Unreported Cases

INTRODUCTION

UNREPORTED CASES is a continuing feature of THE DELAWARE JOURNAL OF CORPORATE LAW. All unreported cases of a corporate nature that have not been published by a reporter system will be included. The court's opinions are printed in their entirety, exactly as received.

To expedite the attorney's research, all cases are headnoted according to the National Reporter key number classification system.* Indices are provided for case names, statutes construed, rules of court, and key number and classifications for this issue.

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ANDRA v. BLOUNT

No. 17,154

Court of Chancery of the State of Delaware

March 29, 2000

Plaintiff brought this unfair dealing action seeking to recover damages equivalent to the appraised value of her stock. Plaintiff, a nontendering shareholder in a tender offer/back-end merger, sought class certification in order to spread her litigation costs over a classwide recovery and obtain an order requiring defendants to pay her attorneys' fees. This would make it easier for her to find legal representation and increases the possibility of obtaining a full recovery.

The court of chancery, per Vice Chancellor Strine, concluded that while a nontendering stockholder with appraisal rights who is squeezed out in a back-end cash-out merger after a tender offer, may not challenge the disclosures issued in connection with that tender offer, she may pursue her claim that the back-end merger price was rendered unfair by breaches of fiduciary duty by the director-defendants. Even where damages equivalent to the appraised value of plaintiff's stock would afford her complete relief, binding case law requires that a minority stockholder *with* appraisal rights should have no less access to a full remedy than a minority stockholder without appraisal rights.

1. Corporations ☞ 307, 310(1), 320(1)

A nontendering stockholder with appraisal rights who is squeezed out in a back-end cash-out merger after a tender offer may not challenge the disclosures issued in connection with that tender offer when the tender offer was effected by a majority stockholder who already possessed the voting power to force the back-end merger.

2. Corporations ☞ 182.4(2), 307, 310(1), 320(1)

Where nontendering stockholder can allege no personal harm caused to her by allegedly inadequate disclosures, dismissal of disclosure claims is appropriate but nontendering stockholder may pursue claim that the back-end merger price was rendered unfair by breaches of fiduciary duty by the director-defendants.

3. Corporations ⟹ 202, 320(6)

A minority stockholder with appraisal rights should have no less access to a full remedy than a minority stockholder without appraisal rights.

4. Corporations ⟹ 189(14), 307, 310(1), 320(1), 320(12)

In an unfair dealing action, nontendering stockholder may spread her litigation costs over any classwide recovery and may obtain an order requiring the defendants to pay her attorneys' fees, thus making it easier for her to find legal representation and enabling her the possibility of a full recovery.

5. Corporations ⟹ 182.4(6), 207.1

If relegated to an appraisal action, a nontendering stockholder will have to cover her attorneys' fees out of any recovery she (and the usually small group of appraisal petitioners) obtain and will be unable to proceed as a class representative on behalf of all similarly situated stockholders.

6. Corporations ⟹ 189.4(6), 307, 310(1), 319(.5), 319(5)

Because a plaintiff without appraisal rights would be able to pursue an unfair dealing claims on a class action basis and seek recovery of her attorneys' fees, it would be inconsistent with *Rabkin* and *Cede* to deny a plaintiff with appraisal rights the same opportunity.

7. Pretrial Procedure ⟹ 679

When addressing a motion to dismiss, the allegations of the complaint must be accepted as true, and plaintiff must be accorded the benefit of all reasonable inferences that can be drawn from the complaint.

8. Corporations ⟹ 207.1
Pretrial Procedure ⟹ 556, 556.1, 557

Persons should only be permitted to litigate claims that involve actual or threatened injury to themselves.

9. Pretrial Procedure ⚷ 556, 556.1, 557

A plaintiff who fails to secure adequate disclosures in advance of a stockholder decision may not, after declining to pursue a preliminary injunction, pursue litigation of the adequacy of disclosures issued in connection with a tender offer where the plaintiff herself did not tender.

10. Corporations ⚷ 310(1), 320(1), 320(4)

So long as plaintiff can state a claim for breach of fiduciary duty in connection with a merger, plaintiff can press an unfair dealing claim.

11. Corporations ⚷ 307, 310(1), 320(1), 320(2), 320(4)

A plaintiff who can state a claim for breach of fiduciary duty ordinarily should not be relegated to the (implicitly less adequate) remedy of appraisal, where the only remedy is the fair value of the plaintiff's stock; otherwise, there is a risk that victims of fiduciary breaches will be less than wholly compensated for the harm done them, thus creating less than an adequate incentive for fiduciaries to comply with their unremitting duties of loyalty and care.

12. Corporations ⚷ 182.4(1), 182.4(2), 182.4(4), 182.4(6)

An award of fair value in appraisal terms is adequate where the plaintiff's claims center on a valuation issue.

13. Corporations ⚷ 182.4(6), 189(14)

In a class action, plaintiffs' lawyers can take their fees and expenses against any classwide recovery, whereas, in an appraisal action, fees and expenses can be recovered only as an offset against the appraisal award to the group of stockholders who perfected their appraisal rights.

14. Corporations ⚷ 207.1
Pretrial Procedure ⚷ 556, 556.1, 557

Where plaintiff seeks class certification on an unfair dealing claim, and such plaintiff lacks standing to litigate disclosure claims, it may be necessary to limit such a class to similarly situated, nontendering stockholders.

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Anne C. Foster, Esquire, and Thad J. Bracegirdle, Esquire, of Richards, Layton & Finger, Wilmington, Delaware; and J. Michael Rediker, Esquire, of Ritchie & Rediker, Birmingham, Alabama, of counsel, for defendants T. Morris Hackney, James S. Scott, Reese H. McKinney, Jr., and Meadowcraft, Inc.

STRINE, *Vice Chancellor*

[1-3] In this opinion, I conclude that a non-tendering stockholder with appraisal rights who is squeezed out in a back-end, cash-out merger after a tender offer may not challenge the disclosures issued in connection with that tender offer when the tender offer was effected by a majority stockholder who already possessed the voting power to force the back-end merger. In this scenario, the non-tendering stockholder can allege no personal harm caused to her by the allegedly inadequate disclosures. Therefore, dismissal of her disclosure claims is appropriate. In contrast, however, the non-tendering stockholder may pursue her claim that the back-end merger price was rendered unfair by breaches of fiduciary duty by the director-defendants, who include the majority stockholder. Even though the plaintiff has indicated that "damages equivalent to the appraised value of [her] stock" would afford her "complete relief for the wrongs complained of in this action,"[1] the import of binding case law such as *Rabkin v. Philip A. Hunt Chemical Corp.*[2] and *Cede & Co. v. Technicolor, Inc.* ("*Cede II*")[3] is that a minority stockholder *with* appraisal rights should have no less access to a full remedy than a minority stockholder without appraisal rights.
[4-6] In this unfair dealing action, the non-tendering stockholder may

[1]Pl. Letter to the Court, at 1 (June 7, 1999).
[2]Del. Supr., 498 A.2d 1099, 1104 (1985).
[3]Del. Supr., 634 A.2d 345, 367 (1993).

spread her litigation costs over any classwide recovery and may obtain an order requiring the defendants to pay her attorneys' fees, thus making it easier for her to find legal representation and enabling her the possibility of a full recovery. If relegated to an appraisal action, the non-tendering stockholder will have to cover her attorneys' fees out of any recovery she (and the usually smaller group of appraisal petitioners) obtain and will be unable to proceed as a class representative on behalf of all similarly situated stockholders. Because a plaintiff without appraisal rights would be able to pursue an unfair dealing claim on a class action basis and seek recovery of her attorneys' fees, it would be inconsistent with *Rabkin* and *Cede* to deny a plaintiff with appraisal rights that same opportunity. Although reasonable minds can differ on the policy wisdom of this approach, it is the one that I as a trial judge must adopt because it is the one most consistent with a faithful reading of our Supreme Court's teachings in this area.

I. Procedural Background

The defendants in this action — the directors of Meadowcraft, Inc., Meadowcraft itself, and MWI Acquisition Co., a corporate entity used by Meadowcraft's majority stockholder as an acquisition vehicle — seek dismissal of this case on the grounds that the plaintiff, Mary D. Andra: (1) lacks standing to challenge the adequacy of disclosures issued in connection with a tender offer in which Andra did not tender; and (2) is relegated to an appraisal action in challenging the price of the back-end merger in which she was squeezed out as a Meadowcraft stockholder.

The tender offer/back-end merger at issue here was initiated by Meadowcraft's then 73% owner, director, chairman, and chief executive officer, defendant Samuel R. Blount, in May 1999. At that time, Blount offered to buy each of the Meadowcraft shares he did not own for $10 a share. To the extent that he did not receive a tender from each Meadowcraft stockholder, Blount announced his intention to cash out the non-tendering stockholders through a merger that — once recommended by the Meadowcraft board and put to the stockholders for their approval — he had the votes to effect.

After the announcement of these proposed transactions, Andra brought an action alleging that the disclosures issued by the defendants in connection with the tender offer were materially incomplete and misleading. She moved for expedited proceedings to enable the court to consider an application for a preliminary injunction that would prevent the consummation of the tender offer until the Meadowcraft stockholders were provided with adequate disclosures. This court scheduled a preliminary injunction hearing, to be preceded by expedited discovery.

On June 7, 1999, Andra withdrew her request for a preliminary injunction. Her counsel explained this decision as follows:

> *The expedited discovery plaintiff has taken to date has confirmed the views of plaintiff and her counsel that her claims are meritorious*; however, plaintiff has also concluded that damages would be an adequate remedy for the public shareholders of Meadowcraft . . . .
>
> Plaintiff sought a preliminary injunction in connection with the tender offer for Meadowcraft's public shares by Meadowcraft's 73% shareholder in order to provide Meadowcraft's minority shareholders with material disclosures which would inform their decision whether or not to tender or await the second step merger and seek appraisal. *If plaintiff prevails at trial, damages could be awarded which would be equivalent to the appraised value of Meadowcraft stock thereby giving the shareholders complete relief for the wrongs complained of in this action.* Accordingly, plaintiff hereby withdraws her application for a preliminary injunction, and the June 15, 1999 hearing can be removed from the Court's calendar.[4]

After Andra abandoned her effort to enjoin the tender offer, the offer closed. Through the offer, Blount acquired enough shares to enable him to cash out the remaining Meadowcraft stockholders through a short-form merger pursuant to 8 Del. C. § 253. Andra did not tender into Blount's offer. Rather, she refused the merger consideration and apparently preserved her appraisal rights but eventually did not attempt to prosecute an appraisal action.

II. The Key Factual Allegations Of The Complaint

Andra's second amended complaint asserts that the defendants breached their fiduciary duties of loyalty and care by: (1) failing to disclose all material facts in connection with the tender offer, and (2) consummating the tender offer/back-end merger on terms unfair to Meadowcraft's minority

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[4]Pl. Letter to the Court, at 1-2 (June 7, 1999) (emphasis added).

stockholders.[5] The basic allegations of the complaint that support Andra's claims are as follows:

- Meadowcraft, a producer of casual outdoor furniture, including wrought iron furniture, went public in November 1997 — only 17 months before Blount bought back the public's shares. At the time of the initial public offering ("IPO") at $13 a share, Blount touted the long-term earnings prospects of Meadowcraft.

- In October 1998, Meadowcraft issued a very bullish annual report to its stockholders that suggested that the company's prospects for future earnings growth were favorable, noting that "Meadowcraft Inc. is clearly positioned to be a growth company in 1999 and beyond."[6]

- In late 1998, an investment bank, Interstate/Johnson Lane, a predecessor to Wachovia Securities (both hereinafter referred to as "Wachovia"), was retained to represent a special committee of Meadowcraft directors. In January 1999, Wachovia performed analyses suggesting that the fair value of a share of Meadowcraft stock was in the range of $12.21 to $17.22 (the "January 1999 Wachovia Analyses").

- The January 1999 Wachovia Analyses were done in connection with a third party offer by Masco Corporation of $16 a share for the shares of Meadowcraft held by the public and $13 plus $4 in other consideration for the shares of Blount and Meadowcraft's president, defendant William McCanna, if Meadowcraft hit certain earning targets in the ensuing

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[5]The defendants were legitimately confused about whether the second amended complaint sets forth an unfair dealing claim. Nonetheless, Andra contends that she intended to assert such a claim and I find that the facts pled in that complaint support such a claim. At this stage of the litigation, I feel constrained to read her complaint as asserting such a claim. *Cf. Brehm v. Eisner*, Del. Supr., _ A.2d _, slip op. at 44-45 (Feb. 9, 2000) (reversing trial court for dismissing with prejudice an 88-page amended complaint the plaintiff never sought to further amend at trial court level).

[6]Second Am. Compl. ¶ 16, at 8.

three-year period. During negotiations with Masco, the special committee insisted that the proposed acquisition be subject to approval by a majority of Meadowcraft's minority stockholders.

- Shortly after the preparation of the January 1999 Wachovia Analyses, Masco and Meadowcraft postponed merger talks. Masco later informed Meadowcraft that it was no longer interested in the transaction.

- On February 10, 1999, Meadowcraft announced the company's second quarter earnings, which were about $6 million lower than in the comparable quarter of the previous year and which reflected lower sales.

- Aside from $1 million in Masco merger discussion-related professional fees, the major causes of this loss of income were disclosed as "the difficulty of factoring certain receivables [which was] expected to continue for the remainder of the fiscal year and recent customer store closing announcements."[7] I refer to these as the "Receivables and Retailer Issues" later in this opinion.

- Following this release, the market price for Meadowcraft's stock plummeted from the $9.125 a share range to $6.25 a share.

- In early March, Meadowcraft's president, William McCanna, approached NationsBank about financing a leveraged buyout ("LBO") of Meadowcraft. McCanna received analyses from Tom NationsBank indicating that a $10 per share LBO could be financed without new equity.

- After Blount learned of McCanna's LBO inquiry, Blount essentially terminated McCanna. In his resignation letter, McCanna proposed that Meadowcraft

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[7]Second Am. Compl. ¶ 26.

buy out his shares at $10 apiece. Blount agreed to try to accomplish that.

- In advance of Meadowcraft's third fiscal quarter, which is one of its best due to the seasonal nature of demand for Meadowcraft's outdoor furniture products, Blount decided to buy out the 27% of Meadowcraft shares he did not own.

- To that end, on April 9, 1999, Blount announced his intention to offer $8 apiece for the public shares. To finance the offer, Blount intended to use the same NationsBank financing McCanna had arranged. Andra contends that the buyout offer was in substantial part an excuse for Blount to cover his need to cash out the outgoing president, McCanna.

- A special committee of Meadowcraft directors was formed to consider Blount's offer. One of the members, defendant James M. Scott, was a lawyer whose law firm lists a business affiliated with Blount as a "representative client." Another member, defendant T. Morris Hackney, receives over $140,000 a year as his share of lease payments from Meadowcraft for Meadowcraft's use of a manufacturing facility owned by another company in which Hackney is a major stockholder. Thus the independence of two of the three special committee members is, at the very least, doubtful.

- Blount announced that he would not sell his Meadowcraft shares. Thus the special committee had no real ability to develop interest in another value-maximizing transaction because all it could market was a minority stake in Meadowcraft. With Blount's 73% block, it was unlikely that alternative buyers would emerge.

- In mid-May 1999, the special committee ultimately got Blount to pay $10 a share and agreed to support a back-end merger at that price. The special committee did not demand a majority of the minority voting provision.

- The $10 a share price was $3 below the IPO price and $6 below the Masco offer. Moreover, though Wachovia issued a fairness opinion supporting the $10 price, the same personnel at that investment bank had performed the January 1999 Wachovia Analyses just four months before suggesting that $10 was below the low end of a fair range of value for Meadowcraft stock.

- In the May 19, 1999 tender offer disclosure documents, no mention was made of the January 1999 Wachovia Analyses nor was it disclosed that Blount had forced out McCanna over the LBO issue and had agreed to help secure a purchase of McCanna's shares at $10 a piece.

III. Legal Analysis

[7] In addressing the defendants' motion to dismiss, I must accept the allegations of the complaint as true and accord Andra the benefit of all reasonable inferences that can be drawn from the complaint.[8]

The defendants' motion addresses two claims: (1) the claim that the tender offer disclosures were incomplete and materially misleading; and (2) the claim that the tender offer/back-end merger was substantively unfair and resulted from breaches of the defendant-directors' duties of loyalty and care. For somewhat different reasons, the defendants argue that Andra cannot press either claim. I address these arguments in turn.

A. Does Andra Have Standing To Press Her Disclosure Claims?

With regard to the narrow issue of whether Andra may press her disclosure claims, the relevant facts are few:

- Before the tender offer, Blount owned 73% of the shares of Meadowcraft. As a result, the tender offer in no way enabled him to acquire the voting power necessary to effect, with Meadowcraft board approval, a squeeze-out merger. Blount already possessed such power.

- Andra's second amended complaint challenges the adequacy of the disclosures in connection with the tender offer, arguing that the inadequacies deprived Meadowcraft stockholders of the

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[8] *Grobow v. Perot*, Del. Supr., 539 A.2d 180, 187 n. 6 (1988).

"ability to make an informed choice between tendering and seeking appraisal in the follow-up merger. The omission of the information described [in the second amended complaint] has deprived shareholders of essential information about the merits of seeking appraisal and the likelihood that such a proceeding would result in a materially higher per share payment for the shares."[9]

- The omissions primarily complained of were the lack of discussion of the January 1999 Wachovia Analyses and of the reasons for and complete terms of the McCanna resignation.

- The court afforded Andra an opportunity to litigate her preliminary injunction motion within a time frame that would have enabled the Meadowcraft stockholders to receive corrective disclosures before having to choose whether to tender.

- Andra eschewed that opportunity, based on her belief that a damages award identical to an appraisal remedy would be adequate.

- Andra did not tender into the tender offer, but instead preserved her appraisal rights.

Based on these facts, the defendants contend, and I agree, that Andra has no standing to challenge the disclosures issued in connection with the tender offer. Neither her second amended complaint nor her briefs on this motion explain how those disclosures could have possibly injured Andra. The theory of her complaint in this action is that the inadequate disclosures worked injury because they induced stockholders to tender rather than to seek appraisal. But Andra herself sought appraisal and did not suffer injury of this nature.[10]

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[9]Second Am. Compl. ¶ 46; *see also id.* ¶ 43.

[10]At oral argument, Andra's attorneys belatedly argued that she was injured because the insufficient disclosures resulted in an inadequate number of appraisal-eligible stockholders and thus made the prosecution of an appraisal action by Andra and her attorneys economically impractical. I understand the logic of this theory. *See* § III. B. of this opinion, *infra*. But I am not persuaded that our law should recognize as cognizable damage a plaintiff's claim that *others were misled* and therefore did not join her (who was not misled) as potential co-petitioners in an appraisal action. Acceptance of such a theory would force the court to entertain extremely attenuated claims premised on speculation about what percentage of stockholders might not have tendered if adequate disclosures had been made. When the named plaintiff claims that she was actually misled by

[8] In *Abajian v. Kennedy*,[11] Chancellor Allen dealt with an analogous situation. In that case, a non-tendering stockholder alleged that the disclosures made in connection with a series of related transactions, which included a "'Dutch auction' self-tender offer," were inadequate. Chancellor Allen declined to address a motion to dismiss those claims for failure to state a claim for the following reason:

> I do so because I am inclined to accept defendants' position as correct, that if plaintiffs did not sell any shares in the self-tender, they have no standing to complain about any defects that may appear in the Offer to Purchase. The facts allege[d] do not support an inference that non-tendering shareholders were injured by any defects that arguably may be contained in the Offer to Purchase. This is not a case in which a tender offer is used to put one in a position thereafter to force a cash out merger on non-tendering shareholders. In such a case a non-tendering shareholder may be dramatically if indirectly affected by deception in the tender offer document. *See Freedman v. Restaurant Associates Industries, Inc.*, Del. Ch., C.A. No. 9212 (Sept. 19, 1990).[12]

This reasoning is sound and is consistent with the proposition that persons should only be permitted to litigate claims that involve actual or threatened injury to themselves.[13]

Nor do I see any public policy purpose that would be served by allowing a plaintiff like Andra to assert claims that could not have possibly injured her personally. By denying Andra standing at this stage of the litigation, I by no means set a precedent that denies stockholders the

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disclosures herself, Delaware Courts must engage in this exercise in speculation, which involves an "inherent risk of error . . . [of] counterfactual determinations . . ." *Steiner v. Sizzler Restaurants Int'l, Inc.*, Del. Ch., CA. No. 11994, mem. op., 1991 WL 40872, at *3, Allen, C. (March 19, 1991). Andra cites no precedent in favor of also engaging in such speculation at the behest of stockholders who were not themselves misled by the defendants' conduct, and no compelling justification for this problematic extension comes to mind. In this respect, Andra had the opportunity to avoid this "harm" by pressing her preliminary injunction motion. Therefore, her request to gin up injury based on assumptions that a sufficient number of Meadowcraft stockholders would have otherwise not tendered to make an appraisal action economically viable is less than compelling. Moreover, 3% of the Meadowcraft shares were not tendered — enough shares that one cannot conclude that an appraisal action was not feasible.

[11]Del. Ch., C.A. No. 11425, mem. op., 1992 WL 8794, Allen, C. (Jan. 17, 1992).

[12]*Abajian*, 1992 WL 8794, at *8.

[13]*See, e.g.*, *Guy v. Sills*, Del. Ch., C.A. No. 16201, let. op. at 3, 1998 WL 409346, at *1, Chandler, C. (July 10, 1998) (To obtain standing, "a plaintiff must assert facts that he has been injured in a way that is unique to him in his individual capacity[.]").

opportunity to press disclosure claims in a timely and effective manner. Given our law's traditional deference to free and informed stockholder votes and investment decisions, it obviously makes sense to enable plaintiffs to press disclosure claims in advance of the time stockholders must choose. Such timely actions provide the opportunity for corrective disclosures that permit the stockholders — who are making the decision — to decide the issue in a fair manner, thereby respecting the primacy their views should have and reducing the need for courts to shape necessarily imprecise and somewhat speculative post-decision remedies for inadequate disclosures. [9] Indeed, the value conferred by plaintiffs who attempt to secure adequate disclosures in advance of a stockholder decision may well justify some relaxation of traditional standing requirements.[14] For example, had Andra actually pressed her preliminary injunction motion, perhaps it would be good policy to let her continue to litigate her disclosure-based claims, even though she decided not to tender.[15] Andra, however, stands in a far different position. She had the opportunity to serve her fellow stockholders in that manner, but turned her back on it. Allowing her at this stage to press claims that do not involve injury to her would invite gamesmanship. That is, to accord Andra standing would encourage named plaintiffs to file disclosure claims in connection with appraisal-eligible transactions, sit on those claims until after the other stockholders have made their decision, perfect their own appraisal claims and thus preserve their own personal options, and then simultaneously pursue appraisal and a class action for damages. This incentive system strikes me as perverse, in that it encourages

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[14]In the recent case of *In re Marriott Hotel Properties II Limited Partnership Unitholders Litig.*, Del. Ch., C.A. No. 14961, mem. op., 2000 WL 128875, Lamb, V.C. (Jan. 24, 2000), Vice Chancellor Lamb applied such an approach to a plaintiff who alleged that disclosures were inadequate in advance of the tender decision, who was aware *before* the tender decision of "all or nearly all of the non-disclosures or misrepresentations about which he now complains after making that decision" and who alleged that the transaction was unfair before the tender decision, but who nonetheless tendered anyway. *Id.*, mem. op. at 47, 2000 WL 128875, at *21. But because the plaintiff had moved to correct the disclosures through a preliminary injunction application before the tender decision, there were "valid jurisprudential reasons to permit [him] to continue acting as class plaintiff" notwithstanding these facts. *Id.* "To rule otherwise would discourage plaintiffs and their counsel from acting promptly to litigate disclosure claims in advance of the conclusion of a transaction. This is directly at odds with the interests of the class who are best served when full and complete disclosures are made in a timely fashion." *Id.*, mem. op. at 47-48, 2000 WL 128875, at *21.

[15]Given that Andra believed that tendering was foolish in view of information she knew about that was not disclosed to other stockholders, a decision by her to tender could have raised its own standing issues. But public policy considerations might favor allowing a stockholder who actually attempts to litigate disclosure claims at the preliminary injunction stage to continue with these claims regardless of her voting or tendering choice. *See Marriott*, mem. op. at 47-48, 2000 WL 1288875, at *21 (resolving a similar situation in favor of plaintiff primarily on the policy ground that pre-vote litigation of disclosure claims serves an important interest).

named plaintiffs not to litigate disclosure claims at the time when such claims can still be used to promote a genuinely free stockholder choice — before the vote.

Permitting non-tendering stockholders to pursue such actions also exacerbates the always-extant risk that representative litigation is being pursued more for the benefit of the lawyers in the case than of the class whose interests are supposedly being advanced. This risk seems substantial when a tactical decision is made to eschew the opportunity to give the class members the information they need to make an informed judgment for themselves whether to tender or seek appraisal (through a timely injunction action) for the stated reason that the class representative and her lawyers can (they assert) secure a remedy for any harm suffered by the class through a damages suit (that the members of the class may or may not be interested in pursuing).

Andra notes and I acknowledge that this court has sometimes taken the position that there was no need to deal with disclosures in advance of a transaction because later money damages would suffice.[16] Yet more of this court's cases have emphasized that disclosure issues are best dealt with in a timely manner enabling informed stockholder choice.[17] Andra herself cited several cases along these lines in obtaining expedited treatment of this case.[18]

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[16]*E.g.*, *Cattle v. Carr*, Del. Ch., CA. No. 17727, mem. op., 1988 WL 19415, at *5, Allen, C. (Feb. 9, 1988) (finding applicable the principle that "money damages may provide an adequate remedy where a tender offer appears to be defective in terms of disclosure").

[17]*E.g.*, *State Wisconsin Investment Board v. Bartlett*, Del. Ch., C.A. No. 9612, order at 6, 2000 WL 193115, at *2, Steele, V.C. (Feb. 9, 2000) (ORDER) (stating that "[i] t is important that this Court protect the corporate franchise of Delaware shareholders[,]" that the shareholder franchise "can never be more important than when they are asked to vote upon a board approved and recommended merger[,]" and that the shareholder vote must therefore "be enjoined and postponed for fifteen days or until such later time as the parties may agree in order to assure that shareholders have had adequate time to assimilate information necessary to assure that they may cast an informed vote"); *Sonet v. Plum Creek Timber Co.*, Del. Ch., C.A. No. 16931, mem. op., 1999 WL 160174, at *11, Jacobs, V.C. (Mar. 18, 1999) (stating that "because the only source of the facts that will inform [the Unitholders' vote on proposed conversion of a limited partnership into a real estate investment trust] are conflicted fiduciaries . . ., only a most stringent disclosure standard, enforced by careful judicial scrutiny, can assure that the Unitholders' right to vote will have meaning" and therefore that where "the disclosures fell short of that standard . . ., the Unitholders are entitled to injunctive relief that will cure the informational gap"); *Matador Capital v. BRC Holdings*, Del. Ch., 729 A.2d 280, 298 (1998) (granting preliminary injunction requiring corrective disclosure and extension of tender offer); *Marriott*, mem. op. at 47-48, 2000 WL 128875, at *21.

[18]*See* Aff. in Support of Pl.' s Motion to Expedite ¶ 6 ("'Where, as here, there are material deficiencies in the disclosure documents recommending shareholder action, this Court has held that injunctive relief is the appropriate remedy. *See, e.g.*, *Gilmartin v. Adobe Resources Corp.*, Del. Ch., C.A. No. 12467, Jacobs, V.C., [mem.] op. at 29 (Apr. 6, 1992) ("[t] he right to cast an informed vote is specific, and its proper vindication in this case requires a specific remedy such as an injunction, rather than a substitutionary remedy such as damages'); *Eisenberg v. Chicago Milwaukee Corp.*, Del. Ch., 537 A.2d 1051, 1062 (1987) (shareholder's right to make informed, uncoerced decision requires specific, not substitutional remedy for which damages would be neither meaningful

By scheduling the preliminary injunction, I clearly gave Andra a fair chance to secure relief requiring full disclosure as a condition to the procession of Blount's tender offer. She, therefore, cannot attribute her decision to a belief that predecisional injunctive relief was unavailable.

I thus grant the defendants' motion to dismiss Andra's disclosure claims for lack of standing.

B. Can Andra Press An Unfair Dealing Claim Against The Merger When She Concedes That The Appraisal Remedy Is Sufficient To Remedy Any Harm She Has Suffered?

In her second amended complaint, Andra alleges facts that state a claim that the tender offer/back-end merger was subject to the entire fairness standard of review and that the price offered by Blount was in fact unfair. In essence, Andra contends that Blount took advantage of his 73% position to squeeze out the minority stockholders at an unfair price, and used short-term adverse developments as a lever to extract the real, long-term value of Meadowcraft for himself at an inequitably advantageous price. No adequate procedural protections were afforded to the minority, because the Meadowcraft special committee had no bargaining leverage and could not feasibly seek out other transactions, was comprised of a majority of directors with an arguable interest in securing Blount's continued favor, did not exercise its authority to say no to a merger with Blount, and failed to demand the same "majority of the minority" protection from Blount that they had wanted from Masco. As a result of Blount's oppression and the other directors' allegedly supine reaction, Andra claims Blount was able to buy out the minority at a price that was well below the fair market value of Meadowcraft as identified by the special committee's own investment banker just five months before and that was $3 below the November 1997 IPO price.

Given that I must draw all reasonable inferences in Andra's favor, I cannot dismiss her complaint for failure to state a claim. Nonetheless, the defendants contend that the complaint should be dismissed on the alternative basis that Andra should be relegated to the appraisal remedy.

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nor adequate); *Sealy Mattress Co. of New Jersey, Inc. v. Sealy, Inc.*, Del. Ch., 532 A.2d 1324, 1342 (1987) (holding that an injunction is the remedy most likely to obtain disclosure of the information necessary to achieve an informed decision and eliminate the offer's coercive aspects); *Joseph v. Shell Oil Co.*, Del. Ch., 482 A.2d 335 (1984) (holding that permitting minority stockholders to tender shares without curing defendants' omissions would forever deny tendering stockholders their rights to be treated fairly, and would constitute irreparable harm).").

[10] Ordinarily, one would reject the defendants' assertion out of hand. In the wake of *Rabkin v. Philip A. Hunt Chemical Corp.*[19] and *Cede II*,[20] it has become nearly impossible for a judge of this court to dismiss a well-pled unfair dealing claim on the basis that appraisal is available as a remedy and is fully adequate. Although the Supreme Court has never held that this court cannot limit a plaintiff to an appraisal remedy if that remedy is fully adequate, its prior holdings are reasonably read as indicating that so long as a plaintiff can state a claim for breach of fiduciary duty in connection with the merger, he can press an unfair dealing claim.[21] The unavailability of a class action and fee shifting in appraisal actions makes an unfair dealing action more attractive from the perspective of plaintiffs, thus leading to the litigation of lawsuits that require a determination of the fairness of the process used and the price paid when appraisal lawsuits addressing solely the issue of fair price would otherwise be sufficient.[22]

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[19]498 A.2d at 1104.

[20]634 A.2d at 367.

[21]*Wood v. Frank E. Best, Inc.*, Del. Ch., C.A. .No. 16281, mem. op. at 13, 1999 WL 504779, at *5, Chandler, V.C. (July 9, 1999) ("For good or ill, however, as *Cede* makes clear, a colorable allegation of breach of entire fairness is sufficient to proceed with an equitable entire fairness action, despite the availability of appraisal as an alternative remedy."); *see* Jack B. Jacobs, *Reappraising Appraisal: Some Judicial Reflections*, Speech at 15th Annual Ray Garrett, Jr. Corporate and Securities Law Institute, Northwestern University School of Law, at 12 (Apr. 27, 1995) (hereinafter, "Reappraising Appraisal") ("*Rabkin* held that if there was any procedural unfairness in connection with a merger, even if the only result was an unfair price, appraisal would not be adequate to remedy the wrong, and therefore, would not be exclusive. To minority stockholders, *Rabkin* offered an easy way to circumvent appraisal -by simply filing a stockholders fiduciary duty action that alleged unfair dealing.").

[22]Vice Chancellor Jacobs has succinctly captured the essential differences between a statutory appraisal action and an equitable fiduciary action:

> Appraisal is purely a creature of statute. Its underlying concept is that a stockholder dissenting from a merger or other triggering transaction is entitled, without having to prove wrongdoing or liability on anyone's part, to a determination of the fair value of his investment by an independent agency, usually a court. The only party held liable is the surviving corporation, and the measure of recovery is the fair or intrinsic value of the corporation's stock immediately before the merger. Post-merger synergies or values are not to be considered. In most states, including Delaware, the right to court-awarded attorneys fees in an appraisal is highly limited.
>
> In contrast, a stockholders' class action for breach of fiduciary duty is a creature of equity. To obtain a monetary recovery, the plaintiff shareholder must prove wrongdoing and establish liability. The parties from whom the recovery is sought are normally the corporation's directors and executive officers. The measure of the recovery is not limited to the statutorily appraised value, and in some cases, may include post-merger values computed as rescissory damages. Because the proceeding is equitable in nature, a court-awarded fee, payable by the corporation or from any fund created by a successful plaintiff, is available.

Reappraising Appraisal, at 3.

[11] The present case tests the limits of *Rabkin* and *Cede II*. I understand those cases as in large part resting on the rationale that a determination of fair value in an appraisal action may not always be sufficient to address the harm caused by breaches of fiduciary duty in the context of mergers.[23] Because an entire fairness action permits this court the flexibility to shape a remedy fitting to the breach (e.g., rescissory damages when justified), a plaintiff who can state a claim for breach of fiduciary duty ordinarily should not be relegated to the (implicitly less adequate) remedy of appraisal, where the only remedy is the fair value of plaintiff's stock. Otherwise, there is a risk that victims of fiduciary breaches will be less than wholly compensated for the harm done them, thus creating less than an adequate incentive for fiduciaries to comply with their "unremitting" duties of loyalty and care.[24] Here, however, Andra expressly concedes that damages "equivalent to the appraised value of [her] stock" are a "complete" remedy "for the wrongs complained of in this action."[25] In fact, the fiduciary breaches that Andra alleges all ultimately relate to issues of fair value. For example, Andra claims that the Receivables and Retailer Issues were merely short-term setbacks that did not adversely affect the long-term value of Meadowcraft. According to Andra, Blount used these short-term problems as a pretext to extract the long-term value of Meadowcraft for himself at an unfair price. Quite obviously, the question of whether the Receivables and Retailer Issues were one-time problems or more sustained problems affecting the long-term, intrinsic value of the company is one that will be central in an appraisal proceeding.

Indeed, even Andra's key disclosure issue centers on a valuation issue. Andra asserts that the January 1999 Wachovia Analyses should have been disclosed. The defendants contend that those Analyses were immaterial because they were based on information that was no longer relevant as of May 1999, in major part because the Receivables and Retailer Issues had changed the underlying earnings potential of Meadowcraft in a fundamental and enduring way.

[12] This case is not therefore one in which an award of fair value in appraisal terms will be inadequate to make Andra whole for her core claim.[26] This contrasts with the obvious situation where an appraisal would not be an adequate remedy. Posit a scenario where a 43% stockholder who is the company's chairman and chief executive officer consummates a tender offer followed by a back-end, squeeze-out merger. Suppose the stockholder

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[23] *Rabkin*, 498 A.2d at 1104-08; *Cede II*, 634 A.2d at 367.

[24] *Quickturn Design Systems, Inc. v. Shapiro*, Del. Supr., 721 A.2d 1281, 1292 (1998).

[25] Pl. Letter to the Court, at 1 (June 7, 1999).

[26] Moreover, because Blount now owns all of Meadowcraft, an award against that company essentially comes out of the pocket of the (allegedly) primary wrongdoer.

offered $25 a share, which is by any measure "fair," and obtains tenders from enough minority stockholders to enable him to cash out the remaining minority stockholders in a short-form merger at the same price. Undisclosed by the 43% stockholder, however, is the fact that a well-funded third party was willing to make a tender offer for $28 a share but had been rebuffed by the 43% stockholder, who did not even disclose the offer to the rest of his hand-picked board. In such a scenario, an appraisal remedy would not be sufficient to remedy the monetary harm that might have been suffered by the stockholders as a result of any breach of fiduciary duty they might prove had been committed by the 43% stockholder. While $25 is a fair price, they had arguably been wrongfully denied the opportunity for $28. That is not this case.

[13] In this case, the only apparent inadequacies of the appraisal remedy are that Andra does not get to represent a class and thus neither do her attorneys and that the appraisal action will not involve a determination that there was a fiduciary breach and the concomitant possibility for an award of attorneys' fees against the defendants. The availability of a class action is probably the more important and its primary utility (like the possibility of fee-shifting) also relates to the subject of litigation costs.[27] In a class action, the plaintiff's lawyers can take their fees and expenses against any class-wide recovery, whereas in an appraisal action the fees and expenses can be recovered only as an offset against the appraisal award to the usually far smaller group of stockholders who perfected their appraisal rights. It is much less attractive, for example, to act as an attorney for fifty-seven appraisal stockholders who own small blocks than as counsel for a class comprised of all, or at least most, of the company's stockholders. Hereinafter, I sometimes refer to both these advantages of an unfair dealing action as the "Litigation-Cost Benefits."[28]

Thus this case requires a policy choice between two models placing a primary emphasis on different values. Under one model, a plaintiff should be limited to appraisal if an appraisal award would be sufficient to redress the direct harm flowing from the fiduciary breach, regardless of whether it denies the plaintiff the Litigation-Cost Benefits of an unfair dealing claim. This model would stress the primacy of appraisal (when that statutory remedy is available) and the efficiency of avoiding unnecessary

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[27]Randall S. Thomas, *Revising the Delaware Appraisal Statute*, 3 DEL. L. REV. 1, 27-28 (2000) ("Although the named petitioner can spread its costs of prosecuting an appraisal action over the entire group of shareholders seeking appraisal, and thereby pay only a portion of the total costs of the action, a small shareholder will only find an appraisal petition cost-justified where many thousands of shares are also seeking this remedy.").

[28]As I use it here, the term obviously refers solely to the cost benefits from the perspective of a plaintiff or plaintiff's lawyer.

determinations regarding fair process when a single inquiry into price will suffice.

The other model would stress the need to provide a full and adequate remedy for fiduciary breaches and would take into account the real-world significance of procedure and litigation costs in that regard. To the extent that fiduciaries believe that they can avoid responsibility to the entire class of their stockholders and require a relatively small group of appraisal petitioners to bear (out of any recovery) the substantial costs of an action to prove an unfair price, fiduciaries may not be adequately deterred from engaging in faithless behavior. This model would also recognize that a plaintiff who has an appraisal remedy minus the costs of litigation is in fact worse off than a plaintiff without an appraisal remedy who can obtain an a class-wide award of quasi-appraisal damages plus the possibility of an award of attorneys' fees paid by the defendants.

In considering which model is most in keeping with the Supreme Court's teachings in this area, candor requires an acknowledgement that it is the Litigation-Cost Benefits of a class action that most often makes an unfair dealing claim so much more attractive than appraisal from a plaintiff's perspective, not the theoretical possibility of an award of (rarely granted) rescissory damages. Class actions and fee shifting are crucial if litigation is to serve as a method of holding corporate fiduciaries accountable to stockholders. Without them, collective actions problems would make it economically impractical for many meritorious actions to be brought.[29] Indeed, one wonders whether Andra could have found counsel to bring this lawsuit on a non-class action basis.

Choosing one of these models essentially boils down to a policy decision best made by a legislature, not a court. But the dilemma arises in this context not out of an ambiguity in the language of the Delaware General Corporation Law ("DGCL"),[30] but out of the understandable difficulty our

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[29]*Reappraising Appraisal*, at 11 ("The post-*Weinberger* [*v. UOP, Inc.*, Del. Supr. 457 A.2d 701 (1983)),] experience shows that for dissenting shareholders with relatively small. investments and unable independently to afford competent counsel the improved appraisal remedy remains ineffective. That is because *Weinberger* could not eliminate appraisal's structural problems, or the relative superiority of the damage class action, which offered reasonable attorneys' fees and the prospect of rescissory damages.")

[30]Nothing in 8 Del. C. § 262 expressly states that appraisal is an exclusive remedy. In this case, moreover, there is no tension between an unfair dealing action and other parts of the DGCL. Because Blount only gained his ability to consummate a § 253 short-form merger through an essentially unitary tender offer/back-end merger transaction, no contention can be made that permitting an unfair dealing action to proceed against him is inconsistent with the efficient, relatively process-free merger method § 253 contemplates. In a situation, by contrast, where a majority stockholder already holds sufficient shares to conduct a short-form merger *before* any of the conduct which the plaintiff attacks occurred, allowing an unfair dealing attack on the merger might well conflict with § 253 because it would require (through the burden-shifting rules applicable

courts have had in distinguishing between those situations in which a plaintiff should be limited to an appraisal remedy and those in which a plaintiff may also pursue an equitable action for breach of fiduciary duty.

This case presents that policy choice nicely. After all, if the unavailability of a class action and an attorneys' fee award renders appraisal an inadequate remedy for a plaintiff such as Andra who concedes that a fair value award is otherwise sufficient, that would create a clear *per se* rule that every well-pleaded claim that a merger is unfair as a result of fiduciary breaches may proceed on an equitable, non-statutory basis, alongside any appraisal action.[31] Put another way, if Andra may press an unfair dealing claim in this context, then any plaintiff with appraisal rights may also.[32]

Although the Supreme Court has never explicitly addressed the issue in this stark manner, *Rabkin* and *Cede* place a higher value on the full remediation of fiduciary breaches than they do on channeling claims into the more streamlined and confined appraisal remedy process — even when that process can make a plaintiff whole as to its claim (putting litigation costs to the side).[33] *Rabkin*, for example, stresses the need for a full remedy of the harm caused by "faithless acts" and "procedural unfairness" and emphasizes the anomaly that "stockholders who are eliminated without appraisal rights can bring class actions, while in other cases a squeezed-out minority is limited to an appraisal."[34] In this same vein, why should a plaintiff with appraisal rights be denied access to the Litigation-Cost Benefits of an unfair dealing action when a plaintiff without appraisal rights has access to those Benefits? And a forest-level reading of two of the Supreme Court's opinions in (the still-ongoing) *Cede* case shows the substantially greater weight the Supreme Court has given to a full remedy of fiduciary breaches than to considerations of judicial economy or litigation efficiency.[35]

The substantial procedural advantages of equitable actions has naturally led to a strong preference for such actions over the otherwise seemingly attractive (from a plaintiff's perspective) prospect of appraisal actions focused solely on a fair value remedy. Until legislative action is taken to make it more economically feasible for attorneys who represent

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under our law's business judgment rule and entire fairness standards) the majority stockholder to set up a special committee or to make the merger contingent on the support of a majority vote of the minority stockholders in order to avoid the burden of proving "entire fairness.". *See Kahn v. Lynch Communications Systems, Co.*, Del. Supr., 638 A.2d 1110, 1117 (1994).

[31]Subject to the caveat mentioned in note 30 for a "pure" short-form merger under 8 Del. C. § 253.

[32]Again, with the probable exception adverted to in notes 30 and 31.

[33]*See Wood*, mem. op. at 13, 1999 WL 504779, at *5.

[34]498 A.2d at 1107-08.

[35]*See Cede & Co. v. Technicolor, Inc.* ("*Cede I*"), Del. Supr., 542 A.2d 1182 (1988); *Cede II*, 634 A.2d at 367.

plaintiffs with small shareholdings to prosecute an appraisal action, such attorneys (and their clients) will continue to prefer, as a general matter, equitable actions over appraisal actions.[36] And because I can discern no reasoned basis, per *Rabkin* and *Cede*, to deny Andra access to a potential attorneys' fee award or a class-based sharing of litigation costs when a similarly situated plaintiff without appraisal rights would have such access, I conclude that she may proceed with her unfair dealing claim.

[14] An important caveat is in order, however. When Andra presents her class certification motion, which she is duty-bound to do promptly, I will give careful consideration as to whether Andra can represent a class including tendering stockholders. Because Andra has no standing to litigate the disclosure claims, it might be necessary to limit her to representing the non-tendering stockholders who are situated similarly to her. Absent an effective challenge to the disclosures in connection with the tender offer, tendering stockholders may well be subject to the defense that they are estopped from challenging the fairness of a transaction whose benefits they willingly accepted.[37]

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[36]An incisive article by Professor Randall S. Thomas advances several provocative ideas about how to reform the appraisal statute and better balance the competing policy interests at stake. *See* Randall S. Thomas, *Revising the Delaware Appraisal Statute*, 3 DEL. L. REV. 1, *passim*; *see also Reappraising Appraisal*, at 17 (advancing several possible reforms as a basis for legislative consideration).

As Professor Thomas's article suggests, however, such reform requires the type of comprehensive restructuring and authorial freedom legitimately exercisable only by the legislative branch of our government, with advice from the Delaware State Bar Association's Corporate Law Council. Given the complexity of the problems and the zero-sum nature of some of the necessary trade-offs, no one should be surprised if, in the absence of legislative action more clearly specifying the relative weight to be given to (seemingly rival) values such as litigative efficiency, transactional predictability, and fairness to minority stockholders, judge-made case law is not capable of sensibly and reliably balancing those values.

[37]*Bershad v. Curtiss-Wright Corp.*, Del. Supr., 536 A.2d 840, 848 (1987) (a party who voluntarily accepts the benefits of a transaction with knowledge of all material facts may not later challenge that transaction).

In noting this issue, I am by no means unaware of the effect such a decision could have on the feasibility of this action from the standpoint of Andra's counsel and the apparent logical inconsistency that lack of feasibility might create in view of my reasoning. If this feasibility problem arises, however, it will result from Andra's own tactical decision to drop her preliminary injunction motion and will be a case-specific problem that does not undermine the more generally applicable reasoning that undergirds my decision that plaintiffs like Andra may press unfair dealing claims. When the class certification motion is presented, these issues can be examined in greater depth, if necessary, with the fuller input of the parties.

IV. Conclusion

For the foregoing reasons, I grant the defendants' motion to dismiss Andra's disclosure claims and deny the defendants' motion to dismiss her unfair dealing claim. IT IS SO ORDERED.

CANTOR FITZGERALD, L.P. v. CANTOR

No. 16,297

Court of Chancery of the State of Delaware, New Castle

March 13, 2000

Plaintiff, a Delaware Limited Partnership, brought charges against limited partners claiming a breach of contractual and fiduciary duties embodied in their 1996 partnership agreement. The limited partners, as chief executive officer and controlling shareholder of a Delaware corporation, had entered into a licensing agreement to provide software for the brokerage of U.S. Treasury securities and were competing with the partnership, the main business of which was the brokerage of these securities. Additionally, a third party defendant corporation was charged with aiding and abetting these breaches of fiduciary duties and tortious interference with the contract between the limited partners and the partnership. Plaintiff sought permanent injunction, imposition of a constructive trust on third party's revenues, damages, various forms of declaratory relief, and attorney fees.

The court of chancery, per Vice Chancellor Steele, held that: (1) even though there was insufficient evidence to support the award of injunctive relief, other equitable relief, and ancillary money damages, the limited partners had breached their contractually imposed fiduciary duty of loyalty; (2) the defendant corporation had aided and abetted the limited partners' breach of fiduciary duty and interfered with the partnership agreement; and (3) the limited partners' egregious breach of the partnership agreement along with defendant corporation's was the type of conduct warranting an award of attorney and expert witness fees.

1. Contracts ⟹ 93(5), 94(1)
   Reformation of Instruments ⟹ 15, 19(1), 20

A court of equity will not grant reformation unless it can be demonstrated that the party seeking such form of relief acted under the influence of fraud or under a misapprehension resulting from mutual mistake.

2. Contracts ⟹ 93(1)
   Reformation of Instruments ⟹ 15, 19(1), 19(2)

A unilateral mistake cannot be a basis for reforming a contract.

3. Contracts ⟹ 93(1), 93(5)
   Reformation of Instruments ⟹ 15, 19(2), 20

When a unilateral mistake is accompanied not only by the other party's knowledge thereof, but also, by his silence, it is the equivalent of a mutual mistake; while not strictly a mutual mistake, equity will reform the instrument.

4. Contracts ⟹ 175(.5), 175(3)
   Evidence ⟹ 596(1)
   Reformation of Instruments ⟹ 45(2)

In order to prevail, a claim for reformation must be supported by clear and convincing evidence.

5. Contracts ⟹ 147(1)
   Reformation of Instruments ⟹ 16

In considering reformation claims, the court will focus on the parties' understanding at the time the agreements were drafted.

6. Reformation of Instruments ⟹ 1, 16

Reformation, when granted, reforms an agreement to match the expectation and understanding of the party seeking reformation; absent such an understanding, there can be no basis for reformation.

7. Fraud ☞ 58(1)
Reformation of Instruments ☞ 16, 20, 21, 45(2)

Even if defendants can be shown to have had an understanding that the agreements to be reformed provided what the defendants now seek to obtain through reformation of an agreement, to justify reformation, there must also be evidence that defendant's original understanding was fraudulently induced.

8. Reformation of Instruments ☞ 1, 10, 11, 15, 16

Contracts are not reformed to provide parties with bargains they failed to obtain through negotiations.

9. Contracts ☞ 143(2)

A contract is ambiguous only when the provisions in controversy are reasonably or fairly susceptible of different interpretations or may have two or more different meanings.

10. Contracts ☞ 143(2), 152, 175(.5), 175(2)
Evidence ☞ 448, 450(5)

When a partnership agreement is clear on its face, extrinsic evidence may not be considered.

11. Contracts ☞ 143.5, 147(3)

A section of a partnership agreement must be viewed in the proper context of the entire agreement.

12. Contracts ☞ 175(.5), 175(2)
Evidence ☞ 448, 450(5)
Partnership ☞ 22, 366

When the language of an agreement is clear on its face there is no need to resort to extrinsic evidence in order to understand its meaning.

13. Partnership ⚷ 353, 363, 366

Although a general partner may have the power to amend a partnership agreement, this general power may not be used to avoid express provisions of a settlement agreement.

14. Contracts ⚷ 143(2), 143.5, 147(3), 152

Where the meaning of a particular section of an agreement is unclear, the court examines the agreement as a whole in an attempt to ascertain that meaning.

15. Contracts ⚷ 143(2), 154

If an agreement is not ambiguous and if one party's interpretation is the only reasonable interpretation, it is the correct interpretation.

16. Contracts ⚷ 143(1)
Partnership ⚷ 352, 366

The basic approach of Delaware Revised Uniform Limited Partnership Act is to permit partners to have the broadest possible discretion in drafting their partnership agreements and to furnish answers only in situations where the partners have not expressly made provisions in their partnership agreement. DEL. CODE ANN. tit. 6, §§ 17-101 to 17-1111 (2000).

17. Contracts ⚷ 143(1)
Partnership ⚷ 352, 366

Because it does not specifically provide otherwise and because of its overall policy of freedom of contract, the Delaware Limited Liability Company Act was held to allow parties to agree in LLC agreement to vest exclusive jurisdiction in a foreign jurisdiction. DEL. CODE ANN. tit. 6, § 18-101 to 18-1009 (2000).

18. Partnership ⚷ 366

The Delaware Limited Liability Company Act and the Delaware Revised Uniform Limited Partnership Act are designed to give maximum effect to the parties' freedom of contract.

19. Partnership ⟹ 366, 370

Delaware courts have not found limited partners subject to default fiduciary duties in the absence of a fiduciary relationship.

20. Partnership ⟹ 366

In some cases, where a fiduciary relationship was found to exist, the court has found that limited partners may be subject to fiduciary duties.

21. Partnership ⟹ 366, 370

To the extent that a partnership agreement empowers a limited partner with discretion to take actions affecting governance of the limited partnership, the limited partner may be subject to the obligations of a fiduciary.

22. Partnership ⟹ 366

The limited partner owes a fiduciary duty of loyalty to the partnership and to the other partners when it controls the general partner through the votes of at least half of its directors.

23. Partnership ⟹ 363, 366

Even where a partnership agreement provides that the limited partners shall not participate in the operation, management or control of the partnership, to determine the limited partners power to affect the limited partnership's governance, the court will examine whether the limited partner has actually been involved in the governance and operation of the partnership or has been entitled to designate a majority of the general partner's board of directors.

24. Partnership ⟹ 366

Delaware law permits partners to agree on their rights and obligations to each other and to the partnership even where Delaware law might impose different rights and obligations absent such agreement. DEL. CODE ANN. tit. 6 , § 17-1101 (2000).

25. Contracts ⇐ 143(2), 175(.5), 175(2)
Evidence ⇐ 448
Partnership ⇐ 351, 366

Only when the partnership agreement is silent or ambiguous, or where principles of equity are implicated, will a court begin to look for guidance from the statutory default rules, traditional notions of fiduciary duties, or other extrinsic evidence.

26. Partnership ⇐ 351, 366

The court's reliance on statutory default and fiduciary duties is limited to situations where a partnership agreement establishes a fiduciary relationship.

27. Contracts ⇐ 143(2)
Equity ⇐ 21
Partnership ⇐ 351, 366

The court's reference to statute can be supported by equitable principles springing from a fiduciary relationship as well as a partnership agreement that was silent on the scope of the corresponding fiduciary duties.

28. Equity ⇐ 21

A fiduciary relationship can exist when one merely places trust in the faithful integrity of another, who as a result gains superiority or influence over the first; a fiduciary is one who owes to another the duties of good faith, trust, confidence, and candor.

29. Equity ⇐ 21
Partnership ⇐ 366

The duty of loyalty that parties may impose upon one another by mutual assent in a contract, whether management, operational, or governance responsibilities follow or not, is a mutual exchange of a promise to treat one another with good faith, trust, confidence, and candor.

30. Equity ☞ 21
Fraud ☞ 7

The duty of loyalty is a promise articulated to define a mutually agreed relationship explicitly beyond that of any implied duty of good faith in an ordinary contract.

31. Partnership ☞ 366

Upholding the right of partners to agree by a mutual exchange of dependent promises that they will not act in ways that threaten to destroy the common mission and purpose of the partnership upholds the Delaware Revised Uniform Limited Partnership Act's policy of affording partners the broadest possible discretion in drafting their partnership agreements.

32. Partnership ☞ 366

The scope of the duties owed by the parties must be determined by reference to the nature of a particular business enterprise.

33. Partnership ☞ 366

A company's existence and effectiveness depends upon its partners' loyalty to the partnership.

34. Torts ☞ 12

The elements of tortious interference are: (1) a valid contract, (2) defendants' knowledge of the contract, (3) an intentional act by defendants that is a significant factor in causing the breach of the contract, (4) lack of justification for defendants' acts, and (5) resulting injury.

35. Equity ☞ 21
Fraud ☞ 7
Partnership ☞ 366

The elements of aiding and abetting a breach of a fiduciary's duty are: (1) the existence of a fiduciary relationship, (2) a breach of the fiduciary's duty, (3) a knowing participation in the breach by the non-fiduciary defendant, and (4) resulting damages to plaintiff.

36. Contracts ⇐ 97(1), 97(2)
Estoppel ⇐ 89.1, 90(1)

Acquiescence arises where a complainant has full knowledge of his rights and the material facts and (1) remains inactive for a considerable time or (2) freely does what amounts to recognition of the complained of act or (3) acts in a manner inconsistent with the subsequent repudiation which leads the other party to believe the act has been approved.

37. Contracts ⇐ 316(1)
Estoppel ⇐ 52.10(1), 52.10(2)

Waiver is a voluntary and intentional relinquishment of a known right.

38. Contracts ⇐ 147(1), 236, 238(2)

Parties may modify a contract by conduct or words, but the alleged modification must be of such specificity and directness as to leave no doubt of the intention of the parties to change what they previously solemnized by formal document.

39. Equity ⇐ 10, 11, 12, 13, 21
Injunction ⇐ 22
Partnership ⇐ 363, 366

Without evidence that a defendant has caused specific quantifiable harm or that it currently unconscionably, fraudulently, or unfairly engaged in revenue producing enterprises upon which a constructive trust could be imposed, there can be no basis for extreme forms of relief, such as a permanent injunction or the removal of the offending limited partners from the partnership.

40. Equity ⇐ 21
Partnership ⇐ 70, 366

That a court finds insufficient quantifiable evidence that limited partners caused harm to the partnership that can be addressed by a specific monetary award of damages is irrelevant to the issue of whether they have breached their fiduciary duty of loyalty or have engaged in actions that caused harm.

41. Equity ☞ 54

Equity must try to right wrongs with adequate remedies that destroy no party in the process.

42. Equity ☞ 39(1)

Where the parties face the need to close the open issues arising from their legal relationship and to encourage predictable and acceptable conduct in the future, the appropriate focus on remedy should be a declaratory judgment which allows the parties to move forward after assessing the costs of past misjudgment about the relative rights of the parties to the offending actors.

43. Equity ☞ 3, 54

Equity arose from a distinct interest not only in redressing injury but in preventing and mitigating inequity where possible, and is more focused upon the specific nature of the dispute at hand and the promotion of reasonableness in the specific and particularized relationships.

44. Costs ☞ 194.16

The Delaware Court of Chancery follows the American rule which requires parties to bear their own litigation expenses except that the court may award fees where equity so provides.

45. Costs ☞ 194.16, 194.44

Fees can be awarded only when the party against whom the fees are assessed acted in bad faith, fraudulently, negligently, vexatiously, wantonly, or oppressively.

46. Costs ☞ 194.16, 194.44

To constitute bad faith, the defendants' action must rise to a high level of egregiousness.

47. Costs ☞ 194.16, 194.44

Actions may be egregious where defendants' position is indefensible or where no reasonable man or woman could differ on the outcome.

48. Costs ⟹ 194.16, 194.44
Customs and Usages ⟹ 19(1)

Defendants' bear the burden of proving by a preponderance of the evidence that their actions were justified by the parties' prior course of dealing.

49. Costs ⟹ 194.16, 194.44
Equity ⟹ 54

Bad faith is demonstrated where defendants forced the partnership into a position where it had no choice but to defend its business position by attack litigation in its most expensive form: a request for expedited injunctive relief; equity cannot condone such action.

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Saul B. Shapiro, Esquire, Marc S. Reiner, Esquire, and Susanne E. Rosenberg, Esquire, of Patterson, Belknap, Webb & Tyler LLP, New York, New York, of counsel, for defendant Rodney Fisher.

STEELE, *Vice Chancellor*

A Delaware corporation enters into a licensing agreement to provide software for the brokerage of U.S. Treasury securities. Its Chief Executive Officer and controlling shareholder are members of its Board of Directors as well as limited partners in a Delaware partnership whose core business is the brokerage of U.S. Treasury securities. In addition to other less salient claims, the partnership alleges that the limited partners have breached a contractually created fiduciary duty of loyalty. May the partners of a Delaware limited partnership agree in their partnership contract that all partners, including those limited partners who do neither manage, operate nor govern the partnership, should be subject to a fiduciary duty of loyalty? For the reasons below I conclude that they may. The limited partners have breached those fiduciary duties imposed upon them by contract and the corporate vehicle they used for this purpose aided and abetted those breaches and tortiously interfered with the Partnership Agreement. While I conclude that the partnership fails to carry its burden of persuasion that injunctive relief, other equitable relief, and ancillary monetary damages are appropriate to remedy its complaints of wrongdoing, the partnership is entitled to declaratory relief and an award of attorney's fees for an egregious breach of the partnership agreement.

I. Background

A. The Parties

Plaintiff Cantor Fitzgerald, L.P. ("CFLP" or the "Partnership") is a Delaware limited partnership that owns 99.5% of Cantor Fitzgerald Securities, a New York general partnership. Through this affiliate, CFLP is a leading inter-dealer and institutional broker of U.S. Treasury securities ("Treasuries") and other government securities. Counterclaim defendant CF Group Management, Inc. ("CFGM"), a New York corporation, serves as CFLP's managing general partner. Howard Lutnick ("Lutnick"), CFLP's President and Chief Executive Officer owns and operates CFGM.

Defendant Cantor Fitzgerald, Incorporated ("CFI"), a Nevada corporation, served as CFLP's managing general partner until January 2, 1996. CFI is a CFLP limited partner. Defendant Iris Cantor ("Cantor") is CFI's Chief Executive Officer and is the trustee of the Iris Cantor Trust, CFI's controlling shareholder. Under CFLP's partnership agreement dated August 28, 1996, (the "1996 Partnership Agreement"), Cantor is also a CFLP limited partner.

In 1987, CFLP's predecessor spun-off its Workstation Research Department to create Defendant Market Data Corporation ("MDC,"), a Delaware corporation. Cantor is a member of MDC's Board of Directors

and, as trustee of the Iris Cantor Trust, votes MDC's controlling shares. Defendant Rodney Fisher ("Fisher") is a shareholder of MDC and serves as its Chairman and Chief Executive Officer. He is also a CFLP limited partner. MDC is not a CFLP partner. Lutnick, also a shareholder of MDC, served on MDC's Board of Directors until June 1996.

B. Cantor Fitzgerald's Formative Years & the Development of its Data Business

Iris Cantor's late spouse B. Gerald ("Bernie") Cantor founded Cantor Fitzgerald[1] in 1945. In 1972, Cantor Fitzgerald acquired Telerate Systems, Inc. ("Telerate"). Through Telerate, Bernie Cantor created the practice of putting live bids and offers for government securities over a network, a practice referred to as "screen brokerage." Screen brokerage enabled market participants to see, in real time, the prices at which trades occurred. The advent of screen brokerage dramatically altered the Treasuries industry and positioned Cantor Fitzgerald as the world's leading broker of Treasuries.

In the mid-1980s Cantor Fitzgerald hired Fisher, formerly an employee of Telerate. With Andrew Seidel, another Cantor Fitzgerald employee, Fisher identified a business opportunity for Cantor Fitzgerald: to perform simple calculations on bids and offers displayed over the Telerate system and to sell the resulting information to the financial community. Bernie Cantor, intrigued by the business' prospects, housed the business in Cantor Fitzgerald's Workstation Research Department.

C. Cantor Fitzgerald Spins-Off its Workstation Research Department to Form MDC

In 1987, Cantor Fitzgerald spun-off its Workstation Research Department to form MDC. At the time Cantor Fitzgerald established MDC as an independent company, MDC engaged in a data enhancement business, selling information provided to it by Cantor Fitzgerald. MDC obtained information automatically provided by Cantor Fitzgerald's customers as they made trades through Cantor Fitzgerald and repackaged it into a useable form then sold to third parties.

The parties dispute the reason why Cantor Fitzgerald decided to spin-off its Workstation Research Department. CFLP maintains that Cantor Fitzgerald spun-off the Department to enhance its profitability and to avoid customer backlash. According to this theory, some of the customers who

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[1]"Cantor Fitzgerald" refers to the family of companies, other than MDC, owned or controlled by Bernie Cantor prior to the formation of CFLP in September 1992.

purchased data from the Department were the very same customers who provided the data, in raw form, for free by executing their trades through Cantor Fitzgerald. The continuation of this data enhancement business as part of Cantor Fitzgerald allegedly concerned dealers who feared that the dissemination of trading data would create pressure to narrow the "spread" between bids and offers and thereby reduce their profits. According to CFLP, transforming the Department into an independent MDC would preserve Cantor Fitzgerald's ability to profit from its data while making it easier to sell the data to its customers and reducing the risk of customer and dealer backlash.

Defendants, however, maintain that Cantor Fitzgerald spun-off the Workstation Research Department to enable the Department to conduct business with the entire financial community including Cantor Fitzgerald's competitors, many of whom would not conduct business with the Department while it was controlled by Cantor Fitzgerald. I do not consider the reasons for the spin-off proffered by CFLP and the Defendants to be inconsistent. Both proffers, taken together, are consistent with the goal of maximizing the Department's profits. Accepting Defendants' proffer does not, however, lead to the conclusion that CFLP spun-off the data enhancement business so that the new entity, MDC, could compete directly with Cantor Fitzgerald in its core line of business, brokering Treasuries. It does lead to the inescapable conclusion that, at that time, Cantor Fitzgerald did not object to data enhancement transactions with its competitors when the transactions were profitable and did not threaten harm to its core business.

D. Formation of CFLP

Until 1992, CFI operated as the holding company for Cantor Fitzgerald's businesses. On September 25, 1992, CFI, whose sole shareholders were Bernie and Iris Cantor, transferred essentially all of its assets to a new entity, the limited partnership CFLP, in exchange for a significant ownership interest in CFLP.[2] CFI became CFLP's initial Managing General Partner. CFI and CFGM were CFLP's only general partners. Bernie Cantor, other members of the Cantor Family, senior executives and employees of Cantor Fitzgerald and trusts set up by Bernie or Iris Cantor for family members held CFLP's limited partnership interests.[3]

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[2]Agreement of Limited Partnership of Cantor Fitzgerald, L.P., dated as of September 25, 1992, Section 6.01(b).

[3]Tr. Trans. Vol. II at 322; Pretrial Order at 10.

The partners amended CFLP's partnership agreement several times between 1992 and 1996.

E. The 1996 Litigation, Settlement Agreement and Amendments to the Partnership Agreement

In January 1996, following procedures set forth in Section 3.01(g) of the Agreement of Limited Partnership of Cantor Fitzgerald, L.P. dated May 23, 1995 ("1995 Partnership Agreement"), a committee of five persons selected by CFI determined that Bernie Cantor was "Incapacitated." Section 3.01(f) of the 1995 Partnership Agreement provided that, upon such a determination, CFGM would replace CFI as Managing General Partner with day-to-day control of CFLP and CFI would become a Co-Managing General Partner. Iris Cantor disputed the committee's determination.

The parties litigated the dispute in this Court and, on May 7, 1996, resolved their legal differences by entering into a settlement agreement after one day of trial (the "1996 Settlement Agreement"). The 1996 Settlement Agreement released their claims against each other and provided, *inter alia*, that CFI would withdraw as Managing General Partner and as a General Partner and would become "a Limited Partner for all purposes under the Partnership Agreement; *provided however* that CFI shall not thereby be deemed to have "withdrawn" for purposes of Section 9.02(d) of the Partnership Agreement."[4] CFGM became CFLP's sole Managing General Partner.

The parties to the 1996 Settlement Agreement agreed to amend the existing Partnership Agreement to reflect the terms of the 1996 Settlement Agreement.[5] CFGM authored the amendments and the resulting Agreement became the 1996 Partnership Agreement, which remains in effect at this time.

F. MDC's Dealings with Chicago Board Brokerage

On June 4, 1996, MDC held a board meeting to discuss the possible provision of broker system software to third parties. According to the draft

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[4]1996 Settlement Agreement ¶ 1 (emphasis in original). Section 9.02(d) of the 1995 Partnership Agreement states that a General Partner who has withdrawn from the Partnership may elect to have its General Partner Units converted into Limited Partner Units or to have its interest redeemed. It also states the consequences and conditions attached to either election.

[5]Section 2(d) of the 1996 Settlement Agreement provides that "the parties agree to take all steps necessary or appropriate to implement and effectuate the provisions of this Section 2, including executing such amendments to the Partnership Agreement not inconsistent with the terms of this Agreement as the Managing General Partner shall reasonably request. . . . To the extent applicable, this Agreement shall itself be deemed an amendment to the Partnership Agreement."

minutes of the meeting, Lutnick stated that "MDC's pursuit of these opportunities would be harmful to Cantor Fitzgerald."[6] The final minutes reflect that he stated that "MDC's pursuit of these opportunities would be a negative for Cantor Fitzgerald."[7] By fax and regular mail dated June 11, 1996, Lutnick sent a one sentence letter to Iris Cantor which stated: "I hereby resign from the Board of Directors of Market Data Corporation effective immediately."[8]

Defendant Fisher testified that MDC did not pursue the proposed business deals in the forms discussed at the June 4, 1996, meeting.[9] But CFLP soon heard rumors that some of the parties identified as possible business partners at the June 4, 1996, meeting were discussing development of an interactive trading system.[10] Between October 1997 and March 1998, CFLP executives visited trade shows where MDC promoted a product it touted as its Market Trader Broker System.[11]

In October 1997, CFLP's general counsel, Stephen M. Merkel, sent a letter to Cantor informing her that CFLP understood MDC was "designing an electronic trading system for U.S. Government Securities in cooperation with the Chicago Board of Trade" and that the activity constituted a breach of the Partnership Agreement.[12] Fisher, his legal counsel and legal counsel for MDC received copies of the letter. On February 9, 1998, MDC entered into a contract to license software for the MarketPower Broker System to Chicago Board Brokerage, L.L.C ("CBB").[13] MDC publicly announced the deal on March 19, 1998.

G. Commencement of This Litigation, Procedural History and Remaining Claims

On April 6, 1998, CFLP filed this action against Iris Cantor, CFI, Fisher, MDC and CBB. Shortly thereafter CFLP moved to enjoin preliminarily the launch of MarketPower. After a hearing on May 29 and July 6 -10, 1998, I concluded that CFLP had "a reasonable likelihood of establishing at a trial on the merits that defendant limited partners breached

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[6]PX56 at MDC030546.
[7]PX57 at MDC031209.
[8]DX899.
[9]Tr. Trans. Vol. XXXII at 6082-83.
[10]Pretrial Order at 11; DX86 No. 13; DX93 No. 52.
[11]Pretrial Order at 11.
[12]PX16.
[13]CBB is a Delaware limited liability company and a joint venture of Ceres Trading Limited Partnership, a limited partnership controlled by the Chicago Board of Trade, and Prebon Yamane (USA) Inc.; Pretrial Order at 12; PX23 (Licenses Between Chicago Board Brokerage, L.L.C. and Market Data Corporation dated Feb. 9, 1998).

their fiduciary duty of loyalty to the general partner and the partnership" but also found that "CFLP will not suffer imminent harm so damaging to its core business resulting from the breach of that duty of loyalty that it exceeds the harm to the defendants if they are enjoined from further development and use of MarketPower pending a final hearing."[14]

In the seventeen months following the preliminary injunction hearing, this Court decided dozens of motions, issued over thirty opinions, granted dozens of requests for telephone conferences to address evidentiary issues, and conducted a two-month trial. Several claims have been settled or dismissed.[15] Defendant CBB and Counterclaim Defendant Lutnick are no longer parties to this action. CFLP, Fisher, MDC and Cantor/CFI have submitted 12 post-trial briefs on three separate subjects: evidentiary issues, merits and harm/remedies. The Court held post-trial oral argument on December 6 and 7, 1999, and all outstanding, relevant, evidentiary issues were resolved in opinions dated January 10 and 13, 2000.

The remaining claims of the Third Amended Complaint allege (1) that Cantor, CFI and Fisher breached their contractual and fiduciary duties in Sections 3.03(a)-(b) of the 1996 Partnership Agreement, and (2) that Defendant MDC aided and abetted these breaches of fiduciary duties and tortiously interfered with the contract between CFLP, CFI, Cantor and Fisher. CFLP seeks in relief a permanent injunction, imposition of a constructive trust on MDC's revenues, damages, various forms of declaratory relief, and attorney's fees.

Counterclaimants, Defendants Fisher, Cantor and CFI (the "Limited Partner Defendants"), seek reformation of Section 3.03(b) of the 1996 Partnership Agreement. Defendants Cantor and CFI also seek various forms of declaratory relief, reformation of the 1996 Settlement Agreement and reformation of Section 3.03(a) of the 1996 Partnership Agreement. A counterclaim against CFLP and a third-party claim against CFLP's general

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[14]*Cantor Fitzgerald LP. v. Cantor*, Del. Ch., 724 A.2d 571, 574 (1998).

[15]On November 5, 1998, this Court dismissed CFLP's sixth cause of action against MDC for breach of a confidentiality agreement and CFLP's eight cause of action against CFI, Cantor and Fisher for tortious interference with a confidentiality agreement. *See Fitzgerald v. Cantor*, Del. Ch., C.A. No. 16297, Steele, V.C. (Nov. 5, 1998) and *Fitzgerald v. Cantor*, Del. Ch., C.A. No. 16297, Steele, V.C. (Dec. 30, 1998). On January 14,1999, this Court dismissed portions of CFLP's Counts II, IV and V alleging claims against CBB and further confidential information claims against the non-CBB Defendants. *See Fitzgerald v. Cantor*, Del. Ch., C.A. No. 16297, Steele, V.C. (Jan. 14, 1999). As a result, the part of CFI's and Cantor's First Counterclaim based on CFLP's allegation of misuse of confidential information is no longer ripe. On March 23,1999, this Court granted CFI and Cantor's motion to dismiss CFLP's ninth cause of action alleging improper transfer of shares of CFI. *See Fitzgerald v. Cantor*, C.A. No. 16297, Steele, V.C. (Mar. 23, 1999). Six days later, this Court granted CFLP's cross motion for summary judgment on CFI's and Fisher's books and records counterclaim. *See Fitzgerald v. Cantor*, Del. Ch., C.A. No. 16297, Steele, V.C. (Mar. 29, 1999).

partner CFGM assert breach of the implied covenant of good faith and fair dealing in connection with the 1996 Settlement Agreement.

This is the Court's Opinion on these remaining claims. As discussed below, I find that the 1996 Partnership Agreement is clear and unambiguous on its face, that it imposes both contractual and fiduciary duties on the Limited Partner Defendants, that the Limited Partner Defendants' actions breached these duties, that MDC aided and abetted the Limited Partner Defendants' breach of fiduciary duty, that MDC tortiously interfered with the 1996 Partnership Agreement and that Plaintiff CFLP is entitled to declaratory relief and an award of attorney's fees. Because resolution of the Limited Partner Defendants' claims of reformation do not affect the final disposition of the case, these claims are addressed first below.

II. Limited Partner Defendants' Reformation Counterclaims

CFLP contends that Section 3.03 of the 1996 Partnership Agreement prohibits CFI and its Affiliates from engaging in "Competitive Activities."[16] Iris Cantor and CFI seek, in the event this Court concludes that CFLP's interpretation of the 1996 Partnership Agreement is correct, to have the Court reform Sections 3.03(a)-(b) of the 1996 Partnership Agreement to provide that CFI and its Affiliates may engage in Competitive Activities subject only to the economic consequences set forth in Article XI and to other provisions of the 1996 Partnership Agreement. They also seek reformation of the 1996 Settlement Agreement to provide: (1) that CFI is not subject to any obligations imposed by Section 3.03(a) that do not also apply to other limited partners; (2) that, to the extent that Section 3.03(b) subjects CFI to any duty to refrain from engaging in Competitive Activities, Article XI provides the partnership's sole remedies; and, (3) that MDC is entitled to all the protections provided to "Affiliated Entities."[17] Defendant Fisher seeks to reform Section 3.03(b) in a fashion similar to that sought by cantor and CFI except that, rather than have Section 3.03(b) reformed to provide that he may engage in Competitive Activities, he seeks reformation to be able to act "as chairman and CEO of MDC in connection with MDC's business with CFLP's competitors, including CBB" without violating Section 3.03(b).[18]

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[16]The definition of "Competitive Activities," a defined term in the 1996 Partnership Agreement, is discussed below at Section III A.

[17]"Affiliated Entities," a defined term in the 1996 Partnership Agreement, refers to the group of entities owned, controlled or under common control with CFLP. *See* 1996 Partnership Agreement, Section 1.01.

[18]Rodney Fisher's Answer to Plaintiff's Third Amended Complaint, Affirmative Defenses and Counterclaims ¶ 53 (hereinafter Fisher's Answer).

[1-4] A Court of Equity will not grant reformation "unless it can be demonstrated that the party seeking such form of relief acted under the influence of fraud or under a misapprehension resulting from mutual mistake."[19] "A unilateral mistake cannot be a basis for reforming a contract."[20] When a unilateral mistake, however, "is accompanied not only by the other party's knowledge thereof, but, also, by his silence, it is said to be equivalent to a mutual mistake; at any rate, while strictly not a mutual mistake, equity will reform the instrument."[21] To prevail, the claim for reformation must be supported by clear and convincing evidence.[22]

Defendants' counterclaims for reformation assert: (1) that at the time the relevant Agreements were drafted, Defendants believed the Agreements provided the protections they now seek to obtain through reformation; and, (2) that, at the time of drafting, CFLP knew Defendants' beliefs and withheld from Defendants the fact that the Agreements did not match Defendants' expectations. During discovery, however, before they added their reformation claims, Defendants repeatedly stated that they did *not* have an understanding of the terms of the Agreements when they were drafted. Despite some rather elegant courtroom sophistries emanating from the mouths of well-prepared witnesses for Defendants, those entirely believable admissions during discovery failed to transmute into clear and convincing contrary evidence at trial.

A. CFI's and Cantor's Alleged Understanding of the Agreements

On October 28, 1998, the same day on which this Court granted Defendants' motions to add claims for reformation,[23] in response to CFLP's interrogatory that asked when Cantor concluded that the Partnership Agreement limited CFI's right to compete and subjected CFI to the provisions of Article XI, Cantor responded that: "Mrs. Cantor does not have an independent understanding of the Partnership Agreement or its amendments."[24]

Prior to adding their claims for reformation, Cantor and CFI asserted that they, as of May 1, 1998, had a "current lay understanding" that the change in MDC's Affiliated Entity status adversely affected their economic

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[19]*Gracelawn Memorial Park, Inc. v. Eastern Memorial Consultants, Inc.*, Del. Ch., 280 A.2d 745, 748 (1971), *aff'd*, Del. Supr., 291 A.2d 276 (1972).

[20]*Matter of Enstar Corp.*, Del. Supr., 604 A.2d 404, 413 (1992).

[21]*Colvocoresses v. W. S. Wasserman Co.*, Del. Ch., 28 A.2d 588, 589-90 (1942) (citations omitted).

[22]*Id.* at 590.

[23]*Fitzgerald v. Cantor*, Del. Ch., C.A. No. 16297, Steele, V.C. (Oct. 28, 1998).

[24]PX 179 at No. 11.

interests, that Section 3.03(a) does not impose a duty on CFI and its Affiliates to refrain from engaging in Competitive Activities, and that Section 3.03(b) does not impose liability on Cantor for using MDC to engage in Competitive Activities.[25] In her affidavit dated January 9, 1999, however, Cantor noted that during her deposition she testified that her "lay understanding of [her] rights and obligations under the CFLP Partnership Agreement was based solely on conversations with [her] attorneys" and testified that the "statements that [she] made about [her] lay understanding were all based on conversations with the Slotnick Firm after CFI entered into the [1996] Settlement Agreement."[26] Cantor did not retain the Slotnick firm until after she signed the 1996 Settlement Agreement. The attorneys who interacted with Cantor did not have any communications regarding "the CFI Defendants' rights under the Partnership Agreement, the Settlement Agreement or otherwise, to cause or permit MDC or any of Defendants' other Affiliated Entities, to engage in Competitive Activities" or "MDC's continued classification as an Affiliated Entity after execution of the Settlement Agreement" before she signed the 1996 Partnership Agreement on August 28, 1996.[27] Therefore, Cantor and CFI have expressly denied any contemporaneous knowledge about the effect of Sections 3.03(a) or (b), the right of CFI or its Affiliates to engage in Competitive Activities or the effect of MDC's classification as an Affiliated Entity.

Despite these express denials, Cantor asserts that she had a general understanding that, as consideration for the 1996 Settlement Agreement's terms favorable to CFGM that she would achieve a "free, independent, strong company, and that [she] would be going home with something that [she] could make into a wonderful company."[28] The basis for this understanding is a discussion between Cantor and Lutnick over lunch at the Hotel du Pont in Wilmington, Delaware. Cantor testified that Lutnick asked her to trust him and assured her that he would "never harm MDC."[29] Cantor does not contend that Lutnick informed her that MDC either would or would not be allowed to compete. Cantor, in fact, repeatedly denied that Lutnick said anything about MDC's right to compete.[30] She also confirmed that her

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[25]PX178 at Nos. 28, 40 and 44.

[26]Cantor Aff. 1/9/99 ¶¶ 2, 5.

[27]Slotnick Aff. 2/3/99 ¶ 3; Crocker Aff. 2/3/99 ¶ 3.

[28]Tr. Trans. Vol. XXVI at 5043.

[29]*Id.* at 5032.

[30]Cantor was asked whether Lutnick told her "anything that would cause [her] to believe that MDC did not have the ability to enter into competitive activities." Cantor responded: "No." Tr. Trans. Vol. XXVI at 5032. Cantor was asked whether Lutnick "mention[ed] MDC and competitive activities in any manner, form or shape during the course of the meeting." Cantor responded: "No. Mr. Lutnick never mentioned that." *Id.* at 5033. Cantor also testified that "Mr. Lutnick never explained anything to me about MDC. I wasn't there to talk about MDC." *Id.* at

belief that MDC would be independent and free to compete was based on her previously existing understanding of the relationship between MDC and CFLP and not on any events that occurred during that time period.[31] Nonetheless, she testified that at the time she signed the 1996 Settlement Agreement, she believed that MDC had the right to do business with CFLP's competitors.[32]

B. Fisher's Alleged Understanding of the Agreements

On October 28, 1998, the same day on which I granted Fisher's motion to add a claim to reform Section 3.03(b) "so that Fisher's actions as Chairman and CEO of MDC in connection with MDC's business with CFLP's competitors, including CBB, are not violative of [Section 3.03(b)] of the Partnership Agreement,"[33] Fisher answered CFLP's interrogatory that asked whether "doing business with competitors of Cantor Fitzgerald" constitutes "Competitive Activity" under the Partnership Agreement. Fisher objected on the bases of attorney-client privilege and work-product doctrine but also asserted under oath that "Mr. Fisher has no independent understanding of the Partnership Agreement."[34] Between May and October 1998, Fisher provided the identical answer to at least ten additional requests seeking information on topics that included whether amendments to the Partnership Agreement (including the amendment to change MDC's status as an Affiliated Entity) adversely affected Partners and whether Fisher is bound by the Partnership Agreement.[35] A short time later he confirmed that, even as of November 1998, he still had "no independent understanding of the specific provisions of the Partnership Agreement."[36]

In marked contrast to his discovery responses, Fisher stated at trial that he had an understanding that "MDC, from the day we were founded on August 1, 1987, was free to do business with the entire financial community and that, of course, included Cantor Fitzgerald's competitors."[37] Fisher's understanding is based on his contention that MDC had engaged in

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5043. *See also*, Pretrial Order at 12 (all parties stipulated that "[a] t no time during the negotiations leading to the May 7,1996 Settlement Agreement among CFI, CFLP and CFGM . . . did the parties . . . discuss MDC's right or ability to compete with CFLP while CFI remained a Partner of CFLP").

[31]*See* Tr. Trans. Vol. XXXV at 6566 (Cantor confirmed that "it wasn't anything that happened in that time frame, in May, that led [her] to believe [she was] getting a free MDC" and that that was "something that [she] thought [she] always had.").

[32]Tr. Trans. Vol. XXVII at 5050.

[33]Fisher's Answer ¶ 53.

[34]PX26 at Response 1.

[35]*See, e.g.*, PX 183 Nos. 3, 4, 6, 28-30, 41-42; PX 184 Nos. 17-18.

[36]PX 186 at No. 19.

[37]Tr. Trans. Vol. XXXI at 5937.