Plainly, Boyce's conduct does not meet this difficult standard. In the absence of a special fee shifting provision in the contract signed by him, I will not require Boyce to pay RHIS's fees relating to this litigation.

IV. CONCLUSION

For the reasons stated above, plaintiff's claim for permanent injunctive relief for violation of the non-compete covenant is DENIED. Plaintiff's claim for permanent injunctive relief on the non-solicitation agreement is GRANTED in part, and damages allowed to the extent specified in this opinion. Plaintiff's claim for an award of attorney's fees is DENIED.

Plaintiff should submit an appropriate form of order on notice within 10 days of the date of this opinion.

SAITO v. McKESSON HBOC, INC.

No. 18,553

Court of Chancery of the State of Delaware, New Castle

July 10, 2001

Pamela S. Tikellis, Esquire, and Robert J. Kriner, Jr., Esquire, of Chimicles & Tikellis, LLP, Wilmington, Delaware; Robert S. Green, Esquire, and Robert A. Jigarjian, Esquire, of Girard & Green LLP, San Francisco, California, of counsel, for plaintiff.

Thomas J. Allingham II, Esquire, Anthony W. Clark, Esquire, and Paul J. Lockwood, Esquire, of Skadden, Arps, Slate Meagher & Flom LLP, Wilmington, Delaware; Jonathan J. Lerner Esquire, of Skadden, Arps, Slate Meagher & Flom LLP, New York, New York, of counsel; and James E. Lyons, Esquire, of Skadden, Arps, Slate Meagher & Flom LLP, San Francisco, California, of counsel, for defendant.

CHANDLER, *Chancellor*

The plaintiff, Noel Saito, is currently a shareholder of record of McKesson HBOC, Incorporated ("McKesson HBOC" or "defendant"). Through this action, he seeks, pursuant to 8 *Del. C.* § 220, court-ordered access to certain books and records of the defendant. A trial was held on May 7, 2001. This Opinion constitutes my decision in the case.

I. FACTS[1]

A. The Merger

On October 17, 1998, McKesson Corporation ("McKesson"), HBO & Company ("HBOC"), and McKesson Merger Sub, Incorporated entered into an Agreement and Plan of Merger that provided for McKesson's acquisition of HBOC in a stock-for-stock transaction. The transaction closed on January 12, 1999, and the name of the combined company was changed to McKesson HBOC, Incorporated ("McKesson HBOC"). The plaintiff purchased his original McKesson shares on October 20, 1998, and continues to hold McKesson HBOC shares today.

B. The Restatement

Three months after the merger, in April 1999, McKesson HBOC publicly announced that its auditors had discovered certain accounting irregularities in HBOC's financial records. Specifically, the auditors found that certain contingent software sales at HBOC had been recorded as revenue despite the contingencies. Ultimately, on July 14, 1999, McKesson HBOC announced that it would have to restate its financial statements in a total amount that exceeded $325 million.

C. The Aftermath

Shortly after the announcement of the restatement, plaintiffs in several jurisdictions filed lawsuits against both McKesson HBOC and its subsidiary HBOC. One such lawsuit is a currently-pending derivative

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[1]I limit my recitation to only those facts germane to the present dispute. Thus, some of the details of the transactions and the parties will be discussed in a very abbreviated manner. For a complete and detailed description of the facts, see my discussion in the related case, *Ash v. McCall*, Del. Ch., C.A. No. 17132, Chandler, C. (Sept. 15, 2000), mem. op. "Sept. Decision").

action filed in this Court by the plaintiff and several other plaintiffs. This lawsuit is captioned *Ash v. McCall* and has been assigned Civil Action Number 17132. On September 15, 2000, this Court issued its Opinion regarding the then-pending motions to dismiss the *Ash* case.[2] In that Opinion, the Court dismissed all of the plaintiffs' claims but granted leave to amend the complaint to reassert certain claims not dismissed with prejudice. Moreover, the Court invited the plaintiffs to use the "tools at hand . . . to develop additional particularized facts in order to allege properly an oversight claim that will meet the demand futility standard and to avoid the standing requirement of Delaware's continuing ownership rule."[3]

Of the multiple plaintiffs in the *Ash* case, one chose to heed the Court's advice and demanded access to corporate books and records under 8 *Del. C.* § 220. After several procedurally deficient attempts, on February 7, 2001, the plaintiff served the defendant with a proper demand letter demanding access to certain of the defendant's books and records.

In the demand letter, the plaintiff stated the purpose for making the demand as follows:

> The examination and inspection of the books and records demanded herein is requested for the purpose of enabling Mr. Saito, through his duly empowered attorneys: (1) to further investigate breaches of fiduciary duties by the boards of directors of HBO & Co., Inc., McKesson, Inc., and/ or McKesson HBOC, Inc. related to their oversight of their respective company's accounting procedures and financial reporting; (2) to investigate potential claims against advisors engaged by McKesson, Inc. and HBO & Co., Inc. to the acquisition of HBO & Co., Inc. by McKesson, Inc.; and (3) to gather information relating to the above in order to supplement the complaint in Ash v. McCall. et al., C.A. No. 17132 in accordance with the September 15, 2000[,] Opinion of the Court of Chancery of Delaware.[4]

To foster those three purposes, the plaintiff seeks access to the following eleven categories of books and records:

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[2]*See Ash v. McCall, supra*, n. 1.
[3]*Id.* at 47.
[4]Pl.'s Trial Ex. 6.

1. All sales agreements and documents related to sales agreements (including documents, which have been referred to as "side letter," containing terms and conditions of any agreements not included within the agreement itself) between HBO & Co. ("HBOC") or [McKesson HBOC, Inc.] and [33 certain specified entities identified in actions filed by the Securities Exchange Commission and the Department of Justice.]

2. All documents evidencing communications between the following persons and entities or representatives thereof regarding: (i) "side letters"; (ii) backdating of sales contracts; (iii) sales contingent upon terms not contained within the main sales contract; or (iv) accounting practices at HBOC, McKesson HBOC, or HBOC and the post-merger subsidiary of the Company ("HBOC sub"):

a. HBOC or HBOC sub and any [of the 33 entities identified in the first request];

b. Arthur Andersen and any entities identified in [Request No. 1] above;

c. Bear Sterns and any entities identified in [Request No. 1] above;

d. Arthur Andersen and [B]ear Stearns;

e. Arthur Andersen and Deloitte & Touche;

f. Bear Stearns and HBOC or HBOC sub;

g. Arthur Andersen and HBOC or HBOC sub; and

h. Deloitte & Touche and HBOC or HBOC sub.

3. All documents concerning Arthur Andersen's pre-merger review of the internal controls of HBOC.

4. All documents concerning verification by Arthur Andersen of any representations about revenues and/or expenses made by HBOC management during the due diligence process in preparation for or in connection with HBOC's merger with McKesson, Inc. (McKesson").

5. All documents related to or reflecting the verification by McKesson, its employees, directors or advisors that the revenues and/or expenses reported in the financial statements of HBOC that were incorporated by reference in the amended joint proxy statement, issued in connection with the merger

between McKesson and HBO & Co., were properly and accurately reported.

6. All documents reflecting the reaction of an [sic] discussions among or communications with any members of the Board of Directors of HBOC, McKesson or McKesson HBOC concerning (i) reports dated April 14, 19997 [sic] and August 19, 1998[,] by the Center for Financial Research and Analysis (CFRA); (ii) any other published public analysis of the accounting practices of HBOC prior to and following HBOC's merger with McKesson; (iii) any public response to such published reports by any employee of HBO & Co.; or (iv) any HBOC, McKesson or McKesson HBOC shareholder reaction to such published reports.

7. All documents relating to or reflecting communications among of [sic] between members of HBOC management and/ or HBOC's board of directors concerning HBOC's purpose in pursuing a merger with McKesson or any other entity between January 1, 1997[,] and October 17, 1998.

8. All documents concerning the decision to change the structure of the merger of HBOC and McKesson from a "merger of equals" to an acquisition of HBOC by McKesson.

9. All documents, including board minutes or other documents evidencing any communications with or among HBOC's or McKesson HBOC's Board of Directors related to the termination or resignation of the following individuals: Jay Gilbertson, Albert Bergonzi, Charles W. McCall, Mark A. Pulido, David Held, Jay Lapine, Michael Smeraski and Dominick DeRosa.

10. All documents concerning SEC, Department of Justice or any other governmental agency investigation of any individual listed in Request No. 9 above, or any other employee of HBOC, McKesson, McKesson HBOC or HBO sub between January 1, 1997 and the present.

11. All documents reflecting discussions among or communications with McKesson HBOC's management or members of its Board of Directors about whether to initiate litigation against any past or present employee of HBOC, McKesson HBOC or HBO sub or against any advisor to or auditor of any of the foregoing entities in connection with the

restatements of HBOC's and/or the Company's financial results for fiscal year 1997, 1998 and 1999.[5]

In general, the defendant objected to producing most, if not all, of the categories of documents and records the plaintiff seeks. Despite the continuing objections, it did eventually supply the plaintiff with approximately 1000 pages of documents to which it believed the plaintiff was entitled had he a proper purpose (which the defendant argues he does not). The documents produced consisted of: (1) certain minutes from the meetings of the McKesson HBOC Board; (2) certain minutes from the meetings of the McKesson HBOC audit committee; (3) tolling agreements between McKesson HBOC and numerous third parties that protect McKesson HBOC's litigation rights; (4) employment and termination agreements between McKesson HBOC and former employees identified in the demand; (5) correspondence relating to McKesson HBOC's retention of its auditors; and (6) reports to the McKesson HBOC Board regarding auditing or accounting issues.

The defendant argues that the plaintiff is not entitled to other books and records because they are beyond the scope of his asserted purposes; the plaintiff is not entitled to documents relating to claims which he has no standing to pursue; the plaintiff is not entitled to documents from the wholly-owned, and legally distinct, subsidiary HBOC; and, the plaintiff is not entitled to records of third parties that the defendant has in its possession as a result of formal and informal discovery in various lawsuits.

The parties have fully briefed their respective arguments and the matter was tried before the Court on May 7, 2001. This is my post-trial decision.

II. ANALYSIS

The Delaware General Corporation Law expressly provides shareholders with the right to inspect the books and records of the corporations in which they have an ownership interest.[6] This right,

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[5] *Id.*

[6] 8 *Del. C.* § 220(b) provides in pertinent part that:

> Any stockholder, in person or by attorney or other agent, shall, upon written demand under oath stating the purpose thereof, have the right during the usual hours for business to inspect for any proper purpose the corporation's stock ledger, a list of its stockholders, and its other books and records, and to make copies or extracts therefrom. A proper purpose shall mean a purpose reasonably related to such person's interest as a stockholder.

however, is not absolute. A shareholder seeking access to the corporation's books and records must demonstrate (1) that the shareholder has demanded inspection of the records in the proper form and manner, and (2) that the shareholder has a proper purpose for making such a demand.[7] A "proper purpose" means "a purpose reasonably related to such person's interest as a stockholder."[8]

If the Court finds that the shareholder has a proper purpose for making such a demand, the Court must determine the scope of the relief that shall be granted. "In determining the scope of inspection relief, the overriding principle is that only those records that are 'essential and sufficient' to the shareholder's purpose will be included in the court-ordered inspection."[9] The plaintiff bears the burden of meeting this standard.[10] The scope of inspection afforded shareholders under this statute is narrowly tailored and is less far-reaching than typical discovery under Court of Chancery Rules.[11]

After some initial skirmishes concerning the form and manner of the demand, there are no longer disputes as to the procedural propriety of the present demand. Rather, the defendant primarily challenges the plaintiff's purported purposes and the scope of relief to which he is entitled, if any.

The plaintiff has asserted three purposes for his demand.[12] All three center around investigating and "ferreting out" allegations of wrongdoing regarding the merger of HBOC and McKesson. While there is one central theme to the three purposes, the plaintiff directs the inquiry towards two

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[7]*See* 8 *Del. C.* § 220(c). *See also Security First Corp. v. U.S. Die Casting and Dev. Co.*, Del. Supr., 687 A.2d 563, 566-67 (1997).

[8]8 *Del. C.* § 220(b).

[9]*Helmsman Management Services, Inc. v. A & S Consultants, Inc.*, Del. Ch., 525 A.2d 160, 167 (1987). *See also Security First Corp.*, 687 A.2d at 570.

[10]*Thomas & Betts Corp. v. Leviton Mfg. Co., Inc.*, Del. Supr., 681 A.2d 1026, 1035 (1996).

[11]*See Carapico v. Philadelphia Stock Exchange, Inc.*, Del. Ch., C. A. No. 16764, Lamb, V. C. (Sept. 27, 2001), mem. op. at 10, n.13.

[12]The defendant has expended great energy in arguing that the plaintiff, at deposition, has disavowed his proffered purposes in his demand letter. I find that defendant's narrow reading of his deposition testimony is unwarranted and somewhat misleading. Reading his deposition as a whole, I find that the plaintiff was, and is, concerned by the possible wrongdoing that might be the cause for the restatements. Thus, reading the record as a whole, I am convinced that the plaintiff has not disavowed the purposes set forth in the demand letter. *See Security First Corp.*, 687 A.2d at 567-68 ("The failure of plaintiff's key witness to articulate certain 'magic words' while testifying at trial is not fatal.... [W]e understand that the trial court considered the totality of the trial record in making its findings. Accordingly, we find that the Court of Chancery properly relied on all of the evidence adduced at trial" in determining whether the plaintiff had a proper purpose for making a demand.)

different groups: the various boards of directors and the advisors to those boards.

It is well settled that the investigation into corporate waste and mismanagement is a proper purpose for a books and records inspection under § 220.[13] Moreover, "a stockholder may demonstrate a proper demand for the production of corporate books and records upon a showing, by a preponderance of the evidence, that there exists a credible basis to find probable corporate wrongdoing. The stockholder need not actually prove the wrongdoing itself by a preponderance of the evidence."[14] The plaintiff's request will fail to meet this standard if it evinces a "mere curiosity or desire for a fishing expedition. But the threshold may be satisfied by a credible showing, through documents, logic, testimony, or otherwise, that there are legitimate issues of wrongdoing."[15]

I find that the record in this case evinces credible evidence of possible wrongdoing. McKesson HBOC was forced to restate its financial statements to reflect accounting irregularities totaling $325 million. This led to the public admission of the irregularities, the termination of certain high-ranking executives, and the institution of criminal proceedings by federal authorities. While the ultimate involvement or culpability, if any, of the defendant in this wrongdoing is unclear on this record, the plaintiff has met his burden at this stage to gain access to books and records to examine the defendant's conduct. Thus, to the extent that the plaintiff seeks access to the books and records of the defendant to foster this purpose, in general, I find that he has set forth a proper purpose for a demand. The full breadth of my finding, however, is limited.

First, for reasons discussed below, I find that this plaintiff has asserted a proper purpose for examining potential wrongdoing only as to the McKesson board, and the resulting McKesson HBOC board, from the time he purchased his stock. Thus, the plaintiff has not asserted a proper purpose for examining potential wrongdoing by the HBOC board or the McKesson board prior to the purchase of his shares. Moreover, for reasons also discussed below, I am not persuaded that this books and records action against McKesson HBOC is the appropriate vehicle for examining potential claims against non-party advisors involved in counseling the boards involved in the merger, and, thus, he is not entitled to books and records solely designed for that purpose.

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[13] *Security First Corp.*, 687 A.2d at 567.

[14] *Id.* at 565.

[15] *Id.* at 568. *See also Thomas & Betts, supra*, showing that this purpose must be supported by credible record evidence.

For reasons unknown, this plaintiff, Saito, is the only plaintiff from the *Ash* case to file a books and records action. This is important because the original *Ash* plaintiffs counted among their number shareholders of all the various companies involved in this litigation. Saito, however, only purchased his shares three days after the acceptance of the merger agreement and, thus, held shares originally in McKesson and now in McKesson HBOC. He was never a shareholder of HBOC.

As I noted in the *Ash* opinion:

> Section 327 of Delaware's General Corporation Law requires a shareholder plaintiff asserting derivative claims to allege that he was a stockholder of the corporation at the time of the transaction of which he complains. In addition to this statutory requirement, it is also settled law in Delaware that a derivative plaintiff must be a stockholder at the time he commences suit and must maintain such stockholder status throughout the course of litigation. This is known as the continuous ownership requirement.[16]

Because this plaintiff, as the sole plaintiff in this action, cannot satisfy the continuous ownership requirement for bringing and maintaining a derivative suit against either HBOC or McKesson for conduct occurring before his purchase of McKesson shares, he has not shown that he has a proper purpose for investigating acts prior to that time and is not entitled to books and records designed to examine that pre-purchase conduct.[17]

Moreover, plaintiff has offered no affirmative authority that would sanction the use of a § 220 action against a company to attempt to develop a separate and distinct cause of action against financial advisors to that company during a transaction. As noted above, I have found that the investigation of possible wrongdoing is a proper purpose. It is also well-settled that a secondary "improper" purpose is generally irrelevant and not fatal.[18] Here, however, rather than seeking documents for a proper purpose that might also happen to support an improper purpose, the plaintiff seeks categories of documents that go directly towards examining the conduct of certain advisors with the purported intent of developing claims against

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[16]*Ash v. McCall*, Del. Ch., C.A. No. 17132, Chandler, C. (Sept. 15, 2000), mem. op. at 31 (internal citations omitted).

[17]*Accord, Landgarten v. York Research Corp.*, Del. Ch., C.A. No. 8417, Berger, V.C. (Feb. 3, 1988).

[18]*See Carapico v. Philadelphia Stock Exchange, Inc.*, Del. Ch., C.A. No. 16764, Lamb, V.C. (Sept. 27, 2000); *Skouras v. Admiralty Enterprises, Inc.*, Del. Ch., 386 A.2d 674 (1978).

them. In this fashion, plaintiff has invoked his books and records statutory right as a vehicle for obtaining discovery implicating potential claims against third parties. Plaintiff offers nothing to support this use of § 220.

In summary, I conclude that this plaintiff has demonstrated a proper purpose in seeking to investigate corporate wrongdoing by the then-McKesson and now McKesson HBOC boards for acts or conduct by them following the purchase of his shares on October 20, 1998.

Having found that the plaintiff has identified a proper purpose for an inspection of the corporate books and records, the Court must now determine the scope of the relief that shall be granted. "In determining the scope of inspection relief, the overriding principle is that only those records that are 'essential and sufficient' to the shareholder's purpose will be included in the court-ordered inspection."[19] The plaintiff bears the burden of meeting this standard.[20]

Because the scope of this plaintiff's "proper purpose" is limited as noted above, the scope of the examination to which he is entitled will similarly be quite limited. The plaintiff is effectively limited to examining conduct of McKesson and McKesson HBOC's boards *following* the negotiation and public announcement of the merger agreement. Thus, the scope of the examination will be limited to only those documents, or categories of documents, "necessary and sufficient" to foster that purpose. By this, I mean that the plaintiff, regardless of the denominated categories in his demand letter, is entitled to examine any books and records of McKesson and McKesson HBOC designed to ferret out possible wrongdoing by the boards of these two companies. This inspection, however, is temporally limited to those books and records reflecting the boards' conduct following his purchase of McKesson stock on October 20, 1998.

The scope of the plaintiff's Court-awarded inspection of books and records is also limited to those books and records of the company in which he owns, or owned, shares, here McKesson and McKesson HBOC. HBOC and HBOC sub are separate, subsidiary corporations from the parent McKesson HBOC. I do not find that the plaintiff has provided any evidence that the subsidiary was created to perpetrate fraud or that it is a mere alter ego of the parent, thus warranting disregard for its existence as a separate legal entity.[21] Ultimately, while McKesson HBOC, as the parent,

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[19]*Helmsman*, 525 A.2d at 167. *See also Security First Corp.*, 687 A.2d at 570.

[20]*Thomas & Betts Corp.*, 681 A.2d at 1035.

[21]*See Carpico, supra*, mem. op. at 11; *Skouras*, 386 A.2d at 681; *Landgarten, supra*. The defendant, in its brief, argues that this Court's recent decision in *Salovaara v. SSP, Inc.*, Del. Ch., C.A. No. 18903, Chandler, C. (Jan. 10, 2001), let. op., changes the law in this area by

may have certain books and records of its subsidiaries in its custody or control, the plaintiff's inspection is limited to the books and records of the parent, McKesson or McKesson HBOC.

III. CONCLUSION

I find that the plaintiff's proffered purpose for his demand, to examine allegations of corporate misconduct, is a proper purpose. That finding, however, is limited to the plaintiff's examination of corporate conduct following the purchase of his McKesson shares. Moreover, because he would lack standing to challenge the conduct of the HBOC and McKesson boards prior to his stock ownership, he has not shown that he has a proper purpose for investigating that same conduct. Plaintiff also has failed to persuade the Court that using a § 220 action against a company in which he owns shares is a proper vehicle for examining the conduct of third-party advisors to the company with the ultimate view of filing separate actions against the third-party advisors.

Finally, the scope of plaintiff's Court-ordered inspection is limited to those books and records of McKesson or McKesson HBOC designed to investigate conduct by the respective boards following the purchase of his shares. The parties are to work together, as best possible, to identify those records that are responsive to the scope identified above. To the extent those records have not previously been provided to the plaintiff, the defendant is hereby ordered to provide access to the books and records.

IT IS SO ORDERED.

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focusing on who, the parent or the subsidiary, has possession, custody, or control of the subsidiary's records. This misreads the *Salovaara* decision. There, the nature of the relationship among the parties was such that a finding that the subsidiaries were "alter egos" or instrumentalities of the parent was justified. There, the "parent" corporation was the general partner of an intermediate layer of limited partnerships that were, in turn, the general partners of the target "subsidiaries" (also limited partnerships). Of this three-tiered structure, only the target subsidiaries were operating entities. The "parent" and middle layer were both created primarily to build and support the structure involved. Thus, to the extent that the parent corporation had custody or control of financial records of *these* "subsidiaries," a shareholder of the parent could inspect the books and records of the subsidiary.

The present action is different; HBOC had a completely separate existence prior to the merger with a separate board and separate books and records. Thus, there is no evidence that HBOC is so closely related to the parent that ignoring its separate corporate existence is appropriate.

IN RE SILICONIX INC. SHAREHOLDERS LITIGATION

No. 18,700

Court of Chancery of the State of Delaware, New Castle

June 19, 2001

Kevin G. Abrams, Esquire, Srinivas M. Raju, Esquire, J. Travis Laster, Esquire, and Lisa R. Stark, Esquire of Richards, Layton & Finger, Wilmington, Delaware; Norman M. Monhait, Esquire, of Rosenthal, Monhait, Gross & Goddess, P.A., Wilmington, Delaware; and Steven G. Schulman, Esquire, Daniel B. Scotti, Esquire, and U. Seth Ottensoser, Esquire, of Milberg Weiss Bershad Hynes & Lerach LLP, New York, New York, for plaintiff.

A. Gilchrist Sparks III, Esquire, R. Judson Scaggs, Jr., Esquire, Jessica Zeldin, Esquire, and Patricia R. Uhlenbrock, Esquire of Morris, Nichols, Arsht & Tunnell, Wilmington, Delaware; and Alan R. Friedman, Esquire, Jonathan M. Wagner, Esquire, Douglas Gray, Esquire, and Theresa A. Buckley, Esquire, of Kramer Levin Naftalis & Frankel LLP, New York, New York, for defendant Vishay Inter-technology, Inc.

Robert K. Payson, Esquire, Stephen, C. Norman, Esquire, Kevin R. Shannon, L. Esquire, Matthew E. Fischer, Esquire, and Brian C. Ralston, Esquire of Potter, Anderson & Corroon, LLP, Wilmington, Delaware; and Norman J. Blears, Esquire, Michael L. Charlson, Esquire, and Steven G. Mason, Esquire of Heller, Ehrman, White & McAuliffe, LLP, Menlo Park, California, for defendant Mark Segall.

Lawrence C. Ashby, Esquire, Richard D. Heins, Esquire, Philip Trainer, Jr., Esquire, and Richard I.G. Jones, Jr., Esquire, of Ashby & Geddes, Wilmington, Delaware; and David Mark Balabanian, Esquire, Alfred C. Pfeiffer, Jr., Esquire, and Jason A. Yurasek, Esquire, of McCutchen Doyle Brown & Enersen, San Francisco, California, for defendants Everett Arndt, Lori Lipcaman, King Owyang, Michael Rosenberg, and Glyndwr Smith.

Lewis H. Lazarus, Esquire, and Michael A. Weidinger, Esquire, of Morris, James, Hitchens & Williams, LLP, Wilmington, Delaware; and Samuel R. Miller, Esquire, and Julie M. Kennedy, Esquire, of Folger, Levin & Kahn LLP, San Francisco, California, for defendant Siliconix incorporated.

NOBLE, *Vice Chancellor*

I. INTRODUCTION

Lead Plaintiff Raymond L. Fitzgerald ("Fitzgerald"), a shareholder in Defendant Siliconix incorporated ("Siliconix") brings this consolidated action,[1] *inter alia*, to challenge the stock-for-stock tender offer by Defendant Vishay Intertechnology, Inc. ("Vishay") through its wholly-owned subsidiary, Vishay TEMIC Semiconductor Acquisition Holdings Corp. ("Acquisition") for the 19.6% equity interest in Siliconix that Acquisition does not already own.[2]

Fitzgerald has moved to enjoin preliminarily the tender, now scheduled to expire at midnight on June 22, 2001, because of alleged breaches by Vishay and the directors of Siliconix of their fiduciary duties to Siliconix shareholders.

In support of his motion, Fitzgerald makes these arguments. First, Fitzgerald alleges that the Defendants' disclosures to the minority shareholders contained material misrepresentations and omitted material facts. Second, he contends that the offered price is unfair; and, because of disclosure violations and the coercive nature of the tender proposal, Defendants cannot satisfy the burden therefore imposed upon them to demonstrate the fairness of the price. Finally, as a result of alleged repeated breaches of fiduciary duties and the oppressive structure of the proposed tender, Fitzgerald argues that the tender must be judged by the entire fairness test, a standard, Fitzgerald asserts, that Defendants cannot satisfy.

Following expedited discovery and briefing, I heard argument on Fitzgerald's Motion for a Preliminary Injunction on June 15, 2001. I now conclude that, based on the current record, Fitzgerald has not demonstrated a reasonable probability of success on the merits of his claims. Accordingly, his motion for a preliminary injunction must be denied.

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[1]Fitzgerald asserts (i) individual claims on behalf of himself and a purported class comprised of the other Siliconix minority shareholders and (ii) a derivative action on behalf of Siliconix.

[2]For simplicity, I will refer to Vishay and Acquisition collectively as Vishay.

II. FACTUAL HISTORY

A. The Parties.

Fitzgerald has owned Siliconix stock since February 1991. His holdings have a market value in excess of $4 million.

Vishay, which is listed on the New York Stock Exchange, is a manufacturer of passive electronic components and semiconductor components. It owns 80.4% of the equity in Siliconix.

Siliconix is listed on the NASDAQ. It designs, markets, and manufactures power and analog semiconductor products. It is the leading manufacturer of power MOSFETS ("metal oxide semiconductor field effect transistors"), power integrated circuits, and analog signaling devices for computers, cell phones, fixed communications networks, automobiles, and other electrical systems. In March 1998, Daimler-Benz sold its TEMIC semiconductor division, which included an 80.4% equity interest in Siliconix, to Vishay.

Defendant Felix Zandman ("Zandman") is the chairman, chief executive officer, and controlling stockholder of Vishay. Defendant King Owyang is a director, president, and chief executive officer of Siliconix. He was appointed to these positions by Vishay in 1998 following Vishay's acquisition of its equity interest in Siliconix.

Defendants Mark Segall ("Segall") and Timothy Talbert ("Talbert") are directors of Siliconix and served on the Special Committee formed to evaluate a Vishay proposal to acquire the minority interests in Siliconix.

The other individual Defendants are directors of Siliconix and are either employees of Vishay or have an on-going close business relationship with Vishay.

B. Background to the Tenders.

Since acquiring its interest in Siliconix, Vishay has assisted in marketing Siliconix' products, and the company itself is frequently referred to as "Vishay Siliconix." Siliconix has been successful since Vishay's acquisition. The price of the stock, however, as with many technology stocks, has fluctuated greatly during the last many months from a high of $165 in March 2000 to a low of under $17 in December 2000. Its profits have increased significantly, and it has been successful in developing and bringing to the market many new products. Nonetheless, the recent economic downturn has adversely affected Siliconix, particularly because of its dependence on the cell phone industry. For example, Siliconix' net

sales in the first quarter of 2001 were $88.1 million; for the comparable period in 2000, its sales were $114.6 million. Over the same period, profits decreased by 65%.

Early this year, Vishay began to consider acquiring the remaining Siliconix stock that it did own. According to Vishay, it determined that it should evaluate opportunities to reduce costs and seek synergies that could be achieved through an acquisition of the minority Siliconix shares. Fitzgerald's view is that Vishay started to look seriously at acquiring Siliconix because its price was starting to rise from its December low and its prospects were improving. If Vishay did not act quickly, it would be forced to pay significantly more for the Siliconix minority interests.[3]

C. The Cash Tender Offer.

On February 22, 2001, Vishay publicly announced a proposed, all-cash tender offer for the publicly-held Siliconix common stock at a price of $28.82 per share. It also announced that if it obtained over 90% of the Siliconix stock, it would consider a short-form merger of Siliconix into a Vishay subsidiary for the same price. Vishay determined the price by applying a 10% premium to the then market price of Siliconix stock. Vishay made no effort to value Siliconix. Fitzgerald maintains that the tender offer price of $28.82 per share was grossly inadequate and asserts that the public announcement was an effort to keep the price artificially depressed. Among other factors, he points out that the price represented a 20.1% discount from Siliconix' average closing price for the six-month period prior to the announcement of the cash tender offer.

D. Appointment of the Special Committee.

In its February 22, 2001 press release, Vishay requested the opportunity to "discuss its tender offer with a special committee of independent, non-management Siliconix directors who are unaffiliated with Vishay."[4] In response, the Siliconix board designated a Special Committee consisting of directors Segall and Talbert. Both members of the Special Committee had done extensive work with Vishay. Segall had been its

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[3]The record also suggests that eliminating Fitzgerald, who had been an active Siliconix shareholder and a vocal critic of Vishay, as a stockholder was a factor in Vishay's decision to acquire the minority interest in Siliconix. Registration Statement at 30.

[4]It is not disputed that all Siliconix directors, because of their deep involvement with Vishay, suffered serious conflicts of interest (except for directors Segall and Talbert, about whose independence there is debate).

attorney until shortly before the tender. Talbert had been active in providing banking services to Vishay in the 1980s. Both were friends of Vishay management, including particularly Avi Eden ("Eden"), who was Vishay's principal representative for the Siliconix tender effort.[5] Talbert was appointed to the Siliconix board shortly before the February 22, 2001, announcement of the tender offer with the purpose, at Eden's suggestion, that he would also serve on the Special Committee. Members of the Special Committee were to be paid a separate $50,000 fee and there were discussions about a "special fee" to be determined later. The parties again differ as to whether this "special fee" was to provide a financial incentive for the Special Committee to agree with Vishay or whether it was simply a means of an after-the-fact check on whether the fee was commensurate with the effort involved.

Fitzgerald maintains that the actions of the Special Committee, throughout its existence, have constituted nothing more than a sham —essentially two Vishay loyalists, supinely pursuing their engagement without vigor or effectiveness.

The Defendants' version of the conduct of the Special Committee, as one would expect, is quite different. Its mandate was to take reasonable and necessary steps to evaluate the transaction and to negotiate with Vishay. Following its appointment, the Special Committee sought outside professional assistance. After discussions with representatives of at least five investment banking firms, the Special Committee engaged Lehman Brothers ("Lehman") as its financial advisor. After consulting with three prominent law firms, the Special Committee chose Heller, Ehrman, White & McAuliffe ("Heller Ehrman") to provide legal counsel. Neither Lehman nor Heller Ehrman had any relationship with Siliconix or Vishay.

Fitzgerald points out that Segall discussed the retention of both the financial expert and the legal advisor with Eden. Fitzgerald would have the Court believe that this was an opportunity for Eden to veto any of the advisors. The Special Committee, on the other hand, would have the Court believe that this was simply a double check on potential conflicts of interest.[6] Although I cannot resolve this dispute, I do accept that both Lehman and Heller Ehrman were independent.[7]

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[5]Talbert, with his wife, holds slightly over 2,000 shares of Vishay stock. Segall's new employer participated as a member of the syndicate that placed shares of Vishay common stock and received a fee from that effort in the approximate amount of $30,000.

[6]Segall Declaration at ¶ 5.

[7]Lehman's proposed compensation consisted of a $50,000 retainer, $250,000 for a fairness opinion, if requested, and a transaction fee of $1.75 million to be paid upon the closing of certain transactions. This aspect of compensation for investment bankers is not unusual.

The Special Committee met regularly with its advisors. Although recognizing that Vishay could not be compelled to sell its stake in Siliconix and that Vishay could commence a unilateral offer at any time, nonetheless, according to the Defendants, the Special Committee attempted to evaluate Vishay's February cash tender proposal and to negotiate the best terms, including price, that it could obtain for the minority shareholders.

On April 5, 2001, the Special Committee and its advisors met with Vishay. The Special Committee expressed the view that $22.82 per share was not a fair price for Siliconix. The parties agreed to resume their discussions after Lehman had completed its due diligence and valuation work on Siliconix and the special committee had had an opportunity to review that work.

E. The Stock-for-Stock Exchange.

In the meantime, Siliconix' stock had risen above the $28.82 per share cash offer price. Vishay management was unwilling to increase the cash offer and therefore started to consider a stock-for-stock transaction. On May 2, 2001, the Special Committee again met with Vishay. Vishay was again told that the Special Committee did not consider $28.82 per share adequate, and Vishay floated the possibility of a stock-for-stock deal. Because of the stock-for-stock possibility, Lehman was directed by the Special Committee to analyze Vishay to form a view as to what the value of the Vishay stock would be in terms of such an offer. Fitzgerald alleges that Lehman at this meeting took the position that it would have endorsed an offer in the range of $34 to $36. The Special Committee advised Vishay that the $28.82 price was inadequate. Vishay drafted a merger agreement for consideration by the Special Committee, and the parties conducted on-going negotiations for several weeks about a potential merger.

On May 9, 2001, Zandman made a presentation at an analysts' conference during which he discussed not only Vishay's business but also the business of Siliconix. He spoke of Siliconix ' "very good market position" and its status as "number one" in its industry. He indicated that the economic cycle was hitting the bottom, in his opinion, and reflected that Siliconix historically has emerged from downturns ahead of Vishay.

Indeed, all proposals submitted by investment bankers for the Siliconix work provided that the bulk of the fees would be payable upon the closing of the transaction. (Segall Declaration, ¶ 4) Fitzgerald responds that the compensation arrangement for Lehman provided an incentive for it to approve the transaction.

He expressed his view that Siliconix was experiencing a "bottoming up, " but he went on to caution that the outlook for Siliconix was unsettled.[8]

On May 23, 2001, Vishay informed the Special Committee that it was considering proceeding with a stock-for-stock exchange offer without first obtaining the Special Committee's approval. Two days later, Vishay announced the exchange offer under which it would exchange 1.5 shares of Vishay common stock for every share of Siliconix common stock. The exchange ratio was simply the ratio of the Siliconix and Vishay stock prices as of the February 22 proposal. Unlike the February 22 cash tender announcement, the share exchange carried no market premium for the Siliconix shareholders.

Again, both sides have different perceptions of Vishay's motivations for announcing the stock-for-stock exchange tender on May 25, 2001. According to Fitzgerald, Vishay had to move quickly to take advantage of the temporary market pressure on Siliconix stock because it perceived that Siliconix' stock price and operating performance were likely to rebound with improvements in the national and global economies and that Siliconix moves in periods of recovery ahead of Vishay. Also, Vishay, according to Fitzgerald, sought to take advantage of the continuing adverse impact of the February 22 announcement on Siliconix' stock price.

Vishay's disputes Fitzgerald's explanation. Vishay explains that it announced the stock-for-stock offer because of its perception of a continuing deterioration in the electronic components market generally and Siliconix' market niche in particular. The record suggests that Siliconix' sales were continuing to fall. Vishay also observes that the tender offer was at a premium over the February 22 closing price.

Fitzgerald points out that Vishay initiated the stock-for-stock exchange offer without affording the Special Committee any opportunity to evaluate the fairness of the offer. On May 25, 2001, Vishay filed with the Securities and Exchange Commission its S-4 Registration Statement and Schedule TO. Amendments with updated information were also filed on June 1, 2001. The offer to exchange/prospectus was distributed to Siliconix shareholders during the week of June 4, 2001.

Vishay's offer contained a non-waivable "majority of the minority" provision providing that Vishay would not proceed with its tender offer unless a majority of those shareholders not affiliated with Vishay tendered their shares. Vishay also stated that it intended to effect a short-form

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[8]Fitzgerald contrasts this optimism concerning Siliconix with the largely pessimistic view of Siliconix' future that Vishay has disclosed to the target stockholders of its pending tender offer.

merger following a successful tender offer, but it noted that it is not required to do so and that there might be circumstances under which it would not do so. The Registration Statement also advised the minority shareholders that if Vishay pursued the short-form merger, it would be at the same per share consideration as the exchange offer and that objecting shareholders could invoke their appraisal rights under Delaware law.

When the exchange offer was announced, Vishay was trading for $25.81, an equivalent of $38.71 per share of Siliconix. Since then, the price of Vishay has dropped to roughly $20, thereby producing an imputed value of roughly $30 for each Siliconix share. One of the reasons for the decline may have been the announcement on May 30, 2001, by Vishay of a major debt offering.[9]

The Special Committee advised Vishay that is was unlikely to approve the 1.5 exchange ratio as fair, but the record is unclear what steps were taken to seek enhancement of the terms of the tender offer. For example, Eden testified that he could not recall either of the Special Committee members requesting an increase in the exchange ratio. In contrast, according to Segall, on May 30, 2001, he spoke with Eden and urged Vishay to improve the unilateral tender offer by increasing the exchange ratio or providing some sort of protection in the event that Vishay's market price declined.[10]

On June 8, 2001, Siliconix filed with the Securities and Exchange Commission its Schedule 14D-9 setting forth its disclosures concerning Vishay's offer. It reported that the Special Committee has determined to remain neutral and make no recommendation with respect to the tender offer. The Special Committee never requested Lehman to prepare a fairness opinion as to the exchange offer. According to Segall, the Special Committee did not seek a fairness opinion because until May 23, 2001, it was still negotiating terms with Vishay. Until the terms were finalized, it would have been premature to seek a fairness opinion. Segall notes that after the process changed from a negotiated agreement to a unilateral tender offer, the Special Committee did not seek a fairness opinion because it did not consider it customary or appropriate to obtain a fairness opinion in the context of the unilateral tender offer.[11]

Fitzgerald argues that the Special Committee knew that if it asked for Lehman's opinion, Lehman would render an opinion that the exchange ratio was inadequate, especially given Lehman's reservations about giving

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[9]Amendment No. 1 to Registration Statement at 28.
[10]Segall Declaration at ¶ 9.
[11]Segall Declaration at ¶ 8.

a fairness opinion at below $34 per share. Fitzgerald's reference to Lehman's reluctance to give a fairness opinion below $34 per share is based upon some notes made by a meeting attendee.[12] On the other hand, Lehman's principal representative on the Siliconix project does not recall expressing such an opinion, even tentatively.[13] In any event, Amendment No. 1 to the Registration Statement recites:

> [At a meeting of Vishay and the Special Committee following commencement of the stock-for-stock offer, representatives of the Special Committee] expressed the view that the special committee would not be likely to recommend the offer at the then current price levels of Vishay stock, which at such levels, provided value of less than $34 per Siliconix share.[14]

Fitzgerald argues that the exchange ratio constituted an inadequate and unfair price. He draws this conclusion from the fact that companies comparable to Siliconix are selling at price earnings multiples and EBIDTA multiples significantly higher than those represented by the exchange ratio. Fitzgerald contends[15] that International Rectifier, a similar, but not as profitable company, as Siliconix, has been trading at a price earnings multiple of approximately 23.9x and a LTM EBITDA multiple of approximately 15.lx, which are more than double the multiples for Siliconix represented by the exchange ratio.[16] In support of his contention that the offer is unfair, Fitzgerald submitted the report of Gilbert Matthews who concluded that the Vishay offer is "materially lower than the fair value of Siliconix."[17]

The disclosures made by Vishay in its Registration Statement and by Siliconix in its Schedule 14D-9 are, of course, critical to the issues presented in this matter. I discuss the disclosures made in those documents more thoroughly throughout the balance of this memorandum opinion, especially during my discussion of the sufficiency of the disclosures.

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[12]Deposition of Mark Segall, Ex. 2.

[13]Deposition of Joe C. Stone at 96.

[14]Amendment No. 1 to Registration Statement at 28.

[15]Plaintiff's Opening Brief, at 18.

[16]I note (but do not allow it to affect my analysis) that the price of International Rectifier stock fell by one-third on the day of argument of Fitzgerald's motion for a preliminary injunction.

[17]Report of Gilbert E. Matthews at 1.

III. ANALYSIS

A. The Applicable Legal Standard.

In order to obtain a preliminary injunction, Fitzgerald must demonstrate: (i) a reasonable probability of success on the merits of his claim; (ii) a threat of imminent, irreparable harm if injunctive relief is denied; and (iii) a balancing of the equities favors granting the relief.[18]

B. Probability of Success.

I first set forth the established legal principles dealing with when a tender offeror may be under a duty to offer a fair price. I next address Fitzgerald's argument that the proposed transaction must be judged under the entire fairness standard, not only because of its potential impact on the merits of the dispute, but also because of its potential to expand the scope of Defendants' disclosure obligations. I then turn to the critical issues associated with the adequacy of the disclosures made by Defendants to the minority shareholders. I conclude with an assessment of whether the pending tender offer is coercive.

1. Fair Price Issues.

In responding to a voluntary tender offer, shareholders of Delaware corporations are free to accept or reject the tender based on their own evaluation of their best interests.[19] "That choice will normally depend upon each stockholder's individual investment objectives and his evaluation of the merits of the offer."[20] However, this Court will intervene to protect the rights of the shareholders to make a voluntary choice. The issue of voluntariness of the tender depends on the absence of improper coercion and the absence of disclosure violations. Thus, "as a general principle, our law holds that a controlling shareholder extending an offer for minority-held shares in the controlled corporation is under no obligation, absent evidence that material information about the offer has been withheld or

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[18] *See, e.g. Unitrin, Inc. v. American General Corp.*, Del. Supr., 651 A.2d 1361, 1371 (1995); *Ivanhoe Partners v. Newmont Mining Corp.*, Del. Supr., 535 A.2d 1334, 1341 (1987).

[19] *In re Life Technologies, Inc. Shareholders Litig.* ("Life Technologies"), Del. Ch., C.A. No. 16513, Lamb, V.C. (Nov. 24, 1998) (Bench ruling transcript at 4.); *In re Marriott Hotel Properties II Limited Partnership Unitholders Litig.*, Del. Ch., Consol. C.A. No. 14961, mem. op. at 39-42, Lamb, V.C. (Jan. 24, 2000).

[20] *Eisenberg v. Chicago Milwaukee Corp.*, Del. Ch., 537 A.2d 1051, 1056 (1987).

misrepresented or that the offer is coercive in some significant way, to offer any particular price for the minority-held stock."[21]

Accordingly, Vishay was under no duty to offer any particular price, or a "fair" price, to the minority shareholders of Siliconix unless actual coercion or disclosure violations are shown by Fitzgerald. In short, as long as the tender offer is pursued properly, the free choice of the minority shareholders to reject the tender offer provides sufficient protection. Because I conclude that there were no disclosure violations and the tender is not coercive, Vishay was not obligated to offer a fair price in its tender.

2. Entire Fairness Standard.

Fitzgerald argues that a preliminary injunction should issue because the Defendants cannot demonstrate that the transaction is entirely fair. He contends that both the fair dealing and the fair price prongs of the entire fairness standard are implicated because the Siliconix directors (including the Special Committee members) breached their duty of care and their duty of loyalty to the Siliconix shareholders. Briefly, the Siliconix board is alleged to have breached its duty of care by not carefully evaluating the proposed transaction and then developing with appropriate assistance from investment banking professionals and sharing with the stockholders a recommendation as to the response to the tender offer that would be in the shareholders' best interest. The alleged breach of the duty of loyalty flows directly from the concededly conflicted status of at least a substantial majority of the board, which certainly is not uncommon in instances where the controlling stockholder seeks to acquire the balance of the shares in the subsidiary. However, unless coercion or disclosure violations can be shown, no defendant has the duty to demonstrate the entire fairness of this proposed tender transaction.[22]

It may seem strange that the scrutiny given to tender offer transactions is less than the scrutiny that may be given to, for example, a merger transaction which is accompanied by more general breaches of fiduciary duty by the directors of the acquired corporation. From the standpoint of a Siliconix shareholder, there may be little substantive difference if the tender is successful and Vishay proceeds, as it has indicated that it most likely will, with the short-form merger. The Siliconix

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[21] *In re Ocean Drilling & Exploration Co. Shareholders Litig.* ("*Ocean Drilling*"), Del. Ch., Consol. C.A. No. 11898, Chandler, V.C., mem. op. at 6-7 (Apr. 30, 1991); *See also Solomon v. Pathe Communications Corp.*, Del. Supr., 672 A.2d 35, 40 (1996).

[22] *See Life Technologies, supra*, Bench ruling transcript at 3-4.

shareholders may reject the tender, but, if the tender is successful and the short-form merger accomplished, the shareholder, except for the passage of time, will end up in the same position as if he or she had tendered or if the transaction had been structured as a merger, *i.e.*, as the holder of 1.5 Vishay shares for every Siliconix share held before the process began (or as someone pursuing appraisal rights) and with no continuing direct economic interest in the Siliconix business enterprise.

The difference in judicial approach can be traced to two simple concepts. The first is that accepting or rejecting a tender is a decision to be made by the individual shareholder, and at least as to the tender itself, he will, if he rejects the tender, still own the stock of the target company following the tender.[23] The second concept is that the acquired company in the merger context enters into a merger agreement, but the target company in the tender context does not confront a comparable corporate decision because the actual target of a tender is not the corporation (or its directors), but, instead, is its shareholders.[24] Indeed, the board of the tender target is not asking its shareholders to approve any corporate action by the tender target. That, however, does not mean that the board of the company to be acquired in a tender has no duties to shareholders.

> But addressing that question in the circumstances of this case involves one in considering an anomaly. Public tender offers are, or rather can be, change in control transactions that are functionally similar to merger transactions with respect to the critical question of control over the corporate enterprise. Yet, under the corporation law, a board of directors which is given the critical role of initiating and recommending a merger to the shareholders (see 8 Del. C. § 251) traditionally has been accorded no statutory role whatsoever with respect to a public tender offer for even a controlling number of shares. This distinctive treatment of board power with respect to merger and tender offers is not satisfactorily explained by the observation that the corporation law statutes were basically designed in a period when large scale public tender offers were rarities; our statutes are too constantly and carefully massaged for such an explanation to account for much of the

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[23]Of course, if a short-form merger is effected, the time for continued holding of the stock may be short.

[24]*See In re Home Shopping Network, Inc. Shareholders Litig.*, Del. Ch., C.A. No. 12868 (Consol.), Chandler, V.C., mem. op. at 29 (May 19, 1993).

> story. More likely, one would suppose, is that conceptual notion that tender offers essentially represent the sale of shareholders' separate property and such sales—even when aggregated into a single change in control transaction—require no "corporate" action and do not involve distinctively "corporate" interests.[25]

As noted, the General Assembly has imposed specific duties on the directors of corporations entering into merger agreements, 8 *Del. C.* § 251, but it has not chosen to impose comparable statutory duties on directors of companies that are targets of tender offers.[26]

In a similar vein, Fitzgerald maintains that the Siliconix board (or perhaps its Special Committee) was required by *McMullin v. Beran*,[27] as well as other authority,[28] to take a position on whether the Siliconix shareholders should accept the tender and to inform them of that decision and the reasons for it. The board's failure, which Fitzgerald maintains reflects breaches of both the duty of care and the duty of loyalty, to provide this assistance to the shareholders likewise mandates an entire fairness evaluation.

McMullin teaches, *inter alia*, that in the context of a merger of a subsidiary with a third party (thereby effecting a complete sale of the subsidiary) where the controlling shareholder wants the merger to occur and the minority shareholders are powerless to prevent it: (i) the directors of the subsidiary have "an affirmative duty to protect those minority shareholders' interests";[29] (ii) the board cannot "abdicate [its] duty by leaving it to the shareholders alone" to determine how to respond;[30] and (iii) the board has a duty to assist the minority shareholders by ascertaining the subsidiary's value as a going concern so that the shareholders may be

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[25]*T.W. Services, Inc. v. SWT Acquisition Corp.*, Del. Ch., CA. No. 10427, mem. op. at 28-30, Allen, C. (Mar. 2, 1989) (footnotes omitted).

[26]Fitzgerald cites *Kahn v. Lynch Communication Systems, Inc.*, Del. Supr., 638 A.2d 1110 (1994) and *Kahn v. Tremont Corp.*, Del. Supr., 694 A.2d 422 (1997), in support of his contention that the structure of the transaction requires the entire fairness analysis. Both of these cases, however, involve "self-dealing" where the controlling shareholder stood on both sides of the transactions. Here, of course, Vishay stands on only one side of the tender.

[27]*McMullin v. Beran*, Del. Supr., 765 A.2d 910 (2000). In *McMullin*, ARCO owned 80.1% of the common stock of ARCO Chemical. It sought the sale of the entire Chemical company through a merger of Chemical into a subsidiary of Lyondell. The directors of Chemical approved the merger agreement before submitting it to all of Chemical's stockholders.

[28]*See e.g.*, *Gilmartin v. Adobe Resources Corp.*, Del. Ch., C.A. No. 12467, Jacobs, V.C. (Apr. 6, 1992).

[29]*McMullin v. Beran*, *supra*, 765 A.2d at 920.

[30]*Id.*, 765 A.2d at 919.

better able to assess the acquiring party's offer and, thus, to assist in determining whether to pursue appraisal rights.[31]

Many of the pertinent factors in *McMullin* are similar to the Siliconix circumstances. In *McMullin*, the controlling shareholder owned a little more than 80% of the subsidiary, and half of the subsidiary's directors were employed by the parent. In both cases, the ultimate question for the minority shareholders was whether to acquiesce in the proposed transaction or to rely upon the appraisal remedy.[32] Although there are many similarities, there is one large difference: *McMullin* involved a merger of the subsidiary into a third-party, a transaction for which the subsidiary board sought the approval of the minority shareholders.

The question thus becomes: does *McMullin* apply with full force, as Fitzgerald seems to contend, to a tender offer by a controlling shareholder for the remaining 20% of the stock held by the minority (where a short-form merger may follow) or does it primarily define or confirm standards governing mergers under the facts of that case?

When one looks at both the *McMullin* and Siliconix transactions from the perspective of the minority shareholders, their need for (and their ability to benefit from) the guidance and information to be provided by their boards in accordance with the principles of *McMullin* is virtually indistinguishable. The most likely ultimate puzzle for the minority shareholder, as noted above, is (a) take the consideration offered or (b) seek appraisal. However, this analysis must focus on the source of the duties motivating the result in *McMullin*. The Supreme Court was careful to note throughout its opinion that the duties involved were statutory duties imposed by 8 *Del. C.* § 251 (relating to mergers) and the "attendant" fiduciary duties.[33] The Court emphasized that fiduciary duties are "context specific"[34] and the context of *McMullin* was, of course, a merger. In the face of a carefully crafted opinion, I cannot read into it a new approach to assessing the conduct of directors of a tender target, one that would

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[31] *Id.*, 765 A.2d at 922.

[32] "Effective representation of the financial interests of the minority shareholders imposed upon the Chemical Board an affirmative responsibility to protect those minority shareholders' interests. This responsibility required the Chemical Board to: frost, conduct a critical assessment of the third-party Transaction with Lyondell that was proposed by the majority shareholder; and second, make an independent determination whether the transaction maximized value for all shareholders. The Chemical Directors had the duty to fulfill this obligation faithfully and with due care so that the minority shareholders would be able to make an informed decision about whether to accept the Lyondell transaction tender offer price or to seek an appraisal of their shares. *Id.*, 765 A.2d at 920.

[33] *Id.*, 765 A.2d at 920.

[34] *Id.*, 765 A.2d at 918-20.

essentially overrule cases such as *Solomon v. Pathe Communications Co.*, *Life Technologies*, and *Ocean Drilling*.[35] In addition, the minority shareholders in *McMullin* were powerless; the parent was voting for the merger and it did not matter how they voted. Here, the Siliconix minority shareholders have the power to thwart the tender offer because it will go forward only if a majority of the minority shares are tendered. Accordingly, I conclude that *McMullin* cannot be read to require application of the entire fairness test to evaluate the proposed transaction.[36]

To the extent that *McMullin* may be read to require the subsidiary board to guide the minority shareholders in their decision to accept or reject a tender, I note that there may exist circumstances where there is no answer to the question of whether to accept or reject. Sometimes the facts in favor of and against acceptance of the tender will balance out. On this preliminary record, I am not persuaded that the Special Committee's decision not to take a position was not reasonably supported by the information available to it.[37] There are a number of competing factors. For example, the tender consideration, whether in reference to the frequently mentioned $34 per share or the Lehman analysis reciting a wide range of potential values, is at the low end. On the other hand, factors such as liquidity and the possibility that the Siliconix price might decline if the Vishay offer is withdrawn may be interpreted as supporting a tender.[38]

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[35]Defendants urge that the intended transactions here; (i. e., a tender for all shares on a stock-for-stock basis likely followed by a short-form merger) be viewed in substance as one overall merger effort. I decline that invitation for two reasons. First, Delaware law has recognized the tender followed by the short-form merger as separate events. To view it otherwise would preclude, as a practical matter, the efficiencies allowed by the short-form merger process. Second, in this instance, there is no guarantee (although it is most likely) that Vishay will complete the back-end merger.

[36]Defendants also assert that, to the extent that Delaware law may be construed to require actions or disclosures by the board of the tender target beyond the truthful and complete disclosures required for Schedule 14D-9, it would be preempted by federal securities law. In particular, it is my understanding that Defendants argue that Delaware law cannot impinge upon the rights of the board to recommend acceptance or rejection of the tender or to express no opinion or state that it is unable to take a position. Because of my disposition of the substantive issues in this preliminary proceeding, I need not now reach Defendants' preemption contentions. (*See* 17 C. F. R. § 240-14e-2(a)).

[37]I am relying in particular upon the Segall Declaration at ¶ 10; the Segall Deposition at 69-76; and the Schedule 14D-9 at 9-12.

[38]One of the reasons given was that because Vishay was proposing a stock-for-stock tender, the Special Committee could not conclude whether the value was adequate because fluctuations in Vishay's stock price meant that there was not a fixed number to assess. While that is inherent in valuing any stock-for-stock transaction (although in today's market for stocks in the technical sector predictability may be especially difficult to attain) it does not ordinarily afford a basis for avoiding a recommendation because risk of stock price fluctuation is but one of many uncertainties associated with providing guidance of this nature.

Regardless of how one assesses the Special Committee's obligation to make a recommendation, once the Siliconix board set forth the reasons for that decision in its Schedule 14D-9, its full and complete disclosure obligation was in effect. The sufficiency of those disclosures is considered subsequently.

I will now turn to the issues of disclosure and coercion, as to at least one of which Fitzgerald must demonstrate a reasonable probability of success, if he is to prevail on his motion for a preliminary injunction.

3. Disclosure.

A majority stockholder, in this instance, Vishay, who makes a tender to acquire the stock of the minority shareholders owes the minority shareholders a fiduciary duty to disclose accurately all material facts surrounding the tender.[39] The significance of that is enhanced where, as here, the acquiring Company effectively controls the acquired company. When the directors of the tender target company communicate with the shareholders, for example, through a Schedule 14D-9, they must, while complying with their ever-present duties of due care, good faith and loyalty, communicate honestly.[40] A fact is material if there is a "substantial likelihood" that its disclosure "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[41] Delaware law does not require disclosure of "all available information" simply because available information "might be helpful."[42] The plaintiff has the burden of demonstrating materiality.[43] In the context of a preliminary injunction proceeding regarding a tender offer, the issue becomes whether there is a reasonable probability that a material omission or misstatement has been made "that would make a reasonable shareholder more likely to tender his shares."[44]

With these principles in mind, I will turn to the alleged disclosure violations.[45] Fitzgerald alleges relatively few instances of misleading

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[39]*Malone v. Brincat*, Del. Supr., 722 A.2d 5, 11 (1998); *Stroud v. Grace*, Del. Supr., 606 A.2d 75, 84 (1992); *Lynch v. Vickers Energy Corp.*, Del. Supr., 383 A.2d 278 (1978).

[40]*Malone v. Brincat, supra*, 722 A.2d at 10.

[41]*Skeen v. Jo-Ann Stores, Inc.*, Del. Supr., 750 A.2d 1170, 1174 (2000).

[42]*Id.*

[43]*Loudon v. Archer-Daniel-Midland Co.*, Del. Supr., 700 A.2d 135, 143 (1997).

[44]*Ocean Drilling, supra*, mem. op. at 3.

[45]Fitzgerald may be suggesting that *McMullin v. Beran* dictates enhanced disclosure responsibilities. To comply with their substantive mandate to guide shareholders, those with fiduciary duties to shareholders need not only disclose all material information but, so the argument goes, they must also provide or generate additional information (*e.g.*, a fairness

disclosures; most of his challenges allege a failure to disclose material facts.

(a) Fitzgerald asserts that Vishay has misled the Siliconix stockholders by painting an unduly pessimistic picture of Siliconix' future.[46] The Registration Statement reports Vishay's "perceptions of a continuing deterioration in the electronic components market generally and in the space which Siliconix operates in particular."[47] Siliconix also reports negative information about the future in the Schedule 14D-9.[48] Of particular concern to Fitzgerald are apparently inconsistent statements by both Zandman, the Chairman of Vishay (to analysts on May 9, 2001, that Siliconix was then experiencing a "bottoming up" of its business), and Owyang, the Chief Executive Officer of Siliconix, (in a February 6, 2000, press release to the effect that Siliconix can manage downturns in the economy and "respond aggressively when our markets recover"). The Registration Statement does predict that Siliconix' stock price and performance will "rebound further."[49]

To put these superficially inconsistent statements in context, Zandman, in his May 9 remarks to analysts, also stated that he was not confident about the "bottoming up" and that the stock price might go down. The Registration Statement qualifies the "rebound further" language, seized upon by Fitzgerald, by noting the rebound's dependence on improvements in the national and global economies.[50] It further disclosed that Siliconix historically has recovered earlier in economic upturns than has Vishay. I do not find these statements, when placed in context, to be inconsistent or misleading. Vishay and Siliconix management believe that Siliconix' future will be unsettled and challenging. Perhaps Fitzgerald disagrees with this assessment, but he has not made any serious attempt to show that it is wrong. As to the apparent inconsistencies, they are largely a function of the timeframe of the assessment. The Registration Statement (and Zandman's comments and Owyang's comments for that matter) makes clear

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opinion.) If that is so, then the universe of material information arguably would expand. First, given my understanding of the application of the principles of *McMullin v. Beran*, as set forth above, I do not envision any new disclosure requirements in this context. Second, *McMullin v. Beran* cited *Skeen v. Jo-Ann Stores, Inc.*, *supra*, with approval and confirmed that no new disclosure standard had been prescribed.

[46]*See Zirn v. VLI Corp.*, Del. Supr., 681 A.2d 1050, 1057 (1996)

[47]Registration Statement at 33.

[48]Schedule 14D-9 at 7, 10.

[49]Registration Statement at 31.

[50]Although Fitzgerald argues that the "rebound" language is "buried" in a later section of the Registration Statement, I do not find that it was set forth in a manner that would keep the unwary stockholder from finding it. *See Joseph v. Shell Oil Co.*, Del. Ch., 482 A.2d 335, 341 (1984).

that Siliconix' recovery is dependent on improved economic conditions, the timing of which neither Vishay nor Siliconix can be expected to predict with confidence.

(b) The Registration Statement and the Schedule 14D-9 contain five-year projections for Siliconix and two-year projections for Vishay.[51] Fitzgerald argues that they are "bare-bones" projections without any detail or the assumptions or methodologies used to prepare them. Vishay points out that the projections are by their nature uncertain[52] and contends that speculative information, such as projections, need not be disclosed.[53] Vishay reasons that, if projections need not be disclosed, there is no need to provide the details and assumptions relating to the projections. Although Vishay presents an accurate statement of the law generally, there are instances where such "soft information" would be material. "Indeed, it would be impossible for there to be meaningful disclosure about many transactions if that was the case, because determining the advisability of a transaction often requires a comparison of the transactional value to be received to the value that would likely be received in the event that the transaction was not effected."[54] Under these circumstances, there is not a "substantial likelihood" that the details and assumptions underlying the projections "would significantly alter the total mix of information already provided" to the shareholders.[55] Fitzgerald has not made a preliminary showing that the details and assumptions justify overcoming the reluctance of courts to order disclosure of "soft information." Such information might be "helpful," but here it has not been shown to be material.

(c) Next, Fitzgerald asserts that the Registration Statement is misleading when it sets forth that Siliconix' forecasts were prepared by "Siliconix management."[56] More specifically, he argues that the disclosure is misleading because it fails to describe the role of Vishay management in preparation of the forecasts. Owyang reviewed Siliconix' 2001 sales forecast with Gerald Paul, President of Vishay, in March 2000. Following that conversation, the sales forecast was revised downward by about 10%. Fitzgerald points out that the revisions occurred after the February tender

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[51]Registration Statement at 34; Schedule 14D-9 at 12.

[52]*See* Registration Statement at 33.

[53]*See McMillan v. Intercargo Corp.*, Del. Ch., C.A. No. 16963, mem. op. at 15-16, Jacobs, V.C. (May 3, 1999) ("In cases where the inherent unreliability of the projections is disclosed to stockholders in the proxy statement or is otherwise established, the projections have been found not material.").

[54]*R.S.M., Inc. v. Alliance Capital Management Holdings L.P.*, Del. Ch., C.A. No. 17449, mem. op. at 44, n. 39, Strine, V.C. (Apr. 10, 2001).

[55]*Skeen v. Jo-Ann Stores, Inc.*, *supra*, 750 A.2d at 1174.

[56]Registration Statement at 34.

offer was announced and suggests that, by then, Paul had an incentive to reduce the sales forecast to make Siliconix' prospects appear more bleak.

I am satisfied, at least preliminarily, that the Siliconix shareholders have not been misled. First, the Schedule 14D-9 discloses that "Vishay participates in Siliconix' budgeting and forecasting processes."[57] Second, the forecasts, including the reduction in the sales forecast, were prepared, in fact, by Siliconix management. There was input from Vishay,[58] including a recommendation that the sales forecast be revised downward, but Owyang's deposition testimony[59] leads me to conclude, on the current record at least, that the forecast revision was a Siliconix decision and not a Vishay decision. That Siliconix management discussed these and other considerations, for that matter, with Vishay management at the time does not make the disclosure misleading. Furthermore, both forecast scenarios are set forth in Schedule 14D-9 and, indeed, even now, Siliconix is evaluating the need for another downward revision.[60]

(d) Fitzgerald next criticizes both the Registration Statement and the Schedule 14D-9 for not describing new patents, new products, and the product pipeline of Siliconix. The successful history of Siliconix in introducing new products, including its recent, success, is, however, set forth in the Registration Statement.[61] The inference to be drawn is that the innovations will not cease. In any event, I do not consider an explanation of the intellectual property or product pipeline to be required because it does not add materially to the "total mix" of information available to the shareholders.

(e) The Registration Statement discloses a patent infringement suit recently filed by Siliconix. Fitzgerald complains that it provides no details about the anticipated recovery. Vishay and Siliconix management hope to negotiate an [. . . . . **confidential** . . . . . .]. Because the litigation is new, because no formal damage analysis has been prepared, and, more importantly, because the estimates are, as characterized by

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[57]Schedule 14D-9 at 11.

[58]Owyang deposition, Ex. 9.

[59]*Id.*, at 138-42.

[60]*Id.*, at 158.

[61]Registration Statement at 31. Segall explained why he did not believe that the intellectual property pipeline or product pipeline required any specific disclosure in the Schedule 14D-9. The Special Committee, as part of Lehman's due diligence, had asked it to review Siliconix' intellectual property and product pipeline. Lehman, as the result of that due diligence, did not identify any non-public information that materially affected Lehman's review of Siliconix. In essence, it appears that Segall relied upon Lehman's due diligence to determine that there was no non-public information relating to intellectual property or product development. (Segall Declaration, ¶ 7).

Fitzgerald, "hopes," the information is not material.[62] If there were a more objective basis for the recovery than what can be found in the present record, its disclosure might well be required.

(f) A similar issue arises with respect to Fitzgerald's claim that Vishay should have disclosed valuation information relating to his derivative action against Vishay and certain Siliconix directors. Again, the speculative nature, at the early stages of the derivative effort, of any recovery for the benefit of Siliconix precludes a finding of materiality. The existence of the litigation is disclosed. Vishay has denied Fitzgerald's allegations. Thus, Vishay, rightly or wrongly, has set forth its views of the benefits to Siliconix from the derivative litigation; whether Vishay is right or wrong in this regard cannot be determined at this stage of the proceedings. Moreover, the law does not require fiduciaries to admit wrongdoing in this context.[63]

(g) Fitzgerald complains that the projections for Vishay span less than two years. He does not provide an adequate basis for concluding that there are projections beyond two years, and Vishay cannot be required to disclose that which does not exist. As with the Siliconix projections, the details and assumptions are not material.

(h) Next, Fitzgerald notes the failure to disclose projections for the combined entity following the transaction and the lack of meaningful pro forma information. Vishay's response is that it has disclosed all that it has.[64] Furthermore, Vishay asserts that any projections about the proposed, combined entity would be speculative, especially because of the difficulties asserted with projecting both the timing and success of any synergies that may result. Accordingly, Fitzgerald has not provided a basis, even preliminarily, for finding a disclosure violation.

(i) The reasons for the Vishay tender are the basis for the next disclosure issue. Both sides have strikingly different versions. Fitzgerald says that Vishay tendered because of "Siliconix' rapidly improving prospects and increasing stock price and Vishay's desperate desire to eliminate Fitzgerald as a Siliconix stockholder."[65] Vishay, on the other hand, says that it tendered for the minority's stock because of movements

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[62]*See, e.g.*, *TCG Securities, Inc. v. Southern Union Co.*, Del. Ch., C.A. No. 11282, mem. op. at 13, Chandler, V.C. (Jan. 31, 1990).

[63]*See Wolf v. Assaf*, Del. Ch., C.A. No. 15339, mem. op. at 14, Steele, V.C., (June 16, 1998).

[64]Fitzgerald asserts that, based on the deposition of William Clancy (at 105), Vishay has projections of the combined entity. I have reviewed the excerpts of the Clancy deposition provided by Fitzgerald and cannot conclude that any useful projections or pro forma financial information can fairly be said to have been created.

[65]Fitzgerald's Opening Brief, at 28.

in the stock market and Vishay's perception of the continuing deterioration in the electronic components market.[66] I cannot reconcile the conflicting versions or conclude, on this preliminary record, which is correct, and thus, Fitzgerald has not met his burden of a preliminary showing that there was a disclosure violation.

(j) Vishay did not disclose to the Siliconix shareholders the basis for its proposed tender offer of $28.82 per share in February or the exchange ratio of 1.5 shares for each share of Siliconix that now is before the Siliconix shareholders. It appears that the tender offer price reflects a 10% premium to market and that the exchange ratio was based on the relative market share price at the time the cash tender was proposed, without any premium. When a tender offeror is not under a duty to offer a "fair" price, it is unclear why the offeror must reveal the basis for its pricing proposal.[67] In the cases relied upon by Fitzgerald,[68] because of specific fiduciary duties to their shareholders, the boards were required to disclose that the pricing consciously was not a fair market price: in one, the tender was for what the corporation could afford in the circumstances, and in the other, the price was not developed through normal models used to determine fair market value. The unusual nature of the methodologies, in the specific context of those cases, required the disclosure. For the exchange offer here, the exchange ratio was established based on proportional stock values as of a certain date. In any event, that is not the type of information that would likely influence (even in the absence of a premium to market) a shareholder's decision not to tender.

(k) Fitzgerald contends that Vishay did not properly describe that the back-end, short-form merger might not occur. Vishay set forth its intentions to complete the back-end merger, but it also notes that it could change its intent and that it is not legally obligated to complete the merger. I find the disclosure on this point to be accurate and complete. Fitzgerald also asserts that Vishay should have predicted the likelihood of a successful tender. That is inherently unknown and too speculative to be a required item of disclosure, even though one entity is said to hold more than one-third of the minority stock.

(l) Fitzgerald raises several disclosure issues dealing with Lehman's work for the Special Committee. He attacks the valuation ranges prepared by Lehman using three different methodologies: comparable

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[66]Vishay's Answering Brief, at 11.

[67]*See Life Technologies, supra*, Bench ruling transcript at 16-17.

[68]*Kahn v. United States Sugar Corp.*, Del. Ch., C.A. No. 7313, mem. op. at 14-15, Hartnett, V.C. (Dec. 10, 1985); *In re Staples, Inc. Shareholders Litig.*, Del. Ch., C.A. No. 18784, mem. op. at 45, String, V.C. (June 5, 2001).

companies analysis ($23.13 to $59.13 per share); comparable transactions analysis ($14.04 to $58.09 per share); and discounted cash flow analysis ($29.68 to $38.81). These ranges are said to be so broad that they offer little help to the shareholders. As a general matter, that would be an accurate observation. However, Lehman was dealing with projections for a company that had completed its best year but was in the throes of an economic downturn, thus leading to uncertainty and a corresponding range of inputs that affected the first two methodologies in particular. The ranges provided by Lehman were accurately-disclosed,[69] and importantly, the proposed effective exchange price falls at the low end of all of the ranges, particularly at the very bottom of the range provided by the discounted cash flow method. Thus, the shareholders have the benefit of the work product that the Special Committee obtained from Lehman. That work product indicates Lehman's view that the effective price, while within the range of reasonableness, is a low price. Given the Special Committee's duties, as I understand them, there was no requirement that a formal fairness opinion be obtained and in the absence of a duty to obtain one, and in the absence of having one, there was no duty to supply one to the shareholders.

(m) Fitzgerald argues that, during its evaluation of the $28.82 per share tender offer, Lehman, on behalf of the Special Committee, concluded that a fair price for Siliconix could not be less than $34 per share. At the end of April, an individual's meeting notes reflect that Lehman was "unsure" about a fairness opinion at less than $34 per share.[70] According to Fitzgerald, investment bankers use the term "unsure" as code that should be interpreted to mean that $34 per share is a floor for the fairness opinion. He argues that the $34.00 per share floor should have been disclosed to the shareholders. I find that Fitzgerald has been unable to satisfy on this record the materiality requirement because the number was preliminary.[71] Furthermore, Fitzgerald refers to a range of $34 to $36 per share that the Special Committee focused on during its negotiations with Vishay (before Vishay decided to proceed with its unilateral exchange offer). I do not doubt that the shareholders would find those numbers helpful, but again, they are not material. Negotiating positions can be taken for many reasons, some of which are not meaningfully related to value. The position may have been taken (and the record is far from clear on this) simply in what turned out to be a futile effort to obtain a higher price. In any event, the

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[69]Schedule 14D-9 at 12-19.

[70]Deposition of Mark Segall, Ex. 2.

[71]*See, e.g.*, *In re Triton Group Ltd. Shareholders Litig.*, Del. Ch., C.A. No. 11429, Chandler, V.C. (Mar. 11, 1991); *In re Anderson Clayton Shareholders Litig.*, Del. Ch., 519 A.2d 680 (1986) (disclosure of intermediate opinion).

best understanding of Lehman's position that it developed after obtaining the information that it deemed appropriate and having had time to reflect upon the information it obtained, including information about the market in which Siliconix participates, can be found in the Schedule 14D-9, which discloses its analysis.

(n) Fitzgerald next turns to the alleged conflicts of interest of the Special Committee members. Where there are material conflicts, disclosure of information sufficient to allow the shareholders to assess and understand those conflicts is necessary.[72] The Registration Statement[73] and the Schedule 14D-9[74] both disclose that the Special Committee members had "prior business relationships with Vishay." It was disclosed that Segall had been a partner with the law firm that represents Vishay, had recently represented Vishay personally, and had represented Vishay when it acquired its interest in Siliconix. It was also disclosed that Talbert in the 1980s had, in effect, been Vishay's banker and now owns Vishay stock. The personal friendship of Segall and Talbert with Vishay executives and a limited volume of business done with Vishay by Segall's current employer were not disclosed. Under current Delaware law, personal friendship is not an indication of disloyalty.[75] Similarly, the apparently limited business relationship between Segall's employer and Vishay does not trigger any significant issue of conflict. Thus, any additional disclosures that could have been made would not have been material.[76]

(o) The sufficiency of the disclosures as to why the Special Committee failed to take a position on whether shareholders should accept or reject the tender must also be considered. The disclosure that the Special Committee was unable to come to a recommendation, and the reasons behind its inability to do so, are material because those facts may well be viewed by minority shareholders as tending to suggest that there are reasons for considering rejection of the exchange offer. Also, once Siliconix disclosed the reasons for the Special Committee's neutrality, those disclosures had to be complete and truthful. As noted above, several relevant factors were identified. While it would have been more helpful if there had been a focus on the relative significance of the factors to the

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[72]*Oliver v. Boston University*, Del. Ch., C.A. No. 16570, Steele, V.C. (July 18, 2000, revised July 25, 2000).

[73]Registration Statement at 48.

[74]Schedule 14D-9 at 3.

[75]*See Crescent/Mach I Partners L.P. v. Turner*, Del. Ch., C.A. No. 17455, Steele, J. (Sep. 29, 2000).

[76]I recognize Talbert may have been hand-picked to serve on the Special Committee, but merely because one is selected by someone to be a director does not mean that he is beholden to that person.

Special Committee's decision, the disclosure on its face appears complete, and Fitzgerald has not made a preliminary showing that the explanation given was either misleading or incomplete.

(p) Finally, Fitzgerald has identified a number of matters that he contends should have been disclosed, such as the reasons why the Special Committee contested the original tender offer of $28.82 per share, what the negotiating points between the Special Committee and Vishay were, and the Special Committee's discussions with Lehman over its transactional analysis. Fitzgerald has failed to show that any of these were material because they involve intermediate steps and there is no right to a "play-by-play" of the negotiation or review process.[77]

In conclusion, I have not found that, on this preliminary record, Fitzgerald had made the necessary showing to establish any disclosure violation. Accordingly, I will now turn to a consideration of whether or not the tender is coercive.

4. **Coercion.**

A tender offer is coercive if the tendering shareholders are "wrongfully induced by some act of the defendant to sell their shares for reasons unrelated to the economic merits of the sale."[78] The wrongful acts must "[influence] in some material way" the shareholder's decision to tender.[79] I now turn to the instances alleged by Fitzgerald to constitute actionable coercion.

(a) Fitzgerald contends that the timing of Vishay's actions created coercive pricing conditions in three ways.

First, he alleges that the transaction was timed to take advantage of Siliconix' temporarily low price. Vishay, however, did not propose the transaction at an historic low. Indeed, the price of Siliconix, as of the time of the exchange offer, had risen significantly from its then recent low in December 2000. (The stock had been as high as $144.50 in March 2000.) Given the volatility of the Siliconix stock, like many stocks in the technology sector, it is difficult to give either credit or blame to Vishay based on any timing decision. Moreover, Vishay has provided a credible

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[77] *Arnold v. Society for Savings Bankcorp. Inc.*, Del. Ch., C.A. No. 12883, mem. op. at 17, Chandler, V.C. (Dec. 17, 1993), aff'd in part & rev'd in part, Del. Supr., 650 A.2d 1270 (1994).

[78] *Ivanhoe Partners v. Newmont Mining Corp.*, Del. Ch., 533 A.2d 585, 605, *aff'd.*, Del. Supr., 535 A.2d 1334 (1987); *Ocean Drilling, supra*, mem. op. at 10-11; *Eisenberg v. Chicago Milwaukee Corp., supra*, 537 A.2d at 1051, 1061.

[79] *Ivanhoe Partners v. Newmont Mining Corp., supra*, 533 A.2d at 605-06.

explanation that it chose to pursue the balance of the minority shares because of industry conditions and its needs to achieve the benefits of consolidation with Siliconix. In a context where a company was tendering for its own stock, this Court observed:

> If these [timing and the unwarranted decision not to pay dividends] were the only relevant circumstances (and if proper disclosure was made of all material facts), the Court would have difficulty concluding, at least on this preliminary record, that the Offer is inequitably coercive. In what sense do corporate directors behave inequitably if they cause the corporation to offer to purchase its own publicly-held shares at a premium above market, even if the market price is at an historic low? So long as all materials facts are candidly disclosed, the transaction would appear to be voluntary.[80]

Although there may be circumstances where the timing of a tender could be deemed coercive because of market conditions, they are not present here.

Second, the original tender offer of February 2000, according to Fitzgerald, was intended by Vishay to keep the Siliconix price depressed. That tender offer set forth a price per share of $28.82. If it was intended as a "cap, " it was unsuccessful because Siliconix traded as high as $32.67 per share on May 23, 2001. All two-step merger transactions may be said to have some effect at "capping" the price,[81] but an announcement, such as the one Vishay made in February (and one which Vishay apparently was lawfully entitled to make), cannot be said to have a coercive effect three months later, at least without more proof than is available at this stage of the proceedings.

Third, Fitzgerald asserts that, by using the temporarily low price and its alleged market manipulation efforts, Vishay has demonstrated to the minority shareholders that their future as Siliconix shareholders will be adversely affected by these on-going market manipulations to deny them a fair value for their Siliconix holdings. If the announcement in February did not constitute market manipulation to establish a coercive environment

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[80]*Eisenberg v. Chicago Milwaukee Corp.*, 537 A.2d at 1061 (involving a tender offer shortly after the Black Monday of October, 1987); *see, e.g.*, *Sealy Mattress Co. of New Jersey, Inc. v. Sealy, Inc.*, Del. Ch., 532 A.2d 1324 (1987); *MacLane Gas Co. Limited Partnership v. Enserch Corp.*, Del. Ch., C.A. No. 10760, Chandler, V.C. (Dec. 9, 1992) *aff'd*, Del. Supr., 633 A.2d 369 (1993) (TABLE).

[81]*See Ocean Drilling, supra*, mem. op. at 7.

for the tender, the unspecified "on-going" efforts similarly do not evidence actionable coercion.

(b) Vishay's failure to commit absolutely to pursue the short-form merger, following a successful tender, on the same terms as the tender, Fitzgerald argues, constitutes actionable coercion. The implicit threat is said to be that the short-form merger might be consummated on less favorable terms, and, notwithstanding the protection afforded by their appraisal rights, Siliconix shareholders will be wrongfully induced to respond favorably to the tender out of fear that they might be faced with reduced consideration in the context of the short-form merger or, perhaps worse, as Vishay has disclosed as a possibility, they may find themselves for an extended period of time or even permanently as members of an even smaller minority. The question is whether Vishay's position, and its disclosure to the Siliconix shareholders, constitutes actionable coercion. This Court has considered whether the refusal to commit to a second step merger following a tender is coercive and has concluded that it is not.[82] I see nothing in the facts of this case to persuade to deviate from this line of authority.

(c) Fitzgerald has also observed that Vishay's Registration Statement[83] reflects Vishay's intent to delist Siliconix shares from the NASDAQ. The threat of delisting, with its potentially significant adverse impact on liquidity, was viewed by the Court in *Eisenberg v. Chicago Milwaukee Corp.* as the final factor that led to the conclusion that the tender there was coercive.[84]

The Registration Statement, however, provides, "We [Vishay] intend to cause the de-listing of the Siliconix shares from NASDAQ following consummation of the offer <u>and</u> the short-form merger." (emphasis added). Thus, there is no threat by Vishay to delist the Siliconix stock until after completion of the short-form merger, at which time, by definition, there would be no more publicly traded Siliconix stock.

The Registration Statement also provides that the Siliconix "could be" de-listed if the tender is completed but the short-form merger is not carried out.[85] The Registration Statement refers readers to another section[86]

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[82]*Id.*, *supra*, mem. op. at 5 ("I am not persuaded that this structural feature of the exchange offer is actionable coercion."); *Life Technologies*, *supra*, Transcript at 9-11 ("not an argument that leads me to believe that the offer is coercive.") (intention, but not absolute commitment, to engage in second step.)

[83]Registration Statement at 44.

[84]*Eisenberg v. Chicago Milwaukee Corp.*, *supra*, 537 A.2d at 1062.

[85]Registration Statement at 44.

[86]Registration Statement at 40 (Purpose of the Offer: the Merger; Appraisal Rights).

to explain both the reasons for, and the consequences of, a potential delisting. Unlike *Eisenberg*, where the acquirer vowed to initiate the delisting,[87] here any delisting would depend upon the success of the Vishay tender. Thus, this is not threatening or coercive but, instead, is the disclosure of a potential (and undeniably adverse) consequence to those shareholders who do not tender, if the tender is successful. By itself, or in conjunction with, the other allegedly coercive circumstances, Fitzgerald has not demonstrated that the delisting statement constitutes coercion, at least at this preliminary stage.

(d) In some sense, Fitzgerald laments the position of a minority shareholder in a corporation where one shareholder controls more than 80% of the stock. If the tender is successful and he does not tender, Fitzgerald will either be a member of an even smaller minority or his stock will be the object of a short-form merger that will divest him of his pure stake in Siliconix. Perhaps these circumstances are not happy ones, but they are allowed by law and inherent in the nature of his holdings and, thus, while perhaps encouraging him to tender, do not constitute actionable coercion.[88]

Accordingly, Fitzgerald has not succeeded in demonstrating, at this time, that he has a reasonable probability of success on the merits of his claims.

C. Irreparable Harm.

Because Fitzgerald has not demonstrated a reasonable probability of success on the merits of his claims, I will only briefly touch upon the remaining prongs of the preliminary injunction standard.

As a general matter, a plaintiff seeking to enjoin preliminarily a tender offer must show that, in the absence of the interim relief: (i) the injury could not easily be undone and (ii) damages would not be an adequate remedy.[89]

The assessment of the likelihood of irreparable harm depends to some extent on the nature of the injuries suffered. For example, if the injury is one arising out of a material disclosure violation, irreparable harm will more likely be found because "Delaware law recognizes that an after-

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[87] *Eisenberg v. Chicago Milwaukee Corp., supra*, 537 A.2d at 1062 ("Those directors have disclosed that they intend to seek to eliminate a valuable attribute of the capital preferred stock, namely, its NYSE listing.")

[88] *See In re Grace Energy Corp. Shareholders Litig.*, Del. Ch., C.A. No. 12464, Hartnett, V.C. (June 26, 1992).

[89] *See, e.g., Kingsbridge Capital Group v. Dunkin' Donuts, Inc.*, Del. Ch., C .A. No. 10907, mem. op. at 14, Chandler, V.C. (Aug. 7, 1989).

the-fact damages case is not a precise or efficient method by which to remedy disclosure deficiencies."[90] Of course, if the contemplated tender is completed,[91] it will be hard to unwind.

On the other hand, because of Fitzgerald's extensive argument about fair price and the entire fairness standard with an emphasis on the fair price component, it is reasonable to infer that the ultimate principal concern will be one of value. Damages can be awarded and, indeed, have been awarded after a trial that followed denial of a preliminary injunction application addressed to halting a tender offer.[92]

D. Balance of the Equities.

I need not engage in any extended consideration of this prong of the preliminary injunction standard. I simply note a reluctance, under these circumstances, to deprive the Siliconix shareholders of the opportunity to exchange their shares for Vishay stock or of the opportunity to exercise their majority will to derail the tender under the "majority of the minority" tender aspect of the proposed transaction, if that is their collective wisdom.

IV. CONCLUSION

For the foregoing reasons, an Order denying Fitzgerald's Motion for a Preliminary Injunction will be entered.

ORDER

NOW, this 19th day of June, 2001, for the reasons set forth in the Memorandum Opinion of this date,

IT IS HEREBY ORDERED, that Plaintiff Raymond L. Fitzgerald's Motion for a Preliminary Injunction be, and the same hereby is, denied.

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[90] *In re Staples, Inc., supra*, mem. op. at 57; *Sonet v. Plum Creek Timber Co.*, L.P., Del. Ch., C.A. No. 16931, mem. op. at 19, Jacobs, V.C. (Mar. 18, 1999.

[91] Of course, if a majority of the minority does not tender its shares, there will not be irreparable harm.

[92] *Kahn v. United State Sugar Corp.*, Del. Ch., C.A. No. 7313, Hartnett, V.C. (Dec. 10, 1985); *see also, Ocean Drilling, supra*, mem. op. at 7; *cf. Andra v. Blount*, Del. Ch., C.A. No. 17154, Strine, V.C. (Mar. 29, 2000).

WHELEN v. SECURITIES COMMISSIONER OF THE STATE OF DELAWARE

No. 18,675

Court of Chancery of the State of Delaware, New Castle

December 10, 2001

John L. Reed, Esquire, and Thomas P. McGonigle, Esquire, of Duane, Morris & Heckscher, LLP, Wilmington, Delaware, for appellants/ respondents below.

Peter O. Jamison, III, Deputy Attorney General, Department of Justice, State of Delaware, for appellees.

LAMB, *Vice Chancellor*

I.

This is an appeal from an Opinion and Order issued December 18, 2000 by an administrative hearing officer ("Hearing Officer") appointed to act in a matter filed before the Securities Commissioner of the State of Delaware. The Hearing Officer found that William N. Whelen, Jr., a broker-dealer agent with Simon Securities, Inc., violated various sections of the Delaware Securities Law. Furthermore, the Hearing Officer found that Simon Securities and its President, William J. Byrd, III, failed to supervise Whelen, in violation of 6 *Del. C.* § 7316(a)(10). As a result of these findings, the Hearing Officer imposed sanctions on Whelen, Byrd, and Simon Securities (collectively "Appellants") and ordered Byrd to make restitution payments.

In this Opinion, I will evaluate the scope of an arbitration agreement entered into between the parties and its effect on the Hearing Officer's power to award restitution. Further, I will determine whether there is enough evidence in the record to support the Hearing Officer's findings that the Appellants violated the Delaware Securities Act. Finally, I will determine whether the statute of limitations should have barred the proceeding below.

II.

The facts underlying the issues on this appeal date back to 1993. At that time, Emerson Pepper approached William N. Whelen, Jr., a broker-dealer agent with Simon Securities, Inc., seeking to raise capital for First State Poultry, Inc. Whelen agreed to help Pepper and began soliciting a number of potential investors, including Ronald and Donna Mitchell, who were Whelen's long time clients. The Mitchells agreed to invest $50,000 in First State Poultry in the form of a two-year debenture yielding 10% annually. On or about July 6, 1993, the Mitchells sent a check for $50,000 to the bank that was acting as an escrow agent for the debenture offering.

In August 1993, the National Association of Securities Dealers ("NASD") and the United States Securities and Exchange Commission ("SEC") conducted a review of Simon Securities. During the review, a NASD officer contacted persons who had invested in First State Poultry and determined that the investors were not adequately apprised of the risks associated with their investments.

In light of the NASD's findings, William J. Byrd, III, President of Simon Securities, contacted Whelen and ordered all of the investors' money returned. Byrd also summoned Whelen to a meeting with Byrd's attorney. At this meeting, Byrd testified, he instructed Whelen to engage in full disclosure with respect to any investments that Whelen offered to his clients. Byrd also testified that he told Whelen not to get involved with the First State Poultry offering "at this level." Byrd explained that he was leaving open the possibility that Simon Securities might, in the future, be willing to assist First State Poultry in obtaining financing through the Sussex County Industrial Revenue Authority. After the meeting, Byrd testified, he monitored Whelen's activities on a daily basis by talking to him on the telephone and reviewing his outgoing correspondence.

Byrd also sent a letter to Pepper informing him that an SEC audit brought to light serious concerns regarding the underwriting of First State Poultry. The letter went on to state that it was in the best interest of all the parties to return the money to the investors and suggested that Pepper direct the bank to do so. Pepper later instructed the bank to do so and the funds were returned.

Pepper also mailed a letter to each investor, that he claims was drafted by Whelen, falsely stating that their investments were being returned because First State Poultry was unable to obtain a mortgage commitment for the construction of its chicken processing facility.

Beginning sometime afterward, Pepper wrote to the Mitchells and others to re-solicit their investment in First State Poultry. At the hearing

below, Pepper testified that, while he typed and mailed the letters, Whelen was the draftsman. Pepper also stated that he was not aware of any involvement by Byrd or Simon Securities in the attempt to resolicit investments in First State Poultry. Pepper's resolicitation proved successful. The Mitchells (among others) agreed to reinvest under the originally agreed upon terms.

In January 1994, Pepper allegedly sent the Mitchells a stock certificate indicating that they owned thirty shares of stock in First State Poultry. The stock was not registered with the Delaware Division of Securities. Mr. Mitchell, confused by the receipt of a stock certificate because he thought he had purchased debentures, contacted Pepper for an explanation. Unable to get any clarification from Pepper, Mr. Mitchell called Whelen and asked about the stock certificate. According to both Whelen and Mr. Mitchell, Whelen explained that he was not involved with the resolicitation and that Mr. Mitchell would need to resolve the issue with Pepper. Whelen's lack of knowledge of the stock issuance is contradicted by Pepper's testimony and by the fact that he drafted and signed a document captioned "proposal" that listed all the shareholders of First State Poultry and their respective ownership interests in the company. The "proposal" shows that Whelen and Pepper were to be the principal shareholders of First State Poultry.

The Mitchells let the issue go and over the next few years received and accepted dividend payments from First State Poultry totaling over $17,000. In September 1995, however, the Mitchells demanded that First State Poultry return their $50,000 principal investment in full, as originally promised. First State Poultry refused and, that same month, the Mitchells filed suit in the Superior Court claiming that they had been defrauded by Pepper and First State Poultry. On September 11, 1998, the Mitchells filed a second civil complaint in the Superior Court naming Whelen and Simon Securities as defendants and making the same allegations they had previously made against Pepper and First State Poultry. In May 1999, after reaching an agreement with Whelen and Simon Securities to submit their dispute to binding arbitration before the NASD, the Mitchells stipulated to the dismissal of their second Superior Court action.

Also on September 11, 1998, the Delaware Division of Securities (the "Division") filed an administrative complaint with the Hearing Officer for the State of Delaware against Pepper and the parties to this appeal, Whelen, Byrd, and Simon Securities (collectively "Appellants"). The Division alleged that the Appellants violated various provisions of the Delaware Securities Act, 6 *Del. C.* Ch. 73 (the "Act"), in obtaining financing for First State Poultry. On April 21, 1999, the Division filed a

First Amended Complaint with the Hearing Officer that added a charge of fraud against Whelen. On September 14, 1999, the Division filed a Second Amended Complaint with the Hearing Officer that added allegations of dishonest and unethical conduct by Whelen. The Division claimed that Whelen's misconduct in connection with the resolicitation was hidden from the Division until May 6, 1999, when the Division learned of Whelen's misconduct during an interview of Pepper.

In March and August of 2000, Deputy Attorney General Richard Hubbard, who was designated initially by the Securities Commissioner and later by the Attorney General to act as Hearing Officer, conducted a hearing on the Division's complaint. The Hearing Officer issued a Default Order against Pepper requiring that he make restitution to the Mitchells and pay a fine of $70,000. A short time later, Pepper filed for bankruptcy in federal court. The Appellants then moved to stay the proceedings under the automatic stay provisions of federal bankruptcy law. The Hearing Officer denied the motion and the hearing continued, coming to a conclusion on August 23, 2000.

On December 18, 2000, the Hearing Officer issued an Opinion and Order making the following findings in connection with the resolicitation of investments in First State Poultry:

(i) Whelen was, in general, willfully dishonest in violation of 6 *Del. C.* § 7316(a)(7);
(ii) Whelen willfully caused the offer of an unregistered stock in violation of 6 *Del. C.* §§ 7304 and 7316(a)(2);
(iii) Whelen willfully violated 6 *Del. C.* § 7303 and 7316(a)(2) by omitting information as to the risks associated with the First State Poultry stock;
(iv) Whelen violated 6 *Del. C.* § 7316(a)(7) by selling a security that was unsuitable for his client;
(v) Simon Securities failed to supervise Whelen reasonably in violation of 6 *Del. C.* § 7316(a)(10); and
(vi) Byrd failed to supervise Whelen reasonably in violation of 6 *Del. C.* § 7316(a)(10).

As a result of these findings, the Hearing Officer:

(i) revoked Whelen's registration as a broker-dealer agent in Delaware;
(ii) ordered Whelen to pay a fine in the amount of $25,000;

(iii) ordered Simon Securities to pay a fine in the amount of $10,000;
(iv) suspended the broker-dealer license of Simon Securities for one hundred twenty (120) days;
(v) ordered Byrd to make restitution in the amount of $69,945.21;
(vi) suspended Byrd's broker-dealer agent license for sixty (60) days; and
(vii) fined Byrd $10,000 to be suspended upon full payment of restitution.

On February 15, 2001, Appellants filed a complaint in this court pursuant to 6 *Del. C.* § 7324 seeking to have the Hearing Officer's Opinion and Order set aside. They contend that the Hearing Officer's findings of fact are not supported by competent, material and substantial evidence in the record and the conclusions of law are erroneous. The matter was submitted to the court on the parties' briefs.

III.

A. The Standard of Review

The Act designates the Court of Chancery as the forum for judicial review.[1] The Delaware Supreme Court has opined that assignment of jurisdiction to this court is due to "the area subject to regulation and the need for injunctive relief in enforcement."[2] In reviewing such orders, the findings of the Commissioner as to the facts, if supported by competent, material and substantial evidence, are conclusive.[3] The statute by its silence implicitly recognizes the authority of this court to determine questions of law *de novo*.[4]

B. Review of the Hearing Officer's Factual Conclusions

Appellants argue that there is no document or other type of record evidence showing that Whelen engaged in a conspiracy to violate the Delaware Securities Act in connection with the resolicitation. Also,

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[1] 6 *Del. C.* § 7324(a).
[2] *Blinder Robinson & Co. v Bruton*, Del. Supr., 552 A.2d 466, 470 (1989).
[3] 6 *Del. C.* § 7324(b).
[4] *Blinder Robinson & Co.*, 552 A.2d at 470 (citing, *DuPont v. DuPont*, Del. Supr., 216 A.2d 674, 680 (1966))

Appellants contend that assuming, *arguendo*, that the Division proved that Whelen engaged in a conspiracy to violate the Delaware Securities Act, there is no evidence to sustain a violation for failure to supervise by Simon Securities and/or Byrd.

1. Review of the Hearing Officer's conclusion that Whelen engaged in a conspiracy to violate the Delaware Securities Act.

Appellants claim that the sanctions imposed against Whelen should be overturned because the Hearing Officer's findings of fact are not supported by competent, material and substantial evidence. In support of this claim, they argue that that there is no single document or other type of record evidence showing that Whelen engaged in a conspiracy to violate the Delaware Securities Act. Relying on *Weick v. State*,[5] Appellants contend that the Division is required to prove not only that Whelen agreed with Pepper to engage in conduct that violates the Act, but also that Whelen committed an overt act in furtherance of the agreement.

Appellants interpretation of *Weick* is incorrect. The *Weick* court interpreted 11 *Del. C.* § 512[6] and found that in order to obtain a conspiracy conviction the State must prove the existence of an unlawful agreement and that an overt act in furtherance of the agreement had been committed. The court did not state, as Appellants claim, that the person charged with the crime had to commit the overt act. Furthermore, the *Weick* court relied on the Delaware Criminal Code Commentary, a part of the legislative history of the conspiracy statute, for the proposition that "[a]n important change in the former law is a requirement that an overt act be committed in pursuance of the conspiracy . . . . It is sufficient that any of the conspirators has committed an overt act."[7] Consequently, the Division did not have the burden of proving that Whelen committed an overt act in furtherance of the agreement. It only had to prove that an agreement had been made and *either* Whelen or Pepper committed an act in furtherance of the agreement.

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[5]Del. Supr., 420 A.2d 159 (1980).

[6]That section provides as follows: "A person is guilty of conspiracy in the second degree when, intending to promote or facilitate the commission of a felony, the person: (1) Agrees with another person or persons that they or 1 or more of them will engage in conduct constituting the felony or an attempt or solicitation to commit the felony; or (2) Agrees to aid another person or persons in the planning or commission of the felony or an attempt or solicitation to commit the felony; and the person or another person with whom the person conspired commits an overt act in pursuance of the conspiracy."

[7]*Weick*, 420 A.2d at 164-65.

I find that competent, material and substantial evidence exists that proves the existence of an agreement and an overt act in furtherance of the agreement. First, Pepper testified that he and Whelen met several times to discuss resoliciting investors for First State Poultry. Second, contrary to Appellants' claim that not one piece of paper exists evidencing an agreement between Pepper and Whelen, the record reveals a document entitled "proposal" that was drafted and signed by Whelen. The document states that Whelen and Pepper would be the principal shareholders of First State Poultry and lists the remaining shareholders and their stakes in the company. The meetings together with this documentary evidence clearly amounts to competent, material and substantial evidence that Pepper and Whelen had an agreement to resolicit funds from investors. Further, Pepper's testimony stating that he contacted investors and convinced them to reinvest satisfies the overt act requirement.

Based on the existence of the conspiracy between Whelen and Pepper, I affirm the Hearing Officer's conclusions that Whelen was, in general, willfully dishonest in violation of 6 *Del. C.* § 7316(a)(7); Whelen willfully violated 6 *Del. C.* §§ 7303 and 7316(a)(2) by omitting information as to the risk of First State Poultry stock; and Whelen violated 6 *Del. C.* § 7316(a)(7) by selling a security that was unsuitable for his client.

2. Review of the Hearing Officer's conclusion that Byrd and/or Simon Securities failed to supervise Whelen in violation of 6 *Del. C.* § 7316(a)(10).

The Hearing Officer found that Byrd and Simon Securities failed to supervise Whelen in violation of 6 *Del. C.* § 7316(a)(10). The Appellants argue that assuming, *arguendo,* that the Division proved a violation of the Act by Whelen, no evidence exists to support the failure to supervise finding against Simon Securities and/or Byrd.

I have reviewed the record below and find that the Hearing Officer's conclusion that Byrd and/or Simon Securities violated 6 *Del. C.* § 7316(a)(10) by failing reasonably to supervise Whelen as to the second offering of First State Poultry is not supported by competent, material and substantial evidence. The Hearing Officer's findings were based entirely on the fact that Simon Securities and Byrd were aware of Whelen's misconduct in connection with the initial offering of First State Poultry and, while they took certain steps to increase Whelen's supervision, failed to prevent the second solicitation from occurring. Unlike the Hearing Officer, I refuse to infer from the fact that a second solicitation did occur

a conclusion that Byrd and/or Simon Securities "failed reasonably to supervise" Whelen.[8]

The evidence is uncontested that Byrd, upon learning of the findings by the SEC and the NASD, telephoned Whelen and ordered all the investors' money returned. In addition, Byrd promptly summoned Whelen to a meeting in Doylestown, Pennsylvania with Byrd and his attorney where Whelen was warned not to get involved in the First State Poultry offering "at this level." The Hearing Officer interpreted Byrd's comment to mean that, while Whelen should not directly solicit investments from Simon Securities' customers, Byrd had no objection to Pepper making the solicitations. The record indicates, however, that during the hearing, Byrd was asked to clarify what he meant by the phrase "at this level" and he stated that he told Whelen not to get involved at all unless the Industrial Revenue Authority in Sussex County was interested in funding the deal. Following the meeting, Byrd stepped-up his supervision of Whelen and began monitoring Whelen's activities on a daily basis by talking to him on the telephone and reviewing Whelen's out-going correspondence. All of these factors suggest that Byrd, in his supervisory capacity, took reasonable steps to monitor Whelen's conduct.

Further, there is not a single piece of paper, record, account form, telephone record, or any testimony in the record that indicates that the second solicitation on behalf of First State Poultry occurred on Simon Securities premises, with Simon Securities equipment, using Simon Securities letterhead, or that Simon Securities was otherwise involved with or even aware of the second solicitation. Even the Division's complaint alleges that the "conspiracy" between Whelen and Pepper was formed in Pepper's home. Simon Securities and/or Byrd cannot be held strictly accountable for Whelen's misconduct when it occurs at the home of a co-conspirator and outside the scope of his employment.

For these reasons, I reverse the Hearing Officer's findings of violations by Simon Securities and Byrd, together with the suspensions, fines and restitution imposed on them. It should be noted, however, that the Mitchells are free to pursue all claims against Simon Securities and Whelen in the arbitration proceeding.

C. Review of the Hearing Officer's Legal Conclusions.

The Appellants raise four arguments seeking to overturn the Hearing Officer's conclusions of law. First, the Appellants claim that the award of

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[8] 6 *Del. C.* § 7316(a)(10).

restitution against Byrd is void because the issue of restitution is subject to the binding arbitration agreement between the Mitchells and Simon Securities. Second, the Appellants contend that there can be no finding of a violation for the sale of unregistered securities because the securities at issue were exempt from registration pursuant to §§ 7304 and 7309(b)(9) of the Delaware Securities Act. Third, Appellants claim that the Hearing Officer's Opinion and Order is void *ab initio* because the proceeding below was stayed pursuant to federal bankruptcy law and no request for relief from the stay or severance of the non-debtor parties from the proceeding was sought. Finally, the Appellants maintain that all of the Division's claims are barred by the applicable statute of limitations. I will address these arguments in turn.

1. Review of the Hearing Officer's decision to exclude Byrd from the arbitration agreement.

On May 26, 1999, a Stipulation of Dismissal was entered into between the Mitchells and both Simon Securities and Whelen. It stated in pertinent part:

> WHEREAS, the parties have agreed to submit this dispute to binding arbitration before the National Association of Securities Dealers.

Based on this agreement, the Hearing Officer held that the restitution remedy was unavailable as to Whelen and Simon Securities. Nevertheless, the Hearing Officer found that the restitution remedy could be pursued against Byrd since he is not listed as a party in the Stipulation of Dismissal.

I have already concluded that the Hearing Officer's factual conclusion that Byrd and Simon Securities failed to supervise Whelen is not supported by competent, material and substantial evidence. Nonetheless, I will consider whether the agreement to arbitrate between the Mitchells and Simon Securities precluded the Hearing Officer from awarding restitution against Byrd as a matter of law. Appellants claim that the Hearing Officer's decision to exclude Byrd from the arbitration agreement ignores the principles established in *Olde Discount Corporation v. Tupman*.[9] Furthermore, Appellants argue that the Hearing Officer's decision contradicts strong public policy and case law of this State favoring arbitration of claims. For the reasons discussed below, I find that the

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[9] 1 F.3d 202 (3d Cir. 1993).

Mitchells' agreement to arbitrate their claim for restitution against Simon Securities precluded the Hearing Officer from making an award of restitution in their favor against Byrd.

It is obvious from the decision that Byrd's only source of potential liability to the Mitchells flows from his employment as President of Simon Securities. Indeed, under the Hearing Officer's order, Byrd's liability to pay restitution is based solely on a finding that he, as President of Simon Securities, failed to supervise Whelen. The Hearing Officer made the same finding as against Simon Securities but did not enter a restitution order against the corporation due to the existence of the arbitration agreement. In the circumstances, it is hard to see how the claim against Byrd is distinguishable from the claim the Mitchells agreed to arbitrate against Simon Securities. Indeed, it is only reasonable to assume that Simon Securities will be obliged to indemnify Byrd for any restitution he is ordered to make to the Mitchells.[10]

Simon Securities, however, agreed to arbitrate the Mitchells' claim for restitution and should not be threatened with the possibility of paying two such awards.[11] Conversely, Simon Securities could win the arbitration claim, but, nevertheless, have to foot the bill for the restitution order against Byrd. Thus, allowing the Hearing Officer to award restitution against Byrd permits the Mitchells to "end run" the arbitration agreement by seeking the same relief in another proceeding.[12]

Treating the claim against Byrd as within the scope of the arbitration agreement is also consistent with Delaware public policy, which favors resolving disputes through arbitration.[13] Moreover, Delaware courts have found that an arbitration agreement ordinarily encompasses the disposition of the entire dispute between the parties on which an awarded judgment may be entered.[14] Since liability against Byrd and Simon Securities for restitution would be based on the same facts and legal arguments, Delaware public policy dictates that both should be covered under the arbitration agreement.

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[10]This is particularly true because there is no finding that Byrd's "failure to supervise" was accompanied by any independent misconduct that made him part of the underlying conspiracy.

[11]*Olde Discount Corporation*, 1 F.3d 202.

[12]*Id.*

[13]*Graham v. State Farm Mutual Automobile Insurance Co.*, Del. Super., 565 A.2d 908, 911 (1989).

[14]*Pullman Inc. v. Phoenix Steel Corp.*, Del. Super., 304 A.2d 334, 338 (1973).

2. Review of the Hearing Officer's conclusion that Whelen willfully violated 6 *Del. C.* §§ 7304 and 7316(a)(2) by offering unregistered stock in First State Poultry to the Mitchells.

Appellants argue that the stock offering in this case was exempt from registration pursuant to 6 *Del. C.* § 7309(b)(9) because the offerings were made to fewer than twenty-five persons. Under 6 *Del. C.* § 7309(d) the burden of proving an exemption is on the person claiming it. I find that the Appellants have failed to meet their burden and thus affirm the Hearing Officer's holding that Whelen willfully violated 6 *Del. C.* §§ 7304 and 7316(a)(2) by offering unregistered stock in First State Poultry.

The Hearing Officer, has, pursuant to regulation, conditioned the exemption created by 6 *Del. C.* § 7309(b)(9). Specifically, §§ 502(b)(3) and 502(b)(4) of the Rules and Regulations to the Act provide that issuers relying upon the exemption created by 6 *Del. C.* § 7309(b)(9) must make certain filings with the Delaware Securities Division. It is undisputed that the proper filings were never made with the Delaware Securities Division. Hence, Appellants cannot claim to be exempt from registration by § 309(b)(9) of the Act.

The Appellants also argue that the Hearing Officer's decision should be reversed because the Division's administrative complaint did not charge them with failing to comply with the exemption filing requirements of § 502(b). This argument misunderstands the securities registration scheme under the Delaware Securities Act. The unlawful conduct here was not the Appellants' failure to comply with the exemption filing requirements of § 502(b) of the Rules and Regulations, but rather the Appellants' sale of unregistered securities. The exemption filing requirements of § 502(b) become relevant in a proceeding under the Securities Act only when an issuer claims that its offering was exempt from registration under § 7309(b)(9) of the Act. As stated above, because the necessary filings were not made with the Delaware Securities Division as required by § 502(b) of the Rules and Regulations, Appellants failed to meet their burden of proving that the securities at issue were exempt from registration under § 7309(b)(9) of the Act. The Hearing Officer, therefore, did not err in finding that Whelen willfully violated 6 *Del. C.* §§ 7304 and 7316(a)(2) by offering unregistered stock in First State Poultry.

3. Review of the Hearing Officer's decision to continue the proceeding after Pepper filed a Chapter 7 bankruptcy petition and triggered the automatic stay provision of the United States Bankruptcy Code.

Appellants argue that Pepper's voluntary filing of a Chapter 7 bankruptcy petition triggered the automatic stay provisions articulated in § 362 of the United States Bankruptcy Code and, as a result, prevented any further action against any of the Appellants. In support of their argument, Appellants cite *In re Related Asbestos Cases*.[15] There, the court held that an automatic stay does not apply to cases against non-debtors, and that proceedings against the debtors could be severed so as to permit the action to move forward against the non-debtor co-defendants. Based on *In re Asbestos*, Appellants argue that, because no severance occurred, the Hearing Officer was not permitted to proceed and, as a result, his Opinion and Order is unenforceable and must be set aside as a matter of law.

The Division argues that the Hearing Officer correctly held that, to the extent there was a stay arising out of a bankruptcy proceeding initiated by Pepper, that stay would only apply to proceedings against Pepper. Alternatively, the Division argues that Pepper was effectively severed from the proceedings on January 27, 1999 when a final order of default was entered against him.

Delaware law is unclear with respect to Appellants' argument that the Division was required to formally sever Pepper from the proceedings before it could pursue claims against the non-debtor Appellants. Also, the Division cites no authority supporting its contention that Pepper was effectively severed from the proceedings when a final order of default was ordered against him. The fact that I have already reversed the Hearing Officer's decision to award the Mitchells restitution damages allows me to resolve this issue without addressing either argument.

In their opening brief, Appellants cite *In re Mcorp*[16] for the proposition that 11 U.S.C. § 362(b)(4)'s "police or regulatory power" exception to the automatic stay does not apply when the regulatory agency is pursuing pecuniary damages. Nevertheless, governmental actions such as license suspensions are exempt from the automatic stay provisions articulated in § 362 of the United States Bankruptcy Code.

Aside from the Division's award of restitution, its remaining claims against the Appellants arise from its regulatory and policing authority.

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[15] 9 Bankr.Ct.Dec. 874 (N.D.Cal. 1982).
[16] 101 B.R. 483 (S.D. Tx. 1989).

These claims are, as Appellants concede, exempt from the automatic stay provisions articulated in § 362 of the United States Bankruptcy Code. As a result, I find that, putting to one side the Division's claim for restitution (which has already been reversed on other grounds), the Hearing Officer did not err in pursuing the Division's remaining claims because they all arise from the Security Commissioner's regulatory or policing authority.

4. Review of the Hearing Officer's conclusion that the Division's claims against Appellants were not time barred by 6 *Del. C.* § 7330.

Section 7330, Title 6, of the Delaware Code ("Statute of Limitations") reads as follows:

a) In any administrative, civil or criminal action brought by the Commissioner seeking registration suspension or revocation, fines, costs, restitution or imprisonment, no more than 5 years shall have passed from the date of the violation to the date of the initiation of the proceeding.

b) This 5-year limit shall not apply to registration denial proceedings.

The Division filed its initial complaint on September 11, 1998. The record reveals that the Mitchells' second $50,000 check is dated September 14, 1993.

Appellants argue that, because the Division has set forth no evidence supporting that the alleged misconduct occurred between September 11, 1993 and September 14, 1993, all of the Division's claims regarding the second solicitation are barred by the 5-year statute of limitations articulated in 6 *Del. C.* § 7330(a). Furthermore, Appellants argue that 6 *Del. C.* § 7330(a) operates as a statute of repose, not a statute of limitations, and as a result is not tolled by fraudulent concealment.

I find it unnecessary to decide the question whether or not § 7330(a) is a statute of repose or, instead, is susceptible to principles of equitable tolling. I reach this conclusion because I am satisfied that there is evidence in the record from which the Hearing Officer could properly conclude that actions that constituted a part of the conspiracy between Whelen and Pepper to violate the securities laws in connection with the resolicitation occurred within 5 years of September 11, 1998. Specifically, the record reflects the fact that the Mitchells dated their check on September 14, 1993

and mailed it to Pepper who later negotiated it. Also, at some later time, Pepper caused First State Poultry to issue share certificates to the Mitchells and the other investors. These acts were all in furtherance of the second solicitation and were all squarely within the 5-year period of limitations. For that reason, it is immaterial whether the record shows expressly that the initial contact to resolicit the Mitchells or the other investors occurred before September 11, 1993.

V.

For the foregoing reasons, the Hearing Officer's findings as to Whelen are affirmed along with all sanctions imposed on him. Conversely, I reverse the Hearing Officer's findings of violations by Simon Securities and Byrd, together with the suspensions, fines and restitution imposed on them. **IT IS SO ORDERED.**