunctive relief. I reach this conclusion for two reasons.

First, the ultimate relief Pelmar seeks is the right to have a partnership management meeting with Morgas and Pantheon so as to have an opportunity to convince them that Lachmar should not seek arbitration with TLC and Trunkline at this juncture. But as a practical matter I see no reason to first abort the ongoing arbitration in order to afford Pelmar this opportunity. Under the partnership agreement Pelmar has a right to call a meeting for this purpose on 10 days notice. Should it do this, and should it be able to convince Morgas and Pantheon of its views, the partners certainly have the power to cause Lachmar to call off the arbitration.

[4]Secondly, Pelmar could have done this at any time during the past three months. In fact it caused a meeting to be convened on March 1 but was apparently content at that meeting to voice its objection to the methods used by Morgas and Pantheon in orchestrating and calling the January 16 emergency meeting as opposed to putting forth the meat of its position on the merits. I note also that Pelmar waited almost a month—from January 16 to February 13—to seek a meeting of management, and waited some two months after the event—from January 16 to March 15—to bring this suit. I further take note that during the interim a suit was commenced in New York on behalf of TLC to enjoin the arbitration.

Thus, I cannot help but get the impression that Pelmar here is attempting to assert technical grounds dealing with notice of a management meeting, etc. as a purely tactical basis for delaying the arbitration procedure. I am convinced on the present record that Pelmar well knows that the outcome would not be different even in the event that the requested relief was granted to it, and that as a consequence it is simply attempting to buy time based upon what it, in its minority partner position, feels to be in the best interest of Lachmar. Viewed from this perspective I fail to see how Pelmar itself is threatened with any immediate irreparable harm when measured against the ultimate relief that it seeks, and accordingly I conclude that its application for a preliminary injunction should be denied.

I am bothered, however, by the refusal of Morgas and Pantheon to disclose to Pelmar the legal advice they received on behalf of the partnership and on which they apparently based their determination as combined 60% partners that it would be in the best interest of Lachmar to demand arbitration. I realize that Pelmar is aligned in its corporate structure with the parties against whom arbitration is sought by Lachmar. Nonetheless, all three partners are subsidiaries of parent corporations which obviously entered into an understanding to construct and purchase the two tankers and to pay them off through the commercial activities of one of their members. The Lachmar partnership was the device structured to carry out this enterprise. As such, I think that the potential for conflicts of interest between the partners was a realistic possibility from the outset and, having chosen the partnership form, I do not feel it to be justifiable now for the two partners to withhold legal advice given to the partnership from the third simply because that partner's interest in the partnership is at odds with their interest in the partnership.

Since all parties are before the Court, I shall deny the application for the preliminary injunction but, as a condition thereto, I direct the

defendants to disclose to Pelmar within 10 days any legal advice given to and on behalf of Lachmar on the subject of the suspension by TLC and Trunkline prior to the time that Lachmar's demand for arbitration was made. IT IS SO ORDERED.

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## READING CO. v. TRAILER TRAIN CO.

No. 7422

*Court of Chancery of the State of Delaware, New Castle*

March 15, 1984

The plaintiff, Reading Company, stockholder of Trailer Train sued Trailer Train seeking a declaration that Trailer Train's proposed agreement with creditors of its wholly owned subsidiary, American Railbox Car Company, constituted a waste of corporate assets. Due to decreased box car use and other market factors, Railbox was indebted to Trailer Train in the amount of $43 million. Under the proposed agreement Trailer Train would contribute up to $42 million over four years. The loans were to be repaid by Railbox from operating revenues. The plan was based on a study which predicted an upswing in box car utilization by 1987. The plaintiff contended that the additional loan would never be repaid and attacked the plan on the following grounds: 1) the board was not provided with sufficient information; 2) the board ignored or disregarded known facts; 3) the board acted out of self-interest and a conflict of interest; and 4) the plan would waste Trailer Train's assets. The court of chancery, per Vice-Chancellor Longobardi held that: 1) the board of directors enjoyed a presumption of sound business judgment; 2) the board had met their burden of informing themselves of all material information reasonably available to them; and 3) the plaintiff had not met its burden of proving a reasonable probability of success on the merits.

1. Corporations ⟹ 393

A board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose.

2. Corporations ⟹ 393

To invoke the protection of the sound business judgment rule, directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them.

3. Corporations ⟹ 187

The standard of intrinsic fairness will be applied only when the fiduciary duty is accompanied by self-dealing.

4. Injunction ⟹ 151

In seeking a preliminary injunction, the plaintiff has the burden of proving a reasonable probability of success on the merits and that it will suffer irreparable injury if the court fails to issue the requested relief.

Richard R. Wier, Jr., Esquire, and Walter P. McEvilly, Jr., Esquire, of Prickett, Jones, Elliott, Kristol & Schnee, Wilmington, Delaware, for plaintiff.

Allen M. Terrell, Jr., Esquire, Richard G. Elliott, Jr., Esquire, and Thomas A. Beck, Esquire, of Richards, Layton & Finger, Wilmington, Delaware, for defendant.

LONGOBARDI, *Vice-Chancellor*

The Plaintiff, Reading Company ("Reading"), sued Trailer Train Company ("Trailer Train"), seeking a declaration that Trailer Train's proposed agreement with creditors of its wholly owned subsidiary, American Rail Box Car Company ("Railbox"), constitutes a waste of corporate assets. Reading contends the debt restructuring agreement which obligates Trailer Train to an additional loan of up to $54,000,000 will never be repaid.

A motion for preliminary injunction was heard and this is the Court's decision on that motion.

Trailer Train was incorporated in 1955 by several operating railroads in order to provide a fleet of standardized railroad flat cars for lease to railroads. Over the years, 40 railroads have become stockholders of Trailer Train. Reading became a stockholder in 1961. By requiring a purchase of 500 shares of stock, each of the stockholders is given a seat on Trailer Train's Board of Directors. In 1971, Reading entered into reorganization under the bankruptcy laws and in 1976 conveyed its rail properties to the Consolidated Rail Corp. ("Conrail"). Thereafter, it discontinued all railroad operations but it retained its stock in Trailer Train.

Under the pooling concept, participating railroads were required to sign Trailer Train's Form A Car Contract. The stockholder was then entitled at a special rate to use the cars from the pool on its own lines and to interchange those cars with other railroads including non-shareholder railroads. Those shareholder and non-shareholder railroads with Trailer Train cars in their possession pay a car hire fee set by Trailer Train.

In 1974, Railbox was formed as a wholly owned subsidiary of Trailer Train. Its purpose was to provide a pool of standardized box cars. Like Trailer Train, Railbox is and has been dominated by the operating railroads. Its 23 member Board of Directors includes 20 Directors which serve on Trailer Train's Board. Of the 20 Directors, only 1 represents a non-operating railroad company. In effect, Trailer Train's management is almost identical to Railbox's management and Trailer Train provides Railbox with all its general and administrative services.

The passage of time has not been kind to Railbox's fortunes. Box car utilization has diminished over the ensuing years and the decline has been marked by at least the following circumstances:

(a) Severe seasonal imbalance in loadings and, therefore, in box car fleet productivity;

(b) A long-term downward trend in plain (unequipped) box car loadings;

(c) A rapid shift of grain loadings from plain box cars to large covered hopper cars, many of them furnished by shippers;

(d) A very rapid shift of rail merchandise traffic from the box cars largely used prior to the rise of truck competition to piggyback or rail-truck intermodal movement (cars for the latter being largely supplied by Trailer Train);

(e) Increasing specialization of the residual market for box car loadings, a market now substantially limited to a few commodity groups which require box cars fitted with loading-restraining and/or shock-cushioning devices necessary to avoid physical damage to the lading, as well as cars of greater length (50 feet or longer) and increased loading capacity reflecting both additional length and interior height (high cube cars).

To further burden Railbox, the operating railroads have seen fit to buy their own box cars and to frequently use them to the exclusion of Railbox's cars. Lastly, motor carrier competition has diverted business from box car utilization and, if railroads are used in a piggy-back mode, it is the intermodal rail car, the flat cars, and its special application forms, which have become more popular.

As Trailer Train prospers, Railbox has drifted into debt. In late 1981, Trailer Train loaned Railbox $30,000,000. In the Spring of 1982, it loaned an additional $13,000,000. Of the $43,000,000 now due, only $13,000,000 is secured. Worried about their fiduciary responsibilities, Trailer Train's management decided to get independent advice and retained the firm of Paul, Weiss, Rifkind, Wharton & Garrison ("Paul Weiss"). That firm advised an independent study should be conducted and a decision was reached to retain Temple, Barker & Sloan, Inc. ("Temple Barker"). The study, completed in September, 1982, was pessimistic and confirmed that box car utilization rates would remain lower until at least 1987. It also revealed that another $30,000,000-$40,000,000 was not going to solve the problem. In September, 1982, Trailer Train's president called a special meeting of the Board of Directors at which the pessimistic Temple Barker report was presented. At the meeting, the Board called upon Mr. Newlon of the Paul Weiss firm to advise them of their fiduciary duties and responsibilities in connection with additional loans to Railbox. In this regard, it must admitted that at this very early stage, Trailer Train's Board was conscientiously pursuing their duties, albeit on a tightrope.

The Board also commissioned another study from Booz Allen & Hamilton, Inc. ("Booz Allen"). That study, completed in October, 1982, appeared to be more pessimistic than the Temple Barker report although both predicted an upswing in box car utilization at about 1987. That report was presented to the Board on October 27, 1982.

The Trailer Train Board met again on December 2, 1982, and Newlon again advised them of their duty as Directors. Following the advice and a review of the Booz Allen report, the Board resolved to make no further loans to Railbox.

With new management in place and with a view towards resolving in problems facing Trailer Train and Railbox, Trailer Train contacted First Boston Corporation ("First Boston"). Affidavit of F.M.R. Smith, paragraph 2. Because Railbox was Trailer Train's wholly owned subsidiary and the managements were interlocking, First Boston frequently advised both Trailer Train and Railbox. It was Railbox, however, which formally retained First Boston. Railbox also retained Robert Hallock of Kirkland & Ellis. By the Spring of 1983, First Boston made a proposal for restructuring the Railbox debts. This proposal became known as Plan A. In essence, the plan required Trailer Train and the railroads to lease Railbox's box cars with certain additional obligations fixed on Trailer Train. The Railroads and the creditors of Railbox refused to participate in the plan and, therefore, it expired. Later, in the Summer of 1983, a new Plan evolved which came to be known

as Plan B or the "Workout." The Workout was presented to Trailer Train's Board in September, 1983. As presented, the Plan proposed that Trailer Train would contribute up to $42,000,000 over 4 years. The commitment amounted to a total infusion of $78,000,000 over a span of 6 years. The loans were to be repaid by Railbox from operating revenues. The economic projections supporting such a proposition were based primarily on the Temple Barker & Booz Allen reports together with management's update calculations and its projections. First Boston concurred that there was a reasonable probability of success. The critical aspect of the proposal and one of the most heatedly contested by the Plaintiff is management's projection of an extraordinary percentage increase in box car utilization rates sometime around 1987. It is noteworthy, however, that the conclusions were not entirely speculative because the Temple Barker and Booz Allen reports were supportive of that conclusion.

Between the September and November, 1983, Board meetings, continued negotiations with the creditors resulted in the Workout being modified so that Trailer Train would commit $54,000,000 over 4 years (1984-1987) with no yearly contribution in excess of $13,500,000. Thirty million of the outstanding $43,000,000 debt would be considered a contribution to capital and other creditors and equity lessors would contribute $24,000,000 again the total of $78,000,000.

On December 1, 1983, Trailer Train's Board, with 5 dissenting votes, approved a resolution authorizing management to execute the Workout agreement. The Plaintiff contends that the Board's decision was not based on a sufficient amount of information on the Workout. On the other hand, the affidavit by F.M.R. Smith, paragraphs 10, 11 and 12, indicates a fully comprehensive evaluation of the Workout and its attendant problems. Not the least of the discussions are those references to possible scenarios if the Workout was not approved. These included the institution of law suits against Trailer Train, its Board and stockholders by Railbox's creditors, the piercing of the corporate veil which would ordinarily insulate Trailer Train, the probability of Railbox's bankruptcy and the attendant credit problems Trailer Train would encounter as a result of that bankruptcy. Further, Trailer Train's negotiations for $800,000,000 in loans for new equipment would be affected so that Trailer Train would inevitably pay more for the loans than would otherwise be available. Finally, the restructuring of Railbox's debts would provide Trailer Train with substantial tax benefits calculated at $10,000,000-$12,000,000.

The Plaintiff attacks the decision of the Board on the following bases:

1. The Board was provided insufficient information on the Workout.

Plaintiff contends that the box car utilization rates were "unrealistic and inconsistent with" the Booz Allen report. In addition, it points to several areas of additional information which might have been helpful. Furthermore, Plaintiff alleges that there were no explanations for the utilizations projected by management. All of these allegations amount to a contention that the Board failed to make an informed judgment. Plaintiff also alleges that the Board received no independent legal and financial advice.

2. The Board ignored or disregarded known facts or facts it should have known.

Plaintiff attacks the projections and conclusions of the Workout. Principally, Plaintiff contends the projections were based on a fleet of 25,000 box cars when it should have known that 10,000 cars had been returned to investors. Plaintiff also contends that the Board should have known that the projections fly in the face of known trends in the industry.

3. The Board acted out of self-interest and a conflict of interest.

Plaintiff contends that the Board became an unwitting tool of the railroad industry generally and, rather than being concerned about the viability of Trailer Train, the Board was more concerned with the reputation of the railroad industry.

4. The Workout will waste Trailer Train's assets for it won't work.

Based on Paul H. Reistrup's affidavit, filed after the Board's decision, Plaintiff points to an expert's opinion that the Workout will not succeed.

Based on the foregoing, Plaintiff contends that any evaluation of its burden of proof in these proceedings should consider that the business judgment rule is not applicable. Alternatively, Plaintiff contends that the burden of proof on the merits will shift to the Defendant because the "intrinsic fairness" burden will be imposed. Under these conditions, it contends that it has shown a probability of success on the merits and if the injunction is not granted, it will suffer irreparable harm.

[1,2]As a first step, it is important, then, to determine from the complaint, the motion and supporting affidavits what the Plaintiff seeks to prove and what relief it ultimately will request. In this case, the basic premise of the complaint is that Trailer Train's decision to participate in the Workout by providing, *inter alia*, $54,000,000 over 4 years to its subsidiary, Railbox, constitutes a waste of corporate assets.

Trailer Train counters by contending that since Railbox is a wholly owned subsidiary of Trailer Train, the loan is only one of numerous incidents of control and management that has occurred since Railbox's creation and the decision by the Board cannot be assailed by the Court because of the business judgment rule. Under that rule, "A board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose. A court under such circumstances will not substitute its own notions of what is or is not sound business judgment." *Sinclair Oil Corporation v. Levien*, Del.Supr., 280 A.2d 717, 720 (1971). The protection of the rule is afforded directors, who in the exercise of their business judgment on the transaction in question, were disinterested. "To invoke the rule's protection, directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Having become so informed, they must then act with requisite care in the discharge of their duties." *Aronson v. Lewis*, Del.Supr., _____*A.2d*_____ (1984), No. 203, 1983, at 13, Moore, J. (Mar. 1, 1984). The standard for director liability is "predicated upon concepts of gross negligence." *Id.* at 14. In this regard, Reading contends that the business judgment rule is not applicable because the Board ignored or disregarded facts it should have known. In short, the argument suggests the Board's decision was not an informed one because the presentation of information to the Directors was not complete and was too abbreviated, that it contained information that was faulty, that the utilization projections were not explained and industry trends in utilization were ignored. A mere perusal of the record on these issues, however, indicates just the opposite. There is no question that Reading and their experts disagree with the basis for and the judgment of the Board. But that is not the question that must be resolved. The business judgment rule allows for the possibility that other people might disagree with a board's decision. Indeed, it is acknowledged that a board's decision, otherwise properly based, could be wrong and still withstand attack. And this is as it should be. In the context of our corporate business world, courts should be loathe to interfere with the internal management of corporations or to interfere with their business decisions unless statutory or case law indicates they have overstepped their bounds. But corporations should not be bounced back and forth, with every decision scrutinized, merely because somebody else has a different opinion. The stockholders have made their choice and they are entitled to that Board's unfettered lawful exercise of its management prerogatives. With regard

to all of Plaintiff's arguments on this issue, the Court considers them expressions of opinion which are different from those expressed and exercised by the Board. The Court believes that the record makes it abundantly clear that this Board was conscientious in the exercise of its responsibilities. Look, for instance, at their repeated requests for legal advice. Look, for instance, at their demand for an additional study after reading the Temple Barker report. In addition, these are people admittedly knowledgeable about the railroad industry. Almost to the man, they are representative of operating railroads. They know the trends in the business. They knew about the increased usage of motor freight carriers and the effects of deregulation. And they certainly knew that the reports and projections which were utilized during the December, 1983, Board meeting were based on a fleet of 15,000 box cars rather than 25,000 box cars. The projections for 1987 were based on contingencies about which ordinary and reasonable people might differ but that can be said for almost every projection of future events.

These issues are clouded by a veil of insinuation that suggests that the Board did what it did because it was a tool of the railroad industry and, as a consequence of its decision, it was serving railroad interests rather than Trailer Train's interest. The argument loses force because Trailer Train is the railroad industry, or at least an important cog in it, and what affects the industry affects Trailer Train. Being responsive to one's business environment appears to be a necessity for survival. Secondly, this appears to be a backhand approach to assailing the decision of the Court of Appeals for the Third Circuit in the *Matter of Reading Co.*, 711 F.2d 509 (3d Cir. 1983). In that case, the matter of goals, purpose and design for this corporation and how it operates and utilitzes its profits has been decided adversely to the plaintiff and is now a matter of *res judicata*. Reading did not successfully attack Trailer Train's motives in its operation in that court and it cannot be allowed to relitigate that issue in this Court.

The present record is replete with evidence which shows Trailer Train's vital interests in the restructuring of Railbox's debt. The following list demonstrates that Trailer Train and its stockholders had very much to gain by proceeding with the Workout:

1. Railbox's creditors have threatened to sue Trailer Train, its Board and stockholders unless the Workout is approved.

2. Trailer Train's ability to finance a new fleet of intermodal cars costing $800,000,000 would be jeopardized and, in the face of any litigation, would cost at least 1/2 of 1% more.

3. Without the Workout, there is a strong probability the creditors would force Railbox into bankruptcy and, according to First Boston and Kirkland & Ellis, that would seriously impair Trailer Train.

4. Trailer Train had an optimistic forecast of box car utilization as well as a pessimistic one.

5. Trailer Train was advised by First Boston that there was a reasonable probability the Workout would succeed.

6. Trailer Train would gain valuable tax advantages by proceeding with the Workout.

7. Trailer Train would get a release from Railbox's creditors.

Under all of these circumstances, it is difficult to see how Reading would succeed on the merits of its complaint.

Reading has pleaded alternatively, however, that the business judgment standard is not applicable in the present situation. It contends that the intrinsic fairness test would be applicable and, under that standard, the burden of proof would shift to the Defendant at the time of trial on the merits. Reading's position is that Trailer Train's Board and Railbox's Board were practically the same and, since the Directors stood on both sides of this parent-subsidiary transaction, Trailer Train has to prove the terms of the transaction were intrinisically fair to Trailer Train and its stockholders.

At first blush, one can read excerpts from any number of cases which say practically the same thing. The very words, "on both sides of the transaction" and "parent-subsidiary dealings" conjure up "intrinsic fairness." But it is not every transaction between parent and subsidiary with Directors on both sides that would allow judicial review utilizing the intrinsic fairness standard. The applicability of the standard "depends upon the presence of fair advantage usurped or at least secured through control . . . ." Folk, *The Delaware Corporation Law* 78 (1972). If it were otherwise, the everday business occurrences between an parent and its subsidiary would be subject to the intrinsic fairness scrutiny. Indeed, Professor Folk has captured the essence of the problem in the following quotation:

> In the application of the intrinsic fairness rule, the mere fact that interlocking directors are involved in an intercorporate transaction does not of itself cause the higher burden of proof called for under such rule to shift to the party sought to be charged with accountability. In other words, self-dealing on the part of a dominant fiduciary must first be established in order for the intrinsic fairness rule to be successfully invoked.

*Id.* at 80.

Usually, the complaining parties attempting to invoke the intrinsic fairness rule in a parent-subsidiary transaction are the minority stockholders in the subsidiary. In this case, we have the unique situation of stockholders holding a minority interest in Trailer Train complaining about Trailer Train's commitment of $54,000,000 to its subsidiary. Admittedly, then, it is Trailer Train's use of these assets which forms the basis of this minority stockholders' complaint. And the only construction which can fairly characterize the complaint, then, is that this loan of $54,000,000 is unfair to Plaintiff because it jeopardizes its investment and Trailer Train's viability. But the burden of Trailer Train's decision does not unfairly or improportionately fall on Reading. The risk falls on each and every stockholder in Trailer Train in a proportion equal to their holdings in the company. Where then, under these circumstances, is the use of domination and control utilized to the disadvantage of only Reading?

This principle was more succinctly posed in *Getty Oil Company v. Skelly Oil Company*, Del.Supr., 267 A.2d 883 (1970), when Chief Justice Wolcott decided: "A basic ground for judicial interference with business judgment on the complaint of minority interests is an advantage obtained by the dominant group to the disadvantage of the corporation or its miniority owners." *Id.* at 887.

As a matter of interest, the transaction in the case *sub judice* poses a transaction more akin to those dictated by third parties than by an agreement in isolation between Trailer Train and Railbox. From the facts presented, it is clear that the creditors involved in this case have dictated the terms of the Workout to the near exclusion of Trailer Train or Railbox. *Cf.*, *Getty Oil Corporation v. Skelly Oil Company, supra*, at 887; *Meyerson v. El Paso Natural Gas Co.*, Del.Ch., 246 A.2d 789 (1967). Under these circumstances, our courts have invariably determined the business judgment rule to be applicable.

[3]The gist of all the preceding is that the standard of "intrinsic fairness" will be applied only "when the fiduciary duty is accompanied by self-dealing . . . ." *Sinclair Oil Corporation v. Levien, supra*, at 721. And, in the context of this case, it could only be applied if there were allegations of usurpation of advantage at the expense of minority interests. I find that wanting in these pleadings.

In all fairness, the only remaining element of Reading's argument that could be interpreted to fit under the prerequisites of "self-dealing" or "advantage usurped at minority interests costs" is Reading's allegations concerning Trailer Train being an alter ego for

the railroad industry. Under this premise, the argument goes, Trailer Train adopted the Workout because it was in the railroad industry's best interests and, since Reading is not an operating railroad, all of it was at Reading's expense. To ascribe these motives is tenuous, at best, but it belies other important facts that the Court listed previously. There was a firm basis for deciding that the Workout was in Trailer Train's best interests. If it benefited anybody else, so be it. But that is no legal reason to strike the terms of the transaction. Furthermore, Reading knew since the day it first bought stock in Trailer Train that Trailer Train was designed to serve the needs of the railroad industry. Indeed, without paying dividends, it has plowed back its profits in an ever expanding fleet of modern specialized rail cars designed to promote and expedite railroad interests. Reading participated in those programs as a stockholder to its distinct advantage. When it sold its railroad holdings, it voluntarily held its stock in Trailer Train and now seeks to attack that which it subscribed to, fostered and enjoyed. To allow it to successfully attack those motives now would be inconceivable.

[4]In seeking a preliminary injunction, Reading has the burden of proving a reasonable probability of success on the merits and that it will suffer irreparable injury if the Court fails to issue the requested relief. In addition, the Court must balance the equities in this situation, weighing the conveniences and the injuries that will befall the parties if relief is granted or denied. *New Castle County, Etc. v. Board of Educ.*, Del.Ch., 451 A.2d 1156 (1982). Injunctive relief constitutes the "strong arm of equity jurisdiction, and should never be utilized unless a clear case of imminent, irreparable injury is presented . . . ." *Petty v. Penntech Papers, Inc.*, Del.Ch., 347 A.2d 140, 141 (1975).

Based on all the foregoing, it is apparent that Plaintiff has failed to carry its burden in proving a reasonable probability of success on the merits. On this basis alone, the Court denies the application for injunctive relief. There is another aspect of the case, however, that requires comment. Even if the Court had gotten as far as having to balance the equities in this situation, the Court would have denied the motion for preliminary injunction. Considering all of the disasterous results which would attend Trailer Train's abstinence from the Workout as against the possible jeopardy of Reading's relatively minor investment, the Court would have ruled the same way.

IT IS SO ORDERED.

## SACHS v. R.P. SCHERER CORP.

No. 7537

*Court of Chancery of the State of Delaware, Sussex*

April 2, 1984

Plaintiff Sachs, a shareholder of R.P. Scherer Corporation, sought a preliminary injunction to prevent a proposed reclassification of the common stock of the R.P. Scherer Corporation by defendant directors and certain shareholders who collectively own 50.26% of the outstanding voting stock of the corporation. The plaintiff, who purports to bring this suit as a class action on behalf of himself and certain public shareholders of the corporation, based his action on the charge that defendant's action would result in the breach of a fiduciary duty based on an improper motive.

The court of chancery, per Chancellor Brown, held that plaintiff failed to establish a basis for preliminary injunctive relief. The chancellor stated the complaint itself was unverified and was based upon the information and belief of counsel.

1. Injunction ⟹ 134

Where plaintiff's case is based upon speculation more so than upon fact, plaintiff will have failed to establish a basis for preliminary injunctive relief.

2. Corporations ⟹ 320(13)

Record on plaintiff shareholder's application for preliminary injunction to enjoin reclassification of the common stock of the corporation failed to establish that reclassification was an attempt by defendant principal shareholder to entrench present management.

3. Injunction ⟹ 145

Where the only affidavit filed in support of plaintiff's application is that of plaintiff's New York counsel and it goes only to verify the proxy materials and to set forth certain trading prices for the common stock of the corporation and there is nothing offered other than counsel's argument that present value of the stock will be reduced by the reclassification plan, the complaint itself is unverified.

4. Corporations ⟹ 310(1)

Managerial entrenchment is basically a matter of improper motivation in violation of a fiduciary duty.

5. Injunction ⟹ 151

An application for preliminary injunction to enjoin reclassification of the common stock of the corporation will not be granted where the record failed to demonstrate either a probability of success on the merits upon a final hearing or that plaintiff and others similarly situated were likely to suffer immediate irreparable harm in the event of a preliminary injunction.

Joseph A. Rosenthal, Esquire, of Morris & Rosenthal, Wilmington, Delaware for plaintiff.

Martin P. Tully, of Morris, Nichols, Arsht & Tunnell, Wilmington, Delaware, for defendant.

BROWN, *Vice-Chancellor*

Plaintiff is a shareholder of R. P. Scherer Corporation ("the corporation") who purports to bring this suit as a class action on behalf of himself and certain public shareholders of the corporation. The transaction he seeks to attack is a proposed reclassification of the common stock of the corporation which is to be submitted to a vote of all shareholders at a meeting of shareholders noticed for tomorrow, April 3, 1984.

Named as individual defendants are the directors of the corporation along with certain shareholders, designated in the proxy materials as the "Principal Stockholders," who own collectively 50.26% of the outstanding voting stock of the corporation. The Principal Stockholders have stated their intention to vote for the reclassification plan. Thus, its passage at tomorrow's meeting is assured. Plaintiff seeks a preliminary injunction to prevent the defendants from filing the documents necessary to consummate the proposed transaction pending further proceedings on the allegations of the complaint.

For present purposes the proposed reclassification plan may be summarized as follows. The corporation is currently authorized to issue 24,000,000 shares of common stock. At present, there are 7,837,963 shares outstanding. The transaction under attack proposes that the certificate of incorporation be amended to reduce the number of authorized common shares from 24,000,000 to 16,000,000. It is further proposed that a new class of 8,000,000 shares of Class B common stock be authorized. It is then proposed that each share of common stock be reclassified into 1/2 share of New Common stock and 1/2 share of Class B common stock. Thus, under the reclassification, each

owner of the present common stock will end up owning an equal amount of New Common and Class B common in its stead.

The basic differences in the two classes of common stock will be as follows. The New Common will have one vote per share and it will vote as a class to elect 1/3 of the directors of the corporation. The Class B common will have 10 votes per share and it will vote as a class along with the New Common to elect the other 2/3 of the directors. Per share dividends on the New Common and the Class B common will be equal, and the two stocks will share equally in the event of a liquidation.

As to transferability, the New Common will be freely transferable on the over-the-counter market, the same as the present common stock. The Class B common, however, will be restricted and will not be transferable except by sale, assignment, gift or bequest to a co-beneficial owner, such as a shareholder's spouse, his parents, lineal descendants, a trust, etc. That is to say, the Class B common will retain its 10-votes-per-share voting power and other special attributes only in the event of transfers of this type. At the same time, the Class B common will be convertible into the New Common at any time on a share-per-share basis at the option of the holder. Moreover, if a share of Class B common is transferred in violation of the restrictions on its transferability, it is automatically converted into a share of the New Common. In other words, the Class B common can be sold or traded to one not in family privity with the holder, but in that event it is converted into equal amounts of New Common, with one vote per share, as opposed to remaining Class B common with 10 votes per share. Thus, the proxy statement advises that there will be no trading market for the Class B common and that it will not constitute "OTC margin stock."

At present the corporation has an 80% supermajority voting requirement as to certain merger and acquisition transactions. This 80% requirement was adopted by a majority of the shareholders of the corporation in 1982 in the face of a hostile tender offer. The tender offer was withdrawn following the adoption of the supermajority requirement. This leads to the basis for the plaintiff's contentions.

Plaintiff contends that the reclassification plan is designed to unfairly increase the voting power of the defendant Principal Stockholders at the expense of the public minority shareholders for the sole purpose entrenching present management in office. Plaintiff says that this result is designed to come about in the following manner.

Plaintiff says that the Class B common as such will have no value to anyone other than the defendant Principal Stockholders since its

primary attribute is the 10 votes per share that it carries with it. Particularly since the Class B common cannot be traded commercially and retain its restricted characteristics, and since it will have no value as margin stock, plaintiff suggests that the practical effect of the reclassification will be to force those in the 49.74% minority (and who are still left in the minority even with the enlarged voting power of the Class B common) to sell their Class B common so as to realize something for it. In order to do this, however, they will first have to exercise their option to convert Class B common into New Common, or, alternatively, this will occur automatically in the event of an attempted sale and transfer in violation of the transferability restrictions on the Class B common. By either method, the sale of a Class B share converts it into a share of New Common, carrying with it one vote rather than 10 votes.

Thus, plaintiff suggests, as the Class B shares are gradually sold off and converted by the present minority, each 10 votes represented by a share of Class B common will be reduced to one vote represented by the share of New Common received in exchange. Thus, while the Principal Stockholders quietly retain their Class B common with its 10 votes per share, the public minority will be systematically reducing its voting power. Eventually, according to plaintiff's figures, the point will be reached where the Principal Stockholders will come to possess more than 80% of the voting power of the corporation by simply sitting tight with their Class B common shares while the remaining holders of the Class B stock, as to whom it otherwise has no value, liquidate their holdings in favor of the transferability features of the New Common stock.

Plaintiff points out that while the Principal Stockholders at present can collectively prevent the 80% vote required for certain business combinations from being achieved, they do not at present have the power to approve a business combination by an 80% vote. Thus, he argues that it is evident from the manner in which the reclassification plan has been structured that it is designed to acquire 80% voting power for the defendant Principal Stockholders so as to place them in complete control of the fate of the corporation. In the process, he argues that the value of the present common stock to the minority will be reduced since, in effect, it is being cut in half in favor of a Class B stock that has no trading value. Thus, plaintiff would conclude that it is the purpose of the reclassification plan to entrench present management at the expense of the present minority and thus a wrong which should be enjoined at this preliminary injunction stage of the proceedings.

[1,2]Having thus analyzed the matter, I am persuaded that on the present record the plaintiff has failed to establish a basis for preliminary injunctive relief. As defendants point out, the most striking feature of plaintiff's case at present is that it is based upon speculation more so than upon fact. At best, his theory of managerial entrenchment is supported only by arguable inference from the facts set forth in the proxy statement.

[3]The complaint itself is unverified and is based upon the information and belief of counsel. The only affidavit filed in support of the application is that of New York counsel for the plaintiff and it goes only to verify the proxy materials and to set forth certain trading prices for the common stock of the corporation for the months of January and February. There is nothing offered other than the argument of counsel to support the contention that the present value of the corporation's stock will be reduced by the reclassification plan.

[4]Moreover, entrenchment being basically a matter of improper motivation in violation of a fiduciary duty, it is noteworthy that plaintiff has taken no discovery of any of the defendant directors as to their professed reasons for recommending the reclassification plan nor has he offered any documentary evidence other than the proxy statement from which an improper motivation on the part of some or all of the defendants might be inferred. Compare, *Crouse-Hinds Co. v. Internorth, Inc.*, 634 F.2d 690 (2nd Cir.1980).

In contrast to this, the Chairman of the Board of the corporation has offered his affidavit in which he disavows the entrenchment of management as being a motivation for the proposal and in which he outlines the reasons why the reclassification plan is being implemented as part of a long-term growth plan for the corporation. In short, without going into it, he asserts that there is a valid business purpose for the reclassification plan, and that it was and will be adopted by the defendants as being in the best interests of the corporation only after consultation with Goldman, Sachs & Co., the corporation's financial adviser.

In addition, as to plaintiff's argument that the plan has been spawned solely to permit the defendant Principal Stockholders to overcome the 80% supermajority requirement insofar as it pertains to approving certain business combinations, the defendants point out that at present the board of directors has the power to waive the requirement of a supermajority vote if it deems it in the best interests of the corporation. Plaintiff does not dispute this. Thus, since the defendant Principal Stockholders have the power now by their collective vote to remove—and thus control—the board of directors (a fact which

plaintiff also does not dispute) defendants suggest that it is somewhat ludicrous to attempt to infer an improper motivation to them when, in effect, they already have, collectively, the power which the plaintiff accuses them of attempting to wrongfully acquire through the reclassification plan.

Finally, I think it appropriate to note that this is not a situation in which the action is about to be approved by a single majority shareholder, or by members of a family who can be characterized as having the characteristics of a single majority shareholder. Rather, while there is a family connection between some of them, their number includes persons and a corporate entity who apparently are otherwise independent of each other except to the extent that they have agreed to pool their interests so as to constitute a majority voting position within the corporation.

[5]Accordingly, I cannot find on the strength of the present record that plaintiff has demonstrated either a probability of success on the merits upon a final hearing or that he and the other minority public shareholders are likely to suffer immediate irreparable harm in the event that a preliminary injunction is not granted. These being the requirements for the issuance of preliminary injunctive relief, *Gimbel v. Signal Companies, Inc.*, Del.Ch., 316 A.2d 509 (1974), *aff'd*, Del.Supr., 316 A.2d 619 (1974), it follows that the plaintiff's application for preliminary injunction must be denied.

IT IS SO ORDERED.

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## THOMAS v. DELAWARE ADOLESCENT PROGRAM, INC.

No. 684

*Court of Chancery of the State of Delaware, New Castle*

March 30, 1984

Plaintiff Thomas instituted this action asking that the court order the defendant, Delaware Adolescent Program, Inc. (DAPI), to specifically perform a "Transportation Agreement" with Thomas. Plaintiff also sought a preliminary injunction restraining both DAPI and defendant, James Young, from performing a contract which

allegedly tortiously interfered with the "Transportation Agreement" between Thomas and DAPI. In response to this complaint, both defendants filed a motion to dismiss for failure to state a cause of action. Subsequent to substantial discovery proceedings, defendants asked that the court treat their motion to dismiss as a motion for summary judgment.

The court of chancery, per Vice-Chancellor Longobardi, granted summary judgment to defendant DAPI while holding that plaintiff's employment with DAPI was terminable at will by either party, and, as such, DAPI's determination not to renew plaintiff's contract for another year because of budgetary restraints was a legally valid decision. The court also granted summary judgment to defendant Young because plaintiff failed to show a pre-existing contract covering the school year in question and also failed to establish the elements of tortious interference with the prospective contractual relation of another.

1. Judgment ⟹ 178, 181(2)

The function of a summary judgment is to provide an expeditious and economical termination of a lawsuit when there is no genuine issue as to any material fact.

2. Judgment ⟹ 181(2)

Summary judgment will not be granted if the pleadings, affidavits, and other proof raise a genuine issue as to any facts material to the dispute between the parties.

3. Judgment ⟹ 181(2)

To obtain summary judgment, movant must demonstrate to a reasonable certitude that there is no triable issue of material fact.

4. Statute of Frauds ⟹ 51

An oral contract to perform services for specified period exceeding one year violates the statute of frauds even though the contract may be terminated within one year. DEL. CODE ANN. tit. 6, § 2714 (1953).

5. Statute of Frauds ⟹ 115(1)

Even though an oral contract is reduced to writing, the statute of frauds requires that the writing be signed.

6. Estoppel ⟹ 56

An equitable estoppel arises whenever a party, by his voluntary conduct, has either deliberately or unconsciously led another party in reliance upon that conduct to change his position for the worse.

7. Estoppel ⟹ 90(2)

Whenever one party, relying upon conduct of another party, changes his position to his detriment, the person whose conduct has brought the situation about may not impeach the transaction.

8. Estoppel ⟹ 83(1)

Representation relied upon to operate as an estoppel must be of a nature to lead a man of prudence to take action.

9. Master and Servant ⟹ 8(1)

Whether a contract of employment is for a fixed or indefinite duration is a question of fact to be decided at trial.

10. Master and Servant ⟹ 8(1), 20

Hiring for an indefinite period of time is a hiring at will and is terminable at the will of either party. The burden of proving the contrary must be assumed by the party who asserts that the employee is engaged for a definite period.

11. Master and Servant ⟹ 30(1)

In a situation involving an employment contract of indefinite duration, an employer's determination not to renew an employee's contract for another year because of budgetary restraints is a legally valid decision.

12. Master and Servant ⟹ 30(1)

In determining whether an employment relationship is terminable at will, it is inconsequential whether the relationship is classified as one of employer-employee or as one of employer-independent contractor.

13. Torts ⟹ 26(2)

The factors to be considered in determining whether a valid action exists for tortious interference with a prospective contractual relation are:

(a) whether there is active competition between the parties;

(b) whether any wrongful means are used;

(c) whether an unlawful restraint of trade is created or continued; and

(d) whether there is, at least in part, a purpose to advance a competitive interest.

14. Torts ⟹ 26(2)

Where a competitor employed no unlawful means and simply offered a lower price, no action for tortious interference with a prospective contractual relation exists.

J. Jay Lazzeri, Esquire, of Brown, Shiels & Chasanov, Dover, Delaware, for plaintiff.

William D. Fletcher, Jr., Esquire, and Harold Schmittinger, Esquire, of Schmittinger and Rodriguez, Dover, Delaware, for defendants.

LONGOBARDI, *Vice-Chancellor*

The Plaintiff, Solomon Thomas, instituted this action requesting this Court to order the Defendant, Delaware Adolescent Program, Incorporated ("DAPI"), to specifically perform a "Transportation Agreement" with Thomas. Additionally, Thomas seeks a preliminary injunction restraining both DAPI and Defendant, James Young, from performing their contract which allegedly tortiously interferes with the "Transportation Agreement" between Thomas and DAPI.

In response to this complaint, both Defendants filed a motion to dismiss for failure to state a cause of action. Because there has since been substantial discovery, the Defendants now request the Court to treat their motion to dismiss as a motion for summary judgment.

DAPI, among other things, provides transportation for pregnant teenage girls to and from locations where they receive education and medical services. For at least ten years prior to the institution of the suit, Thomas provided various transportation services for DAPI. During that period, Thomas was employed by DAPI as a bus driver for New Castle and/or Kent Counties and, at certain times, as a transportation supervisor responsible for overseeing the statewide transportation needs of DAPI. He also owned three vehicles which he provided to DAPI for transportation. Two of the vehicles were used in Kent County and one was used in New Castle County.

The business relationship between Thomas and DAPI was always based on an oral agreement with the exception of one document signed by Mr. Thomas on December 1, 1978. The complaint is not based on that document in any way. During July of 1979, it is alleged that the parties were desirous of establishing a more formal relationship and, in furtherance of that objective, drafted a "Transportation Agreement" setting forth the duties and responsibilities of the parties for the next two years. Thomas states that he prepared the document and Lulu Mae Nix, a director of DAPI, typed it. It is admitted by all

involved that the document was never executed by the parties. Furthermore, Thomas testified that he had no intention of binding himself to the contract until it was signed by DAPI. The unexecuted "Transportation Agreement" provided for services through the 1979-1980 school year. DAPI paid Thomas for his services until DAPI decided not to hire Thomas for the 1980-1981 school year.

Plaintiff now argues that at some time during the 1979-1980 period, he was informed by a Mr. Hill of DAPI that the Sussex County Center was going to be split and, as a result, there would be two centers serving the Sussex County area. Thomas alleges that in reliance upon this statement and the long-standing relationship between the parties, and in accord with a provision in the unexecuted "Transportation Agreement" requiring him to maintain adequate rolling stock, he purchased at some time during that school year three vehicles at a cost of $34,000.00.

DAPI, on the other hand, says its decision to terminate Thomas' services was economically justifiable and perfectly legal. Apparently, due to budgetary restraints stemming from a lower grant from the General Assembly, DAPI claims it was no longer able to afford Thomas' services which amounted to more than $60,000 in the 1979-1980 school year. The record shows the organization only budgeting $25,000 for transportation services, apparently for the entire state, and so informed the Plaintiff in July of 1980. Thomas allegedly then advised DAPI that he could not agree to provide services for $25,000.

Thereafter, DAPI contacted Mr. Young, the other Defendant. He agreed to provide services during the 1980-1981 school year for Kent County for the amount of $25,200. Mr. Thomas also submitted a bid on July 21, 1980, but according to the minutes of the DAPI Board, his bid "was not within the range that the Board could consider." Part of the difference in the asking price between Thomas and Young was that Young did not include the cost of duties as transportation supervisor for Sussex County. Thomas had been paid around $14,000 for that title in the past. Nevertheless, the Board was aware that Thomas charged $31,860 for Kent County in 1979-1980. After studying the cost that Thomas charged for Kent County and Young's proposal to do the work for $25,200, DAPI chose Young.

[1-3]The function of summary judgment is to provide an expeditious and economical termination of a lawsuit when there is no genuine issue as to any material fact. *H. and S. Manufacturing Co. v. Benjamine F. Rich Co.*, Del.Ch., 164 A.2d 447 (1960). Summary judgment will not be granted, however, if the pleadings, affidavits and other proof raise a genuine issue as to any facts material to the dispute

between the parties. *Nash v. Connell*, Del.Ch., 99 A.2d 242 (1953). Procedurally, the moving party bears the burden of showing to a reasonable certitude that no such disputes are present. *Moore v. Sizemore*, Del.Supr., 405 A.2d 679 (1979); *Adams v. Kline*, Del.Super., 239 A.2d 230 (1968).

The Plaintiff, of course, argues that the Defendants have not met their burden. He feels that the "Transportation Agreement" of July, 1979, should be specifically enforced even though it was never signed. Plaintiff states unequivocally that it was a "valid oral contract for the definite term of two years." Plaintiff's Answering Brief, page 4. It is further argued that the Statute of Frauds does not preclude specific performance because of a judicially created exception, namely, equitable estoppel. In furtherance of that argument, Thomas asserts that he justifiably relied upon DAPI's misleading conduct. An injustice would result, he claims, if DAPI were not made to follow the terms and conditions of the "Transportation Agreement." Specifically, he points to the unexecuted contract which was prepared, at least in part, upon request of the Defendant. Further, he directs the Court's attention to statements made by Hill to Thomas during their trip to Sussex County (discussed *infra*) and finally, he refers to the long-standing relationship that existed between the parties.

The Defendants argue that neither party is bound by the document because neither signed it and Delaware's Statute of Frauds, 6 *Del.C.* §2714 prohibits the enforcement of an unwritten contract if performance cannot be accomplished within one year. Moreover, the Defendants argue that equitable estoppel is not applicable in this case because there is no basis for it in the record. Without a basis for consideration of the issue, the Defendants contend there can be no factual disputes.

It is undisputed that the "Transportation Agreement" was never formally executed by the parties and there is ample uncontroverted evidence in the record which establishes that there was no oral contract between the parties. Conversely, there is no legal basis in the present record upon which parties might disagree about the existence of an oral contract. Neither side manifested an intent to be bound to a two year contract in July, 1979, or anytime thereafter. In fact, the Plaintiff, the proponent of the alleged oral contract, stated at his deposition at pages 32 and 33:

Q. And why did you not sign it?

A. I did not sign this until I signed it in front of Mr. Hill.

Q. I think he is working up to it. Go ahead.

A. So, this one had not been signed by DAPI and I saw no reason to sign it until DAPI signed it.

Q. Fair enough. In other words, *you did not want to be bound by it until you knew DAPI was going to be bound by it?*

A. *Well, yes.*

(Emphasis added.)

[4,5]Even assuming arguendo that there was an oral contract for two years, the contract would otherwise fail because the Statute of Frauds, 6 *Del.C.* §2714,[1] prohibits its enforcement. An oral contract to perform services for a specified period exceeding one year violates the Statute of Frauds even though the contract may be terminated within one year. *Guyer v. Haveg Corporation*, Del.Super., 205 A.2d 176 (1964), *aff'd*, Del.Supr., 211 A.2d 910 (1965). Even though an oral contract is reduced to writing, the statute clearly requires that the writing must be signed. *Acierno v. McCall*, Del.Supr., 264 A.2d 513 (1970).

[6-8]The Plaintiff alternatively pleads equitable estoppel. He claims he bought three vehicles in reliance on Defendant's conduct. In Delaware, an equitable estoppel arises whenever a party, by his voluntary conduct, has either deliberately or unconsciously led another party

1. 2714. Necessity of writing for contracts; definition of writing; evidence.

(a) No action shall be brought to charge any person upon any agreement made upon consideration of marriage, or upon any contract or sale of lands, tenements, or hereditaments, or any interest in or concerning them, or upon any agreement that is not to be performed within the space of one year from the making thereof, or to charge any person to answer for the debt, default, or miscarriage, of another, in any sum of the value of $25 and upwards, unless the contract is reduced to writing, or some memorandum, or notes thereof, are signed by the party to be charged therewith, or some other person thereunto by him lawfully authorized in writing; except for goods, wares and merchandise, sold and delivered, and other matters which are properly chargeable in an account, in which case the oath or affirmation of the plaintiff, together with a book regularly and fairly kept, shall be allowed to be given in evidence in order to charge the defendant with the sums therein contained.

(b) For the purposes of this section, "writing" includes microphotography, photography and photostating, and a microphotographic, photographic or photostatic copy of any agreement covered by this section. Such copy or copies having been regularly made and kept in the course of business shall be equally competent as evidence as the original of such agreement, where the original is inaccessible or has been destroyed or otherwise disposed of in good faith in the regular course of business and where the mode of making such microphotograph, photograph or photostat was such as to justify its admission as a true copy of the original.

in reliance upon that conduct to change his position for the worse. *Wolf v. Globe Liquor Co.*, Del.Supr., 103A.2d 774 (1954); *Jones v. Savin*, Del.Super., 96 A. 756 (1916); *Marvel v. Ortlip*, 3 Del.Ch. 9 (1866). Whenever the other party, relying upon that conduct, changes his position to his detriment, the person whose conduct has brought the situation about may not impeach the transaction. *Marvel v. Ortlip, supra.* Moreover, "the representation, in order to work an estoppel, must be of a nature to lead naturally, i.e., to lead a man of prudence to the action taken." *Colvocoresses v. W. S. Wasserman Co.*, Del.Super., 190A. 607, 613 (1937).

Plaintiff's argument is that he was induced into buying the vehicles because of statements made by Hill to Thomas during a trip to Sussex County. Concerning those statements, Thomas testified as follows:

> Q. What specifically were you relying upon for you to purchase the vehicles you have identified in this paragraph?
>
> A. Well, I was told that they—
>
> Q. Before you go any further, who were you told by?
>
> A. Mr. Hill.
>
> Q. When were you told this?
>
> A. On a trip. I can't recall the date that we went down to Lewes and on the way back, he said that he was going to have to move out of Lewes and he was going to move up to the Racetrack in Georgetown. And that he was going to split the centers by putting one over in Laurel or Seaford, so there would have been two centers in Sussex County. That was the reason for purchasing the vans and stationwagon.
>
> Q. The statement or the contention of the statement you have just stated is the full basis for you going out and purchasing these things?
>
> A. Yes.
>
> Q. No other statements were made to you by DAPI?
>
> A. No, no other statements.

Deposition of Solomon Thomas, p. 37.

I fail to see how DAPI misled Thomas by that statement and thereby induced him to reasonably rely on it to the extent of buying three vehicles. Although the Plaintiff supervised operations in Sussex County since 1977, the evidence indicates that the Plaintiff never provided vehicles for Sussex County.[2] The statement made by Hill simply indicates that the Sussex County centers were going to be split. Nothing was said about using three vehicles in Sussex County. Thus, neither the statement nor the longstanding relationship between the parties provides a basis for invoking the equitable estoppel doctrine and this decision necessarily precludes any factual debate about whether the reliance was reasonable.

The Plaintiff also claims that the Court should look at the unexecuted "Transportation Agreement" as a basis for equitable estoppel. I find no merit in this argument. The Plaintiff clearly indicated he did not want to be bound by the document. It seems obvious that he should not expect DAPI to be bound by it. Moreover, the unexecuted document in no way implies that Thomas would be required to provide vehicles for the Sussex County operations.

[9-11]In support of their decision to terminate Thomas' services, the Defendants argue that his employment relationship was terminable at will. The Plaintiff, in opposition, cites the basic proposition that whether a contract of employment is for a fixed or indefinite duration is question of fact to be decided at trial. See 53 Am.Jur.2d *Master and Servant* §27 (1970). I agree that this is sound law when there is genuine factural dispute; however, in this case, it is clear that there is no fixed period of duration. It is the rule in Delaware that hiring for an indeterminable period is a hiring at will and is terminable at the will of either party. *Heideck v. Kent General Hosp., Inc.*, Del.Supr., 446 A.2d 1095 (1982); *Haney v. Laub*, Del.Super., 312 A.2d 330 (1973). In other words, ". . . contracts of employment which mention no period of duration, which are in a true sense indefinite and without stipulation for an implied minimum period, are terminable at the will of either party; and the burden of proving the contrary must be assumed by the party who asserts that the employee is engaged for a definite period." 53 Am.Jr.2d *Master and Servant* §27 (1970). It is clear that the duration of Thomas' employment with DAPI was terminable at the will of either party. Thus, DAPI's determination not to renew

2. Thomas testified that "Susex owns their own buses." Deposition of Solomon Thomas, p. 4.

Thomas for another year based on budgetary restraints was a legally valid decision.

[12]In his brief, the Plaintiff also disputes Defendant's categorization of Thomas' status as an employee terminable at will. He claims he was an independent contractor for DAPI and he offers evidence to support that proposition. Certainly, there is evidence that might support such finding, such as a reference in the "Transportation Agreement" to Mr. Thomas as an independent contractor. It is inconsequential, though, whether Thomas was an independent contractor or an employee of DAPI. As indicated above, his employment relationship with DAPI as still terminable at will.

For the reasons set out above, Defendant DAPI is granted summary judgment.

The Defendants also seek summary judgment in favor of James Young. It is alleged that Defendant Young entered into a contract with DAPI knowing that DAPI and Thomas had a pre-existing contract and thereby tortiously interferred with the contractual relation between the Plaintiff and DAPI. As noted above, the Court has found that there was not a pre-existing contract between the Plaintiff and DAPI for the 1980-1981 school year. (The record indicates that Young was contacted after the parties failed to reach an agreement in July of 1980.)

[13]What remains of this theory is the kind of tortious interference described in the *Restatement of Torts Second* §768 (1979); that is, tortious interference with a prospective contractual relation by a competitor. Under this doctrine, the factors to be considered are:

> (1) One who intentionally causes a third person not to enter into a prospective contractual relation with another who is his competitor or not to continue an existing contract terminable at will does not interfere improperly with the other's relation if
>
> (a) the relation concerns a matter involved in the competition between the actor and the other and
>
> (b) the actor does not employ wrongful means and
>
> (c) his action does not create or continue an unlawful restraint of trade and
>
> (d) his purpose is at least in part to advance his interest in competing with the other.

(2) The fact that one is a competitor of another for the business of a third person does not prevent his causing a breach of an existing contract with the other from being an improper interference if the contract is not terminable at will.

[14]Under the circumstances of this case, the Court has no difficulty in determining that no factual dispute exists with regard to this issue. As a matter of fact, there is no factual dispute that the doctrine itself is not applicable in this situation. Young did not employ wrongful means. He was simply a competitor who offered a lower price. The record shows nothing more. In fact, the record even indicates that DAPI sought out Young after deciding it could not meet the proposed charges.

Thus, because the Plaintiff has failed to show this Court any preexisting contract covering the school year in question and because Plaintiff has failed to meet the elements of tortious interference with a prospective contractual relation of another, Defendant James Young is hereby granted a summary judgment.

IT IS SO ORDERED.

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## WESLEY COLLEGE, INC. v. GIRARD BANK DELAWARE

No. 822

*Court of Chancery of the State of Delaware, Kent*

January 20, 1984

Wesley College applied for a temporary restraining order to compel defendant, Girard Bank, to return securities which were the issue of the suit. The court of chancery, per Vice-Chancellor Hartnett, denied the request because the college had not carried its burden of showing that no irreparable harm would result from granting the temporary restraining order. In addition, the court set forth that a temporary restraining order is to be used to preserve the status quo, which would not be the result if the order were granted. Thus, the bank was permitted to mount a defense before being deprived of the securities.

1. Injunction ⟹ 133

Plaintiff's request for a mandatory injunction places a great burden on it, especially at the temporary restraining order stage. Plaintiff must show that upon granting the temporary restraining order no irreparable harm will occur before a hearing can be held.

2. Injunction ⟹ 150

A temporary restraining order is granted only to maintain the status quo.

3. Injunction ⟹ 133,150

A request for an injunction requiring defendant bank to turn over to plaintiff securities at issue does not maintain the status quo.

4. Injunction ⟹ 150

The defendant must have an opportunity to present a defense before the court will grant a mandatory injunction which upsets the status quo.

George H. Jones, Esquire, Carol P. Braverman, Esquire, of Twilley, Jones & Feliceangeli, Dover, Delaware, for plaintiff.

Richard H. May, Esquire, of Young, Conaway, Stargatt & Taylor, Wilmington, Delaware, for defendant.

HARTNETT, *Vice-Chancellor*

Plaintiff filed a complaint seeking to compel defendants to return to plaintiff certain stocks and bonds pledged to defendant Girard Bank Delaware ("Girard") in 1975 as security for a loan. Plaintiff urges that the loan for which the stocks and bonds were pledged has been paid and it is entitled to a return of the securities. Despite its effort to couch its request for relief as a request to prevent defendants from taking certain action, what it really seeks is the affirmative relief of a mandatory injunction compelling the return of the securities.

Girard maintains that while the 1975 loan has been paid, the securities are still pledged to Girard as partial security for a later loan from Girard to the plaintiff. It urges that the 1975 Note securing the 1975 loan provided that the securities pledged remained pledged for any future loans despite the fact that on August 16, 1983, Girard marked the Note as being "cancelled" and returned it to the plaintiff. Girard has never returned the securities.

The plaintiff, on June 30, 1983, borrowed money from another bank and granted that bank a first security interest in the securities.

That bank is now insisting that the plaintiff procure the securities from Girard and deliver them to it. In the absence of the securities the second bank threatens to call the loan which may result, claims the plaintiff, in its demise as a college, thus working immediate and irreparable harm.

Plaintiff, while it notified Girard of its request for a temporary restraining order the afternoon before the 11:30 a.m. hearing on January 18, 1984, did not so notify the other defendants.

[1][2][3][4]Plaintiff's request for a mandatory injunction places a great burden on it. The burden is especially great at the temporary restraining order stage. A temporary restraining order is granted only to maintain the true status quo in order to prevent immediate and irreparable harm. The true status quo here is that Girard has possession of the securities. In addition, I am not convinced that any irreparable harm will occur before a hearing on a preliminary injunction can be held at which time the individual defendants will have an opportunity to defend themselves and Girard will have the opportunity to mount its defenses. If plaintiff were to be granted its prayer at the present time it would receive all the relief that it can ultimately be entitled to in this action and it might be impossible to restore the true status quo if defendants prove to be correct.

The application for a temporary restraining order is therefore denied.

IT IS SO ORDERED.