ployers to claim deductions for their contributions, they must first qualify under section 401 of the Internal Revenue Code of 1954, and all "qualified" plans are exempt from registration.[67]

The exact meaning of the Daniel court's assertion that ERISA was designed to "*complement* the securities laws" is uncertain to this writer. However, the court did state that ERISA is concerned with "ongoing administration of pension funds" in order to protect the interest of its participants, while the purpose of the federal securities laws is directed at the "prevention of fraud in the sale or acquisition of that interest."[68] The power to compel disclosure under the anti-fraud provisions[69] does place a greater burden of accountability on the trustees than ERISA's provisions,[70] concerning matters of material facts needed to make an informed investment.

Edward J. Schwabenland

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67. *See* Student Symposium, *supra* note 5, at 202–05. There the author advocates that exemptions from registration under the Securities laws be denied to pension funds in order to increase and improve the disclosure requirements and their effectiveness. However, this article had been written while the Welfare and Pension Plans Disclosure Act was in effect. Under ERISA, which has corrected many of the weaknesses of the previous act, such advocacy is unnecessary.

68. *Supra* note 51, at 99,293.

69. *Supra* note 4.

70. 29 U.S.C. § 1132 (1974) (Civil Enforcement); 29 U.S.C. § 1109 (1974) (Liability for Breach of Fiduciary Duty).

Unreported Cases

INTRODUCTION

UNREPORTED CASES will be a continuing feature of THE DELAWARE JOURNAL OF CORPORATE LAW. Significant unreported cases that have not been published by a reporter system will be included. The courts' opinions are printed in their entirety.

To expedite the attorney's research, all cases are headnoted according to the NATIONAL REPORTER key number classification system.* Cumulative indices are provided for case names, statutes construed, rules of court, and key numbers and classifications.

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TANZER, ET AL v. INTERNATIONAL GENERAL INDUSTRIES, INC., ET AL

No. 4945

Court of Chancery of the State of Delaware, New Castle

December 23, 1975

Plaintiffs seek a preliminary injunction to prevent a merger. Under the merger, minority holders of common stock in the subsidiary corporation will receive a cash payment thereby eliminating them as stockholders. The majority of minority shareholders have approved the merger.

The court denied the application for an injunction and held that there is no automatic rule of law that a merger cannot occur if its purpose is to serve the interests of a majority shareholder, and the subsidiary's public shareholders are not entitled to receive a premium payment above the fair value of the stock merely because the parent gained a special benefit.

1. Corporations ⇐ 584

Evidence was insufficient to establish under any legal test of fairness a requirement that the subsidiary's public stockholders were entitled to receive a premium payment above the fair value of the stock for the special benefit gained by the parent such as increased borrowing potential and improved cash flow.

2. Corporations ⇐ 581

There is no automatic rule of law that a merger cannot occur if its purpose is to serve the interest of a majority shareholder.

3. Corporations ⇐ 584

There may be legitimate interests of subsidiary corporations and minority shareholders which can outweigh even the fairest price.

QUILLEN, *Chancellor*

IGI owns 81% of Kliklok and 100% of KLK. The plaintiffs, owners of 50 shares of Kliklok common stock, seek a preliminary injunction to prevent the effectuation of a merger of KLK into Kliklok. Under the terms of the merger, IGI will become the sole stockholder of Kliklok and minority holders of common stock of Kliklok will receive a cash payment of $11 per share. Statutory appraisal rights are available to the minority shareholders who dissent.

The merger has been approved by the shareholders of Kliklok. There are 313,377 minority shares of common and 184,284 of such shares were represented at the meeting. Of those voting, 158,305 common shares

were voted in favor of the merger and 19,860 were voted against the merger. Thus, over 50% of the total minority common shares have indicated approval of the merger and, of the shares voted, almost 90% have indicated approval. The record does not disclose any information as to ownership of the minority shares.

The principal reason for the merger, and evidently the only reason for the merger, is to facilitate future long term debt financing by IGI. Insofar as the issues in this case are concerned, there are no disclosure problems resulting from the proxy statement.

A peripheral point in the plaintiffs' argument has been directed to the fairness of the price. Under the facts of this case, I think price should be noted prominently in this opinion. I do not believe the record supports a reasonable probability of success to a plaintiff who attacks this transaction because the price is unfair, even given the ownership of Kliklok by IGI and granting an intrinsic fairness test of responsibility and giving the plaintiff the benefit of careful scrutiny by the Court at the preliminary injunction stage.

The question presented is whether the merger should be enjoined because the purpose is to serve the interest of the parent. It should be noted in this regard that IGI has a legitimate and present and compelling business reason to be the sole owner of Kliklok. IGI is not freezing out the minority just for the purpose of freezing out the minority.

It is difficult in this day not to be mindful of the manipulation potential in any situation where a majority shareholder is eliminating a minority. But the statute does not prohibit a majority shareholder from serving an interest of its own. Nor do the plaintiffs cite any case which require a merger to be enjoined solely because it is serving the interest of a parent corporation. It has to be done with fairness to the minority. But, if there is fairness to the minority and no outside interest affected, it is not necessary to view the interests of an eighty per cent corporate owner and the corporation as totally divergent. The plaintiffs' case does not rest on any independent corporate interest of Kliklok. The fact that Kliklok will pay the interest on a loan used to purchase the minority shares when IGI is the sole owner does not inject a detriment to its corporate purpose.

[1] The situation presented here is one of shareholder economics. The interest of the plaintiffs is their economic interests. The real question raised by the plaintiffs is whether there must be recompense flowing to the subsidiary's public stockholders for the special benefit gained by the parent such as increased borrowing potential and improved cash flow. It is certainly possible to make an argument for a premium payment above the fair value of the stock. Private contracts frequently reflect such premiums. But no case has been cited in the statutory corporate merger context which requires such a payment under any legal test of fairness.

Over fifty per cent of the common stock held by the minority has been voted for a merger plan which will pay the minority shareholders a price

which is higher than the stock exchange price has been since 1972. Dissenters have a statutory appraisal right. The price was fixed through the services of an outside expert investment banking firm. The plaintiffs have presented no evidence as to the fairness of price.

[2] There is no equitable reason why the merger should be enjoined. Nor is there any automatic rule of law that a merger cannot occur if its purpose is to serve the interests of a majority shareholder. There is not present here any legitimate conflicting interest. The instant merger, judged by the present record, is fair and, in this context, I do not find the plaintiffs have a reasonable probability of success to enjoin this merger. I therefore deny the application for a preliminary injunction.

[3] I emphasize that this case arose in a limited factual context. Other cases will have different economic realities or other influential factors. There may be legitimate interests of subsidiary corporations and minority shareholders which can outweigh even the fairest price. But I do not find such interests present here.

SCIENCE ACCESSORIES CORP. v. AMERICAN RESEARCH & DEVELOPMENT

A DIVISION OF TEXTRON, INC., SUMMAGRAPHICS CORP., ET AL.

No. 4342

Court of Chancery of the State of Delaware, New Castle

June 6, 1975

Plaintiff, Science Accessories Corporation, brings a renewed motion for preliminary injunction against defendants, (1) barring them from soliciting or accepting orders from any of plaintiff's remaining customers and (2) altering the status quo as regards defendant Summagraphics' stock ownership or its basic assets. Plaintiff contended that an increased threat of irreparable injury existed because of a steady decline in plaintiff's business. The new evidence presented by plaintiff merely strengthens the showing of breach of fiduciary duty by employees but does not justify the relief sought.

1. Corporations ⇐ 314(1), 315

Evidence showing an employee's many unexplained absences from work, his alleged deceptions, his PXE notebook, and his long distance phone calls, merely strengthens the preliminary finding that this employee, and perhaps others, breached a fiduciary relationship as plaintiff's employees by participating in the organization of defendant corporation. But this breach of trust does not justify granting a preliminary injunction which is

largely directed against defendant corporation. Defendant corporation is not automatically the alter ego of the individual defendants.

2. Corporations ⟸ 308(3)

When defendant employee developed a breadboard which was patented alone by another individual, who received a relatively small equity in defendant corporation, plaintiff has failed to show that this product constitutes an "invention or discovery" within the meaning of the employee invention agreement.

3. Corporations ⟸ 313, 314(1)

An employee of plaintiff has a duty to attempt to obtain a discovery which he has developed for the plaintiff employer corporation. That duty is personal to the employee. Breach of that duty would not justify preliminary injunctive relief against defendant corporation.

QUILLEN, *Chancellor*

This case comes before the Court on a renewed motion for preliminary injunction and motion to amend the complaint filed by Science Accessories Corp. (SAC), a motion to strike filed by Summagraphics, and cross-motions to compel discovery filed by SAC and Summagraphics. The letter will deal solely with the first application.

Plaintiff, claiming to have new evidence enhancing the probability of ultimate success, seeks a preliminary injunction barring defendants from (1) soliciting or accepting orders from any of plaintiff's remaining customers and (2) altering the status quo as regards Summagraphics' stock ownership or its basic assets. It says that an increased threat of irreparable injury exists because of a steady decline in plaintiff's business resulting from Summagraphics' competition.

After considering plaintiff's arguments, I conclude that the new evidence does not sufficiently enhance the probability of ultimate success to warrant granting the relief sought. As to irreparable injury, there has been no showing of a causal connection between Summagraphics' sales and the decline in plaintiff's business. In this regard, Summagraphics' averment that none of its major customers have been plaintiff's customers remains uncontradicted.

[1] A large part of the evidence plaintiff now presents (e.g., Whetstone's many unexplained absences from work, his alleged deceptions, his PXE notebook, long distance phone calls to First State Street Investments) merely strengthens the preliminary showing that Whetstone, and perhaps others breached a fiduciary relationship as plaintiff's employees by participating in the organization of Summagraphics. See *Craig v. Graphic Arts Studio, Inc. and Reproduction Center, Inc.*, Del. Ch., 166 A.2d 444 (1960). But their breach of trust does not justify the relief

sought here which is largely directed against Summagraphics. Summagraphics is not automatically the alter ego of the individual defendants.

[2] Plaintiff says that Whetstone's description of his development of the breadboard and the fact that Brenner received a relatively small equity interest in Summagraphics show that Whetstone primarily developed the device and that it constitutes an "invention or discovery" within the meaning of the Whetstone invention agreement, belonging to plaintiff as a matter of contract law. However, after weighing the Novak and Whetstone affidavits and the fact that Brenner alone obtained the patent for the digitizer, I conclude that plaintiff has not yet demonstrated the probability of success on this theory which is necessary for preliminary relief.

[3] Neither has there been a sufficient showing of success on corporate opportunity grounds. Plaintiff says that Whetstone has admitted that he never discussed with Brenner the possibility of plaintiff's marketing the device. Assuming that this admission sufficiently rebuts Whetstone's previous averment affirmed by Brenner that Brenner did not wish to deal with plaintiff, and that Whetstone had a duty to attempt to obtain the discovery for plaintiff, that duty was personal as an employee. Breach of that duty would not justify preliminary relief against Summagraphics.

Consequently, the motion for a preliminary injunction is denied.

ARTESIAN W. C. v. SMALLEYS D. V., INC., ET AL.

No. 4818

Court of Chancery of the State of Delaware, Sussex

July 1, 1975

Plaintiff Artesian Water Company seeks a temporary restraining order and ultimate declaratory relief against defendants, collective developers of a development known as "Taylortowne." It is alleged that plaintiffs agreed to install for defendants water lines and facilities for supply and distribution of water to three sections of "Taylortowne" in return for payment of the cost of installation of the water supply facilities and an exclusive right granted to plaintiff to maintain and operate its water lines through certain of defendants' roadways, easements and utility reservations. Plaintiff has a suit pending in Superior Court to recover the full debt allegedly owed. Because of this failure to pay, plaintiff has elected to terminate further supply of water to unoccupied structures. The water mains are being turned on again by someone other than plaintiff.

Temporary restraining order granted, commencing in ten days to allow defendants' to seek relief before the Public Service Commission.

1. Public Service Commission ⇐ 2, 6.7, 612

Since Public Service Commission has statutory authority to regulate termination of services and to prohibit discontinuance of service for nonpayment where there is a bona fide dispute as to the bill, a utility may not unilaterally terminate service to a consumer for nonpayment when a bona fide dispute exists as to either liability or the accuracy of the bill.

2. Public Service Commission ⇐ 2, 6.2

Where the utility has terminated or threatens to terminate service, the remedy of the customer is prompt application to the Commission for relief.

3. Public Service Commission ⇐ 2, 6

Under no circumstances, after a utility has turned off its water, has a customer the right to simply turn the utility's service back on himself so as to avoid the trouble of seeking an available administrative determination of the utility's right to turn it off in the first place.

BROWN, *Vice Chancellor*

Plaintiff Artesian Water Company ("Artesian") seeks a temporary restraining order and ultimate declaratory relief against the defendants, the collective developers of a development known as "Taylortowne." It is alleged that by various written agreements with the defendants Artesian agreed to install water mains, lines, conduits and other facilities for the supply and distribution of water to Section 1 of Taylortowne, and later to Section 2 and Section 3. It is further alleged that pursuant to the initial written agreement, defendant Smalleys, Dam Venture, Inc. granted to Artesian an exclusive right to construct, maintain and operate its water lines through certain of Smalleys' roadways, easements and utility reservations. The aforesaid agreements provided also that Artesian would be paid by defendants for the cost of installation of the water supply facilities.

Artesian asserts that it has billed the defendants in excess of $19,000 for such installation costs for which it has not been paid. Because of the continued failure to be paid, Artesian has elected to terminate any further supply of water to any structures of Taylortowne which are not presently occupied and furnished with water service, which it claims it has a right to do under its tariff, rules and regulations as approved by the Delaware Public Service Commission.

It now appears that as Artesian turns off its appropriate water valves to carry out its termination of service, someone, presumably on behalf of one or all of the defendants, proceeds to turn them back on. Artesian charges that this situation has a clear potential for physical violence, and is causing it immediate and irreparable harm by virtue of the defendants' forcibly obtaining unmetered and, therefore, unbillable water service at Artesian's expense and in violation of its legal right to curtail service to

those who refuse to pay their bills. It asks for immediate restraint pending further decision of the Court on the merits of the matter.

Defendants acknowledge their failure to pay, but state that it is due to their position that they do not owe the full sum of $19,000. They point out that the overall installation costs amounted to some $125,000, and that they have paid over $100,000 to date. They say that they have financing arrangements to cover the balance of the costs which can be drawn upon promptly. They dispute, however, that they owe the cost of all off-site installation since the off-site facilities were constructed by Artesian so as to also provide a portion of water lines which will serve a nearby development with which defendants have no connection.

Artesian has brought suit in the Superior Court to recover the full debt and defendants argue that they can offer their defenses there and that the matter can be resolved in the law court without the need for equitable intervention. They assert that they require pressure in the water lines in the area now under construction for construction related reasons, including plumbing inspections, and that absent this limited water service building progress will be seriously impaired while the debt action is being litigated. They argue that Artesian's attempt to curtail all water service amounts to nothing more than economic coercion designed to cause them to forego their defense to the debt action. They cite Artesian's refusal to put a meter on the disputed service lines so that defendants can pay for what they use pending the litigation as evidence of this intent.

It is clear that under Artesian's tariff regulations it has the right to discontinue water service when a bill for such service remains unpaid for 40 days. It is also clear under such regulations that no land owner or unauthorized person has a right to turn water on or off at any corporation stop or curb stop. Artesian further has approved authority to discontinue water service for nonpayment of any charge accruing under an application for service. Artesian charges that the defendants' obligation for the off-site installation costs, including the lines which will also go to serve the other area, is clearly set forth in the agreements, and that consequently Artesian is really being used by defendants to finance a portion of their development costs.

Thus, as I view it, the questions presented by Artesian's application here are twofold. First, as a regulated public utility, does it have a right to discontinue needed water service to developers in an area under construction for nonpayment of a disputed bill covering off-site installation of water lines where the controversy arises out of an interpretation of written construction agreements between the parties? Second, do the defendant users of the service have the right to utilize the self-help approach of turning the utility's water back on as they see fit as opposed to utilizing an appropriate legal remedy?

[1-2] Both questions appear to be covered by the obvious import of *Artesian Water Co. v. Cynwyd Club Apartments, Inc.*, Del. Sup., 297

A.2d 387 (1972). There it was pointed out that a utility may not unilaterally terminate service to a consumer for nonpayment where a bona fide dispute exists as to either liability or the accuracy of the bill. It was further held that the Public Service Commission has statutory authority to regulate such termination of services and to prohibit discontinuance of service for nonpayment where there is a bona fide dispute as to the bill. Furthermore, for the future guidance, the court stated as follows at 297 A.2d 390:

> "We add these additional policy considerations in support of the result reached here: As a matter of fairness and practicality, the public utility must be protected against arbitrary non-payment by consumers of bills as to which there is a pretended dispute, just as the consumer must be protected from arbitrary termination of service for nonpayment of bills as to which there is a bona fide dispute. The function of making a quick, initial screening of the bona fides of the dispute must rest somewhere; the Public Service Commission is the most appropriate tribunal for that screening. If, upon complaint to the Commission, a bona fide dispute is not made to appear, discontinuance of service may be permitted; otherwise not."

[3] It thus appears that in the scheme of things the Public Service Commission has initial regulatory authority over whether or not a utility has the right to terminate service for nonpayment of a disputed bill, and the standard is whether or not the reasons advanced for nonpayment amount to a bona fide dispute. It seems further contemplated that where the utility has terminated or threatens to terminate service, the remedy of the customer should be prompt application to the Commission for regulatory relief. Under no circumstances can I conceive at this point that a customer has the right to simply turn the utility's service back on himself so as to avoid the trouble of seeking an available administrative determination of the utility's right to turn it off in the first place.

Since the normal position of the parties is reversed in this case (i.e., the utility seeking a restraining order to prevent the defendants from helping themselves to the terminated service, with no effort by defendants to contest the utility's present right to terminate) it would appear that a little equity is called for so as to get the situation right-side-up.

Accordingly, subject to the condition that Artesian continues to leave its water valves open to the lines servicing defendants' property for a period of ten days from the date hereof, I will grant a temporary restraining order, to commence July 11, 1975 at 5:00 p.m., and to continue thereafter subject to the further order of the Court, enjoining the defendants and each of them, their agents, servants and employees from interfering in any way with Artesian's water lines, valves and other service facilities, such restraining order to be effective only upon Artesian giving bond, with surety, in the sum of $1,000. The delay of ten days in the effective date of the restraining order is to allow defendants an opportunity to seek relief in a proper manner before the Public Service Commission as contemplated by the Supreme Court in its aforementioned decision, and their failure to do

so within that time span will be accorded its logical weight hereafter. In the event of application to the Public Service Commission by either side, and any preliminary or final ruling made thereon, counsel are to advise the Court forthwith.

EAST COAST RESORTS, INC. v. ESTHER M. LYNCH, ET AL.

No. 553

Court of Chancery of the State of Delaware, Sussex

July 17, 1975

Plaintiff seeks damages for breach of a covenant not-to-compete and for interference with contractual relations, and applies for a preliminary injunction to prevent defendant, a former employee of plaintiff's real estate brokerage firm, from working as a rental agent for defendant firm. Defendant brings a motion to dismiss. The court held that the likelihood of plaintiff's ultimate success was not reasonably probable in light of the factual dispute concerning the manner in which the defendant terminated her employment with plaintiff. The court denied defendant's motion to dismiss on the grounds that plaintiff might be entitled to damages if it were shown that defendant real estate brokerage firm knowingly induced defendant rental agent to avoid her contract with plaintiff.

1. Contracts ⇦ 116 (2), 117 (2)

Restrictive covenants in employment contracts which restrain competition are enforceable if the restraint is reasonable with respect to time and area and is reasonably necessary for the protection of the employer.

2. Injunction ⇦ 63

Injunctive relief may be granted against a business competitor whose improper conduct induces an employee to breach previous business commitments.

3. Contracts ⇦ 215 (1)
Injunction ⇦ 61 (2)

Where there are sufficient facts to show that an employee subject to a covenant not-to-compete within a period of one year is terminated from his employment at the wish of his employer, the restrictive covenant not-to-compete is no longer effective.

4. Social Security ⇦ 361

Covered employment does not include services performed by an individual for an employer as a real estate agent or solicitor "if all such service

performed by such individual for such employer is performed for remuneration solely by way of commissions." 19 DEL. C. § 3302 (10) (H).

5. Injunction ⇐ 137 (4)

Preliminary injunctions will not issue unless complainant satisfies the court that there is reasonable probability of ultimate success, and improbability of success may arise from evidence of disputed questions of fact as well as questions of law.

BROWN, *Vice Chancellor*

This is a decision on the plaintiff's application for a preliminary injunction. The plaintiff, East Coast Resorts, Inc., is a real estate brokerage firm located and operating in the Bethany Beach area. The defendants are Esther M. Lynch, known within her profession as Sue Lynch, and her present employer, Crowley, Evans & McCaffrey, Inc. as well as Thomas R. Crowley and Richard McCaffrey individually.

The basis for the complaint is that the defendant Lynch is violating her former employment contract with the plaintiff and further that the other defendants knowingly induced her to do so for the purpose of gaining a business advantage over the plaintiff.

Plaintiff seeks a preliminary injunction against Sue Lynch to prevent her from working as a rental agent for the defendants or anyone else in the Bethany Beach — Ocean View area for a period of one year hereafter. In addition, plaintiff seeks an accounting and damages against the other defendants for all rentals for this calendar year procured by the defendants from or on behalf of persons who were formerly rental clients of the plaintiff.

Based upon the sworn complaint and affidavits, it appears that the defendant Lynch was hired by the plaintiff in 1973 and sent to real estate school at the plaintiff's expense to be trained for her employment. Her terms of employment were established in a letter sent to her by the plaintiff which she formally accepted. In consideration of the real estate school tuition and 30 days on-job training with the plaintiff after completion of such school, the defendant Lynch agreed to work for the plaintiff for a period of one year after the issuance to her of her real estate license. Thereafter the following critical language appears in the employment letter:

> "In the event you terminate your employment within one year prior to the issuance of your license your accounts with both companies will be charged for the tuition and salary advanced while you were attending school.
>
> "In addition, in consideration of the above, you will not work as a salesperson or real estate agent in the role of rental houses and/or lots or any other real property within the corporate limits of Bethany Beach, Delaware or Ocean View, Delaware for one year after the date of termination of your employment with Resort Homes, Inc. and East Coast Resorts, Inc."

Ms. Lynch thereafter worked as a rental agent for the plaintiff during 1974 and, according to the term employed by the plaintiff, was placed in a position of "high visibility" in that her picture was displayed by plaintiff on its resort rental advertisements and circulated in the Washington, D. C. area as well as in lower Delaware. By October of 1974 the summer rental season had ended and work was slack. At this point, there is a dispute as to whether Ms. Lynch quit work for plaintiff voluntarily or involuntarily. Plaintiff says that she asked to be laid off because there was nothing for her to do with the understanding that she would resume her duties after the first of the year. But in any event, Ms. Lynch thereafter sought and was awarded unemployment compensation which would seem to indicate an involuntary termination.

Ms. Lynch says that as a condition of her receiving unemployment compensation she was required to seek other employment, which she did. As a result she was hired by the defendant Crowley, Evans & McCaffrey, a competitor of the plaintiff in the Bethany Beach area. Her new employer applied to the Delaware Real Estate Commission for a transfer of her sales license. Plaintiff would not cooperate in transferring her license but did not appear at a designated Commission meeting to protest such transfer. As a result the Commission, on February 6, 1974, approved the transfer of Ms. Lynch's license to Crowley, Evans & McCaffrey while pointing out that it was making no judgment on any contractual obligation she might owe to the plaintiff.

Ms. Lynch has since worked for Crowley, Evans & McCaffrey as rental agent in the same area. Now, in July, plaintiff brings this action to stop her, claiming that it is being injured because she is using the reputation developed by plaintiff as well as her knowledge of its customer list for the benefit of another, all of which is being done within a year of her termination with the plaintiff and, therefore, in violation of the covenant in her former employment contract.

[1–3] It seems without question that a restraint against competition contained in a restrictive covenant in an employment contract can be enforced provided that it is reasonable with respect to both time and area and is also reasonably necessary for the protection of the employer. *John Roane, Inc. v. Tweed,* Del. Supr., 89 A.2d 548 (1952). Also in a proper case, injunctive relief may lie against a competitor for improper conduct in inducing customers or employees to forsake previous business and employment commitments. Compare *Bowl-Mor Company, Inc. v. Brunswick Corporation,* Del. Ch., 297 A.2d 61 (1972). At the same time, it has also been held that where an employee subject to a covenant not to compete within a period of one year is terminated from his employment at the wish of his employer, the restrictive covenant not to compete is no longer of any effect. See *Stewart In-Fra-Red Commissary v. Conner,* Del. Ch., 205 A.2d 3 (1964).

Several factors militate against granting preliminary injunctive relief here. In the first place, the language in the employment letter which purports to impose the restriction against competition is subject to differing constructions. The first paragraph clearly refers to the obligations of Ms. Lynch if *she* terminated her employment within one year of receiving her license. The next paragraph commences with the words "[in] addition," and then goes on to restrict her right to work as a real estate salesperson and rental agent for a one-year period after termination. Thus, there is ample room for argument that the one-year restriction only applied if *she* broke off the employment relation within one year after receiving her license, but not if she was laid off by plaintiff or ceased to be an employee by mutual consent.

Secondly, although plaintiff was on notice in December 1974 that Ms. Lynch was seeking a transfer of her real estate license to a competitor, and aware that this was accomplished in February 1975, there is nothing in the present record to indicate that it thereafter gave either Ms. Lynch or Crowley, Evans & McCaffrey, Inc. notice of its intention to hold her to what it felt was her obligation under the employment contract. In fact, plaintiff has allowed Ms. Lynch to work for her new employer for some five months before now bringing this action in the midst of the peak summer rental season. Thus, even assuming that improper conduct by Ms. Lynch can be established, plaintiff has voluntarily permitted half of the period of protection to pass before attempting to assert its claimed rights.

In addition, the restraint sought against Crowley, Evans & McCaffrey is based on its alleged inducement to cause Ms. Lynch to breach her contract with plaintiff, and at this point this charge is based on information and belief.

[4] Finally, although not mentioned by counsel, I take note that by an amendment to the unemployment compensation statutes, effective May 27, 1974, covered employment does not include services performed by an individual for an employer as a real estate agent or solicitor "if all such service performed by such individual for such employer is performed for remuneration solely by way of commissions." 19 DEL. C. § 3302(10)(H). Ms. Lynch's agreement with plaintiff provided for no salary as such, but rather provided that she would receive a draw of $125 per week against commissions. Yet she apparently drew unemployment compensation which, assuming it was proper for her to do so, would indicate a deviation from the terms of the employment agreement on which plaintiff seeks to rely.

[5] A preliminary injunction will not issue unless the complainant satisfies the court that there is a reasonable probability of ultimate success, and the improbability of success may arise from evidence on disputed questions of fact as well as because of questions of law. *Allied Chemical & Dye Corporation v. Steel & Tube Co. of America,* Del. Ch., 122 A. 142 (1923). In view of the factual dispute concerning Ms. Lynch's severance from active employment in October 1974, considered in light of *Stewart In-Fra-Red*

Commissary v. Conner, supra, I am not satisfied that plaintiff has carried its burden here.

On the other hand, I do feel that the complaint contains sufficient allegations to withstand defendants' motion to dismiss for failure to state a claim. If plaintiff, on all the evidence, can establish that Crowley, Evans & McCaffrey did knowingly induce Ms. Lynch to take steps to avoid her contract with plaintiff, or perhaps assisted her in doing so, plaintiff may be entitled to such damages as it can prove. Compare *Wright v. Scotton,* Del. Supr., 121 A. 69 (1923).

Plaintiff's motion for a preliminary injunction is denied. Defendants' motion to dismiss the complaint for failure to state a claim is denied.

COUNCIL 81, AMERICAN FEDERATION OF STATE, COUNTY, AND MUNICIPAL EMPLOYEES, ET AL. v. STATE PERSONNEL COMMISSION, ET AL.

No. 4665

Court of Chancery of the State of Delaware, New Castle

July 30, 1975

Plaintiff brings a motion for summary judgment seeking a permanent injunction to compel the defendants to meet with plaintiffs after a public meeting but before rules are adopted by the commission. The court held that the defendants were not required under 29 DEL. C. § 5938(e) to meet with plaintiffs after a public meeting whose purpose was to discuss adoption of amendment of the rules. Under 29 DEL. C., § 5914, the public hearing is the culmination of the amendment process as prescribed by the statute.

1. Labor Relations ⇨ 177

Delaware statute requiring State Personnel Commission and Director to meet with the bargaining representative of public employees at reasonable times and to negotiate in good faith with respect to any adopted or amended rules does not require further meetings after the public hearing. 29 DEL. C. § 5914.

QUILLEN, *Chancellor*

The plaintiffs seek a declaratory judgment and permanent injunction that, with respect to rules to be adopted or amended, the Director and the Commission are required, if requested by Council 81, to meet and negotiate with Council 81, in addition to other times, after a public hearing but before the rules are adopted or amended. The defendants do not

believe it is their obligation to meet with Council 81 after the public hearing but before rules are adopted by the Commission.

As part of the statute intended to reconcile and make harmonious the law establishing the merit system and the law recognizing the right of public employees to organize, the General Assembly enacted 29 DEL. C., § 5938(e) which in pertinent part required "[t]he Director and the Commission [to] meet with the exclusive bargaining representative at reasonable times to negotiate in good faith with respect to any rule to be adopted or amended. . . ." The purpose of this statute was to require negotiation as to merit system rules to be negotiated at the Commission level. *Laborers' International Union of North America, Local 1029 v. The State of Delaware, Acting Through The Department of Health and Social Services, et al.*, Del. Ch., 310 A.2d 664 (1973).

The statute, at 29 *Del. C.*, § 5914, provides that rules proposed by the Director, as amended by the Commission, "shall become law upon completion of the public hearing" and further, that the Commission after a public hearing, "on its own motion, may establish, adopt and amend . . . rules."

I decline to declare that the Commission is required to meet with the exclusive bargaining representative after the public hearing. In my judgment, in a view I noted in declining the application for a preliminary injunction and in which I adhere to now after a full consideration of the case, the public hearing was, under the statute, meant to be the culmination of the amendment process under the law. This does not mean, of course, that the Director and the Commission can necessarily satisfy its duty to "meet at reasonable *times* to negotiate in good faith" by one session prior to the public hearing. But the statute contemplates that a public hearing shall be the last stage before action.

This indeed makes sense. It is the public that foots the bill and any special privilege given any group of employees, no matter how vital their status, should not rise above the rights of the public at large. It is no answer to say the Commission represents the public. We are not here dealing with delicate matters of personal privacy. We are dealing with public rules governing public employees. The public should have the right to scrutinize its representatives. There should here be no special privilege higher than that public right.

The plaintiffs' motion for summary judgment is denied.

DPF INCORPORATED v. INTERSTATE BRANDS CORPORATION

No. 4856

Court of Chancery of the State of Delaware, New Castle

October 2, 1975

In this "books and records" inspection case under 8 Del. C. § 220, plaintiff, record holder of over 30% of the defendant's stock, moves to strike from the defendant's answer certain affirmative defenses alleging unclean hands. In addition, plaintiff moves for judgment on the pleadings on the basis of the purposes stated in its demand for inspection.

The court held that since it was conceded that plaintiff was a stockholder of record and had owned shares prior to the disputes surrounding tender offer share acquisitions, and the victims of any fraud were not before the court with complaint, the unclean hands affirmative defenses were immaterial and insufficient as a matter of law and should be stricken insofar as the plaintiff's § 220 claim was concerned. However, since it appeared that plaintiff could already have access to all the information it was reasonably and fairly entitled to receive for the purpose of valuing its stockholding, and since the court refused to hold as a matter of law that the pendency of litigation elsewhere cannot constitute a defense to a "books and records" petition, plaintiff's motion for judgment on the pleadings on the basis of the purposes stated in its demand was denied.

1. Corporations ⇐ 181(8)

Affirmative defenses alleging unclean hands due to alleged illegal and inequitable scheme to gain absolute control of the corporation, acquisition of stock in violation of the Securities Act of 1934, acquisition of the stock in violation of the Investment Act of 1940, and acquisition of stock through a fraudulent tender offer were immaterial and insufficient as a matter of law and stricken insofar as the stockholder's § 220 claim was concerned since it was conceded that plaintiff was a stockholder of record and had owned shares prior to the disputes surrounding tender offer share acquisitions, and the victims of any fraud were not before the court with complaint, 8 DEL. C. § 220.

2. Corporations ⇐ 181(1)

By statute, a proper purpose for inspection of books and records means a purpose reasonably related to such person's interest as a stockholder. 8 Del. C. § 220(b).

3. Corporations ⇐ 181(8)

The burden, in a books and records case, is on the stockholder to establish that the inspection he seeks is for a proper purpose. 8 Del. C. § 220 (c).

4. Corporations ⇐ 181(1)

Stockholder's motion for judgment on the pleadings on the basis of the purpose stated in his demand for inspection of the corporation's books and records, stated purpose of which was to enable stockholder to value its stockholding in corporation, denied, since it appeared that stockholder could already have access to all the information it was reasonably and fairly entitled to receive for the purpose stated, and since stockholder was not entitled to engage in a general fishing expedition. 8 Del. C. § 220.

5. Corporations ⇐ 181(1)

Stockholder's motion for judgment on the pleadings on the basis of the purpose stated in its demand for inspection of the corporation's books and records, stated purpose of which was to enable stockholder to protect the value of its stockholding and to aid stockholder in its action against the corporation, denied, since the court refused to hold as a matter of law that the pendency of litigation elsewhere cannot constitute a defense to a "books and records" petition. 8 Del. C. § 220.

QUILLEN, *Chancellor*

This is a "books and records" inspection case under 8 *Del. C.*, § 220 by the record holder of over 30% of the defendant's stock. The matter comes before the Court on a motion to strike affirmative defenses.

[1] Certain affirmative defenses allege unclean hands due to: an alleged illegal and inequitable scheme to gain absolute control of the corporation; acquisition of stock in violation of the Securities Act of 1934; acquisition of the stock in violation of the Investment Act of 1940; and acquisition of stock through a fraudulent tender offer. Paragraphs 15–18 of Answer. Since it is conceded, however, that the plaintiff is a stockholder of record [8 *Del. C.*, § 220(a)], these affirmative defense allegations do not constitute a valid defense to § 220 portion of the complaint. *Kerkorian v. Western Air Lines, Inc.*, Del. Ch., 253 A.2d 221 (1969), aff'd *Western Air Lines, Inc. v. Kerkorian*, Del. Supr., 254 A.2d 240, 241–242 (1969); *General Time Corp. v. Talley Indus. Inc.*, Del. Supr., 240 A.2d 755, 756 (1968). Even the common law allegations fail because it is conceded that plaintiff owned 100 shares prior to the disputes surrounding tender offer share acquisitions and because the victims of any fraud are not before the Court with complaint. The unclean hands affirmative defenses, as they stand, appear to me to be immaterial and insufficient as a matter of law and should be stricken insofar as the § 220 claim is concerned. IT IS SO ORDERED.

[2–3] The question then becomes one of proper purpose. Under the statute, a proper purpose means "a purpose reasonably related to such person's interest as a stockholder." 8 *Del. C.*, § 220(b). The burden in a

books and records case is on the stockholder to establish that the inspection he seeks is for a proper purpose. 8 *Del. C.*, § 220(c). In the case it is averred in paragraph 6 of the answer and in the amendment to the answer that the purported purposes set forth in the demand are improper.

Initially, I am somewhat at a loss to deal with the issue of proper purpose on a motion to strike. The burden is on the plaintiff, and there is a denial in the answer that the purported purposes are proper. Therefore, the parties agreed that the Court could consider the matter as one involving a motion for judgment on the pleadings. The only record as to purpose is the demand itself. Notwithstanding the existence of affidavits of counsel in the record, I hesitate to consider the application as one for summary judgment because of the absence of notice and the possible desire of the parties to enlarge further upon the record. There are record problems in the case, but the briefs make some practical concessions which the Court will consider. But considering the motion as a motion for judgment on the pleadings does not solve all the problems when there is a general averment of improper purposes as appears in paragraph 6 of the answer here. But I will do the best I can given the somewhat confusing, at least to me, procedural context in which we are working.

Paragraph 6 of the demand by the plaintiff's Chairman of the Board and Chief Executive Officer reads as follows:

> "6. I, on behalf of DPF, which is a stockholder of record of Interstate, hereby demand, pursuant to Title 8, Delaware Code, Section 220, that DPF be afforded the right during usual business hours to inspect, and to make copies or extracts therefrom, the books and records of Interstate which consist of, record, summarize, reflect, report, or contain a reference to any of the following matters:
>
> > 'a. For each monthly and quarterly period during the fiscal years 1973, 1974, and 1975, and on both a production unit or profit center and a companywide basis, all Interstate statements of earnings, (including but not limited to statements of manufacturing expenses, administrative expenses, sales expenses and truck and transport costs and raw materials reports), balance sheets, budgets, cash flow statements and other reports on operations or financial conditions.
> >
> > 'b. Any budgets or projections of earnings of Interstate for the remainder of fiscal year 1975 and for any other periods for which such budgets or projections have been prepared.' "

However, as defendant argues, the stock is not only traded on the New York Stock Exchange; it is also registered with the Securities and Exchange Commission pursuant to Section 12 of the Securities Act of 1934, facts evidently not in dispute. The only purpose stated in paragraph 6 is "to enable DPF to value its stockholding in Interstate."

[4] In my judgment, on this motion as a matter of law, given the bare record in the case, the plaintiff could well already have access to all

the information that it is reasonably and fairly entitled to receive for the purpose stated. The plaintiff is not entitled to engage in a general fishing expedition. *Business Capital Corporation v. Interphoto Corporation,* Del. Ch., C. A. 3616, letter opinion by Vice Chancellor Marvel dated July 23, 1971. The plaintiff is not entitled to judgment on the pleadings on the basis of the purpose stated in paragraph 6 of the demand.

Paragraph 7 of the demand reads as follows:

> "7. Further, I, on behalf of DPF, which is a stockholder of record of Interstate, hereby demand, pursuant to Title 8, Delaware Code, Section 220, that DPF be afforded the right during usual business hours to inspect, and to make copies or extracts therefrom, the books and records of Interstate which consist of, record, summarize, reflect, report, or contain a reference to any of the following matters:
>
> 'a. For each monthly and quarterly period during the fiscal years 1973, 1974 and 1975, and on both a production unit or profit center and a companywide basis, all Interstate statements of earnings, (including but not limited to statements of manufacturing expenses, administrative expenses, sales expenses and truck and transport costs and raw materials reports), balance sheets, budgets, cash flow statements and other reports on operations or financial condition.
>
> 'b. Any budgets or projections of earnings of Interstate for the remainder of fiscal year 1975 and for any other periods for which such budgets or projections have been prepared.
>
> 'c. Contracts or agreements between Interstate and any of its officers or directors currently in force.
>
> 'd. Contracts, agreements, purchase orders or other commitments currently in force between Interstate and any of its suppliers, vendors or customers, if such contract, agreement, purchase order or other commitment is (i) of a total value in excess of $50,000 or (ii) has either no stated termination date or a stated termination date after December 31, 1975.
>
> 'e. Proceedings of Interstate's Board of Directors, any committee appointed by the Board of Directors, or any management committee on or after June 16, 1975, including any minutes of these proceedings.
>
> 'f. The trading of Interstate common stock on the N.Y.S.E. from June 16, 1975 through August 1, 1975, including any delays or suspensions in such trading or request for such delays or suspensions.
>
> 'g. Any proposed acquisition of, merger with, or investment in Farmbest or any other company by Interstate which has been considered by Interstate's Board of Directors or any officer or committee of Interstate at any time on or after June 16, 1975.'
>
> "The purposes for which the inspection requested in this paragraph 7 is sought are to enable DPF to protect the value of its stockholding in Interstate and to aid its Action against Interstate. As the largest stockholder of Interstate common stock DPF has a vital interest itself

> in informing itself of and evaluating the current management policies, operations and financial condition of Interstate. This is especially so in view of the activities of Interstate's management during the Offer, as stated in part in paragraph 4 above, which indicate that improper transactions have been and may still be under consideration which would dilute the value of DPF's stockholding and would waste the assets of Interstate in an attempt to perpetuate management's control of Interstate. The requested inspection also specifically relates to these alleged improper activities by management during the Offer, and thus is sought in aid of the Action which challenges those activities."

The purpose stated is "to protect the value of its stockholding in Interstate and to aid its Action against Interstate." The latter reference is to a pending suit by the plaintiff in the Southern District of New York. The defendant argues in essence it is improper to use § 220, books and records, as a substitute for normal discovery procedures in a lawsuit elsewhere. The plaintiff says that investigation of improper management conduct falls within the definition of a proper purpose [*Nodana Petroleum Corporation v. State ex rel. Brennan,* Del. Supr., 123 A.2d 243 (1956)] and the pendency of litigation elsewhere does not make the request improper [*Trans World Airlines v. State ex rel. Porterie,* Del. Supr., 183 A.2d 174 (1962); *State ex rel. Foster v. Standard Oil,* Del. Supr., 18 A.2d 235 (1941); *Sack v. Cadence Industries Corp.,* Del. Ch., C.A. 4747 (Letter Opinion of Vice Chancellor Brown dated April 9, 1975)].

But the cases cited do not necessarily support as a blanket proposition that litigation pending elsewhere is not pertinent on the issue of proper purpose. The *Trans World Airlines* case and the *Foster* case were both stock ledger cases. List cases are not always valid precedent for books and records cases. The considerations may be quite different. For example, compare: *E. L. Bruce Co. v. State ex rel. Gilbert,* Del. Supr., 144 A.2d 533 (1958) and *State ex rel. Armour & Co. v. Gulf Sulphur Co.,* Del. Supr., 233 A.2d 457 (1967), aff'd, Del. Supr., 231 A.2d 470 (1967). The *Sack* case involved books and records but it was brought by a shareholder who was not a party to the foreign litigation and had no means of discovery in that litigation.

Indeed, two of the cases expressly considered the litigation elsewhere. The Superior Court in the *Foster* opinion, in 1941, noted the power of the Court of Chancery to require inspection of books and records as an incident of the litigation there pending and also indicated that if "the allowance of the statutory right constituted in any manner an interference with the course of litigation in the Court of Chancery, the writ would be refused." 18 A.2d 238, 239. Vice Chancellor Brown at page 8 in the *Sack* case noted the same caveat.

[5] Thus, it is hard to say, as a matter of law, the pendency of litigation elsewhere cannot constitute a defense to a "books and records" petition. See also *Henshaw v. American Cement Corporation,* Del. Ch., 252 A.2d 125 (1969); *Holdsworth v. Goodell-Sanford, Inc.,* Me. Supr., 55

A.2d 130 (1947); *State ex rel. Linihan v. United Brokerage Co.*, Del. Supr., 101 A. 433 (1971). Nor can I say in this case that the demand in paragraph 7 is not essentially related to the New York litigation.

Consequently, as to both paragraphs 6 and 7 of the demand, the motion for judgment on the pleadings will be denied. IT IS SO ORDERED. I do note, however, that I agree with the plaintiff that disclosure per se would not violate Section 10(b) of the Securities Exchange Act. The burden of any misuse, of course, would fall on the plaintiff. *E. L. Bruce Co. v. State ex rel. Gilbert, supra; Credit Bureau of St. Paul v. Credit Bureau Reports,* Del. Ch., 290 A.2d 689 (1972) aff'd Del. Supr., 290 A.2d 691 (1972); *Schnell v. Chris-Craft Industries, Inc.*, Del. Ch., 283 A.2d 852 (1971).

TUCKMAN v. AEROSONIC CORPORATION, ET AL.

No. 4094

Court of Chancery of the State of Delaware, New Castle

October 21, 1975

Defendants, certified public accounting firms, bring a motion to dismiss the complaint against them on the basis of the three year statute of limitations. Instrument Technology Corporation purchased an interest in Aerosonic Corporation owned by the defendant Frank. This was followed by a merger of Aerosonic Corporation and Instrument Technology Corporation. Plaintiff alleges that defendants knowingly allowed financial statements (which failed to disclose certain facts) to be included in the proxy statement and negligently failed to disclose such facts in the financial statements. The court held that the statute does not apply to allegations of fraudulent self-dealing involving fiduciaries or outside experts who knowingly conspire with fiduciaries. However, the statute does apply to allegations of negligence.

Motion to dismiss based on negligence is granted. Motion to dismiss based on fraudulent concealment is denied.

1. Limitation of Actions ⇐ 5(2)
   Equity ⇐ 87(1)

Where the statute of limitations bars the legal remedy, it shall bar the equitable in analogous cases or in reference to the same subject matter, when legal and equitable claims so far correspond that the only difference is that one remedy may be enforced in a Court of Law and the other in a Court of Equity. A *fortiori,* where a legal claim is joined in an action in equity under the principle of complete relief, the statute should be applied.

2. Limitation of Actions ⟸ 99(1)

Under the *Bovay* rule, the statute of limitations is applied to derivative actions which seek recovery of damages or other essential legal relief but is not applied in cases involving allegations of fraudulent self-dealing when those seeking the benefit of the statute are officers and directors who profited personally from their misconduct.

3. Limitation of Actions ⟸ 99(1), 100(7)

If outside experts, on whom many must depend for the integrity of corporate affairs, knowingly conspire with self-dealing fiduciaries to defraud those very persons who in practicality would rely on their advice, the same trust principles of *Bovay* should apply for the statute of limitations.

4. Limitation of Actions ⟸ 55(3), 100(7)

Oral argument to the effect that filings with the SEC and accountants' certifications constitute fraudulent concealment cannot save a count from the statute of limitations when the count has simple negligence as its underlying basis.

QUILLEN, *Chancellor*

This letter constitutes the Court's opinion on the motion to dismiss by Laventhol, Krekstein, Horwath & Horwath and Horwath & Horwath to dismiss the complaint against them on the basis of the three year statute of limitations. 10 *Del. C.*, § 8106; *Patterson v. Vincent*, Del. Super., 61 A.2d 416 (1948). The only causes of action against the moving defendants are the fifth and sixth causes of action. The plaintiff was a stockholder of old Aerosonic Corporation (herein A. Corp.).

The case arises in the context of the purchase by Instrument Technology Corporation of the 18% interest of A. Corp. owned by the defendant Frank, followed by the merger of A. Corp. and Instrument Technology Corporation. The complaint must be viewed as it is written for the present motion. It is alleged that the Laventhol firm was the Certified Public Accountant for ITC during the relevant period and that the Horwath firm was Certified Public Accountant for A. Corp. for the fiscal period ending May 31, 1969.

The Fifth Cause of Action alleges both firms "knew that the Financial Statements included in the Proxy Statement failed adequately to disclose the facts as to the matters set forth in paragraph 28 and thus . . . participated in the conspiracy to defraud shareholders of A. Corp."

The Sixth Cause of Action alleges that the two firms "in the ordinary course of conducting an audit and preparing financial statements should have known of the matters set forth in paragraph 28, and were negligent in failing to disclose such in the Financial Statements in the Proxy Statement."

The only relief sought from these defendants is money damages.

The date of the challenged proxy solicitation material is December 16, 1969. The special meeting of shareholders which approved the merger was held on January 9, 1970. The merger itself was effectuated on January 12, 1970. The complaint in this action was filed on January 15, 1973, more than three years after the merger. It thus appears that the causes of action alleged accrued not later than January 12, 1970, the date of the merger, and, if the three year statute of limitations applies, the motion to dismiss is meritorious.

[1] There is no reason by the nature of the suit (individual, class, and derivative) that the three year statute of limitations cannot apply. *Bokat v. Getty Oil Co.,* Del. Supr., 262 A.2d 246 (1970). Moreover, it is an established rule that where the statute bars the legal remedy it shall bar the equitable in analogous cases or in reference to the same subject matter and when a legal and equitable claim so far corresponds that the only difference is that one remedy may be enforced in a Court of Law and the other in a Court of Equity. *Perkins v. Cartmell,* 4 Harr. 270, 274 (Del. Ch., 1845). In a *fortiori,* where a legal claim is joined in an action in equity under the principle of complete relief, the statute should be applied.

[2] As to the Sixth Cause of Action, the allegations merely state a claim for negligence. There is no reason why the normal limitations period should not apply in a negligence case. Thus the statute of limitations is applicable unless the plaintiff can prevail under the doctrine of fraudulent concealment discussed *infra.*

[3] As to the Fifth Cause of Action, the question is whether the rule in *Bovay v. H. M. Bullesby & Co.,* Del. Supr., 38 A.2d 808 (1944) applies. Chancellor Duffy recently dealt with the *Bovay* rule in *Halpern v. Barran,* Del. Ch., 313 A.2d 139, 142 (1973). He said:

> "The statute of limitations applies to derivative actions which seek recovery of damages or other essentially legal relief; however, in extraordinary cases which involve, as a minimum, allegations of fraudulent self-dealing, the benefit of the statute will be denied to those corporate officers and directors who profited personally from their misconduct."

Chancellor Duffy did not decide whether the rule in *Bovay* extends beyond officers and directors to others who exercise effective control of the corporation.

Assuming the *Bovay* rule can be routinely extended so far as to include Certified Public Accountants, a questionable proposition, it is not alleged that the moving defendants here were fiduciaries in this case. Nor is it alleged that there was self-dealing by the moving defendants. Accordingly, reliance on the *Bovay* exception appears at first blush to be misplaced.

[4] At oral argument, however, the plaintiff attempted to avoid these deficiencies by arguing that the accountants were fiduciaries or came within the *Bovay* exception because they conspired with fiduciaries [*Schleiff v. The Baltimore & Ohio Railroad Company,* Del. Ch., 130 A.2d 321, 332 (1955)]. The first argument fails on the pleadings, but the second has some merit. Indeed, in the Fifth Cause of Action, paragraph 38 does allege that these defendants "*knew* that the Financial Statements included in the Proxy Statement failed adequately to disclose the facts as to the matters set forth in paragraph 28, and thus defendants H & H, LKH & H . . . participated in the conspiracy to defraud shareholders of A Corp." The language would appear fairly to fit the argument that was made in the *Schleiff* case, given the other allegations of the complaint. The complaint does allege an abuse of a fiduciary duty resulting in personal profit. Thus, this case is distinguishable from the conclusions reached by the Court as to General Motors in the *Schleiff* case. The question then becomes one of policy. Should those who conspire to defraud with self-dealing fiduciaries be found by the same standard for statute of limitations purposes as the fiduciaries themselves? Compare *Jackson v. Smith,* 254 U.S. 586, 41 S. Ct. 200, 65 L. Ed. 418 (1921). The answer to the question is difficult in the relative vacuum of the bare pleadings. But, if outside experts, on whom many must depend for the integrity of corporate affairs, knowingly conspire with self-dealing fiduciaries to defraud those very persons who in practicality must rely on their advice, it is difficult to see why the same trust principles of *Bovay* should not apply for statute of limitations purposes.

Accordingly, as to the Fifth Cause of Action, I think the *Bovay* exception is applicable and the motion to dismiss on the bare plea of the Statute of Limitations should be denied. IT IS SO ORDERED.

The plaintiffs also argue that the statute of limitations is tolled due to the fraudulent concealment by the moving defendants of the causes of action. *Lieberman v. First National Bank,* Del. Supr., 45 A. 901 (1900). Given the comments above, it is only necessary to consider this allegation in relation to the Sixth Cause of Action. In the *Halpern* case at 313 A.2d 143 Chancellor Duffy discussed fraudulent concealment as follows:

> "Fraudulent concealment requires something affirmative be done by a defendant, some 'actual artifice' which prevents a plaintiff from gaining knowledge of the facts, or some misrepresentation which is intended to put the plaintiff off the trail of inquiry. Nardo v. Guido de Ascanis & Sons, Inc., Del. Super., 254 A.2d 254 (1969) . . .

Paragraph 29 of the complaint alleges that the moving defendants "knew *or* should have known, that the Proxy Statement was materially deficient, and was false and misleading in each respect set forth in paragraph 28." Even considering this allegation along with the allegations in the Sixth Cause of Action, it does not seem to me that the plaintiff can resist the instant motion on the doctrine of fraudulent concealment.

Initially, there does not appear to be any express allegation of fraudulent concealment. That would seem dispositive under the *Halpern* case at 331 A.2d 143-144. Secondly, as to the negligence count, there is no allegation of fraud at all. Insofar as negligence is concerned, the Sixth Cause of Action in paragraph 40 emphasizes the "should have known" language, as indeed it must to be consistent with the theory of the cause of action. Even considering the oral argument to the effect that the filings with the SEC and accountants' certification constitute the fraudulent concealment, such concealment cannot save a count which has simple negligence as its underlying basis.

Moreover, as the defendants note, the complaint itself specifically alleges no acts other than the preparation of allegedly false financial statements which constitutes the alleged tort itself. Under the *Halpern* case at 331 A.2d 143–144, where commingling on the books was expressly alleged, this does not appear to constitute a recitation of any specific artifice or misrepresentation by which it is claimed that defendants succeeded in concealing from plaintiffs the wrongs of which they complain. It certainly cannot support fraudulent concealment when the tort alleged is negligence.

I conclude that the statute of limitations bars the Sixth Cause of Action against the moving defendants. The motion to dismiss that cause of action is granted.

FARLAND v. WILLS, ET AL.

No. 4888

BANK OF AMERICA v. GAC PROPERTIES, INC., ET AL.

No. 4914

Court of Chancery of the State of Delaware, New Castle

November 12, 1975

Farland, a holder of debentures, sued GAC Credit and others in a three count complaint alleging fraudulent transfer of assets, an unconscionable exchange offer for the debentures, and misrepresentations in a prospectus covering the Exchange Offer. He brings suit on behalf of a class and requests preliminary injunctive relief, including enjoining of the outstanding Exchange Offer and appointment of a temporary receiver. Bank of America sued the same defendants, as trustee under an Indenture, alleging fraudulent conveyances and violations of the Delaware Corporate Law, and requested injunctive relief to freeze any property transferred, and to prohibit further transfers, and to establish a constructive trust. The Court held, inter alia, that Farland had failed to establish that preliminary

relief was justified, that it was inappropriate to take any action to interfere with the debenture holders' right to respond to the Exchange Offer, and that there was no utility demonstrated for the appointment of a receiver. The relief sought by Bank of America was found to be the most appropriate.

1. Corporations ⇐ 181(7)

Where transactions about which complaint is made are described in the prospectus, failure to label the transactions as fraudulent, illegal, or unfair does not make the representations in the prospectives false and misleading.

2. Corporations ⇐ 114

Where over 55% of Debenture holders have already accepted an Exchange Offer, the matter of acceptance of the offer is most appropriately left to the judgment and discretion of the holders of those Debentures.

3. Corporations ⇐ 553(2)

The appointment of a receiver is discretionary with court even where a corporation is insolvent, the statute being permissive not mandatory. 8 Del. C. § 5291.

4. Receivers ⇐ 16

The Court of Equity has inherent power to appoint a receiver pendente lite even for solvent corporations so as to preserve property involved in litigation, the question being whether such appointment is necessary for the prevention of manifest wrong and injury and whether the plaintiff, without such appointment, is in danger of suffering irreparable loss. Rule 149.

5. Receivers ⇐ 44

Where appointment of a receiver on the application for preliminary relief by one debenture holder might frustrate not only the goal of Credit, but also the hopes and expectations of a majority of debenture holders, such receiver will not be appointed where the utility has not been demonstrated and where it could trigger consequences not beneficial to the debenture holders.

6. Corporations ⇐ 540

Where the Delaware Uniform Conveyance Act is applicable, the definition of insolvency under the Delaware Statutes is likewise applicable. 6 Del. C. § 1302(a).

7. Corporations ⇐ 540

The Delaware statutory definition of insolvency has been said to be broader than both insolvency in the bankruptcy sense (deficit net worth) and insolvency in the equity sense (inability to pay debts as they mature).

8. Fraudulent Conveyances ⇐ 61

The condition of being insolvent within the Uniform Fraudulent Conveyance Act can ultimately be determined only by a fact and figure balancing of assets and liabilities, and similar evaluation is necessary under the Delaware capital impairment standard. 8 *Del. C.*, § 160.

9. Equity ⇐ 25

Where the circumstances are such that transactions appear so unconscionable as to require some equitable relief, and where there is in the record a recognized basis for that relief the Court is not narrowly limited to statutory definition.

10. Corporations ⇐ 152, 376

The Delaware statute forbids a corporation from purchasing its own capital stock when the capital of the corporation is impaired or when such purchase would cause any impairment of the corporation, and while a formal appraisal is not required, the directors are under a duty to evaluate the assets on the basis of acceptable data and by standards which they are entitled to believe reasonably reflect present values. 8 DEL. C. § 160.

11. Corporations ⇐ 376

It is generally true that the acquisition of its own capital stock is not ordinarily an essential corporate function, and a corporation should not be able to become a purchaser of its own stock when it results in a fraud upon the rights of, or injury to, the creditors.

12. Corporations ⇐ 337(3)
Equity ⇐ 10

Where an Indenture contract provides for repayment as its prime obligation, it should not be read to contemplate the wrongful elimination of one corporation's liquidity at the expense of the debenture holders on the part of a company owing the other corporation.

13. Fraudulent Conveyances ⇐ 116

If preliminary relief on the basis of a fraudulent conveyance is appropriate under either Delaware or Florida law, it must be based on actual intent to delay, hinder or defraud creditors. 6 *Del. C.*, § 1307, *Fla. Stat.* § 726.01

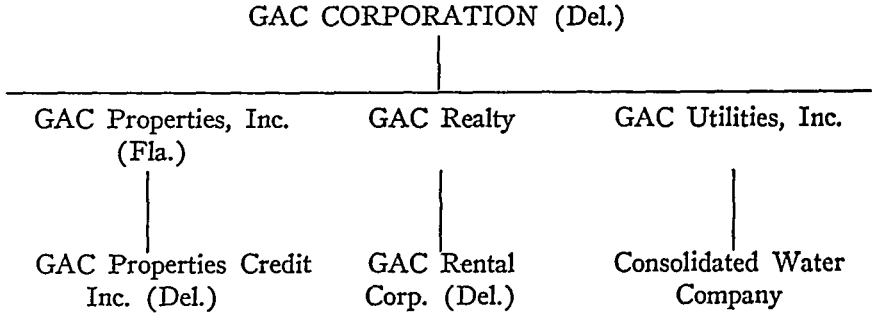
QUILLEN, *Chancellor*

This letter constitutes the opinion of the Court in applications for preliminary injunctions in two pending cases.

In Civil Action No. 4888, Farland, a holder of $25,000 worth of 12% Debentures issued under an Indenture dated November 15, 1970 and maturing on November 15, 1975 (1975 Debentures) has sued Credit and the other defendants in a three count complaint alleging fraudulent transfer of assets, an unconscionable exchange offer for the debentures, and misrepresentations in the September 12, 1975 prospectus covering the Exchange Offer. The plaintiff brings suit on behalf of a class and requests preliminary injunctive relief, including the enjoining of the outstanding Exchange Offer, and appointment of a temporary receiver.

In Civil Action No. 4914, BOA sues the same defendants as trustee under the Indenture dated November 15, 1970 from Credit. The trustee alleges fraudulent conveyance and violations of the Delaware Corporate Law and requests injunctive relief to freeze any property transferred and to prohibit further transfers plus the establishment of a constructive trust.

It is important to understand the GAC corporate structure insofar as it is pertinent here. This is probably most easily shown in graph form:



I include GAC Utilities, Inc. and Consolidated Water Company because they are involved in the terms of the outstanding Exchange Offer presently pending.

The important fact to bear in mind when discussing the corporate relationships and transactions is that Properties owns Credit. Thus, the position of the debenture holders, the only public investors in Credit, is antagonistic to Properties to the extent that creditor interests and ownership interests clash.

It is necessary to have some understanding of the relationship between Properties and Credit. Properties sells land as retail, primarily in installments. Credit provides financing for Properties by purchasing the installment land contracts. The contracts purchased by Credit are somewhat seasoned by the payment of the down payment and six installments. It had been anticipated that the land sales by Properties and the contract

purchases by Credit would be sufficient to move the necessary cash from Credit to Properties.

The nature of the business is such that purchasers have no personal liability on their contract, and in the event of default, the contract is canceled and the monies paid retained. Properties also has obligations for development costs which can exceed the initial cash receipts of the long term purchase contracts (up to fifteen years). Properties is dependent upon Credit for a flow of cash which permits Properties to perform its development obligations which in turn generates new receivables and maintains the collectibility of receivables already held.

For a variety of reasons, Properties' business has suffered. Installment land sales netted cancellations in 1971 by $128,457,000. By 1974, this total had declined to $19,489,000. The trend is continuing in 1975. Credit concedes that the transfer transactions, which are challenged in these lawsuits, were made because Properties had a cash shortage and was not generating sufficient cash through the sale of eligible receivables (land sale installment contracts to Credit). The defendants claim that Properties expended approximately $45,000,000 from January 1, 1974 through March 31, 1975 for purposes which, directly or indirectly, maintain collectibility of Credit's receivables. Farland, on the other hand, maintains Properties paid GAC and others millions of dollars siphoned from Credit.

Prior to September 30, 1974 Properties owned 50,500 shares of common stock of Credit constituting all of the outstanding shares of Credit. Indeed, under the 1970 Indenture and the operating agreement, Credit is not authorized to issue shares to anyone except Properties and its subsidiaries. The complaints in the cases center on three types of transactions: the purchase by Credit of its own stock from Properties and the purchase of fixed assets by Credit from Properties and the purchase of a lease by Credit from Rental.

As to the first, it is undisputed that on the dates listed below Credit purchased the number of shares listed for the amount of money listed.

Date	*Shares*	*Price*	
September 30, 1974	1,000		
December 31, 1974	10,146	$17,600,755	(1974 Total)
March 31, 1975	1,582	$ 2,527,435	
June 30, 1975	368	$ 591,232	
September 17, 1975 (as of July 31, 1975)	116	$ 188,743	
October 17, 1975 (as of August 31, 1975)	121	$ 195,651	

These stock purchases were the first undertaken although dividends had been paid previously.

As to the second, as of March 31, 1975, the company purchased certain real estate, machinery, equipment, furniture and fixtures owned by Properties or its subsidiaries for $12,132,713, representing the net book value of the assets on the books of the affiliates ($14,960,570) net of applicable mortgage debt ($2,827,857). The assets have been rented to the affiliates on a net lease basis whereby all costs of ownership related to the property are paid for by the lessee. Rental is computed at the rate of 110% of depreciation for depreciable assets which, in turn, is computed principally on a straight-line basis over the estimated useful lives of the assets. The depreciation charges are based upon a continuation of the rates used by the affiliates prior to the sale. Non-depreciable real estate has been rented at the rate of 1.43% of the net book value of the property per month.

As to the third, Credit purchased a lease from Rental for $1,787,662. In particular, as of March 31,1975, Properties sold all of its real property and improvements, except for its land inventory and one hotel, to Rental, for the net book value of the property, less mortgage debt assumed, and leased back the property under a net full payout lease. Rental payments provided for in the lease are computed at the rate of 110% of depreciation on depreciable property and at 1.43% of cost per month over 120 months on non-depreciable land. Credit simultaneously purchased the lease from Rental for $1,787,662.

In total, Credit has thus transferred liquid assets in excess of $35,000,000 between September 30, 1974 and the present day. These transfers have been undertaken admittedly as an alternate method of moving cash from Credit to Properties.

There is presently outstanding approximately $35,600,000 principal amount of the 1975 Debentures. On November 15, 1975 Credit will be obligated to pay this principal amount to the holders of the 1975 Debentures and to pay them approximately $4,300,000 in interest on their 1975 Debentures for a total of $39,900,000. The interest figure is evidently in dispute according to the pleadings.

In addition, Credit has outstanding $43,654,000 of 11% Debentures issued under an Indenture dated September 1, 1971 and maturing on September 1, 1977 (1977 Debentures). Chemical as trustee has intervened as a plaintiff and seeks relief similar to BOA.

It is somewhat difficult to get a handle on the case due to the considerable diverse views parties take of the corporate relationships, the operating agreement, and the actions to be taken in the future. But it seems to me that it is best, as a matter of preliminary consideration, to turn first to the second and third causes of action of Farland. His prayer for relief is that this Court "declare the Exchange Offer null and void, . . . and enjoin preliminarily . . . the defendants from proceeding with, making effective, and consummating the Exchange Offer to the 1975 Debenture holders . . .".

I am not satisfied that a case for relief as to the Exchange Offer has been made. The Court believes it inappropriate to take any action to interfere with the debenture holders right to respond to the Exchange Offer. Several reasons support this conclusion.

[1] In the first place, with the exception of the last two stock purchases not determined by September 12, 1975, the transactions about which complaint is made are described in the prospectus. Even as to the last two transactions, Credit announced its intention to continue the practice. I cannot conclude on this application for preliminary relief that the failure to label the transactions as fraudulent, illegal, or unfair make the representations in the prospectives false and misleading.

[2] In the second place, over 55% of the 1975 Debenture holders have already accepted the Exchange Offer. I see no compelling reason why the matter of acceptance of the offer is not most appropriately left to the judgment and discretion of the holders of the 1975 Debentures as BOA has recommended. *Campbell v. Loews, Inc.*, Del. Ch., 134 A.2d 565, 567 (1957).

In the third place, if the plaintiff Farland does not consent to the Exchange Offer and it is consummated, Farland will have nothing to object to since he will receive one hundred cents on the dollar.

In the fourth place, if the Exchange Offer is not successful, Credit has indicated it will not have sufficient funds to pay the 1975 Debentures making a default in that issue as well as a default in the 1977 Debentures under the cross default provisions. It thus appears that the Exchange Offer may be the only means to avoid bankruptcy.

In the fifth place, the debenture holders are facing a current option and it is not clear to me what the relative benefits of plaintiff's remedy may be as compared to the Exchange Offer.

As to the preliminary relief sought in regard to the Exchange Offer, I conclude that Farland has failed to establish that preliminary relief is justified.

[3, 4] I think it useful secondly to turn to the prayer of Farland which requests this Court to appoint a receiver to take charge of the property of Credit. The Court may in its discretion appoint a receiver pendente lite "if cause therefore be shown". Rule 149. The justification by Farland for the appointment of a receiver is the insolvency of the corporation. 8 *Del. C.*, § 5291. The statute of course does permit the Court to appoint a receiver in cases of insolvency. It seems to me the question on the receivership is whether it is necessary for the prevention of manifest wrong and injury and whether the plaintiff, without such an appointment, is in danger of suffering irreparable loss. *Gray v. Newark*, Del. Ch., 79 A. 735 (1911). *Whitmer v. William Whitmer & Son, Inc.*, Del. Ch., 99 A. 428 (1916).

It is true that the Court of Equity has inherent power to appoint a receiver even for solvent corporation pendente lite so as to preserve property involved in litigation. *Lichens Co. v. Standard Commercial Tobacco Co.*, Del. Ch., 40 A.2d 447 (1944). *In Re North European Oil Corp.*, Del. Ch., 129 A.2d 259 (1957). But, as the defendants argue, the appointment of a receiver would frustrate the present effort of Credit to bring about an agreement among the debenture holders which would enable the company to continue operations. Specifically, the appointment of a receiver would automatically trigger default provisions in both the 1970 Indenture and the 1971 Indenture so that both issues of debentures would become due and payable.

Even with insolvency the appointment remains discretionary. *Banks v. Christiana Copper Mines, Inc.*, Del. Ch., 99 A.2d 504 (1953). *Kinney v. Arbington Co.*, Del. Ch., 151 A. 257 (1930). The utility of a receiver must be demonstrated. *Argenbright v. Phoenix Finance Co.*, Del. Ch., 142 A. 793 (1928). *Foster v. Delaware Valley Drug Co., Inc.*, Del. Ch., 114 A.2d 228 (1955). *Boggs v. Belvue*, Del. Ch., 156 A. 202 (1931).

[5] In this case, to appoint a receiver on the application for preliminary relief by one debenture holder, might well frustrate not only the goal of Credit but also the hopes and expectations of a majority of the debenture holders. Even if the present situation was produced by the defendants, the debenture holders are facing a *current* option and, as noted already, it is not clear to me what the relative benefits of the plaintiff's remedy may be as compared to the Exchange Offer. I therefore decline at this time to appoint a receiver because the utility has not been demonstrated and, as trustee argued orally, it could trigger consequences not beneficial to the debenture holders.

In the Farland reply brief, and at oral argument, Farland suggests the Court make use of 8 *Del. C.*, § 102(b)(2) and § 302(b). I do not believe that the case is in a posture for the Court to administer and enforce any compromise or agreement made pursuant to those provisions. The section contemplates a specific proposal and I do not believe the Court should move blindly to assert its statutory power. Indeed, the only compromise that has been proposed is the Exchange Offer.

Thus, I reject three specific remedies being sought by Farland as inappropriate but, in so doing, I make no decision on the underlying dispute. The balance of the prayers present the Court with more difficulty and necessarily involve the Court in the merits of the controversy. Since the additional relief sought by Farland is included in the relief sought by the trustee, I find it useful to concentrate on the trustee's lawsuit and to have the relief entered in that proceeding. I will rely, however, on the arguments made by Farland as well.

The main thrust of the plaintiffs' attack is that the property transfers were fraudulent conveyances (6 *Del. C.*, § 1304, 1307) or purchases by the corporation of its own stock while capital was impaired (8 *Del. C.*, § 160).

These alleged statutory illegalities have some problems of proof attached to them. Credit had and continues to have a book surplus. Credit made a timely interest payment of $2,400,000 on the 1977 Debentures as recently as September. Credit says it carries receivables at the estimated collectible amounts unrelated to market. BOA has by a general affidavit indicated present fair salable value [8 Del. C., § 1302(a)] of the receivables would be lower, as it would. But the question is obviously how much lower. Was Credit insolvent at the time of the transactions in question?

[6] The definition of insolvency under the Uniform Fraudulent Conveyance Act (the Delaware Act) is broad. If the Act applies, and I tend to think it does insofar as the stock purchases are concerned (8 *Del. C.*, § 169 makes Delaware the situs of ownership of capital stock of Delaware corporations), the liberal definition of 6 *Del. C.*, § 1302(a) is applicable:

> "A person is insolvent when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured."

[7, 8] It has been said that this definition is broader than both insolvency in the bankruptcy sense (deficit net worth) and insolvency in the equity sense (inability to pay debts as they mature). *Larrimore v. Feeney,* Pa. Supr., 192 A.2d 351 (1963); *Cellar Lumber Co. v. Holley,* Ohio App., 224 N.E.2d 360 (1967). But there is no precise evidence and the condition of being insolvent within the Uniform Fraudulent Conveyance Act can ultimately be determined only by a fact and figure balancing of assets and liabilities. *Hay v. Duskin,* Ariz. App., 455 P.2d 281 (1969). Similar evaluation is necessary under the capital impairment standard of 8 Del. C., § 160. The admissions relied on by the plaintiffs relate to cash flow only and therefore it seems to me that they fall short of establishing insolvency, even as a preliminary matter.

Thus, it is very difficult for me to determine on the present record whether Credit was insolvent at the time of the transfers being attacked or thereby was rendered insolvent. It is equally difficult to determine if capital was impaired. I could make a guess but speculation without a record does not justify judicial relief on a theory premised on the speculation. Even for preliminary relief, the Court must be able to find a reasonable probability as to the necessary facts.

It is also somewhat questionable to conclude as a preliminary matter that all these transfers were made with the actual intent to defraud. 8 *Del. C.*, § 1307; *Fla. Stat.*, § 726.01. The plaintiff Farland has argued the point well noting the financial embarrassment of Credit, the nature of the consideration, the related transferees, and the nature of the transactions. But, under the view I take of the case, I do not find, in regard to the stock purchases, it is necessary to judge the actual intent of the defendants. I feel there is a less severe judgment which justifies the same relief and which is included in the prayers of the plaintiffs and indeed argued by Farland in the brief.

[9] I do not believe that this Court is narrowly limited to statutory definitions in the present situation. In my judgment, even as a preliminary matter, the circumstances are such that the transactions here appear so unconscionable as to require some equitable relief. I find in the record a recognized basis for relief. And I might add that this Court's special responsibility in the corporate field supports my conclusion.

While it is perhaps premature to characterize Credit's behavior in a precise statutory sense, it seems to me probable that the stock purchases, which are continuing, constitute fraudulent conduct, at least in an equitable sense, as to 1975 and the 1977 Debenture holders.

[10] Initially, one cannot help but be struck by the cavalier manner in which Credit acted. Approaching the problem from a corporate law context, our statute, 8 *Del. C.*, § 160, forbids a corporation from purchasing its own capital stock "when the capital of the corporation is impaired or when such [purchase] would cause any impairment of the capital of the corporation." While a formal appraisal is not required, the directors are "under a duty to evaluate the assets on the basis of acceptable data and by standards which they are entitled to believe reasonably reflect present 'values'." *Morris v. Standard Gas and Electric Co.*, Del. Ch., 63 A.2d 577, 581 (1949). It is clear that no effort was made in this regard although the accounts receivable are discounted 40% for reserves for development costs, cancellations, credits, property taxes and mortgages. As the prospectus says: "Installment land sales contracts are not marketable except at very substantial discounts." If one looks at the nature of the receivables (no credit investigation, no personal liability, long term contracts), the market depression (described at length by defendants on pages 8 and 9 of their opening brief), and percentage of total assets in receivables (92.5% on December 31, 1975 to 81.1% on June 30, 1975 as set forth in BOA's brief), the need for a current market valuation is apparent. It is also apparent to break through the circular nature of the defendants' argument. The high value of the receivables is used to justify a stock purchase made necessary to maintain the high value of receivables. At some point, it seems to me that the receivables need to be related to a market under the circumstances of this case.

[11] While I think it is important to note the manner of corporate operation, I do not believe it is necessary for me to conclude preliminarily that there was an actual impairment of capital. This Court has noted "the obvious dangers and abuses inherent in a corporation's dealing in its own shares" and that "creditors . . . may be prejudiced even though the purchase be made in good faith." *Propp v. Sadacca*, Del. Ch., 175 A.2d 33, 38 (1961); aff'd sub nom., *Bennett v. Propp*, Del. Supr., 187 A.2d 405 (1962). A corporation should not be able to become a purchaser of its own stock when it results in a fraud upon the rights of *or* injury to the creditors. 6A *Fletcher Cyclopedia Corporations*, § 2854; see *In re International Radiator Company*, Del. Ch., 92 A. 255 (1914); *Pasotti v.*

United States Guardian Corporation, Del. Ch., 156 A. 255 (1931); *Hegarty v. American Commonwealth Powers Corporation,* Del. Ch., 174 A. 273 (1934). With these principles of law in mind, I turn to the facts present here as to stock purchases.

Initially, Credit is purchasing its own stock. It is generally true that the acquisition of its own capital stock is not ordinarily an essential corporate function. *Brophy v. Cities Service Co.,* Del. Ch., 70 A.2d 5, 8 (1949).

Second, Credit is legally bound to pay the 1975 Debenture holders on November 15, 1975 and needs cash. Whatever the effect on capital invasion, the stock purchase transaction deprived Credit of liquid assets essential to meet maturing obligations.

Third, Credit not only now admits it will be unable to pay the debentures which mature on November 15, 1975, but Credit also knew *at least* on year end analysis of calendar year 1974, when Credit was *publicly* projecting that only 75% to 80% of the debentures could be retired and the remainder would require refinancing, that it would not be able to pay the 1975 Debenture holders. It was also clear on 1974 year end analysis, as evidence by public statement, that refinancing was not immediately available. Notwithstanding this situation, largely created by the 1974 stock purchases, Credit continued to purchase its own stock from Properties during 1975 and continued to deplete the liquid assets necessary to pay the debenture holders.

Fourth, Credit is wholly owned by Properties and must so remain. There can be no advantage to Credit as a separate corporate entity in holding treasury stock. The purchase is without any direct material consideration.

Fifth, Credit has announced its intention to continue to purchase stock and has thus demonstrated a wilful disregard for the rights of the debenture holders.

Sixth, since Credit is wholly owned by Properties, there is self dealing. The saving of the interdependent corporate structure is simply using for selfish purposes liquid assets needed to pay creditors.

[12] Just as it is no answer for Credit to say capital is not invaded, it is no answer to such behavior to say the Indenture contract permits such stock purchases by its income formula approach. The Indenture contract provides for repayment as its prime obligation and should not be read to contemplate the wrongful eliminating of Credit's liquidity at the expense of the debenture holders on the part of Properties. The debt of the debentures is senior to any amounts owing the GAC group. Whatever the ultimate pigeonhole, a probable case of equitable fraud has been made by the 1975 Debenture holders as to the stock purchases. Given the cross default provisions, the 1977 Debenture holders also have made a case.

[13] Turning to the purchase of fixed assets and the purchase of the lease, the record lacks evidence in regard to "fair consideration" as well

as the previously discussed deficiency concerning "insolvency." Therefore, if preliminary relief on the basis of a fraudulent conveyance is appropriate, under either Delaware or Florida law, it must be based on actual intent to delay, hinder or defraud creditors. It is important to note that these transactions took place at the end of the first quarter of 1975 when the 1974 year end picture is clear. The conveyances of liquid assets for fixed assets were made under circumstances when the result was necessarily to hinder and delay the 1975 Debenture holders. *J. I. Kelly Co. v. Pollack,* Fla., 49 So. 934 (1909). As noted before, Credit was financially embarrassed and the transfers were to related transferees. Moreover, the nature of the transactions should be examined.

The 1970 Indenture restricts the business of Credit by providing that Credit will not "engage in any business other than dealing in eligible receivables or activities incidental thereto." In essence, Credit claims that the asset purchases and lease purchases were incidental to dealing in eligible receivables because they permitted Properties to continue sales and development work and thus aided Credit in maintaining its present receivables and in gaining new receivables. Furthermore Credit maintains that the $13,900,000 figure is only a fraction of the total asset figure on the Credit balance sheet.

I cannot agree that the $13,900,000 figure is not material when the transaction involves the transfer of liquid assets by a corporation which will have to meet approximately $39,000,000 of debt and interest less than eight months after the transfer. Nor can I agree that these sales are merely "incidental" to dealings in eligible receivables. They have nothing to do with eligible receivables. They are a wholly separate means of generating cash flow from Credit to Properties and involve Credit in business activities not permitted by the Indenture. The Indenture after all is directly related to the interests of 1975 Debenture holders. Indeed, had the trustee so requested, violation of the Indenture alone might have been an independent basis for relief.

I conclude as a preliminary matter that under either 6 *Del. C.,* § 1307 *Fla. Stat.,* § 726.01, the transfers of the fixed assets and lease were with the intent to delay, hinder or defraud the 1975 Debenture holders. Given the cross default provisions, the 1977 Debenture holders have a case as well.

As to all the transactions, given Credit's announced intention, without a favorable result of the Exchange Offer, "to seek the Court's protection under the bankruptcy law," it appears that irreparable harm has been established. The debenture holders have the choice of a substituted, less favorable contract or some proceedings in bankruptcy.

In my judgment, the relief sought by BOA in Civil Action No. 4914 is the most appropriate for the present.